Southeast Asian Affairs 2002, pp. 237–52

THE PHILIPPINE DEVELOPMENT PUZZLE[1]

Arsenio M. Balisacan and Hal Hill

Introduction

The Philippines is one of the world's major development puzzles. In the immediate aftermath of the Pacific War, and despite extensive wartime destruction, it had one of the highest per capita incomes in East Asia: above South Korea and Taiwan; significantly higher than Thailand, Indonesia, and China; and below only Japan, the then Malaya, and the city states of Hong Kong and Singapore.

Among newly independent countries, its initial conditions were favourable. American rule from 1898 had been comparatively benign by colonial standards. The transition to formal independence was relatively painless, compared with some of its neighbours. Also unlike some of its neighbours, it had no really serious communal or ethnic divides. Its education standards were amongst the highest in the developing world. By dint of its colonial experience, it had privileged access to the market of the world's largest economy, a facility that continued until the expiration of the Laurel-Langley Agreement in 1974. The country's civil institutions were comparatively well developed, too. It possessed a reasonably democratic political system, albeit of the "winner-takes-all" variety. Its judiciary and legal system were quite well developed and somewhat independent. Its press was open and vigorous. Finally, while not especially resource-rich, the country possessed ample agricultural land to sustain a generation and more of rapid agricultural growth.

Yet its development outcomes have been disappointing by any yardstick. In 2000, its real per capita gross domestic product (GDP) was about the same as that of 1980 (see Figure 1). Its per capita income was overtaken by South Korea and Taiwan in the 1950s, Thailand in the 1970s, Indonesia in the 1980s, and China in the 1990s (see Figure 2). It missed out almost completely on the Asian boom from the late 1970s until the mid-1990s (see Table 1). In particular, the restructuring from the mid-1980s, which witnessed the large-scale migration of labour-intensive industries to China and the lower-wage ASEAN economies, largely bypassed the Philippines. By the 1980s and early 1990s, the Philippines became an increasingly marginal player in the region's trade and investment

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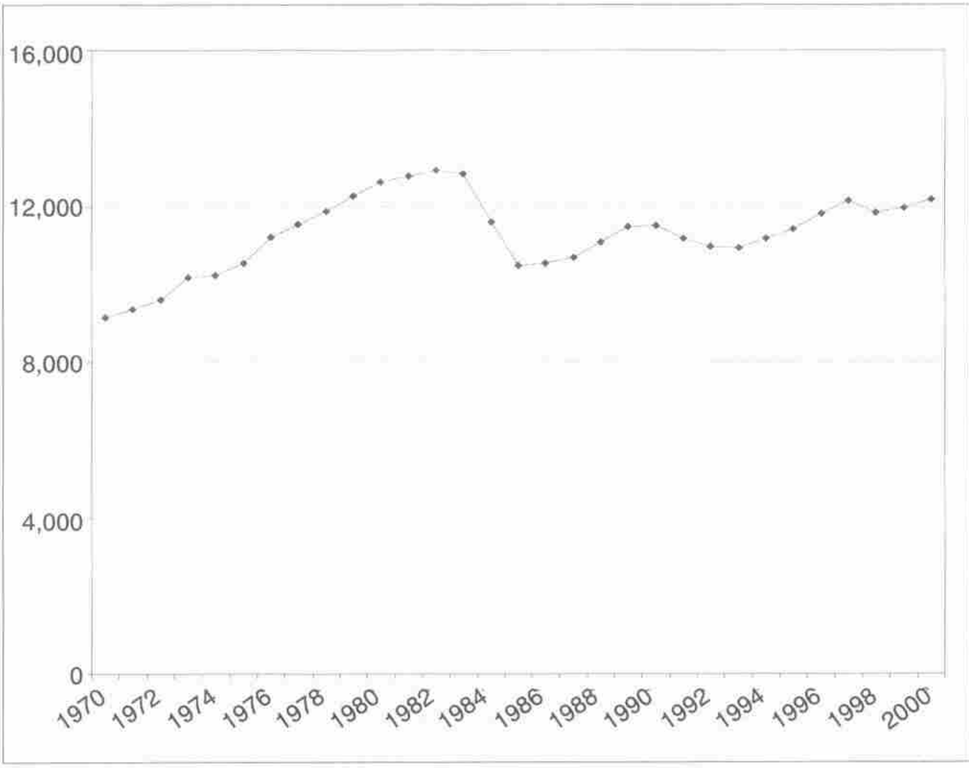
ARSENIO M. BALISACAN is Professor of Economics at the University of the Philippines, and HAL HILL is Professor of Economics at the Australian National University.

flows. In consequence, its social indicators stagnated, in marked contrast to its high-growth neighbours.

