

Alonso i Terme, Rosa

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## Why has Latin America sped up ahead of the Philippines in economic and political reform?

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## UP School of Economics Discussion Papers

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### **Why Has Latin America Sped Up Ahead of the Philippines in Economic and Political Reform?**

by

Rosa Alonso I Terme

Assistant Professor, UP School of Economics

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# **Why Has Latin America Sped Up Ahead of the Philippines in Economic and Political Reform?\***

**Rosa Alonso I Terme**

## **Abstract**

This paper compares trends in key economic, political and social development outcomes in the Philippines with those of Latin America, particularly since the 1990s. To do so, it uses standard indicators of development, including measures of institutional quality and good governance. The paper finds that Latin America is not only at a higher level of development, but has also made faster progress in most areas than the Philippines. This is especially the case as regards GDP per capita, poverty, education, health, infrastructure, social protection, right to life and security of the person and corruption. The Philippines, however, performs significantly better as regards gender and race and in some “niche” areas of ICT, including high-tech exports, while posting slightly higher ratings in government effectiveness. Both regions do well in the areas of macro-economic management and financial sector development. Overall performance as regards the quality of democracy is also roughly comparable. The paper argues that key policy drivers of the divergence include Latin America’s: a) higher and better public spending; b) greater transparency and integrity in both the public and private sectors; and c) freer and more competitive markets.

**Keywords:** public economics, development economics, political economy, economic systems.

**Journal of Economic Literature Classification Codes:** H11, O11, P16, P51

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**We must make haste. Too many people are suffering.**

***Populorum Progressio* n. 29. Papal Encyclical of Paul VI (1967)**

## **Introduction**

Both policy-makers and the public at large have repeatedly expressed disappointment at the meager rate of poverty reduction that has taken place in the Philippines over the past few decades. The disappointment has been even greater when poverty has failed to come down at times of strong macro-economic performance and fast GDP growth as in 2011-2013. Although progress is satisfactory in some areas, improvement in overall development indicators has lagged that of many other developing countries. This is the case in critical areas such as income per capita, poverty, inequality, transport, access to (and price of) water and electricity, sanitation, education and health and, until 2010, corruption, and overall governance. These largely disappointing results have typically been contrasted with the better performance of other middle –and even low—income countries.

At the same time, the Philippines performs quite well in a number of areas which are of great relevance to the well-being of its population, such as gender and racial discrimination. These areas, in which the Philippines has lessons to share with many developing –and developed—countries, are not sufficiently highlighted when assessing overall progress and wellbeing.

Recent research on development outcomes and its drivers in the Philippines has tended to focus on comparisons with East Asian countries. Latin America, however, is as useful a comparator for the Philippines. Historically, Latin America shares with the Philippines its Spanish and American colonial heritage. More recently, both regions have been characterized by unequal patterns of wealth and income distribution, intensive trade and other economic and political linkages with the United States and a relatively long-standing history of democracy. Despite these commonalities, no recent comparison of the development outcomes in both regions and their drivers together with identification of potential areas for mutual learning has been elaborated. This paper attempts to fill the gap.<sup>1</sup>

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<sup>1</sup> Some comparisons with Latin America have emphasized shortcomings of both regions (Nelson, 2007). Latin America, however, is by far the most advanced region in the developing world (well ahead of East Asia). This paper will focus on drawing lessons from Latin America's accomplishments for the Philippines.

In addition to providing a comparative picture of development outcomes in both regions, the paper also aims to shed some light on the drivers of divergent outcomes. Although some lessons from the Philippines for Latin America will be pointed out, the focus of the analysis lies in drawing lessons for the Philippines.<sup>2</sup> The paper also covers performance in often under-emphasized areas of well-being such as gender and racial discrimination, democratic representation, violence and crime.

The approach to and definition of development used will thus be multi-dimensional. It will build on Amartya Sen's idea of freedom as encompassing the capabilities that allow a person to lead "the kind of life he or she has a reason to value." (Sen, 1999) As such, the paper will address: a) political freedoms; b) economic facilities; c) social opportunities; d) transparency guarantees; and e) protective security. Sen's framework will be complemented with Christian Ethics to provide positive content to the kind of (individual and social) life one has a reason to value.<sup>3</sup> In this way, the framework will be extended to a set of positive values on the "good society" going beyond negative freedoms and human capabilities. These positive values are the pursuit of the common good with a preference for the poor with freedom, justice and mercy as guiding principles.

Where aggregate measures for the Latin America region are available, the Philippines will be compared to the Latin American average. When a regional average is not available, the Philippines will be compared to Argentina, Brazil, Chile, Colombia, Guatemala, Mexico and Peru. These countries have been selected because they constitute a roughly representative sample group for the region, including more advanced upper-middle income countries, such as Argentina, Brazil and Mexico as well as less advanced middle income countries such as Colombia, Peru and Guatemala.

The time period covered will vary issue-by-issue depending on data availability. For most dimensions, it will cover from either 1960 or 1980 until the present. For some areas, however, only data after 1990 or even the year 2000 is available. Quantitative as well as qualitative information will be used as needed and available. Unless otherwise mentioned, data is gathered from the World Development Indicators of the World Bank's Database.

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<sup>2</sup> The significantly superior performance of the Philippines in the areas of race and gender is largely driven by differences in pre-Hispanic culture. Unlike in policy areas --where lessons from one region for the other are more straightforward--, how to address this culturally driven gap in Latin America is a more complex issue which needs to be addressed from within the region and lies beyond the scope of this paper.

<sup>3</sup> Sen leaves that question largely open while ruling out some types of lives which in his view --largely because of not entailing sufficient freedom--do not meet the requirements of "a life one has a reason to value." He does not, however, explicitly propose a positive definition of what a kind of life one has a reason to value is or what its objectives are, presumably because maximizing freedom permits people to live a great variety of "lives" all of which "people have a reason to value."

The paper also outlines areas for future research –potentially in complementary papers--, particularly regarding issues where the most useful policy lessons for both parties can be learned.

## **POLITICAL DEVELOPMENT**

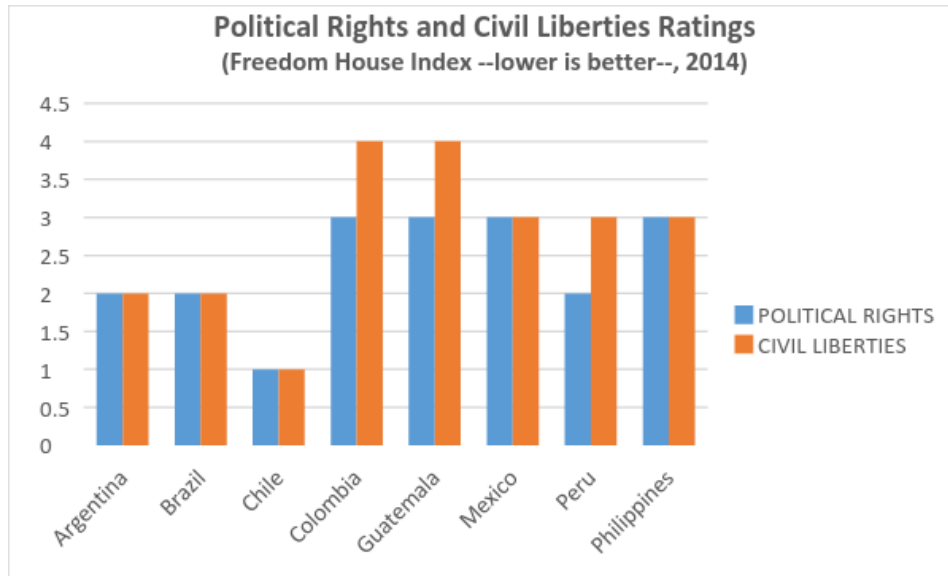
**Political development will be assessed using indicators in three essential areas: a) freedoms; b) governance; and c) representativeness.** These three areas reflect the core intrinsic values of freedom and justice, but they also include important instrumental values such as efficiency (e.g. as in government effectiveness).<sup>4</sup> The first two dimensions (freedom and governance) are well-researched and aggregate quantitative indicators exist to assess them. For the third dimension (representativeness), a more disaggregate assessment will be carried out since there are no aggregate indicators that take account racial, gender and income diversity in the representativeness of government as a whole.

**As regards political freedoms, the Philippines is rated somewhat below the Latin American average.**

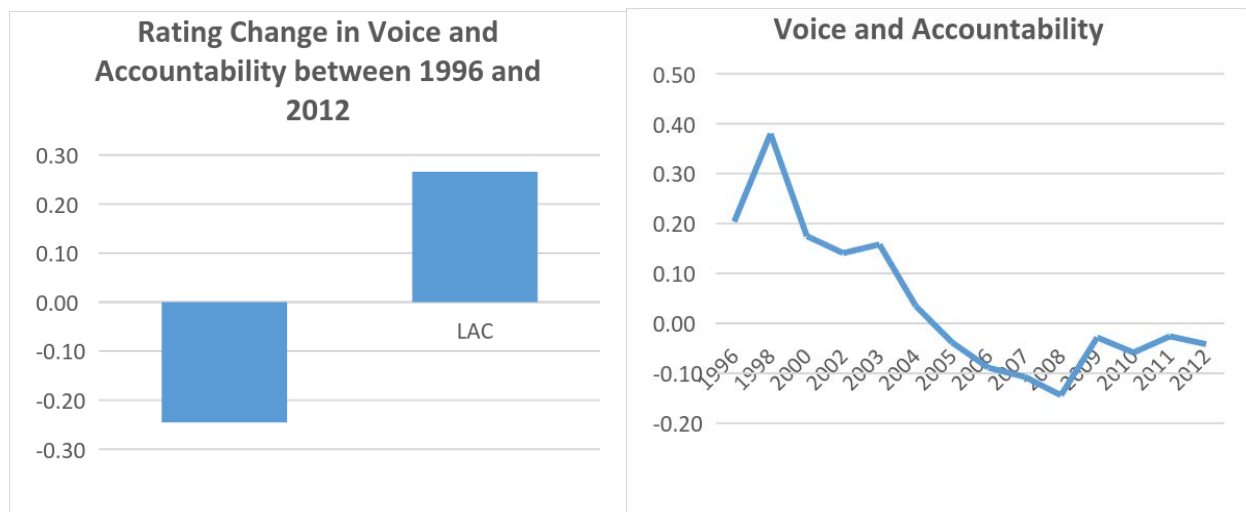
The Freedom House Index on political rights and civil liberties rates the Philippines at 3 (with 7 being the worst and 1 the best ratings). This places the country below the Latin American comparator group median, at the same level as Mexico and above Guatemala and Colombia as far as civil liberties are concerned (though at their par on political rights) and below Argentina, Brazil, Peru and Chile. Similarly, the World Justice Project rates ‘fundamental rights’ in Latin America ahead of the Philippines (with respective ratings of 64 versus 57, with a higher rating being better). The areas where the Philippines has the largest gap with Latin America are the right to life and security of the person (39 versus 66), freedom from arbitrary intermission with privacy, due process of law and rights of the accused (40 versus 50) and effective guarantee of freedom of belief and religion (64 versus 74). The only sub-area in which the Philippines out-rates Latin America as far as fundamental rights are concerned is freedom of opinion and assembly (77 versus 73) and freedom of opinion and expression (69 versus 67).

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<sup>4</sup> Economic and social justice is a different –though partly related—matter which will be addressed in the relevant subsequent sections of this paper.

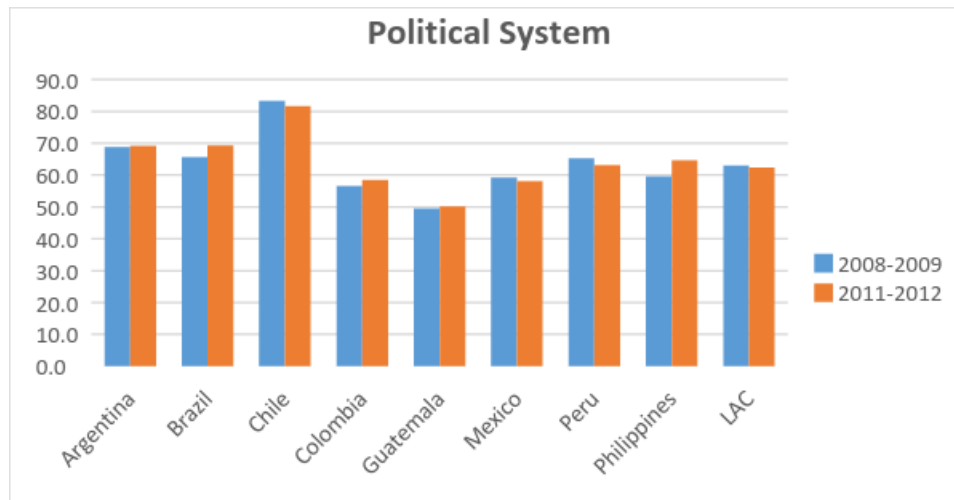


**Kaufmann and Kraay's related voice and accountability indicator also places the Philippines well below the Latin American average.** At a -0.04 score (in a -2.5 to 2.5 spectrum with 2.5 being the best and -2.5 the worst ratings), the Philippines only fares better than Guatemala and Colombia. Of particular concern is the fact that, while performance in this important dimension of political development since 1996 in Latin America has improved, in the Philippines it has significantly deteriorated.



**In 2011-2012, however, the Philippines rated slightly above the Latin American average in the Global Quality of Democracy ratings as regards its political system.** While in 2008-2009 it was slightly below the Latin American average, it had caught up to just above it by the time of the last observation available. The fact that the Philippines does better in this index than in the previous two is likely due to

the fact that, in addition to Freedom House's political rights and civil liberties indices and corruption, it includes areas where the Philippines does relatively well, such as gender gaps and political stability.



**As regards governance, the Philippines has improved since 1996 and it is rated at a level comparable to Latin America's in government effectiveness, though it still lags regarding corruption.** The two dimensions of governance considered here are government effectiveness and corruption as measured by the Kaufman and Kraay index. Government effectiveness "reflects perceptions of the quality of public services, the quality of the civil service and the degree of its independence from political pressures, the quality of policy formulation and implementation, and the credibility of the government's commitment to such policies." Government effectiveness in the Philippines is perceived to have improved since 1996. It is now rated at 0.08, up from -0.18 in 1996 and slightly above the Latin American country comparator group average of 0.05.

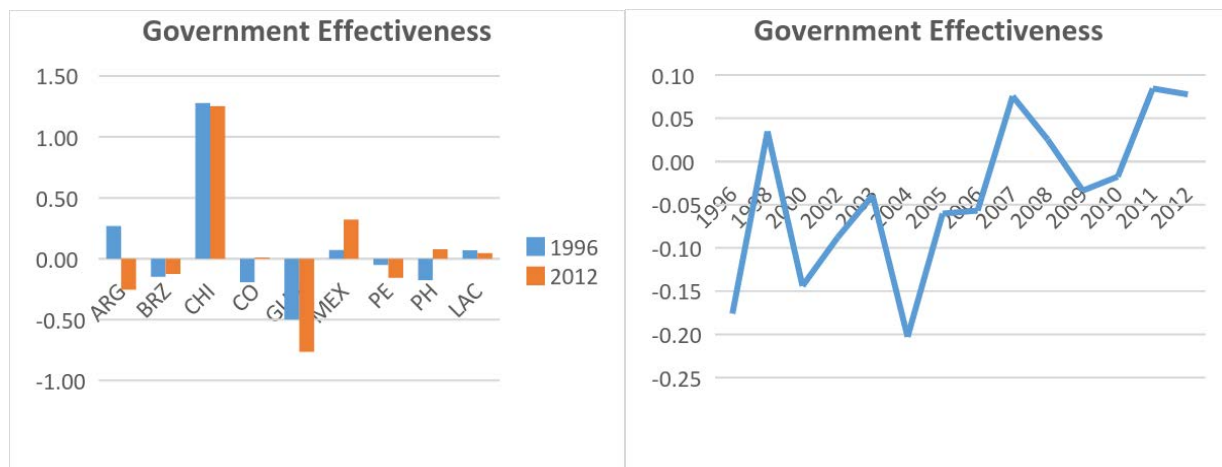
**Contrary to popular perceptions in the Philippines, therefore, the government's effectiveness in carrying out its mission is not weak.**<sup>5</sup> On the contrary, if one considers that Latin America has a significantly higher income per capita, human capital and overall level of development level than the Philippines, one ought to consider its government effectiveness rating quite satisfactory. This is consistent with other research, such as the finding that government efficiency in the education and

<sup>5</sup> Although the Kaufman and Kraay index is a perception index, it includes a wide range of perceptions from actors in the private sector, civil society and international organizations in addition to the general public.



health sectors is comparable to or even above the level of other East Asian countries and it is the low level of government spending that is to blame for poor development results (World Bank, 2011).<sup>6</sup>

**The result is also particularly satisfactory if one takes into account the fact that perceptions of “the quality of public services” are impacted by the level of resources devoted to these services.** Therefore, given the dearth of resources available for public services in the Philippines, the fact that the “government effectiveness” rating is even above the level of a region which devotes a much higher level of resources to these services speaks well of government capacity in the Philippines. This finding is also consistent with the view that, in the area of governance, the shortcomings of the Philippines are not in the area of government capacity or bureaucratic efficiency, but rather private versus public goods provision and state capture/political corruption.<sup>7</sup> This view is borne out by the following indicator.

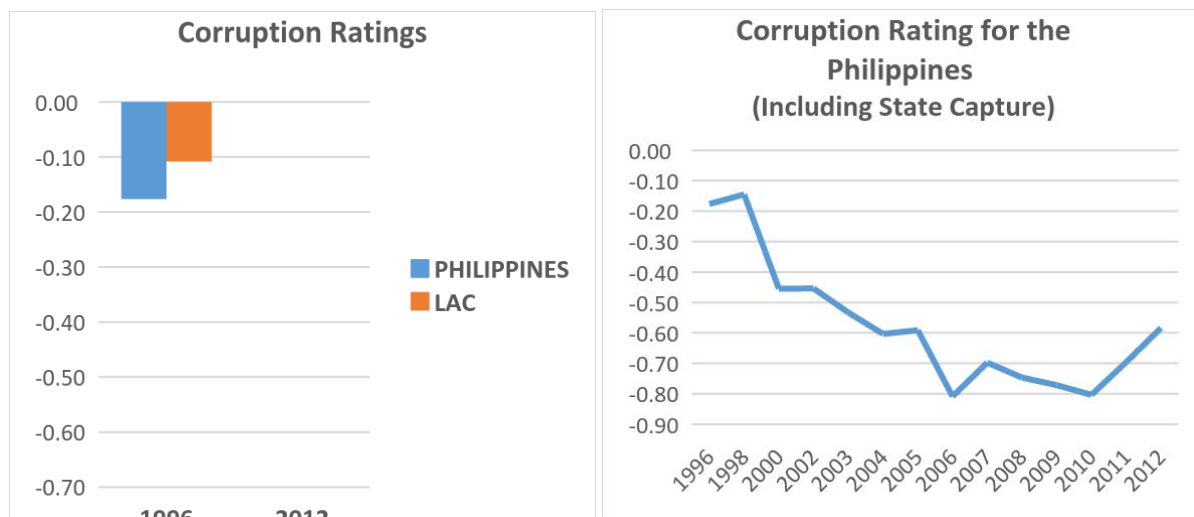


**As regards corruption (including state capture), the Philippines does quite poorly and is significantly below the Latin American average.** The index defines corruption as “perceptions of the extent to which public power is exercised for private gain, including both petty and grand forms of corruption, as well as “capture” of the state by elites and private interests.” In this dimension of governance, the country’s rating and ranking is low and it has worsened significantly since 1996, although it began to improve again in 2010. Between 1996 and 2012, the ranking of the Philippines went from number 55 to number 93 (in a –granted-- expanded set of countries) and its rating worsened from -0.18 to -0.58. This result is consistent with the largely held view of the government’s failure to faithfully represent the common

<sup>6</sup> The study uses data envelopment analysis to assess the input-output efficiency of education spending in delivering education outcomes and of health spending in delivering health outcomes. The study does find, however, that transport spending is inefficient in achieving outcomes (likely due to politicization and corruption).

<sup>7</sup> Another issue affecting government efficiency is excessive and overly-complex regulation.

good and its distortion toward patronage-style private goods programs and the interests of the elites aside from corruption narrowly defined.<sup>8</sup>



**Representativeness is an essential yet largely overlooked area of political development.** If a government is not representative of all its citizens, it is unlikely to reflect the common good and the wellbeing of those who are under-represented will not be appropriately taken into account. This will result in unbalanced institutions elaborating unbalanced policies to the detriment of the under-represented and, ultimately, of the common good. It will also violate basic justice, the intrinsic equality, dignity and political freedom of every human being and the preference for the poor and vulnerable.

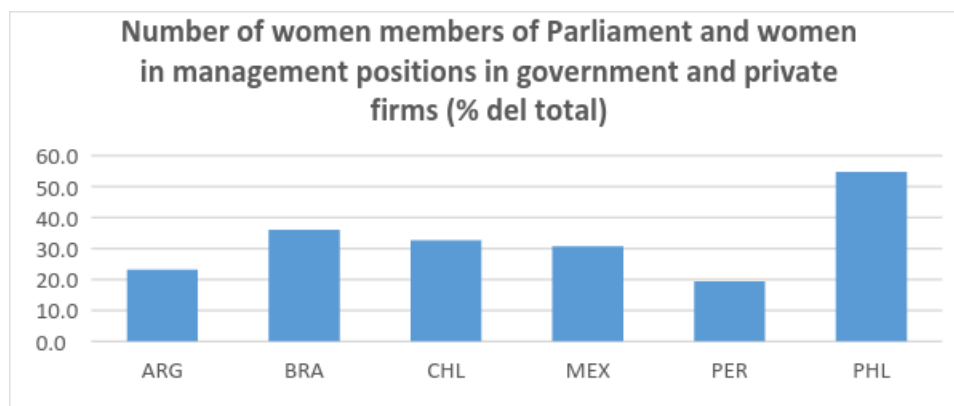
**This violation of basic justice and freedom has taken place against women globally.** Women only achieved political representation in the 20<sup>th</sup> century and are still grossly under-represented in governments and Parliaments across the world. It has also affected ethnic minorities in some countries, such as groups of African descent in the diaspora and indigenous populations in countries of European settlement. Groups can also be under-represented for religious reasons (such as Catholics in the history of the US presidency) or for linguistic reasons (such as Catalans in Spanish government cabinets). Finally, groups can be under-represented because of economic reasons. This may be the case either legally – through property and literacy requirements for either voting or standing for election or through private

<sup>8</sup> The deterioration in the corruption index after 1997 may be partly due to decentralization given the presence of even more widespread corruption at the local level.

financing of electoral campaigns—or, in practice, as when there is a strong social prejudice against the poor and/or preference for the “well-heeled.”<sup>9</sup>

**As regards the representation of women in politics and in the economy and society at large, the Philippines does much better than Latin America and is in fact one of the world’s top performers.**

Probably because of a pre-colonial history of matriarchal (or at least more egalitarian) societies, women in the Philippines are among the best represented in the world in all areas of society.<sup>10</sup> The opposite is true in Latin America, with traditional indigenous societies being strongly patriarchal<sup>11</sup>. The percentage of women members of Parliament and women in management positions in government and private firms in the Philippines, at 55 percent, is twice the average level in our Latin American country comparator group.



**The percentage of women in Parliament in the Philippines, however, is only 19 percent, exactly the same share as in our Latin American comparator group average.** A degree of preference for men in “high-powered” political positions probably exists in the Philippines. However, since women are much better represented in other “high-level” spheres of economic and political life, low female representation in Congress is more likely to reflect a preference by women. In particular, since the

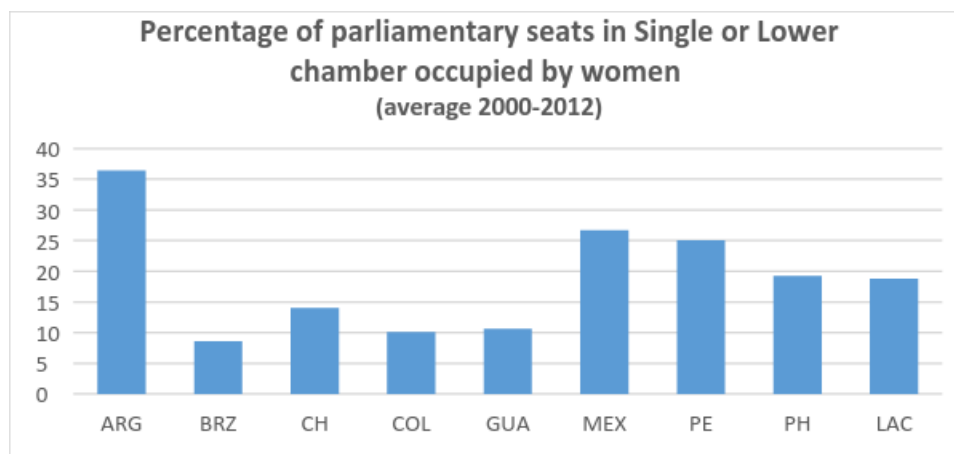
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<sup>9</sup> Discrimination against women has often been justified using religion and culture almost everywhere in the world. These social constructions have built images of the relegation of women to the “private sphere” as part of the “natural order” or even as a pillar of the “good society.” This is a social construct that is yet to be overcome. Racial discrimination, on the other hand, has been mostly socio-economically and politically driven without typically “enjoying” the philosophical backing of organized religion even when backed by it *de facto*.

<sup>10</sup> The fact that discrimination against women in the Philippines is less than in most other countries does not imply that it does not exist. Men still dominate top positions in most economic, political and other institutions.

<sup>11</sup> Discrimination seems to be less pronounced in Latin American societies with a stronger European heritage; Presidents like Michelle Bachelet (Chile), Eva Peron and Cristina Fernandez de Kirchner (Argentina), Laura Chinchilla (Costa Rica), Violeta Chamorro (Nicaragua) and Dilma Rousseff (Brazil) show progress in the representation of women in some Latin American societies, including at the highest levels. The Philippines has had two women presidents: Corazon Aquino and Gloria M. Arroyo.

percentage of women in Parliament is so low, this means that the percentage of women in management positions in government and the private sector to yield a total 55 percent representation rate must be particularly high.<sup>12</sup> Therefore, low female representation in Congress may be due to the high cost of running for office as well as a preference by women to stay away from an institution they do not have a particularly positive perception of.<sup>13</sup> However, the low representation of women in Congress, with its attending poor reflection of women's perspectives, preferences and approaches does have a high price tag for public policy-making, the overall governance of the country and overall development results.



