

The Dynamics of Regional Development: The Philippines in East Asia

Hal Hill

Australian National University

Arsenio Balisacan

University of the Philippines and SEOMEQ-SEARCA

Sharon Faye Piza

University of the Philippines

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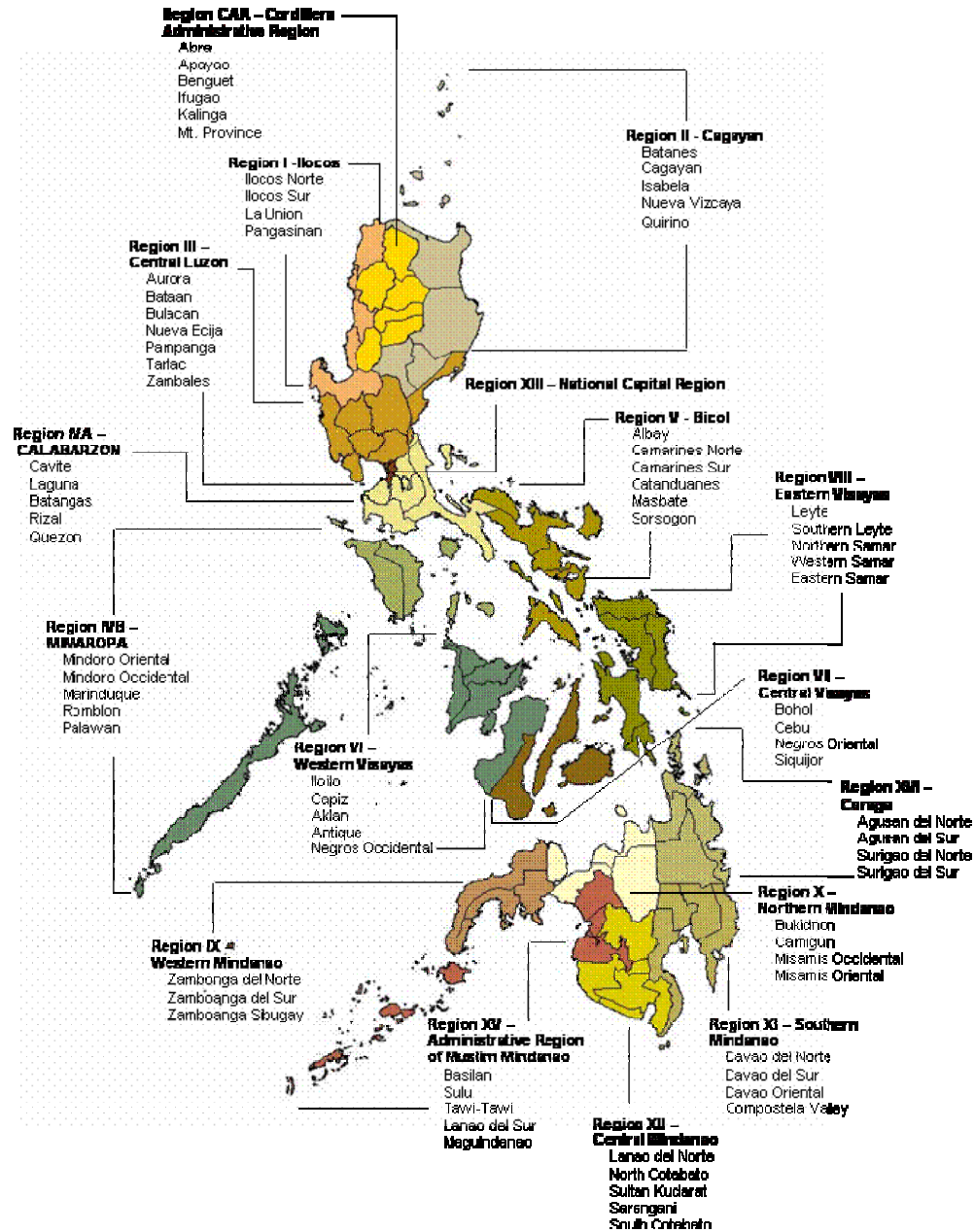
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1. INTRODUCTION

New economic geography has come of age' (Neary, 2001).

'... one of the best ways to understand how the international economy works is to start by looking at what happens inside nations. If we want to understand differences in national growth rates, a good place to start is by examining differences in regional growth; if we want to understand international specialization, a good place to start is with local specialization.' (Krugman, 1991, p. 3)

'Regional development policies have failed in all countries – federal and unitary alike – to reduce regional inequalities.' (Shankar and Shah, 2003, p. 1437)

'[Decentralization is neither] a plague or a panacea' (Bird and Villancourt, 1998, p.1).

'What is happening now to the Philippines is one of the best arguments why countries which face chronic fiscal deficits should go slow in the decentralization process.' (Diokno, 2003, p. 11)

The Philippines: regional dimensions

7,000 islands; 110 ethnic groups; 170 spoken languages; second largest archipelagic nation in the world.

Economic activity very uneven: NCR & surrounds produce 55% of GDP. Great diversity (10:1) in poverty incidence among regions.

Regional policy framework: historically weak centre; pendulum swung between devolution and central authority. Major decentralization in 1991; an 'early decentralizer'.

Broader context:

Most developing countries decentralizing; sometimes linked to transition from plan to market; sometimes in wake of a major economic-political crisis. Some big bang, others incremental.

Generally accompanied by liberalization. In process, sub-national dynamics change, sometimes profoundly. The ability to 'connect' to the global economy often the key to regional growth. Conversely, problems in 'by-passed regions' may become more serious.

2. THE ISSUES

Regional economics now at the forefront of development economics.

Why? To do with analytics; policy; transitions from crises or command economies; uneven spatial impacts of rapid global integration.

Some key questions/motivations in thinking about decentralization in the context of liberalization/globalization :

Why do some regions grow faster than others; are the factors similar to those explaining inter-country differences?

What determines trends in sub-national inequality; why does regional inequality vary so greatly, within countries and over time; is it a cause for concern; what sorts of policies for by-passed regions?

Why is the spatial location of economic activity so uneven in many countries?

What is 'regional policy'; what are the key issues and lessons in decentralization reforms; why are some programs more successful than others?

As national boundaries become less important, will cross-border 'natural economic zones' become more important, perhaps in an 'EU-type' world?

Is regional (sub-national) competition likely to improve local-level (and hence national) governance quality?

