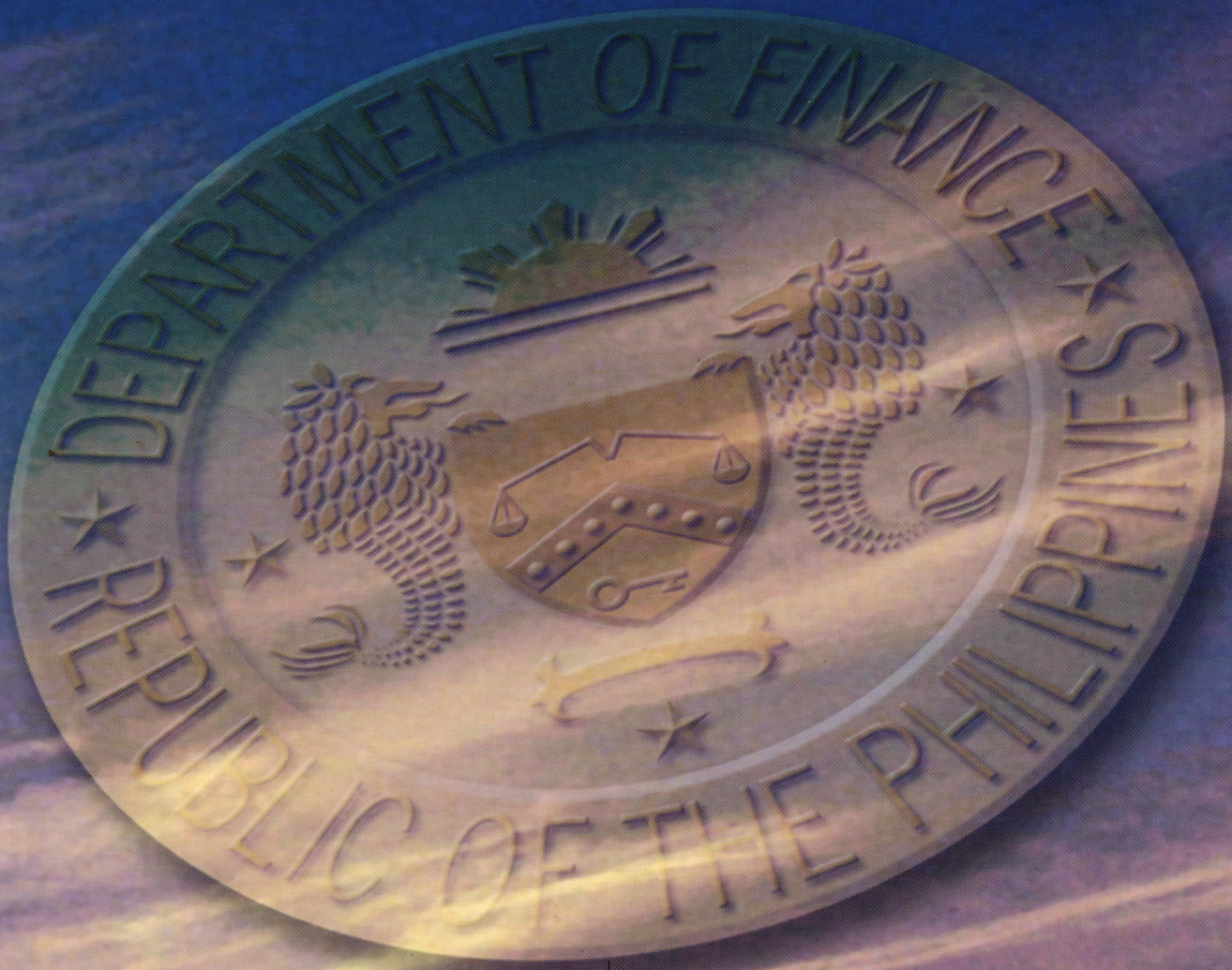

REPUBLIC OF THE PHILIPPINES

DEPARTMENT *of* FINANCE

2001 ANNUAL REPORT

WEATHERING *the* DIFFICULT TIMES

2001 will be remembered as the year when the Philippines once again proved its resiliency in surviving both political and economic turbulence.

The Year began with the impeachment of a president followed within less than a month by another bloodless transition of political power. The changeover, while swift and generally accepted, was not seamless. Ripples of discontent continue to muddy both the political and economic outlook. The country was in need of direction and focus, and for the most part, as stalled reforms once more inched forward, hope began to glimmer once more on the horizon.

For the Department of Finance, the immediate task was clear: the fiscal deficit must be reined. Three years of fiscal slippage has eroded much of the credibility of government, and this had to be reversed to inspire economic confidence.

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DEPARTMENT *of* FINANCE

Under Executive Orders 127, 127-A and 292, the Department of Finance is responsible for the following:

1. Formulation, institutionalization and administration of fiscal policies in coordination with other concerned subdivisions, agencies and instrumentalities of government;

2. Generation and management of the financial resources of government;

3. Supervision of the revenue operations of all local government units;

4. Review, approval and management of all public sector debt, domestic or foreign; and

5. Rationalization, privatization and public accountability of corporations and assets owned, controlled or acquired by the government.

LETTER *to the* PRESIDENT

Her Excellency
President Gloria Macapagal Arroyo
Malacañang, Manila

Dear Madam President:

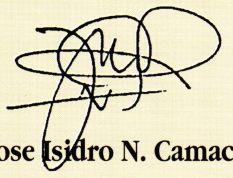
I have the honor to submit the 2001 Annual Report of the Department of Finance and its attached agencies and bureaus.

The report highlights the activities of the Department during the year as it continued to pursue the objectives of fiscal consolidation. These accomplishments were made possible with the strong support of its attached agencies and bureaus.

Furthermore, let me emphasize that the ascencion to power of Your Excellency has inspired us to move ahead with the necessary reforms even as challenges abound and seem difficult to overcome.

As we prepare for the years ahead, rest assured that the entire DOF family is committed to support Your Excellency as we strive to achieve our dream of a better life for all Filipinos.

Very truly yours,



Jose Isidro N. Camacho
Secretary

MESSAGE

from the SECRETARY

The year 2001 was marked by a period of risks and uncertainties. The global economy faltered as the U.S. economy slowed, while Japan remained in the doldrums. With the sharp decline in exports, many export-oriented developing countries posted sluggish economic growth, adversely affecting income and consumption. But amidst harsh external conditions that were compounded by political instability in the domestic front, the Philippine economy managed to post a healthy performance.

The transfer of power in January 2001 bolstered economic recovery as the new economic team wasted no time in pursuing critical economic and structural reforms. Public governance, which was the cause of the downfall of the previous administration, was strengthened with the new administration's strict adherence to the principles of greater transparency and accountability.

Renewed investor confidence and stable financial markets promoted a conducive macroeconomic environment. As a result, the country's Gross Domestic Product posted a 3.4 percent growth, the highest in Southeast Asia during the year and exceeding expectations from the private sector. On the other hand, inflation remained within single-digit level while domestic interest rates continued their downward trend.

In the fiscal sector, the National Government deficit was contained at P147 billion, from an estimated high of P225 billion. This is a remarkable feat, as it was achieved without reining in the budget for priority areas like infrastructure, agricultural modernization, health care and education.

The government continued to maintain a balanced mix of foreign and domestic borrowings. A decline in domestic interest rates during the year prompted the government to borrow about 87 percent of its financing requirements from the local market without being worried about a "crowding out" effect. The balance was financed with external funds in the form of Official Development Assistance (ODA) and sovereign bonds.

