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On 15 November 1935 the leaders of the Philippine Commonwealth accepted a daunting task. In just ten years, in time for the grant of independence that was to come on 4 July 1946, they would have to oversee a program of massive economic adjustment in the national economy. Colonial economic preferences with the United States, including duty-free trade from 1909 to 1934, led the Philippines to send more than two-thirds of its commodity exports to American consumers and to become attached to American-made products, which accounted for two-thirds of all imports. According to the terms of the Tydings-McDuffie Act, as the Philippine Independence Act of 1934 was popularly known, this duty-free relationship would end with independence. At that time, Philippine products would be subject to full U.S. duties. With the imposition of the full tariff in 1946, Philippine exports to the United States, and imports coming from the United States, were expected to decline significantly. Philippine leaders had just ten years to divert trade from the United States and develop new industries to replace American imports.

Few observers thought ten years would be enough time to complete the adjustment process. Philippine leaders publicly discussed the future in apocalyptic terms (Philippine Economic Association 1933). The U.S. Tariff Commission also made public a report that predicted dire consequences after 1946 (U.S. Tariff Commission 1937). Curiously enough, as the Joint Preparatory Committee on Philippine Affairs (JPCPA) was about to convene in 1937 to make recommendations for measures to facilitate the adjustment process, President Manuel Quezon of the Philippines lobbied American leaders for an early grant of independence in either 1938 or 1939. Given the prevailing consensus on the economic problems independence would bring in 1946, the suggestion that it should come even earlier seemed ludicrous. Could such a demand be taken at face value?

Yes, it could! Students of Quezon, Philippine colonial politics, and the transition to independence proclaim in near unanimity that Quezon really did not want independence (Biedzynski 1990; Onorato 1989; Tarling 1977; Wheeler 1964). Yet if Quezon was so opposed to independence, why did he demand early separation from the United States in 1937? The accepted wisdom is that Quezon, like all Philippine leaders, used the independence issue to gain political power and that he ultimately became trapped by his own rhetoric. This led to contradictory behavior where he had to publicly insist on independence as soon as possible but work privately against it. Thus it is argued when forces beyond his control led to an offer of independence in 1934 Quezon was forced to accept despite his own belief that it was not in the best interest of the nation (Friend 1965; Ileto 1984; Onorato 1986; Grunder and Livezey 1951, 222). His demand for early independence is generally seen as a political ploy to appeal to Philippine nationalism.

This common perception of Quezon needs to be reexamined. Quezon hardly seemed a leader trapped by his own rhetoric. Alfred W. McCoy notes Quezon's mastery of Philippine politics (McCoy 1988). His leadership skills were noted by Japanese and British observers at the time, as well as by Americans (Goodman 1967; Onorato 1978, 1981). Indeed, Quezon seemed to manipulate Philippine politics at will to promote his personal political interests. He had the constitution amended to extend his tenure in office as president of the Commonwealth and he reorganized the legislature at the same time so that he could better control it (Hayden 1942). He repeatedly engineered the political defeat of those who opposed him (McCoy 1988). Most significantly for the issue at hand, he was able to muster enough support to reject the first American offer of independence contained in the Hare-Hawes-Cutting Act in 1933. Even if there was little support for continued American sovereignty over the Philippines, it is not inconceivable that Quezon could have publicly opposed independence and still survived politically.

Given his ability to dictate the course of Philippine politics, other explanations for Quezon's behavior need to be explored. An examination of the Commonwealth economy and Philippine-American relations from 1935 to 1940 clearly shows how American policy prevented the Philippines from making necessary adjustments during this period. The economic restrictions the U.S. placed on Philippine agriculture and industry during the Commonwealth made it impossible for the Philippine government to implement a coherent program of Import Substituting Industrialization (ISI) or Export Oriented Industrialization (EOI). Appropriate incentives could not be offered to the private sector, and the power of the Commonwealth government to initiate change was severely limited. The restrictions were so severe that the Philippines actually became more dependent upon the United States during these years. Signs of underdevelopment can even be detected. The evidence suggests that even if the war had not intervened, the Philippines would have made little, if any, progress towards its goal of adjusting to the loss of preferential access to the American market in 1946 because of the restrictions imposed by American policy. The evidence also suggests that at least some Philippine producers understood this to be the case and were not as concerned about Philippine independence as is generally thought.

In the first part of this paper, the process of economic adjustment will be discussed in theoretical and historical perspective. In the second, the policies regulating the economy and foreign economic relations of the Philippine Commonwealth will be examined to show how they offered little room for the Philippines to carry out the process of economic adjustment. Third, an examination of key Philippine export industries will follow, showing how they were harmed by American policies. In some cases they would have been better off had the Philippines been fully independent. Early independence from the United States would have speeded up the adjustment process in these industries. Fourth, the barriers to the development of domestic industry will be identified. Fifth, the evidence indicating increased dependence and underdevelopment will be presented.

Economic Adjustment in Theory and Practice

The development experience of East Asia and Latin America suggests that there are two distinct and mutually exclusive strategies for industrialization. The first, import substituting industrialization (ISI), replaces imports with locally made products. To implement a program of ISI a government must protect domestic manufacturers with some combination of high tariffs, import quotas, or foreign exchange licensing. These protective measures frequently permit the value of a nation's currency to rise, which makes foreign equipment and imported raw materials for industry cheaper than they would otherwise be. There are two phases to ISI: a first or easy phase that is focused on the production of consumer nondurables and a second, harder phase, that is focused on consumer durables and capital goods. The second strategy, export-oriented industrialization (EOI), usually follows a period of ISI. Global markets are targeted as nations specialize in manufactured exports in which they have a comparative advantage. The early phases of EOI are marked by specialization in labor intensive manufactured exports while in later phases the production of more technologically sophisticated products with higher value added emerges. It is generally argued that EOI requires the reverse of the policies that made ISI possible. The national currency must be devalued to reflect its true market value and barriers to imports must be eliminated to allow for correct factor pricing (Haggard 1990; Gereffi and Wyman 1990).

