



# **Why the Philippines is not (yet) in a middle-income trap**

And why we should worry nonetheless

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For the EMIT Project

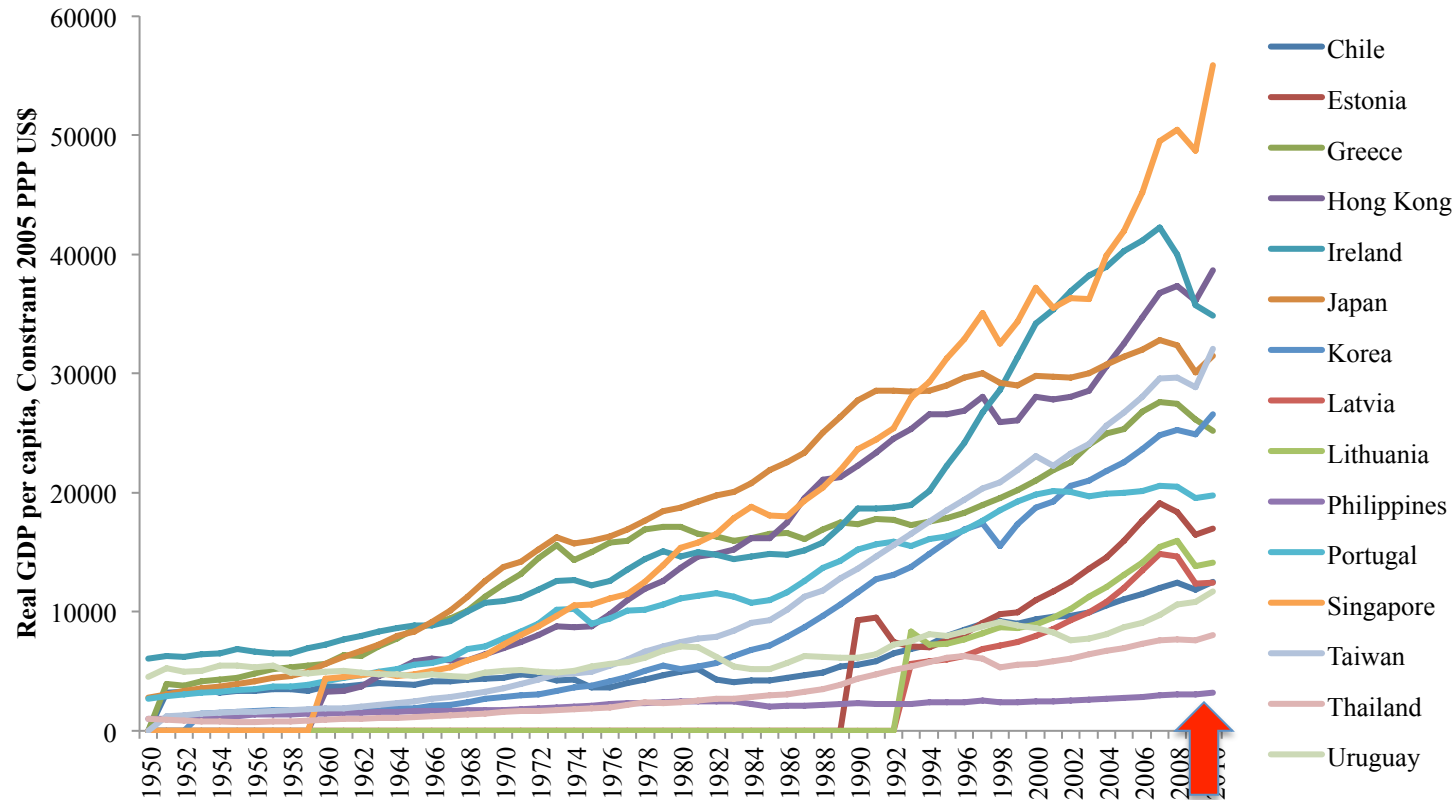
# 1. The idea of it

# Middle-income trap

*Original issue:* Why do some economies grow rapidly for a time but then stagnate long after without graduating into high-income economies?

*Hypothesis:* [Such economies are] “unable to compete with either low-wage economies or highly skilled advanced economies” [Kharas and Kohli 2011]

# *El demonio de las comparaciones*



Source: Zander, Tulder, Pelkmans-Balaoing [2016]

# The usual explanation

- Rapid growth: “catch-up” using known technology and low wages to export to developed countries;
- Employment expands, wages rise, initial advantage eroded; also diminishing returns to using borrowing technology.
- Ultimately a slowdown: lose advantage to other countries.
- Indicated change: shift to more knowledge-intensive industries.

# The usual prescription

Measures at the macro-economic/macro-development level

- investment in physical infrastructure
- higher education and R&D
- foreign direct investment (source of technology)
- Involvement in regional trade and production networks
- diversification of trade and output

