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### **The Philippines: Fiscal Behavior in Recent History**

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# THE PHILIPPINES: Fiscal Behavior in Recent History

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2<sup>nd</sup> AC-UPSE Economic Forum



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UNIVERSITY OF THE PHILIPPINES  
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# The Philippines: Fiscal Behavior In Recent History

By

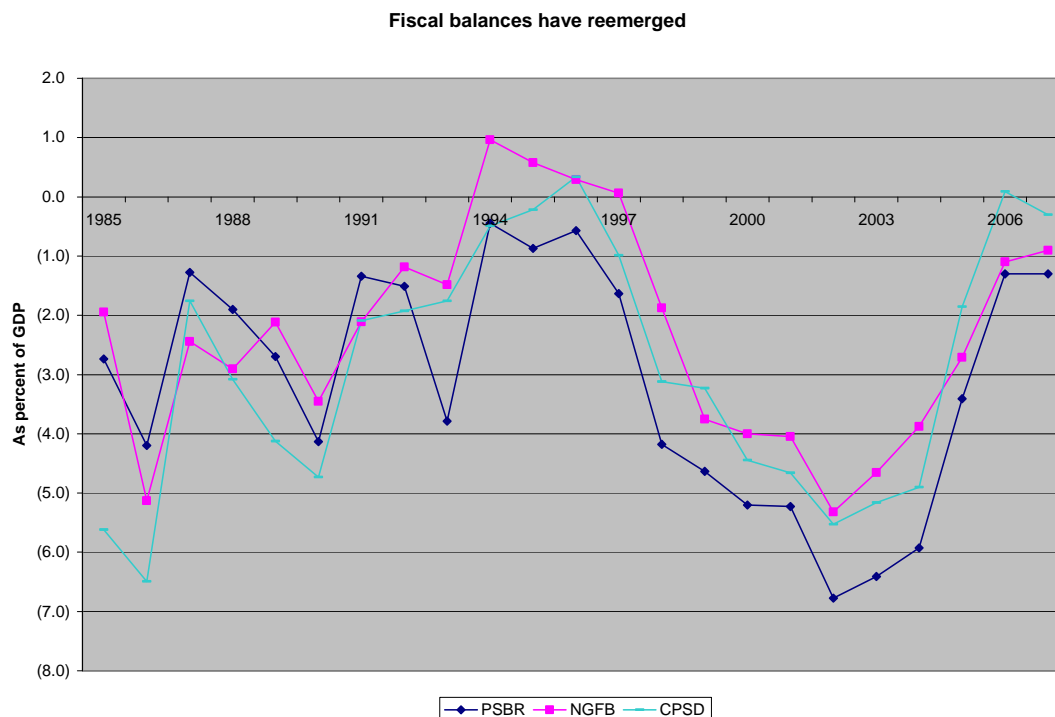
Benjamin E. Diokno<sup>1</sup>

## I. INTRODUCTION

The Philippine national government experienced large and unsustainable budget deficits in the 1980s. After a brief period of near balanced budget in the mid-1990s, large budget deficits have reemerged in recent years. But unlike the heavy fiscal imbalances in the early 1980s which were caused by large investment in public infrastructure and low tax effort, the return of large fiscal deficits in recent years was accompanied by falling tax effort and underspending for education, health and public infrastructure. With deficits rising and investment in human capital and public infrastructure deteriorating, an appropriate question is: what has caused the poor fiscal performance of the Philippines in recent years? Is it the result of unfortunate events, macroeconomic shocks or misdirected fiscal policy?

FIGURE 1

Various measures of fiscal deficits: NGFB, CPSD, PSBR



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There are at least three possible ways of measuring the fiscal health of the Philippines: the national government fiscal balance (NGFB or NGAB for national government account balance), the consolidated public sector financial position (CPSFP or CPSD for consolidated public sector deficit), or the public sector borrowing requirement (PSBR). The NGFB or NGAB which measures the fiscal performance of the national government alone is the one generally understood by policymakers, the media practitioners and the general public. Among the three measures, NGAB is no doubt the narrowest and the least accurate in describing the 'true' fiscal position of the government. The CPSD, on the other hand, is the combined deficits of the national government, the monitored government-owned and controlled corporations, government financial institutions, local governments, and other public sector entities. CPSD is a better measure of the public sector's true state of finances than NGFB. From the economic standpoint, PSBR is perhaps the most relevant measure of fiscal imbalance. It is the deficit of the national government and the 14 monitored corporations less the budgetary assistance to the monitored corporations in the form of equity contributions and net lending. It measures the amount the government has to borrow domestically or externally to finance the combined deficits of the national government and the monitored state corporations.

This paper will present the historical fiscal data by administration during the last 27 years. The administrative periods are as follows: Marcos, 1981 to 1985; Aquino, 1986 to 1992; Ramos, 1993 to 1998; Estrada, 1999 to 2000 and, Arroyo, 2001 to 2007. For the Ramos and Estrada administrations, the attributed periods do not correspond to their exact term of office, 1992 to 1998 and 1999 to 2000, respectively. The fiscal policy of the President is defined by the years the executive drafted and passed the general appropriations act (GAA).

The focus of this study will be on the tax system and spending policy of the government and the way the deficit is financed.

The paper is organized as follows. Section II discusses the revenue performance of five administrations during the past quarter of a century; the performance of the Arroyo administration is ongoing and should be seen as work in progress. Section III discusses the pattern of government expenditures during the last 27 years and the budgetary priorities under different administrations. Section IV discusses the three different measures of fiscal imbalance under four different administrations. The mode of financing the deficit and the levels of public debt during the period under review is discussed in Section V. In Section VI, we summarize the results of a previous study on the economic and fiscal policy determinants of public deficits in the Philippines.<sup>2</sup> The final section discusses some conclusions and implications for policy.

## **II. REVENUE PERFORMANCE**

The government should be able to raise enough resources to finance the needed public goods, social programs for the poor, and priority infrastructure for growth and development. The general policy of the Philippine government regarding tax collection is that "the rule of taxation shall be uniform and equitable. The Congress shall evolve a progressive system of taxation."<sup>3</sup>

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<sup>2</sup> Benjamin E. Diokno, "Economic and Fiscal Policy Determinants of Public Deficits: The Philippine Case," *Discussion Paper No. 0702*, School of Economics, University of the Philippines, February 2007.

<sup>3</sup> Article VI, Sec. 28, Par. 1, The 1987 Constitution of the Republic of the Philippines.

In practice, taxation has multiple objectives. First, raise revenues equitably. If this were the sole objective of government, a progressive tax system is the best option. In principle, progressive taxes are equitable in that those who earn more are taxed more. In addition, the deadweight loss associated with progressive taxes is the least. Furthermore, Brennan and Buchanan (1980) have suggested that a progressive income tax system can control the size of government because it is difficult to collect, hence, there is less to spend. In practice, however, incomplete information and difficulty to administer progressive taxes encourages tax evasion and other distortions.

Still with the objective of raising revenues, higher tax rates should be imposed on goods with relatively low price elasticity. Goods for which demand is relatively price inelastic would provide a stable tax base. This form of tax is called a Ramsey tax. The downside is that many goods with relatively inelastic demand are basic necessities (e.g., rice which is staple food in the Philippines) and constitute a large part of a poor man's budget. This inverse elasticity rule is not the best option if equity is the government's highest priority.

Another objective of tax policy is efficiency, that is, to ensure the proper allocation of resources, with or without externalities. Externalities which could be negative or positive occur when the behavior of one economic agent affects the behavior another economic agent, without such behavior being appropriately priced. Pigouvian taxes try to correct such externalities. Sin tax is an example of taxes used to correct a negative externality. The aim is to alter consumption of certain *bad*s (e.g. cigarettes and alcoholic beverages) by penalizing smokers and drinkers. For a negative externality like carbon monoxide emissions, government requires emissions testing for vehicles before allowing them to be registered. For a positive externality like a largely inoculated population, government provides immunizations as part of their basic health care package; government intervention is in the form of a Pigouvian subsidy (or negative tax).

In designing the appropriate tax system, policymakers should consider some normative aspects such as (a) vertical and horizontal equity and (b) administrative simplicity.

One of the most important practical aspects of tax design, especially in developing countries, is the administrative capacity of government to collect taxes properly. If the government is able and information is complete, then a progressive form of direct tax would be the best taxing scheme. On the other hand, if the revenue collection institution is weak it may be better to depend more on indirect levies like value-added tax (VAT) and excise tax.

There is growing consensus that a tax system should be relatively flat and broad. Broadening the tax base by reducing exemptions permits marginal tax rates to be lower, and flatter, compared to a tax system with a narrow tax base. The trade-off between the tax base and the tax rate arises because the government has a revenue target that it must meet, if not surpass. As will be shown later, during the period under review, measures undertaken to simplify the Philippine tax system in the mid-1980's led to increased tax effort in succeeding periods. However, in late 1990's, the tinkering of the tax system resulted to a decline in tax effort.<sup>4</sup>

In practice, the reduction of tax dispersion and the introduction of VAT may not necessarily lead to the desired increase in tax revenues. In the case of Latin America, the short run revenue goal was not attained with the abovementioned tax reforms. Tax revenues will only grow to the extent that tax administration and compliance improve.<sup>5</sup>

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<sup>4</sup> Diokno (2005)

<sup>5</sup> Edwards (1996)

A final consideration in the design of a tax system is tax elasticity. A tax system should be responsive to changes in the economy. In times of economic growth, tax revenues should increase without having to enact new tax laws or raising existing tax rates. Paderanga (2004) observed that tax buoyancy in the Philippines had stagnated in 1999 and 2000 and attributed it to tax evasion.<sup>6</sup> Diokno (2005) argued, however, that the observed stagnation of tax buoyancy could have been due to other factors, such as: first, the 1996 amendment to the Expanded Value Added Tax (EVAT) law which had the effect of narrowing the VAT base; second, the restructuring of the tax on oil products as part of the oil industry deregulation; and finally, the change in the system of taxation of ‘sin’ products – cigarettes and liquor -- from ad valorem to specific.<sup>7</sup>

TABLE 1  
National Government Account and Primary Balance, 1981-2007  
In percent of GDP

Particulars	1981-85	1986-92	1993-98	1999-2000	2001-07
	Marcos	Aquino	Ramos	Estrada	Arroyo
<b>A. REVENUES</b>	<b>11.7</b>	<b>15.9</b>	<b>18.7</b>	<b>15.7</b>	<b>15.3</b>
1. Tax	10.3	13.1	16.2	14.1	13.2
Direct	2.6	4.1	6.0	6.1	5.9 *
Indirect	3.6	4.8	5.6	4.8	4.0 *
Taxes on International Trade	3.6	4.1	4.5	2.9	2.8
Other Offices	0.5	0.2	0.1	0.3	0.3
2. Nontax	1.4	2.7	2.4	1.6	2.2
<b>B. EXPENDITURES</b>	<b>14.5</b>	<b>18.6</b>	<b>18.9</b>	<b>19.6</b>	<b>18.4</b>
1. Current Operating Expenditures	9.0	14.8	15.3	15.9	15.6
Personal Services	3.5	5.2	6.2	6.8	6.0
Maintenance and Other Operating Expenditures	3.1	2.7	2.3	2.4	1.9
Interest Payments	1.5	5.6	4.0	3.9	5.0
Domestic	1.0	4.1	3.0	2.7	3.2
Foreign	0.6	1.5	1.0	1.2	1.8
Allotment to Local Government Units	0.6	0.6	2.2	2.5	2.4
Petroleum Price Stabilization Fund	0.0	0.1	0.1	0.0	0.0
Subsidies	0.3	0.4	0.3	0.2	0.2
Tax Expenditures	0.0	0.2	0.2	0.1	0.1
2. Capital Outlay	4.9	3.1	3.5	3.6	2.7
Infrastructure and Other Capital Outlays	2.6	2.4	2.7	2.9	1.9
Others	2.2	0.6	0.8	0.7	0.8
3. Net Lending	0.6	0.8	0.1	0.1	0.1
<b>C. NATIONAL GOVERNMENT ACCOUNT BALANCE</b>	<b>(2.8)</b>	<b>(2.8)</b>	<b>(0.2)</b>	<b>(3.9)</b>	<b>(3.1)</b>
<b>D. EXPENDITURES (excluding interest payments)</b>	<b>12.9</b>	<b>13.1</b>	<b>14.9</b>	<b>15.7</b>	<b>13.4</b>
<b>E. PRIMARY SURPLUS/DEFICIT (A-D)</b>	<b>(1.3)</b>	<b>2.8</b>	<b>3.8</b>	<b>0.0</b>	<b>1.9</b>

Source: Department of Budget and Management

\* Average for this administration only includes FY 2001-2006 since FY2007 breakdown for direct and indirect taxes is still unavailable.

<sup>6</sup> Tax buoyancy measures the point elasticity of taxes with respect to changes in GDP.

<sup>7</sup> Diokno (2005)

Tax revenue is a crucial factor in reducing the probability of persistent budget deficits. In the case of the Philippines, there were two major tax reforms during the period under study. The first was the 1986 Tax Reform Program (TRP) and the second was the 1997 Comprehensive Tax Reform Program (CTRP). Diokno (2005) argues that while the 1986 tax reform program contributed significantly to fiscal improvements in the late 1980s and early 1990s, the 1997 CTRP was a major contributor for the progressive decline in tax effort.

During the period under review, the tax effort, defined as taxes as percent of GDP, was at its lowest in 1982(9.9 percent), peaked in 1997 (17.0) and decelerated to a new low of 12.3 percent in 2004. Direct taxes had the largest contribution to total taxes during the last three administrations (Ramos, Estrada and Arroyo). International trade taxes, in percent of GDP, progressively declined largely because of the government's commitment to lower tariffs under various trade liberalization agreements.

During the final years of the Marcos administration, 1981 to 1985, overall revenue effort averaged 11.7 percent while tax effort averaged 10.3 percent.<sup>8</sup> The tax system can be characterized as one that is heavily dependent on indirect taxes and therefore regressive. Indirect taxes and international trade taxes, separately, accounted for about 35 percent of total taxes. A plausible explanation is the nature of the Philippine economy during the period: most import-substituting industries goods were heavily dependent on imported intermediate goods which were the tax bases for import duties and excises. The contribution of direct taxes to total taxes averaged only 25 percent (Table 1).

Recognizing the inherent weaknesses of the tax system, Corazon Aquino, a few months after she took power in 1986, reformed the tax system. Operating under a revolutionary government, Aquino exercised both executive and legislative powers, and consequently succeeded in overhauling the weak tax system with virtually no resistance.

The aim of the 1986 tax reform program (TRP) was to simplify the tax system, make revenues more responsive to economic activity, promote horizontal equity, and promote growth by correcting existing taxes that impaired business incentives.

On the personal income tax system, the dual tax schedules were unified with the lower 0-35 percent schedule adopted for both compensation and professional incomes. To minimize revenue loss and preserve the relative burden of individuals, ceilings on allowable business deductions were proposed and adopted. Unfortunately, due to strong lobby by various professional groups, this complementary measure was not fully implemented. Passive incomes were taxed at uniform rate of 20%, which rendered passive income taxation neutral with respect to investment decisions involving bank deposits and royalty generating ventures. Personal exemptions were increased to adjust for inflation and to eliminate the taxation of those earning below the poverty threshold income. Married taxpayers were given the option to file separate returns which lowered tax burden on married couples by removing the effects of the progressive rates on their combined incomes.

The tax on corporations was simplified. A uniform rate of 35 percent on corporate income replaced the two-tiered corporate tax structure. Tax on inter-corporate dividends was eliminated and the tax on dividends was phased out gradually over a period of three years. The exemptions

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<sup>8</sup> Revenue effort is defined as total revenues as a percent of Gross Domestic Product (GDP) while tax effort is defined as total tax revenues as percent of GDP.



from income taxes of franchise grantees were withdrawn. The imposition of an income tax on franchise grantees put this previously favored group on an equal footing with similarly situated individuals or firms. Uniform franchise taxes were imposed on similar types of utilities.

One of the major reforms designed to simplify the tax structure and its administration was the introduction of the value-added tax (VAT). The new system has the following features: (a) uniform rate of 10% on sale of domestic and imported goods and services and 0% on exports and foreign currency denominated sales; (b) 10% in lieu of varied rates applicable to fixed taxes (60 nominal rates), advance sales tax, tax on original sale, subsequent sales tax, compensating tax, miller's tax, contractor's tax, broker's tax, film lessors and distributor's tax, excise tax on solvents and matches, and excise tax on processed videotapes; (c) 2% tax on entities with annual sales or receipts of less than P200,000; (d) adoption of tax credit method of calculating tax by subtracting tax on inputs from tax on gross sales; (e) exemption of the sale of basic commodities such as agriculture and marine food products in their original state, price regulated petroleum products and fertilizers; (f) additional 20% tax on non-essential articles such jewelry, perfumes, toilet waters, yacht and other vessels for pleasure and sports.

**TABLE 2**  
**Government Revenues, 1981-2007**

As percent of total revenues

Particulars	1981-85	1986-92	1993-98	1999-2000	2001-07
	Marcos	Aquino	Ramos	Estrada	Arroyo
<b>1. Tax</b>	<b>88.0</b>	<b>82.7</b>	<b>87.0</b>	<b>89.8</b>	<b>86.0</b>
Direct	25.4	30.8	37.2	43.5	45.5 *
Indirect	35.0	36.9	34.2	33.7	31.0 *
Taxes on International Trade	34.9	30.9	27.8	20.4	21.0
Other Offices	4.7	1.4	0.8	2.4	2.5
<b>2. Nontax</b>	<b>12.0</b>	<b>17.3</b>	<b>13.0</b>	<b>10.2</b>	<b>14.0</b>

Source: Department of Budget and Management

MEMO ITEM:

1. The share of tax and nontax revenue are as a percent of total revenues.
2. Items under tax revenue are computed as the share of total tax revenue.