The term "structural adjustment" is often used to describe the process of transition from ISI to EOI. This term was coined by the World Bank and refers specifically to programs first implemented in 1979 to assist nations faced with chronic balance-of-payments problems. Through structural adjustment loans the World Bank prodded many developing and newly industrialized nations to dismantle widespread and popular ISI programs in the 1980s and implement EOI. The World Bank encouraged adjusting nations to remove protective barriers to trade and to put an end to nonmarket pricing in finance, industry, and agriculture. The ultimate goal was to make a nation's products more competitive in both domestic and international markets (Vinod et. al. 1991; Mosely et. al. 1991).

While theoretically based in the literature of neoliberal economics, which advocates a noninterventionist laissez-faire state, the export orientation of World Bank structural adjustment programs was patterned after the experience of the East Asian NICs (newly industrializing countries), South Korea and Taiwan. They made the transition from ISI to EOI in the early 1960s and used EOI as a strategy to promote rapid economic growth in the 1960s and 1970s (Wade 1990, 52–72; Westphal 1978; World Bank 1993). Their experience was often contrasted to that of Latin America where, it was argued, ISI was never really abandoned. The World Bank's understanding of structural adjustment clearly drew upon these stylized distinctions between ISI and EOI (Haggard 1990; Gereffi and Wyman 1990).

Closer examination of East Asia, however, demonstrates that ISI and EOI are not mutually exclusive strategies and that EOI was not the product of a laissez-faire state. The literature on the role the state played in promoting industrialization in South Korea and Taiwan is vast. EOI was accomplished in these nations with a variety of state-led export promotion schemes including tax breaks for exporters, duty drawback schemes, the creation of duty-free export processing zones and financial subsidies (Amsden 1989; Wade 1990; Woo 1991). Also interesting is the literature that shows South Korea and Taiwan continuing the process of ISI in strategic sectors of the economy even after the adoption of EOI (Luedde-Neurath 1986; Wade 1990).

Thus we have two versions of structural adjustment, a stylized version proffered by the World Bank that juxtaposes ISI and EOI and a real process of structural adjustment in which elements of ISI and EOI are combined to promote overall economic development. In the theoretical world of the World Bank, where ISI regimes are dismantled and EOI promoted, structural adjustment is supposed to be completed within five to seven years (Vinod et. al. 1991). In the real world the process takes much longer. It took Taiwan and South Korea approximately ten years to complete the process of ISI and another ten years to see results from EOI (Gold 1986; Amsden 1989; Wade 1990).

Economic Adjustment, the Philippine Commonwealth, and the Tydings-McDuffie Act

It is with these distinctions in mind that we turn our attention to the Philippine Commonwealth. Though unaware of the current terminology, Philippine leaders knew they would have to implement some form of EOI or ISI, or both, to adjust to the loss of duty-free access to the American market. In 1937, though, the year Quezon requested early independence, a priority strategy had not yet been identified. The National Economic Council was still debating whether to focus efforts on cutting production costs in existing export industries, developing new products for export, and finding new markets for export, or developing domestic manufactures to replace imports from the United States (Hodsoll 1937). The export strategy would have required access to foreign markets, possible currency devaluation and export incentives. The import substitution strategy, in turn, would have required higher tariffs, quotas for imports and foreign exchange controls. A cursory review of the conditions the United States imposed on the Philippines during the Commonwealth shows the Philippines did not have the ability to implement either EOI or ISI.

The primary purpose of the Tydings-McDuffie Act was to limit Philippine exports to the United States. It did so in three ways. First, it imposed duty-free quotas for several Philippine exports. These included the four largest agricultural commodity exports—sugar, coconut oil, tobacco products, and cordage—which accounted for about 50 percent of all Philippine exports. Exports above quota were allowed only if the full U.S. duty was paid. For all of these commodities, the United States was the major market. Well over 90 percent of sugar and coconut oil and roughly 55–65 percent of tobacco and cordage products went to the United States (Technical Committee to the President of the Philippines 1944, 34). The quotas were particularly onerous because they targeted industries with the highest value added. In addition to those just mentioned, quotas were imposed on canned pineapple and embroidered garments. No quotas were imposed on unprocessed raw materials.

Second, an export tax was to be imposed on all Philippine products, the proceeds of which were to be used to pay off the bonded indebtedness of the Commonwealth government. During the first year of the tax, set to begin in 1941, Philippine exports would be charged 5 percent of the rate of the American tariff on like goods. The rate of tax would increase each year by 5 percent of the rate of the American tariff until the final year of the Commonwealth, when an export tax equal to 25 percent of the full American tariff would be assessed. Upon independence in 1946, Philippine goods would be subject to the full American tariff—an effective four-fold increase in the tax on Philippine exports to the United States (U.S. Congress 1934, 469–70).

Third, Congress tightened the noose around Philippine exports even further in several pieces of legislation passed after the Tydings-McDuffie Act. In an amendment to the Revenue Act of 1934, a special excise tax was imposed on coconut oil from the Philippines, and on any oil made in the United States from Philippine copra. Additionally, the Jones-Costigan Sugar Act of 1934 imposed an excise tax on sales of Philippine sugar in the United States. Though the coconut and sugar excise taxes were to be returned to the Philippine treasury, the government was prohibited from using the proceeds of the coconut tax to assist the coconut industry (Kirk 1936). The return of the sugar excise tax was subject to U.S. congressional authorization each year. After an initial disbursement to offset losses to sugar producers in 1935, no funds were returned during the life of the Commonwealth (Nakano 1997). The 1934 Sugar Act also reduced the quota for Philippine sugar and converted the duty-free quota into an absolute quota. Meanwhile, the Cordage Act of 1935 doubled the duty-free quota for cordage in the Tydings-McDuffie Act of three million pounds, but converted it to an absolute quota (Kirk 1936).