# Algebra: how long will it take?

- Temporal criterion: time to traverse middle-income category

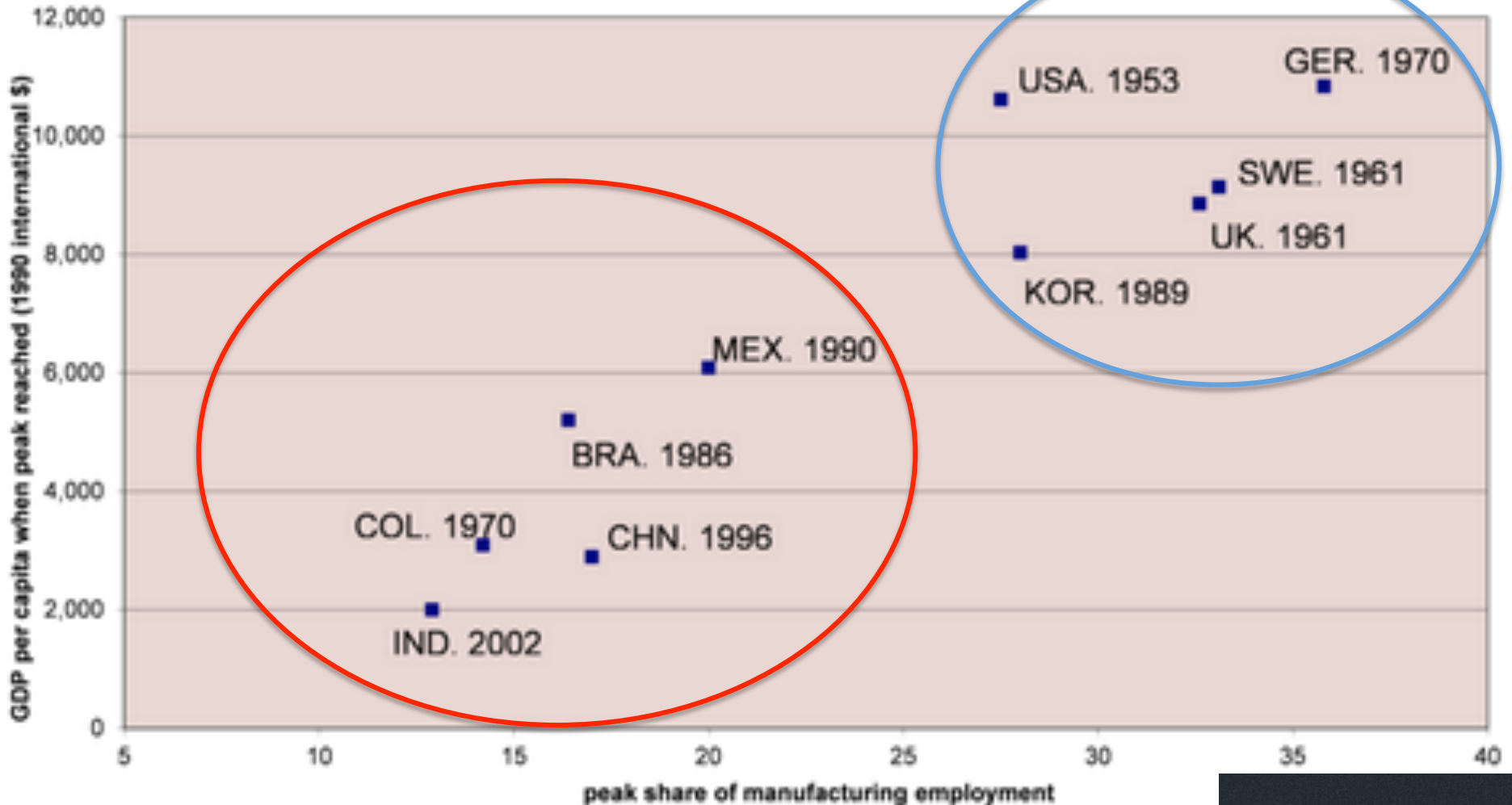
	LMI to HMI	UMI to HI	LMI to HI
GNI per capita (2012 \$ PPP)	\$1,045- \$4,125	\$4,125- \$12,615	\$1,045- \$12,746
Heuvelen [2015]	22-28 yrs	16-22 yrs	44 yrs
Implied growth rate	5-6%	5-7%	6%
Felipe [2012]	28 yrs	14 yrs	42 yrs
Implied growth rate	5%	8%	6%

# Structural criterion?

- From experience, those who transited saw “**peak manufacturing**” at 25% or more of labour force.
- Now fewer countries able to achieve this: now peak at 13-16%.
  - Rodrik [2015]: “premature deindustrialisation”
  - Fabella [201“development progeria” [Fabella ]
- What does it represent? Possibilities:
  - general labour skills; technological levels of firms; middle class consumption; middle class politics



# Premature deindustrialisation?



Source: [http://rodrik.typepad.com/dani\\_rodriks\\_weblog/2013/10/on-premature-deindustrialisation](http://rodrik.typepad.com/dani_rodriks_weblog/2013/10/on-premature-deindustrialisation)

# Structural criterion?

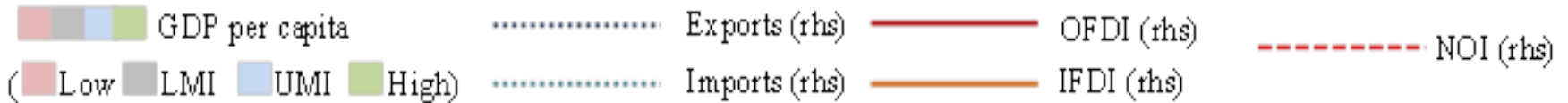
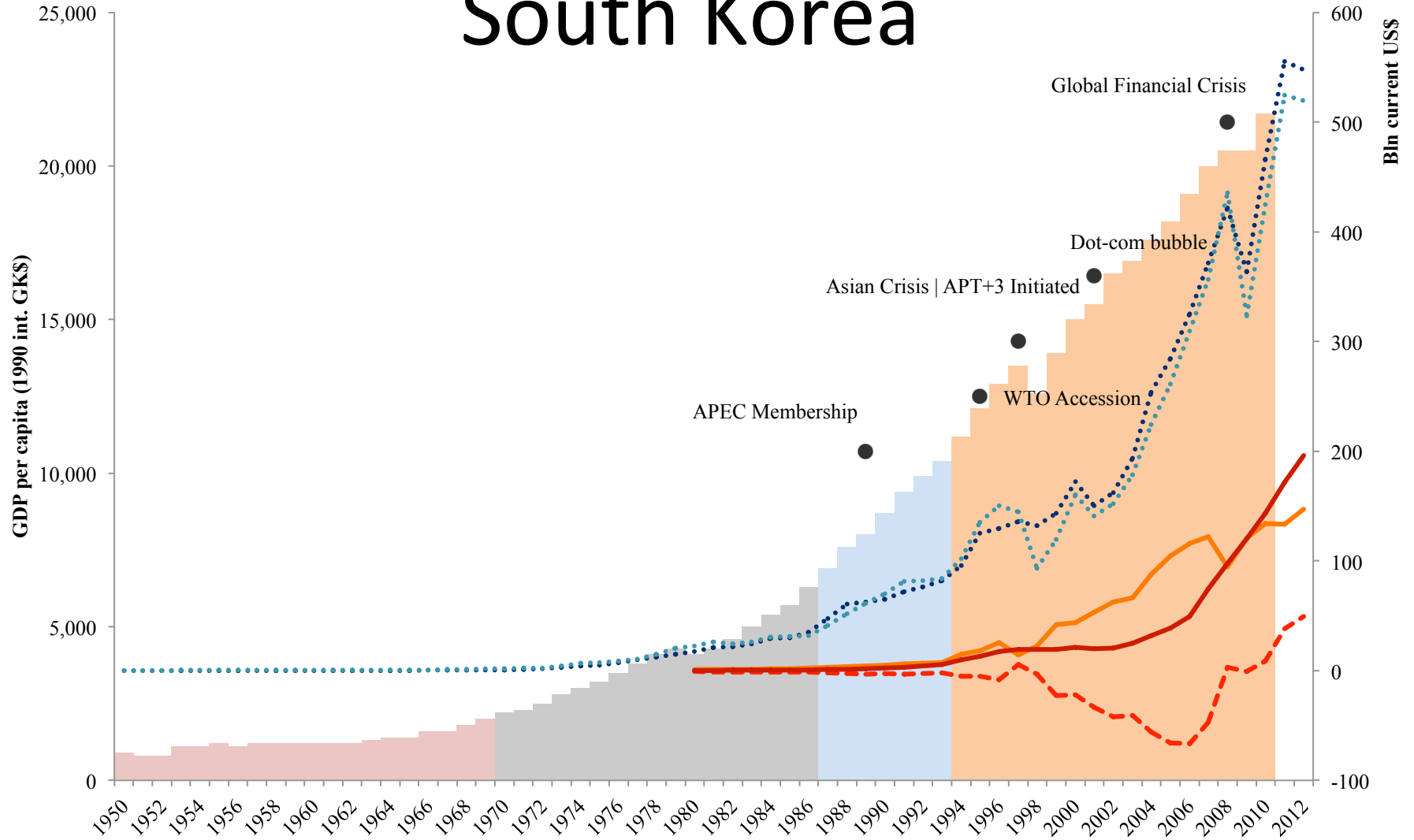
Table 1: Peak and Current Manufacturing Shares, Selected Economies  
(Ordered by year of peak manufacturing employment share)