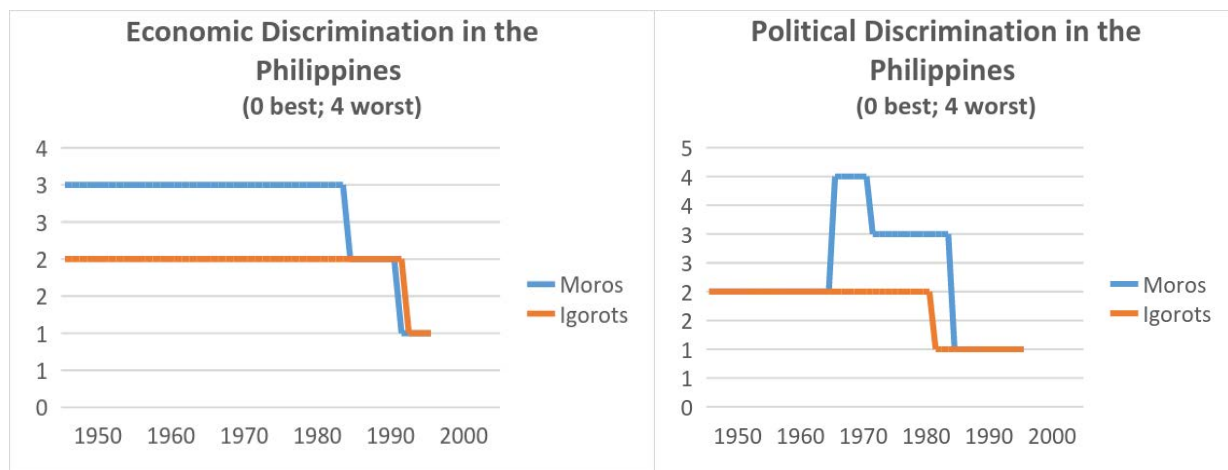
**Until recently, Latin America has had a history of exclusion –or at least under-representation-- of indigenous peoples in its governments while the Philippines is significantly more color-blind.** The deeper history of European colonization in the Americas, including the transfer of large European population groups to the new continent, resulted in a strong post-colonial system of political domination by the descendants of Europeans in economic and political systems. This is reflected in the analysis carried out by the Minorities at Risk project of the Center for International Development and Conflict Management at the University of Maryland which codes and rates the situation of ethnic minorities across the world.<sup>14</sup>

<sup>12</sup> However, in the civil service, women account for high shares of director and assistant secretary positions, a smaller share of under-secretary positions and only a minority of secretary positions (since secretaries are career politicians).

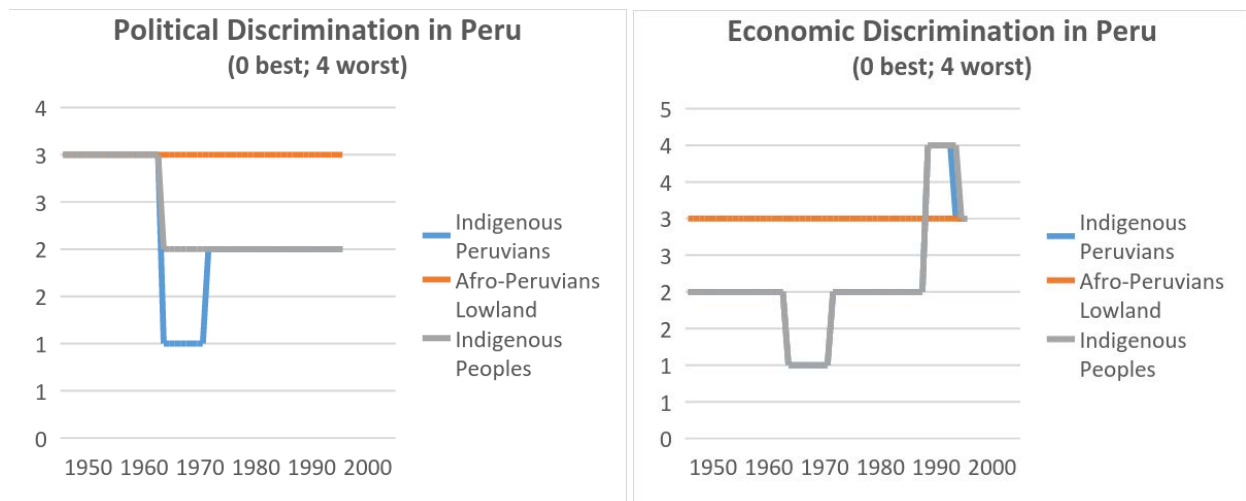
<sup>13</sup> This is the impression of the author from her conversations with professional and academic women in the Philippines. It is consistent with the lower participation of women in corruption found by international research. Moreover, in a country in which government is reasonably effective and open to women managers as is the private sector, Congress, being more focused on power battles, weakened by patronage and corruption and requiring high levels of funding is likely to appear as a relatively less attractive option for women.

<sup>14</sup> The Minorities at Risk (MAR) Project is a university-based research project that monitors and analyzes the status and conflicts of politically-active communal groups in all countries with a current population of at least 500,000.

**In the Philippines, on the other hand, there is a much less visible color pattern as far as government representation is concerned (as well as in other areas of society).** Even minority groups in the Philippines are rated as suffering less discrimination than their counterparts in Latin America. In the Philippines, the only groups classified by the University of Maryland project as “minorities at risk” are the Igorots and the Moros and, in 2003, their economic and political discrimination rating, at 1 (in a scale of 0 to 4 from better to worst), was quite low. Moreover, the rating has improved over time particularly, since the inception of democracy, and it is set to improve even further as the recent peace agreement with the Moro leaders of Mindanao is implemented.



**European domination in Latin America is slowly being reversed as democracy becomes consolidated, educational opportunities advance and indigenous-led governments come to power.** As of 2003 (the last year for which data is available), however, Peru still scored below the Philippines for all three minority groups at risk—indigenous Peruvians, lowland indigenous Peruvians and Afro-Peruvians—in both economic and political discrimination. The same was the case for Mexico, where all three groups identified as minorities at risk were facing a level of economic and political discrimination rated at 3.



**These indicators, however, do not fully capture the extent of social discrimination, which is often deeper and more resilient to policy change than either political or economic discrimination.**<sup>15</sup> There are unfortunately no perception-based survey indicators on how discriminated groups (whether women, or other vulnerable or discriminated groups, including the poor) feel about the level and nature of their discrimination. As social discrimination is concerned, a different set of tools is needed to address it, focusing on education by the formal education systems, the family, the mass media and organized religion. Education helps set perceptions and values of what is good and what is true and, hence, it can make the deepest and most lasting contribution to eradicating all discrimination whether social, economic or political. This campaign, however, is not as far advanced as it ought to be whether in the Philippines, in Latin America, or more broadly.

**The World Justice Project’s Indicator on “equal treatment and absence of discrimination” shows a slight advantage of the Philippines over Latin America.** In a scale where 100 is the best and 0 the worst ratings, the Philippines is rated at 57 while our Latin American comparator group average stands at 54. The Latin American countries with the lowest rating ---and highest discrimination---are those with the highest percentage of indigenous populations---Guatemala (43) and Peru (48).

**There is also no perception-based data on whether the poor feel discriminated against.** As *the Voices of the Poor* study reflected (World Bank, 2000), one of the greatest sources of suffering of the poor is how they are treated by the non-poor. This mistreatment affects their behavior, including their

<sup>15</sup> For instance, survey data may reveal the persistence of discrimination as perceived by Muslim Filipinos despite the country’s good ratings on political and economic discrimination.

willingness to interact with government even as regards accessing social services. Elite surveys carried out in the Philippines and in some Latin American countries such as Brazil reflect a higher level of “social consciousness” by the elites in Latin America. In the Philippines, on the other hand, a large share of survey respondents felt that “the poor bear some of the responsibility for their own poverty,” that it is each *individual’s* responsibility to pull themselves out of poverty and that inequality is good for the country’s prosperity (Reis and Moore 2005: 222).<sup>16</sup> This does not, however, imply that the poor are treated worse at the individual level in the Philippines than in Latin America, especially because of the inter-action between the income and the race factors in discriminatory attitudes toward the poor. The absence of perception-based survey data of the poor does not allow us to make that comparison.<sup>17</sup>

**Party-based political systems together with more stringent limitations on private campaign financing result in a greater ability of the poor to run for office in Latin America than in the Philippines.** As has been repeatedly argued, politics in the Philippines is dominated by the wealthy. The *Rulemakers. On How the Wealthy and Well-Born Dominate Congress* documents that pattern by going over the economic background of members of Congress (Coronel et al. 2007). This is also the case in local politics, which are often dominated by local political dynasties of the well-off (De Dios, 2007). In Latin America, on the other hand, there has been a significant increase in politicians of modest backgrounds running for office and, recently, many of them have even become heads of state.<sup>18</sup>

**In Latin America, programmatic-party based systems have facilitated a much greater focus on governmental provision of public versus private goods than in the Philippines.**<sup>19</sup> The prevalence of individual seat constituencies in the Philippines, jointly with its history and political culture, have fostered the provision by individual politicians of political patronage and private goods. In Latin America, on the other hand, political parties have, to a much larger extent, focused on the institutional provision of public goods. This differential pattern, together with the greater “social consciousness” –including of the elites-- in Latin America, can help explain why more resources have been devoted to effective pro-poor policy measures there than in the Philippines, resulting in greater poverty reduction.

### **Economic Facilities**

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<sup>16</sup> Some religious denominations have also fostered discrimination against the poor, especially the Calvinist-Puritan view that the poor are not only poor, but also damned as economic success is seen as an indicator of God’s grace and salvation. The greater US-Puritan influence in the Philippines may help explain differences with Latin America.

<sup>17</sup> On the contrary, arguably, the conflation of poverty with racial difference in Latin America tends to result in greater discrimination resulting in stronger political polarization and estrangement among social groups.

<sup>18</sup> This is the case for Peru, Bolivia, Ecuador and Venezuela.

<sup>19</sup> On the preference for private over public goods in the Philippines see Alonso I Terme (2014).

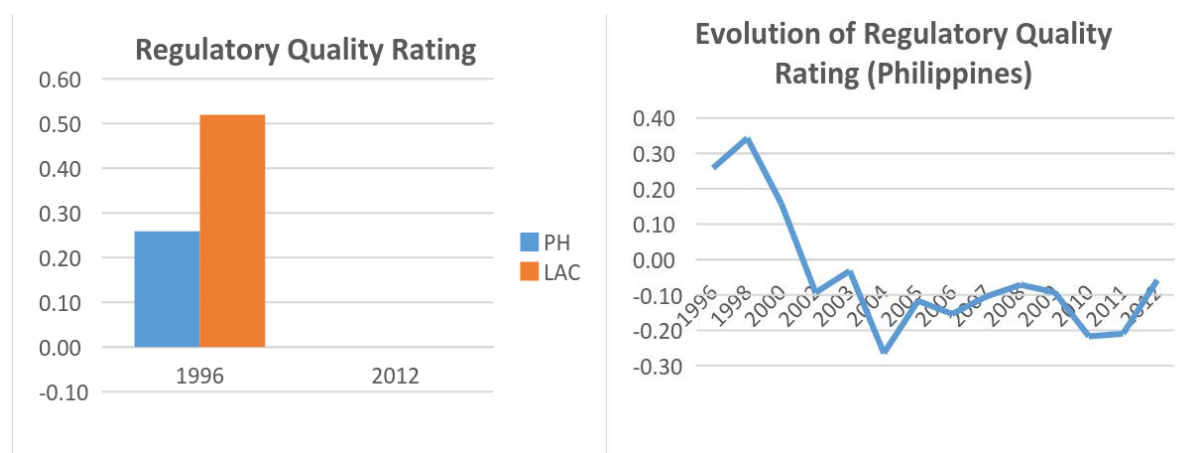
**According to Amartya Sen, “economic facilities refer to the opportunities that individuals enjoy to utilize economic resources for the purpose of consumption, or production or exchange” (Sen, 1999).**

This area of wellbeing includes, therefore, both the freedom to produce and exchange (economic freedom) as well as the capacity to consume (basically determined by the interplay of income and prices). Both of these capacities are important and are inter-related. Let us take each in turn.

**The ability of an individual to utilize resources for the purpose of production and exchange depends on a number of factors concerning economic freedom.** These factors include government regulation, bureaucratic red-tape and barriers to entry either by government –such as high or multiple business license or other fees and requirements—or by market incumbents.

**Quality of private sector regulation is an area where Latin America is well ahead of the Philippines.**

Using WWGIs regulatory quality for private sector development indicator, we see that the rating for the average of our Latin American comparator group is well above that of the Philippines. Moreover, the rating for the Philippines has deteriorated since 1996, though it began to improve again between 2011 and 2012.<sup>20</sup> This indicator is closely related to investment climate data.



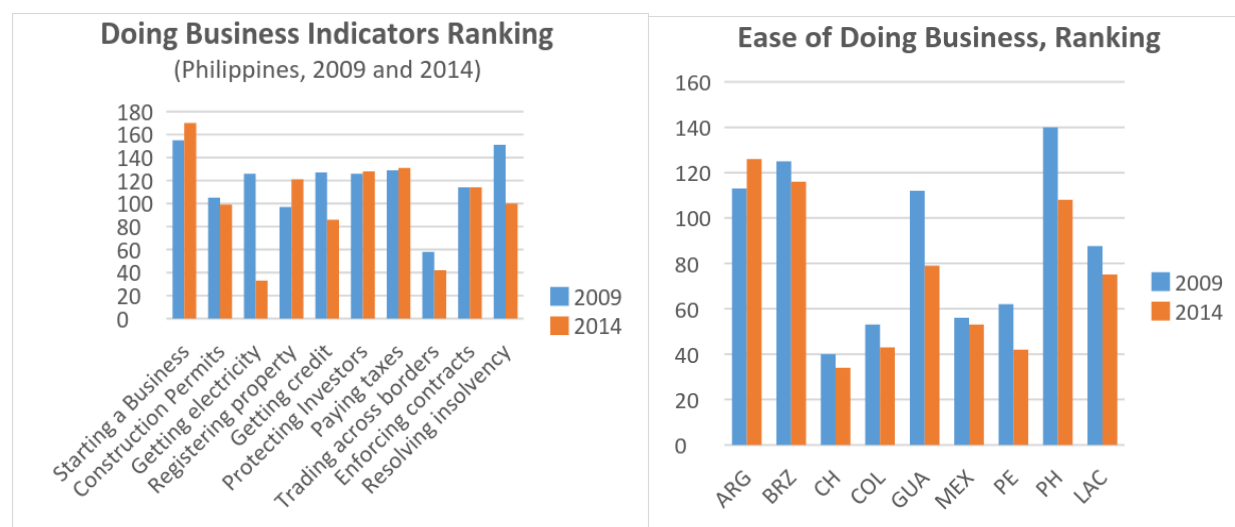
**The same recent improvement can be seen in the ranking of the Philippines in the Doing Business Indicators of the World Bank, though it still ranks below the Latin American comparator average.**

There have been important improvements in areas such as getting electricity, getting credit, resolving insolvency and trading across borders. The country, however, still ranks rather low in a number of

<sup>20</sup> There are also legally-imposed investment limitations such as the ones enshrined in the Constitution in the Philippines, limiting foreign investment to 40 percent in key sectors (such as real estate, public utilities and natural resources including energy), as well as laws forcing banks to devote a certain share of credit to agriculture, and restrictions on rice imports.



critically important areas for investment such as starting a business, construction permits, registering property and protecting investors.



**Of particular concern is the difficulty of starting a business, in which the Philippines is still ranked at number 170, the lowest of all our sample.** This low ranking is confirmed by the World Economic Forum's Competitiveness Index in which the Philippines is ranked 145 out of 148 countries in number of procedures for starting a business. This high burden for starting a business is doubtless an important deterrent to investment. Moreover, this heavy burden for non-incumbents restricts market entry and protects incumbents weighing particularly heavily on the potential micro and small entrepreneurs for whom these costs may prove unbearable.

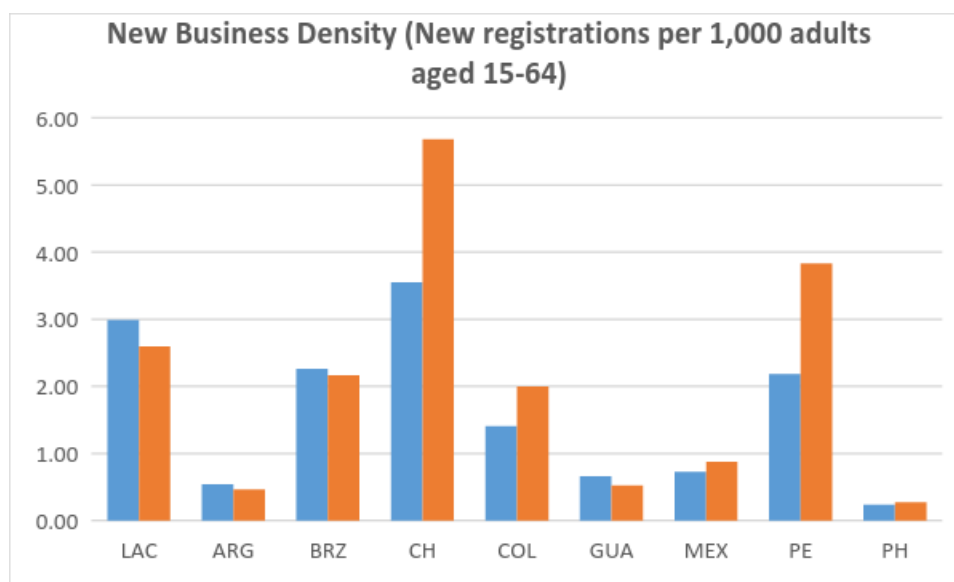
**These barriers for small businesses are compounded by a high level of fees to be paid by firms.** The *Paying Taxes* 2014 issue of the World Bank finds that the level of corporate profits that go into "other taxes" in the Philippines (i.e. aside from corporate income taxes and labor taxes), at 14 percent, is very high compared to 1 percent in Mexico and Malaysia and 3 percent in Indonesia and Taiwan (World Bank, 2013). This is likely due, at least in part, to the high level of business fees in the country.<sup>21</sup>

**The result of the absence of government involvement in electricity generation and the Meralco monopoly in electricity distribution is the highest electricity price in East Asia after Japan** (World Bank, 2010). Unlike in other countries in the region, the government does not have a price-setting electricity

<sup>21</sup> Taxes on businesses and permits and licenses alone accounted for 42 percent of local governments' (LGUs) own resources in the Philippines in 2013. To these costs on businesses, one needs to add real estate taxation which accounted for a further 31 percent of LGU's own revenues. In LAC, most local government revenues come from the central government and local revenues as a percent of total revenues or GDP are typically low (Gold, 2011: 200-1).

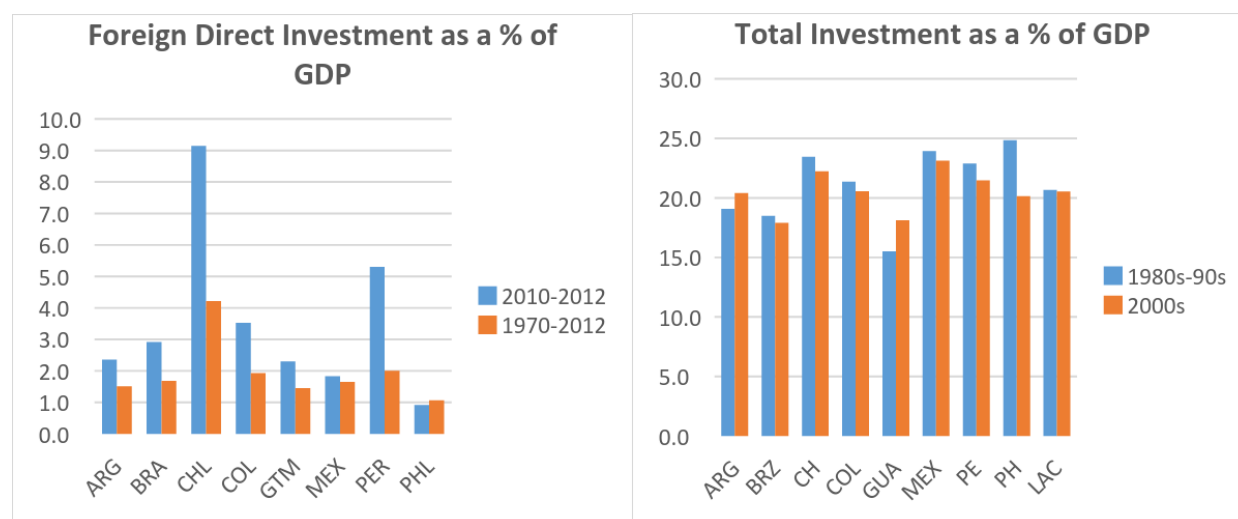
generator. Moreover, the constitutional limit on foreign investment in utilities (up to 40 percent only) leaves the Filipinos in the worst possible situation—without public provision and without competition. The sector is instead left in the hands of a private oligopoly which is ineffectively regulated. This oligopolistic pricing in generation combines with an also ineffectively regulated Meralco monopoly in distribution. Non-competitive pricing --driven by the absence of public participation in the sector, constitutional limits on foreign entry, and ineffective regulation-- poses important *de facto* constraints on economic freedom and seriously hampers the growth of the manufacturing (and any energy-dependent) sector in the Philippines. Needless to say, it also significantly hampers the population's access to electricity (covered later on in the paper). In Latin America, on the contrary, the electricity sector is government-run, has a public price-setting company or, at least, is more effectively regulated.

**The Philippines also has important problems of market concentration and market dominance in the manufacturing sector.** Many markets are dominated by a very small number of firms engaged in non-competitive pricing as reflected in high price-cost margins. These practices raise prices for other producers as well as final consumers. Ultimately, as poignantly stated by Aldaba (2008): “weak competition is one of the fundamental factors that explain limited growth, productivity, and employment in the economy.” Market concentration is also reflected in a particularly low level of business entries compared to our country sample.



**This difficult business environment, particularly barriers to entry, helps explain the low level of foreign direct investment (FDI) in the Philippines.** The level of FDI in the Philippines is among the lowest

in middle income countries, whether one compares it with East Asia or Latin America. The fact that the total investment to GDP ratio is *not* significantly below the Latin American average points to the existence of barriers to entry by foreign firms. This low level of FDI favors the continuation of market concentration in the hands of local elites and hampers competition, spill-overs of technology and other “know-how”, productivity growth, overall investment and, ultimately, economic growth and poverty reduction.

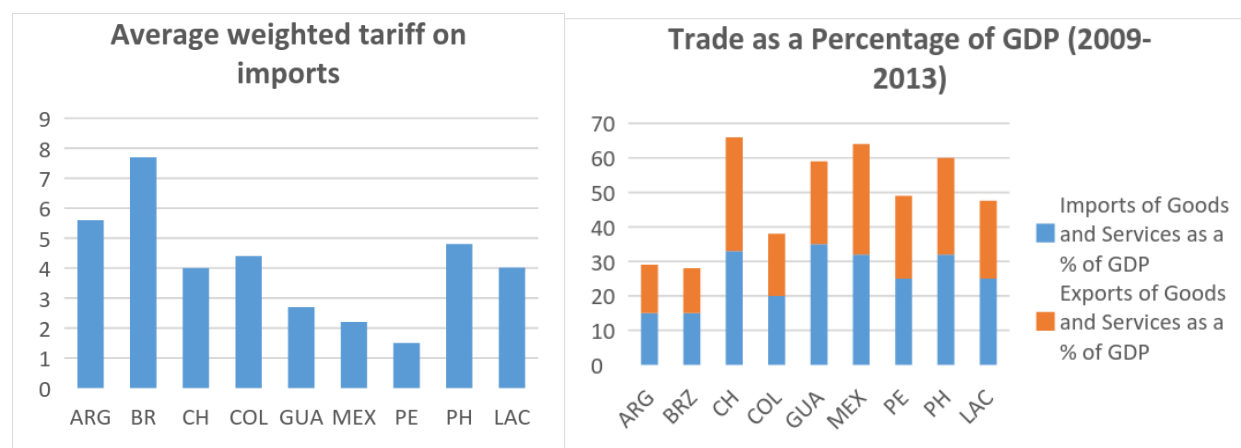


**In the Philippines, foreign investment faces limits in critical sectors such as utilities, natural resources, banking, land ownership, education, public works, mass media, advertising and others.** These limits, together with lack of government participation in utilities and natural resources, leaves these critical sectors with insufficient competition and in the hands of local elites. The limits seem to be related to the low level of foreign investment in the country. Evidence to this effect is the fact that, when liberalization increased in the transportation, communications and storage a sector, growth significantly picked up (Aldaba 2008: 12-13). Much room remains in opening up sectors whose liberalization could significantly boost investment as happened in Latin America in natural resources, energy, utilities, transport and ICT.

**The low level of FDI hamstrings the country’s ability to fully reap the fruits of the many strengths of its private business and banking sector.** The World Economic Forum’s Competitiveness Index ranks the Philippines favorably among a group of 148 countries in a number of areas with potentially strong synergies with FDI. These include reliable professional management (32), venture capital availability (40), firm-level technology absorption (40) and FDI and technology transfer (42). These strengths are complemented by other high private sector rankings such as customer orientation (20), willingness to delegate authority (26), extent of staff training (27), financing through local equity market (27),

affordability of financial services (31), soundness of banks (36), ease to access loans (37), regulations of securities exchange (38) and availability of financial services (40). Limits to FDI are thus of particular concern in a country with such strengths and which, due to its overall gap between productivity and production costs, needs to compete in the relatively high-end market in which foreign firms can make an especially important contribution to investment and technological change.

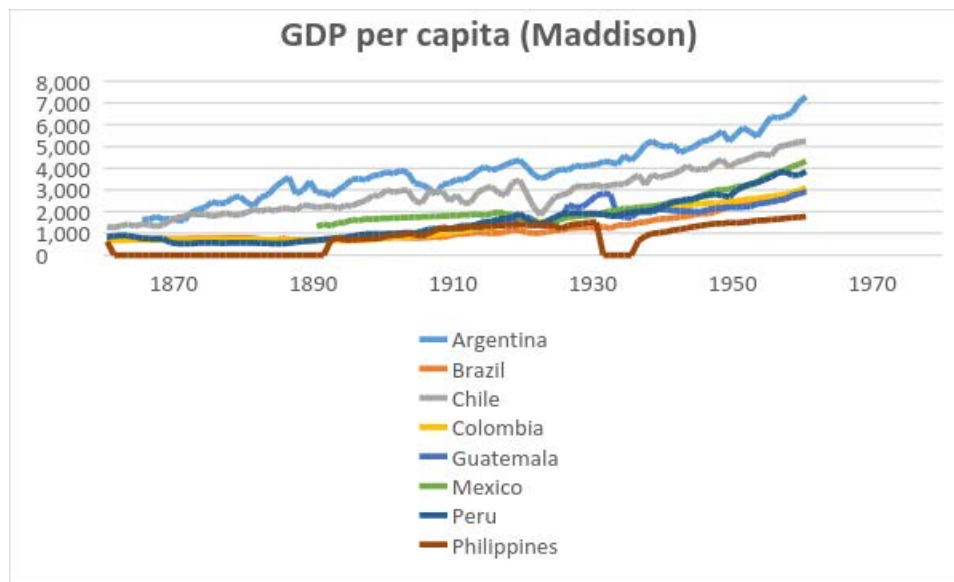
**As regards restrictions to trade, the average weighted tariff rate is low in all our sample countries and most economies have relatively high trade openness indices.** The Philippines' average weighted tariff on imports is slightly above the Latin American comparator average, but its trade openness index, with imports and exports amounting to 60 percent of GDP, is very high. This is particularly striking since the Philippines is one of the larger economies in our sample. This high level of openness of the Philippines is due to levels of both imports and exports of goods and services above our comparator average.



