On changing the economic provisions of the 1987 Constitution:
More foreign investment does not mean more development

Statement for the House Committee on Constitutional Amendments
on the Proposed Amendments to the 1987 Constitution
IBON Foundation, January 26, 2023

There is a strong desire for change. The social and economic situation of the majority of Filipinos has long lagged behind the country's potential for real and equitable progress. IBON can only officially speak for itself but we would like the committee to know that we are in contact on this matter with among the widest networks of people's organizations and NGOs in the country and our position closely reflects their sentiments.

IBON Foundation opposes the proposed amendments to the economic provisions of the 1987 Constitution. The economic provisions of the 1987 Constitution are best retained and not subjected to any revisions or amendments.

We have five major points inviting the committee to be more circumspect about charter change, specifically of the economic provisions, and to put foreign investment in its proper historical and development context.

First, we agree about the potential benefits from foreign direct investment (FDI) to varied sectors and areas of economic activity. These are already highlighted by proponents of changing the economic provisions. We will not dwell on them aside from point out that the frequent resort to anecdotal evidence of benefits of specific investments commits the fallacy of composition and more attention has to be given to the macroeconomic and long-term impacts of foreign investment.

Second, foreign investment has to be strictly regulated to contribute to national development. The potential benefits from FDI are well-known and real – but they are neither intrinsic nor spontaneous. These benefits will only materialize with the appropriate foreign investors in the relevant sectors and, even then, only in the right policy context.

We are of the view that foreign investment's contribution can only materialize in the context of meaningful industrial policy, or industrial and technology policy, or national industrialization policy, however it may be called. It is critically important to first be clear about how exactly FDI is going to be made to contribute to long-term national development before asking how to attract FDI. The current foreign investment fetish places the cart before the horse and erroneously treats FDI as a good in itself.

FDI will operate according to its rational self-interest and judicious regulation is needed for it to support the country's development needs. Foreign capital seeks to profit from their investments in the Philippines – not strategically develop the country which is the unique purview of the government – and it is natural for them to consistently use their accumulated capital and other capabilities to their individual corporate advantage even at the expense of strategic objectives of the host country.

Recall for instance our experience with Intel, Hanjin and the Malampaya gas investments. In their time, they all invested billions of dollars, booked billions of dollars in exports (or provided energy in the case of Malampaya), and employed thousands of Filipinos. Yet because of our overly liberal approach there is little beyond immediate short-term gains. After decades of operation the Philippines has yet to develop any semblance of indigenous electronics, shipbuilding, or natural gas industries which would indicate strategic national development. Foreign manufacturing locating in the country is not equivalent to national industrial development.

This is aside from how our scarce mineral, forestry and fishery resources will be exploited with limited benefits for the local economy and in many cases even lost forever. Farmers' organizations we work with also fear that foreign investor interest in land will tend to drive land prices up and dislocate communities. Consumer groups worry that pricing of utilities will fall more and more beyond the scope of government regulation and compromise affordability and access.

Third, foreign equity restrictions can be an important tool for development. They are not binding constraints. Indeed, after decades of liberalization, they are among the last remaining regulatory tools to build national industrialization and technology policy on. It would have been better to have a bigger basket of policy measures at hand but we are forced to make do with what we have left. If anything, economic policy should be directed to expanding our economic policy toolbox.

Equity limits are effective measures for exercising control over foreign capital, learning production advantages, and capturing economic surpluses. Constitutional compulsion is a powerful point of policy leverage and the economic provisions can be wielded to the country's benefit. The Constitutional right and authority to regulate foreign investment is a powerful policy instrument that should be used more.

We will actually lose policy flexibility by removing the restrictions particularly if foreign capital increases their presence in the country. More than ever, policymaking will become bounded by what is acceptable to foreign investors in the country. We will become even less able to pursue historically effective measures to build national industry – e.g., ownership limits or requiring joint ventures in strategic industries, local content, technology transfer, and other performance requirements.

It is a myth that the developed countries developed because they liberalized – they liberalized because they first developed. This is the clear historical lesson from the experience of major industrialized countries.

South Korea and Taiwan until the 1980s were protectionist- and development state-driven economies that regulated foreign investment. Likewise with the United States (US) and Europe in the 19th and early 20th century, and with Japan until at least the 1950s. Russia and China had their respective periods of Socialist revolution in 1917 and 1949 and the attendant regulatory bias stretches until today. China, the world's fastest growing large economic power, has a very restrictive formal and informal mechanisms and exercises a wide range of controls on foreign capital.