In addition to limiting Philippine exports to the United States, the Tydings-McDuffie Act limited the Philippines' ability to control imports. First, American exporters were guaranteed unlimited and duty-free access to the Philippines until 1946, despite the quotas and taxes applied to Philippine goods going to the United States. Second, the United States retained control over Philippine tariffs. Any changes in the Philippine tariff (from which American goods were exempt) had to be approved by the United States. Third, the Philippine peso was pegged to the dollar at a rate of 2:1, a rate which had been established over thirty years earlier, and was to remain convertible for the duration of the Commonwealth. The Philippines could not alter the value of its currency. Fourth, the United States retained control over the foreign affairs of the Philippines. The Commonwealth government was not allowed to enter into independent trade negotiations with third countries (United States Congress 1934, 459–70).

It was argued at the time that the Tydings-McDuffie Act would provide incentives to Philippine producers to either divert investment to new industries or cut costs in existing industries to make them competitive in the American market after 1946. The act, however, was clearly designed to protect American agriculture from Philippine commodities and preserve the position of American manufacturers in the Philippine economy until 1946 (Kirk 1936; Filipino Rehabilitation Commission 1945, 24–25; Grunder and Livezey 1951, 204; Jenkins 1954, 36–37). These goals could not be achieved without restricting the ability of the Philippines to make needed economic adjustments. During the Commonwealth, which began in the middle of a global depression, the Philippines had restricted access to foreign markets. The depression had curtailed global trade substantially as nations erected barriers to imports to protect domestic producers. Indeed, this was exactly what the United States was doing to the Philippines. In essence, the Philippines was being asked to diversify its markets when its only real market was the United States, from which it was being cut off. With the peso tied to the dollar, the world's strongest currency, Philippine goods were overpriced in many potential markets anyway. And without control of the tariff the Philippines could not use the most common incentive for EOI, a differential tariff for exported goods and imports.

Cutting tariffs for imports in exchange for export expansion and for all materials used in the production of exports was not an option. Neither was it possible to negotiate trade treaties with third parties (Hartendorp 1958, 43–44).

There was little room for ISI either. Tariffs and quotas were determined by the United States and used to protect American interests, not promote Philippine industry. And with the Philippine peso convertible and pegged to the dollar, foreign exchange controls were not possible.

Analysts have conceded that Philippine leaders were constrained in their ability to implement adjustment measures by American policies (Taylor 1964, 89; Golay 1966, 98; 1998, 358; Jenkins 1954, 140). Some have identified the lack of tariff autonomy as the major barrier to adjustment (Apostol 1927; Stine 1966, 26, and 131; Doeppers 1984, 16–30; Caoili 1986, 35; Gopinath 1987, 107–37). The evidence presented above, however, suggests that the problem went far beyond the lack of tariff autonomy. It makes clear the Philippine Commonwealth was denied every major tool necessary to carry out needed economic adjustments in the national economy. There was no possibility of success. As the evidence below will show, the economy would have been better off had the Philippines been granted immediate independence as Quezon requested.

Agricultural Adjustment and Tydings-McDuffie Act

The primary fear in 1935 was that Philippine independence and the loss of the duty-free American market would destroy Philippine agriculture. The quotas imposed by the Tydings-McDuffie Act, however, stemmed the previously rapid growth of the sugar and coconut oil industries and prevented industrialization in the abaca and cordage industry long before the date scheduled for independence. The excise tax on Philippine coconut oil substantially lowered the value of Philippine copra as well, and prevented adjustments in the industry that could have made it more efficient. The unrestricted entry of duty-free American goods during the Commonwealth also harmed the tobacco industry, making it impossible for the Philippines to expand cigarette production for domestic consumption. A cursory examination of each of the four major export industries clearly demonstrates the adverse effects the Tydings-McDuffie Act had on the promotion of ISI and EOI in Philippine agriculture.

Sugar

Analysis of the effects Philippine independence would have on the national economy and the difficulties to be faced in the adjustment process have invariably centered on the effects the termination of tariff preferences would have had on sugar. By 1930 over 99 percent of Philippine sugar was sold in the U.S., and by 1933 sugar accounted for 34 percent of the value of all Philippine exports (Technical Committee 1944, 34, 40, 78). Since studies at the time indicated that Philippine sugar would not be competitive in the U.S., if the full tariff was imposed, much of the fear of independence in the Philippines was inspired by the potential collapse of the sugar industry (JPCPA 1938, vol. 1, 48). Indeed, it was to save sugar that various attempts were made during the Commonwealth to reverse or postpone independence (Friend 1964; Wheeler 1964; Larkin 1993).

To survive after 1946 the Philippine sugar industry needed to cut its costs of production, which were twice as high as Cuba's, the major competitor in the American market (Technical Committee 1944, 58). Rather than encourage Filipino producers to cut costs by increasing production and take advantage of economies of scale, the absolute quota basically stemmed growth while production costs were still high, taking away any incentive to lower costs by expanding production. With an oversupply of sugar in the world economy Philippine sugar was also precluded by treaty from selling to nations other than the U.S. (Larkin 1993, 206–7).

The rapid growth of the sugar industry that had taken place in the four years preceding the Commonwealth came to an abrupt end. From 1930 to 1933 sugar exports from the Philippines to the United States had increased from 830,000 short tons to 1,271,000 short tons, an increase of 65 percent. The Tydings-McDuffie Act imposed a duty-free quota of about 952,000 short tons, which later became an absolute quota under the Jones-Costigan Sugar Act of 1934. This was 25 percent less than actual exports in 1934 and only 60 percent of milling capacity. After a dramatic decrease in sugar exports in 1935, the result of the retroactive application of the sugar quota to 1934, exports stabilized at 970,000 short tons from 1936 to 1939 (Technical Committee 1944, 40; Houston 1954c, 387). The Tydings-McDuffie Act effectively halted the growth of the Philippine sugar industry.

