Myths and Fallacies in Economic Policy Debates

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A fallacy is often based on a correct argument but applied to a wrong set of circumstances. A myth is worse than a fallacy because it is not true or correct. Myths and fallacies are used across the spectrum of debates on economic policies. Some fallacies keep acquiring a life of their own, and the object of this paper is to expose them as such. The fallacies discussed are often used in debates on industry and trade, social amelioration and macroeconomics. Specifically, the first of these fallacious arguments falls under the protectionism and industrial policy. A second group of policies relates to debates designed to help improve the condition of the poor. A few important examples are cited in the area of national economic management.

MYTHS AND FALLACIES IN ECONOMICS ARE OFTEN ENcountered in policy discussions, as well as in more theoretical arguments. Whether used intentionally or not, they are the result of ignorance about economics or the economic effects of the policies being discussed.

A fallacy is often based on a correct argument but applied to a wrong set of circumstances. This is what makes it a fallacy. One example is this: A policy that is designed to produce a short-run outcome is kept for a long time to produce a similar long-run result. Many common fallacies are of this type.[1]

A myth is worse than a fallacy. A myth is a story that cannot be true, like the story of Superman or Atlantis. It is a fairy tale. Used in an argument, it is an untruth. Of these two forms of stupidity, myths are probably worse, since they fail the test of reality not only in certain circumstances but also in principle.

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Little is new. The myths and fallacies of today are the same myths and fallacies of yesteryear. Myths and fallacies are used across the spectrum of debates on economic policies. Some fallacies acquire a life of their own, and it is best to expose them as such. These fallacies are most common in the discussion of policies affecting industry and trade, social amelioration and macroeconomics. The social policy arena is especially full of contentious arguments. A particular economic policy is often used to justify a social objective that is contradictory to the achievement of that objective. It is often the case that the policy that is employed is the wrong tool.

THE FALLACY OF PROTECTION AS A TOOL OF PROGRESS

IN the realm of industrial policy and trade, the dominant argument that has been used often in the Philippines is to stress the importance of protection of industry as the means for achieving industrial and economic growth.

The reverse of the fallacy of protectionism is an argument for the promotion of industry based on the idea of selling to other countries to produce a trade surplus. This line of thought, known as mercantilism, is an equally fallacious argument for industrial progress. However, in the Philippines the mercantilist argument never had a chance, which was just as well.

The protectionist prescription dominated the policy landscape for decades. Our leaders embraced protectionism when they crafted the Constitution in the 1930s. The NEPA (National Economic Protectionism Association), Philippine Chamber of Industries circa 1950s and 'Filipino First' were a potent combination of organizational clout and slogans in this respect. Protectionism was a kind of flag-waving. It prescribed various forms of limitations against foreigners and foreign entities, ranging from the distribution of goods at retail, promotion of investment, ownership of economic assets and participation in banking and finance.

What follows are examples of fallacious arguments with regard to protectionism.

> Fallacy: 'Protection of industry is the best way to achieve economic progress. Protection will strengthen fledgling industries by assur-

> ing them a larger market. This large market would become an instrument for improved efficiency and growth.'

This argument has long been proven wrong (and at a high cost!) in the national experience. Yet we still get many commentators proposing protection as a principal means of encouraging industry. Many highly protected industries that were supported by policy in the past became a burden to the people and the government, and even the enterprising businessmen who made short-term profits for themselves. For these businessmen, the short-term profits might have been welcome in the beginning. This was in fact one reason why many industries and Filipino entrepreneurs seized the opportunities of industrial import substitution during the 1950s and the 1960s. Over time, however, the continuous prosperity of these industries depended only on continuing favors granted by the government, not on their internal dynamics of growth. This came either from the protracted continuation of bad policies or the grant of financial favors from the financial institutions owned by the government.

As a result, it became difficult for the country to pursue structural reforms in the economy, especially when those reforms required the liberalization of tariffs, investment rules and participation by more investors and more industrialists. Protected industries became the obstacle to further progress, improved economic efficiency and economic redirection.