Note also:

Weaker centre (and therefore less commitment to egalitarian outcomes) and uneven connections to the global economy may result in a collection of internationally-oriented enclaves better connected globally than to their hinterlands.

This the most likely scenario for increased regional inequality.

Motives for decentralization vary: from belief that decentralized states function better, to fear of territorial disintegration.

Reconciling the 'death of distance' alongside growing importance of clusters, increasing returns to scale.

Paradoxically, international barriers to commerce may decline as sub-national barriers increase. Does decentralization lead to 'over-grazing' of fiscal capacities?

Some other unresolved questions: (a) No consensus on how far, how quickly to decentralize. (b) No obvious growth correlations. (c) To what level of local govt? (d) Modelling the determinants of inter-regional growth still in its infancy. (e) Evidence on LT trends in inter-regional inequality mixed: is there a 'Williamson curve'?

3. EAST ASIAN COMPARISONS

Some lessons from the developing East Asian 'giants'.

China: A key regional issue is rapid increase in inequality. No sign of convergence. Drivers:

(a) Large differences in international orientation and connections.

(b) Restrictions on labour mobility, so factor markets could not adjust.

(c) Centre's 'retreat from inequality'.

Note recent change in policy direction.

Indonesia: Some similarities with Philippines. Eg, archipelago; decentralized in wake of crisis; resource-rich, conflict-prone 'frontier zones'.

But differences, too:

(a) Soeharto record of highly centralized but broadly even regional devt; grants and infrastructure investments the key.

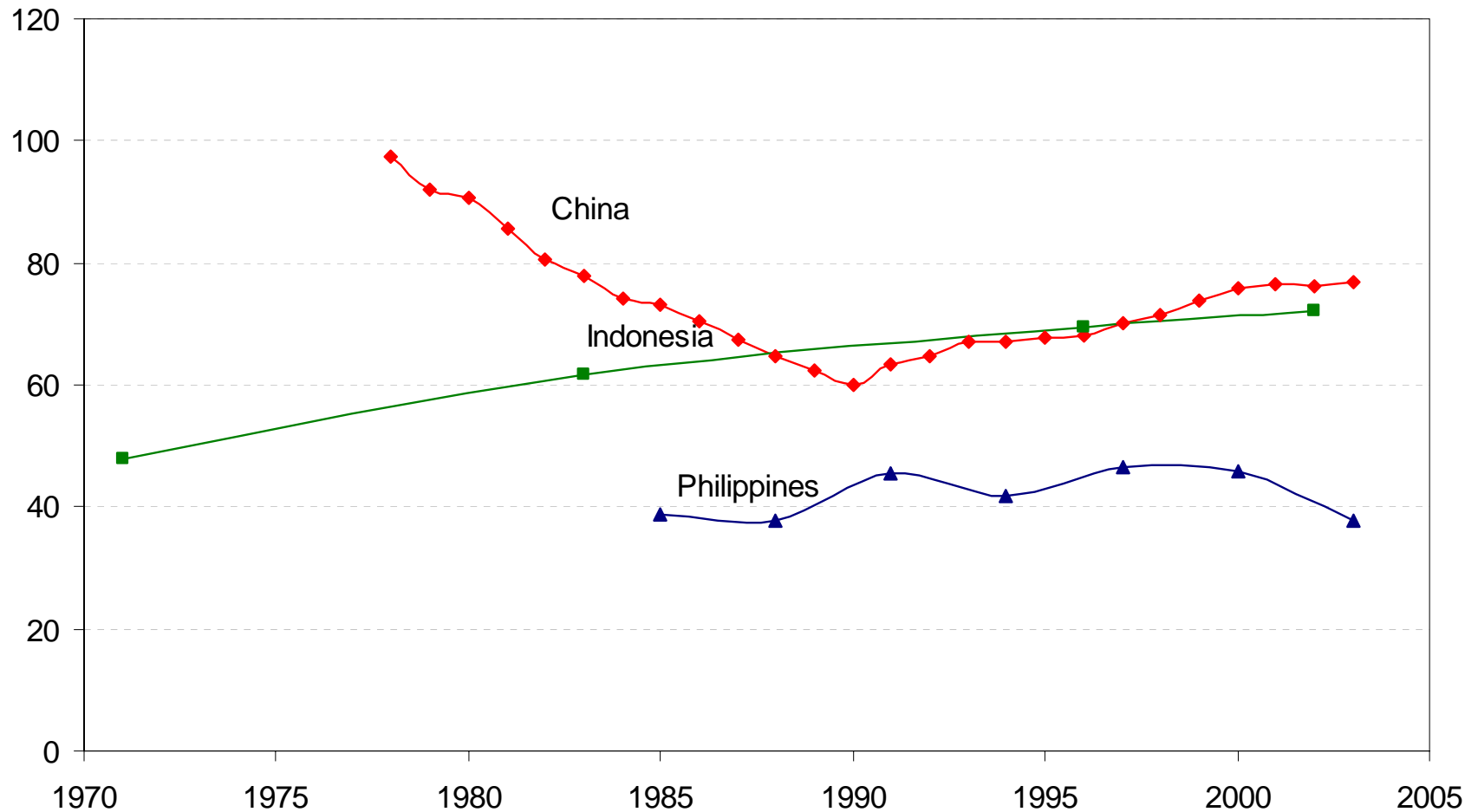
(b) Resource rich enclaves also differ.

(c) Economic geographies differ; no 'Java', nor 'Java/Outer Islands' parallels in Philippines.

See comparative patterns of inter-regional inequality.

Philippines in East Asia

Coefficient of variation of regional* per capita incomes



*Provinces in China and Indonesia while regions in the Philippines

4. THE PHILIPPINE EXPERIENCE

(a) The Evolution of Regional Policy

Historically weak centre.

'Regional awareness period' from 1970s; several reasons.

Beginnings of decentralization in late Marcos period. L^o GC of 1991.

World Bank (2005): Philippines a 'fast starter' in decentralization; the region's 'strongest history of democratic decentralization'.

(b) Current Regional Structures

See Figure re current and 1980s admin organization. Unitary state; 17 regions (all but one administrative only); second tier of govt, comprising democratically elected 'Local Govt Units' (LGUs).