FIGURE 1
Real GDP Per Capita, 1970–2000



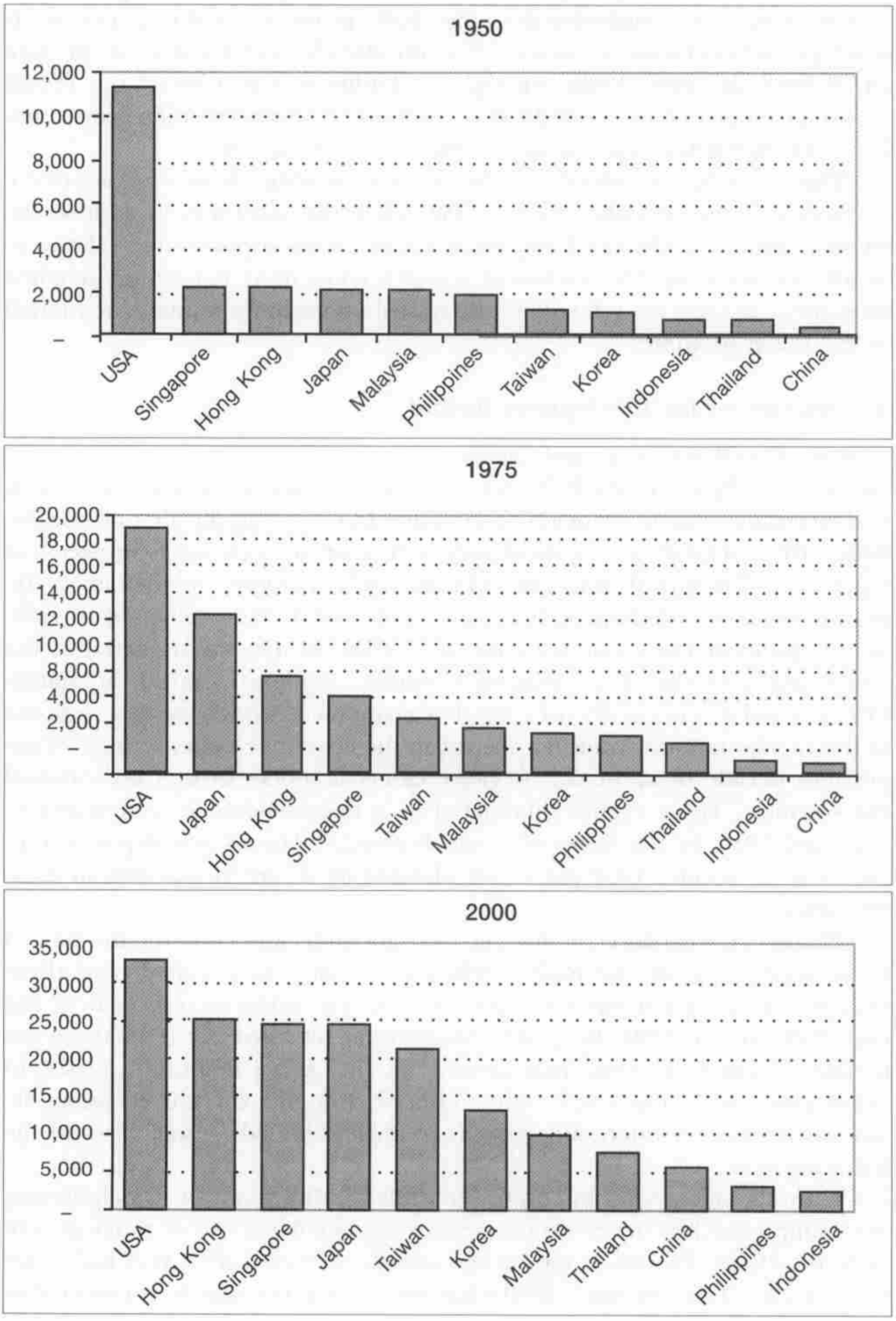
NOTE: In pesos, 1985 prices.
SOURCE: National Statistics Co-ordination Board.

TABLE 1
Southeast Asian Economic Growth, 1950–2000
(Annual average growth of GDP, %)

	1950–60	1960–70	1970–80	1980–90	1990–2000
Indonesia	4.0	3.9	7.6	6.1	4.2
Malaysia	3.6	6.5	7.8	5.3	7.0
Philippines	6.5	5.1	6.3	1.0	3.2
Singapore	n.a	8.8	8.5	6.6	7.8
Thailand	5.7	8.4	7.2	7.6	4.2

SOURCES: Lim Chong Yah, *Southeast Asia: The Long Road Ahead* (Singapore: World Scientific, 2001), p. 38; World Bank, *World Developement Report 2002* (Washington, D.C.: World Bank, 2002).

FIGURE 2
Real GDP Per Capita
(In US$, Constant prices based on 1999 PPP exchange rates)



SOURCE: World Economic Outlook database, International Monetary Fund; World Developement Indicators, World Bank.