	Employment Shares (%)				Output Shares (%)			
	Peak		Latest		Peak		Latest	
	Year	Level	Year	Level	Year	Level	Year	Level
* United Kingdom	1970	34.7	2008	12.0	1970	28.9	2010	10.7
* United States	1970	26.4	2009	10.4	1972	23.8	2010	12.9
Argentina	1970	22.6	2005	11.5	1976	38.7	2010	20.5
Philippines	1971	11.3	2008	8.6	1973	28.9	2008	21.4
* Japan	1973	27.5	2008	18.4	1973	32.4	2010	19.4
Brazil	1986	16.4	2007	13.4	1980	33.3	2010	16.2
* Korea, Republic of	1989	27.8	2008	16.8	2010	30.3	2010	30.3
Mexico	1990	20.0	2008	16.9	1988	23.2	2010	18.3
India	2001	14.8	2005	13.6	1995	18	2010	14.7
Indonesia	2002	12.9	2008	12.0	1997	29.4	2010	24.8
China, People's Republic of	2010	16.9	2010	16.9	1978	40.5	2010	29.6

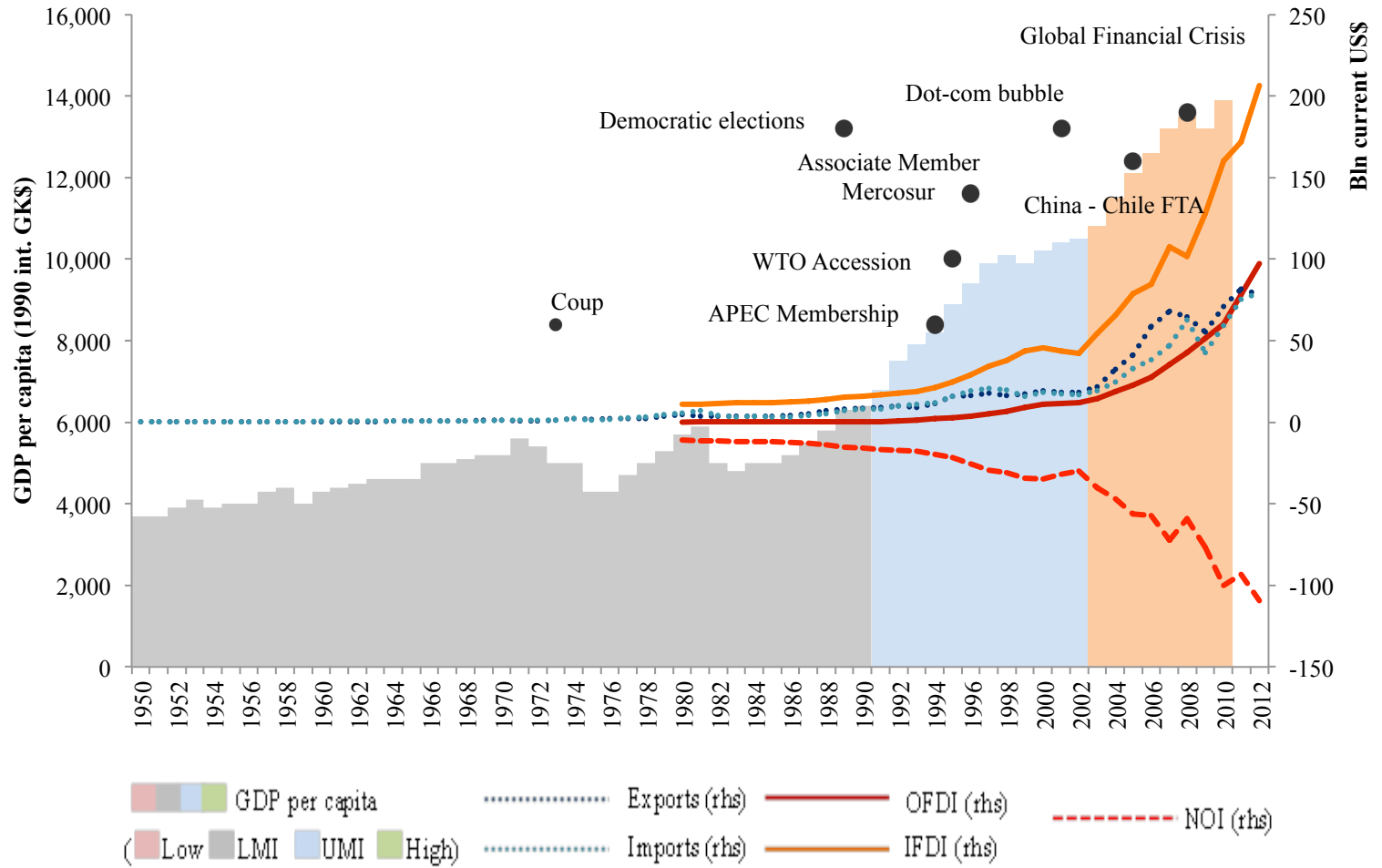
Notes: Peak shares are calculated as 7-year (centered) moving averages from 1970 to 2010. The peak is the highest of all these moving averages.

