

# ELITE POWER AND CONTROL: PHILIPPINES TELECOMMUNICATIONS SECTOR, 1940-1993

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## ABSTRACT

The political structure in the Philippines has been shaped by the desire of a small elite to maintain political and economic control by concentrating power in the executive, leaving the legislature and the judiciary relatively weak. American influence, foreign ownership and elite monopoly in this sector stalled the development. The Philippines case is particularly interesting because it provides an opportunity to study the underlying causes of success and failure in the telecommunications sector. The dynamic of power and control shows the inadequacy of the policy and domestic regulations. The article focuses on Philippine Long Distance Telephone (PLDT) and a number of other closely related enterprises. To maintain control of political and economic rents, the Philippines elite have helped shape a political structure that has stunted the development of efficient institutions for market governance and resources mobilization. The institutional failure is clearly reflected in the main characteristics of the Philippine regulatory system (Peltzman, 1976). Though the initial form of the country's regulatory institutions was borrowed from the United States, some key aspects were modified to adapt those institutions to the Philippines's political structure. The history of the telecommunications sector in the Philippines provides strong evidence that the commitment capabilities of government have had a significant impact on investment in the sector.

*Keywords: Monopoly, PLDT, political structure, economic rents, and efficient institution*

## INTRODUCTION

President Fidel Ramos in his inaugural speech in June 1992, argued that it was time to "dismantle the oligarchy whose rent-seeking elite have dominated the economy not through possession of skill at entrepreneurship or superior intelligence but through monopoly or access to political power."<sup>1</sup> The political structure in the Philippines has been shaped by the desire of a small elite to maintain political and economic by concentrating power in the executive, leaving the legislature and the judiciary relatively weak. American influence, foreign ownership and elite monopoly in this sector stalled the development. The Philippines case is particularly interesting because it provides an opportunity to study the underlying causes of success and failure in the telecommunications sector.

To maintain control of political and economic rents, the Philippines elite have helped shape a political structure that has stunted the development of efficient institutions for market governance and resources mobilization. Telecommunications was dominated by the Philippine Long Distance Telephone Company (PLDT), a

virtual private monopoly owned by a politically influential family. While there were about 60 provincial telephone companies, a government telephone system, and two international submarine cable companies before liberalisation, PLDT owned and controlled the infrastructure through which all calls passed. Through this, PLDT controlled over 95 percent of the market. Because of its monopoly position, PLDT neglected customer service and failed to upgrade its system. The National Telecommunications Commission (NTC), the industry regulator, was unable to compel PLDT to provide more phones, improve its service, or protect the consuming public from the latter's monopolistic abuses.

## **THE ELITE IN PHILIPPINES – A STRONG PATRONAGE SYSTEM BUILT BY THE US**

The Philippines became a U.S. colony in the closing years of the nineteenth century, soon after four centuries of Spanish rule had come to an end. An important legacy of Spanish domination was an open based exports of primary products by large farms, a pattern that continued under the U.S. rule. Over time, a strong patronage system arose headed by an agrarian elite with close ties to U.S. politicians and business leaders. The groups' small size, common interests and pervasive kinship network enabled it to overcome internal political and economic rivalries in the region worked to foster the economic and political dominance of this group as well, since the U.S. government was interested in establishing a political system in the Philippines that would remain stable and friendly to the United States. Through a process of negotiated independence, this elite group gradually acquired the knowledge, skills and institutions necessary to run the government and following independence in 1946, the group took control. The country's institutions reflected the dualism of Philippines society, the objectives of the U.S. government, and the elite's desire to maintain its privileges. Several features were especially prominent, such as competitive politics, qualifications control and plurality rule, dominant executive, weak judiciary, two-party system with weak, indistinguishable parties, weak constitutional restrictions on rent extraction, free trade and economic parity rights for U.S. citizens.

As part of the conditions for independence and future assistance, the U.S. government imposed a number of long-term restrictions on Philippine government policies that were intended to maintain its influence in the country (Wurfel, 1988, 14). The Philippines agreed to accept a U.S. military presence in the country and to maintain a fixed rate change and free trade with the United States (free trade was to be phased out gradually after 1954). The Philippine Congress also amended the 1935 constitution to grant U.S. business 28-year parity with Filipinos in exploiting natural resources and operating public utilities. The 1935 constitution (Fernando, 1974) had restricted these activities to Filipino-controlled enterprises. In other areas, only joint ventures were permitted with at least 60 percent Filipino equity. To preserve U.S. interests in the country, the United States offered substantial foreign aid, credit, trade and investment opportunities for the elite. This level of U.S. involvement helped make Philippine international commitments credible, providing U.S. investors in the Philippines with a sense of relative safety. The leverages also allowed U.S. politicians to mediate among the Filipino elite and thus contribute to the long-term stability of the system. As a result, the flow of foreign

investment and loans to the country was greatly facilitated (De Guzman, 1988; Gonaza, 1982; Manapat, 1991, 1993).