Unfavorable market conditions prevented the government from pursuing the scheduled disposition of some big-ticket items, rendering the country's privatization program less significant as a source of additional revenues. Gross revenues from privatization suffered substantial decline to P1.28 billion from P6.89 billion in 2000.

Indeed, financing an expanding economy and a growing demand for public goods poses an enormous challenge. This is why we are relentless in our efforts to improve efficiency in our revenue system through administrative and legislative reforms. At the same time, rationalizing the government's expenditures program becomes necessary. These will be our fiscal thrust over the medium-term.

I commend all the officials and staff of the Department for your unwavering support for our fiscal agenda. As our country continues to compete with the rest of the world, I enjoin everybody to keep on striving for better ideas and support our strong resolve to put our fiscal house in order. Together, let us continue to put the Department on the forefront toward our goal of social and economic development.

Jose Isidro N. Camacho
Secretary

ECONOMIC HIGHLIGHTS

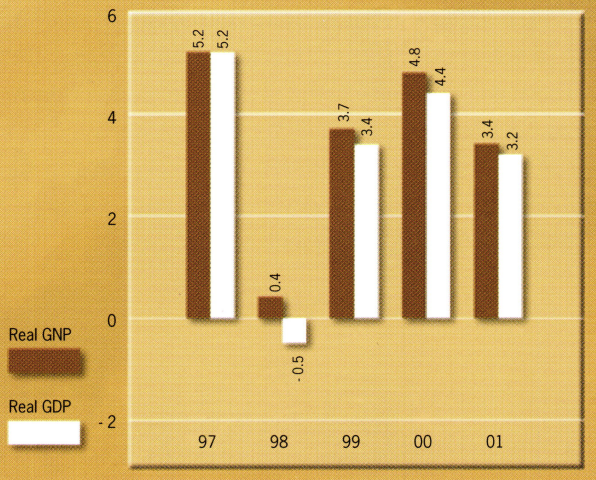
The Philippine economy showed remarkable resiliency in 2001 amid adverse external and internal developments made worse by the September 11 incident. Real Gross Domestic Product and Real Gross National Product expanded by 3.2 percent and 3.4 percent, respectively. The economy's performance was notable for three reasons. First, growth was sustained despite the steep downturn in exports. Second, the growth rate was among the highest in East Asia. Third, the growth rate surpassed the private sector's forecast of 2.5–3.0 percent growth.

The country's sustained growth was mainly anchored on the services sector which rose 4.4 percent on account of the continued expansion of telecommunications (8.8 percent), trade (5.6 percent) and private services (4.4 percent) sub-sectors. Meanwhile, agriculture registered an output gain of 3.7 percent, an acceleration from last year's growth of 3.3 percent due to good weather and the government's continued implementation of agricultural modernization program. The industry sector slowed down to 1.3 percent due to the downturn in manufacturing and utilities sub-sectors.

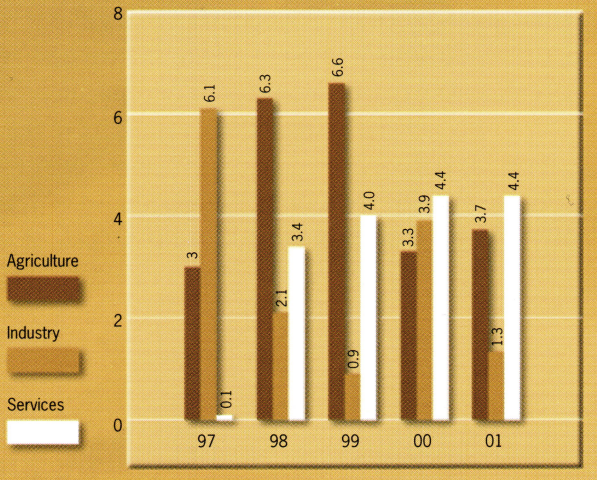
On the demand side, personal consumption expenditure continued to be the main driver of growth, gaining 3.6 percent on the strength of improved rural incomes, as well as higher remittances from Overseas Filipino Workers (OFWs). On the other hand, investment rose 1.3 percent amid cautious investor sentiment. Meanwhile, the recovery of the export sector suffered a reversal as demand fell due to the global economic slump. Net exports in 2001 fell 45.9 percent as electronics exports plunged 24.8 percent.

Prudent fiscal and monetary policy coupled with favorable farm product output helped maintain a manageable inflation rate, averaging 6.1 percent in

Output Growth
(in percent)



Real GDP Growth, By Sector
(in percent)



2001. The uptick from the 4.4 percent average in 2000 reflects mainly the pass-through of world oil prices on domestic petroleum product prices and subsequently on the prices of prime commodities.

With manageable inflation and the decline in international interest rates, domestic interest rates trended downwards from their peak levels despite the May 1 siege and the Argentinian crisis. From 11.8 percent on January 22, 2001, the bellwether 91-day T-Bill rate declined to 8.9 percent on December 17, 2001. The firm resolve of the National Government to keep interest rates low by rejecting high bid rates kept the 91-day T-bill rate stable.

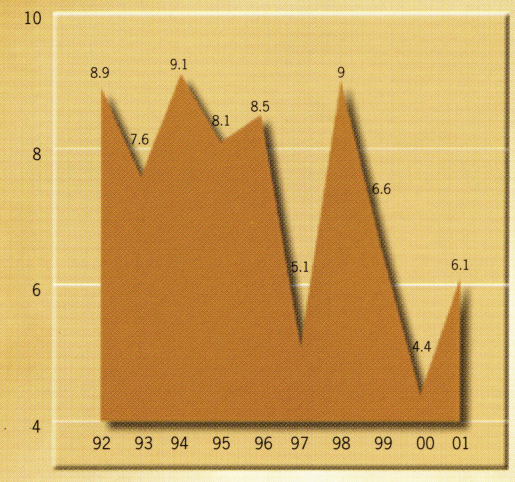
The country's reserve position remained healthy due to higher foreign investments and gold holdings of the Bangko Sentral. Gross international reserves (GIR) was recorded at US$15.7 billion as of end-December 2001, equivalent to 5.0 months of imports of goods and services.

The confluence of negative news pulled down the local stock market with the Philippine Stock Index (PHISIX) tumbling 21.8 percent (yoy) in 2001. The decline however was an improvement over the 30.2 percent fall in stock prices in 2000 – an indication of a more upbeat investor sentiment.

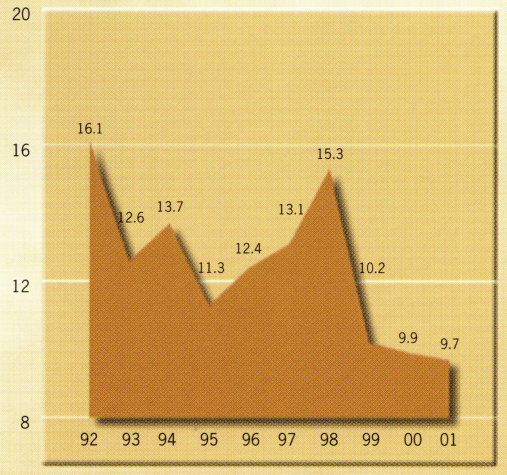
The movement of the exchange rate in 2001 was dictated by turn of events. The peso showed its vulnerability to negative developments, touching its lowest level of P55/US$ on January 18, 2001 at the height of EDSA Dos. The peso quickly rallied to P48-50/US$ from February to May. However, jitters after the widely publicized Abu Sayyaf attacks and the Argentinian crisis battered the peso to almost P54/US$1 in July but appreciated closer to P51/US$ in the last quarter, finally settling at an average of P50.99/US$1 in 2001.

