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## Improving Industrial Relations and Reducing Adjunct Costs of Production and Trading: Steps Toward Improved International Competitiveness

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A major and critical ingredient for the economic success of the North-east Asian and three ASEAN countries is the fact that wages in these countries have been determined largely through the workings of the demand for and supply of labor services. This ensures a strong linkage between productivity changes and wage adjustments. In these countries, the rise in the real wages over time resulted from the much higher increases in labor demand due to high investment rate and economic growth than from the increases in labor supply. As such, the labor markets provided the appropriate price signals for the efficient allocation of labor resources and investments in human capital formation in the context of the changing world commodity markets and the countries' evolving comparative advantages (World Bank 1993, Chapter 6).

### Labor productivity in the Philippines: a discordant note?

The Philippine experience differs sharply from those of the other East Asian countries. Specifically, until the late 1980s, there had been a **negative relationship** between changes in real wages and labor productivity in the Philippines. During the 1970s and early 1980s, real wages in the industrial sector fell substantially. At

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the same time, labor productivity improved. In the late 1980s, meanwhile, real wages increased despite the drop in labor productivity (Table 1). What may account for this negative relationship is the political economy of wage determination and labor relations in the Philippines.

The decline in industrial real wages during the 1970s was a reflection of the inconsistency between the government's labor and industrial policies. Labor policies during the 1970s were characterized by the curtailing of labor rights, following the South Korean example at that time. However, in contrast to the South Korean case wherein the government succeeded in raising the real returns to labor by following a development and industrial strategy that made labor increasingly scarce (and therefore needed to be paid more) through adept economic management and high economic growth, the industrial policy in the Philippines during the 1970s did not substantially increase industrial labor absorption. Given a high growth in the supply of labor, this led to the decline in the real wage. Moreover, security of employment deteriorated as firms became vulnerable to domestic financial stringency and external economic shocks. The deterioration of the industrial relations environment during the early years of the Aquino government was most likely a delayed reaction to the in-

**Table 1**  
**Indices of Labor Productivity and Real Wages**  
(1980 = 100)

	<i>Labor Productivity</i>		<i>Real Wages</i>	
	<i>Agriculture</i>	<i>Manufacturing</i>	<i>Farm Workers</i>	<i>Unskilled Laborers Manila</i>
1970	97	57	109	214
1980	100	100	100	100
1990	93	90	143	170
1993	88	80	150	174

Note: Real wages for farm workers is based on daily wages (in cash and kind) of farm workers without meals in major crops deflated by the CPI for outside national capital region.

Source: Khan 1995, pp. 3, 7

appropriate policy regime during the 1970s and early 1980s.

With the increased political power of the labor unions during the Aquino administration, real wages in the formal sector increased during the latter 1980s primarily through minimum wage adjustments. Labor productivity growth, however, was sluggish. As a result, among the ASEAN countries, it was only in the Philippines where real wage cost in efficiency terms increased. Given the country's troubled industrial relations environment and rising real wages in efficiency terms (i.e., rising labor costs), together with political uncertainty and risks on personal security, it is not surprising that the Philippines was bypassed by the Japanese, South Koreans and Taiwanese in their

search for investment sites in Southeast Asia during the late 1980s and early 1990s.

In his comparison of the level of labor productivity in the Philippines and other selected countries in the Pacific Basin relative to the United States from 1970 until 1990, Golub (1995) found that labor productivity in the Philippines, which was about 27 percent of the United States in 1970, declined secularly to about 14 percent of the United States in 1990. The average **decline** in labor productivity in the 1970-1990 period was 0.5 percent per year. In contrast, real wages rose by an average of 0.2 percent per year in market exchange rate terms and by an average of 2.3 percent per year in purchasing power parity terms. The higher rate of increase

of wages and benefits in purchasing power parity terms reflects the impact of the real appreciation of the peso during the period. As a consequence of the growth of compensation in real terms in tandem with the decline in labor productivity, the relative unit cost of Philippine labor rose from about one-half that of the United States in 1970 to being higher than the unit labor cost of the United States by 1987. In effect, **Philippine labor, when productivity and exchange rate changes are taken into consideration, has become more expensive than US labor by 1990 compared to its only being half as expensive in 1970.**

While the Philippines saw a rise in its unit labor cost relative to the United States, the United States experienced a much higher rise in productivity of its labor (at 3.0 percent per annum) compared to the rise in its real wages and benefits (at 1.7 percent per annum) during the period. This means that the unit labor cost of US labor declined secularly during the 1970-1990 period.