Indeed, it is not an exaggeration to say that among the worst victims of protectionism were the businessmen themselves. They were enticed by policy signals into committing their resources and their future to highly protected business activities. When the first signs of lack of sustainability of their enterprises became evident, they developed the habit of turning to the government for further protection and for additional privileges. If they were not wiped out by the failure of the business, they became perennial complainers against sensible change in policy. In this way, they became obstacles to structural reforms.

The costs to the nation were substantial. The protectionist policy made Filipino workers poorer. Of course, those employed in the industries had their jobs. But because the protected industries failed to experience productivity growth, wages failed to rise. In the end, when the

industries could not survive, these same workers lost their jobs. The phenomenon of Filipino workers seeking employment abroad is in fact a shameful condemnation of the failure of industrial policy to provide the employment needed at home.[2]

The government suffered. It failed to realize new revenues that it had hoped to receive from viable, tax-paying industries. And it gave away a lot of tax benefits and subsidies, direct and indirect, which comprised the incentive package to encourage industry. Many state lending institutions, the first credit window of the industrialists, bankrolled the failures. In the end, these institutions were saddled with loans that could not be collected. They themselves had to face the prospects of bankruptcy without further state subsidies. The other private banks that followed the lead of the government experienced the same problems.

The nation suffered. The savings of the nation were squandered. These industries and their businessmen were rewarded with credit, tax and other fiscal benefits so that they would grow into sound industries that could stand on their own and lead the economy further. But they could pay back to the nation very little in terms of efficiency gains.[3] Savings are supposed to finance sound investments. They represent the nation's ticket to growth in the next period. The failure of the investment means the waste of that investment and the reduction of future prospects.

The consumers suffered the most. They paid high prices for poor quality products. Protectionism often began by preventing competition from reaching the local market or pricing it out through prohibitive tariffs or through import controls. This practice provided enormous monopoly benefits to local industrialists. Thus, consumers were denied a choice of products or goods.

> Fallacy: 'The economic success of our Asian neighbors is due to the strong role of the state in promoting and protecting industry.'

If this proposition were true, there would be many, not few, successful Asian economies. Moreover, almost all those that have adopted a strong role for the state to promote growth would have become economic successes. And surely, this would include our country even during the earlier decades. But the fact is that these successful Asian coun-

tries were indeed only a handful of success stories for a long time and there is a much longer list of countries that have adopted protectionist policies whose experience is the opposite of high growth. What they achieved were low growth rates, inefficient industries, falling productivity and massive unemployment.

The list of countries that have attained high and extraordinary economic growth rates over a sustained period in recent times includes South Korea, Taiwan, Singapore, and among the latecomers, China and our other partners in the Association of Southeast Asian Nations (ASEAN). In spite of the recent economic crisis in Asia, these Asian countries remain a unique set of countries that have achieved high rates of economic growth over a sustained period. However, it is not protectionism that explains their success. What distinguished many of these successful countries was that they used the market mechanism effectively and sensibly in much of their policy endeavors. They allowed the factors of production in their economies to be priced in accordance with market forces. When some other policies—including highly protectionist elements—interfered with those pricing policies, they utilized other policy tools to correct any price distortion induced by protection. In general, they encouraged greater flexibility in the pricing of resources and promoted investments in accordance with those pricing decisions.

Early during their industrialization period, they did not price labor too high and thus encouraged labor-intensive industries. They priced capital more sensibly—that is, by setting a realistic interest rate to encourage savings and therefore investments and by not excessively subsidizing capital acquisition with low interest rates. They introduced domestic policies that reduced the inflation on basic goods like food. They allowed the raw material inputs used by industry to be priced at world prices, especially when they were encouraging their exports. They also acquired raw material inputs at world prices, without slapping any duties on their importation.

The factors of production were priced relatively more correctly, thereby reducing the gross and adverse impacts of protective price distortions.[4] In short, the net value of their actions as state promoters of industry was to compensate for the many problems that the policy of protection brought. The other components of their industrial policy

allowed them to correct for the distorting effects of their protection policies.

> Fallacy: 'The size of the domestic market depends on the size of the population.'