The financial system remained generally sound with its total resources rising to P4.09 trillion, from the previous year's level of P4.06 trillion. The resources of the commercial banking system rose by 1.9 percent in 2001 while that of thrift banks expanded by 1.2 percent. The commercial banking system remained healthy with capital adequacy ratio improving to 16.0 percent (as of end-December 2001), higher than the 8.0 percent Basle standard and the 10.0 percent domestic requirement. The rising non-

Average Inflation Rate
(in percent)



91-Day Treasury Bill Rate
(in percent)



performing loans (NPLs) of banking institutions proved to be a cause of concern as it rose 17.4 percent in 2001 from 14.9 percent in 2000.

FISCAL MANAGEMENT

NG Deficit

The fiscal deficit in 2001 stood at P147.0 billion which is equivalent to 4.0 percent of GDP. This figure was slightly above the P145.0 billion programmed for the year, but it is a substantial improvement over the P225 billion estimated deficit for 2001 had there been no change in leadership.

The taming of the deficit was made possible through revenue enhancement reforms and prudent spending program and without scrimping on the budget for priority expenditures like infrastructure, agricultural modernization and social services.

2001 Deficit

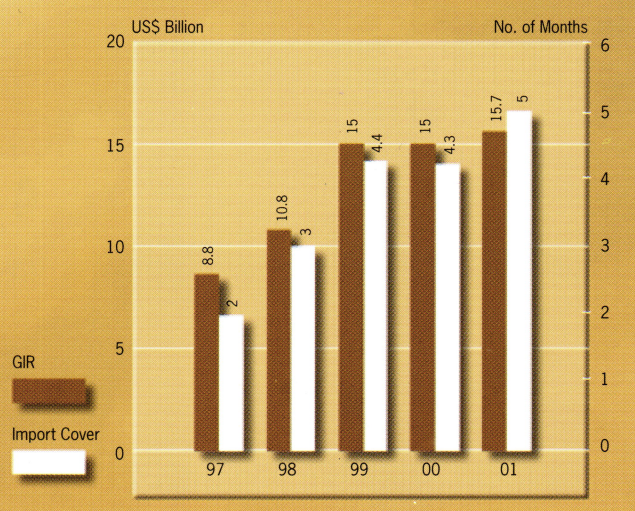
	2001			
2000	**Potential**	**Target**	**Actual**	**Deviation**
P134.2 B	**P225.0 B**	**P145.0 B**	**P147.0 B**	**Just 1.4% Above Program**

Total revenue collection reached P563.7 billion, exceeding the program by P5.5 billion. BIR and BOC account for the bulk of the collection although their collection performance was dampened by the economic slowdown. BIR exceeded its target by P0.6 billion but BOC suffered a drastic collection shortfall of P8.9 billion vis-à-vis the program. The shortfall though was offset by robust investment income posted by the Bureau of the Treasury and higher collection of fees and charges, exceeding the targets by P21.5 billion and P1.1 billion, respectively.

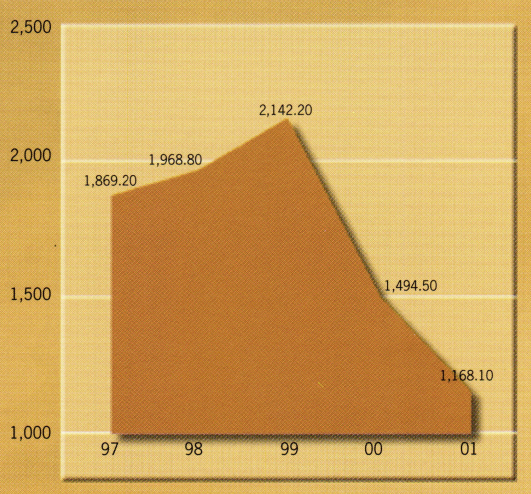
2001 Revenues

	2001		
2000	**Target**	**Actual**	**Deviation**
P514.8 B	**P558.2 B**	**P563.7 B**	**1.0% Ahead of Program**

Gross International Reserves
1997 - 2001



Stock Market Index
1997 - 2001



On the expenditure side, overall spending was restrained at P710.7 billion or 19.5 percent of GDP, which is 1.1 percent more than the full year target. The bulk of public spending went to local government units (LGUs) to accelerate the rural development thrust of the government. LGUs' allotment share during the year reached P118.2 billion compared with P99.8 billion the previous year. This partly explained the higher level of actual expenditures for 2001. Expenditures would have gone higher were it not for the fiscal discipline measures implemented early on during the year. These measures included the issuance by the President of Administrative Order No. 5 (fiscal discipline measures across all agencies), deferment of salary adjustments, lower interest payments, and reduction of subsidies and transfers to government owned and controlled corporations (GOCCs).

2001 Expenditure

	2001		
2000	**Target**	**Actual**	**Deviation**
P649.0 B	**P703.2 B**	**P710.7 B**	**1.1% more than the program**

Consolidated Public Sector Financial Position

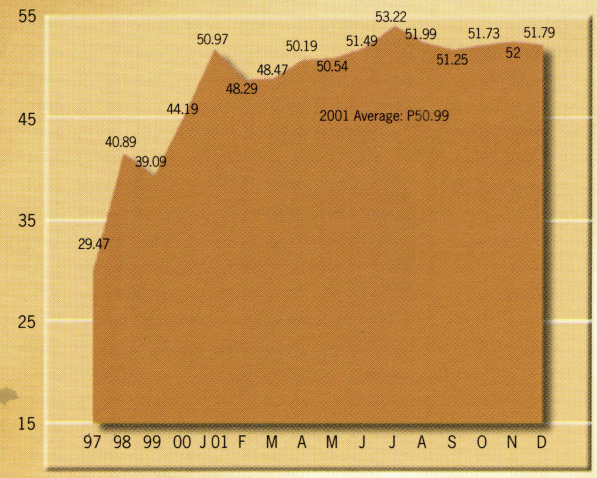
In 2001, the overall deficit of the consolidated public sector was recorded at P147.6 billion, equivalent to 4.1 percent of GDP. Although the deficit grew 2.7 percent over last year's level, it is lower than the programmed level of P166.5 billion or 4.6 percent of GDP.

2001 Consolidated Public Sector Financial Position (In Billion Pesos)

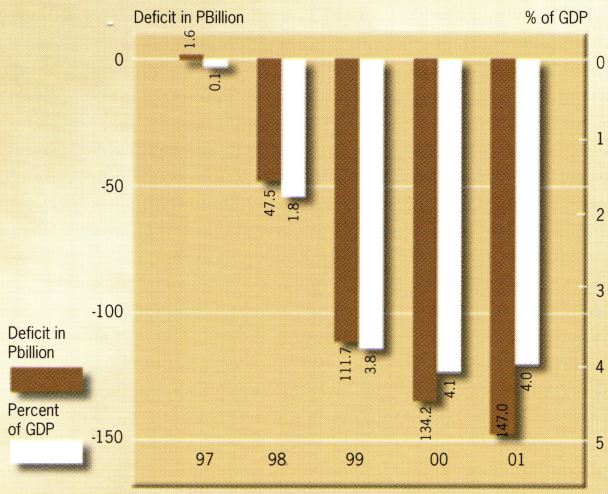
	2000 Actual	2001 Program	2001 Actual
National Government	(134.2)	(145.0)	(147.9)
CB Restructuring	(19.1)	(27.1)	(23.5)
14 Monitored Gov't. Corporations	(19.2)	(23.0)	(21.7)
Oil Price Stabilization Fund	0.3	0.0	0.8
Adjustment of Net Lending and Equity to GOCCs	4.2	4.0	4.4
Other Adjustments*	(6.6)	0.0	0.0
Social Security Institutions	15.5	10.5	15.6
Bangko Sentral ng Pilipinas	0.2	5.0	15.0**
Government Financial Institutions	2.8	4.8	4.8
Local Government Units	3.8	4.2	4.2
Timing Adjustment of Interest Payments to BSP	0.5	0.2	(0.2)
Other Adjustments	0.1	0.0	0.1
TOTAL	**(151.7)**	**(166.5)**	**(147.6)**

