IMPACT OF FOREIGN AID IN ECONOMIC DEVELOPMENT OF DEVELOPING COUNTRIES: A CASE OF PHILIPPINES

Mahmoud Kamal Abouraia

Business Administration Department,
Ibn Rushd College for Management Sciences,
Saudi Arabia
m_kamal100@hotmail.com

ABSTRACT

Developing countries have always relied on foreign assistance to enhance their economic development. The Philippines as a developing nation has been a recipient of foreign assistance from individual countries and from multilateral organizations. The study dough to establish the impact of foreign aid on the economic growth of the Philippine's the study was guided by three objectives which included to identify the types and forms of foreign aid in the Philippines; to identify the costs and benefits of foreign aid to the Philippines and to establish the factors affecting foreign aid effectiveness in the Philippines. The study was guided by the public choice and the public interests theory and also includes an empirical literature on the effectiveness of foreign aid. The researcher conducted a regression analysis of foreign aid in consistent with the economic growth of the Philippines. The OLS regression of the model yielded an adjusted R2 of .634, so 63.4% of the variation in the dependent variable is explained by the empirical model. The coefficients of all the variables except social aid have the expected signs, and all of them are significant at the 0.05 or 0.01 level. The coefficients of FDI and ODA per capita have a positive impact on GDP growth as expected. The current system of aid allocation encourages developing countries to keep their savings rate lower in order to receive more foreign aid. Donors should give the governments in these countries incentives to increase their savings by encouraging them to cut unproductive private government consumption. They should give incentives to lower corruption and implement effective policies. Donors could then reward these governments with an increasing amount of aid, if they meet all these targets of increasing savings, lowering corruption, and implementing good monetary, fiscal or trade policies.

Keywords: *economic development, foreign aid, Philippines*

1. Introduction

The existence of foreign assistance has been on the global scene as it has been in existence since the creation of national states and republics. The developed or rich countries have always assisted the developing or poor countries to achieve similar achievements to provide livelihoods for their citizens. There have been different views in terms of the effects of foreign aid on the recipient country. The history of foreign aid can be traced back to the 1940s following the destruction that was caused during the Second World War. Some of the post Second World War challenges were the collapse of the international economic systems characterized by shortage of capital required for infrastructure reconstruction. In the past four decades, however, there has been an increase in foreign aid towards developing countries. The concept of foreign assistance is a voluntary action which is dependent on the recipient country from a donating country, governments, private organizations, individuals, which are for providing support to the recipients' economic growth. In terms of foreign aid effectiveness of economic development has been brought back to attention in the recent past (Ouattara, 2006). In the less developed countries, foreign assistance plays an important role as another means for income at an average of 12.5% of the gross domestic product and a source of external income (Pallage and Robe, 2001). There is evidence from researchers that there exists a positive relationship between economic development and foreign aid as it complements domestic resources and also supplements domestic savings.

Among the Asian countries, the Philippines receive one of the largest amounts to foreign assistance from bilateral donors such as the United States and Japan; it also receives foreign aid from multilateral donors such as the Asian development bank and the World Bank. Japan, china, the World Bank and the Asian development bank are the largest donors of foreign aid to the Philippines in that order. Canada and the European institutions are the least contributing donors. Japan was the largest contributor of foreign aid to the Philippines accounting to $2.66 billion which translates to 31.69 percent share of the country's total official development assistance (ODA) commitment. The World Bank assistance to the country amounted to $2.185 billion; China donated an estimated $1.16 billion or 13.73 percent share of total ODA commitments that year and the Asian development bank contributing $667 million programmable aid budget in the year 2011. The Philippines is an archipelago of more than 7,000 islands and has a fast growth in population of 89 million. The Philippines is the fastest urbanizing nation in Asia and manila as the 11th largest city in the globe. The country is well endowed with natural resources for development purposes such as its strong human capital, biological diversity and mineral wealth. The higher rates of its migrant workforce provide large remittances for the nation. Despite these positive endowments, the government has identified that there are a range of governance issues and has often undertaken motivated anti-corruption measures and reforms.

The economic development in the Philippines was approximately 5.1 % between years 2000 to 2008, but this had no significant influence in the reduction of poverty. The poverty rates in the country have gone down by a third as compared to a half in the 1980s, whereas the high rates of rural/urban and regional inequalities continue to hinder further progress. In terms of its MDGs commitments, the Philippines are on track on achieving some of this showing positive progress on water and sanitation, child mortality and disease control. However, it will need to intensify efforts on gender equality, maternal mortality, primary education and reproductive health. The official development assistance to the Philippines was US$562 million in 2006 which translated to a 0.4 % of the gross national index. The largest donors were Japan, the World Bank and the Asian Development Bank, but inflows from china are not included in the statistics. The medium-term plan 2004-2010 sets out the government of Philippines development agenda which is also linked to the public investment programme of 2005-2010 with a three year rolling set of priorities. The national economic and development authority is mandated with spearheading the government's development agenda. The Philippine government exhibits strong leadership over aid management and coordination and chairs the Philippines development forum with the World Bank, and has developed a number of sectoral working groups to improve aid coordination.