We grant that the successful use of these measures in other country and historical contexts cannot be mechanically appropriated. The direction of regulation is nonetheless clear and the process of learning-by-doing and developing creativity amid current global conditions will not happen with concrete practice. The diminution of state capacity from decades of free market thinking – and well-meaning anti-corruption or pro-efficiency impulses – is however a current limitation that needs to be painstakingly overcome. (The Philippines has among the smallest shares of public employment to total employment and of public expenditure to GDP in the world.)

Fourth, the Philippine experience is that vastly growing foreign investment inflows haven't contributed to national economic progress as promised. Foreign investment is a means to development and not, as it is often virtually portrayed, an end of development. It is important not to lose sight of what foreign investment is ultimately meant to contribute to.

Despite the supposedly restrictive provisions of the 1987 Constitution, foreign direct investment (FDI) has grown substantially since the 1980s both in absolute amounts and as a share of GDP. (**See Table 1** and **Chart 1**)

Annual foreign investment inflows are over forty times larger than in the early 1980s – from an annual average of US$186.8 million (equivalent 0.5% of GDP) in 1980-1984 to US$8.56 billion (2.5% of GDP) in 2015-2019 and US$8.67 billion in 2020-2021 (2.3% of GDP). The inward stock of FDI increased ninety-fold from US$1.28 billion in 1980 to US$113.71 billion in 2021, and in effect eight-fold as a percentage of GDP from 3.5% to 28.9% over that same period.

However, the share of industry and agriculture in the Philippine economy has fallen continuously over that period of rising FDI and globalization. (**See Charts 2** and **3**) In the late 1990s, the economy became a service economy more than a producing economy with the share of services greater than of industry and agriculture combined.

Deployments of overseas Filipino workers spiked in the 2000s after this to cement our over-dependence on overseas work and remittances. The foreign exchange from overseas Filipinos became particularly important to meet growing trade deficits, much of which is even due to the import-intensive nature of foreign investment in the country. (**See Chart 4**)

The largest share of foreign investment has historically gone to manufacturing. Yet domestic manufacturing is a smaller share of the economy and employment now than in the 1950s. Most manufacturing in the Philippines is not even Filipino anymore with FDI accounting for as much as 70% of total approved manufacturing investments in the last 20 years.

This erosion of our economy is not an aberration. On a global scale, there has not been any breakout industrialization by any underdeveloped country in the last four decades of globalization. The last major examples were the newly industrialized countries (NICs) of South Korea and Taiwan in the 1970s and 1980s. None of the so-called NICs since then have reached developed country status.

It is also striking that the Philippines today has more foreign investment in absolute terms and as a share of GDP than Taiwan, South Korea and China did in their respective periods of economic take-off. (**See Table 1**)

Will more foreign investment necessarily make things better? This is unlikely without a rethinking of our overall development strategy and the appropriate role of foreign investment.

Fifth, current global conditions of growing protectionism, investment controls, and eroding multilateralism make relaxing foreign equity restrictions even more inappropriate. The most powerful capitalist economies in the world have been at the forefront of thousands of protectionist measures since the onset of the protracted global crisis in 2008. The trade war between the US and China grabs headlines but protectionism is also on the rise across Europe, Russia, India, Japan and elsewhere.

The development benefits of trade and investment liberalization during widespread liberalization are dubious to begin with but certainly become even more questionable when more and more countries are becoming protectionist. The emerging restrictive global policy environment is a context to be navigated and not ignored or wished away.

The United Nations Conference on Trade and Development (UNCTAD) has been reporting declining investment liberalization and, on the other hand, growing investment restrictions since the 2008/09 global financial and economic crisis; this accelerated especially since the pandemic and growing concern for national economic security worldwide. (**See Chart 5**) UNCTAD notes that an average of 35% of new investment measures since 2020 have been towards greater investment restrictiveness compared to less than 16% before the 2008/09 global crisis. Even the World Economic Forum (WEF) points out increasing restrictiveness of FDI rules and regulations since 2008.

Growing numbers of countries are also terminating international investment agreements seen as disadvantaging national development with more risks and costs than benefits. UNCTAD reports an almost tripling of international investment agreements from a little over 100 terminated in the period 2001-2010 to nearly 350 in 2011-2021. This includes countries as near as Indonesia, or further such as India, Ecuador, Venezuela and Bolivia, to as far away as South Africa.