\* Does not include FY 2006-07 since BIR revenue collection breakdown between direct and indirect taxes are unavailable.

As a result of the 1986 tax reform program, average tax effort rose to 13.1 percent during the Aquino administration (1986-1992) and to 16.2 percent during the Ramos administration (1993-1998). Revenue effort rose steadily until the next round of tax reforms. Tax effort increased from 10.7% in 1985 to 15.4% in 1992, then peaked at 17.0% in 1997. The share of direct taxes to total taxes increased while that of trade taxes decreased. Income taxes could have performed better, and the tax system's fairness enhanced, had BIR implemented fully the approved reform imposing ceilings on allowable deductions. Overall responsiveness of the tax system to changes in economic activity improved from an average of 0.9% from 1980-1985 to an average of 1.5% from 1986 to 1991. The buoyancy coefficient for import duties rose from an average of 0.5% before the reform to an average of 1.89% from 1986 to 1991

The share of nontax revenues soared to 17.3 percent of total revenues during the Aquino years owing to the sale of sequestered assets of former President Marcos and his cronies.<sup>9</sup> With government's thrust toward privatization, 30 percent of outstanding stocks of the Philippine National Bank were offered to the public and listed in the stock exchange in 1989.<sup>10</sup> In addition, as an initial effort to deregulate the oil industry, the Philippine National Oil Company was partially privatized in 1994. A minority but significant share of ownership was sold to the Saudi Arabian Oil Company.<sup>11</sup>

The 1986 tax reform program resulted in higher tax effort that peaked in 1997. Attempts were made to improve upon this tax performance by reforming the tax system in 1997. The objectives of the 1997 Comprehensive Tax Reform Program (CTRP) are the following: (a) make the tax system broad-based, simple and with reasonable tax rates; (b) minimize tax avoidance allowed by existing flaws and loopholes in the system; (c) encourage payment by increasing the exemption levels, lowering the highest tax rate, and simplifying procedures; and (d) rationalize the grant of tax incentives which equaled P31.7 billion in 1994.

The main features of the 1997 CTRP are as follows. First, after a brief experiment with the Simplified Net Income Taxation or SNITS that was legislated in 1992, the income tax system reverted to a uniform rate schedule for both compensation and professional income of individuals. The rate structure was reduced to 7 brackets. Personal and additional exemptions were increased even as it allowed the deduction of premium payments for health and/or hospitalization insurance from gross income. Second, the corporate income tax (CIT) rate was reduced to 34%, but effective 1 January 1999, the rate was reduced to 33% and on 1 January 2000 and onwards was decreased to 32%. Third, minimum corporate income tax (MCIT) will be imposed beginning on the fourth year from the time a corporation commences the business operations. Fourth, fringe benefits granted to supervisory and managerial employees shall be subject to a tax equivalent to the applicable CIT rate of the grossed-up monetary value of the fringe benefit.

Fifth, Republic Act 8241 (Improved VAT Law) amended the coverage of RA 7716 (Expanded VAT Law). The major changes as a result of the amendment are the following: (i) restore the VAT exemptions for cooperatives (agricultural, electric, credit or multi-purpose, and others provided that the share capital of each member does not exceed P15,000); (ii) expanded the coverage of the term "simple processes" by including broiling and roasting; (iii) expanding the coverage of the term "original state" by including molasses; (iv) exempting from the VAT the following: importation of meat; sale or importation of coal and natural gas in whatever form or state; educational services rendered by private educational institutions duly accredited by CHED; house and lot and other residential dwellings valued at P1 million and below, subject to adjustment using CPI; lease of residential units with monthly rental per unit of not more than P8,000, subject to adjustment using CPI; and sale, importation, printing or publication of books and any newspaper. In effect, the VAT tax base was narrowed rather than broadened.

Sixth, as part of the legislation deregulating the downstream oil industry, taxes on oil products were restructured from ad valorem to specific taxation. The overall effect of the reform was to lower taxes on oil products, including zero tax on liquefied petroleum gas (LPG).

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<sup>9</sup> Diokno (1995)

<sup>10</sup> <http://www.pnb.com.ph/history.asp>

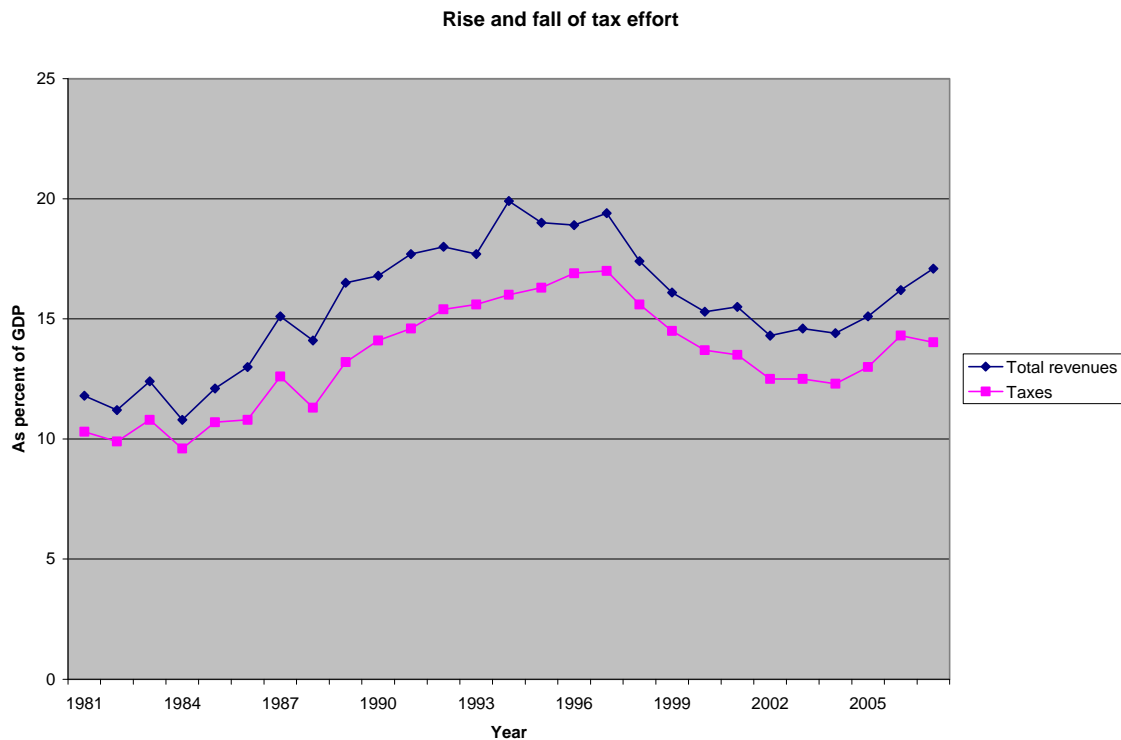
<sup>11</sup> Sicat (2003)

Finally, the tax on ‘sin’ products – cigarettes and liquor – was restructured from ad valorem to specific. The advantage of an ad valorem tax is that it factors in price changes, thus revenues adjust with price changes (usually increases) without need for new tax legislation. As a compromise, and to minimize the potential revenue loss, some form of indexation was introduced. However, the process of implementation is unrealistic and impractical since the adjustment process would still require congressional imprimatur.

In sum, what came out of Congress was a water-down version of the original 1997 CTRP program. Congress failed to pass the crucial rationalization of fiscal incentives and the broadening of the value-added tax base. Worse, the Tenth Congress passed 9 tax laws granting incentives and raising exemptions. The reason for this unwanted outcome was the delay in the approval of the 1997 CTRP tax proposals and the subsequent posturing of politicians who were then aspiring to run in the 1998 national and local elections. Some measures which were legislated were not even implemented, such as, the VAT on banks and financial intermediaries, the tax on fringe benefits, and the minimum corporate income tax.

The most serious negative consequence of the 1997 CTRP program was the progressive deterioration of the tax effort -- from a peak of 17 percent before the reform to its level of 12.3 percent in 2004. The peaks and troughs of tax and revenue efforts in the Philippines are shown in Figure 2 below.

**FIGURE 2**  
**Tax and Revenue Effort, 1981-2007**  
*As percent of GDP*



Direct tax revenue became the primary contributor of tax effort with a share of 37 percent. Indirect tax revenue, with a 34 percent share, was a close second. While privatization efforts continued, including the sale of Petron<sup>12</sup> in 1994, the share of nontax revenues dropped to 13 percent for this period. The Manila Waterworks and Sewerage System (MWSS) was also privatized in 1997 to 1998 giving two private companies twenty-five year concessionaires for managing their respective areas, a downsized MWSS maintaining its regulatory function.<sup>13</sup>

During the Ramos administration, after a series of tax legislation, the tax base became narrower. Congress passed, and the President approved, 10 new tax measures that raised revenues and 28 tax measures that decreased revenues through the grant of incentives and higher exemptions. Among these measures is the Expanded Value-Added Tax Law (E-VAT) that was subsequently amended by Republic Act 8241. The E-VAT sought to widen the VAT tax base. However, various law suits challenging its constitutionality led to its amended version that reversed E-VAT's original intention, leading to increased exemptions from VAT.

During the truncated Estrada administration, overall revenue effort and tax effort decreased to 15.7 percent and 14.1 percent, respectively. The share of direct taxes to total taxes rose to 43.5 percent while the share of indirect taxes was practically unchanged. The share of trade taxes dropped sharply, however. (Table 2) Tax buoyancy, which measures the point elasticity of taxes with respect to changes in GDP, stagnated in 1999 and 2000.<sup>14</sup> The decrease in overall tax effort and tax buoyancy can be partly attributed to the new and revised tax laws enacted during the Ramos administration.

The decrease in international trade taxes as percent of GDP, from an average of 4.5 to 2.9 percent, was not surprising. It was a consequence of the trade liberalization and globalization efforts in the 1990s. This began with the growth of trade cooperation in the Association of Southeast Asian Nations (ASEAN) with the ASEAN Free Trade Agreement (AFTA) in 1992. Furthermore, the Philippines joined the World Trade Organization (WTO) in 1994 and the Asia Pacific Economic Cooperation (APEC).

During the Estrada administration, Congress passed Republic Act No. 8761 that imposed value-added tax on certain services that were previously exempt from VAT. This was passed in February 2000, prior to the impeachment proceedings of President Estrada. In February 2001, a month after Arroyo replaced Estrada, the same Congress, pursuant to Republic Act No. 9010, subsequently deferred this expansion of the VAT tax base. This policy reversal has contributed to the decrease in tax effort in succeeding years.

During the Arroyo administration, direct, indirect and international tax effort decreased with overall tax effort dropping to an average of 13.2 percent for the period 2001-07. Only nontax effort defied the fall, inching up by an average of 0.6 percent. This, however, is not a reason to cheer since nontax revenues are largely proceeds from privatization which are not a sustainable source of income.

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<sup>12</sup> Petron is the oil refinery and marketing subsidiary firm of the state-owned Philippine National Oil Company (PNOC).

<sup>13</sup> The 1997 Asian financial crisis affected the success of this privatization effort since the contracts did not include a mechanism for foreign exchange adjustments. This resulted in a sharp increase in water rates, and finally, one of the two concessionaires was turned over to the MWSS regulatory office.

<sup>14</sup> Paderanga (2004)

In 2004, one of the services, bank and non-bank financial intermediaries not performing quasi-banking functions, which was included in the deferred imposition of VAT in RA 8761, was subject instead to gross receipts tax. In 2005, two new tax laws were enacted. First, Republic Act 9334 imposed biennial increases of the excise taxes on liquor and tobacco until 2011. Taxes on distilled spirits, wines and fermented liquor are in specific amounts upon effectivity of the law in 1 January 2005. Taxes are to be automatically adjusted every two years beginning 1 January 2007 until 1 January 2011. Taxes on tobacco products are a combination of ad valorem and specific taxes. Ad valorem taxes are imposed only on cigars with rates ranging from 10 percent to PhP 50 plus 15 percent if the net (excluding VAT and excise tax) retail price per cigar is greater than PhP 500. Tobacco products are subject to a specific tax of PhP 1 per kilogram of tobacco product subject to a 6 percent increases every two years. Cigarettes packed by hand or machine have specific taxes that are subject to specific increases biennially.

Second, Republic Act 9337 amended several provisions in the 1997 National Internal Revenue Code (NIRC). The most significant amendment was the increase in the VAT rate from 10 percent to 12 percent. The corporate income tax rate was raised to 35% until 2008 and then will decrease to 30% starting 2009. Another important provision is the earmarking of incremental revenues from RA 7660 (Documentary Stamps Tax); RA 8240 (Excise Tax on Tobacco Products) and the newly increased VAT. The VAT increase may partly explain the increase in indirect taxes as a percent of GDP from 3.6 percent in 2004 to 4.7 percent in 2006 (Appendix A).

What lessons have been learned from the two major tax reforms during the last quarter century? First, tax reforms should be done at the start, not towards the end, of any administration. The implication is that the incoming administration should be ready with a core of tax proposals within months of its assumption to office. Second, the probability of success of a tax reform program is enhanced if it is presented as a critical component of a comprehensive public sector reform program. Third, future tax reform programs should aim to recover what was lost in the area of corrective taxation. Taxes from goods with negative externalities – that is, cigarettes, liquor and petroleum products – used to account for a large part of total taxes. In recent years, the share of these taxes has been eroded. Fourth, ad valorem system of taxation is superior to specific taxation in an environment where getting new taxes and upward adjustment of existing taxes are difficult to legislate. A consistent policy is to broaden the base of the value added tax which, by definition, is ad valorem in character to include practically all commodities, including cigarettes, liquor and oil products.

Fifth, tax reforms require broad political support: from the Executive Department, legislature, business community and the citizenry. A joint legislative-executive tax commission<sup>15</sup> should be reconstituted by law in order to develop broad multi-party support for tax legislation, and in order to minimize the delay in developing a tax reform package at the start of every administration.

Sixth, presidential leadership is crucial in the design and legislative authorization of a tax system. The president should be willing to exercise his broad powers in order to develop an appropriate tax system. He should not allow his own men and members of Congress to unnecessarily tinker with the tax structure if it is not defective. At the same time, when presented with flawed tax legislation, the President should be willing to use his veto power, including line-item veto.

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<sup>15</sup> Before martial law was declared in 1992, there used to be such a joint legislative-executive tax commission (JLETC). During the martial law years, with the closure of Congress, a purely executive tax body, the National Tax Research Center, replaced it which is under the Department (Ministry) of Finance.

### III. GOVERNMENT EXPENDITURE: PATTERN AND PRIORITIES

Government expenditure is the primary policy instrument used by government to direct the economy to a path of growth and development. Government spending, as authorized in the national budgets, is expected to reflect national priorities. There is no universal prescription as to the appropriate size and distribution of the national budget. But the level of spending on government programs and activities depends on the priorities and preferences of policymakers (the legislature and the President). However, there are several core functions which any government is expected to provide: public goods, such as national defense, conduct of foreign policy, administration of justice, and the maintenance of peace and order.

Economic growth theory emphasizes the importance of capital accumulation in the attainment of economic growth -- the higher the stock of capital, the higher the level of economic output in the long-run. Governments invest in physical infrastructure in order to increase the productive capacity of an economy. Government spending on public infrastructure reduces transaction costs for businesses and signals the commitment of government to ensure profitability for prospective investors. In a study by the World Bank, Philippine investment in physical infrastructure for the year 2005 was less than 2 percent of GDP – a level that is considerably lower than the World Bank prescribed 5 percent of GDP to lead to a sustainable economic growth.<sup>16</sup>

In practice, government also provides goods and services that are private in nature, the so-called publicly provided private goods. Examples of these are education, basic health care and housing. This spending behavior could be justified on several grounds. First, as part of the redistributive role of government, providing education for all enhances the changes of the poor to get better employment and consequently higher income. Second, there are positive externalities associated with a well-educated and healthy population. Finally, these education and basic health care are considered as investment in human capital that is crucial for economic growth and development.<sup>17</sup>

Another policy direction that is believed to have an effect on national government financial health is fiscal decentralization. In theory, it is argued that compared to national officials, local authorities are more attuned to the preferences of their constituents and that they make decisions based on the preferences of their local constituencies.<sup>18</sup> Moreover, increased spending and revenue-raising responsibilities for local governments enhances accountability. Fiscal decentralization allows the national government to focus on broader issues such as interjurisdictional externalities and income redistribution.

Serious decentralization efforts took place in the Philippines after 1992. The 1991 Local Government Code of the Philippines was enacted with the aim of creating self-reliant local governments. In general, there is a mismatch between revenue raising and spending

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<sup>16</sup> World Bank [2005].

<sup>17</sup> Most governments may not have enough resources to provide such goods. In order to enhance efficiency, government must resort to handles, other than taxes, such as user fees.

<sup>18</sup> The theory of local public good argues that efficiency is enhanced through a process by which constituents reveal their true preferences for local public goods by 'voting-with-their-feet,' i.e. citizens move to the locality that offers their most preferred taxing-expenditure mix.

responsibilities, owing to variations in the tax base and the unequal distribution of income across local governments; this provides the rationale for intergovernmental fiscal transfers (IGFTs). In the Philippines, the IGFTs -- called internal revenue allotment (IRA) -- is largely an unconditional block grant, except for 20% which is required to be allocated to development purposes. The total IRA is 40% of all internal revenue, based on actual collections in the third preceding fiscal year.

