A STUDY OF PHILIPPINE MANUFACTURING CORPORATIONS*

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I. INTRODUCTION

MOST COUNTRIES of Asia are poor and underdeveloped. Unfortunately, the Philippines fall in this category. One often tends to take a monolithic view of underdevelopment. Some underdeveloped countries, however, are more developed than others, even though their economic performance in terms of per capita income may not differ greatly.

Before the Second World War, there were only a few industries in the Philippines, and most industrial goods were imported from her "mother country" at that time, the United States. In the postwar period however, the Philippines began to industrialize by restricting the import of "unessential" goods while encouraging domestic production. Visitors from industrial countries to the Philippines readily note the large number of manufactured goods that are imported; this reinforces their preconceived notion that the country is not industrialized. Compared with other countries in Asia, however, the industrial base of the Philippines is broad.

For underdeveloped countries, "industrialization" essentially means increasing manufacturing activities. Industrialization, in other words, means "manufacturization." This view is historically justified. All developed countries today were originally agricultural; their development started with the increase of manufacturing activities. One can argue, however, that increase in productivity is the key to development and that it therefore does not matter where the increase takes place. In this case, it is important to undertake activities which yield the largest increase in productivity; it is possible to develop a country by concentrating on agricultural and extractive industries. But this view is not well received, for development is usually considered to be synonymous with industrialization.

The task of industrialization is difficult. Shortage of capital and lack of human

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skills are often cited as obstacles. Nor should we forget cultural and institutional barriers to industrialization. As successfully demonstrated by Japan, industrialization can take place within the institutional framework of Asian societies as well as in the West. Apparently, then, industrialization is possible within a broad institutional framework. Industrialization, however, is built on certain premises such as rationalism and economic calculation, and in certain cultural contexts it may not be possible.

A number of papers and monographs have been written on the topic we will deal with in this paper. The reader unfamiliar with Philippine industrialization would profit from consulting John Power and Gerardo Sicat [10], Amado Castro [3] [4], Frank Golay [5], and G. Hicks and G. McNicoll [7]. All of their work approaches the problem of industrialization by analyzing government policies and examining aggregate data. Although the reliability of aggregate data can be questioned, the macro approach is important in order to gain an overall view of the problem. To study Philippine industrialization, however, we took manufacturing corporations and examined them from various aspects in an approach that has not been heretofore undertaken. We hope that this paper will contribute to a better understanding of Philippine industrialization and provide some useful insights into it.

II. THE RESEARCH DESIGN

Since it would be too time-consuming to study all corporations in the manufacturing sector, we have limited their number to a manageable size for the purposes of this paper. This could have been accomplished by means of a random sample, but since the data for small corporations are of low reliability, we decided to take all corporations above a certain size. Value added is the ideal indicator of the manufacturing activity of corporations, but this data was not readily available . The most available indicator was the amount of sales.

We also limited our study to the year 1968. This was the last year for which data were readily available. Nineteen sixty-eight was, in general, a normal year. Athough it is more informative and useful to study corporations over a longer period of time, due mainly to data limitations this was not undertaken here.

First, we obtained a list of 1,000 corporations from [2]. These corporations recorded sales of at least 1.9 million pesos in 1968. From among the 1,000, we took only those in the manufacturing sector which sold over 5 million pesos. This cut-off point netted us a total of 254 corporations.

There are many aspects of corporations which are not apparent to an outsider. Therefore, we had to rely on information submitted by the corporations to government agencies or published by the corporations themselves, such as financial statements, lists of stockholders, and brandnames.

The lists of stockholders and financial statements were obtained, insofar as possible, from the Securities and Exchange Commission (SEC). Although we were able to obtain all the desired financial statements, information on owner-

ship was not complete for some corporations. Corporate files at the Board of Investments helped supplement this. Brandnames were studied for the light they throw on licensing agreements.

The information collected at government agencies was supplemented by interviews with corporations when more data were needed. Not all corporations granted us interviews. We had particular difficulties with Chinese and Chinese-Filipino corporations.

Other data on corporations were not systematically collected, although we did gather additional fragmentary information on corporations through interviews or from articles in various newspapers and journals.

III. THE SAMPLE

The sample consisted of the 254 largest manufacturing corporations in the Philippines.[1] The names of individual corporations are listed in papers written at University of the Philippines.[2]

The distribution of corporations by sales is shown in Table I. Since one dollar

TABLE I
THE DISTRIBUTION OF MANUFACTURING CORPORATIONS BY AMOUNT OF SALES

Sales (million pesos)	Number of Corporations
5.0– 5.9	27
6.0– 6.9	24
7.0– 7.9	8
8.0– 8.9	13
9.0– 9.9	6
10.0– 19.9	81
20.0– 39.9	50
40.0– 59.9	16
60.0– 99.9	15
100.0–199.9	11
Over 200	3
Total	254

was worth four pesos in 1968, 5 million pesos, the amount of minimum sales, were worth about $1.25 million. The largest sales recorded, 532.9 million pesos,

1 The distinction between manufacturing and commercial firms is not very clear-cut for the Philippines. This probably holds true for most underdeveloped countries. We interpreted commercial firms to be those engaged in the sale of goods that do not undergo transformation in their hands. Thus assembling, packaging, and bottling we considered to be manufacturing operations. In cases where firms are engaged in both manufacturing and commercial activities, those whose manufacturing operations accounted for more than 5 million pesos were included in our sample.

2 See [12], [13], and [14]. These studies list 256 corporations; 2 of them were later found to be commercial firms.

were made by a conglomerate firm engaged in a variety of manufacturing operations. The median was in the range of 10.0–19.9 million pesos.

