Philippine Institute for Development Studies
Surian sa mga Pag-aaral Pangkaunlaran ng Pilipinas

Why Inequality Matters in Poverty Reduction and Why the Middle Class Needs Policy Attention

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DISCUSSION PAPER SERIES NO. 2015-55 (Revised)

March 2016

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Why inequality matters in poverty reduction

and why the middle class needs policy attention

by

Jose Ramon G. Albert and Martin Joseph M. Raymundo[1]

ABSTRACT

While the Philippines has had a new economic growth trajectory in recent years, the country has had little progress in reducing poverty and in making growth more inclusive. This paper examines trends in macroeconomic statistics, and the progress government has had in its Philippine Development Plan and in achieving the Millennium Development Goals. It discusses the need to address the lack of political inclusion. It also looks into income distribution and income inequality; and proposes a definition of the middle-income class, laying down seven income classes based on the national poverty lines. It also profiles the middle-income class vis-a-vis other income classes given the potential of the middle-income class to sustain economic growth. It argues that government need not only focus its attention to the poor, but also strengthen the middle class toward improving opportunities and reducing inequalities.

Key Words: income inequality, inclusive growth, middle-income class

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1. Introduction

At the end of the millennium one and a half decades ago, 189 member countries of the United Nations adopted the Millennium Declaration that espoused global commitments to poverty reduction, broad-based human development, and protecting the environment. The following year, the UN Secretary General's Road Map for implementing the Millennium Declaration formally defined eight goals, supported by 18 quantified and time-bound targets by 2015, and 48 statistical indicators to monitor these goals, which subsequently became known as the Millennium Development Goals (MDGs). For instance, for poverty reduction, the goal was to reduce by half the proportion of people in extreme poverty from 1990 to 2015, with one of the indicators for measuring this poverty reduction goal and target as the percentage of the population with incomes less than $1 a day in 1990 purchasing power parity (PPP) prices (which has been updated last October 2015 to $1.90 in 2011 PPP prices). The number of targets and indicators for monitoring the MDGS was subsequently further expanded to 21 targets and 60 indicators. Although many conferences of the UN as well as other global meetings involved commitments for action, what was different about the MDGs was that countries politically committed to a specific set of time-bound development targets and that this road map for world development by 2015 had a morally compelling character. Further, the framework subsequently crystallized resources from development partners to assist countries, especially those of less means toward attaining the MDGs.

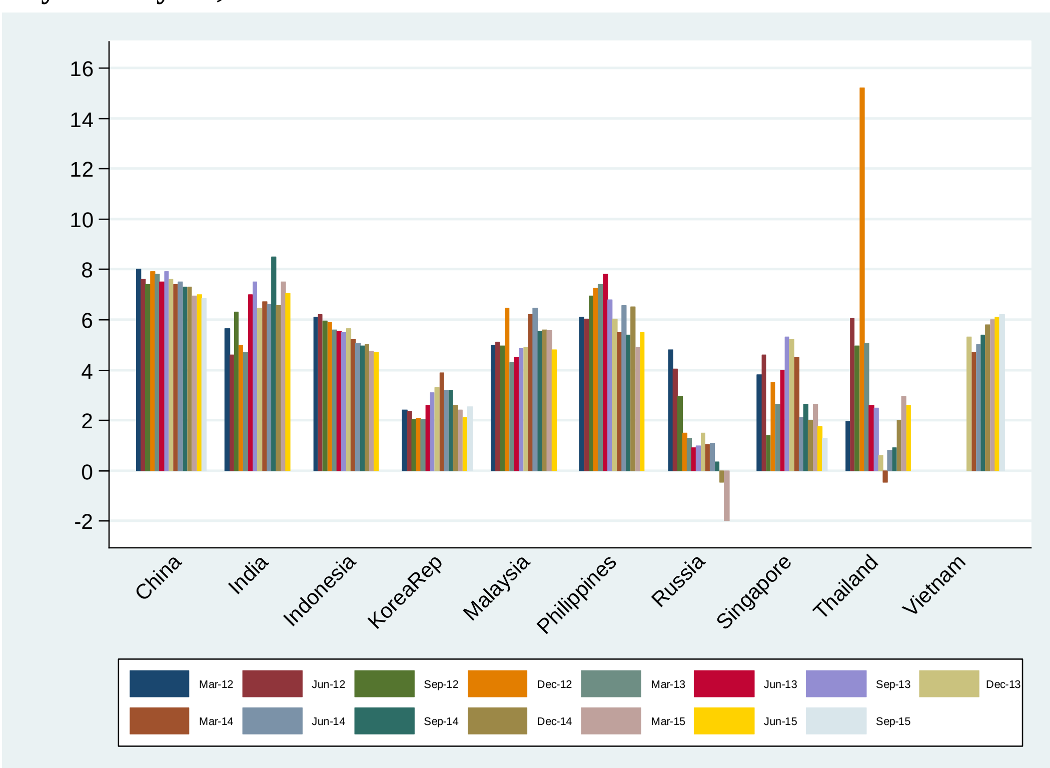
As 2015 comes to a close, the jury is out: new estimates from the World Bank (Cruz et al., 2015) suggest that humanity has met the MDG target on poverty reduction ahead of the 2015 deadline with the proportion of persons living below $1.90 (in 2011 PPP prices) falling from 37.10 percent in 1990 to 16.27 percent in 2010. Much of that progress has been in Asia-Pacific region, particularly on account of substantial reductions in extreme poverty in China and India. For other MDGs, while stunning achievements have been made, the world has fallen short of targets for the MDGs. But while there is much to celebrate about with the stellar performance of the world in the MDGs, there remains an unfinished development agenda with uneven progress across the MDGs, uneven progress across regions and nations of the world in each goal, and uneven opportunities for people to share in the benefits of development, wealth and opportunities.

In this paper, we firstly examine the macroeconomic performance of the Philippines and trends in social indicators in the context of the MDGs. We then look into some challenges in moving forward with the 2030 Sustainable Development Goals (SDGs), particularly given the income distribution. Finally, we propose a definition of the middle income class, and profile this class vis a vis other groups of the income distribution, given the potentials of the middle income class for sustaining growth and prosperity in Philippine society.

2. The Macro Economy, the Philippine Development Plan and the MDGs

For a number of years, the Philippines has been labelled as a "sick man of Asia." Recent economic growth in the Philippines, as measured by growth in the gross domestic product (GDP), has suggested that the country has shed off this reputation and instead moved in a different growth trajectory, becoming part of the list of emerging markets. Economic growth in the Philippines has been at par with, and even surpassed other countries in the Asia-Pacific region (Figure 1).

Figure 1. Quarterly growth rates (in percent) of selected Asia-Pacific economies, year-on-year, 2012-2015



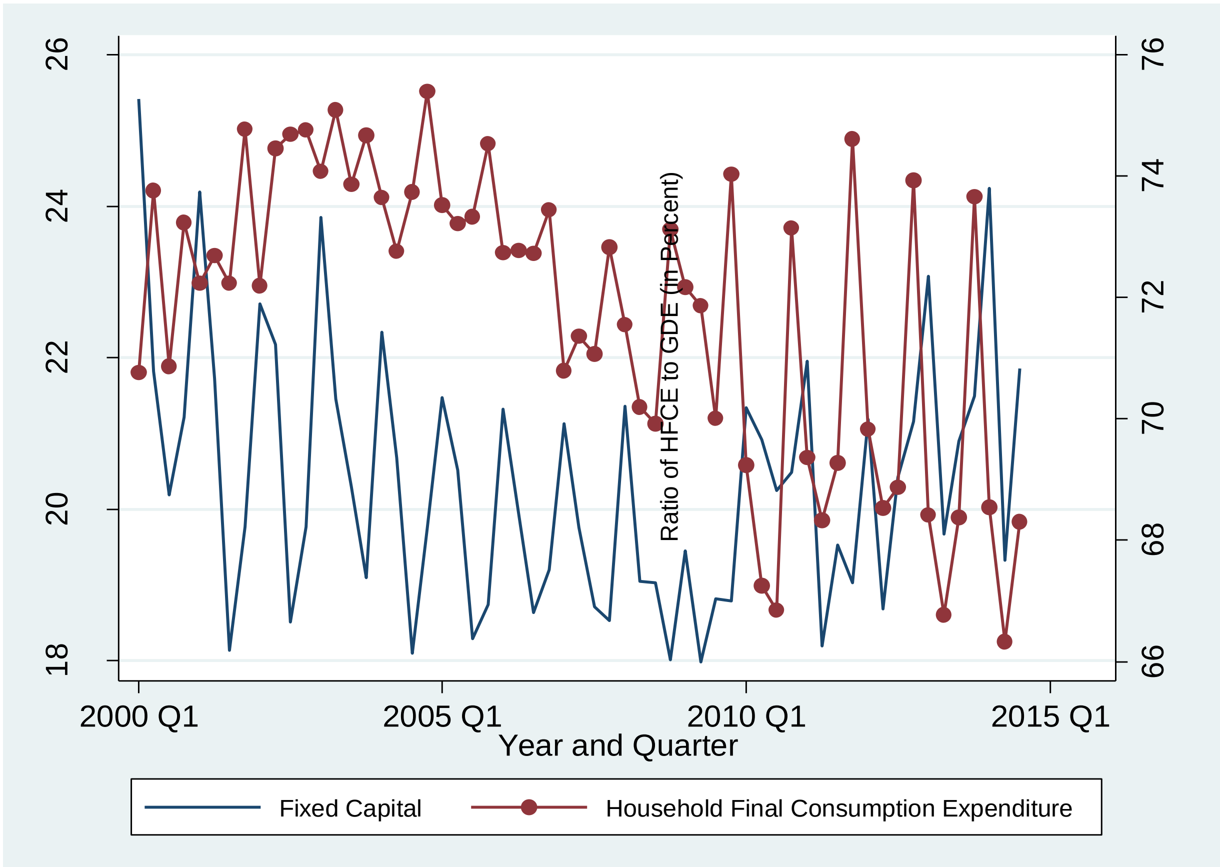
Source: Used by Economic and Social Commission for Asia and the Pacific, calculated from CEIC Data Company Ltd. (Economic and Social Council 2015)

The growth rate of 6.3 percent in the period 2010-2014 was even the highest five-year average during the past 40 years. Last month, the PSA reported that the Philippine economy posted a third quarter growth of 6.0 percent for 2015. The PSA has also has estimated inflation at about 1.7% in first 8 months of 2015, with the decrease in global oil prices and electricity rates in the country, as well as slower increases in food prices driving inflation even below the country's inflation target for the year of 3 to 5 percent.

There are continued volatilities in the domestic financial market, just like the rest of East Asia (given the likely slowdown of the economy of China), but underlying fundamentals in the financial system of the country remain very sound especially, with low levels of non-performing loans, high capital adequacy ratios, and macroprudential measures in place by monetary authorities to mitigate risks. The Philippine peso is also rather stable in real terms, very flexible, and is also in line with market fundamentals, offering a cushion in case there would be large capital outflows.

On the demand side, exports have not been very strong when compared to other ASEAN economies. Ironically the meagre exports saved the economy from the effects of the global slowdown given the country's reliance on domestic consumption that has driven the economy supported by low food inflation, a continued decline in fuel prices, and sustained increase in remittances from overseas. It can be observed that in the period from 2000 to 2014, the ratio of household final consumption expenditure to total gross domestic expenditure (GDE) has been slightly decreasing (although fourth quarters tend to be upticks in recent years), but investments (as measured by fixed capital to gross domestic expenditure) have been on the rise, especially in recent years. Robust private fixed capital formation in both construction and durable equipment, have also provided additional support to recent economic growth. Government expenditures have not risen as much despite the massive government budgets for the year, suggesting some issues in absorptive capacity for budgets and procurement problems, especially in public infrastructure spending.

Figure 2: Ratio of Fixed Capital and Household Final Consumption Expenditure to Gross Domestic Expenditure



Source: Philippine Statistics Authority (PSA)

On the production side, economic growth has been fairly broad-based. The contribution to the economy's growth and the share of the economy's output is more on the services and industry sectors. Growth drivers in services sector are business process outsourcing (BPO), real estate and renting, retail trade, tourism, among other business activities, while in industry, especially in manufacturing, subsectors driving growth are food processing, chemicals, and communication equipment. Agricultural output has largely grown in a positive direction in the past five years, although during the first half of year, agricultural output was flat largely an effect of drought from El Nino, but there was a slight recovery in the third quarter of 2015. There is optimism that fourth quarter GDP will be the best performing among the quarter growths, but this last quarter growth may not still be enough to meet the government economic growth targets for the year.

The Philippine economy is currently dominated by the services sector, not only in output but also in employment. As pointed out by Albert, Dumagan and Martinez (2015), output share of agriculture to the economy has not been dominant. Contrary to the popular view that the Philippines was once an agricultural economy, the country's economic output has always been dominated by services, and understandable so, as even during the Spanish colonization, Filipinos were largely traders. The output share of agriculture after World War II in 1945 was less than a third (29.7), and this has continued to decline over the years to 11.3% in 2014. As regards employment, the agriculture sector has also had decreasing trends in its share of total employment from 45.2% in 1990 to about a third (31.0%) in 2013. In the same period, the service sector took increasing shares of total employment from two-fifth (39.7%) in 1990 to more than half (53.4%) in 2013. Thus, the country has become less agricultural in recent times, with services and industry sectors getting more of the share of the economy, in both output and employment.