There is no consensus on the impact of aid on economic growth in the literature. Rostow (1990) opines that foreign aid is the imposition of the developed countries on the less developed countries as a prerequisite for economic development. On the contrary, Hayter (1971) views foreign aid it is a form of modern imperialism and may not lead to the anticipated economic benefits. Tadesse (2011) argues that foreign capital inflows are popular due to their potential to finance investments and the perception of their ability to enhance economic development in the recipient country. The growing departure in reduction and asset rates, import-export gap (foreign exchange constraints to import capital goods) and budget deficits in less developed countries make them to depend highly on inflow of foreign capital. The large deficit between developing and developed nations has led to the sustenance of the foreign assistance initiatives (Andrews, 2009). This status quo has led to the frequent inflow of capital from developed countries to developing countries in an attempt to reduce the gap while overcoming their problems. According to Andrews (2009), there is evidence e to suggest that although African countries have been receiving aid for several decades there has been no significant change to their destinies. Most of these countries continue to exhibit slow development rates. Girma *et al.* (2005) opine that the less developed countries lack the sufficient local sources to finance investments and the foreign capital to import technology and goods. The foreign assistance received when used can assist to directly fill the savings investment gap and indirectly fill the foreign exchange gap. The official aid that is given to governments can also assist in funding the government spending and reward for a small domestic tax base.

The definition of foreign aid is provided by the development assistance committee (DAC) of the organization for economic cooperation and development (OECD) as the sum of grants that are forwarded recipients received by the sectors of the donating country. Where they seek to promote economic development in the recipient country and are provided for through financial concession terms such as a 25 % of the total grant or aid (Tarp, 2009).

1.1 Despite massive inflow of aid to developing countries

Although there has been extensive flow of foreign aid to developing nations and extensive empirical work for decades on the aid-growth link, the aid effectiveness literature remains controversial. An important objective of foreign aid to less developed countries is to enhance their economic development and welfare, this is more often measured by the impact that it has on economic growth. Despite decades of transfer of foreign capital to the developing countries, there is evidence from numerous studies that seeks to unmask the relationship between aid and economic development, but there has been less evidence of achieving these objectives (Durbarry *et al.*, 1998). The Philippines, between the 1966 and 1986 period under the rule of President Marcos, received $33 billion as foreign assistance. However, vast amount of the aid was diverted to the president’s accounts and family accounts in foreign nations (CBO, 1997). Consequently, poor people in this country did not benefit from the inflow of foreign aid.

Girma *et al.* (2005) study on 25 sub-Saharan Africa countries, from 1970 to 1997 showed that the aid appears to be ineffective. Their study found that in terms of receiving aid these countries only saw 0.6 percent development in their GDP per year following this period. Tarp (2009) agrees that aid is still an important tool for enhancing the growth outlook of poor countries. Likewise, Arndt, Jones and Tarp (2009) found that there was a reduced positive impact of aid on economic growth. These studies, therefore, point a case for the effectiveness of aid. The UNDP (2000) assert that although there may be a significant growth on the national GDP there still is a discrepancy the true essence of development growth. Many empirical studies (most of them being cross-country) have used econometric analysis to test the aid-growth relationship at the macro level, complemented by case-study evidence at the project level. While micro-based(project level) evaluations have found that in most cases 'aid works' (Cassen *et al.*, 1986), those at the macro level have yielded more ambiguous results, often failing to find significant growth effects.

According to McGillivray (2009) foreign aid plays an essential role fulfilling saving gap, accumulating physical and human capital stock and developing infrastructure in the host countries. The study will focus on the concept of aid effectiveness on economic growth by seeking perceptions of levels of poverty and basic living standards in Philippines. This includes the access to such services as health and education and food security which are significant determinants of the human capital, which participates in the economic growth of the country. Clemes and Gani (2003) study found that there was an effect of aid on human development, which was found in health and education and also showed a significant correlation in terms of human development among the lower-middle countries. The Gross Domestic Capita is mostly associated with economic growth and ignores several issues of development such as standard of living, levels of education and health.

1.2 Objectives of study

1. To identify the types and forms of foreign aid in the Philippines
2. To identify the costs and benefits of foreign aid to the Philippines
3. To establish the factors affecting foreign aid effectiveness in the Philippines

2. Literature Review

This section includes the empirical literature on the impact of foreign aid to economic development that comprises data and research from developing countries from Asia and also from Africa. The literature also provides a synopsis of the types and forms of foreign aid to developing countries. The chapter also includes a review of theories of foreign aid assistance.

2.1 Theories of Foreign Aid

2.1.1 Public Interest Theory

The public interest theory remains as the most significant theory towards foreign aid and has been in existence for the last 50 years. The public interest theory argues that foreign aid is necessary to fill a financing or investment gap, and this will in turn lift countries out of the so-called poverty trap (Sachs, 2005). According to Anwar (2000), points out that it is the donor countries politicians who are assumed to make decisions to provide aid to less developed countries in order to assist them serve their motives. The public choice theory argues that the major political motive of these politicians is to become reelected and, therefore, stay in power.