** Capital expenditures for the San Roque Multipurpose project and BSP dividends*
*** January to November actual only*

Average Peso/US$ Rate
1997 - 2001



Fiscal Deficit
1997 - 2001



The deficit was a result of the negative fiscal position of the National Government (P147.0 b), Central Bank Restructuring (P23.5 b) and Monitored Government Corporations (P21.7 b). However, the surpluses posted by the other public sector helped reduce the actual deficit for the year. Social Security Institutions which include the Social Security System (SSS), the GSIS and the PHIC, registered a substantial aggregate surplus of P15.6 billion or P5.1 billion above the program while the Bangko Sentral ng Pilipinas recorded a net income of P15.0 billion which was P10.0 billion above the target. Both GFIs and LGUs also managed to meet their targets for the year, registering surpluses of P4.8 billion and P4.2 billion, respectively.

RESOURCE MOBILIZATION

The government's favorable revenue performance in 2001 has enhanced its ability to mobilize greater resources to the different sectors, thereby contributing to a higher level of output and sustaining economic growth.

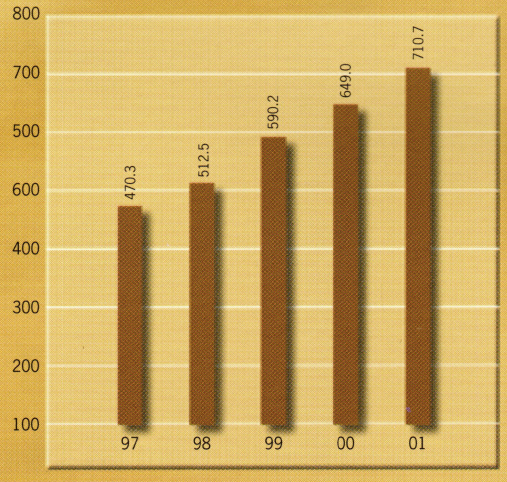
Revenue Generation

In 2001, the government recorded a revenue inflow of P563.7 billion, which is 9.5 percent higher than the 2000 level of P514.8 billion and above the program by P5.5 billion. Tax revenues accounted for P489.9 billion or 87.8 percent while non-tax revenues contributed P73.9 billion or 12.2 percent. The sustained growth in collections reflects the continuing recovery of the economy and the improving collection efforts arising from the implementation of reforms in tax administration.

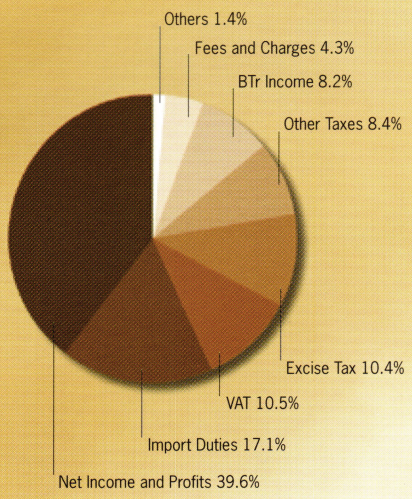
The BIR accounted for the bulk of the total tax collection of P489.9 billion, contributing P388.7 billion or 79.3 percent. BOC and Other Offices fetched P96.2 billion and P4.9 billion, respectively. BIR exceeded its target for the year by P0.6 billion but BOC recorded an underperformance of P8.9 billion relative to its target due largely to the slowdown in imports and the higher share of non-dutiable imports.

On the other hand, the bulk of non-tax revenues stemmed from BTr income which accounted for P46.4 billion or a share of 62.7 percent. Collections

Expenditures
(in Billion Pesos)



2001 Revenue Collections
(By Percentage Share)



from fees and charges reached P24.3 billion, reflecting a 32.9 percent share and a 35.5 percent increase over last year's level of P17.9 billion. Meanwhile, receipts from privatization dropped to P1.2 billion from the previous year's level of P4.6 billion as unfavorable market conditions delayed the privatization of some big-ticket items.

2001 NG Cash Budget Performance (in billion pesos)

	2000 Actual	2001 Program	2001 Actual	Difference vs. Program
Revenues	514.8	558.2	563.7	5.5
BIR	360.8	388.1	388.7	0.6
BOC	95.1	105.1	96.2	0.9
Other Offices	28.2	40.2	32.4	7.6
o.w. Fees and Other Charges	17.9	23.2	24.3	1.1
Privatization	4.6	10.0	1.2	(8.8)

By type of tax, collections from net income and profits accounted for the largest share (40 percent), followed by import duties (17.1 percent), value added taxes (10.5 percent) and excise taxes (10.4 percent).

BORROWINGS

The government's borrowing program in 2001 was intended primarily to finance the deficit, service maturing debt obligations and build up the cash reserves of the Bureau of the Treasury.

On a net basis, the government raised P175.2 billion in borrowings of which P152.3 billion was sourced domestically while P22.9 billion came from foreign sources. The resulting financing mix was 87:13 in favor of domestic borrowings. The heavy reliance on domestic borrowings, mostly on long-term instruments, was triggered by declining domestic interest rates and the supportive monetary stance of the Bangko Sentral.

2001 NG Financing

Particulars	2000	2001		
		Target	Actual	Deviation (%)
Net Domestic Financing	99.9	163.3	152.3	-6.8
Net Foreign Financing	103.9	10.4	22.9	120.2
Net Borrowings	203.8	173.8	175.2	0.8
Deficit Financing	134.2	145.0	147.0	1.1
Change in Cash	69.6	28.8	28.2	-2.1

The DOF likewise continued to access financing from official development assistance (ODA) being the cheapest source of foreign funds and having long maturity features, concessional interest rates and grant element. ODAs likewise play a key role in the government's development objectives as they are generally geared towards programs to alleviate poverty.

The DOF also took advantage of the low interest rate regime and favorable market sentiment on Philippine sovereign debt, which paved the way for the issuance of sovereign bonds and notes. One of the issuances, the HSBC $220 million swap, was voted as the "Most Innovative Debt Deal" by Finance Asia and "Best Synthetic Bond Deal" by the Asset.

2001 NG Borrowing Program

Particulars	Amount
DOMESTIC	
Treasury Bills	P 58.0 B
Fixed Rate Bond Swap	P 11.8 B
Zero Coupon Bonds	P 35.0 B
Long Term Bonds and Notes	P 83.5 B
1 Year Landbank Bonds	P 9.3 B
US$ Linked Peso Notes	P 30.0 B
Citicorp FCDU Placement	US$ 125.0 M
FOREIGN (Commercial)	
CSFB	US$ 200.0 M
JP Morgan	US$ 100.0 M
HSBC	US$ 220.0 M

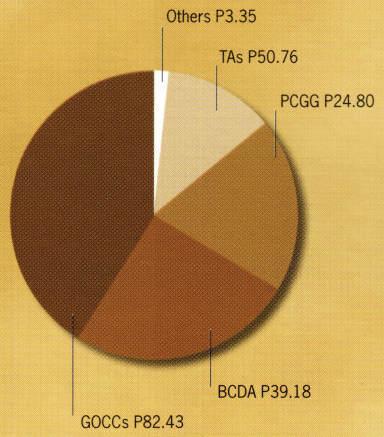
Privatization

Unfavorable market conditions dampened government's privatization efforts and delayed the sale of some big ticket items scheduled for disposal during the year. As a result, gross revenues from privatization declined considerably to P1.28 billion, from P6.89 billion a year ago. Of this amount, P1.17 billion was remitted to the National Treasury, broken down as follows: P0.52 billion from Privatization and Management Office (PMO), P0.51 billion from Presidential Commission on Good Government (PCGG) and P0.14 billion from Bases Conversion Development Authority (BCDA).