Overall employment rate has been marginally increasing, if not been relatively flat. Consequently, some analysts have characterized growth in the Philippines to be jobless. However, there is actually evidence of a structural transformation resulting in the job market, with employment increasing outside of the agriculture sector, and more quality jobs being created throughout the economy (Albert, 2014).

Although the Millennium Declaration was only a political commitment that was not legally binding, the Philippines, together with the rest of the 189 signatory UN member countries, worked seriously on achieving the MDGs, putting these global commitments at sync with its national development plans. The Philippine government enacted several enabling policies and directives to foster a suitable enabling environment for achieving the MDGs. For instance, the Department of Interior and Local Government (DILG) formulated a Memorandum Circular No. 2004-152: *Guide to Local Government Units (LGUs) in the Localization of the MDGs*; the National Anti-Poverty Commission passed an en banc resolution directing LGUs to adopt 13 core local poverty indicators; while in the legislature, the House of Representatives established a "Special Committee" for the MDGs. (Capones 2008). Government also implemented a number of key programs, chiefly a conditional cash transfer program as a social protection mechanism to incentivize poor households in investing in their human capital (particularly the schooling and health of their members) toward improving their chances of improved income prospects in the future when beneficiary children have gained better education attainments.

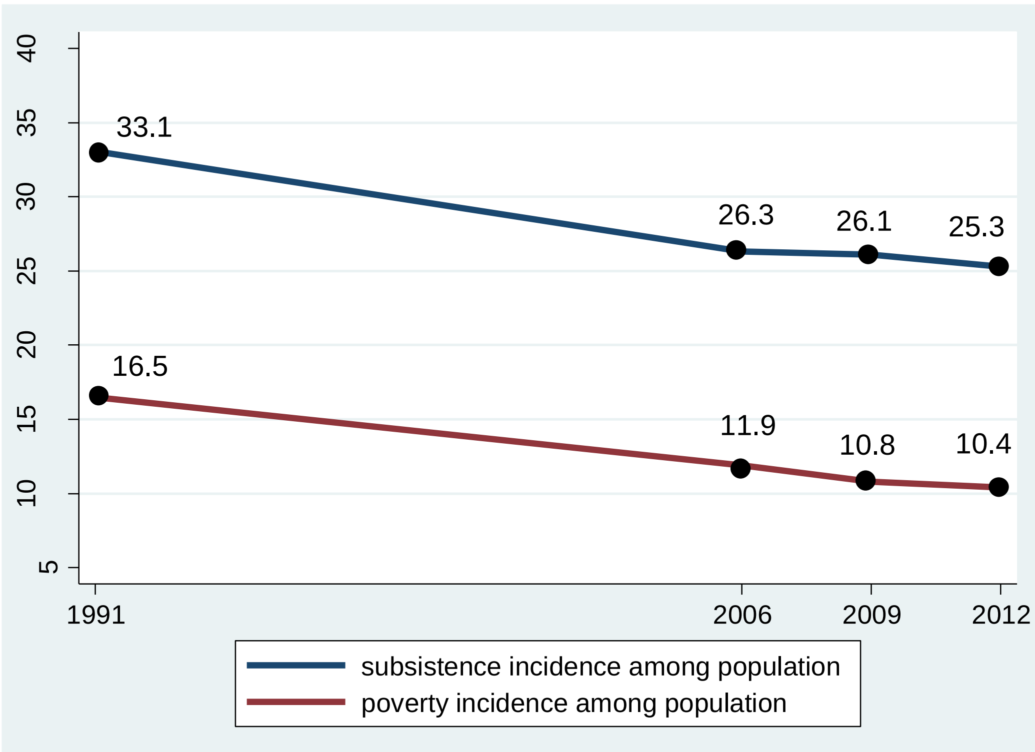
Official poverty estimates have traditionally used income data sourced from the triennial Family Income and Expenditure Survey (FIES) conducted by the Philippine Statistics Authority (PSA), and national poverty lines estimated separately using benchmarks on the cost of minimum basic food and non-food requirements for a reasonable welfare level. In 2013, the PSA's predecessor institutions, namely the National Statistical Coordination Board and the National Statistics Office, released first semester poverty estimates based on the 2006, 2009 and 2012 FIES. Since 2014, the PSA has also been releasing official poverty statistics using another household survey, the Annual Poverty Indicator Survey (APIS), which is conducted on non-FIES years. A report by Albert, Dumagan and Martinez (2015) suggest, however, that these official poverty estimates from the 2013 APIS, and the first semester FIES waves in 2009 to 2012 are incomparable not only because the survey instruments for the income data, though similar, are not equivalent, but also because the FIES questionnaire has several pages of questions on household expenditures, while the APIS questionnaire has a much simpler module on expenditures (and other non-monetary indicators) before the income questions are asked to respondent households. Thus, the government's interpretation of a "decrease" in poverty from the first semester of 2012 (using the 2012 FIES first semester data) to the first semester of 2013 (using the APIS 2013) that was re-echoed by the World Bank in its Philippine Economic Update, August 2014 edition[2] is not a good reading of the trends in poverty conditions in the country.

The last set of comparable official poverty rates based on the full year income data of the 2006, 2009, and 2012 FIES showed that poverty has virtually remained unchanged, despite the recent stellar economy growth in the country (see Figure 3). Official statistics on poverty incidence continued to remain rather high at about a fourth of the population, with little prospects of reaching the Philippine Development Plan (PDP) target of having the proportion of the population who are poor at 18.0% -20.0% by 2016. In the sixth year of the current administration, the PDP core agenda of incorporating the benefits of the poor in the process of

[2] http://www.worldbank.org/en/country/philippines/publication/philippines-accelerating-public-investment-to-sustain-growth-that-benefits-the-poor

economic growth has consistently proved to be elusive. Similarly, when one examines trends in the subsistence poverty rates that pertain to the proportion of Filipinos with incomes less than the national food poverty thresholds (which may be interpreted as extreme poverty incidence) while we find reductions from the 1990 baselines, there have been no changes in recent times for the subsistence (or extreme) poverty rates.

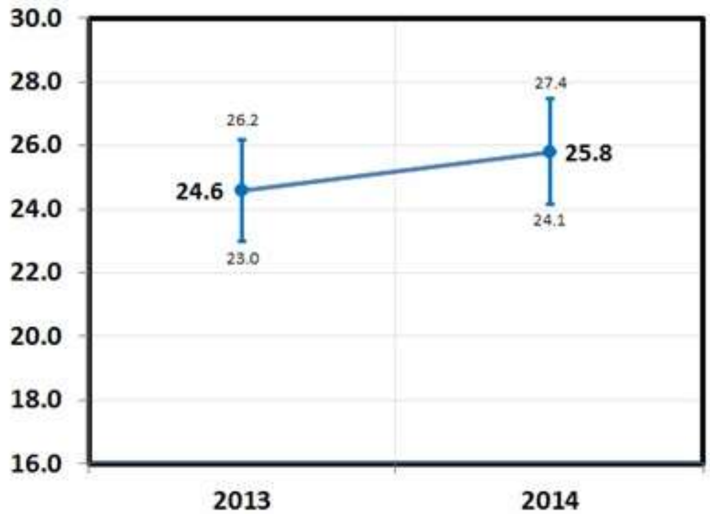
Figure 3: Official Poverty Rates for 2006, 2009 and 2012 (based on full calendar year)



Source: Philippine Statistics Authority (PSA)

As regards recent and comparable official poverty estimates from the first semesters of 2013 and 2014, sourced from the APIS, we similarly observe no changes in poverty given the error margins (see Figure 4), although it is even likely that poverty conditions may have even worsened nationally as these estimates of official poverty incidence do not include sample households from Batanes and Leyte, the latter of which was heavily affected by super typhoon Yolanda. The PSA has yet to renew household survey operations in Leyte to replace its "master sample of households" in this area.

Figure 4: Official Poverty Rates in First Semesters of 2013 and 2014 (with 90 percent confidence intervals)

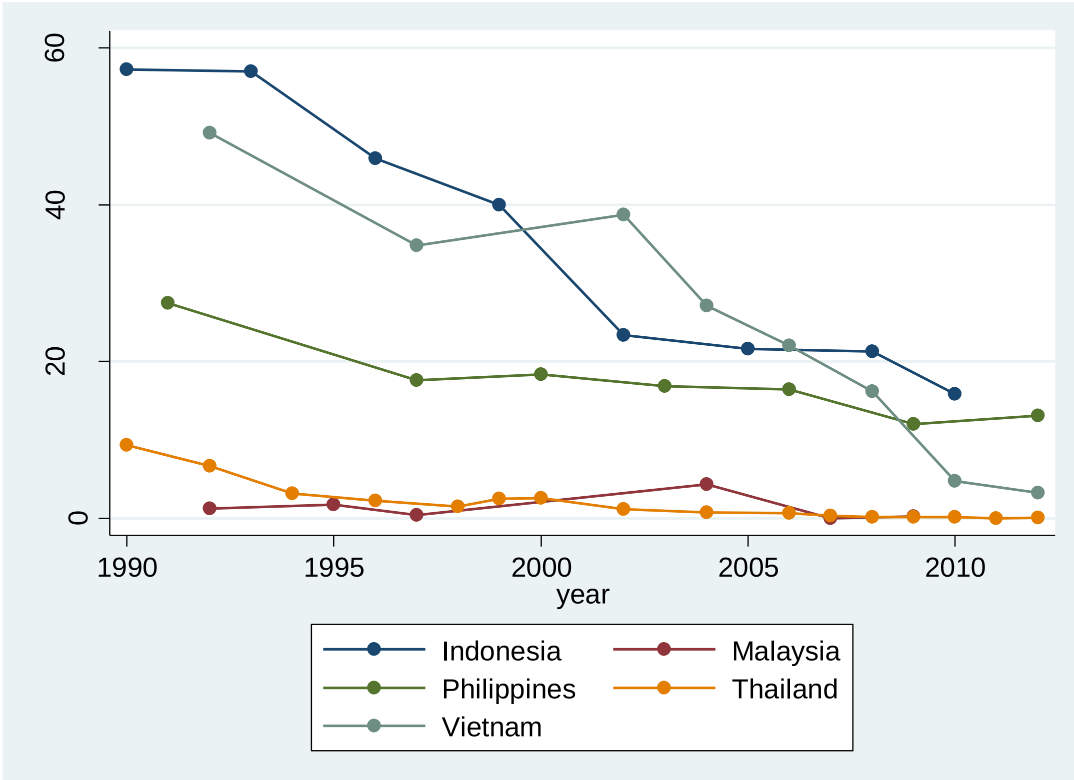


Source: PSA

When examining trends (see Figure 5) in recent World Bank estimates of poverty incidence[3] among selected Association of South East Asian (ASEAN) countries (using $1.90 per day international poverty lines in 2011 PPP prices), we find that while the Philippines managed to reach the poverty MDG target even as early as 2009, but the reduction in poverty has not been at par with performance of ASEAN neighbors in reducing poverty. From the mid 1990s to 2010, Vietnam, and Indonesia have shown dramatic improvements in welfare conditions, especially as these economies have been experiencing considerable and sustained economic growth as well as implementing a number of successful and well-targeted pro-poor programs. By contrast, poverty has been at a standstill in the Philippines. Some have suggested that the massive investment in the conditional cash transfer (CCT) program has been a failure, but the cash assistance actually given to poor families in the CCT would not be enough for the households to exit poverty, and, in fairness, they were designed to be so. The CCT is meant to be an investment especially in children of poor families so that these families can be incentivized to send them to school, and get health services (such as deworming). Poverty will be ultimately expected to reduce in the long term but not in the short and medium term as the children beneficiaries are still currently in school, and prospects for improved income (as a result of better education attainments) have yet to be realized.

[3] Sourced from World Bank's Povcalnet http://iresearch.worldbank.org/PovcalNet/index.htm .

Figure 5: Trends in $1.90 Poverty Rates in Selected ASEAN countries: 1990-2015



Source: World Bank Povcalnet

The trends in the lack of considerable changes in poverty rates, whether using the official poverty lines or $1.90 international poverty lines even in recent times of economic growth, show that some segments of Philippine society are being left out of economic growth processes, and thus the Philippine government has made inclusive growth the cornerstone of its most recent PDP. The Philippines has yet to ensure that its recent economic growth benefits everyone. The wealthiest Filipinos[4] whose wealth continues to rise will need to make more investments in the country that will ultimately assure sustained growth and progress.

One can further examine the performance of other countries and regions across the world and observe that part of the reason for varying performances are differences in starting conditions (Albert *et al*. 2015). Patterns in poverty reduction differ across economies also because of policy differences in addressing economic growth and income distribution (Ravallion, 2013).