Global FDI flows have also been falling since 2016 and especially in 2020 upon COVID-19. The next few years will be uncertain depending on the direction of post-pandemic supply chain restructuring, the impact of policies to deal with the economic shock, as well as geopolitical tensions.

Slowing global growth, growing investment restrictions, and countries' efforts to cope with their respective economic slowdowns are resulting in slowing global trade and investment. (See **Charts 6** and **7**) These trends that have been going on for some time now should at least prompt serious reflection on giving undue focus on export- and FDI-led development over domestic-led development.

In any case, the correlation between restrictiveness to foreign investment according to the OECD and foreign investment inflows is by no means strong and absolute. (**See Chart 8**) There are evidently many things beyond investment policy restrictions that determine foreign investment flows.

Taking all these into consideration, IBON's position is categorically to retain the economic provisions as they stand. The economy's development lies in using the protections in the Constitution to gain from foreign investment, not in taking away the protections and giving rationally self-interested profit-seeking foreign investment even greater rein over the domestic economy.

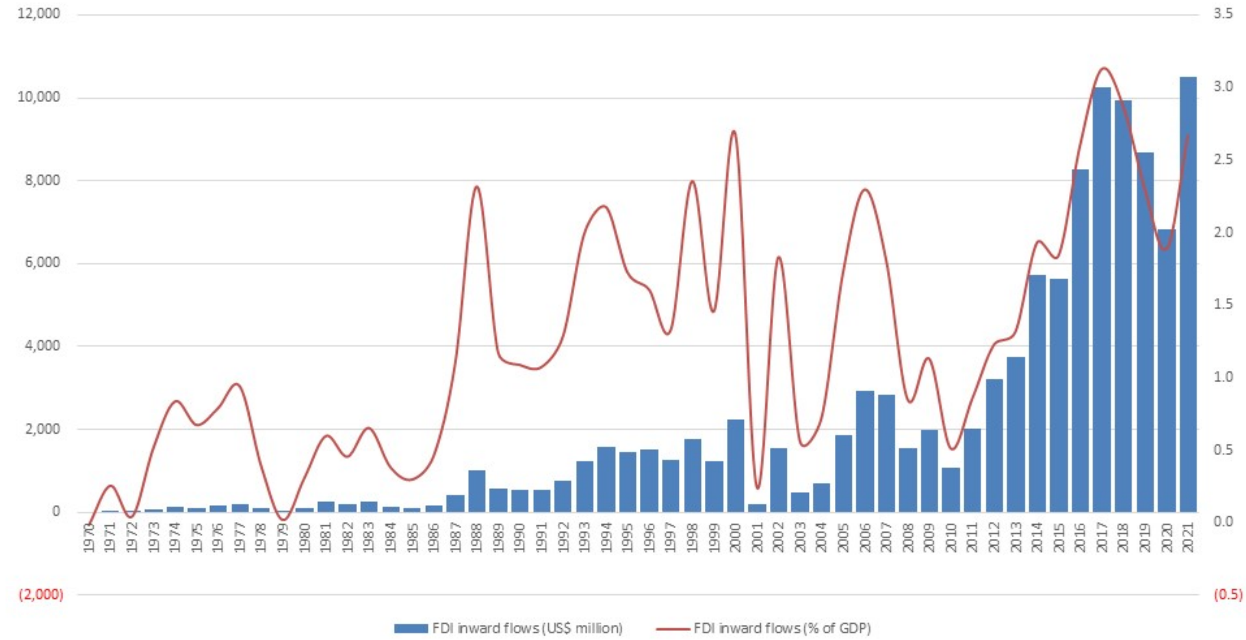
Foreign capital can contribute to development but we are of the view that responsible government intervention and regulation is needed to create meaningful linkages and long-term benefits for the economy. ###

