ADB

ERD POLICY BRIEF SERIES
Economics and Research Department
Number 5

What Else Besides Growth Matters to Poverty Reduction? Philippines

Arsenio M. Balisacan
Ernesto M. Pernia

Asian Development Bank
http://www.adb.org

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

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

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

The **ERD Policy Brief Series** is based on papers or notes prepared by ADB staff and their resource persons. The series is designed to provide concise nontechnical accounts of policy issues of topical interest to ADB management, Board of Directors, and staff. Though prepared primarily for internal readership within the ADB, the series may be accessed by interested external readers. Feedback is welcome via e-mail (policybriefs@adb.org). The views expressed herein are those of the authors and do not necessarily reflect the views or policies of the ADB.

ERD POLICY BRIEF NO. 5

What Else Besides Growth Matters to Poverty Reduction? Philippines

Arsenio M. Balisacan
Ernesto M. Pernia

February 2002

Arsenio M. Balisacan is Professor of Economics, University of the Philippines; Ernesto M. Pernia is Lead Economist, Economics and Research Department, Asian Development Bank.

For the most part of the past quarter century, the Philippine economy performed poorly, especially seen against the backdrop of the dynamic East Asian economies. Spurts of growth were often followed by bust and stagnation. Not surprisingly, absolute poverty among a significant proportion of the population has persisted. The country's real per capita GDP at the turn of the 21st century was just about the same as that in the early 1980s, which is also partly attributable to unabated population growth.

The growth episodes in the late 1980s through the 1990s, despite interruption in the late 1990s owing to the Asian financial crisis and the El Niño drought, appear to be fundamentally different from the previous ones. Growth took place in an environment of relative political stability, economic deregulation, and institutional reforms. While policy coordination problems (e.g., in public investments) persisted, it can be said that the economy at the end of the 20th century was more market-oriented than it ever was (Bautista and Tecson 2002).

How well has this recent growth performance influenced the welfare of the poor? If growth has not been good enough, what else matters critically to poverty reduction?

This note summarizes the results of empirical research on the determinants of poverty reduction in the Philippines from the late 1980s to the late 1990s (Balisacan and Pernia 2002). Departing from the usual approach to examining the link between growth and poverty using cross-country averages, the study analyzes the variations in the growth-poverty performance across the country's 75 provinces to identify the key factors directly and indirectly affecting the well-being of the poor.

Overall Growth and Poverty Reduction

Nationally representative household survey data suggest that average household welfare, as measured broadly by per capita consumption expenditure (appropriately adjusted for provincial differences in cost of living), increased by 41 percent between 1985 and 1997, or an average of 3.4 percent annually. In contrast, the increase in real per capita GDP during this period was much lower at 1.2 percent a year.

Significant poverty reduction appears to have taken place between 1985 and 1997, although part of the gain was eroded by the combined effect of the Asian financial crisis and the El Niño drought in the late 1990s. The average consumption expenditure of the poorest 20 percent of the population increased by 28.6 percent during this period. That poverty fell significantly is quite robust to alternative assumptions about poverty lines and conventional poverty indices. For example, when the spatially consistent poverty lines suggested by Balisacan (2001) are applied to the distribution of per capita consumption expenditures, poverty incidence is shown to have declined from 41.5 percent in 1985 to 25.0 percent in 1997, or an annual average decline of one percentage point for every one percentage-point increase in overall per capita income. This appears to be consistent with earlier findings from cross-country analysis that the incomes of the poor move one-for-one with overall income growth (e.g., Dollar and Kraay 2001).

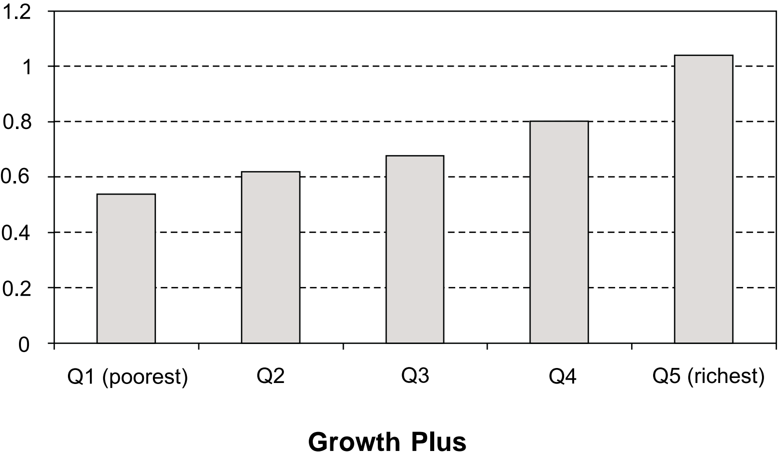
What Do Subnational Data Show?

The real story, however, is not as straightforward as it seems. Other variables that have direct impacts on the well-being of the poor may be correlated with the growth variable; if these variables are omitted from the analysis, their impacts would be wrongly attributed to growth. For example, local infrastructure, institutions (e.g., social capital), and agrarian structure vary considerably across provinces and correlate strongly with provincial mean incomes. Not surprisingly, changes in the welfare of the poor during the 1980s and 1990s vary widely across provinces.