[4] http://www.rappler.com/business/214-who-s-who/85686-filipinos-forbes-billionaires-list-2015

The lackluster changes in poverty are a clear result of the lack of changes in the entire income distribution, i.e. the high levels of inequality in income and opportunities are barriers to improved and sustained poverty reduction. (See Albert, Dumagan and Martinez, 2015). The poorest 20% Filipinos own only between 6% to 7% of the country's total income while in a perfectly equal society, the poorest 20%, the next 20% all the way to the richest 20% Filipinos, should own 20% of total national income. Moreover, this level of inequality has been unchanged as shown by various measures of inequality such as the Palma ratio and Gini coefficient. In particular, as regards the Palma, we see that the top ten percent have an accumulated income of three times the accumulated income of those at the bottom 40 percent of the income distribution (see Table 1).

Table 1. Selected Statistics on Income Inequality and (Per Capita) Income Distribution in the Philippines: 2003, 2006 and 2009

Statistics	2003	2006	2009	2012
Average Per Capita Income (in Nominal PHP)				
Poorest 20 Percent	7827	9395	12253	13952
Lower Middle 20 Percent	14073	16453	21021	23969
Middle 20 Percent	22053	25700	32121	36848
Upper Middle 20 Percent	36157	42448	52092	59556
Richest 20 Percent	97877	115570	139975	158596
TOTAL	35598	41913	51492	58584
Share of Bottom 20 Percent in National Income	6.15%	6.42%	6.90%	6.86%
Palma ratio (i.e., income of the top 10% to bottom 40%)	2.97	3.12	2.93	2.9
Gini	0.454	0.455	0.445	0.444

Note: Authors' calculations from FIES 2003, 2006, 2009 and 2012.

As pointed out by Milanovic in a blog[5], Simon Kuznets in the 1960s argued that every income distribution should be judged by three criteria: adequacy, equity and efficiency.

- **Adequacy** is ensuring even the poorest have an income level consonant with local customs and economic ability of the society.

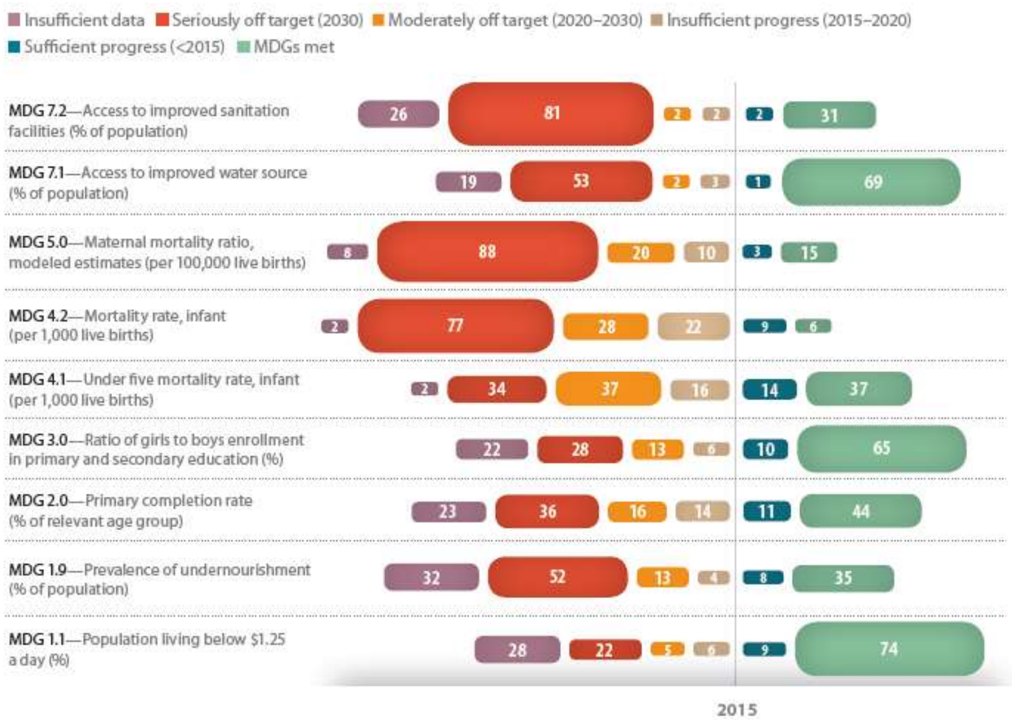
[5] http://glineq.blogspot.com/2016/02/inequality-structural-aspects.html

- **Equity** is absence of discrimination whether it is a discrimination in current incomes, as for example in racial or gender wage gaps, or in future possibilities (what we now call inequality of opportunity).
- **Efficiency** is achievement of high growth rates.

The achievement of higher growth rates requires greater equity, as a significant part of the population is otherwise socially excluded, not allowed to contribute, or because it leads to the fragmentation of society and political instability. The country will need to formulate and institute various reforms to lessen inequalities that prevent us from reducing poverty.

As regards the MDGs, progress has been very uneven. Asia has yielded the fastest progress in reducing poverty and improving access to social services, and yet, even in Asia, while the incidence of poverty has been reduced, given the size of the population in Asia, the number of people living in extreme poverty are in the hundreds of millions.

Figure 6. Extent of progress toward achieving the MDGs, by number of countries

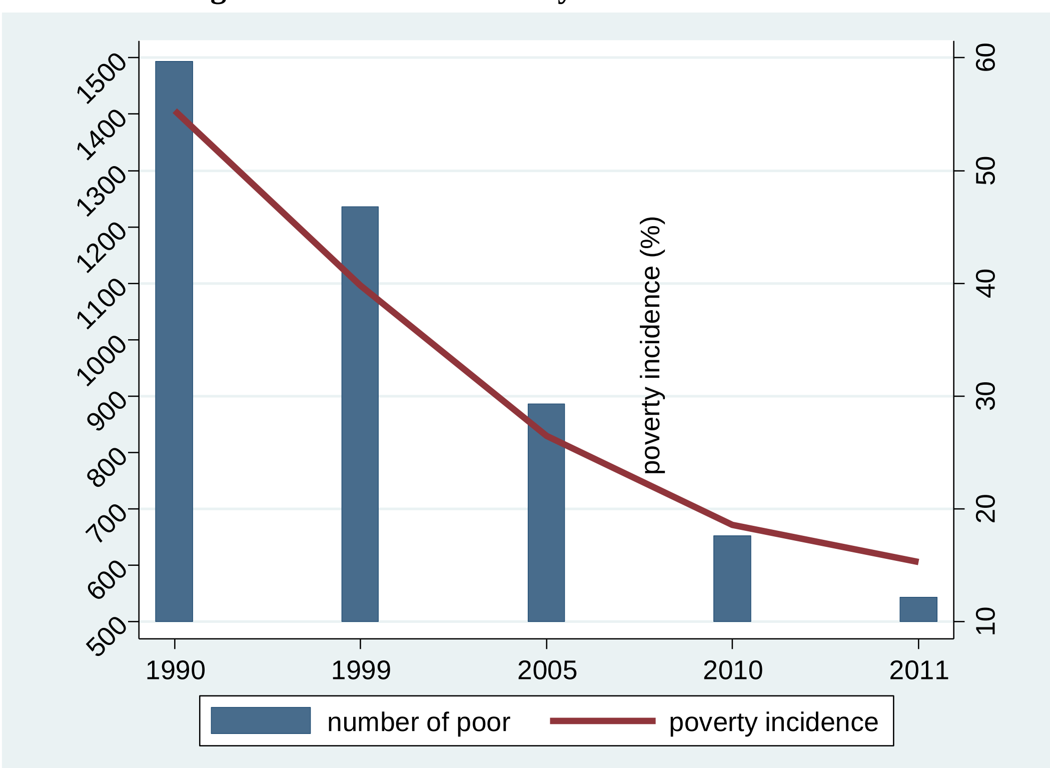


(Source: World Bank) http://www.worldbank.org/en/publication/global-monitoring-report/report-card/progress-towards-the-mdgs

Sub-Saharan Africa has had to deal with many development challenges given continuing food insecurity, very high child and maternal mortality, a large number of people living in informal settlements, an increase in extreme poverty, and an overall shortfall in attaining a majority of the MDGs. Latin America, the transition economies, as well as the Middle East and North Africa, have shown slow or no progress on some of the MDGs, with persistent (and even rising) inequalities preventing progress on attaining other MDGs.

In the Millennium Development Goals section of its recent 2015 Key Indicators publication, the Asian Development Bank (2015) noted that the proportion of individuals with incomes less than $1.25 a day (in 2005 constant PPP prices) was greatly reduced, from more than half (55.3%) of the Asia-Pacific population in 1990 to 15.3% in 2011. The number of people living in extreme poverty rate in Asia and the Pacific also decreased to 544 million in 2011 from almost 1.5 billion in 1990 (Figure 7), and this reduction is largely on account of the reduction of poverty in China and India.

Figure 7: Number and Proportion of People in the Asia and Pacific Region Living on Less than $1.25 a Day

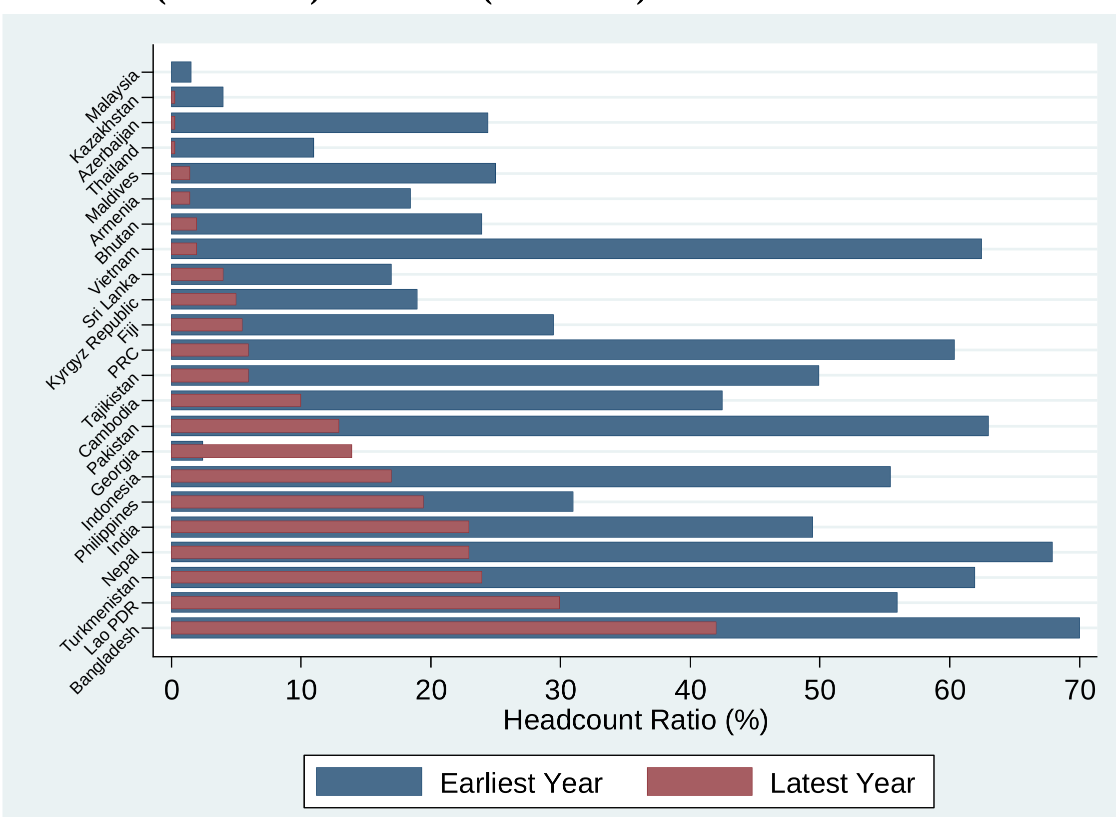


Source: ADB Key Indicators 2015, Asian Development Bank estimates using data from PovcalNet (downloaded 12 January 2015)

Such reduction in extreme poverty incidence correlates with a reduction in other poverty measures, such as the poverty gap ratio, from 11% in latest years coming from 26% across countries in developing Asia. The Asian Development Bank (2015) also indicated that in earliest years of MDG monitoring, fourteen developing economies had a population of workers living below the international poverty line of $1.25 a day (in 2005 PPP prices) exceeding 20%, and this has dropped to only five economies in recent years.

Although poverty has been substantially reduced in developing Asia, the rate of progress across economies has been uneven (Figure 8). At least one in every five individuals have income or consumption below $1.25 per day (in 2005 PPP prices) in the economies of Bangladesh (43.3%), India (23.6%), Lao People's Democratic Republic (Lao PDR) (30.3%), Nepal (23.7%), Pakistan (21.0%), and Timor-Leste (34.9%).

