Dependency Theory and the Philippines' BOP Performance

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【研究論文】

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Abstract

This paper presents a critical exploration of the relationship between the Philippine's turbulent colonial past and its current economic state and whether Dependency Theory can explain said relationship, using the Philippines' Balance of Payments quarterly reports for the 2003-2017 period. It is divided in five sections: (1) Introduction; (2) Colonialism in Okinawa and the Philippines, a brief description of how colonialism developed in both areas; (3) Dependency Theory, an explanation of the theoretical basis for the analysis contained in this paper; (4) The Phillipines' Balance of Payments, an analysis of the country's Balance of Payments throughout the 2003-2017 period; and (5) Conclusions.

The conclusion reached is that Dependency Theory suffices for explaining more than half of the reasons why the Philippines reported deficit, and in the case of surplus Dependency Theory has a strong relationship with the majority of the driving forces behind the causes for surplus.

Introduction

The author adopts Dos Santos' Dependency Theory (DT hereafter) in an effort to explain periods of macro-economic deficit in the Philippines within its historical colonial context, along with a general description of the periods of macro-economic surplus in the country.

For this paper, the author seeks to determine whether DT can explain the reasons for deficit and surplus in trimesters between 2003 and 2017 period. Quarterly reports were chosen over yearly BOP reports because they present with more precision the macroeconomic fluctuations of a country. The 2003-2017 period marked a time for a fruitful study of economic fluctuations as a wealth of consistent data over a long period was readily available for analysis of the national economy of the Philippines. The author selected the balance of payments (hereupon BOP) as the study's unit of observation given the large quantity of information related to a country's economic performance contained therein. Moreover, the BOP can reveal a range of important economic indicators used universally for measuring national economic performance. The applicability of DT as a means for the explanation of deficit was discussed through the methodology, described in the third section.

The Philippines, for example, has long been a region of the world targeted by imperial powers for the expansion of their global markets, converting the archipelago into a dependency.

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Complicating these efforts of colonial expansion have been the conflicting internal interests of the various economic classes and ethnic groups, which have both historically challenged and accepted the whims of the colonizing powers. McFarland described in his work that the Philippines is a highly complex region comprising at least seven thousand islands whose inhabitants interact with one another through any of the various 110 languages. The United States' Central Intelligence Agency observes that it also is rich in culture and natural resources, and that the country has been striving recently to increase its manufacturing and service industries. As with various other island territories in the Pacific Ocean, the Philippines has extraordinary strategic value as an entrepôt and for garrisoning military troops.

Despite the various dynamics the Philippines shares with other island territories, it is an island nation that cannot yet be labeled as a "developed country". Philippine historical conditions beg the question: is there an important relationship between the Philippines' colonial past and its present-day socio-economic contradictions?

1. Colonialism in Okinawa and the Philippines

Readers might ponder what intersections of experience the people of the Phillipines have with the people of Okinawa, given the fact that the Japanese prefecture shares with the Philippines a background of colonialism and low economic development, when compared to other prefectures of Japan.

According to Hoshino, Okinawa has different layers of colonial history. Before becoming a Japanese prefecture, Okinawa, then known as the Ryukyu Kingdom, was a colonial subject first of the Satsuma domain, afterwards a domestic colony of Japan proper, in the aftermath of the Second World War a military colony of the United States and ultimately returned back to Japan in 1972. Throughout this time all the way to contemporary everyday Okinawa, the prefecture suffers from a series of socio-economic contradictions that run parallel to those of the Philippines.

Okinawan economic dependence on external geo-political actors has always been present, with varying degrees of intensity and benefit to the Okinawan commoner. The prefecture's economic development has always moved to the interests and whims of capital from either the Japanese mainland and more recently to that of foreign countries as well.