Per capita income is the primary driver of the size of the domestic market. The number of people does not increase the size of the market unless the people have income that is high enough to represent actual demand for goods. An economy with a small population can have a very large market if its market is the world (for example, Singapore and Hong Kong). For some products, the size of the market in Hong Kong or Singapore is so much larger than our country, in spite of their small population. Add the size of the export markets for their goods and the comparison is in large multiples.

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Until India and China, the two largest countries with the largest economies in terms of population, began to improve their respective trade and industrial policies by encouraging some competition in the industries that they began to liberalize, these two countries had only potential to create a market. As their domestic per capita incomes began to rise because of productivity growth and wage increases, the size of their domestic markets consequently enlarged.

> Fallacy: 'Economic development depends mainly on industrialization. And industrialization begins with heavy industry.'

This view is—pardon my saying so—pigheaded. The true calculus behind economic development is based on economic efficiency and comparative cost advantage. When the argument starts with the assertion that economic development is not possible without industrialization, be sure that the next sentence says that the industry at the initial stage needs protection.

We should be reminded that some progressive countries never had a steel mill. Steel mills—and power, fertilizer, and cement plants, etc—grow where the market can justify it. In short, it is more correct to state

that industrialization is a consequence of economic development rather than its cause.

> Fallacy: 'Planners know better than the people how to order economic and social priority. Social planning is the key to improving the welfare of citizens.'

The Soviet system was based on the belief that the central planner knew better than the people. The Soviet Union no longer exists and the countries of Eastern Europe formerly within the Soviet bloc now view their subjection to the economic system of that country as a history of lost opportunities. This is why these countries are now wasting no time in emulating their Western neighbors.

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Until China decided to experiment with economic liberalization at the level of rural communities in the 1970s, it was destined for the same fate. Then, it gradually broadened the experiments to special economic zones, using market tools as encouragement for enterprise and economic activity. Now, China has integrated many of the lessons that it learned from these experiments and from contacts with the capitalist world. And it is on course to undertake further economic liberalization in many parts of the economy. Indeed, the price is right! China is on course to become a member of the World Trade Organization, the ultimate organization of capitalist countries.

> Fallacy: 'Government planners and bureaucrats know better than businessmen.'

This kind of thinking continues to afflict some government planners in the same way that it deluded central planners in the failed economic systems mentioned above. I will not be surprised if some of these planners are still found at the National Economic and Development Board, Bureau of Investments, and many government departments. Sometimes one hears proposals from some quarters for the government to do more strategic planning, targeting industries and other activities, etc. Yes, this kind of thinking still exists even in the private sector.

What is critical for government planners to do is to set the right conditions for doing business. Some of these measures would be along the following lines: improve policies to ease the burden of bureaucratic and administrative requirements on business; remove complex provisions that only produce intermediaries and experts who raise the set-up costs of doing business; and declog overburdened economic infrastructure by channeling investments to them. More than ever, the most important work of government planners is to allow prices to settle at the right levels by using the market mechanism, not the big stick of regulation, control or state power.[5]

Years of consultations with private businessmen will not produce the right winners in industry if the prices of all the factors of production—labor, capital, inputs from abroad and from within (such as electricity, infrastructure in transport and communications, etc)—are unfavorable toward making those industries efficient. The businessman who stakes his investment and who shoulders the risks of failure knows better than the government bureaucrat how to solve his own business problems.

The impressive expansion of Philippine exports in recent years, especially in manufacturing (for example, the semiconductor exports), provides a counterpoint to all the foolish debates in the past about industrial policy. For the first time, the country has been experiencing a sustained double-digit export growth rate and a taste of export surpluses. Hong Kong, South Korea, Taiwan and our other Asian neighbors began to experience the same phenomena early during their discovery of export prosperity at least two decades before we began to experience ours.

