國立中山大學　大陸研究所

碩士論文

中國與菲律賓農村發展之比較研究 ： 以鄉鎮企業與中小企業為重點

A Comparative Study of the Rural Development between Mainland China and Philippines: A Focus on Township and Village Enterprises (TVEs) and Small and Medium Enterprises (SMEs)

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A Comparative Study of the Rural Development between Mainland China and Philippines: A Focus on Township and Village Enterprises (TVEs) and Small and Medium Enterprises (SMEs)"

A Masters Thesis
Submitted by:

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Institute of Mainland China Studies
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In Partial Fulfillment
Of the requirements for the Masters Degree
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ENDORSEMENT

In partial fulfillment of the requirements for Masters Degree in Mainland China Studies, this masters thesis entitled **"A Comparative Study of the Rural Development Between Mainland China and Philippines: A Focus on Township and Village Enterprises (TVEs) and Small and Medium Enterprises (SMEs)"** has been prepared and submitted for panel review by **Helen Grace Dacillo Acharon**, acceptance of which is hereby endorsed.

Prof. Teh-Chang Lin, Ph.D.

Adviser

摘要

這篇論文主要比較中國的鄉鎮企業（TVE）和菲律賓的中小型企業（SME）。鄉鎮企業和中小型企業被認為是“經濟產權”，為迅速的城市化和扶貧行業帶來的不利影響作為 fiscalizer，尤其在農村地區更顯著。雙方發揮了重要作用，即在國內生產總值（GDP）的貢獻和就業率。雖然兩個國家在某些方面不同，作者就兩個國家的兩個地區，即中國廣西壯族自治區和菲律賓的 Socsksargen 地區，來提出可能影響他們的經濟表現的共同點和分歧。從收集到的數據，再評估菲律賓中小型企業與中國大陸鄉鎮企業相比之下增長緩慢的的原因。農村工業化是從三個重要因素的角度來看：社會，經濟，和政府的支持。就這三個因素來考量，中國的鄉鎮企業是成功的，因為所有的三個因素對他們十分有利。儘管有政府的支持和豐富的自然資源，易取的海外主要市場提供的經濟機會，菲律賓因大規模農村地區的貧困，人民缺乏技能和創業能力，和其他因素如廣泛的武裝衝突和各大小團體的威脅，經濟已顯疲憊狀態。

此外，這份文件很清楚的顯示原來的要點，這要點也在第 4 章裏—“中國的鄉鎮企業和菲律賓的中小企業越成功，就對鄉村的發展越有利” 提到。1978 年改革後，中國已經證明了這點。從 1979 年的水平，中國的鄉鎮企業在 1990 年顯著上升 13 倍以上—這是從 1 40 萬到 1 850 萬。這包括其他的增長因素，如產值，就業和稅收減免。1978 年的改革特徵—門戶開放政策，去集體化和去中央化等巨大的政策，都是農村工業化的催化劑，可是其鄉鎮企業的增長是一個 SULNAM（自發的，無組織，無領袖，非意識形態，非政治性的運動）的現象。因此，社會和經濟

因素與當地政府提供的支持遠超過其他因素。無可否認，13 億人口中 8 億人在農村的中國，這是經濟增長和社會產權其中一個強大的支柱。

Abstract

This thesis evaluates the comparison between China's Township and Village Enterprises (TVEs) and Philippines' Small and Medium Enterprises (SMEs). TVEs and SMEs are considered "economic equity" programs of the two countries that serve both as a fiscalizer of the adverse effects of rapid urbanization and as poverty alleviation industry, more specifically in the rural areas. Both economic equities play an important role in Gross Domestic Product (GDP) contribution and employment rate. Although the two countries differ in some aspects, the author compared two regions from each country, namely Guangxi Zhuang Autonomous Region in China and SOCSKSARGEN Region in the Philippines, to situate the shared commonalities and differences that may affect their economic performance. From the data gathered, the research proceeded to evaluate the reasons for the slow growth of SMEs in the Philippines as compared with the TVEs in Mainland China. The rural industrialization was viewed from the perspective of three important factors: societal, economic, and government policy support. After examining these three factors, China's TVEs proved to be successful because all the three factors have been favorable to them. On the Philippines' side, despite all the government support and economic opportunities attendant to it such as its richness in natural resources and good trade access to major foreign markets, there seemed to be sluggish economic growth brought about by societal factors like massive poverty in the rural areas, lack of skills and entrepreneurial capabilities, and other factors such as the prevalence of armed conflicts between the government and the various threat groups in some regions.

Furthermore, this paper has driven home the point as exhaustively shown in the discussions in Chapter 4 that - “the more successful China’s TVEs and Philippines’ SMEs are, the better for the rural development of the country”. China has proven this after the 1978 reforms when in 1990 TVEs dramatically rose 13 times more from its 1979 level - that is from 1.4 million to 18.5million. This included other factors of growth like output value, employment and taxes remitted. While the features of the 1978 reforms - open door policy, decollectivization and decentralization, among others, were macro policies which fertiled the soil for rural industrialization in China, its TVEs growth was in a SULNAM (Spontaneous, Unorganized, Leaderless, Non-ideological, Apolitical Movement) phenomenon. Thus, it was more of societal and economic factors with the local government providing the policy support. Undeniably, it is one of the strong pillars of China’s economic growth and social-equity considering that 800 million of the 1.3 billion population of China is in the countryside.

<u>Dedication</u>

For my father and best friend,

HERVE CUTAMORA ACHARON

"…you gave me the greatest gift anyone could give another person…

you believed in me."

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We are all inventors, each sailing out on a voyage of discovery,

Guided each by a private chart, of which there is no duplicate.

The world is all gates, all opportunities.

---Ralph Waldo Emerson

As we travel along life's endless paths, we are always making discoveries, by accidents and sagacity, of things which we were not in quest of. My journey in Taiwan has been what I may call, "a good accident". What brought me in this beautiful island was my desire to reach for my dreams and of course, the generosity and noble intentions of Tita Gloria Mercado, MNSA. The past two years have held challenges and brought experiences like I've never known before. National Sun Yat-sen University has not only provided me a quality education but also a comforting refuge of security and belongingness. My stay in Taiwan has taught me some values which molded me to become the person I am today: **maturity** – I am not just referring to the age but to the wisdom I acquired with every major event I encountered – my decision-making ability has perked up and my receptiveness in handling situations beyond my control has improved (I've been tested lately with my father's death); **independence** – after living with my parents for 23 years, living on my own has been one great leap for my adult life (I can go home past the curfew). But along the harum-scarum, devil-may-care road to freedom, I have learned to understand that independence and responsibility goes hand in hand; **humility –** according to Zen Master Li Yuansong, enlightenment can only come after humility – the wisdom of realizing one's own ignorance, insignificance and

lowliness, without which one cannot see the truth; and lastly, **gratitude** – nothing is more satisfying than feeling grateful for all the good things in your life. I learned that appreciation is one way of recognizing the significance or value of the people and things around me. They say that feeling gratitude and not expressing it is like wrapping a present and not giving it.

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you’ve always been there for me despite the distance. Know that I’m always here for you, too; To my former supervisors and officemates in Equitable PCI Bank – Ma’am Babes, Sir Hernan, Ate Grace, Kuya Jhe, Ate Leah, Ate Marsha, Ate Sharon, Ate Mona, Sir Sonny, Sir Jinny, Eeyan, Hirvey, and Alain; and to my loyal friends - Erick, Dacoy, Grace, Carla, Little, and Mariz – beyond words, I truly appreciate your presence in my life.

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My God will never ask me to do something difficult and then leave me hanging to do it on my own. I must completely trust Him so I can also trust and have confidence in myself through Him. No matter what He tells me to do, He will always, all the time, provide me with the ability to do and accomplish it.

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ABBREVIATIONS

BSMBD	-	Bureau of Small and Medium Business Development
BSMED	-	Bureau of Small and Medium Enterprise Development
CBBEs	-	Countryside Barangay Business Enterprises
CSMI	-	Council on Small-and Medium-Scale Industries
DBP	-	Development Bank of the Philippines
DTI	-	Department of Trade and Industry
FGD	-	Focused Group Discussion
GDP/GNP	-	Gross Domestic Product/Gross National Product
GFIs	-	Government Financial Institutions
GLF	-	Great Leap Forward
ILO	-	International Labor Organization
IMF	-	International Monetary Fund
LDCs	-	Less Developed Countries
MNCs	-	Multi-National Companies
NICs	-	Newly Industrializing Countries
PBSP	-	Philippine Business for Social Progress
RCC	-	Rural Credit Cooperatives
R&D	-	Research & Development
RP	-	Republic of the Philippines
SBGFC	-	Small Business Guarantee and Finance Corporation
SMED	-	Small and Medium Enterprise Development
SOC	-	Social Overhead Capital
SOEs	-	State-Owned Enterprises
SULONG	-	SME Unified Lending Opportunities for National Growth
TVEs	-	Township and Village Enterprises
UNCTAD	-	United Nations Conference on Trade and Development
UNDP	-	United Nations Development Program
UP-ISSI	-	University of the Philippines Institute of Small Scale Industries

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CHAPTER 1
Introduction

A. Background

Development is the most important challenge facing the human race and it could mean differently to many people. However, for purposes of this paper, development is operationally defined as the "process of improving the quality of human lives". It encompasses the three facets of the development process as follows: a). raising people's living levels – their incomes and consumption levels of food, medical services, education, etc. through relevant economic growth processes; b). creating conditions that are conducive to the growth of people's self-esteem through the establishment of social, political, and economic systems and institutions that promote human dignity and respect; and, c). increasing people's freedom by enlarging the range of their choice variables, as by increasing varieties of consumer goods and services.[1]

Development in a more encompassing sense goes beyond the provision of the minimum basic needs and also includes the strengthening of institutions as well as systems that support the transformation processes.[2] More challenging however in the development sphere is the purposive focus on rural development[3]. The broad spectrum of rural development activities include: small farmers' agricultural progress; the provision of physical and social infrastructure; the development of rural nonfarm industries; and the

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[1] Michael P. Todaro, *Economic Development* (New York: Addison Wesley Publishing Company, 6th edition, 1999), p. 685
[2] Speech of President Fidel V. Ramos on Philippines 2000 at the National Defense College of the Philippines, 1998
[3] In some literatures and articles is synonymously referred to as countryside development.

capacity of the rural sector to sustain and accelerate the pace of these improvements over time.[4]

Rural industry has been an important part of China's economy for centuries, but it played an especially important role during the golden age of TVEs, from 1978 through 1996. During this period TVEs played the catalytic role in transforming the Chinese economy from a command economy to a market economy. Springing up in the rural areas, which were much less rigidly controlled than the cities, the entry of TVEs provided competition to state-run industrial enterprises and drove the process of marketization forward in the entire economy. TVEs increased rural incomes, absorbed rural labor released from farms, and helped narrow the urban-rural gap.

TVEs had a special distinction during this period because of their unusual ownership and corporate governance setup. Originating under the rural communes, most TVEs were collectively owned: TVEs thus presented the unusual spectacle of publicly owned enterprises growing rapidly and providing the competitive challenge that dissolved the monopoly previously held by public (state-run) enterprises. A diverse set of TVE models adapted to a range of different conditions and ended up fundamentally changing nearly every part of the Chinese economy[5].

Beginning in the 1980s, China's reform leaders progressively internationalized the rural areas around major coastal cities, especially in the key delta regions. Township

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[4] Todaro, pp. 699-700

[5] Barry Naughton, "Rural Industrialization: Township and Village Enterprises" in *The Chinese Economy Transitions and Growth.* (London, England: The MIT Press, 2007), p. 271

and village enterprises (TVEs) penetrated global markets. The number of these enterprises surged, and they grew rapidly to account for well over half of national rural output. They thus quickly became more important than farming in the rural economy, and they facilitated the relocation of labor out of agriculture. By the early 1990s, they accounted for over 30 percent of total national gross value of output and over a quarter of export earnings. They had thus become one of the most dynamic sectors in the Chinese economy and a major force for structural change. In addition, the fact that they were operating outside the state plan meant that they were also an important element in the "privatization" of the Chinese economy. The development of rural enterprises has thus been one of the most distinctive features of economic reform and economic growth in China over the past decade. As China's reforms evolve, they have the potential to generate further growth and change[6].

TVEs underwent a further dramatic transformation after 1995-1996. Most obviously, TVEs privatized. A range of different local approaches were used, but the result was that by the new millennium, TVEs had undergone a dramatic conversion to a mostly privately run ownership structure. The ownership transformation is best understood in the context of large changes in the overall economic environment in which TVEs operated. After the mid-1990s, TVEs were forced to undergo substantial restructuring. Product market competition intensified, and credit became scarcer and more expensive. Newly private TVEs responded to these pressures, but some firms went out of business, and the collectively owned TVE sector shrank. Overall, the ability of the

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[6] Chen Chunlai et al., 'Rural Enterprise Growth in a Partially Reformed Chinese Economy" in *Rural Enterprises in China*. (New York: St. Martin's Press, Inc., 1994), p. 4

sector to absorb rural labor declined. TVEs today face significant challenges, but TVEs overall have continued to grow and evolve and take on new roles in China's economy. Rural industries today are less tied to their local government and community, and are rapidly taking new forms and roles.

Rural household businesses were very important in China's traditional economy, leading it to be called "bottom heavy" because of the preponderance of small, household-based, flexible, and market-oriented production units. Rural households spun and wove cotton, raised silkworms, and reeled silk thread; they cured tobacco, milled grain, and made noodles. Households made mud bricks and hewed timber, carted goods to market, and ran shops and businesses. Most of China's rural areas were knit into a dense web of markets and sideline occupations. The most important nonagricultural undertakings were handicraft operations processing agricultural goods and converting them into market goods[7].

The organic link between growing and processing agricultural product in the countryside was broken under the command economy. When the state established its monopoly control over agricultural goods during the 1950s, rural processing businesses were inevitably cut off from their supplies. Grain, cotton, silk, peanuts, and soybeans – the staple supplies of nonagricultural businesses – were taken by the state immediately after the harvest. In fact, during the 1950s the countryside became de-industrialized. As the rural population was organized into agricultural collectives, nonagricultural

[7] Naughton, p. 272

production declined, and the state itself took over virtually all manufacturing production[8]. Of course, these policies were an integral part of the creation of the command economy system.

The harmful effects of this policy on the rural areas were soon evident. Household income declined in commercialized rural areas where a high proportion of income previously came from sideline activities. Some formerly prosperous, densely populated regions found they had difficulty supporting large populations on the tiny amount of agricultural land available per capita. Many specialized handicrafts fell into decay as state factories moved into mass production. One among the many strands of policy during the Great Leap Forward was an effort to change the overwhelming dependence on agriculture in rural areas by creating Communes and encouraging them to engage in a wide range of nonagricultural undertakings. Under the new Communes, villages were encouraged to start factories and construction teams, as well as service undertakings of all kinds. But the drain of manpower from agriculture proved to be disastrous, especially in the less developed provinces. Virtually all these Commune-sponsored enterprises shut down during the terrible post-Leap crisis in 1961-1962.

A second attempt to develop rural industry occurred during the Cultural Revolution era. After 1970, during the Maoist "new leap forward", the government encouraged a new wave of state-sponsored rural industrialization under the rubric of "commune and brigade enterprises." This time, care was taken to avoid the problems that

[8] Fei Hsiao-t'ung, *Rural Development in China: Prospect and Retrospect.* (Chicago: University of Chicago Press, 1989)

crippled the GLF. Movement of workers out of agriculture was carefully controlled; rural industries were tied to the agricultural collectives; and rural industries were constantly exhorted to "serve agriculture." The communes and brigades that had been organized during the GLF served as platforms for industrial development and rural industry began to revive rapidly during the 1970s under Cultural Revolution era policies[9].

This 1970s rural industrialization was very different from traditional rural industry, which had primarily processed agricultural products. The new exhortation to "serve agriculture" was interpreted narrowly to mean supplying producers' goods to agriculture. Policy during the 1970s stressed the "Five Small Industries", rural industries that included iron and steel, cement, chemical fertilizer, hydroelectric power, and farm implements. Rural industries were expected to replicate the heavy-industry-based Big Push development strategy: the factories were small relative to urban factories but large compared to rural workshops and factories in most countries. The Five Small Industries were all capital-intensive industries usually thought to be characterized by significant economies of scale[10]. They did not employ very many workers, relative to the expensive investment required, and government subsidies were important in some sectors. As a result, through 1978, rural industries did not absorb a significant part of the rural labor force, which was still overwhelmingly engaged in agriculture: 90% of the rural labor force was engaged primarily in agriculture in 1978.

[9] Ibid, 273
[10] Christine Wong, "Rural Industrialization in the People's Republic of China: Lessons from the Cultural Revolution Decade" in Joint Economic Committee, U.S. Congress, *China under the Four Modernizations.* (Washington, DC: U.S. Government Printing Office, 1982), p. 394

Rural industries in the 1970s were a peculiar product of the command economy. If it had been feasible to integrate rural industries at that time into the command-economic system, they would have been, but since most industries were low-tech firms serving a few local customers, it was much more practical to leave them outside the plan. At the same time, rural enterprises were firmly ensconced in the existing collective structures in the countryside, as their very name – commune and brigade enterprises – indicated. Workers in rural industry sometimes got paid in work points, and rural-industry profits were sometimes used to raise the value of work points for the collective as a whole. Revenues earned from rural enterprises were regularly channeled by community governments to public works and aid-to-agriculture projects[11]. In a sense, rural collectives were being allowed to share in some of the income-earning potential created by the state's monopoly over industry. Maoist China was well-known for its promotion of rural industry, but the type of industry fostered was a curious offshoot of the command economy. As of 1978, China still lacked the dense network of small-scale, nonagricultural activities that characterize prosperous country sides in Asia, but which China had suppressed in the 1950s.

During 1979 the central government shifted its policy toward rural enterprises in important respects. The general liberalization of that time included a relaxation of the state monopoly on purchase of agricultural products, allowing more to remain on rural markets and thus available to rural enterprises for processing. The new policy was "Whenever it is economically rational for agricultural products to be processed in rural

[11] Christine Wong, "Interpreting Rural Industrial Growth in the Post-Mao Period" in *Modern China*. (Washington, DC: U.S. Government Printing Office, 1982), p. 3

areas, rural enterprises should gradually take over the processing work". TVEs, since they were collective firms, were still ideologically safe: urban firms were encouraged to subcontract work to TVEs. Once rural industries were allowed to perform agricultural processing, they were essentially free to engage in whatever activity they could find a market for. The highly restrictive Cultural Revolution model of rural industrialization was relaxed, and rural industrialization was permitted in response to multiple market opportunities. Of course, state firms and state procurement monopolies fought to maintain their monopolies, and there were policy twists and turns and slow progress in the sensitive areas. Nevertheless, local government officials quickly recognized the economic implications of TVE development, and became vigorous advocates and defenders of TVEs. Indeed, for many localities, TVEs were the only available path out of poverty.

Between 1978 and the mid-1990s, TVEs were clearly the most dynamic part of the Chinese economy. TVE employment grew from 28 million in 1978 to a peak of 135 million in 1996, a 9% annual growth rate. TVE value added, which accounted for less than 6% of GDP in 1978, increased to 26% of GDP in 1996, notwithstanding the fact that GDP itself was growing very rapidly during this period. The growth of nonagricultural income raised rural incomes and made a contribution to shrinking the urban-rural gap. Not only has TVE growth been rapid, but that growth has also played an important role in the transformation of the Chinese economy, as TVEs have created competition for existing SOEs and served as a "motor" for the entire transition process. In industry TVEs presented mounting competition for SOEs throughout the 1980s and early 1990s. SOE monopoly profits were competed away as aggressive TVEs drove price relationships into line with underlying costs. SOEs had to implement new incentive programs and improve efficiency in order to survive in the face of the TVE competitive onslaught. In the foreign trade area TVEs provided opportunities for Chinese exporters to move into new labor-intensive manufactures. In the end TVEs transformed virtually every aspect of the Chinese economy[12].

Township and village enterprises can be likened to the Philippines' small and micro enterprises. These enterprises provide alternative livelihood to the millions who otherwise would be unemployed[13]. The Philippine government, for some years now, has adopted a policy of relying on the private sector as the engine of growth. As such, the government has been getting out of activities which the private sector is in a better position to undertake, and concentrating on improving the business environment to enhance the competitiveness of its industry and services sectors. The government is giving special attention to the development of entrepreneurs and small and medium enterprises or SMEs[14]. SMEs in the Philippines are defined as business activities or enterprises with total assets, excluding land, valued at between PhP1,500,001 to PhP15 million after financing for small enterprises and between PhP15,000,001 and PhP100 million for medium enterprises. Micro-enterprises, meanwhile, are those with total assets, excluding land, valued at PhP1.5 million or less after financing.

[12] Naughton, pp. 274-275
[13] "Current situation of SMEs and the SME Development Plan," http://www.dti.gov.ph/contentment/66/69/files/SME.ppt (accessed November 24, 2007)
[14] Brenda Mendoza and Gilberto Llanto, "SMEs in the Philippines" in *Entrepreneurship and SMEs in Southeast Asia.* (Singapore: Institute of Southeast Asian Studies, 2004), p. 150

In terms of number of workers, micro-enterprises are those with less than 10 workers while small and medium enterprises are those with 10 to 99 and 100 to 199 workers, respectively. Data on SMEs in the Philippines are sadly inadequate. Nevertheless, it is estimated that SMEs and micro-enterprises (excluding cooperatives, farmers, and the informal sector) account for 99 percent of the country's total number of enterprises. SMEs are also estimated to account for 67 percent of total employment and around 33 percent of gross domestic product. Philippine SMEs are typically family-owned; domestic market oriented with multi-functional management, workers and equipment; innovative; and use resources more efficiently than large enterprises. However, these are usually characterized by low productivity, low level of technology and skills, lack of records and low product quality. These also suffer from lack of access to financing, markets, and information. Given the characteristics and importance of SMEs and micro-enterprises to the economy, the Philippine government has more often than not adopted a policy of supporting and promoting the development of SMEs[15].

