Gleaning the current economic situation from relevant aspects of international finance and macroeconomics

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Introduction

Concerns about the regional currency crisis on South and Southeast Asia have mounted in the aftermath of the Thai economic collapse, unmatched even by the Latin American and Mexican Crisis of 1994. Such concerns are valid because of the possible global effects the crisis may have on the industrial economies, whose funds exposure to this part of the world has grown substantially over the last decade in terms of lending, exports and international competitiveness.

The extent by which Thailand, Indonesia, Malaysia and the Philippines have become financially integrated internationally has only been made evident in the crisis of 1997. The reforms instituted in the past will make it difficult for these economies to isolate themselves from the general integration created by the international flow of capital.

As the dust begins to settle, the crisis has become more real—businesses are having difficulty acquiring or paying off loans, laborers are laid off either because of business closure or cost cutting measures, while the eroding purchasing power of consumers dampens demand. An assessment of the current economic situation cannot be dissociated from developments occurring internationally since sentiments of foreign investors are generally towards the whole region, the Philippines banded together with Thailand, Malaysia, and Indonesia.

This paper thereby focuses on four main areas: (1) an assessment of the currency crisis from the point of view of the country’s main creditor, (2) the aftermath of the currency crisis, (3) discussions on why the Philippines has been singled out for possible early recovery, and (4) an outlook for 1998 combined with an examination of important issues that need to be addressed.

Assessment of the Regional Crisis

It has become evident that the currency turmoil was basically a result of the massive scale of the shift of funds of the region. This was brought about by a perceived lack of confidence in the capabilities of countries in South and Southeast Asia to sustain growth achieved in the past decade, reinforc ing expectations of a decline in investment yields. Thailand, being the most exposed due to its buildup of short-term external borrowings, was the first to collapse, creating a domino effect on its neighbors. Not even the strong economies of Taiwan, Hong Kong, and Singapore were spared, though the damage wrought by the crisis upon these economies were less severe compared to the ASEAN-4 (IMF’s term to represent Thailand, Malaysia, Indonesia and the Philippines). International financial institutions like the International Monetary Fund (IMF), Overseas Economic Cooperation for Development (OECD), World Bank, and Asian Development Bank (ADB) are now assessing the events towards the run-up of the crisis in the hope of avoiding another worldwide economic decline of this nature. The bail-out packages are but temporary remedial measures. The reforms necessary to avail of them will have rippling effects on the region and their major trading partners.

The IMF has, in particular, been one of the first to come up with an interim assessment of the crisis and has identified four major factors that explain the scale of the massive flow of funds into and out of the region.

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1. The ASEAN-4 exhibited successful performance that contributed to the rapid growth of net capital inflows into the region in the 1990s. Only the Philippines was identified as the laggard among the four countries. Its growth only averaged above 5% compared to the 7% growth for the rest. This impressive economic performance of Thailand, Indonesia and Malaysia was initially led by growth in trade. Economic indicators suggested stability in the region since inflation was moderate and there was almost an absence of fiscal imbalance (except for the Philippines whose deficits have run through the 1990s). Private savings shortfall was more associated with investment opportunities offering potentials for greater returns because of past growth performance. Such opportunities attracted foreign capital into these economies. However, this has placed a strain in the capacity of these countries to continually deploy funds to productive areas and, faced with competition, compromised prudent financial intermediation.

2. Changes occurred in the external environment, particularly in the industrial economies where asset yields declined and spreads narrowed. These same developments contributed to a reversal of the flow when yields turned upwards, as was the case when the US Federal Reserve recently raised short-term interest rates because of the continuing domestic expansion. A change in the external environment, also traced to developments in the US, is the weakening of the dollar in 1994 to early 1995. Since the currencies of the ASEAN-4 were inherently pegged to the dollar, the balance of trade in this region generally improved. A reversal of this trend happened in mid-1995 when the dollar recovered against most strong currencies. Not only did exports decline but the high cost of imports created downward pressures on profitability.

3. The macroeconomic performance of the ASEAN-4 in the early part of this decade brought about a risk of overheating, raising questions about the sustainability of the exchange rates. The growth in demand was putting a strain on resources, undermining competitiveness, while continued inflow of funds increased the cost of sterilization. Funds inflow, in turn, made it difficult to justify fiscal consolidation, given the healthy state of public finance.

