

Is Economic Openness Good for Regional Development and Poverty Reduction? The Philippines

Ernesto M. Pernia
Pilipinas F. Quising

Asian Development Bank
P.O. Box 789
0980 Manila
Philippines

©2002 by Asian Development Bank
October 2002
ISSN 1655-5260

The views expressed in this paper
are those of the author(s) and do not
necessarily reflect the views or policies
of the Asian Development Bank.

The **ERD Policy Brief Series** is based on papers or notes prepared by ADB staff and their resource persons. The series is designed to provide concise nontechnical accounts of policy issues of topical interest to ADB management, Board of Directors, and staff. Though prepared primarily for internal readership within the ADB, the series may be accessed by interested external readers. Feedback is welcome via e-mail (policybriefs@adb.org).

ERD POLICY BRIEF NO. 10

**Is Economic Openness Good
for Regional Development
and Poverty Reduction?
The Philippines**

**Ernesto M. Pernia
Pilipinas F. Quising**

October 2002

External influences on a country's urban and regional development are not new. Such were common during colonial times when cities became the strategic contact points of the colonizer with the colony. The evolution of ports and local transport systems were strongly shaped by the trade and investment decisions of colonial authorities. Indeed, the location of ports had a decisive impact on the choice of what were to become the primary and secondary urban centers.

Urban primacy or spatial concentration that characterizes many developing countries appears to have been heightened, not lessened, by globalization. Capital and trade flows tend to operate in the world economy via the national capitals that evolve into megacities. This view is supported by empirical evidence on the tendency of foreign direct investment (FDI) to locate in and around the metropolises of East Asian countries (Fuchs and Pernia 1987). A contrarian view suggests that trade openness spurs growth of the countryside, given that exports are not directly linked to the domestic market and producers are induced to locate outside major urban centers where production costs are lower (Krugman and Livas 1996).

This brief derives from research on the relationship between economic openness and regional development (Pernia and Quising 2002). The study analyzes data on the Philippines' 14 regions over the period 1988-2000, during which significant liberalization measures were introduced into the economy. Economic openness is indicated by the ratio of regional exports to gross regional domestic product (GRDP). Regional development is denoted by the growth of GRDP per capita, and poverty reduction is proxied by increases in consumption expenditure per capita of the poorest quintile. More balanced regional development simply means more dispersed development (or narrower disparities) across the regions.

Patterns of Regional Development

Concentrated spatial development characterizes the economy. Metro Manila, or National Capital Region (NCR), continues to dominate all other regions, with a GRDP per capita in 2000 more than twice that of the national average, almost double that of the next highest in the Cordillera Autonomous Region (CAR), and more than

five times that in the poorest region, Bicol (Table 1). CAR's relative development has picked up recently owing to special attention from the government. More importantly, this region includes Baguio, a popular tourist destination and site of a major export processing zone. By contrast, Bicol has traditionally been the most backward region, partly because destructive typhoons pass through it several times a year.

Table 1. GRDP per Capita, Expenditure Per Capita of Poorest Quintile, and Regional Shares of Exports and FDI

REGION	GRDP per capita (1985 prices) ₱		Expenditure per Capita Poorest Quintile (1985 prices) ₱		Share of Exports (percent)		Share of Approved FDI (percent)		
	1988	2000	1988	2000	1988	2000	1988	2000	
	A	Metro Manila	26,090	29,577	3,183	3,680	57.1	23.6	42.7
B	CAR	11,066	14,952	2,021	2,063	0.0	6.5	0.0	1.9
	Ilocos	5,675	6,873	2,087	2,236	3.7	0.1	0.1	0.0
II	Cagayan Valley	5,942	7,150	1,849	2,344	0.1	0.0	0.0	0.0
III	Central Luzon	10,546	10,673	2,535	2,924	4.6	7.3	21.0	9.6
IV	Southern Tagalog	12,784	13,179	1,917	2,516	3.7	52.3	28.8	63.4
V	Bicol	4,789	5,227	1,546	1,487	0.4	0.1	0.1	0.0
VI	Western Visayas	8,586	9,869	1,785	1,949	1.3	0.2	0.6	1.7
VII	Central Visayas	9,696	11,118	1,256	1,365	6.7	5.6	3.2	5.2
VIII	Eastern Visayas	5,334	5,828	1,433	1,493	5.9	1.0	0.1	0.0
IX	Western Mindanao	6,393	7,494	1,536	1,446	1.8	0.5	0.5	0.0
X	Northern Mindanao	10,356	11,659	1,722	1,703	5.1	0.8	0.0	0.0
XI	Southern Mindanao	11,784	11,181	1,797	2,089	7.2	1.9	2.9	0.1
XII	Central Mindanao	8,800	7,786	1,813	1,709	2.5	0.3	0.0	0.0
	Philippines	11,215	12,178	2,002	2,266	100	100	100	100