Econometric estimation techniques that control for these other province-specific factors suggest a weaker response of the average welfare of the poor to overall income growth. For instance, for the poorest quintile of the population, a 10 percent increase in overall per capita income raises their average welfare by just about 5 percent. This indicates that indeed other factors exert direct effects on the poor's well-being, apart from their effects on income growth itself. Put differently, the quality or type, not just speed, of growth—or "growth plus"—is critical to poverty reduction.

How well has growth affected the welfare of the other income groups? Figure 1 summarizes the differential effects based on provincial panel data for the 1980s and 1990s. It shows that growth tended to disproportionately (and monotonically) favor the higher income quintiles of the population.

Figure 1. **Percent Change in Consumption Expenditure per 1% Change in Average Income**



Growth Plus

If the upper ranges of the income distribution tend to benefit more than proportionately from overall economic growth, what policies or institutional arrangements could enhance the benefits of growth for the poor?

Schooling, if accompanied by improvements in access to markets, technology, and information, raises the welfare of the poor. Complementarities are important, especially in rural areas where infrastructure is grossly inadequate. Returns to schooling for the poor will be higher the more accessible are the complementary factors.

Investment in infrastructure also helps mitigate geographic “poverty traps.” High transport costs can lead to such traps as the poor are impeded in taking advantage of economic opportunities elsewhere.

Changes in economic incentives facing the poor, most importantly the price of agricultural products relative to the price of goods in other sectors of the local economy, have a profound impact on poverty reduction. This result is not surprising: income poverty in the Philippines is a largely rural phenomenon. Of the rural poor, nearly two-thirds are dependent on agriculture for employment and income. Agriculture-dependent households appear to have benefited from the trade and exchange rate reforms in the 1990s. These reforms have effectively reduced the overvaluation of the currency, thereby improving the relative profitability of the tradable sectors, including agriculture.

Where the distribution of land is highly unequal, poverty will be hard to alleviate. Highly inequitable distribution of land breeds social tension and political unrest, thereby inhibiting economic growth. It also limits the ability of the poor to invest in human capital formation and in productivity-enhancing techniques. Given imperfections in credit markets, especially in rural areas, access to land better enables households to smooth consumption during shocks, such as during the Asian financial crisis. In the Philippines, there is evidence that in areas where the agrarian reform program has been successfully implemented, it has had a direct salutary effect on the welfare of the poor.

In land-scarce, labor-abundant developing countries, investment in productivity-enhancing land improvements, such as irrigation and drainage, is an important policy instrument for poverty reduction. Indeed, in the Philippines, irrigation has had a pro-poor

bias. It is land quality, not farm size *per se*, that tends to positively influence the incomes of the poor.

Even local politics matters. The provincial panel data suggest that lack of political competition due to political dynasties hurts the lower-income groups, particularly the poorest. This is consistent with the view that dynasty in local politics adversely affects economic efficiency and, consequently, local economic growth, thereby restricting the access of the poor to basic services and goods.

The political party affiliation of local chief executives also matters. Resources for employment generation and poverty reduction tend to flow more favorably to local governments run by administrators with direct ties to the country's ruling political party (or President).

Conclusion

Evidently, economic growth explains a lot but not everything about poverty. Institutions and other factors do matter, too. Thus, while growth is indeed good for the poor, it is not good enough. How much is not good enough can be investigated further by analyzing subnational data for other countries as well. This approach seems superior to the analysis of aggregate cross-national data. As subnational analysis is extended to more countries, the determinants of poverty reduction—besides growth—could be more clearly identified, thereby helping better inform country poverty reduction strategies and policies.

References

Balisacan, A. M., 2001. "Poverty in the Philippines: An Update and Reexamination." *Philippine Review of Economics* 38(1):16-51.

Balisacan, A. M., and E. M. Pernia, 2002. Probing Beneath Cross-National Averages: Poverty, Inequality, and Growth in the Philippines. Working Paper Series, Economics and Research Department, Asian Development Bank. Forthcoming.

Bautista, R., and G. Tecson, 2002. "International Dimensions." In A.M. Balisacan and H. Hill, eds., *The Philippine Economy.* New York: Oxford University Press. Forthcoming.

Dollar, D., and A. Kraay, 2001. Growth Is Good for the Poor. World Bank Policy Research Paper No. 2587, Washington, D.C.

ERD POLICY BIRIEF SERIES

No. 1 Is Growth Good Enough for the Poor?
Ernesto M. Pernia
October 2001

2 India's Economic Reforms
What Has Been Accomplished?
What Remains to Be Done?
Arvind Panagariya
November 2001

3 Unequal Benefits of Growth in Viet Nam
Indu Bhushan, Erik Bloom, and *Nguyen Minh Thang*
January 2002

4 Is Volatility Built into Today's World Economy?
J. Malcolm Dowling and *J.P. Verbiest*
February 2002

5 What Else Besides Growth Matters to Poverty Reduction? Philippines
Arsenio M. Balisacan and *Ernesto M. Pernia*
February 2002

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