These basic institutional features changed somewhat over time and with them the commitment capabilities of the Philippines government. For the telecommunications sector these changes induced a pattern of stagnation and growth. As the economy parity and free trade agreements with the United States expired, the Philippines expanded its economic ties to Europe and Japan, diminishing the prominence of relations with the United States. These trends meant fewer guarantees for U.S. direct investors in the Philippines. Indeed, as time passed, U.S. businesses found it increasingly difficult to defend their interest through the legal system. An important example of this difficulty concerned interpretation of how U.S. investments made under the Parity Amendment should be handled after 1974. U.S. corporations had assumed that they could maintain their ownership over the land they had purchased before 1974, but the Supreme Court disagreed, obligating them to sell their lands by the end of 1974. However, this did not jeopardize foreign lending because loans could be more effectively backed by threat of various sanctions. As a consequence, many U.S. businesses divested their assets in the Philippines and concentrated on lending, trade and some joint-ventures (Manapat, 1991, 1993).

During the 1950s, the Philippines introduced import and foreign exchange restrictions in response to the downward trend in the relative price of primary products in international markets, large government deficits driven by the reelection concerns of incumbent presidents, and increased demand for foreign assets under exchange rate regime that resulted in foreign exchange shortages. In fact, with the consent of the U.S. government, a set of expanding import and foreign exchange controls was imposed on the economy beginning in 1950 (Wurfel, 1988, 14-15). These moves ushered in a period of import-substitution-based industrialization and the emergence of a large industrial urban working class and burgeoning middle class. These developments introduced new elements into Philippines politics that reduced the cohesiveness of the old elite and raised serious challenge to their continued rule (Wurfel, 1988: 20-22, 112-113). As education and employment opportunities improved, the non-elite populations gained greater independence. Patron-client relationships started to break down and it became increasingly costly to satisfy clients. Voters outside the political machines gained importance, and the influence of the non-elite on policy-making increased. Given the structure of the Philippine government, these dynamics intensified policy uncertainty.

As new players entered the political game, conflicts arose within the existing institutions, which had designed specifically to prevent a shift in the balance of power away from the elite. Demands for a constitutional overhaul began to build. In 1970, largely under political pressure from students, Congress voted to form a constitutional convention. The controversial re-election of President Marcos in 1969 also seems to have played a role in this decision (Abueva, 1972). By then, even the elite had grown dissatisfied with the rules of the game (Fernando, 1974) and hoped that a new constitution would correct the problems of "excessive centralization of power in the presidency and the penetration of partisan politics into every type of government decision" (Wurfel, 1988: 108).

Meanwhile, President Marcos was looking for ways to prolong his rule beyond the end of his second term in office in 1973. The increasing political turmoil, especially the formation of the constitutional convention provided him with the

opportunity he was waiting for. He lobbied for support at the convention and, using the pretext of political agitation, declared martial law in September 1972. With the strong support of the military and of members of the elite who felt threatened by the rise of the new political forces Marcos was able to suppress the opposition. His position was further strengthened by the support of the U.S. government and its allies, [ this is Marcos political trends of the early 1970s and later became a threat to their own long-term interests – US- Philippines] (Wurfel, 1988: 191-330). Congress was prevented from convening, elections were suspended and opposition political leaders were co-opted, imprisoned or exiled. Labour and peasant organisations were suppressed and strikes were outlawed.

To help legitimize Marcos's continued rule, he kept the constitutional convention open, despite the move by its members to suspend deliberations. More than a dozen delegates were arrested, and a similar number went underground or fled the country. Marcos then prevailed on the convention to pass a set of transitional provisions for the new constitution being drafted, confirming the legitimacy of all presidential orders and decrees and giving the president extraordinary powers. The new constitutions, ratified in plebiscite of dubious legitimacy, effectively abolished the old Congress and took away all forums from the opposition.

The judiciary was neutralized as well. Though the Supreme Court proclaimed that the new constitutions had not been properly ratified, it dismissed the challenge to the constitutionality of martial law, apparently apprehensive about its own survival. The two swing votes in the court feared that Marcos would claim that he could replace the members of the court following ratification of the new constitution since one of his transitional powers was the right to remove any justice by appointing a successor (Wurfel, 1988: 117). The Supreme Court ruling conferred some legitimacy on the martial law regime and Marcos moved boldly and virtually unchecked, serving as both legitimacy and executive. He prevented the Supreme Court from ruling on the constitutionality of any law by keeping a number of court seat vacant. All lesser judges had been required to submit signed resignations, which were kept on file, allowing Marcos to free himself of the constraints of the judiciary while maintaining the appearance of constitutionality (Wurfel, 1988: 133).