Efforts to develop SMEs gained momentum in the 1960s with the creation of the University of the Philippines Institute of Small Scale Industries (UP-ISSI) in 1966 to extend assistance to small-and-medium-sized industries. In 1969, the "Magna Carta for Social Justice and Economic Democracy" was adopted to signify the government's commitment to the development of small-scale industries. However, it was deemed to have provided for a limited form of assistance since it was focused only the financial needs of the sector. In 1970, the National Council for Small and Medium Industries was created to "integrate all government agencies servicing small-and medium-scale

[15] Ibid, pp. 151-153

industries and establish guidelines for government policies to ensure the stability and continued growth" of the sector. The Council was replaced in 1974 by the Commission on Small-and Medium-Scale Industries which was renamed Council on Small-and Medium-Scale Industries (CSMI). The CSMI was established to coordinate and integrate the policies and programmes of all agencies involved in the development of small-and medium-sized industries to make these more responsive to the needs of said industries. It was abolished in 1981. It was also in the 1970s when a supervised credit programme was implemented by the UP-ISSI and the Social Security System to provide long-term financing to small industries and the Development Bank of the Philippines (DBP) became the primary institution for financing small-and medium scale industries in the rural areas at very attractive and liberal terms and conditions.

With the change in administration in 1986, the development of micro, cottage, small and medium industries was lodged with the Department of Trade and Industry (DTI), specifically with its Bureau of Small and Medium Business Development or BSMBD (which has been renamed to Bureau of Small and Medium Enterprise Development or BSMED) and its Micro Industries Development Programme. Other programmes and projects were also developed in conjunction with the private sector and non-government organizations such as the Philippine Business for Social Progress (PBSP). To spur the rapid development of the rural areas, Republic Act (RA) No. 6810 or the Countryside Barangay Business Enterprises (CBBEs) law, also known as the Kalakalan 20 law, was enacted in December 14, 1989. The said law was patterned after the "Law 20" of Italy. It aimed to remove bureaucratic restrictions on the setting up of, and provide incentives to, CBBEs to encourage these to grow in as free an economic environment as possible, and in the process, encourage those in the informal sector to join the formal sector. The Kalakalan 20 law expired on 13 December 1994.

On 4 January 1991, RA 6977 or the "Magna Carta for Small Enterprises" was enacted "to promote, develop, and assist small-and medium-scale enterprises through the creation of a Small and Medium Enterprise Development (SMED) Council, and the rationalization of government assistance programmes and agencies concerned with the development of small-and medium-enterprises, and for other purposes." RA 6977 as amended by RA 8289 on 6 May 1997 requires banks to lend at the minimum 6 per cent and 2 per cent of its net lending portfolio to small-and medium-enterprises, respectively. It also created the Small Business Guarantee and Finance Corporation or SBGFC to source and adopt development initiatives for globally competitive small and medium enterprises in terms of finance, technology, production, management and business linkages, and provide, promote, develop and widen in both scope and service reach various alternative modes of financing for small and medium enterprises, including but not limited to, direct and indirect project lending, venture capital, financial leasing, secondary mortgage and/ or rediscounting of loan papers to small business, secondary/regional stock markets. The SBGFC is attached to the DTI and is under the policy, programme and administrative supervision of the SMED Council. SBGFC was merged with the Guarantee Fund for Small and Medium Enterprises on 30 July 2001 with the issuance of Executive Order No. 8 and the surviving entity (SBGFC) was renamed SB Corporation. The merger was made to enable the new organization to be more responsive to the credit requirements of the SME sector and to widen the coverage of alternative financing instruments needed to make Philippine businesses competitive in a rapidly globalizing environment.

Under the 2001-2004 Medium-Term Philippine Development Plan, the promotion of SMEs shall be pursued to enhance the competitiveness of the industry and services sectors. In line with this strategy, the Philippine Government is working with the banks to enable the latter to understand and service the needs of SMEs, and hence be encouraged to reduce bank requirements and lend more to SMEs. Alternative sources of financing are being pursued, including guarantee programmes and micro-financing. Relative to micro-financing, the Bangko Sentral ng Pilipinas recently opened a rediscounting facility for banks engaged in micro-finance lending. The facility will be made available to rural and co-operative banks to maximize their ability to serve enterprises that would not otherwise qualify for credit from big commercial banks.

Industry clustering which will facilitate the provision of cluster-specialized resources such as technology, skills or networking infrastructure as well as marketing and distribution support to SMEs is being promoted to increase the pace of development of SMEs in the rural areas. The improvement of facilities of existing provincial SME Development Centres to enhance their capacity to provide SMEs with information, training and advisory services is being looked into along with the feasibility of putting up a National Business Registry to track all business firms from start-up to closure and provide an up-to-date picture of the status and location of business establishments at any time. The numerous existing training programmes for SME entrepreneurs, managers and workers are being rationalized in co-ordination with the private sector to improve content and delivery as well as to ensure that these address the needs of SMEs[16].

To situate the commonalities and differences between the two economic equity programs of China and the Philippines, the socioeconomic profiles of one of the major regions of each country, namely, Guangxi Zhuang Autonomous Region and SOCSKSARGEN Region are included in the study. China and Philippines differ in some aspects but the two regions selected for comparison share a number of attributes that may affect their economic performance.

B. Research Motivation

From embracing an alternative socialist system in the 1950's to implementing autarky in the 1960's until finally opening up to the rest of the world economy in 1978, China definitely underwent various reforms and economic policies which shaped the modern Chinese economy we see today. To some extent, reforms pushing for decentralization, marketization, and decollectivization largely influence the Chinese economy into what it looks like today – fueling its massive economic growth of 9.5% annually over the past 5 years[17]. While several studies analyzing the impact of Chinese economic growth on foreign trade relations, politics, and regional security exist, no literature consciously integrates key elements of modern Chinese economic reform and analyzes it as a potential model for economic development yet. Hence, the purpose of

[16] Ma. Lucila A. Lapar, *Growth and Dynamics of Small and Microenterprises: Does Finance Matter?* PIDS Working Paper no. 91-12. (Makati: Philippine Institute of Development Studies, 1991)
[17] "China to pursue new growth model in years ahead," *The Philippine Star*, September 29, 2006

this study is to analyze one of the key reforms China undertook over the past decades in the light of seeking opportunities and insights that could apply for the Philippine context.

Mao always believed that development will have to start from the farmers. A product of decentralized economic planning, township and village enterprises were small to medium scale enterprises initiated by farmer groups to increase opportunities for earning more income. Decentralized by nature, these enterprises were autonomous in decision making, pricing, marketing, labor management, and in closing or merging with other enterprises as it deems fit. Essentially, township and village enterprises opened up or even fueled development in the rural regions, where over 800 million Chinese live by providing an alternative source of livelihood even without government direct intervention. Essentially the first ones to enter the "market" and initiate reform in a socialist economy, these enterprises were responsible for bringing economic development to the bottom as well. It accounts for 41 percent of contribution to GDP, making it the largest single group[18]. No wonder, even the Chinese government admits that, "township and village enterprises are an important force in promoting the new surge in the national economy." And even more compelling considering that 800 million of China's 1.3 billion population lives in the rural areas.

In 2001, SME accounts for 99.6 percent of the total number of firms in the Philippines. However, unlike the model of China wherein township and village enterprises account for the largest contribution to the GDP, the opposite is true for the

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[18] "Isn't China's Economy State-run?" http://www.chinainsight689.com/china_economy_state_run.htm (accessed November 24, 2007)

Philippines, wherein SME accounts for only 32 percent of the value added to GDP. Comparing to other Asian neighbors, productivity of Philippine SME does not fare well at all[19].

China provided an excellent economic development paradigm with the TVES in the core. Essentially, this insight is validated by the fact that several other nations, especially the least developing ones, are actually pushing for the development of micro-enterprises. Development should not just come from the top – it should also come from the bottom. However, this may not hold true for the Philippines where there exist fierce competition and great difficulty to enter the market. Policies, therefore, must focus on diminishing these barriers to entry in two ways – making capital and information, the two ingredients of business success, highly available. As to how the Philippine government will do this will be the focus of this study. Although the Philippine government is exerting great effort to push for the development of these enterprises, the challenge is to keep on improving, such that in the truest sense, economy can be driven from the bottom as well.

Picking up some lessons learned from an economic giant in the region is very logical especially after the pronouncement of the Arroyo Administration in 2002 to go into deep engagement with China. This policy pronouncement is coming from the strategic position of China in the region. China and the Philippines are geographically close to each other and share lots of similarities. Both sides have great potential in

[19] "Current Situation of SMEs and the SME Development Plan," http://www.dti.gov.ph/contentment/66/69/files/SME.ppt (accessed November 24, 2007)

cooperation in various sectors, such as agriculture, fishery, infrastructure, machinery, tourism, etc.[20]

Figure 1 – Strategic Proximity Map – Philippines –China (Source: Center for Space and Remote Sensing, National Central University, 2001)[21]

The configuration of the 7, 107 islands of the Philippine archipelago is grouped into three – Luzon, Visayas and Mindanao. The author grew up in the biggest island of Mindanao which is considered to be the richest in terms of natural resources. However it is facing two conflict fronts by both the Muslim secessionist group and the communist insurgents. Despite its vast resources 4 out of the 6 Regions which comprise it are ranked among the poorest.[22] Hence, the result of this study could be input to the on-going refinements in SMEs policies of the Philippines.

[20] "Speech of H.E. Ambassador Song Tao at Guangxi-Philippines Trade and Economic Cooperation Promotion Conference" http://ph2.mofcom.gov.cn/aarticle/chinanews/200804/20080405478128.html (accessed July 5, 2008)
[21] Center for Space and Remote Sensing, National Central University, 2001
[22] Mindanao Development Framework, 2004

Figure 2 – The Philippine Map (Source: OP Home, 2003)[23]

C. Research Problem and Hypothesis

Hypothesis

The more successful TVEs and SMEs are, the better the rural development of the country.

China's rural enterprises are economic entities established by various levels of local government in the countryside or by the peasants themselves. They may be run by towns (zhen), townships (xiang), districts (qu), and villages (cun), or by peasants either as

[23] "The Philippine Map" http://www.gov.ph/aboutphil/images/bigmap.gif (accessed November 5, 2007)

individuals, as partnerships, or in cooperation with their village. Their undertakings encompass all types of economic activity, including agriculture, industry, construction, transport, commerce and services. Since Chinese statistics provide a breakdown based on ownership of or responsibility for the assets, it is possible to distinguish between rural and urban enterprises, because rural enterprises are owned by the successors to the commune system and by the peasants while urban enterprises are owned by the various levels of state government and by urban residents[24].

It should be noted that the classification of enterprises by type of ownership and control does not always correspond precisely to a classification by location. In the urban economy, there are some collectively or privately owned enterprises that are outside the plan, but their significance is small in urban economies relative to state enterprises. Furthermore, some rural enterprises may operate in or close to urban areas[25].

Rural enterprises operate outside the state plan. Unlike urban state enterprises, they are subject to "hard budget constraints" in that their owners (the peasants or the townships) do not have any guaranteed budget income from above. They buy inputs and sell outputs in free markets, without having to fulfill plan obligations to the state. Despite this market orientation, however, their origins in the collective system mean that they commonly have a strong linkage with governments at township level and below[26].

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[24] Chunlai et al, pp. 8-9
[25] Ibid, p. 9
[26] Ibid, p. 10

The total number of rural enterprises increased to over 20 million in 1992, more than a threefold increase from 1984. Their total labor force by 1992 was over 105 million, exceeding total employment in state enterprises. While the number of township and village enterprises has remained about the same over the longer term, employment in these two sub-categories rose from 28 million in 1978 to 51.5 million in 1992. The increase in the average employment of township and village enterprises from 19 in 1978 to about 34 in 1992 is a significant development[27].

Even by 1987, rural enterprises were more important in the rural economy than was agriculture. Rural enterprises are spread across all the sectors of the economy but, in 1990, 74.1 percent of total output value of all rural enterprises came from industrial activities. Indeed, their industrial output value accounted for around one-third of all industrial output value. In terms of ownership, the encouragement given to private and new types of cooperative ventures since 1978 has created a much more complex economic system. The most dynamic growth has taken place in individually owned enterprises, even though their labor force and total revenue reflected their smaller size and lower levels of capital intensity. At the end of 1991, these made up 92 percent of the total number of rural enterprises, employed over 50 percent of the total workforce, and produced 33 percent of the gross value of output[28].

The growth of township enterprises has also had a significant effect on government budgets at all levels. In 1987, tax paid by township and village enterprises

[27] Ibid, p.11
[28] Ibid, pp. 12-13

amounted to 16.81 billion yuan, 7.2 percent of the total state budget income of 234.66 billion yuan and 12.2 percent of industrial and commercial tax revenue of 138.07 billion yuan. By 1992, rural enterprise tax payments had risen to 47.02 billion yuan, or 15 percent of all tax income and 11.2 percent of all state budget income. Taxes on township enterprises also accounted for a considerable share of revenue at county level. According to information from counties in suburban Shanghai and in southern Jiangshu where rural enterprises are highly developed, industrial and commercial taxes, product taxes and income taxes from rural enterprises generally made up 70-80 percent of county budget income in the late 1980s.

Furthermore, from 1980 to 1987, enterprises run by townships and villages spent 85.36 billion yuan on reinvestment, on supporting agricultural production, and on collective welfare activities. This was 9.8 percent more than state budget expenditure of 77.78 billion yuan on supporting agricultural production and other agricultural activities over the same period. Apart from formal levies, rural enterprises are also called upon to make all kinds of informal payments and transfers to the local community. The wealth generated by these enterprises is thus important for many aspects of the economy. Furthermore, this feature of rural enterprises' economic significance has continued to expand as their proportional share in the economy has grown.

The development of rural enterprises also accelerated the development of small towns. From 1981 to 1985, the growth of township enterprises led to the establishment of more than 1300 small towns annually. Once again, this figure has to be treated with caution since many of these towns may have existed previously as commune headquarters and their reclassification as towns to some extent merely reflects the administrative reforms that have taken place. Also, the rules for reclassification were changed in 1984 to allow for a smaller proportion of non-agricultural population in towns, and there are many perceived advantages to local officials in gaining the new status, including additional budget expenditures and the rights to establish administrative units associated with town status.

Nevertheless, the growth of rural industries has been one of the factors enabling the reclassification to take place. As a result of these changes, the proportion of population classified as urban, which had been under 20 percent for most of the period since 1949, jumped to 32 percent in 1984 and reached nearly 47 percent in 1987. The demand for industrial products generated by this growth of towns and rural enterprises also had a feedback effect on urban industry. According to one source, in 1987 township enterprises consumed products worth 30 billion yuan from state-run enterprises[29].

The above brief analysis has illustrated the dramatic growth that has taken place in recent years in China's rural enterprises. It has also demonstrated the burgeoning significance of those enterprises (a) as an outlet for the savings being accumulated in the countryside following the first stages of the reforms; (b) for the subsequent relocation of labor out of traditional agriculture; (c) for the finances of local government, especially revenues received through taxes and profits; and (d) for the rate of urbanization.

[29] Ibid, pp. 10-14

Small and medium enterprises (SMEs) play a crucial role in the development of the Philippine economy. They represent 99.6 percent of all businesses registered in the country and employ 69.9 percent of the total labor force. In addition, they account for 32 percent of the country's gross domestic product (GDP).[30] Underscoring the importance of SMEs in the country's economic growth and development, President Gloria Macapagal-Arroyo has included in her 10-point national development agenda the creation of 6-10 million jobs in six years, through more opportunities given to entrepreneurs, a tripling of the amount of loans available to SMEs, and the development of 1-2 million hectares of land for agri-business.

Prior to the 10-point agenda, President Arroyo had called on her administration to craft the SME Unified Lending Opportunities for National Growth (SULONG) program. The program is geared towards expanding the enterprise base by graduating micro, small and medium enterprises to higher levels of classification by providing them with more access to government assistance. "Sulong" is a Filipino word which means "move forward", and is an appropriate rallying call by the present administration to make SMEs an even more productive sector.

Building on the previous administrations' efforts to develop SMEs in the Philippines, the National SME Agenda has, as an essential ingredient, the greater communication and closer coordination among key agencies mandated to support SMEs, resulting in less duplication of efforts and in more complimentarily of assistance programs offered by various government agencies.

[30] Medium Term Philippine Development Plan (2006-2010), 2005

Led by the Department of Trade and Industry (DTI), the program calls for the concerted efforts of key players in its various elements, namely human resource development and entrepreneurship training, market development, product development and technology intervention, advocacy for enabling environment, and financing[31].

This thesis is essentially a comparative study of the rural development between Mainland China and Philippines focusing on township and village enterprises (TVEs) and small and medium enterprises (SMEs), respectively. The author will examine some of the factors which contributed to the acceleration in the growth of rural enterprises, concentrating on the favorable fundamentals that encouraged local governments to promote that development and the role of the national government itself. Then analyze these key factors China undertook over the past decades in the light of seeking opportunities and insights that could apply for the Philippine context. Specifically, the research study will seek answers to the following questions:

1. What are the factors which contributed to the growth of TVEs in Mainland China and what is the current state of TVEs vis a vis China's overall economic growth?
2. Given the fact that the Philippine government recognizes the important role of the SMEs in the economy by giving opportunities for these enterprises through various support programs, what are the reasons for the slow growth of SMEs in the Philippines?

[31] Rhodora M. Leano, "SMEs in the Philippines" in *CACCI Journal, Vol. 1, 2006*

3. In the light of the findings of the preceding research questions, what abstractions of lessons learned for both countries and policy recommendation can be drawn as inputs to Philippine rural development policy?

Chapter II
Theoretical Framework

A. Theories

The Classical Theories

Among the classical political economists the three most original contributors to dynamic theory were Smith, Ricardo, and Marx. The theoretical contribution of Marx was, however, so distinctive that it is customary to single out Marxian theory from the main body of classical political economy.

Prior to founding of the classical school, another group of economists had, earlier in the eighteenth century, also studied the process of economic growth. In France the physiocrats analyzed the scope for advances in both total output and output per worker, concluding that these could only be generated by the agricultural sector: only labor employed in exploitation of the land was capable of generating surplus output in excess of the value of material inputs and the labor employed. Expanded agricultural output leads in turn to an increased supply of food and raw materials to other branches of the economy, permitting an expansion of manufacturing output also; but manufacturing itself could never generate economic growth, for artisans add to their raw materials only the value of their own labor.

The physiocrats' ideas represented a reaction to contemporary economic policy in France, which discriminated against agriculture while deliberately promoting, and subsidizing, the development of manufacturing. This policy was geared to generating national self-sufficiency in manufacturers. In so doing it reflected the mercantilist philosophy of the times.

From the work of Adam Smith – the founding father of the classical school – onwards, there is a recognition that a growth dynamic can be generated in manufacturing as well as agriculture: this sector too can generate advances not only in total output but in labor productivity. The classical, indeed, perceived the scope for productivity advances to be greater in manufacturing than in agriculture, and some saw in this fact reason for considerable pessimism concerning the prospects for sustained overall advances in productivity and mass welfare.

These developments in perception were associated with the articulation of a number of propositions concerning the causes of growth, some of which were completely new, and with a new elaboration also of the constraints to growth[32].

Among the most notable features of classical growth theories are the following:

1. The importance of market expansion as a stimulus both to expansion of total output and to raising labor productivity.
2. The importance of profits as the source of finance for new investment, in contrast to the unproductive use of land rents and the zero or minimal savings capability of wage-earners.

[32] Diana Hunt, *Economic Theories of Development: An analysis of Competing Paradigms*. (Maryland: Barnes & Noble Books, 1989), pp. 9-10

3. The potential of an agricultural sector dominated by renter land owners to impose a brake on overall economic growth (Ricardo).
4. The need to liberalize trade as a means of enlarging the market (Smith) and of permitting the exploitation of comparative advantage (Ricardo).
5. The importance of technological change in raising labor productivity and in helping to meet the food and raw material demands of a rising population.

In the early twentieth century Arthur Young took Adam Smith's emphasis on the extension of the market a step further, arguing that technical innovation can itself generate an extension of the market through raising labor productivity and, hence, incomes and demand.

Turning to Marxian dynamic theory, among the basic points that Marx emphasizes are the following:

1. The motive force of the capitalist system, and one of the factors that differentiates it from earlier modes of production, is the capitalist's drive to accumulate wealth through productive investment.
2. Capitalism is based on the antagonistic relationship of two classes, capitalist and proletarian. The former own the means of production and use the power derived from this ownership to extract and appropriate surplus value from the workers, the surplus value being used to finance further accumulation.
3. The drive to accumulate leads the capitalist to search constantly for means, including technical innovation that will enable him to raise his rate of profit

and/or undercut his competitors. The consequent development of the productive forces is the positive aspect of capitalism.

4. Meanwhile, capitalist competition also undercuts and destroys all backward pre-capitalist producers (artisans, peasants) as well as the less efficient capitalists.
5. As individual capitals expand, in association with technological advance, plant size rises, and labor becomes more specialized and routinized and also increasingly interdependent. Simultaneously workers become increasingly alienated from the labor process and the capitalist class.
6. The anarchic nature of capitalist competition leads to periodic crises caused by an underlying tendency to a decline in the rate of profit and by recurrent phases of overproduction and under consumption. In these periods labor is laid off and wages fall.
7. As the scope for further uncoordinated development of the productive forces approaches exhaustion, a final crisis will lead the working class to appropriate the means of production and instigate the transition to a new, egalitarian mode of production. Lenin, however, provided grounds for doubting whether the colonies would experience the same pattern of capitalist development as the imperial powers.