During the years when our Asian neighbors were flourishing, the standard thinking in the country was focused on targeting and identifying export potentials, not on clearing the path for policies to make businessmen decide what exports would make profits. The recent surge in exports was less the result of targeting exports than of preparing investment promotion policies where industries could take advantage of the country's comparative advantage in trade. It is also a major phenomenon that none of the import substituting industries that were

promoted in a previous era had become the basis of this export prosperity. Exports began expanding in impressive terms when private investors began to take advantage of the opportunities offered by the Philippine economy—the promise of economic liberalization and the commitment expressed by the government to pursue those policies. This change in policy outlook ushered in structural reforms in many directions of the economy. They included the following: reduction of tariffs and removal of quantitative controls on imports; adoption of a market-based exchange rate for the peso; liberalization of capital flows, especially on the repatriation of profits by foreign investment; and opening of banking to foreign investment.

Additional impetus was provided by developments within ASEAN. The ASEAN Free Trade Agreement (AFTA) area has provided a major magnet for future investments by industrial countries seeking further markets. The AFTA is yet to come, but the agreement has been forged and the calendar for the future expansion of the regional economy has been set. So the decisions concerning market potential, exports and future investment needs that affect the future in the Philippines (and elsewhere in ASEAN) are being followed by economic agents interested in the prospects of the larger ASEAN market.

The successful growth of the Philippine export sector has also been strengthened by an improvement in the domestic investment climate, aside from the measures and developments just mentioned. The establishment of industrial estates has helped to reduce the set-up time for locational decisions made by new and expanding investments. The transformation of the former military bases into industrial economic zones for exports by the early 1990s helped to increase this success. Private industrial estates set up by private enterprises along the Southern reaches of Manila (the Calabarzon region) have also encouraged rapid growth of new factories. Within these zones, businesses have been able to have their imports administered more easily by customs and the opportunities for nefarious practices that killed businesses with undue delays have been significantly reduced, if not eliminated. Here also, the factories can secure their raw materials at world prices.

FALLACIES OF A BIG HEART FOR THE POOR

SOCIAL amelioration policies should be undertaken with an understanding of their true objectives and direct costs to society. Knowing their direct costs would make it possible to weigh the correct strategies for achieving the goals of social development.

The problem is that social amelioration policies are often undertaken without this awareness. Policy makers hate to see the tax bill, but they see what the immediate benefits that certain quick fix measures would bring. So they devise means to ameliorate social conditions indirectly. It is this folly that makes them choose policies that seem to correct the problem. They shift the cost to others. Little do they know that the total cost is borne by society and by the same people for whom the amelioration policies were supposedly intended.

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This is the formula of the bleeding heart reformer: If low income is the problem, raise the income by legislating it. If high prices are the problem, reduce the price by regulating or controlling them.

The appeal of these measures to social reformers is very high. They think that such measures help the cause of the poor. In fact, the policies when adopted inevitably contribute to the further immiserization of the already poor and failure to uplift the condition of other segments of the population who are not targeted by the policies. For instance, such policies could worsen the conditions of the middle class, which as a group are really bystanders in the framing of social policies for alleviating the conditions of the poor.

The measures succeed only in a temporary alleviation of the immediate condition. They are mere palliatives. It is not surprising that the policies, when adopted, could become long run causes of misery for the same groups of the population who are supposed to benefit from them. Below are examples of the fallacy of the big heart for the poor.

Fallacy: 'Raising the national minimum wage periodically to a level that catches up with inflation will improve income distribution and therefore the welfare of labor.'

If inflation is the issue, the correction lies in anti-inflation policy, which is essentially a macroeconomic approach. Raising the level of the minimum wage would benefit the employed person near the minimum wage level. However, this person could lose his/her job if the employer is required to pay a higher wage and the business cannot afford the new wage bill. If the laborer does not lose his/her job because the employer can afford the additional wage cost, it is possible that the next person in search of employment might find it harder to get employed.

If the level of employment in an economy is high (for instance, if there is full employment or a very low rate of unemployment), a minimum wage hike would probably benefit all employed laborers. And there would be few, if any, losers. But consider the prevalent condition of a high unemployment rate. In 1998, the unemployment rate in the country was estimated to be 9.4 percent of the labor force. During good economic years, the unemployment rate was not lower than 8 percent of the labor force. In fact, not all people who are employed receive the minimum wage. About 34 percent of employed laborers[6] in the country are likely to be receiving less than the minimum wage. This estimate is probably quite optimistic.