Since 1987, the privatization program has resulted in the disposal of 486 assets/corporations, generating gross revenues of P200.52 billion, of which P126.33 billion was remitted to the Bureau of the Treasury.

Privatization
1987 - 2001

P200.52 Billion Gross Sales



Accounts Disposed	
TAs	359
GOCCs	109
PCGG	16
BCDA	1
Others	1

TAX REFORMS

In 2001, the DOF continued to pursue much needed tax reforms, focusing on tax administration. The BIR implemented a more intensified conduct of audits, the use of metering machines for documentary stamp taxes, an improved withholding tax system using the tax remittance advice system, a strict monitoring of LGU remittances and a more enhanced compromise settlement program.

At the BOC, duty collections were enhanced through the following measures: auction sales of forfeited cargoes; settlement and redemption of seized cargoes; liquidation of forfeited bonds by bonded manufacturing warehouses; penalties from erring brokers, banks and importers; and additional billings from post liquidation of import entries.

Bureau Of Internal Revenue

- Intensified Conduct of Audits
- Voluntary Assessment Program
- Documentary Stamp Tax Metering System
- Improved Withholding Tax System
- Compromise Settlement Program
- Strict Monitoring of Local Government Units

Bureau Of Customs

- Proceeds from Auction Sales of Forfeited Cargoes
- Penalties from Erring Brokers, Banks and Importers
- Liquidation of Forfeited Bonds by Bonded Manufacturing Warehouses
- Settlement and Redemption of Seized Cargoes
- Additional Billings from Post Liquidation of Import Entries.

DEBT MANAGEMENT

The National Government debt outstanding (net of relent, guaranteed and contingent debt) expanded by 10.1 percent in 2001 to P2.38 trillion, from P2.17 trillion in 2000. The increment was attributed to the depreciation of the peso and higher borrowings to finance the budget deficit and service maturing obligations.

Domestic liabilities, which account for 52.3 percent of the total debt, rose by 16.8 percent to P1.24 trillion as against last year's level of P1.07 trillion. On the other hand, foreign debt which constitutes 47.7 percent rose by 3.5 percent to P1.14 trillion, from P1.09 trillion recorded a year ago.

Our debt service relative to exports and GDP stood at 12.6 percent and 7.1 percent, respectively. Although these ratios showed increasing trends, they were still lower than the debt service ratios in the early 1990s.

In line with its debt management program, the government managed to improve the country's debt maturity profile with the share of medium and long term debt improving to 82 percent compared with 78 percent last year.

GOVERNMENT CORPORATE SECTOR

In 2001, the National Government continued to pursue various fiscal reforms to enhance financial discipline and better resource management among government-owned and controlled corporations (GOCCs).

GOCC Fiscal Operations

The combined net financing deficit of 14 major non-financial GOCCs, the government financial institutions (GFIs) and the social security institutions (SSIs) amounted to P1.3 billion as against P0.9 billion in 2000.

The GFIs' full year surplus of P4.8 billion, which is a substantial 190 percent higher over the previous year's level of P2.8 billion, helped curb the combined deficit of the government corporate sector. The sector's growth was attributed largely to higher earnings on bonds and securities and the postponement of low priority capital expenditures in compliance with cost cutting measures under Administrative Order No. 5 issued by President Arroyo.

Meanwhile, the adoption of cost cutting measures also helped SSIs maintain a surplus of P15.6 billion, close to the 2000 surplus level of P15.5 billion.

However, the gains from GFIs and SSIs were overshadowed by the negative fiscal position of the 14 GOCCs which stood at P21.7 billion. Efforts made by the National Power Corporation to accelerate implementation of various power projects and the suspension of the concession fee payments by the Maynilad Water Corporation to the MWSS pending the resolution of the proper handling of its foreign exchange losses accounted for the higher deficit of the GOCCs.

Government Corporate Sector Fiscal Position (in Billion Pesos)

	2000 Actual	2001 Actual
GOCCs	(19.2)	(21.7)
GFIs	2.8	4.8
SSIs	15.5	15.6

Guarantees, Net Lending and Subsidy

In support of the priority programs of the government, the DOF endorsed the provision of guarantees for several loans with high positive economic impact. The guarantees, which amounted to P766.9 billion, included the P747.5 billion intended for power-related projects and P0.94 billion for relending facilities of the government financial institutions.

Net Lending support was likewise extended to GOCCs for debt servicing of their obligations. Total net lending support amounted to P3.94 billion. The major recipients were NPC, P2.17 billion; NEA, P1.06 billion; and PNR, P0.53 billion.

A total of P0.12 billion in subsidy was endorsed by Fiscal Incentives and Review Board. The recipients were: National Kidney Transplant Institute (NKTI), P9.5 million; Philippine Health Insurance Corporation (PHIC), P10.9 million; Light Rail Transit Authority (LRTA), P5.0 million; and National Food Authority (NFA), P90.0 million.

A mangrove reforestation site in Region 7, one of the environmentally sustainable projects being undertaken by local governments supported by the MDFO's CBRM Program.

MUNICIPAL DEVELOPMENT FUND OFFICE

The Department of Finance, through the Municipal Development Fund Office (MDFO), continued to mobilize resources from Official Development Assistance (ODA) by providing loans and grants to various development projects of Local Government Units (LGUs). Projects eligible for technical assistance include the following:

- expansion and upgrading of municipal and urban infrastructure and services;
- strengthening of capabilities in municipal investment and development planning, revenue administration and project preparation;
- strengthening of capabilities to implement natural resource management (NRM) projects.

Total disbursements for the year amounted to US$3.5 billion as against the previous year of US$1.47 billion, reflecting a significant improvement in the disbursement of funds.

Total fund releases grew 16.7 percent to P2.8 billion in 2001 from P2.4 billion in 2000. On the other hand, the total withdrawal applications processed

soared 150 percent to P1.1 billion in 2001 from the previous year's level of P0.755 billion. Meanwhile, the total number of Certificate of Availability of Funds (CAF) processed and approved doubled to 1,252 in 2001 from 680 in 2000.

Apart from being the administrator and cashier of MDFO-administered projects, the MDFO is also tasked to strengthen itself as a development agency through the institutionalization of technical and financial capability within its operations. This is being done through the Community Based Resource Management Project (CBRMP) and the Local Government Finance and Development Project (LOGOFIND) being implemented and operationalized by the MDFO.

Under the LOGOFIND, 36 feasibility studies have been completed and appraised as of end-December 2001. Seventeen of these studies, amounting to P270 million, were approved by the MDFO Technical Review Committee (TRC) and the MDFO Policy Governing Board (PGB). In support of these studies or subprojects, training and capacity building were conducted on sub-project development which included FS Preparation Program, Orientation Conference, Procurement, Detailed Implementation Plan, Financial Plan Preparation and Logical Framework Formulation. Meanwhile, support mechanisms were continually prepared to ensure the successful implementation of the LGU Resource Mobilization and Performance Monitoring component, which include the adoption and conduct of seminar/workshop on the revised format for LGU fiscal monitoring system, the incorporation of the monitoring system to the Manual of Operations for Treasurers and the development of an on-line information system.