Also in the early twentieth century, Schumpeter sought to make an analytical break with the classical growth theorists. A clear distinction is drawn between growth and development: for Schumpeter growth is a slow and rather insignificant process, resulting from investment in additional capital financed largely by reinvestment of profits.

Development is an innovatory process. It is this that provides advancing economies with their real dynamic. The key actors in development are not producer capitalists reinvesting profits, but the entrepreneurs who perceive opportunities for using existing resources in new ways and who organize and implement the exploitation of these opportunities, and the banks who create the credit that enables the entrepreneurs to finance new enterprises. In the early stages of the industrial revolution capitalist and entrepreneur were usually one and the same, but with time their functions have become separated.

These were the main elements of dynamic theory that were available in the 1940s and 1950s for the early development economists to draw upon[33].

Leading Theories of Economic Development

Every nation strives after development. Economic progress is an essential component, but it is not the only component. Development is not purely an economic phenomenon. In an ultimate sense, it must encompass more than the material and financial side of people's lives. Development should therefore be perceived as a multidimensional process involving the reorganization and reorientation of entire economic and social systems. In addition to improvements in incomes and output, it typically involves radical changes in institutional, social, and administrative structures as well as in popular attitudes and, in many cases, even customs and beliefs. Finally, although development is usually defined in a national context, its widespread realization

[33]Hunt, pp. 34-36

may necessitate fundamental modification of the international economic and social system as well[34].

The post-World War II literature on economic development has been dominated by four major and sometimes competing strands of thought: (1) the linear-stages-of-growth model, (2) theories and patterns of structural change, (3) the international dependence revolution, and (4) the neoclassical, free-market counterrevolution. In addition, the past few years have witnessed the emergence of a fifth approach that has been called the new or endogenous theory of economic growth.

Theorists of the 1950s and early 1960s viewed the process of development as a series of successive stages of economic growth through which all countries must pass. It was primarily an economic theory of development in which the right quantity and mixture of saving, investment, and foreign aid were all that was necessary to enable Third World nations to proceed along an economic growth path that historically had been followed by the more developed countries. Development thus became synonymous with rapid, aggregate economic growth[35].

The Linear-Stages Theory

When interest in the poor nations of the world really began to materialize following the Second World War, economists in the industrialized nations were caught off guard. They had no readily available conceptual apparatus with which to analyze the

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[34] Todaro, p. 69
[35] Ibid, p. 70

process of economic growth in largely peasant, agrarian societies characterized by the virtual absence of modern economic structures. But they did have the recent experience of the Marshall Plan, under which massive amounts of U.S. financial and technical assistance enabled the war-torn countries of Europe to rebuild and modernize their economies in a matter of a few years. Moreover, was it not true that all modern industrial nations were once undeveloped agrarian societies? Surely their historical experience in transforming their economies from poor agricultural subsistence societies to modern industrial giants had important lessons for the "backward" countries of Asia, Africa, and Latin America. The logic and simplicity of these two strands of thought – the utility of massive injections of capital and the historical pattern of the now developed countries – was too irresistible to be refuted by scholars, politicians, and administrators in rich countries to whom people and ways of life in the Third World were often no more real than U.N. statistics or scattered chapters in anthropology books.

A. Rostow's Stages of Growth

Out of this somewhat sterile intellectual environment, fueled by the cold war politics of the 1950s and 1960s and the resulting competition for the allegiance of newly independent nations, came the stages-of-growth model of development. Its most influential and outspoken advocate was the American economic historian Walt W. Rostow. According to the Rostow doctrine, the transition from underdevelopment to development can be described in terms of a series of steps or stages through which all countries must proceed. As Rostow wrote in the opening chapter of his *Stages of Economic Growth:*

> This book presents an economic historian's way of generalizing the sweep of modern history…It is possible to identify all societies in their economic dimensions, as lying within one of five categories: the traditional society, the pre-conditions for take-off into self-sustaining growth, the take-off, the drive to maturity, and the age of high mass consumption…These stages are not merely descriptive. They are not merely a way of generalizing certain factual observations about the sequence of development of modern societies. They have an inner logic and continuity…They constitute, in the end, both a theory about economic growth and a more general, if still highly partial, theory about modern history as a whole.

The advanced countries, it was argued, had all passed the stage of "take-off into self-sustaining growth," and the underdeveloped countries that were still in either the traditional society or the "preconditions" stage had only to follow a certain set of rules of development to take off in their turn into self-sustaining economic growth.

B. The Harrod-Domar Growth Model

One of the principal tricks of development necessary for any takeoff was the mobilization of domestic and foreign saving in order to generate sufficient investment to accelerate economic growth. The economic mechanism by which more investment leads to more growth can be described in terms of the Harrod-Domar growth model. Harrod and Domar have provided a model of growth in which the rate of growth of output which is warranted is given by the planned savings rate divided by the planned capital: output ratio. Since current investment plans are largely independent of current savings and consumption plans, there can be no certainty that output will actually grow at the warranted rate, for investors may be forced to adjust to unanticipated changes in demand.

Such adjustments entail short-run variations in the capital: output ratio followed by adjustment of investment plans.

Both Harrod and Domar were concerned that the planned savings rate “s” in Western Europe and North America was too high for the maintenance of stable growth, for actual “s” warranted a long-run growth rate in excess of that permitted by the rate of growth of the labor force. The physical impossibility of carrying out a rate of investment at full employment sufficient to match “s” would generate periodic deflationary pressures. According to the model there are three concepts of growth: (1) warranted growth, which is the rate of output growth at which firms believe they have the correct amount of capital and therefore do not increase or decrease investment, given expectations of future demand; (2) natural rate of growth, which is the rate at which the labor force expands, a larger labor force generally means a larger aggregate output; and (3) actual growth, which is the actual aggregate output change.

Two possible problems are observed in an economy according to the Harrod-Domar model. First, the relationship between the actual and natural (population) growth rates can cause disparities between the two, as factors that determine actual growth are separate from those that determine natural growth. Factors such as birth control, culture, and general tastes determine the natural growth rate. However, other effects such as the marginal propensities to save and consume influence actual output. There is no guarantee that an economy will achieve sufficient output growth to sustain full employment in a context of population growth. The second problem identified in the model is the relationship between actual and warranted growth. If it is expected that output will grow, investment will increase to meet the extra demand. The problem arises when actual growth either exceeds or fails to meet warranted growth expectations. A vicious cycle can be created where the difference is exaggerated by attempts to meet the actual demand, causing economic instability.

Although the Harrod-Domar model was initially created to help analyze the business cycle, it was later adapted to explain economic growth. Its implications were that growth depends on the quantity of labor and capital; more investment leads to capital accumulation, which generates economic growth. The model also had implications for less economically developed countries; labor is in plentiful supply in these countries but physical capital is not, slowing economic progress. Less developed countries do not have sufficient average incomes to enable high rates of saving, and therefore accumulation of the capital stock through investment is low. The model implies that economic growth depends on policies to increase investment, by increasing saving, and using that investment more efficiently through technological advances. The model concludes that an economy does not find full employment and stable growth rates naturally[36].

Structural-Change Models

Structural-change theory focuses on the mechanism by which underdeveloped economies transform their domestic economic structures from a heavy emphasis on traditional subsistence agriculture to a more modern, more urbanized, and more industrially diverse manufacturing and service economy. It employs the tools of

[36] Todaro, pp. 71-75

neoclassical price and resource allocation theory and modern econometrics to describe how this transformation process takes place. Two well-known representative examples of the structural-change approach are the "two-sector surplus labor" theoretical model of W. Arthur Lewis and the "patterns of development" empirical analysis of Hollis B. Chenery.

A. The Lewis Theory of Development

Basic Model

One of the best-known early theoretical models of development that focused on the structural transformation of a primarily subsistence economy was that formulated by Nobel laureate W. Arthur Lewis in the mid-1950s and later modified, formalized, and extended by John Fei and Gustav Ranis[37]. The Lewis two-sector model became the general theory of the development process in surplus-labor Third World nations during most of the 1960s and early 1970s. It still has many adherents today, especially among American development economists.

In the Lewis model, the underdeveloped economy consists of two sectors: a traditional, overpopulated rural subsistence sector characterized by zero marginal labor productivity – a situation that permits Lewis to classify this as surplus labor in the sense that it can be withdrawn from the agricultural sector without any loss of output – and a high productivity modern urban industrial sector into which labor from the subsistence sector is gradually transferred. The primary focus of the model is on both the process of

[37] John C. H. Fei and Gustav Ranis, *Development of the Labor Surplus Economy: Theory and Policy*. (Homewood, Ill: Irwin, 1964)

labor transfer and the growth of output and employment in the modern sector. Both labor transfer and modern-sector employment growth are brought about by output expansion in that sector. The speed with which this expansion occurs is determined by the rate of industrial investment and capital accumulation in the modern sector. Such investment is made possible by the excess of modern-sector profits over wages on the assumption that capitalists reinvest all their profits. Finally, the level of wages in the urban industrial sector is assumed to be constant and determined as a given premium over a fixed average subsistence level of wages in the traditional agricultural sector. At the constant urban wage, the supply curve of rural labor to the modern sector is considered to be perfectly elastic.

B. Structural Change and Patterns of Development

Like the Lewis model, the patterns-of-development analysis of structural change focuses on the sequential process through which the economic, industrial, and institutional structure of an underdeveloped economy is transformed over time to permit new industries to replace traditional agriculture as the engine of economic growth. However, in contrast to the Lewis model and the original stages view of development, increased savings and investment are perceived by patterns-of-development analysts as necessary but not sufficient conditions for economic growth. In addition to the accumulation of capital, both physical and human, a set of interrelated changes in the economic structure of a country are required for the transition from a traditional economic system to a modern one. These structural changes involve virtually all economic functions, including the transformation of production and changes in the composition of consumer demand, international trade, and resource use as well as changes in socioeconomic factors such as urbanization and the growth and distribution of a country's population.

Empirical structural-change analysts emphasize both domestic and international constraints on development. The domestic ones include economic constraints such as a country's resource endowment and its physical and population size as well as institutional constraints such as government policies and objectives. International constraints on development include access to external capital, technology, and international trade. Differences in development level among developing countries are largely ascribed to these domestic and international constraints. However, it is the international constraints that make the transition of currently developing countries differ from that of now industrialized countries. To the extent that developing countries have access to the opportunities presented by the industrial countries as sources of capital, technology, and manufactured imports as well as markets for exports, they can make the transition at an even faster rate than that achieved by the industrial countries during the early periods of their economic development. Thus, unlike the earlier stages model, the structural-change model recognizes the fact that developing countries are part of a highly integrated international system that can promote (as well as hinder) their development.

The best-known model of structural change is the one based largely on the empirical work of Harvard economist Hollis B. Chenery, who examined patterns of development for numerous Third World countries during the postwar period[38]. His empirical studies, both cross-sectional (among countries at a given point in time) and time-series (over long periods of time), of countries at different levels of per capita income led to the identification of several characteristic features of the development process. These included the shift from agricultural to industrial production, the steady accumulation of physical and human capital, the change in consumer demands from emphasis on food and basic necessities to desires for diverse manufactured goods and services, the growth of cities and urban industries as people migrate from farms and small towns, and the decline in family size and overall population growth as children lose their economic value and parents substitute child quality (education) for quantity[39].

The International-Dependence Revolution

During the 1970s, international-dependence models gained increasing support, especially among Third World intellectuals, as a result of growing disenchantment with both the stages and structural-change models. Essentially, international-dependence models view Third World countries as beset by institutional, political, and economic rigidities, both domestic and international, and caught up in a dependence and dominance relationship with rich countries. Within this general approach are three major streams of thought: the neocolonial dependence model, the false-paradigm, and the dualistic-development thesis.

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[38] Hollis B. Chenery, *Structural Change and Development Policy.* (Baltimore: Johns Hopkins University Press, 1979)
[39] Todaro, p. 81

A. The Neocolonial Dependence Model

The first major stream, the neocolonial dependence model, is an indirect outgrowth of Marxist thinking. It attributes the existence and continuance of Third World underdevelopment primarily to the historical evolution of a highly unequal international capitalist system of rich country-poor country relationships. Whether because rich nations are intentionally exploitative or unintentionally neglectful, the coexistence of rich and poor nations in an international system dominated by such unequal power relationships between the center (the developed countries) and the periphery (the LDCs) renders attempts by poor nations to be self-reliant and independent difficult and sometimes even impossible.

Certain groups in the developing countries (including landlords, entrepreneurs, military rulers, merchants, salaried public officials, and trade union leaders) who enjoy high incomes, social status, and political power constitute a small elite ruling class whose principal interest, knowingly or not, is in the perpetuation of the international capitalist system of inequality and conformity by which they are rewarded. Directly and indirectly, they serve (are dominated by) and are rewarded by (are independent on) international special-interest power groups including multinational corporations, national bilateral-aid agencies, and multilateral assistance organizations like the World Bank or the International Monetary Fund (IMF), which are tied by allegiance or funding to the wealthy capitalist countries. The elites' activities and viewpoints often serve to inhibit any genuine reform efforts that might benefit the wider population and in some cases actually lead to even lower levels of living and to the perpetuation of underdevelopment.

In short, the neo-Marxist, neocolonial view of underdevelopment attributes a large part of the Third World's continuing and worsening poverty to the existence and policies of the industrial capitalist countries of the Northern hemisphere and their extensions in the form of small but powerful elite or comprador groups in the less developed countries. Underdevelopment is thus seen as an externally induced phenomenon, in contrast to the linear-stages and structural-change theories' stress on internal constraints such as insufficient savings and investment or lack of education and skills. Revolutionary struggles or at least major restructurings of the world capitalist system are therefore required to free dependent Third World nations from the direct and indirect economic control of their First World and domestic oppressors[40].

One of the most forceful statements of the international-dependence school of thought was made by Theotonio Dos Santos: Underdevelopment, far from constituting a state of backwardness prior to capitalism, is rather a consequence and a particular form of capitalist development known as dependent capitalism…Dependence is a conditioning situation in which the economies of one group of countries are conditioned by the development and expansion of others. A relationship of interdependence between two or more economies or between such economies and the world trading system becomes a dependent relationship when some countries can expand through self-impulsion while others, being in a dependent position, can only expand as a reflection of the expansion of the dominant countries, which may have positive or negative effects on their immediate development. In either case, the basic situation of dependence causes these countries to be both backward and exploited. Dominant countries are endowed with technological, commercial, capital and socio-political predominance over dependent countries – the form this predominance varying according to the particular historical moment – and can therefore exploit them, and extract part of the

[40] Todaro, pp. 82-83

locally produced surplus. Dependence, then, is based upon an international division of labor which allows industrial development to take place in some countries while restricting it in others, whose growth is conditioned by and subjected to the power centers of the world[41].

B. The False-Paradigm Model

A second and a less radical international-dependence approach to development, which is called the false-paradigm model, attributes Third World underdevelopment to faulty and inappropriate advice provided by well-meaning but often uninformed, biased, and ethnocentric international "expert" advisers from developed-country assistance agencies and multinational donor organizations. These experts offer sophisticated concepts, elegant theoretical structures, and complex econometric models of development that often lead to inappropriate or incorrect policies. Because of institutional factors such as the central and remarkably resilient role of traditional social structures (tribe, caste, class, etc.), the highly unequal ownership of land and other property rights, the disproportionate control by local elites over domestic and international financial assets, and the very unequal access to credit, these policies, based as they often are on mainstream, Lewis-type surplus-labor or Chenery-type structural-change models, in many cases merely serve the vested interests of existing power groups, both domestic and international.

In addition, according to this argument, leading university intellectuals, trade unionists, future high-level government economists, and other civil servants all get their training in developed-country institutions where they are unwittingly served an unhealthy

[41] Benjamin J. Cohen, *The Question of Imperialism: The Political Economy of Dominance and Dependence.* (New York: Basic Books, 1973)

dose of alien concepts and elegant but inapplicable theoretical models. Having little or no really useful knowledge to enable them to come to grips in an effective way with real development problems, they often tend to become unknowing or reluctant apologists for the existing system of elitist policies and institutional structures. In university economics courses, for example, this typically entails the perpetuation of the teaching of many irrelevant Western concepts and models, while in government policy discussions too much emphasis is placed on attempts to measure capital-output ratios, to increase savings and investment ratios, or to maximize GNP growth rates. As a result, desirable institutional and structural reforms are neglected or given only cursory attention.

C. The Dualistic-Development Thesis

Implicit in structural-change theories and explicit in international-dependence theories is the notion of a world of dual societies, of rich nations and poor nations and, in the developing countries, pockets of wealth within broad areas of poverty. Dualism is a concept widely discussed in development economics. It represents the existence and persistence of increasing divergences between rich and poor nations and poor peoples on various levels. Specifically, the concept of dualism embraces four key elements:

1. Different sets of conditions, of which some are “superior” and others “inferior,” can coexist in a given space. Examples of this element of dualism include Lewis’ notion of the coexistence of modern and traditional methods of production in urban and rural sectors; the coexistence of wealthy, highly educated elites with masses of illiterate poor people; and the dependence

notion of the coexistence of powerful and wealthy industrialized nations with weak, impoverished peasant societies in the international economy.

2. This coexistence is chronic and not merely transitional. It is not due to a temporary phenomenon, in which case time could eliminate the discrepancy between superior and inferior elements. In other words, the international coexistence of wealth and poverty is not simply a historical phenomenon that will be rectified in time. Although both the stages-of-growth theory and the structural-change models implicitly make such an assumption, the facts of growing international inequalities seem to refute it.

3. Not only do the degrees of superiority or inferiority fail to show any signs of diminishing, but they even have an inherent tendency to increase. For example, the productivity gap between workers in developed countries and their counterparts in most LDCs seems to widen with each passing year.

4. The interrelations between the superior and inferior elements are such that the existence of the superior elements does little or nothing to pull up the inferior element, let alone "trickle down" to it. In fact, it may actually serve to push it down – to "develop its underdevelopment."[42]

The Neoclassical Counterrevolution

In the 1980s, the political ascendancy of conservative governments in the United States, Canada, Britain, and West Germany brought with it a neoclassical counterrevolution in economic theory and policy. In more developed nations, this counterrevolution favored supply-side macroeconomic policies, rational expectations

[42] Todaro, pp. 84-85

theories, and the privatization of public corporations. In developing countries it called for freer markets and the dismantling of public ownership, statist planning, and government regulation of economic activities. Neoclassicists obtained controlling votes on the boards of the world's two most powerful international financial agencies – the World Bank and the International Monetary Fund. In conjunction and with the simultaneous erosion of influence of organizations such as the International Labor Organization (ILO), the United Nations Development Program (UNDP), and the United Nations Conference on Trade and Development (UNCTAD), which more fully represent the views of Third World delegates, it was inevitable that the neoconservative, free-market challenge to the interventionist arguments of dependence theorists would gather momentum.

The central argument of the neoclassical counterrevolution is that underdevelopment results from poor resource allocation due to incorrect pricing policies and too much state intervention by overly active Third World governments. Rather, the leading writers of the counterrevolution school, including Lord Peter Bauer, Deepak Lal, Ian Little, Harry Johnson, Bela Balassa, Julian Simon, Jagdish Bhagwati, and Anne Krueger, argue that it is this very state intervention in economic activity that slows the pace of economic growth. The neoconservatives argue that by permitting free markets to flourish, privatizing state-owned enterprises, promoting free trade and export expansion, welcoming investors from developed countries, and eliminating the plethora of government regulations and price distortions in factor, product, and financial markets, both economic efficiency and economic growth will be stimulated. Contrary to the claims of the dependence theorists, the neoclassical counterrevolutionaries argue that the Third World is underdeveloped not because of the predatory activities of the First World and the international agencies that it controls but rather because of the heavy hand of the state and the corruption, inefficiency, and lack of economic incentives that permeate the economies of developing nations. What is needed, therefore, is not a reform of the international economic system, a restructuring of dualistic developing economies, an increase in foreign aid, attempts to control population growth, or a more effective central planning system. Rather, it is simply a matter of promoting free markets and laissez-faire economics within the context of permissive governments that allow the "magic of the marketplace" and the "invisible hand" of market prices to guide resource allocation and stimulate economic development. They point both to the success of countries like South Korea, Taiwan, Hong Kong, and Singapore as "free market" examples and to the failures of the public-interventionist economies of Africa and Latin America[43].

The neoclassical challenge to the prevailing development orthodoxy can be divided into three component approaches: the free-market approach, the public-choice approach, and the "market-friendly" approach. **Free-market analysis** argues that markets alone are efficient – product markets provide the best signals for investments in new activities; labor markets respond to these new industries in appropriate ways; producers know best what to produce and how to produce it efficiently; and product and factor prices reflect accurate scarcity values of goods and resources now and in the future. Competition is effective, if not perfect; technology is freely available and costless to

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[43] Ian Little, *Economic Development: Theories, Policies, and International Relations.* (New York: Basic Books, 1982)

absorb; information is also perfect and costless to obtain. Under these circumstances, any government intervention in the economy is by definition distortionary and counterproductive. Free-market development economists have tended to assume that Third World markets are efficient and that whatever imperfections exist are of little consequence.