Martial law completely changed the institutional structure of the Philippines. A small group of the elite, Marcos's cronies, could enjoy the spoils of absolute power for an unspecified period (Manapat, 1991, Hawes, 1987). However, opposition to their rule was growing from elite and non-elite quarters alike. In search of a stable outcome, in addition to use of force, they attempted to introduce a new system of governance in which the legislature served as a new arena for political brokerage, while Marcos maintained the powers of the president and prime minister. Meanwhile, in 1978 rumours of Marcos's illness spread among the elite and signaled the possibility of an abrupt end to the existing regime (Wurfel, 1988: 234). This created a succession crisis. Wary of serious changes in their fortunes, Marcos's cronies began to act in such a short-sighted, blatantly venal that Marcos's regime collapsed long before his death.

A successful coalition of opposition political parties and personalities took control of the government in 1986. Given the relatively small size of (Manapat, 1991, Hawes, 1987) Marcos's crony group, the opposition coalition was quite diversified and span a very wide range of interests, including those of the now larger and influential middle class. As a result the new government was initially rather

unstable and the ruling coalition went through a number of realignments. The institutional structure that emerged from this process resembles that of the pre-martial law system, but with fewer restrictions on the participation of non-elite groups and more safeguards against the abuse of power by the executive. For example, the composition of Electoral Tribunals has been changed to proportional representation of parties in Congress. Also, in the case of martial law, the president is required to convene and notify Congress of the declaration (Manapat, 1991).

While politics is now more competitive and open in Philippines, the old elite has managed to maintain a large part of its control of the system. The Presidential Commission on Good Government (PCGG) created in the early days of Aquino administration to dismantle the Marcos crony system, hit major obstacles after a few months as its findings began to implicate many members of the elite still in positions of power (Manapat, 1991; Clad, 1987a, Clad, 1987b). Many of the investigations were closed and the commission failed to recover any significant part of the assets transferred abroad by Marcos and his cronies.

However, the thing to remember is that, Aquino would not have gained immediate recognition nor have been selected to run for office without her relationship to a prominent male politician. Corazon Aquino was the wife of Benigno "Ninoy" Aquino, the candidate who opposed Ferdinand Marcos and exposed his corruption. Marcos had demonstrated his abuse of power by manipulating his men to assassinate Ninoy Aquino. As the widow, Corazon Aquino was urged to run in the election against Marcos. The political party of her husband was sure that Aquino was the best candidate to defeat Marcos in the 1986 election. Not only was she seen as the victim of Marcos' corruption but "almost as a Madonna, a saint in contrast to the wily, corrupt Marcos" (Richter 1990). Yet again, Aquino expressed her disappointment and frustration towards Philippines political structure right after the failure of PCGG to dismantle crony system by saying, "...All talk of political structure is pointless if the very spirit of democracy is weak..." (Sunstar, 2006).

## **INVESTMENT AND OWNERSHIP**

Under the institutional structure of the Philippines the group in power faced in high probability of ending up on the losing side some time in the future, so its members had to devise mechanisms for protecting their assets when they were out of office (Hawes, 1987). One way was to shift from sectors with non-salvageable assets such as public utilities and to place some assets outside the country. Thus as the probability of turnover in the executive branch increased, real investment tended to fall. Another protection mechanism was to finance investment with debt rather than equity, which helped shift the risk by the original owners. Foreign debt was particularly desirable for this purpose because foreign lenders had strong leverage over the elite and default by any borrower could hurt those controlling the government (Boyce, 1992).

The relatively strong degree of enforceability of international borrowing contracts had other far-reaching effects as well. The elite group in power could borrow against the future income of the country and then invest the proceeds abroad (Boyce, 1992). Essentially, once in power, members of the elite tried to cash in as much of the country's long-term surplus as possible and then to allocate their portfolios inside and outside the country, according to expected returns. The more

the group could cash in, the more of its assets it tried to shift out of the country, fearing retaliation from future ruling groups who would be left with less to extract. However, to be able to borrow and keep assets abroad, Philippine enterprises had to make some investments at home. Thus, real domestic investment role along with foreign borrowing, but not dollar to dollar. Direct foreign investment was not as secure as foreign lending because it was more vulnerable to regulations and taxation. As a result, at the economic party agreement with the United States neared its ends, foreign investment declined. Foreign investors sought to share of their subsidiaries with the Philippines elite and limited their involvement to simple lending and contracting whenever the transfer of intangible assets was not a major concern (Boyce, 1992).