## 2. How does all this apply?

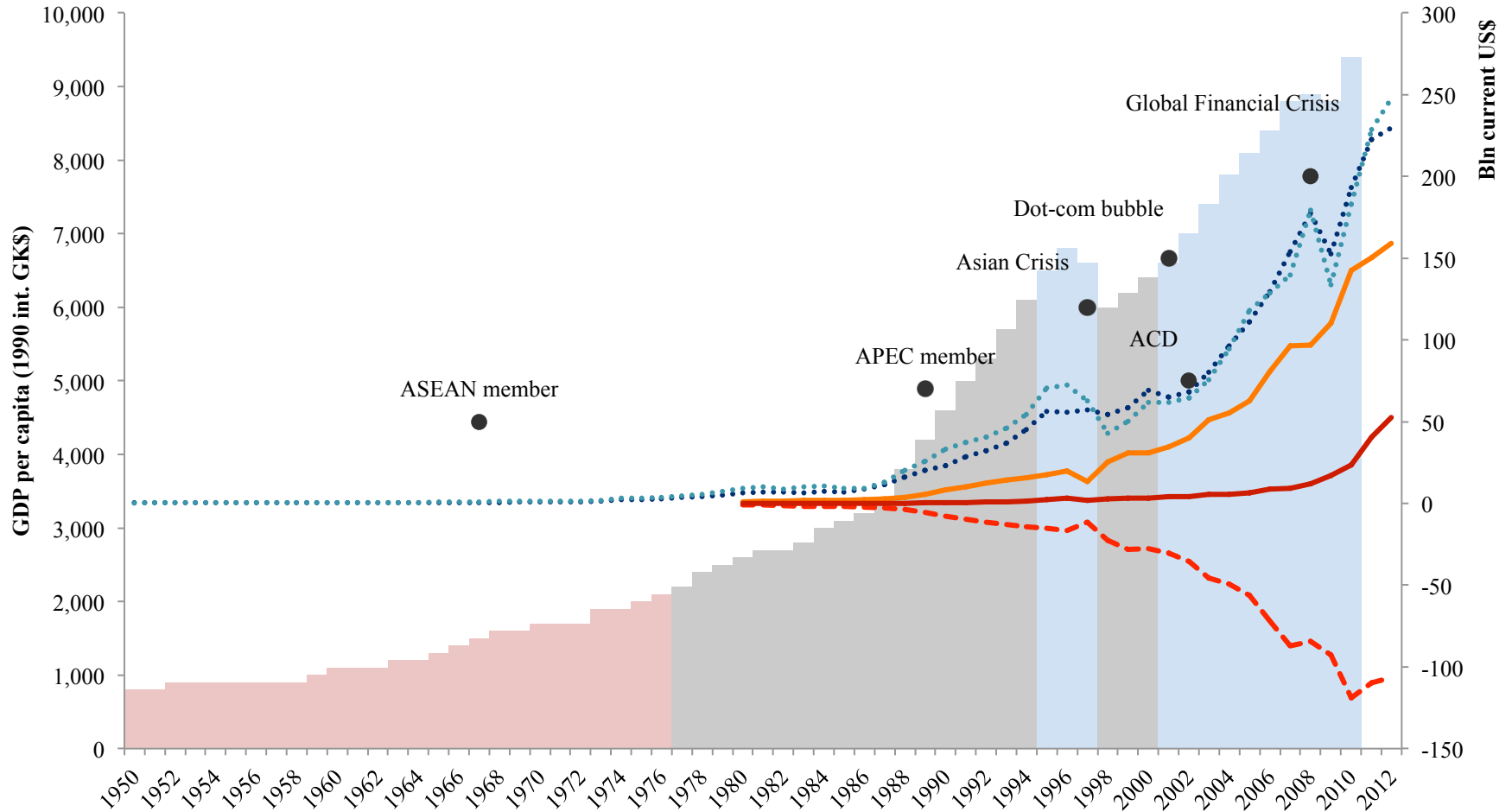
# South Korea



# Chile



# Thailand



GDP per capita

Exports (rhs)

OFDI (rhs)

NOI (rhs)

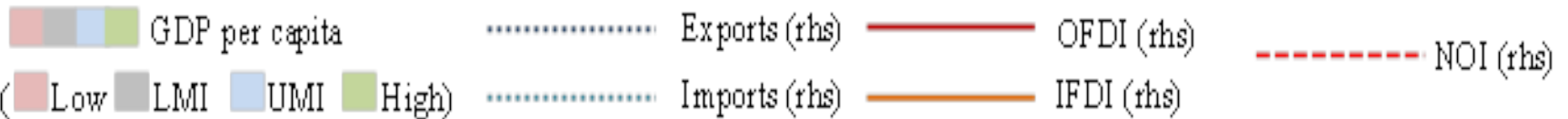
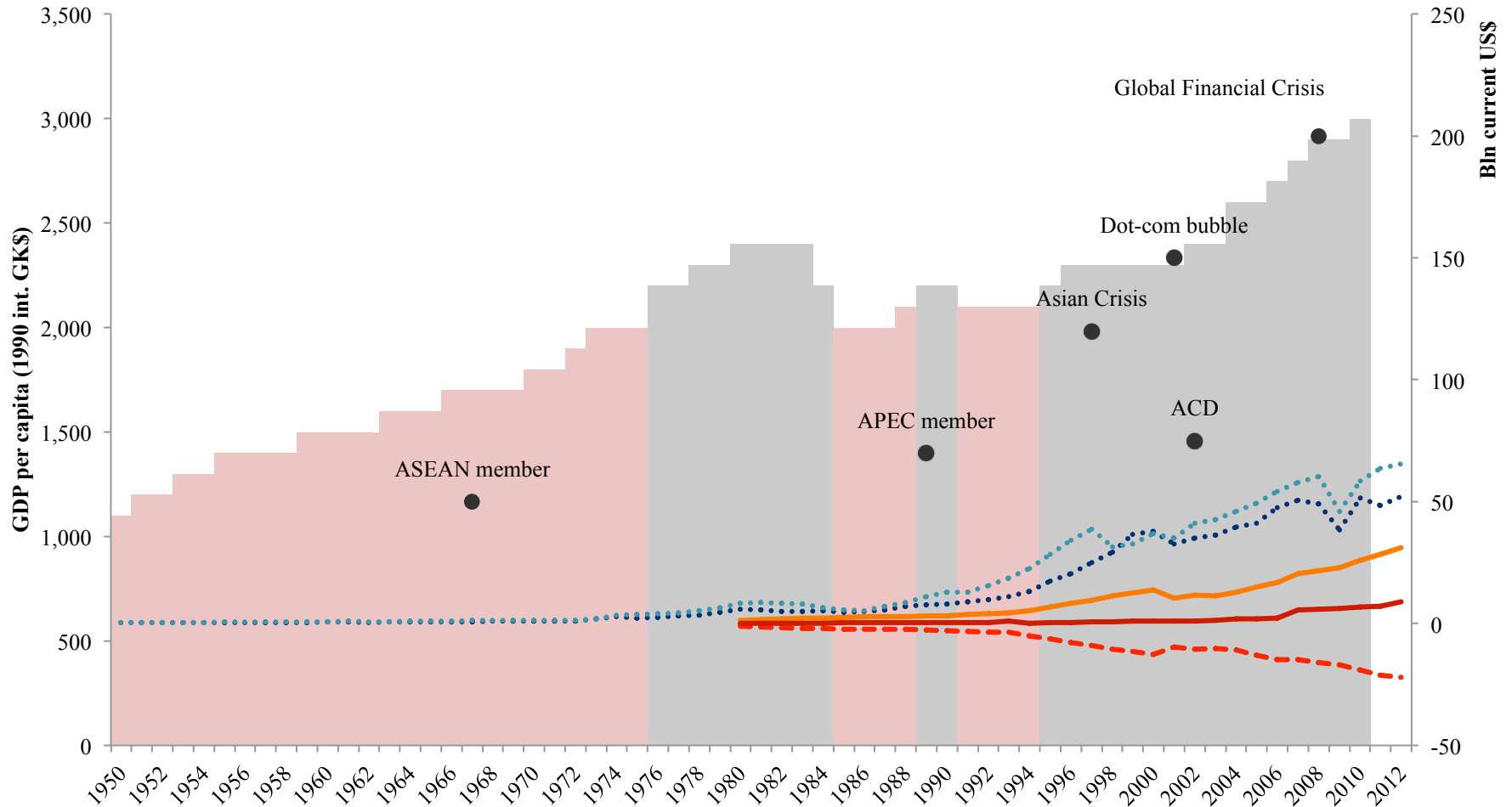
Low
  LMI
  UMI
  High