The distribution of corporations by industry is given in Table II. The scope

TABLE II
THE DISTRIBUTION OF CORPORATIONS BY INDUSTRY (%)

Industry	Number	(%)
A. Food, beverages & tobacco	80	31.50
1. Dairy products	4	1.57
2. Sugar	20	7.87
3. Flour	6	2.36
4. Other foods	18	7.09
5. Beverages	4	1.57
6. Liquor	6	2.36
7. Tobacco	12	4.72
8. Copra	10	3.96
B. Textiles	34	13.39
1. Textiles	31	12.21
2. Industrial textiles	3	1.18
C. Chemicals	50	19.69
1. Petroleum	4	1.58
2. Paint	6	2.36
3. Fertilizer	3	1.18
4. Drugs	14	5.51
5. Soap & cosmetics	5	1.97
6. Batteries	3	1.18
7. Matches	2	0.79
8. Others	13	5.12
D. Metal fabrication	25	9.84
E. Household appliances	11	4.33
F. Machinery & equipment	17	6.69
1. General machinery	7	2.76
2. Transport	10	3.93
G. Others	37	14.56
1. Paper & paper products	11	4.33
2. Rubber	7	2.76
3. Glass	3	1.18
4. Cement	9	3.54
5. Construction materials (not classified elsewhere)	4	1.57
6. Animal feed	2	0.79
7. Others	1	0.39
	254	

of manufacturing activities is surprisingly wide. Although one finds no integrated steel mills, no modern shipyards, or any petro-chemical complexes, the list is nonetheless impressive. It is true that many of these corporations are "turn-key" projects or are engaged merely in assembly or similar operations using imported materials, but it would be unfair to categorize all of these corporations as

"assembly" or "packaging" industries. For example, although the steel industry is without an operational integrated mill, there are cold mill and metal fabrication facilities.[3]

IV. FOREIGN PARTICIPATION

Foreign corporations started operations in the Philippines for two different reasons. Foreign companies came to the Philippines to maintain and expand their supply of raw materials and to obtain mineral resources and plantation crops. In the case of manufacturing companies, these local items undergo light processing before being sent back to the parent companies. In the case of pineapple, foreign companies operate plantations and canneries and ship the finished product back to the home market.

The second reason concerns exports. Foreign corporations set up subsidiaries when it proved cheaper to undertake certain stages of manufacturing in the Philippines than to ship the finished products themselves from the home country. Transportation costs could be a determining factor, as in the case of beverages. The availability of major raw materials in the Philippines could be another. In cases where technology can be transferred fairly easily, it is uneconomical to ship raw materials abroad only to have the finished products sent back again. Also, foreign corporations began to set up packaging and assembly operations when the importing or finished products was made difficult and when foreign producers were forced either to lose the market or to develop later stages of production in the Philippines.

Tables III and IV give the ownership of corporations by nationality. Table III breaks down corporations by industry and by nationality of ownership. Nationality control of a corporation is determined by which nationality owns the largest number of common stocks.[4] Since control is based on the largest number of shares, Filipino corporations may have foreign equity investment. Similarly, foreign corporations may have Filipino capital. Therefore, the table does not give much information on the extent of foreign capital participation in Filipino manufacturing corporations.

Table IV divides corporations into "domestic" and "foreign." "Domestic" corporations are those with a majority of shares owned by Filipino citizens, and

[3] One should note that the wood industry is not classified here. This is because the wood industry in the Philippines consists mostly of logging and lumbering. There were fifty corporations in this industry with gross sales of over 5 million pesos in 1968. Some have facilities to produce plywood as well as lumber, but an even larger part of their sales comes from logging. The wood industry is therefore better classified as an extractive rather than a manufacturing industry, thus excluding it from the scope of our study.

[4] According to the Philippine Corporation Law (P.A. No. 1459 [1906]), as amended in 1956, all shares have voting rights without distinction. Their votes determine (1) changes in the number of directors, (2) changes in the amount of capital, (3) amendments to the articles of incorporation, (4) the adoption of by-laws, and (5) the voluntary dissolution of the corporation. Shares classified as voting stock (usually common stock), however, have the exclusive right to determine the election of directors. The owners of such voting stocks control corporate policy.

TABLE III
THE DISTRIBUTION OF CORPORATIONS BY INDUSTRY SHOWING OWNERSHIP BY NATIONALITY

Industry	Total Number of Corporations	Control				
		Filipino	American	Chinese	Japanese	Others
A. Food, beverages & tobacco	80	53	16	5		6
1. Dairy products	4	1	2			1
2. Sugar	20	15	3			2
3. Flour	6	6				
4. Other foods	18	11	6			1
5. Beverages	4	1	3			
6. Liquor	6	5		1		
7. Tobacco	12	8		2		2
8. Copra	10	6	2	2		
B. Textiles	34	29	1	2		2
1. Textiles	31	27		2		2
2. Industrial textiles	3	2	1			
C. Chemicals	50	20	27			3
1. Petroleum	4	0	3			1
2. Paint	6	3	3			
3. Fertilizers	3	3				
4. Drugs	14	2	12			
5. Soap & cosmetics	5	2	2			1
6. Batteries	3	2	1			
7. Matches	2	1				1
8. Others	13	7	6			
D. Metal fabrication	25	18	4	2	1	
E. Household appliances	11	6	5			
F. Machinery & equipment	17	10	7			
1. Gen. machinery & equipment	7	3	4			
2. Transport	10	7	3			
G. Others	37	30	7			
1. Paper & paper products	11	9	2			
2. Rubber	7	4	3			
3. Glass	3	2	1			
4. Cement	9	9				
5. Construction materials (not classified elsewhere)	4	3	1			
6. Animal feed	2	2				
7. Others	1	1				
Total	254	166	67	9	1	11

"foreign" corporations are those with a majority of shares owned by aliens. Domestic corporations are divided into "Filipino" and "Chinese-Filipino." This division was motivated by the desire to examine the extent of the participation of Filipinos of Chinese ancestry in the Philippine manufacturing sector. A Chinese-Filipino is defined as a Filipino citizen who bears a Chinese name. A Filipino is defined to include all other Filipino citizens, thereby including Euro-

