15 Ensuring Sound Macroeconomic Policy

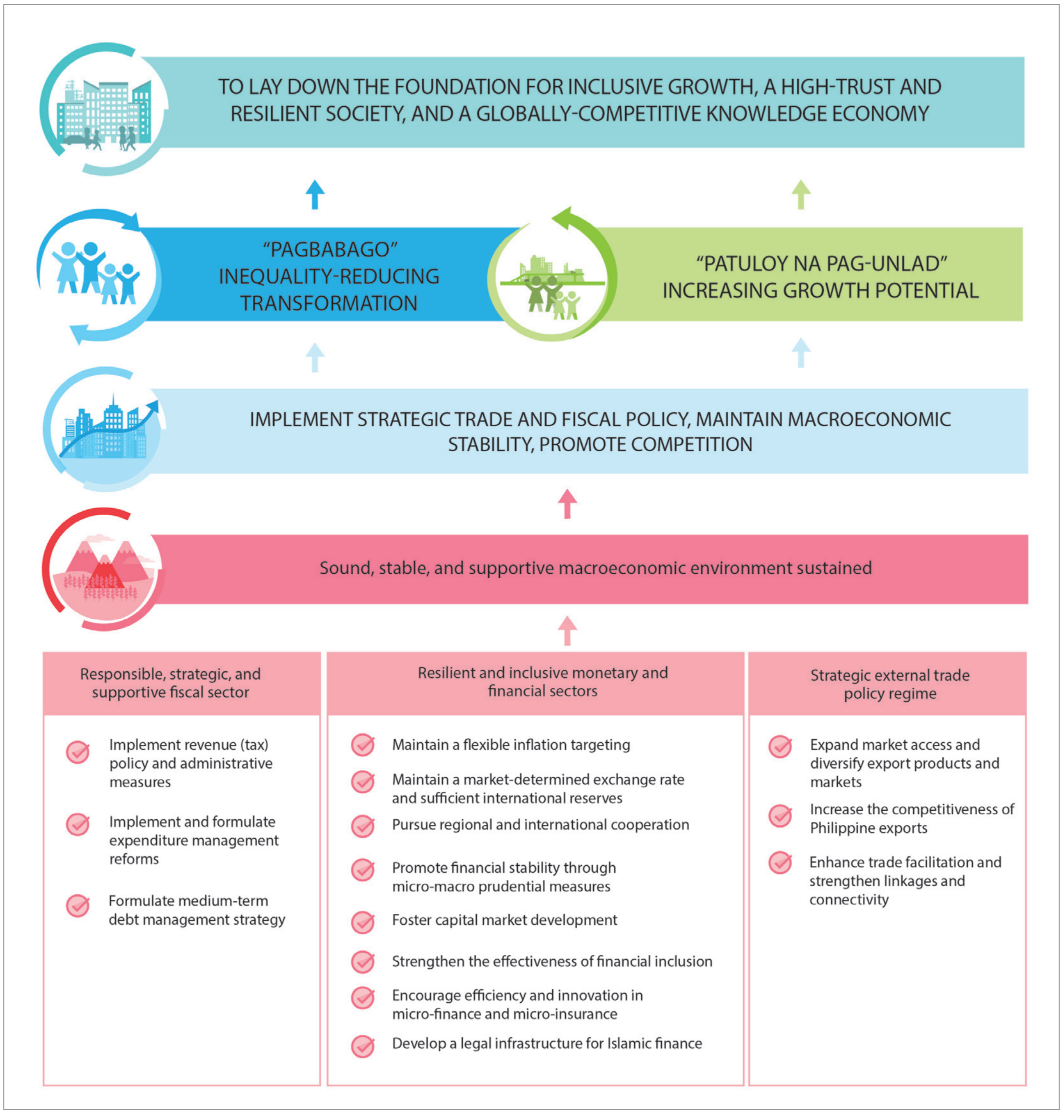
CHAPTER 15

Ensuring Sound Macroeconomic Policy

The country's macroeconomic fundamentals remained conducive to supporting a dynamic and sustainable economic growth trajectory, pushing the 2017 gross domestic product (GDP) growth to 6.7 percent. Effective monetary policy and a strong financial sector also ensured overall price stability which has supported the expansion of access to economic opportunities. Moreover, improved government revenue performance, the passage of the first package of the Tax Reform for Acceleration and Inclusion (TRAIN) Act, as well as improvements in transparency and expenditure and debt management, are expected to push key government programs that will improve the country's competitiveness and sustain growth momentum.

