



Philequity Corner (April 24, 2017)
By Wilson Sy

Build, build, build!

Last week, the country’s economic managers and Cabinet members responsible for the infrastructure program presented the Duterte administration’s ambitious infrastructure plan. The team identified high-impact projects that will boost economic growth while also proposing to build new roads and mass transport systems that will solve the country’s traffic problems. In upgrading the country’s outdated infrastructure, the government aims to address bottlenecks that hamper economic growth in order to unlock our country’s growth potential.

Pump priming the economy for growth

In our book Opportunity of a Lifetime (Chapter 5 – Fiscal Reform in the Philippines), we discussed how the Arroyo administration implemented eVAT in 2005 to put the fiscal house in order. Doing this saved the country from a fiscal crisis and laid the groundwork for our country’s economic recovery.

Now, the country benefits from an outstanding fiscal position, which was affirmed by our upgrade into investment grade territory in 2013 (*Investment Grade*, April 1, 2013). Since then, the government’s balance sheet has remained strong and our budget deficit is actually manageable. Considering this, the Philippine economy is ready for take-off.

The implementation of various big-ticket infra projects is expected to address bottlenecks and unlock our country’s economic potential. Further, these initiatives will diversify our country’s growth drivers through the development of other sectors and by stimulating growth in the provinces.

Golden age of infrastructure

According to the administration’s economic managers, the government has allotted P8.4t for infra spending in President Duterte’s six-year term. This year, the budgeted amount is equivalent to 5.4% of GDP, more than double the 2.6% average of the past six administrations over the last fifty years. In addition, the government aims to raise infra spending to 7.4% of GDP by 2022. Below, we show some of the proposed major projects, as enumerated in last week’s presentation.

| Project | Benefit |
|--|---|
| NLEX-SLEX Connector Road | Reduce travel time from Alabang to Balintawak to 30 minutes |
| Mega Manila Subway Project | 25-km underground subway system to connect Mindanao Avenue in Quezon City to NAIA and FTI in Taguig |
| Metro Manila Rapid Bus Transit System | Efficient mass transit system in EDSA and other major thoroughfares |
| Mindanao Railway | Shorten travel time within the Mindanao region; more efficient transport of agricultural goods |
| Clark Green City | Creation of new urban center; address traffic and congestion in Metro Manila |
| Clark International Airport - new terminal | Reduce congestion in NAIA and traffic in nearby locations |
| Manila-Clark Railway | 1 hour travel time from Metro Manila to Clark |
| Subic-Clark Cargo Railway | More efficient transport of goods; lower transport costs |

Source: www.build.gov.ph

Infra upgrade will drive economic growth

The Duterte administration's infrastructure program is expected to provide many benefits to the country and the economy. We enumerate some of these below.

- 1) Boost economic growth.** The massive spending on infrastructure projects will spur economic activity. If these projects are executed properly, we see economic growth reaching 8 to 10% in the medium to long term. These initiatives are expected to unlock bottlenecks, increase productivity and diversify economic growth across many industries while also stimulating growth in provinces.
- 2) Job creation.** The construction of large-scale infra projects and the resulting economic development from these initiatives will create millions of jobs for Filipinos nationwide.
- 3) Improved flow of goods.** Better roads, railways, airports and sea ports will improve the flow of commodities and products not only within the country, but also to and from the country. This will result in lower transportation costs and increased competitiveness for many industries. Thus, improved infrastructure may aid the development of many industries such as manufacturing, agriculture and mining.
- 4) Development of tourism.** The tourism industry will immensely benefit from better airports and roads, which should lead to increased investments in the sector.
- 5) Reduction of traffic congestion.** Metro Manila is notorious for its congested cities and hour-long traffic jams. Various studies have shown that these cost billions of pesos for the economy. Better roads and improved mass transport will reduce travel times and result in higher productivity.
- 6) Decongestion of Metro Manila.** Building green cities and urban centers outside Metro Manila will address overconcentration in the country's capital. These projects will decentralize and diversify economic development while also stimulating the economic expansion of other provinces.

National government offices to move out of Metro Manila?

One of the important initiatives proposed by some key members of the Cabinet is the plan to move national government offices out of Metro Manila. The most viable alternative is probably the Clark Green City, which will be built to house a government district and an alternative urban center. Government offices such as Malacanang, Senate, Congress, Supreme Court and other major government institutions may be transferred to Clark once the city is developed. Transportation Secretary Art Tugade has said that he is willing to be the first to relocate his entire department to Clark. We thus hope that other government offices will follow Secretary Art's lead.

The plans for Clark Green City draw similarities to Putrajaya, a planned city in Malaysia which was designed to consolidate government offices in one location and decongest Kuala Lumpur. Another example that comes to mind is Washington, DC in the US.

Urban centers in Clark and Subic

The move is expected to significantly contribute in decongesting Metro Manila. Studies have shown that about two to three million people will move out of Metro Manila when a new government district is built in Clark. Further, it will result in countryside development, particularly in the provinces of Pampanga and Bataan. Note that there are many infra projects that will be constructed in Clark and Subic, on top of an existing airport in Clark and a sea port in Subic. Thus, the development of urban

centers in these areas will spur the economic development of Northern and Central Luzon. Also, building full-fledged urban centers in the countryside will diversify the geographic drivers of economic growth.

The importance of tax reform

The construction of large-scale projects in the government's infra program will need massive sources of funding. Without additional revenue generating measures, an increase in government spending for infrastructure will cause the budget deficit to breach 3% of GDP. Note that this is a key threshold which is monitored by credit rating agencies.

This is where tax reform comes in. Implementing the tax reform package will allow the government to maintain fiscal responsibility while increasing infrastructure spending. Even considering the revenue losses that will result from the lowering of personal income taxes, the tax reform package will still be a net positive for government revenues (*Tax Reform – The Next Big Catalyst*, February 20, 2017). Needless to say, the accomplishment of the government's infrastructure program will hinge on the successful and timely passing of the comprehensive tax reform package.

Similarities between Trump and Duterte

Many have talked about the similarities of US President Donald Trump and President Duterte. Aside from their firebrand personalities, the Trump and Duterte governments actually have very similar plans. In past articles, we discussed that Trump and Duterte's economic agenda both focus on tax reform, fiscal stimulus and infrastructure spending (*The Trump Card*, December 12, 2016).

Next leg of secular bull market

Since Trump's election win in November 2016, we have seen the US stock market reach new highs on the back of talks about Trump's pro-growth agenda, which includes tax reform and infrastructure spending. We thus believe that with the Duterte government's decisiveness and political will, the administration's infrastructure program (touted as "Build build build") will be successfully implemented, especially if the comprehensive tax reform package is passed. These initiatives will spur faster economic growth and will give rise to the next leg of the secular bull market in Philippine stocks.

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