A number of caveats need to be attached to this gloomy assessment. First, it is important not to overstate the initial conditions. Second, the country's performance looks deficient partly because of the neighbours it keeps. Thirdly, it is important to emphasize that the really pronounced divergence in its development performance occurred in the decade and a half from the late 1970s until the early 1990s. Finally, the Philippines weathered the recent economic crisis more successfully than most major Southeast Asian economies. For once, being the "East Asian exception" was good news.

This article has two objectives: the first is to provide a brief overview of the development record since around 1980, while the second is to address the larger question of why the Philippines has often underperformed relative to its obvious potential. The discussion is highly condensed. For a more detailed assessment, readers are referred to the contributions in the volume mentioned in the initial footnote.

An Overview of the Development Record

Economic Growth and Structural Change

As shown in Figure 1, the 1970s was a decade of continuous expansion, with GDP growth averaging 5.8 per cent annually.[2] In every year during that decade, both GDP and GDP per capita growth were positive, with peaks in excess of 8 per cent GDP growth twice, in 1974 and 1977. However, by the late 1970s, growth was more subdued, at less than 6 per cent. It then collapsed in 1984, as both political and economic crises set in. The former was triggered by the assassination of the then opposition leader, Benigno Aquino, at Manila International Airport in August 1983. The economic crisis was partly a response to this incident, but its roots lay deeper, in the economic policy settings of the previous decade in particular; negative external shocks further complicated the situation. These events culminated in a deep economic contraction in 1985 and 1986, in the midst of which Ferdinand Marcos was deposed after twenty years of rule.[3] GDP per capita plunged by almost 20 per cent in these two years.

Thereafter, a patchy economic recovery got underway. However, this proved to be short-lived. By the early 1990s growth had again stalled, and there were two years of contraction. This was a much milder recession than the mid-1980s, and by 1994 the growth momentum returned. By 1998, there was further dislocation, this time caused by the Asian economic crisis, in combination with a severe El Nino-induced drought. On this occasion the downturn was very brief, and growth — albeit subdued — was restored the following year.

Thus, the main point to emphasize is that, unlike many of its neighbours, the Philippines has never experienced a sustained period of rapid growth since the 1970s. The 1970s was its best decade, but even then very high rates were a rarity. Moreover, since 1980 it has never had more than four consecutive years of positive growth in GDP per capita. Finally, what growth there has been has been rather anaemic, rarely above 3 per cent per capita. Thus, with frequent years of decline, it is easy to understand why progress has been minimal.

Growth among the principal sectors of the economy has generally followed the aggregate picture, once account is taken of sector-specific factors (see Table 2). All major sectors grew quite strongly in the 1970s, the growth momentum fell sharply in the 1980s, while the pick-up in the 1990s was mixed. As would be expected, the sharpest fluctuations have occurred in industry. Agriculture grew strongly in the 1970s, driven particularly by creditable performance in food crops. However, for a number of reasons, growth petered out in the following decades, and per capita agricultural output actually fell marginally. If there has been a sectoral success story, the closest thing would be services. It is the only sector to have recorded positive per capita growth in all three decades, while growth has been positive every year, except for the two severe recession years in the mid-1980s.

Because economic growth has been generally slow, the really sharp and rapid structural transformation common in East Asia is not evident. The share of agriculture in GDP has declined steadily (see Table 3). But whereas the

TABLE 2
Annual Growth of Sectors by Decade
(In percentage)

Sector	1970s	1980s	1990s
Agriculture, Fishery & Forestry	3.70	1.54	1.49
Agriculture industry	5.79	2.44	2.00
Crops			
Livestock & Poultry			
Fisheries			
Forestry	–2.66	–6.02	–13.54
Industry	7.99	0.88	2.48
Mining & Quarrying	6.77	3.79	–1.45
Manufacturing	6.55	1.21	2.33
Construction	14.18	–0.72	2.91
Electricity, Gas and Water	13.67	5.66	5.34
Services	5.16	3.54	3.71
Transportation, Communication & Storage	7.58	3.74	4.40
Trade	5.86	3.32	3.55
Finance	8.44	3.25	5.57
Occupied Dwellings & Real Estate	1.21	2.74	2.16
Private Services	4.95	5.47	3.60
Government Services	4.61	3.41	3.63
GDP	5.79	2.01	2.78
GNP	5.88	1.81	3.57

SOURCES: National Statistics Co-ordination Board.