Notwithstanding the gains, much remains to be done to maintain the economy's solid foundation and promote an enabling and supportive macroeconomic environment. Policy and administrative reforms need to be advanced to sustain recent improvements in revenue performance. Absorptive capacity of implementing agencies need to be improved to ensure the accomplishment of the government expenditure program. Financial market infrastructures should be strengthened and financial inclusion should be improved further to support a more robust and inclusive economic growth. Trade facilitation should also be improved to make the country more integrated in the global production networks (*See Figure 15.1*).

Figure 15.1 Strategic Framework to Sustain a Sound, Stable, and Supportive Macroeconomic Environment



Accomplishments

National Government (NG) overall revenue target was attained and the first package of the comprehensive tax reform program was passed. Revenue effort in 2017 reached 15.7 percent, slightly surpassing the target of 15.6 percent, on the back of an intensified tax administration. Tax effort improved to 14.2 percent but fell short of the 14.5 percent target. The Bureau of Internal Revenue (BIR) missed its target by only 1 percent, even as its collections grew by 13 percent. Bureau of Customs revenues were up by 16 percent and almost on target. Local sources of local government units' (LGUs) revenue as a share of total current operating income also increased to 35.7 percent as of third quarter of 2017, compared to the full-year target of 35.4 percent. This is due to increases in real property and business taxes.

The first package of the tax reform program was passed into law in December 2017, benefiting 99 percent of taxpayers from the progressive reduction in personal income taxes. However, if the numerous mitigating measures approved by Congress (e.g., unconditional cash transfers, fuel subsidy, etc.) are fully implemented, the additional expenditures could exceed the funds earmarked from incremental revenues.

Overall spending remained below target despite improvements in infrastructure spending. Total government expenditure increased by 10.8 percent in 2017, driven by the strong upturn in capital outlays. Primary spending (i.e., expenditures net of interest payments) increased to 15.9 percent of GDP in 2017, but fell short of the target of 16.5 percent. Infrastructure and other capital outlay increased by 15.4 percent and exceeded its target by 3.5 percent. However, personnel services recorded an 8.4 percent underspending despite an 11.8 percent growth, while maintenance and other operating expenses fell short of the program by 1.9 percent despite a 10.8 percent growth. On the other hand, lower interest payments provided additional fiscal space for the government. As a result, total expenditures were 2.9 percent below target despite a 10.8 percent increase. The budget deficit also declined to 2.2 percent of GDP, smaller than the 2.4 percent incurred in 2016, and below the 3 percent target.

Government debt remained sustainable. NG outstanding debt stabilized at 42.1 percent of GDP in 2017, 1.1 percentage point above the full-year target of 41 percent, due to the pre-funding activity undertaken for 2018. The share of foreign debt declined to 33.2 percent (₱2.2 trillion) of the total debt. The average residual maturity of NG debt declined to 9.8 years, still within the target of 7 to 10 years. For 2017, 18.6 percent of gross financing came from foreign borrowing, lower than the target of 20 percent.

Inflation increased but remained within the target range, allowing the Bangko Sentral ng Pilipinas (BSP) to keep key policy rates unchanged. Headline inflation rose to 2.9 percent in 2017[1] from 1.3 percent in 2016, which is well within the 2.0-4.0 percent target. The uptick was driven mainly by higher prices of food, petroleum products, and electricity rates during the review period.