What has been the level of public expenditures and its distribution during the last quarter century? The following observations appear warranted.

*First, government expenditures as percent of GDP has declined in recent years.* From an average percentage share of 14.5 percent during the final years of Marcos, spending peaked at 19.6 percent during the Estrada administration, and then dropped to 18.4 percent in recent years (Table 1).

*Second, investment in public infrastructure has been less than optimal, and has declined in recent years.* Ideally, an increasing share of the budget should be allocated for public infrastructure that is needed to increase the economic capacity for growth of a country. During the final years of the Marcos regime, one-third of the budget was spent on capital outlays.<sup>19</sup> The share of capital expenditure dropped sharply to an average of 3.1 percent of GDP during the Aquino administration, as the government allocated a big part of its budget for the servicing of public debt incurred during the Marcos years. Infrastructure and other capital outlays in percent of GDP declined slightly from 2.6 percent during Marcos' final years to 2.4 percent during the Aquino years. It rose to 2.7 percent during the Ramos years and 2.9 percent during and Estrada years, before hitting a historic low of 1.9 percent during the Arroyo administration. According to a World Bank report, Philippines: Meeting Infrastructure Challenges (2005), "middle income countries in East Asia will, on average, need to spend over 5 percent of GDP on infrastructure to meet their needs over the next 10 years." The figures show that the Philippines are far from this target.

### **A. Government Spending by Object of Expenditures**

*Third, current operating expenditures as share of total budget has progressively increased.* It rose sharply from 62.7 percent during Marcos' final years to 84.9 percent during the Arroyo years. It averaged around 80 percent during the terms of Aquino, Ramos and Estrada (Table 3). Personal services consistently received the largest share with an average of 39.3 percent for the entire period under study. Spending on personal services consist mainly salaries and wages of government employees and other benefits. As percent of the budget, personal peaked during the Estrada years (an average of 42.5 percent). Maintenance and other operating expenditures, as percent of total expenditures, progressively declined from 34.3 percent during the Marcos years to 12.1 percent during the Arroyo years. This is alarming because funds for maintaining existing infrastructure fall under this budgetary item. The financial grant to local governments has increased significantly with the approval of the 1991 Local Government Code. The decentralization law of 1991 devolved some functions to local governments and increased the local governments taxing powers.

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<sup>19</sup> The term capital outlay is not exactly equal to infrastructure spending. It is a broader term that includes: (a) infrastructure and other capital outlays; (b) corporate equity; (c) capital transfers to local government units; (d) capital transfers to the Philippine National Bank and Development Bank of the Philippines; and, (e) comprehensive agrarian reform program land acquisition and credit.

Fourth, debt servicing has been an increasing drag on the productive part of the budget. Interest payment as percent of the budget was highest during the Aquino years (an average of 37.6 percent). However, there has been a steady improvement during the Ramos and Estrada years, as the share of interest rates to total budget declined to 26.4 percent and 24.4 percent, respectively. Unfortunately, the decline has been reversed -- the budget share of interest payment has risen to 32 percent during the Arroyo years.

TABLE 3  
**National Government Spending, by Object, 1981-2007**  
*As percent of total expenditures*

Particulars	1981-85	1986-92	1993-98	1999-2000	2001-07
	Marcos	Aquino	Ramos	Estrada	Arroyo
<b>1. Current Operating Expenditures</b>	<b>62.7</b>	<b>79.2</b>	<b>80.7</b>	<b>81.3</b>	<b>84.8</b>
Personal Services	39.0	35.5	40.7	42.5	38.1
Maintenance and Other Operating Expenditures	34.3	18.6	14.9	15.0	12.1
Interest Payments	17.1	37.6	26.4	24.4	32.0
Domestic	60.5	72.8	74.1	68.5	63.6
Foreign	39.5	27.2	25.9	31.5	36.4
Allotment to Local Government Units	6.7	4.1	14.1	15.8	15.7
Petroleum Price Stabilization Fund	0.0	0.4	0.5	0.1	0.0
Subsidies	2.8	2.7	2.1	1.3	1.3
Tax Expenditures	0.0	1.2	1.4	0.9	0.8
<b>2. Capital Outlay</b>	<b>33.2</b>	<b>16.5</b>	<b>18.6</b>	<b>18.3</b>	<b>14.7</b>
Infrastructure and Other Capital Outlays	52.9	82.1	77.4	81.4	71.8
Others	47.1	17.9	22.6	18.6	28.2
<b>3. Net Lending</b>	<b>4.1</b>	<b>4.4</b>	<b>0.7</b>	<b>0.5</b>	<b>0.5</b>

Source: Departement of Budget and Management

Notes:

1. For the major categories, the computed share is in percentage of total national government expenditures.
2. For the sub-categories – current operating expenditures (COE) and capital outlays (CO) -- the share is as a percentage of total COE and CO, respectively. Furthermore, for the item Interest Payments, the share of domestic and foreign is as a percentage of total interest payments.

## B. Sectoral Priorities

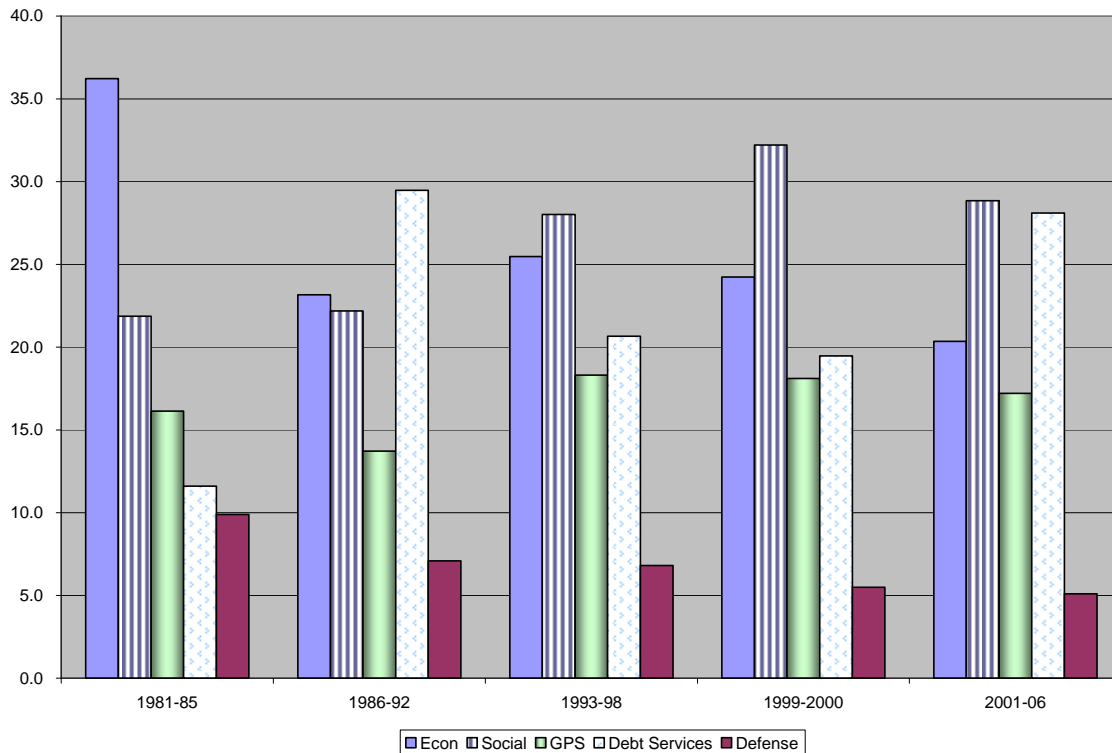
Fifth, government expenditure for economic services peaked during the final years of Marcos, declined during the Aquino years, and after a slight recovery during the Ramos and Estrada years, it hit rock bottom during the Arroyo administration. Economic Services include: (a) agriculture, agrarian reform and natural resources; (b) trade and industry; (c) tourism; (d) power and energy; (e) water resource development and flood control; (f) communications, roads and other transportation; (g) other economic services; and, (h) Subsidy to Local Government Units. The largest part of this sector's spending went to infrastructure with an average of 41 percent going to communications, roads and other transportation (CRT). Agriculture, agrarian reform and natural resources and other economic services tie as the second top priority for this economic sector. In recent years, CRT continued to have the largest share of economic sector spending with subsidy to local government units coming in second. The subsidy to local government units, as percent of GDP, increased from 0 to 1.1 percent as a result of the 1991 Local Government Code which devolved basic services to local governments, such as: agricultural extension and



on-site research; community based forestry projects; tourism facilities, promotion and development; and, telecommunication services.

**FIGURE 3**  
**Budget Priorities: Debt Service Rising, Social and Economic Services Falling**

*As percent of total expenditures*



Sixth, in general, the share of social services to total government spending has been increasing; but during the Arroyo administration, spending for social services as percent of GDP, dropped to 5.3 percent of GDP from an all-time high of 6.4 percent during the preceding regime. Social services sector consists of: (a) education, culture and manpower development; (b) health; (c) social security and labor welfare; (d) land distribution (CARP); (e) housing and community development; (f) other social services; and, (g) subsidy to local government units. During the period under review, education, culture and manpower development had consistently received the lion’s share of government spending for this sector. Education spending spiked at 65 percent of social services spending during the Aquino administration, but has been decreasing ever since; under Arroyo’s watch (2001-2007) it fell to a historic low of 53 percent. On the other hand, expenditures for social security and labor welfare and subsidy to local government units (SLGUs) increased significantly. Social security and labor welfare increased in recent years because of the Personnel Benefits Fund established for the retirement fund of uniformed personnel. For SLGUs, the initial share of 0 has increased to 21 percent because of social expenditure responsibilities devolved to local governments (primarily, basic health care and social welfare services) and intergovernmental transfers.

Seventh, there was no clear pattern for the expenditures for General Public Services. Spending for this sector peaked during the Ramos administration with an 18.3 share of total government spending.

TABLE 4  
Sectoral Shares of National Government Expenditure, 1981-2006

Particulars	1981-85	1986-92	1993-98	1999-2000	2001-06
	Marcos	Aquino	Ramos	Estrada	Arroyo
<b>I. As share of national government spending</b>					
<b>A. Economic services</b>	<b>36.2</b>	<b>23.2</b>	<b>25.5</b>	<b>24.2</b>	<b>20.3</b>
Agriculture, Agrarian Reform & Natural Resources	19.3	26.6	25.7	22.3	23.4
Trade & Industry	7.6	5.1	4.2	2.5	2.0
Tourism	0.8	0.6	0.7	0.8	0.7
Power and Energy	8.1	4.8	3.2	1.7	1.0
Water Resource Development & Flood Control	3.6	5.5	4.0	3.5	4.4
Communications, Roads & Other Transportation	41.0	39.8	39.9	42.2	38.3
Other Economic Service	19.5	14.9	3.1	3.0	1.6
Subsidy to Local Government Units	0.0	2.6	19.3	23.9	28.7
<b>B. Social Services</b>	<b>21.9</b>	<b>22.2</b>	<b>28.0</b>	<b>32.2</b>	<b>28.8</b>
Education, Culture & Manpower Development	60.8	65.1	60.3	56.1	52.9
Health	20.2	16.4	9.2	7.3	5.7
Social Security & Labor Welfare	4.2	4.2	8.7	12.6	17.1
Land Distribution (CARP)	0.0	1.4	0.0	1.4	1.7
Housing & Community Development	11.0	2.2	2.5	3.0	0.9
Other Social Services	3.8	8.4	0.5	0.4	0.4
Subsidy to Local Government Units	0.0	2.2	18.7	19.1	21.4
<b>C. Defense</b>	<b>9.9</b>	<b>7.1</b>	<b>6.8</b>	<b>5.5</b>	<b>5.1</b>
<b>D. General Public Services</b>	<b>16.1</b>	<b>13.7</b>	<b>18.3</b>	<b>18.1</b>	<b>17.2</b>
<b>E. Net Lending</b>	<b>4.3</b>	<b>4.4</b>	<b>0.7</b>	<b>0.5</b>	<b>0.4</b>
<b>F. Debt Service (Interest Payments)</b>	<b>11.6</b>	<b>29.5</b>	<b>20.7</b>	<b>19.5</b>	<b>28.1</b>
<b>II. In percent of GDP</b>					
<b>A. Economic services</b>	<b>5.1</b>	<b>4.4</b>	<b>5.0</b>	<b>4.8</b>	<b>3.7</b>
Agriculture, Agrarian Reform & Natural Resources	1.0	1.2	1.3	1.1	0.9
Trade & Industry	0.4	0.2	0.2	0.1	0.1
Tourism	0.0	0.0	0.0	0.0	0.0
Power and Energy	0.5	0.2	0.2	0.1	0.0
Water Resource Development & Flood Control	0.2	0.2	0.2	0.2	0.2
Communications, Roads & Other Transportation	2.1	1.7	2.0	2.0	1.4
Other Economic Service	0.9	0.7	0.2	0.1	0.1
Subsidy to Local Government Units	0.0	0.1	1.0	1.2	1.1
<b>B. Social Services</b>	<b>3.0</b>	<b>4.2</b>	<b>5.5</b>	<b>6.4</b>	<b>5.3</b>
Education, Culture & Manpower Development	1.8	2.7	3.3	3.6	2.8
Health	0.6	0.7	0.5	0.5	0.3
Social Security & Labor Welfare	0.1	0.2	0.5	0.8	0.9
Land Distribution (CARP)	0.0	0.1	0.0	0.1	0.1
Housing & Community Development	0.3	0.1	0.1	0.2	0.0
Other Social Services	0.1	0.3	0.0	0.0	0.0
Subsidy to Local Government Units	0.0	0.1	1.0	1.2	1.1
<b>C. Defense</b>	<b>1.4</b>	<b>1.3</b>	<b>1.3</b>	<b>1.1</b>	<b>0.9</b>
<b>D. General Public Services</b>	<b>2.2</b>	<b>2.6</b>	<b>3.6</b>	<b>3.6</b>	<b>3.1</b>
<b>E. Net Lending</b>	<b>0.6</b>	<b>0.8</b>	<b>0.1</b>	<b>0.1</b>	<b>0.1</b>
<b>F. Debt Service (Interest Payments)</b>	<b>1.5</b>	<b>5.6</b>	<b>4.0</b>	<b>3.9</b>	<b>5.1</b>

Source: Government Authorities

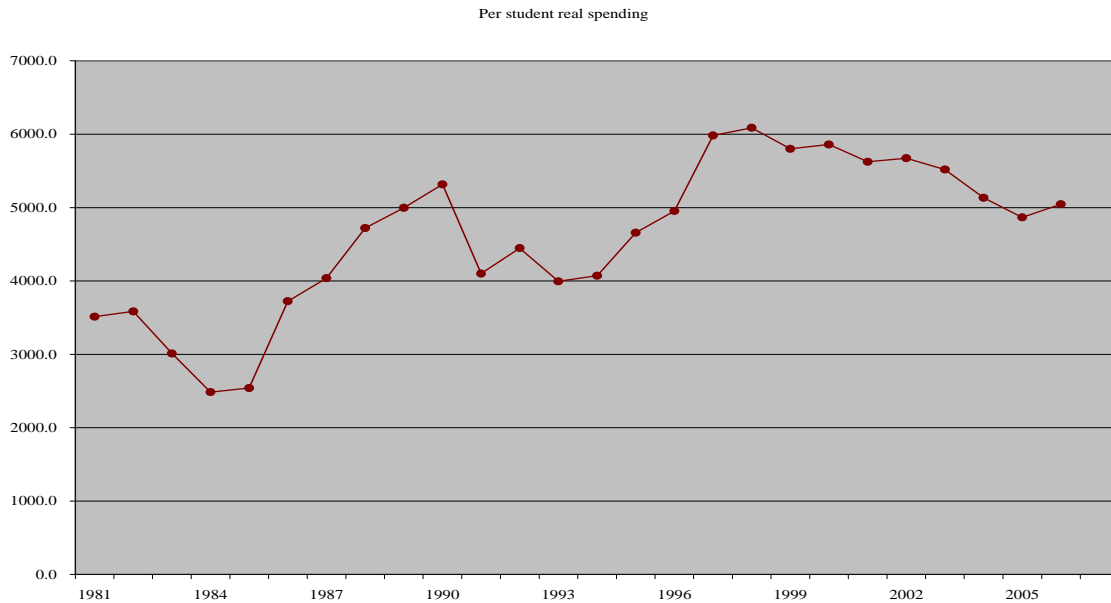
MEMO ITEMS:

1. In Section I: (a) subtotals for sectors (*italicized*) are as a share of total NG expenditures.  
(b) sub-sector shares are a percent of respective total sector spending

*Eighth, real per pupil spending on basic education has been on the rise since Aquino took power in 1986, peaked during the Estrada administration, but has been falling at an average rate of 2.4 percent per year from 2001 to 2007. In nominal terms, total education expenditure and per pupil spending has increased. But correcting for inflation, real per pupil government spending on basic*

education has been on the decline under the Arroyo administration (Figure 4). Growth in total nominal spending for basic education spending has slowed down during the past two administrations from a high of 15.6 percent, in the early 1980s, to a current low of 3 percent.<sup>20</sup>

**FIGURE 4**  
**Waning Support for Basic Education**  
*Real per pupil spending in 2000 prices*



**TABLE 5**  
**Average National Government Basic Education Spending,**  
**By Administration, 1981-2006**

<sup>20</sup> Basic education spending refers only to the actual expenditures of the Department of Education, Culture and Sports. Source of basic data: the Department of Budget and Management (DBM), Fiscal Statistics Handbook, 2005.