With opportunities for growth curtailed, efforts at adjustment in sugar seemed feeble at best. The largest mills acquired more land and purchased other mills in efforts to rationalize production. The larger millers and planters also invested in other sectors of the economy. Small planters frequently converted sugar land to the production of other crops. As a result of these actions, the total land devoted to sugar declined by almost 45 percent from 1934 to 1940, from 306,000 hectares to 167,000. Production declined by 35 percent. Initially the government intervened forcefully, ordering the destruction of excess sugar in 1935 to stabilize prices. Planters and millers were compensated for their losses with funds returned to the Philippines from the newly imposed sugar excise tax. Once the Commonwealth came into existence in November 1935, however, the government limited its role to leading the effort to repeal the excise tax and to maintain tariff preferences in the American market after independence. Meanwhile, the Philippine National Bank prevented planters from investing funds lent for sugar production in other endeavors as Quezon tried to influence the negotiations over milling contacts so that planters would receive a larger share of the final product. The government also purchased two sugar refineries in an effort to lower the domestic prices of refined sugar, a move much criticized by coconut and abaca growers, the owners of sugar mills, and American colonial officials (Houston 1954c; Larkin 1993, 201–36).

Yet these measures could do little to compensate for the decline in exports after 1934 and falling global prices after that. The major costs of the adjustment process fell on small sugar planters, tenants, and hired hands, whose poverty was already well known, as larger planters cut costs by lowering wages, laying off workers and increasing rents (Runes 1939). As a result, the incidence of labor strife in the sugar fields of Central Luzon rose dramatically after 1937. The number of incidents increased from twelve per year (1935–1937) to forty-nine per year (1938–1941) (Larkin 1993, 219). The immediate effect of the sugar quotas was the birth of social revolutionary activism in the rural Philippines.

The Coconut Industry

Second in importance to sugar, the coconut industry accounted for 27 percent of the value of all Philippine exports from 1927 to 1936. At least four million individuals were wholly or partially dependent upon the industry, twice as many as sugar. The two major exports of the Philippine coconut industry were coconut oil and copra, the dried meat of the coconut used for processing oil. Each accounted for about

10 percent of Philippine exports during the Commonwealth (Technical Committee . . . 1944, 72, 78). The Philippines had produced copra and some oil in the nineteenth century but oil exports stopped near the end of the century and did not begin again until duty-free access to the American market was granted in 1909. By 1934 about 145,000 tons of coconut oil were being exported each year, 93 percent going to the American market. A duty of two cents per pound in the United States on imported coconut oil, roughly 67 percent ad valorem, protected American producers from most foreign competition. As a colony, however, the Philippines did not have to pay this tax (Technical Committee 1944, 81).

The United States tried to restrict further development of the Philippine coconut industry during the Commonwealth in three ways. First, the Tydings-McDuffie Act imposed a quota of 200,000 tons on coconut oil exports to the United States. Second, the export tax scheduled for 1941 was to be applied to all coconut exports. Third, the Revenue Act of 1934 imposed an excise tax of three cents per pound on all fats and oils derived from the processing of Philippine copra.

It was the copra industry that was hit first and hardest by these measures. The primary culprit was the excise tax. It effectively doubled the price of coconut oil in the U.S. and alternatively caused a nearly 50 percent decline in the market price of Philippine copra. From 1923 to 1929 the price of copra never fell below four cents a pound. Even after the depression hit the price stood at 3.5 cents in 1930. In 1935, however, the first year of the excise tax, copra prices stood at two cents a pound, falling to as low as 1.6 cents in 1940. This meant the three cents per pound excise tax accounted for roughly two-thirds the price of oil made from Philippine copra. The impact of these price changes was dramatic. Though copra exports to the U.S. increased by 50 percent from 1936 to 1940, the value of those exports declined by 36 percent, a decline in real value of about 55 percent. While the global depression had some effect on prices the real value of copra exports to third countries—without the excise tax—declined by only 22 percent. Since approximately 65 percent of Philippine copra went to the U.S., about 43 percent of the decline in the real value of all copra exports could be attributed to the excise tax (Technical Committee to the President of the Philippines 1944, 34, 72, 76).

It was for this reason that Philippine copra producers supported Quezon's bid for early independence. Their primary goal was to obtain most favored-nation treatment from the United States for their copra, which they felt required elimination of the excise tax (Kalaw 1937; Montenegro 1937).

The situation for coconut oil was significantly different from that of copra. Neither the quota nor the excise tax seemed to have any effect on coconut oil exports. From 1930 to 1936, exports averaged 145,000 tons, well below the quota. This figure rose only slightly to 160,000 tons from 1936 to 1940, still well below the quota. The value of coconut oil exports rose slightly, too, averaging $11 million from 1930 to 1936 and $12 million from 1937 to 1940. While the quota seemed to have had little to no effect on the quantity of exports and the excise tax seemed to have had little effect on their value, the export tax, however, posed a real threat. With the imposition of the export tax, oil producers in the Philippines would effectively begin paying a portion of the American tariff on processed oil. Since the margin of profit for Philippine-based coconut oil processing was less than the anticipated export tax, the U.S. Tariff Commission predicted the Philippine-based industry would lose its ability to compete in the American market even before the five-year transition marked by the export tax ended (U.S. Tariff Commission 1937, 118–21, 144, and 149; Houston 1954a, 160).

Why did the excise tax have so little effect on Philippine coconut oil exports when even the slightest increase in the rate of duty would cause their demise? Profits for Philippine-made coconut oil depended upon market share in the United States, which was based on the relative costs of producing coconut oil compared to American producers. While the excise tax effectively increased the production costs for coconut oil, it did not affect the relative costs of coconut oil processed in the Philippines compared to that processed in the U.S. American and Philippine producers of Philippine coconut oil could both lower the price at which they purchased copra to compensate for the tax or raise the price of the oil they sold. The export tax, however, would make coconut oil processed in the Philippines more expensive than oil processed in the United States, thus leading to the demise of the industry. It was clear that Philippine coconut oil could not pay the full tariff and still compete in the American market. The American tariff on coconut oil gave birth to the industry and would now destroy it.

