

Why the Poor Remain Poor?

*By Dante B. Canlas**

Computing poverty lines and incidence by households using data from the 2006 Family Income and Expenditures (FIES), the results indicate that matters have taken a turn for the worse since 2003. What account for this turn of events? To answer this question, I have put together insights from some papers that some colleagues and I are writing for a volume entitled *Causes of Poverty*. Let me start with the main factors behind the weak or absence of progress in the fight against poverty.

Causes

Demographic factors

Based on the 2000 Census of Population, which is the only one available at the moment, annual population growth is 2.36%. As of 2003, total fertility rate stood at 3 live births per woman during her reproductive life. The dependency ratio is about 64%. All of these cited statistics are high by the standards of middle-income countries in East and Southeast Asia.

Poverty incidence by household in 2003 stood at about 25%. Family size correlates positively with poverty incidence. Poverty incidence, for example, in families with two children is 9.8%. This rises to 31.1% in families with 5 children, and further up to 54.9% in families with 8 children.

Households with large family sizes, on the average, end up with low per capita investments in education and health for their children. As the number of children increases mean expenditure for education per student declines. Similarly, health expenditure per sick member of the household declines with the number of children. With meager investments in human capital, family members end up with low wage offers once they assume their roles as workers.

Intergenerational Correlation of Education and Health Outcomes

It's getting to be an empirical regularity: education and health outcomes tend to be correlated across generations. The educational attainment and nutritional status of children of well-educated parents tend to be high. Many factors are no doubt at work in producing these outcomes, including, demographic, biological, and financial. About the latter in the context of education, it is well-known that education, particularly for tertiary education and private basic education, is largely self-financed. Without credit markets for education, children of low-income families find it difficult to access education. Upon

* Professor, UP School of Economics. Statement read at *A Centennial Conversation: Poverty: Facts, Theories and Remedies* held at NISMED, UP Diliman on January 31, 2008.

entry in the elementary grades, children from poor households without any pre-schooling are at a disadvantage, raising the likelihood of dropping out. At this stage, there is evidence that returns from tertiary education have outpaced returns from the lower education levels (22% vs. 10% in 2004), exacerbating the income inequality between graduates of tertiary education and the rest without college degrees. Similarly, there is evidence that health outcomes are also inter-generationally correlated. In consequence, we observe poverty being transmitted across generations.

Labor Market Roots of Poverty

The operation of the labor market is central to understanding poverty. After all, for most families, the major source of income is labor earnings.

On the labor supply side, the poor, given their high dropout rates, and limited access to education and training and basic health care end up being unskilled and with low productivity. This situation results in low wages and earnings, and high turnover rates. Their spells of unemployment are frequent and of long duration, resulting in foregone on-the-job training.

Meanwhile, on the labor demand side, the sectors and sub-sectors that are emerging require skills that the poor members of the labor force do not have. These are in services like retail and wholesale trade, telecommunications and transport, finance and insurance, and information technology, and health care. Lacking skills, the poor cannot master the production techniques required by these sectors. Meanwhile, in the course of economic development, low-wage, low skill jobs in agriculture, manufacturing, and construction are extinguished. The unskilled become either unemployed or underemployed in informal jobs like hawking, and vending in the urban areas.

The poor end up filling up jobs at the bottom of the occupational ladder. The daily wage in real terms of the highest occupational grouping, namely, government and private sector executives is at least four times that of laborers and unskilled workers. This wage differential has persisted over long periods of time, and seems to be widening over time. In 2004, this real wage ratio was about 4.2; in 2006, this went up to 4.6.

In the aggregate, labor's share of the national income has not improved much. The ratio of compensation of workers to GDP from the *National Income Accounts* is on the average about 0.24. The rest goes to producers' income, some of which though may be labor income. Still labor's income share is low given the country's stage of economic development. This functional distribution of income may be explained by, for one, relative factor supplies. Labor remains the abundant factor of production and as a result draws a lower share of the national income. In addition, as the economy undergoes transformation through time, manufacturing declines in importance with some sub-sectors in services gaining prominence. However, the average real wage of the employed in emerging service jobs is not able to compensate for the average real wage of the extinguished jobs. Furthermore, the preponderance of unskilled workers among the employed also dampens labor's income share.

As employment at low wages persists, poverty incidence remains high. Given that labor income in the form of wages and salaries account for at least 50% of family income, the inability to increase the share of labor income gives us no reason to be optimistic that poverty in the Philippines will be eliminated in the near term.

Meanwhile, the self employed have limited access to financing. They face a high fixed cost of bank credit and are highly likely to be rationed out of formal bank credit. Enterprise growth is hampered with low returns to any investment the self-employed make. As a result, many of them end up poor, trapped in livelihood activities with low returns.

Faced with high land costs and a limited housing market, they squat on idle lands, whether public or private, that lack basic amenities, thereby contributing to environmental problems. Some occupy hazardous sites; when disaster strikes they are pushed deeper into poverty.

What can be done to turn the tide in the fight against poverty? The answers are many, but the most urgent are widely understood.

Overcoming Poverty

An Active Population Management Program

To slow down the population growth rate, an active population management program spearheaded by the national government in partnership with local government units and civil society is mandated.

Scaled up Investments in Quality Education and Health

To produce skilled and productive workers able to master the advanced production techniques that continue to emerge in the era of globalization, investment in education and other forms of human capital like health must be stepped up. To be able to raise the level of scientifically trained manpower, which is needed for technological progress, investment in R&D is indicated. Support to higher education must be geared towards R&D activities.

Sustained Increases in Labor Demand

High labor demand is derived from increased and sustained private investments. Accumulation of physical capital must be complemented with skilled workers and infrastructure supportive of private production. The government needs to increase profoundly its investments in social overhead capital.

Financial Reforms

Clearly, there is a need to address absent credit markets for education and the needs of credit-starved small enterprises. A credit market allows people to shift resources across time. With education loans, claims to future income can be used to finance cost of investments in education in the current period. Similarly, small enterprises without surplus funds can carry out their potentially productive opportunities if they can access credit.

Social Safety Nets

Many of the poor have to rely on social safety nets and other poverty-alleviation programs like food aid to ease their misery. These include the handicapped, elderly, and displaced indigenous people. These safety nets need to be evaluated and monitored to minimize program leaks.