Table 1: Foreign direct investment indicators, 1970-2021

Annual averages, unless specified	1970-74	1975-79	1980-84	1985-89	1990-94	1995-99	2000-04	2005-09	2010-14	2015-19	2020-21
FDI inward flows (US$ M, annual ave)											
Philippines	**42.9**	**117.1**	**186.8**	**448.8**	**942.2**	**1,445**	**1,031**	**2,228**	**3,154**	**8,559**	**8,670**
South Korea	122.0	96.8	146.1	911.8	1,094	5,057	8,762	10,368	10,161	11,188	12,792
Taiwan	52.5	79.2	153.8	789.6	1,154	1,764	2,567	5,011	2,034	6,168	5,729
China	*nda*	*nda*	617.4	2,620	16,028	42,057	50,894	86,204	122,441	137,027	165,150
FDI inward flows (% of GDP)											
Philippines	**0.3**	**0.6**	**0.5**	**1.1**	**1.5**	**1.7**	**1.2**	**1.6**	**1.2**	**2.5**	**2.3**
South Korea	1.2	0.2	0.2	0.5	0.3	1.0	1.3	1.0	0.8	0.7	0.7
Taiwan	0.6	0.3	0.3	0.7	0.6	0.6	0.8	1.3	0.4	1.1	0.8
China			0.2	0.7	2.9	4.5	3.4	2.5	1.5	1.1	1.0
FDI inward flows (% of GFCF)											
Philippines	**1.8**	**2.3**	**1.8**	**6.1**	**6.9**	**8.0**	**6.4**	**8.4**	**5.8**	**10.0**	**11.3**
South Korea	5.2	0.6	0.6	1.8	0.8	3.3	4.3	3.3	2.6	2.3	2.5
Taiwan	2.5	1.1	1.1	3.1	2.2	2.3	3.4	5.3	1.8	4.8	3.6
China			0.7	2.4	8.7	13.8	9.2	6.3	3.4	2.6	2.6
FDI inward stock (US$ M, end of period)		(1980)									
Philippines		**1,281**	**2,354**	**3,072**	**5,271**	**12,429**	**12,737**	**22,931**	**56,646**	**94,593**	**113,711**
South Korea		1,139	1,585	4,426	14,850	41,850	87,766	121,933	179,441	241,657	263,253
Taiwan		2,405	3,048	8,405	14,177	22,996	37,678	54,435	67,905	98,552	115,911
China		1,074	4,104	17,204	74,151	186,189	245,467	472,148	1,084,353	1,769,486	2,064,018
FDI inward stock (% of GDP)											
Philippines			**4.9**	**7.2**	**6.9**	**11.3**	**14.0**	**13.1**	**15.1**	**22.5**	**28.9**
South Korea			1.7	1.9	2.2	4.8	9.6	10.9	12.1	13.5	15.4
Taiwan			5.0	5.2	5.6	6.6	9.8	12.1	12.4	14.0	15.7
China			0.7	3.0	8.4	15.7	14.4	9.8	9.8	11.9	12.5
Real GDP growth (%)											
Philippines	**5.4**	**6.2**	**1.3**	**2.7**	**1.9**	**3.6**	**4.6**	**4.5**	**6.2**	**6.6**	(2.7)
South Korea	10.4	10.6	7.6	10.2	8.6	6.0	6.0	3.8	3.9	2.8	1.6
Taiwan	10.0	10.3	7.5	9.2	7.3	5.9	4.3	3.4	4.7	2.5	4.4
China	8.0	6.7	9.6	9.9	10.9	9.1	9.2	11.5	8.6	6.7	5.2

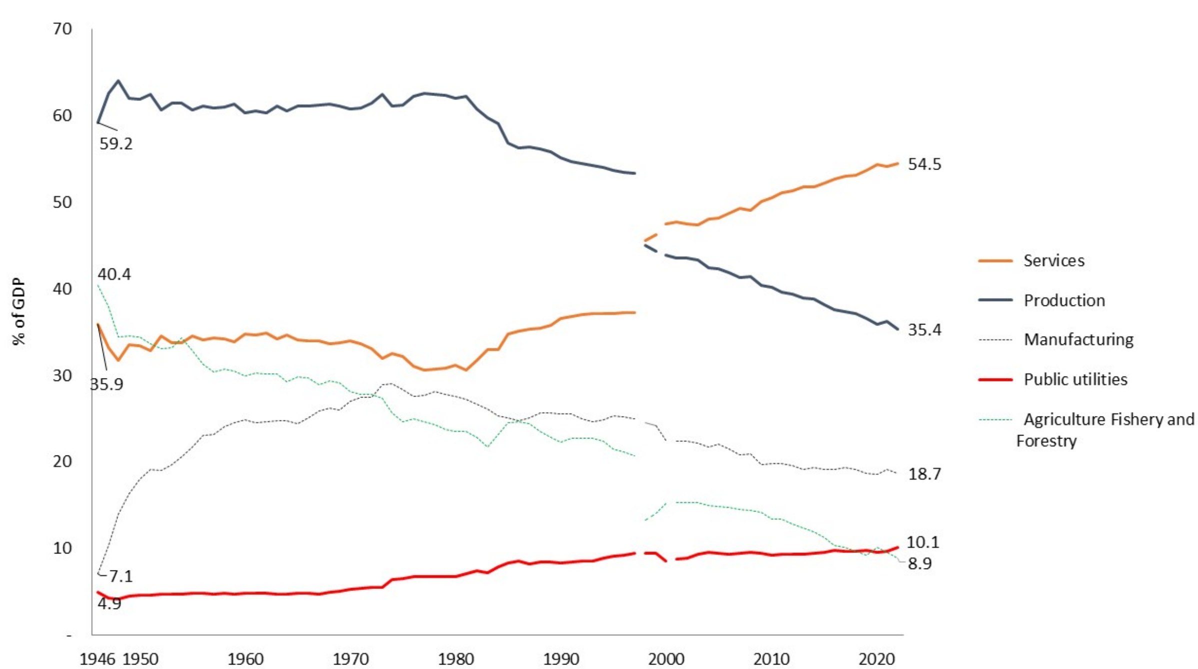
Sources: FDI data from UNCTAD; growth data from World Bank, except Taiwan 1970-1999 (FRED) & 2000-2019 (ADB), and Vietnam 1971-84 (UNdata)