Public-choice theory, also known as the **new political economy approach,** goes even further to argue that governments can do nothing right. This is because public-choice theory assumes that politicians, bureaucrats, citizens, and states act solely from a self-interested perspective, using their power and the authority of government for their own selfish ends. Citizens use political influence to obtain special benefits (called "rents") from government policies that restrict access to important resources. Politicians use government resources to consolidate and maintain positions to extract bribes from rent-seeking citizens and to operate protected businesses on the side. Finally, states use their power to confiscate private property from individuals. The net result is not only a misallocation of resources but also a general reduction in individual freedoms. The conclusion, therefore, is that minimal government is the best government[44].

The **market-friendly approach** is the most recent variant on the neoclassical counterrevolution. It is associated principally with the writings of the World Bank and its economists, many of whom were more in the free-market and public-choice camps during the 1980s. This approach recognizes that there are many imperfections in Third

[44] Merilee S. Grindle and John W. Thomas, *Public Choices and Public Policy Change: The Political Economy of Reform in Developing Countries.* (Baltimore: Johns Hopkins University Press, 1991)

World product and factor markets and that governments do have a key role to play in facilitating the operation of markets through "nonselective" (market-friendly) interventions – for example, by investing in physical and social infrastructure, health care facilities, and educational institutions and by providing a suitable climate for private enterprise. The market-friendly approach also differs from the free-market and public-choice schools of thought by accepting the notion that market failures are more widespread in developing countries in areas such as investment coordination and environmental outcomes. Moreover, phenomena such as missing and incomplete information, externalities in skill creation and learning, and economies of scale in production are also endemic to LDC markets. In fact it is the recognition of these last three phenomena that gives rise to the newest school of development theory, the new or endogenous growth school of thought.

The New Growth Theory

The poor performance of neoclassical theories in illuminating the sources of long-term economic growth has led to a general dissatisfaction with traditional theory. In fact, according to traditional theory, there is no intrinsic characteristic of economies that causes them to grow over extended periods of time. The literature is instead concerned with the dynamic process through which capital-labor ratios approach long-run equilibrium levels. In the absence of external "shocks" or technological change, all economies will converge to zero growth. Hence rising per capita GNP is considered a temporary phenomenon resulting from a change in technology or a short-term equilibrating process in which an economy approaches its long-run equilibrium.

Unsurprisingly, this body of theory fails to provide a satisfactory explanation for the remarkably consistent pace of historical growth in economies around the globe.

Endogenous Growth

The new growth theory provides a theoretical framework for analyzing endogenous growth, persistent GNP growth that is determined by the system governing the production process rather than by forces outside that system. In contrast to traditional neoclassical theory, these models hold GNP growth to be a natural consequence of long-run equilibrium. The principal motivations of the new growth theory are to explain both growth rate differentials across countries and a greater proportion of the growth observed.

Models of endogenous growth bear some structural resemblance to their neoclassical counterparts, but they differ considerably in their underlying assumptions and the conclusions drawn. The most significant theoretical differences stem from three factors: models of endogenous growth discard the neoclassical assumption of diminishing marginal returns to capital investments, permit increasing returns to scale in aggregate production, and frequently focus on the role of externalities in determining the rate of return on capital investments. By assuming that public and private investments in human capital generate external economies and productivity improvements that offset the natural tendency for diminishing returns, endogenous growth theory seeks to explain the existence of increasing returns to scale and the divergent long-term growth patterns among countries. And whereas technology still plays an important role in these models, it is no longer necessary to explain long-run growth[45].

Conceptual Framework

At the firm level, SMEs have the advantage of flexible specialization. They are able to react and respond swiftly to changing demand and supply conditions and product differentiation. Then, a SME embodied higher incentive system and at the same time reduced principal-agent costs connected to monitoring especially at small or family level enterprises. In theory, considering that SMEs suffer from the lack of scale economies and credit facilities, the gains from small-scale production are amplified when agglomerations of small firms are formed and when credit system is effective. As the number of TVEs increases, spill-over effects arising from the creation of positive externalities are spread throughout rural areas, the resulting multiplier effect having an enhancing effect on local development.

Although clustering itself does not necessarily bring about large benefits to individual firms, it is essential if the sequential externalities required for collective efficiency are to be generated. A cluster can be defined as many SMEs operating in the same type of product in the same geographical area. Specialization, and the division of labor within firms results, over time, in the development of a pool of semi-skilled workers. New enterprises spring up in the form of new suppliers, producers, and traders. The interaction of these economic agents reduces transaction costs thus inducing further

[45] Todaro, pp. 90-92

market entry. The ongoing proliferation of SMEs results in the emergence of a network of enterprises operating in a range of activities including the production of spare parts and specialized equipment and the procurement of second hand equipment. Over time specialized support associations develop in such areas as technical skill development, management and marketing. Indeed, competitive pricing and the speed of adoption of innovation are two of the key ingredients in the success of SMEs.

By interacting with each other and with other enterprises and economic agents, such as suppliers, traders, and larger enterprises these small enterprises are able to enhance their productivity, the quality and design of their products and engage in minor innovation and incremental upgrading of their products and processes. The adaptation of technological products and processes to suit local conditions and markets has augmented their success. In China, if many areas the TVEs development passed through a series of phases, from the initial stage with very simple non-farm income generating activities (connected to agriculture) to an advanced TVE sector, in other areas their development is still at the initial stage.

In SME theory the SMEs development and in particular the cluster long term socio-economic success is based on the collective efficiency that results from interaction between the enterprises at both similar and different production stages. "Collective efficiency is defined as the competitive advantage derived from local external economies and joint actions" (Schmitz, 1995; Becattini, 1990), underlining both the importance of both competition and cooperation between SMEs. Competition between firms may be viewed as a necessary condition for technical upgrading and productive efficiency, whereas collaboration enables firms to pool resources when market conditions dictate it or when it is cost efficient to do so, for example, in the case of sharing expensive pieces of machinery or information. Competitive efficiency and cooperation, via the exploitation of the economies of scale and scope, result in collective efficiency within the agglomeration or cluster. The sustainable TVEs development in local areas depends on their capability to utilize the benefits of clustering, and in particular on spill-over effects arising from the creation of positive externalities. However, this capability is generated from factors which are often external to the small enterprise such as the human and physical infrastructure, which in turn are necessary condition (but not sufficient) for generating positive externalities from SMEs sector, and long term growth perspectives.

As it has been long recognized by development economists social overhead capital SOC is usually defined as comprising those basic services without which primary, secondary, and tertiary productive activities cannot function (Hirschman, 1958, p. 83). SOC or human capital and physical infrastructure, is of strategic importance for economic development both at national and local level. The upgrading of human capital (from the simple worker to the managerial class), technology and production and marketing skills still relies heavily on macro-policy variables such as education, infrastructure and industrial and trade policy. Since on one hand the market alone will not ensure the right provision of these goods and may oversupply goods which have negative externalities such as environmental pollutant firms. Without the support of government, public and private institutions, the upgrading of human and physical capital can only, at best, be partial, and the potential for generating positive externalities (Volpi, 2000), and ultimately growth, limited. Empirical analysis has produced some evidence for collective TVEs. It has been estimated that, between 1986 and 1993, collective TVEs provincial development has been affected by the human capital availability, infrastructure presence and by credit policies implemented at macro level (Biggeri, et al., 1999)[46].

The preceding readings are therefore the basis for the conceptual framework of the study, wherein two relevant economic factors of rural development – TVEs for Mainland China and SMEs for the Philippines will be assessed to extract the success as well as failure factors. TVEs and SMEs are considered "economic equity" programs of the two countries that serve both as a fiscalizer of the adverse effects of rapid urbanization and as poverty alleviation industry, more specifically in the rural areas.

Based on the literatures reviewed, **Figure 3** below is the synthesis of all the relevant theoretical base and how it was utilized in the conceptual framework of the study. As shown in the diagram, the focus of the study is a revisit to the experiences of China in rural development, more specifically on TVEs. The growth of TVEs which was the engine for rural industrialization was viewed from the perspective of the societal factors like how the farmers and the rural folks was able to do it on their own after the decollectivization, the economic opportunities or market conditions brought about by the open door policy, and the role of the government, more specifically, the local government units were focused into in this study.

[46] Mario Biggeri, *The Township and Village Enterprise: the Success of Small and Medium Enterprises in Rural China.* (Department of Economics, University of Florence, 2001), pp. 17-18

On the other hand, the Philippine experience in countryside development through the SMEs were likewise reviewed from the modalities of the government policy framework and support mechanism, the economic opportunities attendant to it, as well as the societal factors like massive poverty in the rural areas, lack of skills and entrepreneurial capabilities and other factors. Despite government support, after 1986, the fall of the 20 years Marcos dictatorship there seems to have a sluggish growth in the SMEs sector.

Both China's TVEs and the Philippine SMEs are viewed as essential to rural or countryside industrialization and economic growth. For both countries, the rural areas constitute approximately 80% of its population. Further the growth of the TVEs for China and SMEs for the Philippines is expected to spur rural development and eventually, the development of the entire country. This study will therefore look at the commonality as well as the diversity of the two countries' experiences and abstract learning to emulate. More so, on the Philippine context as it endeavored to make its SMEs, the engine of growth in this complex time of nation building. **Figure 3** is a comprehensive diagram of the study which showed the conceptual sense as to how the research proceeded in attaining its objectives.

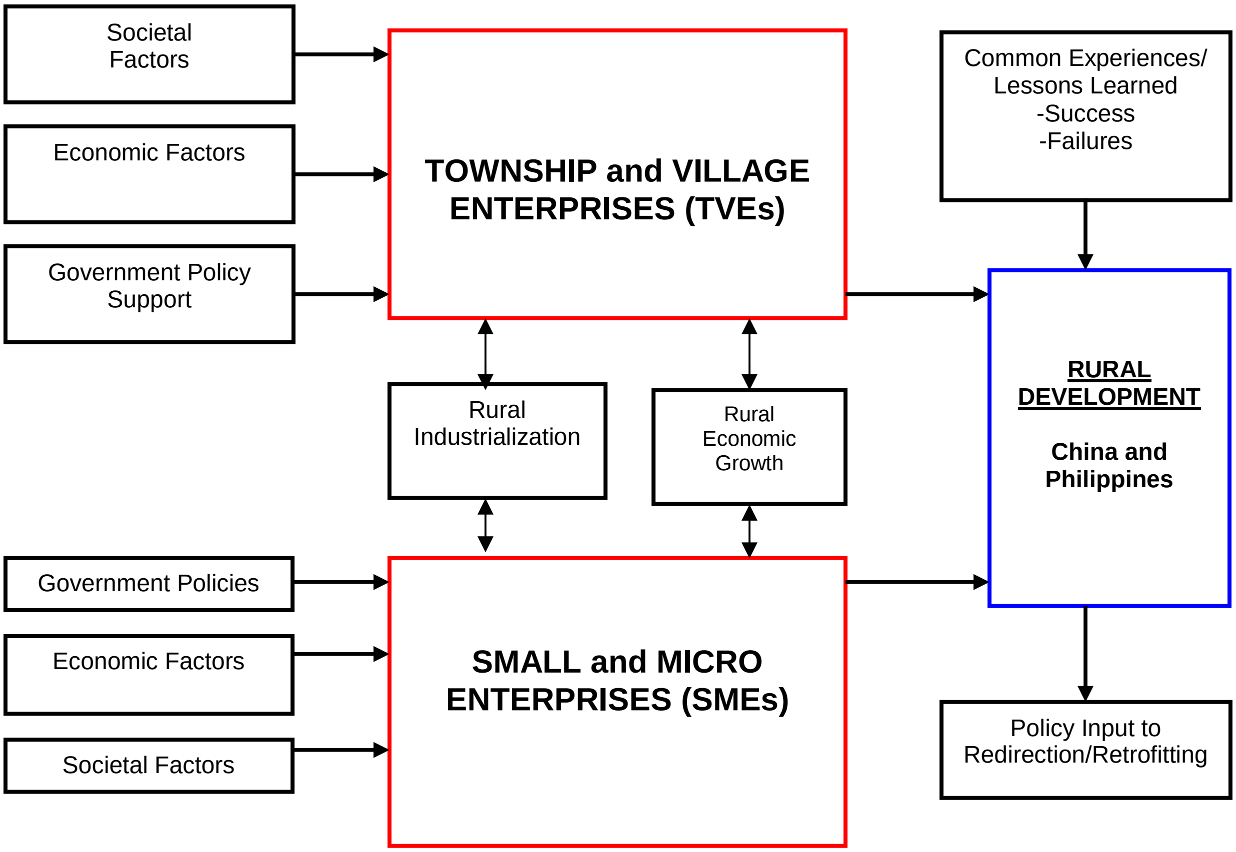

FIGURE 3: Conceptual Framework of the Comparative Assessment of China and the Philippines Rural Development (Todaro, 2000)[47]

[47] Todaro, 2000

Chapter III
Research Method

A. Research Design

The design of the study was essentially an applied operations research type wherein the researcher used both descriptive and analytical approach[48] to rationally compare the pattern of the rural development both in Mainland China and Philippines; identify the factors which contributed to the success of the TVE's and the lessons to be applied in the Philippine context; identify the reasons why SMEs only contribute a little to the Philippines' GDP despite the various programs that the government is providing; and subsequently, come up with a package of recommendations both in policy and programs that will optimize the Philippine development policy on SMEs.

The researcher took off from the empirical data and past studies at the National Sun Yat-sen University library. To focus the policy directions, the researcher interviewed representatives form the Department of Trade and Industry (DTI) and Small and Medium Enterprise Development Council and private individuals who are stakeholders in the Philippine SME dynamics as key informants. The data for the document analyses were built up from both the primary and secondary sources. The two data sources – document analyses and interview of key informants will be analyzed further to validate the results and to reaffirm the credibility of the final outcome of the study.

[48] Iluminada Espino, "Operations Research: An Introduction" in *Manual in Research Writing, Elizabeth Ventura ed.* (Quezon City: National Defense College of the Philippines, 2002), p. 37

B. Research Instrument

Document Analyses

The researcher initially conducted an in depth research on the past and related studies on TVEs and SMEs in China and Philippines, respectively. The data were taken from various sources such as private and business organizations in Manila, published books and articles, and papers and documents provided by the Department of Trade and Industry (DTI) and the Small and Medium Enterprise Development (SMED) Council. These sets of information to include existing policy, programs and practices will ascertain the level of performance in the past up to the present.

The data generated will be configured and disaggregated either as primary or secondary data. The primary data are the results of the key informants' interviews that were conducted; while the secondary data are from pertinent policies, memoranda, and other official documents that were analyzed. The process of identifying the relevant points in the data collection and content analysis are niche into the theoretical factors that were initially identified in Chapter 2 of this thesis.

Interview of Key Informants[49]

The results of the document analyses, both from the primary and secondary data will be used to formulate the interview guide for key informants. The researcher will conduct the interviews herself using a predetermined interview guide questionnaire, except with those who are otherwise restricted or constricted by the interviewees

[49] Nestor N. Pilar, "Philippine Policy Structure" in *Manual in Research Writing Elizabeth Ventura ed.* (Quezon City: National Defense College of the Philippines, 2002), p. 62

schedule or availability, wherein a written response to the interview guide were instead made. The researcher however will make follow through telephone calls to elucidate on certain information. Essentially, the responses from the interviews will be used to validate the existing data for more qualitative insights on the rural development of Mainland China and Philippines.

This instrument enabled the researcher to spontaneously elicit data, as well as gain factual analysis and opinion from acknowledged experts on the subject, thus expanding the perspective of the scope of the study. A copy of the interview guide of key informants and the list are included as attachments in the annexes portion of this study.

Focused Group Discussion

After the consolidation of the results and first level analysis of the documentary review, and the interviews of key informants, the researcher initiated a focused group discussion (FGD) composed of the selected policy makers and major stakeholders in the Philippine SMEs. They were asked to sit together for a focused group discussions on the topic. The high-level assessment, which presupposes thorough downstream processing of data before it was put in the table for discussions[50].

This thesis as presented in **Chapter 1** is on a strong proposition that the more successful TVEs and SMEs are, the better the rural development.

[50] William N. Dunn, *Public Policy Analysis: An Introduction.* (New Jersey: Prentice Hall Inc., 1994), pp. 196-197

C. Data Analysis

The qualitative data were appreciated using the textual analysis method in assessing the expert respondents' consensus opinion, perception, knowledge, responses, and recommendations emerging from their actual experiences and understanding, as well as from documents gathered. The inputs of the interviews were used as comparative bases in presenting the operational experiences of the major stakeholders in the Philippines rural development dynamics[51].

D. Research Analytical Paradigm

While several studies analyzing the impact of Chinese economic growth on foreign trade relations, politics, and regional security exist, no literature consciously integrates key elements of modern Chinese economic reform and analyzes it as a potential model for economic development yet. From embracing an alternative socialist system in the 1950s to implementing autarky in the 1960s until finally opening up to the world economy in 1978, China definitely underwent various reforms and economic policies which shaped the modern Chinese economy we see today – fueling its massive economic growth of 9.5% annually over the past 5 years[52]. With this backdrop, there is indeed a need to analyze one of the key reforms China undertook over the past decades in the light of seeking opportunities and insights that could apply for the Philippine context. The fit of procedures and the research problems are as follows:

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[51] Gloria J. Mercado, *Philippine-Taiwan Relations in a One-China Policy: An Analysis of the Changing Relational Pattern.* (National Sun Yat-sen University: PhD in Mainland China Studies Dissertation, 2007), p. 170

[52] "China to pursue new growth model in years ahead," *The Philippine Star,* September 29, 2006

1. To answer the first research problem of the study, official records of both countries, past studies, researches and policy reviews from various academic institutions and non-government organizations were revisited, perused and analyzed to get a comprehensive review of the past rural development, as well as the current state using the theories of development.
2. To respond to the second research problem of the study, the secondary data that were collected were compressed into key policy and program points and were used as the basis of the interview of key informants. The results of the interview were used to surface the varying views of the stakeholders and the identification of key policy option areas and program strategies of Philippines and Mainland China for rural development.
3. Finally, the third research problem of the study was drawn up from the focused group discussion to come up with a solid conclusion, recommendation and prioritization of options to ensure the model among the theories of development that could be used as possible alternative for Philippine rural development policy.

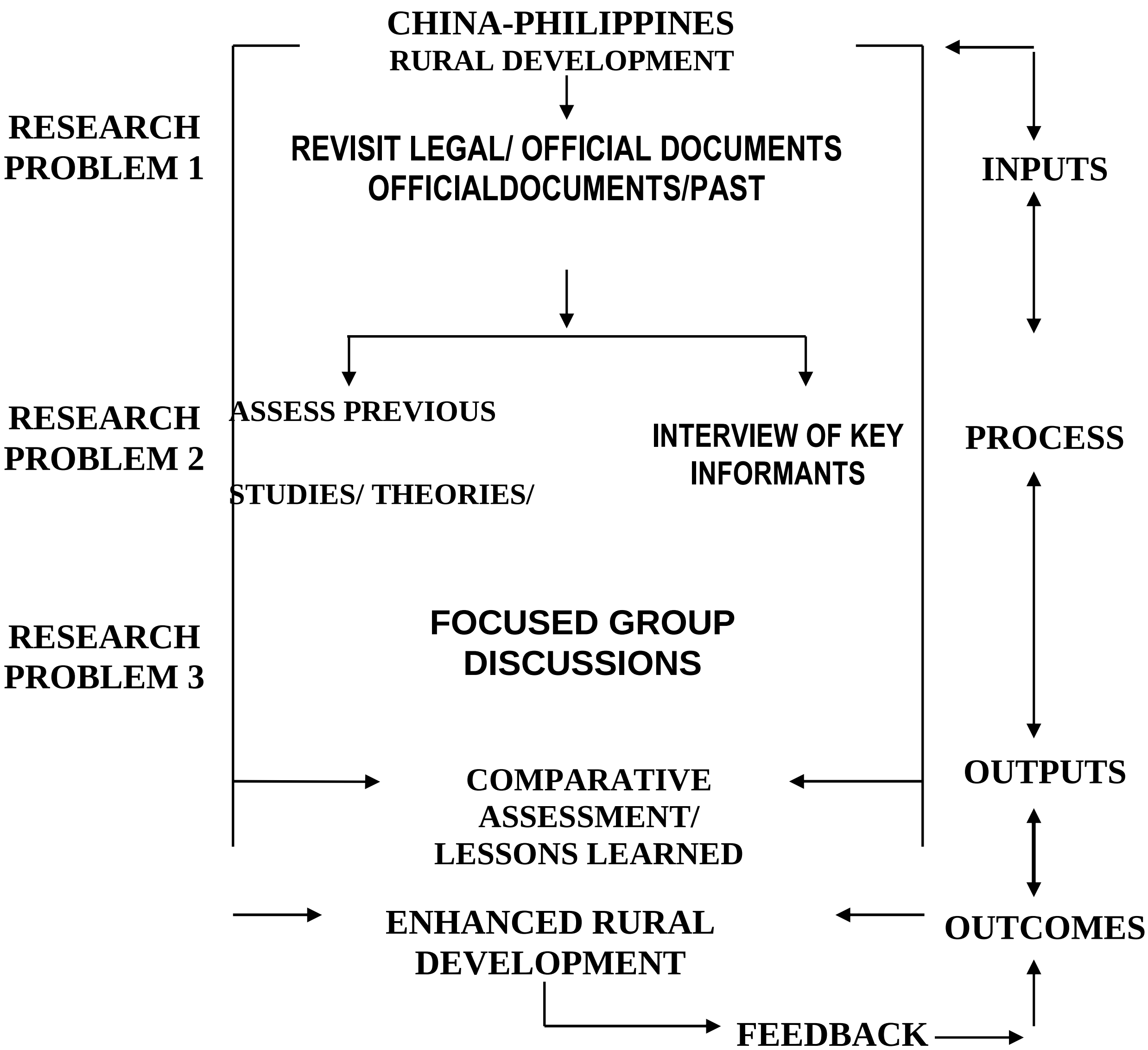

FIGURE 4: RESEARCH FRAMEWORK[53]

[53] This research analytical framework was taken from - Gloria Jumamil -Mercado, "Integrated Development for Mindanao: Its Implications to National Security"(NDCP, 1993) and was published in *National Security Review,* No.2, Vol.XVII, 2nd Quarter, 1996, p 80

Chapter IV
Results and Discussions

Countries across the globe have entered into a new and more challenging economic environment. It is vastly more competitive than in the last few decades – witness just China – more globalized, and more fast changing. It is also seeing the rapid emergence of the knowledge-based economy. East Asian countries are rethinking their economic strategies, to stay relevant and sustain growth and higher living standards in this new environment.