A high rate of increase of the minimum wage could also hurt many of those who already have employment and whose productivity is way above the minimum wage. Their wage increases might be sacrificed to pay for the wages of those whose productivity is not justified by the higher wage.

A high wage rate arises because of the strong demand for labor relative to the existing supply. A strong demand for goods translates into a high demand for labor. It is also related to the productivity of labor. Countries with dynamic economies—those that develop efficient industries and strong export performance—are likely to have a strong demand for labor and therefore their wage rates go up fast. Look at the examples of our successful, immediate neighboring countries.

It is clear that Philippine labor policy has prematurely emphasized welfare legislation ahead of job-producing employment strategies. This

has ultimately caused a great majority of laborers in the country to suffer from low-income unemployment, if not from unemployment. The economically successful countries of the Asian region have jobs aplenty today because they emphasized investment promotion, job creation, on-the-job training and economic efficiency in industry as employment creating policies. These countries have very high labor productivity. They are also countries where wage rates are quite high relative to Philippine wages. Therefore, it is not surprising that Filipino labor (even those receiving much higher wages than the required minimum wage) seek jobs in these countries as temporary contract laborers.

The issue for current policy makers is how to redirect labor market policies so that it is possible to rapidly exhaust the open supply of labor available at low wage rates. This requires raising the demand for jobs within the economy through a higher level of investments that at the same time creates job opportunities per peso of additional investment. It is also important to formulate policies that make labor highly productive. In such a setting, the supply of unemployed labor would be absorbed in the productive sector and wage rates would rise fast, as was the experience of many economically successful Asian neighbors.

It would also be useful for the government to help steer organized labor sector leadership to seek policies that help rather than obstruct investment. Actually, the stance of organized labor has improved in recent times, but more work along the lines of creating a national consensus for job growth with industry is still needed. As long as many laborers do not benefit from advanced labor laws, the gains of labor are limited. In a more understanding environment of cooperation, the demand to raise the minimum wage among the labor class will become much more realistic.[7]

> Fallacy: 'Price controls or price regulation will make goods affordable and will improve the welfare of the consuming public.'

Price controls are often used as the solution for correcting the high prices of basic commodities. In extraordinary times, they might be needed as temporary measures. But whenever they are resorted to, it would be useful to make provisions for their temporary character. A definite date for their removal should be part of the policy. Once in

place, however, price controls are difficult to remove. Price controls immediately create an active constituency of interest groups for their prolongation.

The coalition of interest groups to retain price controls and make them a feature of a long range policy includes organized groups that are the immediate beneficiaries of controls, social reformers with compassionate concerns (bleeding hearts), and politicians whose gains are populist in nature.

What is bad about price controls is that they often have very distorting influences on incentives for market players. For instance, price controls prevent the supply incentives of sellers from being realized. Thus, the supply of goods might even become more constricted. Price controls in this sense reduce the natural incentives available to producers to produce more of the goods under control or to bring existing inventory fully to the market.

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Oftentimes, price controls require government to import the essential goods. By itself, this could also contribute to macroeconomic imbalances, which are another problem to deal with.

High prices, as already mentioned, are likely to be part of a macroeconomic issue. An anti-inflation policy stance in macroeconomic policy would require balancing aggregate demand with aggregate supply.

> Fallacy: 'Rent control enables the poor to enjoy affordable and cheap housing.'

Rent control in its present form was introduced when, under Martial Law and in response to the energy crisis, the President decided to control many types of prices affecting vulnerable groups in the population, including rent for housing. While all price controls were gradually lifted, the one on low rentals has remained. Every time the rent control law is about to lapse, legislators find a way to extend it—by controlling the percentage of rent increases that can be charged.

In the past, retired public officials and school teachers as well as enterprising businessmen supplemented their retirement years by in-

vesting in apartment dwellings to be rented out. In this way, the supply of dwellings for the poor increased. Nowadays, only the foolish will do such a thing. The private sector has ceased to build apartment dwellings for rent, except those cutting up their existing housing into rooms for rent or to those renting houses for the very rich. This explains in part the existence of a worsening and serious housing shortage in the country. The housing gap has grown bigger. The government has been forced to play a larger role in housing provision. But its efforts to set up a large low-cost housing program as a means of providing relief for a population facing poor housing availability is constrained by financing problems.