2.1.2 Public Choice Theory

This is a contrasting theory of foreign aid; the theory contends that foreign aid is ineffective and possibly damaging to recipient countries (Bauer, 2000; Easterly, 2001). The recent examination in the literature has shown that foreign assistance has no effect on development or any of the other indicators of poverty thus supporting the public choice theory proposition (Boone, 1996; Svensson, 2000; Brumm, 2003; Djankov *et* *al.,* 2008; Williamson, 2008). Anwar (2000), according to Public Choice Theory, all political decision making processes reflect the interaction of different utility maximizing actors: politicians, voters, bureaucrats and interest groups. In order to examine donors' decisions on development aid, we need to consider their utility maximizing behavior within the different donor countries (bilateral aid) and within international organizations (multilateral aid). In their quest to maintain power by reelection to the office they have to appease the electorate (Landau, 1990). This support can be gained in different ways and by different means. One way of gaining this support is through giving of aid to poor and developing countries. Giving aid to poor and developing countries is normally justified by politicians on the basis of wanting to appease poverty and hunger in developing countries. This can be called the "moral appeal" of foreign aid (Michaelowa, 2003).

According to Grindle and Thomas (1991) the public choice theory is also referred to as the new political economy approach argues that governments cannot do anything right. Similarly, citizens are viewed in the public choice theory as using their political influences to gain special benefits (rents) from the policies adopted by the government such as rationed foreign exchange and import licenses that further limits access to significant resources. The politicians according to the perspective use government resources to maintain and consolidate and maintain their positions of power. Similarly, bureaucrats and public officials use their positions to get bribes from rent-seeking citizens and to run protected business on the side.

The states also use their power to confiscate private belongings from the population. This often leads to the misappropriation of resources but also limits the individual freedoms of the citizens. The conclusion, therefore, is that minimal government is the best government (Grindle and Thomas, 1991). For instance, under the leadership of President Marcos in the Philippines, there was no development in economic growth despite receiving aid. The Philippines received 33 billion US dollars between 1966-1986 as foreign assistance which was channeled through the president and the family and transferred to their personal bank accounts. Consequently, poor people in this country did not benefit from the inflow of foreign aid (Lohani, 2004).

3. Empirical Literature

Rajan and Subramanian (2008) conclude that aid has had no systematic effect on growth and assert that this conclusion holds across methodologies, time periods and forms of aid. Thus, and as advocated by the authors (2008), an appropriate research agenda may be to unpack the different effects of aid on growth by focusing on intermediate outcomes which are proximate determinants of income growth. Chenery and Strout (1966) adopting empirical data from less developed countries show that foreign aid has a significant positive effect on the recipient country economic growth. Other researchers however have disrupted this, findings that indeed foreign aid has often had a negative impact on economic growth of developing countries as it negatively affects economic growth by replacing the local savings (Leff, 1969; Griffin, 1970). The main argument is that foreign aid in its negative impact offsets the advantages of transferring resources and that it undermines or weakens governance by increasing the return to corruption or increase in lending for the developing countries. Djankov *et al.* (2008) opines that foreign assistance has a significant negative effect on the changes in political institutions more specifically democracy.

Djankov *et al.* (2008) argues that the negative impact of aid on the political institutions is wider than those caused by natural resource windfalls. Likewise, an earlier study by Rajan and Subramanian (2007) found that the developing countries manufacturing sectors were undermined by the detrimental effect of assistance of aid inflow on their governance. There have been both negative and positive effects of the effectiveness of aid in the literature on the economic development. Khan *et al.* (1992) opine that approximately that foreign aid led to the decline of national savings in Pakistan in the era of 159-1960 t0 1987-1988. There has been a negative impact of foreign assistance of Pakistan national savings during the same duration (Shabbir and Mahmood, 1992). Adopting Mozambique as a case study, Arndt *et al.* (2007) show that the effects of foreign assistance across diverse drivers and growth; beginning with a long-run growth of accounting estimates and find that aid has a significant role in developing infrastructure and also enhancing access to education and health. Similarly, Arndt *et al.* (2009) found that foreign assistance has a strong and statistically significant causal effect on growth in the long-term with point estimates at levels suggested by growth theory.

Aid has supported rapid reconstruction and seems to have crowded-in private and foreign investment, but has also brought substantial governance and economic management challenges (Arndt *et al.,* 2007). Burnside and Dollar (1997) was emphatic that there is a relationship between foreign assistance and economic development but it requires a positive policy environment. Their study used 56 countries with 6 four year time periods of 1970-1973 which showed that foreign assistance was associated with good economic policies and the impact was positive and strong. There is evidence that foreign assistance is conditionally effective with good policies, low rates of corruption conflict and governance (Collier and Dollar, 2001). Notwithstanding the support that Burnside and Dollar stance has combined (Dovern and Nunnemkamp, 2007; John and Sackey, 2008), there are other studies that indicate no important association among aid and growth. Easterly *et al.* (2003) found different results when they added more data and also extended the year range from 1993 to 1997. Although they do not actually argue that aid is ineffective, they find that with the introduction of the new data, the positive relationship between aid and growth withers away. That aid reduces the incentives to invest, especially when the recipient is assured that future poverty will call for more aid. Gibson *et al.* (2005) this occurrence is referred to as the Samaritan's Dilemma.

Foreign assistance can also lessen the recipient country's competitiveness (Rajan and Subramanian, 2005), leading to the Dutch disease (a condition that reduces competiveness of the manufacturing sector due to overabundance of foreign assistance). The ills of aid, according to Reusse (2002), include inertia, easy money, ignorance, complacency and the fact that an interventionist paradigm is imposed on recipients of aid regardless of their internal socio-cultural dynamics. The culture has always been associated with the economic activities and performance of a people, in this case a nation. Calderisi (2006) associates the underdevelopment of the African continent to the diversity in the culture. Pomerantz (2004) argues that donors have not made efforts to comprehend the context with which aid could be made to work. According to Sen (2004), the issue at hand is the manner in which the culture matters towards the effectiveness of aid. Sen (2004) argues that culture influences political participation, gives people a sense of identification and similarly influences economic behavior. Landes (2000) opines that the history of economic development shows that culture does indeed make all the difference.