The post-reversion economy formula of military bases, public works and tourism (known as the three K economy), McCormack pointed, is an accurate example of the dependence of Okinawa on external actors to attain the development level of mainland Japan which has not yet been achieved. Far from disappearing, dependence in the prefecture has only mutated into more sophisticated forms. The abusive taxing, production, and land administration systems imposed by Satsuma domain have changed and evolved since long ago, but their remnants, in the form of Okinawan contemporary industrial structure, are still in place and more rooted than ever. In terms of economic development, this is arguably the main similarity between the southernmost prefecture of Japan and the Philippines.

The Philippines has had three different colonial invaders. Spain, which started its era in the archipelago, according to Agoncillo and Guerrero, on March 17th, 1521 (Agoncillo and Guerrero,

1984). The United States, which forced itself into the Philippines after winning the Spanish-American war of 1898, puting an end to more than three hundred years of Spanish domination, only to make the archipelago fall now into American hands. And the last colonial power to invade the archipelago was Japan, starting its colonial domination in 1945 after defeating the USAFFE (United States Armed Forces in the Far East), a Filipino-American joint force.

Speaking from the economic perspective, the three colonial powers caused in the archipelago the loss of capacity of international trade, which was destroyed at first by the Spanish galleon policies. Pre-colonial Philippines had a variety of trade relations with other Asian countries, especially China. Nonetheless, Spain, in accordance with the prevailing doctrine of mercantilism, closed access to the colony after a short time of imposing its sovereignty over the archipelago, letting the Philippines to trade only with Mexico (another Spanish colony) and China. This was the only foreign trade activity and main source of income for the colony for more than two centuries (Agoncillo and Guerrero, 1984).

After the Spanish period, international trade was further stunted by mercantilist measures adopted by the USA and Japan to take advantage of Philippine resources (Ninkovich 2001; Agoncillo and Guerrero 1984; Fast and Richardson 1979; Hartendorp 1967; Zaide 1957; Blair and Robertson 1903). During the American era the Philippines was forced to neglect trade ties with Great Britain, the Netherlands, China, France, Germany and Spain, and by 1930 the Philippine archipelago depended on mainland United States for 79% of its exports and 63% of its imports (Ninkovich 2001).

Finally, under the Japanese occupation, the Philippines suffered the seizure and looting of its industries, such as lumber, mining, shipyards, electric companies, manufacturing, and key logistics like the railroad, marine transportation lines and others. The archipelago was also tied financially to Japan in the form of loans and bonds from the Japanese Government via the Southern Development Bank (Hartendorp, 1967).

2. Dependency Theory:

The main postulates of Dependency Theory are that the world capitalist system is divided into a center and a periphery, or similar names, as core-periphery, metropolis-satellite, dominant country and dependent country, and others (other writers on dependency added a third division, the semiperiphery). According to Brewer, this center of the system develops at the expense of the periphery, while the periphery becomes more and more dependent on the events that happen in the center (Brewer 1990). In addition, Peet considered that development and underdevelopment are interdependent structures within the global economic system, instead of being a consequence of the character of the individuals in the underdeveloped economy (Peet 1991).

Dos Santos defined the center as countries that can achieve self-sustaining growth, while the dependent countries are those that grow only as a reflection of the dominant (center) country (Dos Santos 1970). In other words, the periphery can grow to a certain level, but only if the center is performing well. The incorporation of countries from the periphery into the capitalist economy is intended to supply the demands of the center.

According to Dos Santos, there are three forms of dependence, colonial, financial-industrial, and technological-industrial (Dos Santos 1970). Colonial dependence began in the 16th century, when the European colonial states, commercial capital and financial capital were in synchronicity, dominating the economies of the colonies through trade monopoly, colonial monopoly of natural resources and the monopoly of the labour market. Based on the colonial exploitation background of the Philippines described in the first part of this paper, it can be affirmed that the country matches the description of a dependent country, and that it had to fulfill the demands of three different dominant countries: Spain, the United States, and Japan.