TABLE 3
Shares of Sectors in Current Price GDP
(In percentage)

Sector	1970	1975	1980	1985	1990	1995	2000
Agriculture, Fishery & Forestry	29.92	30.22	25.82	24.43	21.86	21.42	16.54
Agriculture industry	25.74	27.51	23.22	22.55	21.01	21.18	16.42
Crops	16.24	18.47	14.88	13.46	11.99	12.49	10.10
Livestock & Poultry	4.93	3.90	3.19	3.28	4.22	4.18	3.41
Fisheries	4.93	5.19	4.66	4.79	3.83	3.49	2.53
Forestry	4.18	2.72	2.59	1.88	0.85	0.24	0.12
Industry	31.48	35.21	38.48	35.85	34.46	32.23	30.87
Mining & Quarrying	1.79	1.57	2.05	1.98	1.54	0.88	0.62
Manufacturing	24.54	25.59	25.45	24.80	25.01	23.02	22.11
Construction	4.32	6.69	9.39	6.42	5.73	5.70	5.21
Electricity, Gas and Water	0.83	1.36	1.59	2.64	2.19	2.62	2.92
Services	38.60	34.56	35.71	39.72	43.68	46.36	52.59
Transportation, Communication & Storage	3.44	3.79	4.52	5.51	5.16	4.74	5.69
Trade	9.52	10.42	11.89	14.14	14.40	13.65	14.20
Finance	3.01	3.20	3.58	3.06	3.85	4.17	4.64
Occupied Dwellings & Real Estate	8.33	6.26	5.21	5.45	5.77	6.81	6.85
Private Services	7.52	5.48	5.45	6.70	7.55	8.92	11.41
Government Services	6.79	5.42	5.05	4.87	6.96	8.06	9.80

NOTE: Each entry is three-year average of year indicated, previous year, and suceedding year (e.g., 1970 entry = average [1969, 1970, 1971]).
SOURCE: National Statistics Co-ordination Board.

more general pattern is for the share of industry to expand, in the Philippine case it too has shrunk, albeit marginally. The consistent gainer, as implied by the growth rates, has been services. Its share of GDP has risen an extraordinary 50 per cent since 1980, and during both good times and bad. Confirming its status as an East Asian outlier, the share of manufacturing in GDP has actually shrunk since the 1970s.

The country's slow growth has also been reflected in the expenditure accounts. The share of personal consumption is high by East Asian standards. Its share rose sharply in the first half of the 1980s, predictably as a protective strategy during the economic downturn. However, once ratcheted up to over 70 per cent, it has failed to decline in response to positive growth. While the rising consumption shares have cushioned living standards during hard times, it has been achieved partly at the cost of falling investment. Since 1990, the share of investment has been around 10 percentage points below that prevailing for much of the 1970s. This, in turn, reflects the fact that the country's savings rate has been low. Levels of savings and investment were quite strong during much of the 1970s. Both, but particularly investment, declined sharply in the 1980s recession. Investment then recovered somewhat, albeit to levels much below its neighbours, whereas savings remained anaemic, at essentially OECD (Organization for Economic Co-operation and Development) levels. With such a low savings rate, and an inability to run much more than a 3–5 per cent current account deficit (anything higher would in any case be dangerous), Philippine growth has struggled to get above 6 per cent.

The Policy Framework

How have the post-Marcos political structures impinged on economy policy-making processes and outcomes? This is a very large and complex issue, but at the risk of oversimplification the following observations appear pertinent.

The Philippines is now a more democratic society, nationally and (since 1992) locally. Civil society is undoubtedly stronger. Its economy is more open and diversified. There are considerable checks and balances on government, both from inside and outside. Once a reform is passed into law, there is a reasonable prospect that it will be durable. But there remain notable weak points, putting aside the immediate challenge of bedding down the legitimacy of the young Arroyo administration. Three in particular stand out.

First, the political system is highly personalistic. It can produce competent or barely competent presidents (for example, Ramos and Estrada respectively). This can happen in any country, of course. The particular problem in the Philippines is that regime changes have major consequences since, with its U.S. style of government, they percolate right through the system. Unlike most of its neighbours, where the civil service remains largely intact when regimes change, in the Philippines regime changes affect the top civil service layer, at the level of secretary, the next (under secretary), quite often the third tier (assistant secretary), and sometimes even the fourth (director level).

This has two immediate implications. One is that it reduces the likelihood of policy consistency. If much of the top echelons of a department turn over every six years, there is a distinct possibility of change of direction. Investors will calculate that they have policy certainty for no more than six years, and in practice much less, owing to settling-in and "lame duck" periods, and turnover within administrations. Another implication is that below these senior echelons, there simply is no pool of high-level talent to anchor policy consistency, since poor salaries and a lack of career structure constitute major deterrents. A more general consequence is that, unlike a system of career public service, it is more difficult to deeply entrench pro-reform lobbies within the bureaucracy.

A second challenge is that it is often difficult to get reforms through the system, because there are so many points at which progress can be stymied. The bureaucracy, the legislature (both national and regional), the palace itself, and the judiciary can all be employed by lobbyists determined to resist reforms. Moreover, different pressure points may be important in different administrations. Under Estrada, it was widely perceived to be the President himself, whose so-called "midnight Cabinet" of "drinking buddies" could overturn decisions taken by the "daytime Cabinet". Ramos had problems with the legislature, while Aquino's Cabinets became well known for its policy rifts, particularly in their early years.