Indeed the effectiveness of aid can be attributed to culture as evidenced by the difference of effects of aid between countries. For instance, Korea and Ghana in the 1960s were comparable in terms of their growth, however, after thirty years, South Korea has become an economic giant whereas Ghana is still reliant on foreign aid. Huntington (2000) asserts that although many issues might clarify this, culture has to be a large part of the explanation. Hyden (2006) has admitted that culture may not be dismissed by political scientists as it is the foundation on which not only formal, but also informal institutions arise. The government plays a significant role in the regulation of economic policies. According to Singh (1985) the states intervention in the economy of a country has often had negative impacts of economic growth and thus reduces the significance of foreign aid. Burnside and Dollar (1997) a prerequisite for foreign aid to be effective is the existence of a good macroeconomic policy environment. Aid has been found to be ineffective when there are no sound policies (Tadesse, 2011). Burnside and Dollar (1997 and 2000) found that aid has an optimistic result on growth in a setting of good fiscal, monetary, and trade policies.

Two meta-studies focusing on the effectiveness aid have been drawn based on the limitation of space, but also due to their contemporary and comprehensives in terms of the coverage of empirics of aid. These studies comprise studies by Tsikata (1998) and Doucouliagos and Paldam (2008). Likewise, Hansen and Tarp (2000) and McGillivray et al. (2006) are also contemporary and comprehensive in their review of the literature in foreign aid. Tsikata's (1998) study shows that there is still debate on the effect of foreign aid towards economic growth showing that there are still poor relationships between growth and foreign aid in the empirical literature. However, the study finds that there has been a positively significant impact of the economy of developing countries as long as there are conducive policy conditions for economic growth. This publication was done after the World Bank (1998) publication report, Assessing aid and could not have anticipated the criticism after the findings of Burnside and Dollar (1997, 2000). Some of their World Bank colleagues, which aid is effective in contributing to economic growth only under conditions of good policies. Tsikata (1998) finds that in terms of the impact of foreign assistance on the growth of domestic and savings and investment; the outcomes were mixed, with some pointing to an important association in countries that thrived in supporting the adjustment effort.

Doucouliagos and Paldam (2008) study does not support the significant relationship between aid and economic growth as found by McGillivray *et al.* (2006) that foreign assistance does not sustain the positivity found by the argument on aid influences on financial development; is established following a rising twist in the indication since the late 1990s to an optimistic and important relationship; neither do the outcomes support the confident assumption that Hansen and Tarp (2000) found. Doucouliagos and Paldam (2008) argue that even after 2006 there is cumulative indication to demonstrate that aid does not endorse economic development. They additionally show that the stated aid-growth association was weaker in the 1970s and 1980s, but improved in the 1990s and 2000s; this improvement however does not suggest that there was no recent indication of insignificant relationships as recent as suggested by McGillivray *et al.* (2006). However, this evidence does show that there was improvement in the association between aid and growth during this period as contrasted as in the earlier literature.

3.1 Forms of Foreign Aid

3.1.1 Project Aid

Though there has been a decline of ODA in form of project aid from themid-1990s, ODA to specific projects still exist. Project aid is dominated by funds channeled to interventions in sectors such as health, education, rural development including agriculture, transport and power, housing, and water supply and sanitation. However, small amounts of project aid are channeled to industrial, mining, trade and cultural projects (Riddell, 2007). Many ODA funded development projects aim at achieving specific outputs by providing resources, skills and systems which the recipient country needs.

3.1.2 Programme Aid

Programme aid is defined by OECD as financial contributions not linked to specific activities (as cited in Riddell, 2007). The programme aid is divided into two forms, the balance of payments (BOP) support and the budget support. Under the budget support, aid funds are provided to boost aggregate revenue and increase overall spending. Aid funds channeled to ministries of finance are termed as General Budget Support (GBS) while those channeled to particular sectors are termed as Sector Budget Support (SBS). Under the GBS, donors provide funds for implementation of development and poverty alleviating strategies paying attention to the capacity of the recipient governments to use funds efficiently.

3.1.3 Technical Assistance

Technical Assistance (TA) includes the provision of skills, knowledge know-how and advice. For many decades, technical assistance has also been provided in form of teaching staff mainly in primary and secondary education in developing countries. Furthermore, more specialized trainers have continually performed skills training functions to meet their needs and to achieve their immediate objectives. For example, the London-based Overseas Development Institute (ODI) has been running its fellowship scheme for graduate economists and placing them in key ministries in developing countries (Riddell, 2007). Despite this positive impact of TA, there have been several problems associated with it. Some of these problems include high costs of providing the TA (especially the consultancy costs).