Though there were no prohibitions against state ownership, economic assets remained largely private. Private ownership of an enterprise meant the total loss of the associated surplus once the ruling group was out of power. Turning an enterprise into the group members' private property, in contrast, could help maintain the group's control over the assets and at least part of the returns. Thus many foreign-owned enterprises were 'Philippinised' but not nationalized, as similar enterprises in other developing countries had been. Philippine leaders could put pressure on foreign investors to sell assets to members of the ruling coalition rather than to the government. Also, on those occasions when the enterprises of rival groups could be expropriated or when failing domestic firms fell into government hands, the ruling coalition arranged for its members to purchase the enterprises and secure them as their private property.

Since the non-elite had no access to executive power, their investments could never be safe. As a result, ownership was highly concentrated in the hands of the elite, with most enterprises owned by families or cliques of friends. Corporate forms of ownership with widespread subscription were rare. When an elite group was in control of a corporation, its members could siphon off profits to their private accounts and leave other shareholders with little return. As a result the non-elite rarely invested their savings in corporate stocks, and the elite who invested committed very little money to corporations they did not control. Consequently, the Philippine stock market remained underdeveloped.

Under the martial law regime, incentives to invest greatly diminished for all but the Marcos cronies, who were able to acquire the enterprises of opposition members and to create investment incentives to themselves (Hawes, 1986; and Manapat, 1991). Thus lack of commitment did not reduce investment in the early years of martial law. However, investment did not rise significantly either, because the cronies understood that their rule would end someday and that when it did, their losses could be substantial. Foreign borrowing and capital flight became more important, especially after 1978. Investment finally came to a halt after 1983, when the Marcos regime entered a crisis stage, and foreign lending ceased following the assassination of the opposition leader, former Senator Benigno Aquino (Manapat, 1991).

## **IMPLICATIONS TO THE TELECOMMUNICATIONS SECTOR**

Discussion on implication to the telecommunications sector will be limited to the Philippine Long Distance Telephone (PLDT) and a number of other closely related

enterprises. To maintain control of political and economic rents, the Philippines elite have helped shape a political structure that has stunted the development of efficient institutions for market governance and resources mobilization. The institutional failure is clearly reflected in the main characteristics of the Philippine regulatory system (Peltzman, 1976). Though the initial form of the country's regulatory institutions was borrowed from the United States, some key aspects were modified to adapt those institutions to the Philippines's political structure. The history of the telecommunications sector in the Philippines provides strong evidence that the commitment capabilities of government have had a significant impact on investment in the sector.

In the telecommunications sector, the historical dominance of a small and competitive elite has become an impediment to credible regulatory policy in the Philippines. The prominent weakness is in the regulatory mechanism especially commitment to cost and investments. Some policy credibility may nevertheless exist, even in the absence of other commitment mechanisms, if opportunistic policy changes by the government would bring private investment to a standstill that imposes large costs to the government. In a country where existing investment in a sector is grossly inadequate and there is a large pool of new technology that could be imported, private operators can guarantee a minimum return on their investments, because of their ability to "punish" the government in case of adverse regulations. However, this implicit contract mechanism works effectively only in a stable environment. When the benefits of implicit expropriation fluctuate as a result of changes in the country's political or economic conditions, in some situations the government may find it worthwhile to engage in rent extraction and to jeopardize investment. Thus strong commitment is necessary to reduce the risk of such possibilities.

The international network is far more difficult to expropriate through regulatory action than the domestic network. Regulators have no control over a company's agreements with foreign operators on the settlement price of international calls. If regulators try to lower international long-distance rates for calls originating in the home country, the company can claim that it needs to collect more to pay high settlement costs. It can also limit the number of outgoing calls, forcing domestic customers to have their calls originate outside country. Revenues will then be collected by foreign counterparts and will not depend on rates set domestically. Thus, contracting problems not too much affect telecommunications firms in their international circuit investments, rather investments continue largely independent of the domestic regulatory situation.

During colonial rule, the administration depended on U.S. institutions and adhered mainly to the strategic interests of the United States in the Philippines. As a result, the danger of opportunistic policy changes was minimal, and government credibility was high. Thus, effective performance and rapid growth should be expected in this period. The basis for telecommunications regulation in the colonial period was a vague law requiring regulators to approve a "fair" rate of return on investments. A decision by the Supreme Court set the fair rate at 12 percent on revalued assets. All public utilities, including telecommunications, were regulated by a single agency, the Public Service Commission. All decisions were made by the commissioner, a centralization of authority that placed the administration in firm control of regulatory decisions (Friedland, 1988).

PLDT was franchised in November 1928 as a U.S. owned company (Friedland, 1988, Manapat, 1993), allowed to operate in a number of large cities and all intercity routes. The franchise was for 50 years and stipulated a one (1) percent tax on the company's gross receipts in lieu of all other taxes. The company soon took over many of the local telephone companies in Manila and other population centers and supplemented them with long-distance circuits. During the depression of the 1930s, the company's local service stagnated, but it continued to invest in long-distance services. Investment in local service resumed after 1934, and until 1940 the number of telephones grew at an average rate of 8.6 percent a year. The Japanese invasion during World War II destroyed most of PLDT's network. Thus, during the depression and the war, the company invested vigorously (Manapat, 1993).

