(Lack Of) Economic Prospects for the Rest of 2005

Maricar Paz M. Garde

As the political crisis drags on, the economy's prospects for the rest of the year are indeed dismal. Due to weak export performance and fiscal uncertainties, the Asian Development Bank (ADB) forecasts growth to be 4.6% this year, slower than 2004's 6.1%. This projection has not yet factored in the impacts of the protracted political crisis, though these are bound to have consequences on the economy.

The eventful week in July when the Hyatt 10 resigned and the opposition staged rallies has taken its toll. The exchange rate rose to P56 per US dollar, while the Philippine Stock Exchange Index (Phisix) went down 23.50 points or 1.3 percent. Portfolio investments dropped during the third week of July, with some $13.8 million repatriated out of the country. With no resolution to the looming crisis, investors are shying away from the Philippines. They are in a "wait and see" mood, so the country is losing much needed opportunities which new investments could have created.

Signs of economic contraction will lead households to tighten consumption. Consumers will put off buying big ticket items such as cars or computers to save for the rainy days. This is more bad news for the economy, since Personal Consumption Expenditures (PCE) make up around 70 percent of the GDP. Lower consumption will of course diminish business profitability and eventually dampen output.

What makes the situation even more difficult is the external economic environment. The steady climb of the global price of oil is expected to slow down output in East Asia. ADB projects regional growth at 6.8 percent this year, slightly lower than 2004's 7.6 percent. The slight downturn in economic expansion may however only be true for countries not experiencing political instability. The decline might be sharper in the Philippines due to our crisis.

A regional downturn would certainly hurt our exports. For the past five years, around 15 percent of our exports go to ASEAN. A slowdown would diminish demand in ASEAN economies, which in turn, would weaken our export performance.

The need for prudent fiscal spending leaves the government unable to pump-prime the economy. As of July, the Bureau of Internal Revenue (BIR) and the Customs have missed their collection targets. The suspension of the expanded VAT means we are losing revenues crucial to fiscal stability. The government insists that the budget deficit is still below its cap. However, if poor collection continues and the expanded VAT law remains suspended, the deficit will balloon by the end of the year. Rising inflation due to sharp increases in the world price of oil makes monetary expansion by the Central Bank unlikely. Hence we find ourselves with bleak economic prospects and few policy options.

Some sectors remain optimistic amidst all these. Investments may not be too severely affected, while remittances from Overseas Filipinos Workers (OWFs) will keep the economy afloat. Businesses have their hopes pinned on the usual holiday spending. However, the odds seem to be stacked against us. Weak export demand means less foreign currency coming in, while high oil prices jack up our imports bill. The market is still jittery and any unfavorable news could send the Peso and stock prices falling further. Add rising prices, poor fiscal performance, and possibly weak demand to these aforementioned factors, and an economic upturn in the last quarter becomes unthinkable.

At this point, there is no denying the ramifications of the political crisis to the economy. We should now be asking how severe the downturn will be and how will it affect welfare: Will more people be jobless this year? Will poverty worsen? How will the downturn affect next year's economic activity? We have no answers at this time, what is clear only is that the political stalemate must be resolved in order to save the economy.

This is not the first time the economy is held hostage by a political crisis. In 2001, the failed impeachment trial of former President Joseph Estrada resulted in economic contraction. At that time, the East Asian countries were gradually recovering from the 1997 financial crisis. The Philippines, relatively less affected by that Crisis, was expected to recover more quickly. However, political instability slowed down the recovery process. We have not learned our lesson yet.

As long as our institutions are weak, we will keep falling into this pattern. Each political crisis that erupts will push the economy downward, in a cycle that not only hurts current economic conditions, but long term growth prospects as well.

Maricar Paz M. Garde is an Assistant Professorial Lecturer at the Economics Department of De La Salle University Manila.