Little was done to help the coconut industry adjust to these circumstances. Philippine leaders did make significant efforts to have the excise tax and export taxes repealed. Indeed, there was some legal basis for repealing the excise tax because it was not levied on other tropical oils. The tax could have been considered a violation of the most favored nation principle which the United states applied as a general rule to its foreign trade. The Philippines, however, was a colony, not an independent country whose trade with the United States was dictated by treaty. The tax stood. With somewhat more success, Philippine leaders gained the repeal of the export tax for coconut oil through an amendment to the Tydings-McDuffie Act in 1939. The industry was still subject, though, to the full American tariff in 1946.

Any adjustment within the coconut industry to make it more competitive required capital, which the Philippines did not have. The dramatic decline in the value of copra left little profit for planters to invest. Moreover, the proceeds from the excise tax, which were to be remitted to the Philippine government, could not be used to subsidize the coconut industry. This tax provided a substantial fund for the Philippine government and by 1939, it was reluctant to push for the repeal of the tax as coconut planters desired. Though the funds were invested in a variety of endeavors, most analysts argue they were wasted on frivolous projects or pork barrel spending (Houston 1954a; Nakano 1997). As a result of Quezon's efforts, the Tydings-Kocialkowski Act of 1939 amended the Tydings-McDuffie Act and eliminated the strict prohibition on the use of the excise tax for adjustment of the coconut industry. It was probably not a coincidence that in May of that year, as the act was about to be passed, Quezon sent a mission to study the highly efficient coconut industry in Ceylon and make recommendations for restructuring the Philippine industry. The government subsequently created the National Coconut Corporation to implement the proposals recommended by the mission. With a program and funds, some adjustment might have been possible by 1946 had not the war intervened (Houston 1954a).

Abaca and Cordage

Abaca, the raw fiber from which cordage was made, was historically the most important of Philippine exports. During the first ten years of American rule (1898–1908) it accounted on average for 62 percent of the value of all exports. By the time of the Commonwealth, however, it had dropped to fourth place on the list of Philippine exports, accounting for only 9 percent of value from 1931 to 1940 (Technical Committee 1944, 87–97). While the industry was plagued by antiquated methods of production and a complicated distribution network that insured low prices to planters, little was done to make the industry more efficient for the period after independence. In an early study of the abaca industry Charles Houston attributed blame to the planters themselves. More recently, Norman Owen has applied a dependency and world-systems framework to explain the development of Philippine abaca (Houston 1954b; Owen 1984). By the time of the Commonwealth, however, it is clear that the inability to make adjustments in abaca and cordage were primarily a function of American policy.

Philippine abaca was less dependent on the American market than any other agricultural export of the Philippines. Only about 30 percent went to the United States (Technical Committee 1944, 89). Abaca was also on the U.S. duty-free list so it would not be subject to American tariffs after independence (though it was to be assessed the export tax beginning in 1941). Cordage, on the other hand, benefited from tariff preferences since the U.S. imposed a duty on imported rope and twine. Unlike any other product manufactured in the Philippines, cordage could also pay the full tariff in the American market and still undersell the American product. Furthermore, the much sought-after manila variety of abaca, from which manila rope was made, was indigenous to the Philippines. The nation had a global monopoly on the commodity.

The Philippines was in a position to dominate the world market for high quality cordage. Indeed, the volume of Philippine cordage exported to the United States rose dramatically in the years prior to the Commonwealth. A quota of three million pounds was imposed on Philippine cordage exports in the Tydings-McDuffie Act, which was about half of what the Philippines had been exporting to the United States. Not satisfied, American cordage makers had Congress impose an absolute quota of six million pounds in the Cordage Act of 1935. This quota effectively set limits to the growth of the Philippine industry. The Philippines was the only nation on which the United States imposed a quota on cordage. Again, had the Philippines been an independent nation this quota would have violated the principle of nondiscrimination that guided American trade policy. The Philippines was a colony, however, and U.S. cordage makers could get away with another act of discrimination. Since the United States ran an average surplus of $5.5 million in its fiber trade with the Philippines, which imported such items as brooms, brushes, wires, cables, and cotton manufactures, quotas on cordage helped maintain a trade imbalance in this product category (Houston 1954b, 410). The combination of quotas for the Philippines but unrestricted duty-free access for the United States made it impossible for the Philippines to adjust the fiber industry.

J. S. McDaniel, the head of the American Cordage Institute and the person most responsible for the quota on Philippine cordage, was a caricature of the arrogant, rapacious imperialist. His behavior illustrates well the political hurdles to adjustment faced by the Philippines during these years. He repeatedly threatened the Philippine abaca industry with destruction during the Commonwealth if the Philippines did not accept an absolute quota on Philippine cordage exports to the United States. He threatened to boycott Philippine abaca and smuggle specimens to other countries to break the Philippine monopoly on the commodity (JPCPA 1938, 3: 919). In a particularly self-righteous and venomous letter to Quezon, he explained how Philippine cordage exports were "a serious menace to the economic and political security of the Philippines." He complained that Philippine factories worked three shifts a day (to the standard single shift in American factories) and that Philippine producers used the "low price" method, which required no sales or advertising expenses. (Though he did accuse the Philippines of using circulars to advertise their low price.) To justify his position McDaniel argued that it was not discrimination to target an industry that had not yet developed. McDaniel's efforts made it impossible for the Philippines to promote the growth and adjustment of the one major domestic industry that needed no preferences to survive in the American market and could have adjusted with minimal effort (McDaniel 1934).