Chart 1: Philippines FDI inward flows, 1970-2021 (US$ million, % of GDP)



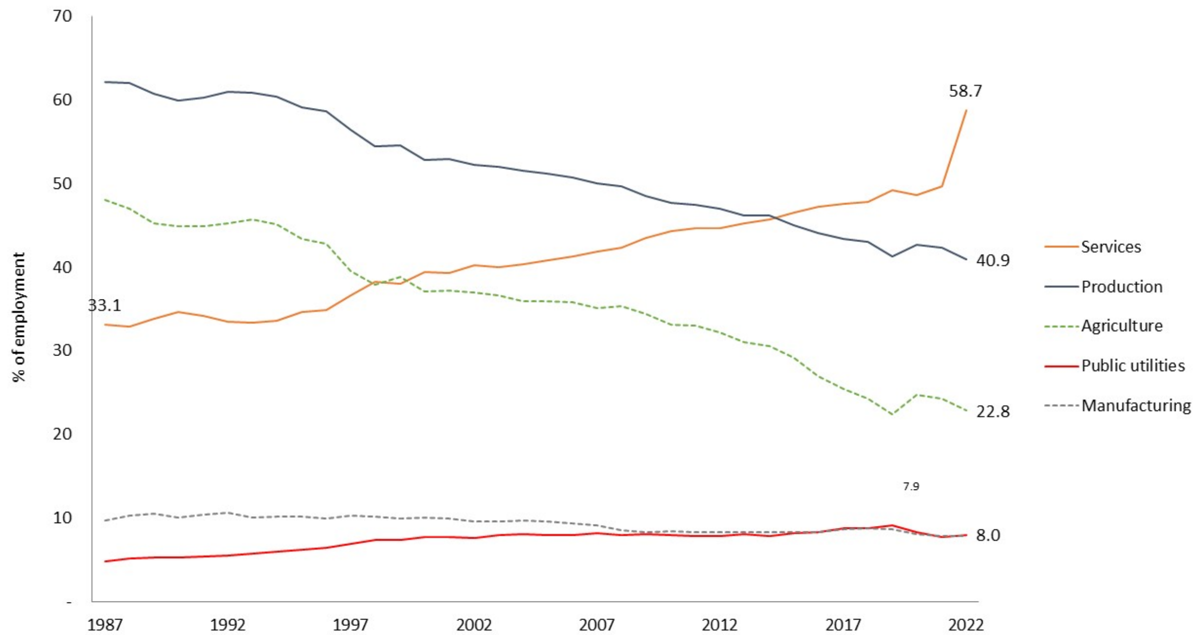
Source: UNCTAD

Chart 2: Industry share of gross domestic product*, 1946-2022 (%, at constant prices)



