

PHILIPPINES ECONOMIC WRAP-UP
MARCH 24-30, 2001

Summary

In addition to our regular reports on forex, credit and equity markets, this week we note January's reversal of eight consecutive months of increases in aggregate production volumes (year-on-year output fell 2.4%). A debate over how to address shortcomings in revenue collection systems reaches the senior-most levels of government. In an effort to improve the efficiency of credit markets, a bank industry group is preparing to launch a secondary market for fixed-income instruments. And we note a flurry of U.S. interest in Philippine markets.

These weekly reviews are available on the Embassy's web site (<http://usembassy.state.gov/manila>). Readers should note that we will not publish the 'Wrap-Up' on April 13 due to local Philippine holidays. We provide a longer and more detailed review of the Philippine economy in our February 2001 Economic Outlook, which is now available on our web site.

This issue of the Weekly is dedicated to Elvira Dimarucut, who retires on March 30, 2001 from many years as the Embassy's chief expert on Philippine industry and trade. Her contributions to the Weekly and all our other work will be sorely missed, and we wish her all the best in her future endeavors.

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Market and Policy Developments

FOREX REPORT

The value of the Philippine peso continued to weaken. Traders commented that demand for dollars was boosted this week by end-of-month and end-of-quarter remittance requirements. The ongoing depreciation of the Japanese yen and other regional currencies also dragged down the peso. From its March 23 close of P49.135/US\$, the peso sank to close on March 30 at P49.510.

Exchange Rate Tables

Date	Weighted Average (Pesos/US\$)	Closing (Pesos/US\$)	Volume (Million US\$)
FEB 19	47.672	47.850	90.4
20	47.801	47.630	153.1
21	47.925	48.120	138.0
22	48.234	48.350	222.1
23	48.323	48.160	170.5
FEB 26	48.094	48.230	125.0
27	48.263	48.265	129.5
28	48.286	48.280	93.7
MAR 01	48.374	48.470	100.1
02	48.490	48.340	125.5
MAR 05	47.812	47.670	114.5
06	47.666	47.660	121.1
07	47.799	47.905	140.5
08	48.002	47.910	163.0
09	47.982	48.065	164.5
MAR 12	48.177	48.145	138.8
13	48.159	48.160	130.8

14	48.141	48.200	66.0
15	48.367	48.430	148.5
16	48.627	48.500	149.2
MAR 19	48.551	48.505	128.5
20	48.496	48.440	131.7
21	48.580	48.633	150.1
22	48.797	48.955	159.5
23	49.048	49.135	138.0
MAR 26	49.221	49.185	64.8
27	49.120	49.165	87.0
28	49.208	49.215	107.5
29	49.378	49.355	157.1
30	49.371	49.510	122.4

Source: Bankers Association of the Philippines

CREDIT MARKET REPORT

National Treasurer Sergio Edeza said that interest rates have bottomed out, and will only fall further if the inflation forecast improves, as interest rates on the 91-day T-bill dropped 58.7 basis points to 9.059%. This is the lowest rate seen on the 91-day bill since September 2000. Rates on 182-day bills fell a smaller 20.5 basis points to 10.331%, and rates on 364-day bills fell 38.3 basis points to 10.957%. Edeza told reporters that while we liked to consider the falling rates as a 'vote of confidence' in the new government, he also noted that the declines also reflect strong liquidity in the banking sector and continuing forecasts of weak credit growth. Nearly P11 billion worth of bids were received for the P4 billion worth of T-bills on offer at the Monday auction. Edeza further noted that the continuing decline of international equity markets may be driving some investors into the bond markets.

Domestic Interest Rates (in percent)

Treasury Bills

Auction Date	91 days	182 days	364 days
FEB 19	10.525	11.900	12.500
FEB 26	10.456	11.783	12.497
MAR 05	10.328	11.560	12.453
MAR 12	9.893	10.983	11.788
MAR 19	9.656	10.356	11.340
MAR 26	9.059	10.331	10.957

Source: Bureau of the Treasury

Prime Lending Rates of 15 Expanded Commercial Banks

Date of Survey	Average	Range
FEB 21	14.9393	12.25 - 19.00
MAR 01	14.5759	12.25 - 19.00
MAR 08	14.3913	12.00 - 19.00
MAR 15	13.6914	11.50 - 15.25
MAR 22	13.5156	11.25 - 14.656
MAR 28	13.0484	10.75 - 14.50