The average growth of labor productivity per year of the countries in Golub's sample during the 1970-1990 period are as follows:

Japan	—	5.2%
West Germany	—	2.2%
Canada	—	2.1%
Australia	—	2.6%
South Korea	—	6.5%
Mexico	—	3.2%
Malaysia	—	2.0%

Thailand	—	4.4%
India	—	3.4%

From the above, one notes that the rate of labor productivity growth in the other countries was higher than the Philippines'. The sharp rise in the labor productivity of South Korea allowed it to maintain a unit labor cost that was lower than the United States during the period despite the significant increase in real wages in South Korea (at 7.0 percent per annum).

The contrasting experiences of the Philippines and South Korea is worth highlighting. South Korea experienced a sharp rise in real wages but was able to maintain its unit labor cost below that of the United States because of correspondingly substantial growth in labor productivity. In contrast, the Philippines experienced a marginal rise in real wages which was, however, coupled with a declining labor productivity, thereby leading to the rise of the country's unit labor cost from about one-half that of the United States in 1970 to being higher than that of the United States by 1990.

### Need to improve labor productivity

Given the country's relatively more expensive labor vis-a-vis countries like Indonesia, China and Vietnam and as the Philippine economy increasingly relies on labor intensive manufactures and tradeable services (e.g., tourism, data inputting services), it is ap-

parent that the discordant relationship between labor productivity growth and real wage adjustments of the past decade has to change. This calls for better economic management, on the one hand, in order to substantially improve labor productivity and reduce food inflation-induced demands for wage increases, and refinement of the institutional framework of wage determination, on the other.

Specifically, it is important to underscore that in the new trading and economic environment in the region, the Filipino workers, employers and government are, as a team, in competition with the workers, employers and governments of competitor countries in the region.

This therefore calls for:

❖ **ensuring an economic management and policy environment that generates wage employment much more than the growth of the labor force, and**

❖ **labor and management taking greater cognizance of the productivity-wage-competitiveness nexus.**

Since the Philippine government is in the process of implementing reforms towards greater economic outwardness, macroeconomic stability and international competitiveness, **minimum wage setting as the means to effect broad wage changes thus needs to be deemphasized.** As a possible alternative,

the government may place greater emphasis on performance-based bonuses or productivity sharing, following the successful experiences of Northeast Asia. Corollary to this is the need to put greater emphasis on collective bargaining negotiations between workers and their respective employers.

The government can encourage the adoption of performance-based bonus or productivity sharing by momentarily freezing the current minimum wages and instituting guidelines or suggestions (through the National Wage and Productivity Council and the Regional Wage and Productivity Boards) for the employers and employees to consider during their collective bargaining negotiations. If the government, however, continue to emphasize minimum wage setting as the country's main mechanism for broad based adjustments (because the institution of performance-based bonus system is politically difficult to do), **then it is preferable to have labor productivity growth on an industry basis rather than on a regional basis as the major determinant in the process of wage adjustment.**

Singapore's wage adjustments use wage bands by industry (groups) that largely tie wage adjustments to productivity improvements. Indonesia uses minimum wage adjustments cautiously in view of the growing investment and export competition from even

lower wage countries like Vietnam. Thailand's minimum wage is lower than the prevailing wage and therefore minimum wage adjustment is used primarily as an anti-poverty measure rather than as a means for broad-based wage adjustments.