Sources: *Philippine Statistical Yearbook* (National Statistics Office, various issues); *Foreign Trade Statistics* (National Statistics Office, various issues); FIES various surveys; Board of Investments data; Philippine Economic Zone Authority data; National Statistics Coordination Board data.

Evidently, regions bordering Metro Manila benefit from spillover effects. However, part of their relative buoyancy is attributable to international trade and FDI. Most of the export processing zones (EPZs)—are located in four regions: Metro Manila, Southern Tagalog,

Central Luzon, and Central Visayas, which are the main recipients of FDI. Similarly, these regions are the main sources of the country's exports (Table 1).

Among the four regions, Metro Manila's prominence in exports and FDI appears to on the wane, however, over the period 1988-2000. Southern Tagalog, which has seen a mushrooming of EPZs in recent years, has taken over the lead. NCR's loss in exports and FDI, nonetheless, has apparently been offset by increases in domestic consumption. At the other extreme, all four Mindanao regions suffered drastic cuts in both export and FDI shares owing to peace and order problems in a few areas, resulting in adverse publicity for the whole of Mindanao. Overall, exports tend to be better distributed spatially than FDI because agricultural regions are also involved in exports.

An indicator of the welfare of the poor (or poverty reduction) is the consumption expenditure per capita of the poorest quintile. This varies considerably across the regions, with no discernible improvement in interregional inequality over the period 1988-2000. Another measure, poverty incidence (or the proportion of the population below the national poverty line), shows a similar pattern. Poverty incidence is lowest in Metro Manila at 5.6 percent, followed by Central Luzon, Southern Tagalog, and CAR at just under 20 percent. Western Mindanao and Bicol have the highest poverty rates at over 50 percent. What seems surprising is the relatively high poverty rate in Central Visayas (39 percent) despite its relatively high income level and good education and health indicators. This probably reflects sharper intraregional inequality, implying that aggregate economic and social benefits may not be trickling down fast enough to the lower levels (Monsod and Monsod 1999). This suggests the need for a subregional or more micro approach to poverty reduction. It could also reflect below-average performance of the agricultural sector on which the majority of the poor depend, implying the need for appropriate investments in this sector.

Social development differences (education and health indicators) across the regions do not appear to be as marked as the economic disparities. This may suggest that the relative effectiveness of public spending for social sectors at the local level varies little. Overall, poverty indicators track economic indicators more closely than social indicators.

Determinants of Regional Development and Poverty Reduction

Econometric analysis of 5-year panel data on the regions can shed further light on the issue of whether or not economic openness is good for regional development and poverty reduction. The results are distilled below.

Regional development appears to be strongly influenced by the degree of trade openness, as well as by public spending for infrastructure. In turn, regional exports and FDI are determined by SEZs, physical infrastructure, and human capital. In addition, exports are influenced by agricultural terms of trade that favor regions with comparative advantage in agriculture.

The welfare of the poor is significantly influenced by regional development (growth in GRDP per capita). Further, the poor's well-being is directly affected by public spending for social sectors including agrarian reform, human capital, and the availability of roads and electricity.