Tobacco

Like copra, abaca, and cordage, Philippine tobacco was threatened by the Tydings-McDuffie Act in ways that would not have been possible had the Philippines been an independent nation. Though between 50–60 percent of Philippine tobacco was sold in the U.S., Philippine tobacco entered a total of forty-four foreign markets, a greater number than any other Philippine product (JPCPA 1938, 2: 449–50). Thus, it was less dependent on the American market than either sugar or coconut products. The U.S. Tariff Commission, however, was pessimistic about the future of Philippine tobacco, predicting that Philippine cigars, the largest tobacco export, would not survive the imposition of the export tax (U.S. Tariff Commission 1937, 63).

The Philippines, however, was losing money on its tobacco trade with the United States. During the Commonwealth 50 percent of the Philippine market for cigarettes was met by U.S. imports, which accounted for 99 percent of Philippine tobacco imports. The average value of U.S. tobacco exports to the Philippines stood at $5.9 million while the value of Philippine tobacco exports to the U.S., which included both cigars and tobacco filler for cigarettes, stood at only $3.4 million (Technical Committee 1944, 107, and 191). According to the JPCPA, if the full Philippine tariff was applied to American cigarettes they would not be able to compete (JPCPA 1938, Pt. 1, 99). Independence, then, and the application of full Philippine and U.S. duties on each other's tobacco products would have the Philippines losing a small market for cigars and gaining a large market for cigarettes.

As a result of these circumstances, Manuel Gallego of the Manila Tobacco Association made an unusually strong appeal for early independence when he appeared before the Joint Preparatory Committee on Philippine Affairs in 1937. He responded cavalierly to the threat his industry supposedly faced after 1946. Though he requested a continuation of tariff preferences after independence, and a cessation of the export tax, he argued the industry would be able to adjust to the loss of preferences "if given the chance to negotiate new markets." He also asserted the tobacco industry could live with the lower margins of profit that would come after 1946 (JPCPA 1938, 2: 447–61, 463–77).

It is clear American imposed quotas and taxes and duty-free American imports prevented the coconut, tobacco, abaca, and cordage industries from making needed adjustments. Quotas on sugar also led to a crisis that might have been avoided if the Philippines did not have to cut production so much in so little time. Without the power to make adjustments in the major export industries to make them competitive in the United States after independence, the only option left for the Philippines was to find new markets. Yet this was a period of colonial preferences and intensified competition in international trade. By 1937 all markets in the region were dominated by European powers or Japan, and the lack of diplomatic autonomy made it impossible for the Philippines to negotiate trade agreements with these third parties. In a nearly two-week visit to Japan in 1938, President Quezon did not even bring up the topic of a trade agreement, though he appears to have wanted to do so (Goodman 1967, 1982). The special relationship that existed between the Philippines and the United States during the Commonwealth precluded it.

When these factors are considered, Quezon's demand for independence seems much more than posturing; it was a real option. As an independent nation, the U.S. probably would have had to grant the Philippines, most favored-nation trading status, which would have removed the fetters placed on copra and cordage. It would have allowed the Philippine government to protect the local market for tobacco products and would have likely allowed Quezon to negotiate new markets for Philippine products in Japan.

The Tydings-McDuffie Act and Economic Adjustment: Manufacturing

The development of domestic manufacturing was also high on the list of Philippine priorities because of the need to replace imports that were expected to decline once preferential access to the American market was lost (Stine 1966, 7). Estimates of that decline went as high as 60 percent (JPCPA 1938, 2: 565). Yet Philippine leaders could do little. There are several examples of easy ISI that would have been possible had the Philippines been able to protect domestic industry with tariffs, quotas, or foreign exchange controls. No domestic manufacturing could be developed during the Commonwealth, however, as long as American goods entered the Philippines duty-free and in unlimited quantities, and as long as the Philippines could not impose tariffs or quotas on imports from third countries without U.S. approval.

As has already been mentioned, the manufacture of cigarette and fiber products were two industries the Philippines could have developed. The fishing industry is another. In his study of the fishing industry Charles Houston noted the lack of effort put into developing a fishing industry in the Philippines. Alternatively, he was struck by the success of the Japanese industry (Houston 1955, 32–35). Yet the American fishing industry, already well developed, could not compete with Japan at this time either. As a colony, the Philippines had been the number one market for American exports of canned fish. From 1927 to 1936, however, American exports of sardines to the Philippines declined by 70 percent, exports of canned salmon by 80 percent, and exports of canned mackerel by over 90 percent. Japan had become the principal supplier of each item. Under pressure from American exporters the JPCPA recommended an increase in the Philippine tariff on canned fish of 25 percent, enough to protect American exporters from Japanese competition (JPCPA 1937, 1: 102–4). With the American fishing industry able to influence Philippine tariffs in this manner, it is not surprising that the Philippines made no attempt to develop their own industry.

The barriers to adjustment posed by the lack of tariff autonomy were raised even higher by the lack of currency autonomy. Illustrative of this is the textile industry. Like canned fish, Japanese textiles increasingly came to dominate the Philippine market in the 1930s at the expense of American producers, despite the fact that Japanese exporters paid a tariff of roughly 105 percent. When Philippine leaders sought to raise the tariff even higher they were prevented from doing so by the United States, which feared retaliation against American cotton exports to Japan (U.S. Congress 1939, 1–2, 103, 330).

Japan's ability to dominate the Philippine market despite this prohibitive tariff requires some explanation, however. Daniel Doeppers attributes it to improved product design, lower wages and lower costs vis-a-vis American competition (1984, 18). An astute observer at the time, however, argued Japanese competition was the product of a depreciated yen that allowed Japan to sell its products at prices lower than either the Philippines or the United States (Hodsoll 1937, 7). While both explanations probably account for some of the competitive advantage Japan had in textiles, the inability of the Philippines to either raise the tariff or devalue the currency made efforts to compete futile. Doeppers (1984) notes how Vicente Madrigal, successful industrialist and Quezon compadre, was encouraged to enter the textile industry but failed in his efforts, succumbing to competition from Japanese imports. Given Madrigal's success in other business endeavors, and assuming Quezon would not have encouraged him to enter the industry without some guarantee of government support, his failure is striking. Even a Presidential crony could not succeed if the government did not have the tools to protect him. Madrigal's failure is strong evidence that a strategy of import substitution, even in ventures typical of the early, easy phase of ISI, could not succeed without protective tariffs and currency manipulation. As long as the Philippines could not raise its tariff, restrict foreign exchange or devalue its currency, it had no hope of competing against other nations in the region. It could not even protect the domestic market against third country imports as the case of Japanese textiles demonstrated.