3.1.4 Humanitarian Aid or Emergency Aid

The definition of humanitarian aid is defined according to its purpose, that is, ''to save lives, alleviate suffering and enable those suffering to maintain (or retain) their human dignity during and in the aftermath of natural disasters and man-made crisis''. Humanitarian aid has been successful in most cases in achieving its tangible outcomes such as saving lives, providing food to the hungry; healthcare and medicines to those vulnerable to acute disease in emergencies; and water, sanitation and shelter to those whose homes have been destroyed. However, the sustained internal conflicts in war prone areas reduce resources to meet development objectives as more resources are directed to meet humanitarian needs (Kabete, 2008).

3.1.5 Food Aid

Food aid comprises of programme food aid and humanitarian food aid. Programme food aid may relieve the foreign exchange constraint to the import of the necessary intermediate inputs or by providing fiscal resources through counterpart funds generated by the local sale of programme food aid (Barret, 1998). These resources can be used by the recipient country to invest in agricultural research and extension and improvement of rural infrastructure in particular. However, programme food aid may have Dutch disease effects on domestic food producers and thus hurting the food sector's competitiveness in the world markets.

4. Research Methodology

The study will use data from the World Banks database on the amount of official development assistant received by the Philippines covering the period from 2009-2012. Net official development assistance (ODA) contains payments of finances made on enterprise terms (net of repayments of principal) and endowments by authorized agencies of the members of the Development Assistance Committee (DAC), by multilateral organizations, and by non-DAC countries to endorse economic growth and wellbeing in nations and territories in the DAC list of ODA beneficiaries. It comprises loans with a funding component of at least 25 percent (calculated at a rate of discount of 10 percent). In order to measure the impact of foreign assistance to the economic development of the Philippines, the study used the gross domestic product (GDP) as per the latest global rankings by the World Bank. The latest GDP rating of the Philippines is at 250,182Million US Dollars. GDP per capita plays an instrumental role in human development. The income level of citizens of a country are high it is likely that there is also a higher standard of living which also enhances their chances to afford and access health and educations services. There is a positive statistical correlation between GDP and human development (Anand and Ravallion, 1993). This impact is felt due to the lowering of poverty rates and increase the expenditure among the public in terms of education and health. So the coefficient of GDP per capita is expected to be positive.

5. Findings and Analysis

Table 2 indicates the ordinal least regressions of the variables of foreign direct investments, official development assistance and their perceived impact on GDP growth. The OLS regression of the model yielded an adjusted R^2 of .634, so 63.4% of the variation in the dependent variable is explained by the observed model. The coefficients of all the variables except GDP growth show positive signs, and are significant at the 0.05 or 0.01 level. The coefficients of FDI and ODA per capita have a positive impact on GDP growth as expected.

It goes without saying, that a poorer country will receive more aid. The aid is donated by multilateral organizations such as the IMF and the World Bank which is as a result of the difference between the country's savings and the required investment amount to achieve a sustainable economic growth (Easterly, 2001). A poorer country will then have a poor savings rate and as such receives more foreign aid based on this calculation of aid. In Africa, foreign aid is a significant source of income for countries that have an average GDP of 12.5 percent and also as a source of external capital (Pallage and Robe, 2001). The results show that FDI positively influences human development. When ODA as a share of GDP increases a factor, GDP increases by 0.00435; the value 0.0035 may appear insignificant, but the value of the GDP ranges from 0 to 1. So, for instance, if the GDP of Philippines country rises from 0.1 to 0.10435, the HDI increases by 4.35%. Furthermore, development takes time, and there are several factors that influence it.

Similarly, the regression results suggest that ODA has a positive impact on development. Precisely, an increase in ODA by one percent increases the GDP growth by 0.0035. The t-statistic for this variable is 3.420, which shows that this coefficient is significant at the 0.01 level. Therefore, ODA plays an important role in the development of the economy.

6. Research Discussion

Foreign direct investment; net inflows (% of GDP) in Philippines was last measured at 0.56 in 2011. Through a qualitative analysis, the study found that the Philippines have been a recipient of Foreign Direct Investments (FDI). Foreign direct investment can be loosely defined as the Will refer to the investment done by a foreign individual or corporation in a country with the purpose of having an influence over the development of the firm's long term strategy. FDI and TNCs affect economic growth (and other magnitudes of growth) through three important mechanisms which include the skill and technology effects, size effects and structural effects. The size effects refer to the net contribution of the FDI to the recipient country investments and savings thereby affecting the growth rate of the base of production (Bosworth and Collins, 1999). Majority of the potential benefits and costs of foreign assistance are achieved from the unintended effects of foreign direct investments more so through the skills transfer and technologies (Baldwin *et al.*, 1999) or either through the changes in structures in the market through linkages and competition (Kokko, 1996).

FDI in the Philippines has had a cyclical manner. Following the Asian crisis there was a massive outflow of FDI from the Philippine economy. In the early 2000s, the Philippines had a basic policy towards the liberalization of the economy. Although the country faced global economic uncertainties and risks in the 2000s it still showed some elasticity in its economy. The private sector plays a significant role in the economy of the Philippines with the sector contributing over 90 percent of the employment and the gross domestic product. In response to promoting the private sector, the Philippine government has embarked on a long-term strategy on the challenges and constraints facing the sector which include financial sector weaknesses, the lack of ability to pursue and win contracts and infrastructural constraints. The efforts have also included the formulation of legal reforms to assist in the improvement of the governance and economic situation in the economy.