Financial-industrial dependence consolidated its existence at the end of the 19th century, with the center dominating investment capital; and with the expansion of capital overseas, to the periphery, through investment in raw materials and agriculture for consumption in the hegemonic centers. In modern terms, it was a period of tremendous growth of Foreign Direct Investment. Because of this pattern of capital investment, countries in the periphery developed productive structures devoted to the export of products for consumption in the center. This pattern of investment and production, Dos Santos stated, produced what the United Nations' Economic Commission for Latin America called "foreign oriented development" (Dos Santos 1970).

Technological-industrial dependence started in the postwar period, with the expansion of multinational corporations' investment in underdeveloped countries. This form of dependence is caused by the international commodity and capital markets. It is considered that Dos Santos could not elaborate enough on this subject because MNC investment overseas was still a relatively new issue at the time the author was publishing his work during the 1970s. The work of Bornschier and Chase-Dunn was used to complement Dos Santos' explanation of technological-industrial dependence.

Investment opportunities in the periphery are limited, due to the small size of the internal market and low opportunities for export, and are absorbed by multinational companies due to the unavailability of financial, technological and world market resources to the local elites in the periphery. Furthermore, the transplantation of technology and organizational forms from the center to the periphery creates a disparity between the technologically optimal scale of production and the domestic market of the peripheral country. Ultimately, Bornschier and Chase-Dunn described, the industrial structure produced by dependence on MNCs is mostly monopolistic, does not absorb labor properly, and underutilizes the productive forces, provoking economic stagnation, unemployment, underemployment, and marginalization of the population, relative to countries that are less penetrated by MNCs and to the growth potential of the peripheral country (Bornschier and Chase-Dunn, 1985). Import of capital goods and an overt dependence on the performance of the export sector are byproducts of this form of dependence.

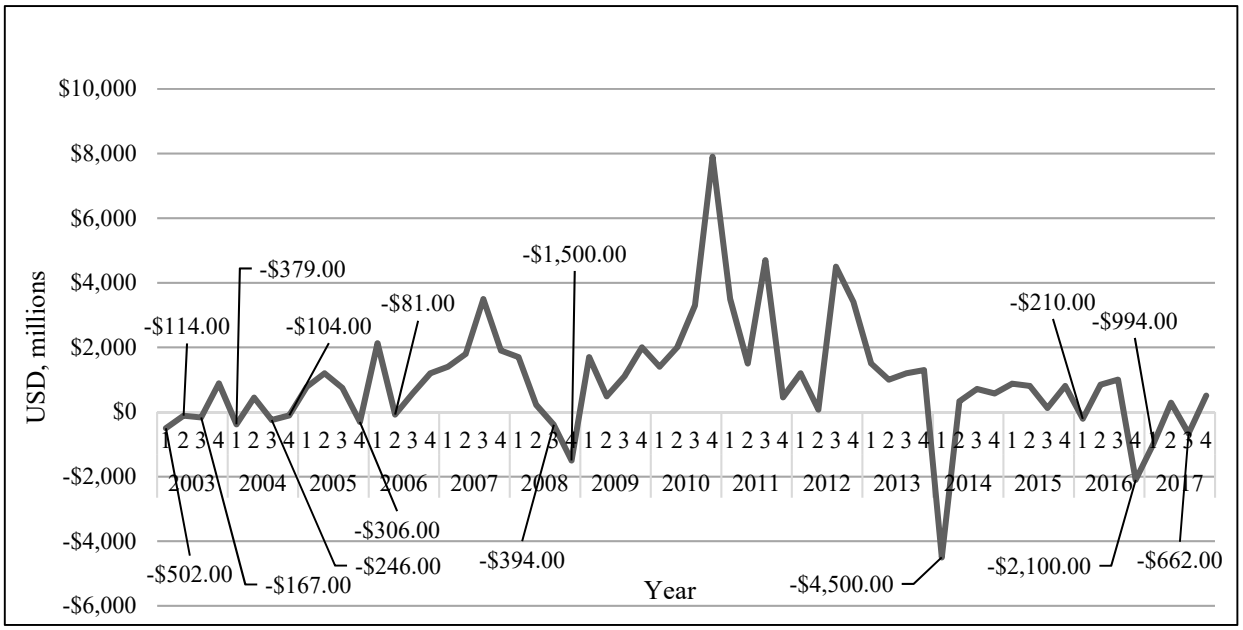
Based on Dos Santos' description of financial-industrial and technological-industrial dependence, the author considers that dependency is therefore represented by components of the BOP that rely on overseas actors to grow or decline, such as Foreign Direct Investment, Exports; and to a lesser extent income generated by Filipino nationals overseas (Overseas Filipino Workers, OFW), because OFW not always migrate to countries that could be considered capitalist centers.