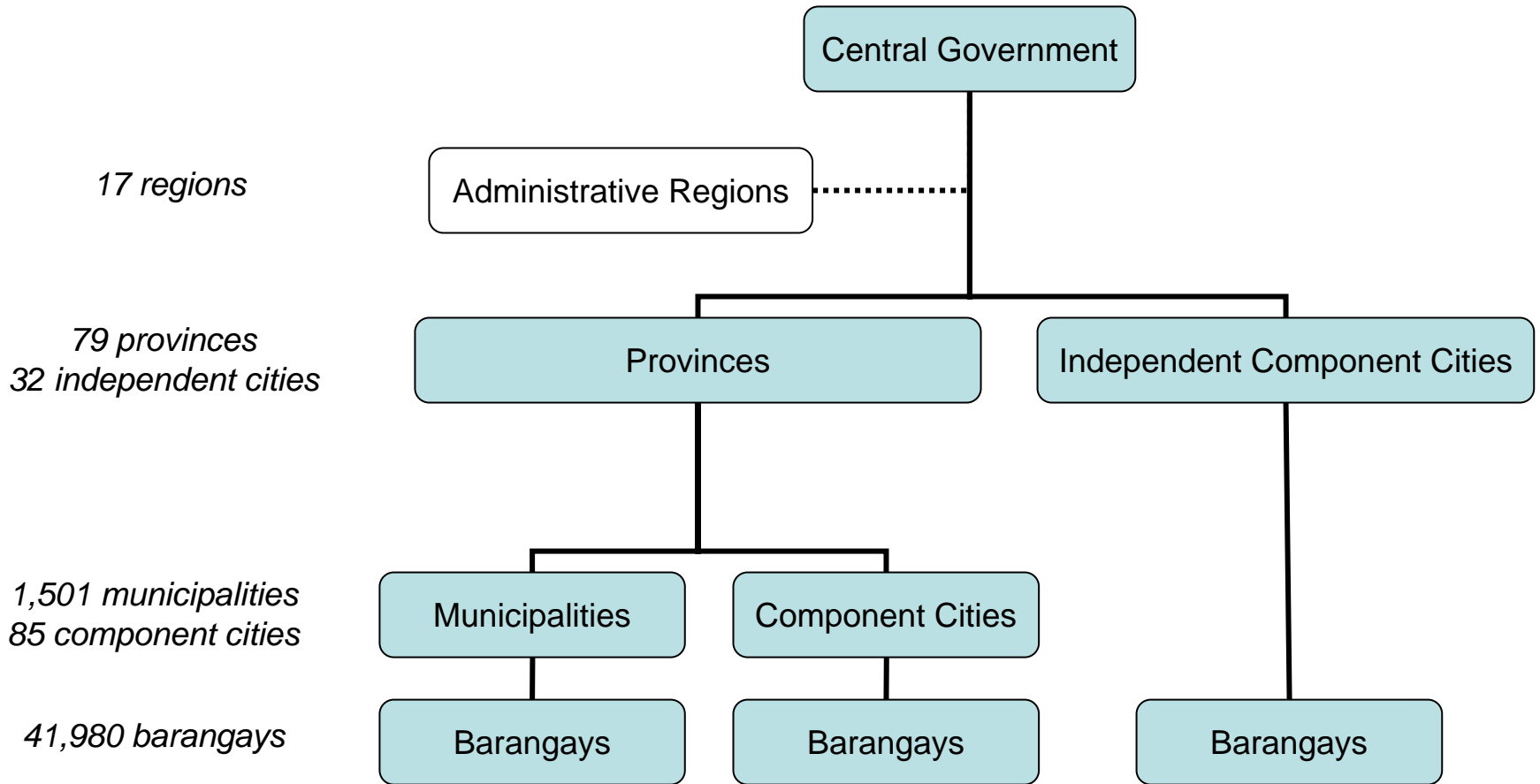
Some increased fragmentation among the cities.

The LGC specifies responsibilities and resources of each tier.

Generally follows conventional divisions; but principles v/s practices diverge considerably; education retained by the central govt (CG).

LGUs tend to be 'family dominated'; weak bureaucracies (even more so than the CG).

Current local government structure



(c) An Overview of Regional Development Patterns

See Tables; mainly regions for statistical and presentational convenience.

Classifying regions: geography v/s typology.

(i) Patterns of spatial concentration:

Manila & surrounds dominate, 55-60% of GDP; Luzon share rising.

(ii) Income disparities over time:

Large disparities; Manila pcy more than double #2; 12 times poorest. Note major locations of poverty; Mindanao, ARMM in particular, very poor. No major trends over time, reflecting in part slow aggregate growth (note China comparison). Very slight convergence, both α (declining regional inequality) and β (poorer regions catching up to richer ones).

(iii) Economic structures:

Reflect interplay between levels of development, natural resource endowments, and connections to the global economy.

Note cases of ag-dependent (mostly obvious); services-dependent (some obvious, some puzzling); M-dependent (mostly obvious).