4. Financial and other structural weaknesses became more evident as the not for speculative attacks on the currencies of the region. Hedge funds, which are largely unregulated, were found to have great influence over capital movements with the existence of only a few dominant speculators.

As long as portfolio investments comprise a relatively large share of funds inflow, small fragile economies like the ASEAN-4 would be seriously disadvantaged.

There seems to be no immediate short-term solutions to the problems faced by most affected countries. The only course seems to be more borrowings from international credit institutions.

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Philippines Economic Performance in the Aftermath of the Currency Crisis

The Philippines joined the race towards realizing the so-called Asian economic miracle rather late as it grappled with its own internal political problems and difficulties in instituting reforms. Its economy took off only in 1994 register-
ing moderate growth thereafter. The currency contagion caught the Philippines by surprise and a mad scramble to defend the peso took place.

The Peso Devaluation

The attack of the baht in May 1997 sent jitters to international investors whose immediate reaction was to seek safer havens for their funds until the turmoil subsides. The contagion effect on the Philippine peso prematurely depressed overall growth for 1997. The Bangko Sentral ng Pilipinas (BSP) faced tremendous pressure to defend the peso but had to give in to a de facto devaluation of the currency in July 2, losing about $1.5 B in the process and reducing international reserves to a critically low level of about $9.7 B. (The country has to maintain a comfortable reserve position equivalent to about three months of importation requirements.)

The BSP's basic stance is for non-intervention if changes in the exchange rate reflect shifts or adjustments in the fundamentals of the economy. However, the BSP, to maintain movements in prices and interest rates, intervenes when the currency faces speculative attacks. With pressures building up on the peso, the BSP allowed the currency to move within a wider band, and intervened when the upper limit was reached. This allowed for adjustments based on circumstances in the foreign exchange markets. More importantly, this prevented further decreases in international reserves and allowed adjustments in interest rates to levels that supposedly can support the economy and discourage speculative activities. Despite these efforts, however, the currency still lost 35% of its value by the end of 1997.

Overall Economic Performance

Despite the currency crisis, the Gross National Product (GNP) and Gross Domestic Product (GDP) managed to register growth rates of 5.8% and 5.1%, respectively. This is lower than 1996 levels but higher compared to growth rates for 1994 and 1995. Net factor income from abroad, which is the difference between GNP and GDP, grew by 23%. From the supply side, the service sector and industry accounted for most of overall growth. The finance sector seemed to have proven some resiliency against the contagion effect of the currency crisis as it posted growth of 12.4%, transportation, communication and storage being a distant second and registering growth of only 7.9%. Construction, under the industrial sector, enjoyed a good year in 1997 as it registered the highest growth, rate of 16.3% while mining and quarrying performed dismally at -3.2%. The biggest slump for mining and quarrying was experienced in the first and second quar-

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ters. The rebound of growth in the third and fourth quarters was not enough to offset losses in the first half of the year. From the demand side, the highest growth rate was registered by fixed capital formation at 12.2% (much accounted for by growth in construction at 15.8%). This was supported by major infrastructure projects all over the country during the year. The growth rate of government consumption went down to 3.6% as all government agencies reduced spending during the last half of 1997.

Performance of the External Sector

The export sector seemed to have benefited from the peso devaluation as it registered double digit 1997 growth rates on a quarterly basis. On an annual basis, however, exports grew by 8.9% (in constant terms) last year. Semiconductors and electronic microcircuits took the lead, followed by garments and finished electrical machinery. The Philippines registered one of the highest growth in exports in the region (in dollars terms registering 22.8%). One must bear in mind, however, that the country is starting from a much lower base compared to its neighbors.

Growth in imports almost matched growth in exports at 8.7%, thus mitigating any positive effects the devaluation of the peso may have had on the balance of trade. The country's major export products remain import-dependent. Among the principal imports, fuel and related products registered the highest overall growth of 13.6% followed by base metal and machinery (other than electrical machinery) at 15.6% and 11.5%, respectively.

Since the growth in exports exceeded growth in imports, trade deficits narrowed to US$10.7B compared to US$11.9B the previous year. Thanks to the continued rise in OFW remittances, the current account deficit is still manageable. The government is currently seeking foreign loans at reasonable terms to augment international reserves, which stood at US$9.7B as of November last year.

Net factor income from abroad continued to create a buffer for foreign exchange needs of the country. Overseas contract workers, being the largest holders of foreign currency taken together, held back their remittances in the wake of the crisis in anticipation of higher proceeds from the devaluation. Remittances and conversions were expected to increase in the first half of 1998 as the peso stabilizes at P40.

