

## In 2005, "PHILIPPINES IS IT!"

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There continues to be a lot of misery in the newspapers about the Philippine economic situation. Article after article talks about impending fiscal collapse, infrastructure deficiencies and horrific corruption levels. Key export industries like electronics and garments are said to be packing up for China. Continuing economic decline seems to be the only possible future for Philippines.

Don't believe it.

The economy grew by a solid 6.3% in the third quarter of 2004, hardly a recessionary environment. And, to business leaders in the key growth sectors like outsourcing, telecommunications and now mining, the near term outlook is among the best in the world. The reasons they provide for such optimism are not always obvious.

First of all, the continuing significant drop in value of the Philippine peso might seem like a dire harbinger of poor economic potential. But for export-focused companies, this has created a tremendous windfall that makes Philippines more competitive against other countries. A leading electronics CEO said to a group of us a couple months ago, "If the peso drops by 10%, then most of my costs drop by 10% and this is good for my business." Who can argue? Cynics have even stated that the one undeniable thing the Philippine government is doing to improve the competitive position of its country is to destroy the value of its currency.

Second, cost competitiveness and quality in competitors like India (for outsourcing) and China (for manufacturing) are declining. The growth in India (the king of outsourcing) has been so strong over the past few years that salary costs are rising out of proportion. At the same time, quality of service is now generally felt by industry leaders to be declining relative to Philippines as employee turnover rates have become destructively high and the quality of new hires is poor. Adding to all of this, the Indian rupee has increased in value relative to the US dollar making their labour even less competitive compared to Philippines.

In electronics, China has been a very powerful growth force over the past few years. Because of this, production costs among the coastal locations have risen dramatically and are now said to be approaching Philippine levels. Costs are still lower in the interior of the country but quality is lower also because of lack of experience. And, the Chinese currency is felt by most of the world's financial analysts to be greatly undervalued. What happens when the Chinese government stops buying billions of dollars worth of American treasury securities in its frantic attempt to hold down the value of its currency? It is only a matter of time until they stop this madness and allow their exchange rate to rise. This imminent adjustment will dull China's attractiveness relative to Philippines.

Third, infrastructure required for outsourcing (mainly telecommunication, power and office space) is said by almost all

analysts to be superior in Philippines to its main competitors.

Fourth, the mining industry will become an important contributor to economic development now that the Supreme Court of the Philippines has ruled in favour of the country's prosperity. Philippines is the 5th most mineralized country in the world and as metal prices are at historically high levels because of demand from China, progress will be swift. Various projects are already said to be standing by ready to start work. The economic impact of this industry should be felt over the next couple of years as long as there are no political interruptions.

Senior managers in the outsourcing industry are excited about their businesses and glad to be in Philippines. The only worries they speak of have to do with how to handle all the growth. The worldwide potential of services outsourcing has, according to them, so far only begun. "It's like 1965 in manufacturing," they say. Titanic growth is said to be coming over the next 2 to 5 years as companies become more comfortable with services outsourcing. Among all of this, Philippines will be front-and-center. One American who runs a large call center operation here said it best, "for right now, PHILIPPINES IS IT!"

Telecommunications is another growth industry that is gearing up for tremendous growth. Most people are aware that Philippines has established itself as a world leader in wireless communications. These days, industry leaders say GSM technology is "old news" and the next phase of development will be more profound still. Broadband wireless is the new technology and the zealots who run the Philippine industry are sprinting for world leadership in it. If these crazed revolutionaries are able to do for us in broadband what they did in GSM, then in 2 to 4 years Philippines will have fully functional telecom infrastructure that will be greatly superior in cost and performance to the old fixed-line technology that exists in most rich countries.

The electronics industry in Philippines – our largest export earner – will not expand much over next year but it is not going to disappear either. Business leaders say we will hold onto the business we have.

This situation may change over the longer term – say 4 or 5 years down the road – as China intensifies its grip on worldwide manufacturing. But for the time being, electronics is safe in Philippines.

For 2005 then, it seems that the various sunrise sectors will supply all of the growth we can handle and we will hold on to most of our current key export industries. As long as there are no significant shocks to the world economy, then the near term future looks very positive for Philippines. Our current economic growth rates exceeding 6% should be maintainable and possibly expanded.