Imports (rhs)

OFDI (rhs)

IFDI (rhs)

# Philippines



# Just algebra: how long will it take?

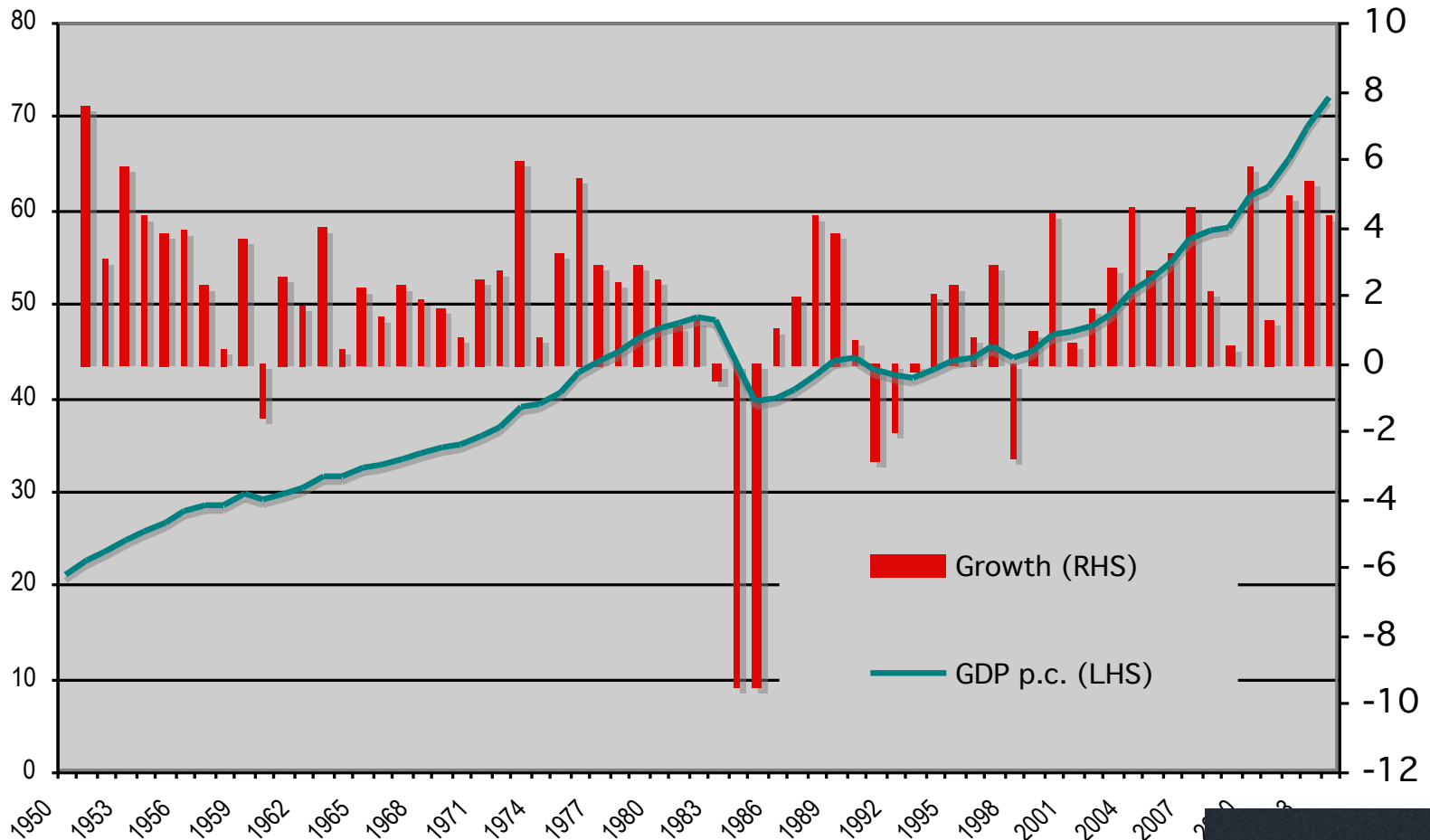
- Empirical question: Suppose Philippine GNI grows at 5-7 percent *indefinitely*?
- Then the following trajectories result:

GNI growth	5 %	6%	7%
Cross LMI (years)	4.4	3.5	2.9
Cross HMI (years)	34.7	27.3	22.5
Total (years)	39.1	30.8	25.4

\*Assumes annual population growth rate of 1.3 percent.