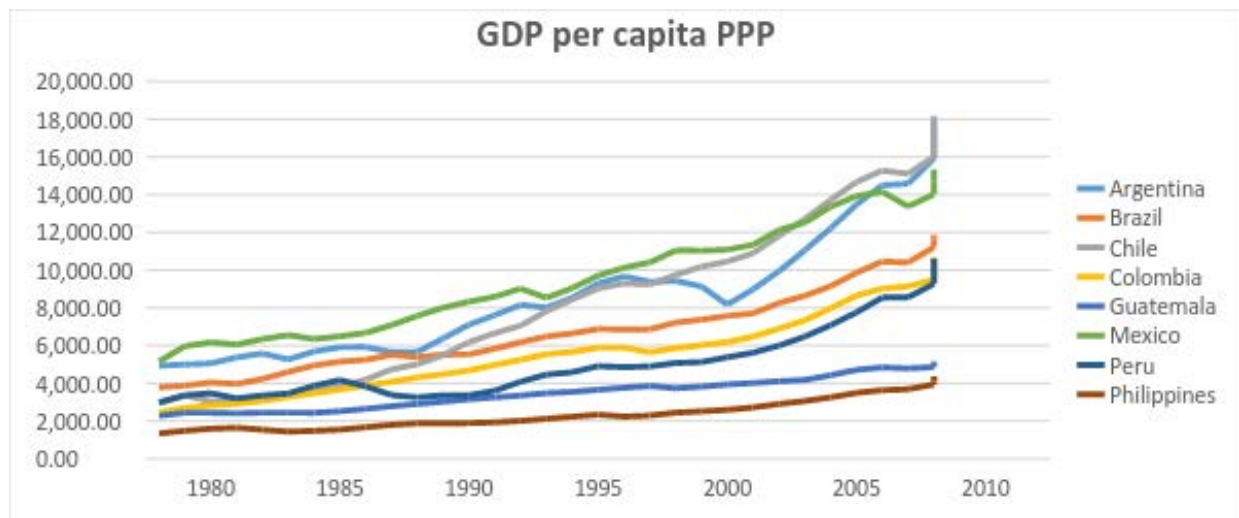
**The Philippines suffers from uneven tariff protection creating important price distortions and artificially high prices brought about by heavy import restrictions in key sectors such as rice.** Due to a policy of selective protection, effective rates of protection have become highly uneven causing large price distortions and resource misallocation. Most tariff peaks are concentrated in agriculture and manufacturing of food, drugs, medicines, car manufacturing and chemical products. (Aldaba 2008: 22). Moreover, the Philippines has not liberalized its rice market and, contrary to many other countries, it implements its protectionist policy, not through subsidies but through tariffs. This leads to a price of rice that is estimated to be around 40 percent above the world market price. This high price of the most basic staple in the country constitutes a grave affront to equity and a heavy burden on the poor, aside from raising labor costs and causing economic inefficiency in resource allocation. In Latin America, on

the other hand, there is no equivalent restriction on the trade of basic staples and liberalization has been found to be a key factor in the sector's recent export success (see below).

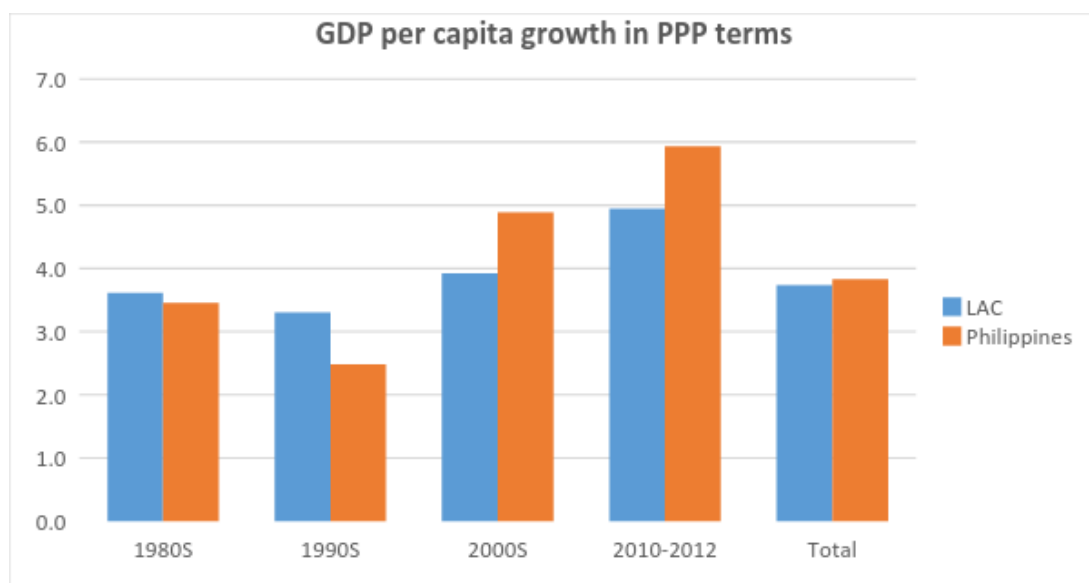
**As regards income levels (reflecting “freedom of consumption”), Latin America is well ahead of the Philippines, a gap which developed historically and accelerated since the 1940s.** In 1870, income per capita in the Philippines was at the same level as in Mexico and was comparable to that of Colombia and Brazil. By 1902, however, it had fallen to half the level of Mexico, though it was still close to Colombia and Brazil. The gap expanded rapidly in the 1940s and continued to grow thereafter.

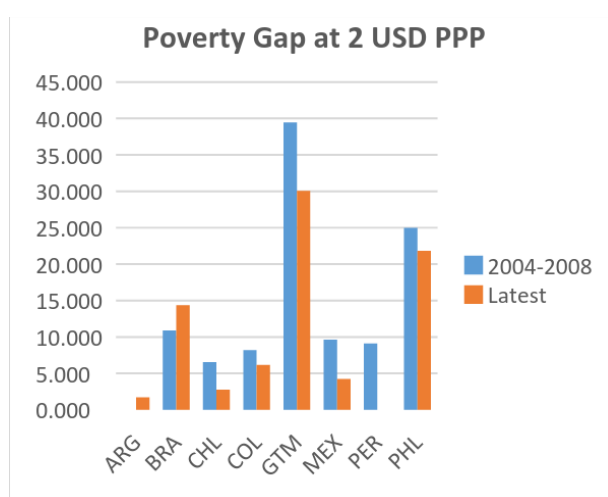
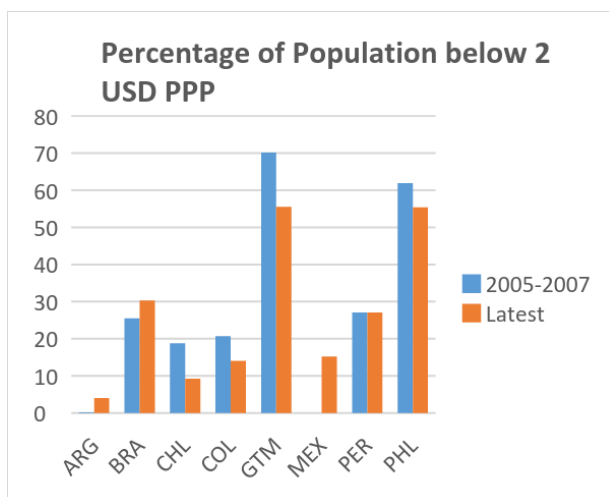


**The income gap continued to expand in the 1980s and 1990s.** It is important to note this fact since, traditionally, the relatively poor performance of the Philippines compared to that of other East Asian countries is explained by the good performance of the East Asia region. The fact that the income gap has also grown significantly with the Latin America region raises the question of what has gone wrong in the Philippine development model and what lessons the Philippines can learn from Latin America (as well as East Asia).

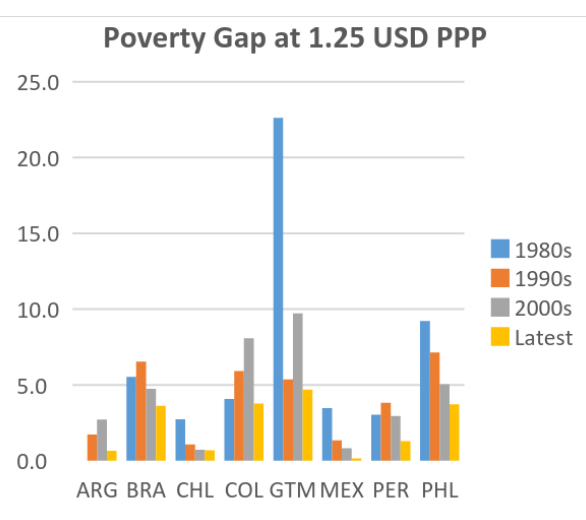
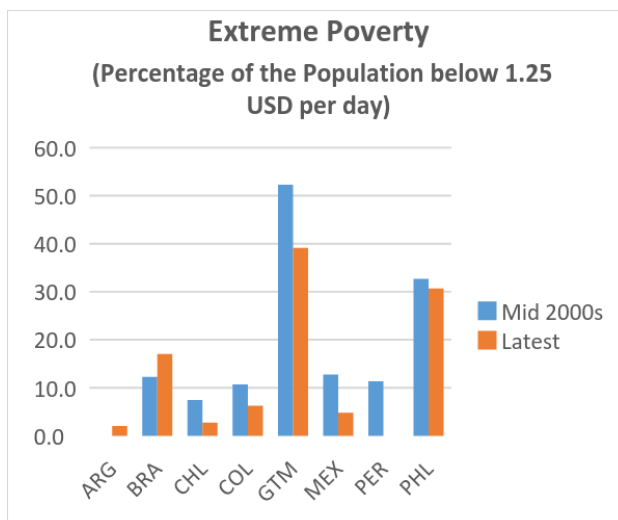


Since the 2000s, however, growth in the Philippines has sped up and it has been even faster than in Latin America. Despite faster growth, however, poverty has failed to decline noticeably in the Philippines and it is much higher than in all our Latin American comparator countries except Guatemala, which has by now also caught up with the Philippines. The poverty gap is still higher in Guatemala, but it is falling faster than in the Philippines.





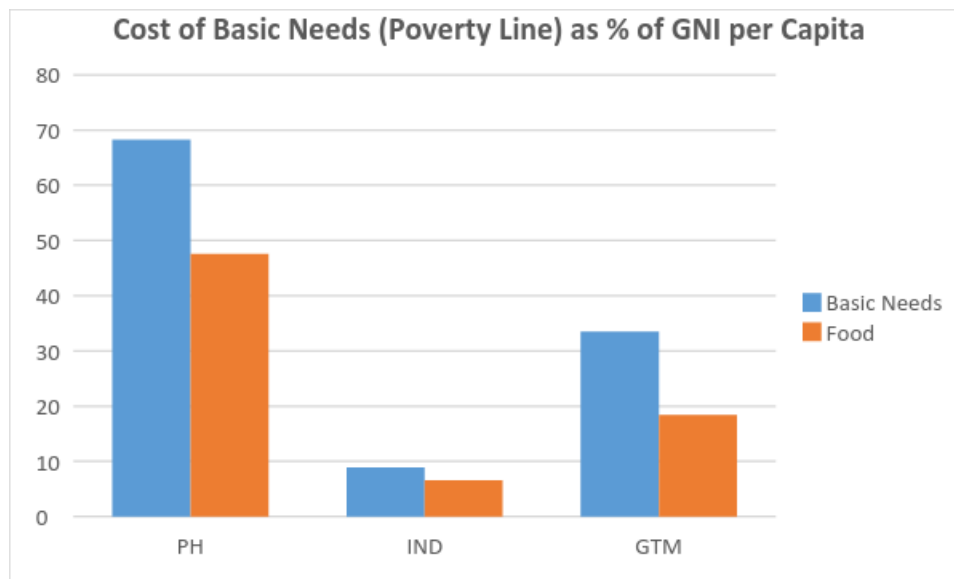
**Extreme poverty has declined rapidly over the 2000s in most Latin American countries, but less so in the Philippines.** Even in Colombia and Guatemala, where the poverty gap in the mid-2000s was larger than in the Philippines, extreme poverty has declined by more. Guatemala provides a useful comparator because, despite lower growth than the Philippines since 2000, it has reduced poverty and the poverty gap much faster.<sup>22</sup> The extreme poverty gap in the Philippines, however, has declined slowly but consistently from the 1980s up to the present.



<sup>22</sup> This has to do with the nature of growth and the growth-elasticity of poverty in each country. As we will see in the section on social opportunities, Guatemala is devoting twice the share of its budget to education and health as compared to the Philippines. This can help explain the pattern of growth.

**The high price of basic needs in the Philippines relative to its average income per capita is an outlier in our sample countries and may help explain the Philippines' high wages and slow employment growth.**

The relative cost of basic needs in the Philippines –reflected in its poverty lines--is multiples of that in comparator countries. In the Philippines, one needs to earn 68 percent or 48 percent of the average gross national income per capita in order to be above the basic needs and the food poverty lines respectively. This is a very high percentage, which is a multiple of that in other lower-middle income countries.

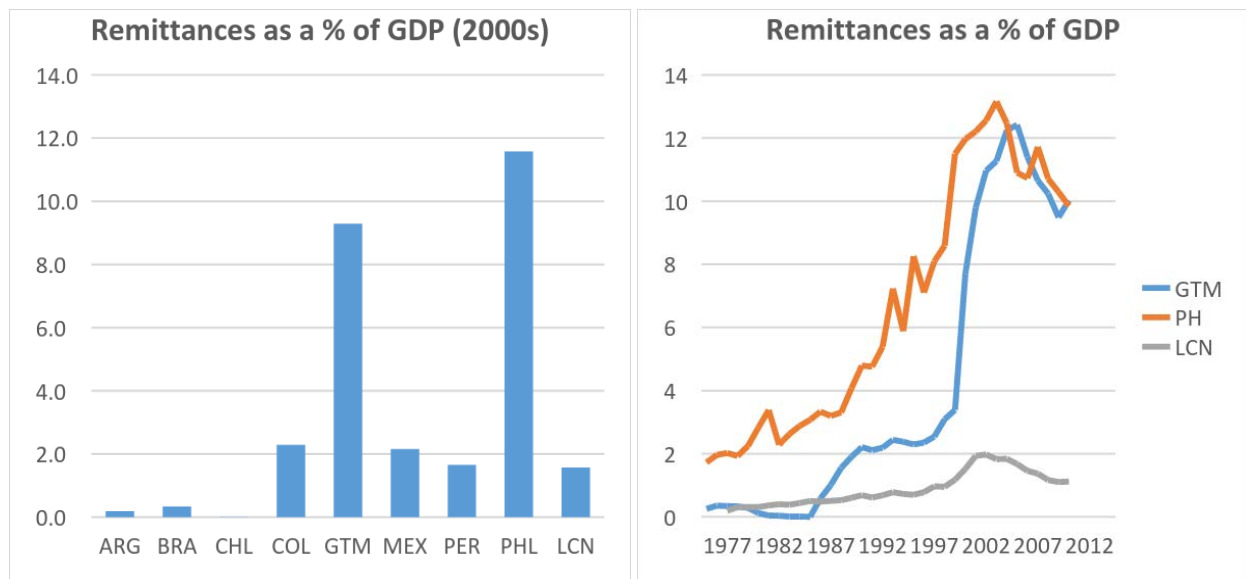


**The reasons behind the relatively high poverty line in the Philippines likely include expensive rice, electricity, water, housing and medicines among other goods and services.** The protectionist policy toward rice implemented through trade barriers in the Philippines, as mentioned above, results in a price of rice that is roughly 40 percent above the world level. The privatization of water and electricity has also led to low levels of access and high prices of these basic utilities, further inflating the cost of basic needs (with electricity costs being the second highest in Asia after Japan (World Bank 2010).

**Basic drug prices in the Philippines are the highest in East Asia outside Japan and about 15 times the WHO reference price** (Ball and Tisocki: 8). The absence of a genuine public health care system and, in particular, of a government monopsony in the purchase of drugs jointly with tariff protection (Aldaba 2008: 22) and the absence of VAT exemption on basic medicines, the charging of the cost of senior citizens VAT exemption on other drug purchasers and high retail mark-ups result in extremely high drug prices.



**High prices may also be due to the fact that the Philippines has one of the highest rates of remittances to GDP in the world.** Emigration from the Philippines shot up since the mid-1980s. This has led to a dramatic rise in remittances which, in turn, push up the cost of non-tradable goods and services --since they do not correspond to any increase in national production—leading to higher imports and higher domestic consumption levels. This in turn increases the country's wage levels. The fact that a significant share of remittances is spent on real estate can also help explain its high cost in the Philippines, especially in cities like Manila. According to a private real estate company, Global Property Guide, Manila seems to have one of the highest housing price to income ratios among Asian cities. The ratio in Manila stands at 20.5 compared to Kuala Lumpur (6.1), Singapore (7.3), and Bangkok (9.2) and is only exceeded by Shanghai (31.1) and Jakarta (23.5). (Cruz 2008).

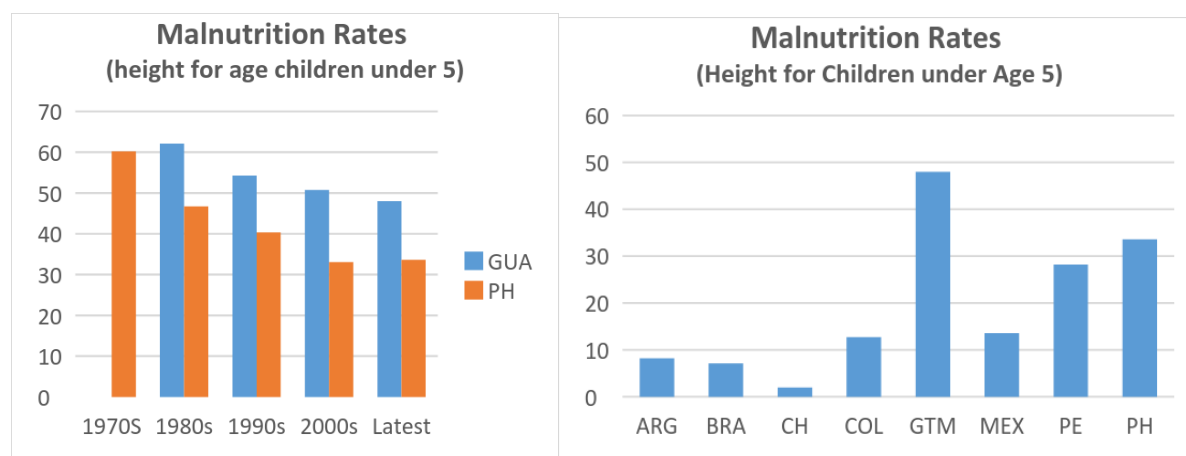


**The high level of poverty in the Philippines and Guatemala results in widespread material deprivation including high rates of malnutrition in both countries while the average rate is low in the LAC region.**

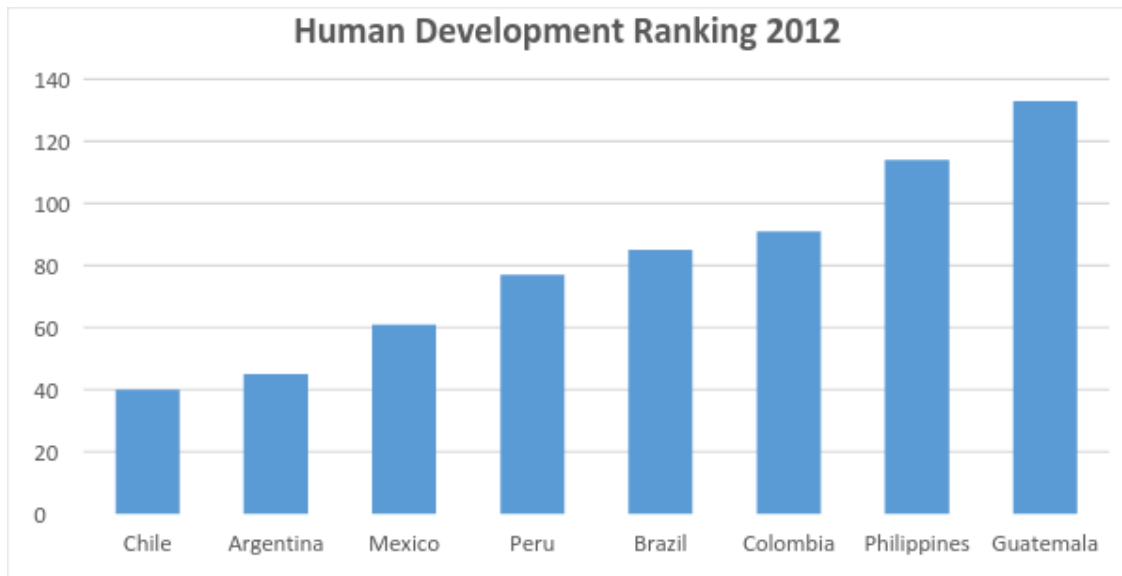
Malnutrition rates are much higher in both Guatemala and the Philippines than in our other Latin American comparator countries. Significant proportions of the population are undernourished in both countries (30.5 percent in Guatemala and 16.2 percent in the Philippines), compared to a 9 percent Latin American average.<sup>23</sup> From the 2000s to the present, the depth of the food deficit has decreased by 45 percent in Latin America and by 14 percent in the Philippines while, in Guatemala, it has increased by 9 percent.

<sup>23</sup> Other indicators of malnutrition (such as percentage of children under 5 who are under weight or anemic) portray a similar picture.

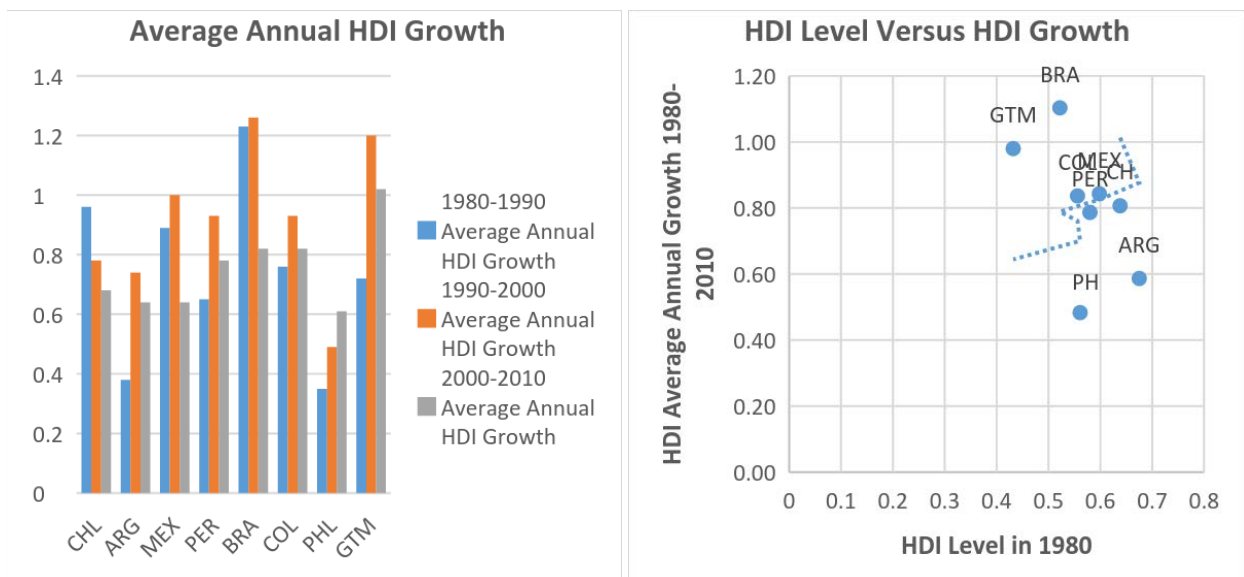
**Child malnutrition rates are also particularly high in Guatemala and the Philippines.** In the Philippines, despite high growth rates, child malnutrition as measured in the percentage of children under height increased by 1.3 points between 2008 and 2011 while the percentage of underweight children declined by 0.5 points over the same period. This stagnation in malnutrition reflects the stagnation in poverty rates despite high rates of economic growth. In Guatemala, with better progress on poverty reduction, the decline in malnutrition among children between 2002 and 2009 has been greater, declining by 6 points when measured by height and by 5 points when measured by weight.



**The UNDP's Human Development Index –which includes education, life expectancy and income—rates all our sample countries above the Philippines except for Guatemala.** The Philippines does reasonably well, however, in the index which subtracts the HDI ranking from the income per capita ranking, an indicator of how well a country does in life expectancy and years of education given its income level. In this index (in which the higher the score, the better), the Philippines rates at 11 compared with -14 for Guatemala or a 0.3 for our Latin American country sample average.

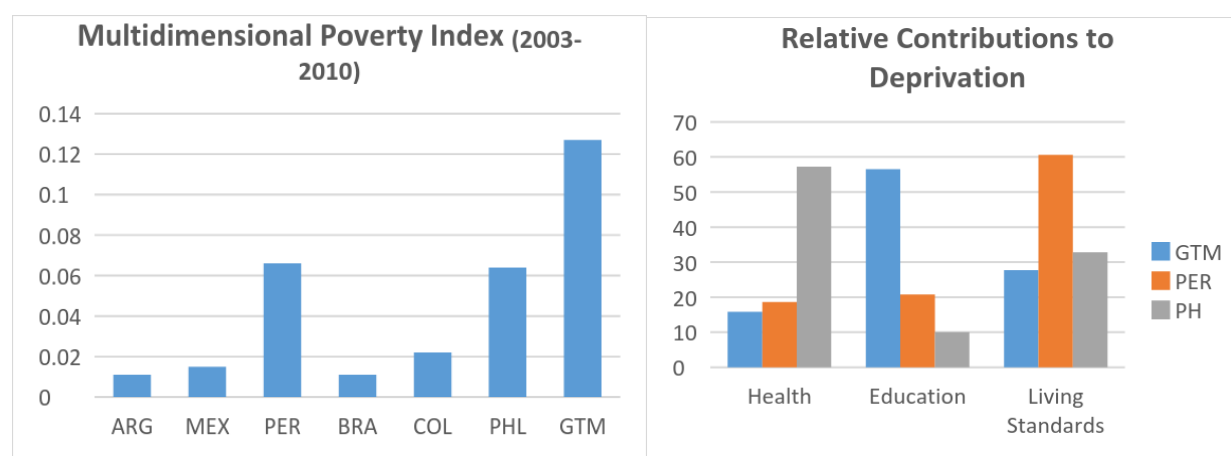


Nevertheless, the rate of improvement of the HDI since 1980 in the Philippines has been much slower than in our Latin American comparator countries. At an average 0.5 percent annual growth rate since 1980, it is the lowest growth rate of all our sample and it is an outlier in the inverse relationship between HDI level and HDI growth since 1980. In fact, the HDI annual growth rate for the Philippines over the period is only about half of what its 1980 level would predict. The HDI annual growth rate in the Philippines, however, has increased over the past two decades.



The multi-dimensional poverty index of UNDP rates the Philippines above Guatemala and Peru, but below our other sample countries. The factor that weighs most heavily in deprivation in the Philippines, with a contribution to poverty much higher than in any other country, is health. As we will see in our

next section, this is due to a low level of government expenditure on public and primary health, low levels of access to sanitation and to an own water source as well as poor housing and nutrition.



**Poverty also results in poor dwelling conditions, with a significant impact on overall wellbeing, health, education, security and social standing.** The importance of dwelling in sound, sanitary housing cannot be overestimated. As the World Health Organization has repeatedly stated, scientific evidence on the links between housing and health has grown substantially in recent decades. Some of the most important housing-related health risks include respiratory and cardiovascular diseases from indoor air pollution, illness and death resulting from exposure to temperature extremes, the spread of communicable diseases such as tuberculosis and risks of home injuries.<sup>24</sup> People dwelling in unsafe housing are also more likely to be victims of natural disasters, from flooding to earthquakes. In addition, poor housing makes studying near-impossible, greatly affecting the life-long chances of children and youth in such housing moving out of poverty. As far as security is concerned, houses in informal settlement and other marginal areas are often subject to theft, with the attendant insecurity for their dwellers. Moreover, informal settlers do not own their land and may be forced to move at any time, creating a strong sense of vulnerability. Finally, in many counties there is a social stigma against people living in informal settlement areas, which further aggravates their wellbeing and social integration.