The challenges for FDI in the Philippines may be attributed to the policy environment for doing business. According to the doing business statistics from 2006-2009 show a decline of the Philippines economy which ranged from a ranking of 126 in 2006 to 140 in 2009; Alburo (2000) associates the decline in the political and economic fundamentals of the Philippines as contributing to the decline in FDI. The effectiveness of FDI for the host country is enhanced by the existing policy environment which is related to investments and trade. The Philippines has also been a recipient of foreign aid in the form of humanitarian end emergency aid over the years. Recently, the country was struck by a category five typhoon, typhoon Yolanda in November 2013. The typhoon affected 16.1 million people across nine regions. It displaced around 4.1 million people, including over 101,000people in 381 evacuation centers and around four million people outside evacuation centers. The Government reported 6,201 fatalities and 1,785 persons missing. A total of 1.1 million houses were damaged, of which close to 551,000 were totally destroyed (World Bank, 2014).

7. Conclusion

The current system of aid allocation encourages developing countries to keep their savings rate lower in order to receive more foreign aid. The donating countries should provide the recipient countries with incentives to grow their savings by assisting them to reduce unproductive private government consumption. These include the provision of incentives for effective policy implementation and reduce corruption levels. This would then enhance the donors to provide the governments with an increase in aid on condition that they meet the targets in terms of lower corruption rates, increasing savings and adopting and implementation of positive fiscal, monetary and trade policies. Empirical studies (Franco-Rodriguez, 1998; Burnside and Dollar, 2000; Boone, 1996; Feeny, 2005) have shown that foreign assistance has been widely discussed as being endogenous. For instance, consider the difficulty of simultaneity prejudice owing to the likely endogeneity of foreign assistance. The chief aim recommended for this in the aid-growth regressions is that it is hard to observe aid as a lump-sum transfer that does not take into thought the level of revenue of the beneficiary country. Benefactors may be inclined to assign fewer or additional aid to nations that do not tend to thrive in terms of their economic performance. If the aid depends on the level of revenue, it cannot consequently be exogenous with regards to growth as has been usually assumed.

Developing countries should create a favorable environment to attract foreign direct investment because multinational companies have a significant role in the provision of jobs and expertise to the recipient country. However, the recipient country should also make efforts to promote domestic investments. This should be done through the creation of incentives in banks to enhance local savings which further promotes the strength of the banking system. This involves strengthening of the local small and medium enterprises to participate in the industrial and manufacturing sectors by the lowering of taxes from profits for investments in new innovative technologies and industries. The recipients' governments should be a priority for the donors and governments. This is a deviation from implementation of programs that assist in the decrease and increase of economic development. They should, however, as a government be more involved in education and awareness initiatives for their citizens in an effort to meet their basic needs. Donors and the recipients countries should be able to realize that although the incomes of the country may rise or fall but the important thing is that the citizens are happy, healthy and educates that can have a long term impact on the country's future.

Most of the empirical studies focus on economic development in the macro-economic sense without knowledge that the concept of development is larger than just the statistically significant improvement in GDP. The situation on the ground could be that there is still widespread poverty in the community level despite the country's attainment of appreciable levels of macro-economic development. The impact of foreign aid on economic growth will depend on how aid is utilized for development. The policy framework

European Journal of Business and Social Sciences, Vol. 3, No. 4 , pp 166-180, **July 2014.** **P.P. 166 - 180**
URL: *http://www.ejbss.com/recent.aspx*
ISSN: 2235 -767X

that is implemented should be aimed at maximizing the utilization of the overseas development assistance in a bid to promote the local labor productivity and also for the growth and expansion of promoting exports and substituting import industries as it will have a long term impact on the country's per capita growth of the recipient economy (Burnside and Dollar, 2000; Mallik, 2008). The relationship between GDP Growth and the increase of the relationship between FDI and GDP (FDI/GDP (%) can be clearly established. The recipient country should thus adopt policies that are in tandem with the transnational companies. Competitiveness of a country that may draw FDI from Transnational Corporations is controlled by Strong Institutions, Economic Stability, and Comparative Factors the first taking in more importance every year. Because of these reasons, countries have to employ active policies that can bring Economic Stability and that can create a suitable investment environment for the country.