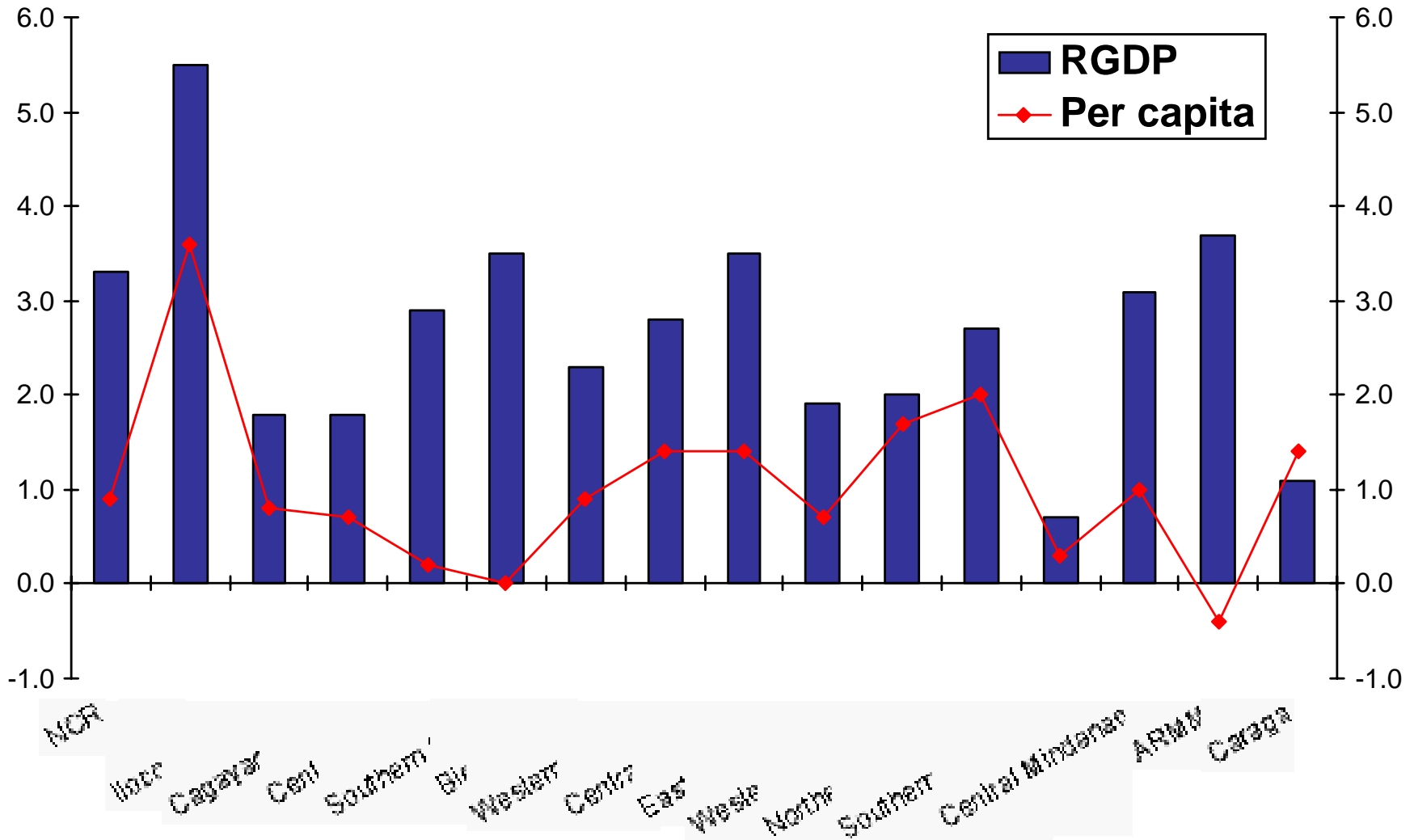
Economic performance, 2003

Region	Per capita RGDP	Composition of RGDP			RGDP growth rate 1985-2003
		Agriculture	Industry	Services	
<i>Philippines</i>	<i>100.0</i>	<i>15.0</i>	<i>31.8</i>	<i>53.2</i>	<i>3.0</i>
NCR	275.8	-	37.1	62.9	3.3
CAR	129.9	11.0	56.5	32.5	5.5
Ilocos Region	53.7	36.0	8.9	55.1	1.8
Cagayan Valley	52.3	45.8	7.5	46.7	1.8
Central Luzon	75.2	20.5	32.7	46.8	2.9
Southern Luzon	85.7	20.2	37.5	42.3	3.5
Bicol Region	43.3	22.7	16.1	61.2	2.3
Western Visayas	83.5	22.6	25.7	51.7	2.8
Central Visayas	93.4	10.4	27.9	61.7	3.5
Eastern Visayas	50.5	29.9	25.7	44.4	1.9
Western Mindanao	62.1	40.2	14.8	45.0	2.0
Northern Mindanao	101.8	28.6	30.2	41.2	2.7
Southern Mindanao	92.4	25.2	25.2	49.6	0.7
Central Mindanao	76.6	40.2	28.0	31.8	3.1
ARMM	23.2	48.6	10.3	41.1	3.7
Caraga	47.8	38.0	18.0	44.0	1.1

Note: Average per capita GDP for the Philippines in 2003 prices is Php 52,470.

Source: National Income Accounts

Income Growth Rates 1985-2003



Source: National Income Accounts, NSCB

Regional comparison, 1975-2003

Region	1975-1985	1985-1995	1995-2003	1975-2003
<i>RGDP average growth rate in 1985 prices, %</i>				
<i>Philippines</i>	2.5	2.5	3.9	3.2
Luzon	2.6	2.8	4.0	3.4
National Capital Region	2.4	2.8	4.3	3.4
Central and Southern Luzon	2.6	3.1	3.6	3.4
Other Luzon	3.0	2.3	4.3	3.4
Visayas	2.4	2.1	4.0	3.2
Central Visayas	2.7	2.6	4.8	3.7
Other Visayas	2.3	1.7	3.4	2.8
Mindanao	2.2	1.7	3.6	2.6

Source: Regional link series 1975-2003, National Income Accounts.

Regional comparison, 1975-2003

Region	1975-1985	1985-1995	1995-2003	1975-2003
<i>Share in national GDP, %</i>				
Luzon	62.6	64.8	66.4	64.5
National Capital Region	28.8	31.6	34.4	31.5
Central and Southern Luzon	23.3	23.2	21.9	22.8
Other Luzon	10.5	10.0	10.1	10.2
Visayas	16.7	16.3	15.8	16.2
Central Visayas	6.4	6.5	6.7	6.5
Other Visayas	10.3	9.8	9.1	9.7
Mindanao	20.8	19.0	17.2	19.1

Source: Regional link series 1975-2003, National Income Accounts.

Regional comparison, 1975-2003

Region	1975-1985	1985-1995	1995-2003	1975-2003
<i>Share in total population, %</i>				
Luzon	54.3	55.1	55.9	55.0
National Capital Region	12.3	13.2	13.1	12.8
Central and Southern Luzon	22.8	23.9	25.7	24.0
Other Luzon	19.2	18.0	17.1	18.2
Visayas	23.2	21.4	20.3	21.7
Central Visayas	7.9	7.5	7.4	7.6
Other Visayas	15.3	13.9	12.9	14.1
Mindanao	22.5	23.5	23.7	23.2

Source: Regional link series 1975-2003, National Income Accounts.

Social indicators, 2003

Region	Life expectancy at birth	Adult functional literacy rate	Primary & secondary enrolment rate	Human development index	
				1990	2003
<i>Philippines</i>	68.3	84.2	91.5	0.713	0.721
NCR	70.0	94.6	92.3	0.944	0.814
CAR	66.2	85.5	95.7	-	0.656
Ilocos Region	69.5	88.4	91.6	0.592	0.649
Cagayan Valley	67.0	84.3	92.6	0.560	0.600
Central Luzon	70.9	86.8	91.0	0.695	0.652
Southern Luzon	68.9	88.7	92.7	0.654	0.646
Bicol Region	68.6	79.8	90.7	0.488	0.536
Western Visayas	68.3	81.5	93.9	0.527	0.603
Central Visayas	70.7	81.6	90.3	0.528	0.589
Eastern Visayas	65.6	76.5	90.1	0.473	0.522
Western Mindanao	66.3	73.0	93.6	0.458	0.528
Northern Mindanao	68.6	82.6	90.1	0.531	0.609
Southern Mindanao	68.8	77.4	90.9	0.571	0.621
Central Mindanao	66.5	80.0	93.1	0.479	0.555
ARMM	54.2	65.9	80.3	-	0.374
Caraga	64.8	80.5	92.9	-	0.525

Note: Enrolment rate estimates are for 2002.