**All countries in our group have reduced the proportion of the urban population living in slums, but the Philippines has reduced it by the least.** One of the targets under MDG number 7 of “ensuring

<sup>24</sup> WHO estimates that almost 2 million people in developing countries die from indoor air pollution caused by the burning of biomass and coal in leaky and inefficient household stoves. Many more are injured.  
<http://www.who.int/hia/housing/en/>

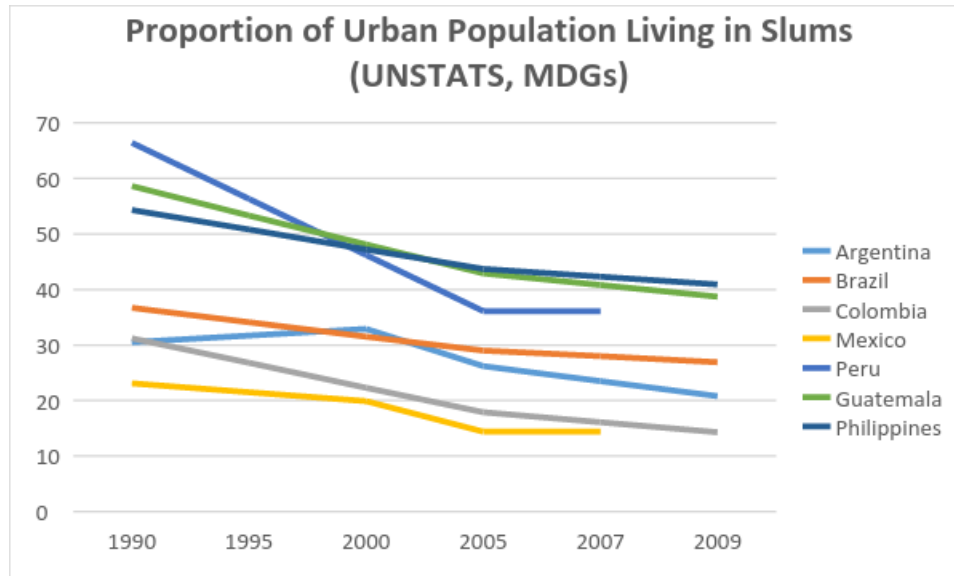
environmental sustainability” is the proportion of the urban population living in slums. Since 1990, this percentage has declined on average by 38 percent in our Latin American comparator group and by 25 percent in the Philippines. The largest reduction has taken place in Colombia (54 percent), which is reputed to have some of the most ambitious and effective slum upgrading programs in the world, followed by Peru (46 percent), Mexico (38 percent) and Guatemala (34 percent). Hernando de Soto in *The Mystery of Capital* (De Soto 2000) cites the Philippines as having some of the most convoluted systems for purchasing land in informal settler areas.<sup>25</sup>

**As UN Habitat and the urban development literature have concluded, effective programs are holistic and focus on slum upgrading rather than relocation:** “Rather than forced evictions or relocations, which have exhibited its limitations and undesired effects on livelihoods, cities as diverse as Medellin, Port Moresby, or Rio de Janeiro –and yet so similar, in so far as in all of them pockets of wealth and poverty co-exist in close proximity– have approached holistically to the upgrading of slums, with satisfactory results.”<sup>26</sup> (UN Habitat 2011: 4). Holistic slum upgrading programs, however, are expensive and may be beyond the resources available in the Philippines at current tax levels. At least, a simpler legal and regulatory framework and exempting slum dwellers from taxes and fees when they try to purchase land would be of great help. After all, Guatemala, with an even lower tax-to-GDP ratio than the Philippines and much higher population growth, has achieved significantly faster progress in slum upgrading.

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<sup>25</sup> In the Philippines, if a person has built a dwelling in a settlement on either state-owned or privately-owned urban land, to purchase it legally he would have to form an association with his neighbors in order to qualify for a state housing finance program. Needless to say, this is a time-consuming and difficult process. The entire process would necessitate 168 steps involving 53 public and private agencies and taking 13 to 25 years. Fees on land purchase by the poor, moreover, are steep and if they stop paying at any point, they lose the land. Moreover, if the dwelling happens to be in an area still considered “agricultural,” the settler will have to clear additional hurdles for converting that land to urban use—45 additional bureaucratic procedures before 13 entities, adding another 2 years to the requirements.

<sup>26</sup> “Similarly, urban development literature has progressively recognized that the material enhancement of a slum, for which institutional and regulatory changes must occur in the first place, is only part of the story. To unlock upgrading and inclusion of slums, there are other dimensions that need to be addressed focusing on a second area: governance. Social, cultural and economical conditions need also be upgraded along, with the active involvement of members of the community, lest the almost imminent failure of the project. Not only amenities are crucial, but also social cohesion and thus its *sine qua non*, urban safety.” (UN Habitat 2011: 4).



## Social Opportunities

**Social opportunities refer to access to education and health as well as the ability to interact with others in society without discrimination.** Social opportunities are not only an essential component of wellbeing, but they also greatly affect access to other freedoms, such as economic opportunity. As regards education and health, Latin America has made much faster progress than the Philippines though the latter does better in terms of discrimination.

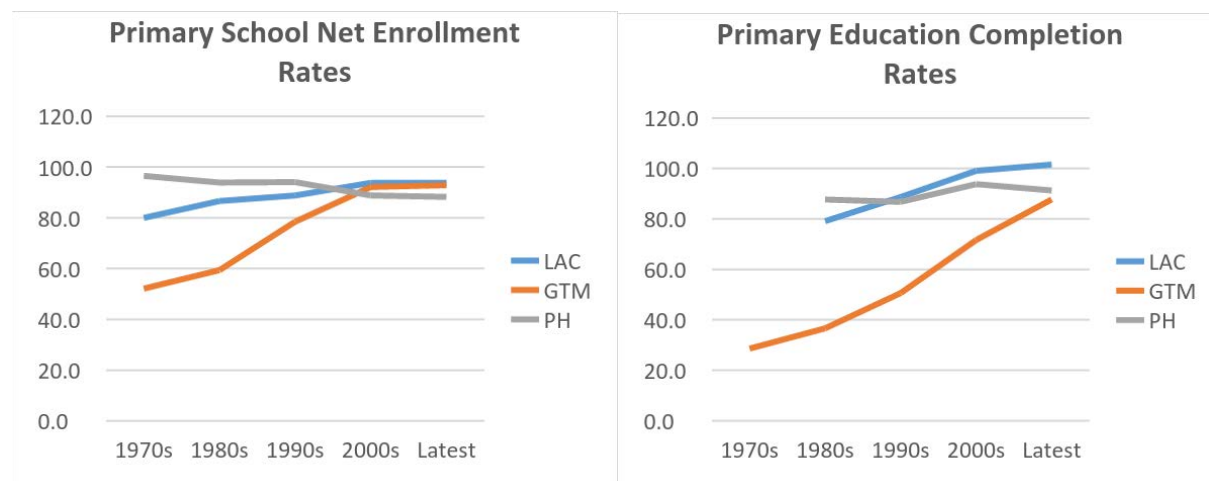
**As far as basic literacy is concerned, all countries have registered improvements over the past few decades, but the Philippines has a below-par rate of improvement since the 1990s.** The Philippines made significant progress in literacy rates over the 1980s, but it has stagnated since the 1990s. Most Latin American countries, on the other hand, have continued to increase their literacy rates, even those countries that stood at already high levels. Youth literacy, however, continued to improve in the Philippines, with the literacy rates of those aged between 15 and 24 increasing from 95.1 percent in 2003 to 97.8 percent in 2008, one point rate higher than that achieved by our Latin American comparator countries.

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## Adult Literacy Rates

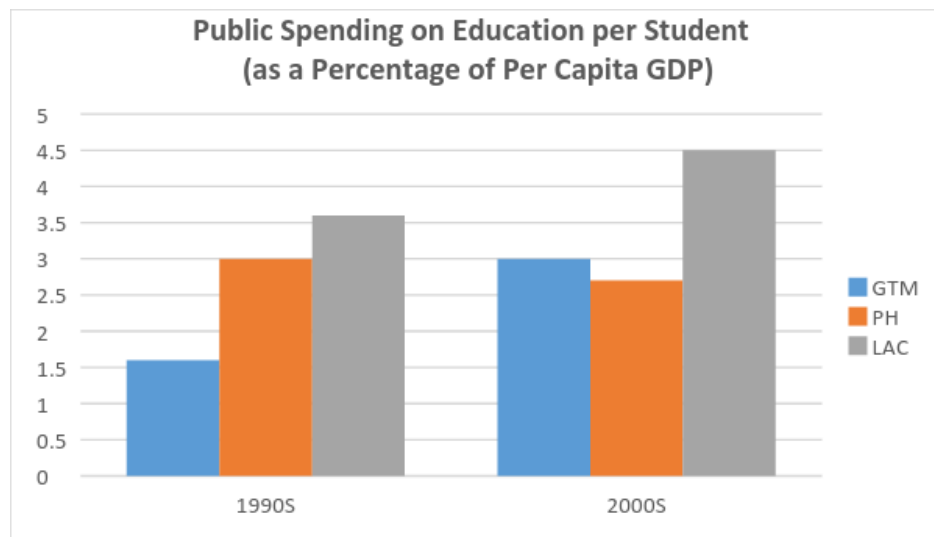
	1980s	1990s	2000s	Latest	Change since 1990s
LAC		86	90	92	6
ARG	94	96	97	98	2
BRZ	75		89	90	
MEX	83	88	92	94	6
CHILE	91	94	98	99	4
PER	82	87	88	90	2
COL		86	93	94	7
GUA		64	69	76	12
PH	83	94	94	95	2

**Primary school net enrollment and completion rates have increased rapidly in Latin America, but decreased in the Philippines, placing it below all our country comparators.** The decline in enrollment rates in the Philippines was particularly rapid between the late 1990s and the late 2000s, as it dropped from 98.4 in 1998 down to 88 percent in 2008-2009. Completion rates peaked in 2001 and have been on the decline since then and until 2009, which is the latest data available. During the same period, both enrolment rates and completion rates grew steadily in Latin America, doing so particularly steeply in Guatemala.



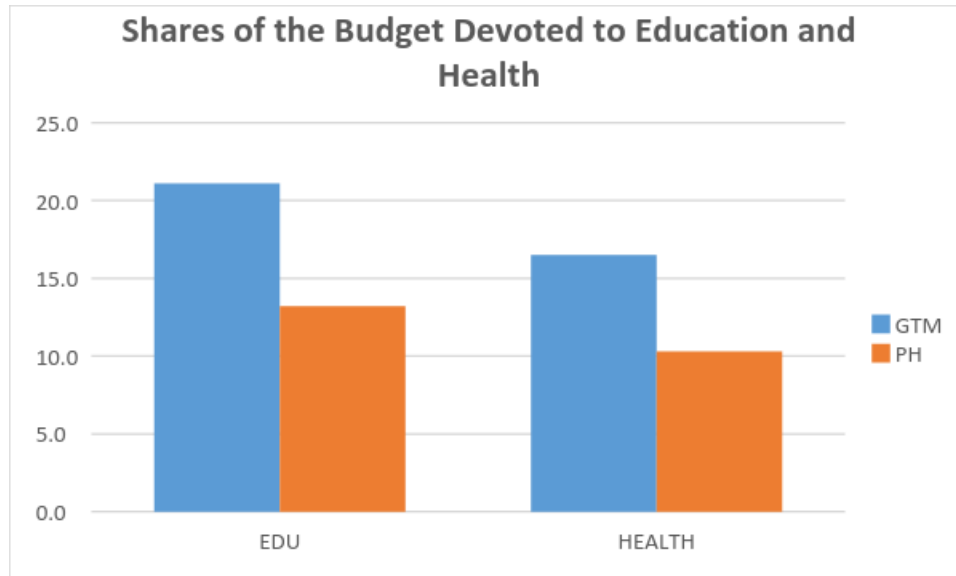
**The worsening performance in the Philippines and the improvement in Guatemala coincide with a dramatic reduction in education spending in the Philippines and a strong scale-up in Guatemala (and the rest of Latin America).** In the Philippines, public spending on education as a percentage of GDP plummeted from 3.8 percent in 1998 to a nadir of 2.4 percent in 2004 before increasing slightly thereafter up to 2.7 percent in 2008-2009 in the wake of the 2005 tax reform. This can explain the much faster progress in social outcomes in the former than in the latter.

**According to the latest data, however, public education spending as a percentage of GDP in Latin America (at 4.7 percent) is 67 percent higher than in the Philippines (2.7 percent).** This is mainly due to the much smaller size of the budget in the Philippines compared to Latin America although education spending as a percentage of total public expenditure is also lower in the Philippines (13 percent as opposed to 18 in Latin America or 21 percent in Guatemala). Public education spending per student as a percentage of GDP is thus much lower (and falling) in the Philippines despite much slower population growth than experienced in Guatemala.



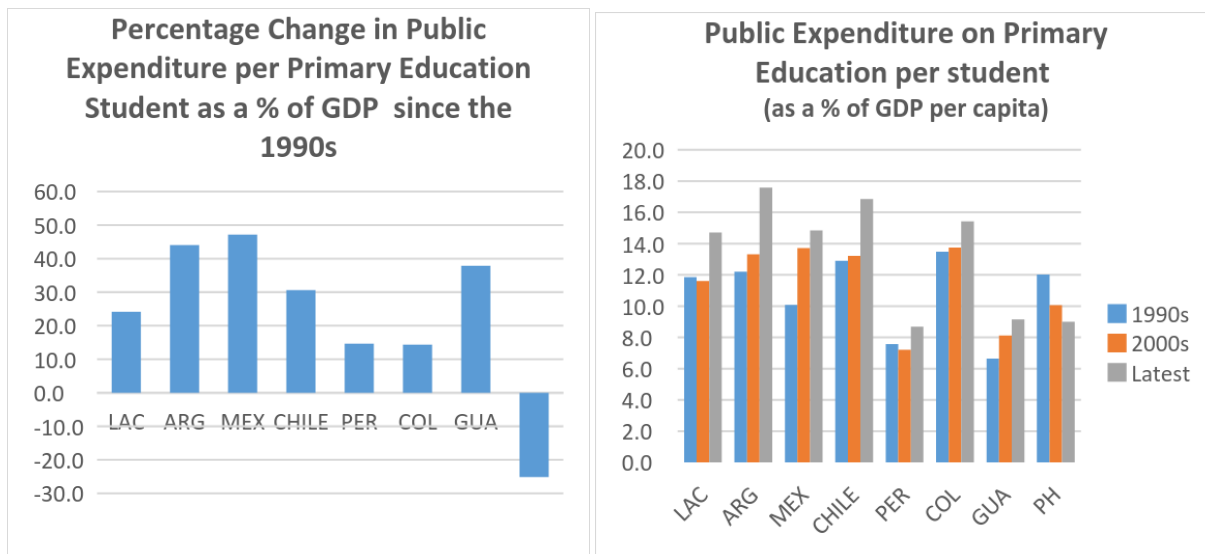
**Moreover, Latin American countries give higher priority to education within their budgets than the Philippines.** The share of government expenditures devoted to education amount to 13 percent in the Philippines and 17 percent in our comparator country sample. Moreover, Guatemala, to compensate for its low expenditure to GDP ratio, devotes a particularly high share of its budget to education –at 21 percent-- (and health), a level that is 60 percent higher than in the Philippines. Part of the explanation for the higher priority devoted to education and health in both regions is the fact that local governments in Latin America seem to devote twice the share of their budgets to education and health than the Philippines (40 versus 20 percent).



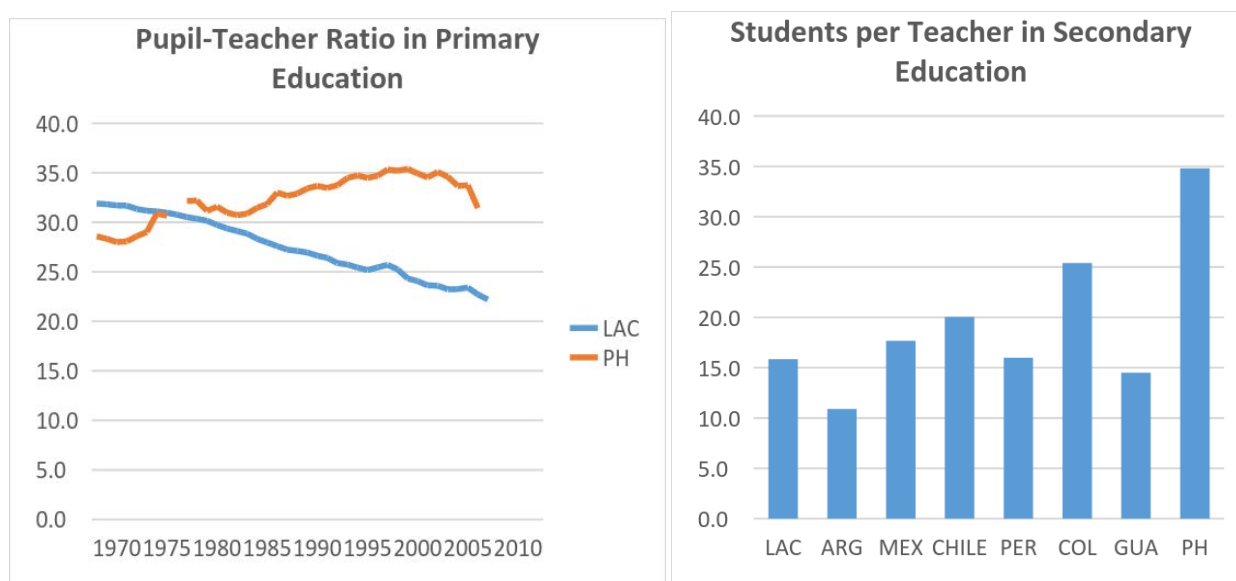


**Primary education spending per student as a percentage of GDP per capita suffered the same fate.**

Guatemala again provides a useful comparator as it almost doubled its public education spending as a percentage of GDP over the same period, rapidly increasing enrollment and completion rates. Between the 1990s average and the latest observation, public spending on primary education per student as a percentage of per capita GDP increased by 38 percent in Guatemala and by 24 percent in Latin America while it declined by 25 percent in the Philippines. These patterns, moreover, cannot be ascribed to fast population growth in the Philippines since, over the 2000s, annual population growth averaged 1.9 percent compared to 2.5 percent in Guatemala.



**As a consequence, the primary education pupil-teacher ratio in Latin America has declined from 31 to 21 since the 1970s while, in the Philippines, it has increased from 29 to 31.** The pupil-teacher ratio in the Philippines peaked in 2000-2005 at around 35, before declining thereafter in the aftermath of the 2005 tax reform and the subsequent (modest) increase in education spending. In Philippine secondary education, the pupil-teacher ratio has increased from 31 to 35 since the 1970s, while in Latin America it has stayed at less than half that level with 15-16 pupils per teacher over the whole period.



**Persistence to grade 5 is ten points lower in the Philippines than in our Latin American comparator country sample and it declined during the budget crunch of 2000-2005, rising thereafter.** The percentage of a student cohort that persisted to grade 5 in the Philippines increased from 64 to 79 percent between 1989 and 2001 and it subsequently declined steadily to a nadir of 74 percent in 2005. This trend follows that of expenditure per student as a percent of GDP, which also peaked in 2001 and declined in the subsequent years to reach its lowest point in 2005, rising modestly after that. In our country sample, only Peru and Guatemala have persistence levels that are similar to those of the Philippines. Persistence to the last grade of primary school in the Philippines followed the same pattern

of decline between 2001 and 2005 (going from 75 to 70 percent) and rising back to 76 percent by 2008 after spending increased again.<sup>27</sup>

**Progression to secondary education in the Philippines followed the same pattern, rising in the 1990s, declining after 2001 and bottoming out in 2004.** The progression rate in the Philippines is similar to that of our Latin American country comparators. The repeater rate, on the other hand, is much lower in the Philippines (at around 1-2 percent) than the Latin American average of 8 percent. It is doubtful, however, that this shows a difference in education quality in favor of the Philippines, since attrition rates, a better gauge of the quality of education, are significantly higher.

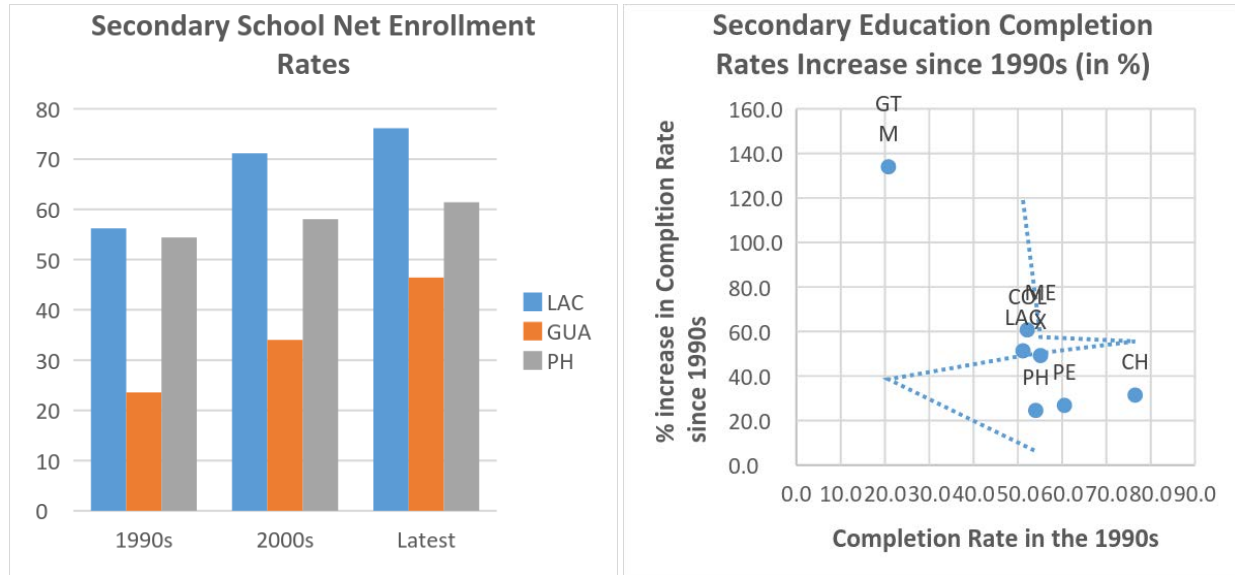
**Enrollment in pre-primary education has increased steadily since the 1970s in both the Philippines and the Latin America region, but it is over 40 percent higher in the latter.** Pre-primary education is increasingly recognized as essential to developing the psycho-social skills needed for success in primary education, especially for under-privileged children. This is one of the reasons why countries across the world are scaling up their pre-primary school programs. Between the 1970s and 2011, the enrollment rate in pre-primary education rose from 12 to 73 percent in the Latin America region. In the Philippines, it rose from 6 to 51 percent between the 1970s and 2009 (the latest observation available). With the ongoing implementation of the “K through 12” program in the Philippines, the enrollment rate in pre-primary education should continue to increase.<sup>28</sup>

**Secondary education enrollment and completion rates increased in all countries, but in the Philippines they did so at a much slower pace than its 1990s level would have predicted.** In the 1990s, for instance, the net enrollment rate was 56 percent in both the Philippines and in the Latin America region as a whole. By the time of the last observation, it had increased to 76 percent in Latin America while it stood at only 61 percent in the Philippines. Similarly, since the 1990s, secondary education completion rates have increased by only 25 percent in the Philippines, but grown by 51 percent in the Latin America region and by 134 percent in Guatemala.

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<sup>27</sup> It also declined steadily between 1983 and 1988, going from 64 to 57 percent.

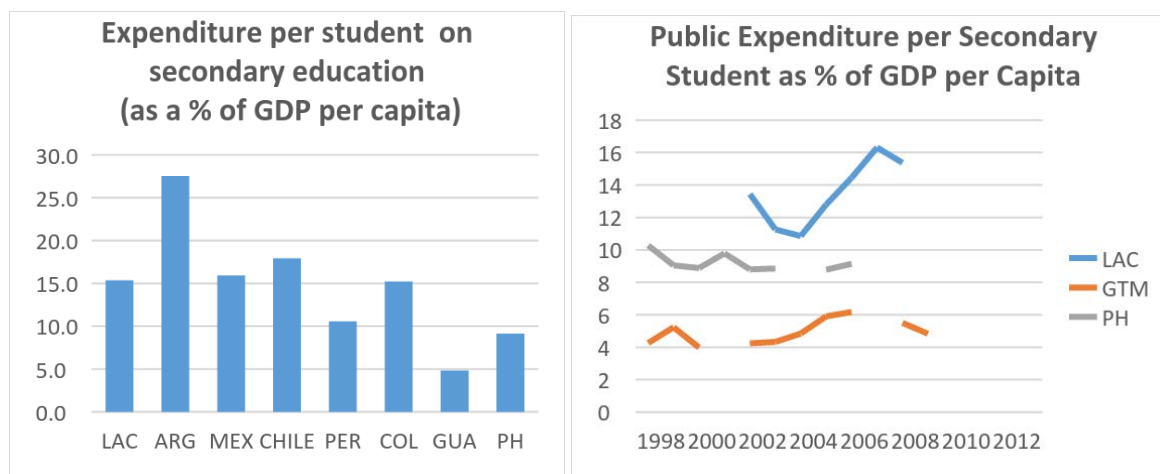
<sup>28</sup> However, because it is the local government at the neighborhood or “barangay” level that is charged with running pre-primary education, resources are extremely scarce, coverage nowhere near universal and common resourcing and standards very hard to set and harder to implement.



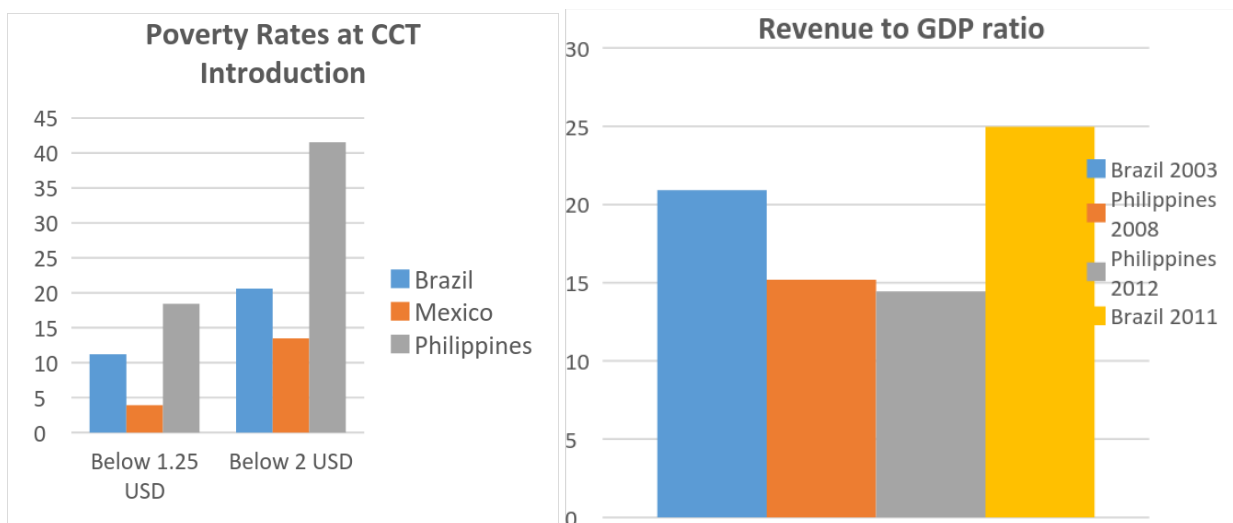
Again, public expenditure can help explain divergent performance as public spending on secondary education is much higher and has grown much faster in Latin America than in the Philippines. Public expenditure on secondary education per student as a percentage of per capita GDP in Latin America is 68 percent higher than in the Philippines. Moreover, in the Philippines, it declined by 11 percent between 2000 and 2006 before rising again slightly over 2007-2008 while, in Guatemala, it increased by 55 percent between 2002 and 2008 before declining again thereafter.<sup>29</sup> Therefore, net enrollment rate patterns –and to an extent completion rates—follow neatly public expenditure trends in both countries.<sup>30</sup>

<sup>29</sup> Expenditure on secondary education in Guatemala began declining in 2009 or 2010 (there is no data for 2009). As expenditure declined, in 2011, the growth rate in the net enrollment rate dropped from an average of 2.5 over the previous 6 years to 0.5 percent.