TABLE IV
THE DISTRIBUTION OF CORPORATIONS BY TYPE OF OWNERSHIP AND INDUSTRY

Industry	Total	Foreign		Domestic	
		Subsidiary	Non-Subsidiary	Filipino	Chinese-Filipino
A. Food, beverages & tobacco	80	16	11	32	21
1. Dairy products	4	3			1
2. Sugar	20		5	15	
3. Flour	6			4	2
4. Other foods	18	7		3	8
5. Beverages	4	3			1
6. Liquor	6		1	4	1
7. Tobacco	12	1	3	1	7
8. Copra	10	2	2	5	1
B. Textiles	34	2	3	16	13
1. Textiles	31	1	3	14	13
2. Industrial textiles	3	1		2	
C. Chemical	50	28	2	14	6
1. Petroleum	4	4			
2. Paint	6	1	2	2	1
3. Fertilizer	3			3	
4. Drugs	14	12		1	1
5. Soap & cosmetics	5	3			2
6. Batteries	3	1		2	
7. Matches	2	1		1	
8. Others	13	6		5	2
D. Metal fabrication	25	5	2	7	11
E. Household appliances	11	3	2	5	1
F. Machinery & equipment	17	6	1	7	3
1. Gen. machinery & equipment	7	3	1	3	
2. Transport	10	3		4	3
G. Others	37	5	2	19	11
1. Paper & paper products	11	2		4	5
2. Rubber	7	3			4
3. Glass	3		1	1	1
4. Cement	9			9	
5. Construction materials (not classified elsewhere)	4		1	2	1
6. Animal feed	2			2	
7. Others	1			1	
Total	254	65	23	100	66

peans and Americans who have acquired Filipino citizenship. Foreign corporations are divided into "subsidiary" and "non-subsidiary" categories. A subsidiary corporation is one owned by a foreign corporation engaged in a related line of business. Corporations controlled by foreigners whose primary business is in the Philippines are included under the heading non-subsidiary. These latter operations are owned mostly by Chinese, Spaniards, and Americans who were either

born in the Philippines or who have lived there for a long time.

The existence of non-subsidiary foreign corporations reflects the colonial experience of the country. Chinese were brought by colonial rulers to the Philippines to act as middlemen in economic transactions and to help the economy run smoothly. Many have stayed on in the country since the Philippines gained independence but have not obtained citizenship. The Spanish first came to the country as rulers, and many decided to remain when the Philippines became an American colony. Probably out of pride, many chose not to become Filipino citizens. Americans came at the end of the nineteenth century. Under American control, Americans had more privileges and rights than Filipinos and other nationalities. After independence, they remained the most privileged foreigners. In the economic sphere, their rights and privileges are the same as those of Filipino citizens. They control various lines of business in the country.

Among the 254 corporations treated here, 88 are foreign owned. These 88 corporations are spread over different areas of the manufacturing sector. The flour milling, animal feed, and cement industries are the few areas where foreign controlled corporations are absent. There are more foreign than domestic corporations in the dairy, petroleum refining, drug, soap and cosmetic industries. All corporations engaged in the refining of petroleum are foreign owned.

Among foreigners, Americans are dominant: of eighty-eight foreign corporations, sixty-seven are American owned. This dominance is related to the "special" relationship between the two countries in this century.

The Philippines were ceded to the United States with the defeat of the Spanish in the Spanish-American War at the end of the nineteenth century. The American period lasted until 1946, interrupted only by the comparatively brief Japanese occupation. Although the postwar period has not been a colonial period, the Philippines extended to Americans rights and privileges enjoyed only by Filipinos. This is the parity clause in the U.S.-Philippine trade agreement which necessitated an amendment to the Philippine Constitution. According to the clause, no law can give Filipinos any advantage not afforded to Americans. This clause has provided a favorable political environment for American business.[5]

Some American corporations came to the Philippines before the Second World War, but the majority came afterwards. This was partly in response to the trade and exchange restrictions imposed by the Philippine Government. Starting in the early 1950s and lasting until 1962, the country was under exchange controls. Imports were available only to those who received exchange allocations. Thus, American corporations which had been exporting their products to the Philippines

[5] Another advantage for Americans has been the investment guarantee program run by the Agency for International Development of the U.S. Government (now administered by the Overseas Private Investment Corporation). This program provides insurance for the loss of investment funds due to expropriation and exchange restrictions. Thus American investors are assured that they can convert local currency into dollars and that they will run little political risk. This insurance is provided for a premium of less than 1 per cent of the guaranteed coverage. The insurance program may not play a crucial role in determining investment, but it does help in eliminating a large part of the uncertainty facing an outside investor.

faced the possibility of losing the Philippine market. They had to choose between losing the market or setting up subsidiaries in the country. Since American companies did not want to risk a large amount of capital, and because Philippine trade and exchange policy discouraged the importation of "unessential" consumer goods and placed priority on the import of component parts and raw materials, American investment in assembly and packaging firms became a fixed pattern.[6]

Not all American investment in the Philippines can be explained in this way. Some subsidiaries were set up to supply processed goods to the parent company. Some would have been established irrespective of Philippine trade and exchange policy whenever the export of finished goods would not pay or whenever manufacturing proved more profitable abroad. A large number of American corporations set up in the postwar period, however, were designed to import parts and raw materials from the parent company and assemble or package them for the Philippine market. Under the commercial and exchange policies of the postwar period, this investment offered an alternative to the export of commodities. This type of investment did not, of course, contribute to Philippine foreign exchange earnings.[7]

What is surprising is that only one corporation of the 254 is controlled by a Japanese firm. Japan's economic relations with the Philippines began late in the postwar period. Recently Japan exceeded the U.S. in the total amount of external trade with the Philippines. Japanese products are found in abundance in department stores and super-markets, and billboards displaying Japanese brandnames are ubiquitous. Yet there is only one corporation controlled by Japanese, and it does not even produce for the Philippine market; it processes raw materials which are sent back to the parent Japanese company. Thus there are no Japanese-owned corporations or subsidiaries producing goods in the Philippines for the domestic market. Rather, Japan's business interests take the form of commodity trade, licensing, and joint ventures with minority equity participation.[8]

It is commonly believed that Japanese investment will increase if the Treaty of Amity, Commerce, and Navigation between the Republic of the Philippines and Japan is ratified by the Philippine Congress. The Treaty was negotiated in Tokyo in 1960 and passed by the Japanese Diet but has not been ratified by the Philippines. This belief in increasing Japanese investment in the future is

[6] This pattern was first pointed out by B.G. Bantegui in [1].

[7] The possibility of setting up efficient firms using technologies available in developed countries is not very promising. Developed countries have a large domestic market, and their industrial technology is often oriented to mass-production. Furthermore, a large number of skilled workers are often required. Underdeveloped countries have neither large domestic markets nor large numbers of skilled workers. As a consequence, foreign manufacturing in underdeveloped countries tends to be a half-hearted operation.