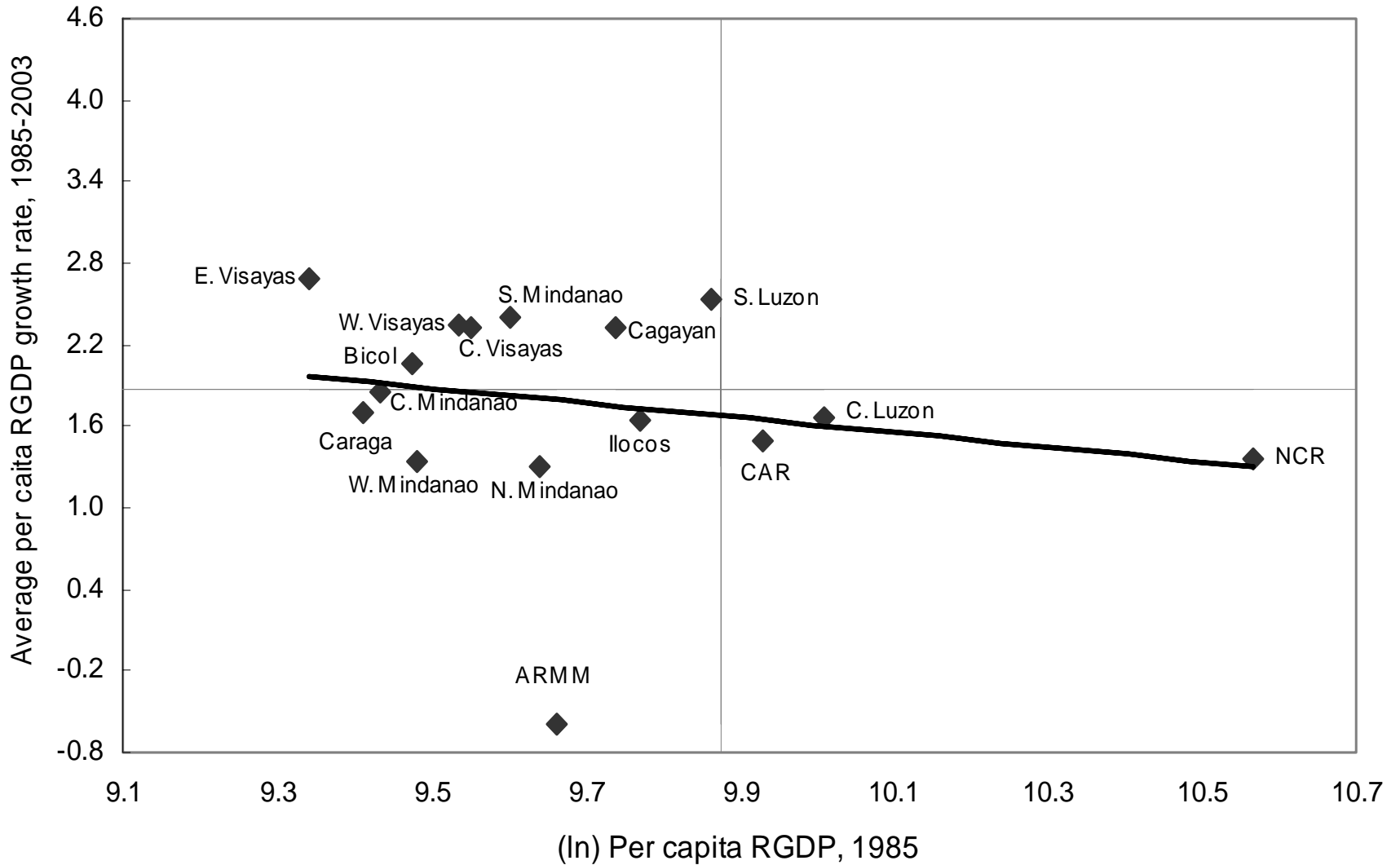
Source: FLEMMS 2003, APIS 2002, UNDP-HDR and various issues of the Philippine Human Development Report.