The CBRMP likewise gained substantial success in 2001 as a total of 90 subprojects amounting to P1.49 billion were approved and implemented in 90 LGUs compared with the target of 70. With respect to physical accomplishments, the participating CBRMP LGUs were able to undertake the following:

- establishment of 156 central and satellite nurseries;
- survey and mapping of 16,795 hectares of upland areas;
- planting of 12,470 hectares of upland areas;
- survey and delineation of 3,463 hectares of coastal areas;
- protection and management of 2,584 hectares of coastal areas;
- delineation and survey of 1,914 hectares of mangrove areas;
- planting and rehabilitation of 1,813 hectares of mangrove areas;

The LOGOFIND Project under the MDFO extends assistance in the building of a public market in Siquijor.

- construction and rehabilitation of 107 kilometers of farm-to-market roads;
- establishment of 49 water system level 1 and 2;
- grading of 5-kilometer trail/footpath; and
- construction of 2 units of institutional/post harvest facilities.

The CBRMP also readily extended technical assistance to various natural resource and environmental management programs through its partner agencies like the Department of Environment and Natural Resources (DENR), the Department of Agriculture (DA), Bureau of Forestry and Aquatic Refources (BFAR) and the Local Government Academy (LGA).

NATIONAL CREDIT COUNCIL

The National Credit Council's (NCC) efforts during the year were geared mainly towards the continued implementation of Executive Order 138 which provides for the adoption of market-oriented credit policies, as well as the rationalization of directed credit programs (DCPs).

The NCC completed the draft rules on the proper handling and administration of funds for the phase-out or transfer of government directed credit programs (DCPs) from Government Non-Financial Agencies (GNFAs) to Government Financial Institutions (GFIs). Once implemented, the said rules are expected to hasten the transfer of DCPs to GFIs.

In line with the implementation of EO 138, the NCC, through the Executive Committee, likewise approved a Pro-forma Memorandum of Agreement (MOA) that spells out the arrangement between the GNFAs and the GFIs on the transfer of DCP funds. Moreover, the NCC conducted a workshop with COA Auditors to assess the progress of the audit of DCPs and to resolve issues related to the conduct of audit.

The NCC also spearheaded the formulation of Performance Standards for Credit Cooperatives in consultation with various stakeholders. This set of standards is aimed at strengthening the credit cooperatives based on internationally accepted standards. It is expected that through these standards, credit cooperatives will be able to provide quality and sustainable financial services to its members and support the government policy of increasing private sector participation in the delivery of financial services to the basic sector.

The year also saw the NCC initiating efforts to formulate an appropriate regulatory framework for microfinance in line with President Gloria Macapagal Arroyo's pronouncement in her SONA to "make microfinance a cornerstone to fight poverty." The framework is envisioned to shield the financial

DOF Assistant Secretary and NCC Executive Director Gil S. Beltran discusses the advantages of putting in place the Performance Standards for credit cooperatives.

system from unsound practices by deposit-taking institutions, protect small and unsophisticated clients and promote the establishment of accurate, reliable and transparent set of financial information for all types of microfinance institutions. In this regard, a sub-committee under the NCC Executive Committee was created to draft the framework.

Pursuant to EO 138, the NCC continued to perform its role of evaluating proposed foreign loans and project proposals with credit component referred by Technical Committee of the NEDA Investment Coordinating Committee (ICC). These project proposals require NCC endorsement before they could be approved by ICC Cabinet Committee. For 2001, the NCC reviewed and endorsed five (5) project proposals to the ICC for consideration and approval.

The NCC likewise focused on technical and advocacy work which included the following:

- Conduct of regional symposium on the operating guidelines of the Agro-Modernization Credit and Financing Program (AMCFP) in coordination with the Agricultural Credit Policy Council;

- Briefings with various government and non-government agencies on government policies on credit per EO 138;

- Provision of technical assistance in the drafting of the Implementing Rules and Regulations (IRR) of the People's Development Trust Fund (PDTF); and

- Provision of technical assistance to the Bangko Sentral ng Pilipinas (BSP) in drafting pertinent circulars for the regulation of microfinance.

Visit by the NCC Executive Committee members led by Undersecretary Juanita D. Amatong to a model cooperative in Davao under the Credit Union Empowerment & Strenghtening (CUES) Project of the USAID.

INTERNATIONAL COOPERATION

In 2001, the DOF continued to be a key and active player in world affairs and in various economic fora, spearheading many initiatives undertaken by ASEAN and APEC.

Enhanced Ties with Sovereign Investors

In 2001, the government instituted measures to enhance its relations with foreign investors. An Investor Relations Office was set up at the Bangko Sentral in mid-July 2001 with a coordinating role for all economic agencies. For its part, the DOF undertook roadshows that covered all major financial markets, including regular briefings and teleconferences with investors and rating agencies.

This successful investor communications program did not only enhance the attractiveness of Philippine sovereign debt but also showcase the

Philippines as a safe haven for foreign investments. The country also successfully contained bond market reaction to the September 11 incident and the Argentine debt default, performing within the expected range in reference to its emerging market peers.

Appreciation ceremony for the First U.S. Dollar T-Bill issuance by the Republic of the Philippines.

The DOF's commitment to fiscal consolidation and the strong performance of the economy enabled the country to gain upgrades in its sovereign ratings. Moody's and Standard and Poors upgraded the country's rating outlook from negative to stable while London-based international ratings agency Fitch maintained a stable outlook on the country's sovereign ratings. These pronouncements served as a strong acknowledgment by the international community that the Philippines is back on a sustained path to recovery.

ASEAN

- Following their agreement during the Special ASEAN Finance Ministers Meeting, the ASEAN Finance Ministers tasked the Philippines to be the main counterpart of the ASEAN and ADB for the setting up of a surveillance unit which will monitor economic and financial indicators in ASEAN. Integral to the establishment of a surveillance unit is the formulation of an "early warning system model" which has been put in place, along with an accurate and reliable financial and economic database. The model serves as a warning device for ASEAN economies to adopt appropriate policy response to avert financial and economic crisis.

- The DOF, along with the Bangko Sentral, took the lead in the technical negotiations of the RP-Japan Bilateral Swap Agreement. The negotiations resulted in a US$3 billion RP-Japan BSA that was signed during President Arroyo's state visit in Japan last September 2001.

APEC

- As coordinator in the APEC initiative on Credit Rating Agencies, the DOF coordinated the research study on the review of practices, assessment, strengths and weaknesses in the methodology of international rating agencies. Accordingly, the DOF prepared the initial draft on the Terms of Reference for the consultants. The recommendations in the research study were recognized and accepted by APEC member-countries as an important policy move towards greater transparency.

Multilateral Institutions

- The government maintained the value of the Republic's subscription in the following multilateral financial institutions:
  (a) payment of P11.4 million for the maintenance of value (MOV) of Philippine subscription to the International Bank for Reconstruction and Development (IBRD);
  (b) partial settlement of obligation to International Fund for Agricultural Development (IFAD);
  (c) partial payment of US$ 109,430.75 to the Asian Development Bank (ADB) 4th General Capital Increase; and the encashment of P15.9 million for the Article 6.2(b) notes to ADB.

FRONTLINE OPERATIONS

Revenue Operations Group

The Revenue Operations Group (ROG), which is tasked to evaluate, process and monitor applications for tax and duty exemption, granted a total of P 6.6 billion in tax and duty exemptions in 2001. This is 8.3 percent less than last year's level of P7.2 billion. The decline is attributed to lower tax and duty exemptions granted to the National Power Corporation and the telecommunications companies. A total of 8,764 applications for exemptions were filed, of which 108 were denied and 82 put under seizure/protest cases.