A third challenge, systemic in nature, concerns the extent to which deeply entrenched and high levels of inequality impede reform. The Philippines has never experienced a Taiwan-style land reform nor, unlike Malaysia and Indonesia, has there been an administration determined to cater to a poor rural constituency. Thus, powerful land-owning groups and business conglomerates have been a continuing feature of the country's history. This does not of course preclude the possibility of effective reformist administrations, as evidenced by Ramos, which by accelerating economic growth can certainly help the poor. But, it is contended, the political system is such that distributionalist objectives will always be difficult to achieve, and their reforms may be overturned subsequently.

Macro and International Dimensions

If post-independent Philippine history was characterized by stop-go economic policy, macroeconomic and trade policy were surely at the heart of the problem. It is, therefore, not surprising that they have been central to the reform efforts since the mid-1980s. This is one area where the achievements have been significant; they have arguably been the key contributors to the improved development outcomes.[4]

Philippine macroeconomic outcomes have traditionally lagged its high-growth East Asian neighbours, though by general developing country standards they have not been disastrous. The bases of the Philippines' macroeconomic problems are of course well known: chronic budget deficits, being in turn monetized by a politicized central bank, which was also attempting to run a quasi-fixed exchange rate regime. The results were moderately high inflation, a black market foreign exchange rate, and periodic balance of payments crises.

In the case of *exchange rate and monetary policy*, the reform momentum got underway in the late 1980s. The international capital account was progressively opened, culminating in full peso convertibility in 1992, one of the first major economic policy initiatives of the incoming Ramos administration. As part of the reform, a new institution was created in 1993, the Bangko Sentral ng Pilipinas (BSB), and the debts from the old central bank were taken off its books. The new regime emphasized inflation targeting, and a floating exchange rate within a managed band. The results were immediately obvious: inflation remained under control throughout the 1990s, in the range of 6–9 per cent. Perhaps more importantly, the peso convertibility removed an endemic source of corruption, both petty and grand, and was fundamental in instigating a more outward-looking mentality among investors.

Initially, in the mid-1990s, the authorities basically attempted to emulate its neighbours, and run monetary policy with a quasi-fixed exchange rate in the context of an open capital account. Here the familiar Mundell-Flemming problem began to surface, albeit in milder form owing to the much smaller volume of capital flows as compared with its neighbours.[5] For a fortunately short period, in fact, Philippine conditions and policy settings were quite similar to those of the soon-to-be crisis economies. The real exchange rate began to appreciate mildly, threatening export competitiveness and also complicating the trade liberalization process then underway. Capital flows were increasingly directed towards non-tradable activities. Domestic banks became significant international borrowers, a trend hastened by the gap between domestic and international interest rates, and the perception that the authorities would hold the nominal rate more or less constant.

This period was short-lived, as the crisis began to impact by August 1997. The BSB's reaction, like its counterparts elsewhere, was to defend the peso via higher interest rates. This quickly proved futile, and the peso then fell sharply, approximately halving its rate against the U.S. dollar in the next six months. But this was a most unusual balance of payments crisis by Philippine standards.[6] First, the trigger was mainly external, that is, the contagion from Thailand. Second, it did not lead to a general financial crisis, as occurred in Thailand, Malaysia, and Indonesia. Finally, growth was only mildly interrupted.

There has also been major progress since the 1980s with *fiscal policy*. Successive governments have almost always run fiscal deficits. Although there has rarely been a complete loss of fiscal discipline, these deficits have invariably peaked around election time. The years 1969 and 1985 stand out during the long Marcos period. These deficits have typically resulted in difficult fiscal adjustments, and often a sharp peso depreciation.

The most painful adjustment period occurred in the first half of the 1980s. Real per capita expenditure almost halved. There were very large cuts in infrastructure expenditure, which arguably laid the basis for later problems.

And debt service rose sharply: at one stage interest and debt payments absorbed more than 40 per cent of the budget. From the late 1980s, significant progress occurred. The ratio of government revenue to GDP almost doubled from the recession years 1983–85 (9.6 per cent) to 1997 (17 per cent), by which time the country's tax effort was nearly comparable to that of Indonesia and Thailand. Faster growth, a simplification of tax scales and more vigorous collection procedures all contributed. The resumption of growth, combined with some workouts, also meant that the debt service burden was progressively lightened over this period. At the same time, the fiscal deficit, narrowly defined, peaked at 8.5 per cent of GDP in 1986. The position then improved steadily, and for three years — 1994–96 — a slim surplus was recorded. With the onset of the crisis, there was however a quick return to deficits.[7]

The Philippines now has a President who in her earlier academic writings had stressed the importance of sound fiscal management. One has to hope that President Arroyo and Professor Arroyo are one and the same person.

The Philippines has had a history of perverse *trade policy* interventions, which have been extensively documented in earlier studies.[8] Here, too, there has been significant progress since the late 1980s, to the point where openness appears to be quite deeply rooted in the polity and community at large, and the country now has one of the more open trade policy regimes. Average rates of protection have fallen, the dispersion in these rates is lower, and there is less reliance on non-tariff barriers (NTBs). Nevertheless, the country is a much less significant international commercial player than most of its neighbours, as a result of past barriers to trade and investment, and an unwelcoming business environment.