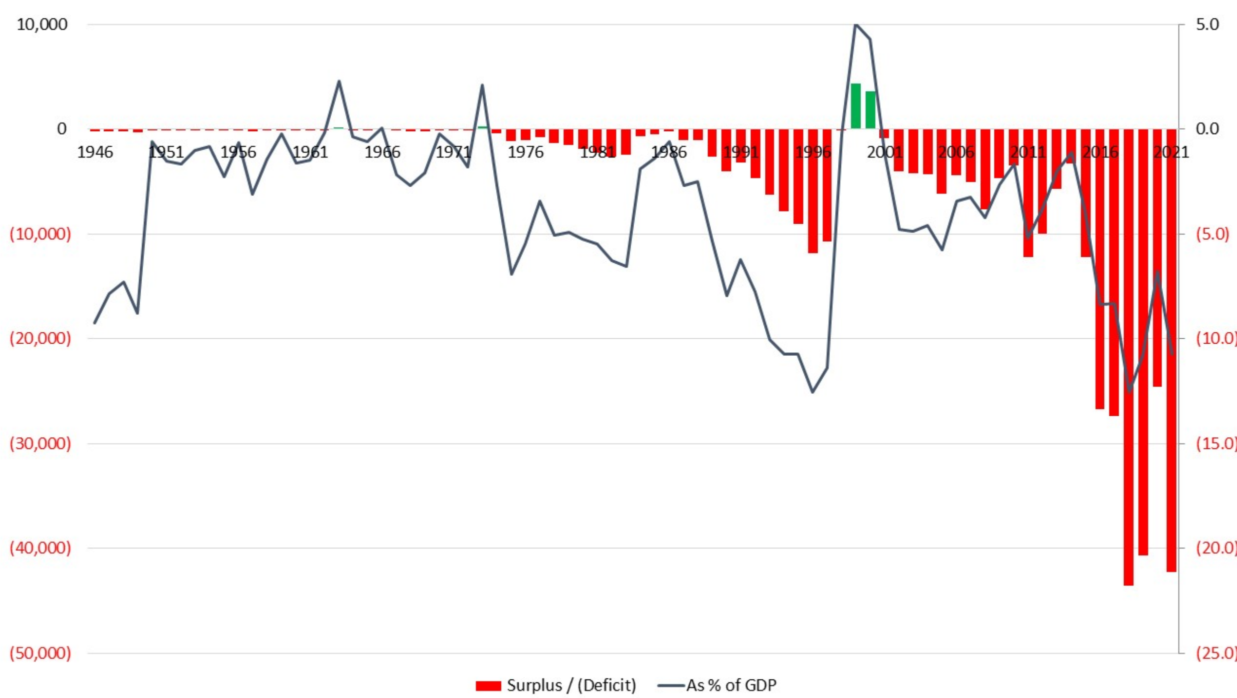
** "Production" is manufacturing, agriculture, mining & quarrying, and construction; "Public utilities" are electricity, gas & water, transport, storage & communication; and remaining sectors are "Services"*
Note: 1946-1997 at constant 1985 prices, 1998-1999 at constant 2000 prices, 2000-2022 at constant 2018 prices
Source: PSA

Chart 3: Employment by sector, 1987-2022 (% of total)



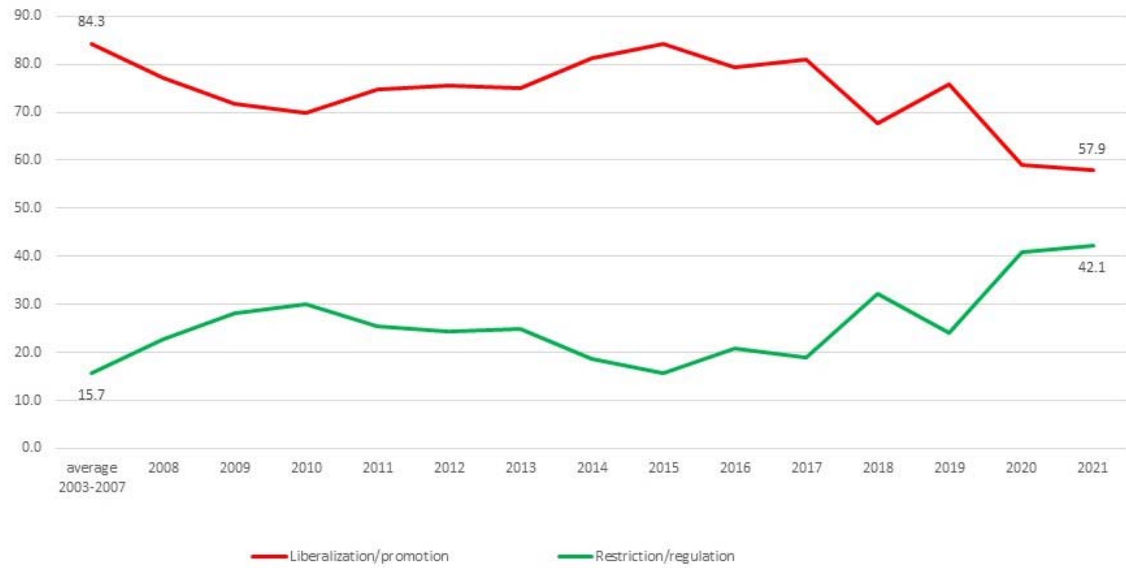
Source: PSA

Chart 4: Trade surplus/deficit, 1946-2021 (US$ million, % of GDP)



