

Chapter 10. Study on Governance and Regulation: A Summary

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Chapter 10

STUDY ON GOVERNANCE AND REGULATION: A SUMMARY

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The Role of the State

The year 1998 was indeed a special year for the Filipino people. Mabuhay for the Philippine Centennial. While we celebrated 100 years of Philippine independence last June, the year of the Centennial was in fact a year of changes. Among others, the power of the state peacefully transferred from the Ramos administration to the Estrada administration. This big change in politics clearly shows that democracy in this country works. The change of administration, however, does not necessarily mean changes in economic policies, since the country had already undergone some fundamental changes in the recent past. As a matter of fact, the Estrada administration has reiterated that market-oriented policy reforms, most of which were adopted during the Ramos administration, will be pushed through under the new administration as well.

As for my country, Japan, there were also some significant changes especially in the economy. The Japanese government finally conceded that the economy is in the worst recession after the World War II and that the major banks of the country have enormous amounts of bad loans. Furthermore, recognizing that financial instability, and thus the credit crunch, due to the bad loan problems is the main cause of the prolonged stagnation of the economy, the government brought in a package of bailout programs for the banking sector. Under the bailout scheme, two of the eighteen major banks were already nationalized. We really hope that such recent developments will pave the way for the Japanese economy's recovery. Stated quite frankly, I am now a little bit optimistic of my country's economic situation compared to that of the previous years. For the Japanese, too, 1998 was a year of changes.

The emerging markets, especially East Asia, have been confronting economic and even political turmoil, which originally arose from the financial crisis of mid-1997. The primary cause of the crisis is a government failure to restrain the entrepreneurs, financial institutions in particular, from being too bullish. Last December, a report issued by the World Bank charged the IMF and U.S. of mishandling the Asian crisis. The report contains a blow-by-blow account of how misjudgments – by global investors and Asian officials – multiplied the damage. Furthermore, the report calls for a tremendous slowdown in the movement on deregulate financial markets in developing countries. Also in last December, U.S. Treasury Secretary Robert Rubin reportedly told the National Foreign Trade Council that many people are suffering terribly as a result of this crisis and that it is imperative the international community and the affected nations focus on strengthening social safety nets as a component of building a market-based system. It seems that 1998 was a year of changes for the people in Washington as well.

The role of the state is the main theme of the World Development Report 1997 and the report starts with the following statements: "Around the globe, the state is in the spotlight. Far-reaching developments in the global economy have us revisiting basic questions about government: what its role should be, what it can and cannot, and how best to do it". While we discuss the issues related to governance and regulation in this volume, it should be noticed that we are going to raise such basic questions about government. The report also states as follows: "Most important, we now see the markets and government are complementary: the state is essential for putting in place the appropriate institutional foundations for markets. And government's credibility ... can be as important for attracting private investment as the content of those rules and policies". I would like to confess that I was personally so surprised when I found these sentences in the report, since it seemed to me that such assertion clearly showed a great change of the institution's way of thinking. Similarly, however, Prof. Joseph E. Stiglitz claims that:

"There is a third way – or, I should say, many third ways – between the extremes of total government control of the economy and complete laissez-fairer. At different stages of development or in different situations, countries will and should choose different points along this spectrum".

Thus we are most grateful if we could successfully discuss where we are and which point along that spectrum we should choose in the specific context of the Philippines. Now let me summarize the discussions in this volume.

A Summary of the Discussions

The first paper by Raul V. Fabella traces the genesis of the soft state which is normally characterized by control over-reach largely in an attempt to widen the rent extraction which leads to sparse enforcement and even open violations and corruption. He suggests that re-engineering the soft state in our times is really reverting to the Smithian Agenda but he warns that walking away from past involvements is easier said than done. He argues that the public face of state disengagement is economic efficiency, but more importantly the redemption of governance. It is found that the Philippines remains a soft state and while it has embarked on the fateful journey towards the market with some tangible results, the way forward becomes progressively harder.

In the second paper by Ma. Lourdes Sereno and Raphael P.M. Lotilla, an important distinction is made between the scope of judicial review as it existed before the 1987 Constitution and as articulated in the present Constitution, and as effectively exercised by the Supreme Court. They argue that the pivotal element on which the issue of judicial reviewability rests is not on the technical vis-à-vis the non-technical nature of the act, but rather, the manner of the exercise of the powers of the two other branches of the government. It is also described that with the advent of the 1987 Constitution, the political question doctrine has been reduced in scope. The question of judicial reviewability on economic policy making is also discussed. Lastly, it is observed that the Supreme Court has given

a strong signal, by requiring utmost observance of each provision of the Constitution, over those which seems unclear, or those for which a more definitive legislative interpretation or enactment is required.

