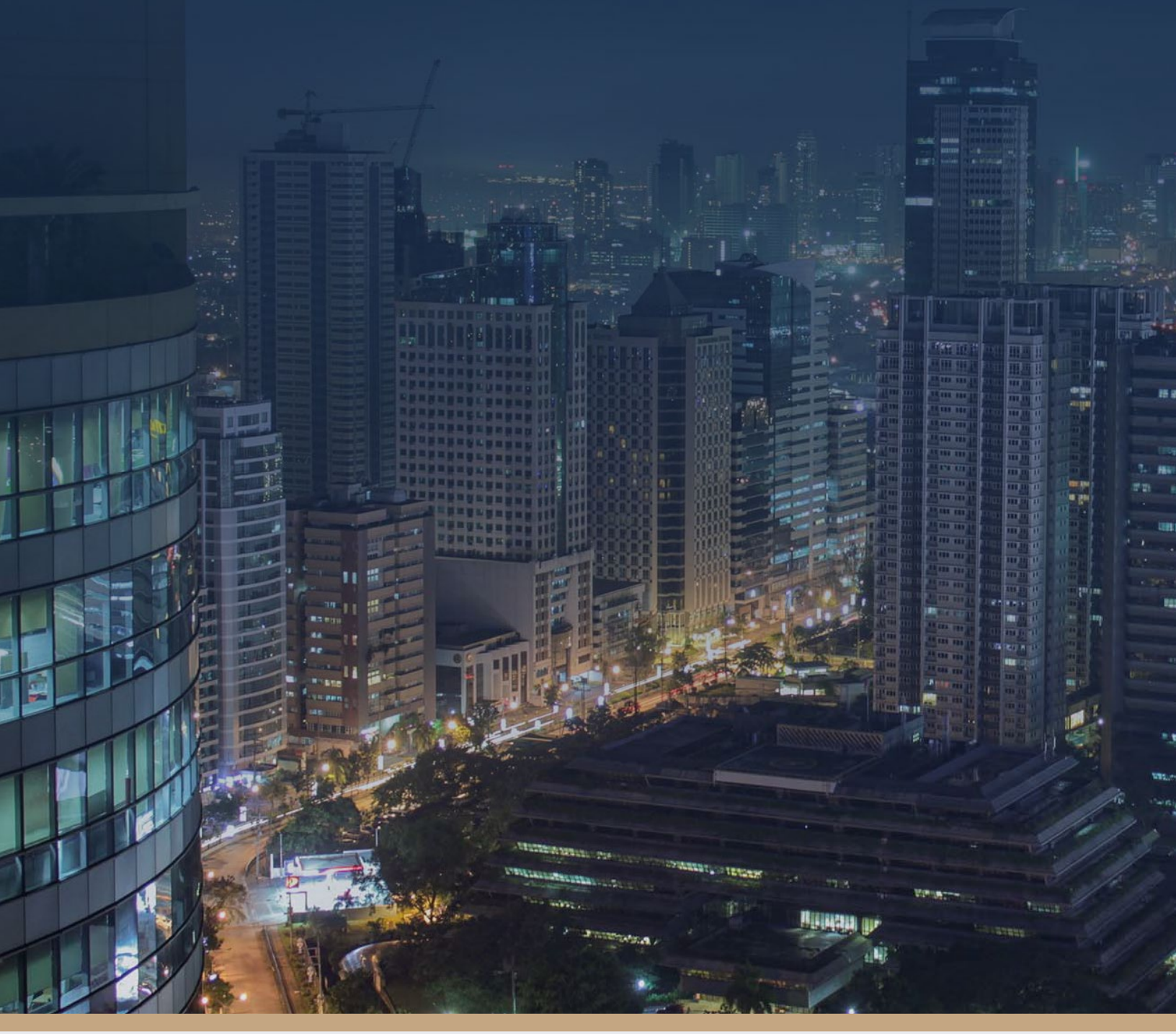
AN ADRIANOPLE GROUP REPORT | JULY 2020

Lessons and Successes

HOW PHILIPPINE ECONOMIC ZONES SURVIVED COVID-19



Adrianople Group

Helping Economic Zones Unlock Their Full Potential

Who we are

Helping Economic Zones Unlock Their Full Potential

The Adrianople Group is the world's only business intelligence firm exclusively focused on studying economic zones. We are the world's premier provider of intelligence and information services for economic zones around the world from Rwanda to Brazil.

Table of Contents

Summary

Special Economic Zones (SEZs) play a major role in the economy of the Philippines. COVID-19 has forced the country's SEZs to take drastic measures to curb the spread of the disease.

City workers wearing protective suits disinfecting the streets of Manila.
Image Source: MSN

This Report

This report highlights the successes and failures of Philippine SEZ's efforts to deal with the COVID-19 pandemic. More specifically, it:

- Summarizes the actions taken by the Philippine Economic Zone Authority (PEZA) and other government agencies in response to the pandemic.
- Illustrates the economic impact that COVID-19 will have on SEZs and local communities.
- Analyzes long term legal changes which may result from COVID-19 era legislation.
- Highlights success stories in different industries.
- Explores the long-term impact of COVID-19 on the future of SEZs in the Philippines.

Introduction

Introduction

COVID-19 has brought the end of an era to Philippine economic zones.

Over the last three years, SEZs in the Philippines have experienced slow growth due to various underlying issues. COVID-19 now poses an existential threat to the already weakened SEZ program.

Effects of COVID-19 in the Philippines

As of June 30, 2020, COVID-19 has resulted in the loss of 1,266 lives in the Philippines, with a noticeable higher proportion in urban centers. The data shows that local government units (LGUs) hosting SEZs, Highly Urbanized Cities (HUCs) and Independent Component Cities (ICCs) were found to have an average of 474 COVID-19 positive cases and 37 deaths, compared to only 14 positive cases and one death reported in Component Cities and Municipalities hosting SEZs.

The higher number of reported positive cases and reported deaths in HUCs and ICCs has mainly been attributed to urban congestion. HUCs and ICCs with SEZs had an average population density of 175 persons per hectare based on the 2015 census of population. Component cities and municipalities with SEZs, on the other hand, only had an average population density of two persons per hectare.

Sheila Coronel, a Filipino professor at the university of Columbia, describes why the effects of COVID-19 are particularly devastating in the Philippines:

> ***"The pandemic threatens to break the already frayed fabric of communities that had not yet recovered from the drug war.*** *[...] Shacks no bigger than a flatbed truck house large families whose members sleep side-by-side on wooden or cement floors. In the slums, where people are packed like bees in a hive, there is no such thing as social distancing."*[F1]

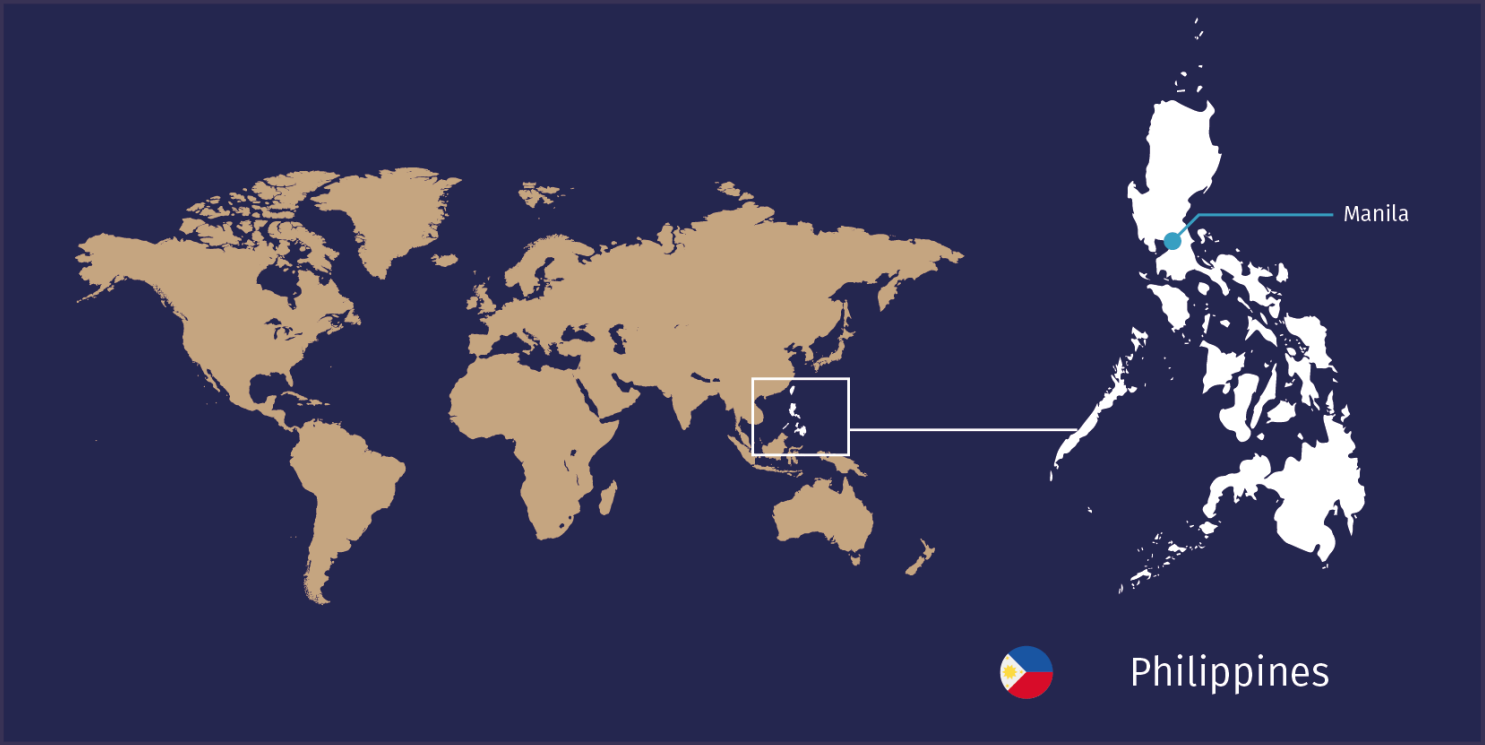
The Philippines, due to a shortage of medical workers and an already stretched health care system, has the highest mortality as a proportion of its population in Southeast Asia with 4.57 deaths from COVID-19 per million inhabitants. It also has one of the highest fatality rates for infected people at nearly 6.6%.[F175]

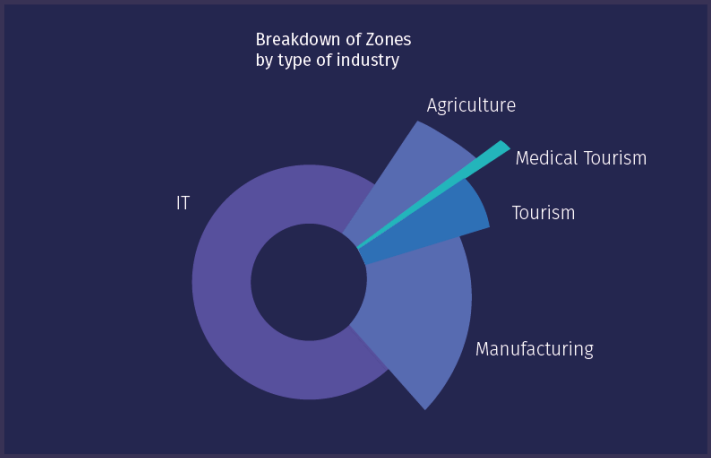
Despite all the challenges, the country's SEZs have managed to stay open for business having taken measures to protect their tenants from COVID-19.

It remains to be seen whether COVID-19 will present the Philippines with an opportunity to re-invent and reinvigorate zones, or whether the outbreak will destroy the already weak zone program in the country.

Background: Economic Zones in the Philippines

AG Infographic License: The following infographics are in the Public Domain. It can be used, altered, or modified for any purpose





There are a total 404 zones in the Philippines

Philippine economic zones received **$2.3 billion USD** in investment in 2019

Zones account for between **60% and 80%** of all exports in the Philippines

Economic zones have created between **5 and 7 million** indirect jobs

Economic zones contributed **$1.39 billion USD** in taxes from 2016 to 2018

More than **1.5 million workers** are employed in economic zones

There are between **4000-4600** business registeres in zones

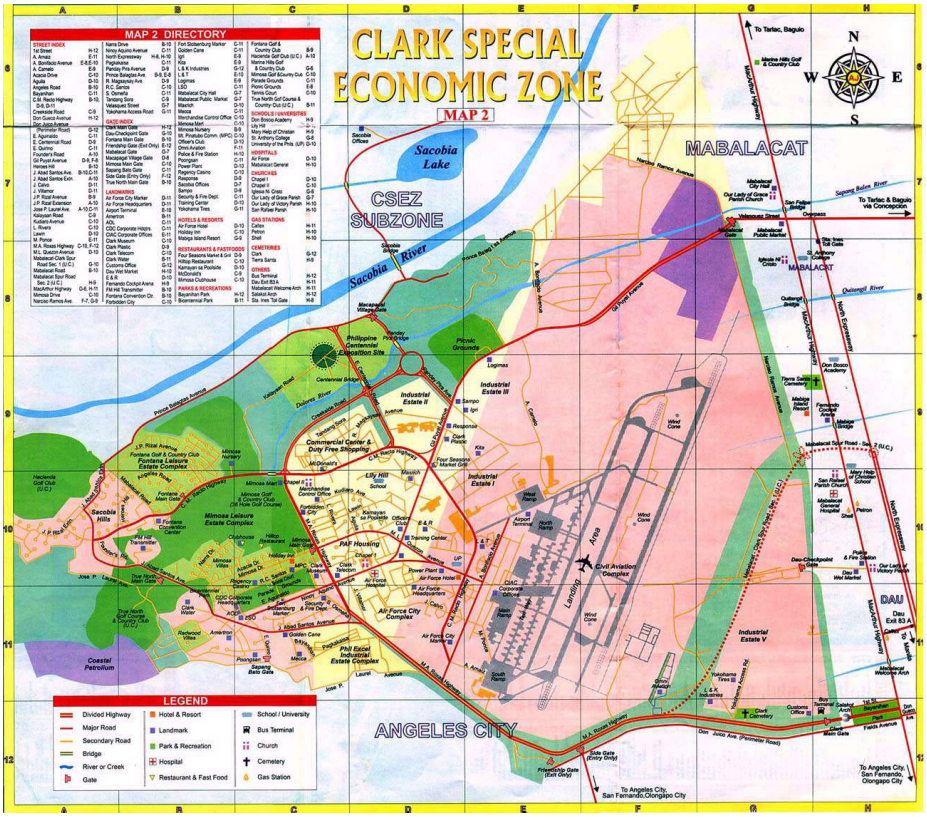
% OF EXPORTS

$3.5 billion out of $5.9 billion of the Philippine's exports originate in is economic zones

% OF FDI

$960 million out of $7.6 billion of the Philippine's Foreign Direct Investments went into economic zones

Map of Clark Freeport:



The largest zone in the Philippines is the Clark Freeport.