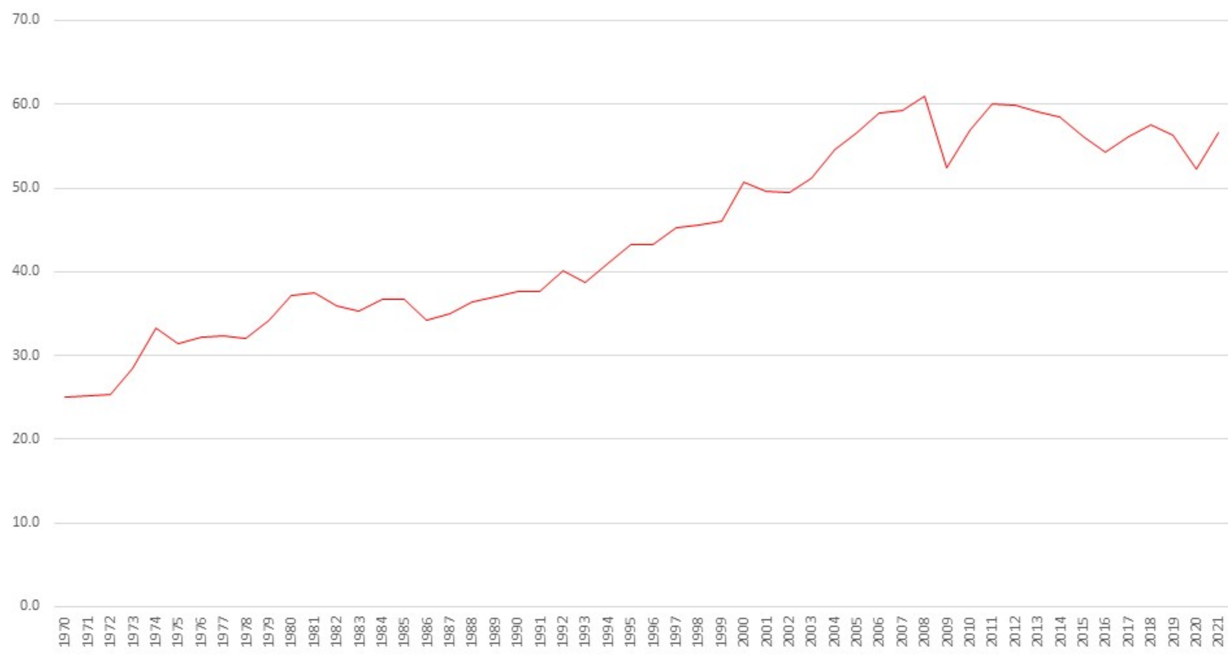
Source: PSA

Chart 5: Changes in national investment policies, 2003–2021 (% of total)