### **FOREIGN OWNERSHIP AND US HEGEMONY – 1946-1959**

The continuity of pre-independence institutions, the strong leverage of the U.S., and the concession granted to US citizens provided a predictable and safe investment environment for both Filipino and U.S. businesses. These factors contributed to a stable and robustly growing economy. PLDT realized high profits and performed well under foreign ownership based on the commitment powers of the U.S. government. The U.S. army took control of the company's network in 1945 and in 1947, after some preliminary rehabilitation, control of the company was transferred to General Telephone and Electronics Corporation (GTE), a U.S. company that acquired some 28 percent of PLDT's common stock. Most of the remaining shares were held by other U.S. corporations, often as a means of portfolio diversification rather than control. The Filipino elite also acquired a small share of the company. Between 1947 and 1959, PLDT rapidly increased its fixed assets and telephones in service. The pre-war system was completely restored in 5 years and then growth continued consistently until 1959. Between 1950 and 1959, the number of the telephones in service grew 14.4 percent a year (Esfahani, 1994).

During this period the company enjoyed decent, though declining, real rates of return on its assets and equity. Telephone tariffs had been set at relatively high levels after the war to attract the investment needed to rebuild the system. Rates were then kept nominally constant throughout the 1950s, and real values eroded very slowly because inflation was low. PLDT was ensured of receiving reasonable return on its investments for several reasons. First, the U.S. influence meant that the company could count on the legal and political leverage at its disposal to prevent its profitability from failing too far below the competitive rate of return on capital. Second, the profitability of a currency devaluation, which could have hurt PLDT, was low, given the fixed exchange rate stipulated by the independence agreements between the Philippines and the U.S. Moreover, any planned devaluation would have been known well ahead of the time because of the requirement for prior U.S. approval. Third, PLDT's customers were mainly the foreigners and Filipino elite. They were concerned about the availability and quality of service, and were not interested in a confrontation with PLDT that could jeopardize service expansion at a time when there was still a great deal of excess demand. Essentially, GTE's control of technology and rate of investment allowed it to capture part, though not all, of the surplus of PLDT's operations (Manapat, 1993).



These same factors influenced of the Philippine's government forthcoming attitude in meeting PLDT's foreign exchange needs during the country's balance of payments difficulties in the second half of 1950s (Hawes, 1987). Many other businesses were rationed. This point is clearly reflected in PLDT's *Annual Reports* during those years. PLDT was even spared the exchange rate tax instituted in the 1950s to effectively devalue the peso. The government did impose some restrictions on remittances of dividends to foreign shareholders, but that was a uniform policy affecting all businesses and the fixed exchange rate imposed by the U.S. government did not restrict debt amortization, the company could easily circumvent remittance restrictions by increasing its foreign exchange debt in place of raising equity.

On the whole, U.S. influence implied ownership security, institutional continuity, and economic stability, all factors that made the investment environment relatively safe. In addition, GTE's control of technology and investment and the excess demand for telephones among the elite ensued the company that confrontation with the government was unlikely. Telephone services grew fast (GTE, 1976).

By the late 1950s, the U.S. role in the Philippines had changed, as the Philippines elite grew more independent and established new relationships around the world. The U.S. government lost its influence as a source of commitment for domestic policies. Sensing the growing weakness of the commitment mechanisms and lacking close ties to those of the government, PLDT sharply reduced its investment in the domestic telephone network during 1960-1963. A balance of payments crisis exacerbated the problem and ultimately created an open conflict between PLDT and the government when no price increase was granted despite a major devaluation in 1962. The conflict fully confirmed PLDT's perception of an impaired commitment mechanism in the new environment. Interestingly, on the international side of its operation, where commitment was not a serious concern, PLDT continued to invest without hesitation.

As a major balance of payments crisis developed in 1960s, the government negotiated with the U.S. and the International Monetary Fund (IMF) authorities on a stabilization plan (Esfahani, 1994). The IMF recommended a major devaluation and decontrol because it had not faced much foreign exchange rationing. The devaluation, however, could be very costly for the company, which depended on imported equipment and foreign capital and whose controlling shareholders evaluated their profits in U.S. dollars. Had the government committed itself to adjust telephone tariffs in line with the devaluation, the company could have gone forward with a major expansion project it had prepared in 1960. But the company had little reason to believe that prices would be adequately adjusted. Holding down public utility prices was a practical means of controlling inflation, and the government needed to keep inflation down to avoid further devaluations that could initiate its stabilization efforts.