# The past record

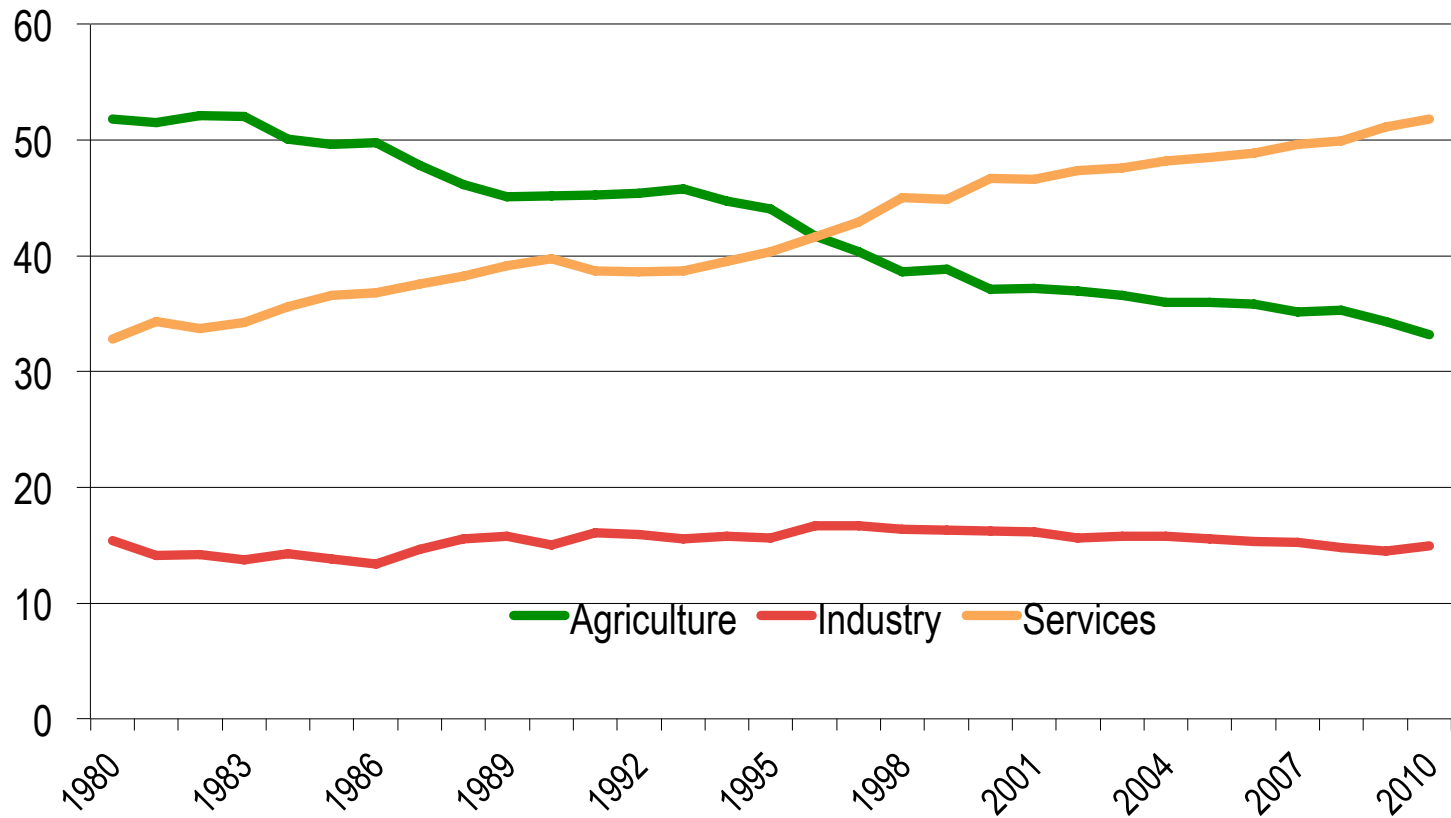


# *Pasawáy*

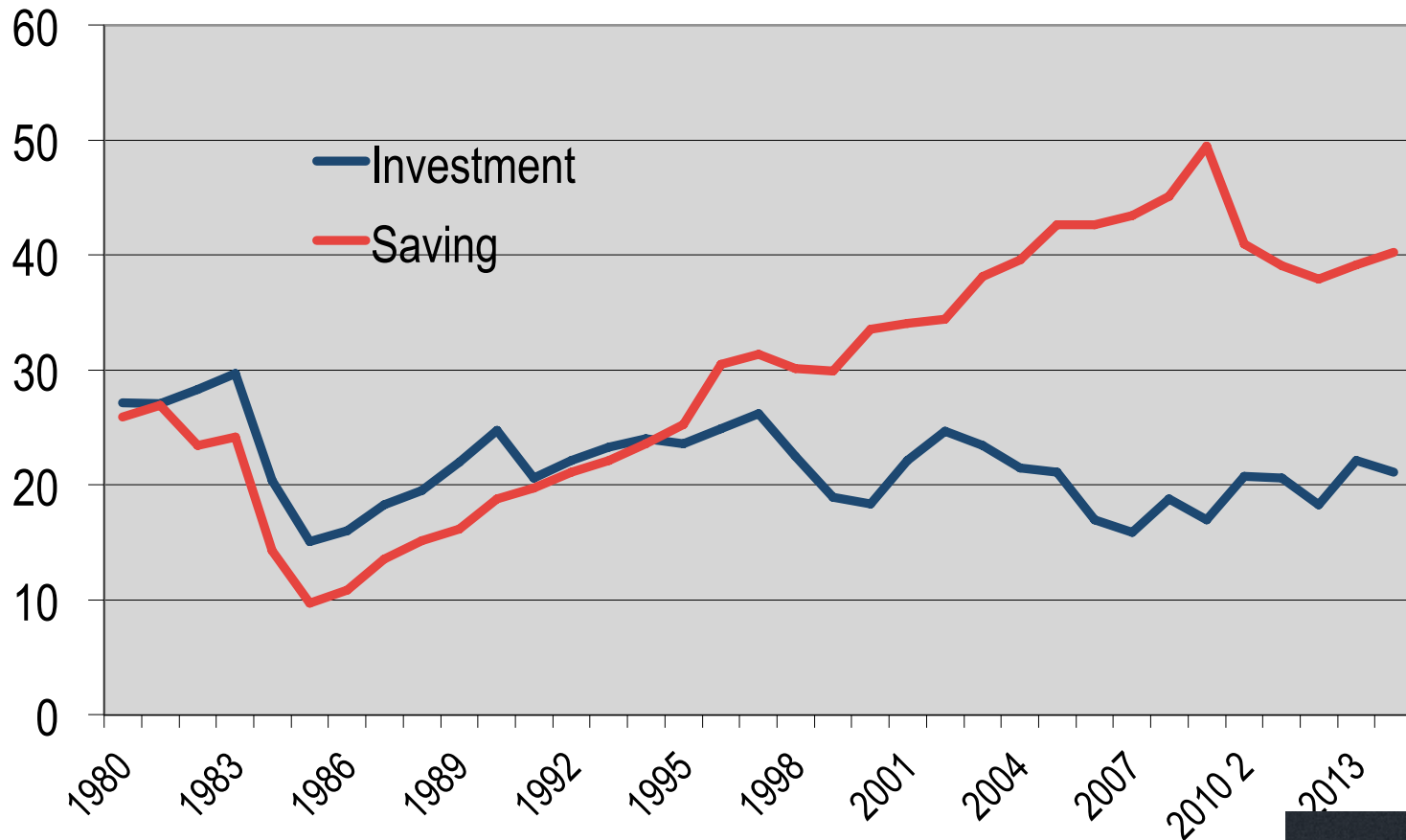
Philippines' "deviant behaviour" [de Dios and Williamson 2015] (deviation from the East Asian pattern):

- Large current account surpluses from overseas remittances and IT-BPM service exports
- Saving exceeds investment
- Low inward FDI and low home investment as well
- Low goods export (manufactures and agriculture)
- Consumption trumps exports and investment
- Services dominate output, employment, exports
- Bi-modal economy: omitted industrialisation, premature de-agriculturisation

