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ARTICLES

COMMENTS

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PRE

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A joint publication of the UP School of Economics (UPSE)
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Comment on "Mapping feasible routes rowards economic diversification and industrial upgrading in the Philippines"

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The paper is very rich empirically and adds to our understanding of Philippine industrialization.

My first general point is that the Philippines is home to some really high-quality analysis of industrialization, most of it, of course, within the University of the Philippines School of Economics itself. These volumes of works provide a rich intellectual narrative that the paper does draw on and arguably could draw on more.

The second general point is that the paper should try to further put the story in some kind of comparative international context. I like the way the authors have drawn out quite a lot of comparative stories, statistics, and policy in the analysis. I have a couple of other observations on situating the analysis in a regional and global context which may be important to consider. First, I think that it is important to remember when discussing industrialization that manufactures are mainly tradable, and so the global context matters. The big global industrial story over the past 20 to 30 years is the emergence of China on a massive scale, initially producing labor-intensive products, and now products that are much more skill-intensive. The scale is such that it has lowered the global price of manufactures. For countries like the Philippines who are, in a sense, in the same game, the relative cost factors are important. That is, China has lowered the global price of manufactures, and so it is actually harder in some ways to compete in the international marketplace.

Another point to keep in mind is the international organization of global manufacturing production. Here, I suggest that the authors make a bit more of the fact that so much of industrial output, especially in East and Southeast Asia, is occurring in what is sometimes called global production networks or global value chains. More than half of intra-ASEAN and intra-East Asian trade occurs within these networks. In that sense, for rapid industrialization, countries inevitably have to be in that game. I think the authors can emphasize that the Philippines has somewhat missed out on these opportunities. Prema-Chandra Athukorala's chapter in the book *Pro-poor development policies: lessons from the Philippines and East Asia (essays in honor of Arsenio Balisacan)* calls the performance of

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the Philippines a case of "arrested industrialization." It is striking what a minor participant the Philippines is in these global production networks compared to the countries that the authors mentioned. So when the authors discuss upgrading and diversification, I think they need to think about it at least partly in this context.

It is not rocket science how to get into these production networks. In fact, if I understand correctly, the Philippines participated quite strongly in them during the reforms of the 1990s, but it has somewhat dropped since. This relates to my next point. In the regional-global context, the star currently in these networks is Vietnam. Vietnam's share and participation in these networks is rising rapidly; the Philippines, by and large, is not. Furthermore, amidst the global trade and economic uncertainty, concerning whether countries are going to be forced to be in either a China- or a US-dominated world, firms are diversifying. Vietnam has been the first country to which risk-averse firms are diversifying, which tells something about the opportunities that Vietnam seized through its attractive policy reforms. This is despite Vietnam being a latecomer, one that was historically way behind the Philippines. I think part of the story links to "route two" in the schema presented in the paper presented but I think that this general story should be brought out more clearly.

Several other points need to be mentioned. In the case of sectoral analysis studies, I think it is important to stand back and also look at the aggregate story for the economy as a whole. It comes out quite clearly in the latest ADB *Asian Development Outlook* that the Philippines is doing pretty well comparatively. The authors have rightly emphasized that the Philippine service sector has been performing strongly. So, the general question needs to be posed, if the economy is growing at five or six percent, does it really matter which sectors are leading and which sectors are lagging?

Next, I think it is implicit in the analysis—but I suggest making it more explicit—that when we are talking about competitiveness, which is a pathway to diversification and upgrading, it is important to go back to the basics. In this light, I think it is worth unpacking some of the variables used in the econometrics. For example, just to highlight some important factors on the supply side, indicators for education suggest that the Philippines is lagging somewhat. Another is logistics performance indicators such as port competitiveness, and also the costs of utilities. In this area, the Philippines, while it has improved, still lags in the region. Lastly, a discussion on basic competitiveness indicators such as access to financial instruments may be added since these are foundations for diversification and upgrading, particularly for SME operations.

A few additional points could also be referred to in the paper. First, since we are talking about tradable goods, it would be useful to discuss whether trade policies and exchange rates are a constraint. Second, sometimes case studies can be illuminating because they are illustrative of some of the issues discussed in the paper, and it would be interesting to briefly make reference to them. A classic case in Southeast Asia would be the automotive industry, where Thailand moved pro-actively to become the regional hub, even though the Philippine auto industry was established earlier. Thirdly, care must be taken in classifying activities as “low-end” or “high-end’ using old factor-intensity classifications. Multi-product industries like electronics, which are fairly low-end in lower-wage economies, can also be highly R&D-intensive in advanced economies. Fourth, the paper could also touch on another opportunity that Philippines probably missed out on, or at least it could have grown much faster in, which is the traditional labor-intensive products like footwear (e.g., the Marikina footwear industry). Fifth, the question of how minimum wage regulations might have affected the competitiveness of some industries might deserve mention.

Lastly, in an era of heightened uncertainty and volatility, it may be worth saying a little bit about how this connects to the authors’ story. It does, for example, connect to diversification. We learned during the pandemic that countries cannot just rely on international markets for supply, and that there may be a case for thinking about how to ensure that there is at least some industrial capacity in certain strategic sectors. Moreover, supply chain disruptions have occurred well before and even after the pandemic due to wars and climate issues and other factors. One current example is how China could (and has) imposed economic sanctions on the exports of trading partners with which it has disagreements. In the current circumstances of strained bilateral relations, and given China’s massive scale, is this an issue that Philippine policy makers should worry about, and if so, what should be done? This is another diversification issue to contemplate.

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