In 1961, PLDT decided to postpone its expansion plan, even though the peso had not yet been devalued. Holding off on investment gave the company some leverage against the government. The company did not formally seek to obtain a rate increase before devaluation, but when the new administration announced a 95 percent devaluation in January 1962, PLDT and other public utilities immediately file for rate increments. Utility owners argued that they would have difficulty financing expansion projects without a rate increases (Ronquillo, 1965). The Public Service Commission was slow to respond. PLDT announced publicly that it would

not invest until a rate increase was approved (Ronquillo, 1963). The confrontational tone of the company's *Annual Report*, published in March 1962, attested to the poor relationship between the company and the commission.

Unmet demand mounted as the telephone network grew very slowly after 1960, and the company hoped that further delays in investment would incite the elite to press the government to grant a rate of increase. But the government, concerned with the failure of the stabilization plan, found the cost of satisfying the demands of public utility companies too high. The Public Service Commission was instructed to take no action on the rate increase application until further notice. The government's stabilization policies worked, and inflation remained relatively low, exports picked up and GDP grew at a reasonable rate. However, the decline of import-substitution industries and the mounting deficiencies in infrastructure soon slowed GDP growth. Finally, the weakening of the economy, the pressures generated by the shortages, and the confidence of the stability prices prepared the stage for approval of public utility tariff increases in June 1964. PLDT received a 40 percent rate increase for its local services effectively 1 January, 1965. The company immediately launched its expansion plan.

Had the owners of the major public utilities been close allies of the Macapagal administration, which took office and initiated the devaluation in January 1962, rate increases might have been granted earlier. In particular the owners of two major companies in the power and telecommunications sector was Meralco, which had been taken over from U.S. interests in 1961 by the powerful Lopez family, political opponent of Macapagal (Manapat, 1991, Bacungan, 1988; Ronquillo, 1963, 1965).

An important aspect of PLDT's investment withholding strategy during 1960-1963 was its focus on the domestic side of operations. On the international side, PLDT was eager to continue investing in joint ventures. The company's international circuit investments were generally unaffected by the kinds of contracting problems it faced domestically, and it continued such projects largely dependent of the domestic regulatory conditions. Indeed, a submarine cable project from the Philippines to Guam, with links to Hawaii and the U.S. mainland, was implemented during 1963-1964 at the height of conflict with the government. This project boosted the company's profitability during the second half of the 1960s far more than the 40 percent rate increase approved for local services. The share of long-distance revenues – in which international calls play an important role – in total revenue jumped up from less than 20 percent in 1964 to more than 45 percent in 1967 (Esfahani, 1994).

## **PHILIPPINISATION, 1964-1970**

PLDT's Philippinisation in the second half of the 1960s provides clear evidence for the deeper dynamics of elite power (Clad, 1987a). With the Parity Amendment set to expire and the absence of commitment remaining a serious problem, GTE<sup>2</sup> would sooner or later have to divest its PLDT assets (De Luna, 1986). Foreign ownership could be suggested that under the Philippine political structure, allies of the president would be able to outbid others for the divested assets and that investment would be high in the first few years, with the company relying heavily on foreign debt financing. And, since PLDT was a corporation, with a large number of passive investors, the rate of return for the stockholders would decline as those received large payoffs.

In the mid-1960s, GTE was negotiating to sell its shares in PLDT (GT&E<sup>3</sup>, 1976; U.S. Sec, 1977). The details of the ownership transfer described here became public in 1977 as a result of investigations carried out by the U.S. Securities and Exchange Commission (U.S. SEC) and GTE management. A legal case was filed in U.S. District Court in Washington, D.C. by the U.S. SEC on 12 January, 1977, against a group of Filipino businessmen controlling PLDT. The case was settled out of court, with the defendants accepting a court injunction without admission of guilt. By 1966, GTE had found a group of interested Philippines investors headed by Jose Conjuango, Jr., and negotiations reached an advantage stage. But soon after the inauguration of President Marcos, high level government officials urged GTE not to sell its interest in PLDT to the Cojuango group for political and security reasons – Cojuango had been an ally of the Liberal party leadership, which lost the 1965 election to Marcos. GTE was told to deal with another group of Philippine nationals the owners of the Philippines Telecommunications Investment Corporation (PTIC) (U.S. SEC, 1977).

The new group, led by Ramon Cojuango (Jose Cojuango's cousin), Luis Tirso Rivilla (Ramon's brother-in-law), Alfonso Yuchengo (a banker) and Antonio M. Meer (a lawyer), formed PITC to take over GTE's shares in PLDT. A deal was concluded in 1967 and a new board of directors took over in December of that year. GTE received a stake in the holding company (22.5 percent, as reported by Manapat, 1993), that enabled it to appoint one director to the board of PLDT. The terms of the contract provided that GTE's shares in the company would be bought for approximately US\$7 million in cash and US\$7 million in promissory notes (GTE, 1976: US Sec, 1977). According to Meer (Tiglaio, 1993c), the loan was guaranteed by the Development Bank of the Philippines. The notes were to be written off through a 5 to 7 percent commission on PLDT's purchase of GTE equipment "caused" by the PITC group.