It is home to 1,038 registered businesses which together are worth $6.14 billion USD

Image Source: [Clark Lab]

In 1995, the Philippines began experimenting with special economic zones managed by PEZA, the Philippine Economic Zone Authority. Initially, 26 locations were identified as “ecozones,” which stand for “economic zones”, not to be confused with “ecological zones”. The initial SEZs proved successful, and the country expanded its program.

As of January 2020, the country is home to 404 special economic zones, dispersed into 24 Highly Urbanized Cities (HUCs) and Independent Component Cities (ICCs), and 100 Component Cities (CCs) and municipalities.[F18] The zones host a number of industries such as manufacturing (with products that range from garments to metals) , tourism, gambling, agriculture, logistics, shipping, and medical tourism.

Combined these SEZs play a significant role in the economy of the Philippines. They account for between 60% and 80% of total exports out of the country, and 12% of all FDI in the Philippines.[F7][F11][F144][F14] Zones employ 1.5 million people directly, and 7 million indirectly.[F144][F10] 4,600 companies are registered in PEZA zones.[F144]

Incentives Enjoyed by Businesses in Economic Zones

Tenants in the zones enjoyed a variety of incentives.

FISCAL INCENTIVES:

- 4- to 6-year tax holiday that temporarily exempts certain industries from all corporate income taxes
- 5% corporate tax rate after the tax holiday ends
- Possibility to extend corporate tax holiday under certain conditions
- Variety of industry specific corporate tax exemptions
- Tax and duty free importation of raw materials, capital equipment, machinery, and spare parts
- Exemption from export tax
- Exemption from all local government taxes and licensing fees
- Exemption from wharfage dues
- Exemption from various logistics fees
- Coverage of costs for all government licensing fees
- Zero VAT on purchases made inside zones under certain conditions

Note that certain taxes, such as the real estate tax, are collected in the zone at normal rates.

REGULATORY INCENTIVES:

- Expedited VISA process for foreign workers
- Permission to employ foreigners
- Simplified Import / Export regulations
- Exemption from many province, city, and municipal regulations
- Guaranteed repatriation of foreign investment earnings

Challenges Faced by Economic Zones Prior to COVID-19

Prior to COVID-19, economic zones in the Philippines already faced serious challenges which threatened the integrity of the program.

Due principally to uncertainty over tax law, investments fell 44% in 2018 and 12.6% in 2019. [F12] In 2018, SEZs received USD2.38 billion in investments. By 2019, that figure had fallen to USD2.13 billion, these figures already revealed weaknesses. [F12]

USD590 million worth of investments were made in the manufacturing sector in 2019, down by 5% from 2018. The Information Technology (IT) industry invested USD300 million into SEZs in 2019, down 30% from 2018. [F13]

Since 2016, the Administration of President Rodrigo Roa Duterte (PRRD) has endeavored to introduce a series of economic reforms to accelerate the reduction of poverty, and to sustainably address inequality. These reforms are embodied in the proposed Comprehensive Tax Reform Program (CTRP). Package 1 of these reforms has been achieved through Republic Act (RA) No. 10963, also known as the Tax Reform for Acceleration and Inclusion (TRAIN).

The attempt to pass Package 2, known as the Corporate Income Tax and Incentive Reform Act (CITIRA) drew controversy because the tax reform proposal would lower corporate taxes everywhere in the Philippines and close tax loopholes reducing the competitive advantage of SEZs. As a result of the uncertain impact of the pending law on businesses inside SEZs, many major companies have disinvested and relocated their resources to more promising jurisdictions.

The latest iteration of CITIRA, now known as the Corporate Recovery and Tax Incentives for Enterprises (CREATE), has been incorporated as a component of the post-COVID-19 Philippine Program for Recovery with Equity and Solidarity (PH-PROGRESO).

For a full explanation of the tax reform debates in the Philippines click *here*.
In addition to questions of uncertainty regarding corporate taxation, government regulatory agencies suffer from generalized inefficiency.

The government has been very slow in approving new IT parks and SEZs. An estimated USD3 billion in projects have been delayed across the country.
[F8] Major foreign development projects such as the Japanese-funded Subic Bay Freeport Zone and Chinesebacked Sangley Point International Airport project have faced major challenges. Despite theFilipino government's efforts to urge the foreign investors along, the projects continue toaccumulate delays.[F4][F5]

A number of zones are also embroiled in individual conflicts and legal disputes. For example,the Mactan Economic Zone was embroiled in a long running conflict with the Mactan-Cebu International Airport over the construction of a runway which would extend into the zone. [F6]

Zones have had a long history of intense conflicts with militant labor unions. The law that created SEZs stipulated that a body composed of one representative each from the Departmentof Labor and Employment (DOLE), the labor sector, and the business and industry sectors was to be created. This has been unsuccessful and the police have been required to set up offices onsite, this has resulted in accusations of union busting. [F25][F26][F27]

Risk from Natural Disasters

Even without COVID-19, the Philippines has been facing several geo-hazard risks.

One of the most devastating natural disasters has been Super Typhoon Haiyan, which hit the central Philippines, destroying the production plants inside the Leyte Industrial Development Estate (LIDE), and disrupted the operations in other SEZs in the Visayas. The LIDE Management Corporation, in close collaboration with the business locators and the LGU of Isabel, Leyte, immediately embarked on the clearing of roads, and the rehabilitation of electricity and water services to the SEZ.

Being situated along the Circum-Pacific Belt, also known as the Ring of Fire, the Philippines has its share of earthquakes. Although most infrastructure inside SEZs could withstand strong tremors, support infrastructure has been affected. An earthquake that had its epicenter in the geothermal fields of Leyte resulted in severe damage to major transmission lines, and led to a three-month total black out for the islands of Leyte and Samar, and the interruption of electricity supply to Luzon and the Visayas islands. The SEZ was able to mobilize its power generators to continue operating.

Volcanic eruptions also affect the area. On January 13, 2020, Taal Volcano on Luzon, the largest island of the Philippines, erupted. As a direct result of the eruption, 39 people died, and a cloud of toxic ash spread around the volcano in a 14 km radius. Demand for N95 masks increased rapidly as a result of the eruption, and depleted the country's stockpiles only weeks before the spread of COVID-19 in the country.

The eruption affected business operations in 60 zones located near the Taal Volcano. [F30] Initially, PEZA officials attempted to reassure investors that the eruption would not significantly impact economic zones in southern Luzon.[F28] However, PEZA was forced to order zone operators in the vicinity to relocate business operations to avoid the toxic volcanic fallout.[F29] PEZA estimated that zones in the region lost roughly 10% of their capacity as a result of the eruption.[F33]

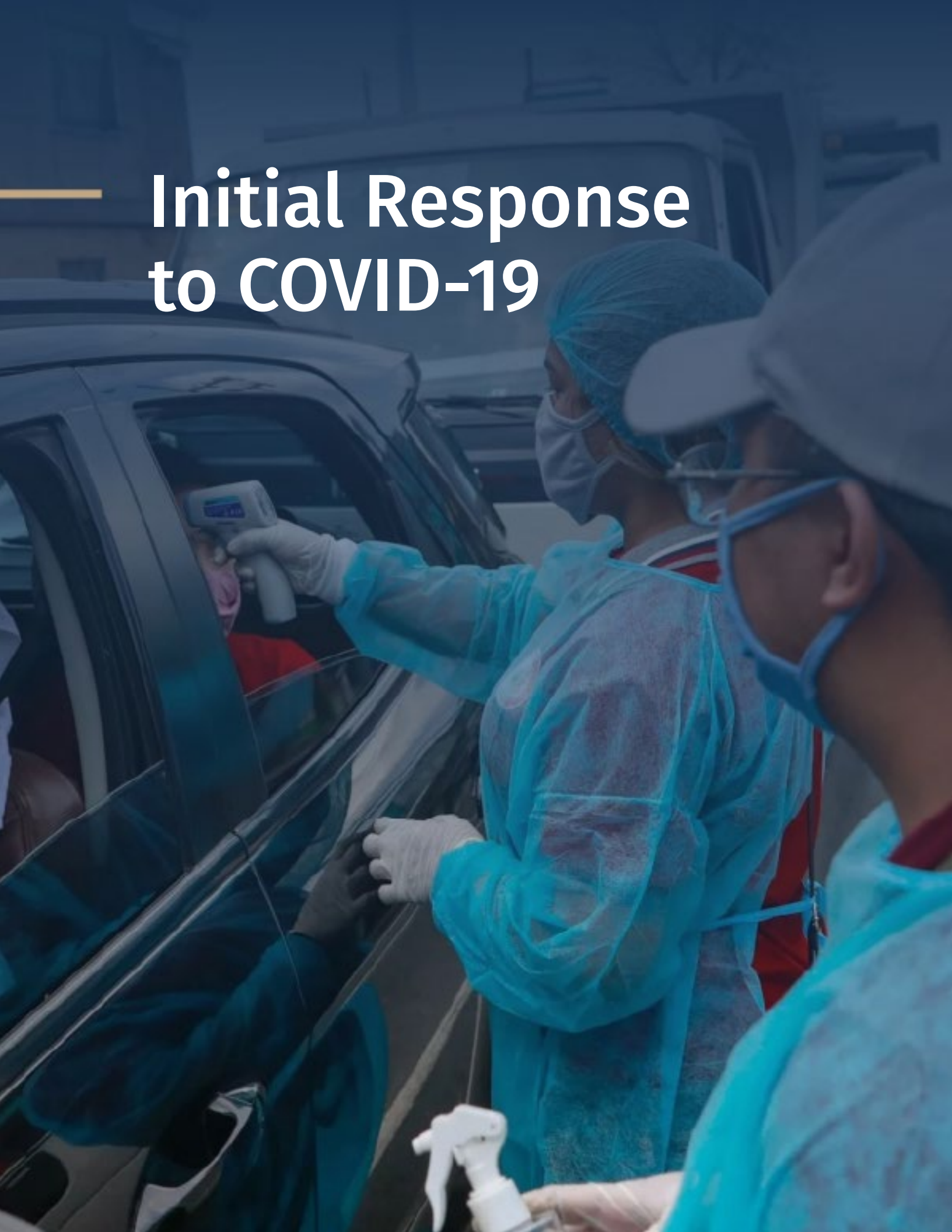
To reduce the impact PEZA decided to give zones affected by the volcanic eruption tax holidays. This relief included the extension of the ordinary income tax holiday, tax and duty-free importation of face masks, and other relief benefits.[F31][F32] PEZA also made it compulsory for future ecozone developers to get geohazard clearance on top of the environmental compliance certificate (ECC).

These experiences provided SEZ management, business locators and LGUs with ample impetus to prepare for natural hazards to minimize disruptions to SEZ operations.

While none of the zones in the region were directly damaged by the eruption, the Philippine Army (PA) began training SEZ workers, as if they were army reservists, to respond to disasters.[F30] The government announced that it would implement disaster preparedness measures for all of the zones throughout the country. These measures would not be implemented in time for the COVID-19 lockdown.[F30]

The Philippines is located along the Ring of Fire, a path where many of Earth's earthquakes and volcanic eruptions occur.

Initial Response to COVID-19



Initial Response to COVID-19

Optimism for the SEZs in 2020 would soon be dashed by the onslaught of COVID-19.

Despite these challenges, 2020 might have been a good year for SEZs if COVID-19 had not struck when it did. For example, as late as mid-February, **Fitch Ratings revised its outlook of the Philippines, upgrading its credit rating from BBB+ to A on hopes that the corporate tax reform controversy had been settled.**[F51]

PEZA also had ambitious plans for various new types of economic zones, such as defense industrial complexes which would allow the Philippines to produce military equipment and weapons of its own.[F56]

The House of Representatives passed the 2020 House Bill (HB) 6489, on March 9, proposing the creation of the Leyte Ecological Industrial Zone (LEIZ). Once approved, the LEIZ would be the first ecological industrial zone in the Philippines.

On January 28, 2020, the first cases of COVID-19 in the Philippines were confirmed. Since then the number of cases in the country continued to increase exponentially, with 157,918 by August 15.

COVID-19 has negatively impacted businesses from nearly all industries in the Philippines. Within two weeks of the first reported case, consumer spending began falling. Ben O. de Vera reported in the INQ Inquirer Business on May 7, 2020, "the COVID-19 lockdown...**since mid-March already cost the Philippines forgone output worth 5.8 percent of its gross domestic product (GDP)**".

The *Bangko Sentral ng Pilipinas* (BSP-of the Philippine Central Bank) immediately cut interest rates, pre-empting the possibility of a much worse crisis ahead. [F52] Other government agencies announced the implementation of a four-day workweek to curb the spread of the virus.[F64] Major producers associations, such as the Confederation of Wearable Exporters of the Philippines, began implementing forced leave among its workers due to the fall in demand of their products.[F62] Hospitals began rationing personal protective equipment (PPEs), and preparing for the worst. Most shipping to the Philippines from countries with high numbers of infections, such as China, stopped.

The entire country braced itself for the worst epidemic in recent human history. And PRRD issued Proclamation No. 929 declaring a state of calamity throughout the Philippines due to COVID-19.

Central Government Response to COVID-19

In the months following the outbreak, the government would pass a variety of measures designed to curb the spread of COVID-19 and prevent an economic recession, many of these directly affected SEZs hampering their activity.