[8] As of June 30, 1970, direct Japanese investment amounted to $11.3 million and went to twenty-four Philippine corporations. A large part of the $11.3 million was invested in the mineral and mineral processing industry. More recently, however, several Japanese firms have begun joint ventures in the manufacturing sector. These firms are Aji-no-moto (26.7), Matsushita Electronics (40), Toshiba (31.2), Hitachi (30), and Teijin (40), where the number in the parentheses indicates the percentage of shares held by the Japanese corporation.

often misinformed.[9]

For Filipinos, Japan was the enemy during the Second World War. There were no diplomatic relations between the two countries until 1956 when the Philippines ratified the San Francisco Peace Teraty. In 1958 the trade protocol was signed upon which the present economic relationship between the two countries is based. There is no Philippine law against Japanese business operations. Japanese receive the same treatment as that accorded other foreigners except Americans.

If there is any advantage for Japanese business in getting the presently pending treaty ratified, it would lie in the legal clause which states that the trade protocol can be terminated with six months notice; this would take three years in the case of a treaty. The likelihood of termination in such a case, however, is remote.

V. DOMESTIC CORPORATIONS

Filipinos own 166 of the 254 corporations in our survey. The existence of a Filipino majority seems to refute the allegation that the economy is dominated by foreigners. Of the 166 corporations, however, 66 are owned by Chinese who have acquired Filipino citizenship. Many Filipinos say of them, "Filipino by citizenship, Chinese at heart" and do not consider them real Filipinos.

The majority of immigrants from China and their descendants, whether they have acquired Filipino citizenship or not, keep their "Chineseness" and do not intermarry with other nationalities. Since they carry Chinese names and look distinctly Mongolian, there is no problem identifying them. We therefore considered all Filipinos with Chinese names to be Chinese-Filipinos. In countries such as the Philippines, however, where there are many *mestizos* of mixed blood, it is sometimes difficult to determine whether or not a person is Chinese-Filipino or not. Some Chinese want to become assimilated to Philippine society and therefore adopt non-Chinese names or intermarry with Filipinos. Others, however, observe Chinese customs and traditions and belong to the Chinese community. A non-Chinese name may have been adopted in many cases to escape harassment rather than to become integrated into the society. Several people in this latter category were listed in our survey; we based our classification of their "nationality" on their degree of closeness to the Chinese community.

If Chinese-Filipino corporations are excluded, the number of Filipino corpora-

[9] The fact that there is no commercial treaty between the two countries may have an adverse psychological impact on potential Japanese investors, but the ratification of the Treaty by the Philippines would not necessarily bring about a large increase in Japanese investment. The extent of Japanese investment is partly dependent on how Japanese corporations take to joint ventures with minority shares. According to Republic Act 5455, approved in 1968, which regulates all direct foreign investment and operations as long as foreign equity does not add up to more than 30 per cent of the total (40 per cent in the preferred area), the joint venture does not need prior governmental authorization. Under the present policy, majority foreign equity holdings are unlikely to be approved except in the preferred pioneer area where the enterprise produces a new product or uses an important new process. Even here, however, foreign equity must be reduced to less than 40 per cent within twenty years. To date, no Japanese firm has entered the pioneer area.

tions is reduced to 100. These 100 corporations cover the range of Philippine industries. Industries dominated by Filipinos are sugar, liquor, textiles, fertilizers, batteries, cement, and animal feed. These industries are all capital intensive except for liquor and batteries. This gives rise to the hypothesis that the amount of invested capital, on the average, is highest for Filipino corporations. This hypothesis is supported by the fact that industries which require a large amount of capital also need political connections—and politics are monopolized by Filipinos. The Government had large investment funds and can guarantee loans from international agencies. A large part of government funding comes from reparations payments from the Japanese Government which average roughly $28 million a year. Funds also come from the sale of P.L. 480 agricultural surpluses. Those with political connections are able to take advantage of these funds since decisions on who receives government loans or guarantees are largely political. In all underdeveloped countries where capital is scarce, capital intensive industries seem to be closely associated with politics.[10]

Some of the 100 "Filipino" corporations are under foreign management or have a substantial amount of foreign investment. Corporations with foreign minority shareholders are treated in this paper as being domestic, but their control (in terms of who determines corporate strategy) may be in the hands of foreigners. Passive Filipino stockholders and those who follow policies mapped out by foreigners are sometimes referred to as "our kind of people" by foreign executives; Filipinos call them "dummies." Foreigners can control corporations even with a minority of shares if they can find enough of "their kind fo people." Going through the lists of stockholders which were available to us, we found that about 15 out this group of 100 corporations were managed completely or to a considerable extent by foreigners. This reduces the number of Filipino controlled corporations to about 85, but since we could not examine the stockholders of all corporations, 85 may be considered the maximum number of corporations owned and managed by Filipinos.[11]

[10] The following quotation makes a similar observation on the importance of political acumen in Philippine business operations. ". . . in the Philippines . . . entrepreneurs have been recruited from the political dominant cacique class and . . . their success as entrepreneurs is highly dependent upon their skill in combining political acumen with entrepreneurial initiative. Their viability as businessmen frequently was more dependent upon their capacity to manipulate politically factors influencing the distribution of credit and foreign exchange resources, than upon their skill as managers and entrepreneurs." [6, p. 451]

[11] We determined the nationality of stockholders and executives on the basis of their citizenship, but some of those we classified as foreigners identify strongly with Filipino society and culture. Also, many Filipinos are reluctant to identify their corporations as foreign. For example, about a dozen corporations are managed by Soriano y Sia. Soriano y Sia is operated by Andre Soriano, Jr. and Jose Maria Soriano, the sons of the late Andre Soriano, Sr. They are ethnically Spanish, but following the Second World War, they acquired United States citizenship; many Filipinos consider them Filipino entrepreneurs rather than American. The fact that Soriano enterprises are publicly held corporations may also add to the comparative mildness of the nationalistic feeling directed against them. Such feelings are usually directed most intensely towards American corporations.