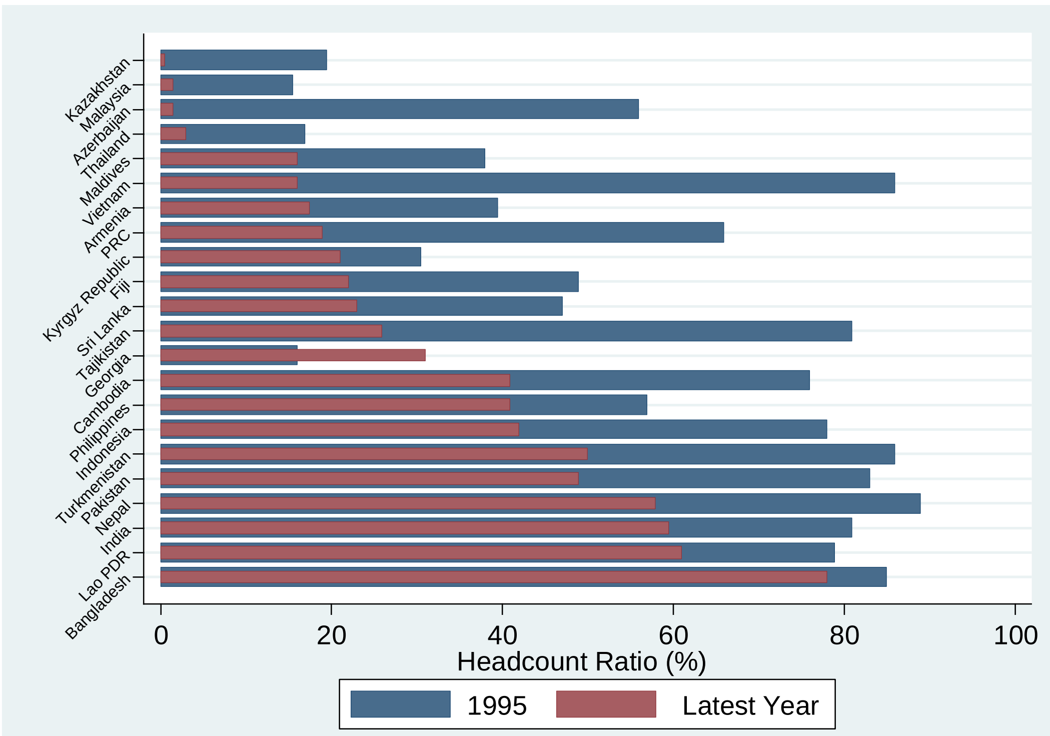
Figure 8: Proportion of Population Living on Less than $1.25 a day, Earliest (1990–2003) and Latest (1998–2012) Years



Source: ADB Key Indicators 2015

The Asian Development Bank (2015) also suggests that moderate poverty (defined with in terms of $2 per day threshold in 2005 PPP prices) has also been reduced in the Asia and Pacific region, but its decline has not been as stellar as that of extreme poverty. The proportion of people living below $2 a day, which measures the extent or incidence of moderate poverty, has shrunk from 81.3% in 1990 to 39.4% in 2011. Even though there has been a general fall in the incidence of moderate poverty incidence across economies except for Georgia, less than half (10) of 22 developing economies in Asia-Pacific with data for earliest and latest years have halved moderate poverty since 1995 (Figure 9). There is also a wide variation in the incidence of moderate poverty across economies of developing Asia, ranging from 0.8% (2010) in Kazakhstan to 76.5% (2010) in Bangladesh.

Figure 9: Proportion of Population Living Less than $2 a Day, Earliest (1995[a]) and Latest (1998-2012) Years



Note: a = refers to 1995–2002; Lao PDR = Lao People's Democratic Republic; PRC = People's Republic of China.

Source: ADB Key Indicators, 2015

The Asian Development Bank (2015) expects that 19 out of 21 economies in developing Asia, including the Philippines, either achieved the target of halving extreme poverty prior to the deadline, or are expected to meet such this year (Table 2). Bangladesh has made slow progress in reducing extreme poverty, and is expected to meet the poverty reduction target by 2017. Georgia is the only economy in the Asia and Pacific region that is regressing for the MDG target to reduce extreme poverty.

Note that even at the onset of the MDGs, starting conditions have been different across UN member states, with some countries having more resources available for achieving the MDGs (Albert, Dumagan and Martinez, 2015). The track towards global sustainability will contain a lot of alternative routes per country, which has to do with policy differences in addressing economic growth and income distribution (Ravallion, 2013).

Table 2: Progress Toward Achieving the $1.25 PPP a Day Target

Achievers/On-track	
Armenia	Malaysia
Azerbaijan	Maldives
Bhutan	Nepal
Cambodia	Pakistan
China	Philippines
Fiji	Sri Lanka
India	Tajikistan
Indonesia	Thailand
Kazakhstan	Turkmenistan
Kyrgyzstan	Viet Nam
Lao People's Democratic Republic	
Slow	
Bangladesh	
No Progress/Regressing	
Georgia	

Lao PDR= Lao People's Democratic Republic, PPP = purchasing power parity

Source: ADB Key Indicators 2015

During the United Nations Sustainable Development Summit on 25 September 2015, more than 150 world leaders adopted the 2030 Agenda for Sustainable Development, including the Sustainable Development Goals (SDGs), the successor to the MDGs. The SDGs puts forward a shared vision of where we want to see the world to be in 2030, especially in terms of economic, social, environmental, and governance conditions, with statistics to be produced by member states in 2015 to serve as baselines for monitoring progress. The SDGs have 17 *Global Goals*, more than doubled the 8 MDGs (see Table 2), and are supported by 169 targets (8 times more than the 21 MDG targets). The SDGs are clearly quite ambitious, and without specific guidelines for proper prioritization, the UN member states are left to decide for themselves what they need to do depending on their own contexts. In fact, before the final list of SDGs was released, United Kingdom Prime Minister David Cameron[6] advised to have fewer goals in order to be effective implementation. (The Guardian, 2014). However, the SDGs have been adopted, and there will be a big challenge for national statistical systems to produce the indicators required for global monitoring of the SDGs given that financial resources provided by donors for supporting statistical systems in developing countries have been decreasing in recent times, according to the Partner Report on Support for Statistics (PRESS) of Paris21 (2015).

Table 3. Proposed Sustainable Development Goals, Targets and Elements

Proposed Sustainable Development Goals		Elements for Delivering on the SDGs
	End poverty in all its forms everywhere	Dignity
	End hunger, achieve food security and improved nutrition, and promote sustainable agriculture	People
	Ensure healthy lives and promote wellbeing for all at all ages	People

6 http://www.theguardian.com/global-development/2014/sep/24/un-begins-talks-sdgs-battle-looms-over-goals

4 QUALITY EDUCATION	4) Ensure inclusive and equitable quality education and promote lifelong learning opportunities for all	People
5 GENDER EQUALITY	5) Achieve gender equality and empower all women and girls	Dignity
6 CLEAN WATER AND SANITATION	6) Ensure availability and sustainable management of water and sanitation for all	Planet
7 AFFORDABLE AND CLEAN ENERGY	7) Ensure access to affordable, reliable, sustainable and modern energy for all	Prosperity
8 DECENT WORK AND ECONOMIC GROWTH	8) Promote sustained, inclusive and sustainable economic growth, full and productive employment, and decent work for all	Prosperity
9 INDUSTRY, INNOVATION AND INFRASTRUCTURE	9) Build resilient infrastructure, promote inclusive and sustainable industrialisation, and foster innovation	Prosperity
10 REDUCED INEQUALITIES	10) Reduce inequality within and among countries	Prosperity
11 SUSTAINABLE CITIES AND COMMUNITIES	11) Make cities and human settlements inclusive, safe, resilient and sustainable	Prosperity
12 RESPONSIBLE CONSUMPTION AND PRODUCTION	12) Ensure sustainable consumption and production patterns	Planet

	13) Take urgent action to combat climate change and its impacts	Planet
	14) Conserve and sustainably use the oceans, seas and marine resources for sustainable development	Planet
	15) Protect, restore and promote sustainable use of terrestrial ecosystems, sustainably manage forests, combat desertification and halt and reverse land degradation, and halt biodiversity loss	Planet
	16) Promote peaceful and inclusive societies for sustainable development, provide access to justice for all and build effective, accountable and inclusive institutions at all levels	Justice
	17) Strengthen the means of implementation and revitalise the global partnership for sustainable development	Partnership

(Source: United Nations Sustainable Development Knowledge Platform)

The MDG on extreme poverty reduction had targets on (1) reducing poverty by half their 1990 benchmarks; (2) reducing hunger by half; (3) attaining decent work and economic growth; and (4) reducing income inequalities. In consequence, there have been concerted efforts by governments and multinational organizations to reduce poverty; hunger, and related issues, especially in developing countries (OECD, 2001). Despite having achieved the MDG on reducing extreme poverty, the absolute eradication of poverty (with the international $1.90 PPP per day poverty line) remains a big challenge whether in the near future or even by 2030. The aspirations for *No Poverty* and *Zero Hunger* are quite ambitious.

An initial list of more than 300 statistical indicators to monitor for the SDGs has been identified by the United Nations Statistics Division. Last October 2015,[7] the Interagency Expert Group on SDG Indicators streamlined this list of SDG indicators to 159 "green" indicators that countries and development partners consider crucial for monitoring the SDGs. This list of green indicators

[7] http://unstats.un.org/sdgs/meetings/iaeg-sdgs-meeting-02

have been further expanded to 231 with additional indicators obtained from the indicators that were coded "grey" in October 2015 (which require more discussions).

The SDGs though have provided more attention to issues about distribution and inequality, which the MGDs missed on. While one of the indicators for monitoring extreme poverty was an inequality indicator (i.e. the share of income of the bottom 20 percent), there was no specific target on what this indicator should be. On one hand, this is a challenge: less income inequality would be desirable, but inequality indicators measure relative variability in income. A country where everyone is equally poor will have little income inequality. But a country like the Philippines has had challenges in reducing the poor because of high levels of income inequality. There will be a need for specific targets about reducing inequality. Ravallion (2013) suggested that an upward trend of the overall economy (mostly measured through growth in GDP) does not necessarily reflect an increase in household income or consumption. He points the need to examine whether growth is "pro-poor" or not (Ravallion, 2004).

Empirical evidence suggests that the poor benefit little if not secondarily from a country's growth, in comparison to those living way above the poverty line. The lack of attention to improve the opportunities of the poor and vulnerable segments of society in national economic development plans has been noticeable. It has only been recognized in the past few decades that economic growth is not sufficient by itself, and that inclusive growth should be a primary objective especially for sustaining development, wealth and prosperity.

Throughout its nine chapters, the Philippine Development Plan 2011-2016 has identified the pursuit of inclusive growth, as the primary development agenda in the Philippines. The PDP's rationale of promoting inclusive growth is not confined to merely closing the poverty gap. Five key strategies are laid out to achieve inclusive growth, viz., : (i) promote transparent and responsive governance, (ii) invest massively in physical infrastructure; (iii) boost competiveness to generate employment; (iv) improve access to financing; (v) develop human resources through improved social services.

A decade ago, the now defunct NSCB established a statistical indicator system to monitor the PDP results matrix, i.e., the targeted outcomes for attaining economic and social development goals laid out in the PDP. The indicator system is called the Statistical Indicators of Philippine Development, otherwise known as StatDev.[8] The first edition of StatDev, i.e. 2004 StatDev, was released in July 2005. Assuming that the indicators reflect the actual conditions of the country, the StatDev indicators could be used as an effective evaluation instrument to determine government performance in relation to its socio-economic goals that were defined at the onset of the administration. The StatDev, continued by the PSA, provides inputs to the State of the Nation (SONA) especially as it is released before the SONA (Albert and Raymundo 2015).

The grading system of indicators in StatDev is categorized into three levels of performance according to the estimated probability of meeting the PDP target – good (high probability), average (medium probability) and poor (low probability). Among the 151 indicators of StatDev 2014, 63 of which are in good standing, 32 show middling performance and 56 show poor (see Table 4).

Table 4. Summary of StatDev 2014 Indicators

Chapter/Sector	Performance			Total
	Good	Average	Poor	
Macroeconomy	6	0	3	9
Competitive Industry and Services Sector	6	3	1	10
Competitive and Sustainable Agriculture and Fisheries Sectors	12	12	11	35
Accelerating Infrastructure Development	15	10	14	39
Towards a Dynamic and Resilient Financial	1	0	0	1

[8] The StatDev owes its roots to work by NSCB Technical Staff in the then Statistical Coordination Office (SCO) of the National Economic and Development Agency (NEDA), which established a statistical monitoring system through the Economic and Social Impact Analysis Women in Development (ESIAlWID) Project- Macro Component. The objective of this project component was to develop, maintain, and institutionalize the operation of a system of macro-level indicators for measuring and monitoring the degree of achievement of the economic and social development goals set forth in the then Long-Term and Medium-Term Development Plans of the country.

System				
Good Governance and the Rule of Law	5	5	6	16
Social Development	7	1	5	13
Peace and Security	1	0	3	4
Conservation, Protection, and Rehabilitation of Environment and Natural Resources	10	1	13	24
Total	**63**	**32**	**56**	**151**
Increasing, decreasing, or no status [1/]				24

Note: 1/ For ambiguous indicators and without targets, the pace of performance are classified as increasing, decreasing, or blank (no status) depending on their baseline and latest data.
Source: PSA

The StatDev indicators, however, cannot be considered equal in relevance. For instance, the indicators for agriculture and fisheries on subsistence incidence among population, yield of palay, and yield of tomatoes are not of the same importance to national development. An indicator for the macroeconomy, inflation rate, is also surely viewed by everyone to have a larger impact than Technical and Vocational Education and Training (TVET) certification rate, an indicator identified for social development. Hence, one has to go beyond the summary statistics in Table 4 and look through the indicators and sectoral chapters of the PDP to carefully arrive at a deeper examination of the country's conditions relative to development goals and targets. The choice of the indicators in StatDev and the targets for the PDP were suggested by the government agencies responsible for the sectors.