Among the first government measures implemented to halt the spread of COVID-19 were travel bans. The Inter-Agency Task Force for the Management of Emerging Infectious Diseases (IATF) quickly approved the temporary restrictions on the issuance of visas for travelers coming from China. Just weeks after the first cases were reported in the country, the Philippines had temporarily revoked its VISA on arrival program, and essentially closed its borders.[F140]

Ninoy Aquino International Airport

Lockdown

Passengers attempting to book the last flights out of the country at the Ninoy Aquino International Airport hours after the announcement of a country wide lockdown

Image Source: NBC

In addition to national restrictions, various local government units (LGUs) imposed their own restrictions to curb the spread of the virus. For example, the island of Cebu, home to many of the largest SEZs, imposed a complete domestic air travel ban.[F132]

Virtually all cities took strict measures to curb the disease. General Santos City, the 15th most populated in the country, deployed military and police checkpoints, ordered non-essential businesses to cease operations, and closed all public places.[F138] Luzon, the most populated island in the country and home to the capital city, Manila, implemented an "enhanced community quarantine" that barred all travel and included strict stay at home orders.[F148]

The government has initiated various measures designed to stimulate the economy and prevent a recession. Dubbed as Recharge PH which built on the work of the IATF Technical Working Group for Anticipatory and Forward Planning led by the National Economic and Development Authority (NEDA).

Most notably as part of an accommodative monetary stance this includes a **USD3.76 billion initiative using negative interest rate loans to businesses to encourage employee retention**, aiming to stimulate the economy.[F133]

Subsidies to state-owned companies had been increased by roughly 300% during the first quarter of 2020, and will likely stay high throughout the rest of 2020.[F191] The government-owned Power Sector Assets and Liabilities Management Corp., which provides power to most companies in Philippine ecozones, has granted its customers a grace period allowing the deferment of payments of usual fees to a later date.[F155]

Writing for Business World, commercial lawyer Tiffany Ann would say:

"Indubitably the economy will take the hardest hit. It is a daunting challenge for the government to balance the economy and the health of the populace. While we are, of course, very concerned about people's health, we need to keep the economy going. Some businesses must operate, albeit not 'business as usual' and with very stringent restrictions." [F148]

Children being sprayed with disinfectant before entering a government building

Image Source: Getty

PEZA Response to Government Quarantines

The quarantine measures came as a huge blow to the tenants in PEZA zones.

Soldiers on patrol assisting with relief efforts in the Philippines

Image Source: AP

Many of the measures forced SEZ tenants to make difficult choices and hindered their ability to operate.

PEZA officials worried that the quarantine measures, combined with two years of negative growth, could be a deathblow to the Philippine SEZ program. As a result, PEZA has opposed various quarantine measures and is a major advocate of re-opening the economy.

Describing her concerns surrounding the quarantine rules, PEZA Director General Charito Plaza said:

"My worry is, if these government prohibitions and requirements will stay longer, companies might transfer their production quota to other countries' branches of our investors and ultimately transfer entire investments outside the Philippines."[F149]

Despite these disputes, PEZA is working closely with other government agencies to prevent the curb of the disease, and re-open the economy as efficiently and rapidly as possible.[F167]

PEZA's PR Strategy

PEZA has carefully adjusted its public relations strategy, and has successfully navigated this pandemic.

In terms of its PR strategy, PEZA aspired to achieve several key objectives, namely:

- Reassure current tenants and investors so that they don't leave Philippine SEZs
- Reassure investors of incomplete and future projects so they don't terminate their business plans
- Convince the Philippine public of the long-term value of SEZs
- Rally support from other local, municipal, and national government agencies
- Prevent quarantine measures that hurt its tenants the long-term value of SEZs

PEZA director Charito Plaza speaking at an April 2020 conference about the need to loosen COVID-19 related lockdowns

Image Source: BM

Initially PEZA avoided making public references to COVID-19. Privately, PEZA opposed the implementation of quarantine measures, which they believed would hurt businesses in zones. As late as March, PEZA continued its long running policy of promoting news stories designed to increase public and investor confidence. For instance, PEZA spread news that the town of Sablan had announced plans to become designated as an economic zone. PEZA would also unveil plans to expand economic zones in the northern city of Baguio.[F57] [F58]

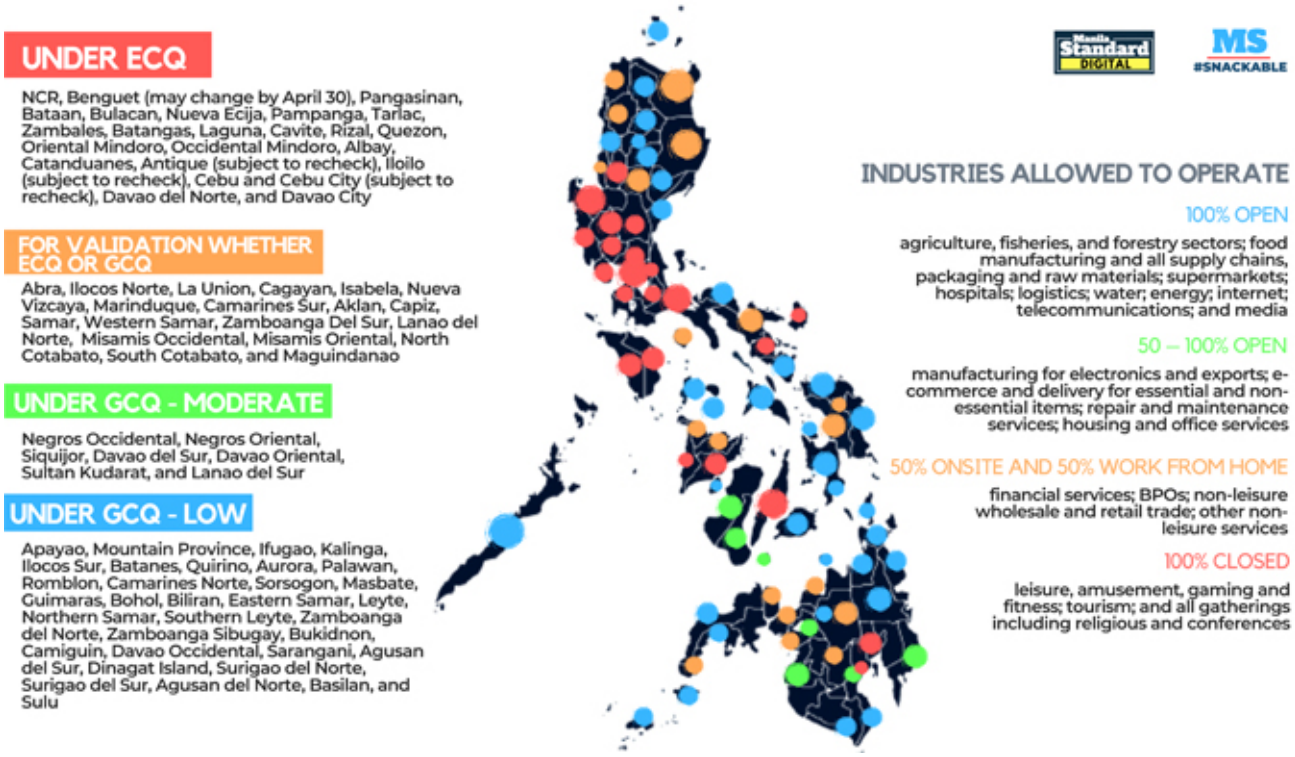
However, as March progressed, the number of COVID-19 cases involving SEZ workers around the country began to rapidly increase.[F60] This would result in a strong response by the central government as well as local governments, forcing PEZA to begin implementing quarantine measures of its own.

PEZA then shifted its PR strategy. Instead of ignoring COVID-19, PEZA would now highlight the effectiveness and efficiency of its measures.

PEZA then changed its promoted stories to those about how businesses in SEZs produce essential medical supplies. In addition, PEZA engages in a wide variety of charitable projects designed to both help vulnerable populations survive the pandemic, and generate positive press.

Quarantine Measures in **Filipino SEZs**

PEZA's successful measures have helped curb COVID-19 in SEZs and allowed economic activity to resume.



Map made by the Manila Standard illustrating which zones are open and closed under Enhanced Community Quarantine (ECQ) in late April 2020. Image Source: Manila Standard

These measures have two key objectives, which must be balanced:

- Preventing the spread of COVID-19 in SEZs
- Allowing its tenants to resume operations

The specific details of the quarantine measures implemented by PEZA evolve rapidly on a week-to-week basis. However, they always seek to balance the two key objectives.[F135]

Describing the challenge of balancing these two objectives, PEZA Director General Charito Plaza said:

> *"We are doing our best not to cripple the economy, but also to protect each other in times like this because, as Filipinos, it is our inherent duty to our flag and our country. At the same time, we want to give the best quality of service to our clients despite the threat of COVID-19."*[F135]

"Social distancing and thermal scanning are being implemented on all vehicles. Facial masks are also required for their employees when going to work. Big companies have also adapted the work-from-home scheme and provided housing for their skeletal workforce who will need to come in."[F142]

One measure PEZA has implemented to achieve its goals is "skeleton crews" that designate limited specified workers as allowed to physically enter the site as they are key to maintaining business activity. This has allowed business to continue despite lockdowns.[F135][F142]

In addition to limiting the number of workers allowed in zones at a time, PEZA also encourages tenants to implement "alternative work schemes" so that workers do not have to be physically located in zones. These include a four-day work week, exemptions from various quarantine protocols for cargo, and a variety of work from home programs.[F135][F136]

PEZA Economic Relief Measures

PEZA has also implemented a number of economic relief measures to help its tenants weather the pandemic.

Soldiers watch on as commuters prepare to go to work

Image Source: Bloomberg

Under normal conditions, PEZA allocates benefits on a “use it or lose it” basis. Tenants who own inactive businesses registered in PEZA zones lose certain benefits. PEZA does this to prevent inactive companies from using up available real estate space in zones. It also prevents companies being registered in zones to avoid taxes, but de facto operating elsewhere in the country.

Due to COVID-19, PEZA has outlined conditions where tenants are able to temporarily cease operations in the zones without losing benefits. These include:[F143]

- Lack of raw materials and inputs due to closure of foreign suppliers
- Shortages of workers to travel bans, stay-at-home orders, and the lack of public transportation
- Cost overruns caused by virus-related expenses such as emergency housing, utility outages, and other expenses

Companies aiming to shut down need to seek permission from PEZA regulators.[F146]

The new quarantine rules also allows companies to partially relocate their equipment and operations overseas for the duration of the crisis.[F146]

PEZA has also implement numerous financial relief measures, such as:[F192]

- 90-day suspension of rent payment
- 30-day suspension of utility payment
- 90-day grace period for all prior unpaid bills
- Deferment of permit and processing fees

March 2020 PEZA Guidelines

On March 5, PEZA would release a number of guidelines for tenants operating in economic zones.[F165]

Workers in hazmat suits disinfecting the streets of San Juan City in the Philippines

Image Source: Asia Times

These guidelines, modified and clarified on March 20, included:[F147][F166]

- Unhampered movement of ecozone cargoes and company shuttle vehicles ferrying workers within the immediate vicinity of the ecozone after the March 20 deadline, unless revoked by the IATF.

- Quarantine measures such as work-from-home arrangements, maintaining a skeletal workforce on-site, provision of housing for the workers either inside or near the zone, social distancing, and use of shuttle services all to be strictly complied with. Provision to employees of face masks, other protective equipment, alcohol, and sanitizers. Also, the frequent sanitizing of the workplace to be observed and practiced.

- Ecozone workers on board company shuttle vehicles to present at PNP- LGU checkpoints: a) valid company identification card; b) Proof of Residence; and c) proof of employment.

- Ecozone workers need not present separate IATF IDs as company-issued IDs would suffice. PEZA certifications/vehicle stickers/placards indicating ecozone destination to be distributed to qualified locators after due vetting by their respective Zone Administrator of the strict compliance with the quarantine measures.

- Joint PEZA-Customs Offices (JPCOs) at the Ninoy Aquino International Airport (NAIA), the Port of Manila, and the Manila International Container Terminal to have no skeletal workforce on Saturdays and Sundays.

Economic Impact of Zone Closures and Quarantines

Economic Impact of Zone Closures and Quarantines

Generalized lockdowns have had significant negative economic impacts on zone tenants and surrounding populations.

A young boy and girl hold hands at a bus terminal in Manila

Image Source: VOA

These guidelines, modified and clarified on March 20, included:[F147][F166]

Hundreds of thousands of workers living near SEZs found themselves unable to work. 68,000 workers in the Cavite Economic Zone, and 100,000 workers in the Mactan Economic Zone would lose their jobs.[F150][F141] In Luzon alone, 750 tenants operating in zones would cease operations, leaving their employees without work.[F164]

Investments into SEZs have continued falling in 2020 by 28% from USD450 million in the first quarter of 2019 to USD330 million in Q1 2020.[F170]

Exports originating in SEZs fell by 66% from USD12.94 billion in the first quarter of 2019 to USD4.36 billion in Q1 2020.[F170]

Case Study: Closure and Reopening of the Cavite Economic Zone

Nearly all SEZs in the Philippines experienced temporary COVID-19-related closures. Due to PEZA's handling the closure of Cavite only lasted four days, with business resuming in less than a week, mitigating the potential economic losses.

Returning to Work
Workers wear masks to enter the Cavite Economic Zone in May 2020
Image Source: Richard A. Reyes

Established in 1995 at the start of the SEZ program in the town of Ternate, Cavite, 30 km south of Manila, the Cavite Economic Zone has grown to become the largest manufacturing zone in the country with 439 tenants in 2020.[F142] Just prior to COVID-19, the zone exported $3.5 billion USD worth of goods.[F151]

In early March 2020, the areas surrounding the Cavite SEZ reported 10 cases of COVID-19. The Provincial LGU declared a "state of calamity" and ordered businesses to cease operations. This order did not apply to the Cavite SEZ, as only PEZA has regulatory jurisdiction over zones.[F142]

The LGU hoped to close the zones to prevent the spread of the virus, whereas PEZA sought to continue business operations, triggering a short dispute.

On the evening of March 19, 2020, PEZA ordered businesses in zones to cease operations.