So long as the rent control stays, new private investments in the provision of housing for rent and for sale will be discouraged. In the meantime, the government-provided housing program requires a huge subsidy that is not likely to be sustainable. The outcome of this is that among the poor middle income public officials and private sector employees who can afford to invest in housing for their own use, the only housing available is often in subdivisions quite distant from their place of work. In the meantime, the phenomenon of squatting has become worse. The country's cities are full of shanties and illegal dwellings.

FALLACIES IN MACROECONOMIC MANAGEMENT

MACROECONOMIC policy is about the management of aggregate expenditure and aggregate supply of output in the context of relative price stability. Two common fallacies in this regard are discussed below.

Fallacy: 'A strong peso is good for the economy.'

This argument used to be a mantra for those in charge of foreign exchange policy. At least, this was their public posture. A strong peso makes the price of imports cheaper, but it also has the effect of making it more costly to export. Thus, a strong peso encourages a balance of payments deficit. In this way, it could become a source of a future balance of payments crisis and therefore hurt the economy.

(The other face of this argument is that a weak peso will be good for the economy. A weak peso would surely make exports attractive to companies, if that were the objective. In fact, economies such as South

Korea and Taiwan in the 1960s until the 1970s used this policy to encourage their export industries to grow. It was a correction of their highly protectionist policy regimes to undervalue their currency at the time. That allowed imports to be unduly more expensive, except those used as inputs to the export industries. The undervaluation of the currency helped these firms to seek an outlet to the world by exporting their products. But the strategy worked as a corrective to the highly protectionist regimes in existence at the time.)

The rate of foreign exchange is a powerful price that could create imbalances in the economy when it goes out of kilter with what appears to be what the market would bear. Stabilizing it is sound policy, but stabilization means allowing it to seek the correct level.

> Fallacy: 'To keep the fiscal deficit under control, it is enough to keep watch on the national government's budget.'

Keeping watch on the national budget—that is, making sure that government expenditures are reasonably covered by tax collections—is very important. But that is only about four-fifths of the issue. The government must also consider how enterprises controlled by the government are being run. To what extent are these enterprises maintaining profitable, or at least viable, operations? These off-the-budget agencies are not truly off-the-national budget indefinitely. If they incur losses through the years, pretty soon they are part of the budgetary problem.

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If the National Food Authority (NFA) is required to sell rice below market cost and to buy *palay* at a high price, pretty soon its capital would be wiped out. (This assumes that waste is not happening in the administration of the NFA's functions.) The agency's credit standing would be ruined. It would not be able to finance its operations, much more pay for its loans, if the capital is impaired. The national budget would then come to the rescue by absorbing the losses or 'recapitalizing the agency,' which is the same as absorbing the loss.

A simple review of the operations of many governmental agencies and that of the instrumentalities of the national government would reveal that many of them have incurred major losses. In the end, the national budget has had to take care of the problems. Any good analyst can construct a financial history of the following government agencies, entities and corporations, as follows:

The National Power Corporation has a huge mountain of losses today. That is why it is being privatized and Congress is dealing with the problem of how much the 'stranded costs' of power generation in the past will be absorbed by the budget.

The Central Bank of the Philippines had to be reinvented in the early 1990s. Its fiscal losses from subsidized credit, guarantees of external debt and foreign exchange losses over the years had prevented it from effectively supervising financial reforms. Its financial restructuring became a requisite of sound policy.

The Philippine National Bank and the Development Bank of the Philippines were two financial institutions designed to help finance economic development. In the process, they became the milking cows of politically induced loans and loans to the import substituting industries of the past, and of bad loans to the sugar sector and other industries. Appropriating new capital to augment their depleted capital from the national budget and transferring their non-performing assets to a national government instrumentality or to a subsidiary often created the appearance of a strong balance sheet.

The predecessors of the National Food Authority were the NARIC (National Rice and Corn Corporation) and the RCA (Rice and Corn Administration). They had to be reinvented after they lost their capital through subsidy and inefficient operations. The NFA is now facing a quandary over the indirect subsidies to keep the prices of basic staples low that they resorted to. The problems afflicting the National Fertilizer Authority are of the same nature.