Selected StatDev indicators are displayed in Table 5. Low inflation rate, sustained economic growth, low unemployment rate, and low poverty are a few of the basic preconditions for overall social and economic development. As regards the macroeconomy, the total number of StatDev indicators that registered a good performance (6) outnumbers those that had a poor performance (3). In the 2010-2014 period, the country had economic growth averaging 6.3% (although historical trends suggest that government may not hit its 2016 PDP target), a low inflation rate, and improvements in the unemployment rate. There are also prospects of sustained and robust economic activity, at least until next year. All of these outstanding economic indicators undoubtedly led to improved credit ratings for the country from Fitch, Moody's and S&P.

Table 5. Sectoral Chapters of PDP with Selected Samples of 2014 StatDev Indicators

Sectoral Chapter	StatDev Indicator	2010	2011	2012	2013	2014	2016 (target)	Probability of Achieving PDP target	Data Source Agency
Macroeconomy	Real GDP growth rate	7.6	3.9	6.8	7.1	6.1	7.5-8.5	☹	PSA
	Number of employment generated (in millions)	0.97	1.16	0.14	0.52	1.02	0.66-0.75	☺	PSA
	Unemployment rate	7.4	7.0	7.0	7.1	6.8	6.5-6.7	☺	PSA
	Inflation rate	3.8	4.6	3.2	3.0	4.1	2.0-4.1	☺	PSA
	Poverty incidence among population	26.3 (2009 FIES)		25.2 (2012 FIES)	24.9 (1st sem; 2013 APIS)	25.8 (1st sem; 2014 APIS)	18.0-20.0	☹	PSA
Competitive Industry and Services Sectors	Global Competitiveness Index ranking	85 (out of 139)	75 (out of 142)	65 (out of 144)	59 (out of 148)	52 (out of 144)	49 (out of 148)	☺	World Economic Forum
	employment generated from industry and services (in millions)	1.07	0.84	0.58	0.78	0.84	0.89-0.92	☺	PSA
Competitive and Sustainable Agriculture and Fisheries Sectors	ratio of rice self-sufficiency (in percent)	81.3	93.9	91.9	96.81	92.04	100.0	😐	PSA
	palay production (in metric ton per hectare)	3.62	3.68	3.84	3.89	4.0	4.53	😐	PSA
Accelerating Infrastructure Development	road density	10.09	10.13	10.21	10.36	10.46	81.91	☹	DPWH
	population with access to potable water	82.9 (2007)	84.4		83.8		86.6	☹	PSA
Towards a Dynamic and Resilient Financial System	average growth of financial system's total assets	9.8 (2006-2010)	6.6	10.1	20.8	9.1	>10%	☺	BSP
Good Governance and The Rule of Law	people's trust in government, government effectiveness	0.36	0.44	0.47	0.47		Above median	☺	MCC
	people's trust in government, control of corruption	-0.34	-0.27	-0.01	0.18		Above median	☹	MCC
	people's trust in government, rule of law	-0.07	-0.04	-0.08	0.10		Above median	☹	MCC
Social Development	Maternal mortality rate per 100,000 livebirths	162 (2006 level)	221				50	☹	PSA
	Infant mortality rate per 1,000 livebirths	25 (2008 level)	22		23		17	☹	PSA
	Under-five mortality rate per 1,000 livebirths	34 (2008 level)	30		31		25.5	😐	PSA
	Net enrolment rate in the elementary level	95.9	97.1	95.1	93.8	92.5	99.0	☹	DepED

	Completion rate in the elementary level	72.1	70.9	73.7	78.4		83.0		DepED
	Prevalence of underweight children under five years of age	20.6 (2008 level)	20.2		19.9		12.7		FNRI
	Number of poor households covered by conditional cash transfer (in millions)	1.04	2.35	3.12	3.94	4.48	2.9		DSWD
	Number of jobs generated in the government community-based employment program (in millions)		1.2	2.3	2.0	3.1	1.0 /year		DOLE
	number of higher education graduates	496,949	522,570	564,769	605,375		601,505		DSWD
	NHIP coverage rate	53.0 (2008)		72.0	67.0	87.0	95.0		PHIC
Peace & Security	crime solution efficiency (in percent)	18.64	28.87	36.67	38.49	41.72	38.3		DILG-PNP
	private armed groups (PAGs) and other threat groups	83	83	83	81	84	43		DILG-PNP
Conservation, Protection & Rehabilitation of the Environment & Natural Resources	Observed population of threatened species, tamaraw	314	274	327	345	382	360		DENR-BMB
	proportion of land area covered by forest	23.8	22.8	22.8	22.8	26.1	30.0	Table 6. Percent NHIP Coverage to Total Population During PGMA's Term	DENR-FMB
	total suspended particulate (TSP) level (air pollution) in Metro Manila (in Ug/Ncm)	150	118	119	118		92		DENR-EMB

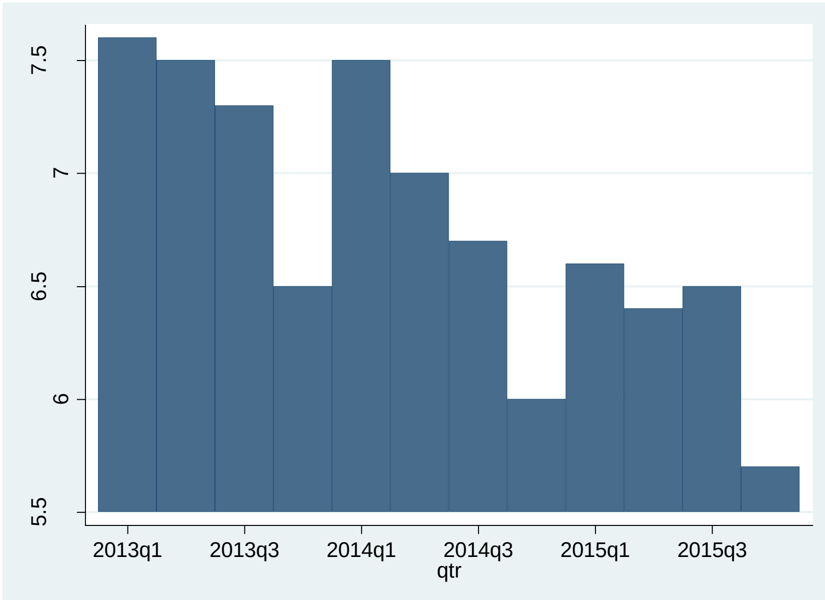
Source: PSA

However, the lack of changes in poverty incidence (i.e. the proportion of poor Filipinos) shows that economic growth is far from being inclusive, and that much has to be done to improve income distribution, to bring the poor beyond the poverty line, and to make the middle class bigger and stronger. On account of population growth, the actual headcount of poor Filipinos even increased, given the lack of significant changes in poverty incidence. The high levels of income inequality in the country (see Albert, Dumagan and Martinez, 2015) are barriers to shared prosperity, equality of opportunities, and sustained economic growth that will be necessary for future poverty reduction.

The current poverty incidence has remained high, despite the efforts in providing jobs and holding inflation steady. One reason for this is the prevalence of poverty among those who are working. Merged microdata files from the FIES and the Labor Force Survey suggest that poverty incidence is actually higher in those who are employed in 2006, 2009, and 2012, and that unemployment is more of an issue among the non-poor. Around 81% of unemployed Filipinos in 2012 belong to non-poor households, with a number of these seemingly unemployed by choice or simply choosy in finding jobs (Albert, Dumagan and Martinez, 2015).

Generation of quality jobs should continue to be prioritized by the government, as far as inclusive growth is concerned. The World Bank Philippine Country Office (2013) further suggests that promoting better job creation is one of the key strategies that could be used by the government to ensure that prosperity and opportunities are shared equally. The StatDev suggests that the administration is well on its way of promoting more opportunities for the unemployed, with employment generated by the current administration having surpassed its PDP target even as early as 2011, with industry and service sectors having largely contributed to employment growth. Albert (2014) suggests that the economy did not have a jobless growth. The unemployment rate has seasonal fluctuations across quarters, with recent trends suggesting a downward reduction (see Figure 10). The unemployment rate was registered at 5.6% in the October round of the 2015 LFS (compared to around 6 to 7 percent in previous years). Among unemployed persons, about two thirds are males, about half are in the age group 15 to 24 years, and a little over a third (35.9 %) is either college graduates, or college undergraduates. Reduction of underemployment has also shown progress, coming from 21% in the same period in 2014 to 17.7% in early 2015.

Figure 10: Trends and Seasonality in Quarterly Unemployment Rate: 2013-2015



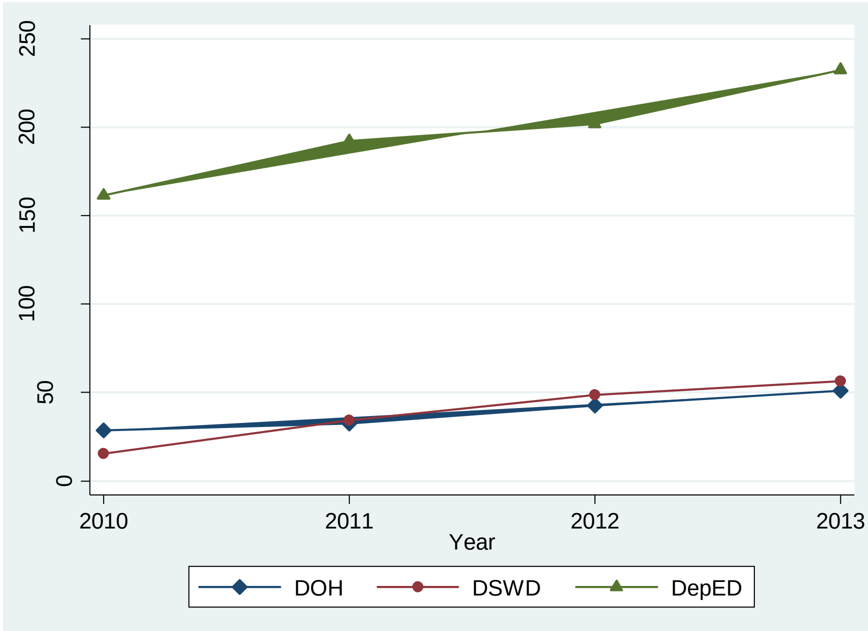
Source: PSA

Achieving the PDP overarching goal of inclusive growth, however, remains farfetched despite the current economic progress experienced by the Philippines. The current and next administrations must formulate and strengthen development strategies which would delve into other possible alternative sources for spurring the "development for all" sustainable development agenda.

3. Progress and Challenges in the Social Sector

Since 2010, a third of the government budget has consistently been provided to the social sector: half of which goes to education, culture and manpower development, less than a tenth goes to health, and between a fifth to a fourth goes to social security, welfare and development. From 2010 to 2013, the Department of Education (DepED), the Department of Health (DOH), and the Department of Social Welfare and Development (DSWD) have been among the top ten departments receiving budget allocations. In this period, the budgets of DepED, DOH and DSWD have increased considerably, with their 2013 budgets increased by 44%, 78% and 268% respectively, from their 2010 budgets (see Figure 11).

Figure 11: Budgets of DepED, DOH and DSWD (in billion pesos): 2010-2013



Source: DBM (http://data.gov.ph/infographics/budget#sector)

Spending on social services has notably increased in recent years, which, for the most part, came from a huge investment in the CCT, more commonly known as the Pantawid Pamilya Pilipino Program (4Ps). Originally introduced in Latin American countries, the CCT program has been implemented and prioritized by the Philippine government as one of the primary social protection programs. From a budget of P4 million in 2007 to support 6,000 households, the budget has increased to P62.6 billion to support more than 4 million households in 2014. The government has made the CCT a flagship program, with the PDP goal of 2.9 million coverage having already been surpassed by late 2012, with 3.12 million household-beneficiaries. With its large budget among social protection programs, the CCT has been put into a lot of scrutiny.

As pointed out in Albert, Dumagan and Martinez (2015), the number of poor household beneficiaries covered in the Conditional Cash Transfer (CCT) has significantly grown over the years, consistent with what the President mentioned in the SONA with the CCT being a flagship social protection program of government. By 2012, the number of CCT beneficiaries has already exceeded the targeted 2.9 million poor households with the 3.12 million households covered.

According to World Bank staff[9], *Pantawid* has also become the third largest CCT program globally, next only to Brazil (8.8 million households) and Mexico (6.5 million households). The CCT has also disbursed 41.7 billion pesos for the entire period of 2013 (DSWD, 2013), thus making the program the largest social welfare intervention that the government has ever implemented. While there are clear costs to the CCT (a very huge budget), but the CCT benefits outweigh the costs considerably, especially given their initial returns: a decrease in the proportion of children aged 5 to 15 who are out of school from 11.7 percent in 2008 to 5.21 percent in 2013 (David and Albert, 2015). Many social protection experts expect that the major impacts of CCT on poverty reduction are to be felt in years to come.