<sup>30</sup> As was the case with primary education, however, repeater rates are lower in the Philippines (at 3 percent) than in Latin America (at 11 percent).

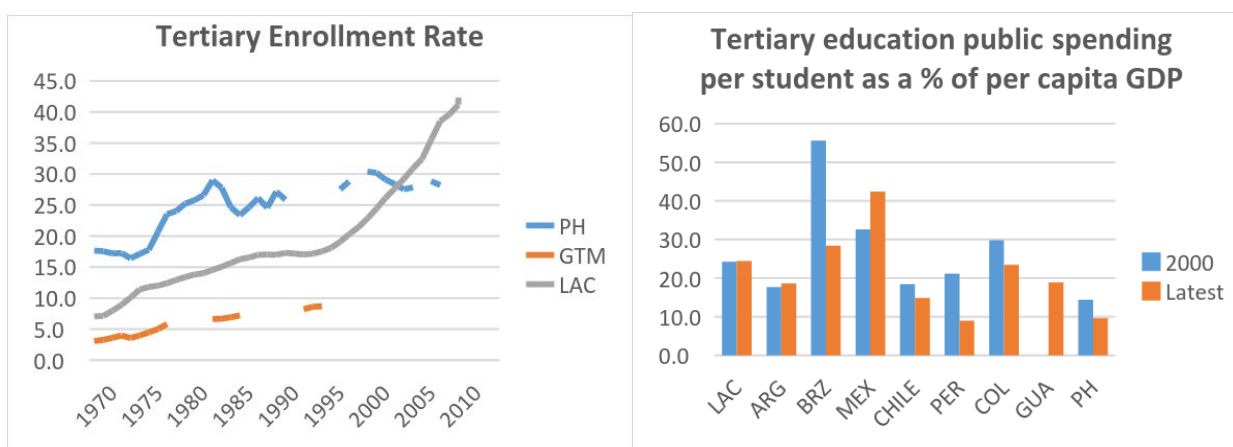


**Both Latin America and the Philippines are supporting the demand side of basic education (and health) through conditional cash transfers (CCTs) for the poorest since the 2000s.** Mexico began implementing its CCT program in 2002 and Brazil (2003) and other Latin American countries followed suit. The Philippines introduced its CCT system in 2008 and has scaled it up since 2010. The level of national income and government revenue of the Philippines when it introduced CCTs, however, was significantly lower and the poverty rate much higher than in Latin America. In the absence of a tax reform to substantially raise fiscal revenues, this disparity raises the question of whether these resources may not have been more usefully devoted to the supply side of education and health systems.



**Tertiary enrollment in the Philippines is lower and has grown slowly than in Latin America and spending per pupil as a percentage of GDP has dropped and is only 40 percent of Latin America's.**

Between 2000 and 2008, tertiary education spending per pupil as a percentage of GDP dropped by 32 percent in the Philippines, going from 60 to 40 percent of the Latin American level. By 2008, it was below all of our country comparators except Peru. Since the 1990s, tertiary enrolment rates in Latin America have grown by 134 percent while in the Philippines they have risen by only 3 percent. The increase in Latin America has taken place in all of our comparator countries, with the lowest increase (50 percent) taking place in Peru and the highest (155 percent) in Chile. Low tertiary enrollment rates and expenditure levels coupled with low levels of FDI do not bode well for productivity growth, especially for a country with a potential comparative advantage in English-speaking skilled labor.



**According to the World Economic Forum’s Competitiveness Index, the Philippines does very poorly in health and primary education and very well in high-end education and training.** The country’s overall ranking, at number 59 (out of 148 countries), is relatively good, having jumped up 19 places since 2007-2008 and being ahead of the number 66 average ranking of our Latin American comparator country sample. On the one hand, health and primary education are some of the areas in which the Philippines has the lowest ranking –number 96. This poor performance is due to rankings of 130 in number of tuberculosis cases (only 17 places from the absolute bottom), business impact of tuberculosis (number 116), primary education (108) and life expectancy (104). On the other hand, the Philippines has an excellent ranking in number of HIV infection cases (11) and very good rankings in extent of staff training (27), quality of management schools (39) and quality of the educational system (40). This high dispersion of rankings points to the country’s overall duality—doing very well at the top and very weakly at the bottom of the human development and income distribution spectrum.

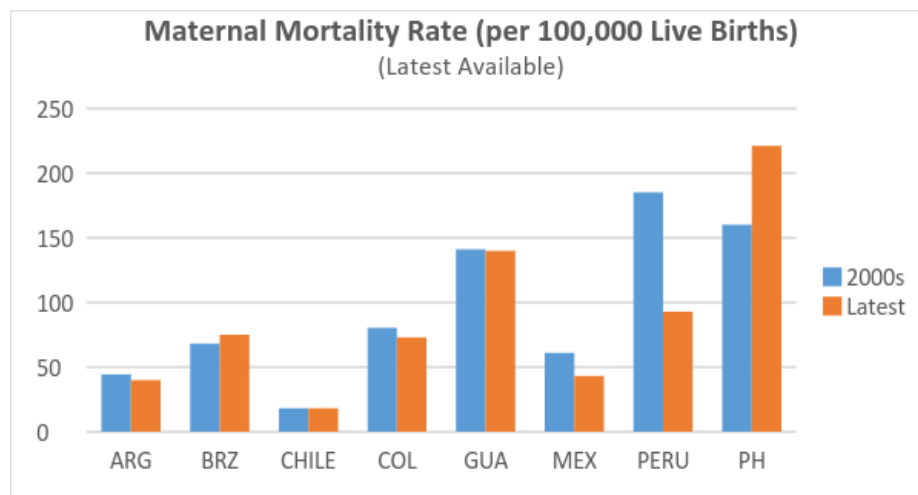
**The Philippines lags the most in the health area, with maternal, infant and child mortality rates being multiples of the average level of our Latin American comparator country sample.** As of 2011, maternal mortality stood at 220 deaths per 100,000 live births, more than three times the average level of our Latin American comparator sample, 58 percent above the level of Guatemala (the worst performer in our Latin American sample) and 38 percent above the Philippine level in the 1990s. Countries like Sri Lanka, Malaysia and Turkey have cut maternal mortality rates in half since 1990 by ensuring births take place in birthing facilities and small hospitals and are assisted by professional midwives with services provided for free at least to those who can’t pay (WHO 2009: 7). It is these kinds of interventions that are needed for poor –and all--mothers in the Philippines.

**The percentage of pregnant women receiving pre-natal care and the percentage of births attended by a skilled health staff has increased in both regions, but is higher in Latin America.** The percentage of women receiving pre-natal care in Latin America (at 96 percent on average) is near-universal. In the Philippines, however, it stood at 78 percent in 2011, down from 91 percent in 2008.<sup>31</sup> In the 1990s, the percentage of births attended by skilled health staff in the Philippines and Latin America stood at 52 and 75 percent respectively. By the time of the latest observation, it had increased to 72 and 86 percent

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<sup>31</sup> The increase in 2008 may have been due to the introduction of the CCT program requiring a pre-natal check-up; low quality and availability of pre-natal care may help explain the subsequent decline. This is consistent with the 2012 program evaluation conclusion that greater care needs to be devoted to the supply sides of both education and health since there are indicators that a greater number of visits to health centers, for instance, has not increased children immunization rates.

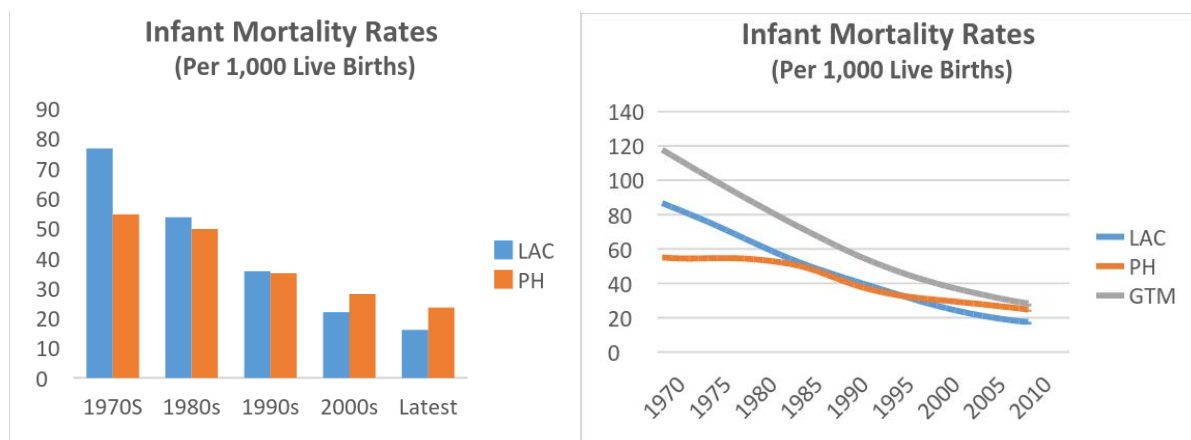
respectively.<sup>32</sup> It would be of great use to have data on the percentage of women who give birth in health facilities –as this is what is genuinely required to bring down maternal mortality. However, the bar in the MDGs has been set so low that all that is available is the MDG indicator of percentage of births attended by a skilled health staff. The staggeringly high maternal mortality rate in the Philippines is one piece of evidence that the current standard is insufficient to significantly bring down maternal mortality rates. It is most likely that in Latin America, a very high percentage of women gives birth in health facilities. This data, however, is not readily available.



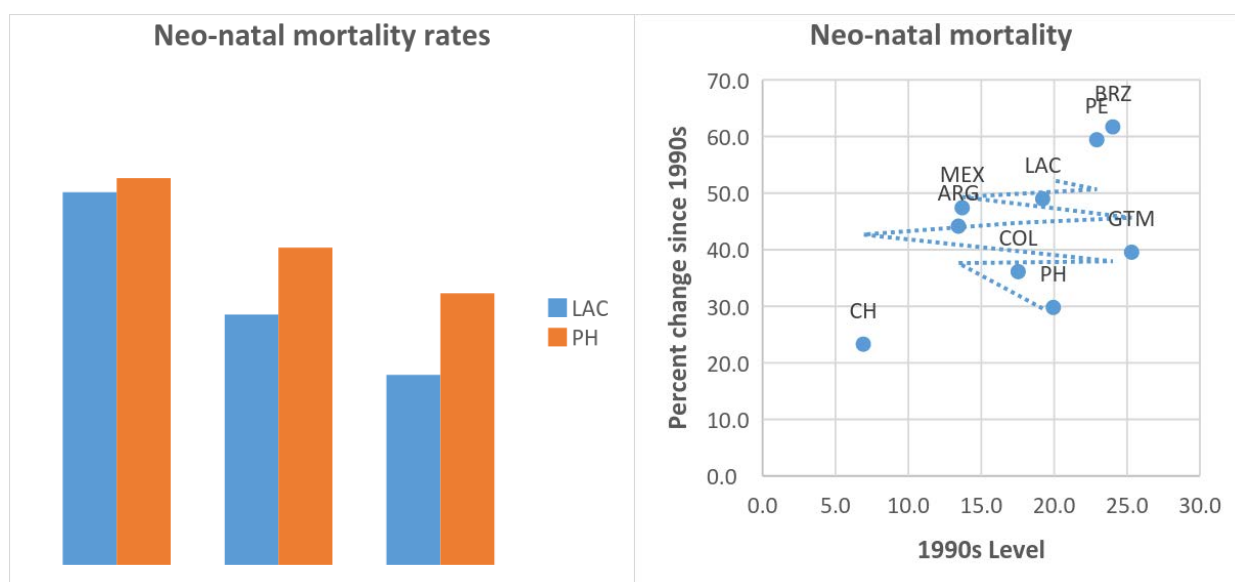
**Infant mortality rates in the Philippines have come down much more slowly than in Latin America and now stand 47 percent above the region's average.** Even the countries with the historically highest infant mortality rates, like Guatemala, have by now caught up with the Philippines.

<sup>32</sup> Many births in Latin America, however, are not only attended by skilled staff, but take place in a hospital. The much higher percentage of births that take place in homes (especially slum shacks) in the Philippines rather than hospitals likely explains the exorbitantly high maternal mortality rate in the country.

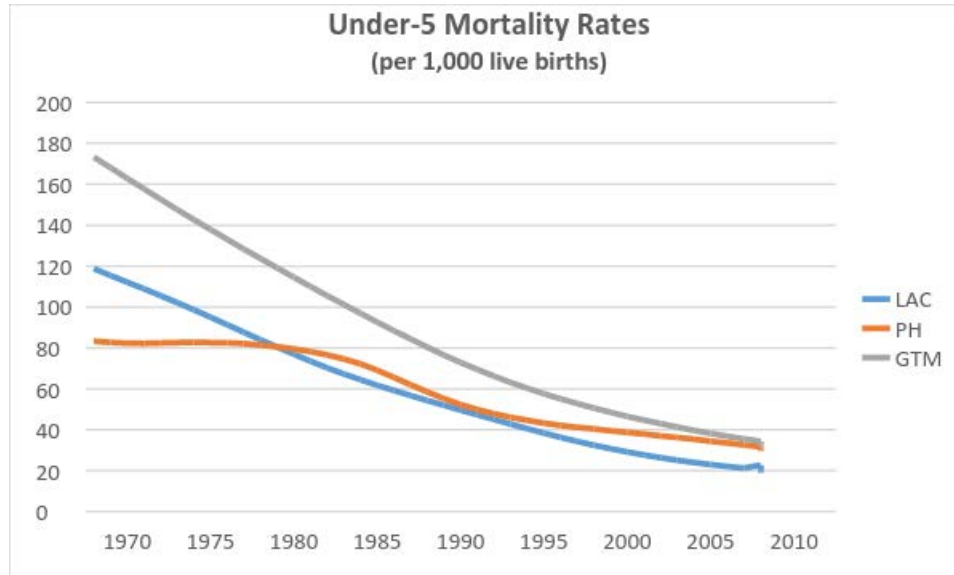




**Neo-natal mortality rates in the Philippines have been coming down at a slower rate than in Latin America and are below the trend line in improvement given their 1990s level.** In the 1990s, the neo-natal mortality rate stood at 19 per 1,000 live births in both the Philippines and Latin America. However, whereas in Latin America, they have fallen by 50 percent since their 1990s level, in the Philippines they have only declined by 30 percent and are currently 43 percent above the Latin American average.

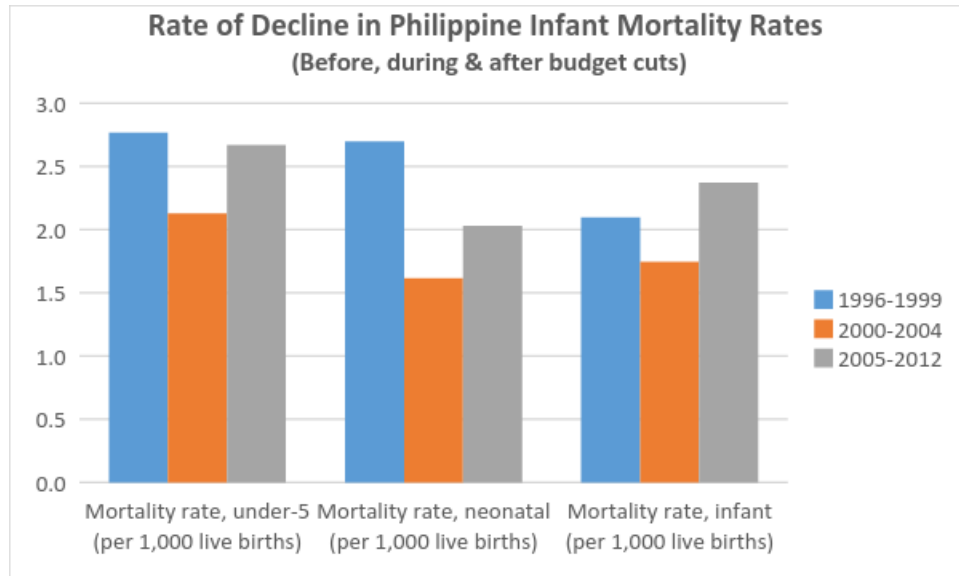


**Similarly, in the 1970s, under-5 mortality rates in the Philippines were 25 percent below the Latin American level while, by now, they stand 57 percent above.** Guatemala again provides a good comparator. Whereas in the 1970s, its under-5 mortality rate was 82 percent above the Philippine level, by 2012, it had already caught up with it (at 32 deaths per 1,000 live births compared to 30 in the Philippines).

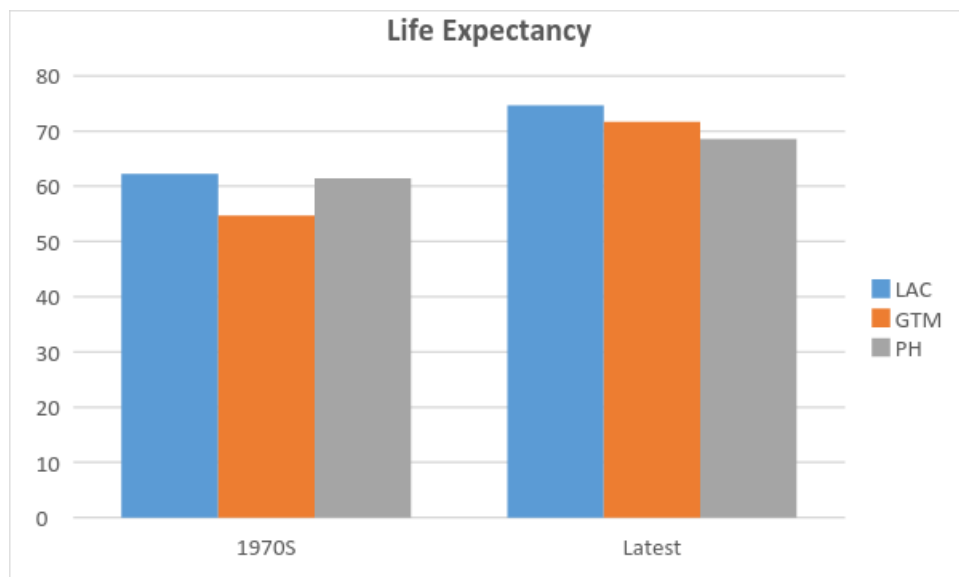


**The rate of decline of neo-natal, infant and child mortality rates in the Philippines slowed down**

**significantly during the 2000-2004 budget crunch and began accelerating thereafter.** As was the case with education outcomes, health outcomes seem to have reacted with great sensitivity to expenditure trends. The rates of decline in under-five, neo-natal and infant mortality rates were 23, 40 and 16 percent lower over 2000-2004 than they had been over 1996-1999. As expenditure began increasing again, over the 2005-2012 period, the rate of decline increased again by 25, 26 and 36 percent compared to the 2000-2004 period. These trends are hopeful as they indicate that expenditure increases *do* result in improved outcomes and, if a tax reform prospers in the coming years, health (and education) outcomes can swiftly pick up with sector spending.

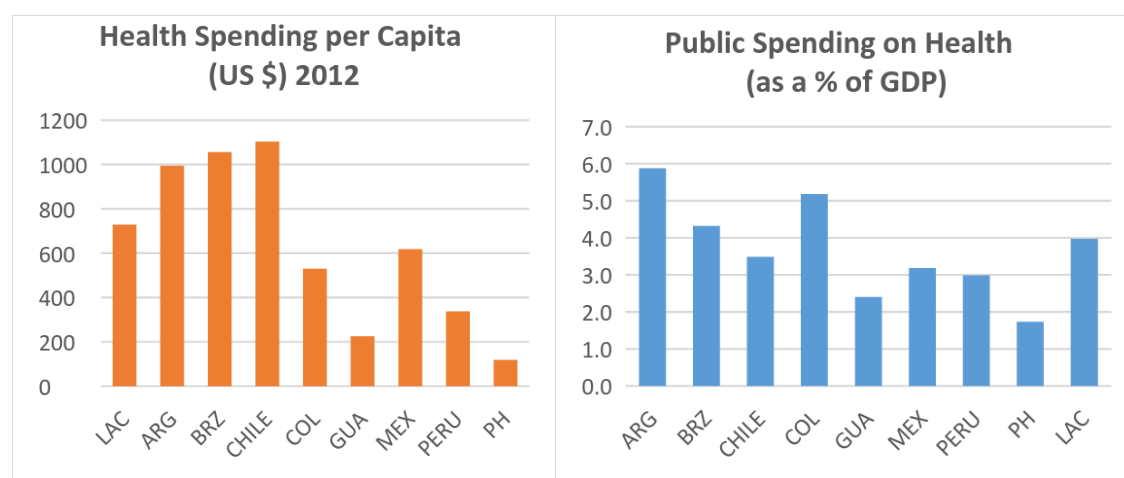


**Though, in the 1970s, life expectancy in Latin America was only one year above the Philippine level, by 2012, it had six additional years.** In the 1970s, Guatemala was 6 years below the life expectancy of the Philippines while, by 2012, it was three years above it. The same pattern is observable in other countries. The fact that HIV infection and violent death rates are significantly lower in the Philippines than in Latin America points to weaknesses in health care, nutrition and basic infrastructure as the reasons behind slow progress in improving life expectancy in the Philippines.<sup>33</sup>

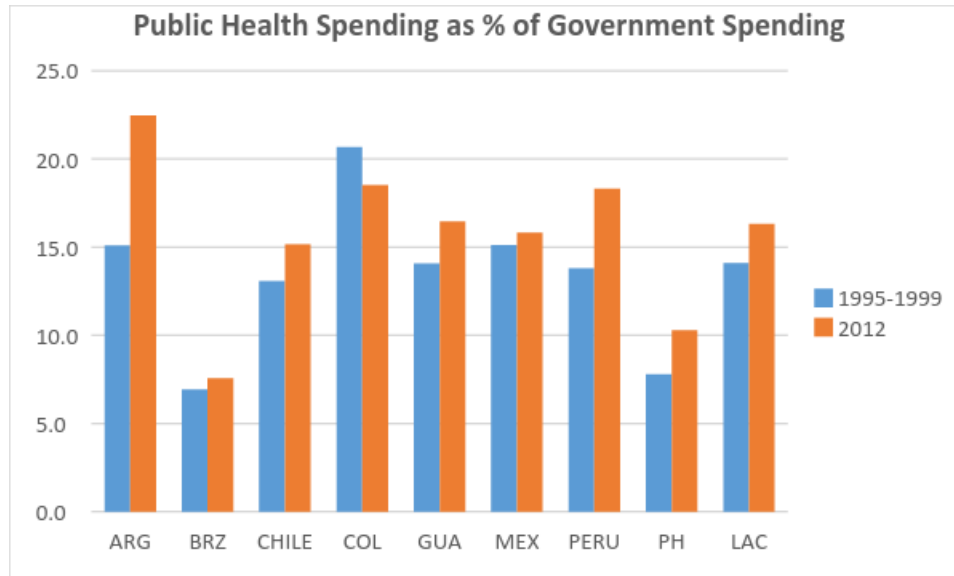


<sup>33</sup> The Philippines ranks 11 out of 148 countries in HIV infection rates in the World Economic Forum Competitiveness ranking. This compares with an average ranking of 79 in our Latin American country average.

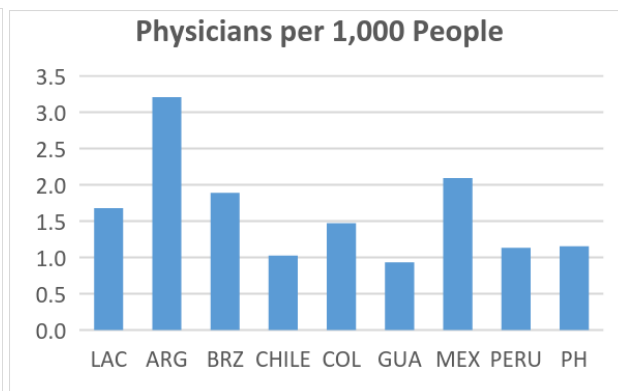
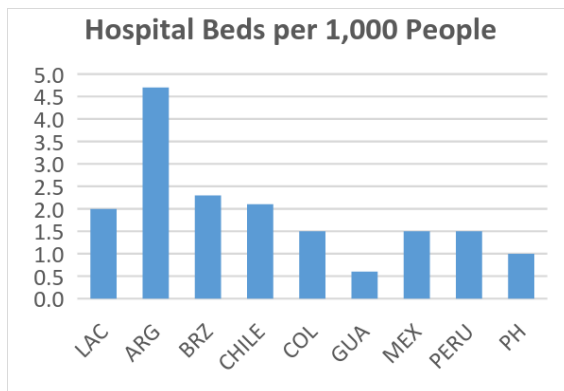
**In 2012, total per capita expenditure on health in Latin America (at 729 USD) was six times the level of the Philippines (119 USD).** Even Guatemala doubles the amount of health expenditure per capita of the Philippines. Public health expenditure as a percentage of GDP also exhibits a large gap, standing at 1.7 percent in the Philippines compared with 4 percent in Latin America and 2.4 percent in Guatemala. The 2012 level in the Philippines is the highest it has been for the period for which data is available (since 1995); after declining in the budget crunch of 2001-2004 it began to recover in 2005.



