



We are pleased to present here our report, **Illicit Financial Flows to and from the Philippines: A Study in Dynamic Simulation, 1960-2011.**

We find that over the 52 years covered by this analysis, the Philippines experienced some \$410 billion in illicit flows, made up of \$133 billion out of the country and \$277 billion into the country. Mispricing of trade accounts for the bulk of these flows. In most countries this is accomplished by overpricing imports and underpricing exports. In the case of the Philippines we also see substantial underpricing of imports for the purpose of saving on customs duties and VAT taxes. When such underpricing of imports occurs, there is almost always a comparable means of completing payment for the underpriced imports, usually by overpricing some other imports, underpricing exports, or via alternative money laundering schemes.

This analysis of illicit financial flows affecting the Philippines is the most methodologically rigorous that Global Financial Integrity has produced. We have developed a structural equations model to capture the main interactions between the official and the underground economies. And we have also developed a vector error correction model to ensure the robustness of the correlations shown by the structural equations. These calculations rather clearly demonstrate the following:

- Illicit inflows significantly reduce the collection of total taxes and bolster the underground economy.
- Illicit outflows reduce domestic savings.
- Increases in import duties and VAT taxes lead to a nearly proportionate increase in import tax evasion.

Global Financial Integrity particularly thanks Dev Kar and Brian LeBlanc for the creative and thoughtful work reflected in this study.

We trust that this analysis may spur the Government of the Philippines to consider effective steps to curb illicit financial flows and maximize domestic resources for development. This is the goal of Global Financial Integrity, working in conjunction with government officials.

Raymond W. Baker

President

February, 2014