The Philippine Economy: Development, Policies, and Challenges edited by Arsenio M. Balisacan and Hal Hill, Quezon City, Ateneo de Manila University Press, 2003, xxv + 466 pp.

Economists and development specialists puzzle over why the Philippine development experience is an outlier among Southeast Asian economies. In the 1950s, Philippine per capita income was higher than those of the Republic of Korea and Taiwan, and significantly higher than the per capita income of Thailand, of Indonesia, and of China. Between 1980 and 2000, while other Southeast Asian countries decisively industrialized, the share of manufacturing in Philippine GDP declined from 25.5 percent to 22.1 percent. Taking the endpoints of that twenty year period (and passing over the deep foreign-debt-induced crisis of the 1980s) real per capita GDP stayed the same, while Thailand's per capita GDP increased to a level three times that of the Philippines. However, in terms of conventional norms, Philippine economic policy has not been catastrophically different from those of its neighbors. As the editors of the volume, Arsenio Balisacan and Hal Hill note, while the Philippine "trade regime has not been as open as that of Singapore, Hong Kong, and Malaysia, but did not differ significantly from that of Indonesia and even Thailand" (p. 38).

The Philippine Economy: Development, Policies, and Challenges examines the same reality, using competent, up-to-date economics research techniques. The publication presents the findings of a research project supported by two government institutions: the Philippine National Economic and Development Authority and the Australian Agency for International Development (AusAID). The Philippine authors represent the leading pioneers, now elders, in their country's economics profession. As would tend to be true in many other developing countries, these authors have also been deeply involved in policy design initiatives and debates that have conditioned economic reform programs since the 1980s.

Chapters in the volume follow a sequence of topics that will be familiar to economists. Part I consists of two chapters: Chapter 1, "An Introduction to the Key Issues," written by Balisacan and Hill and Chapter 2, entitled "Political Economy" by de Dios and Hutchcroft. A conclusion of Chapter 2 is that Philippine state institutions have shown themselves to be "incapable of providing the necessary political foundations required even by the laissez-faire model of development that the IMF, World Bank, and the former colonial power have long been trying to promote in the country" (p. 70). Is a laissez-faire model of development an impossible dream, if the kinds of state institutions needed to operate it are not within reach?

Part II is entitled "Macroeconomic Policy and International Dimensions" and has a chapter on Monetary and Exchange Rate Policy (applying Granger causality tests), Public Finance, and International Dimensions, which reviews the success of the Philippines in opening up its trade regime. In describing the trade and industrial regime, Hill and Balisacan assert that "significant progress has been made since the late 1980s, to the point where openness appears to be quite deeply rooted in the polity and in the community at large, and the country now has a reasonably open trade policy regime" (p. 23). The authors of this

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chapter, Bautista and Tecson, "attribute the decline in overall protection to decades of intellectual effort, gradually percolating through the bureaucracy and the political process. Much of that work was located at the University of the Philippines and the Philippine Institute of Development Studies. Foreign inputs helped, but the domestic impetus was the critical factor" (p. 24). The sensitivity to foreign dependence on ideas is palpable. (In the interests of disclosure, this reviewer admits that he too was associated with both of the above-mentioned institutions.) These chapters and those that follow provide convincing evidence that the Philippines has indeed state-of-the-art economic policies, something that some more successful countries, such as India, China, and Vietnam cannot claim. Monetary policy is based on inflation targeting; the country has low trade protection, with protection for agriculture now slightly higher than for industry. It has achieved low levels of ownership concentration in industry (something that is considered desirable, even though historically, countries that have industrialized have had high, if not brutal, ownership concentrations).

Part III is entitled "The Sectors" and consists of chapters on agriculture, industry, and services. In the agricultural sector, policy reform efforts have succeeded in switching the trade stance toward higher agricultural protection (relative to industry), an achievement that even the author herself, long a proponent of a neutral trade policy, interprets as "early" in the historical experience of other countries (David, chapter 6, p. 215). Following the successful effort to dismantle the industrial policy regime of import-substitution, the Philippine industrial sector is less than half the size of those of Indonesia and Thailand and is about two-thirds that of Malaysia (a country with a strong agricultural export base) (Hill, chapter 7, p. 225). Labor productivity in manufacturing has fallen over the period, and exports are unquestionably less diversified than at the start, with a new heavy concentration in low domestic value-added electronics assembly products (Hill, chapter 7, p. 231). The disquieting reduction in manufacturing's contribution to GDP is matched by what would normally be interpreted as a premature increase in the contribution of services to output. This discrepancy, which authors have called premature deindustrialization, is pointed out, but all three chapters are concerned principally about instances within each sector in which government intervention distorts incentives and prevents private sector responses to the "right prices."

These chapters are exemplary exercises in contemporary economic analysis, in that they identify increases in efficiency, as opposed to achieving economies of scale and learning, as the key (and perhaps sole) source of growth. As a consequence, the analytical approach sets great store by the achievement of efficiency in *each* individual sector and economic activity. Volume authors, for example, express concern over the low rate of growth of productivity in the agricultural sector, a rate of growth that has failed to keep up with population increase and has not been able to compensate for the disturbing fall in industrial productivity. Consistent with the prevailing analytical fashion, the explanation preferred by the authors of these chapters focuses on price distortions. Historically, however, in the case of successful industrializers, it has been the established pattern that agricultural productivity only rises when industrial productivity improves, which, in turn, has depended on increases in the scale of manufacturing activity.