Social and Distributional Issues

Most Philippine social indicators reflect general economic conditions, with stagnation and decline in the 1980s and some hopeful signs in the 1990s. Overall, the picture is mixed, with some very worrying problems alongside significant improvements. This is of course a case of complex, two-way causality, with social conditions being determined by, but also shaping, economic progress.

Demographically, the Philippines is an East Asian outlier. Its population, 75.3 million persons in 2000, has doubled since 1970. Most projections suggest that it will at least double again before stabilizing. In education achievement, the Philippines rates above most countries with similar per capita incomes, with the additional advantage of widespread English-language fluency. It thus has an edge in activities which require middle-level human capital inputs. Reflecting early commitments to public education, about 95 per cent of the population has at least "simple" literacy skills, while about 84 per cent may be said to be functionally literate. Primary school participation is at least 95 per cent of the relevant age group, falling to about 64 per cent for secondary schools. There is no gender bias, and, in fact, female participation is slightly ahead of males.

However, the country's lead is slipping, as these rates stagnate, and other countries catch up. Moreover, in international quality comparisons it rates poorly.

With rapid population growth and a large backlog, employment provision is a chronic problem in the Philippines. The labour force is growing by about 2.8 per cent each year, equivalent now to about 800,000 new job entrants. Rising female labour force participation is also a factor. Unemployment is currently about 10 per cent, with underemployment variously estimated at around 20 per cent. The inevitable consequence is of course large numbers seeking employment abroad. OFWs (overseas Filipino workers), as they are known in-country, have been growing at a phenomenal pace, almost quadrupling from 1980 (about 215,000 persons) to 1999 (around 837,000).

Poverty and inequality continue to be serious problems in the Philippines. But there has been progress since the depths of the mid-1980s crisis. The incidence of poverty fell sharply, by about one-third (41 per cent to 25 per cent), from 1985 to 1997. Moreover, poverty declined the fastest in the sub-periods of higher growth, 1985–88 and 1994–97. The poverty picture of course varies significantly among sectors, regions, and households. Poverty is higher in rural areas and among agricultural workers. About three-quarters of the poor are in agriculture (a similar ratio to that of the 1960s), and so agricultural growth is especially beneficial for the poor. Among regions, Luzon is generally better off, and Metro Manila always records the lowest poverty incidence. Consistently poor regions include Eastern Visayas (about fourteen times the incidence of Manila) and Bicol.

Reverting to the national picture, the distribution of wealth in the Philippines is more unequal than most of its neighbours. It inherited an unequal land distribution from the Spanish *haciendas* of the colonial period, and this seems to have been translated into the modern commercial-industrial sector, and arguably political structures. There have been no major ameliorating factors, either in the form of agrarian reform (as in Taiwan) or a national leadership beholden to an initially poor and rural constituency (as in Malaysia). The question then is whether growth is a sufficient prerequisite for sustained poverty reduction (it is clearly a necessary one). And if distributional policies are pursued, which ones will also simultaneously achieve growth objectives?

There are many other complex social and distributional issues. For example, regional policy and development are important in the Philippines. It is the world's second largest archipelagic nation, and it thus features considerable spatial diversity. Also, beginning in 1991 a significant decentralization programme was initiated, which transferred administrative and fiscal functions to the regions. A long-standing insurrection in Mindanao, the Philippines Muslim south, continues to be a major and unresolved problem, with national and broader Southeast Asian implications. In addition, environmental issues have hardly began to be addressed. Almost all environmental indicators point to a deteriorating situation. Unlike its high-growth neighbours, where a similar worsening may be said to have compensated for rising material prosperity, the Philippines has missed out on both counts.

Towards an Explanation of Slow Growth

We now return to the question of what explains the country's indifferent long-term growth record? The answers are clearly complex, inter-related, and not easily amenable to quantitative analysis. No simple or single theory suffices. There is a need to develop a coherent story relating outcomes to an array of external and internal factors, some narrowly economic, others broader and embedded in political, historical, and institutional factors.

Various schools of thought approach the question from different perspectives, and hence provide different answers. Economists focus on conventional policy weaknesses, for example in trade and macroeconomic policy. Political scientists highlight flaws in the structures of government, both during and after the Marcos period. Sociologists draw attention to the power of vested interests, rooted in the highly unequal colonial past. Others simply point to extraordinary misfortune. Moreover, these various hypotheses are not necessarily mutually exclusive.

"Conventional" Growth Explanations

There is a large literature that attempts to explain international variations in long-term rates of economic growth with reference to a range of policy and country endowment factors.[9] A large set of variables are included, but the core typically consists of proxies which measure macroeconomic outcomes, trade policy, human capital, institutional quality, natural resource endowments, proximity to large economies, and initial levels of per capita income (to capture the "catch-up phenomenon"). Many additional variables could be added to this list.