Foreign multi-national companies (MNCs) should remain an important source of investments, technology and jobs for Southeast Asia. It is far too early to write-off the role of MNC-centered, export-oriented manufacturing. Similarly, many large local companies, operating without the shelter of monopoly privileges, will continue to play a key role in spearheading exports and economic growth. But increasingly, countries in Southeast Asia need to pay greater attention to the development of SMEs.

First, a strong SME sector will help cluster strategies to work. MNCs are increasingly focusing on their core competencies, and outsourcing non-core work to other companies. An important consideration in their investment decisions is thus the availability of competent and high quality suppliers of components and other supporting parts and services, who are able to adapt quickly to new demands. A nimble base of local SMEs adds strength to such clusters. They can help to anchor MNCs in the region, and improve national competitiveness.

Second, in a rapidly changing economic environment, it will be much more difficult to spot winners and pick potential champions. There is also greater churn, and shorter company life spans, in the knowledge-based economy. While Southeast Asian economies will continue to specialize in sectors in which they have competitive advantage, it will not be possible to bet on which companies will succeed. The markets will produce the winners, oftentimes surprising winners. Having a broad and diverse pool of companies, will improve the chances of economic success, and provide greater resilience to national economies.

A third reason for promoting SMEs has to do with the importance of domestic enterprise in general, in capturing value in the knowledge based economy. Many of you would be familiar with the "smile curve", which illustrates that most value accrues to upstream activities like R&D or product development, and downstream activities like branding and marketing. Production, in the center of the curve, is increasingly characterized by narrow margins. This is exacerbated in industries where there is an overcrowding of players in the production segment, as improvements in production machinery and processes have lowered entry barriers. On the other hand, ideas and intellectual property are commanding higher rents and a growing portion of the value pie.

While MNCs play a critical part in moving economies up the value creation curve, we need a complementary strategy of growing domestic enterprises that can capture more of the value, by developing their own products and owning the associated intellectual property[54].

As mentioned in the first chapter, to situate the commonalities and differences between the two economic equity programs of China and the Philippines, the socioeconomic profiles of one of the regions of each country, namely, Guangxi Zhuang Autonomous Region and SOCSKSARGEN Region are included in the study. China and Philippines differ in some aspects but the two regions selected for comparison share a number of attributes that may affect their economic performance.

Guangxi Zhuang Autonomous Region is a coastal province located in south China. It occupies a land area of 236,700 sq km., accounting for 2.5% of the nation's total and ranking ninth among all the provinces and autonomous regions. Thickly crossed by rivers, Guangxi is rich in water resources. The water resources amounted to 174.13 billion cubic meters in 2005, with per capita share of this resource being 3,536 cubic meters. The average annual rainfall stood at 1,444.3 mm during the year. Because of the abundant water resources, Guangxi is estimated to have energy potential with a power generating ability coming to 78.8 billion kw/h annually.

Guangxi is known for having various mineral deposits, and it serves as one of the 10 important production bases of nonferrous metals in China. The number of proven mineral resources comes to 96, including 53 of which the deposits ranks 10th or above

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[54] Denis Hew and Loi Wee Nee, *Entrepreneurship and SMEs in Southeast Asia.* (Singapore: Institute of Southeast Asian Studies, 2004), pp. xvii-xviii

among provinces. The region has especially abundant reserves of manganese and tin, which amount for one third of the national total. In addition, Guangxi takes a leading role in having the reserves of vanadium, tungsten, antimony, silver, aluminum, talcum and so forth. What makes the province a favorite place for mineral development and production is that the mineral resources are found relatively concentrated lying beneath the earth.

The southern section of Guangxi is ringed by seacoast. The Beibu Bay, a natural semi-enclosed bay in the northwest of the South China Sea, covers an area of 129,300 square km, with the depth of water averaging 38 meters, the deepest point at 100 meters down. Located in the tropic zone, the Beibu Bay provides a favorable environment for the breeding and growth of various fish species. It is home to over 500 types of fish and shellfish. Among them over 50 are of economic value. They include red snapper, grouper, Spanish mackerel, butterfish and red coat. The total fish resources amount to 750,000 tons. The Beibu Bay Fish Farm covers an area of some 40,000 square sea miles.

The picturesque scenic spots in Guangxi are famous worldwide, symbolized by Guilin, a natural beauty produced by unique karst geography. At present, the province has established several tourist attractions including three state-level natural scenic spots, 11 state-level forest parks, 30 regional natural scenic spots, 15 state-level cultural and historical relics, 221 regional cultural and historical relics and one state-level tourist resort in Beihai City.

SOCSKSARGEN or Region XII, on the other hand, is composed of the provinces of South Cotabato, Sultan Kudarat, Saranggani and General Santos City. While development efforts in the area may have been deterred, the area is rich with natural resources having been blessed with a vast area of fertile agricultural lands and a bountiful line of fishing grounds along Saranggani Bay and other coastal areas. These bodies of water are teeming with tuna and other marine resources. Its huge land mass also boasts of a rich reserve of minerals and gold. It is for these reasons that the area has been identified as a growth area in the Southern portion of the Philippine archipelago, specifically in the realm of the Brunei-Indonesia-Malaysia-Philippines East Asia Growth Area (BIMP-EAGA) concept. It provides a good trade access to major foreign markets like Brunei, Singapore, Malaysia, Indonesia, Australia, Pacific Islands, Japan, Hongkong, Middle East, Continental Europe and the United States.[55]

Similar to Guangxi Region, SOCSKSARGEN is rich with natural resources, has a vast area of fertile agricultural land, bountiful line of fishing grounds, rich reserve of minerals and gold, and has a good trade access to foreign markets. But SOCSKSARGEN is lagging behind its economic performance despite its favorable economic opportunities because of some societal factors. Below is a table showing the summary of the difference in the two regions' economic performance:

[55] A Sectoral Report on SOCSKSARGEN NGOs and the Academe

	Guangxi Region	SOCSKSARGEN
Goss Domestic Product (GDP)	12.7%	3.38%
Agriculture, Forestry and Fishery	7.3%	2.85%
Industry	18.9%	2.05%
Unemployment Rate	4.15%	8.6%

Note: The figures show the rate of increase as compared with the previous year except for the unemployment rate

Table 1 – Economic Performance of Guangxi and SOCSKSARGEN, 2002 (Source: Province View – China and NEDA websites)[56]

The poverty incidence of the region in 2002, as viewed by province, was estimated at 48 percent in Saranggani; 42.9 percent in Cotabato; 54.3 percent in Sultan Kudarat; and 37.3 percent in South Cotabato. Most of the poor families in the region are located in rural areas and have low access to basic social and economic services, employment opportunities, productive assets, and modern technology. They lack support for inputs, such as infrastructure and capital resources and technical capability to start or sustain income generating activities; and use inefficient/ineffective/inappropriate technology, etc.[57]

Another factor which seems to hinder further economic growth and development in the region is the prevalence of armed conflicts between government and the various

[56] An Introduction to China's Provinces, Municipalities, and Autonomous Regions http://www.china.org.cn/english/features/ProvinceView/167754.htm (accessed June 2, 2008) ; Socio-economic Profile Region XII, 2002 http://neda12.neda.gov.ph/R12_SEP_Chapter3&4.pdf (accessed June 2, 2008)

[57] Socio-economic Profile Region XII website

threat groups in the area has led to the destruction of communities and lives. To cite a UNDP report made from January to August 2000, 6,000 homes were destroyed, 218 soldiers were killed, 357 civilians and 456 from the MILF. More civilians, however, died in the evacuation centers because of unabated disease brought about by overcrowding and the lack of resources (food, waste disposal system & medicines). This massive displacement resulted in the increase of potential insurgents with only 10% of the evacuees willing to return to their homes for fear of military occupation and armed conflicts. The social effects of this situation were seen in what Fr. Intengan called the "hardening of psychological boundaries" between Christians and Muslims, mainly in the SOCSKSARGEN area. This promoted the increase of vigilantism i.e. ambushes, coupled with a higher number of student activists being recruited to the Communist Party of the Philippines, National People's Army and the National Democratic Front (CPP-NPA-NDF). According to those who actually work in the field, much of the resources supposedly allocated by the government for development in these areas do not reach the community. This is attributed to the high level of corruption in government agencies necessitating the intervention of a third party who has the confidence of both government and the community. A cursory study of the recent developmental trends in the area showed that participation of non-government organizations (NGOs) and people's organizations (POs) help bridge this gap between the government and the under-represented or left leaning sectors of the community. More open communication lines and better understanding of the needs of both parties are brought to fore.[58]

[58] A Sectoral Report on SOCSKSARGEN NGOs and the Academe

Mainland China

The Growth of TVEs

At the core of China's "economic miracle" is a massive upsurge of rural industrialization. The decade of the 1980s saw the economy take off in vast areas of the Chinese countryside. By 1987 rural industry surpassed agriculture as the dominant source of total rural income. Total output generated by rural enterprises rose almost ninefold from 1980 to 1987, as output of rural enterprises grew more than 26 percent annually from 1978 to 1990. These industries have yielded close to one-quarter of China's total exports. Between 1978 and 1990, the percentage of the rural labor force engaged in village and township enterprises more than doubled, and the 57 million new jobs created from 1978 to 1986 alone equaled the total number of workers hired in all state-owned enterprises between 1952 and 1986.

Such dramatic growth in any political system would be significant. What makes China's experience analytically noteworthy is that growth occurred without significant political change. While the late 1980s and early 1990s saw all communist governments fall from power in the Soviet Union and Eastern Europe, in China the Communist Party was in the midst of instituting economic reforms that have resulted in rapid and sustained growth. In contrast to its Leninist cousins, China refused to take bitter medicine to transform its economic system quickly with what has come to be known as the "big bang" approach. Most notably, it firmly refused to privatize. The private sector today is booming, but this is a product of the 1990s. China in the 1980s maintained state and collective ownership of enterprises and refused to free prices completely or abolish rationing. But it also reintroduced the market and embarked on reforms around the edges of the old system. Central planning was jettisoned only gradually, with some remnants still evident even today.

Most unexpected was the role that local communist officials played in the rural industrialization process. The rapid takeoff of China's rural industry was the result primarily of local government entrepreneurship[59]. To suggest that government intervention leads to successful economic development is nothing new. The many studies of state-led development in Japan and the East Asian newly industrializing countries (NICs) have highlighted the importance of government policies and institutions. What is new is to cast local government in the lead role of the development process. Even more surprising is that these governments are communist. Such systems have generally been assumed to be incapable of reform.

At the beginning of China's reform era, believers in a rapid market transition assumed that local cadres would simply fade from the scene or become "regulators" in an economy of household entrepreneurs, as the distribution of power shifted to producers. Those who focused on how reform would rob communist officials of their power, which was rooted in the Leninist system of central planning and control, argued that local cadres would resent and resist the reforms.

Those who hold to the accepted wisdom about communist systems would probably think China's economy is booming because local officials are merely taking

[59] Jean C. Oi, *Rural China Takes off.* (London, England: University of California Press, Ltd., 1999), pp. 1-2

advantage of opportunities to line their own pockets. This is inconsistent with numerous stories of cadre corruption. While one cannot discount such explanations, the spectacular and sustained growth of China's economy suggests that corruption alone is an insufficient explanation.

Believers in the market might argue that a better place to look for an explanation of China's rural industrial success (and the NICs' success in general) is the rapid growth in inputs into the system, such as the huge amount of surplus labor available in China. Some have suggested that China's rural industry would be just where it is today, even without state intervention, simply as a result of market forces. Inputs and market demand must be taken into account, but neither explanation addresses the timing of the take-off or the dominance of publicly owned township and village enterprises over private ones.

Others who have explicitly rejected what they see as "statist" view of China have gone to the other extreme, attributing the success of China's rural reforms wholly to "society". Some of these observers have attributed the changes to the "unorganized power of the peasants"; others refer to a "societal takeover." While such conclusions are fashionable in the wake of the demise of communism, they fail to answer the crucial question of where peasants obtained capital and resources to fuel China's economic takeoff when personal savings were meager and the market in its infant stage of development.

Given the failures and problems associated with state intervention not only in Leninist systems but more recently in the East Asian NICs, it is not surprising that some would resist the notion of a successful state-led development effort in post-Mao China. But not all state intervention is the same. Market economies also have some form of state intervention. The experiences of Eastern Europe and Russia suggest that the lack of institutional support forced many new private firms to sink before they learned to swim. As Evans has pointed out, “The appropriate question is not ‘how much’ but ‘what kind’ [of state intervention].”

A different explanation might posit that China properly laid the foundation for reform by first ridding the bureaucracy of possible opposition and installing a new breed of farsighted, well-educated officials eager to serve the interests of reform. The reason China’s local officials have responded more positively to reform is that they are not the same communist officials of the past. Such hypothesis, while useful, can take us only so far. China’s reformers did try to eliminate the deadwood in its bureaucracy to improve and revitalize its cadre force, but their success was limited and appears to have been most evident at the higher levels of government. Many of the local officials who are now leading rapid economic development are the same people who presided over a minimally functioning economy during the Maoist period.

Alternatively, one might also argue that because China is a communist system, its local officials have what Murrell and Olson call an “encompassing interest” that is much stronger than that held by officials in democratic regimes to make their economy grow rapidly. In such situations, the person with dictatorial power has "a property right in his society…Just as the owner of a firm has an incentive to make the firm as valuable and productive as possible." Murrell and Olson have dictatorial leaders such as Stalin in mind, but they state that "any leader with complete control over a society has an encompassing" interest in the productivity of that society. To the degree that such arguments are valid, they would apply primarily to the lowest level of the political system (i.e., the villages) where one-person rule is common. Some village leaders do seem sincerely to believe in the superiority of collective ownership. But villages alone are not responsible for the rapid growth of industry. The theory does not explain the behavior of the supporting cast – the bureaucracy at different levels of local government above the village – in the growth process.

One other explanation is that China is still a mobilization system. Rather than taking local initiative, officials are being forced by administrative fiat to pursue growth to meet central-level targets. The success of the one-child policy certainly suggests that mobilization has not disappeared from the political sense. Such an explanation, while plausible, could never sufficiently explain the degree of enthusiasm with which local governments have spearheaded growth. We know that local cadres during the Maoist period only minimally complied with central directives. An explanation needs to be given for why communist officials at the local levels departed dramatically from their previous patterns of behavior.

There is no need to make assumptions about the nature of communist officials – either that they are corrupt or that they are motivated by lofty ideals that lead them to want to enrich their communities. Compliance with central directives in a communist system cannot be assumed. Whether officials comply is an agency problem like that in any bureaucratic hierarchy.

For China the issue was not whether its bureaucracy was capable of generating economic growth but whether it had the incentive to do so[60]. Local officials in a communist system, like officials in any political system, are rational actors who respond to incentives and existing constraints within the limits of their cognitive ability to evaluate alternatives and process information. Their response to reform can be determined only by looking at the concrete circumstances that affect their behavior as agents: incentives, constraints, skills, and resources available to those who are responsible for implementing reform and the effectiveness of monitoring by the central state as the principal. It cannot be predicted on the basis of past performance or ideological orientation. Bureaucratic behavior is a consequence of whether "net incentive effects upon key officials are positive or negative, and to what degree."[61]

To be sure, the reforms would not have succeeded to the extent that they have if China's peasants had not enthusiastically responded to calls to "dare to stand out" and "get rich first." But one cannot extrapolate from the response of the peasants to

[60] Oi, pp. 3-6
[61] Ibid, pp. 7-8

decollectivization and growth of the agricultural sector to explain the rise of rural industry. To understand the latter, one must examine the role of local governments.

A local-level approach to the study of reform and development recognizes the role of the central government and its political elite in the formulation of policy – it is the center that establishes the institutions of rule. The successful economic reform process in China began with the formulation of policies at the national levels of government by a fairly small political elite led by Deng Xiaoping. Without the green light from above, or at least from key elements within the central leadership, it is unlikely reform would have occurred. But although enlightened reform initiatives from the center are a prerequisite for institutional change, well-intentioned policies do not ensure successful implementation, as the failures in the Soviet Union and elsewhere suggest[62].

There is no single answer as to why rural industries able to grow so rapidly. In Barry Naughton's Rural Industrialization, he cited a confluence of five favorable factors which contributed to rural industrial success: favorable fundamentals, ability to tap into monopoly rents, favorable institutional environment, revival of traditional locational patterns, and organizational flexibility.

1. TVEs faced factor-price ratios that reflected China's true factor endowment.

China's basic economic endowment is that it possesses abundant labor, limited land, and scarce capital. One of the greatest irrationalities of the Big Push strategy was that it gave priority to capital-intensive industries. Urban factories faced an incentive

[62] Ibid, p. 8

environment created by planners of the Big Push strategy: Labor was expensive, since total worker compensation was quite generous, while capital was cheap, because it was often allocated without charge or provided at highly subsidized interest rates. TVEs, by contrast, faced factor prices much more in line with China's real factor endowment. Through the 1980s rural-enterprise worker salaries were less than 60% those of state enterprise workers, and total compensation was much less than half that of urban workers. Once TVEs were cut loose from the Maoist Five Small Industries straitjacket, they adapted quickly to the underlying availability of production factors. TVEs rarely had access to subsidized capital. The bulk of TVE capital was provided at near-market interest rates or came from internally generated funds with a high opportunity cost. **Figure 5** shows that TVEs (in this case village firms) were specialized in those sectors with low capital-labor ratios, where the competitive advantage of their low wages was biggest. Facing realistic factor-price relationships, TVEs faced the right incentives to find lines of profitable business that were most appropriate in the Chinese economy and that, over the long run, gave them an advantageous competitive position. Economic fundamentals were on the side of the TVEs[63].

2. TVEs were able to share in the monopoly rents created for state firms; rural industries were extremely profitable.

Another reason that could explain the pattern of rapid growth of the TVEs is that early TVEs were in a position to benefit from the protected market created for the state-run factories.

[63] Naughton, pp. 275-276

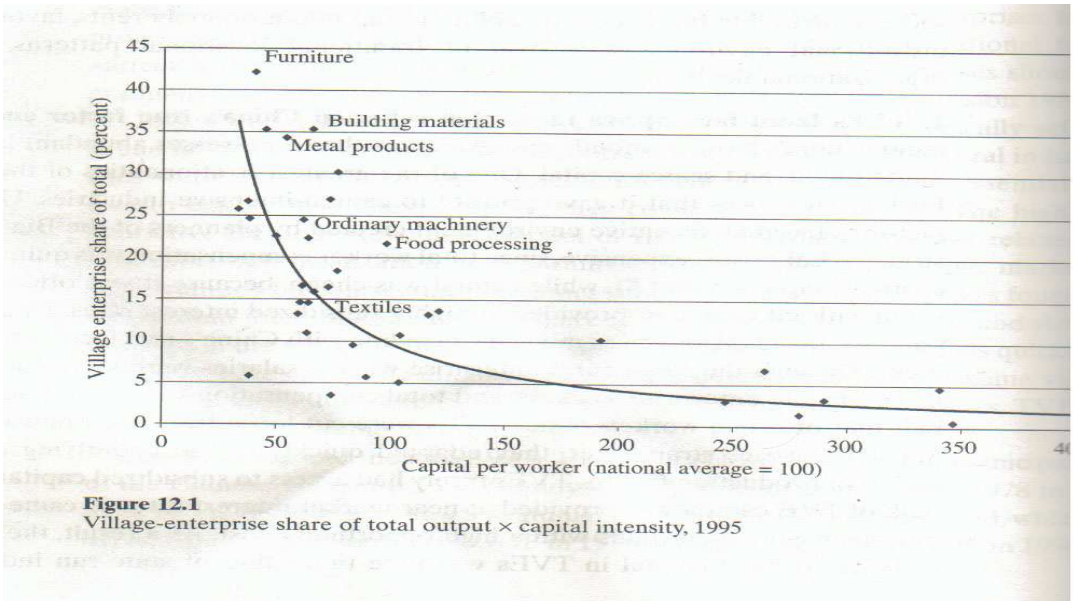

Figure 5 – Village Enterprise share of total output x capital intensity, 1995 (Source: The Chinese Economy Transitions and Growth, 2007)[64]

By easing the state monopoly over industry, the Chinese government allowed TVEs to enter this previously protected market and share in a portion of the monopoly profits. First-mover advantages were large – big enough to repay early entrants with windfall profits. In this situation continued entry only gradually created competition. State firms scarcely noticed the competition at first, because they were protected by a cushion of high profits. As long as they could gain access to low-price raw materials, they were indifferent to a few TVEs producing similar products. But gradually, as entry continued, competition among TVEs and between TVEs and state firms began to compete away monopoly profits and erode profit margins.

The existence of empty niches also contributed to this pattern of high initial profits followed by steadily declining profitability. Empty niches existed for two reasons.