BSP's Intervention, Liquidity Tightening Measures and Controls

Since 1994 the BSP has been a net purchaser of dollars in the market. This position was reversed only in mid-1997. See ECONOMIC, next page
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Questions and doubts have been raised in the past as to the overvaluation of the currency. The BSP had to maintain a balance between supporting the peso at levels that would not be inflationary but much more reflective of market sentiments and one that would not dampen aggregate demand.

Whether in hindsight the BSP should have allowed a much faster decline in the value of the currency early on to avert the effects of the crisis is a matter of individual opinion. The bulk of Philippine exports is still highly import dependent while available foreign capital is inadequate to meet infrastructure needs. Growth in investments cannot be sacrificed and therefore interest rates have to be kept at reasonably lower levels. Attacks on currencies in the region of this nature and scale have been unprecedented.

For the remaining half of 1997, the BSP had to resort to liquidity tightening measures to further prevent rise in inflation as a result of the devaluation. Inflationary pressures intensified, reaching 6.1% in December. On the average, however, inflation was registered at only 5.1% apparently the lowest recorded level over the years. Apparently, businesses were preventing any further rise in the general prices of commodities as they were already faced with stiff competition with both domestic manufactured goods and cheaper imports in the market. Furthermore, food commodities, which are not yet substantially affected by the devaluation because of a better harvest the previous year, comprise 58% of the weight of the consumer price index.

The rise in interest rates is proving to be very costly as it inhibits borrowings seriously needed to manage operations in these difficult times. Already businessmen in Mindanao have protested the failure of some banks to implement the so-called gentleman's agreement between Governor Gabriel Singson and Bankers Association of the Philippines (BAP) President Deogracias Vistan to lower rates. High interest rates are causing payment difficulties for businesses. A few, like Vitarich, Eyco, Victoarias Milling, Nikon and a host of other small and medium scale corporations, have sought debt restructuring or suspension of debt payments.

Banks, for their part, have increased their loan-loss reserves to allow for loan default expected to increase in 1998. Metrobank, currently the biggest commercial bank in the country, has taken out P2.4 billion from its net income to comply with the BSP's requirement to set aside 2% loan loss reserve over the next three years. PCIBank, reportedly the fifth largest bank in terms of assets, is setting aside P200 million every month to increase its loan loss provision for 1998 available, Singson reported that small finance companies in Thailand, which were the most vulnerable to the collapse in the sector, have taken on about a 24% share of real estate loans. A majority of these finance companies has since closed down. Philippine finance companies, on the other hand, are reportedly not significantly engaged in the real estate business.

An added cause for concern is the extent by which the BSP is able to closely monitor the activities of smaller commercial banks in terms of their DOSRI accounts. Orient Bank, which experienced a bank run in February, had to search for viable partners (the bid being won by RCBC) to take on majority ownership of the ailing bank. Lately, it was discovered

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by P2.4 billion. Banks have until October 2000 to comply with this requirement. Already non-performing loans have risen to 2.5% of their loan portfolio and is expected to further rise by another 1% to 1.5% in 1998.

There was increased cause for concern over the exposure of banks to the real estate sector as the crash in Thailand was feared to be duplicated in the Philippines. As of end-march 1997, bank lendings to the sector accounted for only 9.2% of total loan portfolio of 25 sample banks. Towards the end of 1997 this rose to 12.4%. The BSP imposed a 20% ceiling on loans to the sector following the crisis in Thailand, whose banks have an exposure to the real estate sector of only 9.4%. Though figures were not made to have violated BSP rules on limits to loans granted to owners, directors, stockholders and officers of banks, causing a snag in negotiations for its purchase and rehabilitation. Two other small banks, Unisave and Richmond, have also filed for receivership and are seeking ways to save their operations.

The BSP is anticipating more difficulties for the corporate sector and is thereby contemplating another round of increase in the minimum requirement for capitalization to further strengthen the banking system. A minimum capitalization requirement of P4.5 billion has been set for universal banks, for which they have until the middle of 1999 to comply. Commercial banks are required a minimum capital of P2 billion. Thrift banks in first
class municipalities have to put up P 250 million, while those outside the metropolis have to put up P40 million.

