

## Financing Government —(1)

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*The reformulated 1986 national budget envisions an expenditure program that will channel funds to programs and projects intended to alleviate poverty, generate employment and develop the rural and agricultural sector. The 1986 Tax Reform program will partly finance the national expenditures while a substantial portion of the wherewithal will be sourced from the external sector. The reduction of budgetary deficit, expected to reach ₱27.9 billion in 1986, remains to be the prime objective of the government and is proposed to be met through a combination of external and domestic borrowings.*

People in government need to inform the citizens of what they are currently doing in their respective positions. And on the basis of informed comments from the public, they are able to secure feedbacks and suggestions. It is also a chance for them to identify areas where further cooperation and coordination can be promoted to achieve common objectives.

The discussion will be limited to three major fiscal policy concerns of the Aquino administration:

- 1) Consistency of the national budget with the broad social and economic plans of the government;
- 2) Formulation of a comprehensive tax reform program aimed primarily at improving equity and promoting growth and efficiency; and
- 3) Reduction of the public sector deficit over the next several years to forestall any possible crowding out of private sector capital formation.

### Government Spending

A major feature of the 1986 budget, as reformulated, is its consistency with the overall economic plan of the government. Specifically, the revised 1986 expenditure program will ensure that funds will flow to programs and projects intended to alleviate poverty, generate employment, and develop the rural and agricultural sector.

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Government has to provide for agricultural projects since there is a need to develop the countryside and make agriculture and rural-based industries the springboard for creating more employment opportunities and strengthening our economy.

Government also has to provide for the people's education and health if it wants more skilled and healthy people who can better participate in productive activities.

Other areas requiring immediate provision are:

- 1) The maintenance of peace and order since industries have to flourish and people have to pursue their livelihood in a secure environment,
- 2) The salaries of government workers and the operational expenses of government; and
- 3) The adequate maintenance of roads, bridges, irrigation and other infrastructure facilities in order to reverse their sharp deterioration.

After we conducted a careful review of the original 1986 budget, we concluded it was not supportive of the government's economic recovery program. To remedy the situation, the Office of Budget and Management constituted a Task Force to evaluate the budget program and structure and make it more responsive and supportive of the new government. This task force tried to verify and analyze the original classification of activity expenditures on the basis of a previously established priority listing of activities. Additionally, another Task Force was established to identify reserves and ensure primary funding support for programs and projects that relate to the alleviation of mass poverty, the generation of employment, rural development, agri-business development, and the just equitable sharing of the fruits of development. Additional funding for these priority projects are taken from reserves imposed and expenditure cuts on projects and activities that are non-essential and/or low priority.

After reallocation and programming of expenditures, the national government has determined an aggregate expenditure level equivalent to ₱114.4 billion for 1986. With expected revenues of ₱86.5 billion, the government will be incurring a budget deficit of ₱27.9 billion. In terms of expenditure classes, current operating expenses will constitute ₱69.8 billion while capital outlays will amount to ₱14.7 billion. Net lending, representing assistance to government financial institutions as well as advances for debt service obligations of government corporations, and equity contributions to government corporations will reach ₱29.9 billion.

On sectoral basis, ₱18.2 billion has been earmarked for economic oriented activities. The large allocation for economic services is intended to reverse the continuing weaknesses in consumer demand and industrial activities which had resulted from the economic policies of the previous regime. The government will continue to repair, improve and build needed infrastructure like roads, bridges, school buildings and ports in order to facilitate transportation and mobility of essential goods and services. Similarly, a genuine land reform program supported by credit, marketing and technical assistance schemes will be implemented to open more opportunities and increase the income of the rural population.

For the social services sector, the government will spend ₱22.6 billion. The commitment to provide equitable access and opportunity to quality education will continue to be a primary concern with more than ₱11 billion channeled to education, culture and manpower development. The health, nutrition and population control subsector will endeavor to provide the basic health services through the primary health care program, while housing and community development programs shall focus on the creation of work opportunities and self-contained communities outside the crowded urban centers.

And for defense, the government will allocate ₱7.7 billion, enough to enable the armed forces to improve its operational capability and conduct civic action projects in areas where the insurgents exercise significant influence.

Summing up, the 1986 budget has been reformulated to be consistent with an economic program that provides for the start of an economic recovery in the second half of the year.

### Sources of Financing

Even as government streamlines expenditures to make them consistent with the new priorities, the sources of financing emerge as a major policy concern. Accordingly, a major tax reform program was submitted to, and eventually approved by the President. Of course, increasing the revenue yield of the tax system is only of secondary importance, the long-term structural reform measures and one-time amnesties are aimed primarily at improving equity, simplifying tax administration, and promoting growth and efficiency.

The Tax Reform program includes measures to globalize taxes on all incomes except passive incomes; raise personal exemptions under the income tax above the poverty level and provide for their future indexation, reduce and simplify business and sales taxes; abolish export taxes except on logs, and remove all tax and duty exemptions, with a few exceptions. The revenue measures increase taxes on beer, cigarettes and gambling, and raise the mini-

mum imports duty rate to 10 percent. Finally, there are amnesties on income and property taxes and repatriation of foreign assets.

It is anticipated that the tax administration measures will yield ₱5.5 billion in 1986. This non-recurring source of revenue is not even one fourth of the expected budget deficit of ₱27.9 billion. It should be noted, however, that the relative size of the expected deficit for the last three quarters of 1986 is smaller when compared to the P10 billion deficit incurred during the first quarter of 1986 — partly because of the massive election spending and also partly because of revenue shortfall.

The new tax reform program will partly finance the proposed expenditures program. A substantial portion, however, will have to come from other sources. It is expected that ₱8.0 billion of the budgetary deficit will be financed from external sources and a huge chunk of the remainder will be financed through the issuance of Treasury bills in the domestic market.

As a long-term goal, the administration will rely more on an equitable and efficiently managed tax system as a source for financing government spending. Its present reliance on external and domestic borrowing is a reflection of low tax yield associated with a depressed economy and a recognition of the time lag associated with any tax reform measure.

### Budgetary Deficit

The government is expected to incur a budget deficit of ₱27.0 billion in 1986. The proposal is to finance the deficit through a combination of external and domestic borrowings, with heavy reliance on domestic sources particularly the flotation of bills, borrowings from the Central Bank, and SSS treasury notes. The projected financing needs of ₱21.1 billion will not likely to crowd out private sector capital formation because of the substantial excess capacity in the economy.

It is important to make a distinction between the deficits in the early years of the recovery and the deficits that are projected for subsequent years. Deficits in the near term would have a positive impact on the recovery of economic activity. On the other hand, a continuing string of large deficits projected over a number of years could derail economic recovery and sustainable growth in the long run.

The objective is to achieve a sustained reduction in budgetary deficit over the next three years: 4.4 percent of GNP in 1986, to 2.4 percent of GNP in 1987, and to approximately 2 percent of GNP in 1988. The planned targets are hoped to be realized through structural reform measures designed to raise resources for the public sector at minimal cost and spend them most efficiently.

Three areas of concern have been discussed in broad terms: (1) consistency of the budget with the economic plan, (2) tax reforms to improve equity and to promote growth and efficiency, and (3) the reduction of the public sector deficit over the next several years. The government has made substantial progress in these three areas but much remains to be done.