By morning, the **68,052 workers were informed they were out of work by a PEZA memo** that stated: *"No employee shall be allowed entry into [the Cavite SEZs] starting 6:00pm today, except those designated as part of the skeletal force, without express approval of the Zone Administrator."*[F141][F142][F143]

Following the closure, PEZA embarked on a public relations campaign to reassure worried tenants who were upset by the disruption. PEZA began holding meetings with the tenants, trying to juggle their requests with the aims of the Luzon authorities who were trying to implement a strict lockdown. PEZA Director General Charito Plaza gave interviews explaining that zone operations were continuing as normal elsewhere in the country. She cited that 89% of companies operating in zones were continuing to do so as normal, in full compliance with lockdown measures.[F144][F145]

Finally, on March 24, four days after the start of the closure, PEZA decided to re-open the Cavite SEZ, albeit with strict rules governing the operation of companies under quarantine conditions.[F145] PEZA Director General Charito Plaza would say:

"The resumption order aims to attain PEZA's overall goal of business continuity so as not to cripple the economy during this period. We are thinking of the employment of more than 60,000 Filipino workers and maintaining our economy [to survive the] crisis caused by COVID-19. PEZA's exporters are global market-driven, and are most vulnerable to world trade and military wars, local and global disasters, or calamity like the global pandemic COVID-19, amongst others. However, we will do our best to not totally shut down our economy and the livelihood of our thousands of workers. [...] Nevertheless, PEZA will strictly enforce and comply with the health and quarantine measures and requirements as mandated by the National Government. The Authority assures that it values the health and safety of its locators, workers, and surrounding communities and supports the government's effort in trying to stop the spread of COVID-19."[F145]

Only 16 of the 439 companies in the Cavite Economic Zone would resume operations in the week following the decision to reopen.[F151]

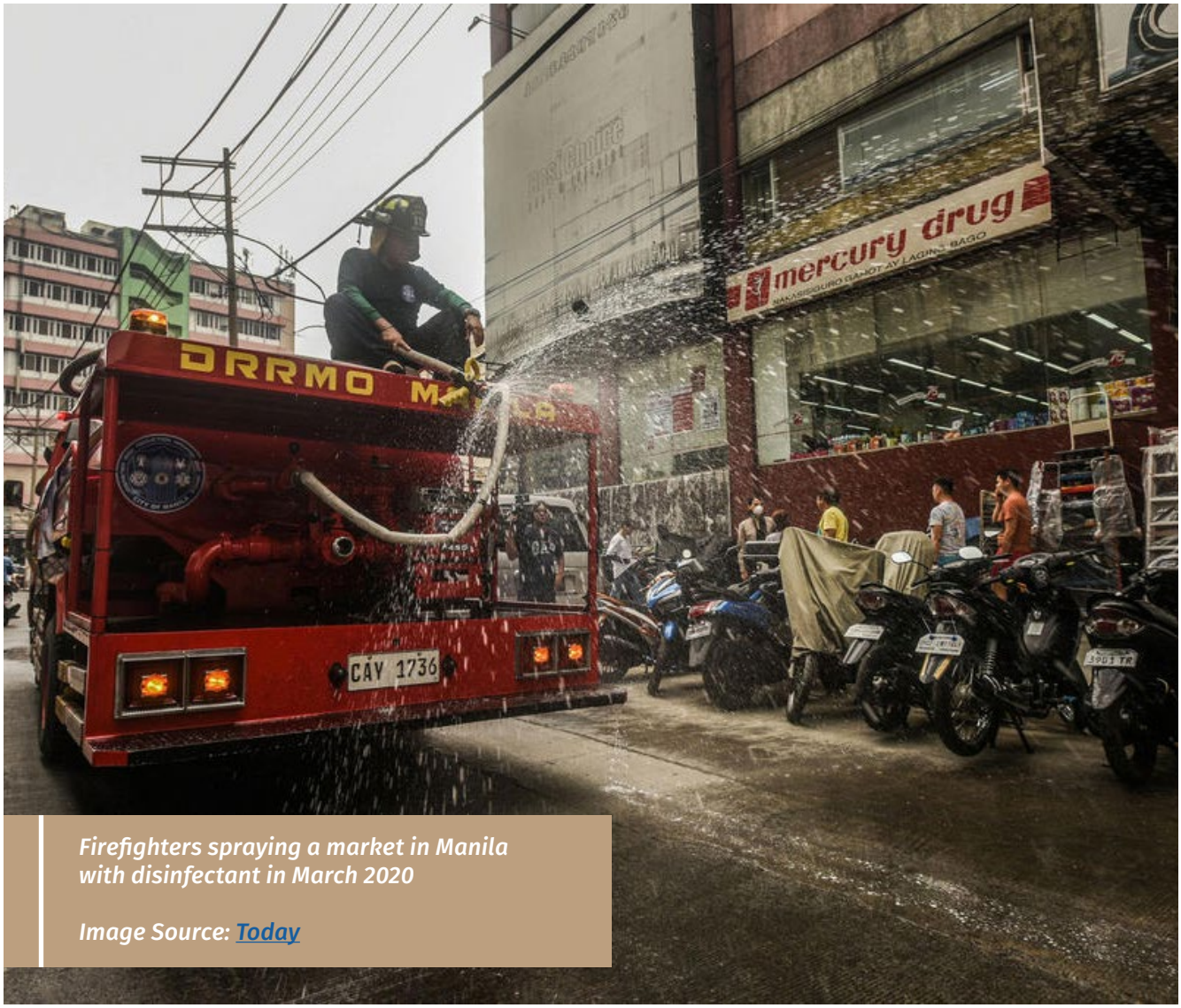
These companies only operated in a limited capacity with a small skeleton crew "barely keeping afloat the export-oriented industry."[F151] The largest tenants, such as the Japanese HRD Group, which manufactures construction materials for houses, would remain closed. As a result, all of the HRD Group's 23,000 workers found themselves without work.[F151]

Over time, more tenants slowly re-opened, with most tenants planning to restart during the summer when the majority of workers could return to their work.

Regulatory Changes

Regulatory Changes

Many legal precedents being set by COVID-19, such as work at home policies, would likely outlast the pandemic. COVID-19 will reshape Philippine SEZ regulations in ways which could make them more competitive in the long term.



Firefighters spraying a market in Manila with disinfectant in March 2020

Image Source: Today

If these legal precedents remain in place, they could provide much needed relief for the country's SEZs.

In the short term, these legal changes have resulted in significant confusion among businesses located in SEZs, increasing costs of doing business and creating many new problems.

Regulatory Changes: Confusion Surrounding Quarantine Regulations

The changing rules caused confusion for both investors and tenants.

Philippine soldier at a COVID-19 checkpoint to scanning the temperature of drivers entering Quezon City on March 16 2020
Image Source: Straits Times

Following every announcement of new quarantine-related rules in the SEZs, PEZA reported its entire staff would be overwhelmed with inquiries and questions.[F147]

Concerning the confusion, PEZA director Charito Plaza would say:

> *"There have been many questions, suggested solutions, interpretations of directives and memos from various agencies at the moment. With our three deputy director generals, zone administrators, zone managers, and few others, we are corresponding 24/7 just to keep everything in order. We are also making urgent solutions so our investors and employed Filipino workers will be assisted."*[F147]

For its part, the Board of Investments (BOI) pitched into the effort by facilitating requests for Enhanced Community Quarantine clarification. Specifically pertaining to:

- IATF Resolutions
- DTI MC 20 08 Guidelines
- PNP Department Order related to Authorized Persons Outside Residence
- Philippine Port Authority Guidelines
- FDA Guidelines related to importations of PPE, etc
- BOC/ MICP Guidelines
- DICT and NTC Advisories
- DENR Advisory/Guidelines
- PEZA Advisory/Guidelines
- DILG Advisory/Guidelines
- DOT Guidelines
- BI Guidelines
- DFA Guidelines relative to ECQ

Despite clarifications, many companies operating in zones continued reporting trouble moving cargo due to complicated and unclear rules surrounding checkpoints.[F149]

To facilitate the quick issuance of pertinent permits, the BOI acted on the following:

- DENR clarification pertaining to the lifting of the suspension order on the transport of wood and wood products
- DICT clarification relative to the issuances of IATF IDs for IT BPOs that were in conflict with DTI MC 20
- DICT and NTC clarification and guidelines on the IATF ID issuances for TELCOS
- Inclusion to the APOR of the Toxic industrial and hospital waste and ATM Service Provider Crew
- Philippine Port Authority resolutions relative to the case of MTKR Sausalito Vessel,which was loading Palm oil in the port of General Santos City wherein the crew members were subjected to a 14-day quarantine
- Approval of LGU Officials, particularly Barangay Chairpersons, to allow the entry and exit of personnel and movement of goods under APOR

- FDA and BOC guidelines on the importations of PPE and other medical devices
- In-kind donations of private sector entities to the Office of Civil Defense (OCD) delivered through the Bureau of Customs (BOC)
- Travel Exemption approval from DFA and BI
- PNP approval to travel and enter into various PNP QCP of Export Oriented shuttle vehicles involved in the manufacturing of medical equipment/parts urgently needed by hospitals

These confusing regulatory changes are expected to end as the Philippines reopens for business.

Regulatory Changes: Worker Housing

One of the most troublesome quarantine regulations for companies in SEZs is the rule that companies have to house workers within their premises.

Workers in the Philippines headed to work in March 2020

Image Source: Aljazeera

A PEZA memorandum stated the new rules:

> *"There shall be no commute or pick-up of employees from place of residence or pick up point to zone."*[F152]

The purpose of this rule was to reduce travel and contact with outsiders and employees of other zone companies, hopefully slowing the spread of the disease.

The rules allowed for off zone housing as long as a strict quarantine was maintained, travel distances limited, and transport was provided by the zone tenants.[F151][F152]

Because companies had to house workers in or near the zone to minimize travel and the potential for infection, many companies struggled to find adequate housing for the workers. For example, **the 16 firms which resumed operations in the Cavite Economic Zone had to house their workers in a nearby touristic resort which was empty as a result of COVID-19**.[F151]

This rule significantly increased operating costs for companies, and forced the government to look for alternative solutions.

PEZA appealed to the government for help to aid its tenants in finding affordable housing for the ecozone workers. On March 28 2020, PEZA Director General Charito Plaza appealed directly to President Rodrigo Duterte for assistance in housing PEZA workers. In the public letter, she explained that **PEZA was home to 1.6 million workers, and finding temporary accommodations near zones was extremely difficult. She proposed that schools, warehouses, and other government buildings could be used to house SEZ workers**. She also asked for government assistance in transportation and protective equipment for the workers, and for a relaxation of the rules.[F153][F154]

Regulatory Changes: Corporate Tax Reform

COVID-19 has become a major lynchpin in the debate about whether or not the Philippines should engage in corporate tax reform.

The last major wave of tax reform in the Philippines was the Tax Reform Act of 1997, which cut tax rates but created numerous exceptions and loopholes.

PEZA, which was only two years old at the time, enjoyed numerous highly favorable tax incentives. Over time, the presence of tax loopholes became increasingly controversial.

Furthermore, neighboring countries had slowly cut their own tax rates such that by 2017, the Philippines had the highest corporate tax rate in the ASEAN region, of 30%.

The country suffered from other disadvantages making it a less desirable location that other ASEAN neighbours, such as poor logistics infrastructure, high cost of electricity, and slow internet.

Supporters argued that tax reform would have several benefits:

- Closing loopholes would increase government revenues
- Lowering taxes would make the Philippines more attractive when compared to its neighbors
- Business accounting and legal costs would be reduced due to a simplified tax code

The Philippine House of Representatives has been debating corporate tax reform since 2017.
Image Source: Office of the President

In 2016, when Rodrigo Duterte ran for President of the Philippines, he vowed to embark on a massive program of tax reform to make the Philippines more internationally competitive. Shortly after winning, he began implementing his plan to reinvigorate the Filipino tax code.

The initial part of the tax reform package, called Tax Reform for Acceleration and Inclusion Act (TRAIN Act) focused almost entirely on personal taxes, and passed in December 2017 with little controversy.

The second part of the tax reform package is focused on corporate taxes. **As part of the second wave of tax reforms, the government planned to standardize and "flatten" incentives, to make them more uniform across the country.**

This caused significant uncertainty for the countries' SEZs. Notably, it threatened to transfer regulatory authority away from existing government agencies, make areas outside of SEZs more tax competitive, and reduce the incentives that could be provided to their tenants.
As a result, two political factions, respectively supporting or opposing corporate tax reform have emerged.

The first camp, which is in favour of the reform, led by the Department of Finance (DOF) and the Department of Trade and Industry (DTI), is supported by a variety of industry and trade organizations such as banks, and real estate associations. It is also supported by Chinese special interest groups, as well as think tanks promoting free market economics.

Opposed to tax reform in the second camp, is a loose coalition of diverse business interests, most notably, as the issue relates to economic zones, is the PEZA. Also opposing tax reform are import and export industry associations, the chambers of commerce of Western countries, and other operators and tenants of the SEZs.

Negotiations over corporate tax reform began in early 2018, and after extensive negotiations, came to a close in late 2019 when the DOF and DTI came to a tentative agreement with PEZA. However, this would not mark the end of negotiations.

The first COVID-19 cases were detected in the Philippines on January 31, 2020, only weeks before the planned implementation date of the new tax reform package. **PEZA withdrew from the negotiations, and argued that COVID-19 justified a more favorable version of the tax reform legislation.** In response, the supporters of the tax reform bill began incorporating COVID-19 into their arguments in favor of tax reform.

While the Corporate Income Tax and Incentives Rationalization Act ("CITIRA") Bill removes the 5% final income tax privilege after the income tax holiday enjoyed by businesses in Investment Promotion Agencies ("IPA"), i.e. PEZA Locators, it still provides for tax incentives to IPA businesses, such as the 18% preferential tax rate and additional allowable deductions to gross income.

The Corporate Recovery and Tax Incentives for Enterprises Act ("CREATE") Bill – an updated version of the CITIRA intended to placate both factions – extends the status quo period on tax incentives of IPA-registered entities from 2-7 years (in the CITIRA Bill) to 4-9 years; thus, enabling these entities further time to adjust to the new tax rates.

