

Philequity Corner (September 7, 2015)
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Promises, Promises

Two weeks ago, we wrote about the financial contagion sweeping across Asia (see *Contagion*, 24 August 2015). This started with China as its stock market crash and yuan devaluation put a spotlight on the deterioration of its economy. Many equity indices and currencies fell as the contagion spread across the globe. However, some countries suffered more than others because of corruption and populism.

Greek tragedy

Earlier in the year, before China's stock market crash, Greece roiled markets as it teetered on the edge of default. In a previous article (see *Greek Drama – The Final Chapter?*, 6 July 2015), we wrote about how the new government's populist policies drained the state's coffers, leading to the closure of banks and the stock exchange. This populist rhetoric threatened the stability not only of Greece, but of the entire European Union (EU).

Brazilian populism

China's slowing growth has caused turmoil the world over, but none more so than in countries that feed its voracious appetite for commodities. One of these is Brazil, which recently reported a 1.7% economic contraction in the 2nd quarter. With prices for oil, iron ore and other industrial commodities falling, the country went from boom to bust. Investors also face a stock market that has fallen 20% from its peak this year, as well as a currency that has lost more than half its value against the US dollar.

Unfortunately, this resource-rich country's fortunes were to be squandered by President Dilma Rousseff. Her populist policies, such as power subsidies and issuance of cheap loans to companies on the verge of bankruptcy, have robbed Brazil of a bright future. With approval ratings now at single digits, Brazil's citizens have taken to the streets to demand her impeachment, accusing her of corruption and blaming her for the country's worst economic slump in 25 years.

Malaysian corruption

Just like Brazil, Malaysia is another nation rich in natural resources yet plagued by corruption. 2 months ago, the so-called 1MDB scandal broke out, with foreign and local publications narrating how PM Najib Razak stole \$700 million from 1Malaysia Development Berhad (1MDB), a government-run infrastructure fund. Instead of calming the public, PM Razak responded by sacking cabinet officials who questioned him as he fended off investigations into his questionable actions. Fed up with their leader's corruption, the citizenry launched a "people power" rally, which had former PM Mahathir Mohamad as one of its participants.

People Power, Yellow Revolution

In that rally, Mohamad said "if the government ignores the law, we have to demonstrate. If you look at Marcos, when he was ruling the Philippines, they had to overthrow him through demonstrations." The sea of people in yellow shirts brought back memories of our own EDSA Revolution, when the color yellow became a symbol for protest movements in the Philippines led by Cory Aquino. While it remains

to be seen whether Malaysia's Yellow Revolution will succeed, the resulting political instability brought about by corruption at the highest levels of government has sent the Malaysian ringgit to historic lows.

Populism, Corruption and Economic Mismanagement

Although Greece, Brazil and Malaysia are not facing exactly the same crisis, the root of their current malaise can be found in 3 things – populism, corruption and economic mismanagement. History has shown that if these 3 factors are present, a country faces a bleak future ahead of it. In the case of Brazil and Malaysia, the blessing of having vast natural resources has turned into a curse as commodity prices fell. It is not just the citizens of these countries that have to worry though, but investors as well. See below a table showing how much the Brazilian real and Malaysian ringgit have depreciated as a result of populist policies and corruption.

Currency depreciation since cycle peak

Currency	% change from cycle peak	Date of peak
Brazilian real	-61%	26-Jul-11
Malaysian ringgit	-31%	27-Jul-11

Source: Wealth Securities, Bloomberg

Learning from history and other countries' mistakes

The situation of Greece, Malaysia and Brazil is something our country should avoid. To prevent a similar downward spiral, it is crucial that we learn from history and other countries' mistakes. History books are replete with examples of countries on the verge of economic miracles, only to see their dreams snuffed out by governments pitting the rich vs. the poor and promising prosperity through subsidies and dole outs.

Beware of populist policies

In our book, Opportunity of a Lifetime, we devoted Chapter 5 to discuss fiscal reform in the Philippines. We explained why the reforms, such as VAT, deregulation and privatization, are some of the reasons behind our secular bull market. Recently though, a bill was filed in Congress proposing to reduce income taxes. While we are in favor of lowering taxes, there will have to be corresponding measures that will offset revenue losses. This is why we understand Finance Secretary Cesar Purisima when he refused to support this bill, saying that we "cannot put our fiscal sustainability and credit rating at risk by doing piecemeal revenue-reducing legislation." If our future leaders resort to populist policies to gain popularity, then all the efforts undertaken by past governments to place our fiscal house in order will be for naught.

False promises

Let us learn from the examples of other countries as corruption and populism led them to ruin. Thus, this campaign season, we should be wary of candidates promising to make life better for us by cutting taxes and subsidizing fuel & food costs. Politicians espousing fiscal irresponsibility will negate all the gains and reforms we have made in the past few years. To remind our readers of the dangers of false promises, we leave you with a few stanzas from the Broadway musical "Promises, Promises" with music by Burt Bacharach and lyrics by Hal David:

Promises, promises

I'm all through with promises, promises now
I don't know how I got the nerve to walk out
If I shout, remember I feel free
Now I can look at myself and be proud
I'm laughing out loud

Oh, promises, promises
This is where those promises, promises end
I don't pretend that what was wrong can be right
Every night I sleep now, no more lies
Things that I promised myself fell apart
But I found my heart

Oh, promises, their kind of promises, can just destroy a life
Oh, promises, those kind of promises, take all the joy from life.

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