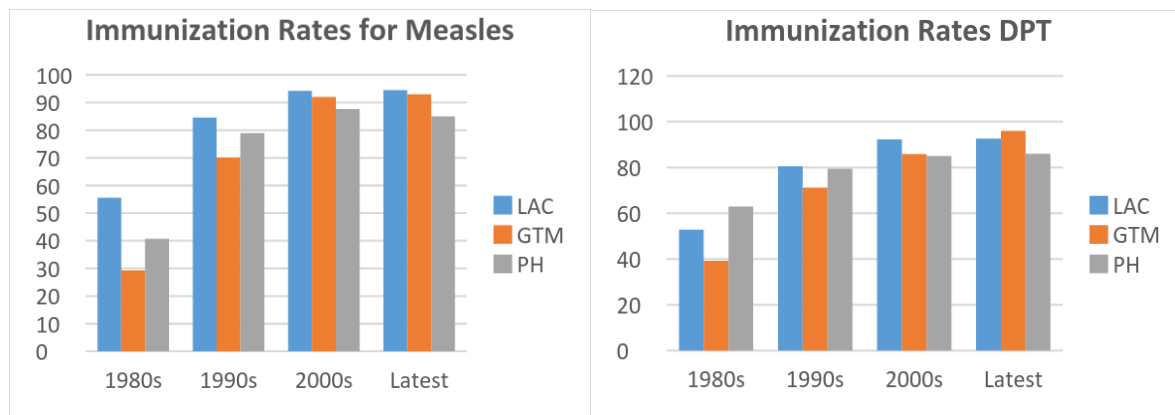
**In addition to having much larger expenditure-to-GDP ratios than the Philippines, most Latin American countries devote much larger shares of their budgets to health.** In 2012, the average share of public expenditure devoted to health by our Latin American comparators was 16 percent, 60 percent higher than the Philippine level of 10 percent. That, however, was a significant improvement for the Philippines as it was 38 percent higher than it was in 1995 or in 2008 and it has been on a steady rise since 2009. A country like Guatemala, with a similarly low public expenditure to GDP ratio, manages to devote a share of its budget to health which is 60 percent above the level of the Philippines. In 2012, total health spending in the Philippines, at 4.6 percent of GDP, was also well below the Latin American average of 7.7 percent.



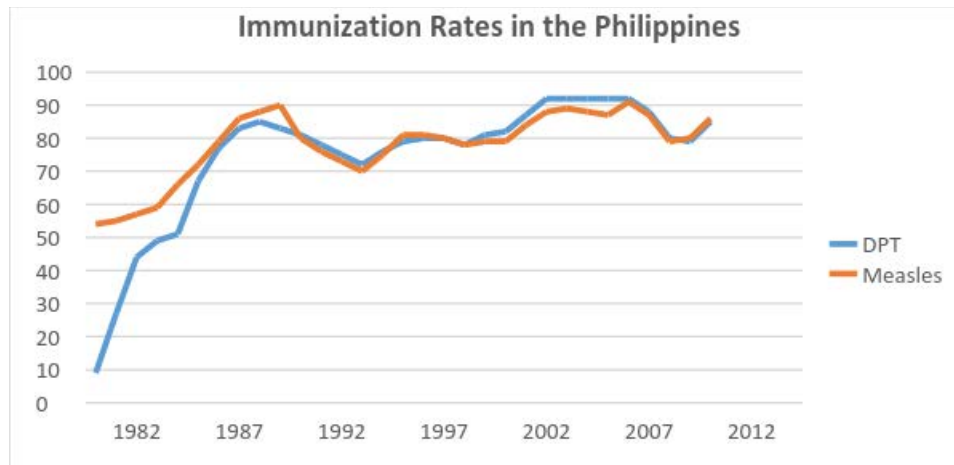
**The number of beds and doctors per 1,000 people in the Philippines is well below the Latin American average while the number of nurses and midwives seems to be much higher.** In 2012, the number of hospital beds per 1,000 people in Latin America (2) was double that in the Philippines (1). Similarly, the number of physicians per 1,000 people was 46 percent higher in Latin America. Data on the number of nurses and midwives per 1,000 people is sketchy, but it seems to be higher in the Philippines, with the World Bank's World Development Indicators recording a level of 4.2 in the Latin America region in 2010 compared to 6 in the Philippines in 2004. This is a hopeful indicator as the presence of nurses and midwives has been found to be more strongly correlated with health outcomes than the number of physicians (World Bank, 2010). However, it is not clear whether the Filipino nurses actually work in the Philippines or are deployed abroad as overseas foreign workers not benefitting the Filipino population.



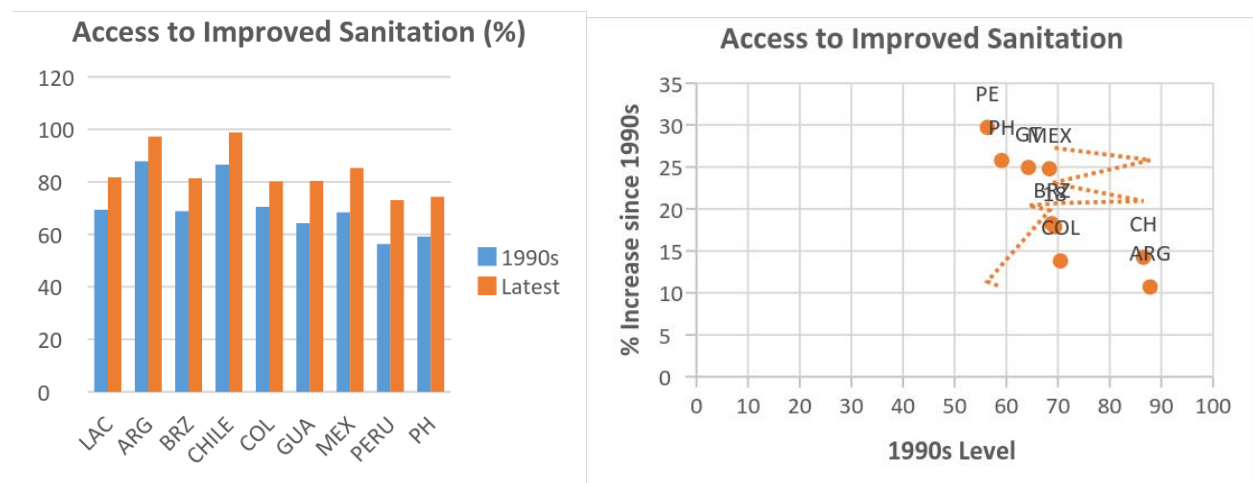
**Immunization rates have grown rapidly in both Latin America and the Philippines, but they are higher in Latin America.** Even countries that used to have lower immunization rates than the Philippines like Guatemala have surged ahead of it by now. In the 1980s, for instance, the measles immunization rate in Guatemala was 38 percent below the Philippine level while now it stands 9 percent above. By the time of the latest observation, immunization rates in Latin America were almost universal (95 percent for measles and 93 percent for DPT). In the Philippines, however, they stood at 86 percent for DPT and 85 percent for measles.



**Moreover, immunization rates in the Philippines declined markedly after the onset of decentralization in 1991 and they are only now nearing again their 1990 level.** As has been the case in many countries, decentralization of health care in the Philippines has negatively impacted many areas including vaccination. While vaccination rates had risen steadily throughout the 1980s, they declined throughout the 1990s. Measles vaccination rates increased from 9 to 85 percent between 1982 and 1990. By 2000, however, they had fallen to 78 percent. They increased again between 2002 and 2009, but have been declining since then, going from 92 percent in 2008 to 85 percent in 2012.



**Sanitation levels have been increasing in both Latin America and the Philippines, but are lower in the latter.** Improved sanitation facilities are essential to hygienic living conditions and hence to health and overall wellbeing. Access to improved sanitation facilities has risen from 69 to 82 percent in Latin America and from 59 to 74 percent in the Philippines between the 1990s and the latest observation. The only country in our sample with the same level of access to sanitation as the Philippines is Peru (at 73 percent), with Guatemala already standing at 80 percent. The percentage increase in the Philippines is just on the expected trend line given its level in the 1990s.



**Access to an own water source in the Philippines—at 48 percent of the population—is extremely low** (World Bank 2010). Access to an own water source is critical to health and overall being, contributing to greater water quality, lower diarrheal diseases and lower prices for consumers aside from saved time

and convenience.<sup>34</sup> However, the measure used since the onset of water privatization by the World Bank and other development agencies is not access to an own water source (or access to piped water), but rather “access to an improved water source.” This indicator only measures physical proximity to a water source and not real access to water (just as proximity to a bank does not ensure access to money). Because of this definition, there is unfortunately no easily-accessible international data on the critical indicator of access to an own water source/in-house piped water.<sup>35</sup>

**The Philippines does better than Latin America in other aspects of social opportunities such as gender and race.** As regards education, for instance, the Philippines enjoys the same equality across genders as our Latin American country samples except Peru and Guatemala, which have a significantly lower education rate for women and girls. Whereas Guatemala and Peru have an 11 and 10 point literacy gap between men and women and our other sample countries have the same rate for both genders, the Philippines has a one point higher literacy rate for women.

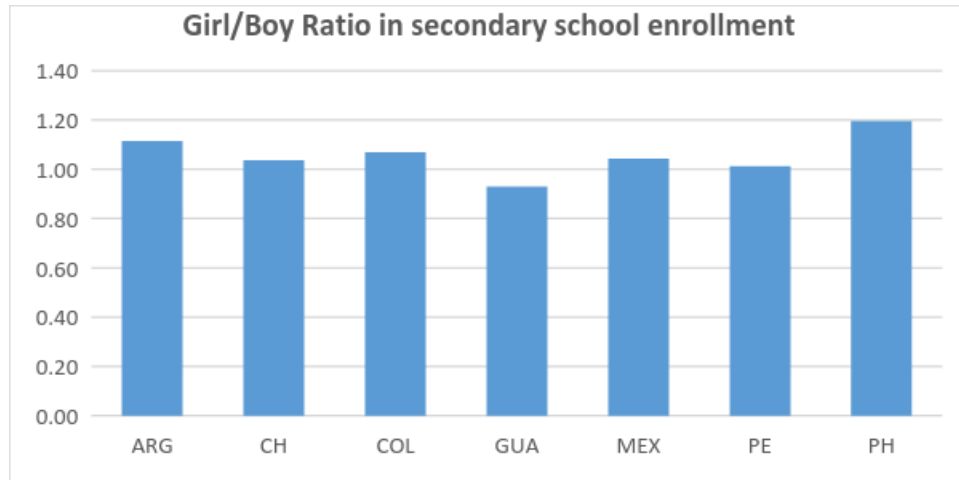
**Enrollment gaps in primary education between boys and girls are practically nil, but the Philippines has the highest girl/boy ratio in secondary school enrollment in our country sample.** Enrollment in primary education now exhibits no significant gaps across genders in any of our sample countries. However, the girl/boy ratio in secondary education stands at 1.2 in the Philippines and at 1.0 in our Latin American country sample, indicating absence of bias against girls in the Philippines probably combined with lower interest in formal education and greater likelihood to engage in work at that age by boys. The women to men ratio in tertiary enrollment rates—at 1.2—is the same in the Philippines and in our comparator country average.

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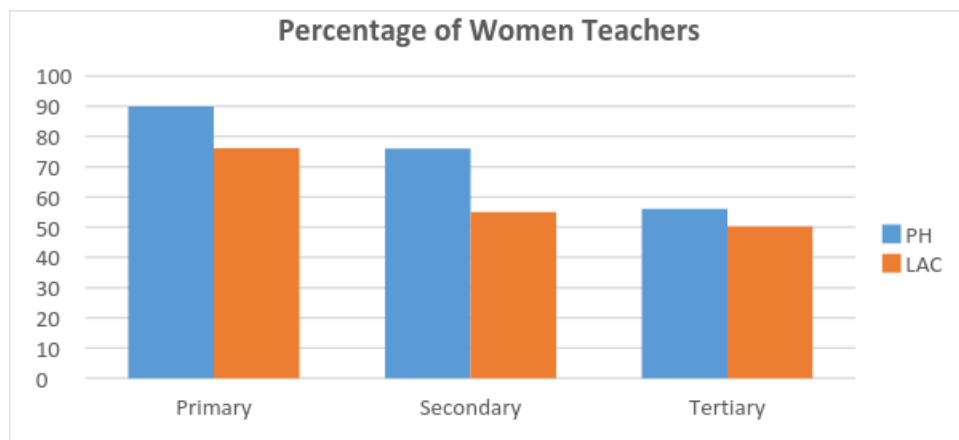
<sup>34</sup> A recent study of Vietnam, for instance, found that households connected to a piped water supply had consistently improved drinking water quality, were at reduced risk of diarrheal diseases and paid less and reported greater satisfaction than those relying on other, non-piped sources. (USAID 2010). The main difference affecting differential prices is that pipe water tends to be a public and non-piped water a private monopoly.

<sup>35</sup> “Access to an improved water source” stands at 92 percent in the Philippines and at 94 percent in Latin America.



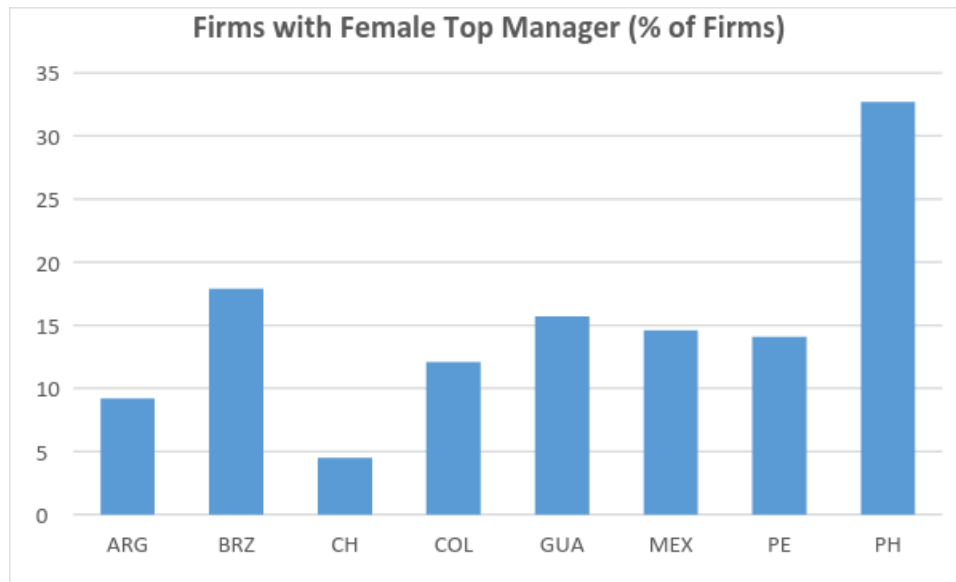


**The percentage of women teachers at all levels of education in the Philippines is higher than in our Latin American country sample.** Teaching being a preferred profession for women, absence of discrimination leads to a higher percentage of women in the profession than men. This is indeed the case both in the Philippines and in Latin America, especially in primary and secondary education. Moreover, the percentage of women teachers in the Philippines is 21, 16 and 6 points higher in primary, secondary and tertiary education respectively than in Latin America. Our sample countries with the strongest discrimination against women –Guatemala, Mexico and Peru—also have percentages of women teachers in primary and secondary education that are around 20 points below the average of our other Latin American sample countries and are the only ones not to provide data on the percentage of women teachers in tertiary education. In fact, when these countries are taken out of our Latin American comparator group, the edge of the Philippines disappears except for primary education.

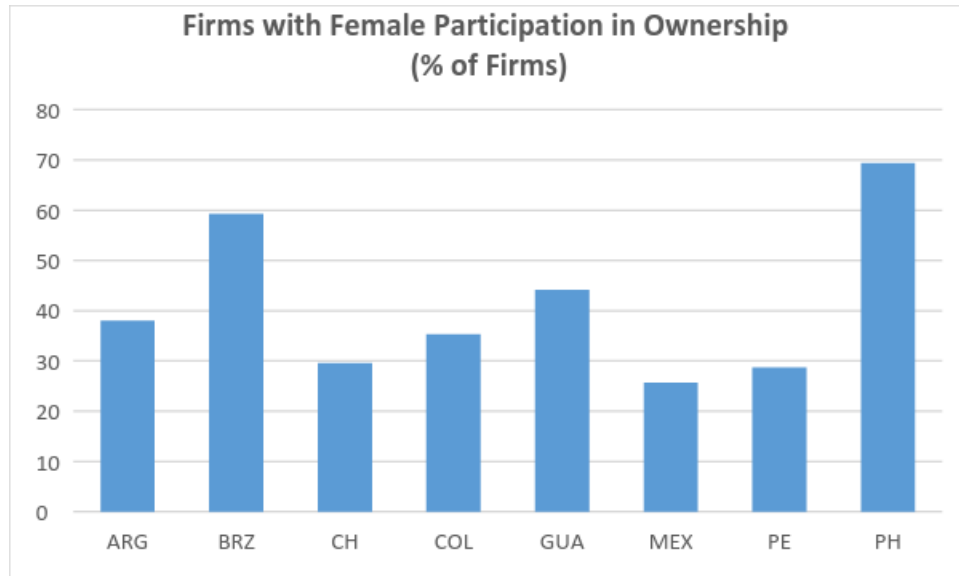


**A further sign of the better social opportunities for women in the Philippines than in Latin America is the much higher percentage of women who are top managers in a firm.** According to the latest data

available, the percentage of top managers in a firm who are women in the Philippines is 33 percent compared with only 12 percent in our Latin American comparator sample. We have also previously mentioned that the percentage of members of Parliament and in management positions in government and private firms who are women, at 55 percent, is almost twice the 28 percent of our Latin American comparator average.

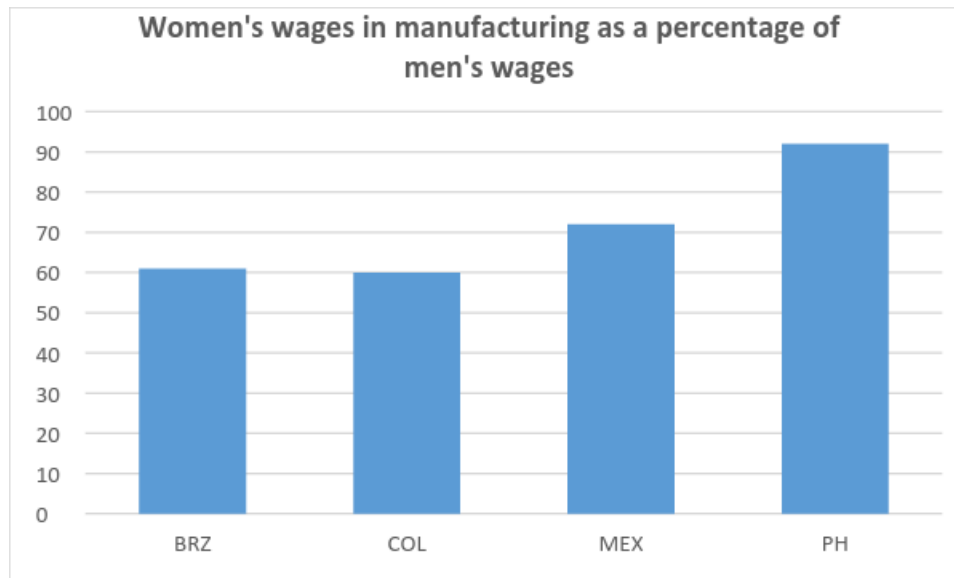


**Similarly, the percentage of firms with female participation in ownership is almost twice as high in the Philippines as in our Latin American country sample.** As of 2009-2010, the percentage stood at 69 percent in the Philippines while it was only 37 percent in our Latin American comparator sample, being highest in Brazil (59 percent) and lowest in Mexico (26 percent).



**Women’s wages in manufacturing as a percentage of men’s wages in the Philippines, at 92 percent, are among the highest in the world and 43 percent above our Latin American comparator average.**

The share of women’s to men’s wages in manufacturing in our Latin American comparator countries is at a very low 64 percent, with a highest of 72 percent in Brazil and standing at 61 percent in Mexico and 60 percent in Colombia (the other countries do not provide data). This shows that whether one looks at the top echelons of the labor market –women in management positions or percentage of firms with female participation in ownership—or at the average worker –as represented by wages in manufacturing—, the social opportunities and, more broadly, social justice for women is at a much more advanced stage in the Philippines than in Latin America.



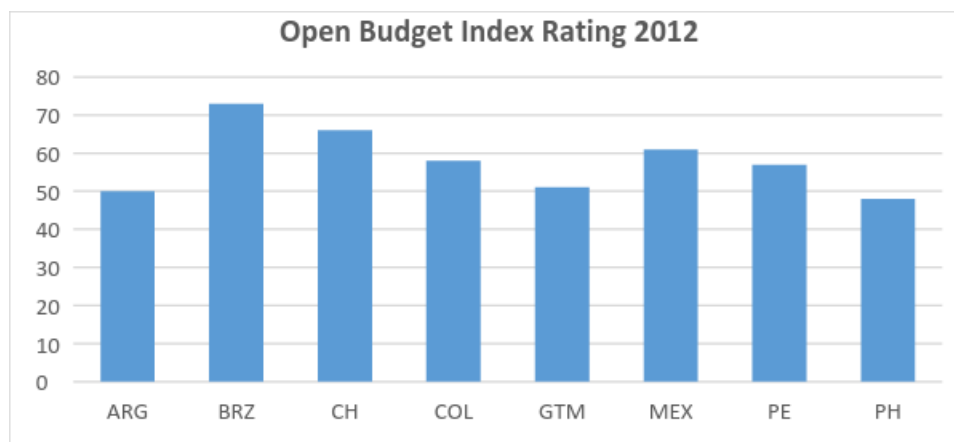
### Transparency Guarantees

Transparency guarantees relate to public and private sector openness toward society. Information availability in a relevant, timely, accurate, and easily understandable manner is an important value in and of itself, contributing directly to the wellbeing of people. In addition, it is an important instrumental value for a well-working democracy and market system.

**The Philippines does worse in the Open Budget Index (OBI) than any of our Latin American country comparators.** In 2012, the latest year for which data is available, the OBI rating for the Philippines was 48, below all of our Latin American country comparators, which had an average rating of 59. Between 2008 and 2010, the Philippines' rating had improved from 48 to 55, but by 2012 it was back down to 48. The areas where the Philippines does the worst are those related to the executive's budget proposal, including the pre-budget statement, the mid-year budget review, the year-end report explaining discrepancies between budget and actual expenditures, the explanation of how audit findings are being addressed and the citizens' budget.<sup>36</sup> Over the 2008 to 2012 period, Argentina, Chile, Colombia,

<sup>36</sup> The sub-areas in which the Philippines receives the worst rating (d) in 2012 are: multi-year estimates of both revenue and expenditure, statement of policy goals in executive's budget proposal, macro sensitivity analysis, information on financial and non-financial assets of the government, arrears, contingent liabilities, presentation of nonfinancial data for program assessment, performance indicators for expenditure programs, use of performance indicators in conjunction with performance targets, issuance of a pre-budget statement by the executive to the public, midyear budget review discussing changes in economic outlook since the budget was enacted, updated expenditure and revenue estimates, year-end report explaining the differences between the enacted levels of funds intended to benefit directly the country's most impoverished populations and the actual outcome and outcome for extra-budgetary funds, executive report on how it has addressed audit findings needing remedial

Guatemala and Mexico improved in their budget openness rating while deterioration took place in the Philippines, Peru and –just marginally—Brazil.



**As regards extractive industries, the Philippines is a candidate to the Extractive Industries Transparency Initiative (EITI) while Guatemala and Peru are already EITI compliant.** Extractive industries are particularly sensitive due to their high and concentrated rents, their history of mismanagement and corruption, their often poor returns to natural resource-rich countries and their poor and their impact on their immediate human and geographical environment. To improve this dismal record, the EITI aims to enhance the transparency and sound management of government and corporate dealings in exploiting natural resources. How well countries do in the EITI index is a good indicator of transparency and general good governance in the sector. Out of our Latin American country sample, only two countries have approached the initiative –Peru and Guatemala—and they are both by now compliant with EITI requirements. The Philippines is a candidate country since 2012, but it does not yet comply with EITI requirement and is due to produce its first EITI report in 2015.

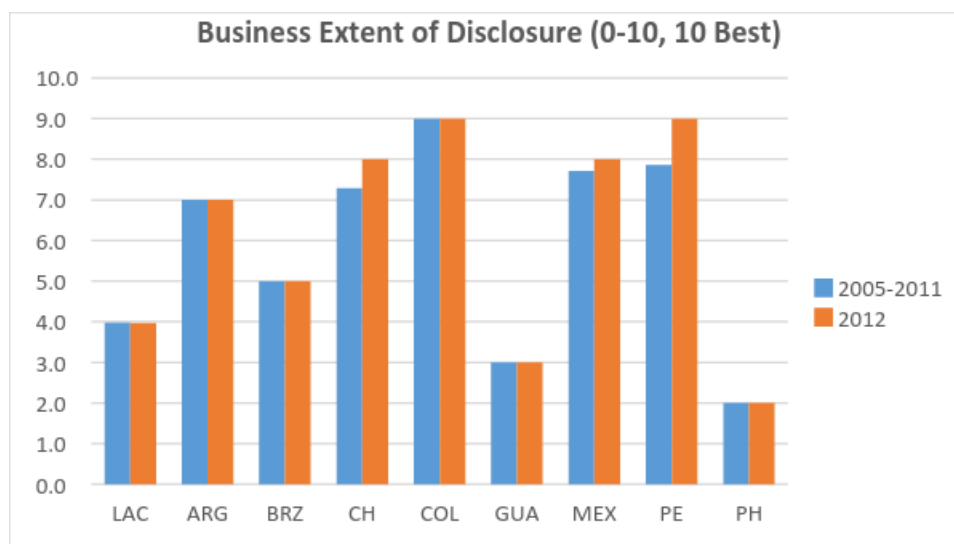
**The Philippines receives a lower rating than our Latin American country comparators as regards open government, but has improved since 2010.** The World Bank’s World Justice Project rates countries across the world on the quality of their justice systems (with 0 being the worst and 100 the best ratings).

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action, audit reports of the annual accounts of the security sector provided to the legislature, existence, quality, consultation and dissemination of the “citizens’ budget.”

One of the sub-indices included in the project is “open government.” In that index, the Philippines is rated at 46. Our Latin American sample, on the other hand, averages a rating of 52, with the lowest-rated country being Guatemala, which like the Philippines, receives a rating of 46.<sup>37</sup> The Philippines, however, has seen an improvement in its open government rating since 2010 when it stood at 38.

**The extent of business disclosure in the Philippines is only half of the Latin American average and has not improved since 2005.** It is rated at 2 compared to an overall Latin American average of 4 and an average in our comparator country sample of 7 (with 0 being the lowest and 10 the highest). Moreover, the rating of some of our Latin American comparator countries has improved over time. For instance, between the 2005-2011 average and 2012, Chile and Mexico’s ratings have increased from 7 to 8 and Peru’s from 7 to 9 while the Philippines has remained at a very low 2. This poor rating of private sector openness in the Philippines may be due to the degree of market concentration and lack of competition discussed above which does not put firms under pressure to perform either price-wise or by providing appropriate information to their consumers and investors.



<sup>37</sup> The open government sub-index assesses the following dimensions: a) the laws are publicized and accessible; b) the laws are stable; c) right to petition the government and public participation; and d) official information is available on request. The Philippines does better than the LAC average in the first dimension, but worse in the other three.

## **Protective Security**

**Security, physical as well as economic, is one of the most fundamental needs of a human being.** The origins of political systems have traditionally been linked by philosophers, as well as arguably by history, with the physical protection of human beings from the aggression of men.<sup>38</sup> In Hobbes' well-known words, without the social contract, "man is a wolf to man." When the most restrictive sets of functions were designed for states in the 18<sup>th</sup> century, protective security was always at their core. Therefore, ability to ensure its citizens' security—from internal as well as external threats—has typically been regarded as the most fundamental responsibility of the state. As history has progressed, the state has also developed the function of protecting its citizens from the vulnerabilities intrinsic to a market system, such as unemployment, risks such as illness or natural disasters and old age. Distributing risk at a society-wide level is most effective while the collective willingness of a society to provide for those most in need is a key hallmark of its social ethics.