The comparative findings of the Golub study, showing the sharp rise in the unit labor cost of the Philippines because of declining (or at best sluggish) labor productivity, indicates that the **government, labor and employers would have to give much more importance to improving productivity** through such measures as policy reforms, improving infrastructure and institutional support structures, higher investment, organizational restructuring, improving the work place, and increasing investments on worker training and upgrading. To a large extent, **the work place is better viewed as a partnership among the employers and the workers both for improved international competitiveness of the firms and for improved human capital and material welfare of the workers.**

#### Need to reduce cost of doing business in the Philippines

Given the situation as noted above that wage rates in the Philippines are no longer low compared to a number of competitor countries like Indonesia and China, it is apparent that the country will have to compensate for this

comparatively high factor cost through other means. This may refer to a lower adjunct cost related to doing business in the country coupled with a comparatively higher and faster growth of labor productivity. Reducing the adjunct costs of production and trading means reducing the cost of transacting with the government as well as reducing the travel cost of transporting goods and services between the production site(s) and the domestic and/or foreign market(s). As such, there is a need to streamline regulatory procedures and improve infrastructural services. The expected end results are faster start-ups of businesses and faster turnaround time for imports and exports. In addition, the economy will be more integrated internally and with the rest of the world. Finally, streamlining regulatory procedures and improving infrastructural services contribute to improved efficiency of production and increased factor productivity. Thus, they will result in lower factor cost in efficiency terms.

#### Reducing transactions costs

Transactions costs can be reduced by:

- ❖ redefining the approach to regulation (i.e., regulatory reform),
- ❖ streamlining regulatory systems and procedures, and
- ❖ upgrading technological support to regulatory procedures.

**Regulatory reform is fundamental in reducing transactions costs.** Inefficiency is endemic where bureaucratic interventions are pervasive in an economy. It is increasingly acknowledged, for example, that the industrial protection regime in the South Asian countries like Bangladesh during the 1960s and 1970s, which was meant to encourage the domestic manufacturing sector through extensive investment and trade controls, was not helpful to the sector. In the end, the protection became mainly a means of enlarging and supporting the bureaucracy.

The Philippines has been vigorously pursuing a process of trade liberalization, deregulation and privatization in order to substantially reduce bureaucratic control over the affairs of business and markets.

**At present, it is in streamlining regulatory systems and procedures, together with technology upgrade, where the benefits to the producers and the consumers would be significant.** Generally, this involves reducing the number of papers to fill up and permits to obtain, the establishment of one-stop shops for all the permits, the establishment of express lanes, and more extensive use of computers toward an electronic data interchange among concerned agencies that will enable electronic transactions by the private sector and the concerned agencies.

**An example of streamlining regulatory systems and technology upgrade is the GTEBNet Project of the Garments and Textile Export Board (GTEB).** The GTEBNet project vision includes the simplification of GTEB procedures, enhancement of the GTEB computer systems, and compliance with the US customs service requirement on the implementation of Electronic Visa Information system for US imports of garments. The GTEBNet project enables exporters to

- ❖ electronically transact with GTEB using computers in their own premises,
- ❖ have access to the GTEB database on quota balances, directory of exporters and subcontractors, and GTEB statistics,
- ❖ transact electronic payment of GTEB assessment fees, and
- ❖ conduct electronic transmission of GTEB-approved TEC/IA to the Bureau of Customs.

The effect is the reduction of processing time from hours to minutes (EDINet Infosheet, EDC 1995).

A similar project on automation is the EXPORTNet, the automation program of the Export Development Council. It essentially involves the use of electronic data interchange for speedy export clearance, export declaration, cargo reservation, and payments/

funds transfer. The result of the electronic data interchange is the elimination of delays and errors associated with paper documents. Important to the automation project is the computerization of concerned agencies—not only of the GTEB and other government clearance agencies—but also of the Bureau of Customs.

The Bureau of Customs is a critical agency with respect to regulatory procedures in exporting and importing. The Bureau has instituted a “green lane” system of clearing shipment for low risk shipments. It is in the process of computerization toward an electronic data interchange. It has implemented the Automated Manifest Clearance System towards strengthening clearance process of manifests. It has also been simplifying forms and codings through customs Memorandum Order 39-93. A Modified Manual Clearance Procedures was implemented to accelerate the processing of import entries and further simplify clearance procedures.