Anticipated Earlier Recovery for the Philippines

The Philippines has been branded a laggard in the race towards achievement of the Asian economic miracle. The country only began to recover from the extended recession of the 1980’s due mainly to internal political strife and economic difficulties. It took time for major structural reforms to be implemented as the political will to put these measures in place were continually contested. The benefits of such reforms as deregulation and liberalization of industries were slowly realized only quite recently (about 1992-1996). Among the more significant reforms put in place were (Wailace, 1996):

1. Entry of new foreign banks into the system
2. Liberalization of foreign exchange transactions
3. Implementation of the expanded value added tax system
4. Deregulation of the oil industry, finance industry, and transportation industry
5. Demonopolization of the telecommunication and airline industries
6. Improvements in energy supply and efforts at privatization of Nepcor
7. Adherence to World Trade Organization (WTO)
8. Privatization of Manila Waterworks and Sewerage System (MWSS)
9. Strengthening of the powers and functions of the BSP and the Monetary Board

As a result of these reforms, the Philippines is believed to be in a better position to break away from the difficulties of the crisis. Clear directions and the determination to pursue these reforms, despite temporary setbacks, are beginning to pay off, albeit slowly. Growth, though moderate by regional standards, is encouraging and with the current low level of infrastructure support the Philippines cannot afford to jump-start the economy without causing greater damage to the benefits that have already been gained. It is essentially this moderate growth and the unlikely chance of overheating that worked in the country’s favor. Assuming the reforms put in place are not reversed by the next administration, the least the country can expect is a slowdown in growth rather than a recession. Much still needs to be done by way of addressing the current crisis as well as the more fundamental problems of increasing production and spreading the gains of economic growth to a wider segment of the population.

Outlook for 1998 and the Job Ahead

To say the least, the prospects for 1998 are dimmed by so many factors, among which are:
- The ill effects of the El Niño phenomenon
- Uncertainty brought about by the coming elections
- The economic instability in the region inhibiting capital flows
- Increased competition as a result of the simultaneous devaluation of currencies in the region
- Diminished demand because of a decrease in purchasing power
- Closure of firms affected by increasing interest rates and debt service burden
- Decline in investments due to high interest rates
- Lay-offs in the work force due to closures or cost cutting measures both domestically and abroad
- Deterioration in the delivery of basic services due to belt-tightening by government

All targets for this year in terms of economic growth have been lowered quite substantially, in practically all sectors, although some like construction, finance and exports will experience greater levels of growth than others. The chances for a double digit inflation is likely towards the third quarter, after the elections. Investments will remain depressed for the whole of 1998 but is expected to pick up in 1999. Imports will inch slightly higher from present levels due to the need to import agricultural products (which is getting to be in short supply abroad), the need to finish current infrastructure projects targeted for completion within the next two years and the high import content of most of the country’s merchandise exports. This will not be a good time for labor to negotiate for wage increases when businesses are encountering difficulties meeting operating needs. More lay-offs are expected especially in small and medium scale companies that will reduce production as the market becomes depressed.

It would be difficult for government to experience a budget surplus this year owing to the expected decrease in collections of taxes and custom duties. Meanwhile, there is only so much the government can do to cut down on the essential services and it would require much political will to trim the government machinery of its excesses.

The job that lies ahead is one of the most challenging for the country. It would entail both monetary and fiscal tightening measures, while at the same time cushioning the negative impact these measures will have on the disadvantaged groups in society. A lot of fiscal and monetary discipline would be called for. On the fiscal side, the passing of the Comprehensive Tax Reform Program (CTRP) provides government with a more permanent source of revenues but it should be supplemented with a better ability to catch tax evaders and not to further burden honest taxpayers. The swiftness with which cases are handled and made transparent will send strong signals to those who believe they can buy their way out of a tax settlement. As revenues are collected, so must the deployment of funds be strictly controlled and channeled into priority areas identified in the recently concluded National
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Economic Summit, done by way of the local government units instead of giving legislators much of a say in this area by way of the pork barrel.

The need to develop infrastructure tops the list. Infrastructure does not only refer to roads and bridges, these being the most visible to the citizenry, but more importantly the complete rehabilitation of most of the country’s seaports and airports, container ports, markets and warehouses to support the growing demand for these as population grows.

There is much that an efficient distribution and logistical support (for the transfer of goods from the production site to the consumers) can do to bring down costs and prices of commodities. There is also a pull effect that this creates on technological improvements in agricultural production.

