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# Factor Mobility and Economic Geography: A Short Critique of the WB's WDR 2009 Report

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The World Bank (WB) presented last week in Manila its World Development Report (WDR) 2009 with the title, "Reshaping Economic Geography". It discusses three main themes of Density, Distance and Division (3Ds): higher density of people through urbanization, shorter distance from home to work, and lower division for people mobility across communities and continents, as among the major factors for the changes in the economic landscape of many countries.

The Report is mainly descriptive. It describes conditions of selected big cities (Tokyo, Mumbai, etc.) and big countries. For instance, it noted three special places: (a) Tokyo is the biggest city in the world, with 35 million out of its 120 million total population packed in just 4 percent of Japan's total land area. (b) USA is the most mobile country in the world, with more than 35 million out of 300 million total population in 2006 changed residence, while 8 million changed states. And (c) West Europe is the most integrated continent, where about 35 percent of its GDP is traded, almost two-thirds within the region.

And in Asia, the Report cited three special places: (a) Mumbai is the most densely populated city with about 300,000 people per sq.km. of land, and this is already twice the population density of already densely-populated cities Seoul, Shanghai and Bogota. (b) China is the most mobile developing country where 60 million migrant workers traveled from home on the last day of the Chinese New Year holidays in 2006. And (c) Southeast Asia is the most rapidly integrating developing region where trade is a big portion of GDP and more than 25 percent of its trade is within the region, more than 50 percent if Northeast Asia (China, Japan, Korea, Taiwan, Hong Kong) is included.

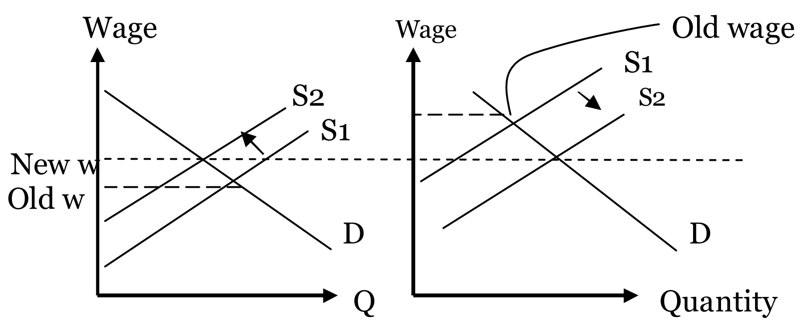
What the Report missed out, in the opinion of this writer, is the provision of a conceptual or theoretical framework that explains the phenomenon cited, can possibly predict future trends, and pave the way for their corresponding policy proposals.

One such conceptual framework is factor mobility across cities, countries and continents. When factors of production (labor, capital, technology, etc.) are unhampered to be mobile across different places, over the long-term, there will be factor price equalization (FPE), even temporarily. Wages on various skills level and industry will become more or less equal across countries. Interest rates and cost of capital too, will be different if there is capital immobility. Once capital is allowed to move freely, investors and entrepreneurs move their money to countries where they earn higher interest income, until interest rates are equalized, assuming foreign currency stability and other risks are identical.

A graphical presentation of two countries can help illustrate how FPE can happen, below. Before labor mobility, average wages are lower in a labor-surplus country, and higher in a labor-deficit country. Once those excess labor have moved out in the former, and labor deficiency in the latter has been filled up, wages would tend to equalize in both countries.

**Graph 1.** Factor price equalization, with or without free trade

Country A (labor-surplus)        Country B (labor-deficit)




FPE as a theorem is fragile because there are plenty of other factors that determine wages, interest rates and rental. Like language, where a more skilled worker from abroad can receive lower wage than a local worker with lower skills because the former does not speak or comprehend well the language in the host country, and the employer puts some weight on how he and his workers can communicate with each other. Other factors will be religion, culture, racial or national preferences, and so on.

FPE can substitute for commodity mobility when there is widespread protectionism of many countries. Under free trade, commodity price equalization (CPE) can happen, even temporarily, across countries (assuming transport cost of the traded goods is low). When prices of commodities are equalized, the prices of factors used in producing and moving said commodities tend to equalize too. But trade protectionism in various guises and alibis is relatively common for many countries these days, so CPE cannot happen soon, but it is a possibility in the future as more people realize the net gains from trade.

Nonetheless, FPE under full factor mobility can address global poverty and inequality, two of the bleeding hearts issue of the WB, the United Nations (UN) and other foreign aid and multilateral institutions.

The main lesson is that countries and governments should tear down various restrictions to factor mobility, especially labor mobility, in order to allow FPE or near-FPE to happen. In this section, two cases of labor mobility restrictions will be discussed. One is restriction by labor-source country, and two is restriction by the host or labor recipient country/ies.