The financial system registered moderate growth, while financial inclusion improved. Total resources of the financial system grew in line with the target by 10 percent to ₱18.9 trillion in end-December 2017. Total assets of the banking system expanded by 11.6 percent, supported by more stable funding base from deposits and a diversified loan portfolio. The value of outstanding microfinance loans increased by 24.5 percent to ₱17.1 billion in end-December 2017, well above the ₱10 billion target for 2017. Microinsurance penetration also expanded to 30.5 percent of the total population as of the third quarter of 2017. This is supported by the number of access points per 10,000 adults, which increased by 5.3 percent to 9.7 as of September 2017, only slightly below the target of 10 for 2017. The BSP rolled out the Basic Deposit Account which features simplified know-your-customer requirements, opening deposit amount of less than ₱100, no minimum maintaining balance, no dormancy charges, and zero reserve requirement.

[1] Based on the new 2012-based Consumer Price Index series.

Reforms in capital markets were undertaken. Recent capital market reforms include legislative and regulatory changes to encourage the contractual savings sector to purchase longer-term maturity investments and infrastructure bonds. New listing rules also allow public-private partnership projects to raise capital through the stock market. In addition, the Expanded Primary Dealer System was launched in November 2017 to reduce the cost of debt through competition. Also, a repurchase market in the Philippines that adheres to international standards was reintroduced in the last quarter of 2017 to strengthen the linkage between domestic and global banks.

Retail payment systems were strengthened. The framework for the National Retail Payment System (NRPS) was adopted to facilitate more convenient, affordable, and secure electronic fund transfers (EFT) and e-payments, thereby encouraging a shift from a cash-heavy to a cash-lite society. As one of the automated clearing houses under the NRPS, the Philippine EFT System and Operations Network for batch EFT credit payment was also rolled out last year.

Platforms to harness the investment potential of overseas Filipinos (OF) remittances were implemented. As of September 2017, a total of 401 Personal Equity and Retirement Accounts were opened, amounting to ₱23.4 million. The costs of sending remittances as a proportion of the amount remitted also fell from 4.7 percent in the fourth quarter of 2016 to 4.3 percent as of third quarter of 2017. As part of the Overseas Workers Welfare Administration's (OWWA) OF reintegration program, financial literacy campaigns were conducted onsite (in destination countries) and in-country[2] to encourage the participation of OFs in economic governance. Meanwhile, the Commission on Filipinos Overseas used social media and mobile application to promote its PESO Sense initiative to reach Filipinos abroad.

Anti-money laundering/financing of terrorism regulatory regime was improved. The first Philippine National Money Laundering and Terrorist Financing Risk Assessment was conducted along with issuances of BSP Circulars to enhance the regulatory framework for money service businesses[3] and to introduce a more risk-based approach, particularly in relation to the conduct of customer due diligence. Efforts to mitigate potential risks associated with the use of virtual currencies (VCs) have also been initiated, such as the issuance of BSP Circular No. 944 to govern the conversion or exchange of any VC into fiat currency or vice versa.

Exports sector exceeded the 2017 target. Exports increased by 12.8 percent to US$48.2 billion, surpassing the target of US$45.1 billion.[4] Electronic products still comprised half (52%) of total exports of goods in 2017. Japan (16%) remained the top export market, followed by United States of America, European Union, and ASEAN each comprising 15 percent, followed by Hong Kong (14%) and China (11%). Similarly, services exports in 2017 grew by 14.1 percent to US$35.6 billion, exceeding the 2017 target of US$34.5 billion. Other business services, including Information Technology-Business Processing Management (IT-BPM),[5] accounted for almost half (47%) of total services exports, followed by travel services (20%) and telecommunications, computer, and information services (16%). However, a 14.2 percent increase in imports to $89.4 billion led the current account deficit to widen to US$2.5 billion or -0.8 percent of GDP in 2017, which is below the full-year target of a surplus of 0.2 percent of GDP.[6]

---

[2] As of September 2017, under the onsite Reintegration Preparedness Program, a total of 171 sessions with 6,381 participants were conducted in 31 posts overseas. For in-country, through the 17 OWWA Regional Welfare Offices, a total of 353 sessions with 15,016 participants (OF Workers and/or their families) were conducted. From Q1-Q3 2017, the BSP conducted eight (8) Financial Literacy Campaigns attended by 1,182 participants.