Particulars	1981-85	1986-92	1993-98	1999-2000	2001-06
	Marcos	Aquino	Ramos	Estrada	Arroyo
<b>I. Basic Education Spending</b>					
A. Total spending					
1. In current prices	5,653	21,873	54,651	89,773	106,760
2. In 2000 prices	30,042	52,626	69,969	91,484	89,419
B. Per Pupil spending					
1. In current prices	565	1,836	3,847	5,720	6,324
2. In 2000 prices	3,027	4,478	4,959	5,830	5,304
<b>II. Growth rates</b>					
A. Total spending					
1. In current prices	15.6	23.2	17.9	5.4	4.2
2. In 2000 prices	(5.7)	13.4	9.0	0.5	(1.2)
B. Per Pupil spending					
1. In current prices	13.7	19.5	14.5	3.0	3.0
2. In 2000 prices	(7.3)	10.0	5.8	(1.9)	(2.4)

SOURCE: DBM, NSCB

MEMO ITEM: Enrolment figures were computed as an average of two succeeding school years.

Sources: Department of Budget and Management, National Statistical Coordination Board

*Ninth, real consolidated (national plus local governments) health spending, decreased during the period 2001 to 2005 – both in total and per capita terms.* Real consolidated health spending contracted at an average of 4.6 percent while real consolidated per capita health spending has contracted at an average of 5 percent. Real national government health spending, both in total and in per capita terms, which had peaked during the Aquino administration had hit its lowest level during the Arroyo administration. It may be argued that the recent decline is to be expected because of the devolution of basic health services to local governments. But real local government health spending has decreased in recent years -- by 4 percent per year since Arroyo took office.

#### FIGURE 5

#### **Failing Support for Basic Health Care, 1981-2005**

*Real per capita basic health expenditures, in 2000 prices*

Deteriorating per capita health spending

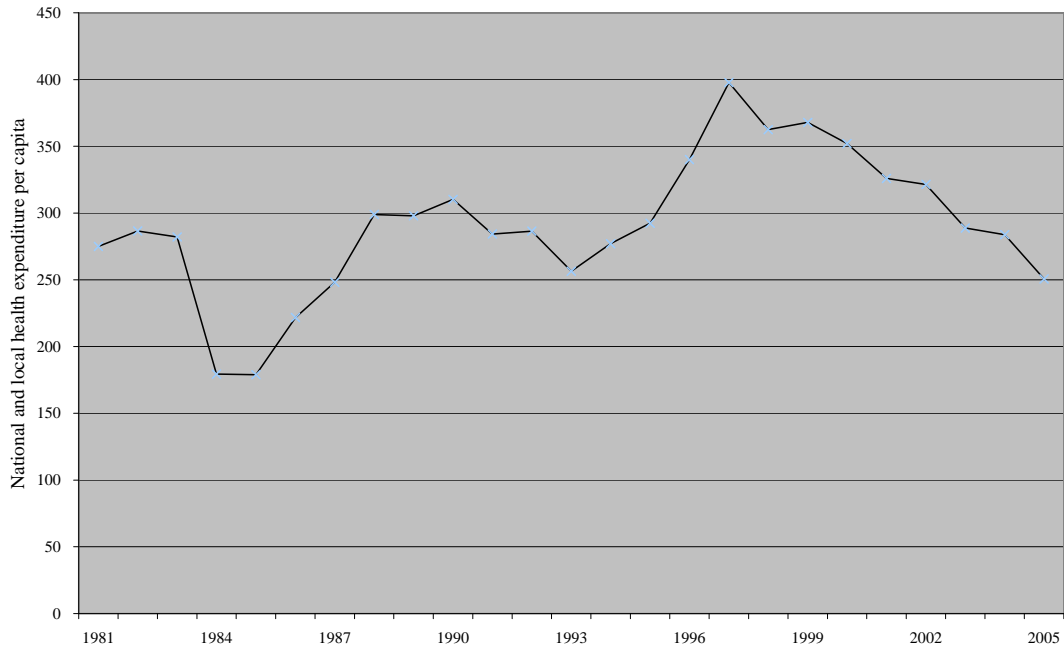


Table 6 shows the pattern of consolidated health spending – that is, for both national and local governments. In current prices, total consolidated health spending has been consistently increasing along with the share local governments. This change in the mix of consolidated health spending, with local government spending overtaking that of the national government, can partly be attributed to the 1991 Local Government Code that devolved the responsibility of Field Health and Hospital and other Tertiary Health Services.<sup>21</sup>

The current trend of health spending has been unsatisfactory. The average growth rates for all of the categories of health spending have been decreasing in recent years. The negative growth in real health spending by local governments combined with the sharp decline in real national health spending show the government’s lack of commitment to better health care (Table 6).

**TABLE 6**  
**Consolidated (National and Local) Government**  
**Health Expenditure, 1981-2005**  
*Average by administration*

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<sup>21</sup> Nolleto, Jose N., ed., *The 1991 Local Government Code with Basic Features*, Metro Manila, Philippines: National Book Store, Inc. 1995.

Particulars	1981-85	1986-92	1993-98	1999-2000	2001-05
	Marcos	Aquino	Ramos	Estrada	Arroyo
<b>I. Total expenditures</b>					
<b>A. Consolidated Health Spending</b>					
1. In current prices (in Million pesos)	2,293	6,945	17,382	26,791	27,699
a. National government	1,931	6,187	8,586	11,835	10,734
b. Local government	362	757	8,797	14,956	16,965
2. In 2000 prices (in Million pesos)	12,416	16,637	22,359	27,315	23,945
a. National government	10,480	14,803	11,096	12,081	9,295
b. Local government	1,936	1,834	11,263	15,234	14,650
<b>B. Consolidated Per Capita Health Spending</b>					
1. In current prices	44	115	249	354	340
a. National government	37	102	123	156	132
b. Local government	7	13	126	197	208
2. In 2000 prices	240	278	321	360	294
a. National government	203	247	160	159	114
b. Local government	37	31	161	201	180
<b>II. Growth rates</b>					
<b>A. Consolidated Health Spending</b>					
1. In current prices	12.9	20.1	15.8	5.9	0.5
a. National government	13.3	21.1	6.4	0.6	(1.0)
b. Local government	12.3	14.5	68.8	10.6	1.8
2. In 2000 prices	(6.4)	10.0	7.0	0.9	(4.6)
a. National government	(5.8)	11.0	(1.5)	(4.2)	(6.0)
b. Local government	(8.0)	4.6	54.8	5.5	(3.4)
<b>B. Consolidated Per Capita Health Spending</b>					
1. In current prices	10.4	17.4	13.2	3.5	(0.6)
a. National government	10.8	18.3	4.0	(1.6)	(1.8)
b. Local government	9.8	11.8	65.0	8.1	0.5
2. In 2000 prices	(8.5)	7.5	4.6	(1.4)	(5.2)
a. National government	(8.0)	8.4	(3.7)	(6.4)	(6.3)
b. Local government	(10.1)	2.2	51.3	3.0	(4.1)

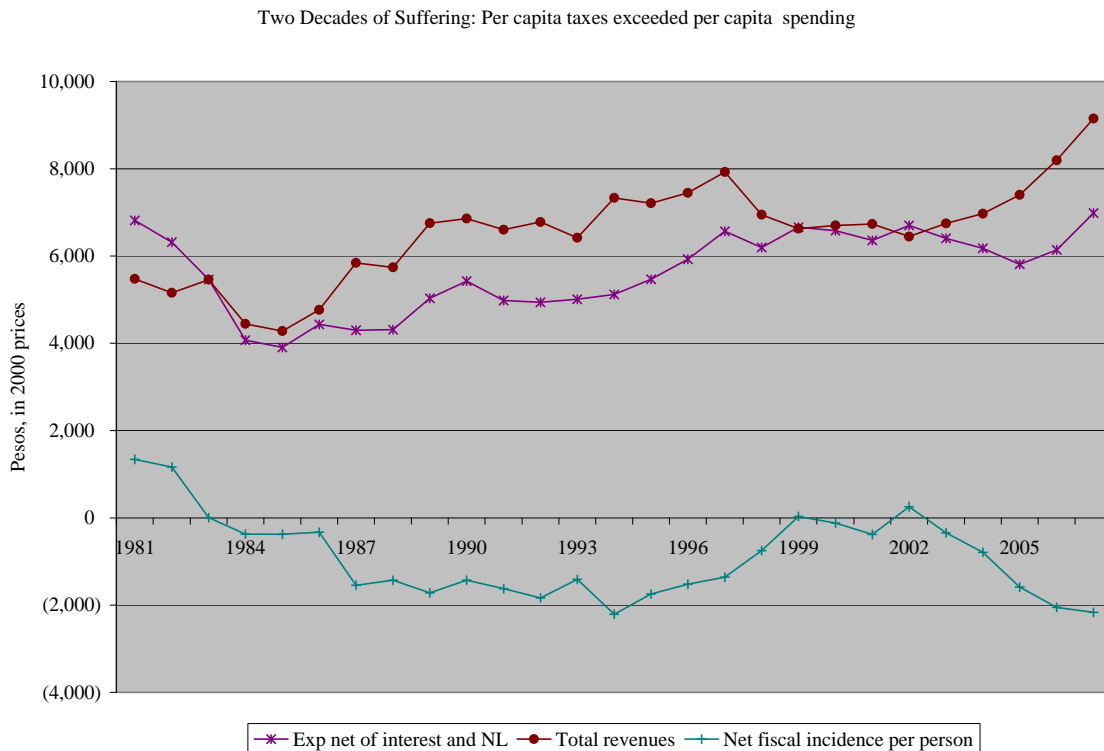
Source: Government authorities

### C. Net Fiscal Impact

What is the net impact of government spending and taxing policies on a representative citizen? A rough approximation of the net effect of government fiscal action on a representative citizen can be derived by deducting from the average 'productive' part of the government spending (that is, total disbursement less debt service and net lending<sup>22</sup>) average revenue. If positive, the representative has received more benefits from government expenditure than what he has paid in taxes or user charges; if negative, he has paid more in taxes and user charges than what he has received in terms of benefits from government programs and projects. Figure 6 indicates that during the past quarter of a century, the representative Filipino had been a net contributor to rather than a net recipient of government services, except for two years, 1999 and 2002. This negative experience for a representative Filipino has deteriorated in recent years.

<sup>22</sup> Net lending is net advances by the National Government for the servicing of government guaranteed corporate debt. It covers the National Government loans outlays to government corporations.

**FIGURE 6**  
**Net Fiscal Incidence, 1981-2007**  
*Per capita expenditure less per capita revenues in real prices, 2000=100*



#### IV. VARIOUS MEASURES OF DEFICITS

This section presents the trends of three different indicators of fiscal health namely: the national government account balance (NGAB), the consolidated public sector financial position (CPSFP) and the public sector borrowing requirement (PSBR).

##### A. National Government Account Balance

The national government account balance compares national government revenues to national government cash disbursements. Balanced budget is achieved when revenues equal cash disbursement (excluding debt repayments and payments on non-budgetary accounts<sup>23</sup>) of the national government during a given year. Budget deficit (surplus) is incurred when revenues are less (more) than cash disbursements excluding debt repayments and payments on non-budgetary accounts.

National government budget fiscal balance averaged 2.8 percent of GDP during the final years under Marcos (1981-85). Corazon C. Aquino took office in February 1986 after Marcos left the Philippines for exile in Hawaii. This promise of a new democracy brought hope to the Filipino people. However, it too brought a huge foreign debt overhang, several coup attempts with the

<sup>23</sup> Non-budgetary accounts are trust liabilities, securities unloaded or purchased, sinking fund, and other accounts not included in the national government budget.

most serious one in 1989 and two major catastrophes: the 1990 earthquake and the 1991 explosion of Mt. Pinatubo.

From a fiscally weak position, where the national government-to-GDP ratio was around 5.1 percent, Aquino was successful in reducing the fiscal imbalance through improved tax effort – largely as a result of the 1986 tax reform program. The servicing of public debt was extremely burdensome, with interest payments averaging about 6 percent of GDP during her entire term. The fiscal imbalance that progressively improved from its initial point of 5.1 percent of GDP reemerged in 1990 because of high interest rates, accelerated payment of the foreign debt and the implementation of the Salary Standardization Law (SSL).<sup>24</sup>

Another benchmark law drafted, passed and enacted during the Aquino administration was the 1991 Local Government Code that increased the revenue and spending revenue responsibilities to local governments. The law increased the national government grants to local governments and also improved the grant system by making its release automatic, formula-based and predictable.

The Ramos administration had budget surpluses for four of its six years in power. During the first two years of this regime, the country was beset by power outages. Mr. Ramos asked, and Congress agreed, for emergency powers for fast-tracking the construction of power projects. The contract for these independent power plants (IPPs) provided for government guarantee to purchase the built capacity whether used or not the power generated is actually utilized. The additional cost associated with this guarantee is incorporated in power rates to date.<sup>25</sup>

In the last couple of years of the Ramos regime, there was a real estate boom and huge foreign direct investment inflow to the Philippines. During this period, the peso was overvalued. With the sharp devaluation of the Thai baht in 1997, at the onset of the Asian financial crisis, the peso depreciated by almost forty percent.

In July 1998, at the height of the Asian financial crisis, Joseph E. Estrada took office. The national government budget deficit rose from 1.9 percent of GDP in 1998 to 3.8 percent in 1999 and 4.0 percent in 2000. This result could be attributed largely to the sharp deterioration in the tax effort and higher interest payments owing to the sharp depreciation of the peso. Tax effort plummeted from 17.0 percent in 1997 to 13.7 percent in 2000 owing to the continuing and expanded tax incentives, the narrowing of the VAT base, and the lowering of tariff walls. Expenditures rose slightly largely because of higher foreign interest payments, owing to the large peso depreciation, and the payment of accounts payables<sup>26</sup> to contractors and suppliers (estimated at around P60 billion), which Estrada inherited from the Ramos administration. In response to the Asian financial crisis, and in an apparent attempt to window-dress the national government fiscal picture, the Ramos administration deferred the payment of valid claims of contractors and suppliers.<sup>27</sup>

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<sup>24</sup> Diokno (1995).

<sup>25</sup> Sicat (2003)

<sup>26</sup> Accounts payable are obligations or commitments of national government agencies, whether current year and prior years, for which services have been rendered, or goods have been delivered, or projects have been completed and accepted.

<sup>27</sup> This was done through Administrative Order (AO) 372 issued in December 1997 instituting economy measures. For figures see Diokno (1999).



In the period 2001 to 2007, the average national government budget deficit was 3.1 percent of GDP. It peaked at 5.3 percent of GDP in 2002 and tapered off to 0.1 percent in 2007. The poor tax effort and high interest payments were the main reasons for the Arroyo administration's poor fiscal position. Taxes as percent of GDP averaged 13.2 percent during the seven-year period – a major departure from the 17.0 percent in 1997. During the same period, interest payments as percent of GDP averaged 5 percent. With weakening tax effort and rising debt servicing costs, the Arroyo government responded by underspending in public infrastructure and social overhead capital (education and health care). This pattern of expenditures is myopic. By not investing in physical infrastructure and human capital, the Arroyo administration has sacrificed the economy's long-term growth.

## **B. Consolidated Public Sector Financial Position**

The consolidated public sector financial position is an indicator of the overall fiscal performance of the public sector of the Philippines. It is the combined surplus (deficit) of the national government (NG), the Central Bank (CB) restructuring accounts, the major non-financial government corporations (MNFGC), the government financial institutions (GFI), the local government units (LGU), the social security institutions, the Oil Price Stabilization Fund and the Bangko Sentral ng Pilipinas (BSP). CPSFP is a better indicator of the public sector's true state of finances than the NGAB.

The CPSF measure was first reported in 1985 in order to correct the erroneous reporting of accounts during the Marcos regime. It has been in deficit during the past two decades, except for the fiscal year 1996, averaging 3.2 percent of GDP. The increase in the consolidated public sector deficit (CPSD) in recent years was largely due to the ballooning national government fiscal deficits and the large losses of some of the monitored nonfinancial government corporations (MNFGCs). Among the major state-owned corporations, the National Power Corporation was the biggest deficit spender in recent years. The National Food Authority has now emerged as the top deficit spender with the recent surge in food prices, especially rice.

During the Aquino years, the CPSD averaged 3.5 percent of GDP. The main contributor to the deficit was the national government, with an average deficit-to-GDP ratio of 2.8 percent, followed by the financially distressed Central Bank of the Philippines (CB),<sup>28</sup> with an average deficit-to-GDP ratio of 2.0 percent. In addition, the government assumed the servicing and liabilities of the Philippine National Bank (PNB) and the Development Bank of the Philippines (DBP) that were at an all-time high of 47.2 billion pesos.<sup>29</sup>

TABLE 7  
**Consolidated Public Sector Financial Position, 1986-2007**  
*Average for each administration*

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<sup>28</sup> The Central Bank is labeled as Bangko Sentral ng Pilipinas (BSP) in Table 7.