The pioneer industrial ventures of the National Development Company have cost the nation a lot of resources directly and indirectly. A review of the portfolio of this company will reveal that there are many projects that are sustained only by subsidies from its resources, which the government keeps providing.

Congress is currently discussing the recapitalization of the Housing Insurance and Guarantee Corporation (HIGC). This corporation was set up to provide guarantees for housing loans in support of the low-cost housing projects of the government. The corporation has guaranteed many housing projects that have remained unpaid. It is losing, if it has not yet lost, its original capital. The corporation is seeking new capital of P50 billion from the national government. The recapitalization of HIGC, a ritual repeated for many other losing public corporations that do not follow prudent business activities, means that the national budget will eventually be refinancing the losses of this corporation.

Need I say more?

NOTES

1. Fallacies remind me of a story once told by one of my former professors years ago, Evsey Domar at MIT. People in a remote village observed that wherever there were epidemics, doctors would congregate. The people concluded from this that the cause of epidemics were the doctors. And so, they tried to solve the problem by killing the doctors!

2. It is to the credit of this country that, at least, labor is allowed to migrate to better paying occupations. In fact, in a curious turn of events, the Department of Labor is often seen as an agency of the government encouraging labor to find jobs abroad! At home, it behaves to protect the rights of labor, and in the process, often becomes an obstacle to increasing the availability of jobs at home. The cost of labor migration is often not counted as a loss in the educational investments that the country has made in the budget for public education. It seems that the foreign remittances of overseas contract workers are often seen as a source of economic bounty.

3. The studies of Philippine economists, based at the UP School of Economics from the 1960s and from the Philippine Institute of Development Studies since the 1970s, have documented many of these results. See for instance, Romeo Bautista, John H. Power and Associates, *Industrial Promotion Policies in the Philippines, Philippine Institute for Development Studies* (1979), for a survey and analysis of the issues.

4. An example is that in general, these economies did not introduce high minimum wage legislation, but they promoted the rapid entry of investments so that the demand for labor would expand fast. Although they provided cheap interest rates for industries that engaged in exports, for the general round of industries, including those designed mainly to serve the domestic market (the import substituting industries), there were no interest rate subsidies coming from government

financial institutions. Also, interest rate policy was designed essentially to match the scarcity of capital, so that savers were attracted to serve. These were the types of policies that I wrote about way back in the 1960s. See GP Sicat, Economic Progress in South Korea and Taiwan, Discussion Paper 69-2, UP School of Economics.

5. There are some exceptions when the market mechanism fails, and supplemental government effort has to be undertaken. These situations are most common in those processes of production with 'external effects' like pollution, and in industries with a naturally declining cost. In the latter case, the case for direct subsidy is strong.

6. People aged 15 years old and older in 1998 numbered 47.4 million. About 66 percent of these persons, or 31.3 million, were in the labor force. During the same period, around 1.6 million were government employees covered by the GSIS and 20.2 million were members of the SSS. All in all, therefore, around 21.8 million were covered by social insurance. This number of laborers would likely comprise the labor force that is covered and receives the minimum wage. A large number of the people who are not covered by social insurance could be people in search of any work. If we assume that four percent of those covered by social insurance are pensioners and therefore not in search of work, then 20.9 million members of the labor force are at least earning the minimum wage. This is only 66 percent of the total active labor force. I find this estimate to be on the high side. There is always a small proportion of those enrolled in the GSIS and the SSS who actually float between a state of employment and unemployment. The statistics of membership in the two social insurance programs report gross number. They do not include net withdrawals from the system. A little more than 34 percent of Filipino laborers are likely to be excluded from the benefits of the minimum wage rate. These statistics are derived from various tables from the 1999 *Philippine Statistical Yearbook* produced by the National Statistical Coordination Board.

7. For example, some legislators recently proposed to raise the minimum wage by legislation. A bill in Congress is said to suggest that the minimum wage be increased by P125 per day, which is an extreme demand, in view of the unemployment problem in the country.