[3] Covering remittance and transfer companies, money changers, and foreign exchange dealers

[4] Actual and target figures are based on the Balance of Payments compiled by BSP. In terms of data released by PSA, merchandise exports reached US$62.9 billion and grew by 9.5 percent for 2017.

[5] Including research and development services, professional and management consulting services and technical, trade-related, and other business services.

[6] Bangko Sentral ng Pilipinas. BSP revises Balance of Payments Projections for 2017. Retrieved from http://www.bsp.gov.ph/publications/media.asp?id=4560

Support to the country's exporters continue to increase. The number of Department of Trade and Industry (DTI)-assisted technology-enabled and technology-based exporters was recorded at 204, more than double the 2017 target of 100. These exporters apply technology innovation[7] to compete in the global market. The number of enrollees[8] who were able to export under the Regional Interactive Platform for Philippine Exporters Plus (RIPPLES Plus) program reached 408 which is 104 percent higher than the target of 200 exporters for the year. New export products certified as *halal* were almost thrice the minimum target of 100 for 2017, with 280 products registered in 2017.

Initiatives to facilitate trade are being implemented. The continued development of online platforms and use of technology in transactions with government such as the TradeNet as the National Single Window (NSW) platform and the Philippine National Trade Repository (PNTR), are steps in the right direction to lower the costs of doing business. The PNTR aims to provide easy access to comprehensive, accurate, and timely information relevant to trade-related transactions. To date, 65 out of the 76 identified trade regulatory government agencies have been engaged in discussions on the adoption of the TradeNet, which is being developed as the NSW platform that will eventually be connected to the ASEAN Single Window gateway.

Moving Forward

Building on the accomplishments in 2017, the sector is poised to achieve its end-of-plan targets. Facilitating appropriate and well thought-out strategies will sustain the country's strong macroeconomic fundamentals that will provide a solid support amidst domestic and external challenges.

Pursue the tax reform program. The balance of Package 1 of the Comprehensive Tax Reform Program (CTRP) (i.e., general tax amnesty, estate tax, bank secrecy, Motor Vehicle User's Charge) is essential to augment revenues and enhance tax administration. Package 2, consisting of the corporate income tax reform and fiscal incentives modernization, was submitted at the start of 2018 for deliberation in the Congress. Meanwhile, Package 4, consisting of capital income and financial taxes, is targeted for consideration in the second half of the year. Reforms in real property taxation and property valuation (Package 3) is also targeted to be passed in Congress by January 2019.

Intensify implementation of tax administration reforms. In addition to a more vigorous enforcement of *Oplan Kandado*, Run After Tax Evaders (RATE), and Run After the Smugglers (RATS) program, tax compliance could be improved through adoption of technology-based reforms such as electronic data sharing and electronic sales reporting system. Tax monitoring could also be enhanced through complete tax mapping and comprehensive taxpayer profiling. It is noted that many of the proposed improvements in information technology and database management intended to enhance tax monitoring and compliance have been moved to later date, i.e., 2018, while the pre-procurement process is ongoing.

Improve LGUs' capacity to mobilize local sources of revenue. To complement the efforts in capacity building of local treasurers, reforms in real property valuation and assessment (CTRP Package 3) need to be pushed. Fiscal provisions of the Local Government Code may also be revisited for possible amendments, while the Idle Land Tax has to be implemented vigorously.

---

[7] Technology-enabled exporters belong to a variety of sectors, such as food processing, game development and animation services, franchising, and logistics.

[8] Enrollees to the RIPPLES Plus belong to the gifts, housewares and holiday decors, wearables and jewelry, and health supplements and cosmetics, among others.

Encourage transparency and mitigate corruption. Amendments to the provisions of Republic Act No. 1405 (Law on Secrecy of Bank Deposits) and RA 6426 (Foreign Currency Deposit Act), which seek to exempt government officials and employees, whether elected or appointed, from the coverage of the Bank Secrecy Law, is crucial to promote greater transparency.