<sup>29</sup> Diokno (1995)

Particular	1986-92	1993-98	1999-2000	2001-07
	Aquino	Ramos	Estrada	Arroyo
<b>I. In Billion pesos, 2000 prices</b>				
<b>A. Public Sector Borrowing Requirement</b>	<b>(56.4)</b>	<b>(51.6)</b>	<b>(159.0)</b>	<b>(165.4)</b>
1. National Government	(63.1)	(6.9)	(125.1)	(123.5)
2. CB Restructuring	0.0	(27.4)	(20.2)	(13.5)
3. Monitored Nonfinancial Government Corporations (MNFGCs)	(14.0)	(22.3)	(12.0)	(32.2)
4. Oil Price Stabilization Fund	0.4	(2.6)	1.1	0.1
5. Adjustments of Net Lending and Equity to GOCCs	0.0	0.2	3.7	3.7
6. Other adjustments	20.4	7.5	(6.5)	0.0
<b>B. Other Public Sector</b>	<b>(23.2)</b>	<b>23.1</b>	<b>34.5</b>	<b>47.2</b>
1. Government Financial Institutions (GFIs)	(1.0)	7.2	3.1	4.8
2. Bangko Sentral ng Pilipinas (BSP)	(47.2)	2.4	(2.0)	2.0
3. SSS/GSIS	13.8	6.1	26.6	26.9
4. Local Government Units (LGUs)	3.0	5.4	7.2	13.4
5. Timing Adjustments of Interest Payments to BSP	8.3	2.1	(0.9)	0.5
6. Other Adjustments	0.0	0.0	0.5	(0.4)
<b>C. Consolidated public sector surplus (deficit) (CPSD)</b>	<b>(79.6)</b>	<b>(28.5)</b>	<b>(124.5)</b>	<b>(118.2)</b>
<b>II. In percent of GDP</b>				
<b>A. Public Sector Borrowing Requirement</b>	<b>(2.4)</b>	<b>(1.9)</b>	<b>(4.9)</b>	<b>(4.3)</b>
1. National Government	(2.8)	(0.2)	(3.9)	(3.2)
2. CB Restructuring	0.0	(1.0)	(0.6)	(0.3)
3. Monitored Nonfinancial Government Corporations (MNFGCs)	(0.6)	(0.8)	(0.4)	(0.8)
4. Oil Price Stabilization Fund	0.0	(0.1)	0.0	0.0
5. Adjustments of Net Lending and Equity to GOCCs	0.0	0.0	0.1	0.1
6. Other adjustments	0.9	0.3	(0.2)	0.0
<b>B. Other Public Sector</b>	<b>(1.0)</b>	<b>0.9</b>	<b>1.1</b>	<b>1.1</b>
1. Government Financial Institutions (GFIs)	(0.1)	0.3	0.1	0.1
2. Bangko Sentral ng Pilipinas (BSP)	(2.0)	0.1	(0.1)	0.0
3. SSS/GSIS	0.6	0.2	0.8	0.7
4. Local Government Units (LGUs)	0.1	0.2	0.2	0.3
5. Timing Adjustments of Interest Payments to BSP	0.4	0.1	(0.0)	0.0
6. Other Adjustments	0.0	0.0	0.0	(0.0)
<b>C. Consolidated public sector surplus (deficit) (CPSD)</b>	<b>(3.5)</b>	<b>(1.0)</b>	<b>(3.8)</b>	<b>(3.2)</b>

Sources: Department of Budget and Management, Bureau of Treasury

Memo item: FY 2006 figures are preliminary, FY 2007 figures are revised.

During the Ramos administration, the CPSD decreased to an average 1 percent of GDP. The improvement was attributable to two factors: healthier national government account (average deficit-to-GDP ratio of 0.2 percent) and financial turnaround of the restructured Central Bank. The national government financial position was aided immensely by higher tax effort and sizable proceeds from sale of state assets (for example, the Bonifacio property) and privatization of state-operated enterprises. With the restructuring of the Central Bank in 1992-93, much of its debts were transferred to the national government. From the total public sector viewpoint, there is no difference. But it has the effect of showing a smaller deficit (larger surplus) for the BSP, and a bigger deficit (smaller surplus) for the national government. However, with cleaner financial books, and an independent Monetary Board, the BSP is now able to pursue monetary policy more effectively.

### C. Public Sector Borrowing Requirement

From an economic standpoint, the public sector borrowing requirement is perhaps the most relevant measure of fiscal imbalance. It measures the amount the government has to borrow domestically or externally to finance the combined deficits of the national government and the major monitored corporations. PSBR, as percent of GDP, averaged 2.4 percent during the Aquino years (1986-92) and 1.9 percent during the Ramos years (1993-1998). It rose during the two-year stint of Estrada – 4.6 percent in 1999 and 5.2 percent in 2000. The dramatic rise in PSBR was attributable to the huge jump in the national government budget deficit owing to the increase in VAT exemptions, inelasticity of tax revenues from petroleum, cigarettes and liquor, and on the expenditure side payment of inherited government accounts payable.

During the Arroyo administration, the PSBR averaged 4.3 percent of GDP. There are two factors: large national government deficits and heavy losses for the monitored government corporations. The average national government deficit, as percent of GDP, reached 3.2 percent. In addition, the losses of the major monitored corporations (MNFGCs) increased by more than 200 percent owing largely to the poor performance of the Napocor and the National Electrification Authority (NEA). The losses of the MNFGCs averaged 0.8 percent of GDP during this period.

#### **IV. FINANCING OF THE DEFICIT AND PUBLIC DEBT**

##### **A. Financing of the Deficit**

If revenues are inadequate to finance planned expenditures, the government has three options to close the budget gap: borrow, print money, or increase taxes. In the past, the Philippine government has resorted to external and domestic borrowing to finance its deficits. It has amassed huge public debt not only to finance previous years' budget deficits but also to pay for losses incurred by other public sector institutions such as poorly performing government owned or controlled corporations, public financial institutions and the Central Bank (CB) but which were later assumed by the national government.

Government borrowing can crowd out investments in two ways. First, if borrowing is largely domestic, this may lead to lower investment because of less loanable funds available for private investors, and thus, to lower output and consumption in the long-run.<sup>30</sup> Second, if debt was incurred to settle other debt rather than to finance government projects in human and physical infrastructure, then crucial public spending is being forgone. The financing of debt negatively affects important public investment spending.<sup>31</sup> A study by the Asian Development Bank [2005] looked at the implications of the current Philippine fiscal policy on government debt. It concluded that the government debt situation is not sustainable given the current policy regime. Furthermore, it found evidence of a weak debt Ponzi game.<sup>32</sup> This implies that the Philippine government is simply borrowing to pay off its current debts. Current government debt is vulnerable to adverse shocks and simple budgetary deficit control policy is inadequate.

During the final years of Marcos, 1981-2005, the government relied more on domestic financing to finance the deficit – on average, 65.6 domestic financing and 34.4 percent external financing.

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<sup>30</sup> Stiglitz [2000].

<sup>31</sup> Diokno [1995].

<sup>32</sup> A government is playing a Ponzi game when it keeps on paying old debts with new ones; see Duo Qin, et. al. [2005].

This pattern of financing was uneven. The share of domestic financing started at about half (50.4 percent) in 1981, dipped to a low of 27.0 percent in 1983 before it soared to as high as 102.5 percent in 1985. Effectively, Marcos borrowed from abroad in 1985 to retire some local debts. The deeper reliance on domestic financing was in response to the higher world interest rates and the weakening of the peso.

TABLE 8  
**Budget Deficit Financing, 1981-2007**  
*In billion pesos, unless otherwise specified*

Particulars	1981-85	1986-92	1993-98	1999-2000	2001-07
	Marcos	Aquino	Ramos	Estrada	Arroyo
<b>Financing</b>	<b>12.9</b>	<b>50.6</b>	<b>13.1</b>	<b>192.8</b>	<b>202.0</b>
Net foreign	3.5	6.9	(2.1)	83.6	89.5
Net domestic	9.4	43.7	15.2	109.2	112.5
<i>Percent share</i>					
Net foreign	32.6	16.4	(20.8)	43.5	49.1
Net domestic	67.4	83.6	120.8	56.5	50.9

Source: Government authorities. See Appendix C.

The Aquino administration relied heavily on domestic sources to finance its budget deficits from 1986 until 1991. In 1992, the financing mix was reversed, with heavier reliance now on foreign financing at 90 percent.

The Ramos administration relied heavily on external financing of the budget deficit. This financing mix that peaked in 1995 (119.8 percent foreign, -19.8 percent domestic) was revised in response to the Asian financial crisis. Recognizing the serious risk of relying heavily on foreign financing, the Ramos administration reduced the share of external financing to 25.1 percent in 1997 and 13.8 percent in 1998.

Estrada pursued a more balanced financing mix – 56.5 percent foreign, 43.5 percent domestic – during his short stint in office.

Arroyo relied heavily on domestic financing (average of 64.5 percent) from 2001 to 2005. But the numbers for net external financing --that is, gross foreign borrowing less amortization – understate the extent of heavy external borrowings that took place in recent years. From 2002 to 2005, the Arroyo administration borrowed over P858 billion, of which global bonds floated was about 619 billion.<sup>33</sup> In 2006, there was a sharp increase in the share of net foreign borrowing to almost 110% (Appendix C).

## B. National Government Debt

From a low of 16 percent in 1981, the national government debt as percent of GDP, peaked at 76.4 percent in 1993, averaged at about 61 percent thereafter before it rose to an all-time high of 78.5 percent in 2004.

TABLE 9  
**Public Debt Statistics, 1981-2007**

<sup>33</sup> In 2006 and 2007, the Arroyo administration borrowed from external sources P284.1 billion and P118.4 billion, respectively. Some P209.9 billion global bonds were floated in 2006.

Particular	1981-85	1986-92	1993-98	1999-2000	2001-07
	Marcos	Aquino	Ramos	Estrada	Arroyo
<b>A. National Government Outstanding Debt</b>					
1. Total Debt (in Billion PhP)	86.5	554.9	972.6	1,678.9	3,402.8
a. Domestic Debt	50.3	303.2	509.1	798.9	1,849.1
b. Foreign Debt	36.2	251.7	463.5	880.0	1,553.7
<i>In Percent of GDP</i>					
2. Total Debt	19.5	58.2	48.2	52.9	69.2
a. Domestic Debt	11.5	31.9	25.2	25.2	37.3
b. Foreign Debt	8.0	26.4	22.9	27.6	31.9
<i>As A Percent of Total Outstanding Debt</i>					
3. Domestic Debt	60.0	54.7	52.5	47.9	54.1
4. Foreign Debt	40.0	45.3	47.5	52.1	45.9
<b>B. Debt Service Expenditures</b>					
1. Interest Payment (in Billion PhP)	7.2	55.0	80.4	123.6	246.5
a. Domestic	4.5	40.7	59.6	84.3	156.4
b. Foreign	2.7	14.2	20.8	39.3	90.1
2. Amortization (in Billion PhP)	3.5	30.2	49.0	93.0	303.7
a. Domestic	1.4	16.5	20.1	53.5	203.3
b. Foreign	2.2	13.7	28.8	39.5	100.4
3. Total (in Billion PhP)	10.7	85.2	129.4	216.6	550.2
a. Domestic	5.8	57.3	79.7	137.8	359.7
b. Foreign	4.9	27.9	49.7	78.9	190.5
<i>In Percent of GDP</i>					
4. Total	2.3	8.8	6.4	6.8	10.8
a. Domestic	1.3	5.9	4.0	4.4	7.0
b. Foreign	1.1	2.9	2.5	2.5	3.8
<i>As A Percent of Total Debt Service Expenditures</i>					
5. Domestic	53.8	66.7	61.6	63.7	64.2
6. Foreign	46.2	33.3	38.4	36.3	33.0
<i>As A Percent of Total National Government Expenditures</i>					
7. Total Debt Servicing Expenditures	16.5	47.2	34.0	35.0	59.5
a. Domestic	8.9	31.6	21.0	22.3	38.6
b. Foreign	7.6	15.6	13.1	12.7	20.9
<i>As A Percent of Taxes</i>					
8. Interest Payments	15.1	42.5	24.9	27.6	38.0
a. Domestic	9.3	30.9	18.4	18.9	24.3
b. Foreign	5.8	11.6	6.5	8.8	13.8
9. Total Debt Servicing	22.6	67.2	39.8	48.6	82.5
a. Domestic	12.2	44.9	24.5	30.9	53.2
b. Foreign	10.4	22.3	15.3	17.6	29.3

SOURCE: Department of Budget and Management, National Statistics Coordination Board, Bureau of Treasury  
MEMO ITEMS:

1. Interest payments as % of tax revenues shows how much the burden is on recurring resources of government.
2. Total debt service exp as % of total spending displays how much of the budget is actually allocated to non-productive purposes.
3. Total debt servicing includes both interest payment and amortization.

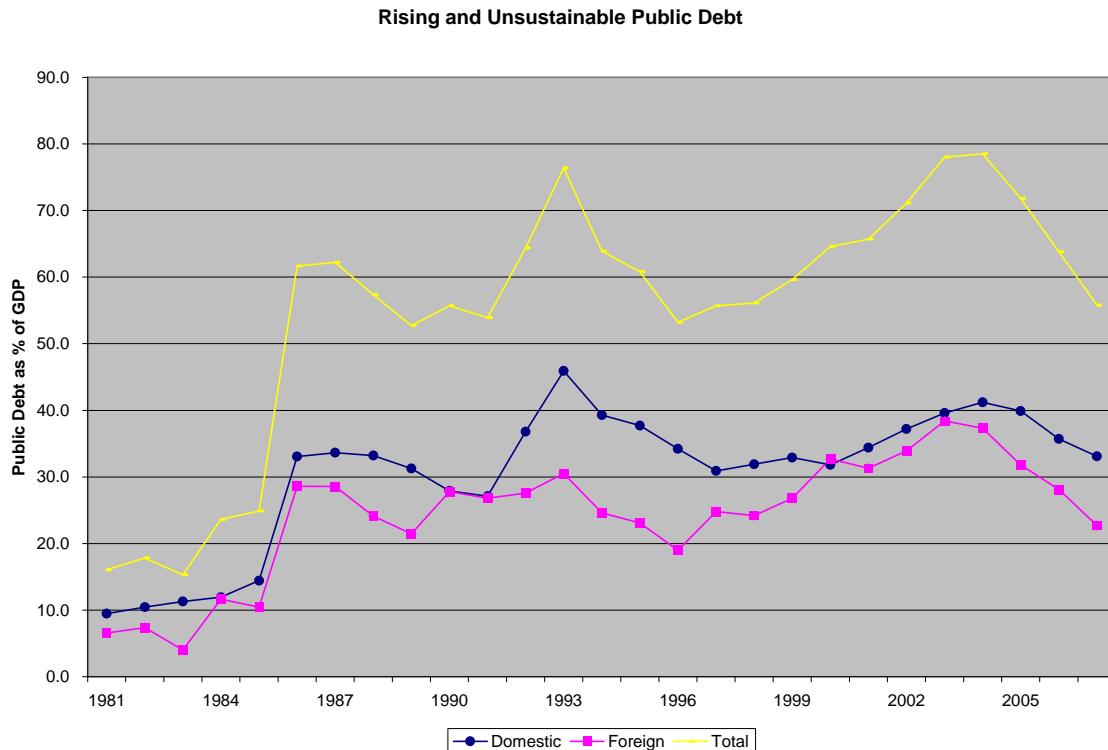
The surge in the debt-to-GDP ratio during Aquino's term can be attributed largely to the decision of the government to assume the losses of major financial institutions like the Development Bank of the Philippines, the Philippine National Bank, and the Land Bank of the Philippines as well as other monitored corporations such as the National Power Corporation. The debt to GDP ratio averaged 58.2 percent for this period from a previous 19.5 percent. Total debt service expenditures as percent of total government spending, on average, soared 47.2 percent from a

previous 16.5 percent. Worse and perhaps a more accurate measure of the debt burden, total debt service expenditures as percent of total taxes zoomed from 22.6 to 76.2 percent.

Total interest payments averaged 42.5 percent of tax revenues from 1986 to 1992. This indicator shows how much government resources are left, after deducting interest payments, for the provision of public goods, publicly provided private goods, and investment in public infrastructure. The ratio of interest payment to taxes went down sharply during the Ramos and Estrada years before it reemerged in recent years (average of 40.3 percent in 2001-2007). Effectively, interest payments had ‘crowded out’ the more important expenditure responsibilities of the government, such as, education, health, and public infrastructure.

During the Estrada administration, there was a slight shift in the nature of the public debt, with the share of domestic debt decreasing and the share of foreign debt increasing. There are two reasons for the shift: first, there was a preference for foreign financing and second, the revaluation of the dollar debt because of the sharp depreciation of the peso after the Asian financial crisis. The total debt-to-GDP ratio declined, however, to 52.9 percent from 48.2 percent under Ramos. Debt was managed well since debt servicing as a share of total spending increased by only 1 percent and interest payments as a percent of tax revenues increased by only 3 percent.

**FIGURE 7**  
**Total Public Debt, 1981-2007**  
*In percent of GDP*



The national government debt-to-GDP ratio averaged 69.2 percent during Arroyo’s watch, the highest among all administrations. Debt servicing – interest plus principal amortization – as percent of total taxes was at its highest under the Arroyo administration. From 2001 to 2007, it averaged 82.5 percent. But the mean statistic hides the sharp rise in the debt burden in recent years – debt servicing-to-tax ratio was 100.6, 96.2, and 99.4 in 2004, 2005 and 2006, respectively

(Appendix D). This means that in 2004, for example, payments for interest and principal amortization exceeded taxes collected.