**According to the 2014 global peace index, the Philippines ranks number 134 compared to an average ranking of 89 for our Latin American comparator country sample.** The Global Peace Index is elaborated by the Institute for Economics and Peace and it gauges global peace using three broad themes: the level of safety and security in society; the extent of domestic or international conflict; and the degree of militarization of each country. According to the 2014 report, the Philippines exhibits a particularly strong "peace deficit" and it scores in the bottom quartile for several indicators, including internal conflict, level of violent crime, political terror and terrorist activity. The recently signed peace agreement with Mindanao should provide a welcome boost to the country's peace in the coming years. Eliminating political terror requires a commitment by government agencies such as the police and the military to the protection of human rights, including of people whose opinions and activities come against government views and the interests of the country's oligarchy. Tackling violent crime will require social justice and a greater investment in security spending. The Philippines seems to have one of the lowest numbers of police per capita in the world, possibly due to decentralization and privatization.<sup>39</sup>

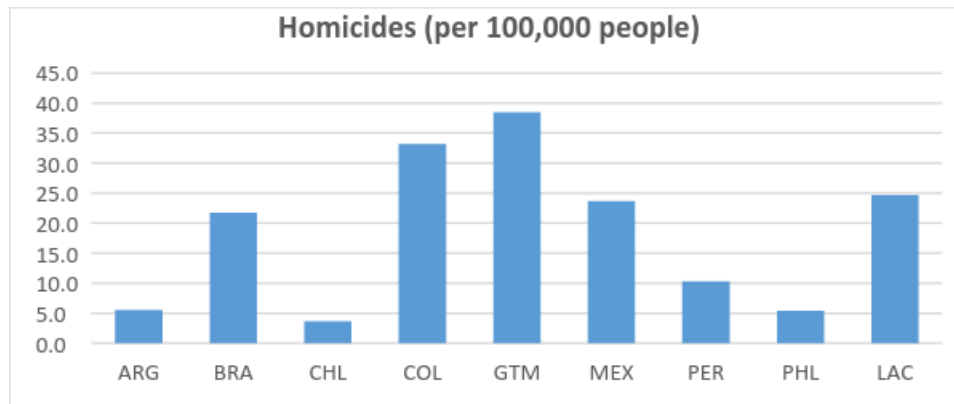
**As regards crime strictly speaking, the Philippines does relatively well with a homicide rate about one fourth of the level of Latin America's.** At 5.4 homicides per 100,000 people, the homicide rate in the

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<sup>38</sup> At the same time, particularly but not exclusively in non-democratic societies, the state itself often becomes one of the main sources of insecurity and violence against its citizens and the citizens of other states (through persecution, war and state terrorism).

<sup>39</sup> The Philippines seems to have 138 police per 100,000 people only compared with 558 in Argentina, 282 in Brazil and Chile, 323 in Colombia, 366 in Mexico and 352 in Peru (various sources).

Philippines is comparable to Argentina's and only above Chile's. The Latin American regional average is 25 per 100,000.<sup>40</sup> Moreover, in the Philippines it has come down from 8 percent over 1995-2000 and 7 percent in the 2000s. This is likely due to the impact of the drug trade and the strategies followed in the war against drugs in the United States and Latin America with their ineffectiveness and their dramatic toll on Latin American lives. The cause of death by injury in the Philippines is also lower, at 8 percent of total deaths compared to 12.5 percent in Latin America.



**The effective protection of the “right to life and security of the person” as well as its “rule of law,” however, are rated significantly worse in the Philippines than in Latin America.** The World Justice Project rates the Philippines well below our country comparators as regards the effective guarantee of the right to life and security of the person (at 39 versus 66 in our Latin American country comparator group, with 100 being the best rating).<sup>41</sup> Since the homicide rate in the Philippines is much lower, the low rating on right to life and security of the person may be due to the above-mentioned poor rating in political terror. Similarly, the rule of law indicator of Kaufman and Kraay, which includes crime, rates the Philippines at -0.55, below our Latin American comparator average of -0.30. Moreover, the Philippine rating has deteriorated since 1996 where it stood at -0.01. These poor ratings are corroborated by the Freedom House Index, which rates the right to life and security of the person in the Philippines at 39 versus 66 in Latin America and the freedom from arbitrary intermission with privacy, due process of law and rights of the accused at 40 versus 50 respectively. The WJP’s order and security indicator rates the

<sup>40</sup> The level of police officers in the Philippines, at 138 per 100,000 people, is less than half of the level in our Latin American comparator country set (360). This discrepancy, however, likely reflects the privatization of policing in the Philippines, where security functions are mainly carried out by private security guards.

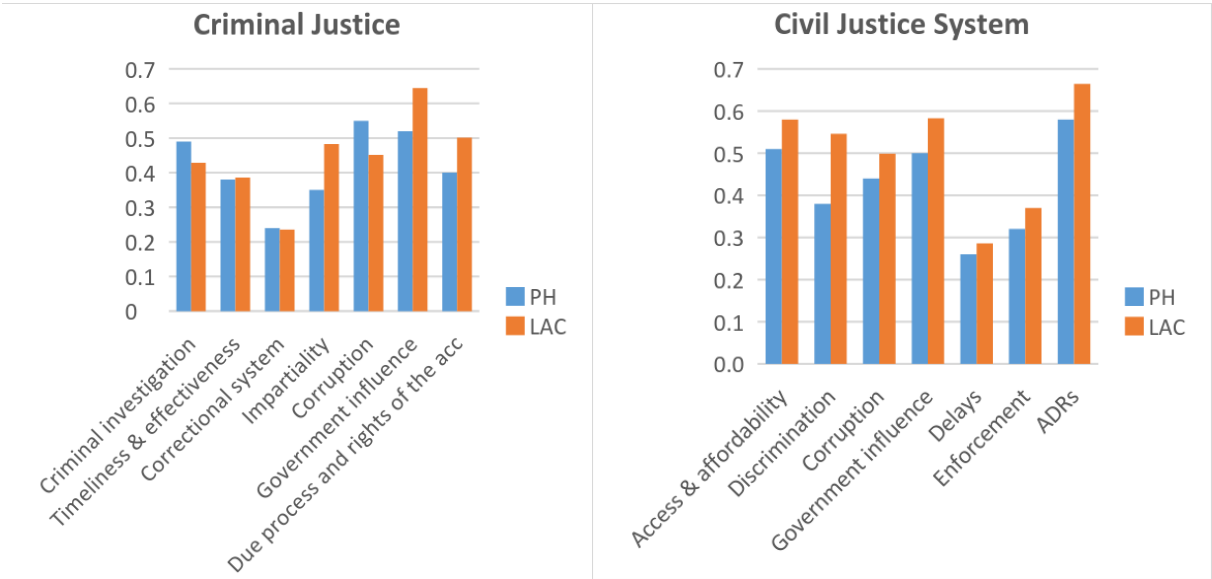
<sup>41</sup> This may be related to: a) the poor performance of the police (Amnesty International warns of widespread torture by Philippine police and in Philippine prisons); b) the high rate of journalist deaths; c) targeted killings of people considered to be a threat orchestrated by the economically and politically powerful; d) state-sponsored persecution and assassination of insurgents. These violations against the basic rights to life and security and to the rule of law also take place in some Latin American countries, but overall, to a lesser extent than in the Philippines.



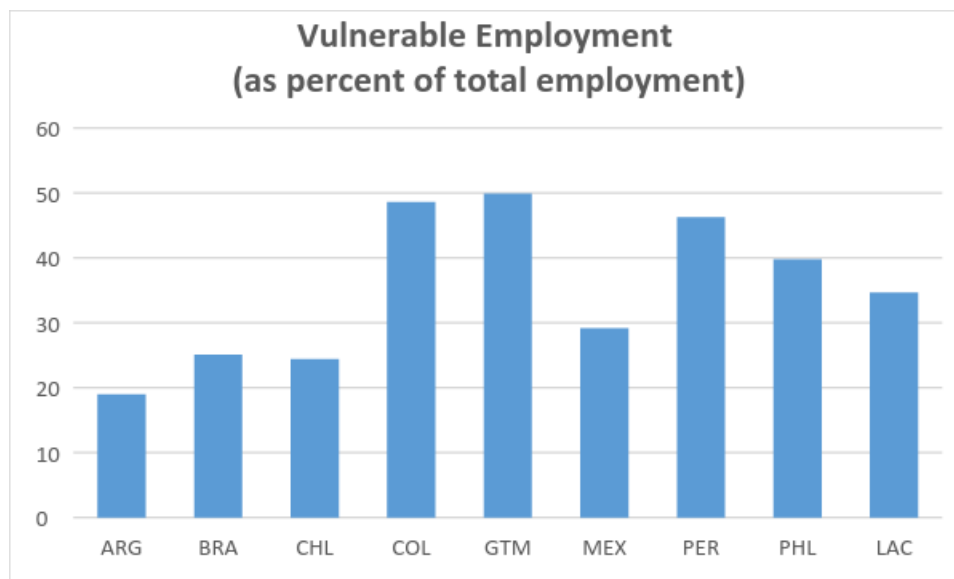
Philippines at roughly the same level as our Latin American country comparators (60 versus 58), with a better rating as regards crime and a worse rating as regards civil conflict. If the Mindanao conflict winds down, this rating should subsequently improve further.

**Overall, however, the criminal justice system in the Philippines receives a very similar rating to that of the Latin America region (42 in the Philippines versus 45 in Latin America).** The Philippines is rated better than Latin America as regards corruption in the criminal justice system (55 versus 45). However, the impartiality of the justice system receives a significantly lower rating in the Philippines (35) than in Latin America (48) as does the indicator on freedom from undue government influence (52 versus 64). The fact that the rate of violent crime in the Philippines is lower than in Latin America, but the rule of law and effectiveness in protecting the right to life and security of the person are rated worse, as are rights of the accused, may indicate relative weaknesses in the Philippine police and justice system.

**Civil justice, also important for ensuring protective security, is rated at 43 compared with 50 in Latin America, with the worst sub-rating being related to delays and absence of discrimination.** The worst rated sub-area in both regions concerns delays (26 and 29 respectively). The Philippines exhibits the largest gap with Latin America as regards the lack of discrimination of the civil justice system (38 versus 55 in Latin America). This discrimination is most likely related to the fact that the same state capture phenomenon that affects other parts of government also pervades the Philippine justice system. The Philippines also lags Latin America as regards undue government influence and corruption in the civil justice system as well as its access and affordability, all indicators of social inequality.



**The rate of unemployment in the Philippines –at 7 percent—is higher than in all our Latin American comparator countries except for Colombia.** Unemployment, underemployment and vulnerable employment are some of the greatest sources of insecurity in a market economy, particularly in the absence of strong social safety nets such as a good unemployment benefit systems. The rate of vulnerable employment in the Philippines, at 40 percent, is five points above the level of our Latin American comparator average (35 percent) and it approximates the 45 percent of the population who are poor and near-poor in the country. In the Philippines, however, the vulnerable employment rate has been coming down slowly but steadily from 45 to 40 percent between 2006 and 2012.



**Maternity leave in the Philippines, at 30 days, is about a third of the Latin American average of 86.**

This poor support to new mothers stands in contrast with other good results of the Philippines in the area of gender, as mentioned above. The country following the Philippines in having the lowest maternity benefits, which is Mexico, has twice as many days as the Philippines (60). A short maternity leave is not only a source of vulnerability, but a great detriment to the quality of life of mothers, children and families. In Argentina, Brazil and Chile –as in many OECD countries--men are equally allowed (some days of) paternity leave, which is a great contribution to the full development of men, women, children, the family unit and society as a whole.



**As a consequence of the low level of public health spending, the private burden in out-of-pocket expenditure on health in the Philippines was 59 percent above Latin America’s level in 2012.** The share of out-of-pocket expenditure in total health spending in the Philippines has consistently been very high compared to its level in Latin America.<sup>42</sup> In the Philippines, it has tended to substitute for government spending, declining between 1995 and 2000 (from 50 to 40 percent); rising from 2001 to 2008 (up to 58 percent), and declining thereafter (to 52 percent in 2012). In 1995-1999, it was 22 percent above the Latin American level; by 2000-2009, it had risen to 29 percent above that level and, by 2012, it was 59 percent higher. This high level of out-of-pocket health expenditure is a very large financial risk for Filipino households, particularly if one considers that half of the population is either poor or near-poor.

<sup>42</sup> In the Philippines, only one out of ten people’s health expenditures are covered by social security (multiplying health insurance coverage by coverage of a specific health need by actual insurance payment rate) (Capuno and Quimbo: forthcoming).



**In the Philippines, the financial risk protection rate provided by health insurance (Philhealth) is particularly low, at 9 percent.** (Capuno and Quimbo, forthcoming). This low protection rate is the combination of many factors including premium costs which the poor cannot afford, limited coverage of claims (with, for instance, out-patient, drug and other health materials needing to be shouldered out-of-pocket despite insurance), need to advance payments out-of-pocket, long repayment lags, high transaction costs in terms of paper-work, long waiting periods to avail of care and poor quality of public health compared to private health facilities. The 9 percent protection rate means that only one out of ten sick Filipinos get full financial support from PhilHealth.<sup>43</sup> The financial risk protection rate of the poor—who need that protection even more—is even lower at 8.4 percent.<sup>44</sup>

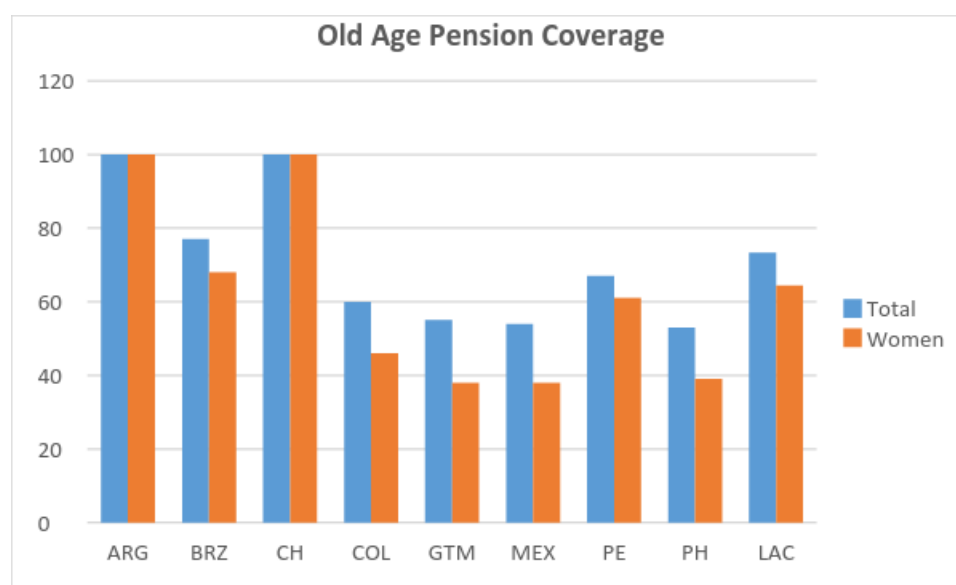
**Social security coverage in the Philippines is comparable to that in Guatemala and Peru, but lower than in our other Latin American comparator countries.** The ILO identifies eight areas of social security coverage and rates a country on whether it provides coverage fully, partially or none at all. The areas are sickness, maternity, old age, employment injury, invalidity, survivors, family allowances and unemployment. The Philippines, Guatemala and Peru provide coverage in 6 out of 8 areas, Mexico in 7 and Argentina, Brazil, Chile and Colombia in all 8 areas. Guatemala has no programs for either family allowances or unemployment benefits. Peru and the Philippines have no family allowances and only partial provision of unemployment benefits. Mexico has only limited provision of unemployment benefits.

<sup>43</sup> The Benefit Delivery Ratio is calculated as the PhilHealth coverage rate times the PhilHealth claim rate times the PhilHealth reimbursement rate.

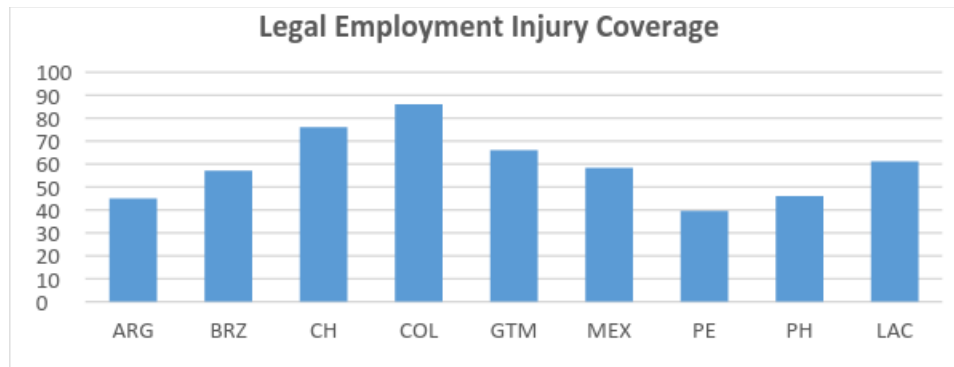
<sup>44</sup> The official enrollment rate in PhilHealth, of course, is much higher, at 82 percent (ILO 2014).

**Old age pension coverage in the Philippines is comparable to that in Mexico and Guatemala, but below the level of our other comparator countries.** (ILO 2014: Annex IV). Some of our Latin American comparator countries have already established European-style universal old age pension systems while others are moving in that direction. The countries that have achieved full coverage (Argentina and Chile) have done so through a combination of contributory and non-contributory pension systems while others (like Brazil and Peru) are moving in that direction. Some are still far from achieving universal coverage, including Mexico, Guatemala, Colombia and the Philippines.

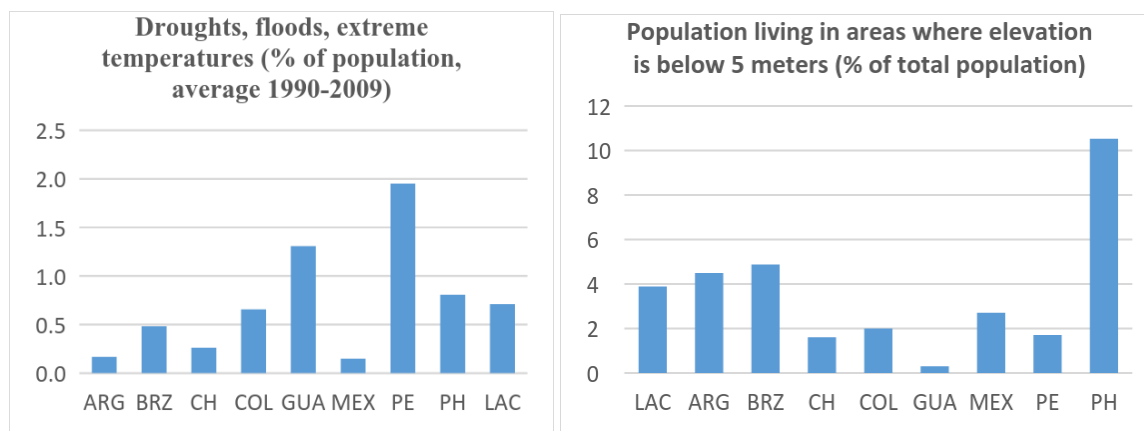
**Overall, the old age pension coverage rate in our Latin American comparator country group, at 73 percent, is well above the level of the Philippines, where it stands at 53 percent.** This is a great source of vulnerability for elderly Filipinos. The introduction of a non-contributory pension system in the Philippines in 2011, given time and funding, should contribute to moving the country into full pension coverage for all its population. Of particular concern is the very low level of pension coverage of women in the Philippines, which stands at only 39 percent compared to a 64 percent average in our Latin American comparator group (likely due to the fact that non-contributory pensions are only starting and the rate of labor force participation rate of women in the Philippines is low).



**The legal employment injury coverage in the Philippines stands at 46 percent compared to 61 percent in our Latin American comparator sample.** (ILO 2014: Annex IV). The lowest coverage rate can be found in Peru (at 40 percent) and the highest in Colombia (at 86 percent).



**The Philippines does not stand out in the percentage of the population exposed to extreme weather, but it does in the severity of the risk and the vulnerability of the population to that risk.** A great source of insecurity is that emerging from the occurrence of natural disasters. In this regard, a higher percentage of Filipinos is vulnerable than in our comparator countries. The percentage of the population exposed to drought, floods and extreme temperatures in the Philippines is similar to that in our Latin America comparator average (8 percent versus 7 percent). What is different is the percentage of the population living in low-lying areas, which is much higher in the Philippines, standing at 11 percent compared to 4 percent in our Latin American comparator group. Moreover, the two most-disaster prone countries in our Latin American country sample –Guatemala and Peru—have a particularly low percentage of population living in low-lying areas. The precarious location of housing of poor Filipinos exposes them to the vagaries of the weather to a much greater extent than it does in Latin America. Given the much higher percentage of the population living in shantytowns in the Philippines, it is also likely that the percentage of precarious housing is significantly higher than in Latin America, contributing to the much higher vulnerability rate of the population. Finally, the severity of the extreme weather conditions is higher in the Philippines, which has been ranked as the third most disaster-prone country in the world (World Disaster Report 2012).



## **Determinants of Differing Performance**

The reasons for the differing development performance of Latin America and the Philippines are manifold. This section will lay out some features of initial conditions that are likely to underlie the differing performance and will then proceed to focus on the intervening policy and institutional variables that are more immediately accountable for the differing results.

### ***Initial Conditions***

**The initial conditions of Latin America and the Philippines are very different, to the advantage of the former.** The best performing Latin American countries—Chile and Argentina—lie far from the equator and are consequently non-tropical. None of the Latin American countries included in our sample are archipelagic while the Philippines has over 7,000 islands. The Philippines, moreover, is one of the most disaster-prone countries in the world (World Disaster Report, 2012). This widely different geography has undoubtedly contributed to differing development patterns. This paper will not go into detail in this difference since it is not actionable through policy. However, it is important to note some of its consequences. For instance, the physical contiguity of the land mass of our Latin American country comparators permitted the development of large political units long before the arrival of European settlers. The Maya, Aztec and Inca empires, to cite only the most prominent, left a legacy of political unity and large economic and state structures compared which the more fragmented political units of pre-colonial Philippines.<sup>45</sup> These state structures began to develop a sense of national unity and government institutions, including bureaucracies, and policies which included an important institutionalized public good provision and redistributive function. These institutions and functions were not developed anywhere near to the same extent in pre-colonial Philippines.<sup>46</sup>

**Latin American countries also had a much larger European presence than the Philippines, with both positive and negative consequences.** The two best performing Latin American countries—Argentina and Chile—have populations that are largely European.<sup>47</sup> These European populations brought European

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<sup>45</sup> See Arias and Girod (2011) on the influence of the persistence of pre-colonial indigenous institutions and De Dios (2007) on the small scale of governance units in pre-Hispanic Philippines.

<sup>46</sup> Greater physical proximity to the United States and Europe may also have favored Latin America.

<sup>47</sup> Comin et al (2010) find a close association between the level of technology in the year 1000 AD and current GNI per capita if one takes into account population movements across continents (but not otherwise). Engerman and Sokoloff (1994) make a similar argument about development in the Americas. This supports my hypothesis of “transport” of human capital, technology and business and political culture across continents.

institutions, human capital and business culture with them as they moved to Latin America.<sup>48</sup> These institutions were rebuilt in the New World to the exclusion of the native population and, like in North America and the other lands of European settlement, they were inclusive of *Europeans*. Like the United States, Canada, Australia and New Zealand, because the excluded native populations in Argentina and Chile were relatively small, these countries were able to prosper despite the exclusionary nature of their institutions and policies. At the other end of the spectrum is Guatemala –followed closely by Peru--, which have a large percentage of native population. In these countries, the degree of “export” of European populations and institutions was much less. The majority indigenous population, moreover, was excluded economically, socially and politically by European settlers, contributing to the relatively poorer performance of these countries compared to their Southern Cone counterparts. Mexico and Colombia lie somewhere between the two extremes. The Philippines, on the other hand, has the largest percentage of non-European population, which has left a positive legacy of racial inclusion, but has also brought with it the continuation –often in an informal manner– of pre-colonial institutions and policies, including fragmentation, under-provision of public goods, insufficient redistribution and patronage.

**There are also important differences across both regions in political culture, possibly due to a different pre-colonial as well as colonial heritage.** The deeper European legacy of Latin America may have contributed to the continent’s deeply-held belief in the centrality of the role of the state in economic development, the conviction that inequality is harmful and contrary to the essence of a genuinely democratic system and hence the commitment to the role of the state in fostering development and a reasonably egalitarian distribution of income.<sup>49</sup> The Philippines, on the other hand, has been more influenced by the non-interventionist ethos and the higher tolerance, and even positive view, of inequality of the United States. The more fragmented and patronage-based nature of pre-colonial society in the Philippines compared with the communitarian character of smaller units and redistributive nature of large empires in Latin America can also help explain the greater focus on the role of the state in public good provision and income redistribution in Latin America than in the Philippines.

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<sup>48</sup> Easterly and Levine (2012) find “find a remarkably strong impact of colonial European settlement on development” backing up “(a) large literature (which) suggests that European settlement outside of Europe shaped institutional, educational, technological, cultural, and economic outcomes.”

<sup>49</sup> Latinobarometro –the survey with the widest coverage in Latin America– consistently finds that Latin Americans consider social justice and an egalitarian distribution of income to be a *sine qua non* characteristic of democracy.



Finally, the deeper European legacy of Latin America can also help explain greater progress in the transition from a Popperian “closed” to a more “open,” less patronage-driven society and polity.<sup>50</sup>

**Finally, having been a direct American colony may have also influenced development in the Philippines.** The American colonial period in the Philippines left a strong legacy of economic and political power concentration in the elite (exacerbating the original legacy of Spain in this regard): “the American colonial era produced a national oligarchy, dominant in both the economic and the political spheres, that remains enormously influential to this day” (de Dios and Hutchcroft 2003: 45). This power inequality may be even greater than it is in Latin America, leading to a concentration of economic and political power in a tiny number of families resulting in a particularly pronounced case of state capture (Hutchcroft and Rocamora, 2003).

**Moreover, Latin American countries became independent after their 1820s revolutions and were able to develop their own institutional systems in relative freedom.** The Philippines, on the other hand, evolved its democracy in captivity. It has been argued that the Philippine rent-seeking state emerged ‘due in large part to the imposition of formal electoral democratic institutions upon an underdeveloped state apparatus’ (Sidel 1999: 140). De Dios and Hutchcroft (2003) go further and argue that the United States actively fostered the creation of a new state-dependent elite in order to weaken the pre-existing landowning elite due to the pro-independence leanings of the latter. The former, instead, became dependent on the United States as the colonial power and on its policies and trading opportunities: ‘The American colonial government successfully co-opted local *caciques* (powerful landowners) into newly formed political institutions, in the process not only strengthening the *caciques*’ power base at the local level, but also extending it upward to both the provincial and the national level’ (Hutchcroft and Rocamora 2003 cited in de Dios 2007: 161-162). Finally, the more recent direct American colonial experience of the Philippines may have also left a deep-set tendency to imitate American institutions and practices in what is a completely different setting. Latin America, though certainly influenced by the United States and Europe, has gone further in charting its own institutional and policy course.

**Despite differing initial conditions, there are important lessons to be drawn from the Latin American experience.** The applicability of the lessons is confirmed by the fact that many of the policies they entail

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<sup>50</sup> Greif and Tabellini (2010) identify “city” versus “clan” culture (open versus closed Popperian institutions) as a key determinant of the great divergence in development trajectory between Europe and China. Latin America seems to be more advanced in the transition from a “clan” political culture to that of the “city.”

coincide with those applied by successful middle income countries in East Asia and even by the Philippines in the past. The following section attempts to draw the most important among these lessons.