However, digital SEZ businesses may be exposed to payment of Value Added Tax for services rendered electronically in the course of trade or business, should House Bill No. 6765 or the Digital Economy Taxation Act of 2020 be passed into law.

If the DOF and DTI succeed in using COVID-19 as a justification to pass corporate tax reform legislation, it could spell the end of Philippine SEZs. Conversely, if PEZA succeeds in using clauses within COVID-19-related economic legislation to covertly protect its incentives, it guarantees the survival of the program for years to come.

Due to the importance of tax reform to Filippino SEZs, we have published a separate study just about the impact of COVID-19 on Filippino SEZs. Click here to read it.

Regulatory Changes: Work From Home

PEZA has given permission to IT companies to let their employees work from home.

A man walks through the empty streets of Manila on March 17 2020

Image Source: Straits Times

Prior to COVID-19, PEZA kept the tax benefits given to companies doing business in SEZs geographically demarcated. The goal of this policy is to avoid the proliferation of companies that exist on paper in SEZs, but in practice operate outside of the zones. To achieve this, PEZA only allowed employees to work from home if they had special letters of authorization issued by the agency.

On March 6 2020, PEZA issued Memorandum Circular No. 2020-011 which would allow IT workers in outsourcing firms to work from home without prior authorization.[F61] Memorandum Circular No. 2020-011 was still very limited in scope. It only automatically applies to workers exhibiting COVID-19-like symptoms, workers exposed to those displaying potential symptoms, and IT workers deemed "critical." The new rules still require companies to seek PEZA authorization if they want to allow other workers to work from home.[F61]

PEZA also allowed the firms to have IT workers working from offices and buildings located outside of the zone for the duration of the pandemic.[F61]

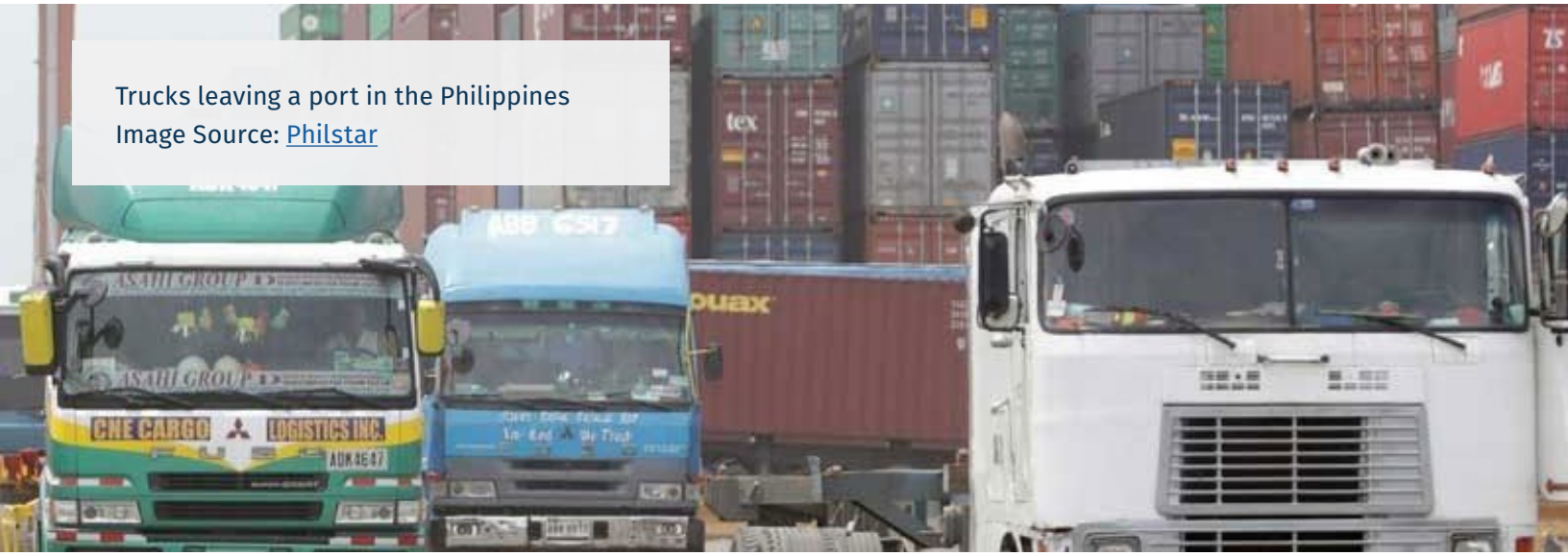
PEZA then allowed I.T. Enterprises to implement work from home operations within a limited period. Per its Memorandum Circular No. 2020-040, I.T. Enterprises could conduct work from home operations to the extent of up to 90% of their total revenues until December 31, 2020. Further, these qualified Locators need not secure a prior PEZA authorization in implementing its work from home scheme until August 31, 2020.

If this precedent proves durable and outlasts COVID-19, this has the potential to enable companies to register their businesses in the SEZs to take advantage of the tax and regulatory benefits, but still maintain a workforce that is physically located outside of the zones.

Regulatory Changes: Access to Domestic Markets

Studies from organisations such as the World Bank have found that economic zones grow faster when manufacturers and service providers can sell their products to consumers in their domestic market.[F63]

Despite this data, prior to COVID-19, many export zones in the Philippines did not allow manufacturers to sell their goods to Filipino consumers. Due to COVID-19, this may change, with manufacturers in SEZs being allowed (and in some cases required) to sell their products to the domestic market.



Trucks leaving a port in the Philippines
Image Source: Philstar

PEZA requires Locators with manufacturing, assembly, or processing activities to meet a 70% export threshold of output. Similarly, Locators performing I.T. services must also meet a 70% threshold of revenues derived from offshore clients.

In line with this, **the Department of Trade and Industry and PEZA are pushing for the creation of domestic ecozones where Locators may sell or render more than 30% of their output or services to the domestic market and still avail of PEZA incentives**.

Recent laws also provide incentives for foreign investment and promote the ease of doing business in the Philippines.

Examples of these changes are the introduction of the One Person Corporation, perpetual existence of corporations, and removal of the minimum paid-up capital requirement as stated in the Revised Corporation Code; and streamlining of procedures for issuances of business licenses/clearance/permits in the Ease of Doing Business and Efficient Government Service Delivery Act of 2018.

In March 2020, the National Economic and Development Authority (NEDA) released predictions that between 30,000 and 60,000 jobs would be lost in the tourism and manufacturing sectors due to COVID-19.[F62] To deal with the job loss, NEDA asked the senate for permission to let exporters sell their products to the domestic market, while exploring whether this measure could be implemented by a PEZA board resolution.[F62]

Strengthening the PEZA argument to allow manufacturers to sell their products domestically were the requests from prominent politicians for ecozone firms manufacturing medical equipment to prioritize domestic markets. Some politicians even attempted to pass regulation to prevent medical equipment manufacturers from selling more than 20% of their products overseas.[F168]

Should the measure be enacted, exporters located in economic zones would be allowed to sell up to 30% of their products to the domestic market, while medical manufacturers could be forced to sell 80% of the products in the domestic market.[F62][F168]

If passed, this regulatory change will set an important precedent by allowing tenants in the SEZs to take advantage of the Philippine's growing middle class of consumers, while in the process helping revitalize the SEZs. If it outlasts COVID-19, then PEZA can expect to see significant growth in many of its economic zones.

Regulatory Changes: Digital Regulation

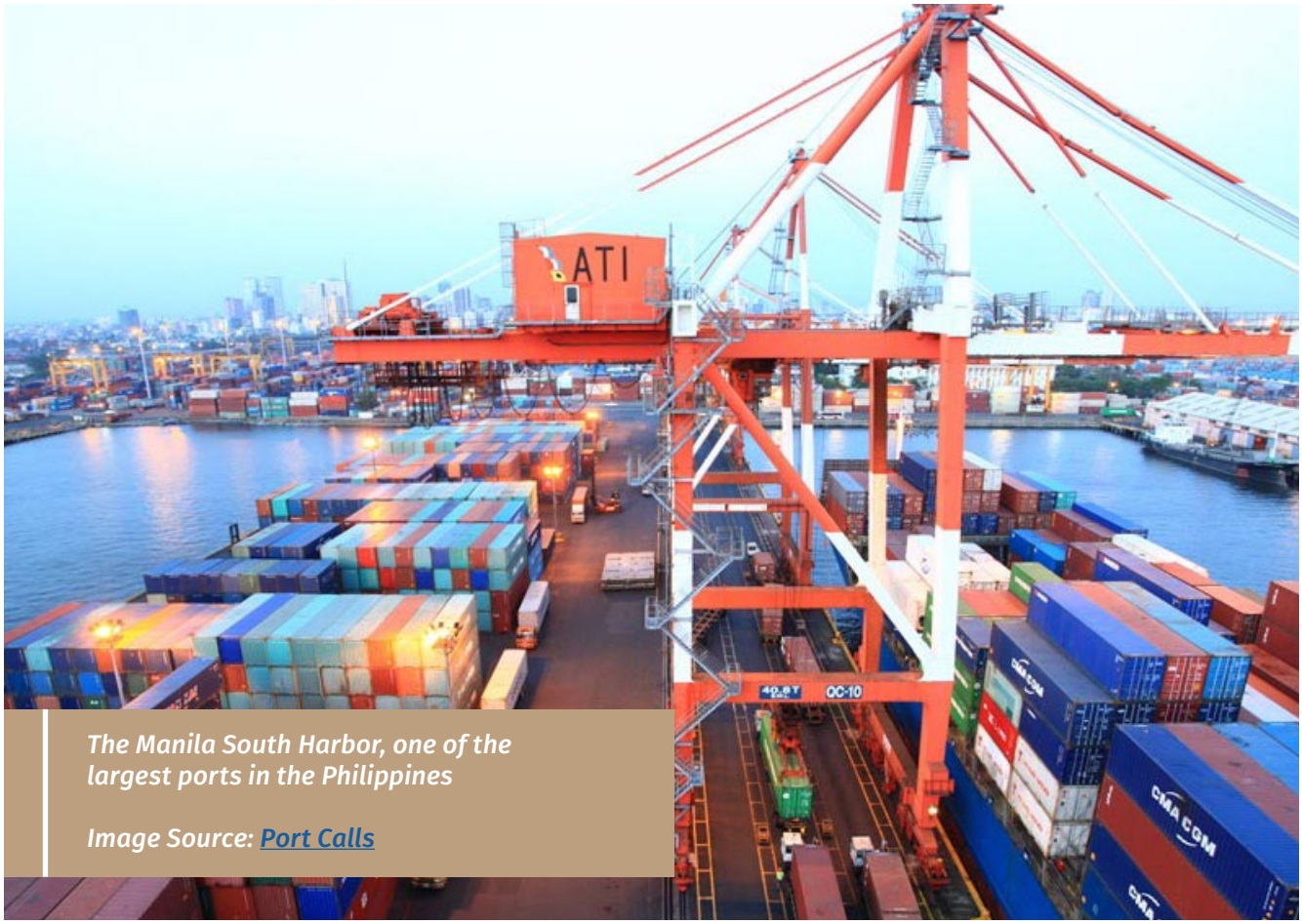
The Philippines has been working to improve the state of its digital economy, as reflected in these legislative initiatives:

- Republic Act No. 11055 (Philippine Identification System Act), implementing a National I.D. to improve access to government services and financial institutions;
- House Bill No. 6122 (Internet Transaction Bill), creating an e-Commerce Bureau to provide an online dispute resolution platform for consumers and merchants;
- Senate Bill No. 1469 (National Digital Careers Act), providing labor standards and incentives for digital career workers; and
- House Bill No. 5913 (Virtual Banking Bill), recognizing Virtual Banks as a new bank classification and providing for the creation and regulation thereof.

Ports and Shipping

Ports and Shipping

Ports play an outsized role in Philippine SEZs.



The Manila South Harbor, one of the largest ports in the Philippines

Image Source: Port Calls

The Philippine archipelago is composed of 7,641 islands, all of which need shipping. As a result, SEZs have thousands of tenants in the import-export industry.

COVID-19 threw the shipping industry into chaos, resulting in conflict and operational difficulties.

In early March, the Philippine Ports Authority (PPA) began warning sea travelers and shippers that COVID-19 would lead to significant issues and delays. The PPA implemented a variety of measures designed to curb the spread of the disease such as the routine fumigation and disinfection of all port terminals, thermal scanning of passengers and workers, the suspension of all events or conferences, the implementation of advanced contact tracing software, and the provision of disinfectants and face masks to all employees and workers.[F129][F130]

The PPA also issued a "no-disembarkment" order applicable to all non-Filipino crew members. Docking rights of foreign vessels from countries with high infection rates were cancelled altogether.[F129][F130]

On March 26, a worker in the Manila International Container Port was reported to have tested positive for COVID-19. As a result, all business operations ceased, and the port was closed for several days to undergo a thorough disinfection.[F156]

As of March 2020, over 8,000 containers including 850 refrigerated containers, which had been cleared for release, were unable to leave the port of Manila. Unclear quarantine rules, failing businesses, unexpected costs, and frequent disinfections all contributed to the container glut in the port.[F158]

A port official complained that "containers are simply not being removed from the terminal."[F158]

The presence of thousands of containers stuck in transit in Philippine ports prompted a government response. Officials of the Inter-Agency Task Force on Emerging Infectious Diseases (IATF-EID) responded by implementing measures to fast track the removal of medical supplies and PPE.[F159] Later, the Bureau of Customs (BOC) would respond to the stuck freight by implementing software to track the excess containers.[F184] And, PEZA lobbied the other regulatory agencies for simpler rules.

Shipping lobbyists argued that the response had been inefficient. COVID-19 had made it hard to offload cargo, and therefore the normal demurrage fees needed to be temporarily suspended.[F179] The Philippine shipping industry requested to extend the free storage period from five to 10 days, and to suspend demurrage fees.[F180]

Demurrage fees are charged to companies for storing cargo, which has not yet been offloaded, incentivizing shippers to rapidly offload their cargos.

Port operators urged the government to maintain the demurrage fees. Asian Terminals Inc., which operates many ports in the Philippines, responded by calling on the shipping industry to remove as many containers as possible from terminals as soon as feasible. It recommended the use of private warehouses and other solutions while the logistics complications caused by the pandemic were resolved.[F183]

As of June, the government began selling shipping containers which threatened to cause congestion.