In hopes of eliminating foreigners, particularly Chinese, from retail businesses, Filipinos passed a retail nationalization law. In spite of the law, they were still unable to break into the retail business. Control of the commercial network of the country remains in the hands of the Chinese community. Filipinos fare better in the manufacturing sector, but not by much. They control and manage about 35 per cent of the 254 largest manufacturing corporations. Although they control national politics, they are doing poorly in the economic sphere which piques the pride of Filipino nationalists.

VI. THE RATE OF RETURN

A Filipino businessman is quoted as saying, "A 25 per cent annual return on investment in the Philippines is considered a minimum; a 35 per cent return ordinary; a 50 per cent return far from unknown" [8, p. 6]. Since capital is scarce in underdeveloped countries, one would expect the rate of return on invested capital to be higher than in developed countries. This view is partially supported by the high interest rates on deposits and loans. A 10 per cent annual interest rate is not particularly high in the Philippines. Since invested capital involves risk, a rate of return reflecting the risk factor is necessarily higher than the normal interest rate. The above quotation is no off-hand exaggeration.

Table V, however, would seem to indicate the contrary. This table shows the

TABLE V
THE DISTRIBUTION OF THE RATE OF RETURN TO NET WORTH

Rate of Return (%)	Foreign		Domestic	
	Subsidiary	Non-Subsidiary	Filipino	Chinese-Filipino
Loss	7	0	25	4
0 – 5.0	2	5	20	16
5.1–10.0	5	3	10	17
10.1–15.0	8	3	19	11
15.1–20.0	9	4	10	5
20.1–30.0	9	6	12	7
30.1–50.0	15	1	2	5
Over 50.0	10	1	2	1
Total	65	23	100	66
Median (%)	21.5	15.3	7.5	8.9
Maximum (%)	297.3	55.1	57.2	51.6

distribution of the rate of return for our four groups of corporations: subsidiary, non-subsidiary, Filipino, and Chinese-Filipino. Rate of return is defined as the ratio of net income to net worth. Net income is profit after corporate income taxes inclusive of dividends on preferred stocks. Net worth is the sum of paid-in capital and accumulated surplus. The median rate of return is 21.5 per cent for the subsidiary group, 15.3 per cent for the non-subsidiary one, 7.5 per cent for the Filipino group, and 8.9 per cent for Chinese-Filipino corporations. None of

these exceed the 25 per cent stated as the minimal rate of return by the Filipino businessman. Corporations which earned the "ordinary rate of return" of 35 per cent were at most 15 per cent of the whole in 1968.

It may be argued that our choice of the year 1968 is arbitrary. Since the year was not a depression one, however, and was normal in several other respects, there is little possibility that the picture would change radically for other years. This is partly supported by Castro's study [4, p. 190]. He computed the rate of return for mining, agriculture, and manufacturing during the period 1955–62 and found that none of these sectors exceeded a 25 per cent rate of return. The maximum was 23 per cent for the mining sector.

A rate of return of 21.5 per cent for subsidiary and 15.3 per cent for non-subsidiary businesses may not be as high as originally expected, but it can be accepted as a reasonable return. The return rate is higher than that of domestic corporations due largely to superior management, marketing know-how, and technology. These are well advanced in highly developed countries where a high return rate reflects not only the return on capital but also the effect of the intangibles brought in from abroad. One reason a corporation seeks direct investment in another country is to further utilize costs already expended on research and development.

According to Table VI which shows the rate of returns by industry and ownership, the average rate of return for foreign subsidiaries exceeds 30 per cent in the following industries: dairy, beverages, drugs, batteries, matches, household appliances, and general machinery. For foreign non-subsidiaries, there is no industry in which the rate of return exceeds 30 per cent; only the copra industry comes close to this figure. There are, however, industries in which foreign companies do not earn a good return. In the tobacco industry, for example, foreign subsidiaries earned returns of only 2.7 per cent; for copra and paper products, there were as many companies which lost money as recorded positive returns. In the case of industries producing paper products, however, the divergence between two foreign subsidiaries was large: one company had been losing money for the past few years, whereas the other earned returns of over 30 per cent. Both are well-known American firms. Another thing we should note in Table VI in connection with foreign corporations is that the petroleum refining industry, which is monopolized by foreign companies, is not doing particularly well. Their average return of 9.9 per cent is not low but much less than one would expect for such big international companies.

It is hard to ask in meaningful terms whether foreign corporate earnings are too high since it is difficult to ascertain what a reasonable rate of return is, but emotion runs high on this issue. Filipino nationalists feel that foreign companies are withdrawing too much from the country by way of high returns. When we examine Table VII showing the rate of returns to paid-in capital, the difference in earnings between foreign and domestic corporations becomes more pronounced. Foreign subsidiaries in one year earn a full one-third of the amount of capital originally brought into the country. A high rate of return is a reward for superior

TABLE VI

THE RATE OF RETURN BY INDUSTRY AND OWNERSHIP (Median) (%)

Industry	Total	Foreign		Domestic	
		Subsidiary	Non-Subsidiary	Filipino	Chinese-Filipino
A. Food, beverages & tobacco					
1. Dairy products	38.4	43.6			9.2
2. Sugar	13.4		16.4	10.8	
3. Flour	5.2			5.2	
4. Other foods	11.0	13.1		4.7	8.5
5. Beverages	45.4	58.3			32.3
6. Liquor	16.7		16.4	22.8	8.7
7. Tobacco	15.8	2.7	16.7	49.6	14.3
8. Copra	10.5	0.0	29.0	10.5	6.0
B. Textiles					
1. Textiles	3.1	11.5	3.1	Negative	9.0
2. Industrial textiles	15.2	11.1		19.7	
C. Chemicals					
1. Petroleum	9.9	9.9			
2. Paint	17.5	15.9	19.6	0.0	21.6
3. Fertilizer	Negative			Negative	
4. Drugs	28.5	30.3		16.0	28.3
5. Soap & cosmetics	19.8	19.8			15.5
6. Batteries	12.5	32.8		10.2	
7. Matches	25.0	36.6		13.4	
8. Others	12.0	16.5		16.4	0.0
D. Metal fabrication	7.5	16.0	7.2	7.9	4.8
E. Household appliances	13.0	33.3	24.7	3.1	3.3
F. Machinery & equipment					
1. Gen. machinery	11.3	34.1	5.6	5.9	
2. Transport	14.1	15.1		15.2	13.2
G. Others					
1. Paper & paper products	9.5	0.0		6.9	9.6
2. Rubber	11.1	28.4			9.4
3. Glass	10.8		12.9	10.8	6.7
4. Cement	5.1			5.1	
5. Construction materials (not classified elsewhere)	14.8		14.3	9.6	20.3
6. Animal feed	0.0			0.0	
7. Others	Negative			Negative	
Total	11.5	21.5	15.3	7.5	8.9

Note: 0.0 indicates that as many corporations lost money as recorded positive returns.

know-how and entrepreneurship; however, without attaching a stigma to it, one can legitimately question whether it is not reasonable to regulate the overseas remittance of profits and to force corporations earning high returns to use a part of their earnings for domestic social development.