Is the current debt situation sustainable? A study by the ADB [2005] looked at the implications of the current Philippine fiscal policy on government debt. It concluded that the government debt situation is not sustainable given the current policy regime. Furthermore, it found evidence of a weak debt Ponzi game.<sup>34</sup> This implies that the Philippine government is simply borrowing to pay off its current debts. The implication is that currently, the Philippine government is simply borrowing to pay off its current debts. Current government debt is vulnerable to adverse shocks<sup>35</sup> and simple budgetary deficit control policy is inadequate. The government's responses to the rising debt and stagnating tax effort are: first, constraining expenditures by underspending in public infrastructure and social overhead (education, health and nutrition) and second, selling state assets. The first response is short-sighted and could adversely affect long-term growth and development. The second response may have merits if the sale of assets is consistent with the desire to narrow the scope of government intervention and the proceeds of asset sales are used to retire more expensive public debt or to invest in productivity-enhancing public infrastructure.

## **VI. ECONOMIC AND FISCAL DETERMINANTS OF PUBLIC DEFICITS**

In recent years, budget deficits have reemerged. With deficits rising and investment in human capital and public infrastructure deteriorating, an appropriate question is: what has caused the poor performance of the Philippines in recent years? Is it the result of unfortunate events, macroeconomic shocks or misdirected fiscal policy?

The results of my previous study are as follows. First, using NGAB, the narrowest measure of fiscal balance, the statistically significant determinants are the following: inflation, domestic liquidity, capital outlays, and tax effort. On the other hand the following variables were found to be statistically insignificant: economic growth, real effective exchange rate (REER), interest payment as percent of GDP, and intergovernmental grant (IRA) as percent of total government expenditures.

Second, using consolidated public sector fiscal position (CPSFP), the broader measure of fiscal balance, the statistically significant determinants of fiscal balance are the following: economic growth, inflation, domestic liquidity, capital outlays, intergovernmental fiscal transfers (IRA) and tax effort. Two variables – economic growth and intergovernmental fiscal transfer – which were not statistically significant using the national government fiscal balance as the explanatory variable for budget deficit turned out to be significant using the consolidated public sector deficit concept.

Third, the negative association of domestic liquidity with fiscal balances implies that in financing the deficit, the government may opt to resort to debt financing first, rather than printing money or increasing taxes. In the Philippine context, monetizing the deficit is not a preferred option because of legal restrictions and financial limitations on the monetary authorities (BSP). On the other hand, passing new tax laws to raise revenues has always been a difficult option politically.

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<sup>34</sup> A government is playing a Ponzi game when it keeps on paying old debts with new ones. [Duo Qin, et.al. 2005]

<sup>35</sup> For example, the recent surge in oil and food prices and the slowdown of the U.S. and world economy could raise inflation and slow the growth of the domestic economy.

Fourth, tax effort has been the most robust determinant of national government fiscal balance or the broader measure of fiscal balance (CPSFP). What is more interesting though is the exploratory regression of tax effort and the tax reform dummy variables. It is found that tax effort is positively related to the 1986 tax reform at a 1% level of significance while it is negatively associated with 1997 CTRP at the 15% level of significance.<sup>36</sup> A plausible explanation why the coefficient of the 1997 CTRP is less significant is that while major reforms initiated in 1986 such as value-added (VAT) are still in place, the VAT's effect was not as potent as before because the tax base was narrowed as a result of the 1997 CTRP.<sup>37</sup>

Fifth, real GDP growth rate (ECONGR) is found to be positively associated with fiscal balance using CPSFP as the explanatory variable, but insignificant if the more limited deficit concept (NGAB) is used. The results suggest that strong economic growth may lead to a better fiscal position. While the effect of economic growth on the national government deficit is unclear, its effect on other public sector entities is unequivocally positive. The monitored corporations, the government financial institutions, and social security institutions including Philhealth<sup>38</sup>, local governments perform better financially when the economy is growing and poorly when the economy is slowing down.

Finally, intergovernmental fiscal transfer (IRA) is found to be positively associated with the consolidated public sector fiscal balance, though its association with the national government deficit is found to be statistically insignificant. The empirical result suggests that the higher the IRA, the higher the consolidated fiscal balance. The explanation is that under existing budget rules, local governments are mandated by law to generate a surplus of at least 5 percent to cover future contingencies; the higher the grant, the higher the mandated overall mandated surplus for local governments, and consequently the higher the consolidated fiscal surplus.

## VI. CONCLUSIONS, OBSERVATIONS AND IMPLICATIONS FOR POLICY

There are similarities and differences between public sector deficits in the early 1980s and those in recent years. Looking at macroeconomic factors, the deficits of the early 1980s and recent years occurred during periods of high oil prices. The two periods differ in that the early 1980's had higher prevailing interest and inflation rates compared to recent years. Interest rates averaged 20.2 percent during the period 1981-1985, whereas interest rates averaged of 7.0 percent in 2001-04. Inflation rates in the early 1980's were almost 300 percent higher than in recent years. In addition, the foreign exchange rate (Peso to U.S. Dollar) was more volatile during the early 1980's.

In order to arrive at more meaningful decisions, policymakers should use the broader measure of consolidated public sector fiscal position (CPSFP) rather than the narrower concept of national government account balance (NGAB) in evaluating the fiscal health of the government. The empirical results for the regression using NGAB as the dependent variable suggest that economic growth rate and intergovernmental fiscal transfers do not affect fiscal balance. But using the

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<sup>36</sup> See Appendix B.

<sup>37</sup> Diokno [2005]. The most important are R.A. 8184 An Act Restructuring the Excise Tax on Petroleum Products; R.A. 8241 Additional exemptions to value-added tax, VAT and more recently R.A. 9010 An Act Deferring the Imposition of VAT on Certain Services Imposed in R.A. 8761.

<sup>38</sup> Philippine Health Insurance Corporation.



broader concept of CPSFP, the results suggest that economic growth rate and intergovernmental fiscal transfers are both associated with fiscal stance positively.

Tax effort has been the strongest positive determinant of the Philippines' fiscal health. During the last quarter century, tax effort was lowest in the two periods when public deficits were large. In the early 1980's, the low tax effort was due largely to a complicated tax system, narrow tax base and an unresponsive tax system; in recent years, it was mainly because of a narrower tax base and an increasingly unresponsive tax system. Public policy must be directed to improving tax effort, not only by correcting existing weaknesses in the tax system (such, as for example, narrow tax base because of the proliferation of fiscal incentives laws), but also by improving tax administration.

Spending priorities have changed overtime. Infrastructure was the focus of public spending during the Marcos years, while spending for social services were the focus during the Aquino and Estrada years. In recent years, both infrastructure and social services received less attention because of the heavy debt burden and low tax effort. From 2001 to 2005, both real per pupil spending on education and real per capita health spending plummeted. Unless reversed, the falling investment in human capital and physical infrastructure would propel the Philippine economy on a lower long-run growth path.

There should be increased spending on both human and physical infrastructure to increase domestic productivity, attract investments and to promote economic growth and development. The results of our econometric work suggest that the effect of investment in physical infrastructure on fiscal balance is positive. Investment in productivity-enhancing capital projects makes private investment more productive, reduces transactions costs, and increases the profitability of private sector businesses.

Public policy, including fiscal and monetary policy, works with a lag. Consider the following examples. First, the decrease in overall tax effort after its peak in 1997 can be partly blamed to the changes in the tax laws that were introduced during Ramos' final years. Second, the surge in public debt as a result of the sharp depreciation of the peso as an aftermath of a misplaced foreign exchange policy and the Asian financial crisis has contributed to the sharp increase in public debt after Ramos. As a result, subsequent administrations – and future generations of Filipinos – have to bear the brunt of adjustment in terms of higher taxes or constrained public services in the future. Third, the decision of the Aquino government to transfer to the national government the losses incurred during the time of Marcos by some government financial institutions and major non-financial corporations helped improved the fiscal picture of the distressed government corporations. But as a result, it magnified the fiscal deficit of the national government and constrained its ability to deliver the appropriate level of public services. Put differently, Marcos' fiscal policy of taxing less, spending more, and using state enterprises to engage in the provision of private goods, made him look good then at the expense of the administrations that followed him. A review of the fiscal behavior of any administration should therefore consider the lag in public policy.

**Appendix A**  
National Government Account Balance, 1981-2007  
*In percent of GDP*

	1981	1982	1983	1984	1985	1986	1987	1988	1989	1990	1991	1992
<b>A. REVENUES</b>	<b>11.8</b>	<b>11.2</b>	<b>12.4</b>	<b>10.8</b>	<b>12.1</b>	<b>13.0</b>	<b>15.1</b>	<b>14.1</b>	<b>16.5</b>	<b>16.8</b>	<b>17.7</b>	<b>18.0</b>
1. Tax	10.3	9.9	10.8	9.6	10.7	10.8	12.6	11.3	13.2	14.1	14.6	15.4
Direct	2.5	2.5	2.5	2.3	3.3	3.1	3.2	3.4	4.1	4.6	4.9	5.2
Indirect	3.5	3.4	3.3	3.6	4.2	4.5	5.4	4.5	4.8	5.1	4.4	4.7
Taxes on International Trade	3.6	3.6	4.5	3.3	3.0	2.9	3.8	3.1	4.1	4.3	5.2	5.4
Other Offices	0.6	0.5	0.6	0.4	0.3	0.2	0.2	0.2	0.2	0.2	0.1	0.1
2. Nontax	1.5	1.3	1.6	1.3	1.4	2.3	2.5	2.8	3.2	2.7	3.1	2.5
<b>B. EXPENDITURES</b>	<b>15.8</b>	<b>15.4</b>	<b>14.4</b>	<b>12.8</b>	<b>14.0</b>	<b>18.1</b>	<b>17.6</b>	<b>17.0</b>	<b>18.6</b>	<b>20.2</b>	<b>19.8</b>	<b>19.1</b>
1. Current Operating Expenditures	8.6	9.3	9.4	8.2	9.7	11.0	14.1	14.2	15.4	16.9	15.9	15.9
Personal Services	3.5	3.1	3.8	3.2	4.0	4.1	4.8	5.1	5.6	5.8	5.8	5.5
Maintenance and Other Operating Expenditures	3.7	3.9	3.2	2.4	2.3	2.5	2.9	2.4	2.9	2.8	2.9	2.5
Interest Payments	0.8	1.0	1.4	2.0	2.6	3.5	5.4	5.7	5.9	6.6	6.0	5.9
Domestic	0.5	0.7	0.7	1.1	1.8	2.5	3.5	4.0	4.4	4.9	4.5	4.7
Foreign	0.3	0.4	0.6	0.9	0.8	1.1	1.9	1.7	1.5	1.7	1.5	1.2
Allotment to Local Government Units	0.5	0.7	0.7	0.5	0.6	0.6	0.6	0.5	0.4	0.4	0.5	1.2
Petroleum Price Stabilization Fund	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.4	0.0	0.0
Subsidies	0.2	0.6	0.3	0.1	0.2	0.3	0.3	0.3	0.6	0.7	0.5	0.3
Tax Expenditures	0.0	0.0	0.0	0.0	0.0	0.0	0.2	0.1	0.1	0.2	0.2	0.6
2. Capital Outlay	6.8	5.5	4.4	3.7	3.9	4.7	2.4	2.1	2.8	3.0	3.4	3.1
Infrastructure and Other Capital Outlays	4.2	2.7	2.8	1.9	1.5	1.9	1.8	1.9	2.3	2.7	3.0	3.4
Others	2.6	2.8	1.6	1.9	2.4	2.8	0.6	0.2	0.5	0.3	0.4	(0.3)
3. Net Lending	0.3	0.7	0.6	0.8	0.4	2.5	1.0	0.7	0.4	0.4	0.5	0.2
<b>C. NATIONAL GOVERNMENT ACCOUNT BALANCE</b>	<b>(4.0)</b>	<b>(4.2)</b>	<b>(2.0)</b>	<b>(1.9)</b>	<b>(1.9)</b>	<b>(5.1)</b>	<b>(2.4)</b>	<b>(2.9)</b>	<b>(2.1)</b>	<b>(3.5)</b>	<b>(2.1)</b>	<b>(1.2)</b>
<b>D. EXPENDITURES (excluding interest payments)</b>	<b>15.0</b>	<b>14.4</b>	<b>13.0</b>	<b>10.8</b>	<b>11.4</b>	<b>14.6</b>	<b>12.2</b>	<b>11.3</b>	<b>12.7</b>	<b>13.6</b>	<b>13.8</b>	<b>13.3</b>
<b>E. PRIMARY SURPLUS/DEFICIT (A-D)</b>	<b>(3.2)</b>	<b>(3.2)</b>	<b>(0.7)</b>	<b>0.1</b>	<b>0.6</b>	<b>(1.6)</b>	<b>3.0</b>	<b>2.8</b>	<b>3.8</b>	<b>3.1</b>	<b>3.9</b>	<b>4.7</b>

SOURCE: Department of Budget and Management

Appendix A (continued)  
**National Government Account Balance, 1981-2007**  
*In percent of GDP*

	1993	1994	1995	1996	1997	1998	1999	2000	2001	2002	2003
<b>A. REVENUES</b>	<b>17.7</b>	<b>19.9</b>	<b>19.0</b>	<b>18.9</b>	<b>19.4</b>	<b>17.4</b>	<b>16.1</b>	<b>15.3</b>	<b>15.5</b>	<b>14.3</b>	<b>14.6</b>
1. Tax	15.6	16.0	16.3	16.9	17.0	15.6	14.5	13.7	13.5	12.5	12.5
Direct	5.0	5.4	5.8	6.3	6.8	6.9	6.2	6.1	6.2	5.7	5.7
Indirect	4.8	5.6	5.2	5.7	6.2	5.8	5.3	4.2	4.1	3.8	3.8
Taxes on International Trade	5.6	4.8	5.1	4.8	3.9	2.9	2.9	2.8	2.7	2.4	2.5
Other Offices	0.2	0.1	0.1	0.1	0.1	0.1	0.1	0.5	0.5	0.5	0.5
2. Nontax	2.1	3.8	2.7	2.0	2.5	1.7	1.6	1.6	2.0	1.8	2.1
<b>B. EXPENDITURES</b>	<b>19.1</b>	<b>18.9</b>	<b>18.4</b>	<b>18.6</b>	<b>19.4</b>	<b>19.2</b>	<b>19.8</b>	<b>19.3</b>	<b>19.6</b>	<b>19.6</b>	<b>19.3</b>
1. Current Operating Expenditures	15.5	15.2	14.4	15.2	15.4	15.9	15.8	16.0	16.6	16.4	16.5
Personal Services	5.3	5.5	5.7	6.2	7.1	7.4	6.8	6.7	6.6	6.7	6.4
Maintenance and Other Operating Expenditures	2.3	2.2	2.3	2.2	2.1	2.4	2.4	2.4	2.4	2.1	1.8
Interest Payments	5.2	4.7	3.8	3.5	3.2	3.7	3.6	4.2	4.8	4.7	5.3
Domestic	3.8	3.5	2.7	2.7	2.4	2.8	2.5	2.8	3.1	3.0	3.4
Foreign	1.4	1.1	1.1	0.8	0.8	1.0	1.1	1.4	1.7	1.7	1.8
Allotment to Local Government Units	2.0	2.2	2.2	2.1	2.3	2.1	2.6	2.4	2.5	2.8	2.7
Petroleum Price Stabilization Fund	0.0	0.0	0.0	0.5	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Subsidies	0.3	0.4	0.2	0.4	0.4	0.2	0.2	0.2	0.2	0.1	0.3
Tax Expenditures	0.3	0.3	0.2	0.3	0.3	0.0	0.2	0.1	0.0	0.0	0.0
2. Capital Outlay	3.5	3.3	3.7	3.3	3.9	3.3	3.9	3.3	2.9	3.1	2.6
Infrastructure and Other Capital Outlays	2.4	2.5	2.8	2.6	3.3	2.7	3.2	2.6	2.1	2.4	1.8
Others	1.1	0.8	1.0	0.7	0.7	0.6	0.6	0.7	0.8	0.8	0.8
3. Net Lending	0.2	0.3	0.2	0.1	0.1	0.0	0.1	0.1	0.1	0.1	0.1
<b>C. NATIONAL GOVERNMENT ACCOUNT BALANCE</b>	<b>(1.5)</b>	<b>1.0</b>	<b>0.6</b>	<b>0.3</b>	<b>0.1</b>	<b>(1.9)</b>	<b>(3.8)</b>	<b>(4.0)</b>	<b>(4.0)</b>	<b>(5.3)</b>	<b>(4.7)</b>
<b>D. EXPENDITURES (excluding interest payments)</b>	<b>14.0</b>	<b>14.2</b>	<b>14.6</b>	<b>15.1</b>	<b>16.2</b>	<b>15.5</b>	<b>16.3</b>	<b>15.1</b>	<b>14.8</b>	<b>15.0</b>	<b>14.0</b>
<b>E. PRIMARY SURPLUS/DEFICIT (A-D)</b>	<b>3.7</b>	<b>5.6</b>	<b>4.4</b>	<b>3.8</b>	<b>3.3</b>	<b>1.9</b>	<b>(0.2)</b>	<b>0.2</b>	<b>0.8</b>	<b>(0.6)</b>	<b>0.6</b>

SOURCE: Department of Budget and Management

Appendix A (continued)  
**National Government Account Balance, 1981-2007**  
*In percent of GDP*

