Joint Private Statement to the Senate on House Bill No. 6608

As the Senate begins deliberations on the Maharlika Investment Fund (MIF), we maintain our view that such is fundamentally flawed and does not achieve the stated economic activities cited in its formation. We hope the Senate will consider the MIF's adverse impact on fiscal prudence, additionality, solvency of pension funds, contingent liabilities, independence of the Bangko Sentral ng Pilipinas (BSP), and government intervention in the economy. While we note that the State-managed pension funds have been removed as funding in the newly passed House Bill No. 6608, also known as the Maharlika Investment Fund Act, it is now the BSP, our government financial institutions (GFIs), and ultimately the national government (NG) that are in harm's way.

We further explain our position using HB No. 6608 as context.

MIF and BSP

HB No. 6608 provides that MIF will source significant funding from the BSP's declared dividends:

> "For the first and second fiscal year upon effectivity of this Act, the BSP shall remit one hundred percent (100%) of its declared dividends, as computed under R.A. No. 7653, as amended by R.A. No. 11211, to the Fund. In the succeeding fiscal years, the BSP shall remit fifty percent (50%) of its declared dividends to the Fund and the remaining fifty percent (50%) to the NG to fund the increase in the capitalization of BSP in accordance with Section 2 of R.A. No. 7653, as amended by R.A. No. 11211, until the increase in the capitalization of BSP has been fully paid. thereafter, BSP shall remit one hundred percent (100%) of its declared dividends to the Fund."

This not only amends the BSP's mandate to promote monetary stability by adding an earnings factor for the MIF in its key performance indicators, but also effectively deprives the BSP of its ability to strengthen itself from its earnings to manage liquidity and inflation, as well as help distressed financial institutions. It compromises the BSP's autonomy, independence, and ability to deliver on its price and financial stability mandates. For example:

1) The BSP imposes reserve requirements on banks, on which it may pay interest. Easing these requirements reduces the "income" of the BSP, and by extension its dividends, but it boosts the economy by lowering the costs of financial intermediation. The BSP's monetary objectives could be at odds with the MIF's need for funding through the BSP's earnings and dividends.

2) The BSP intervenes in the forex market, to create a more stable environment for companies. Such interventions can cause the BSP to gain or lose profits. Should the BSP's forex stabilization efforts be tainted by pressure to maximize dividends for the MIF?

The BSP has consistently been viewed as among our most effective and trusted institutions, which has been key to our economic stability. The MIF could put such effectiveness and trust at risk.[1]

MIF and GFIs

Consider the following provision in HB No. 6608:

> "Investments of contributors may be in the form of marketable or convertible securities, and other forms, as may be determined by the Board of Directors: *Provided,* That security or debt instruments issued by the Maharlika Investment Corporation (MIC) to GFIs <u>shall be guaranteed by the NG</u>:..."[2] (underscoring supplied).

Ostensibly this provision tries to assuage concerns about the riskiness of the GFI exposure to the MIF. This provision however will:

1) Create additional contingent liabilities for the national government at a time when there are serious concerns about the size of the government's outstanding debt, contingent liabilities in infrastructure projects and pension funds, and burgeoning unfunded liabilities in the retirement program for the armed forces. Managing our debt and contingent liabilities is critical to protecting our credit ratings.

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[1] Recent statements to the press by a legislator indicate a re-thinking of the intention to tap the BSP for funding the MIF, but to still rely on dividends from government-owned and controlled corporations (GOCCs). This could be in recognition of the concerns and infirmities in the sourcing MIF funds from the BSP raised in this paper. The plan to fund the MIF from GOCC dividends, on the mistaken notion that such dividends are "surpluses by nature", is still fundamentally flawed in terms of fiscal implications and additionality issues. Sequestered GFI dividends for the MIF will need to be covered by additional borrowings.

[2] *As of this writing, the draft of the revised MIF for Senate deliberations has not yet been circulated.*

2) Make available without limit, the full resources of Land Bank of the Philippines (LBP) and the Development Bank of the Philippines (DBP), who will see such guaranteed lendings to the MIF as "risk-free assets", without requiring any due diligence. While the House correctly protected the pension funds, and now the GFIs via the guarantee, the NG will be left holding the bag, similar to the legacy problem assets of the National Development Corporation.

Conclusion

The MIF is highly questionable as a strategy to achieve the government's stated objectives. This is due to the fundamental flaw that funding of the MIF will not come from significant surpluses from commodity earnings or government operating results. Instead, the funding will be extracted from – and weaken – the BSP, GFIs, and other GOCCs. Weakening the BSP will reduce its ability to fulfill its primary purposes, and relying on the BSP's dividends will engender systemic risks. Giving the GFIs a statutory guarantee for its lendings to the MIF will open the sizeable liquidity of the LBP and the DBP. However, it creates no incentive for diligence, since the risk is passed as a contingent liability entirely to the NG.

Rather than pursue the MIF, we respectfully recommend that the legislature focus instead on working with and strengthening existing institutions and fulfilling developmental aspirations through the budget process as mandated by our Constitution.

Approved:

Foundation for Economic Freedom (FEF)
Management Association of the Philippines (MAP)
UP School of Economics Alumni Association (UPSEAA)