Social indicators, 2003

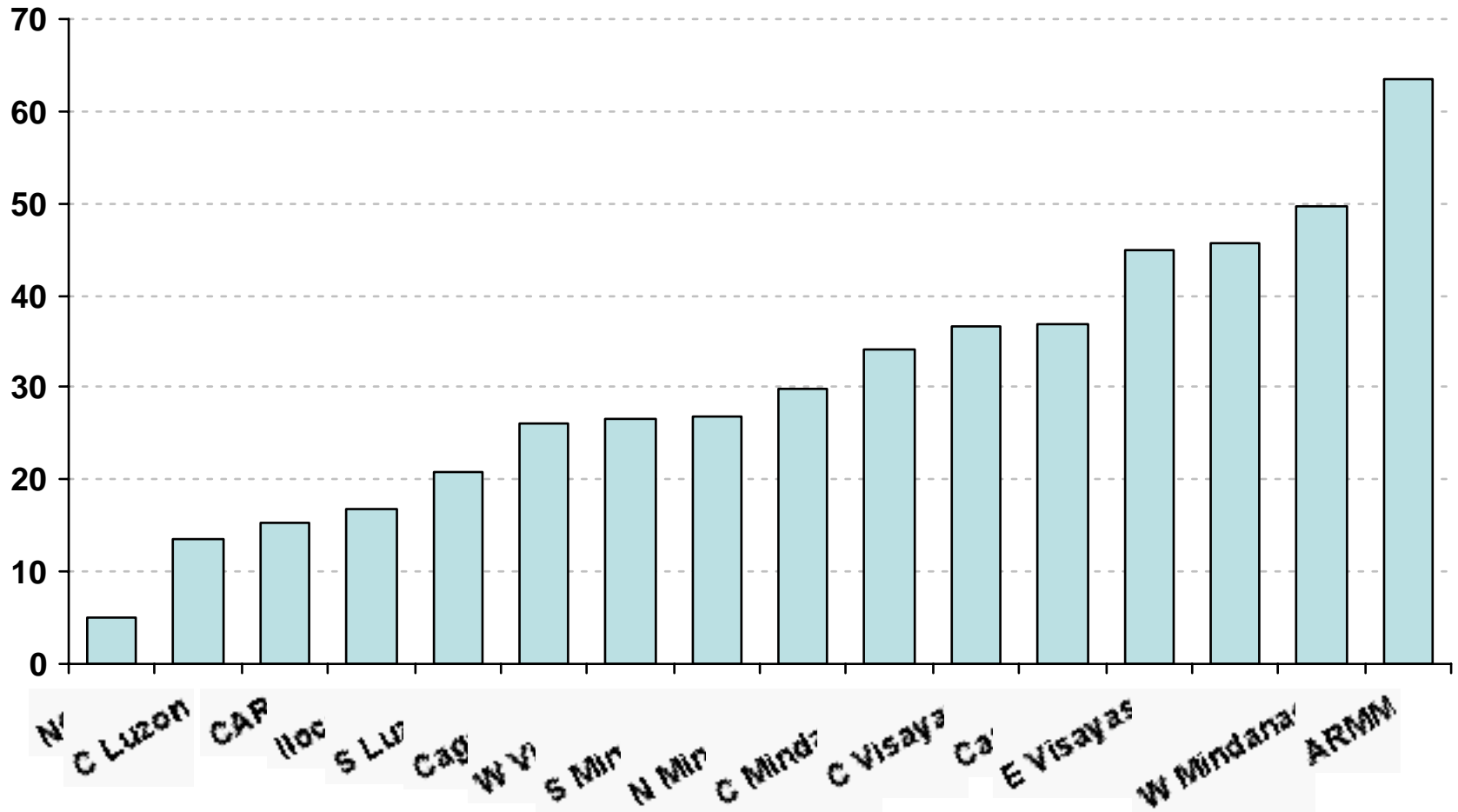
Region	Poverty		Income gini ratio
	Incidence	Contribution to total	
<i>Philippines</i>	26.0	100.0	46.8
NCR	4.9	2.6	43.3
CAR	15.3	1.0	43.1
Ilocos Region	16.9	3.4	41.2
Cagayan Valley	26.2	3.4	47.1
Central Luzon	13.6	5.7	37.6
Southern Luzon	20.8	13.0	43.7
Bicol Region	45.7	10.7	48.9
Western Visayas	26.7	7.8	46.6
Central Visayas	36.6	10.4	47.3
Eastern Visayas	45.0	8.2	49.2
Western Mindanao	49.7	7.6	53.0
Northern Mindanao	29.8	4.1	48.1
Southern Mindanao	26.8	7.2	50.6
Central Mindanao	34.1	4.2	46.2
ARMM	63.4	7.2	40.1
Caraga	36.9	3.7	44.5

Source: Estimates are based on the FIES 2003.