Sources: Bangko Sentral ng Pilipinas; Press reports

STOCK MARKET REPORT

Turmoil on world equities markets continued to spill over into the Philippines, although late-week bargain hunting managed to nudge up the 33-share Philippine Stock Index (PHISIX) 1% over its March 23 close. On the domestic front, one trader said that no significant developments are expected on the corporate or the economic reform fronts from as the country gears up for national elections on May 14. The PHISIX ended the week at 1446.40.

Philippine Stock Exchange Index (PHISIX) and Value of Shares Traded

Date	PHISIX Close	Value (Million pesos)
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FEB 19	1673.96	444
20	1659.08	369
21	1654.86	378
22	1641.05	485
23	1647.00	595
FEB 24	1636.04	498
25	1632.30	344
26	1613.49	995
MAR 01	1570.20	735
02	1596.97	499
MAR 05	1616.54	614
06	1611.47	328
07	1612.81	312
08	1589.57	223
09	1588.39	613
MAR 12	1567.53	196
13	1526.40	348
14	1523.79	266
15	1491.79	383
16	1498.32	309
MAR 19	1507.52	374
20	1491.54	335
21	1471.56	277
22	1466.23	420
23	1431.57	486
MAR 26	1448.37	586
27	1446.99	401
28	1451.55	475
29	1430.16	346
30	1446.40	438

Source: Philippine Stock Exchange

JANUARY MANUFACTURING AND SALES VOLUMES DECLINE

The National Statistics Office's (NSO) latest Monthly Integrated Survey of Selected Industries (MISSI) showed a

2.4% year-on-year decline in aggregate production volume during January 2001. That performance broke from eight months of consecutive year-on-year growth. Seven of sixteen manufacturing sub-sectors posted production declines (led by food manufacturing, electrical machinery, and wearing apparel). Sales volume (down 2.4% from January 2000) contracted after posting year-on-year gains since September 1999. Eleven of the sixteen sub-sectors reported lower sales.

January 2001's performance was widely expected. Businesses, already struggling with rising production and operating costs, as well as softening world demand for major export products, had to deal with challenges posed by escalating political uncertainties (which, among others, saw the peso drop to new lows and domestic interest rates jump). As manufacturers pared output, the average capacity utilization of manufacturing industries declined to 77.3% -- the lowest in two years. Capacity utilization averaged 77.6% and 80% in January 2000 and December 2000, respectively.

The government hopes that full-year 2001 manufacturing gross value added will muster 5-5.5% growth in real terms (compared to 5.6% growth during 2000) for GDP to expand by 3.8-4.3% this year.

 MONTHLY INTEGRATED SURVEY OF SELECTED INDUSTRIES

	Year-on-Year % Change Production Volume	% Change Net Sales Volume
January 2000	12.3	10.1
February	7.7	10.5
March	2.5	10.5
April	(2.4)	8.3
May	12.6	21.0
June	13.5	8.0
July	19.7	5.7
August	9.2	13.2
September	15.9	2.9
October	20.0	3.7
November	39.7	15.8

December	8.7	7.7
January 2001	(2.4)	(2.4)

Source: National Statistics Office

NEW AGENCY TO COLLECT TAXES?

Commissioner of the Bureau of Internal Revenue (BIR) Rene Banez on March 26 told a meeting of the Philippine Chamber of Commerce and Industry (PCCI) that he would recommend to new Congress in July the creation of a new and independent "Philippine Internal Revenue Authority" to replace the existing Bureau. Banez said the improvements in tax administration rendered by the new agency would be accompanied by improvements in tax structures and policies. Banez told the group that BIR was finalizing its ideas for approval by its parent organization, the Department of Finance (DoF), and then the DoF and BIR would engage the private sector and 'civil society' for fine tuning before submitting draft legislation to the new Congress in July.

Speaking separately to reporters on March 27, President Macapagal-Arroyo opined that she "is not yet convinced" of the need to replace the BIR, and suggested that legislation to do so would not be among her top legislative priorities. The president indicated that a comprehensive review of the nation's tax systems was being undertaken by the National Economic and Development Authority to develop an overall response to continued revenue shortfalls.