Despite this issue, the authorities have successfully dealt with a number of COVID-19 related crises.

Cruise ship workers from around the world come from the Philippines. The closing of ports worldwide left many stranded with no way of going home, and came as a serious financial blow to the already impoverished workers.[F131] Nearly 100,000 cruise ship workers around the world would be stuck on their ships as late as May.[F176]

As the Philippines began the process of repatriating cruise ship workers, dozens of boats would arrive per day in the Port of Manila. The Filipino crew members were quarantined for 14 days, then returned to their families. Incredibly, not a single one of the repatriated cruise ship workers tested positive for COVID-19, and the process proceeded without any major issues or outbreaks.[F186][F177]

Despite the chaos, authorities worked hard to ensure that the export reliant Philippines would have continual access to maritime trade.

This was shown in the case when Chinese billionaire Jack Ma donated 500,000 masks and 57,000 COVID-19 test kits, all of which needed to be processed through Philippine ports. Authorities ensured that the process was as smooth and rapid, and that the critical supplies reached hospitals as fast as possible.[F157]

Over time, the quarantine rules imposed on ports were streamlined to help businesses resume despite the pandemic.

Chinese billionaire Jack Ma donated tens of thousands of COVID-19 test kits to the Philippines

Image Source: CNN

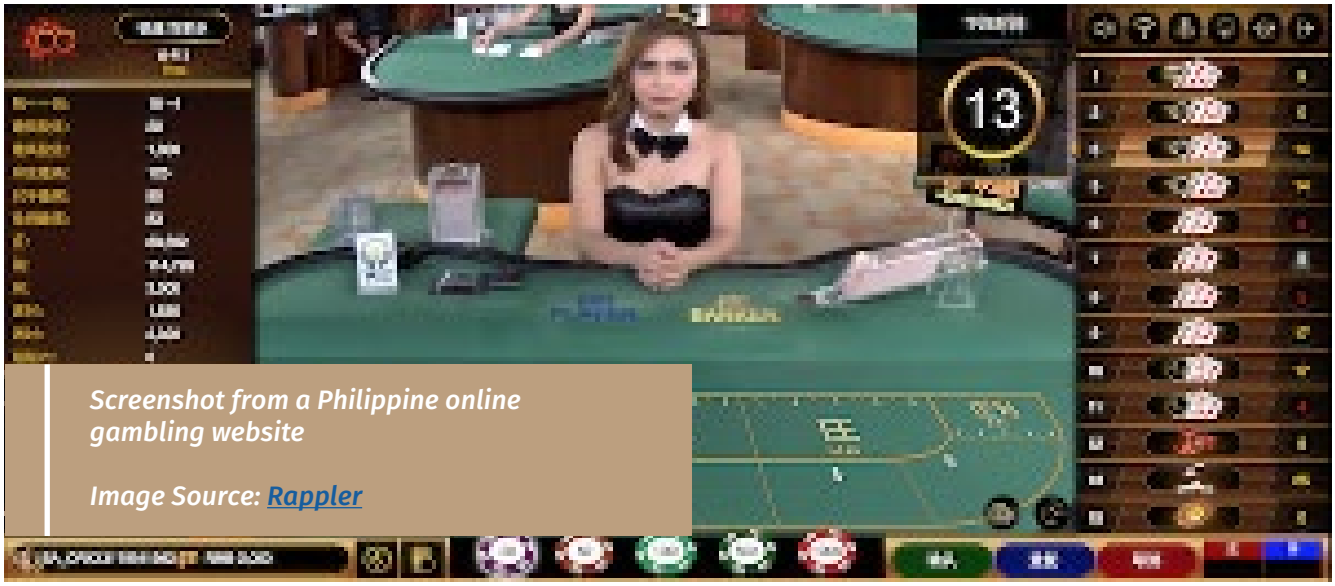
For example, the Department of Transportation (DOTr) and the PPA would amend quarantine rules requiring cargo ships to secure a special permit when going to islands under "community quarantine."[F139] With the streamlining of quarantine rules, the country's largest ports would continue operating at roughly 70% capacity into April, a normal rate during non-pandemic times.[F183] Yard utilization would also remain at 50% capacity, a usual rate.[F183]

Port officials would also continue taxing and accessing goods at normal rates, despite closures and quarantines.[F185]

Online Gambling in Filipino SEZs

Online Gambling in Filipino SEZs

The gambling industry plays a significant role in the economy of Philippine SEZs as most legal casinos are located in SEZs, and many operate as gambling hubs. In addition to physical casinos, the country hosts numerous online gambling websites geared towards an international clientele.



Screenshot from a Philippine online gambling website

Image Source: Rappler

The legal online gambling companies, known as Philippine Offshore Gaming Operators (POGOs), are strictly regulated. As of 2019, there were 60 licensed operators, with many operating out of SEZs.[F35]

POGO licensing fees are the third largest source of revenue for the Filipino government, bringing in more than $1.4 billion USD per year.[F35] With the global pandemic forcing nearly 4 billion people worldwide to stay indoors, online gambling has experienced a boom. Israeli-based online gambling firm Optimove reportedly saw unprecedented increases in its activity:

"The company saw a 43% increase in online poker games and a massive increase of 225% of people who began to play poker online for the first time, when compared to the pre-COVID-19 figures."[F38]

China, the main customer of Phillipine online gambling services has also seen an explosion of activity. Gambling.com reports that online gambling in China increased by 90% in 2020 compared to 2019.[F40]

Online gambling is both illegal and very popular in China. As a result, most Chinese citizens gamble using online casinos based out of Philippine SEZs. These casinos, although legal and state sanctioned to operate in the Philippines, are illegal for overseas Chinese citizens to use.

For years, the Chinese government has pressured countries hosting the online gambling operations, such as the Philippines, to shut their digital casinos down.

Despite the Filipino desire to continue profiting from the $1.4 billion USD industry, and the increased demand from China, POGOs have faced COVID-19 related challenges.

Travel bans implemented by the Filipino government to quarantine the country have made it difficult for the mostly Chinese POGO workers to visit the Philippines.[F37] Furthermore, many Chinese POGO operations had their passports cancelled by the Chinese government.[F45] Instead of obeying the Chinese government, thousands of undocumented Chinese workers have flocked to the Philippines to continue working at illegal online gambling operations.[F45]

Online gambling will likely continue to play an important role in SEZs after COVID-19, despite various legal and other threats to the industry.

If COVID-19 triggers a global recession, then the amount of money spent on online gambling will decrease, potentially hurting the industry.

Due to the importance of the gambling industry in Philippine SEZs, we have created a whole report about how the industry will be affected by COVID-19. Click *here* to read more.

Effects of COVID-19 on Real Estate in Economic Zones

Effects of COVID-19 on Real Estate in Economic Zones

Prior to COVID-19, potential tenants interested in doing business inside SEZs faced a shortage of office space, this situation has now reversed.

Architectural illustrations from the planned Clark Global City, an office real estate project located in the Clark Freeport Zone

Image Source: Clark Global

At the start of the outbreak, the Manila Times reported that:

"Outsourcing firms, for example, lack PEZA-approved spaces to occupy, [a researcher] said, noting that 490,000 sqm out of the 564,600 sqm of available lands in Metro Manila are already pre-leased."[F37]

Only zones in secondary cities and more rural areas such as Cebu, Iloilo, Metro Clark or Bacolod had sufficient office space left.[F37]

COVID-19's effects on the real estate market in SEZs have been severe. In a matter of months, the market has gone from overheated to underexploited. In May, experts estimated that Philippine real estate prices had fallen between 5% and 15%, especially in large cities like Metro Manila.[F178]
Another confounding factor is the presence of the online gambling industry. POGOs, or online gambling operators, occupy a significant amount of real estate space. Economists estimate that if COVID-19 ultimately prevents online gambling companies from doing business in the country, SEZ vacancy will increase by 7.5%, forcing providers to seek other tenants.[F37][F46]

Real estate companies operating in zones have been hit hard by COVID-19. Ayala Land Inc., one of the largest real estate firms in the Philippines, had planned to raise USD300 million in a REITs IPO in February 2020.[F47] Plans for the IPO have been delayed.

Furthermore, a wide variety of new costs have battered the company's bottom line. Faced with a crisis, the company cancelled and postponed many rent agreements for its tenants.[F48] Ayala Land also helped the response effort by converting a number of commercial properties into response centers such as hospitals, testing facilities, and shelters.[F49][F50]

The challenges faced by commercial real estate companies like Ayala Land mean that many commercial projects in zones will face hurdles as the pandemic progresses. Instead of investing in potentially risky projects such as office buildings, real estate companies will focus on preserving the integrity of their current investments.

Many of the materials used in the Philippines come from China. This meant significant delays as many ports banned shipments from China.

As the factories in China began re-opening, the construction industry faced a new problem: the lack of workers due to disease and quarantine.[F128]

Despite COVID-19, some real estate companies predict that the growth of the business process outsourcing sector will continue to drive up demand for offices in economic zones. As late as early March, some real estate companies estimated that outsourcing companies would still need more than 1.2 million square meters of additional office space in 2020.[F59] In April, these figures were revised down to between 800,000 and 1 million square meters.[F161]

Some real estate analysts believe that the government could ban the creation of new economic zones in the Metro Manila region.[F54] This move would increase the price of real estate inside Manila's economic zones, and decrease the price of real estate outside of the zones.

Before the emergence of COVID-19, Speaker of the House of Representatives (HoR), Speaker Alan Peter Cayetano, filed House Bill (HB) 0009 proposing to establish a National Economic Decentralization Plan to facilitate further growth in all regions of the Philippines. This bill proposes the provision of tax incentives for industries that would locate, and/or businesses or enterprises that would relocate outside of the National Capital Region (NCR).

PEZA Lobbying Efforts to Reopen the Economy

PEZA Lobbying Efforts to Reopen the Economy

PEZA clashes with other government regulatory entities over whether or not the lockdown should be extended.

Philippine President Rodrigo Duterte wearing a surgical mask during an April 2020 press conference

Image Source: Asia Times

PEZA has an incentive to end the lockdowns to reinvigorate economic activity in the zones. Government healthcare agencies have the opposite incentive to avoid being blamed for potentially high death tolls.

As a result, PEZA has continuously clashed with other government agencies over the question of whether the lockdown should be extended or ended. PEZA argues that the lockdowns either need to end, or that SEZs would need to be exempted from lockdowns.

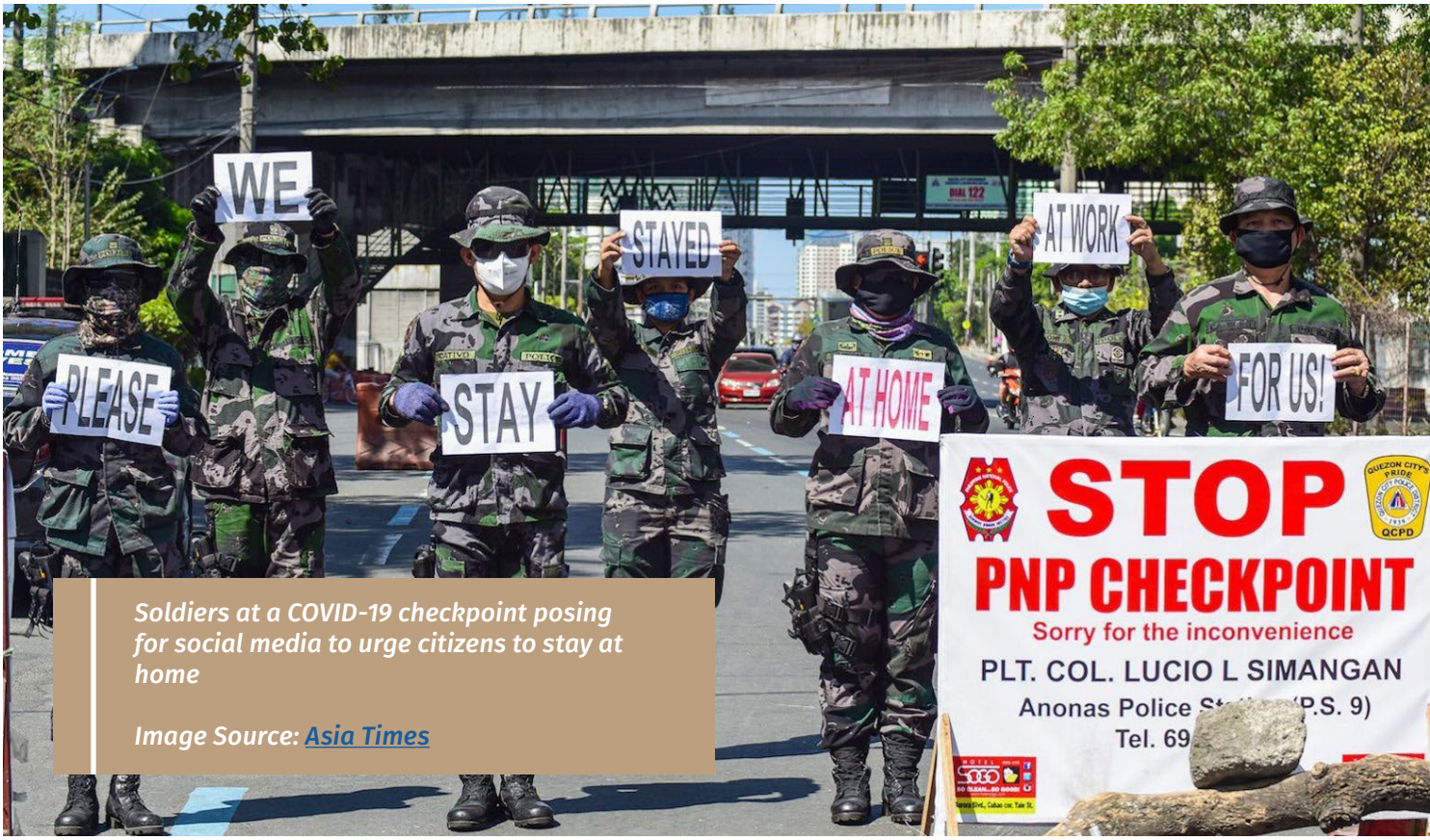
PEZA Director General Charito Plaza would say:

"Extension of lockdown must be selective only in areas where [the tally of] Covid cases is higher, but exempt economic zones which are insulated and provided support and assistance by IATF—not to hamper the passage and flow of trade activities so our industries will continue with their business operations and their workers to continue having jobs; thus, our economy will not be crippled."[F170]

The most consistent inter-agency dispute involving lockdowns would be between PEZA and local governments. PEZA argued that "local governments are issuing rules that do not comply with national guidelines which continue to hamper the mobility of goods and workers."[F174]

The conflict between PEZA and LGUs can be illustrated by the dispute between the Mactan Economic Zone (MEZ) and Lapu-Lapu City, which is home to several special economic zones, particularly the Mactan Export Processing Zones I and II, the Cebu Light Industrial Park, and the Bigfoot IT Park.