[64] Naughton, p. 276

Certain commodities – particularly miscellaneous consumer goods – had simply not been provided by the inefficient command economy, and TVEs jumped in to meet needs until then largely unmet. For example, this response explains much of the early success of the Wenzhou region, where small-scale rural firms specialized in such items as buttons, ribbons, and elastic bands in a variety of colors and specifications; producing these items for a market of one billion led to explosive growth. In addition, a whole series of new markets were created by the sudden growth of rural incomes and the relaxation of rural economic policy. For example, rural housing construction took off, and new rural industries developed to supply building materials to this new market. In both situations, early entrants could expect windfall gains, and the presence of potential windfalls naturally induced extremely rapid entry. Gradually entrants created competition that eroded the exceptional profits available early on[65].

3. The institutional framework surrounding TVEs was favorable to development.

Local governments became enthusiastic partisans of TVE development. At first, local governments were also the de facto owners of many TVEs. Although TVEs were nominally "collectives", it was almost never the case that the "collective" referred to was limited to the workers and managers in the TVE itself. Rather, the TVEs were owned by the rural collectivity as a whole, which in practice was usually represented by the local village or township government. Later, from the 1980s onward, the ownership of TVEs diversified away from local government ownership, but local officials still had powerful incentives to develop TVEs. TVEs provided employment and money to local economies,

[65] Ibid, p. 277

and they were often the only realistic source of both. Local government support contributed to the formation of a favorable environment for TVEs in at least three ways:

(a.) Formal taxes were low on rural industry, so money stayed local. Rural enterprises enjoyed very low tax rates, and particularly low tax rates on profit. By contrast, state-run industrial firms benefited from government price policy, but they also paid the price in a very high tax rate – sometimes 100% - on profits. Rural enterprises enjoyed the benefits of price policy without the corresponding high tax burden. This unbalanced treatment seems peculiar unless we recall that during the early phase of reform China's leaders conceived of rural enterprises primarily as a device to increase the resources available to agriculture. The average rate of profit tax collected from TVEs remained very low: in 1978 this was only 8%, and by 1980 it had declined to 6%. It then gradually climbed to around 20% by 1986, where it has remained since. While formal tax rates are low, profits paid to local government "owners" were often substantial. In the early 1980s firms at the township and village levels paid about 30% of their total profits to local governments to "support agriculture" and social services, as well as additional funds for "management fees". Local governments were especially happy to have these funds because they were classified as "extrabudgetary" and therefore did not have to be shared with higher-level governments (as was the case with budgetary revenues). In turn, most local governments recycled this money back into new and expanded TVEs, since they perceived a high return for their funds in these investments.

(b.) Local governments acted as guarantors for TVEs, so bank capital was available. The sponsorship of China's TVEs by local governments greatly enhanced the access to capital of these new businesses. By contrast, the experience of other transforming socialist economies has been that new start-up businesses proliferate, but that such businesses have difficulty getting access to capital and as a result remain small, undercapitalized, and dependent on informal capital markets. Local government officials acted as intermediaries and guarantors, reassuring local agents of the banking system that their loans would ultimately be repaid. Indeed, in some cases, local government officials actively pressured local branches of the banking system to provide funds to their firms. Despite local government actions supporting and serving as guarantors to TVEs those TVEs had mostly, but not completely, hard budget constraints. Government sponsorship served to spread the risks incurred by these new start-ups, essentially by having the entire local community absorb the cost of failure. Soft budget constraints – implying no responsibility for failed or misguided investments – would have been disastrous in China's rural economy. But it is unlikely that perfectly hard budget constraints for start-up businesses would have been optimal, either – a certain amount of "insurance" provided to startups by local governments almost certainly enhanced welfare. By underwriting a portion of the risk of entry, local governments enabled start-up firms to enter production with a larger size, to start with some mechanization, and to exploit the economies of scale that came from moving away from the smallest form of household production.

(c.) Existing credit institutions were easily adapted to support TVEs. With local governments facilitating the flow of capital to rural enterprises, those firms were able to take advantage of China's relatively abundant household saving. Chinese traditional credit clubs and other forms of informal credit markets were put to good use. As Chinese rural household saving skyrocketed during the 1980s, the supply of funds to the local rural credit cooperatives (RCCs) expanded drastically. The RCCs, nominally independent, locally controlled financial co-ops, had in fact been used before reform primarily to transfer the modest rural savings to urban uses. With the onset of reform the RCCs had much more money, and they also were allowed to lend a much greater proportion of it locally. The result was that the RCCs emerged as the main source of financial resources for the TVEs. Thus RCC loans to TVEs increased because RCC deposits increased, because they were allowed to lend more local deposits in the local areas, and because they increased the share of their local loans that went to TVEs. Local money stayed local, and so those areas that enjoyed successful TVE development early, when profits were high, were able to "snowball" rapidly into significant production scale[66].

4. Revival of traditional economic ties meant that proximity to urban areas fostered rural industry growth.

The growth of China's rural industries has occurred primarily in regions that might more properly be termed suburban, or at least, in areas that are part of the immediate hinterland of cities. Rural industries are also highly concentrated regionally,

[66] Naughton, pp. 277-279

with coastal areas containing a disproportionate share of rural industries. In 1988, three coastal provinces – Jiangsu, Zhejiang, and Shandong – accounted for 17% of China's rural population, but 43% of total rural industry, and exactly half of all township and village-level industrial output. Such geographical concentration is entirely natural. These areas were better located to begin with, having more of the locational assets required for city growth; in turn, because cities had developed, they could also provide transport networks, communications, markets, technology, and other conditions that boost productivity throughout the cities' hinterlands, as well as in the cities themselves. Therefore, it is not surprising to find that "rural" enterprises are more likely to thrive in regions where they can benefit from the spillover effects of the urban economies.

Rather, what is striking is that these organic linkages between cities and countryside had been so thoroughly cut off during the command economy. As a result, even a modest recovery of urban-rural linkages, beginning in the 1970s, resulted in rapid growth of suburban industry, given the low base from which it was starting. The growth of rural enterprises in periurban areas was facilitated by direct cooperation between urban state-run firms and rural factories, primarily in the form of subcontracting. In the three province-level municipalities of Beijing, Shanghai, and Tianjin an estimated 60%-80% of rural industrial output was produced by firms subcontracting with large urban factories. The proportions were only slightly lower in nearby provinces: linkages with Shanghai firms "played a decisive role in the development of TVEs in southern Jiangshu". Such arrangements were facilitated by family relations; rural people who had migrated to the cities and urban youth sent from Shanghai to the countryside during the Cultural

Revolution helped rural firms get started. Later on, rural firms purchased talent from the cities, especially by paying high salaries to technicians and retired urban workers. Urban SOEs were willing to cooperate: as state firms gained a greater interest in profit they sought to reduce costs and subcontracting operations to rural enterprises became increasingly attractive (particularly in the garment industry). Such relationships also allowed urban firms to escape from some of the tight constraints of the state-run industrial system. By entering into relations with rural firms, state firms could gain access to the resources they needed (particularly land and labor) in an environment in which accounting standards and supervision were somewhat less strict than in the state sector. TVEs gave state-firm managers a certain amount of flexibility to escape the rigid controls of the state sector.

5. Organizational diversity accommodated growth.

Finally, a simple but important aspect of TVE development was that there was no single organizational model that TVEs had to follow. In fact, TVEs were sometimes government run, but often and increasingly they were private. Over time a group of true worker cooperatives emerged, as well as employee-owned corporations. TVEs were sometimes bureaucratic, but often highly adaptable. In this respect they were very different from SOEs, which were compelled to adopt a uniform organizational form. As a result of this flexibility, TVEs were able to adapt to a broad range of opportunities. A variety of different regional "models" of rural industrialization grew up, each plausibly suited to a different set of economic conditions.

A steadily increasing share of TVEs was privately run. During the course of the 1980s new small-scale firms were started by entrepreneurs, and many firms started under collective auspices became de facto private firms. Sometimes these firms continued to register enterprises as collectives, because this practice was safe politically. Local officials formed alliances with entrepreneurs – sometimes for mutual benefit, sometimes more predatory in nature – as rural industrialization spread. There was a complex mixture of costs and benefits from this interaction between public and private. After the late 1990s the stigma on private business dissipated, and TVEs became predominantly private. In all periods, because TVEs were not constrained to a single organizational form, localities were able to adapt as the advantages and disadvantages of various options became evident[67].

Diverse Regional Models of TVE Development

Responding to different regional conditions, TVEs developed in different parts of China. Each pattern or model provides information about the forces shaping Chinese rural development.

The Southern Jiangsu (Sunan) Model

Southern Jiangsu, or "Sunan" for short, is the relatively prosperous and developed area of the Yangtze Delta around Shanghai, an area that has been among the most economically advanced regions of China for centuries. Here the dominant model of TVE development was one in which the township and village governments and collective

[67] Naughton, pp. 279-281

ownership maintained the leading role. This model developed in areas of southern Jiangsu where TVEs flourished early, beginning in the early 1970s. TVEs began developing while the collective system was still firmly in place in the countryside. As TVEs expanded, the collectives maintained control, even when the collective system declined elsewhere. Because of the longer history and greater capital resources in these areas, TVEs tend to be much bigger, more capital-intensive, and more technologically sophisticated than TVEs in other parts of the country.

Elements of the southern Jiangsu model appeared wherever TVEs grew up early, close to cities. "Suburban" areas with locational advantages and entrepreneurial village leaderships developed TVEs early under the collectives, and village leaders subsequently tended to maintain control for a decade or more. Subcontracting and technical assistance ties with urban SOEs were often important. Conversely, once this model developed, the collective structure remained sturdy because the TVEs generated profits that could support local government. These villages tended to develop a kind of "corporate village" in which village leaders ran an entire business complex. At the same time, such corporate villages maintained government social services and sometimes even provided welfare benefits to village residents. These "corporate villages" were sometimes suspicious of outsiders, since they wished to protect the lucrative jobs, benefits, and opportunities of locals. These localities were the most likely to directly subsidize agriculture with TVE profits, so that local farmers could join in the general prosperity.

The Wenzhou Model

The town of Wenzhou is only about 300 kilometers south of southern Jiangsu, on the coast of the neighboring province of Zhejiang, but it has a very different geographical setting, and it evolved a very different model of TVE development. Rugged and fairly remote – despite its coastal location – Wenzhou was quite removed from the urban influences so important in southern Jiangsu. From the beginning of its explosive growth, Wenzhou's economy has been based on private ownership. Firms in Wenzhou were initially tiny, based on individual households, and specializing in modest articles of daily use. Wenzhou businesses first flourished selling buttons, ribbons, plastic ID card holders, and other ordinary items. Wenzhou peddlers then took these items throughout China, filling a market need for diverse, inexpensive items that state firms had filled either very poorly or not at all.

Wenzhou is a very special place, with a long cultural tradition of entrepreneurship and spectacular economic growth in the past 25 years. But elements of the Wenzhou model appeared in any place where farmers were willing to seize entrepreneurial opportunities but did not have advantageous suburban locations. In these areas the collectives never successfully developed TVEs into moneymaking propositions. As a result, the collectives were weak and often disappeared early in the reform process. Individually owned firms sprang up in response to opportunity, and they naturally tended toward labor-intensive activities oriented toward the market. Indeed, perhaps the most striking feature of this model in Wenzhou itself is the intense reliance on the market to coordinate all aspects of production. The Wenzhou button industry, for example, developed around individual households that specialized in individual stages of the button-production process. Households that milled plastic blocks into button rounds sold these rounds, in a specialized marketplace, to households that drilled holes in the rounds and finished the buttons. In turn, a different group of households that specialized in mounting buttons on button cards would purchase the finished buttons at another specialized marketplace. Button cards would be sold to peddlers at still another market. In this fashion, production chains linked by markets sprang into existence. This pattern appeared repeatedly for different commodities. Many private businesses – even private banks – developed in this Wenzhou model.

The Pearl River Delta Model

In the Pearl River Delta – the region between Hong Kong and Guangzhou that is the core of the Southeast Coast macroregion – TVEs developed rapidly under the stimulus of foreign investment. This model was pioneered by Hong Kong businessmen who had grown up in the delta and returned to their home villages to start cooperative businesses. In these transactions, village leaders acted as managers of village assets, leasing land, signing contracts for export processing, and coordinating labor and social issues. As in the southern Jiangsu model, nearby urban (Hong Kong) businesses and local governments both played an important role. Production grew rapidly in large factories. In the Pearl River Delta, however, factories were usually export-oriented manufacturers of light, labor-intensive products.

The big difference between the Pearl River Delta model and the southern Jiangsu model is that the Pearl River Delta model is so much more open both domestically and internationally. Of course, the prosperity of the model depends on openness to foreign trade and investment. The TVEs themselves were often partly foreign owned (Hong Kong owned). But these villages also tend to be quite open to workers from other parts of China as well. While the southern Jiangsu corporate villages tended to protect from outsiders the good jobs their own locals held, the Pearl River Delta needed workers for their large labor-intensive export factories. The Pearl River Delta became by far the largest destination in China for migrant workers. Villagers in the Pearl River Delta earned locational "rents" by being open to both foreign and domestic agents[68].

The Transformation of TVEs in the New Century

The entire TVE sector underwent further dramatic transformation after the mid-1990s. First, TVEs faced a more challenging external environment, and their overall growth rate slowed significantly. Second, faced with this external pressure, TVEs restructured and transformed into predominantly privately owned businesses. Finally, new forms of economic cooperation and competition grew up as TVEs adapted to the new challenges and opportunities.

During the mid-1990s fundamental changes occurred in the economic environment in China. These changes were associated with a shift in economic reform strategy. National government policy shifted toward building markets and regulatory institutions. At the same time, macroeconomic policy shifted to a more restrained stance,

[68] Naughton, pp. 282-284

designed to control inflation, and an emphasis was put on greater financial independence and accountability for banks. All these changes translated into a tougher competitive environment for TVEs. At first many TVEs had trouble responding, and the very rapid growth of TVEs came to an abrupt end[69]. Figure 3.2 shows employment of all TVEs. In the 1980s and early 1990s, TVEs created millions of new jobs for rural residents. As the data presented in **Figure 6** show, the pace of TVE job creation dropped off abruptly after 1996. TVE employment only significantly surpassed the 1996 peak of 135 million workers in 2004, when the total inched up to 139 million. This slowdown primarily reflects a change in macroeconomic conditions. Urban firms also had to cope with a more competitive market economy, and they responded either by closing up shop or by developing more effective market responses. Urban firms were forced to expand into market niches previously left empty and to develop nationwide marketing strategies, putting them into head-to-head competition with TVEs. The market for consumer goods shifted from one in which shortages were predictably parts of daily life to one in which virtually all goods were regularly available.

[69] Ibid, p. 285

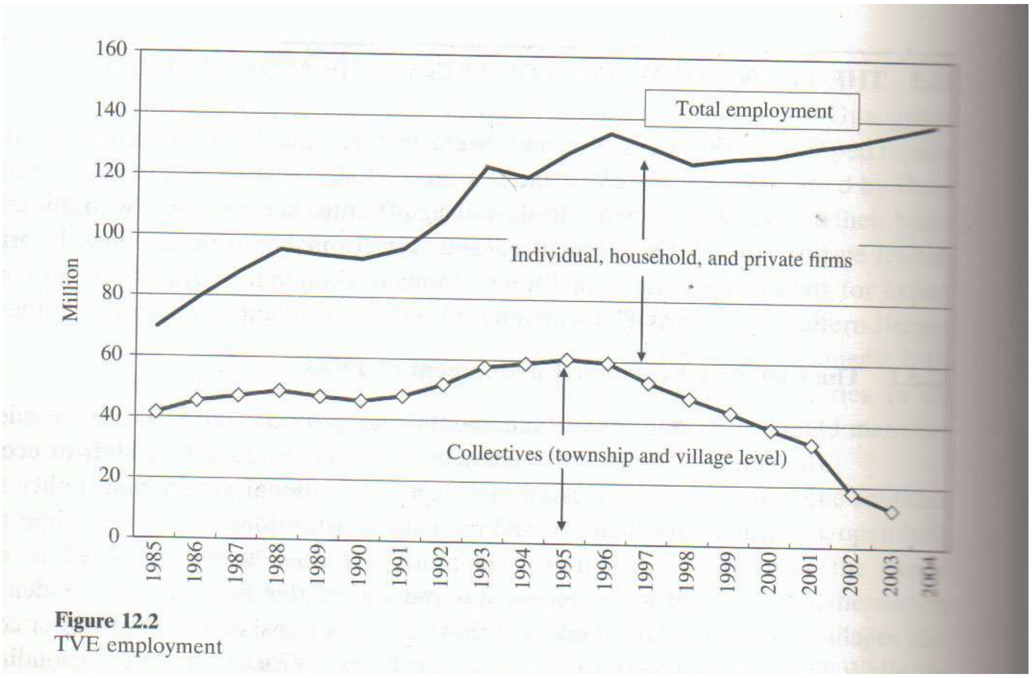

Figure 6 – TVE Employment (Source: The Chinese Economy Transitions and Growth, 2007)[70]

With increased market integration and competition, TVEs lost their protected position. There were few, if any, empty niches for TVEs to exploit. Moreover, as incomes, especially urban incomes, rose, consumers increasingly demanded higher quality products than traditional TVEs, with their outdated technologies, could provide. TVEs seemed to lose their special role in the economy. It is not coincidental that overall structural change in the economy also slowed down after 1996. With TVEs less able to absorb workers from agriculture, the agricultural share of total employment stagnated for several years. It was not until well into the decade of the 2000s that structural transformation resumed and TVEs resumed absorbing labor.

[70] Ibid, p. 286

In fact, TVEs continued to grow after 1996, albeit at rates closer to overall GDP growth than in the past. TVE value added as a share of GDP increased from 26% in 1996 to 30% in 1999, and then leveled off through 2004. TVEs, under pressure, appear to have raised labor efficiency, producing more output without adding workers and thereby, of course, becoming less labor-intensive. TVEs in general have become less special, but they have led the rest of the economy in becoming more private[71].

<u>TVE Restructuring: The Great Privatization</u>

Collectively owned TVEs at one time dominated the entire TVE sector. After the 1980s, even though private firms grew rapidly, collective TVE employment continued to increase through 1995, at which time collectives still accounted for almost half of TVE employment. But the situation has changed dramatically in the 10 years since, and collective firms today represent less than 10% of total TVE employment. Ownership figures are not precise. Certainly in the past there were private firms that operated under the polite fiction of being collectives. As national policy has accepted private business, these firms have come out of the closet and acknowledged their true identity. On the other hand, figures for collectively owned TVEs include only firms 100% owned by the township or village and thus excludes firms where the local government may continue to have a significant, or even controlling, stake. Still, more precise numbers would not change the basic picture: TVEs began as an offshoot of the rural collectives, but today they are predominantly private businesses[72].

[71] Ibid, p.286
[72] Ibid, pp. 286-287

Emergence of New Forms of Rural Industry in the Twenty-First Century

The transformation of the TVE sector in the new century has not been limited to a conversion to private ownership. TVEs have adapted to a more open, competitive environment, and the ties that link TVEs to local governments have become weaker. TVE markets are increasingly interregional. Moreover, many of the seedbed areas of TVE growth have themselves been transformed, from rural regions in proximity to cities, to something like cities themselves, or at least to a densely populated "urbanized countryside" that is knit together with new highway networks.

One of the most striking developments has been the emergence of highly competitive "industrial clusters" in rural and suburban areas. The key feature of a cluster is the large number of firms that contribute to a single specialized product. Typical industrial clusters include scores – perhaps hundreds – of small firms that compete with each other but cooperate to form a link in a relatively complete industrial chain. Clusters may have three or four large firms cooperating with scores of small firms. Typical, though, is an exceptionally fine division of labor among different stages of the production process. Small, competitive firms specialize in extremely narrow activities. Relationships between firms can be quite complex, but they are generally mediated by efficient markets, in which a balance is struck between flexibility and long-term cooperation. Clusters generally produce light consumer goods. Examples include sock industry cluster in Zhuji municipality which is estimated to produce 35% of world sock production, Liushi Township, which produces low-voltage electrical equipment. Both of these are in Zhejiang Province, which can be considered the center of industrial cluster development, with at least 519 recognized industrial clusters.

Industrial clusters are phenomena that have emerged in many places around the world. The shoe industry in Brazil and the garment and luxury-goods industries in Italy display many of the same characteristics. Yet we can also identify in this phenomenon in China some typically Chinese elements that we observed already in the traditional Chinese economy, as well as in the early Wenzhou model of TVE development. The clustering of numerous small producers, linked to a larger marketplace by a series of smaller intermediate-good markets, is a form of industrial organization with a long tradition in China. Today, there are a number of industries where a resurgence of this type of organization has been accompanied by a surge in the competitiveness of Chinese goods on the world marketplace. Indeed, TVE export orientation has remained strong, and it has even increased in recent years. In this sense and many others, the "TVE sector" is again in a period of rapid change and restructuring[73].

Philippines

Poverty in the Philippines – An Overview

In agriculture and industry in the postwar era, the number of medium-sized landholders, salaried workers in public and private sectors, professionals, and the like, has grown. This heterogeneous stratum is often termed "middle class" according to level of income, occupation type and status, pattern of consumption, and so on. Pinches (1996:109) argues that sections of the middle class first came to national political

[73] Ibid, pp. 292-293

prominence over their endorsement of government protectionism in the 1950s and 1960s. Since then, they have been a strong presence in the people power revolutions against two presidents. But, most significantly, since the fall of Marcos, middle-class disaffection with the traditional elite and its sources of power has increased, contributing to domestic pressures for economic and institutional reforms[74].