# Employment shares (in %)



# Saving and investment (as % of GDP)



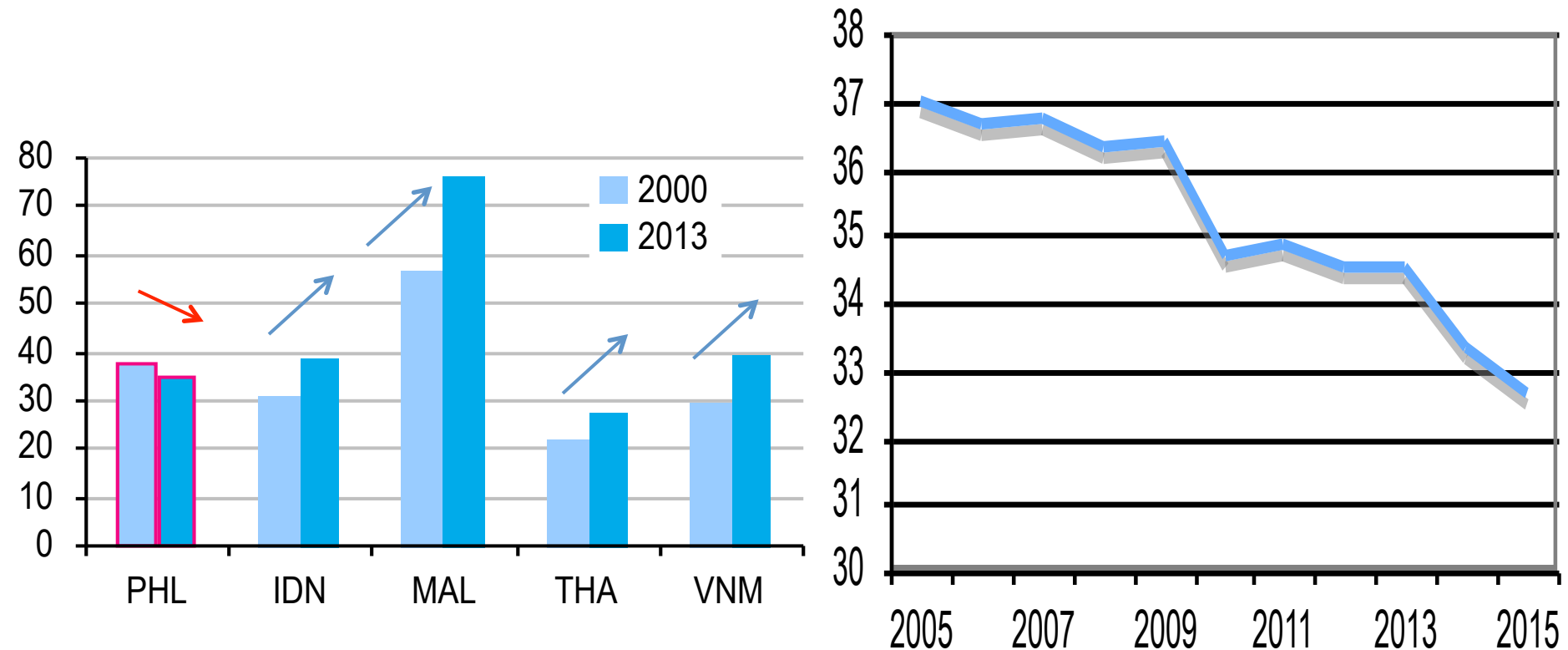
# Farm size

	1960	1971	1980	1991	2002	2012
Average farm area (hectares)	3.59	3.61	2.84	2.17	2.29	1.29
Total number of farms (million)	2.166	2.354	3.420	4.610	4.823	5.563
<i>Of which the share in total number of:</i>						
Farms less than 1 hectare (%)	11.5	13.6	22.7	36.6	40.1	56.8
Farms 1.00 - 2.99 hectares (%)	50.8	47.5	46.1	42.7	40.9	32.0
Total area in (million hectares)	7.772	8.494	9.725	9.975	9.671	7.190
<i>Of which the share in total area of</i>						
Farms less than 1 hectare (%)	1.6	1.9	3.8	7.3	8.6	12.3
Farms 1.00 - 2.99 hectares (%)	23.1	22.2	25.9	30.5	31.0	29.4

Source: *Census of agriculture and fisheries*, various years

Source: MCC-CDT (2016)

# Relative labour productivity in agriculture (%)



Source: MCC-CDT (2016)

# What could go wrong?

- High chance of crossing into HMI : but can we stay there?
- Non-inclusive growth (lagging agriculture and low-productivity services) can lead to social discontent.
- Automation/robotisation and onshoring trends can threaten IT-BPM; makes manufacturing entry difficult
- Dutch Disease renders all tradeables uncompetitive
- Political and economic conditions in OFW regions may change (e.g., falling oil prices).

# What can be done?

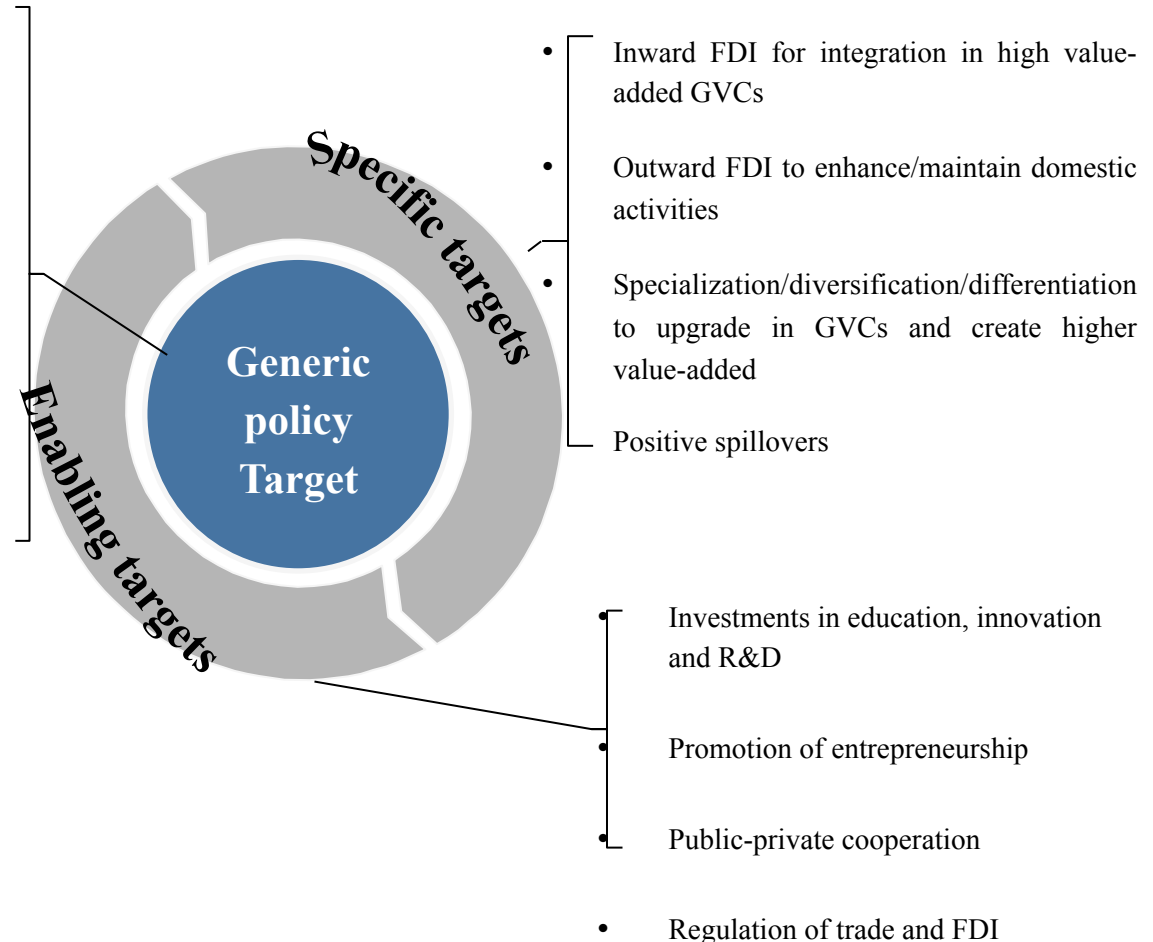
- Complete unfinished business to extend growth momentum
  - link agriculture and SMEs with growing urban markets and chains of higher value-added
  - promote manufacturing employment for inclusiveness
  - complete foundational requirements of education and basic infrastructure
- Pick up from MIT success stories
  - “exogenous” v. “endogenous: development paths (e.g., low v. high FDI dependence).
  - though not completely relevant to deviant behaviour