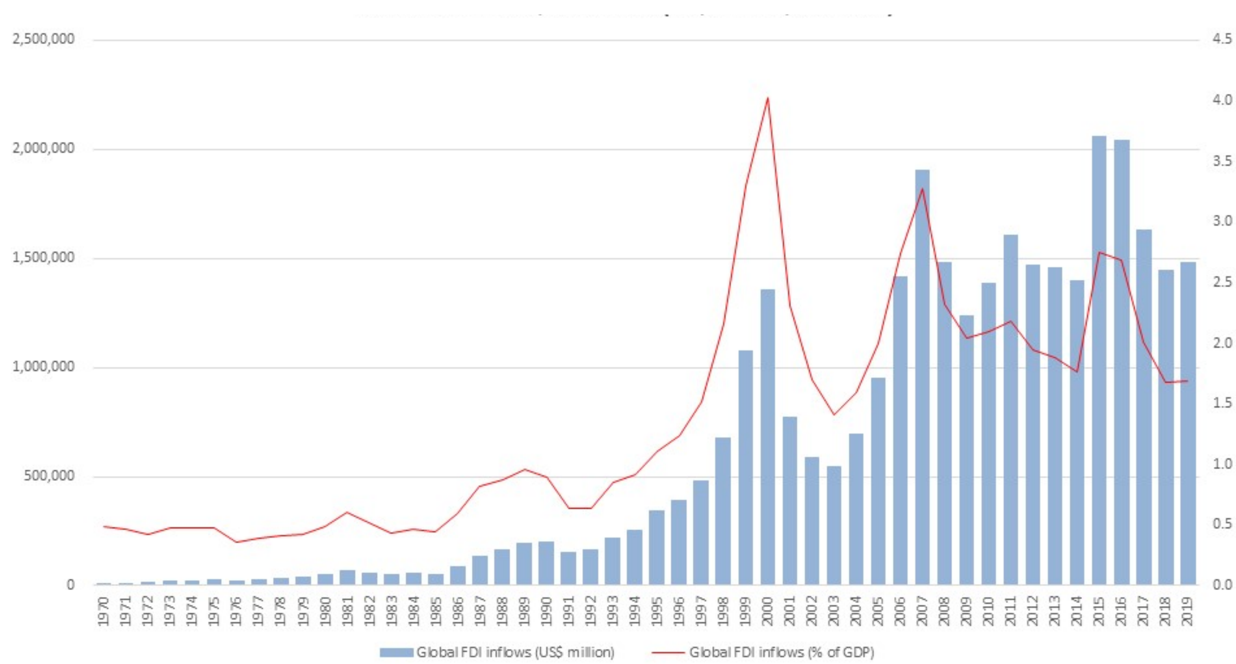
Source: UNCTAD

Chart 6: World trade in goods and services, 1970-2021 (% of GDP)



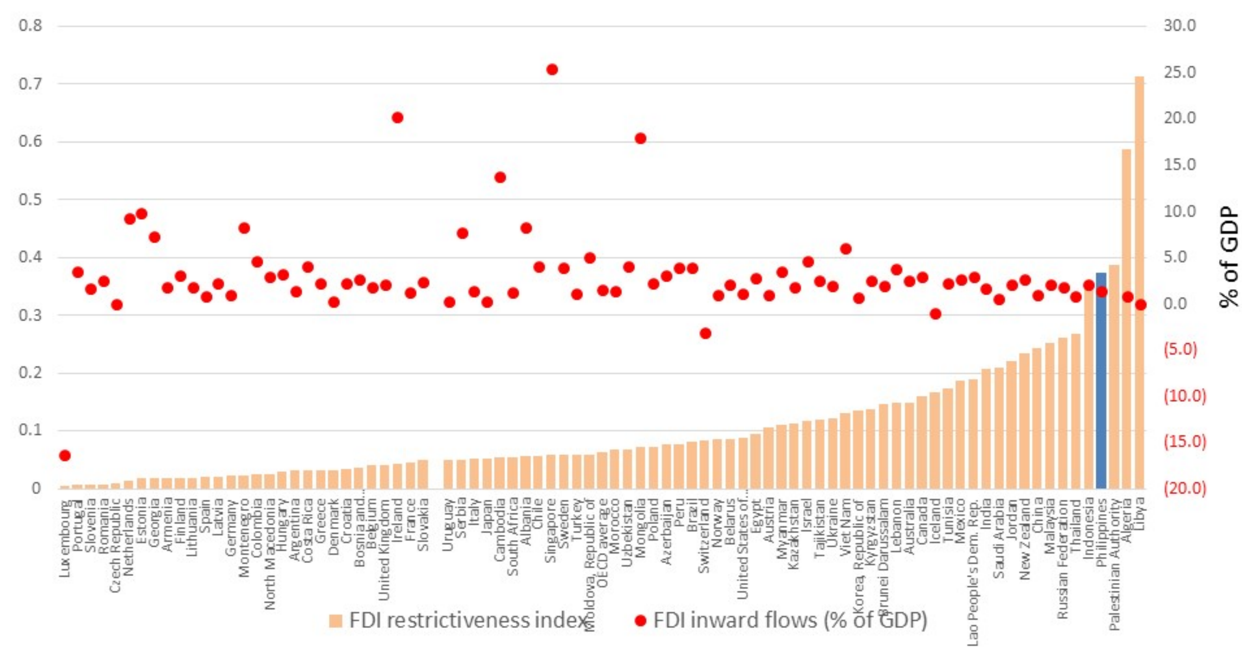
Source: World Bank

Chart 7: Global FDI inflows, 1970-2021 (US$ million, % of GDP)



Source: UNCTAD

Chart 8: FDI restrictiveness index vs. FDI inward flows (% of GDP), 2019



Source: IBON computations on data from OECD and UNCTAD