The middle stratum of Philippine society has proven to be a vital source of medium-scale investment in export manufacturing, particularly garments, footwear and the like. Through international and local subcontracting arrangements, it has been possible for relatively small investors to set up in manufacturing, sometimes as a means to supplement or substitute professional incomes[75]. In the last decade, this phenomenon has extended into consumer and business services and construction[76]. Pinches' research shows that a significant proportion of these "new capitalists" are "women, former salaried professionals, and middle-class Filipinos" who have returned "from periods of residence in North America or Europe", especially when the economy picked up in the early to mid 1990s. Alternatively, they are individuals "with a background in small business" who, over time, have been able to expand those businesses[77]. With the easing of restrictions on foreign investment in areas such as banking, insurance, telecommunications, and parts of retailing in the 1990s, new employment openings have developed in management and other professional areas. In all this, Pinches (1999:279)

[74] Michael Pinches "The Philippines: new rich: capitalist transformations amidst economic gloom" in Richard Robison and David S.G. Goodman (eds) *The New Rich in Asia: Mobile Phones, McDonalds and middle-class revolution.* (London and New York: Routledge, 1996), p. 105
[75] Pinches, p. 121
[76] Michael Pinches "Entrepreneurship, consumption, ethnicity and national identity in the making of the Philippines' new rich" in Michael Pinches (ed.) *Culture and Privilege in Capitalist Asia.* (London and New York: Routledge, 1999), p. 275
[77] Ibid, p. 278

observes that it is worth noting "the absence of a clear divide between the salaried new middle class and the new capitalist entrepreneurs" due to the extensive overlapping among families and individuals. However, throughout, the business interests of the middle classes are generally less dependent on political patronage than those of the traditional elite and are certainly not on any grand scale[78].

It is estimated that SMEs and micro-enterprises account for 99.6 per cent of the country's total number of enterprises. Of the 99.6 per cent, 91.6 per cent are micro-enterprises with the rest accounted for by SMEs (**Figure 7).** SMEs are also estimated to account for 70 per cent of total employment (**Figure 8**) and around 32 per cent of gross domestic product (**Figure 9**).

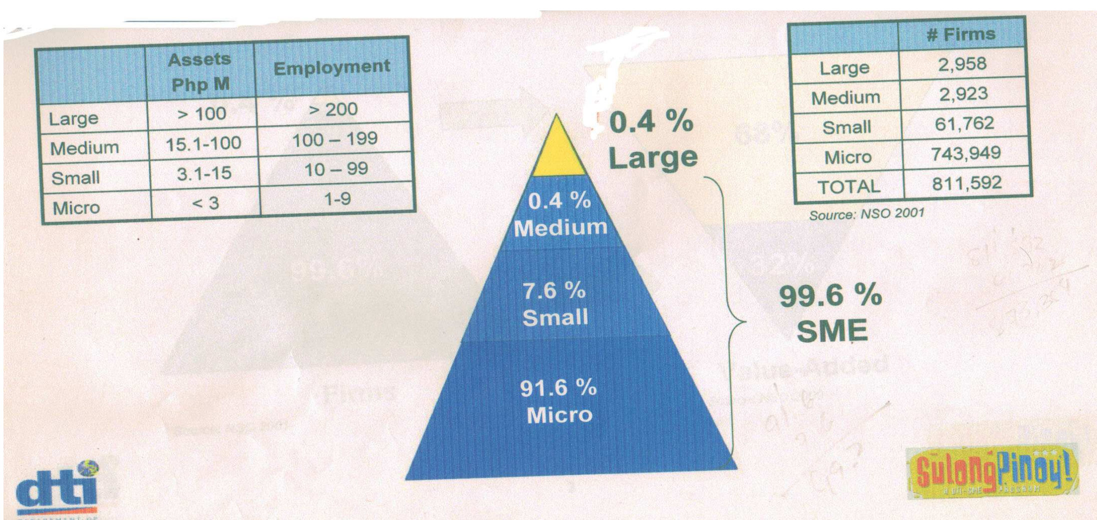

Figure 7 – Profiles of SMEs in the Philippines (Source: DTI)[79]

[78] Garry Rodan, Kevin Hewison, and Richard Robison *The Political Economy of Southeast Asia 3rd ed.* (New York: Oxford University Press, 2006), p. 54
[79] "Current situation of SMEs and the SME Development Plan" http://www.dti.gov.ph/contentment/66/69/files/SME.ppt (accessed November 24, 2007)

The Philippine Government, for some years now, has been giving special attention to the development of entrepreneurs and small and medium enterprises or SMEs.

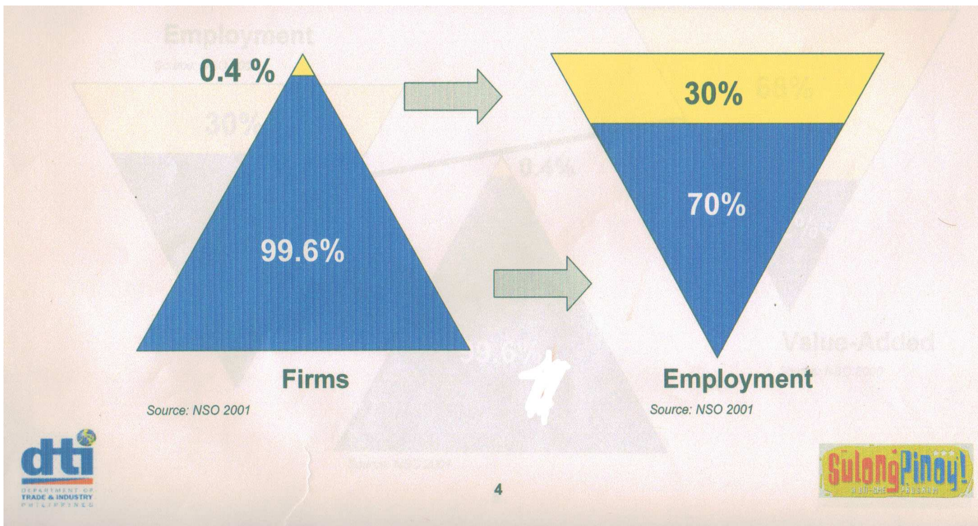

Figure 8 – SME Employment in the Philippines (Source: DTI)[80]

There is a large body of literature providing justifications for supporting the development of SMEs and entrepreneurs/micro-enterprises. These justifications include, among others, the contribution of SMEs to employment generation and economic growth. Vibrant SMEs could also serve as a foundation for a strong and competitive industrial sector as was the case of the newly industrialized countries of East Asia that have relied on dynamic SMEs to boost their competitiveness. SMEs have a vital role in the development of rural areas as these disperse economic activities to the countryside, and

[80] Ibid

hence contribute to a more equitable distribution of income. These use indigenous resources, support export growth and encourage entrepreneurial development.

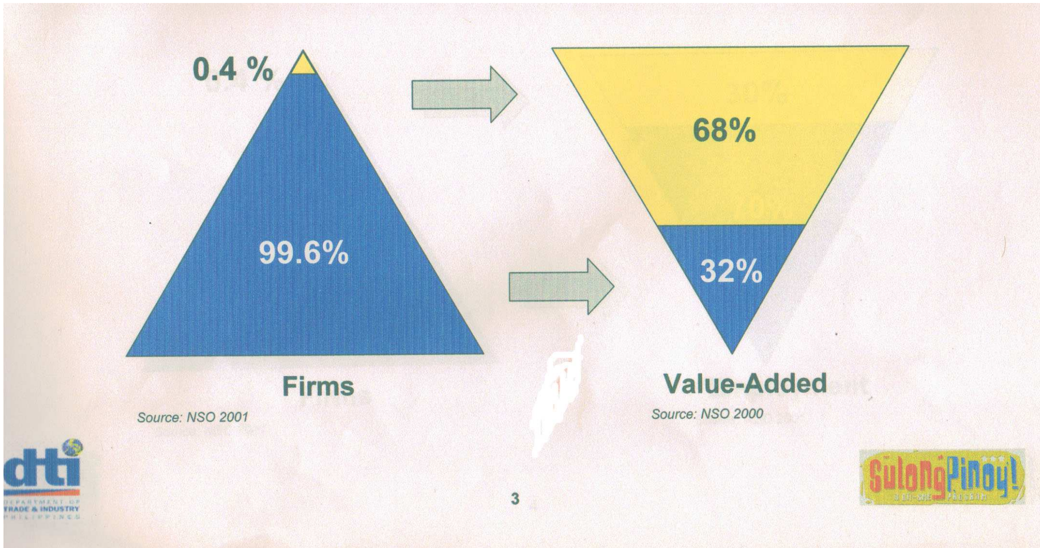

Figure 9 – SME Contribution to Total GDP in the Philippines (Source: DTI)[81]

Being more flexible, SMEs are being increasingly viewed as sources of innovation and agents of change. Thus, these are contributing to the development of new technology, the improvement of skills of workers as well as the development of new products and processes[82]. The development of SMEs also contributes to the expansion and diversification of markets as well as to increasing the savings rate and investment base[83].

But the past quarter century has seen the Philippines lagging behind most of the major East Asian countries (**Figure 10**) in practically all aspects of economic and social

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[81] Ibid
[82] Ponciano S. Intal, *Why, What and Financing SME Development.* Mimeographed. (Manila: De La Salle University, 2002)
[83] Mendoza and Llanto, p. 151

development[84], despite the fact that the Philippine government recognizes the important role of SMEs in the economy. The country's average economic growth was only slightly higher than its population growth, which was, and continues to be, comparatively high by most Asian standards. Further blunting the impact on poverty of whatever growth that occurred has been its persistently high level of economic inequality[85].

	Malaysia	Thailand	RP	South Korea	Japan	China	Indonesia
SME Establishments	94.4%	98%	99.6%	99%	99%	99.7%	99.995 %
Employment	40.4%	55.8%	69.1%	69%	88%	74%	99.04%.
Value Added	26%	n.a.	32.0%	46%	56%	60%	63.11%

Source: JICA & various sources

6

Figure 10 – RP SME Productivity as Compared to other Asian Countries (Source: DTI)[86]

Political Economy Perspectives

Neoclassical economists attribute the generally poor economic record of the Philippines to a policy and institutional mix that "misallocates" resources to areas of inappropriate and inefficient economic activity[87]. They argue that, for most of the postwar era, protectionist trade and macroeconomic policies promoted inefficient

[84] John Weiss, *Poverty Targeting in Asia.* (Massachusetts, USA: Edward Elgar Publishing, Inc., 2005), p. 220
[85] Ibid, p. 221
[86] DTI website
[87] Geoffrey Shepherd and Florian Alburo, "The Philippines", in Demetris Papageorgiou, Michael Michaely and Armeane Choski (eds) *Liberalizing Foreign Trade Vol 2.* (Oxford: Basil Blackwell, 1991), p. 133

manufacturing for the domestic market, while also encouraging a form of business behaviour known as "rent-seeking". Rents are defined in the economic literature in a number of ways; however, in this context, they are understood as additional returns from government interventions in the market. Rent-seeking is, therefore, the effort applied to competition in the political arena over sources of rent – particularly quotas, tariffs, and public monopolies[88]. The neoclassical criticism is that "by substituting political for economic criteria in many allocative decisions", rent-seeking is antithetical to the operation of market forces and, hence, to the development of an internationally competitive economy[89]. However, in recent years neoclassical economists have paid more heed to the institutional foundations of market success. Accordingly, current economic commentary on the Philippines is more than ever concerned with the governance-related issues of corruption, poor regulatory performance, and policy incoherence. But these good governance approaches look to preferred technical institutional changes without properly addressing the power relations that these involve.

The role of the rent-seeking in the political economy of the Philippines has also been highlighted by state-centred historical institutionalists. However, these writers are less concerned with its distorting effects on the market than they are with its consequences for state capacity. Drawing on the example of developmental states in East Asia, they maintain that the Philippines' poor economic record is the direct result of a

[88] James M. Buchanan "Rent Seeking and Profit Seeking", in James M. Buchanan, Robert D. Tollison and Gordon Tullock (eds) *Towards a Theory of the Rent-Seeking Society* (Texas: Texas A&M University Press, 1980), p. 3

[89] Shepherd and Alburo, pp. 155-156

“weak” or “patrimonial” state[90]. Particularly indebted to Weber (1968) on bureaucracy and rational action, they argue that the Philippine polity is unable to steer the course of national economic development because it is constantly subject to the particularistic demands of a wealthy elite or oligarchy. This high level of political patronage (or cronyism) compares with the strong “institutional autonomy” of developmental states, “which is derived from the differentiation of state institutions from the private interests of individuals within society”[91].

An almost regular pattern of boom and bust has characterized the Philippine economy during the period from 1960 to 2002. Bust and stagnation soon followed each episode of boom, fueled largely by massive foreign borrowing and capital-intensive import-substituting industrialization. The period also saw heavy government regulation of the market economy, as well as political instability, natural disasters, and major shocks in global trade and finance. However, notwithstanding the interruption in the late-1990s owing to the combined impact of the Asian economic crisis and the El Nino phenomenon, the growth episodes since the second half of the 1980s appear to have a fundamentally different character from previous ones. Economic growth, albeit meager compared with that in any of the country’s South East Asian neighbors, has taken place in an environment of political stability, economic deregulation and institutional reform. While domestic political squabbling and policy coordination problems persisted, it could not be

[90] Peter Evans, *Embedded Autonomy: States and Industrial Transformation.* (Princeton: Princeton University Press, 1994)
[91] Linda Weiss and John M. Hobson, ”State power and economic strength revisited: what’s so special about the Asian crisis?” in Richard Robison et al. (eds) *Politics and Markets in the Wake of the Asian Crisis* (London: Routledge, 2000), p. 53

denied that the Philippines at the beginning of the new millennium was closer to a market economy than it had ever been in the past[92].

SME Agenda: An Integrated Approach

The SMED Council members meet at least once a month to discuss issues, evaluate activities, and map out short-term plans for SME development. Being the chair of the SMED Council, DTI has reaffirmed its commitment to SME development by creating an SME Development Group composed of DTI-attached agencies and bureaus mandated to support SMEs. The SME Development Group is tasked to implement, coordinate, and monitor the various efforts that go into SME development, namely: Finance, Training/Human Resource Development, Marketing, Product Development and Technology Intervention, and Advocacy for an Enabling Environment (**Figure 11).**

It is an increasing recognition of the important role played by SMEs in the economy that has led the government to support various policies and programmes to promote their growth.

[92] Ibid, p. 221

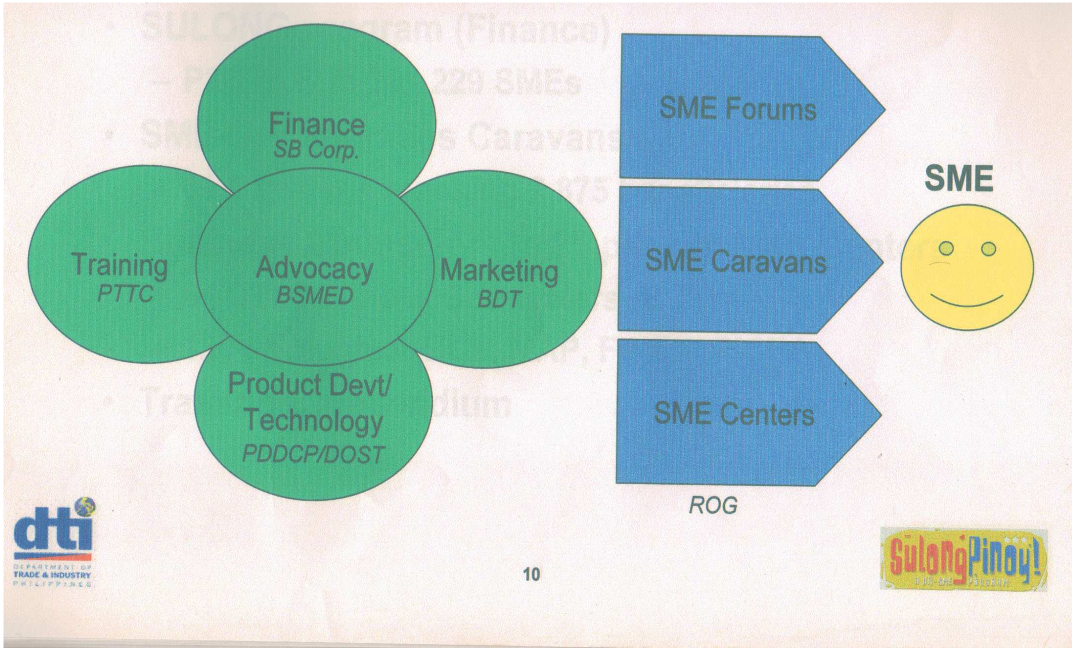

Figure 11 – SME Agenda: An Integrated Approach (Source: DTI)[93]

Finance – SULONG is the brand name for the financing initiative under the Plan. This unified lending programme is the result of a collaboration among government financial institutions (GFIs). Under the SULONG Programme, GFIs apply simplified and standardized lending procedures and guidelines (e.g., standardized application procedures, requirements, fees, and interest rates) to provide SMEs with greater access to capital.

Marketing – Various DTI agencies have been tasked to design marketing programmes to increase the exposure of SME products in domestic and foreign markets, and to improve the distribution of SME products between local manufacturing and trade sectors as well as within each sector. In line with the goal of expanding markets for SMEs, the DTI mounts local and international trade fairs. It showcases the best producers of the entire

[93] DTI website

country and their finest products in one venue for the convenience of institutional buyers, exporters, and export traders.

Training and Human Resource Development – The training and entrepreneurship development programmes of the National SME Agenda seek to provide existing and potential entrepreneurs with the necessary skills and knowledge to become competitive players in the local or global market. It also seeks to create a pool of SME trainers, advisors, and counselors who can effectively assist SMEs nationwide.

Product Development and technology Intervention – There are two main product development objectives under the plan. The first is to create and sustain competitive advantage through product and package design and development, as well as through technology intervention. The second is to create an awareness and understanding of product development, its processes, and the ways in which a company can use it to advantage.

Advocacy for an Enabling Business Environment – Two major laws govern the promotion of SMEs – Republic Act (RA) 6977, or the Magna Carta for Small Enterprises, as amended by RA 8289, and RA 9178, better known as the Barangay Micro Business Enterprises (BMBEs) Act of 2002.

The various initiatives, programmes and incentives that the government has implemented under the National SME Agenda have resulted in varying degrees of success. Thousands of entrepreneurs have already benefited from the programmes and succeeded in their undertakings. But the search for more initiatives that would extend new forms of support to SMEs in an increasingly competitive globalized environment continues[94].

[94] Based on the interviews conducted by the researcher to the key informants.

CHAPTER V

Summary, Conclusions, and Recommendation

This concluding part of the thesis presents the highlights of the findings of the various research instruments used to come up with credible answers to the research problems as spelled out in Chapter 1. The results of the assessment were used as the basis of the conclusion and recommendations, more specifically the policy and program mix model that the researcher endeavored to build[95].

Summary and Highlights of Findings

A. Summary

Chapter 1 of this thesis provided a brief background about how rural economy played an important role in transforming the Chinese economy from a command economy to a market economy. TVEs had a special distinction during this period because of their unusual ownership and corporate governance setup. Originating under the rural communes, most TVEs were collectively owned: TVEs thus presented the unusual spectacle of publicly owned enterprises growing rapidly and providing the competitive challenge that dissolved the monopoly previously held by public (state-run) enterprises. A diverse set of TVE models adapted to a range of different conditions and ended up fundamentally changing nearly every part of the Chinese economy.

Rural industry in China underwent transformation starting from its traditional economy, then the Great Leap Forward era, followed by the Cultural Revolution era, up

[95] Mercado, p. 432

to the golden age of the TVEs. Rural household businesses were very important in China's traditional economy, leading it to be called "bottom heavy" because of the preponderance of small, household-based, flexible, and market-oriented production units. Rural households spun and wove cotton, raised silkworms, and reeled silk thread; they cured tobacco, milled grain, and made noodles. Households made mud bricks and hewed timber, carted goods to market, and ran shops and businesses. But this organic link between growing and processing agricultural product in the countryside was broken under the command economy. When the state established its monopoly control over agricultural goods during the 1950s, rural processing businesses were inevitably cut off from their supplies. Another attempt to develop rural industry occurred during the Cultural Revolution era. After 1970, during the Maoist "new leap forward", the government encouraged a new wave of state-sponsored rural industrialization under the rubric of "commune and brigade enterprises." Policy during the 1970s stressed the "Five Small Industries", rural industries that included iron and steel, cement, chemical fertilizer, hydroelectric power, and farm implements[96]. During 1979 the central government shifted its policy toward rural enterprises in important respects. The general liberalization of that time included a relaxation of the state monopoly on purchase of agricultural products, allowing more to remain on rural markets and thus available to rural enterprises for processing. The new policy was "Whenever it is economically rational for agricultural products to be processed in rural areas, rural enterprises should gradually take over the processing work".

In sum, this chapter has illustrated the dramatic growth that has taken place in recent years in China's rural enterprises. It has also demonstrated the burgeoning

[96] See detailed discussions in Chapter 1 of this thesis

significance of those enterprises (a) as an outlet for the savings being accumulated in the countryside following the first stages of the reforms; (b) for the subsequent relocation of labor out of traditional agriculture; (c) for the finances of local government, especially revenues received through taxes and profits; and (d) for the rate of urbanization.

On the Philippines' side, this chapter presented the efforts of the Philippine government to develop its SMEs which started in the year 1960 with the creation of different institutions to extend assistance to small and medium-sized enterprises and the enactment of laws such as the Magna Carta for Social Justice and Economic Democracy, and among others, to signify the government's commitment to the development of small-scale industries. But these institutions and laws were either abolished or dismissed due to the limited forms of assistance, weak implementation, or change of administration.