We are unaware of any systematic testing of such a relationship against Philippine data. Such a framework might go some way in explaining the country's inferior performance. For example, it has been somewhat more inward-looking than most high-growth economies, and macroeconomic outcomes have not been as good. But such a methodology is unlikely to explain all or even a major part of the divergence. The Philippine macroeconomic record (for example, its inflation rate) has not matched that of Singapore, Malaysia, and Thailand, but it has been broadly similar to that of South Korea and Indonesia for much of the period since 1970. Similarly, its trade regime has not been as open as Singapore, Hong Kong, and Malaysia, but also has not differed significantly from Indonesia and even Thailand over this period. Its stock of human capital has been better than almost all the lower income East Asian economies, while institutional quality has not been markedly inferior. Other variables, such as proximity to major economies, length of coastline, the incidence of political disturbances, and ethno-linguistic fragmentation, are either irrelevant or would make little difference to the story.

Moreover, this growth determinants framework is useful particularly in explaining long-term growth differentials, and is therefore less relevant in coming to grips with the episodic nature of Philippine growth. That is, until about 1980, its growth was slower but not markedly inferior to most of its neighbours. It was the "lost decade" of the 1980s that really separated it from East Asia.

Thus, we get some way in explaining the country's slower growth using this methodology. Just how much, precisely, is a separate study in itself, and beyond the scope of this article. But we can assert with confidence that a considerable part of the story remains unexplained.

Bad Luck

It is often asserted that, at critical junctures in Philippine history, there has been an awful lot of bad luck, or at least unfortunate timing.

For example, from the mid-1970s, the Marcos administration embarked on a strategy of aggressive overseas borrowing. This was partly to boost its own fortunes, but it needs to be remembered that the international financial institutions (IFIs) were concerned about the rapid build-up of petro dollars in the wake of successive oil shocks, and were concerned that they be recycled. Thus, for very different reasons, the objectives of the IFIs and President Marcos coincided. However, shortly after the borrowing commenced, the country experienced a large, negative terms of trade shock. Sugar prices declined sharply in 1974–75 and coconuts in 1979–80, while oil prices rose again in 1978–79. Then in the early 1980s, with a much increased external debt, world interest rates rose substantially.

A second instance is that, from 1984, the country experienced a prolonged political and financial crisis, and this occurred just as the massive East Asian restructuring got underway. The resultant regional boom in trade and investment almost completely bypassed the Philippines. Moreover, from the late 1980s, the commercial environment was soured by a series of adverse events: several coup attempts, a terrible earthquake (Pinatubo in 1991), chronic and severe power shortages, and the removal of the U.S. bases. Each of these was large enough to register one-off several points of GDP growth.

A third example occurred in the 1990s. Just as the economy appeared set for a sustained period of progress during the Ramos presidency, in 1997 the combination of the Asian economic crisis and a severe El Nino-induced drought nipped this growth in the bud.

Finally, owing to protracted instability, the Philippines has never been able to exploit the opportunities presented by its frontier region, Mindanao. This has not only resulted in reduced agricultural growth but also tarnished the international reputation of the country.

The question is how important these factors were, and how much of the misfortune was really endogenous? Other countries have survived sharp declines in their terms of trade, most notably Thailand in the 1970s, and Indonesia in the mid-1980s. For well-managed, prudent economies, these constitute a temporary setback, not a crisis. Much of the problem in the Philippines was not the borrowing strategy *per se*, but the uneconomic projects for which the funds were used. Similarly, natural disasters are quite common in the region. Taiwan, for example, has had many similar experiences. Finally, one could plausibly argue that, while recognizing the deep historical complexities, Mindanao was essentially a home-grown problem. Other countries have been able to manage serious regional insurrections. Thailand and Malaysia immediately come to mind.

Thus, it is difficult to sustain the case that these instances of bad luck and misfortune are the key explanators. They have certainly been very costly, and have often occurred at inopportune moments. But by themselves they cannot explain chronic underperformance.

Institutional/Political Barriers to Good Policy

It is sometimes argued that good economic policy has been frustrated by particular social structures or political institutions. Here, too, there are several strands to the argument, not all of them consistent. It might be tempting to simply assign the ills of the country to the twenty-year rule of Marcos. Obviously, personalities do matter, but can one advance the argument in a somewhat more analytical manner?

One strand of the argument asserts that highly unequal social structures — the "oligarchs" — have infected the political process to the point where serious policy reform, especially that which challenges this group's vested interests, is impossible. While it is true that the distribution of wealth in the Philippines is more unequal than its neighbours, it does not necessarily follow that growth has to be slower. The record of the Ramos administration, in fact, constitutes a partial counter to this hypothesis. That is, there were quite significant reforms, in trade policy, telecommunications, and inter-island shipping. One might quibble about the scope and pace of these reforms, but they do at least underline the fact that the socio-political system is not so ossified as to be incapable of reform.

