ELIMINATING POVERTY
&
PROMOTING ECONOMIC RECOVERY
BY
RAISING WAGES & LOWERING PRICES
VIA AN
INTEREST RATE CAP

A Proposal
of the
CHAMBER OF REAL ESTATE & BUILDERS' ASSOCIATIONS (CREBA)

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Poverty is the root of most evils. Its all-pervading impact respects no age, gender, color or culture. The problems facing our country today ~ breakdown in peace and order, political instability, social unrest, graft and corruption, ignorance and apathy, and many others ~ are all traceable to widespread poverty. Solve poverty, and in time we will have resolved all these ills. Pay lip service to it, and we will witness EDSA 1 successively progressing to EDSA 10.

It is not impossible to eliminate poverty, for no problem can ever be bigger than man. As the saying goes: "where there is a will, there is a way." Indeed, all it takes is will ~ political will.

Poverty in our country stems from the ever-widening gap between income and cost of living ~ a gap arising from the combined impact of extremely low wages on one hand, and high prices of goods and services on the other.

It has been determined that in order to live decently, a family of 6 must earn at least P509 daily. With the current minimum wage of only P250, and the prices of basic commodities, transportation, electricity and water as they are now, a family with a single breadwinner would therefore survive only under subhuman conditions.

The demands of labor for an increase in the minimum wage, and of consumers for lower prices, therefore, are anything but unreasonable. Rather, it is a socio-politicoeconomic imperative ~ nay, a moral and Constitutional imperative ~ for Government to meet these demands expeditiously.

Poverty can be stamped out by raising wages and at the same time lowering prices. And this can be achieved as speedily as Government would wish, at no cost to Government and the business sector, by simply re-engineering our economic structure in such manner that among the 3 major costs of production ~ cost of money, raw materials and labor ~ labor as the human resource is accorded the preference it justly deserves. For as the saying goes: "There can be no labor without capital, nor can there be capital without labor."

The country's cheap labor force ~ which Government touts about as an enticement for foreign investors ~ should not be a source of pride but rather of shame. So should the country's perennial regime of excessively high interest rates. For it is precisely this abnormal combination of cheap labor and high cost of money that not only prevents the country from attaining an "independent economy effectively controlled by Filipinos", but also perpetuates the situation where the country's poor continue to get poorer while the rich continue to get richer.

Difficult as it may sound, reversing this abnormality ~ as the only way to eliminate poverty ~ really requires nothing more than just the political will to take that single all-important step: imposing a fixed and reasonable ceiling on bank lending rates.

History will show that for many decades when the Anti-Usury Law was in force from 1916 to 1976, economic instability of this prolonged duration and endemic poverty of the current magnitude were relatively unknown. Statistics will show that the country's woes set in and took hold only when the tempering influence of the Anti-Usury Law was removed and interest rates were allowed to float freely, to their present range of anywhere from a low of 14% to a high of 36% ~ and this is only during "normal" times. That these rates are excessive by any standard can be readily seen when compared to those of other countries, which governments strive to contain at no more than 3% to 7%.

The corrosive impact of high interest rates spares no one, not even Government, as it serves to trigger a chain of cost- and price- inflation across the entire economic spectrum ~ be it in terms of raw materials or finished goods or services, and be it in industry, agriculture, utilities, commerce or services.

As a leading economist puts it: "*High interest permeates all levels of society with such corrosive effects. Due to high interest rates, the cost of all goods and services unduly spiral, (the price) of low cost homes increase by 3 or 4 times their original costs. High interest shrinks markets, stifles the economy, discourages investments, fuels inflation, decreases wages and income. It is responsible for increasing the deficits of government, the imbalance of trade, the cost of basic utilities ~ water, power, transport, etc.*

It tilts the balance widely in favor of the capital-rich foreign investors, to the chagrin and despair of local entrepreneurs, makes Philippine goods and services uncompetitive in the world market. Yes, high interest makes American apples and oranges cheaper *than Philippine mangoes and for that matter, many foreign goods over locally manufactured goods".* [1]

Conversely, low interest rates means lower prices of all goods, services and utilities. This in itself not only improves the peso's purchasing power, but also enables businesses to generate cost-savings from which they can draw to meet the demand for increased wages. Just as importantly, improved purchasing power enables people to buy more of everything, thereby raising effective demand, which in turn sparks greater business activity and expansion ~ for it is only when the millions of our bread-earners are financially able to buy their needs may the country's producers continue to operate and provide.