Regional Growth Convergence

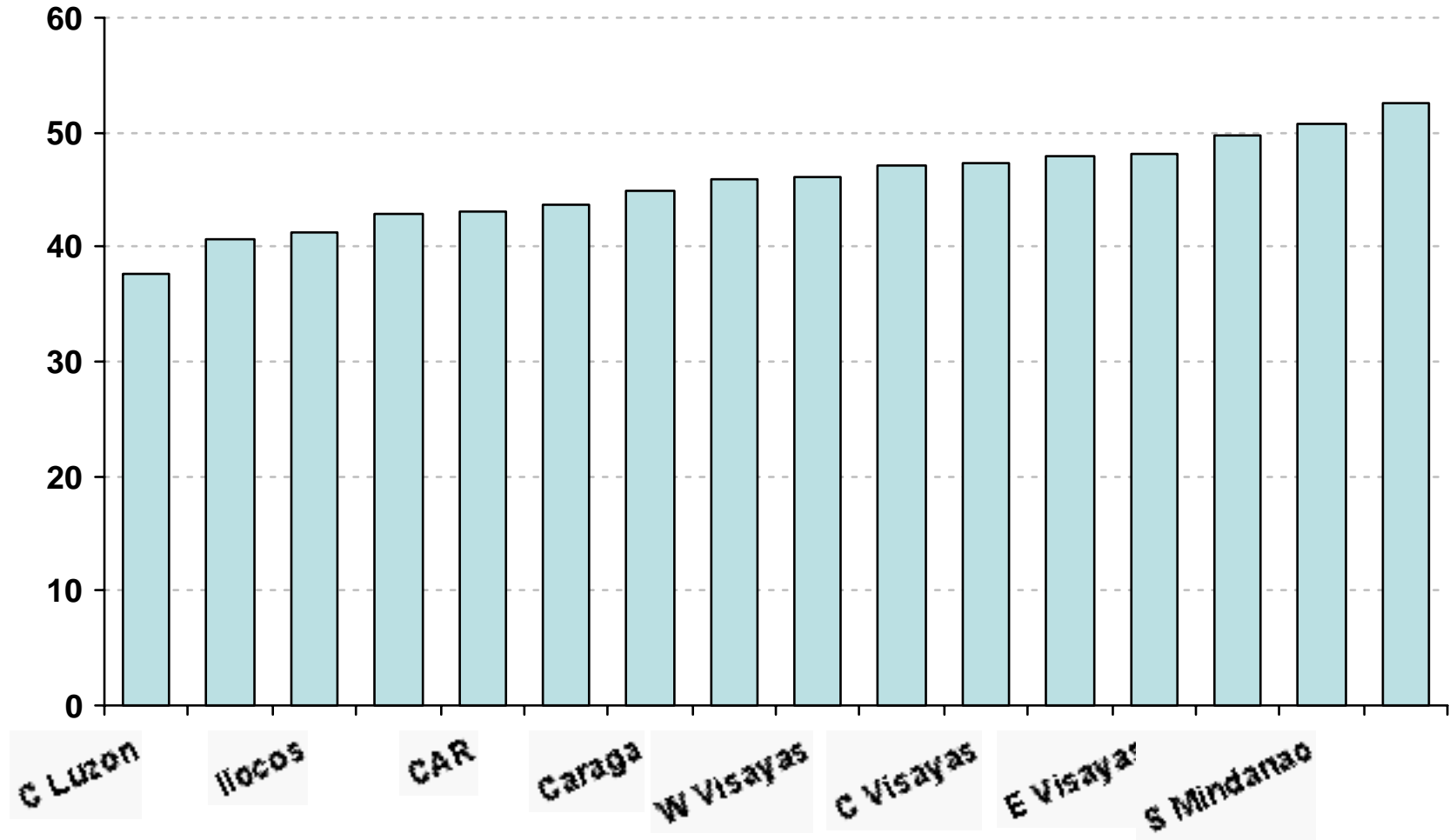


Poverty Incidence, 2003



Source: Estimates based on FIES 2003

Income Gini Ratio, 2003



Infrastructure indicators, 2003

Region	Road density (km/km ²)	Access to potable water (% of HHs)	Access to electricity	Telephone line density per 100	Irrigation serviced (%)
<i>Philippines</i>	0.26	79.4	77.1	8.1	44.7
NCR	5.72	84.6	99.1	25.8	-
CAR	0.15	82.2	72.1	6.3	74.1
Ilocos Region	0.54	89.2	84.9	4.5	64.2
Cagayan Valley	0.19	83.3	74.5	1.0	42.4
Central Luzon	0.41	95.5	93.4	5.3	53.6
Southern Luzon	0.21	85.0	85.1	8.7	49.2
Bicol Region	0.23	71.8	65.4	2.5	49.5
Western Visayas	0.34	69.4	69.0	6.2	38.9
Central Visayas	0.38	71.9	70.1	7.8	55.0
Eastern Visayas	0.20	77.9	61.4	3.2	59.0
Western Mindanao	0.22	58.9	52.6	1.0	46.9
Northern Mindanao	0.32	79.6	69.8	4.8	42.4
Southern Mindanao	0.22	77.3	69.7	6.8	36.1
Central Mindanao	0.19	72.0	56.5	2.9	26.9
ARMM	0.25	40.3	31.7	1.3	14.3
Caraga	0.16	78.7	66.7	5.6	24.5

Note: Road density is adjusted for quality (concrete equivalent).

Irrigation serviced refers to the total irrigated area over the potential.

Source: DPWH, FIES 2003, Philippine Statistical Yearbook

(d) Poverty and Social Indicators:

Economic and social indicators correlate quite closely. But note some deviations: some resource-rich Mindanao regions relatively high pcy but poor social indicators; others quite poor but relatively good education achievements, etc (eg, Ilocos).

(e) The Special Case of Mindanao

History of neglect, cycle of conflict, precarious peace settlements. A high price in at least 3 respects (see PHDR, 2005):

(i) Large number of casualties; extensive displacement.

(ii) Various estimates of direct economic cost; P5-10 billion annually, about 1% of regional GDP; but understates large indirect costs.

(iii) Continued deterioration in relative social indicators. In regional rankings, ARMM provinces dominate the lowest group. Some econometric estimates.

(f) Population, Labour, Migration

Regional demographics reflect economic patterns.

Gradually rising share of Manila & surrounds, reflecting migration patterns and the centre's dominance. A long-established pattern, over-shadowing smaller flows in the past to frontier regions.

Clear correlations between higher pcy's and in-migration. Arguably exacerbates regional inequality, since migrants typically younger, better educated.

Regional labour markets now less regulated, enabling poorer regions to compete for employment.

Internal migration also closely linked to international migration. Latter now very large, with 8 million people abroad, equivalent to almost 1/4 of workforce. Remittances the third largest among developing countries; equivalent to almost 50% of merchandise exports. Probably resulted in increased regional inequality.

(g) Infrastructure and Integration

Infrastructure the key to regional integration; perhaps the major tool of regional policy. Also a major governance issue: long gestation periods have special finance and policy consistency needs; have to deal with natural monopoly issues; and with decentralization, major coordination issues.

Philippine patterns: Regional variations; Mindanao not notably infrastructure-deficient.

Internationally, Philippines ranks poorly: (i) investment/GDP about 1/2 the East Asian average, owing to persistent fiscal problems; (ii) regulatory framework characterized by poor coordination between agencies, tiers of govt, and public-private; (iii) policy environment discourages LT private investors.

Particularly serious in roads. Other sectors perform better, mainly where deregulation has occurred, eg, telecomms, inter-island shipping, domestic civil aviation. Though in all cases, reforms incomplete.

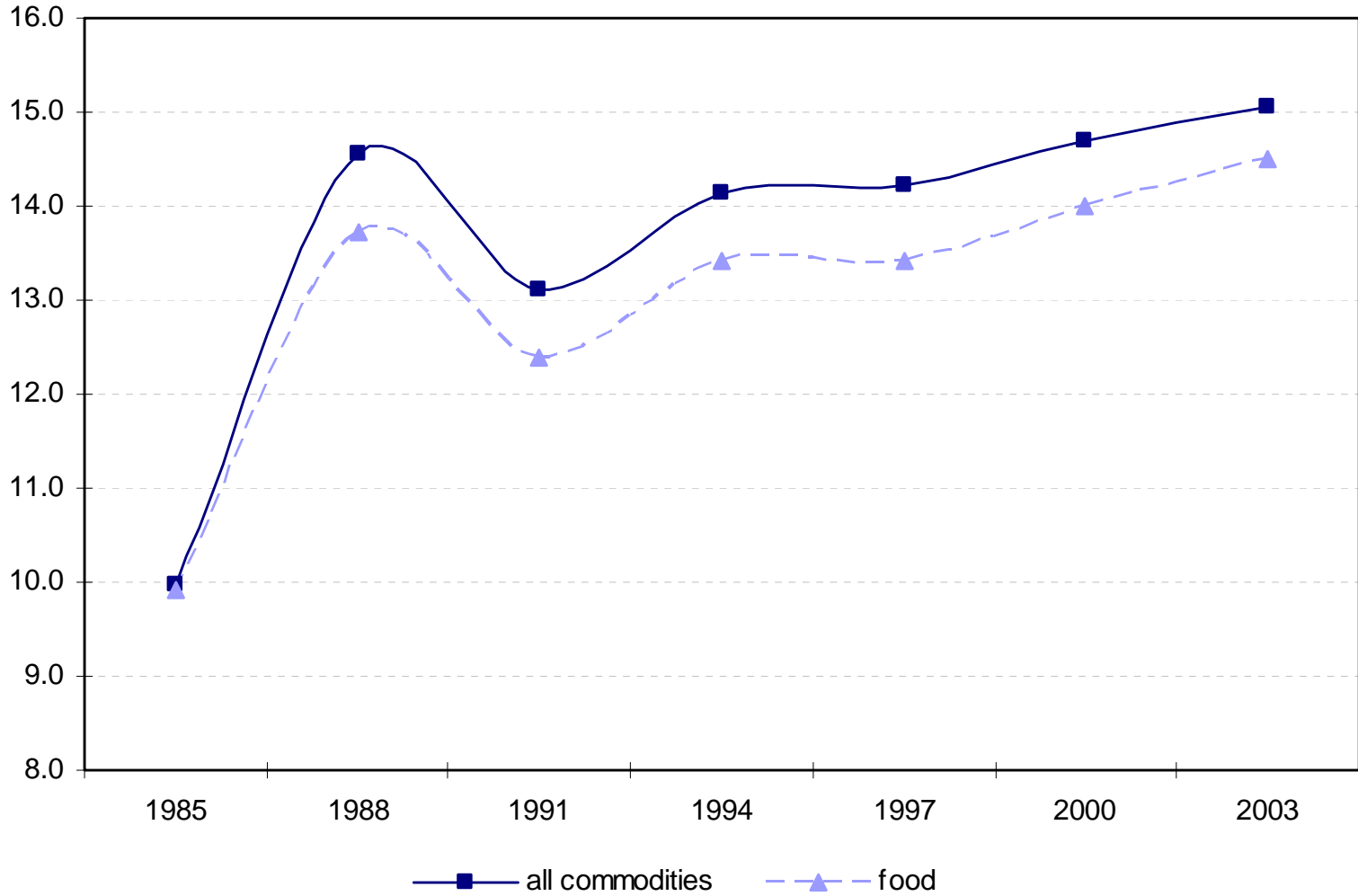
Regional price disparities present mixed picture over time. See Fig.