	2004	2005	2006	2007
<b>A. REVENUES</b>	<b>14.4</b>	<b>15.1</b>	<b>16.2</b>	<b>17.1</b>
1. Tax	12.3	13.0	14.3	14.0
Direct	5.7	6.0	6.2	10.7
Indirect	3.6	4.2	4.7	0.0
Taxes on International Trade	2.5	2.9	3.3	3.1
Other Offices	0.5	0.0	0.0	0.1
2. Nontax	2.1	2.0	2.0	3.1
<b>B. EXPENDITURES</b>	<b>18.3</b>	<b>17.4</b>	<b>17.3</b>	<b>17.2</b>
1. Current Operating Expenditures	15.4	15.0	15.0	14.2
Personal Services	5.8	5.5	5.4	5.3
Maintenance and Other Operating Expenditures	1.7	1.6	1.7	1.9
Interest Payments	5.4	5.5	5.1	4.0
Domestic	3.5	3.5	3.3	2.4
Foreign	1.9	2.0	1.9	1.7
Allotment to Local Government Units	2.3	2.3	2.3	2.3
Petroleum Price Stabilization Fund	0.0	0.0	0.0	0.0
Subsidies	0.1	0.2	0.2	0.3
Tax Expenditures	0.0	0.0	0.3	0.5
2. Capital Outlay	2.7	2.4	2.3	2.9
Infrastructure and Other Capital Outlays	1.9	1.7	1.6	2.1
Others	0.8	0.7	0.7	0.7
3. Net Lending	0.1	0.0	0.0	0.1
<b>C. NATIONAL GOVERNMENT ACCOUNT BALANCE</b>	<b>(3.8)</b>	<b>(2.3)</b>	<b>(1.1)</b>	<b>(0.1)</b>
<b>D. EXPENDITURES (excluding interest payments)</b>	<b>12.9</b>	<b>11.9</b>	<b>12.2</b>	<b>13.2</b>
<b>E. PRIMARY SURPLUS/DEFICIT (A-D)</b>	<b>1.5</b>	<b>3.2</b>	<b>4.1</b>	<b>3.9</b>

SOURCE: Department of Budget and Management

Appendix B

**NGAB, PSBR, CPSD, 1985-2007**

*In percent of GDP*

	1985	1986	1987	1988	1989	1990	1991	1992	1993	1994	1995	1996
<b>A. Public Sector Borrowing Requirement</b>	<b>(2.7)</b>	<b>(4.2)</b>	<b>(1.3)</b>	<b>(1.9)</b>	<b>(2.7)</b>	<b>(4.1)</b>	<b>(1.3)</b>	<b>(1.5)</b>	<b>(3.8)</b>	<b>(0.4)</b>	<b>(0.9)</b>	<b>(0.6)</b>
1. National Government	(1.9)	(5.1)	(2.4)	(2.9)	(2.1)	(3.5)	(2.1)	(1.2)	(1.5)	1.0	0.6	0.3
2. CB Restructuring	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	(1.0)	(1.4)	(1.0)	(0.6)
3. Monitored Nonfinancial Government Corporations (MNFGCs)	(1.4)	(1.1)	0.0	0.4	(0.3)	(1.8)	(0.6)	(0.8)	(1.7)	(0.6)	(0.1)	(0.5)
4. Oil Price Stabilization Fund	0.0	0.0	0.0	0.0	(0.9)	(0.1)	0.8	0.4	(0.5)	0.2	(0.5)	0.2
5. Adjustments of Net Lending and Equity to GOCCs	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
6. Other adjustments	0.6	2.1	1.1	0.6	0.7	1.2	0.6	0.1	1.0	0.4	0.1	0.1
<b>B. Other Public Sector</b>	<b>(2.9)</b>	<b>(2.3)</b>	<b>(0.5)</b>	<b>(1.2)</b>	<b>(1.4)</b>	<b>(0.6)</b>	<b>(0.7)</b>	<b>(0.4)</b>	<b>2.0</b>	<b>(0.0)</b>	<b>0.7</b>	<b>0.9</b>
1. Government Financial Institutions (GFIs)	(3.2)	(2.0)	0.1	0.2	0.3	0.3	0.2	0.3	0.4	0.2	0.3	0.4
2. Bangko Sentral ng Pilipinas (BSP)	(2.7)	(3.0)	(1.6)	(2.1)	(2.3)	(2.0)	(1.7)	(1.6)	(0.1)	0.3	0.2	(0.1)
3. SSS/GSIS	1.0	0.1	0.7	0.6	0.4	1.0	0.6	0.6	0.8	(0.7)	0.0	0.4
4. Local Government Units (LGUs)	0.1	0.1	0.1	0.1	0.2	0.2	0.1	0.1	0.4	0.3	0.1	0.3
5. Timing Adjustments of Interest Payments to BSP	1.9	2.5	0.1	0.0	(0.1)	0.0	0.0	0.2	0.5	(0.1)	0.1	(0.0)
6. Other Adjustments	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
<b>Consolidated public sector surplus/deficit</b>	<b>(5.6)</b>	<b>(6.5)</b>	<b>(1.8)</b>	<b>(3.1)</b>	<b>(4.1)</b>	<b>(4.7)</b>	<b>(2.1)</b>	<b>(1.9)</b>	<b>(1.8)</b>	<b>(0.5)</b>	<b>(0.2)</b>	<b>0.3</b>

Source: Department of Budget and Management, Fiscal Statistics Handbook 1983-2004, Bureau of Treasury

Memo item:

GDP (in Billion pesos: at current prices)	571.9	608.9	682.8	799.2	925.4	1077.2	1248.0	1351.6	1474.5	1692.9	1906.0	2171.9
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Appendix B

**NGAB, PSBR, CPSD, 1985-2007**

*In percent of GDP*

	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006 prelim	2007 revised
<b>A. Public Sector Borrowing Requirement</b>	<b>(1.6)</b>	<b>(4.2)</b>	<b>(4.6)</b>	<b>(5.2)</b>	<b>(5.2)</b>	<b>(6.8)</b>	<b>(6.4)</b>	<b>(5.8)</b>	<b>(3.4)</b>	<b>(1.3)</b>	<b>(1.3)</b>
1. National Government	0.1	(1.9)	(3.8)	(4.0)	(4.0)	(5.3)	(4.7)	(3.8)	(2.7)	(1.1)	(0.9)
2. CB Restructuring	(1.1)	(1.0)	(0.7)	(0.6)	(0.6)	(0.4)	(0.4)	(0.4)	(0.3)	(0.2)	(0.2)
3. Monitored Nonfinancial Government Corporations (MNFGCs)	(0.7)	(1.4)	(0.2)	(0.6)	(0.7)	(1.2)	(1.5)	(1.8)	(0.5)	(0.0)	(0.2)
4. Oil Price Stabilization Fund	(0.0)	0.0	0.1	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
5. Adjustments of Net Lending and Equity to GOCCs	0.0	0.0	0.1	0.1	0.1	0.1	0.1	0.2	0.0	(0.0)	0.1
6. Other adjustments	0.1	0.1	(0.2)	(0.2)	0.0	0.0	0.0	0.0	0.0	0.0	0.0
<b>B. Other Public Sector</b>	<b>0.6</b>	<b>1.1</b>	<b>1.4</b>	<b>0.8</b>	<b>0.6</b>	<b>1.3</b>	<b>1.2</b>	<b>1.0</b>	<b>1.6</b>	<b>1.4</b>	<b>0.9</b>
1. Government Financial Institutions (GFIs)	0.2	0.2	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1
2. Bangko Sentral ng Pilipinas (BSP)	0.1	0.1	(0.1)	0.0	(0.0)	0.0	0.2	0.1	0.1	0.0	0.0
3. SSS/GSIS	0.2	0.7	1.2	0.5	0.4	0.6	0.4	0.5	0.9	0.9	0.8
4. Local Government Units (LGUs)	0.1	0.1	0.3	0.2	0.0	0.5	0.5	0.3	0.4	0.4	0.1
5. Timing Adjustments of Interest Payments to BSP	0.1	(0.0)	(0.1)	0.0	(0.0)	(0.0)	0.0	0.1	0.1	(0.0)	(0.0)
6. Other Adjustments	0.0	0.0	0.0	0.0	0.0	0.0	0.1	(0.1)	(0.0)	(0.1)	0.0
<b>Consolidated public sector surplus/deficit</b>	<b>(1.0)</b>	<b>(3.1)</b>	<b>(3.2)</b>	<b>(4.4)</b>	<b>(4.7)</b>	<b>(5.5)</b>	<b>(5.2)</b>	<b>(4.8)</b>	<b>(1.9)</b>	<b>0.1</b>	<b>(0.3)</b>

Source: Department of Budget and Management, Fiscal Statistics Handbook 1983-2004, Bureau of Treasury

Memo item:

GDP (in Billion pesos: at current prices)	2426.7	2665.1	2976.9	3354.7	3631.5	3959.6	4293.0	4858.8	5418.8	6032.6	6651.3
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Appendix C  
**Budget Deficit Financing, 1981-2007**  
*In Billion Pesos, unless otherwise specified*

	1981	1982	1983	1984	1985	1986	1987	1988	1989	1990	1991	1992	1993	1994
<b>Financing</b>	<b>12.1</b>	<b>14.4</b>	<b>7.4</b>	<b>18.0</b>	<b>12.6</b>	<b>32.0</b>	<b>41.1</b>	<b>39.3</b>	<b>28.7</b>	<b>19.2</b>	<b>41.3</b>	<b>152.6</b>	<b>(15.7)</b>	<b>(22.0)</b>
Net foreign	6.0	4.6	5.4	2.0	(0.3)	3.6	6.8	4.2	8.2	4.1	6.9	14.4	12.9	(11.6)
Net domestic	6.1	9.8	2.0	16.0	12.9	28.4	34.3	35.1	20.5	15.1	34.4	138.2	(28.6)	(10.4)
<b>Percent share</b>														
Net foreign	49.6	31.9	73.0	11.1	(2.4)	11.2	16.5	10.7	28.6	21.3	16.7	9.4	(82.3)	52.8
Net domestic	50.4	68.1	27.0	88.9	102.4	88.8	83.5	89.3	71.4	78.7	83.3	90.6	182.3	47.2

Source: Government authorities

	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007
<b>Financing</b>	<b>11.0</b>	<b>43.4</b>	<b>(27.1)</b>	<b>88.9</b>	<b>181.7</b>	<b>203.8</b>	<b>175.2</b>	<b>264.2</b>	<b>286.8</b>	<b>242.5</b>	<b>236.0</b>	<b>110.1</b>	<b>99.1</b>
Net foreign	(13.3)	(5.9)	(6.8)	12.3	82.8	84.4	22.9	109.1	143.9	81.2	92.7	120.8	56.2
Net domestic	24.3	49.3	(20.3)	76.6	98.9	119.5	152.3	155.0	143.0	161.4	143.3	(10.6)	42.9
<b>Percent share</b>													
Net foreign	(120.7)	(13.6)	25.1	13.8	45.6	41.4	13.1	41.3	50.2	33.5	39.3	109.7	56.7
Net domestic	220.7	113.6	74.9	86.2	54.4	58.6	86.9	58.7	49.8	66.5	60.7	(9.7)	43.3

Source: Government authorities

Appendix D  
**Philippines: Public Debt Statistics, 1981-2007**  
 In Million pesos, unless otherwise specified

	1981	1982	1983	1984	1985
<b>A. National Government Outstanding Debt</b>					
1. Domestic Debt	28,925	35,619	41,685	62,639	82,533
2. Foreign Debt	20,015	25,112	14,820	61,110	59,818
3. Total Debt	48,940	60,731	56,505	123,749	142,351
<i>As A Percentage of GDP</i>					
4. Domestic Debt	9.5	10.5	11.3	11.9	14.4
5. Foreign Debt	6.6	7.4	4.0	11.7	10.5
6. Total Debt	16.0	17.8	15.3	23.6	24.9
<i>As A Percentage of Total Outstanding Debt</i>					
7. Domestic Debt	59.1	58.7	73.8	50.6	58.0
8. Foreign Debt	40.9	41.3	26.2	49.4	42.0
<b>B. Debt Service Expenditures</b>					
1. Interest Payment	2,429	3,560	4,997	10,409	14,652
a. Domestic	1,445	2,312	2,615	5,785	10,261
b. Foreign	984	1,248	2,382	4,624	4,391
2. Amorization	1,468	1,332	3,451	4,473	6,951
a. Domestic	736	541	1,203	1,408	2,907
b. Foreign	732	791	2,248	3,065	4,044
3. Total	3,897	4,892	8,448	14,882	21,603
a. Domestic	2,181	2,853	3,818	7,193	13,168
b. Foreign	1,716	2,039	4,630	7,689	8,435
<i>As a Percentage of GDP</i>					
4. Total	1.3	1.4	2.3	2.8	3.8
a. Domestic	0.7	0.8	1.0	1.4	2.3
b. Foreign	0.6	0.6	1.3	1.5	1.5
<i>As A Percent of Total Debt Service Expenditures</i>					
5. Total					
a. Domestic	56.0	58.3	45.2	48.3	61.0
b. Foreign	44.0	41.7	54.8	51.7	39.0
<b>C. Total Debt Service Expenditures as Share of total spending</b>					
1. Total Debt Servicing	8.1	9.3	15.9	22.2	27.0
a. Domestic	4.5	5.4	7.2	10.7	16.4
b. Foreign	3.6	3.9	8.7	11.5	10.5
<b>D. Debt servicing as percent of tax revenues</b>					
1. Interest payments	7.7	10.5	12.5	20.8	23.9
a. Domestic	4.6	6.8	6.6	11.5	16.8
b. Foreign	3.1	3.7	6.0	9.2	7.2
2. Total debt servicing	12.4	14.5	21.2	29.7	35.3
a. Domestic	6.9	8.4	9.6	14.4	21.5
b. Foreign	5.5	6.0	11.6	15.3	13.8

Source: National Statistical Coordination Board in Philippine Statistical Yearbook

MEMO ITEMS:

1. GDP (in Million pesos: at current prices)	305260	340599	369077	524481	571883
2. Tax revenues (in current prices, Million pesos)	31423	33800	39848	50118	61190
3. Total expenditures	48079	52610	53064	66926	80102



Appendix D (continued)  
**Philippines: Public Debt Statistics, 1981-2007**

	1986	1987	1988	1989	1990
<b>A. National Government Outstanding Debt</b>					
1. Domestic Debt	201,270	229,687	265,447	289,330	300,441
2. Foreign Debt	174,175	195,082	192,888	198,496	299,764
3. Total Debt	375,445	424,769	458,335	487,826	600,205
<i>As A Percentage of GDP</i>					
4. Domestic Debt	33.1	33.6	33.2	31.3	27.9
5. Foreign Debt	28.6	28.6	24.1	21.4	27.8
6. Total Debt	61.7	62.2	57.4	52.7	55.7
<i>As A Percentage of Total Outstanding Debt</i>					
7. Domestic Debt	53.6	54.1	57.9	59.3	50.1
8. Foreign Debt	46.4	45.9	42.1	40.7	49.9
<b>B. Debt Service Expenditures</b>					
1. Interest Payment	21,612	36,905	45,865	54,714	71,114
a. Domestic	15,022	24,224	32,183	41,032	53,323
b. Foreign	6,590	12,681	13,682	13,682	17,791
2. Amorization	13,201	32,920	25,299	28,503	35,232
a. Domestic	7,012	24,281	12,251	16,760	14,952
b. Foreign	6,189	8,639	13,048	11,743	20,280
3. Total	34,813	69,825	71,164	83,217	106,346
a. Domestic	22,034	48,505	44,434	57,792	68,275
b. Foreign	12,779	21,320	26,730	25,425	38,071
<i>As a Percentage of GDP</i>					
4. Total	5.7	10.2	8.9	9.0	9.9
a. Domestic	3.6	7.1	5.6	6.2	6.3
b. Foreign	2.1	3.1	3.3	2.7	3.5
<i>As A Percent of Total Debt Service Expenditures</i>					
5. Total					
a. Domestic	63.3	69.5	62.4	69.4	64.2
b. Foreign	36.7	30.5	37.6	30.6	35.8
<b>C. Total Debt Service Expenditures as Share of total spending</b>					
1. Total Debt Servicing	31.5	58.2	52.3	48.4	48.8
a. Domestic	19.9	40.5	32.7	33.6	31.3
b. Foreign	11.6	17.8	19.6	14.8	17.5
<b>D. Debt servicing as percent of tax revenues</b>					
1. Interest payments	33.0	43.0	50.8	44.7	46.9
a. Domestic	22.9	28.2	35.6	33.5	35.2
b. Foreign	10.1	14.8	15.1	11.2	11.7
2. Total debt servicing	53.2	81.3	78.8	68.0	70.1
a. Domestic	33.6	56.5	49.2	47.2	45.0
b. Foreign	19.5	24.8	29.6	20.8	25.1
Source: National Statistical Coordination Board in Philippine Statistical Yearbook					
MEMO ITEMS:					
1. GDP (in Million pesos: at current prices)	608887	682764	799182	925444	1077237
2. Tax revenues (in current prices, Million pesos)	65491	85923	90352	122462	151700
3. Total expenditures	110497	119907	136067	171978	218096