Push expenditure management reforms. Among the expenditure management reform measures (e.g., shift to Program Expenditure Classification,[9] pilot test of Government Purchase Card (GPC),[10] adoption of one-year validity of appropriation, etc.) the passage of the Budget Reform Bill is a priority as it seeks to improve the linkage between planning, programming, and budgeting of agencies. The bill can help minimize bottlenecks by addressing gaps in planning, as well as in program and project design. In relation to this, the Budget Reform Program has been set up to ensure the smooth transition and effective implementation of the proposed reforms under the Budget Reform Bill. Part of the program is the creation of task teams who will review and streamline processes and procedures. Moreover, the rollout of the Budget and Treasury Management System (BTMS)[11] to big spending departments[12] and the shift from obligation-based to cash-based budgeting can contribute to improving budget utilization of agencies. It is also crucial to extend assistance to implementing agencies to facilitate a smooth transition (*See also Chapter 5*).

Further introduce improvements in the public procurement. In addition to the 2016 amendments to the Implementing Rules and Regulations (IRR) of the Government Procurement Reform Act, the Philippine Government Electronic Procurement System (PhilGEPS) Modernization needs to be fully rolled out. The program intends to upgrade the current system's technology with functionalities that will establish linkages with the BTMS of the Department of Budget and Management (DBM) and the Bureau of the Treasury (BTr). Reforms to level the playing field further by abolishing the preference margin for domestic suppliers and operationalizing the reciprocity provisions should likewise be pursued.

Continue to build capacity of implementing agencies. Capacity concerns reflected in low releases for creation and filling up of positions among agencies emerged as a weighty concern. Operational delays such as late submission of documentary requirements for fund releases were also observed among implementing agencies. To minimize this, implementing agencies and LGUs can continue to receive training under the Public Financial Management (PFM) Certificate Program.[13]

Remain vigilant to price pressures. Upward pressures on inflation may stem from the faster-than-expected rebound in oil prices and peso depreciation. Likewise, the implementation of the tax reform is expected to lead to transitory inflationary pressures and may further add pressure for wage and fare hikes. The government should undertake measures to reduce inflation especially on food to cushion its potential impact on the poor.

Implement additional reforms to strengthen the capital market. Following the gains highlighted in the earlier section, additional reforms need to be completed to further boost the country's capital market. These include the enhancements in the operation of the over-the-counter government bond market for better bond pricing and transparency; and enactment of a Payment Systems Law to improve the regulatory oversight of the BSP and to ensure safe and efficient payment systems.

[9] PREXC is restructuring an agency's budget by grouping all recurring activities as well as projects under the different programs or key strategies being pursued by the agency to meet its objectives and mandates.
[10] GPC is an alternative mode of payment for goods and services that aims to reduce administrative costs and enhance control and liquidity management by limiting the frequency and amount of cash advances.
[11] BTMS is the government's integrated financial management system which will handle the budget execution and cash management function of the DBM and BTr, respectively. It features online and real-time processing, monitoring, and reporting of various financial transactions of the government.
[12] Include the Departments of Social Welfare and Development, Health, Education, and Public Works and Highways.
[13] The Certificate Program is an initiative by the DBM, the PFM Committee, and supported by the Philippines-Australia PFM Program. It aims to enhance the technical skills and competencies of the PFM workforce in the oversight and spending agencies. Source: https://www.dbm.gov.ph/wp-content/uploads/DBM%20Publications/Bulletin/2015/2ndQuarter_%20april-june%20corrected%20pdf.pdf

Promote seamless financial market infrastructure. The passage of a Secured Transactions Law will strengthen the legal framework for the use of personal property as collateral and establish a modern centralized online collateral registry. The rollout of InstaPay[14] should also be accelerated. There is also a proposed merger of the trading platforms for equities and the fixed income securities.[15] However, the proposed single platform must be structured to harmonize the functions of the current exchanges without causing market disruptions during the migration or transition. Other financial market infrastructure that need to be improved include those for post-trade processing (e.g., trade repositories, central counterparties, central securities depository, and securities settlement system).[16]

Hasten efforts to enhance financial inclusion. Economic and financial literacy campaigns need to be scaled up. The enactment of the Collective Investment Schemes Law will boost the participation in the financial system, especially of middle- and low-income households. The current initiative to have a national identification system is also seen to facilitate peoples' access to finance by building credit history and potentially reduce de-risking by international correspondent banks.