(h) Regional Dynamics

Rural-urban dimensions: Not as well developed as countries with excellent infrastructure (eg, Taiwan).

Global & regional: Has more open economy led to deconcentration out of Manila? Mixed evidence, as indicated above.

Variation in regional prices



Source: Family Income and Expenditure Survey

Less centralization biases from trade regime. But infrastructure concentration, particularly links to the global economy, still very powerful. Especially in combination with locational decisions re export zones. Eg, Southern Tagalog's share of exports rose from 4% to 51% 1993-2003. EPZs the spatial equivalent of (eg) Mexico's border zones.

Concentration of rapidly growing service exports from in and around the capital is reinforcing this concentration.

(i) Centre-Region Relations

Assignment of functions broadly consistent with public finance theory, ie, that power should be with jurisdictions best able to internalize the costs and benefits of service provision. Except for special case of education.

LGU expenditure as % of GDP approx doubled since LGC, but still small: 1.6% 1985-91, to 3.3% 1992-2003. LGU expenditure share of total public sector below the (unweighted) average of the 'East Asian six' 26% v/s 33%.

Clarity of expenditure assignments clear in principle, but in practice subverted by loopholes, unfunded mandates passed on from the CG.

So system performs less well on autonomy criterion; CG retains major taxes; tightly controls rates which LGUs may set.

Hence revenue and expenditure misalignments:

- i) Growing imbalance between revenues and expenditures of LGUs; resulting in increasing dependence on CG transfers; from 38% of LGU revenue (net of borrowings) 1985-91 to 65% 1992-2003.
- ii) Very slow progress in downsizing CG agencies
- iii) Perverse incentives among LGU tiers; pressure to become cities.

CG grants in two forms: formula-driven (IRA), and ad hoc 'categorical grants'. But even IRA highly unpredictable, especially during (frequent) fiscal 'near-crises'. Also doesn't meet 'horizontal equity' objectives: per capita grants positively related to pcy's.

Equally, LGUs have poor record on revenue raising. See above. Hence 'substitutive' in nature. Local elites unwilling to tax themselves? Especially, major potential but untapped revenue from property tax. Also, poorly maintained and audited financial records. Little attempt to clean up proliferation of local 'nuisance taxes'.

Note also:

- i) Considerable variation in performance among LGUs.

- ii) Still major inter-LGU coordination issues, especially on inter-jurisdictional issues (eg, infrastructure, environment).
- iii) Is there a link between national fiscal balance issues and IRA commitments? Might be a case for linking increased IRA allocations to national revenue effort, so LGUs add to pressure for fiscal reform.

(j) Local Institutions and Governance Quality

Have reforms delivered better quality governance (as literature generally hypothesizes if bring govt 'closer to the stakeholders'), and is there a reform dividend for better governed regions?

Mixed evidence:

No simple matter to define 'governance quality'. Many attempts. Evidence on service quality (eg, health, roads) very mixed.

No obvious correlates of well-governed regions; Makati v/s Naga! Mixed evidence on 'neighbourhood demonstration' effects.

Are governance standards endogenous to pcy and growth?

LGUs anyway have limited capacity to influence local development.

Local politics remains highly personalistic, so difficult to measure quality of institutions independently.

CG has not supplied the requisite framework, inputs, growth.

‘Voice and exit’:

Local democracy seems to have been more effective at rewarding good performance than at disciplining poor leadership.

Exit - ie, migration - dominated by move to higher income regions.

5. SUMMARY & POLICY IMPLICATIONS

i) Philippine decentralization neither a notable success nor a disappointing failure.

ii) The global economy increasingly shapes the economic geography of a now largely open Philippine economy; trade & remittances in particular. More internationally-oriented enclaves?

iii) Investments in key public goods - especially infrastructure and education - are key drivers of a region’s capacity to connect to the global economy, and to grow faster. Infrastructure decisions perhaps the most important (if ‘unintended’) tool of regional policy

iv) Slower changes in regional socio-economic rankings (eg, cf China) reflect slow overall growth rates. Though more fluidity in rankings if measured at finer levels of disaggregation.

v) Decentralization program quite well formulated, sound principles. But implementation record very mixed: division of responsibilities unclear; widespread CG interference; recurring fiscal 'near-crises'; LGU buck-passing on revenue raising.

vi) Mixed record on vertical and horizontal balances. Growing vertical imbalances; horizontal equity; but small LGU shares (3.3%).

vii) Coordination between and among tiers of govt still inadequate. Also mismatches among LGUs (cities v/s provinces); some staff transfer very slow; compounded by problems in national and local bureaucracies.

viii) Difficult to measure LG quality, but it is clearly highly variable; no obvious and systematic correlates.

ix) Has decentralization ameliorated regional discontent with the centre? Not obvious, especially in case of Mindanao.

x) Towards a national and regional policy reform agenda. Some common elements; but no nation-wide, uniform regional policy program.