BAP PREPARING TO LAUNCH FIXED-INCOME EXCHANGE

The Bankers Association of the Philippines (BAP) is spearheading efforts to launch the country's first fixed-income exchange. The electronic exchange (there will not be an actual trading floor) will provide a secondary market for trading Treasury, bank, and corporate issues, as well as asset-backed securities and other fixed-income funds. Senior BAP officials told the Embassy that the central bank, Securities and Exchange Commission (SEC),

and Philippine Treasury Bureau have already given their "approval-in-principle". Codes and manuals on various areas of policy and operations (including a code of ethics, dealer accreditation guidelines, a manual on risk reference, a manual on best international origination and underwriting practices, and a rule book on governance of the exchange) are in the final stages of completion. The envisioned fixed-income exchange's product profile is patterned after the Luxembourg model, and its rule profile after the London exchange.

According to BAP officials, the envisioned fixed-income market will initially be capitalized at P500 million. BAP intends to put up P100 million -- the maximum 20% share allowed any one industry group under the Securities Regulation Code of 2000. The remaining 80% will be sold to other parties through a road show planned in June. A "shell company" which will eventually evolve into the fixed-income exchange reportedly is in the final stages of incorporation. The BAP targets to launch the fixed-income exchange by July 2001.

BAP officials told the Embassy that they have been working on this project for more than a year. They noted that the BAP had actively involved government regulators from the start and, for this reason, expressed confidence that the long-envisioned exchange would finally see fruition this time around. At this point -- and despite some skepticism from a number of traders -- they did not foresee major technological impediments to running the envisioned exchange efficiently, including the institution of an efficient payment and settlement system.

Admittedly, however, a number of important policies which inhibit active trading have yet to be threshed out with pertinent government agencies. These include BSP-imposed reserve requirements on reverse repurchase transactions and, more critically, a burdensome tax system (including "cascading" documentary stamp taxes). Given current fiscal difficulties, the BAP is working with a consultant to make a strong argument that tax reforms will not necessarily mean revenue losses.

AMERICAN INVESTORS BULLISH ON THE PHILIPPINES

American food giant Kraft Foods International will establish its regional headquarters in the Philippines to oversee its expansion in South East Asia, Indochina, India and the Pacific Islands, the fastest-growing emerging markets worldwide. The Philippines itself accounts for half of Kraft's sales in Southeast Asia. Kraft's merger with Nabisco created one of the world's biggest food concerns, second only to Switzerland's Nestle. Kraft hopes to increase 2001 sales in the Philippines by 45% to P4.5 billion (about \$93 million) from the previous year's P3.1 billion (about \$64 million). Nabisco is expected to contribute 13% to this year's sales. Kraft Foods is a subsidiary of the Philip-Morris group.

Philip-Morris Asia president Duck Song, during a recent courtesy call on President Macapagal-Arroyo, announced that Philip-Morris is separately expanding its Philippine operations, started in the 1950s. Philip-Morris will put up a \$300 million cigarette plant on a 25-hectare lot in First Philippine Industrial Park in Batangas (south of Manila). Construction of the new plant will start middle of this year, and the facility should be fully operational by the end of 2003. Philip-Morris projects that a reduced 0-5 percent tariff on all products imported from ASEAN member countries by January 2003 (provided in the ASEAN Free Trade Area agreement, or AFTA) will boost demand and trading among AFTA member states.

A team of top American executives, led by Philippine-American Chamber of Commerce chair John Howley, has also pledged, during a recent call on the President, to follow up on various investment leads in the country. These include: (a) Prudential Asia Infrastructure Investors Ltd., which has allotted \$75 million out of its investment funds to the Philippines, specifically for transport; (b) Spectrum Technology Corp. has offered to explore and develop oil and gas reserves at no expense to the government; (c) Computer Associates, one of the world's largest software makers, would make the Philippines its regional hub for software development; (d) Continental Airlines plans to increase flights to the country in anticipation of increased traffic; and, (e)

SCS-Wetherill is looking closely at solid waste management projects in the country. The quick succession of business calls and pledges from American executives illustrates renewed business interest in the Philippines.