Returns for domestic corporations seem too low. Witness the 7.5 per cent rate

TABLE VII
THE RATE OF RETURN TO PAID-IN CAPITAL

Rate of Return (%)	Foreign		Domestic	
	Subsidiary	Non-Subsidiary	Filipino	Chinese-Filipino
No information	3	0	0	0
Loss	7	0	25	4
0 - 5.0	2	3	20	14
5.1–10.0	1	4	8	15
10.1–15.0	3	1	10	7
15.1–20.0	4	3	10	9
20.1–30.0	9	6	9	7
30.1–50.0	12	4	9	8
Over 50.0	24	2	9	2
Total	65	23	100	66
Median (%)	32.8	21.8	8.7	9.7
Maximum (%)	720.0	184.6	118.6	81.4

of return for Filipino and 8.9 per cent rate for Chinese-Filipino corporations. These figures appear low, not so much out of comparison with the return rate of foreign corporations, but simply because the interest rate on time deposits apparently is higher than the return on invested capital. Capital would here appear to earn more money in banks than in corporations.

In cases of disequilibrium, the return on invested capital can be theoretically lower than the interest rate, but the real reason for this situation in the Philippines is that the financial statements from which we computed the returns are not reliable. Most corporations are owned by a single family or a small number of closely related families. A corporation is not a purely economic institution whose sole aim is to maximize the rate of return. Its main purpose is to increase the welfare of family members. The rate of return in Philippine manufacturing corporations cannot therefore be strictly compared to that of developed countries where management and ownership are separate.

One factor resulting in a low rate of return is the unnecessary expenditure often lavished on family members occupying high positions in corporations. This often includes foreign travel once or twice a year, large salaries for wives and other family members, expense accounts for automobiles, food, restaurants, and night clubs, as well as expenses for prestige items not strictly needed for business transactions such as helicopters and airplanes. These expenses must be added to earnings when comparing the rate of return with interest rates.

A second factor is the under-reporting of earnings. This is illegal, but investigation by the Bureau of Internal Revenue is often lax and besides, there is a tremendous incentive to under-report profits. The corporate income tax rate is roughly 30 per cent which is low when compared with the rate for developed countries. Many Filipino businessmen try to pay as little tax as possible. Although this may be true of all nationalities, in developed countries such offenders may be caught and have to pay a heavy penalty, but such a possibility seems unlikely in

the Philippines. If an offender does pay, the money goes to the political friend who saves his neck.

These factors reduce the reliability of the rate of returns shown in Table V and contribute to the low rate of return for domestic corporations. Foreign corporations are less likely to under-report earnings, and their unnecessary costs also seem to be much smaller. But foreign corporations may resort to legal maneuvering to maintain or enlarge remittances to the parent company. As pointed out earlier, they exist in order to provide increased sales to the parent company, so they often resort to a variety of procedures to make this possible. It does not matter whether the rate of returns in the Philippines is low or high; subsidiaries can be sacrificed for the benefit of the parent company. If the remittance of profits is difficult owing to government restrictions or to a high tax rate, they can afford to reduce their profits in the Philippines as long as it does not injure the interests of the parent company. If a corporation is set up to supply raw materials to the home country, it can underlist export prices in order to reduce its paper profits in the Philippines. If a subsidiary buys raw materials and parts from a parent company, such items can be overpriced so that the profits of the subsidiary business decline, in effect draining would-be profits out of the country.

"One large U.S. manufacturer, for example, concedes that it penalizes some of its overseas subsidiaries for the good of the total corporation by forcing them to pay more than necessary for parts they import from the parent and from other subsidiaries. Says one of the company's executives: 'We do this in countries where we either anticipate or already face restrictions on profit repatriation. We want some way to get our money out.' " [9] Foreign subsidiaries which are losing money or have a low return may resort to such operations.[12]

Figures should be interpreted with care. The 7.5 per cent rate of return for Filipino corporations and 8.9 per cent rate for Chinese-Filipino corporations may be fictitious. One important question is raised, however, by Table V. Even if the median seems low, is it not possible that there are many corporations which are inefficient and which should eventually be phased out? There are twenty-five Filipino and four Chinese-Filipino corporations listed which lost money and twenty Filipino and sixteen Chinese-Filipino Corporations listed which had less than 5 per cent earnings. Even if we take into consideration under-reporting and unnecessary costs, there seem to be a number of corporations which can be considered potential failures.

We cannot offer a good explanation for the losses and low returns in Chinese-Filipino corporations, except to note the possibility that the scope of their under-reporting is considerably greater than that of Filipino corporations. This cannot be substantiated by evidence, however. For many Filipino corporations, these losses or low returns seem to be genunie. Many companies which lost money are in capital intensive or crowded industries. As shown in Table VI, the median return was negative in textiles and fertilizers, whereas the median was only 3.1

[12] For the practice of under-pricing canned pineapple, see [5, pp. 146–47].

per cent for household appliances and 5.1 per cent for cement.[13]

Textiles and cement are political industries in the sense that, being capital intensive, owners obtain large loans from government financial institutions or from the Reparations Commission. Such money is given to the friends of politicians or, at least, is secured through politicians. In the case of textiles, the major raw material is cotton which is sold to the Philippines by the U.S. under P.L. 480. Cotton is allocated to textile manufacturers by a government agency in charge of the program; who gets what amount is mainly a political decision.