The Bureau of Customs has also been trying to implement many of the recommendations embodied in the eleven-point reform program prepared by the Fiscal Affairs Department of the International Monetary Fund. Phase One of the automated system for customs data (ASYCUDA) is now being implemented at the Port of Manila. It is planned to be implemented at the Ninoy Aquino International Airport and the Manila

International Container Port. The first phase of the ASYCUDA involves the computerized assessment of taxes and customs duties. Together with the first phase of ASYCUDA is the establishment of the Community Training Center of the Philippine Chamber of Commerce and Industry (PCCI) and the Bureau of Customs where importers and exporters can submit their paper import entry declarations for digitized encoding as well as for customs query and up to date tracking of papers without the need to personally go to the arrastre operator's office at the Bureau of Customs. The ASYCUDA will be used in the future in Customs declarations, manifests, accounting, warehousing and trading facilities. It will eventually be part of an electronic data interchange system as elaborated in the EXPORTNet.

The Subcommittee on Tax Administration of the Presidential Task Force on Tax and Tariff Reform has an additional set of recommendations which the Bureau of Customs can implement to further improve customs administration.

Among the recommendations that can be implemented by the Bureau itself are the following:

- ❖ establish formal risk assessment procedures during entry processing whereby high risk shipments are subject to full examina-

tion while low risk shipments/vessels are only randomly chosen;

- ❖ renegotiation with the Societe Generale de Surveillance (SGS) to allow for the imposition of stiff penalties for SGS delays in processing and increase in penalties for improper valuation;

- ❖ delegation of decision-making on routine matters from the Office of the Commissioner to the District Collectors.

#### Recommendations

***The overall objective of the streamlining of regulatory procedures is to move towards time-based processing. It is recommended that the government use this as the focus of its efforts at streamlining regulatory procedures whereby each concerned agency sets definable targets in terms of reduction in processing time.***

***The government needs to pursue further computerization of procedures similar to the programs of the GTEB and the Bureau of Customs.*** The concerned agencies may need to explore lease arrangements with computer service suppliers for technological upgrade of the facilities for faster processing of papers. It is further recommended that government agencies look into the possibility of instituting higher processing fees in exchange for faster and more transparent processing of papers. The proceeds from the

processing fees can be used to pay for the lease or purchase of the computer facilities.

#### Infrastructural development

Infrastructure remains a major bottleneck in the country's drive for international competitiveness. ***The 1995 World Competitiveness Survey indicates that the Philippines ranks close to the tail end of the list of countries with respect to the quality of infrastructure; it ranks lower than the other competitor countries in the region.*** Despite the substantial improvements during the past two years as best exemplified by the end of the power blackouts, the targeted acceleration of economic growth raises the demand for improved infrastructural services.

The World Bank estimates that the Philippines would need about US\$48 billion in infrastructural investments during 1995-2004, representing about 6.8 percent of the Gross Domestic Product (GDP) (The World Bank 1995, p.25). Clearly, this is much more than what the government can finance. Hence, the need for strengthening the partnership between the government and the private sector on infrastructural investments. The government has successfully tapped the build-operate-transfer (BOT) scheme in addressing the power problem in the country. Deregulation in the

telecommunications industry has also generated substantial foreign and domestic private investments in the sector. There are also BOT proposals in light rail transportation and toll roads.

Nevertheless, **there remain areas for further improvement in the provision of infrastructural investments.** First, the current practice of BOT projects in power generation for the state owned NAPOCOR forces the government to assume directly or indirectly many of the commercial risks through the guarantee mechanism. Second, the setting of appropriate user charges for BOT projects like toll roads and the light rail transit would likely be difficult unless there is a clear-cut government policy (and public acceptance of the policy) on user charges of infrastructural facilities. And third, the transactions cost of negotiations on the BOT projects have been substantial.