In the post-Marcos period, as noted above, it is argued that a different type of political obstacle has emerged. This is the assertion that the political system is now no longer able to provide longer term economic policy predictability. In consequence, investors do not think much beyond a six-year time horizon, and probably even less.

Summing Up

As is usually the case in the search for explanations of complex phenomena, we are left with elements of a case, but no grand and all-encompassing answer. All the above factors are relevant, and constitute part of the story. The Philippines failed to grow as quickly as several of its neighbours in the 1960s and 1970s for the reasons adumbrated above. In the second decade of the Marcos administration, the development strategy changed to one of adventurous overseas borrowing. But this came unstuck owing to a combination of reckless investments, ever-increasing cronyism and corruption, increasing community disaffection (especially in the wake of the 1983 Aquino assassination), and external misfortune. The culmination was a serious political impasse and a deep and prolonged economic crisis, which set the country back more than a decade, and from which recovery was slow and painful.

Conclusion

In 2001, looking backwards and forwards, it would be tempting to conclude that the Philippines is at the crossroads, were it not for the fact that such a characterization has a sense of *deja vu*. The past two decades have achieved very little, but the past decade has demonstrated that the Philippines is not inherently a "non-developmental" state, as some have suggested.

Extrapolating from the past to the future, it might be difficult to be optimistic about Philippine development prospects. There have been episodes of growth, but they were short-lived and the growth has rarely matched the levels observed elsewhere in East Asia.

The key question is whether the political system can deliver the sort of substantial reforms of the 1990s in a durable and sustained fashion. The late Aquino and Ramos administrations demonstrated that sound economic policy does deliver results, and seemed to suggest a decisive break with the past. But by 2000, it appeared again as though these achievements might have constituted a temporary aberration, as some of the reform progress was undone by a combination of external circumstances and domestic incompetence.

An optimistic scenario would be that the Arroyo administration would return to something like that of the Ramos period, which featured sensible, pragmatic reform, and a reasonably secure and predictable policy and investment environment. With her academic and bureaucratic background, President Arroyo obviously understands the importance of sound economic management. She also has the prospect of a nine-year presidency, to pursue a coherent economic strategy. Whether this expertise translates into a decade of solid economic development remains to be seen. A decade of 5–6 per cent economic growth would do much to overcome the deeply entrenched problems of poverty and social deprivation, and it would consolidate a pro-reform constituency. Conversely, a return to populist and corrupt politics, like those of Estrada, would undo the gains of the 1990s and consign the country to a dismal future.

NOTES

1. This article draws on the authors' introductory chapter to their co-edited volume, *The Philippine Economy*, to be published by Oxford University Press, New York, in late 2002. The authors wish to acknowledge in particular the work of the contributors to this volume, on whose work they have drawn freely.
2. There is a considerable literature on Philippine economic development in the 1970s, with the most comprehensive being ILO (International Labour Office), *Sharing in Development: A Program of Employment, Equity and Growth for the Philippines* (Geneva: International Labour Office, 1974).
3. For detailed analyses of the 1980s crisis, see R. S. Dohner, P. Intal Jr., "The Marcos Legacy: Economic Policy and Foreign Debt in the Philippines", in *Developing Country Debt and Economic Performance*, edited by J. D. Sachs and S. M. Collins, vol. 3 (Chicago: University of Chicago Press, for the NBER, 1989), pp. 371–614; E. M. Remolona, M. Mangahas, and F. Pante, Jr., "Foreign Debt, Balance of Payments, and the Economic Crisis of the Philippines in 1983–84", *World Development* 14, no. 8 (1986): 993–1018.
4. World Bank, *Philippines — Growth with Equity: The Remaining Agenda* (Washington, D.C.: World Bank, 2000).
5. M. Rodlauer et al., *Philippines: Toward Sustainable and Rapid Growth. Recent Developments and the Agenda Ahead*, Occasional Paper 187 (Washington, D.C.: International Monetary Fund, 2000).
6. M. Noland, "The Philippines in the Asian Financial Crisis: How the Sick Man Avoided Pneumonia", *Asian Survey* 40, no. 3 (2000): 401–12.
7. Note, however, that the official budget position is highly sensitive to definitions. These deficits have either been quite modest or veering towards unsustainably large levels depending on whether central government or consolidated government figures are used. The latter, of course, is the relevant indicator and deficits in excess of 5 per cent of GDP were the norm in the 1980s, and resurfaced in the late 1990s. The years 1994–96 were still in surplus according to this broader definitions, however.
8. See for example, E. M. Medalla, G. R. Tecson, R. M. Bautista, J. H. Power and Associates (1995/96), *Philippine Trade and Industrial Policies: Catching Up With Asia's Tigers*, vols. I and II, Philippine Institute for Development Studies, Makati, and several earlier volumes.
9. See, for example, Chapter 2 of ADB (Asian Development Bank), *Emerging Asia: Changes and Challenges* (Manila: Asian Development Bank, 1997).