The GTE was promised to pay cash commissions, amounting to US\$484,000 by 1976, to be delivered through the Stamford Trading Co., a Bahamian concern whose linkages the U.S. Security & Exchange Commission (SEC) could not be traced. The commission was paid "to provide [the buyers] with sufficient funds to pay back [the loans]. Neither the investment company (PTIC) principals nor the Bahamian company apparently controlled by them and used as a conduit for the GTE payments were expected to perform any service for GTE, the SEC suit contends" (*Wall Street Journal*, 1977). Finally, GTE provided PTIC with an option to purchase 40 percent of GTE Industries Inc., a subsidiary that manufactured telephone equipment in the Philippines. PTIC exercised the option in 1971 in exchange for a US\$486,459 "non-interest bearing promissory note payable at the rate of US\$1 [sic] per annum" (*Wall Street Journal*, 1977).

After the GTE-PTIC deal, other US and Filipino shareholders in PLDT remained by and large passive investors. The PITC group came to dominate the PLDT board and business was directed to enterprises held directly or indirectly by the PTIC group. Although President Marcos had no interest in PLDT under its new name, revelations after his departure in 1986, show that he must have had a major stake in PTIC, represented by the Cojuango family. It was found that in 1978, Ramon Conjuango and Luis Rivilla had transferred 46 percent of PTIC shares with a current market value Peso 170 million to Prime Holdings Co., at the price of Peso 6.5 million (Sison, 1986). Prime Holdings had been formed by two of Marcos's financial advisors, one of whom admitted in 1986 to have acted as Marcos front (Manapat, 1991, 353-366).

Between 1964 and 1970 PLDT experienced one of the fastest periods of growth. Philippinisation promised stronger commitment because direct government ties. GTE had a strong interest in starting the expansion early because, besides the immediate profits, a larger network and an ongoing expansion project could help GTE obtain a larger and a longer-term equipment-supply contracts, thus allowing it to share in the surplus generated by the ownership change.

Soon after the declaration of martial law, the Public Service Commission was broken up into specialized regulatory agencies. The new regulatory agency for the telecommunications sector (except radio) was the Board of Communications. This organizational reform was unaccompanied by change after its formation, the board approved a 35 percent increase for PLDT's local tariffs, supplemented by an additional 5 percent increase the following year (Manapat, 1991, Tiglao, 1988).

## **U.S CONCERN**

During the mid-1970s, the U.S. public was concerned about honesty in business and politics. In response, the U.S. Securities and Exchange Commission (SEC) began investigating business misconduct and asked publicly traded corporations to carry out internal audits about inappropriate trading practices. GTE's audit uncovered its shady deals with PTIC and in February 1976 GTE halted its arrangement with the Conjuango Group, informing them that the commission payments would stop. It also refused to pay some US\$1.7 million that the group had earned under the existing arrangements (GTE, 1976: 22). GTE, however, maintained its stake in PITC. In January 1977, the U.S. Security & Exchange Commission, filed a complaint against the PTIC group. PLDT later faced difficulty to borrow and invest while its contract with GTE were being terminated and the U.S. SEC was preparing an indictment against it (Rosenblatt, 1977). Although the case was quickly settled, the conflict with GTE continued until December 1977, when the GTE quietly "abandoned" its PITC shares (Manapat, 1993: 11-12).

The only visible improvements in the PLDT network during these years were in the number of domestic and international long-distance circuits. Many of the circuits were rented from related telecommunications companies –firms that were franchised as carriers. An important supplier for the domestic long-distance network was Domestic Satellite Philippines, Inc. (Domsat), a company chaired by Ramon Cojuango and directed by a number of well-known Marcos cronies (De Luna, 1986). The main suppliers on the international side were Philcomsat, Philippine Global Communication (PhilCom), and Eastern Telecommunications Philippines, Inc. (Eastern Telecom), all highly profitable firms owned largely by the same group of Marcos associates and front companies. They also had close relationship with PLDT (De Luna, 1986).

PhilCom began in the 1920s as a subsidiary of Radio Corporation of America (RCA), providing international telegraph and telephone services. By 1974, it was 60 percent Filipino owned, with Defense Minister Enrile's family corporation, Jaka Investments, and some PLDT directors as major shareholders (De Luna, 1986). RCA was later sold to Filipino investor. Eastern Telecom was established in 1974 by more or less the same group that had formed Philcomsat, with the British firm Cable & Wireless, holding a 40 percent stake. The verified share of President Marcos in these companies was about 40 percent of the Filipino-owned capital (Isberto, 1986). Entry

into the telecommunications sector increased after martial law. Previously, entry had been restricted because obtaining a franchise from the Congress was politically costly.