Appendix D (continued)  
**Philippine Public Debt Statistics, 1981-2007**

	1991	1992	1993	1994	1995
<b>A. National Government Outstanding Debt</b>					
1. Domestic Debt	337,890	497,917	676,867	664,978	718,395
2. Foreign Debt	334,898	372,897	449,025	416,177	440,227
3. Total Debt	672,788	870,814	1,125,892	1,081,155	1,158,622
<i>As A Percentage of GDP</i>					
4. Domestic Debt	27.1	36.8	45.9	39.3	37.7
5. Foreign Debt	26.8	27.6	30.5	24.6	23.1
6. Total Debt	53.9	64.4	76.4	63.9	60.8
<i>As A Percentage of Total Outstanding Debt</i>					
7. Domestic Debt	50.2	57.2	60.1	61.5	62.0
8. Foreign Debt	49.8	42.8	39.9	38.5	38.0
<b>B. Debt Service Expenditures</b>					
1. Interest Payment	74,922	79,571	76,491	79,123	72,658
a. Domestic	56,347	63,113	56,183	59,806	50,805
b. Foreign	18,575	16,458	20,308	19,317	21,853
2. Amorization	46,560	29,651	36,887	38,844	64,517
a. Domestic	30,354	9,898	11,574	14,981	34,338
b. Foreign	16,206	19,753	25,313	23,863	30,179
3. Total	121,482	109,222	113,378	117,967	137,175
a. Domestic	86,701	73,011	67,757	74,787	85,143
b. Foreign	34,781	36,211	45,621	43,180	52,032
<i>As a Percentage of GDP</i>					
4. Total	9.7	8.1	7.7	7.0	7.2
a. Domestic	6.9	5.4	4.6	4.4	4.5
b. Foreign	2.8	2.7	3.1	2.6	2.7
<i>As A Percent of Total Debt Service Expenditures</i>					
5. Total					
a. Domestic	71.4	66.8	59.8	63.4	62.1
b. Foreign	28.6	33.2	40.2	36.6	37.9
<b>C. Total Debt Service Expenditures as Share of total spending</b>					
1. Total Debt Servicing	49.2	42.2	40.2	36.9	39.2
a. Domestic	35.1	28.2	24.0	23.4	24.3
b. Foreign	14.1	14.0	16.2	13.5	14.9
<b>D. Debt servicing as percent of tax revenues</b>					
1. Interest payments	41.1	38.1	33.2	29.2	23.4
a. Domestic	30.9	30.2	24.4	22.0	16.4
b. Foreign	10.2	7.9	8.8	7.1	7.0
2. Total debt servicing	66.6	52.3	49.3	43.5	44.2
a. Domestic	47.6	35.0	29.4	27.6	27.4
b. Foreign	19.1	17.4	19.8	15.9	16.8

Source: National Statistical Coordination Board in Philippine Statistical Yearbook

MEMO ITEMS:

1. GDP (in Million pesos: at current prices)	1248011	1351559	1474457	1692932	1905951
2. Tax revenues (in current prices, Million pesos)	182275	208706	230170	271305	310517
3. Total expenditures	247136	258680	282296	319874	350146

Appendix D (continued)  
**Philippine Public Debt Statistics, 1981-2007**

	1996	1997	1998	1999	2000
<b>A. National Government Outstanding Debt</b>					
1. Domestic Debt	742,057	749,608	850,931	978,404	1,068,200
2. Foreign Debt	413,180	600,966	645,290	796,952	1,098,510
3. Total Debt	1,155,237	1,350,574	1,496,221	1,775,356	2,166,710
<i>As A Percentage of GDP</i>					
4. Domestic Debt	34.2	30.9	31.9	32.9	31.8
5. Foreign Debt	19.0	24.8	24.2	26.8	32.7
6. Total Debt	53.2	55.7	56.1	59.6	64.6
<i>As A Percentage of Total Outstanding Debt</i>					
7. Domestic Debt	64.2	55.5	56.9	55.1	49.3
8. Foreign Debt	35.8	44.5	43.1	44.9	50.7
<b>B. Debt Service Expenditures</b>					
1. Interest Payment	76,522	77,971	99,792	106,290	140,894
a. Domestic	59,002	58,350	73,525	74,980	93,575
b. Foreign	17,520	19,621	26,267	31,310	47,319
2. Amorization	41,220	47,678	64,717	99,106	86,949
a. Domestic	13,260	17,865	28,761	61,552	45,429
b. Foreign	27,960	29,813	35,956	37,554	41,520
3. Total	117,742	125,649	164,509	205,396	227,843
a. Domestic	72,262	76,215	102,286	136,532	139,004
b. Foreign	45,480	49,434	62,223	68,864	88,839
<i>As a Percentage of GDP</i>					
4. Total	5.4	5.2	6.2	6.9	6.8
a. Domestic	3.3	3.1	3.8	4.6	4.1
b. Foreign	2.1	2.0	2.3	2.3	2.6
<i>As A Percent of Total Debt Service Expenditures</i>					
5. Total					
a. Domestic	61.4	60.7	62.2	66.5	61.0
b. Foreign	38.6	39.3	37.8	33.5	39.0
<b>C. Total Debt Service Expenditures as Share of total spending</b>					
1. Total Debt Servicing	29.1	26.7	32.1	34.8	35.1
a. Domestic	17.9	16.2	20.0	23.1	21.4
b. Foreign	11.3	10.5	12.1	11.7	13.7
<b>D. Debt servicing as percent of tax revenues</b>					
1. Interest payments	20.8	18.9	24.0	24.6	30.6
a. Domestic	16.0	14.2	17.6	17.4	20.3
b. Foreign	4.8	4.8	6.3	7.3	10.3
2. Total debt servicing	32.0	30.5	39.5	47.6	49.5
a. Domestic	19.6	18.5	24.6	31.6	30.2
b. Foreign	12.4	12.0	14.9	16.0	19.3
Source: National Statistical Coordination Board in Philippine Statistical Yearbook					
MEMO ITEMS:					
1. GDP (in Million pesos: at current prices)	2171922	2426743	2665060	2976905	3354727
2. Tax revenues (in current prices, Million pesos)	367895	412165	416585	431687	460034
3. Total expenditures	404195	470279	512497	590161	648974

Appendix D (continued)  
**Philippine Public Debt Statistics, 1981-2007**

	2001	2002	2003	2004
<b>A. National Government Outstanding Debt</b>				
1. Domestic Debt	1,247,683	1,471,202	1,703,781	2,001,220
2. Foreign Debt	1,137,234	1,344,266	1,651,327	1,810,734
3. Total Debt	2,384,917	2,815,468	3,355,108	3,811,954
<i>As A Percentage of GDP</i>				
4. Domestic Debt	34.4	37.2	39.6	41.2
5. Foreign Debt	31.3	33.9	38.4	37.3
6. Total Debt	65.7	71.1	78.0	78.5
<i>As A Percentage of Total Outstanding Debt</i>				
7. Domestic Debt	52.3	52.3	50.8	52.5
8. Foreign Debt	47.7	47.7	49.2	47.5
<b>B. Debt Service Expenditures</b>				
1. Interest Payment	174,834	185,861	226,408	260,901
a. Domestic	112,592	119,985	147,565	169,997
b. Foreign	62,242	65,876	78,843	90,904
2. Amortization	99,605	172,098	243,582	340,771
a. Domestic	54,038	80,944	147,322	222,405
b. Foreign	45,567	91,154	96,260	118,366
3. Total	274,439	357,959	469,990	601,672
a. Domestic	166,630	200,929	294,887	392,402
b. Foreign	107,809	157,030	175,103	209,270
<i>As a Percentage of GDP</i>				
4. Total	7.6	9.0	10.9	12.4
a. Domestic	4.6	5.1	6.9	8.1
b. Foreign	3.0	4.0	4.1	4.3
<i>As A Percent of Total Debt Service Expenditures</i>				
5. Total				
a. Domestic	60.7	56.1	62.7	65.2
b. Foreign	39.3	43.9	37.3	34.8
<b>C. Total Debt Service Expenditures as Share of total spending</b>				
1. Total Debt Servicing	38.6	46.0	56.9	67.8
a. Domestic	23.4	25.8	35.7	44.2
b. Foreign	15.2	20.2	21.2	23.6
<b>D. Debt servicing as percent of tax revenues</b>				
1. Interest payments	35.7	37.4	42.1	43.6
a. Domestic	23.0	24.2	27.4	28.4
b. Foreign	12.7	13.3	14.7	15.2
2. Total debt servicing	56.0	72.1	87.4	100.6
a. Domestic	34.0	40.5	54.8	65.6
b. Foreign	22.0	31.6	32.6	35.0

Source: National Statistical Coordination Board in Philippine Statistical Yearbook

MEMO ITEMS:

1. GDP (in Million pesos: at current prices)	3631474	3959648	4299932	4858835
2. Tax revenues (in current prices, Million pesos)	489860	496372	537684	598014
3. Total expenditures	710756	777881	826497	886826

Appendix D (continued)  
**Philippine Public Debt Statistics, 1981-2007**

	2005	2006	2007
<b>A. National Government Outstanding Debt</b>			
1. Domestic Debt	2,164,293	2,154,078	2,201,167
2. Foreign Debt	1,723,938	1,697,428	1,511,320
3. Total Debt	3,888,231	3,851,506	3,712,487
<i>As A Percentage of GDP</i>			
4. Domestic Debt	39.9	35.7	33.1
5. Foreign Debt	31.8	28.1	22.7
6. Total Debt	71.8	63.8	55.8
<i>As A Percentage of Total Outstanding Debt</i>			
7. Domestic Debt	55.7	55.9	59.3
8. Foreign Debt	44.3	44.1	40.7
<b>B. Debt Service Expenditures</b>			
1. Interest Payment	299,807	310,108	267,800
a. Domestic	190,352	197,263	157,220
b. Foreign	109,455	112,845	110,580
2. Amorization	379,144	544,266	346,269
a. Domestic	253,492	380,939	284,017
b. Foreign	125,652	163,327	62,252
3. Total	678,951	854,374	2,014,069
a. Domestic	443,844	578,202	1,841,237
b. Foreign	235,107	276,172	172,832
<i>As a Percentage of GDP</i>			
4. Total	12.5	14.2	9.2
a. Domestic	8.2	9.6	6.6
b. Foreign	4.3	4.6	2.6
<i>As A Percent of Total Debt Service Expenditures</i>			
5. Total			
a. Domestic	65.4	67.7	71.9
b. Foreign	34.6	32.3	28.1
<b>C. Total Debt Service Expenditures as Share of total spending</b>			
1. Total Debt Servicing	72.0	81.8	53.6
a. Domestic	47.1	55.4	38.5
b. Foreign	24.9	26.4	15.1
<b>D. Debt servicing as percent of tax revenues</b>			
1. Interest payments	42.5	36.1	28.7
a. Domestic	27.0	22.9	16.9
b. Foreign	15.5	13.1	11.9
2. Total debt servicing	96.2	99.4	65.8
a. Domestic	62.9	67.2	47.3
b. Foreign	33.3	32.1	18.5

Source: National Statistical Coordination Board in Philippine Statistical Yearbook

**MEMO ITEMS:**

1. GDP (in Million pesos: at current prices)	5418839	6032624	6651320
2. Tax revenues (in current prices, Million pesos)	705615	859857	932937
3. Total expenditures	942487	1044430	1145100

Appendix E  
**Fiscal Performance: An Overview**

Per capita, real terms (2000= 100)

	1981	1982	1983	1984	1985	1986	1987	1988	1989
<b>A. Nominal terms (in Million PhP)</b>									
1. Total disbursement	48,079	52,610	53,064	66,926	80,102	110,497	119,907	136,067	171,978
2. Interest payments	2,429	3,560	4,997	10,409	14,652	21,612	36,905	45,865	54,714
3. Net lending	929	2,218	2,393	4,423	2,555	15,148	7,077	5,415	3,666
4. Total disbursement net of IP and NL	44,721	46,832	45,674	52,094	62,895	73,737	75,925	84,787	113,598
5. Total revenues	35,933	38,206	45,632	56,861	68,961	79,245	103,214	112,861	152,410
<b>B. In real terms (2000=100, in Million PhP)</b>									
1. Total disbursement	363,159	360,444	330,539	277,293	269,574	369,039	385,912	402,648	453,579
2. Interest payments	18,347	24,390	31,127	43,127	49,310	72,180	118,776	135,723	144,304
3. Net lending	7,017	15,196	14,906	18,326	8,599	50,591	22,777	16,024	9,669
4. Total disbursement net of IP and NL	337,794	320,857	284,506	215,840	211,666	246,268	244,359	250,901	299,606
5. Total revenues	271,415	261,758	284,244	235,591	232,080	264,663	332,187	333,977	401,970
<b>C. Per capita, real terms</b>									
1. Total disbursement	7,331	7,098	6,349	5,232	4,970	6,647	6,791	6,922	7,618
2. Interest payments	370	480	598	814	909	1,300	2,090	2,333	2,424
3. Net lending	142	299	286	346	159	911	401	275	162
4. Total disbursement net of IP and NL	6,819	6,319	5,465	4,072	3,902	4,436	4,300	4,313	5,032
5. Total revenues	5,479	5,155	5,460	4,445	4,279	4,767	5,845	5,741	6,751
6. Net fiscal benefit per capita (C.4-C.5)	1,340	1,164	5	(373)	(376)	(331)	(1,545)	(1,428)	(1,719)
Source: Government Authorities									
Memo items:									
Deflator (2000=100), NSCB	0.13	0.15	0.16	0.24	0.30	0.30	0.31	0.34	0.38
Population, DBM and NSO	49.54	50.78	52.06	53	54.24	55.52	56.83	58.17	59.54

Appendix E  
**Fiscal Performance: An Overview**

Per capita, real terms (2000= 100)

	1990	1991	1992	1993	1994	1995	1996	1997	1998
<b>A. Nominal terms (in Million PhP)</b>									
1. Total disbursement	218,096	247,136	258,680	282,296	319,874	350,146	404,195	470,279	512,497
2. Interest payments	71,114	74,922	79,571	76,491	79,123	72,658	76,522	77,971	99,792
3. Net lending	3,787	5,725	2,258	2,649	5,893	3,696	1,161	1,381	329
4. Total disbursement net of IP and NL	143,195	166,489	176,851	203,156	234,858	273,792	326,512	390,927	412,376
5. Total revenues	180,902	220,787	242,714	260,405	336,160	361,220	410,450	471,843	462,516
<b>B. In real terms (2000=100, in Million PhP)</b>									
1. Total disbursement	503,815	461,075	461,105	454,583	466,289	478,342	513,590	565,919	564,424
2. Interest payments	164,278	139,780	141,838	123,174	115,340	99,260	97,233	93,828	109,903
3. Net lending	8,748	10,681	4,025	4,266	8,590	5,049	1,475	1,662	362
4. Total disbursement net of IP and NL	330,789	310,614	315,242	327,143	342,359	374,033	414,882	470,430	454,159
5. Total revenues	417,895	411,916	432,645	419,332	490,029	493,470	521,537	567,801	509,379
<b>C. Per capita, real terms</b>									
1. Total disbursement	8,267	7,394	7,225	6,959	6,976	6,992	7,336	7,898	7,698
2. Interest payments	2,696	2,241	2,222	1,886	1,726	1,451	1,389	1,310	1,499
3. Net lending	144	171	63	65	129	74	21	23	5
4. Total disbursement net of IP and NL	5,428	4,981	4,940	5,008	5,122	5,468	5,926	6,566	6,194
5. Total revenues	6,857	6,605	6,779	6,420	7,331	7,213	7,449	7,925	6,947
6. Net fiscal benefit per capita (C.4-C.5)	(1,429)	(1,624)	(1,840)	(1,411)	(2,209)	(1,746)	(1,523)	(1,359)	(753)
Source: Government Authorities									
Memo items:									
Deflator (2000=100), NSCB	0.43	0.54	0.56	0.62	0.69	0.73	0.79	0.83	0.91
Population, DBM and NSO	60.94	62.36	63.82	65.32	66.84	68.41	70.01	71.65	73.32

Appendix E  
**Fiscal Performance: An Overview**

Per capita, real terms (2000= 100)

	1999	2000	2001	2002	2003	2004	2005	2006	2007
<b>A. Nominal terms (in Million PhP)</b>									
1. Total disbursement	590,161	648,974	710,756	777,881	826,497	886,826	942,487	1,044,430	1,145,100
2. Interest payments	106,290	140,894	174,834	185,861	226,408	260,901	299,807	310,108	267,800
3. Net lending	3,193	2,634	3,944	2,626	5,620	5,676	1,707	131	9,800
4. Total disbursement net of IP and NL	480,678	505,446	531,978	589,394	594,469	620,249	640,973	734,191	867,500
5. Total revenues	478,503	514,762	563,733	567,141	626,630	699,768	816,159	979,637	1,136,560
<b>B. In real terms (2000=100, in Million PhP)</b>									
1. Total disbursement	613,473	648,974	665,502	707,165	726,272	735,345	726,107	757,382	807,546
2. Interest payments	110,489	140,894	163,702	168,965	198,953	216,336	230,976	224,879	188,858
3. Net lending	3,319	2,634	3,693	2,387	4,938	4,706	1,315	95	6,911
4. Total disbursement net of IP and NL	499,665	505,446	498,107	535,813	522,380	514,303	493,816	532,408	611,777
5. Total revenues	497,404	514,762	527,840	515,583	550,641	580,239	628,782	710,397	801,523
<b>C. Per capita, real terms</b>									
1. Total disbursement	8,175	8,451	8,493	8,845	8,902	8,833	8,548	8,738	9,221
2. Interest payments	1,472	1,835	2,089	2,113	2,439	2,599	2,719	2,594	2,157
3. Net lending	44	34	47	30	61	57	15	1	79
4. Total disbursement net of IP and NL	6,659	6,582	6,357	6,701	6,403	6,178	5,813	6,142	6,986
5. Total revenues	6,629	6,704	6,736	6,448	6,749	6,970	7,402	8,195	9,152
6. Net fiscal benefit per capita (C.4-C.5)	30	(121)	(379)	253	(346)	(792)	(1,589)	(2,053)	(2,167)
Source: Government Authorities									
Memo items:									
Deflator (2000=100), NSCB	0.96	1.00	1.07	1.10	1.14	1.21	1.30	1.38	1.42
Population, DBM and NSO	75.04	76.79	78.36	79.95	81.59	83.25	84.95	86.68	87.57



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