Philippine leaders understood the effect American policy would have on their ability to adjust during the Commonwealth (The Philippine Economic Association 1933). Efforts were made to gain as much control over the economy as possible despite these formal constraints, but most failed. Indicative of the futility of these efforts was an early attempt to gain control of the tariff. In 1933 the Philippine Assembly passed a law giving the American governor general the power to raise and lower tariffs by administrative fiat, upon the recommendation of a Philippine tariff commission or its equivalent. The law was patterned after a similar law in the U.S., which gave the U.S. President the power to raise tariffs on low-priced imports to compensate for the difference in production costs in the United States.

Ironically, it was the lack of manufacturing capacity in the Philippines that justified the rejection of this measure by the American judge advocate general of the War Department and by the U.S. attorney general. Both argued that the law was unconstitutional for it granted broad legislative powers to the Philippine chief executive. Yet the very similar American law had been deemed constitutional. How was the Philippine situation different from the U.S? The Philippines had no domestic industry to use as a frame of reference for determining the rate of tariff needed. Simply put, the Philippines could not use a tariff to develop domestic industry because it had no domestic industry to begin with (Encarnacion 1934b).

Attempts to control the value of the currency failed as well. In 1934, the year the Philippine Independence Act was passed, V. Singson Encarnacion, the acting secretary of Finance, presented to the American governor-general a plan for economic development. This plan called for the creation of a central bank and the establishment of an independent currency whose value would not be determined by the changing value of the American dollar (Encarnacion 1934a). The American governor-general refused to act. It would be fifteen years before the Philippines would be allowed to establish a Central Bank and it would take an approaching balance of payments crisis to push the United States to recommend it (Joint Philippine American Finance Commission 1947).

With no ability to manipulate foreign commerce to the advantage of the private sector, the government created state-owned enterprises (SOEs) to promote adjustment and industrialization. Four SOEs existed in 1935. From 1936 to 1940 the government created fourteen more. Among these were the nation's major railroad, a cement company, a major textile mill, and several canneries for the fishing industry. The government laid the groundwork for a major hydroelectric power project and established facilities to market key agricultural commodities of the nation in an effort to stabilize prices for producers and consumers. It also established a development bank for long-term lending to the private sector. Though on the whole profitable, they fell short of achieving the adjustment goals set for them (Stine 1966, 65–87).

The government also promoted domestic manufactures by encouraging Filipino consumers to buy locally made products. This program of persuasion began in 1935 when the National Economic Protectionism Association was formed to promote national economic self-sufficiency. Radio and newspaper campaigns conducted by the association encouraged Filipinos to buy locally made products and purchase from Filipino retailers. These programs, however, met with limited success (Gopinath 1987, 129–33; Stine 1966).

That the government established a number of SOEs and resorted to persuasion to promote domestic manufactures does not mean that these were the preferred strategies of Quezon and other Philippine leaders (Gopinath 133). And because these strategies failed does not mean they were flawed. The resort to these strategies suggests that Philippine leaders had no other alternatives since the more conventional tools for promoting economic adjustment were not available to them.

An evaluation of what the Philippines attempted during the Commonwealth period indicates that one of the greatest barriers to adjustment was time. Formed in 1935 the National Economic Council did not begin serious deliberations until 1938 and did not submit formal recommendations for government action until 1939 (Stine 1966, 65). The creation of an Agricultural and Industrial Bank to provide long-term lending did not take place until 1939 (114). The National Power Corporation, created in the same month as the Commonwealth, studied four possible sites for hydroelectric development and submitted specific recommendations for one site by 1940. A lack of capital, however, prevented it from doing more than this (66–68). While it is tempting for critics of Philippine leaders to see as wasted time the three to four years that passed before specific recommendations for national economic development were made, this assumes the ten-year timetable for Philippine adjustment to be sufficient. If a more realistic twenty- to thirty-year time frame is considered, it could be argued that Philippine leaders made substantial progress, particularly given the limitations placed upon them by the United States (Hartendorp 1958).

The futility of making any real progress at establishing new domestic industries while the U.S. maintained sovereign control over the Philippine economy became all too clear during the deliberations of the Joint Preparatory Committee on Philippine Affairs (JPCPA). The logic of ISI is to develop the ability to manufacture products for which domestic demand is high. Generally these are consumer nondurables. But if the market for a product in the Philippines was large at this time, it was an important market to American exporters. After hearing requests from American exporters to the Philippines for increased protection from local and foreign competition, the JPCPA recommended that the Philippines take measures to protect American textiles, cigarettes, canned fish, wheat flour and canned milk. For each of these industries the Philippines was the number one foreign market of the United States. Each industry required duty-free access to the Philippines to be competitive. Canned fish, wheat flour, canned milk, and textile producers even required an increase in the Philippine tariff on third countries to remain competitive. At least three of these products—textiles, cigarettes, and canned fish—should have been easy to develop in the Philippines, if the domestic market could only be protected. It could not. The recommendations of the JPCPA clearly indicate the barriers to ISI in the Philippines as long as the U.S. retained control over the tariff. ISI was impossible without economic sovereignty (JPCPA 1938, Pt. 1; Pt. 3, 764–65, 858–60, 1080).

Accelerated Underdevelopment?