Cement and household appliances are faced with the same problem: the market is crowded. There are nine cement and eleven appliance companies in our list. If we add smaller corporations, the number becomes larger. Two cement corporations suffered losses and two more earned only 1 per cent on invested capital in 1968. In appliances there were only two Filipino corporations which earned more than a 10 per cent return; the rest either suffered losses or earned returns of less than a 3 per cent.

Most industries with a low rate of return were set up in the postwar period. The Government apparently had no consistent policy to regulate or give assistance to the private sector. As a consequence, there are many corporations whose utilization of capital is at a very low level owing to too much competition.[14]

It may be unfair to say that no one in the Government realized the grave consequences of too many corporations being set up in the same industry. If anyone did, however, he was overriden by superiors who had something to gain from establishing new firms. Private gain seems to have been larger the greater the amount of capital involved. It was therefore in the interest of politicians to establish as many firms as they could. Gain was not solely restricted to them, however. Incorporators also profited and gains were sometimes so large initially that there was no strong incentive to make a firm a going concern. When machines were bought from foreign sellers using government loans or reparations money, kickbacks were demanded which sometimes amounted to considerable sums. Business would be carried out up to this point and indifference was felt about the future of the corporations involved.

VII. LICENSING AGREEMENTS

Corporations can enter the foreign market by any of three methods. One way is to export a commodity produced in the home country to the foreign market.

[13] In 1968, the median of fixed assets was 4.4 million pesos for foreign subsidiaries, 3.3 for foreign non-subsidiaries, 8.4 for domestic Filipino, and 4.6 for domestic Chinese-Filipino corporations. Among domestic Filipino corporations, the textile, cement, fertilizer, and sugar industries were capital intensive; the median was 21.2 million pesos for textiles, 31.3 for cement, 22.9 for fertilizers, and 15.0 for sugar.

[14] In underdeveloped countries where capital is scarce relative to labor, it is natural to expect that its utilization rate be high. In capital intensive industries in these countries, however, the utilization rate is low. This is because a large part of the capital used to purchase machinery is obtained at low interest rates from governmental or international financial institutions.

Another way is to set up a subsidiary in a foreign country to produce the same commodity for the foreign market. The third way is to find a foreign company which will produce the company's commodity and to receive payments in the form of royalties and fees for the technical skills, marketing, management know-how, and trademark rights granted to the company. A corporation which wants to increase its sales in a foreign market has to choose the best alternative under a given set of circumstances.

When the third method is chosen, licensing agreements are drawn up between two corporations. The licensee produces a commodity taking advantage of the rights granted, and the licensor abstains from exporting the commodity to that country's market. This may be the fastest way to get into a foreign market or to enter a market too small to justify larger investment. Most staffing problems are avoided this way, and advantage can be taken of the licensee's sales capabilities and relations with local governments. This may be better than direct investment for small and medium-size companies whose capital and managerial staffs are limited, but for multinational corporations which are moving aggressively into an overseas market, a subsidiary may be preferable.

There are three government agencies in the Philippines which have information on licensing agreements: the Patent Office, the Central Bank, and the Board of Investments. None of these agencies had complete information on licensing in the early part of 1971 when this research was conducted. The number of licensing agreements registered in the Patent Office is small. We have cause to believe, from information gained from other sources, that most licensing agreements entered into by corporations are not to be found on the books recording such agreements. Patents and trademarks are registered in the Patent Office to protect such rights, but the registry of a licensing agreement evidently does not offer much legal advantage. The Board of Investments has information on licensing agreements of those corporations registered to take advantage of tax incentives, but most of our 254 corporations do not appear in the list of registered enterprises. The Central Bank should have the most comprehensive information on licensing, but from 1962 to 1970 there were no foreign exchange controls, so there was no need for Filipino licensees to provide the Central Bank with copies of their agreements in order to obtain foreign exchange. Since foreign exchange is now once again under government control, corporations will need foreign exchange to pay for royalties and fees, so they will eventually have to supply supporting documents such as licensing agreements to the Bank. At the time of our research, the Central Bank was the ideal place to obtain this information, although we were told that the information was incomplete. Access to corporate files at the Bank was not granted, however, and the study had to rely on other sources. One source of information was the financial statement submitted to the SEC. Another was a report by the UNCTAD secretariat on restrictive business practices.[15]

In the financial statements submitted to the SEC, items such as royalty and

15 [11] incorporates Finance Secretary Virata's report on the Philippines.

technical service fees are included. For 154 of the 254 corporations, we were able to determine whether such payments were being made by examining their financial statements. For the remaining 100 corporations the statement is consolidated, and it was not clear whether such payments were being made or not. Of the above 154 corporations, 35 were paying either royalties or fees.

Surprisingly, eleven out of the thirty-five corporations paying such royalties or fees were subsidiaries. Since a subsidiary is set up with the capital and most or all of the intangible assets of the mother company, there would seem to be no need to draw up a licensing agreement stipulating the terms of payment. Apparently this is often done in underdeveloped countries, however, as a precondition for defending patent and trademark rights against third parties, for tax purposes, or on account of foreign exchange regulations [11, p. 33]. In the Philippines, however, the tax on royalties is 30 per cent which is about the same as the corporate income tax rate. Therefore, there does not seem to be any tax advantage which would motivate a subsidiary to enter into a licensing agreement paying royalties to the parent company. Tax advantage is to be found, instead, in obtaining payment as a technical service fee rather than as royalty, for there is no tax on the former. The eleven subsidiaries mentioned above paid 4.4 million pesos in royalties and 2.4 million pesos in technical service fees for a total of 6.8 million pesos in 1968.

The remaining twenty-four corporations paid 22.6 million pesos in royalties and 0.7 million pesos in technical service fees for a total of 23.3 million pesos. The total amount of payments made by the thirty-five corporations was 30.0 million pesos, equivalent to $7.5 million. Since total national imports for the Philippines in 1968 were $1.133 billion, Government foreign expenditures nearly $21 million, and other invisible payments $676 million, the total royalty payment of $7.5 million seems to have been only a small part of total foreign exchange payments.

Large subsidiaries tend to make consolidated financial statements, so they might include large amounts for royalties and fees. These are alternative forms of profit remittance, however, and do not particularly concern us here. What we are really interested in are payments made by domestic corporations. For these corporations, however, payments do not seem to amount to a large sum.