Efforts should continually be made by government to prevent any crowding out of the private sector regarding the use of borrowed funds. Efforts at privatization of government-run corporations should be sped up so as not to further strain the budget. The Ramos government made the right move of adopting a build-operate-transfer scheme in areas where opportunities exist for this kind of arrangements like tollways and power plants. This further eased the fiscal sector from acquiring more debt.

On the monetary side, controls over the financial system are deemed necessary by way of an efficient and effective monitoring system and requiring greater levels transparency in revealing solvency and liquidity status of financial institutions. Measures should be taken to encourage the banking system to provide innovative products for small savers, the kinds of instruments that provide greater risk-free returns.

Among the lessons to be learned from this crisis is the fact that increased domestic savings is still the best way to close the investment-savings gap. It provides leeway in handling fiscal adjustments with sudden capital outflows. Besides, most domestic savings are earmarked for long term needs of savers such as retirement, the purchase of dwellings and provisions for the future needs of their children. Fund sources of this nature could be harnessed for the most productive uses.

Definitely interest rates should be lowered. However, the lowering of interest rates should occur as a result of increased competition in the delivery of financial services. Efforts should be made into further adding teeth to the financial liberalization efforts of government. Not only should more reputable international banks be allowed to conduct business in the country but they should be allowed to branch out into as many cities and towns that their resources could take. In this way the rural population gets introduced to advanced technology in banking and the subsequent efficiency in the delivery of financial services. Competition will narrow the spreads currently enjoyed by the banking system.

Foreign capital will always be seeking the best returns and there is no reason to prevent even speculative capital from flowing into the system. These inflows, however, should be managed. Fiscal measures could be employed to discourage speculative attacks on the currency while fiscal incentives should be offered for long-term capital inflows. Economic rewards have recently become lopsided in favor of greater investments in financial assets. It is time to give some priority to developing real assets that would support wealth creation. This can be achieved by way of increasing value added in production with improved technology and depth and breadth in human resource development. The economy needs to be weaned from the mere assembly form of manufacturing to developing products using local or transferred technology in the production of components parts.

Among the many resources the country has, nothing is more valuable than its human resource. The Philippines enjoys an advantage of having one of the highest literacy rates in the region. This advantages can be enhanced with the possession of greater technical and vocational skills. Avenues should be provided for greater absorption of graduates in areas were their acquired skills can be put to great use. Again the pull effect of improved technology in manufacturing and in services will create a natural preference for technical training and exposure to the sciences in education.

Finally at the firm level, decision making cannot anymore be dissociated from the effects that liberalization has had on open economies. The benefits of liberalization brings with it certain costs. The constant threat of competition is one of them. Another is the sudden shift in funds flow into and out of the economic system. To remain profitable, the firm will have to continually find imaginative ways to maintain costs at a minimum level while providing the market with good quality products at reasonably lower prices. This is great challenge to businesses and still much can be done by way of providing government support and seeking the cooperation of labor groups.

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The Philippine Housing Sector: Where is it heading?

By Enrique M. Soriano III, Assistant Professorial Lecturer, Marketing Department

I. Introduction

The performance of the Philippine real estate industry is strongly related to the political and economic environment. Specifically, indicators such as level of investments, favorable land prices, and interest rates can spark bullishness or spell bearishness in the industry.

It must be underscored that in the early 80's (1982-1985), the industry performed poorly based on its ODRE (Ownership of Dwellings and Real Estate) rate, the industry's performance indicator registering 0.4% and the country's GNP growth rate pegged at 2.4%.

The industry experienced rapid growth beginning in 1986, immediately after the resumption of President Corazon Aquino in office. Consequently, this period of robust growth was cut short by the attempted coup d'etat on December 1989.

The industry went into a consolidation phase from 1990 to 1992. During that period, the property sector experienced slow growth because of political uncertainties; a series of unfortunate natural disasters; and a severe power shortage. With inflation at double digit levels and interest rates reaching a high of 40%, economic growth dropped to a low of 0.4% in 1991 from 4.5% as shown in Table 1. In general, property prices were flat for the duration.

A marked improvement was noted in the first two quarters of 1994 as the industry's ODRE rate reached a positive 2.0% and 3.0% respectively. The feat was accomplished when the country posted economic gains for the same period, proving that the industry was very much influenced by the overall performance of the Philippine economy.