### ***Institutional and Policy Lessons from Latin America***

#### ***1. More and better spending***

**Latin America raises 10 points of GDP more in public revenues than the Philippines.** As regards policies, the most noticeable difference between Latin America and the Philippines is the much higher revenue and expenditure levels of Latin America. Latin America has traditionally had a higher level of revenues and expenditures than the Philippines. The gap has grown wider over time as Latin American countries have stepped up their tax efforts in the 1990s and 2000s while the Philippines has seen its own revenue effort plummet after 1997.<sup>51</sup> Since the early 1990s, the Latin America and the Caribbean region has increased its tax effort by 3 points of GDP on average while in the Philippines it has fallen by over 4 points.<sup>52</sup> As of 2012, the revenue to GDP ratio of our comparator country sample was 10 points above the level of the Philippines (29 versus 19 percent) as was the tax-to-GDP ratio of the region as a whole (23 versus 13 percent). (WDIs and IDB 2013).<sup>53</sup>

**The much higher levels of public revenues and expenditures in Latin America support education, health and infrastructure spending levels that are multiples of those found in the Philippines.** In 2012, the general government expenditure to GDP ratio in the Latin America and the Caribbean region was almost 10 points above that of the Philippines (at 29.3 versus 19.6 percent). These high levels of spending have enabled Latin America to make very fast progress in the areas of education and health, particularly since the 1990s. In the Philippines, on the contrary, education outcomes even deteriorated between 1997 and 2005 as spending levels were slashed while health outcomes are among the worst of any middle income country and are either deteriorating (maternal mortality) or progressing very slowly (infant and child mortality). Access and affordability of basic infrastructure, such as water, sanitation and electricity is also significantly better in Latin America. This has all been achieved in Latin America with a government debt-to-GDP ratio that is below that of the Philippines (at 35 versus 41 percent).

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<sup>51</sup> 1997 marks a turning point in Philippine development with a significant decline in government revenues and expenditures and a slowing down in progress in education, health and poverty reduction after that date.

<sup>52</sup> Some countries have witnessed much higher increases such as Argentina (12 points), Ecuador (8 points), Bolivia (6 points), Colombia (4.5 points), Peru (4.4 points), Dominican Republic (3.8 points) and Paraguay (3.7 points).

<sup>53</sup> The most successful countries in generating growth and poverty reduction in East Asia (China and Vietnam) also have revenue-to-GDP ratios and social spending levels that are close to those of the Latin America region.

**Latin America has also provided a greater degree of priority than the Philippines to the provision of public goods and services within its budget.** Not only are budgets much larger as a percentage of GDP – let alone in absolute terms—in Latin America than in the Philippines, but the share of the budget devoted to education and health tends to be larger. This is particularly true of Guatemala, which has an even lower tax effort and overall expenditure to GDP ratio than the Philippines, but devotes shares of the budget to both education and health which are 60 percent above the level of the Philippines. The Philippines, on the other hand, continues to devote significant amounts of resources to private goods and transfers –until recently through the Priority Assistance Development Fund and still now through other congressional allocations--, as well as through the Philippine Charity Sweepstakes, Local Government Units, conditional cash transfers and a number of other programs.

**Finally, decentralization may also have resulted in better institutional and policy outcomes in Latin America than in the Philippines.** Decentralization took the developing world by storm in the 1990s. Its results, however, have varied greatly from region to region and from country to country depending chiefly on the political economy of each context. In Latin America, decentralization seems to have genuinely increased voice and representation, directed more resources away from capital cities to other parts of each country (Alonso I Terme and Steinberg, 2006) and increased social spending. Currently, education and health alone account for 40 percent of sub-national spending in the Latin America region (Bossuyt, 2013) while social outcomes have continued to improve substantially since the onset of decentralization.<sup>54</sup> In the Philippines, on the other hand, there are indications that decentralization may have increased the power of local elites<sup>55</sup> while leading to a significant increase in regional inequality in revenues and expenditures and a decline in the budget shares devoted to social services and infrastructure (World Bank, 2011) resulting in stagnant social outcomes in many regions. (Capuno, 2007).

## **2. *Freer, more competitive markets***

**In the aftermath of the debt crisis, Latin American countries undertook radical reforms to liberalize their economies, including their agricultural sectors.** Over the 1980-2010 period, trade restrictions

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<sup>54</sup> According to data from the Bureau of Local Government Finance, on the other hand, the share of education, culture, sports and health in provincial current operational spending in the Philippines was 22 percent in 2013.

<sup>55</sup> It has been argued that one of the reasons for the poor developmental performance of some provinces in the 1990s lies in the 'initial dominance in those areas of political dynasties, which have been revealed to be inimical to subsequent growth. This is because elite capture fosters a patron-client relationship between those who govern and those who are governed' (Capuno 2007: 204); and De Dios (2007).

were removed, leaving Latin American trade systems very open and not featuring any equivalent of the rice protection system of the Philippines, which places rice prices at roughly 40 percent above market levels. This has reduced the price of basic foodstuffs and facilitated the orientation of agriculture towards exports.

**Moreover, the liberalization of the agricultural sector in Latin America has facilitated increased investment, competitiveness, export diversification and growth.**<sup>56</sup> Even in countries with relatively unequal land distribution such as Chile and Brazil, agricultural growth has been strong and government has focused on the provision of public goods such as research and extension and marketing support. Brazil, for instance, has been transformed in 30 years from being a net agricultural importer to “an agriculture trade powerhouse, emerging as the global leader in increasing food exports in the past decade” and currently ranking as the world’s fifth largest food exporter (World Bank 2013 a: 2). By contrast, the Philippines agricultural sector has been largely stagnant suffering from uncertainty in land titles, insufficient access to credit and insufficient provision of public goods (World Bank, 2008). There are also no targets for private banking sector lending to agriculture in Latin America whereas they continue to exist in the Philippines.

**Latin America has also made greater progress in improving the business climate, facilitating market entry and overall entrepreneurial activity.** As a result, markets are much more dynamic and competitive than they are in the Philippines, where a small number of firms and an even smaller number of families control a large number of markets. Doing Business Indicators, Global Competitiveness Forum Indicators and indicators of new market entries are much more positive for Latin America than they are for the Philippines. The Philippines, on the contrary, suffers from important barriers to entry, scoring particularly badly in ease of starting a business and number of new business registrations. Some progress has been made in the Philippines over the past four years, but much remains to be done.

**Oligopolistic pricing affects key markets in the Philippines, such as electricity, inflating production costs and raising prices for individual consumers.** The privatization of key basic infrastructure services such as water and electricity has resulted in dramatically high electricity prices which weigh down the country’s competitiveness and eat at consumer earnings. Access to water is also low and prices high,

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<sup>56</sup> In Latin America, exports of agricultural products have grown at about 8 percent annually since the mid-90s, and now make up about a quarter of the region’s total exports – more than LAC’s share of any other sector in world trade. Latin America is also a bigger player at a global level: it now represents 13 percent of agricultural trade, up from 8 percent in the mid-90s. Agricultural exports have diversified in type of product and destination, with a growing share for China which now accounts for 36 percent of the region’s food exports (World Bank, 2013)

with important consequences for the poor, particularly as regards their health. By contrast, electricity prices are lower in Latin America and, in some countries, water and electricity utilities are being nationalized to ensure access and affordability.

**Natural resources and utilities in Latin America are either publicly run or open to international competition while in the Philippines they are controlled by the domestic elites.** The constitutionally imposed limits on foreign investment in real estate, utilities and natural resources that exist in the Philippines do not exist in Latin America. On the contrary, Latin American governments have largely kept natural resources and their large rents in the purview of the public sector (as copper in Chile, oil in Brazil and Mexico and, more recently, nationalizations in Ecuador, Venezuela and Argentina). When not run by government, these sectors are open to international competition, as in the case of natural resources in Peru. In the Philippines, instead, these sectors and their rents are neither publicly run nor open to international competition, but are instead protected and largely transferred to *domestic* elites. Fortunately, the Philippine Congress is currently considering the removal of such constitutional limits.

### ***3. Cleaner, better oriented governments***

**Latin American countries have made great strides in improving the transparency and integrity of their governments and private sectors.** Latin American countries score much higher as regards fiscal transparency than the Philippines (OBI 2012) while the rating of business sector disclosure in the Philippines is only half the level of Latin America. This is a legacy of the reforms initiated in the 1980s. The contribution of improved transparency to the control of corruption cannot be overestimated. Latin American countries, under the spur of civil society and international organizations (on which they were highly dependent in the aftermath of the debt crisis), underwent a “transparency revolution.” This transparency affected both the public and the private sectors and has yielded a level of fiscal transparency and public dialogue over fiscal issues that has greatly contributed to strengthened institutions and policies.

**Latin American politics has become increasingly more representative and less patronage-driven.** In the 21<sup>st</sup> century, Latin American governments have become much more representative socio-economically, racially and by gender.<sup>57</sup> This may have contributed in some cases to populism, but it has certainly increased the voice of the poor and other formerly excluded social groups. Moreover, up to the 1970s, vote-buying was still rife and patronage politics strong in Latin America. However, as urbanization and

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<sup>57</sup> The most prominent examples are Michelle Bachelet of Chile, Dilma Rousseff of Brazil and Cristina Fernandez de Kirchner of Argentina, Evo Morales of Bolivia and Alejandro Toledo and Ollanta Humala of Peru.

education of the poor proceeded, vote buying declined. Rising incomes of the poor also contributed. Moreover, the increasingly more programmatic party-driven nature of the political system and the relatively lower role of the individual candidate has also contributed to a decline in vote-buying and patronage and strengthened the public goods provision orientation of government policy.

**Latin American progress in the area of governance was implemented through often radical institutional and policy reform.** A large number of Latin American countries –Peru, Bolivia, Colombia and Guatemala are often cited as examples—radically reformed their tax administration agencies. They did so often by completely scrapping the old corrupt agency and beginning from scratch. This has yielded some of the best tax administration reforms ever recorded, such as that of Peru. These reforms were possible because of a genuine political will and ability to take the bull by the horns and pay any political price necessary. The reforms actually yielded high political returns as the population approved of the clean-up operations, appreciated their new interactions with the reformed tax administration agency and enjoyed the improved public services funded with the additional resources resulting from tax policy and administration reform.

**Greater integrity was also facilitated through the orientation of government to public goods provision through programs and interventions which are less liable to mismanagement and corruption.** The other great pillar of improved integrity has come through the re-orientation of the role of the state from market impairing functions and private goods provision to market-supporting functions and public goods provision. The greater the role of the state in private markets and in the provision of private goods and services and the larger the room for discretion, the greater the scope for mismanagement and corruption. As state-owned enterprises were privatized –except sometimes in the natural resource and utility sectors--, markets freed, regulations eased and simplified, tax incentives rationalized, subsidies and discretionary transfers slashed and government reoriented to the provision of public goods and services, corruption fell.

**It was not the setting up of anti-corruption agencies or the hamstringing of the public expenditure process that delivered a reduction in corruption, but greater transparency, reformed government agencies and a re-oriented role of the state.** The Philippines, although it has made some progress in curbing corruption since 2010, it has made significantly less progress than Latin America. It has also advanced much less in the three above-mentioned key areas. In fact, transparency in the public and private sectors is still low, institutional reform –as in BIR or BOC—is timid at best, and the role of the state continues excessively focused on over-regulation, incentive-provision and private transfers. It is

this re-orientation of the role of the state that is needed to yield genuine progress in curbing corruption and increasing overall government effectiveness.

### ***The Political Economy of Differing Institutional and Policy Reform***

#### ***1. The Top 10 Percent versus the Top 0.1 Percent***

**According to standard measures of inequality, Latin America appears even more unequal than the Philippines.** Aggregate measures of income inequality such as the Gini coefficient or even the income share of the top 10 percent do not set the Philippines apart from Latin America. On the contrary, by those standards, inequality in Latin America is even higher than in the Philippines (though it is increasing in the Philippines and declining in Latin America). (WDIs and Gasparini, Cruces and Tornarolli 2009). As has been recently pointed out, however, the key to the hamstringing of markets and democracies across the world is increasingly *not* the top 10 percent, but the top 1 percent or even the top 0.1 percent (Stiglitz 2013; Picketty 2013). In fact, the worrying world trend is the emerging concentration of economic and, increasingly, political power in a tiny number of individuals. This concentration of power is undermining our market systems and weakening our democracies.

**The Philippines has a particularly strong concentration of income and wealth at the very top.** The country has one of the largest shares of billionaires in middle income Asia (World Bank 2013 b). In 2012, Forbes Asia announced that the collective wealth of the 40 richest Filipino families had grown by \$13 billion during the 2010-2011 year, to \$47.4 billion – an increase of 37.9 percent. Filipino economist Cielito Habito has calculated that the increased wealth of those families was equivalent in value to 76.5 percent of the country's overall increase in GDP at the time (Keenan: 2013). It is this handful of families that controls a large number of markets as well as, to a large extent, the political system. In Latin America, on the other hand, the problem is a more traditional one of "the top 10 percent" rather than the "top 1 or 0.1 percent."<sup>58</sup> This difference goes a long way toward explaining the greater autonomy of the political system in Latin America and its greater ability to act for the common good.

**2. A Society Committed to Building a Social Democracy and a Middle Class Willing to Pay for It**  
**Latin America began developing sizable states aimed at becoming European social democracies early in the post-World War II period.** In the aftermath of World War II, most Latin American countries embarked on the task of building import-substitution oriented interventionist states, just like the

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<sup>58</sup> Latin America, of course, is not a homogeneous region and countries like Guatemala may have greater similarities with the Philippines in this regard than with other countries on their continent.

Philippines and most of the developing world. What was characteristic of Latin America, however, was the development of an important role of the state in public good provision --education, health, transport, basic infrastructure, social protection—and income redistribution.

**What Latin American countries had yet to work out was how to pay for their social democracies and who should bear the brunt of the burden.** Arguably, during the 1960s and 1970s and due to the level and structure of the taxation (heavily focused on taxing trade), much of the cost of running government was borne by the wealthy and the poor. The rest was chalked up to a mounting debt and, later on, to deficit monetization leading to rising inflation and, in many cases, hyperinflation which weighed particularly heavily on the middle classes. In the 1990s, in the aftermath of the debt crisis and after the adjustment of the 1980s, a new sustainable and politically-feasible fiscal pact had to be found to continue financing the region's social democracy. The solution was a top-bottom coalition that increased the tax burden and laid it largely on the middle classes (Alonso I Terme and Steinberg, 2006). The current social-democratic and populist regimes in the region are trying to revisit this outcome.

**When the debt crisis of the 1980s hit the continent, Latin American countries liberalized, stabilized and continued to build social democratic states.** In short, the baby was not thrown away with the bath water (as has arguably happened in Eastern Europe in the wake of communism). The harmful import-substituting protectionist-interventionist policies were thrown out the window together with high budget deficits, inflation and macro-economic instability. What was kept and further enhanced was the social project of building a social democracy, but now with a stronger market orientation. Tax systems and tax administrations were reformed and the tax effort increased. Government expenditures were stepped up and redirected toward education and health and away from subsidies and other less productive expenditures. Governance reforms were, overall, quite thorough, with large improvements in both the business climate and the integrity of government institutions.

**The stepped up tax effort has largely been shouldered by the Latin American middle classes.** Like the Philippines, Latin America has been unable to make the wealthy pay their fair share of the tax effort. Personal income tax payments as a percentage of GDP continue to be dismally low in both regions. The difference lies in the fact that the Latin American middle class did not give up on building a social democratic state because of their inability to get the wealthy to pay for it. *They* did. It is from their pockets that the value-added-tax that largely funded fiscal adjustment came from just as it was they who lost jobs in government and state-owned enterprises and were most affected from slashed commercial protection and government subsidies and the privatization of pension systems. But this did



not deter them from the task of continuing to build a government with universal provision of education, health and social protection and with an important role in the provision of public transport and basic infrastructure. Even if they had to pay for it themselves. This is an important difference with the Philippines, where the middle classes emigrate in large numbers and pay for education, health and even infrastructure and security privately, preferring to keep government small (Alonso I Terme, 2014).

**Since the 1990s, Latin American governments have significantly increased their tax efforts while the Philippines has reduced it.** This is a critical difference at the core of the differing performance in education, health and infrastructure in Latin America versus the Philippines. After the initial expenditure cuts to stabilize the economy in the 1980s, Latin American countries proceeded to significantly step up their tax efforts. The increased revenue effort is seen as necessary in order to support the social democracy Latin Americans are committed to building. The increase in the tax effort has been very large and has been shouldered to a large extent by increased revenue from the value-added-tax.

**Guatemala, the only country to continue to have a revenue-to-GDP ratio similar to that of the Philippines, is devoting a share of its budget to education and health that is 60 percent higher.**

Guatemala, which also suffers from elite capture, has been similarly unable to increase its tax effort. However, it has –partially-- compensated for this shortcoming by having a particularly large share of its budget devoted to education and health. As a result, it has had a very rapid rate of improvement in both sectors as well as in poverty reduction while the Philippines is progressing much more slowly in health, was for some time even backtracking in education and poverty is largely stagnant.

**Latin American countries have also implemented radical tax administration reforms, often wholly scrapping their tax administration agencies and setting up new institutions.** At the core of governance and fiscal reform in Latin America has been tax administration reforms. The tax administration reforms of Peru, Bolivia, Colombia and Guatemala are textbook cases of the possibility to turn around tax administration through radical reform. In other countries where corruption was less entrenched, like Argentina or Chile, on the other hand, reform has been more gradual. In all countries, however, tax administration reform was both a hallmark of governance reform and a keystone of a stepped up fiscal effort as tax policy and tax administration reform complemented each other. No such reforms have taken place in the Philippines.

**To conclude, the greater public goods provision, freer and more competitive markets and cleaner, more representative governments that are bearing good fruits in Latin America are needed in the Philippines.** What remains unique to the Philippines is how to achieve this common good within the context of its own unique political economy. How to engineer this political change remains ground for future research and activism, but the nature of the task ahead and its necessity seem clear.

### ***3. The pressure from below***

**Latin America has a very active popular class and a high level of political activism by the poor.** This activism has manifested itself in political participation and strong social demand for public services and income and wealth re-distribution. When not satisfied, the activism has led to social and political unrest followed by elite repression sometimes resulting in civil war. The Latin American dictatorships of the 1970s were to a large extent the consequence of elite resistance to popular pressures for redistribution and social justice. This elite resistance led to the regimes of Pinochet and the Argentinian juntas as well as the civil wars of Guatemala, Nicaragua and El Salvador, to name just a few. The pressure, however, could not be resisted indefinitely and had to be satisfied in some fashion. The solution to this quandary has been the social-democratic policies of Chile, Argentina, Mexico and Brazil since the 1990s and, since the onset of the new century, the social-democratic government of El Salvador and the left-wing populist regimes of Venezuela, Bolivia, Ecuador and Argentina. Costa Rica, with its long-standing social-democratic policies, has been spared in the storm. In Latin America, therefore, political pressure from below for pro-poor policies has been reflected through programmatic party systems into a variety of government programs.

**In the Philippines, on the other hand, political activism by the poor is weak and there is no political party representing a social democratic agenda.** The political space on the left is dominated by the Communist Party of the Philippines and Maoist-leaning guerrillas, none of which participate in elections. Neither the social democracy nor the populism of the Latin American variety advocating for a strong state as a provider of public goods and services and participating in the political process really exists in the Philippines. This is in part due to the single-seat constituency –favoring individuals and patronage-- as opposed to a party-list electoral system as well as the much weaker popular pressure from below.<sup>59</sup>

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<sup>59</sup> The absence of this pressure is likely due to a combination of factors such as the absence of a clear racial barrier between the majority and the elites, the electoral system, the difference in pre-Hispanic indigenous political and

## Conclusions

**Latin America is well ahead of the Philippines and has made faster progress since World War II as regards income, poverty, education, health, infrastructure, social protection and corruption.** Gaps in GDP per capita, poverty, social indicators, infrastructure and many aspects of institutional development favor Latin America over the Philippines. The areas where Latin America has the largest lead include GDP per capita, poverty, secondary and tertiary education enrollment, health outcomes and the right to life and security of the person. Latin America is also well ahead of the Philippines as regards the development of social safety nets and control of corruption.

**In some areas, such as government effectiveness, selected aspects of private sector development, political freedoms, and crime outcomes are comparable or even better in the Philippines.** The Philippines actually out-rates our Latin American comparator country set as far as government effectiveness is concerned. This a good outcome given the overall lower level of development of the Philippines and the much smaller amount of resources devoted to public services. The Philippines is rated and ranked very favorably as well in a significant number of private sector areas including ICT and the financial sector, ranking near Latin America in the latter despite its lower overall development level. Finally, in many indicators of the quality of democracy, including freedoms, the Philippines rates similarly to our Latin American comparator countries. Homicide rates are also significantly lower in the Philippines than in our Latin American comparator country average.

**The Philippines is one of the best performers in the world as regards gender (except in maternity) as well as in HIV infection rates and it is well ahead of Latin America as regards racial discrimination.** The Philippines has one of the smallest gender wage gaps in the world and one of the highest percentages of women in management positions in government and the private sector (55 percent). Education gaps in the Philippines –albeit relatively small–, also favor women and women hold a particularly high share of positions in the teaching profession. The percentage of women in Parliament, however, is as low in the Philippines as in our Latin American comparator country set (19 percent). The only areas of gender in which the Philippines significantly under-performs Latin America are those related to maternity. In the Philippines, maternal mortality rates are three times higher and maternity leave is only a third of the level of our Latin American country comparator average. The Philippines ranks 11<sup>th</sup> out of 148 countries worldwide on HIV infection rates (compared to a 79 LAC average). Indicators of political and economic

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social models, the greater European and stronger American influence in the Philippines, greater economic and political power of the Philippine elites and the harsher political repression of left-wing movements.

racial discrimination are much more positive and progressing faster in the Philippines than in Latin America (though the latest data available is only for 2003 and progress has been made in Latin America since then).

**The areas in which the Philippines does well are mostly outside government and pertain to society – gender, race and HIV—and the private sector, while lagging areas are largely within government.** This raises the question of what intervening institutional and policy reforms Latin America has implemented to enable it to deliver these positive development outcomes.

**The main reason for the weak performance of the Philippines is to be found in policies and institutions and not in initial conditions.** If the main reason for the differing performance between Latin America and the Philippines was due to initial conditions, the country would not have reached a GDP per capita level comparable to that of most Latin American countries in the late 19<sup>th</sup> century nor would it have been ahead of them in education and health indicators until the late 1980s. As policies changed in the Philippines (and budgets were cut), performance accordingly weakened. In Latin America, on the other hand, the opposite happened: revenues and expenditures were stepped up –as were liberalization and governance reforms--and performance improved. The good news therefore is that the weaker performance of the Philippines –both compared to its own track-record and to that of Latin America--is not chiefly due to geography or history, but rather to institutions and policies that are actionable, and can hence be reversed. The political economy of the reversion, however, is not simple.

**Latin America has revenue and expenditure levels that are 10 points of GDP above those of the Philippines resulting in much stronger spending and outcomes in education, health and infrastructure.** Since the 1990s, the gap grew as the revenue to GDP ratio increased by 3 points in Latin America while it fell by 4 percentage points in the Philippines. As the tax effort of the Philippines plummeted, social development outcomes deteriorated as did the poverty elasticity of growth. These were weaker outcomes both with comparison to the historical performance of the Philippines as well as with comparison to Latin America (or East Asia). At times when tax and expenditure levels were higher, results improved and as they weakened, results did as well. The results chain can be clearly traced from expenditures to outputs such as teachers and intermediate indicators such as enrollment and final outcomes like school completion rates (with similar trends in health). This trend confirms that it is not mainly initial differences with Latin America that account for the gap. Institutional reforms, such as decentralization, also seem to have delivered much better and pro-poor results in Latin America.

**Markets are freer and more competitive in Latin America.** Market competition in the Philippines, as indicated by new business density, is one tenth of the average level in Latin America. This reflects an oligopolistic situation in many Philippine good and service markets. Moreover, the fact that utilities such as water and electricity were privatized without allowing for foreign competition due to constitutional restrictions, squarely placed public utilities in the hands of the domestic elites. As a result, public utilities—which are notoriously difficult to regulate properly in any context—do not seem to be properly regulated in the Philippines, possibly due to regulatory capture. This situation burdens the Philippines with relatively low access levels and exceedingly high prices in water and, especially, electricity. The impact of low water access on health and high electricity prices on manufacturing cannot be overestimated. Remaining restrictions to free trade in rice leave the Philippines with the price of its basic staple 40 percent above market levels, an enormous burden for the average Filipino and, especially, for the poor. It is also possible that labor markets are more rigid in the Philippines while the gap between wage levels and productivity is higher due to slow productivity growth owing to insufficient progress in education and a high price level driven by remittances. Other restrictions, such as in inter-island shipping, real estate, natural resources and finance also hamper free market competition.

**Finally, Latin America has made faster progress and is well ahead of the Philippines in terms of transparency and integrity.** This is indicated in better ratings in Transparency International's corruption perception index as well as in Kaufmann and Kraay governance indicators. The private sector also stands out as particularly opaque and receives much lower transparency rankings than the private sector in Latin America. Of particular concern is that voice and accountability ratings in the Philippines have deteriorated over time, not only with respect to other countries, but also with respect to their own previous levels. This is an essential area which combines with weaknesses in investment climate to hamper domestic as well as foreign direct investment. Although there has been some progress in the recent past, as reflected in an improved Doing Business Indicator ranking and in corruption ratings, the overall picture has not fundamentally changed.

**The political economy drivers of differing policies may lie in a combination of state capture by a “Picketty-top” in the Philippines, middle class “opt out” from the public sector and weak political articulation of the needs of the poor.** The political economy drivers of the differences in policies in both regions have only been mentioned in this paper as potential hypotheses to be further explored by future research. The Gini coefficient in Latin America tends to be even higher than in the Philippines, but there are indications that the key difference is concentration of economic power in a very small number of

families in the Philippines leading to *de facto* state capture or inability of government to sufficiently act in the common good, let alone with a preference for the poor. The middle class in Latin America has always been a strong constituency advocating and voting to build a government in the European social-democratic tradition, a view which is further compounded by communitarian-populist pressure from indigenous groups. In the Philippines, on the contrary, the middle class has largely “opted out” of government” (with many completely opting out of the country), preferring to keep it small and providing for their education, health, security and even infrastructure needs privately (Alonso Terme, 2014). The poor, finally, are much more politically active in Latin America, possibly aided by a more conducive programmatic party based electoral system and, in some cases, a history of racial grievance.

**The Philippines, as reflected by its history and current human capital, has enormous untapped potential.** As reflected in performance in previous decades, if the Philippines resolves its weak fiscal effort, it has the potential to quickly return to the strong performance of the past in education and health and expand this progress to government-financed infrastructure. This would, as it did in the past, have an impact on the poverty elasticity of growth. If tax reform and stepped up expenditure on public goods was compounded with removal of red-tape, liberalization and de-regulation, competition and a solution to the utilities crisis, the country would be ripe for greater investment and the emergence of pro-poor sustainable growth. Finally, if Congressional reform was launched to move to an electoral system based on programmatic political parties with strong limits on private campaign financing, government would become more representative of the Filipino population. It is these kinds of reforms that can be “game changers” and catalyze transformation in everything else, including corruption.

**Absence of game changing reforms, on the other hand, is likely to perpetuate the status quo without fostering sustainable inclusive growth or deepening of democratic governance.**

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