***Case 1*** is no other than the Philippines. Before an aspiring overseas Filipino worker (OFW) can work abroad, there are plenty of requirements, tests and fees to pay. Among these are the following (rates as of 2006, could be the same until now):

1. Philippine Overseas Employment Authority (POEA) processing fee, get overseas employment certificate, $100.
2. Overseas Workers Welfare Administration (OWWA) membership fee, $25.
3. OWWA Medicare, P900 (about $19 at P48/US$)
4. Huge "placement fee" with POEA-accredited labor recruitment agency. Here, the amount can range from zero (for those directly hired by the companies abroad) to P200,000 ($4,166) or higher. POEA says many of those "placement fees" are illegal, but this is still widely practiced.

To be accredited by the POEA to be a legitimate manpower recruitment agency, huge payments have to be made, both legal and non-legal fees. So such fees can only be passed on to the aspiring OFWs in the form of high placement fees.

Then there are related expenses like medical certificate from POEA-accredited clinics, clearance from other government agencies (National Bureau of Investigation or the police, etc.).

Under ***Case 2***, two countries will be cited, Canada and Singapore.

A year ago, this writer met a lady at the Manila airport who was going to Canada to become a nanny to her sister's young kids so her sister can concentrate more on her career. She said the processing time for her application took more than 2 years that involved plenty of fees both here in the Philippines and in Canada. This is an example of government standing in the middle of purely private contracts between individuals and in this case, between siblings, on labor mobility. The Canadian government, or any host government, can justify the long processing time and the various fees required because of the expensive security and welfare system that even migrants can be entitled to once they set foot on those rich countries' land. Certain requirements and regulations, taxes and fees, both in the host and source countries, need to be relaxed in order to respect people mobility.

Singapore is a country that often ranks as #1 or #2 freest economy in the world in various studies like economic freedom index, economic competitiveness index, ease of doing business, and so on. Behind this "ease in doing business" image are various taxes and bonds if a person, whether a Singaporean national or an expat, would hire a nanny or house helper. First, there is a bond of S$5,000 per helper to be paid by the employer, to guarantee that the foreign helper will not "misbehave" like getting pregnant while in Singapore. If the helper misbehaves and the government discovers it, the bond is forfeited. Second, there is a S$300 per month (or S$3,600 per year) per maid tax to be paid by the employer. And yet the helper is not entitled to any government health service or any other welfare program, the employer will pay for the bill if the helper will get sick. Since there are more than 80,000 foreign house helpers in Singapore, government revenue from this tax is huge.

These and related rules and expenses discourage some households from hiring a foreign nanny or helper, a move that could have (a) created additional jobs for labor-surplus countries, (b) expanded the productivity of the bread-winner and/or the spouse as they will be freed from some household tasks and they can concentrate more on their career or field of specialization. The government of the labor recipient country can possibly argue that it wants to discourage the huge entry of less skilled workers into its territory, but it is those "less skilled" house helpers and nannies that precisely help the individual and household employers to become more skilled and more specialized as they can concentrate on their work and career as they are unburdened of plenty of routine household chores.

Governments need not declare that they "facilitate" or "encourage" people mobility. People are like water. Water pass through various openings – rivers and alleys, pores and caves, coming from different elevation, ultimately to "equalize" in elevation into lakes and oceans. The same way people find ways to improve their lives, to pursue certain ambitions, and so they seek out places where economic opportunities like employment and entrepreneurship are more abundant, with or without encouragement by governments. What the latter need to do, is to improve its core function of protecting the people's right to life, right to private property, and right to liberty and dignity, and leave most social and economic functions to personal and corporate responsibilities, as well as charity work by various voluntary citizen organizations.

So if factor mobility, especially labor mobility across countries is a good thing as this reduces poverty in poorer countries, and it also reduces inequality among people, then governments should tear down, or at least relax, some of the restrictions on labor mobility. This means that (a) various taxes and fees on people leaving a poorer economy, and (b) various taxes and fees on people hiring a foreign worker or house helper, plus many other regulatory procedures and requirements should be drastically reduced, if not abolished.

This does not appear to be the thrust or trajectory for policy proposals by the WB's WDR 2009 Report. The Report was too focused on the descriptive aspect of changing economic geography in the world, and is generally entertaining to its readers, especially for government policy makers who find nothing wrong with multiple taxes and fees slapped on entrepreneurs and people moving to different places in search of better returns for their labor, capital and technological innovation.

This perhaps explains the behavior of the WB and many other foreign aid and multilateral bodies that rely heavily on taxes, for their initial and augmentation capitalization, as well as payment for the billions of dollars of official loans that the bank extends to borrowing governments. Taxes are the lifeblood of the WB and its sibling or cousin foreign aid bodies. And these bodies are not likely to propose to reduce such lifeblood that sustain their huge and expensive bureaucracies.