In the basic education sector, one of the key performance indicators is the net enrollment ratio in primary education (i.e., the proportion of primary age children in primary school). Seemingly, these education statistics are regressing, despite improved budgets. However, in fairness to the government, starting conditions were quite high in the baseline figures. There are also diminishing returns to improvements or to maintaining a good standing when one starts from a high base. In practice, trying to achieve the MDG target of universal primary education should only have a reasonable target of 95%, but the PDP target (of 99%) was extremely ambitious. The PDP target for this indicator also failed to recognize data issues, i.e. that this ratio is based on two indicators, the number of primary aged students in primary school (sourced from DepED), and the number of primary aged students (sourced from the PSA's projection of the school age population for primary education). There are likely inaccuracies in estimating both the numerator and the denominator for the official net enrollment rate that explain why this indicator is regressing.

David and Albert (2015) have alternatively estimated the proportion of children aged 5 to 15 years old that are in school using the APIS, and have noticed that this ratio has increased from 88.3% in 2008 to 94.8% in 2013. They also suggest that primary school participation increased from 90.8 percent in 2008 to 96.5 percent in 2013, and attribute this increased school participation to three factors: (i) the passage and full implementation of mandatory kindergarten

[9] Powerpoint presentation at DSWD forum on Pantawid Pamilya 2nd Wave Impact Evaluation, Nov 14, 2014, Oracle Hotel .

and the K-12 law or Republic Act (RA) 10533; (ii) the improved budgets for DepED; and, (iii) the expansion of the CCT.

The most common criticism to CCT is its aggregate cost, i.e. that the money could have been better used for other pro-poor programs, especially on livelihood. While it may seem that the budget for the CCT is huge, the actual cash support for beneficiary families is quite small. In 2012, an average family size of 6 needed about P29,765 to cross out of poverty, but the maximum grant amount of P15,000 is only half of the amount required by the poor to exit poverty.

Lifting beneficiaries out of poverty is an ultimate goal of the CCT, however, this is not the primary and immediate purpose of the 4Ps. The assistance provided to the household-beneficiaries serves as an enabling instrument to incentivize poor families to invest in their children's education, since the petty cash granted relieves them from of costs for schooling. Family beneficiaries are required to enrol their children-beneficiaries aged 3 to 18 and to have them maintain at least 85% monthly class attendance. The CCT, together with investments in DepED budget, undoubtedly led to fewer out-of-school children, from about 3 million children in 2008 down to 1.2 million in 2013 (David and Albert, 2015). Using estimates sourced from the National Demographic and Health Survey, we find that the education poverty rate[10] in the country having hardly changed from 5.3% in 1993 to 4.9% in 2008. Clearly, inequities in basic education have started to improve since the government implemented and expanded the coverage of *Pantawid*. Intergenerational poverty, in turn, could be largely alleviated once the children get employed in the labor force with better education and thus better chances of landing higher-paying jobs.

As regards health, despite increasing budgets for the DOH, maternal mortality has yet to reduce from its PDP and MDG baselines. Under-five mortality has been on a decreasing trend, but it has not fallen fast enough. It is well known that maternal mortality tends to be high in economies where access to maternal health care is low, particularly on account of the low proportion of births attended by skilled health personnel. The attendance of a skilled health attendant (medical doctor, nurse, or midwife) during pregnancy, delivery, and the postpartum period has a

[10] Proportion of youth with less than 4 years of schooling

propensity to reduce the risk of maternal deaths. In the Philippines, the lack of available skilled health attendants has yet to been fully addressed, despite the current oversupply of graduates in the nursing profession.

In the realm of social and political inclusion however, there is much to be desired. That the political system is dominated by political dynasties and that the legislature, which is mandated by the constitution to regulate political dynasties, has not yet made leaps and bounds on anti-political legislation suggest that there is a lot of scope for broadening political participation and inclusiveness in the country (Albert, Mendoza, Yap and Cruz, 2015). Belonging to a political family is certainly not by itself evil as we do have various eminent families such as the Tañada family in the Philippines and the Kennedy family in the United States have made important contributions to society. The question is whether the status quo in the political landscape provides equal opportunities to all families (especially those with "unknown" names) to contribute to society. Name recall continues to be one of the biggest factors that influences the majority of the voting public in choosing their leaders, even in the upcoming 2016 elections (according to results of reputable polls).

4. The Middle Income Class as Driver of growth

One of the key issues that has prevented the Philippines from considerably reducing income poverty is the high levels of income inequality. An alternative strategy towards achieving sustained economic growth is to strengthen and increase the size of its middle income class, which remains congruent to ideals of promoting more inclusion. In the international arena, the middle class has already been cited by a number of economic historians and political theorists to be drivers of national development and inclusive growth.

Easterly (2001) posited that targeting economic progress strategies primarily for the middle class could accelerate a country's overall development. He also reported that this middle class strategy has already been at the heart even of ideas going back to the time of Aristotle[11] (306 BC) and

[11] Translated by Benjamin Jowett (The Internet Classics Archive), the book *Politics* written by Aristotle states the importance of middle class in promoting economic homogeneity: "Thus it is manifest that the best political community is formed by citizens of the middle class, and that those states are likely to be well-administered in which the middle class is large, and stronger if possible than both the other classes, or at any rate than either

Madison (1787), and further argued that countries tend to develop faster if the middle class occupies a majority of its population. Landes (1998) attributed England's economic progress from the ascendancy of "the great English middle class" as far back as 18th century. He added that an "ideal" society would have the middle class as its largest group, which in turn, could yield greater equality for all.

More recently, the Asian Development Bank (2010) in its *2010 Key Indicators for Asia and the Pacific* stressed the vital role of the middle class in fostering private sector growth in Asia and the Pacific. In this report, it was pointed out that the middle class in developing Asia has strengthened, and that the middle class plays a crucial role in ensuring a steadier, more sustainable economic progress. In addition, it has been suggested that the middle class could take roles on both sides of supply and demand; being able to generate employment through private sector's business start-ups and microenterprises on one hand, while also boosting investments and production as consumers on the other (Aissa *et al*. 2011). Empirically, a higher income share of the poor and the middle class yields higher economic growth, *ceteris paribus*. Furthermore, economic growth faints when the income share of the rich grows[12] (Dabla-Norris et al. 2015).

Following the definition of Asian Development Bank's definition of the middle class (as those having incomes or consumptions between $2 per day and $20 per day in 2005 PPP prices) and the definitions of Asia-Pacific economies used by the Asian Development Bank, it can be observed that the middle class has grown in Asia-Pacific in both relative and absolute terms (Figure 12). The Asia-Pacific middle class has grown more than thrice in relative terms from 18.5% of the population in 1990 to 59.2% in 2011, and up nearly four times from about 500 million in 1990 to 2.1 billion in 2011. However, the bulk of the middle class in Asia and the Pacific is in the $2–$4 range, which has a high risk of falling into poverty.

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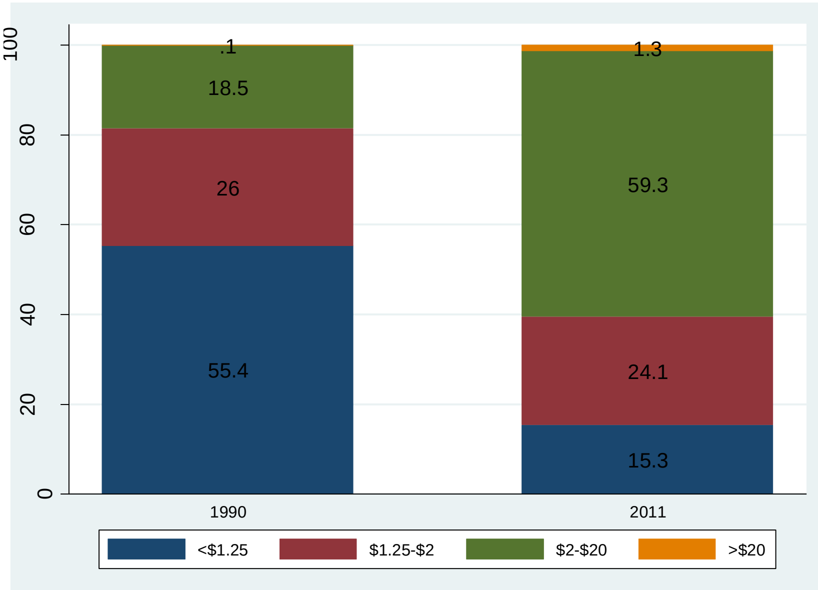
singly; for the addition of the middle class turns the scale, and prevents either of the extremes from being dominant."

[12] A rise of one percentage point (ppt) from the income share of the poor (bottom 20%) and the middle class (second and third quintile) is associated with higher GDP growth, i.e., by 0.38 ppt, 0.33 ppt, and 0.27 ppt, respectively. On the other hand, a one ppt increase from the income share of the rich (top 20%) is associated reflects to a decline in economic performance by 0.08 ppt.

Figure 12: Percentage of People by Income Group, 1990 and 2011



Source: Authors' estimates using data from PovcalNet (downloaded 12 January 2015).

Defining the middle class

While at present, there has yet to be an internationally accepted standard for defining the middle class, some definitions are based on a relative-sense: thresholds set in relation to the average (or median) income. The Pew Research Center (2015), refers to adults whose annual household income falls on two-thirds to double of the national median income as the middle class. In a similar vein, Easterly (2001) defines middle class to include individuals with incomes between the 20th and 80th percentile of the consumption distribution. Birdsall *et al*. (2000) suggests another definition with a relative-sense: those with incomes between 75 and 125 percent of the median per capita income.

Other researchers have defined thresholds for the middle class in an absolute sense. The poverty guru Martin Ravallion (2009), for instance, referred to the middle class as households whose consumption rests from USD 2 per day (median value for 70 national poverty lines) to USD 13 per day (US poverty line). As was earlier pointed out, the Asian Development Bank (2010) similarly used absolute thresholds ranging from USD 2 to USD 20 at 2005 PPP prices.

In the Philippines, Virola *et al*. (2013) preferred using a cluster analysis on income distribution based on the 2012 FIES to define the middle class, yielding this group as those with annual per capita incomes in 2012 ranging from about P64,317 up to P787,572. Meanwhile, Bersales *et al*. (2013) proposed a standardized definition of five classes of socio economic status (A to E) for use by market researchers on the basis of consumer quality (i.e. employment and educational characteristics of the household), household assets, amenities and facilities.

In this discussion paper, we reecho the proposal of Albert, Gaspar and Raymundo (2015) to divide the income distribution into seven income classifications (including the middle income class) based on multiples of the official poverty lines. Table 6 lists the definition of the middle income class, along with six other income classes. While official poverty lines actually vary across urban and rural areas within provinces in the country, we provide in Table 6 an indicative range of monthly family incomes for a household size of five, based on average official poverty lines.

Table 6. Income Classes in the Income Distribution, Indicative Income Ranges of Income Classes, and Sizes of Income Classes in 2012