By division, the Internal Revenue Division granted a total exemption of P3.2 billion while the Revenue Express Lane and Customs and Tariff Division waived P2.3 billion and P1.1 billion, respectively. In terms of applicant, the top 5 applicants accounted for P4.1 billion or 62 percent of the total exemptions during the year. These include the Philippine Veterans Development Industries Corporation (PHIVIDEC) with P1.1 billion, followed by NAPOCOR with P743.9 million, DA/NFA with P523 million, importation under Section 105 of the Tariff and Customs Code with P693 million and telecommunications companies with P1.1 billion.

Taxes and Duties Waived on Importations For the Year 2001

No. of Applications Filed		Duties & Taxes Waived (in Billion Pesos)	
2000	2001	2000	2001
12,629	**8,764**	**7.2**	**6.6**

The ROG: responding to the needs of exporters.

The OSS receiving counter for tax and duty exemption applications.

One Stop Shop Tax Inter-Agency Tax Credit and Duty Drawback Center

The year 2001 was another milestone for the One-Stop Shop Inter-Agency Tax Credit and Duty Drawback Center (OSS-CENTER) as it successfully instituted significant reforms in the administration of tax credit and duty drawback system, namely, the Zero Backlog Program, the Advance Tax Credit Program for Export Winners, the Electronic Information Exchange and the On-Line Verification Project with BOC.

The Zero Backlog Program intends to resolve all pending tax credit claims (TCCs) under the Investment Incentive Group (IIG) of the CENTER. A similar program is also being contemplated for the Duty Drawback Group (DDG) and Tax and Revenue Group (TRG). The implementation of the Program reduced the processing time of TCCs under IIG, DDG and TRG to 30, 60 and 120 days, respectively.

The Advance Tax Credit Scheme for Export Winners is in support of the country's export sector which is a key economic growth driver. The Scheme, which has been made exclusive initially to the Semiconductor and Electronics Industry of the Philippines, established more responsive systems and processes to address the huge backlog of pending VAT credit claims under the TRG. The Memorandum of Agreement and the Supplementary Agreement were formally entered into between the DOF-CENTER and the BIR on October 23, 2001 and December 6, 2001, respectively.

The Electronic Information Exchange established a formal electronic link up between the CENTER and the BIR. The program would not only ensure expeditious processing of tax credit and duty drawback applications of exporters but also prevent any undue tax credit claims. The electronic linkage is

The OSS releasing counter: a new physical layout for greater transparency and flexibility.

regarded as a major innovation as it empowers the CENTER to validate the authenticity of suppliers' invoices through the matching of records with the BIR as well as prevent double availment of claims.

The On-line Verification Program with the BOC allows the CENTER to check and confirm online import transactions and documents presented by claimants to support their tax credit and duty drawback claims. A major advantage of the link up is the reduction in the waiting time for confirmation results.

HUMAN RESOURCE DEVELOPMENT

As a continuing resolve to maintain quality, result-oriented and globally competitive workforce, staff development program in the Department was further strengthened. Scholarship and training guidelines were regularly updated for better application and transparency. Relative to this, a Training Needs Analysis was conducted through a survey questionnaire to determine the training needs of the various groups in the Department, the result of which served as reference in the programming of training priorities.

Qualified personnel continued to avail of foreign and local study grants, such as those sponsored by New Zealand Official Development Assistance (NZODA) Programme, Joint Japan/World Bank Graduate Scholarship Programme (JJ/WBGSP) and the Civil Service Commission – Local Scholarship Program.

During the year, the DOF-Performance Evaluation System was finally pilot-tested to staff of Central Administration Office and Central Financial Management Office, where various divisions came out with their respective Work Programs.

IMF-STI Course on Macroeconomic Management and Financial Sector Issues attended by Ms. Frances Grace B. Belen (1st from right, 2nd row) on November 5-16, 2001 in Singapore.

Meanwhile, new personnel policies were formulated in compliance with CSC-MC Nos. 01, 02 and 03, series of 2001. These include the Program on Awards and Incentives for Service Excellence (PRAISE), Revised Policies on the Settlement of Grievance in the Public Sector and Revised Policies on Merit Promotion Plan.

For improved governance, selected technical personnel were sent to governance-related courses, and various taxation and technical courses to further equip them with technical know-how and capabilities. On the other hand, personnel from the Administration group were sent to training programs dealing on personnel, administrative and financial management.

In response to the needs of the integrees from the deactivated Economic Intelligence and Investigation Bureau (EIIB), a Refresher Course was conducted specially for them.

The Department joined the celebration of the Philippine Civil Service in an austere yet meaningful manner by holding activities that include flag raising ceremony, mass, physical fitness activity, trivia quiz and recognition day for deserving employees.

It was also during the year that the DOF-Gender and Development (GAD) Focal Points Group was reconstituted, consisting of representatives from the different groups of the Department, its bureaus and attached agencies. The reconstitution of DOF-GAD Focal Points resulted in a strengthened enabling mechanism and more concerted GAD efforts among agencies.

OUTLOOK AND FUTURE AGENDA

Prospects for 2002 and Beyond

The Philippine economy's growth momentum is steadily gathering pace with vastly improved external environment and domestic situation. With a better outlook for the future, real GDP is expected to accelerate to 4.5 percent as exports and investments are expected to rebound following the recovery in our major export markets. Exports will grow by around 1.4 - 1.9 percent. Investments will expand by 3.6 percent. By sector, services will continue to pace economic recovery with 5.0 - 5.5 percent growth, while industry will follow with a 3.3 - 4.3 percent expansion. Agriculture will grow 2.7 percent to 3.6 percent amidst the threat of El Nino. Construction and finance will stage a modest rebound, while manufacturing and utilities will post better performance.

Inflation will drop further to a range of 4.5 - 5.5 percent with favorable farm output and prudent monetary stance. Interest rates for the 91-day Treasury Bills will be tempered to around 10.0 percent as the fiscal deficit is expected to be reduced to P130 billion or 3.4 percent of GDP.

Over the medium-term, it is expected that the economy will grow by 5.0 - 6.0 percent with inflation dropping to about 4.5 - 5.0 percent and interest rates stabilizing at 9.0 - 10.0 percent. On the other hand, exports will grow between 9.0 - 10.0 percent. Sustainable growth and macroeconomic stability will be attained through prudent fiscal and monetary management, the continued implementation of structural reforms and improved governance.

2002 Macroeconomic Forecasts		
Gross Domestic Product	–	4.5%
Gross National Product	–	5.0%
Inflation Rate	–	4.5%
Interest Rate	–	10.0%
Forex Rate	–	P52.00:US$1.00
Export Growth Rate	–	1.9%
Import Growth Rate	–	2.4%

Administrative and Legislative Reforms

The government will continue to pursue various policy and institutional reforms in order to maintain macroeconomic stability and sustain the country's recovery efforts. In the fiscal sector, fiscal risks remain, such as the low revenue and tax efforts and the rising contingent liabilities arising from government guarantees. Unless these are appropriately and adequately addressed, the government's fiscal consolidation efforts would be under serious threat.

Thus, over the medium-term, the DOF is committed to pursue fiscal consolidation. This will be undertaken through revenue enhancement, expenditure rationalization and fiscal risk management.

2002 Fiscal Agenda

FISCAL CONSOLIDATION

through:

Revenue Enhancement

Expenditure Rationalization

Fiscal Risk Management

Revenue effort will be enhanced through tax administration and tax structure reforms. The fundamental tax administration reforms include the full computerization of the BIR and BOC, expanding the Large Taxpayers Unit, industry benchmarking and improving the VAT and excise tax yield. Tax structure reforms currently in the pipeline include the indexation of excise taxes on sin products, excise taxes on automobiles, rationalization of fiscal incentives, rationalization of documentary stamp taxes, and the Modified Gross Income Tax Scheme.