How can the government further facilitate private investment in infrastructural facilities without excessive government subsidies through fiscal incentives and guarantees? The World Bank (1995) presents a framework for facilitating private investments in infrastructure. The framework highlights the following:

- ❖ the establishment of a conducive policy, legal and regulatory framework;
- ❖ transparent and competitive mechanisms for approving pri-

vate projects, speedy government decision making, adequate sector planning and project facilitation assistance;

- ❖ unbundling, sharing and management of risks wherein the party best able to manage a risk at least cost should mitigate the risk. The current practice of the government assuming contingent liabilities (obligations under guarantees against both commercial and sovereign risks) is unsustainable; and

- ❖ development of domestic capital markets and of mechanisms to facilitate provision of long-term debt.

The unbundling and more equitable sharing and management of risks would require that the private sector (i.e., sponsors, financiers, insurance companies) would have to shoulder commercial and managerial risks while the government would bear the sovereign or country and policy risks like currency transfer and policy performance (The World Bank 1995, p.14). In order for the private sector to bear the commercial and managerial risks, there may be need for more market oriented user charges and possibly even increased competition and/or privatization in the provision of infrastructural services (e.g., power generation, transmission and distribution). Thus, improving the policy and regulatory framework of infrastructural services provision would encourage

the unbundling and more equitable sharing of the risks of infrastructural investments.

Improving the policy environment for infrastructural development in the Philippines involves the **adoption of more realistic, depoliticized and market-oriented user charges that would encourage the private provision of infrastructural facilities.** The nature and extent of government subsidies in conjunction with the private investment on infrastructural facilities would have to be clearly spelled out. It is apparent from the above policy posture that there would be a **redirection of government infrastructural investments** such that a greater percentage of the infrastructural investments in growth areas where the private sector is interested in and willing to undertake can or should be shouldered largely by the private sector. The government, meanwhile, could give special focus on the infrastructural needs of areas where the private sector is not keen on investing like in poor regions and sanitation projects.

The private sector has responded favorably to the deregulation and liberalization measures of the government in infrastructural services provision, leading to an upsurge in private investments in telecommunications, interisland shipping and interprovincial bus transport. The effect has been a marked improvement in efficiency.

This is perhaps best exemplified by the telecommunications sector. Marked improvements in efficiency also occurred in interisland shipping. For example, the introduction of faster superferries has improved interisland passenger travel. Similarly, roll-on and roll-off services in Mindoro and cargo and passenger services in the Cebu-Dumaguete-Dapitan route have improved with increased private competition arising from rate and route liberalization (Nathan Associates 1994, Executive Summary).

Nevertheless, there remains the need for proactive government intervention in the provision of transportation services that would reduce the cost of operations by the private sector and therefore the cost of transport. For example, the government would need to improve the port of Cebu since it is already inadequate for the current traffic levels. The same is true for the port of Iloilo. More roll-on, roll-off berths would have to be provided in several Visayan ports. Moreover, port security in the port of Cebu is wanting, such that shippers have had to send guards with their cargo sometimes (Nathan Associates 1994, Executive Summary). Relatedly, one of the concerns of exporters is the highjacking and pilferage of goods (Export Development Council, 23 November 1995).

Given the limited funds for infrastructural investments and the

need for efficient infrastructural facilities and services in order to improve the country's international competitiveness, it is apparent that the country would have to have spatial prioritization in the provision of infrastructural facilities and services. ***The country would have to select a few locations at present in its provision of efficient infrastructural facilities for production and international trading (i.e., develop a few priority investment sites such as Subic, Calabarzon, Metro Manila, Cebu, Clark and environs, Davao).*** It is better to have a few "success stories" that would draw attention to the Philippines as a production and investment site. In the priority investment areas, the government may encourage private investment in infrastructure provision based on appropriate user charges while the government would focus on significantly reducing "red tape" and streamlining regulatory procedures (i.e., "hassle-free" transactions).

In the meantime, the rest of the government expenditures for

infrastructure can be spent in improving the interlinkages of the rest of the country with selected major export bases of the country. At the same time, the government in its infrastructure plan would have to improve direct access of major island groups (e.g., Mindanao) to the world market by establishing efficient international airport and port facilities as well as international telecommunications linkups in each major island group. □

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