The upward momentum of the industry's 1994 performance was largely fueled by a more manageable level of interest and inflation and a stable economic climate. Liberalization and deregulation policies encouraged more foreign investments, translating into more opportunities for the property market.

In the construction front, a buoyant demand was experienced because of several government-initiated housing reforms. Notably, the adoption of the multisectoral Social Reform Agenda where the improvement of the Filipinos' living conditions were stressed, and the enactment into law of the Comprehensive Shelter Finance Act of 1994 contributed to this demand.

All these developments, coupled with a more stabilized political situation, propelled the industry into a new accelerated growth phase beginning in 1994. During this time, the Philippines experienced a steady increase in the supply of real estate projects across all product lines in a market that has expanded geographically and structurally.

To clearly understand the housing sector, the latter is classified under three segments, namely: the high-end market or upscale market; The middle market and the low-end market or mass housing segment, which is further segregated into two housing components: non-socialized and socialized housing programs.

Table 2 highlights the major difference of the three segments for better appreciation (see next page).

On top of the elements covered under Table 2, we must also underscore the physical nature of the product which can come in the traditional horizontal development model (i.e. subdivision, villages, townhouse communities, industrial zones, etc.) or under a verbal development concept (i.e. low, medium, and high-rise condominium developments, malls, office buildings, etc.).

II. The housing sector
A. Low and Mass Housing Segment

The residential sector offers the strongest prospects backed by household formation and real incomes rising at an annual average of 2% and 3% respectively, and further enhanced by the availability of a greater variety of affordable financing facilities from both the government and private sectors (Filippo Entrepreneur, 1996).

As previously mentioned, the mass housing/low-end market has two components: the non-socialized housing program packaged and financed by the private sectors and the socialized housing program initiated by both the private sector and several government agencies. 

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The latter is mandated by the government’s Social Reform Agenda, which provides for government financial institutions to provide financing facility to member-beneficiaries who may opt for a long-term payment scheme, i.e. 10 to 20 years.

Presently, there is a substantial backlog of four million homes nationwide in the supply of low and middle-income housing units. The demand is further compounded by an annual average housing requirement of 650,000 to 900,000 units which cannot be fully addressed by government-backed housing initiatives. Thus, there is a significant unmet demand for private players to address. An average of 154,000 units are pumped into the market annually creating a backlog of at least 746,000 units per annum.

The low and middle-income segments definitely offer players potential windfall over the long term. This can be solely attributed to the element of real demand and not based on speculation. Further complementing the local requirements are the overseas Filipino workers who acquire housing units for their respective families. In addition, this unserved demand can also be attributed to the continued concentration of developers on the higher-end segment of the market. Moreover, the consistent increase in land cost had priced out developments in mass housing.

However, there are limiting factors to consider as well. First, the inadequate supply of subsidized government financing and the limited participation of major players have translated into a limited production capability of the industry. Second, the decision of government to gradually pull out from mass-housing development and leave the task to private developers have also significantly affected the supply of these housing units.

Presently, most housing development are located in the CALABARZON (Calamba, Laguna, Batangas, Rizal, and Quezon) in Region IV, apparently because of its title as the center of industrial growth. Other urban areas that have exhibited strong growth and have similarly been transformed into centers of mass housing include Central Luzon, Davao, Cagayan de Oro, Iloilo, and Bacolod.

**B. Middle Market/Emerging Class**

Fifteen years ago, among the three segments, the middle market was probably the most neglected. This can be attributed to several factors, namely:

- The real estate industry was considered a “mom and pop” industry where no significant public companies participated, few private developers created supply, and there was very little active involvement from financial institutions and corporations;
- The market’s conservative stance in considering purchases in real estate and very few private local developers in the residential market;
- The demand was derived from local sources which was primarily user-driven; and,
- The huge disparity between social classes in the Philippine economy.

In light of so many developments in the property sector, the present middle market has been substantially given attention due to several factors such as:

- Rising affluence of middle income professionals.

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<td><strong>Medium End</strong></td>
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- The formation of new business enterprises and the expansion of existing ones
- The shift of more market players toward this lucrative market
- The emergence of innovative and affordable in-house payment facility.
- Market domination primarily by the end-user market.
- Less participation of speculators

It is anticipated that more residential units will flood the market in the next three to four years resulting in a possible inventory buildup and heated competition. However, due to the existing backlog of housing units, this buildup will eventually balance demand and supply as a result of the sustaining requirement of the segment.