8. References

1. Alburo, F. A. (2000). Foreign Direct Investment in the Philippines amidst Crisis and a New Global Environment. Philippine Review of Business and Economics, 3: 43-54.
2. Anand, S., and Ravallion, M. (1993). Human Development in Poor Countries: On the Role of Private Incomes and Public Services. Journal of Economic Perspectives, 7(1): 133-150.
3. Andrews, N. (2009). Foreign aid and development in Africa: What the literature says and what the reality is?. Journal of African Studies and Development, 1(1): 008-015.
4. Anwar, M. (2000). Who Determines the Foreign Aid to Developing Countries: A Public Choice Approach. Journal of commerce, 3: 9-29.
5. Arndt, C., Jones, S. and Tarp, F. (2009). Aid and Growth: Have We Come Full Circle? WIDER Discussion Paper No. 2009/05.
6. Arndt, C., Jones, S. and Tarp, F. (2007). Aid and Development: the Mozambican Case, In Lahiri, S. (ed.), Theory and Practice of Foreign Aid, Frontiers of Economics and Globalization, Volume 1, Amsterdam: Elsevier.
7. Baldwin, R., Braconier, H. and Forslid, R. (1999). Multinationals, endogenous growth and technological spillovers: theory and evidence, CEPR Discussion Paper, 2155.
8. Barrett, C. B. (1998). Food Aid: Is It Development Assistance, Trade Promotion, Both, or Neither? American Journal of Agricultural Economics, 80(3): 566-571.
9. Bauer, P. T. (2000). From subsistence to exchange. Princeton: Princeton University Press.
10. Boone, P. (1996). Politics and the Effectiveness of Foreign Aid. European Economic Review, 40(2): 289–329.
11. Bosworth, B. and Collins, S. (1999). Capital flows to developing economies. Implications for saving and investment, Brookings Papers on Economic Activity, 1: 143-169.
12. Brumm, H. J. (2003). Aid, policies and growth: Bauer was right. Cato Journal, 23, 167–74.
13. Burnside, C. & Dollar, D. (1997). Aid, Policies and Growth. Policy Research Working Paper 1777, World Bank, Development Research Group, Washington D.C.
14. Burnside, C., & Dollar, D. (2000). Aid, Policies, and Growth. American Economic Review, 90(4): 847-868.
15. Calderisi, R. (2006). The Trouble with Africa: Why Foreign Aid is not working. Palgrave MacMillan, New York.
16. Cassen R. et al. (1986), Does Aid Work? Clarendon Press, Oxford.
17. Chenery, H. B. and Strout, A. M. (1966). Foreign Assistance and Economic Development. American Economic Review. New York: American Economic Association. 56(4): 179-773.
18. Congressional Budget Office (1997). The Role of Foreign Aid III Development <http://www.cbo.gov/showdoc.cfm?index=8&seguence=1>
19. Clemes, M. and Gani, A. (2003). Aid Type and Its Relationship with Human Well Being. International Journal of Social Economics. Vol. 30-6.
20. Collier, P. and Dollar, D. (2001). Development Effectiveness: What Have We Learnt? The World Bank Development Research Group.
21. Djankov, S., Montalvo, J. and Reynal-Querol, M. (2008). The curse of aid. Journal of Economic Growth, 13(3): 169-194
22. Doucouliagos, H., and Paldam, M. (2008). Aid Effectiveness on Growth: A Meta Study. European Journal of Political Economy, 24: 1–24.

23. Dovern, J. and Nunnemkamp, P. (2007). Aid and Growth Accelerations: An Alternative Approach to Assessing the Effectiveness of Aid. KYKLOS, 60(3): 359-383.
24. Durbarry, R., Gemmell, N. and Greenaway, D. (1998). New evidence on the impact of foreign aid on economic growth, CREDIT Research Paper 98/8, University of Nottingham.
25. Easterly, W. (2001). The Elusive Quest for Growth. Cambridge: The MIT Press.
26. Easterly, W., Levine, R., and Roodman, D. (2003). New Data, New Doubts: Revisiting Aid, Policies, and Growth. Center for Global Development Working Paper Number 26.
27. Feeny, S. (2005). The Impact of Foreign Aid on Economic Growth in Papua New Guinea. Journal of Development Studies, 14(6): 1092–117.
28. Franco-Rodriguez, S., McGillivray, M. and Morrissey, O. (1998). Aid and the Public Sector in Pakistan: Evidence with Endogenous Aid. World Development, 26(7): 1241–50.
29. Gibson, C. C., Andersson, K., Ostrom, E. & Shivakumar, S. (2005). The Samaritan's Dilemma: The Political Economy of Development Aid. Oxford University Press, Oxford.
30. Girma, S., Gomanee, K., and Morrissey, O. (2005), Aid and Growth: Accounting for Transmission Mechanism in Sub-Saharan Africa, UNU-WIDER, Research Working Paper No.2005/60.
31. Griffin, K. B. (1970). Foreign Capital, Domestic Savings and Development. Bulletin of Oxford University. Institute of Economics and Statistics. Oxford University Press. 32 (2).
32. Grindle, M. S. &Thomas, J. W. (1991). Public Choices and Public Policy Change: The Political Economy of Reform in Developing Countries. Baltimore: Johns Hopkins University Press.
33. Hansen, H., and Tarp, F. (2000). Aid and Growth Regressions. CREDIT Research Paper 00/7. Nottingham: School of Economics, University of Nottingham.
34. Hayter, T. (1971). Aid as Imperialism. Penguin Books Inc., Britain.
35. Huntington, S. P. (2000). Culture Counts. In Lawrence EH and Samuel. PH eds., Culture Matters: How Values Shape Human Progress. Basic Books, New York.
36. Hyden, G. (2006). African Politics in Comparative Perspective. Cambridge University Press, Cambridge.
37. John, L. and Sackey, H. A. (2008). Aid Effectiveness in Africa. The Authors Journal Compilation, African Development Bank.
38. Kabete, N. C. (2008). Foreign Aid and Economic Growth: The Case of Tanzania. Graduate School of Development Studies. The Hague. Netherlands
39. Khan, A.H. L. Hasan and A. Malik (1992). Dependency Ratio, Foreign Capital Inflow and the Rate of Savings in Pakistan. Pakistan Development Review. Islamabad: Pakistan Institute of Development Economics, 3(4): 843-56.
40. Kokko, A. (1996). Productivity spillovers from competition between local firms and foreign affiliates. Journal of International Development, 8(4):517-30
41. Landes, D. (2000). Culture Makes Almost All the Difference. In Lawrence EH and Samuel P. Huntington eds., Culture Matters: How Values Shape Human Progress. Basic Books, New York.
42. Leff, N. H. (1969). Dependency Rates and Saving Rates. American Economic Review. New York: American Economic Association. 59(5).
43. Lohani, S. (2004). Effect of Foreign Aid on Development: Does More Money Bring More Development? Honors Projects. Paper 18.
44. Mallik, G. (2008). Foreign Aid and Economic Growth: A Cointegration Analysis of the Six Poorest African Countries. Economic Analysis and Policy, 38: 251-260.