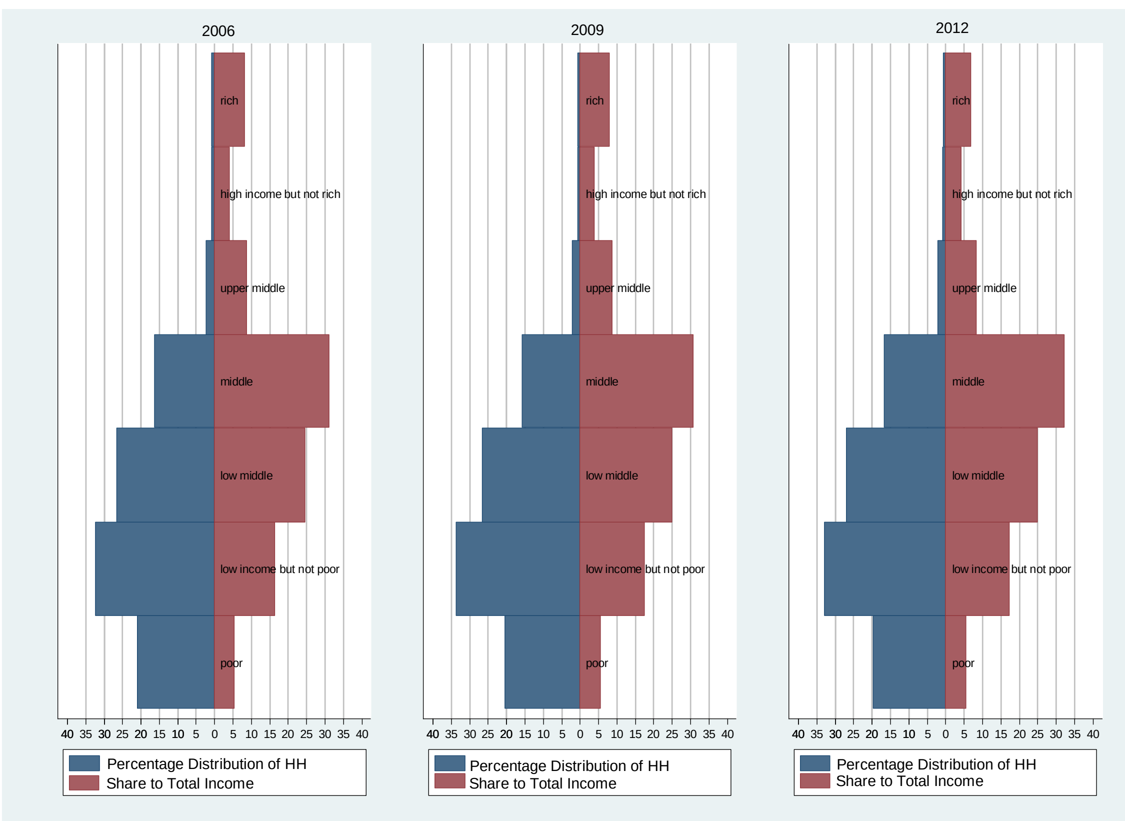
Income Class	Definition	Indicative Range of Monthly Family Incomes (for a Family Size of 5 members)	Size of Class (i.e. Number of Households)
Poor	Per capita income less than official poverty threshold	Less than PHP 7890 per month	4.2 million
Low income (but not poor)	Per capita incomes between the poverty line and twice the poverty line	Between PHP 7890 to PHP 15780 per month	7.1 million
Lower middle income	Per capita incomes between twice the poverty line and four times the poverty line	Between PHP 15780 to PHP 31560 per month	5.8 million
Middle income class	Per capita incomes between four times the poverty line and ten times the poverty line	Between PHP 31,560 to PHP 78,900 per month	3.6 million
Upper middle income	Per capita incomes between ten times the poverty line and fifteen times the poverty line	Between PHP78,900 to PHP 118,350 per month	470 thousand
Upper income (but not rich)	Per capita incomes between fifteen times the poverty line and twenty times the poverty line	Between PHP118,350 to PHP 157,800	170 thousand
Rich	Per capita incomes at least equal to twenty times the poverty line	At least PHP 157,800	150 thousand

Note: Authors' calculations on 2012 FIES, PSA

Marginal changes in income distribution from 2006 to 2012

In a span of three most recent waves of the FIES (2006, 2009, 2012), income distribution in the Philippines has shown only marginal changes (Figure 13). The rich, occupying the top bracket of income classes, accounted for only 0.8% of the total household population. Despite its meager size, the rich had a 7.1% share of the total household income in 2012, coming from 8.4% in 2006. Meanwhile, the poor, occupying the lowest bracket of income classes, only managed to account for a 5.6% share of total household income during the same period, while having a share of 19.7% of the total number of households. This pattern is consistent with the observation that income inequality has hardly changed over the years.

Figure 13. Distribution of households and shares of total household income by income group: 2006, 2009, and 2012



Note: Authors' calculations based on 2006, 2009, and 2012 FIES, PSA

Income shares of the middle class

In 2012, there are about 3.6 million households belonging to the middle class. The middle class accounted for 16.7% of the total number of households, which is slightly higher than the 16.2% and 15.8% registered in 2006 and 2009, respectively. Similar to the cases of other income classes, these changes in the income classification are marginal. Nonetheless, the change in the size of the middle class is notably accompanied by a similar movement in its income share. The income share of the middle class in 2012 is estimated at 32.2% of the total household income in the country. This is also higher than the 31.4% and 30.7% estimated in 2006 and 2009, respectively.

When the middle income class is aggregated with the lower middle (about 5.8 million) and upper middle (about 470 thousand) classes, this combined group comprises about 9 in 20 Filipino families in 2012 (45.1% in 2006, 44.6% in 2009, and 45.8% in 2012). The total share of the incomes of these three income groups comprises about two thirds of the whole country's household income (65.1 percent in 2006, 64.7 percent in 2009, and 65.6 percent in 2012).

Poor households (4.2 million), together with low income but not poor households (7.1 million) constitute more than half of the household population in 2012 (52.7% or about 11.3 million households). However, these two lowest brackets only have a quarter (23.4%) of the total household income in 2012. During the same year, a total of about 330 thousand households or only 1.5% of the aggregate household population, comprise the richest group (about 160 thousand) and the upper income but not rich class (about 170 thousand), which accounts for over a tenth of the total household income (11.4%).

Average per capita income improved in nominal terms, but offset by rise in price

On averaging the per capita income of the seven income groups, all income groups with the exception of the rich earned higher nominal incomes from 2006 to 2012 (Table 5). However, when accounting for inflation, there were no significant changes in incomes between 2009 and 2012 among all income groups, with the rich having been reported to have even lower incomes. This latter result though may be taken with a grain of salt. The data on the highest income group might be grossly underestimated in the FIES. Households from wealthy families are likely not interviewed for the FIES, given the lengthy interview time (of 5 hours per visit for each of the two visits) for the FIES. In addition, the challenge of recalling income (and spending) for the whole year might compromise the accuracy of income and expenditure data in the FIES, especially the income data (which is asked from households after questions on expenditures). Despite the truncated income distribution in the FIES, there are still insights gained in the income distribution.

Table 7. Average per capita income by income group: 2006, 2009, and 2012

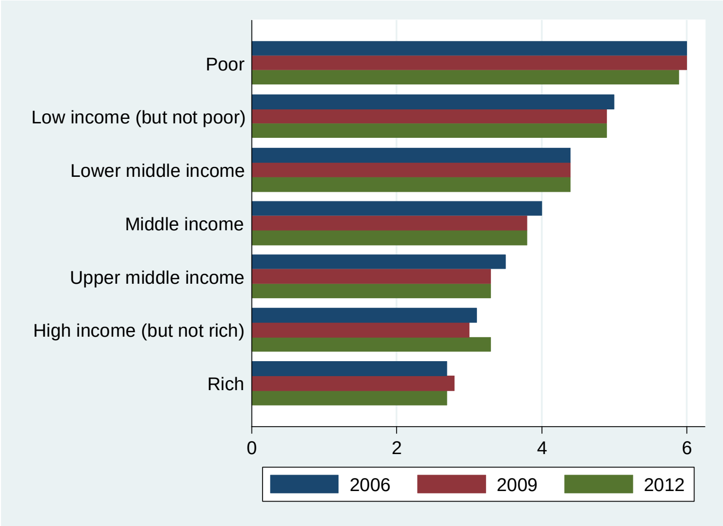
Income Group	At current prices			At constant 2006 prices		
	2006	2009	2012	2006	2009	2012
Poor	9,528	12,229	13,709	9,528	10,425	10,393
Low income (but not poor)	19,754	24,842	27,646	19,754	21,178	20,959
Lower middle	39,597	49,183	54,416	39,597	41,929	41,256
Middle class	83,989	104,112	115,879	83,989	88,757	87,853
Upper middle	171,669	212,670	236,173	171,669	181,305	179,055
High income (but not rich)	244,504	307,886	332,932	244,504	262,477	252,413
Rich	455,657	658,427	607,958	455,657	561,318	460,924

Note: Authors' calculations on 2006, 2009 and 2012 FIES and Consumer Price Index, PSA.

Middle Class characteristics

The average family size of Filipino middle class households is smaller than that of poor and low income families (Figure 14). On average, a middle class household comprises four members, which is lower than the average family size of six among poor households. Rich households have average household sizes of two to three members in 2006, 2009 and 2012.

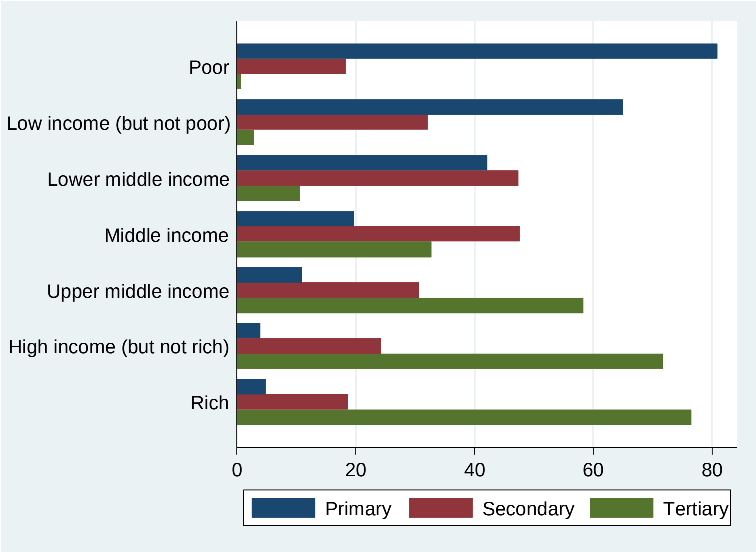
Figure 14. Average family size by income group: 2006, 2009, and 2012



Note: Authors' calculations based on 2006, 2009, and 2012 FIES, PSA

As is expected, educational attainment of the household head increases with increasing income. The middle class, in particular, typically has its household heads[13] finishing up to secondary education (Figure 15).

Figure 15. Educational level of household head by income group: 2012



Note: Authors' calculations based on 2012 FIES, PSA

[13] The household head is determined by the household member being interviewed.

In contrast, the poor and low income classes generally have their household heads attaining only up to the primary level of education, while majority of households from the rich and high income classes have finished at least a college degree. In consequence, efforts by the government to incentivize the poor in investing in the education of their children should pay off, assuming that the labor market will be able to absorb them into higher paying jobs once they attain better schooling. The educational background of parents has been noted to have long-term impacts on their children's developmental outcome. Dubow *et al*. (2009) suggest that parents' educational attainment when a child is 8 years of age significantly predicts the child's educational and occupational attainments, later in 40 years.

Geographically, a majority of middle class households appear to be in three regions - the National Capital Region (NCR), CALABARZON, and Central Luzon (see Table 7). This is understandable given that the largest share of economic activity happens in the NCR and surrounding areas, and the middle class would need to reside in areas of economic activity. The next administration may need to re-examine how to develop areas outside of the NCR, especially in the wake of current and worsening traffic conditions in the NCR. It may be important to think of creating a new political capital, as has been done in Malaysia (with Putra Jaya) and Myanmar (with Naypyitaw). This will require long term strategic planning.

Table 8. Income distribution by income group and by region: 2012

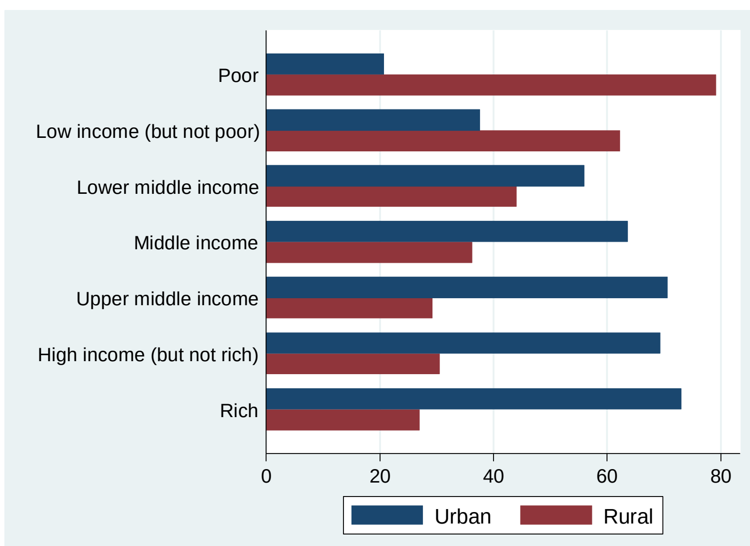
Region/Group	Poor	Low income (but not poor)	Lower middle income	Middle income	Upper middle income	High income (but not rich)	Rich
I - Ilocos Region	3.7	6.2	5.5	4.4	4.3	3.9	3.5
II - Cagayan Valley	3.1	4.5	3.4	2.8	3.1	2.3	2.1
III - Central Luzon	5.7	11.3	14.4	**12.4**	9.0	10.5	8.8
IVA - CALABARZON	6.1	13.2	18.8	**18.8**	17.1	17.6	15.4
IVB – MIMAROPA	3.6	3.3	2.7	2.4	2.0	1.7	3.5
V - Bicol Region	8.9	6.4	3.4	3.1	3.1	2.0	2.9
VI - Western Visayas	8.7	8.1	6.3	6.9	7.4	6.7	7.2
VII - Central Visayas	9.6	7.3	7.1	5.6	6.1	6.2	4.4
VIII - Eastern Visayas	8.0	4.2	2.6	2.5	2.8	4.0	3.4

IX - Western Mindanao	6.1	4.0	2.4	2.1	1.8	3.0	1.4
X - Northern Mindanao	7.6	4.8	3.2	3.0	3.1	3.4	4.4
XI - Southern Mindanao	6.4	5.6	4.5	3.6	3.0	4.4	1.8
XII - Central Mindanao	8.7	4.7	2.9	2.9	2.3	3.0	0.9
National Capital Region (NCR)	1.8	8.7	18.4	**25.6**	31.5	27.1	36.6
Cordillera Administrative Region	1.6	1.6	1.8	2.1	2.2	1.6	2.3
Autonomous Region in Muslim Mindanao	6.4	3.1	1.0	0.2	0.1	0.4	0.0
CARAGA	4.0	2.8	1.7	1.5	1.3	2.1	1.4

Note: Authors' calculations based on 2012 FIES, PSA

Dwelling deeper into the geographical differences in residence of income classes, the middle class is expectedly concentrated in urban areas (Figure 16). The poor and low income families, on the other hand, are highly concentrated in rural areas. Furthermore, the bulk of high income and rich households is difficult to specifically determine given their relatively small population.