Emmanuel de Dios argues that the legislature's current function owes to its general weakness and even subordination in relation to the executive as against the general thought that the congressional power has been excessive, unduly intervening with and indeed distorting initiatives by the executive. He illustrates this framework of relations between the executive and congress by describing the discretion of the executive over the timing and amount of budgetary releases, the practice of delegating the detailed elaboration of laws to the executive and the use of pork barrel politics. The paper uses some concepts from game theory to explain some of the relationships existing between executive and legislative branches, as well as those within congress itself. De Dios concludes that the dilemma for the Philippines is that it is caught in between a strong presidency and a program of weakened executive power— preferably in the context of a thoroughgoing devolution and a stronger bureaucracy— which makes it incur the costs of both.

The paper by Ruperto P. Alonzo gives an overview of the benefits and problems that go along with the process of devolution. While local government units (LGUs) appear to be more competent in providing basic services to people, realities like spillover effects and inequalities among LGUs warrant the intervention of the national government (NG). Certain issues arise from such intervention, the most notable of which are financing arrangements for local projects and differences in development priorities between LGUs and NG. This paper addresses these concerns by proposing some policy guidelines and options for a more efficient transfer of resources to LGUs.

In his paper, Dante B. Canlas reviews some aspects of banking risks in an environment with globally integrated financial markets and he also describes some recent developments in financial markets that lead to excessive risk taking by banks and borrowers. It is suggested that a deposit-insurance system, which an entity like the government must provide, is helpful in building depositor confidence in the banking system. Likewise, the roles played by the central bank for the economy and the banking system are also discussed. He recommends, among other things, that the limited information problem be addressed to best diversify the risks that arise from financial innovations.

Renato Reside provides an initial examination of Philippine capital markets, a review of issues crucial to its development, and of recommendations for further reform. His paper discusses, describes and differentiates the characteristics of the different components of the Philippine bond market— the money and capital markets, in general, and its sub-components, in particular. He finds that it is entirely possible for the weighted average interest rate (WAIR) for commercial paper to fall below the WAIR for T-bills which demonstrates the potential of the Philippine bond market to become a low cost source of funding for private corporations. In spite of this, he enumerates the problems which make it difficult to develop bond markets. A more or less sequential step for moving forward is presented in the paper with the most fundamental first step to restore macroeconomic stability.

According to Marina Fe B. Durano, the lack of information, the difficulty of measurement and the problems of enforcement in the services sector require a regulatory and institutional system that minimizes the transactions cost of both supplier and buyer, thus preventing market failure. In absolute terms, this holds true in the international market where buyers and sellers have distinct traits and preferences that are strongly influenced by their culture and history. Finally, it is concluded that regulation and contract specification remain necessary to balance the conflicting interests between the buyer and the supplier.

Orville Solon and Steven John Pamintuan stress the insufficiency of the regulation in the privatization of MWSS to meet the actual problems that arise during the process and also with respect to both the regulators and the concessionaires due to the regulators' lack of information, inadequate knowledge, and technical training incompetency of the privatization. Their study shows that there are a lot of loopholes in the regulation itself due to the absence of clear and specific methodical guidelines. Furthermore, it is revealed that the regulators fail to fully observe the adequacy of information on cost, performance and compliance to service obligations of the concessionaires. As a result, the information as provided in the regulation turned out to be understated for the actual practice. Thus, a strategy for the effectiveness and strengthening of the regulatory reforms is being recommended. It is also suggested that the regulators themselves be given further training and orientation, necessary preparation must be undertaken to determine the changes to be made in the process, and further guidelines be developed.

Ma. Joy V. Abrenica reiterates that there is a problem in the removal of the barriers in the dynamics of technological convergence. She finds that the success of breaking its grounds depends on some key factors. These include the regulatory simplification, the appropriate safeguarding against the monopolistic tendencies of dominant players, the area of reform as in the interconnection of networks, the correct pricing for the development of an information-based services, and the network competition. Thus, to give solution to the problem, the idea of extinguishing the market power of dominating supplier is highly recommended. According to her, this can be done through the minimum regulatory intervention, a "global" regulating standards and protocols, and with the flexibility in regulation as the observed norm.

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