45. McGillivray, M., S. Feeny, N. Hermes, and R. Lensink (2006). Controversies over the Impact of Development Aid: It Works; It Doesn't; It Can, but that Depend. Journal of International Development, 18(7): 1031–50.
46. McGillivray, M. (2009). Aid, economic reform, and public sector fiscal behaviour in developing countries. Review of Development Economics, 13(3): 526-542.
47. Michaelowa, K. (2003).The Political Economy of the Enhanced HIPC-Initiative, in: Public Choice,Vol. 114, pp. 461-476.
48. Ouattara, B. (2006). Aid, debt and fiscal policies in Senegal. Journal of International Development, 18(8): 1105-1122.
49. Pallage, S. and Robe, M. A. (2001). Foreign aid and the business cycles. Review of International Economics, 9, 641-672.
50. Pomerantz, P. R. (2004). Aid Effectiveness in Africa: Developing Trust between Donor and Governments. Lexington Books, USA.
51. Rajan, R. G. and Subramanian, A. (2007). Does Aid Affect Governance? American Economic Review, 97(2): 322-327.
52. Rajan, R. G. and Subramanina, A. (2008). Aid and Growth: What Does the Cross-Country Evidence Really Show?. The Review of Economics and Statistics, 90(4): 643-665.
53. Reusse, E. (2002). The Ills of Aid: An Analysis of Third World Development Policies. University of Chicago Press, Chicago, London.
54. Riddell, R. C. (2007). Does Foreign Aid Really Work? New York: Oxford University Press.
55. Rostow, W. W. (1990). The Stages of Economic Growth: A Non-Communist Manifesto, Cambridge Press, Cambridge.
56. Sachs, J. D. (2005). The end of poverty. New York: The Penguin.
57. Sen, A. (2004). How Does Culture Matter. In Vijayendra R and Michael W eds., Culture and Public Action. Stanford University Press, Stanford, California (1999). Development as Freedom. Anchor Books, New York.
58. Shabbir, T. and A. Mahmood (1992). The Effects of Foreign Private Investment on Economic Growth in Pakistan. Pakistan Development Review. Islamabad: Pakistan Institute of Development Economics, 31(4): 831-41.
59. Singh, R. D. (1985). State intervention, foreign economic aid, savings and growth in LDCs: Some recent evidence. Kyklos 38, 216-232.
60. Svensson, J. (2000). Foreign aid and rent-seeking. Journal of International Economics, 51, 437–461.
61. Tadesse, T. (2011). Foreign Aid and Economic Growth in Ethiopia: A Cointegration Analysis. Economic Research Guardian, Weissberg Publishing, 1(2): 88-108, December.
62. Tarp, F. (2009). Aid Effectiveness, UNU-WIDER, Working paper 2009/05.
63. Tsikata, T. M. (1998). Aid Effectiveness: A Survey of the Recent Empirical Literature. IMF Paper on Policy Analysis and Assessment, 98/1. Washington, DC: IMF.
64. United Nations Development Program (2000), Human Development Report. New York: UNDP.
65. Williamson, C. R. (2008). Foreign aid and human development: The impact of foreign aid to the health sector. Southern Economic Journal, 75(1), 188–207.
66. World Bank (1998). Assessing Aid: What Works, What Doesn't, and Why. New York: Oxford University Press for the World Bank.
67. World Bank (2014). Philippine Economic Update Pursuing Inclusive Growth through Sustainable Reconstruction and Job Creation. Poverty Reduction and Economic Management Unit Philippine Country Office East Asia and Pacific Region. Report No. 83315-PH. World Bank.

Table 1: Descriptive Statistics

Variable	N	Minimum	Maximum	Mean	Std. Deviation
GDP Growth	516	.26	.91	.5402	.15444
FDI	530	-28.62%	31.62%	1.46%	3.55%
ODA	497	-4.34%	55.80%	19.98%	8.54%

Table 2: Regression Results

Variable	Coefficient	Statistics
GDP Growth	-.0151 ** (.005)	-2.751
FDI	.00435* (.002)	2.415
ODA	.0035** (.00l)	3.420
Adjusted R^2	.634	
F-Statistic	47.564	

** Significant at the 0.01 level. *Significant at the 0.05 level. The numbers in parenthesis represent the standard errors corresponding to each coefficient.

Appendices

Appendix 1: Philippines Official Development Assistance (ODA) and GDP Growth 2009-2012

	2009	2010	2011	2012
Total ODA in US$ Millions	309,270,000	531,190,000	-180,520,000	5,140,000
GDP (current US$) (in millions)	83,908.2	91,371.2	224,095.2	250,182.0
GDP growth (Annual %)	5.0	6.7	3.6	6.8