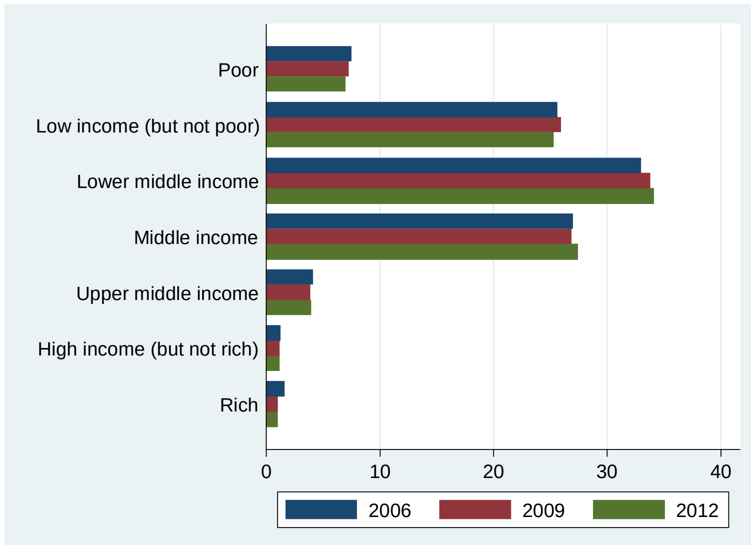
Figure 16. Income distribution by income group and by urban/rural classification: 2012



Note: Authors' calculations based on 2012 FIES, PSA.

Overseas remittances have been a substantial contribution to the stability of the Philippine economy in recent years with 2014 OFW remittances estimated at $ 26.9 billion, with cash remittances accounting for 8.5 percent of the GDP in 2014. Majority of overseas Filipinos belongs to the middle class, particularly in the lower middle class (Figure 17).

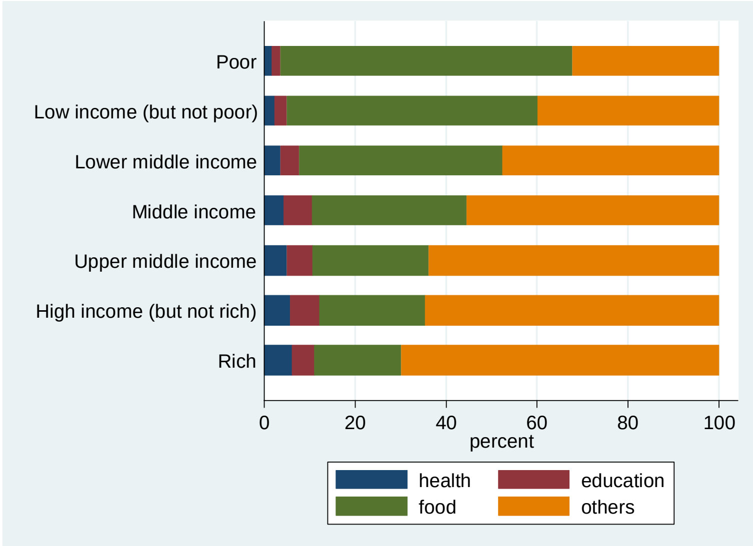
Figure 17. Families of overseas Filipinos by income group: 2006, 2009, and 2012



Note: Authors' calculations on 2006, 2009 and 2012 FIES, PSA

Data sourced from the FIES 2012 further suggests that households from the middle income class spend a big share of their income in human capital investments, such as education and health (Figure 18). The poor, on the other hand, spend the most of their income on food (consistent with Engel's law). Given the poor and low income's small income, the size of spending for food already limits their finances for educational and health spending. The rich and high income group, at first glance, could appear to be spending less on education than the middle class. However, it is important to note that these spending patterns are in shares and not in monetary values. Of the non-food expenses, the share of spending of the high income and rich groups on education and health is greatly outweighed by their spending on other non-food expenses.

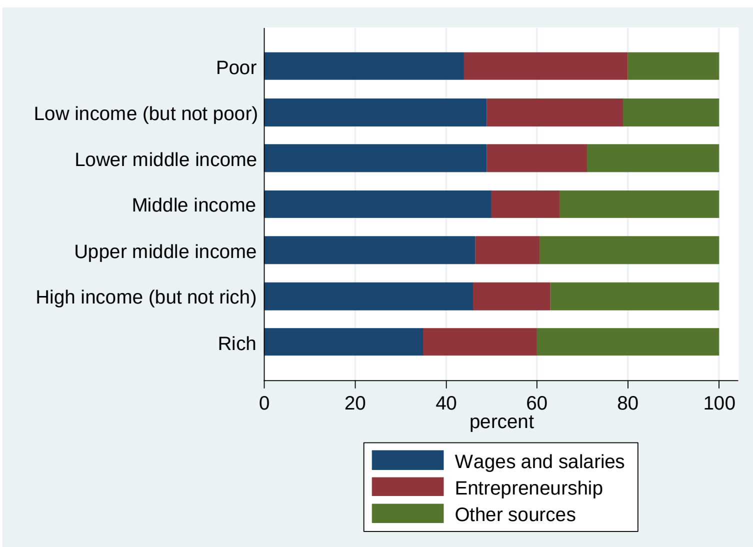
Figure 18. Spending pattern (% to total expenditure) by income group: 2012



Note: Authors' calculations based on 2012 FIES, PSA.

As far as labor and employment is concerned, it can be observed that household heads of the middle income class generally acquire their incomes through fixed regular employment (Figure 19); while in contrast, the poor and low income classes mostly rely on small-scale retail entrepreneurship that is considered part of vulnerable employment.

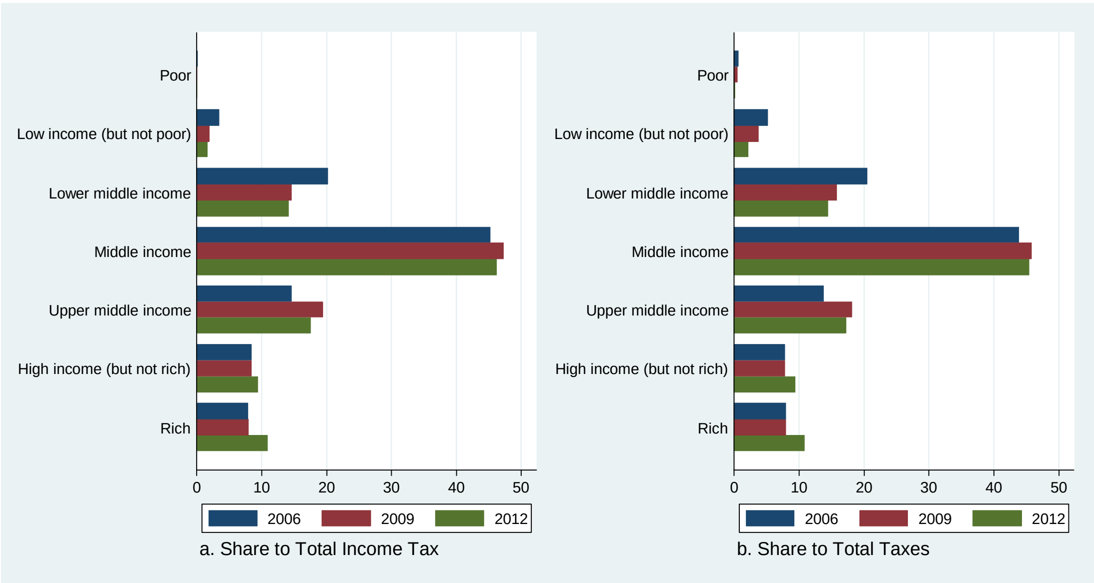
Figure 19. Major source of income of household head by income group: 2012



Note: Authors' calculations based on 2012 FIES, PSA.

With regular wages being the primary source of income by the middle income class, it is thus not surprising why the middle income class consistently accounts for the largest share not only in total income tax payments but also in total taxes (Figure 20).

Figure 20. Share to total income tax and total tax by income group, 2012



Note: Authors' calculations based on 2012 FIES, PSA.

Given that current personal income tax brackets have not changed since 1997, it would be important for government to lessen the tax burden of the middle class, and shift this burden to the wealthier segments of society. Manasan (2015) examines several current proposals in the legislature to reform the Personal Income Tax (PIT) law of 1997. She suggests that while the legislative proposals have differences in some facets, the various proposals for amending the PIT law generally aim to promote progressive taxation (except for two proposals, e.g. SB 2149 and HB 4829). The common grounds for the proposals are based on two premises – the need to eliminate the 'bracket creep'[14] in taxation which forces a higher tax burden to all individual income tax payers, with the lower taxable income brackets having relatively the highest increase;

[14] As discussed by Manasan (2015) - "Assuming that taxpayers pay the correct taxes, individual income taxpayers whose pre-tax incomes rose at the same rate as inflation between 1998 and 2014, such that the purchasing power of their income in 2014 is approximately the same as that in 1998, have had to pay higher taxes in 2014 (not just in peso terms but also in terms of effective tax rates) simply because their taxable income in 2014 have been pushed into the next higher income tax bracket relative to their situation in 1998, a phenomenon that is known as bracket creep."

and relieving the personal income taxpayers (who mostly belong to the middle income class) from a high tax burden, especially when compared to conditions in our ASEAN neighbors.

For the most part, having to pay lesser taxes would strengthen the middle class. With a larger take-home wage, the group could opt to spend more, or to invest more and have long-term financial engagements. However, the national government would still need to find alternative sources of revenue to compensate for the projected losses should one of these proposals be implemented.

5. Conclusions

There has been growing recognition that poverty reduction is at the heart of the development agenda. In consequence, the primary focus of many developing countries such as the Philippines has been to lay out national development plans, and put these plans at sync with global commitments to development, such as the MDGs and its successor, the SDGs. In relation to these national and global development agendas, statistics serve as inputs to assess socio-economic conditions. The StatDev indicator framework, for instance, provides an evaluation tool for the goals laid out in the PDP. As regards macro-economic goals, the country has achieved robust economic growth, low inflation, and improvements in its employment structure. Poverty rates though have not been reduced considerably despite a number of pro-poor programs such as the government's CCT that aim to incentivize poor households into investing in the education and health of their children, thus improving their chances to escape from intergenerational poverty. Still, it must be emphasized that the CCT would be expected to have its long term effect on reducing poverty when children beneficiaries are absorbed into the labor market with better educational attainments. The next government will have to be much more careful though in identifying indicators for monitoring its PDP, as many indicators in the current PDP are not outcome indicators. While the current government has laudably laid big investments in the social sector that will make the income distribution achieve adequacy, equity and efficiency, it is also important to make the political landscape more inclusive.

In recent years, poverty reduction has been rather modest in the Philippines despite rather broad-based economic growth owing to high levels of income inequality. Government programs that target the poor should be expanded to include low-income (i.e. near poor) households. Lower income and lower middle income classes, who are at strong risk of falling into poverty due to income shocks (i.e., illness, death of the provider, natural hazards), should also be provided targeted interventions. However, this will need serious examination of public revenue streams. Finally, it must be pointed out that while overseas workers' contributions to the economy have been a strong source of growth, however, it is our responsibility to have jobs for people in our country that will help them attain their needs and aspirations. The next government will have to be serious in putting the creation of jobs in their agenda by focusing on specific sectors, e.g. manufacturing, agriculture, mining, tourism, with the corresponding reforms and investments in power and infrastructure.

Other development strategies will also be required to boost sustained development. One of these is increasing the size and strength of the middle class. In this paper, we propose seven income classes for the income distribution whose thresholds are based official poverty lines. We profile the middle income class vis a vis other income classes, and note among other things, the differences of the middle income class families with other income classes in terms of demographic composition, educational attainment of household heads, and employment activities. In order to strengthen and increase the size of the middle income class, it will be important for government to reform the current PIT. Through a more progressive taxation, the government can raise the income share of the middle class to support growth. However, the PIT reform should only be a part of a larger reform of taxation policy in order to address projected shortfalls in revenue generation. It may be important to examine the effects of removing PIT altogether, and instead only collect consumption taxes (as the wealthy find too many income tax loopholes) with heavy consumption taxes on luxury items, especially cars, and minimal consumption taxes on basic items (especially those consumed by the poor).

While there may be unintended consequences (i.e., effects of increased urbanization) that may likely occur when the middle class grows in number and their incomes increase, but expanding the size and strength of the middle class will also provide opportunities for more inclusive development, shared prosperity, and sustained growth in the country.

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