Clearly, therefore, lowering interest rates is the key to a robust economy and in turn, to social quietude and effective governance.

It has become evident that it is neither wise nor practicable to leave such a vital task as the determination of interest rate levels entirely to the discretion of monetary authorities who are, after all, not infallible in their perceptions or predispositions ~ as evident, for instance:

1. In the recent juetengate fiasco when the interest rate tool was used by the BSP to resolve a problem that it later admitted was due to political and external factors beyond its control;

2. In the BSP's policy of raising reserve requirements ~ a move that invariably jacks up interest rates ~ allegedly to mop up "excess liquidity" and arrest the fall of the peso against the dollar, when such peso fall is not due to a peso oversupply but rather to an increased demand for dollars during peak seasons on one hand, and on the other, because of an undersupply of dollars due to low export receipts, further exacerbated by depletion of dollar reserves resulting from the BSP's largely futile interventions in the foreign exchange market; and

3. In several previous instances when the BSP ~ at the slightest sign of "capital flight" ~ sacrificed the interest of local investors and the local economy by triggering abrupt rises in interest rates in futile attempts to retain the so-called hot money of foreign portfolio investors.

Neither is it tenable, with the country's flawed banking system, to allow the "free interplay of market forces" in determining the cost of money, when such so-called market forces are not entirely free ~ in view of the apparent existence, however publicly belied, of a banking cartel. To do so would perpetuate the present situation where the entire economy is a helpless hostage to exploitative banking practices.

[1] Atty. Florencio B. Orendain, *"We Will Survive"*, (Keynote Speech at the 17th Annual Convention of the UAP, 10 October 1991)

Nor should banks be allowed to unilaterally raise interest rates by simply invoking the so-called "demand-supply squeeze" allegedly caused by Government's competition with the private sector for credit, considering that such "squeeze" is in fact due to the preponderance of DOSRI loans and corporate loans to the preferred giant conglomerates. It is bad enough that banks are allowed to practically dictate upon the government the rates it must pay for Treasury Bills. Worse, when Government allows banks to set lending rates for private sector loans based on the present formula of a 1% to 7% spread over Treasury Bill rates (depending on whether the borrower is "prime" or "non-prime"), it is in fact allowing these "prime" DOSRIs and conglomerates to enjoy unlimited credit at the cheapest rates, while at the same time condemning the "non-prime" SMEs ~ already suffering as they are from extreme difficulties in availing of credit ~ to still pay the maximum price for what little of it is made available to them.

The folly of Government's extremely tolerant posture toward the excesses of the banking system becomes particularly disastrous in the face of the banking practice of: (a) applying any hike in interest rates not just on prospective loans, but also on those already existing or pre-contracted prior to such hike, under the standardized "escalation clause" in loan/mortgage agreements; and (2) imposing upon corporate borrowers the requirement for officers/stockholders to execute a "Joint and Solidary Security" (JSS) clause as additional loan security (over and above the standard collateral) in the event of foreclosure of the corporate loan.

These twin practices alone ~ considering that any sudden totally unforeseeable and unprogrammed rate hike could easily spell failure by the borrowers to meet the regular contracted obligations as they fall due, and any such delinquency would result not just in corporate bankruptcies but personal bankruptcies as well ~ are not just usurious but downright immoral if not illegal.

The convergence of these situations of indiscriminate misapplication of credit policy on one hand and exploitative banking practices on the other, renders the economy highly vulnerable to collapse, and instantly inflicts incalculable and irreparable harm ~ particularly on the hundreds of thousands of SMEs that are for the most part highly dependent on credit.

Invariably, when this happens everyone suffers. But labor ~ being entirely dependent upon the business sector for livelihood, and with little if any alternative opportunities ~ suffers the worst.