However, trade openness does not appear to directly benefit the incomes of the poor other than through the growth of regional incomes. This is consistent with a recent survey on trade, growth and poverty (Krueger and Berg 2002).

Conclusion

Economic openness appears to be good for regional development and, indirectly, poverty reduction. Nevertheless, it seems that economic openness cannot by itself bring about more balanced regional development, i.e., narrower disparities in regional incomes and poverty. In the postcolonial era, further spatial development is set by domestic market forces and public policy, and external factors tend to follow such set pattern. FDI goes to where there is good infrastructure, human capital, favorable policy environment, and economies of agglomeration. Similarly, non-traditional exports tend to originate in areas with adequate physical and human capital. To foster more balanced regional development, the government must take the lead in providing infrastructure, implementing sound decentralization measures, and improving the climate for private sector investment and productivity.

References

- Fuchs, R. J., and E. M. Pernia, 1987. "External Economic Forces and National Spatial Development: Japanese Direct Investment in Pacific Asia." In R. J. Fuchs, G. W. Jones, and E. M. Pernia, eds., *Urbanization and Urban Policies in Pacific Asia*. Boulder and London: Westview Press.
- Krueger, A., and A. Berg, 2002. "Trade, Growth, and Poverty: A Selective Survey." Paper presented at the World Bank's Annual Bank Conference on Development Economics, Washington, D.C., 29-30 April.
- Krugman, P. R., and R. E. Livas, 1996. "Trade Policy and the Third World Metropolis." *Journal of Development Economics* 49:137-50.
- Monsod, S. C., and T. C. Monsod, 1999. "International and Intranational Comparisons of Philippine Poverty." In A. M. Balisacan and S. Fujisaki, eds., *Causes of Poverty : Myths, Facts & Policies*. Quezon City: University of the Philippines Press.
- National Statistics Coordination Board (NSCB), various years. *Foreign Direct Investment Report.*, Makati City.
- National Statistics Office (NSO), various years. *Foreign Trade Statistics of the Philippines*. Manila.
- , various years. *Philippine Statistical Yearbook*. Manila.
- Pernia, E. M., and Quising, P. F. 2002. Economic Openness and Regional Development in the Philippines. ERD Working Paper Series, Economics and Research Department, Asian Development Bank, Forthcoming.

ERD POLICY BRIEF SERIES

- No. 1 Is Growth Good Enough for the Poor?
Ernesto M. Pernia
October 2001
- 2 India's Economic Reforms
What Has Been Accomplished?
What Remains to Be Done?
Arvind Panagariya
November 2001
- 3 Unequal Benefits of Growth in Viet Nam
Indu Bhushan, Erik Bloom, and Nguyen Minh Thang
January 2002
- 4 Is Volatility Built into Today's World Economy?
J. Malcolm Dowling and J.P. Verbiest
February 2002
- 5 What Else Besides Growth Matters to Poverty
Reduction? Philippines
Arsenio M. Balisacan and Ernesto M. Pernia
February 2002
- 6 Achieving the Twin Objectives of Efficiency and Equity:
Contracting Health Services in Cambodia
Indu Bhushan, Sheryl Keller, and Brad Schwartz
March 2002
- 7 Causes of the 1997 Asian Financial Crisis:
What Can an Early Warning System Model Tell Us?
Juzhong Zhuang and Malcolm Dowling
June 2002
- 8 The Role of Preferential Trading Arrangements
in Asia
Christopher Edmonds and Jean-Pierre Verbiest
July 2002

- 9 The Doha Round: A Development Perspective
Jean-Pierre Verbiest, Jeffrey Liang, and Lea Sumulong
July 2002
- 10 Is Economic Openness Good for Regional
Development and Poverty Reduction?
The Philippines
Ernesto M. Pernia and Pilipinas F. Quising
October 2002

For information and to order, write to
Office of External Relations, Asian Development Bank
P.O. Box 789, 0980 Manila, Philippines
or e-mail adbpub@adb.org