BOP information regarding exports and OFW is complemented with other statistical information gathered from statistic and economic reports produced by the Central Bank of the Philippines and the World Bank as well. Given the colonial background of the Philippines, it is expected that the aforementioned components of the BOP have a decisive influence on the overall position of the Philippines' BOP. Changes (increases or decreases) in FDI, exports and remittances from OFW are expected to have immediate effects on the BOP position due to the dependence the Philippines has on foreign actors to keep its economy afloat.

3. The Philippines' Balance of Payments

This section is an analysis of the 2003-2017 period of the Philippines' balance of payments' accounts with deficit (see graph 1), done with the Department of Economic Statistics of the Philippines Central Bank's balance of payments quarterly reports. The balance of payments is an adequate tool for this study because it contains exhaustive information related to a country's financial position and how it is composed, while also describing a country's domestic economy and its interaction with the rest of the world. Therefore, it is an instrument rich in information pertinent to the study of dependence, especially from Dos Santos' definition of financial-industrial and technological-industrial dependence, which are, in the view of this author, intimately related with how investment and capital behave. The following graph shows the Philippines' yearly BOP position trend for the period under study:

Graph 1 The Philippines' BOP position, 2003-2017 period, quarterly



Data source: Central Bank of the Philippines (2003-2018)

The previous graph shows a BOP position that despite being highly fluctuating it displays surpluses most of the time, with the exception of the amounts expressly displayed in graph 1, which correspond to quarters with deficit observed in this study. First, the quarters with surplus will be

explained at a general level and then we will study into more detail the periods that reported deficit in the BOP position. One or more of the following reasons played an important role in said surpluses:

Exports: Mainly manufactured goods and commodities such as electronics, garments, minerals, coconut products, petroleum products, wood manufactures, processed foods, sugar, forest products, agro-chemicals, machinery and transport equipment. The three main destinations of Philippine exports were Japan, the United States and China.

Surpluses in income: Growth in the income and current accounts of the BOP, mostly thanks to remittances from Overseas Filipino Workers (from now on OFW), but also to other operations such as holdings of debt securities, reduced payments to foreign investors in the country or loans granted by non-residents, foreign companies' reinvestment of earnings in the Philippines, intercompany borrowing (companies with headquarters overseas that lend money to their subsidiaries in the Philippines), decreased interest payments on bonds issued by the Philippine government, gifts and donations.

Surpluses in the capital and financial account: inflows of portfolio investments like foreign issued debt securities, investments of non-residents in equity and debt securities, technical assistance or grants, sales of bonds denominated in foreign currency to non-residents, loans by the Asian Development Bank, and Philippine banks' earnings from mature bonds placed overseas, trade credits granted to resident corporations by non-residents, foreign loan avails and gains in financial derivatives trading.

Surpluses in trade of services: net receipts from travel (tourism), construction, communication, computer/information, and trade services, along with one of the Philippine's fastest growing industry, Business Process Outsourcing (henceforward BPO) services.

Increases in foreign direct investment (hereupon FDI): Placement by non-residents of investment in equity capital, reinvestment of earnings on direct investments, lower repatriation of dividends and profits, expansion of multinational companies.