On March 29, 2020, Lapu-Lapu City Mayor Junard Chan, based on the IATF declaration to implement a general community quarantine, ordered a shut down of all non-essential businesses including those inside the SEZs. Purportedly, this was based on LGU concerns that most of the workers of the SEZ locators were not from the city itself, but from other cities and municipalities of Metro Cebu posing a high risk of introducing COVID-19 into the city.



Soldiers at a COVID-19 checkpoint posing for social media to urge citizens to stay at home

Image Source: Asia Times

PEZA responded with an open letter opposing the lockdown, stating that the zone was taking necessary precautions, the lockdown was too strict, and that the city had no authority over PEZA zones.[F172] After a week of intense negotiations, Lapu-Lapu City conceded, allowing the 97 tenants of the MEPZ to resume limited operations after the business locators agreed to provide service vehicles to shuttle SEZ workers.[F173]

Various lobby groups closely aligned with PEZA would also come out in favor of ending the lockdowns early.

President Danilo C. Lachica of the Semiconductor and Electronics Industries in the Philippines Foundation, would say that the quarantine could be extended for as long as manufacturing operations were allowed to resume, roadblocks were removed, and the transport of goods remained unhampered.[F170]

Foreign Chambers of Commerce would also call for an end to lockdowns.

The European Chamber of Commerce of the Philippines would call for quarantines to be shifted down from the national level to the local level.[F170] The German-Philippine Chamber of Commerce and Industry would caution against extending the community quarantine stating that *"the impact of every additional day of ECQ will be exponentially more painful."*[F170]

A coalition of lobbyists in the shipping industry would eventually form, not only to challenge the quarantine rules, but also to ask for economic relief for the logistics industry.

This coalition included groups such as:[F181]

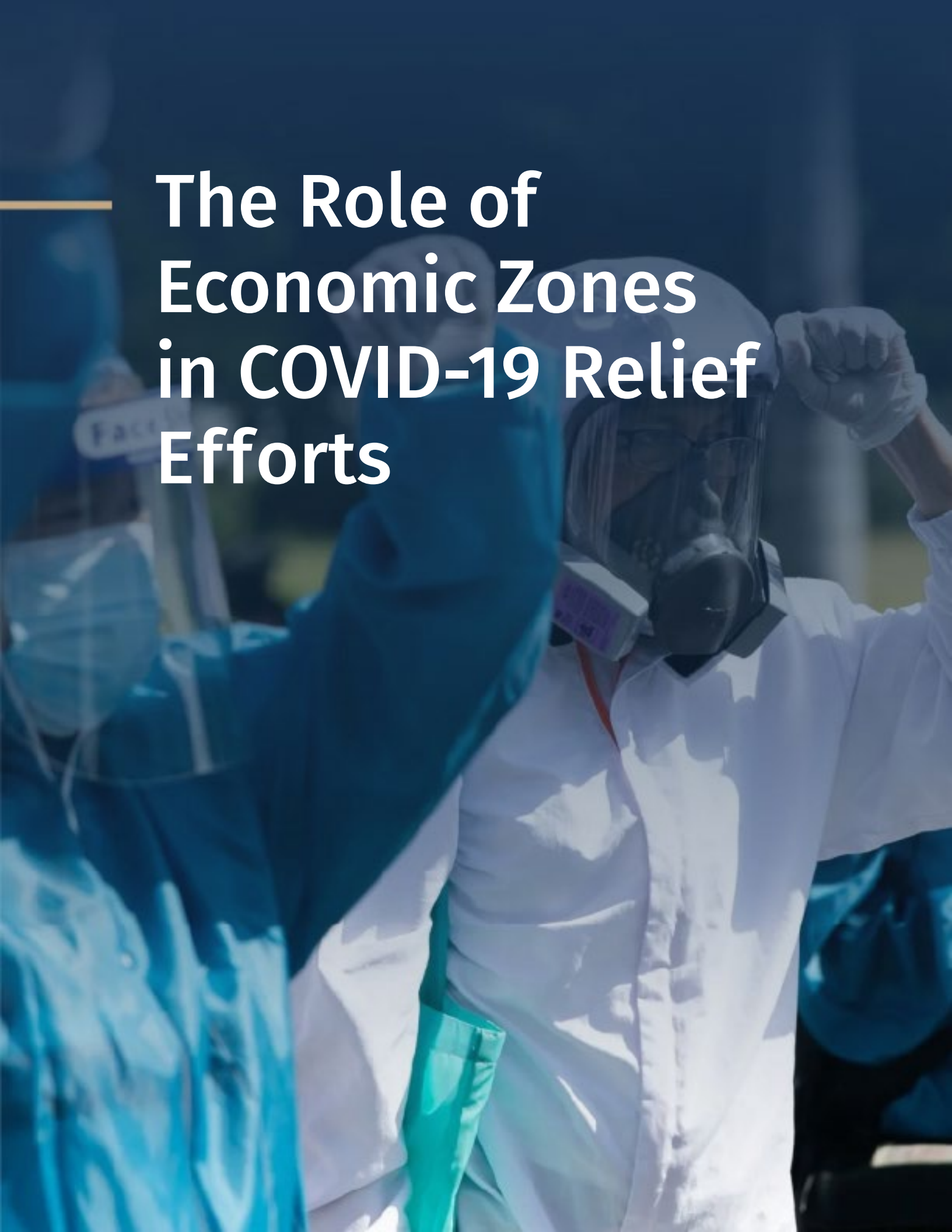
- The Philippine Chamber of Commerce and Industry
- Management Association of the Philippines
- Philippine Exporters Confederation Inc.
- Supply Chain Management Association of the Philippines
- Export Development Council

- Federation of Filipino Chinese Chambers of Commerce and Industry Inc.
- Semiconductor and Electronics Industries in the Philippines Foundation Inc.
- Philippine Association of Multinational Companies Regional Headquarters Inc.
- American Chamber of Commerce of the Philippines
- Australian-New Zealand Chamber of Commerce Philippines
- Canadian Chamber of Commerce of the Philippines
- European Chamber of Commerce of the Philippines
- Japanese Chamber of Commerce and Industry of the Philippines
- Korean Chamber of Commerce Philippines

The coalition would make several demands:[F180][F181][F182]

- Reducing demurrage fees and increasing the number of free storage days in ports
- Creating a process to easily green-light shipments going through PEZA zones and other regulatory agencies
- Lift measures designed to reduce traffic limiting how many trucks can be on the road at the same time
- Automate many functions carried out by the Bureau of Customs
- Ensure that all shipping lines have enough container yards
- Increase the number of usable ports by activating previously unused ports
- Decrease fees paid to the Philippine Ports Authority
- Adopt a moratorium on port congestion surcharges and other penalties

The Role of Economic Zones in COVID-19 Relief Efforts



The Role of Economic Zones in COVID-19 Relief Efforts

SEZs have acted charitably during the COVID-19 pandemic, and continue to work hard to help mitigate the effects of the pandemic on local communities.

The Ninoy Auqino Stadium (left) and World Trade Center (right) were converted into makeshift quarantine housing. Image Source: BM

PEZA zones have become the main centers of production for medical supplies, protective equipment, food, medicine, and other critical goods zones.[F169]

Government-owned facilities such as the Ninoy Aquino Stadium in Malate and the World Trade Center in Pasay City were converted into quarantine centers to accommodate quarantine patients to relieve hospitals of congestion. PEZA similarly helped by converting warehouses and offices into quarantine centers.[F170]

Many private companies located in economic zones would make significant pandemic-related donations. Badan Building Materials Corporation, located in the Alviera Industrial Park Special Economic Zone, would donate 6,600 face masks, normally intended to protect workers which were now not needed, to local charities.[F169]

Alliance Global Group, a large holding company with investments ranging from real estate to food and beverages, donated USD12 million. San Miguel Corporation, another holding company, would donate USD23 million to the recovery efforts. International Container Terminal Services would donate USD7 million. These donations funded among other things, initiatives to feed urban poor families, programs to give hand sanitizers to hospitals, and charity funds to supply personal protective equipment (PPE) to medical professionals.[F171]

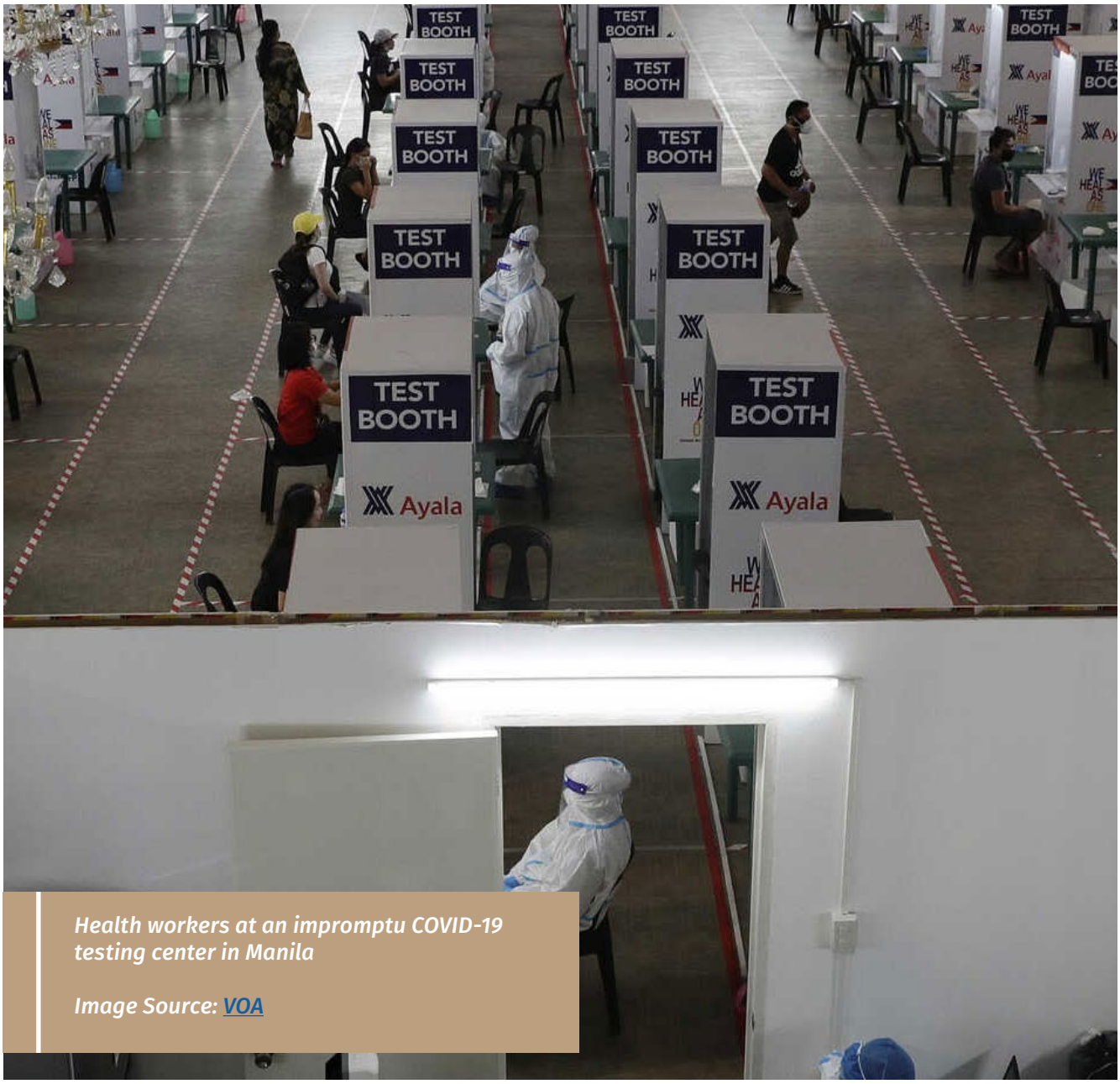
Aid workers hand out supplies to low income communities in Quezon City

Image Source: Aljazeera

In addition to large corporate donors, many smaller PEZA registered companies would also make significant contributions. 137 companies from 45 PEZA-registered economic zones would donate USD1.11 million in cash, USD800,000 in food, USD240,000 in PPEs, and USD50,000 in medical equipment.[F187]

Significant donations were also made by SEZ firms to nonprofits serving low income communities, senior citizens, single mothers, disabled people, the Philippine National Police, and COVID-19 volunteer groups. The nonprofits Project Pearls and SOS Children were among the recipients of significant donations.[F188]

Six companies located in the Mactan Economic Zone would produce large quantities of PPE for the purpose of donating it. These companies were Metro Wear Inc., Globalwear Manufacturing Inc, Feeder Apparels Inc., Mactan Apparels Inc, Vertex One Apparel Philippines and Minoura Philippines Corp.[F189]



Health workers at an impromptu COVID-19 testing center in Manila

Image Source: VOA

Aside from facilitating direct relief efforts, the Davao City Investments Promotion Center (DCIPC) acted on a concern raised by Choidan Power Corp. whereby the BOI Davao Office requested the DOH through Mindanao Development Authority (MINDA) to include in its watch list the supplies of critical drugs used in the treatment of COVID-19, specifically Hydroxychloroquine sulfate and Azithromycin. As a result, the DOH included those drugs in its critical supplies watch list.