2002 Reform Agenda

Tax Administration Reforms

- Full Computerization of the BIR and the BOC
- Expanding the Large Taxpayers Unit
- Industry Benchmarking
- Improving the Value Added Tax and Excise Tax Yield

Tax Structure Reforms

- Indexation of Excise Taxes on Sin Products
- Excise Taxes on Automobiles
- Rationalization of Fiscal Incentives
- Rationalization of Documentary Stamp Taxes
- Modified Gross Income Tax Scheme

On the expenditure side, the DOF will support the DBM's initiative on the Medium-Term Expenditure Framework (MTEF) that has been formulated to serve as the basis in implementing an effective medium-term expenditure program. The MTEF is a multi-year budgeting process that is linked to the medium term revenue program. The MTEF will be complemented by measures to increase transparency, accountability and predictability in budgeting such as the Sector Effectiveness and Efficiency Review (SEER) and the Organizational Performance Indicator Framework (OPIF).

On fiscal risk management, the DOF is currently reviewing its policy on contingent liabilities. It is developing a system that will provide criteria for

approval, rigid screening process, guarantee limits and budget provisioning. It has likewise begun work on the need to reduce risk arising from unfunded or underfunded pension liabilities.

The DOF will strive to further deepen the capital markets. Currently, the development of the capital markets has been hampered by weak regulatory regimes, institutional weaknesses and lack of competition. Thus, we have proposed to Congress various measures that would promote greater financial transparency, accounting and auditing standards, improved corporate governance, shareholder protection and creditor rights. These measures include the following:

- **Securitization Bill** – this bill seeks to establish the tax, legal and regulatory framework for securitization and create a favorable environment for a wide range of asset-backed securities.

- **Special Purpose Asset Vehicle (SPAV) Bill** – this bill seeks to encourage private sector investment in non-performing loans (NPLs) and real and other properties owned and acquired assets (ROPOAs) of the banking system, collectively known as non-performing assets (NPAs).

- **Amendments to the Securities Regulation Code** – this measure seeks to accelerate further development of the capital market. Enhancements will be introduced in activities such as full disclosure of transactions, net capital and capital adequacy ratios and broker-director prohibition.

- **Revised Investment Company Act** – this proposal intends to provide a legal and regulatory framework for the conducive development of the mutual fund industry.

- **Personal Equity and Retirement Account** – this bill seeks to promote long-term savings among public and private employees through the creation of a voluntary retirement plan that carries certain tax privileges.

- **Pre-Need Plan Code** – this measure seeks to strengthen the management and financial operation of pre-need companies and to provide protection to planholders.

- **Corporate Recovery Act** – this bill intends to establish a set of procedural rules that will govern the complex processes involved in the suspension of payments resorted to by ailing enterprises. It defines the rights of debtors and creditors in formal debt relief proceedings and provides the guidelines that can facilitate the resolution of the proceedings.

Hon. Jose Isidro N. Camacho

The

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Cornelio C. Gison **Hon. Jose Isidro N. Camacho** **Juanita D. Amatong**

Nieves L. Osorio **Antonio M. Bernardo**

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President	**Norberto C. Nazareno**	2223 Pasong Tamo, Makati City	818-69-06 (DL), 810-49-01 to 10 (TL), 817-35-66 (Fax)
Philippine Export-Import Credit Agency			
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Ms. Rochelle D. Tomas

Mr. Eric C. Tipgos

Mr. Napoleon P. Micu

Director Ma. Teresa S. Habitan
(not in photo)

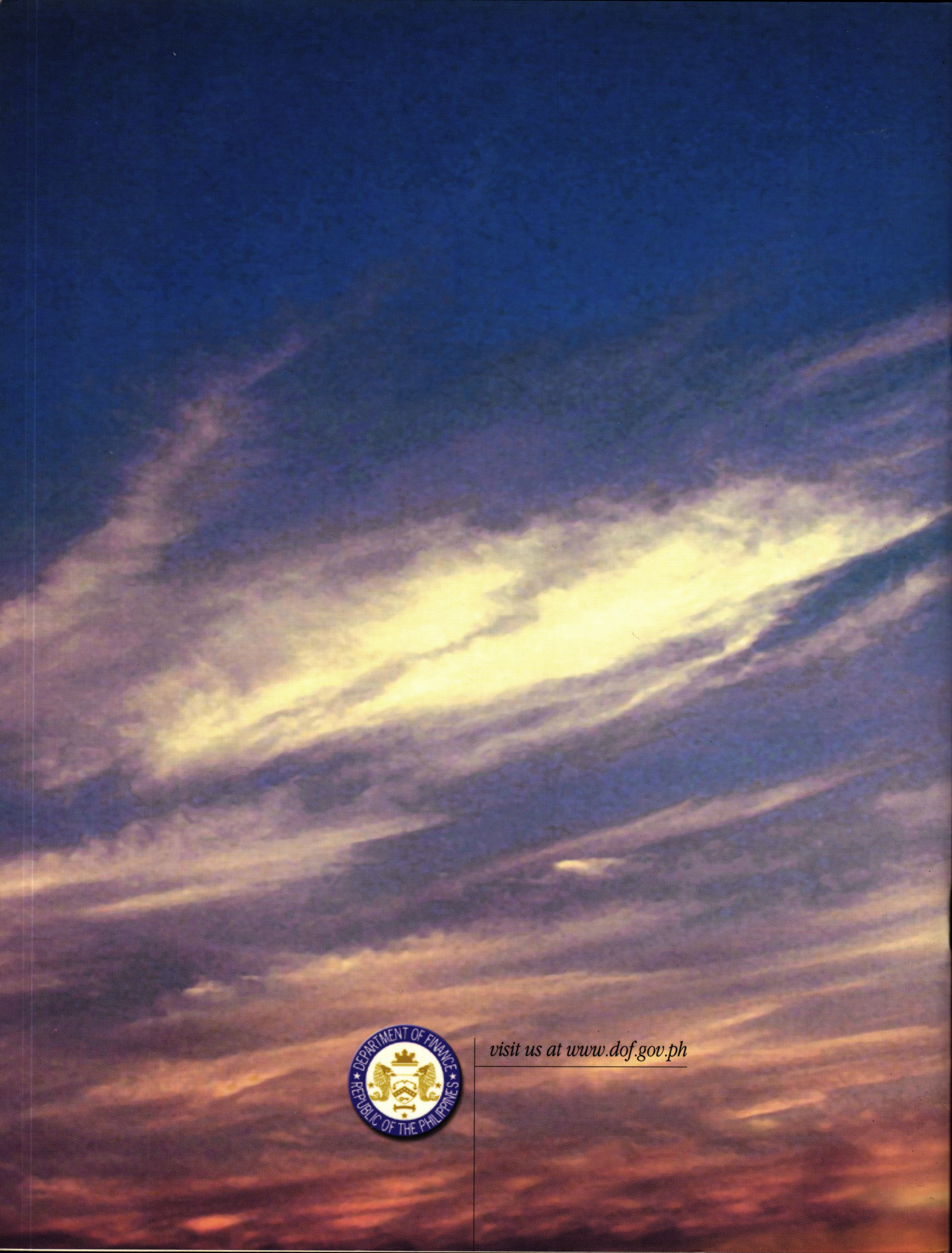
Assistant Secretary Gil S. Beltran
(not in photo)

Assistant Director Joselito S. Almario

Ms. Irene R. Sta. Ines

Mr. Ricardo P. Toquero

Ms. Aurora Luz D. Villaviray



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