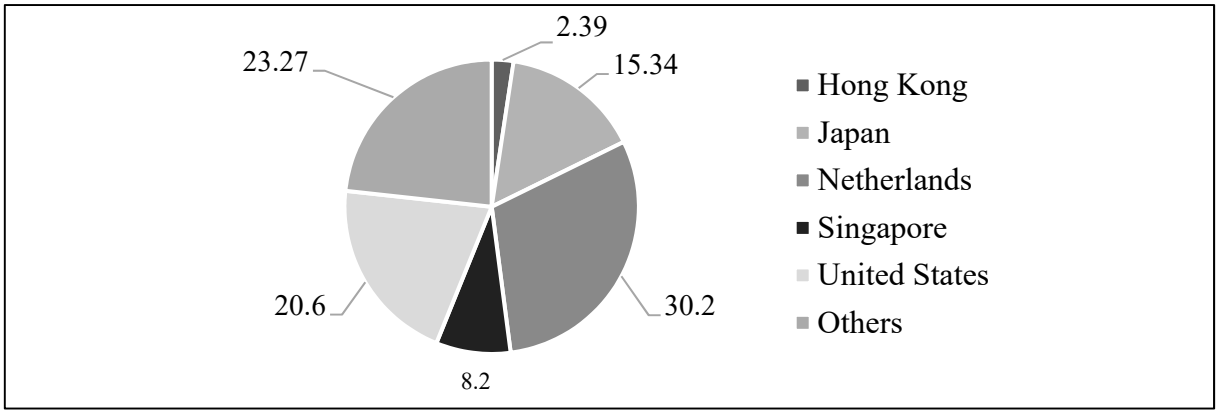
Income from other investments account: Repayment of trade credits extended by domestic corporations to non-residents, residents' investments abroad.

In addition to the reasons mentioned in the previous six categories, the positive outcome reflected in the balance of payments' reports was largely influenced by factors such as the strong and constant flow of remittances from OFW, which is a driving force of surplus in the current transfers account. Governmental incentives to certain industries during times of contraction, as in the incentives granted to the garment industry in 2005 pose an important positive influence on the BOP as well.

Another factor, the Philippines' famous BPO service industry, which is an attraction factor of FDI and income in general owes its success to Filipinos' proficiency in the English language, a legacy of the American colonial period, a comparative advantage that distinguishes the Philippines over other countries of the Southeast Asian region that could offer BPO services like Malaysia or Indonesia. However, growth in FDI is conditioned mainly by the economic conditions in the United States, Japan, the Netherlands, Singapore, and Hong Kong, which are the main sources of

investment to the Philippines for the 2003-2017 period. The 1999-2012 period as well showed almost the same main investors, more than 75% of FDI in the Philippines originated in five countries:

Graph 2 Major foreign direct investors in the Philippines, 1999-2012 (in %)



Source: The Central Bank of the Philippines
(http://www.bsp.gov.ph/statistics/spei/tab32.1.htm)

Information from the Central Bank of the Philippines from a different period (1999-2012) suggests that, in relation to foreign direct investment, the most important investors were the Netherlands (30.2%), the United States (20.6%) and Japan (15.34%). While Singapore (8.21%), and Hong Kong (2.39%) presented important shares of the total equity as well.

Moving on to the analysis of quarters with deficit in the 2003-2017 period, there were fifteen quarters with accounts that presented deficit, and a total of fifty-two different reasons why deficit happened in those quarters. The objective of the analysis was to determine if the main postulates of the Dependency Theory suffice for explaining the Philippines' periods of negative macro-economic performance.