Develop the legal framework for Islamic finance. The passage of an Islamic Banking Law, which remains pending at the Committee level of both Houses of Congress, must be accelerated to develop Islamic banking and promote financial inclusion among Muslim Filipinos.

Implement a strategic market-oriented export strategy focused on market trends and demand for products and services.

Institute a feedback mechanism, with diplomatic posts and trade attachés as main players, to identify and disseminate timely and accurate information on foreign markets. This could fill the information gap on policy and market trends affecting export performance and product demand. The feedback mechanism would be a resource that exporters could use in forming linkages with businesses, malls, shopping centers, and overseas Filipino associations that would help increase visibility of export products.

Increase the visibility of Philippine products through alternative approaches in export promotion. Undertaking more frequent, resource-efficient, and innovative activities such as setting up pop-up stores in shopping centers and malls and maximizing visibility in social media, are alternative and complementary approaches to the conduct of traditional trade fairs that would help raise awareness of foreign markets to Philippine products.

Identify and prioritize high-impact programs. Impact evaluation studies on programs and projects such as the Small Medium Enterprise Roving Academy and the Doing Business in Free Trade Areas should be undertaken to determine if these programs contribute to improving the competitiveness of exporters. This assessment is critical in identifying whether these programs and projects should be continued or if interventions are required to make them more effective.

[14] An automated clearing house for real-time low-value (less than ₱50,000.00) transfer credit under the NRPS

[15] Currently, fixed income securities are traded through the Philippine Dealing & Exchange Corp, the fixed income exchange; while equities instruments are traded through the Philippine Stock Exchange, the equities exchange.

[16] A Capital Market Development Blueprint 2017-2022 detailing an assessment of the current capital market development efforts, as well as the strategy and roadmap for capital market development, is targeted to be released by end 2018 led by the Department of Finance, Securities and Exchange Commission, BTr, and the BSP.

Conduct capability-building programs to cultivate skills in emerging services and to ease restrictions on certain sectors. As the IT-BPM sector faces an expected global slowdown as it moves towards maturity,[17] its annual revenue growth is seen to decelerate[18] to 9 percent until 2022. It is vital that capacity-building programs be pursued to allow the services sector, particularly IT-BPM, to sustain growth and move towards higher-value services (e.g., software development, animation, artificial intelligence, big data analytics, etc.). Continued efforts by the Executive as directed under Memorandum Order No. 16, s. 2017[19] to ease or lift restrictions in certain sectors should be pursued to encourage investments and develop skills that will support further growth *(See also Chapter 9).*

Establish institutions to improve capacity of businesses to meet international standards for products and processes. The issuance and eventual implementation of a National Quality Infrastructure Law would spur the development of a culture of quality, establish institutions and practices that will improve compliance with technical requirements, and promote the adoption of international standards in products and processes[20] *(See also Chapter 9)*.

Strengthen and broaden programs that will promote and maintain an environment conducive for export innovation. There is a need for programs that cultivate partnerships between universities, research centers, industry sectors, and government agencies, such as the Collaborative Research and Development to Leverage Philippine Economy Program of the Department of Science and Technology (DOST), to enhance the technological capacity of businesses for innovation and to encompass more stakeholders *(See also Chapter 14)*.