Of the above twenty-four corporations, six are in cigarettes, four in household appliances, three in paints, three in food, two in synthetic textiles, one in batteries, one in drugs, one in flour, one in cosmetics, one in the match industry, and one in the metal fabrication industry. As pointed out above, the royalties and fees for these twenty-four corporations amounted to 23.3 million pesos. Among the twenty-four, only two are in intermediate industries not involving foreign brandnames. Their payments were for patent or know-how rights, and the payments amounted to only seven thousand pesos. The other domestic corporations paynig substantial amounts in royalties or fees are involved with foreign brandnames and can be readily identified by examining the brandnames of domestic corporations.

Of the 189 non-subsidiary corporations in our list of 254, 35 use foreign brand-

names. Eight are in household appliances, six in tobacco, four in transport, four in paints, three in flour, two in food, two in synthetics, two in liquor, one in drugs, one in batteries, one in chemicals, and one in cosmetics. One brandname in food, two in transport, and two in household appliances are Japanese; most of the others are American.

The largest royalties were paid by the cigarette industry followed by the flour industry. The only industry for which there was no indication of royalties was transport machinery. Of the four domestic corporations assembling cars or motorcycles, two gave detailed financial statements, and two gave consolidated ones. According to the two detailed statements, the corporations did not pay royalties. There are probably no royalty payments under licensing agreements in the transport machinery industry. This raises the question, then, of what accounts for the fact that some industries use foreign brandnames without making any payments while others make payments?

In the case of both the cigarette and the flour industry, raw materials are not purchased from the trademark owner. The cigarette industry blends domestically grown tobacco leaves with imported Virginia leaves. Flour millers use imported wheat. Virginia tobacco leaves and wheat, however, are sold to the Philippines by the U.S. government under P.L. 480 and are not supplied by the brandname owner. Therefore the only way the owner of a brandname can be paid in such cases is to receive money for the use of the name. However, in the transport machinery industry, the owner of the brandname sells parts, and there is no need for royalties if the agreement is written in such a way that the licensee is forced to buy overpriced parts. A licensor normally relies on royalty payments, then, if there is no possibility of tied purchasing. If tied purchasing is possible, the sale of parts or raw materials can be regulated to increase profits. In such cases, royalties are not necessary.

Although no royalties appear to be paid in the transport machinery industry, the household appliance and paint industries present a mixed picture. Some companies pay royalties while others do not. Among the seven household appliance corporations which use foreign brandnames, four corporations payed royalties and one did not; there is no information on the remaining two. In the paint industry, three paid royalties and one did not. This gives rise to the hypothesis that when no royalty is paid, the substitution of local parts or raw materials for imported ones is made difficult by the licensing agreement. Such substitution is probably easier if royalties are paid.

The difficulty of substituting domestically produced parts for imported ones is illustrated in the case of transport machinery by the practice of "deletion allowance." Under this practice a licensor sells in package various parts needed for assembly with the price of these parts itemized. The licensor might charge, for example, $50 for a certain part in a package deal, but if the assembler substitutes a local product for the imported part, he will get only a fraction of the $50 refunded which is often lower than the cost of local production. There is therefore no incentive on the part of licensees to purchase local parts. Many of those

who argued for setting up assembly plants in the initial stage of industrialization hoped that "backward integration" would gradually proceed and that parts would eventually be produced locally, but the "deletion allowance" does not permit such a gradual transition.

Since the Philippines are in an early stage of industrialization and need various types of assistance in the form of expertise, a question remains as to why royalties and technical service fees are of such small importance to intermediate industries. One explanation might be that Filipino corporations cannot afford to pay these fees, but this is not the whole story. There are two additional important explanations. One is purchasing tied to the provider of assistance. For example, a chemical corporation might need instruction on production processes as well as foreign technicians; these may be provided "free" if the corporation buys raw materials from the foreign company giving the assistance. These fees are included in the price of the raw materials. The second explanation is that technical expertise is wrapped up in the capital equipment provided, so that fees for patents and technical assistance are included in the price of the equipment. Technicians to maintain and repair machinery may also be provided "free" in such cases for an extended period of time.

VIII. CONCLUDING REMARKS

Many other aspects of corporations would have to be studied in order to fully understand Philippine industrialization. For example, the sociological background of Filipino entrepreneurs, the sources of industrial capital, and Philippine industrial groupings should be inquired into, but such questions must be left for future research.

Our knowledge of Philippine corporations is far from perfect. This study, however, has hopefully helped point out several problems which must be taken into consideration by Filipinos when seeking to determine future industrial strategy for their country. They would seem to be as follows. (1) Import substitution often leads to inefficiency and the misallocation of resources. What possible alternatives are there? (2) What should be the balance between import substitution and export promotion? (3) Is it not desirable to allow joint ventures with foreign majority equity in the export industry? (4) What benefits are to be gained by setting up capital intensive factories which are run most efficiently in markets far larger than any offered by the Philippines? (5) Is it not preferable to restrict the number of firms in the same industry and permit oligopolistic competition? (6) What should the treatment of American corporations be after 1974 when the Laurel-Langley Agreement expires?

Industrialization is not directed solely toward economic welfare but is pursued with a variety of goals under several constraining influences. For example, in the Philippines the strong promotion of domestic industrialization has led to various nationalistic measures. At the same time, the Philippines have a number of pressing economic problems such as malnutrition, unemployment, and a low level of income. From a purely economic point of view, free trade and capital move-

ment are the best policies for solving these problems while increasing the living standards of the country as a whole. Such policies, however, have to be modified because the Philippines, naturally enough, want to exist as a politically and culturally distinct entity. Some of the policies in pursuit of this latter goal have resulted in a slowing down of economic growth: economics alone is too imperfect a guide to determine optimum, balanced industrial planning.

We would like to emphasize that because of their rapidly growing populations, underdeveloped countries such as the Philippines do not have enough time to pursue industrialization at their own pace. Even if population growth slackens in the near future, a large number of people must still find gainful employment. To accomplish this, the country will have to become involved in international trade to a considerable extent. Success will not be accomplished by duplicating the industrial experience of developed countries. Instead, an attempt should be made to foresee the pattern of future world trade and to place priority on the development of those industries which can compete successfully in the international market.

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