Manufacturing of Medical Devices and Critical Goods in Zones

Manufacturing of Medical Devices and Critical Goods in Zones

Economic zones across the country took a leading role in the manufacture of goods which saw a pandemic-related increase in demand such as ventilators, protective equipment, and sanitizer.

Philippine healthcare workers pose for a picture while wearing their PPE

Firms producing PPE would be entitled to special incentives to ensure their continued production.[F190]

The Inquirer would report:
"Companies operating the country's economic zones have shifted to manufacturing medical supplies and health-care-related products as the new [coronavirus pandemic] triggered an increase in demand for hospital equipment."[F162]
"Electronics companies producing computer chips, for example, are now focusing on making hospital ventilators and RxBoxes, a device that monitors a patient's vital signs. Those in the garment sector, meanwhile, have begun making face masks and PPE for doctors and other medical front-liners."[F162]

Many medical supply manufacturers located in zones succeeded in remaining open despite national lockdowns and quarantines.

When all but two factories in the Freeport Area of Bataan were closed, the Medtecs mask factory remained in operation. Taiwanese firm Medtecs Group manufactures a variety of equipment in SEZs, including medical masks. The masks were then sold to the Department of Trade and Industry, Philippines Red Cross, and pharmacies. As a result of increased demand, the company increased its mostly female workforce from 298 to 318.

The only other company in the Freeport Area of Bataan to remain open was an alcohol manufacturer, which had retooled to produce disinfectant.[F151]

The Lima Technology Center in Batangas province is home to Taiwanese Kinpo Electronics Inc. which normally produces semiconductor and electronic parts. During COVID-19, Kinpo Electronics shifted production to hospital ventilators.[F162]

A wide variety of companies operating in PEZA zones did not only pledge to donate their proceeds and products to help fight COVID-19, but reallocated their production towards critical medical supplies. These companies include Analog Devices, Artesyn, Cypress Manufacturing, Excelitas Technology, i3 Technologies, IMI, Ionics EMS, Maxim Integrated, Microchip Phils., Nexperia, ON Semiconductor, PCA, ROHM Phils., STI Electronics, Team Pacific, and Texas Instruments (TI) Phils.[F169]

Food manufacturers would also redouble their efforts to cope with the coronavirus. Gardenia, a bread manufacturer which operates in Biñan City, would double its daily production to 750,000 loaves of bread to cope with increased demand. The factory would operate 24/7, and increase its workforce.[F162]

In view of the initiatives shown by various SEZ locators, the Philippine government encouraged businesses to repurpose to produce essential items that would address the needs created by the pandemic. **By repurposing their operations, these companies that should have been on temporary shutdown have continued to operate and to provide employment.**

From zero local capacity in coveralls, N95, ventilators and filters in March 2020, the Philippines has begun to become a hub in Southeast Asia for PPEs production. In just five months, the Board of Investments (BOI) mobilized manufacturing hero-companies to repurpose its operations to produce critical COVID-19 items. Through such encouragement, local production capacity now stands at 3.2 million medical-use coveralls, 2.4 million pieces of N95 masks, and more than 6,000 units of ventilators per month; all of which have passed international PPE testing standards.

The BOI also facilitated and closely collaborated with industry players in the repurposing of operations to produce Ethyl Alcohol (with monthly capacity of at least 330,000 liters) and Face Shields (with monthly capacity of at least 14,300 pieces). BOI facilitation also helped increase local production capacity for N88 surgical masks--from just two export-oriented firms with a capacity of about six million pieces per month when Taal volcano erupted, there are now eight firms with an aggregate capacity of almost 56 million pieces a month or an almost 10-fold increase in production capacity.

Whereas previously all raw materials for face masks were imported, two companies will be manufacturing meltblown at 20 tons per month and spunbond non-woven polypropylene at up to 40 tons per month. These materials serve as the middle filter and the hydrophobic outer layer of surgical masks, respectively.

The DTI-BOI managed a project linking industry and the health sector, through the Philippine General Hospital and the Department of Health, in developing a medical-grade prototype to be used in high COVID-risk hospital situations (e.g., Operating Rooms, COVID-19 positive wards, and ICUS).

The Inter-Agency Task Force (IATF), through the Department of Trade and Industry (DTI) and Department of Health (DOH) and in partnership with the Philippine General Hospital (PGH) and the Confederation of Wearable Exporters in the Philippines (CONWEP), has mobilized the local garments and textile industry to mass produce PPE, including the production by CONWEP of 300,000 medical-grade coveralls for the country's health workers.

Through these interventions, interest to engage in more production has emerged from both local and foreign companies from Australia, Indonesia, UK, Taiwan, South Korea, Japan, and the US.

Succes Story: Telecom Industry

Success Story: Telecom Industry

The telecom industry has benefited from the lockdowns due to increased demand from people staying at home and using the internet.

Cell towers on Semirara Island. Image Source: BM

The telecom industry has benefited from the increased demand from people under lockdown increasing internet usage.

A report from the Philippine National Bank from March 2020 suggests that the telecom sector had been the least affected by COVID-19. The report concluded that:

"In our view, business continuity plans and requiring more people to stay at home might increase the demand for call/text/data."[F134]

In the same report, the bank also predicted that even if COVID-19 affected the physical supply of telecom equipment, it would only reduce the quality of telecom services, not the quantity demanded or provided. By contrast, the bank predicted that the gambling, tourism and port industries would be the hardest hit.[F134]

Internet traffic in the country reached all-time highs as millions of citizens browsed the internet while stuck at home.

Succes Story: Business Process Offshoring

Success Story: Business Process Offshoring

The Business Process Offshoring (BPO) industry is one of the largest and most important industries in Philippine SEZs and managed to deal with the pandemic relatively successfully.

Typical BPO firm office in the Philippines

Image Source: Source Fit

A BPO firm is one where a foreign (usually Western) company outsources part of its operations to the Philippines through the internet. For example, a Western bank might employ a Philippine-based customer support workforce. Likewise, a Silicon Valley tech company might make use of a BPO to get extra developers to do the more repetitive tasks involved in software development.

As of 2019, BPOs employed between 900,000 and 1.2 million people in the Philippines, mostly in SEZs.[F137][F199] Roughly 60% of the customers making use of BPO services are based in the United States, with Australia and the UK also taking advantage of the large English speaking workforce.[F199]

BPOs would adapt relatively well to COVID-19. Had the BPO industry failed to take proper precautions, there could have been serious consequences. The cramped working conditions

of BPOs posed a serious risk in terms of spreading the disease, and could have potentially become a significant infection vector. Luckily, early in the pandemic, BPOs quickly took many critical steps to curb the spread of COVID-19.

The nature of the industry meant that working from home was a viable option.

Early during the pandemic, a major trade consortium, the Information Technology and Business Process Association of the Philippines, would start working with government agencies to recommend a number of measures to prevent transmission. These measures included allowing workers to take office laptops home, providing alternative transportation to work to avoid public transportation, avoiding office space when possible, staggering shifts to minimize contact, and only leaving a skeletal workforce in offices.[F137]

In one city, 55 out of 69 registered BPO companies would remain open while in compliance with strict quarantine rules.[F163]

In fact, it is possible that the BPO industry might benefit from a COVID-19 related recession.

During the 2008 recession, the Filipino BPO sector saw significant growth from foreign companies offshoring their business operations to cut costs. Likewise, BPO executives expect the COVID-19 recession to cause a similar increase in demand, mostly from mainland Chinese companies.[F160]

Effect on Investment

After years of difficulties attracting investment, COVID-19 could serve as a catalyst for positive change.

Despite the worldwide pandemic, from January to June 2020 total BOI-approved investments surged by 112% from PhP304.43 billion in the same period in 2019 to PhP645.28 billion this year.

Approved investments from domestic sources went up to PhP626.7 billion, a 166% increase from PhP235.6 billion from the same period last year.

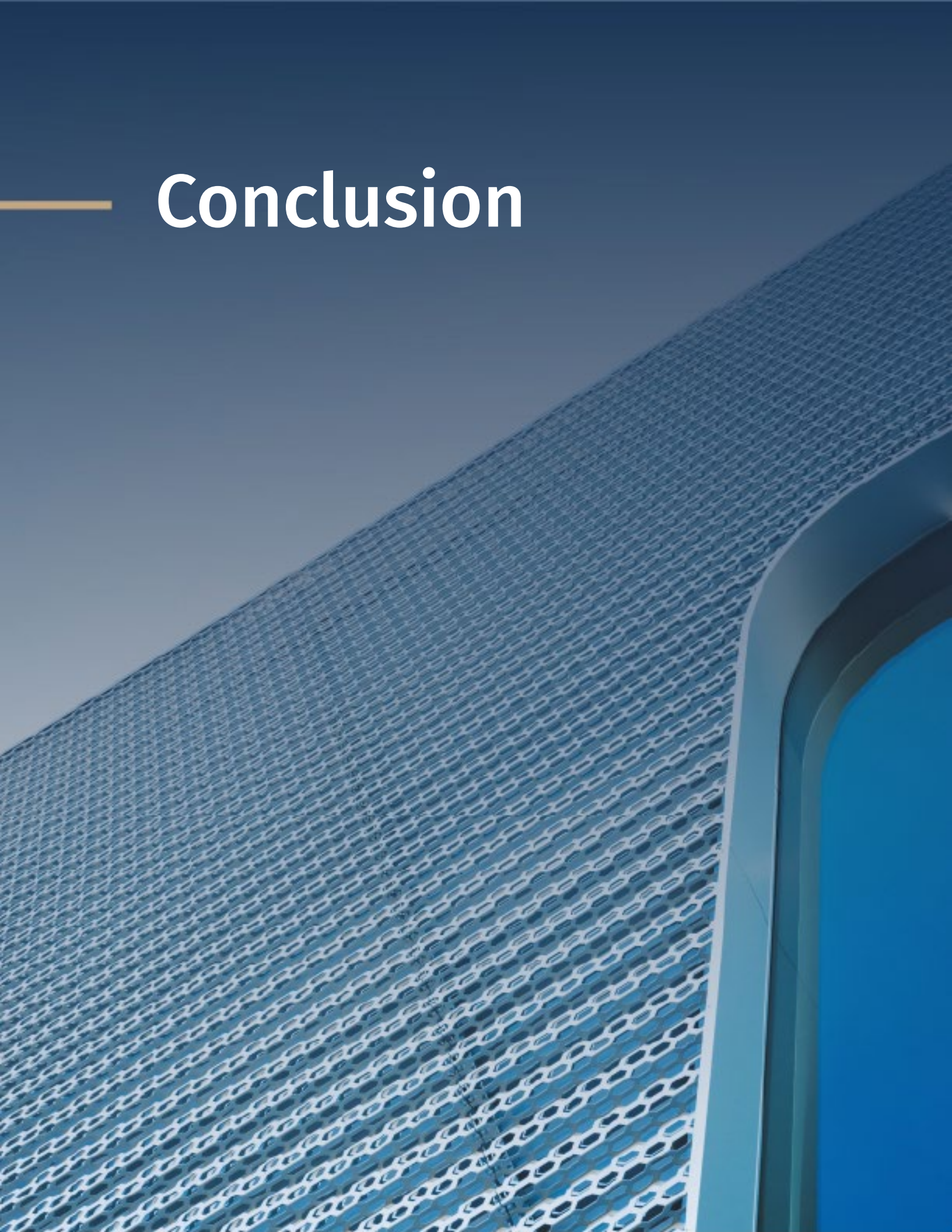
In contrast, approved figures by foreign investors reached PhP18.6 billion, a 73% decrease compared to PhP68.9 billion in the same period a year ago.

Construction/infrastructure have set the pace among industries with PhP530.8 billion as of the first half of 2020.

The transportation and storage sectors remain strong with PhP86.7 billion, a 785% improvement from last year's figure of just PhP9.8 billion. Real estate posted a 16.8% growth to PhP9 billion from Php7.7 billion in 2019. Renewable energy/power, manufacturing and accommodation (tourism) recorded PhP6.6 billion, Php5.3 billion and Php3.8 billion in approved projects, respectively. A total of 96 projects were approved, and upon operation, will generate 27,082 jobs, a jump of 57.3% from 17,214 in the same period last year.

The manufacturing sector is gaining stability as shown by the Philippine Manufacturing Purchasing Managers' Index (PMI) survey of IHS Markit, which reported a manufacturing index score of 49.7 in June 2020, up from 40.1 in May 2020. Similarly, the country recorded an increase in its output index of 51.1 in June 2020, the first monthly increase in four months, from a low of 10.2 in April and 29.4 in May. Indices below 50 indicate a decrease in manufacturing output while indices above 50 indicate an improvement of activity. The change in community quarantine rules boosted the manufacturing output thereby making inroads towards stability, with companies beginning to increase their production as they reopened operations after a long shutdown.

Conclusion



Conclusion

COVID-19 has given PEZA an opportunity to reinvent itself in a time of global crisis.

The skyline of Manila. Image Source: Unsplash

PEZA companies have proven their importance to the Filipino public and to the government. In a time of crisis, they provided critical services to the country. If PEZA succeeds in capturing this opportunity, it might resolve its longstanding tax reform issue, making Philippine SEZs a more attractive place for investors.

By late April, clearer PEZA guidelines allowed some businesses to start resuming limited operations. PEZA reports that 551 of the 835 companies on the island of Luzon, 70 of the 176 companies based in the Visayas archipelago, and 29 out of 31 companies on the island of Mindanao have partially resumed operations.[F174]

Considering the sheer enormity of the global chaos caused by COVID-19, PEZA has done a good job at weathering the storm.

While SEZs in the country face serious challenges and an uphill battle for economic recovery, the gradual re-opening has brought hope back to thousands of tenants and workers across the country.

The confusions surrounding unclear quarantine rules have given way to potentially beneficial legal precedents. Zones, like Cavite, are slowly reopening, and workers are going back to work. Some zone industries, such as Telecoms, BPOs, and medical suppliers, have even managed to turn this tragedy into an opportunity.

SEZs in the Philippines faced many challenges before COVID-19. Perhaps this pandemic will offer them the shakeup they need to fully actualize and resolve their long-standing issues. COVID-19 will mark a new era for SEZs. Ecozones in the Philippines will never be the same again.

For more information, please contact:

Thibault Serlet, Head of Research

Thibault@AdrianopleGroup.com

www.AdrianopleGroup.com