## **REGIME SHIFT**

The anti-Marcos coalition that took over in 1986 included a broad range of interests with many differences to settle. PLDT's first skirmish came less than three weeks after the inauguration and the National Telecommunications Commission ordered a 10 percent cut in PLDT's local residential tariffs "to make telephones more affordable" (Friedland, 1988). Aquino administration seemed to prefer expropriating PLDT's assets through tax increases rather than rate reductions. Philcom and Pilcomsat managed to avoid sequestration attempt as Defense Minister Enrile, participated in coalition against Marcos succeeded in retaining his post (Isberto, 1986). But Philcomsat lost its free and unregulated status and was ordered by NTC to cut rates. Other Marcos-related firms, such as Domsat and eastern Telecom, were less successful in evading penalties; the Filipino-owned shares were sequestered and new directors were appointed.

A new policy was introduced by the new regime – the National Telecommunications Plan developed by the Department of Transportation and Communications. Aquino used the development assistance funds to build telecommunications facilities in areas where they would not be in competition with the private sector.

The events of 1990-92 show the country's settled, non-authoritarian regime, entry into telecommunications sector is difficult. When Fidel Ramos took office in June 1992, he decided to support the entry of new firms into the telecommunications market and to dismantle PLDT's monopoly (Tiglao, 1993a). In February, 1993, he presided at the signing ceremony for a joint-venture between Globe Telecom of the Philippines and Singapore Telecom International, which hope to take over a big part of the market from PLDT (tiglao, 1993). Fidel Ramos reversed the decision by the Aquino on rebidding the disputed privatization projects and allowed Digitel to operate (Tiglao, 1993c). Ramos also replaced the representatives of the PCGG on the board of the PTIC and PLDT. PLDT was financially hard pressed.

## **CONCLUSION**

The political structure in the Philippines has been shaped by the desire of a small elite to maintain political and economic by concentrating power in the executive, leaving the legislature and the judiciary relatively weak. The regulatory system in the Philippines is weak and ineffective and lacks specific and transparent rules due to the same forces that have weakened the judiciary. With the elite maintaining control of the professionals who are supposed to serve as "referees," the government as an institution cannot commit itself to hold to certain policies and to rule out opportunistic regulations. This environment induces movement in the investment of telecommunications firms, characterized by short periods of expansion and long spells of stagnation. Firms grow mainly during the early years of Marcos administrations were those that have close ties with the elite. The close elite ties is also obvious in the Philippine before Marcos for example the late Diosdado Macapagal, who led the Macapagal administration, took office and initiated the

devaluation in January 1962, was the father of the current President Gloria Arroyo-Macapagal. And this family, is the opponent to the Lopez family; owner of Meralco Telecommunications.

The most fundamental way to bring about improvements in the Philippines regulatory system is to shift the balance of power towards the legislature and the judiciary, institutions with inherently greater stability and continuity than the executive branch. A number of important reform opportunities emerged under the new political coalition after the fall of Marcos. Many coalition partners had strained relationships with the telecommunications firms after the installation of the new coalition. Other than role played by the local elite, the early years of the telecommunications and communications sectors in the Philippine also shows a greater role of the United States. However, the United States uses its hegemony and structural power to protect GTE using the SEC in New York clause and regulations.

## ENDNOTES

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<sup>1</sup> Fidel Ramos, "To win the future," inaugural address as President of the Philippines, Manila, 30 June 1992 in Fidel V. Ramos, *Developing as a Democracy: Reform and Recovery in the Philippines 1992-1998* (Hong Kong: Macmillan Publishers, Ltd., 1998), p. 4.

<sup>2</sup> During this time, the holding company, based in New York, became known as General Telephones & Electronic Corp. or GT&E Corp. In March 1970, blasts ripped through the headquarters buildings of GT&E and two other companies in New York; the terrorist group responsible was protesting the companies' participation in defense work at the height of the Vietnam War. In December 1970, GT&E announced that the company would move its world headquarters to Stamford, Connecticut. In 1971, the company adopted a new corporate symbol that became a widely recognized logo in the years to come, featuring the initials GTE placed inside a blue, rounded rectangle, and the company formally changed its name to GTE Corp. in 1982 (2006, <http://www.scripophily.net/astelcomltd.html>).

<sup>3</sup> GTE negotiated ownership transfer of shares in PLDT as a result of investigations carried out by the US Securities and Exchange Commission (U.S. SEC) and GTE management which followed by a lawsuit in U.S. District Court, Washington, D.C. in 1977.

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