Upgrade information and communications technology (ICT), transportation, and logistics infrastructure to boost exports of products and services and to lower costs of production. Infrastructure that will allow the country's exports to reach its full potential must be in place *(See also Chapter 19).*

Develop a framework for local partnerships to meet supply volume requirements of export markets. The framework would facilitate coordination among producers and suppliers and help address constraints faced by exporters that have limited capacity to produce the volume requirements *(See also Chapter 9).*

Enhance and interlink online portals to heighten awareness for Philippine export products and facilitate trade. To broaden the awareness of foreign markets to Philippine products, there is a need to supplement promotion campaigns and maximize the use of online portals with comprehensive information on available products and exporters. The content and design of Tradeline Philippines should be enhanced to provide comprehensive user-friendly information on products, services, and exporters, as well as the Philippines Free Trade Agreements with trading partners. This portal should be linked with the PNTR to maximize the exposure of Philippine exporters and their products to buyers in export markets. The PNTR's eventual connection to the ASEAN Trade Repository would further widen the reach of Philippine products and services. Full implementation of the TradeNet, which will connect all 76 trade regulatory government agencies to the TradeNet platform, should be carried out to facilitate trade, increase transparency in cargo processing, and reduce operational costs and processing time. The conduct of briefings with government agencies and the private sector to introduce the system and promote its use should also be pursued.

---

[17] Dela Paz, C. (27 September 2017). "Philippines' BPO Industry sees slower annual growth of 9% until 2022," Rappler. Accessed from https://www.rappler.com/business/183523-philippines-bpo-industry-growth-projection-2022

[18] Lower than the 17 percent compounded annual growth recorded from 2011 to 2016

[19] Directing the National Economic and Development Authority (NEDA) Board and its member agencies to exert utmost efforts to lift or ease restrictions on certain investment areas or activities with limited foreign participation. Retrieved from: http://www.officialgazette.gov.ph/2017/11/21/memorandum-order-no-16-s-2017/)

[20] Senate Bill No. 707. Retrieved from https://www.senate.gov.ph/lisdata/2422620840!.pdf

Recommendations

Aside from the abovementioned strategies, the following should also be considered to ensure a sound macroeconomic policy supportive of growth of all sectors.

Table 15.1 Supplemental Strategies to Ensure Sound Macroeconomic Policy

CHALLENGES	RECOMMENDED STRATEGIES	IMPLEMENTING AGENCIES
Implement and formulate expenditure management reforms		
• Perpetual operational delays and bottlenecks in program and project implementation due to gaps in planning and in program and project design, leading to low budget utilization rate	• Further amendments to the Government Procurement Reform Act • Assist and build the capacities of implementing agencies and LGUs to facilitate the transition to cash-based appropriation.	DBM
Ensure effectiveness of financial literacy campaigns		
• The number of financial literacy campaigns (FLCs) conducted may not be an appropriate measure of the reach of financial literacy	• Improve the monitoring of FLCs.	BSP
Expand market access and diversify export products and markets		
• Information gap on products demanded by the market	• Institute a feedback mechanism to identify and disseminate timely and accurate information on export markets.	DTI, Department of Foreign Affairs
• Making trade promotion campaigns more innovative	• Increase the visibility of Philippine products through alternative approaches in export promotion.	DTI
Increase competitiveness of Philippine exports		
• Concentrating resources on programs and projects that have maximum impact • Preparing services sector for changes in demand of the market • Improving capacity of businesses to meet international standards	• Conduct impact evaluation studies on current programs, such as the SME Roving Academy and Doing Business in Free Trade Areas, to determine effectiveness and need for continuity or improvements. • Conduct capability-building programs to cultivate skills in emerging services and ease restrictions on certain sectors . • Establish institutions to improve product standards and increase technical compliance.	DTI
• Enhancing the technological capacity of businesses for innovation	• Cultivate partnerships between universities, research centers, industry sectors, and government agencies.	DOST
Enhance trade facilitation and strengthen linkages and connectivity		
• Developing products and higher-value services, lower production and delivery costs • Limited capacity of exporters to produce volume requirements and link to the value chain • Improving accessibility to comprehensive information on products and foreign trade agreements (FTAs)	• Upgrade ICT, transportation, and logistics infrastructure • Develop a framework for local partnerships. • Interconnect Tradeline Philippines to the Philippine National Trade Repository and enhance content and design to include comprehensive and understandable information on FTAs.	DTI