The analysis method consisted of studying each of the fifty-two reasons and determining if there were any recurrent themes or patterns that could help in the definition of categories under which the reasons for deficit could be grouped, and then determining the importance of each category based on how many of the fifty-two reasons fell into each theme. The following seven categories were defined:

1. Problems that are explainable through Dependency Theory: Issues that were described by Dos Santos as part of Financial-industrial and Technological-industrial dependency, and financial relations between the dominant countries and dependent countries. Including but not limited to imports of capital goods, outflows of financial capital, foreign direct investment, loan repayments to financial institutions, and export performance. In general, economic setbacks of the Philippines that have origins from overseas.
2. Problems that have an indirect relation to Dependency Theory: Issues that can be explained with Dos Santos accounts on dependency but can also have origins in other problems such as

poor economic management in the peripheral country, or payments of external debt.

3. Natural disasters or epidemics.
4. Frontloading: The act of buying a twelve-month supply of a specific product (such as fuels and some edibles) in a specific trimester of the year, which can affect more than usual the balance of payments.
5. Imports of raw materials and intermediate goods.
6. Trade in services' account deficit: deficit originated by the Philippine purchase of services as financial, transport, insurance and other kinds of services that offset Philippines' export of services.
7. Sluggishness of the world economy.

After categorizing each of the reasons for the deficit in the Philippines balance of payments' accounts, it was determined that 56.86% were problems explainable through Dependency Theory, while 9.80% had an indirect relationship with Dependency Theory. As for the remainder, it was attributed to natural disasters or epidemics (3.92%); frontloading (3.92%); imports of raw materials and intermediate goods (11.76%); trade in services' account deficit (11.76%), and sluggishness of the economy (1.96%). The following paragraphs explain deficit problems from the four largest categories.

As the percentages demonstrate, more than half of the Philippines' balance of payments problems can be explained by phenomena that was described by Dos Santos in the section of this paper related to Dependency Theory (category 1), especially regarding how the behaviour of foreign capital affects the country's balance of payments and conditions the country's orientation of production. Outflows from national accounts as Capital, Portfolio Investment and Other Investments pose for the Philippines the most negative influence on its Balance of Payments, and this fact confirms that the way the Philippines accumulates capital and reproduces its economy is in great part dependent on external economic centers.

The economic centers, defined in this work as any country that shared a percentage of imports from and exports to the Philippines of more than 10%, are the United States and Japan, since those countries were, according to data from the World Bank's World Integrated Trade Solution and the Central Bank of the Philippines's balance of payments development reports, the main trade partners of the archipelago for the period under analysis. Although China does not meet the criteria defined for being labeled as an economic center, its growing role in Philippine exports and imports for the period analyzed suggests that China soon will become an economic center for the Philippine economy as well.

The next category, with a value of 9.80% was deficit problems that had an indirect relationship with the explanations of Dependency Theory (category 2). This category was named as such because not all the criteria included can be directly traced to a center-periphery kind of economic relations. For instance, trade deficit included in this category is not comprised by capital goods imports. Moreover, while intermediate goods can be produced in countries that are part of the center, there are also high possibilities that those goods could also be produced in other countries from the

periphery. The same condition applies for manufactured goods.

Other elements that form part of this category, like financial transfers from migrant working Filipinos can only be described as partially related to Dependency Theory's accounts, because they also migrate to countries that do not fit Dos Santos' description of a dominant country. According to the International Organization for Migration, more than fifty percent of registered Filipino emigration is to the United States, however, they also migrate to countries such as Saudi Arabia, Kuwait and Malaysia, countries that do not fit into the characterization of a dominant country (Battistella and Maruja 2013).

Outflow of investment has a similar behaviour. In the first half of 2016, the Department of Economic Statistics of the Philippines' Central Bank stated that Philippine portfolio investment was focused mostly in the United States (45.6%), nonetheless investment in a non-dominant country such as Indonesia accounted for a 18.9%. As for the remaining 35.5%, investment was distributed on a wide variety of countries like the United Kingdom, the Cayman Islands, the Netherlands, India, Korea, and others (Department of Economic Statistics of the Philippines 2017).