With these in mind, and in order to restore the time-honored role of the banking system as an instrument for economic growth, CREBA recommends a package of measures, intended to be undertaken through legislation, on an immediate and intermediate basis, as follows:

IMMEDIATE MEASURES:

1. Imposition of a fixed lending rate ceiling of not more than 9% ~ inclusive of processing and other front-end fees ~ which will be uniform for all loans without distinction as to prime or non-prime. This will preclude any abrupt rise in interest rates, even as it would free the interest rate mechanism from any exploitative

influence of both the so-called banking cartel and predatory speculators in the guise of foreign investors. Just as importantly, it will enable borrowers to effectively program business operations particularly in terms of meeting loan obligations, even as it would tremendously boost the local investors' confidence and faith in the government's sincerity to accord them due preference consistent with the Constitutional mandate.

2. Simultaneously, exemption of bank lending transactions from the following taxes: a) Gross Receipts Tax (GRT); b) Value-Added Tax (VAT); c) Documentary Stamps Tax (DST); d) Tax on interest income. Complemented by sectoral credit allocations ~ in line with government thrusts ~ for SMEs and the agriculture, export and housing sectors, this will help ensure that credit is not only accessible but affordable as well.

3. Legislated increase of P100 in the minimum daily wage, commencing one week after effectivity of the interest rate cap, and another P100-increase after one or two years as Congress may deem appropriate.

Considering that the interest rate cap has been tried and tested for decades under the regime of the Anti-Usury Law, these measures cannot by any means be considered radical, novel, or experimental.

These measures are expected to achieve the following:

1. Provide immediate relief to the labor, consumer and business sectors, since this will result in lower production costs. The resulting cost-savings will enable the business sector not only to sustain the minimum wage increases, but also to stabilize if not actually reduce the prices of goods and services.

2. A compounded positive impact on purchasing power and effective demand which will result from the wage increases and price stabilization. This will revitalize businesses and thus spark the economy towards recovery and eventual growth.

3. Global competitiveness for the country's producers, particularly the export sector.

4. Greater impetus for housing activity which is the most highly capital-intensive of all businesses. An increased level of housing and construction activity will catalyze business opportunities for 65 ancillary industries and provide more employment opportunities.

5. For the government, any potential loss from the tax exemptions to be granted (exclusively) to bank lending transactions will be more than offset by (a) greater revenue prospects arising from expanded business activity throughout the entire economy, particularly in the housing/construction sector, as well as the revenue/foreign exchange earnings from a more competitive export sector; and (b) reduced interest burden on its domestic borrowings.

6. For the banking system, an energized business sector would mean greater demand for loans and thus, greater business opportunities as well as lesser non-

performing loans, even as the ensuing improvement in purchasing power would improve savings generation. Fears of any diminution in bank profitability or viability are largely unfounded, as an interest rate ceiling of 9% ~ when coupled with the tax exemption privileges ~ will translate to an effective yield of not less than 12%, even as the banking system's extremely conservative policies on collateral and loan-to-value ratios afford more than ample protection.

As can be readily seen, this package of measures corrects the major flaws in the credit delivery system, addresses the concerns of all sectors including the banking system itself, and ensures that their respective interests are reasonably served.

INTERMEDIATE MEASURES:

1. Legislated ban on the bank requirement for Joint and Solidary Security (JSS) clause currently being imposed on corporate loans. This is wholly unnecessary in view of the banking system's stringent collateral requirements and appraisal/loan-to-value practices, even as it represents an onerous and unjust burden for the individual officers and principal stockholders of a corporation.

2. Abolition of the 20% tax on interest income from bank deposits. This will encourage greater savings.

3. Expansion and strengthening of existing loan insurance and guarantee schemes extended to SMEs and other sectors covered by government-imposed credit allocations, in order to allay fears of possible lending risks.

4. Development of the secondary capital markets to encourage the flow of local rather than foreign capital. This will help insulate the economy from severe dislocations, as in the past, that may arise from the unpredictable flow of "hot money" of foreign speculators.

The economic crisis which has stretched to this unprecedented magnitude, and the length of time that it has inflicted untold misery upon the entire nation ~ without still any relief in sight ~ demand nothing less.