This raises the question of whether manufacturing investment can actually be expected to be driven by efficiency possibilities alone, in a country where the overall growth rate has been volatile and weak over an extended period. The Philippine situation, since the 1980s, shares some analytical elements with the man-made economic catastrophe of post–World War I Germany, as predicted by John Maynard Keynes in his 1920 book, *The Economic Consequences of the Peace*. Analysis of that period showed that if she had depended entirely on her own agricultural sector, Germany would only have been able to feed 40 million people, but as a consequence having industrialized, the country was at that time feeding a population of 67 million. The war reparation payments, however, were predicted to preclude the importation not only of food but also of intermediate goods needed in manufacturing, which given the reality of strictures against the emigration of Germans, would have thrown the urban population upon the mercy of the agricultural sector. A recent laboratory example of this kind of phenomenon was the sudden dismantling of the industrial sector in Mongolia in the 1990s in order to create a market economy.[1] The law of diminishing returns, the analytical idea taught on day one of introductory economics courses, then comes into play as a large proportion of the population is thrown back into the agricultural sector, thus starting a trend toward a fall in productivity in both sectors.

For the Philippines, one could suggest that an analytical counterpart of Germany's reparations payments might be the deep economic crisis and the debt overhang in the post-Marcos era, whose absorption through various channels into the economy is not directly addressed in this volume. As Balisacan and Hill indicate, this question might actually apply to the current situation in "post-Soeharto Indonesia as it grapples with a difficult mix of abrupt political transition and deep economic crisis, much as Filipinos had to in the second half of the 1980s" (p. 7).

Part IV, "Social Dimensions," consists of four chapters: (1) Population, Human Resources, and Employment, (2) Poverty and Inequality, (3) Regional Development, and (4) Environment and Natural Resources. Each of these chapters is best interpreted as an attempt to come to terms with the consequences of zero per capita growth over a twenty-year period. In each of these areas, one might actually draw attention to what has been a heroic performance in the face of an unfavorable overall economic environment. Because of continuing high fertility, population growth remains high by Asian standards, even compared to Indonesia's, but unlike the Indonesian economy, the overall economy of the Philippines has been in the doldrums for 20 years. Dependence on agricultural employment is still high, but has been alleviated somewhat by the rather successful export of labor overseas. Overseas remittances represent the single most important source of foreign exchange in the economy and, arguably, one of the channels by which the consequences of the economic crisis of the 1980s have been absorbed.

Inequality and poverty remain high, and Balisacan, the author of the relevant chapter, is probably right in pointing out that progress is difficult on this front without overall economic growth. As in the other chapters, the data throw up problems that defy standard analysis, such as the fact that schooling does not have a direct impact on the well-being of the poor except when it interacts with an existence of roads variable (Balisacan, chapter 10, p. 333). This is indeed baffling when the analytical lens portrays national productivity as the

[1] Erik S. Reinert, "Mongolia: Underdevelopment of the 1990s as a Morgenthau Plan," http://www.othercanon.org/papers/more.asp?id=24 (accessed September 2, 2004).

sum of individual efficiencies. Could a variable such as the existence of manufacturing employment opportunities also play such a role? One is tempted to ask: given that rates of return on road investment are notoriously spread out over long periods, would not even relatively "inefficient" manufacturing investment have a faster return, both to the educated poor as well as socially?

The regional development chapter is interesting since, as in many other countries, the Philippines has undertaken a spate of policies for decentralization and devolution of state functions. The chapter ably surveys the different issues involved (particularly internal inconsistencies in government policies) and underlines the importance of improving agricultural productivity. The chapter on environment and natural resources puts forward the argument that import-substituting industrial policy, by way of lowering wages (the starting assumption being that resources are fully employed), has a deleterious impact on the environment, since lower wages make land conversion to agriculture cheaper, while export-oriented policy has the opposite effect. Nevertheless, investment in environmental sustainability is deemed to be important.

At the time of writing (August 2004), the Philippine political system is embroiled in a debate, involving some of the economists writing in this volume, about another impending balance-of-payments crisis resulting from continuing fiscal deficits. The country's weak fiscal position is amply analyzed in Chapter 4 "Public Finance" by Sicat and Abdula. These authors show that a high priority has been assigned to debt service, a tendency that has rendered the budget particularly vulnerable to foreign exchange fluctuations. They also suggest that in the 1980s, a substantial debt write-off would have been too radical a response, since it would have isolated the country from international capital markets (p. 114). The authors rightly point out that fiscal health and success in ratcheting up the tax efforts depends heavily on overall economic performance.

Weak fiscal standing apart, the chapters of the book provide convincing evidence that the country has gone a long way toward configuring a more liberalized economic stance, enabling it to take advantage of opportunities in the international economy. This configuration is based on a historically untested development strategy, using a narrower set of instruments than those employed by countries now already developed.[2] As in many other countries, this configuration has evolved during a period of sometimes extended economic crisis. For its success, it depends heavily on the existence of large Harberger triangles and the almost automatic emergence of a fully formed domestic private sector in response to the right prices. The Philippines is an important test case of whether indeed these types of policies are the proper ones to deploy to counter underdevelopment. (Manuel F. Montes)

[2] See Ha-Joon Chang, *Kicking Away the Ladder: Development Strategy in Historical Perspective* (London: Anthem Press, 2002). For a contrary theoretical view, see T. N. Srinivasan and Jagdish Bhagwati, "Outward-Orientation and Development: Are Revisionists Right?" http://www.columbia.edu/~jb38/Krueger.pdf (accessed November 15, 2004).