Because of the restrictions placed upon Philippine exports and because the Commonwealth government did not have the power to manage the nation's foreign trade, the Philippines was unable to implement either EOI or ISI. Structural adjustment of the Philippine economy was not possible. More ominous were the signs of increased dependency on the United States and accelerated underdevelopment that emerged as a result of these restrictions. During the Commonwealth, the American share of Philippine trade grew rapidly, from 65 percent, in 1933, to 70 percent, in 1937, to 78 percent, in 1940, clearly indicating a growing dependence. At the same time, the Philippines was transformed from a nation with a trade surplus to one with a trade deficit. Granted duty-free access to an otherwise highly protected American market from 1909 to 1934, a few key Philippine commodities recorded impressive levels of growth. The extent to which the Philippines benefited from this acute form of dependent development is not clear. The highly unequal relationship between landlord and tenant in the countryside remained unchanged and was probably reinforced during the period of American rule (Paredes 1988). It could be argued, though, that a small urban middle class did begin to emerge (Doeppers 1984). Regardless of the effect on class structure and development, rapid growth of commodity exports enabled the Philippines to maintain annual trade surpluses with the U.S. from 1922 to 1934 sufficiently large to counter trade deficits with the rest of the world.

By 1938, however, just three years into the Commonwealth, the trade surplus disappeared. From 1938 to 1940 the Philippines ran a trade deficit with United States as well as the rest of the world. Though the value of exports increased in 1936 and 1937, they declined in value by 25 percent in 1938, and then leveled off for the next two years. In 1940, the last year of complete figures prior to the war, the value of Philippine exports to the U.S. was the same as it had been in 1934. The quotas had done their job. In the meantime, American exports to the Philippines had risen steadily from 1934 until by 1940 they had increased 2.5 times (Technical Committee 1944, 32, and 243). Unimpeded access to the Philippine market had also done its job. The Tydings-McDuffie Act had encouraged the transfer of resources out of the Philippines, a transfer that was reflected in the trade balance each year. In world-system terms the Tydings-McDuffie Act had increased the flow of surplus from the periphery to the core, a primary indicator of underdevelopment (Frank 1966). That transfer was financed by U.S. remittances to the Philippines, primarily by the refund of the excise tax on coconut oil. These remittances have been characterized as "windfall revenues" (Nakano 1997). What the Philippines should have earned through its exports had been transformed into a gift from its "benefactor."

There is no reason to believe the Philippine trade deficit would have corrected itself had the war with Japan not put an end to the Commonwealth government. Rather than provide the opportunity for adjustment, the Tydings-McDuffie Act and other legislation regulating Philippine-American economic relations made adjustment impossible, increased Philippine dependency on the United States and spawned underdevelopment.

Conclusion

Three conclusions can be drawn from this study of economic adjustment in the Philippine Commonwealth. First, the impediments to adjustment imposed by the Tydings-McDuffie Act and the increasing dependency and underdevelopment that resulted provide grounds for reexamining Quezon's policies vis-a-vis the United States. What most Americans could not see had to be painfully obvious to Quezon and other Philippine leaders; the Tydings-McDuffie Act was the major impediment to adjustment. For the Philippines to continue abiding by its provisions for another six to eight years would have meant only further dependence and the possibility of greater underdevelopment. Quezon's demand for early independence must be seen in this light and thus taken seriously, not dismissed as a negotiating ploy. If this is done, a complete reinterpretation of Quezon and his negotiations with the U.S. from 1937 through 1939 on economic issues, independence, and continued U.S. rule is necessary. Quezon may have been much more the nationalist than is generally accepted. The belief that he was singularly committed to delaying independence would certainly obscure this fact. A more detailed analysis of his actions after 1937 would most assuredly reveal a more complex strategy to solving Philippine economic problems, a strategy in which early independence and a delay of independence were but two possible options for promoting economic adjustment.

Second, placed in proper historical context the Philippine experience suggests that economic adjustment is a never-ending process. It was not until 1950 that the Philippines would make a concerted effort at ISI and not until 1970 that EOI would be attempted in any serious way. In 1979 the Philippines still had to go through a formal structural adjustment program under World Bank guidance. Yet in a 1994 study, Robert Dohner and Stephan Haggard examined the failure of structural adjustment under then Pres. Ferdinand Marcos and expressed pessimism about the ability of the post-Marcos government to fully implement an adjustment program. Sixty years after the start of the Commonwealth, the Philippines still had not adjusted! The Philippine experience suggests there is either something terribly wrong with the Philippines or there is something wrong with our understanding of the adjustment process. Dohner, Haggard, and others suggest that there is something wrong with the Philippines, placing blame on the patrimonial nature of the Philippine state (Dohner and Haggard 1994; Hutchcroft 1998). Yet the patrimonial state can hardly be blamed for the failures of the Philippine Commonwealth. It may be that economic adjustment is a process that is never fully accomplished. Rather, it is an ongoing process shaped by global economic forces that are beyond the control of any nation on the periphery of the world economy.

Third, in terms of concrete policies, Philippine dependence upon the United States is best defined not by what Philippine leaders had to do but by what they could not do. World-systems and dependency theory have been criticized for being too deterministic. Corrections have been made and excellent studies of the development of Philippine agriculture drawing upon these theories have integrated local and global factors in a way that has eliminated that determinism (Owen 1984; Larkin 1993). These studies are deeply historical and analyze development over a long period of time. To draw upon world-system and dependency theory for a study much more focused on a particular point in time, and to make that study relevant for policy analysis, it is the limits to action that need to be emphasized. Philippine leaders had options and used them. They created SOEs against American advice, used persuasion to encourage consumption of domestic manufactures and continually negotiated with the United States in an effort to obtain more room for maneuver. Philippine dependence, however, remained predicated upon the inability of leaders to limit imports or effectively promote exports. The Philippine experience suggests that the existence of a sovereign state with power over commerce and trade is necessary to overcome dependence and underdevelopment. Not until the Philippines achieved its independence was it able to begin the process of adjustment.

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