# Successful pathway: Endogenous growth

## Internal trajectory

- Low/medium trade openness
- Strong growth of trade
- Net exporter
- Medium/high GVC participation
- Integration in high-tech GVCs with medium/high DVA
- Large share of domestically founded lead firms in high-tech GVCs

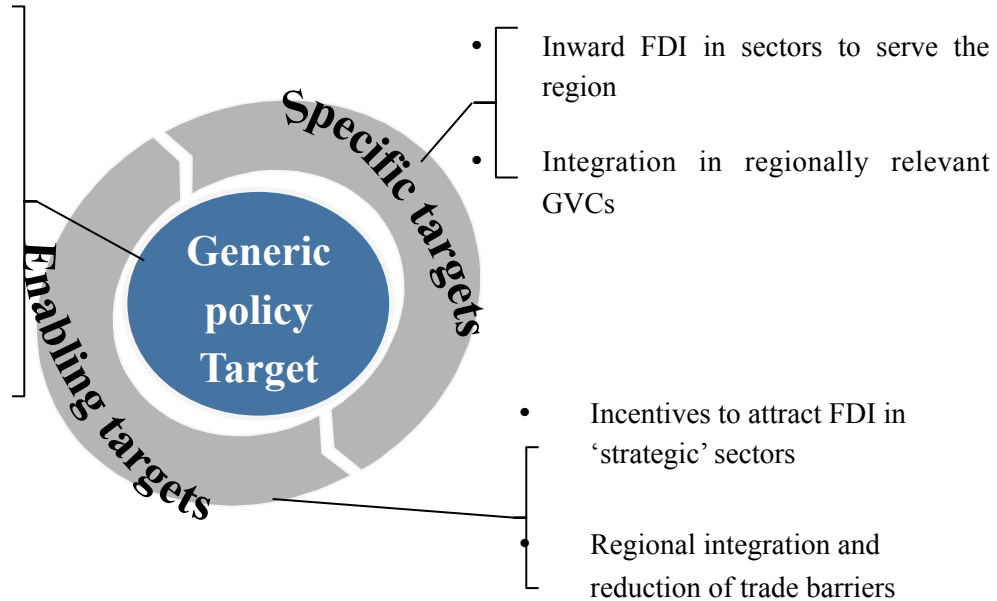


Source: Zander, Tulder, Pelkmans-Balaoing [2016]

# Hub....

## Hub trajectory

- High trade openness
- Medium/high growth of exports
- Low/medium growth of imports
- Net importer
- Medium/high GVC participation
- Integration in medium/high-tech GVCs with low/medium DVA
- Large share of foreign lead firms

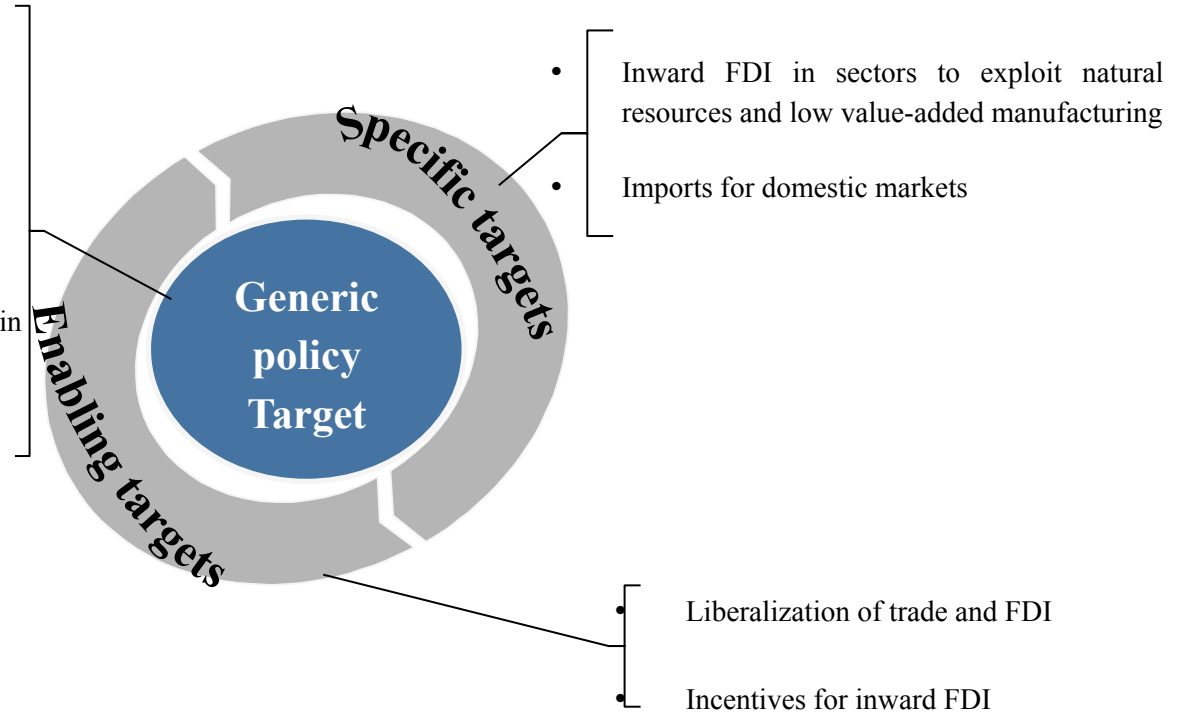


Source: Zander, Tulder, Pelkmans-Balaoing [2016]

# Exogenous growth

## External trajectory

- Low/medium trade openness
- Low/medium growth of trade
- Net importer
- Low/medium GVC participation
- Integration in low-tech GVCs with high DVA
- Large share of foreign lead firms active in low/medium-tech GVCs



Source: Zander, Tulder, Pelkmans-Balaoing [2016]

# What can be done?

- Anticipate new challenges and approaches (better than “build it for whoever may come”):
  - strategise regarding country’s position in the global division of labour
  - formulate policies accounting for heterogenous firms
  - connect with leading global firms based awareness of firms’ strategies and country’s priorities (competitiveness and inclusiveness)
  - form a smarter bureaucracy that engenders trust in its strategic policies and decisions
  - align infrastructure and higher-education (S&T) investments with strategic goals.

**END**