Major market players are now looking at developing affordable housing units near the centers of activity. The concentration in highly-urbanized areas is mainly influenced by the perennial congestion in Metro Manila’s streets. Currently, the demand for medium-cost housing stands at an average of 50,000 units every year and private developers can only supply 10% of the total inventory. Adding the previous years’ backlog will translate into an average of 80,000 to 100,000 units of middle-market demand. This is the real demand that will translate into potential revenues for property players.
**C. High End/Luxury Segment**

In periods of robust and stable growth, this market continues to have a very high concentration of property players because it offers a significant return on investment that is usually derived from the speculative market as well as from a very active pre-selling strategy by developers.

However, in periods of economic uncertainty, as what is being experienced at present, the high-end market is also the most vulnerable due primarily to the artificial pricing brought about by speculative demand and the temporary movement of real estate among investors. Internally, the speculative market, if it continues to go unchecked, can result into a possible glut where developers will continue to go up due to the limited available land in the Central Business Districts (CBDs).

From 1992 up to the middle part of 1997, Makati experienced an average growth of 25% to 28% per annum. Conversely, prices of residential units in the area hovered within the range of P 80,000 to P 20,000 per sq. meter. In the Ortigas CBD, an average of 20% to 30% was recorded during the same period.

During the last 10 years alone, over 30,000 units have been constructed in Metro Manila, and an additional 22,440 units are expected to come on stream in the next four years. Close to 8,800 units will come from Ortigas, Makati and Bonifacio alone and 48% of these units will serve the luxury end of the market.

Compounding the woes in the vertical sector on top of the thin market is the fluctuating cost of materials that will result into a slowdown in construction activities. Presently, there is a perceived glut in the condominium market especially in Ortigas and Makati.

The volatile regional currency crisis and the fluctuating interest rates signaled the end of the property boom especially in the vertical sector. The investor and the end user market took it as the final blow to pull out, albeit temporarily, from the real estate market. It is expected that they will come back as soon as confidence-building measures are properly installed in the economic system. In the meantime, it will be a "wait and see" attitude for the investing public. The only movement in the high-end market is real demand coming from the domestic front. In instances where there is limited foreign participation, it will only be confined to completely developed units mostly catering to the leasing segment.

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**III. Economy**

The regional currency turmoil exacerbated the slowdown in the Philippine economy. A number of other events also contributed: political uncertainty surrounding the run-up to the May 1998 elections; lower capital flows into Asia; and the problems of the Asian economies.

The GNP was up slightly to 6.0% and GDP was recorded at 5.2% (from 5.9% and 5.3% respectively in the first half of the year), but these do not take into account the currency crisis. Interest rates remained at high levels (the 3-month interbank rate was in excess of 23%). The Bangko Sentral, however, has encouraged banks to lower their prime lending rates to stimulate the domestic economy. In doing so, it is allowing market forces to dictate the real value of the peso. (First Pacific Davies, 1997)

The optimistic assumption is that the Philippines has already weathered the storm and is gearing for a steady upturn in the next few months. In contrast to its Asian neighbors who are still reeling from the crisis and are finding it much too difficult to recover, the country is on its way up.

A number of observers has expressed the opinion that the Philippines will be among the first to recover from the present regional financial turmoil. To quote BSP Governor Gabriel Singson: "A major element is the restoration of market confidence. To do so is to first stabilize the exchange rate around levels that are determined by normal forces of supply and demand rather than speculation and panic. Consequently, greater exchange rate stability will pave the way for reduced market uncertainty, more capital flows, and therefore lower interest rates. Lower interest rates will therefore ease the burden of businessmen in the local economy. In addition, prudent fiscal and monetary discipline is indispensable to control government borrowings that add to the increase in interest rates."

Economic growth in the Philippines has been steady over the past few years and the country, having experienced so many crises since 1983, is proving to be more resilient than others. This can be attributed to the fact that, in recent years, the country has steadily moved to become a more market-oriented and open economy. Moreover, these economic foundations built-up through these years are now absorbing the impact of the region's uncertainty with success. Citing Merrill Lynch as quoted in Reuters, January 1998: "The Philippines, Singapore, China, Hong Kong, and Taiwan are stable."

**IV. Conclusion**

Overall, the residential sector witnessed a slowdown in sales activity due to interest rates in excess of 20%, coupled with the fact that developers could no longer afford to offer subsidized loans. What triggered the downturn was the shattered confidence brought about by...