The theoretical and conceptual framework is exhaustively discussed in **Chapter 2** of this study within the purview of the various levels of analysis[97]. Assessing the dynamics of the rural development of Mainland China and the Philippines is conventionally viewed from the Theories of Development lens. How these assessments would configure depends on these theoretical lenses[98]. These lenses differ not only on who they identify as key actors, but in their views about the individual, the state, the society, the international system and structures at the three levels of analysis. The various books, thesis, articles, documents, and other related studies were exhaustively reviewed to come up with the theoretical/conceptual framework, as well as the research

[97] Mercado, p. 435
[98] B. Guy Peters, *Comparative Politics: Theory and Methods.* (New York: New York University Press, 1998), p. 6

paradigm[99]. The research methods as discussed in **Chapter 3** laid down the design of the study which is essentially an operations research type wherein the researcher used a combination of descriptive, qualitative but non-experimental, and analytical approach[100] to rationally analyze the factors which contributed to the growth of TVEs in Mainland China and the current state of TVEs vis-à-vis China's overall economic growth; the reasons for the slow growth of SMEs in the Philippines despite the government support; and the abstractions of lessons learned for both countries and the policy recommendation that can be drawn as inputs to Philippine rural development policy.

To focus the policy directions and the subsequent recommendations, the researcher interviewed representatives from the Department of Trade and Industry (DTI) and from the Small and Medium Enterprise Development (SMED) Council and private individuals who are stakeholders in the Philippine SME dynamics as key informants. The data for the document analyses were built up from both the primary and secondary sources. The three data sources – document analyses, interview of key informants, and focused group, were placed in a triangulation mode of analysis to validate the results. This three-level mode of analysis reaffirmed the credibility of the final outcome of the study[101].

The last two chapters of this thesis are detailed and expansive discussions on the three research problem areas. **Chapter 4** discussed the details of the commonalities and differences between China and Philippines focusing on the regions of Guangxi and

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[99] Mercado, p. 436
[100] Ventura, p. 37
[101] Albano, p. 31

SOCSKSARGEN, respectively. In this chapter, the factors which contributed to the growth of TVEs in China, the overview of poverty in the Philippines, and the importance of SMEs in the development of the rural economy were also discussed. The chapter also included figures and tables to show the current situation of SMEs in the Philippines, share of total output of TVEs in China, and the dramatic change in the ownership composition of TVEs.

The last chapter - **Chapter 5** is the conclusion and recommendations. After rationally back tracking the pattern of rural development between Mainland China and the Philippines and after identifying the factors which contribute to the success and failures of TVEs and SMEs as expansively discussed in Chapter 4, the final chapter is built from the conclusion that the more successful TVEs and SMEs are, the better the rural development; and that government programmes and policies are not enough to sustain the growth of SMEs.

B. Highlights of Findings

This thesis is essentially a comparative study of the rural development between Mainland China and the Philippines focusing on township and village enterprises (TVEs) and small and medium enterprises (SMEs) to examine the factors which contributes to the acceleration in the growth of rural enterprises, then analyze these key factors China undertook over the past decades in the light of seeking opportunities and insights that could apply for the Philippine context. Hence, for **Research Question 1 –** "What are the factors which contributed to the growth of TVEs in Mainland China and what is the current state of TVEs vis-à-vis China's overall economic growth?"; and **Research Question 2 –** "Given the fact that the Philippine government recognizes the important role of the SMEs in the economy by giving opportunities for these enterprises through various support programs, what are the reasons for the slow growth of SMEs in the Philippines?", the highlights of the findings are as follows:

1. We have entered a new and more challenging economic environment. It is vastly more competitive than in the last few decades – witness just China – more globalized, and more fast changing. It is also seeing the rapid emergence of the knowledge-based economy. East Asian countries are rethinking their economic strategies, to stay relevant and sustain growth and higher living standards in this new environment.
2. Foreign multi-national companies (MNCs) should remain an important source of investments, technology and jobs for Southeast Asia. But increasingly, countries in Southeast Asia need to pay greater attention to the development of SMEs for the following reasons:
   (a) A strong SME sector will help cluster strategies to work. A nimble base of local SMEs adds strength to such clusters. They can help to anchor MNCs in the region, and improve national competitiveness.
   (b) In a rapidly changing economic environment, having a broad and diverse pool of companies will improve the chances of economic success, and provide greater resilience to national economies.
   (c) A third reason for promoting SMEs has to do with the importance of domestic enterprise in general, in capturing value in the knowledge based

economy. While MNCs play a critical part in moving economies up the value creation curve, we need a complementary strategy of growing domestic enterprises that can capture more of the value, by developing their own products and owning the associated intellectual property.

3. The decade of the 1980s saw the economy take off in vast areas of the Chinese countryside. By 1987 rural industry surpassed agriculture as the dominant source of total rural income. Total output generated by rural enterprises rose almost ninefold from 1980 to 1987, as output of rural enterprises grew more than 26 percent annually from 1978 to 1990. These industries have yielded close to one-quarter of China's total exports. Between 1978 and 1990, the percentage of the rural labor force engaged in village and township enterprises more than doubled, and the 57 million new jobs created from 1978 to 1986 alone equaled the total number of workers hired in all state-owned enterprises between 1952 and 1986.
4. What makes China's experience analytically noteworthy is that growth occurred without significant political change. Most notably, it firmly refused to privatize. China in the 1980s maintained state and collective ownership of enterprises and refused to free prices completely or abolish rationing. But it also reintroduced the market and embarked on reforms around the edges of the old system. Central planning was jettisoned only gradually, with some remnants still evident even today.
5. Most unexpected was the role that local communist officials played in the rural industrialization process. The rapid takeoff of China's rural industry was the result primarily of local government entrepreneurship. What is new is to cast

local government in the lead role of the development process. Even more surprising is that these governments are communist. Such systems have generally been assumed to be incapable of reform.

6. Believers in the market might argue that a better place to look for an explanation of China's rural industrial success (and the NICs' success in general) is the rapid growth in inputs into the system, such as the huge amount of surplus labor available in China.
7. Some of these observers have attributed the changes to the "unorganized power of the peasants"; others refer to a "societal takeover." While such conclusions are fashionable in the wake of the demise of communism, they fail to answer the crucial question of where peasants obtained capital and resources to fuel China's economic takeoff when personal savings were meager and the market in its infant stage of development.
8. Given the failures and problems associated with state intervention not only in Leninist systems but more recently in the East Asian NICs, it is not surprising that some would resist the notion of a successful state-led development effort in post-Mao China. But not all state intervention is the same. Market economies also have some form of state intervention. The experiences of Eastern Europe and Russia suggest that the lack of institutional support forced many new private firms to sink before they learned to swim.
9. A different explanation might posit that China properly laid the foundation for reform by first ridding the bureaucracy of possible opposition and installing a new breed of farsighted, well-educated officials eager to serve the interests of reform.

The reason China's local officials have responded more positively to reform is that they are not the same communist officials of the past.

10. Alternatively, one might also argue that because China is a communist system, its local officials have what Murrell and Olson call an "encompassing interest" that is much stronger than that held by officials in democratic regimes to make their economy grow rapidly. In such situations, the person with dictatorial power has "a property right in his society…Just as the owner of a firm has an incentive to make the firm as valuable and productive as possible."
11. Local officials in a communist system, like officials in any political system, are rational actors who respond to incentives and existing constraints within the limits of their cognitive ability to evaluate alternatives and process information. Their response to reform can be determined only by looking at the concrete circumstances that affect their behavior as agents: incentives, constraints, skills, and resources available to those who are responsible for implementing reform and the effectiveness of monitoring by the central state as the principal.
12. The successful economic reform process in China began with the formulation of policies at the national levels of government by a fairly small political elite led by Deng Xiaoping. Without the green light from above, or at least from key elements within the central leadership, it is unlikely reform would have occurred.
13. There is no single answer as to why rural industries able to grow so rapidly. In Barry Naughton's Rural Industrialization, he cited a confluence of five favorable factors which contributed to rural industrial success: favorable fundamentals,

ability to tap into monopoly rents, favorable institutional environment, revival of traditional locational patterns, and organizational flexibility.

14. Responding to different regional conditions, TVEs developed in different parts of China. Each pattern or model provides information about the forces shaping Chinese rural development. The Southern Jiangshu Model was one in which the township and village governments and collective ownership maintained the leading role. In the Wenzhou Model, firms were initially tiny, based on individual households, and specializing in modest articles of daily use. And finally, there was the Pearl River Delta Model. In the Pearl River Delta – the region between Hong Kong and Guangzhou that is the core of the Southeast Coast macroregion – TVEs developed rapidly under the stimulus of foreign investment.

15. The entire TVE sector underwent further dramatic transformation after the mid-1990s. First, TVEs faced a more challenging external environment, and their overall growth rate slowed significantly. Second, faced with this external pressure, TVEs restructured and transformed into predominantly privately owned businesses. Finally, new forms of economic cooperation and competition grew up as TVEs adapted to the new challenges and opportunities.

16. The transformation of the TVE sector in the new century has not been limited to a conversion to private ownership. TVEs have adapted to a more open, competitive environment, and the ties that link TVEs to local governments have become weaker. One of the most striking developments has been the emergence of highly competitive "industrial clusters" in rural and suburban areas. The key feature of a cluster is the large number of firms that contribute to a single specialized product.

Typical industrial clusters include scores – perhaps hundreds – of small firms that compete with each other but cooperate to form a link in a relatively complete industrial chain.

17. The middle stratum of Philippine society has proven to be a vital source of medium-scale investment in export manufacturing, particularly garments, footwear and the like. Through international and local subcontracting arrangements, it has been possible for relatively small investors to set up in manufacturing, sometimes as a means to supplement or substitute professional incomes.

18. It is estimated that SMEs and micro-enterprises account for 99.6 per cent of the country's total number of enterprises. Of the 99.6 per cent, 91.6 per cent are micro-enterprises with the rest accounted for by SMEs (Figure 3.3). SMEs are also estimated to account for 70 per cent of total employment (Figure 3.4) and around 32 per cent of gross domestic product (Figure 3.5).

19. The Philippine Government, for some years now, has been giving special attention to the development of entrepreneurs and small and medium enterprises or SMEs. Vibrant SMEs could also serve as a foundation for a strong and competitive industrial sector as was the case of the newly industrialized countries of East Asia that have relied on dynamic SMEs to boost their competitiveness. SMEs have a vital role in the development of rural areas as these disperse economic activities to the countryside, and hence contribute to a more equitable distribution of income. These use indigenous resources, support export growth and encourage entrepreneurial development.

20. But the past quarter century has seen the Philippines lagging behind most of the major East Asian countries (Figure 3.6) in practically all aspects of economic and social development, despite the fact that the Philippine government recognizes the important role of SMEs in the economy.

21. Neoclassical economists attribute the generally poor economic record of the Philippines to a policy and institutional mix that "misallocates" resources to areas of inappropriate and inefficient economic activity. They argue that, for most of the postwar era, protectionist trade and macroeconomic policies promoted inefficient manufacturing for the domestic market, while also encouraging a form of business behaviour known as "rent-seeking". The neoclassical criticism is that "by substituting political for economic criteria in many allocative decisions", rent-seeking is antithetical to the operation of market forces and, hence, to the development of an internationally competitive economy.

22. The role of the rent-seeking in the political economy of the Philippines has also been highlighted by state-centred historical institutionalists. However, these writers are less concerned with its distorting effects on the market than they are with its consequences for state capacity. Drawing on the example of developmental states in East Asia, they maintain that the Philippines' poor economic record is the direct result of a "weak" or "patrimonial" state. Particularly indebted to Weber (1968) on bureaucracy and rational action, they argue that the Philippine polity is unable to steer the course of national economic development because it is constantly subject to the particularistic demands of a wealthy elite or oligarchy. This high level of political patronage (or cronyism)

compares with the strong “institutional autonomy” of developmental states, “which is derived from the differentiation of state institutions from the private interests of individuals within society”.

23. It is an increasing recognition of the important role played by SMEs in the economy that has led the government to support various policies and programmes to promote their growth. The SMED Council members meet at least once a month to discuss issues, evaluate activities, and map out short-term plans for SME development. Being the chair of the SMED Council, DTI has reaffirmed its commitment to SME development by creating an SME Development Group composed of DTI-attached agencies and bureaus mandated to support SMEs. The SME Development Group is tasked to implement, coordinate, and monitor the various efforts that go into SME development, namely: Finance, Training/Human Resource Development, Marketing, Product Development and Technology Intervention, and Advocacy for an Enabling Environment (Figure 3.7).

24. The various initiatives, programmes and incentives that the government has implemented under the National SME Agenda have resulted in varying degrees of success. Thousands of entrepreneurs have already benefited from the programmes and succeeded in their undertakings. But the search for more initiatives that would extend new forms of support to SMEs in an increasingly competitive globalized environment continues.

Conclusion and Recommendations

A. Conclusion

The paper has driven home the point as exhaustively shown in the discussions of the preceding Chapter that - "the more successful China's TVEs and Philippines' SMEs are, the better for the rural development of the country". China has proven this after the 1978 reforms when in 1990 TVEs dramatically rose 13 times more from its 1979 level - that is from 1.4 million to 18.5million. This included other factors of growth like output value, employment and taxes remitted. While the features of the 1978 reforms - open door policy, decollectivization and decentralization, among others, were macro policies which fertiled the soil for rural industrialization in China, its TVEs growth was in a SULNAM (Spontaneous, Unorganized, Leaderless, Non-ideological, Apolitical Movement) phenomenon. Thus, it was more of societal and economic factors with the local government providing the policy support. Undeniably, it is one of the strong pillars of China's economic growth and social-equity considering that 800 million of the 1.3 billion population of China is in the countryside.

On the Philippine side, given its history of sluggish economic growth and high poverty incidence especially in the rural areas, SMEs, especially the micro or cottage enterprises was heavily initiated and supported by the government as a poverty alleviation industry or even as a strategic deterrent to insurgency. Since it is until now a purposive national policy, efforts are heavily undertaken by all levels of government like the local government units, Department of Trade and Industry, National Anti-poverty Commission, Department of Agriculture, Department of Agrarian Reform, Department of

Social Welfare, Department of Education, and of late the Non-government organizations through micro-finance. The slow growth in SMEs is a confluence of societal – lack of entrepreneurial spirit, cultural rigidities, etc. and economic – access to the market, financing and technology. But definitely, government has laid down a comprehensive policy backbone for SMEs to grow and the entire loop of development and governance are in a common belief that its growth with be the engine of countryside development that will carry it through a national mark.

B. Recommendations

All the preceding cursory carefully crafted: a) the factors which contributed to the growth of TVEs in Mainland China and the current state of TVEs vis a vis China's overall economic growth; and, b) the expanse of the support of the Philippine government since it is in a firm resolve that the SMEs is still a weak sector and with the right nurturing from a convergence of support – government and civil society, it is the most potent engine of countryside growth and national development. Against this backdrop of answers to the research problems, the abstractions of lessons learned for both countries and policy recommendation are as follows:

1. China's overall development strategy, with its emphasis in narrowing urban-rural differences and bringing down the barriers between the urban and rural China, has been singularly successful. Rural industry has improved rural living standards; urban technology has moved into the countryside; and, villagers and urbanites are meeting in the marketplace, with the former supplying vastly increased qualities of foods and the latter supplying cash for rural entrepreneurs

and farmers.[53] For the Chinese farmers, the TVEs was the miracle which emerge in their midst - the panacea to the growing rural-urban disparity, and the collateral development issues attached to it. *It is therefore for the best interest of the Philippine government to look deeply into the China experience more specifically on the incentive and regulations to arrest its massive rural-urban migration. The Philippine industrial dispersal program to the countryside can be enhanced to make it more attractive to locator industries.*

2. In the Philippine context, dualism is a very sensitive development issue, especially in the face of massive poverty in the rural areas. While there are enough institutional mechanism at the local government and community level that would increase agricultural productivity and other non-farm incomes - for instance, the functions of the Department of Agriculture and the National Cottage Industries Development Authority, among others were devolved to the local government units (LGUs) in 1992, with the passage of the decentralization law, but it did not prime push rural industrialization, just like the TVEs. The highest level of poverty incidence in the country is still the subsistence farmers who accounts for the majority of the rural population. The imperatives of agricultural modernization, aimed at increasing farmers' income are still wanting in its institutionalization due to financial constraint. That is the mile-long difference between the two counties. Chinese dualism succeeded in many respect to improve farmers productivity on one hand, and develop rural industrialization, on the other hand. *It is therefore recommended, that other than the funding facility*

[53] David Zweig, "From Villages to the City: Reforming Urban-Rural Relations" in *Freeing China's Farmers: Rural Restructuring in the Reform Era.*(London, M.E. Sharpe, 1997), pp. 198-199

through the microfinance scheme coming from both the government and the private sector, government instrumentalities must likewise bullishly provide technical support in terms of market access and product quality standards to make the small producers competitive in the market. The Department of Trade and Industry through its regional and provincial offices must purposively implement in coordination with other concerned government agencies like TESDA, Department of agriculture and others.

3. The decentralization of powers which was the centerpiece of the 1978 reforms, gave the leaders of the townships and villages the autonomy to draw up their own strategies in terms of economic development and what is the best mechanism to promote the welfare and common good of the community. This include resource generation not only through traditional revenue streams, but even through unconventional sources , and entering into cooperative agreements with other local governments, private individuals or even international intermediaries in resource sharing, support infrastructure development, production, market sourcing and expansion, and other governmental functions that will usher local development.

China saw the effectiveness of its autonomy or decentralization as a major component of the reform as early as 1978. The Philippines passed RA 7160, otherwise known as the "New Local Government Code" effectively only in 1992. The ensuing years saw how the LGUs painstakingly learned the ropes of being fully in charged of all facets of governance and development. The earlier discussions has belabored the fact that indeed, in the Philippine setting, there are more than enough laws, policies and enabling mechanisms that can set to motion, agricultural development, rural industrialization and subsequently, countryside development. The deterrent to the triggers is the lack of focus, as government is sidetracked by the pressing issues of growing insurgency, which is rooted on poor state of the rural economy. As both governments face the issues of politicizing development, corruption, vested interests, China managed to rise above it as shown by the growth of TVEs, the Philippines did not. *Since decentralization and bestowing powers to the LGUs are proven imperatives in effective governance, it is recommended that the Philippine government can now Republic Act 7160 – The Local Government Code for review especially on the aspect of economic governance of the LGUs and the incentive/ support to rural businesses and industrialization, among others.*

4. The TEB which is the main government instrumentality tasked to bring the support and reform agenda to the central government has not been very successful in rallying the financial sector to fully support the capital requirements of the TVEs. This is due largely to the staggering reforms of the financial sector which the international community believe is an imperative in the light of China's fast growing economy. Thus far, it had succeeded in the strengthening of the Township Enterprise Law in 1996, by calling for preferential policies on taxes, loans and development fund for the TVEs. *Corollary to the preceding observation, China can learn from the Philippine experience on the Unified Lending Scheme, Magna Carta of Lending, and the Guarantee Loan Fund Facility in support to the capital requirements of the SMBEs, and its stand by*

support facilities through the SMBEs Centers – Financial support, marketing linkages, advocacy, product development, among others. ***These institutional support would ensure the sustainable growth of TVEs or SMBEs***

5. Finally, a special feature of the SMBEs, which is not yet in the governance framework of a communist polity as of the moment, even if it succeeded in its transformation towards a strong market economy, is the role of the NGOs and POs. The law which granted local autonomy is also the very law which institutionalized the participation of NGOs/POs in various facets of local governance. In most conflict driven areas of Mindanao islands and other parts of the country, the local governments established strong partnership and collaboration with the NGOs/POs in setting up the SMBEs, and in shepherding its development considering that the SMBEs in these regions are not only poverty alleviation interventions, but part of the anti-insurgency measures of the government.

On the Philippine context, the SMBEs are not only the heart, but the lifeline of the economy. With the institutional support and mechanisms for its growth and acceleration in placed, it is envisioned, just like the TVEs, to also play the ace role, as the Philippine economy drives fast towards equitable and sustainable development. After all, as David Zweig concluded in his article, "From Village to the City: Reforming Urban-Rural Relations" – *the engine of economic development lies in the countryside and its link to the cities, not in the cities alone.* China's TVEs has advanced with giant strides since the late 1970's and the further development of TVEs will be a significant influence on China's social and economic life. While one of the key intervention areas is the "open door" policy, the dramatic emergence of the TVEs which spurred rural industrialization is both a "puzzle and a miracle", which can only grow in the uniqueness of a market economy within a communist regime. It is therefore without doubt that the Philippine policy makers and the program implementers alike can abstract meaningful learning from the development and growth of the TVEs, as the catalytic agent of rural development. The policy challenges therefore for the Philippines is enormous, and as a developing nation, the Mainland China lessons in development especially the TVEs, are always worth emulating.

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Annex "A"

Questionnaire Guide
Key Informants

Department of Trade and Industry Office

1. **What is the current situation of SMEs in the Philippines as to its contribution to GDP and generation of employment?**

2. **How are the SMEs in the Philippines faring with the other Asian countries?**

3. **What are the policies and programmes set by the Philippine government in order to support the SMEs?**

4. **In your assessment, what do you think are the strengths and weaknesses of the Philippine SMEs?**

5. **In the part of the government, what are its accomplishments in recent years with regards to SME support programmes and policies?**

Small and Medium Enterprise Key Player (Entrepreneurs)

1. **What is the industry are you engaged in?**

2. **How long have you been in the business?**

3. **How much was your initial capital?**

4. **Did you get any assistance from the government?**

5. **Do you have any suggestions for the government on how to improve their policies and programmes for key players like you?**