Raw materials and intermediate goods deficit, with a value of 11.76% was traced back to a variety of products such as: food products, motor vehicles, electronic appliances, materials for electronic products manufacture, chemicals, paper products, iron, steel, crude oil, and fuels.

Deficit in the Trade in Services account with a value of 11.76% as well, meant that the Philippines had to buy more services than it could sell abroad. Most of the services bought were financial services, like participation in the financial derivatives (like swap and future contracts) markets, followed by other services as freight, insurance, and recreation. In the case of freight, financial markets and insurance, they would qualify as another manifestation of the country's dependency upon the centers, given the fact that the Philippines must search for the mentioned services abroad because it does not possess the technology, infrastructure, political stability or normative framework necessary for providing those services domestically, forcing residents to search for these services abroad, where there are surpluses of capital, in countries of the center.

However, in the case of deficit caused by expense in recreation, which was mostly travel, there are other conditions at play that cannot be fully explained by Dependency Theory. The reason why Filipinos spent more on recreation cannot be explained by a center-periphery dynamic. It was, according to the Department of Economic Statistics of the Philippines' Central Bank, due to the stability of the Philippine Peso and improved global security, which encouraged Filipinos to seek recreation abroad (Department of Economic Statistics of the Philippines 2017).

Conclusion

The driving forces for surplus in the balance of payments of the country have a close relationship to Dependency Theory, given the fact that surpluses occurred thanks mostly to foreign direct investment and exports, showing the high level of Philippine dependence on external economic centers like the United States, Japan, the Netherlands, Singapore, and Hong Kong. After the observation of the investment and trade patterns between the Philippines and its three major foreign direct investors, the United States, Japan and the Netherlands, it was determined that

Dependency Theory suffices for explaining the economic exchange patterns between the countries. Whenever economic actors from the United States, Japan or the Netherlands invested less or decided to withdraw revenues from FDI in the Philippines, immediate negative effects were felt in the Philippine economy.

More than fifty percent of the reasons for the deficit in the balance of payments' accounts suffered by the Philippines is a clear example of what Dos Santos described in his work more than forty years ago. The reasons behind deficit in the Capital, Portfolio Investment, and Capital Goods accounts make evident that the Philippines is a country conditioned to develop its economic policy in function to attract production capital and income from economic powerhouses located overseas, in other words, the country is dependent, in Dos Santos' sense of the word. The Philippines Central Bank reports suggest that the country depends on the United States, Japan, and to a lesser but growing degree China. Other important players in Philippine economy are the Netherlands, Singapore, the United Kingdom, Hong Kong, and France.

The remainder of the reasons that caused deficit in the period studied also keep certain level of relationship with Dependency Theory, but to a lesser degree, given the fact that this theory does not explain how periphery-periphery relations occur, with the level of detail it explains center-periphery relations. Therefore, for example in the case of Filipino emigration, Dependency Theory does not suffice for explaining the reasons of emigration to countries such as Malaysia, Kuwait or Saudi Arabia. It is considered that for the satisfactory explanation of the Filipino migration to middle income economies it is necessary to study the phenomenon from the perspective of Dependency Theory and complement it with insights drawn from discussions related to income inequality, chronic political corruption and armed conflict, which may also be reasons for the constant exodus of Filipinos in search for better work and social opportunities in high and middle income countries alike.

Of the seven categories made for classifying the different reasons why deficit happened, only one can be labeled as having no relation whatsoever with issues described by Dependency Theory, the category regarding natural disasters and epidemics. It is considered that although Dependency Theory suffices for explaining a little more than half of the causes of the Philippines' balance of payments accounts' deficit, it needs to be aided by other theories to be able to explain satisfactorily the other half of the causes of deficit observed. In addition to Dependency Theory, future research on Philippine economic issues like trade deficit should also focus on evaluating the effectivity of Philippine governmental policies to encourage the development of local industries to revert trade deficit, especially in the highly specialized services sector, like finance, insurance and logistics.

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