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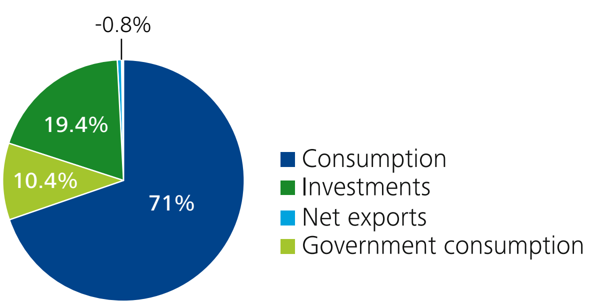
The Philippines
What's next for the Chosen Land?

The state of the nation

The Philippine economy grew by 6.6 percent in 2012. Economic growth was primarily fueled by strong domestic consumption, which accounted for 71% of GDP in 2012. Consumption was primarily driven by remittances from overseas Filipino workers (OFWs), which amounted to a record USD 21.39 billion in 2012 and the growth of the business process outsourcing industry, which generated more than USD 13 billion in revenue in 2012. Growth is expected to continue in 2013, led by the rapid pace of the construction (14% growth in 2012) and BPO sectors.

GDP Distribution in 2012



Beyond the short-term, the Philippines economy is predicted by Moody's to grow at a rate of as much as 8% in 2016 if the current pace of reforms and investments continues. However, President Benigno Aquino III will step down in 2016, so much will depend on how his transition is handled and whether the climate of good governance continues.

There are still challenges though – merchandise exports dropped significantly in early 2013 as demand for the country's semiconductor and electronics products fell – leading to suggestions that the recovery in export revenue may not be as strong as was being predicted by some analysts. However, the Government maintains that exports will still grow again in 2013 and points to a similar, if less dramatic, fall in exports that accompanied the start of 2012.

Credit to the country's strong performance is also attributed to the current administration, under President Aquino, and its policies to uphold the law and fight corruption. This is noticeable in the Philippines' rise on Transparency International's corruption perception index from 134th place in 2010 to 105th in 2012. The President's high approval ratings also provide him with the moral authority to govern and establish political stability.

Outlook for Consumer Business in the Philippines
Deloitte sees 4 major trends shaping the immediate future of the consumer business sector in the Philippines:

- Increasing consumer confidence and stability in government resulting in domestic consumption and consumer spending in affordable luxuries increasing dramatically.
- Consumer products and retail moving from selling based on price to selling based on branding and lifestyle propositions.
- Renewed focus by CB companies (especially fast moving consumer goods) to make capital investments in Philippines after many years of "stagnant growth".
- Intensifying trade spend and fight for on-shelf space as more companies invest in bringing new products into a revitalized growing market.

Outlook for the Financial Services industry
As the financial services market grows, Deloitte sees 3 key issues that the industry must focus on:

- Developments in the planned impacts of the formulation of ASEAN economic community.
- Increase in the usage of virtual channels in banks to lower distribution costs.
- Banks placing a greater emphasis on the build out of their fee income.

Outlook for the Technology, and Telecommunications Industry
The telecommunications and technology market continues to evolve, which Deloitte believes will spur the economy on:

- Revenue outlook for the telecommunication industry is more stable as service providers are shifting away from price-based competition. Wireless data services are gaining momentum and the completion of major network & IT modernization programs will allow stronger focus on quality and customer experience.
- Roll-out of high-speed 4G (LTE) mobile services is progressing, but due to the limited coverage and high device prices a stronger uptake is only expected in the mid-term.
- The BPO sector is seen to continue its strong growth track record in 2013 keeping the Philippines as one of the top global outsourcing destinations. The key is the appreciation of the Peso to the US$ driven by increased capital inflows due to the recent investment-grade rating for the Philippines and current US monetary policies.

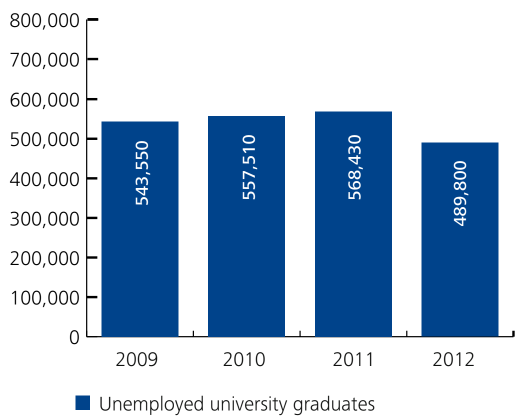
In spite of the recent advances that the country has achieved, its inadequate infrastructure is constraining further economic growth. The Philippines currently scores 3.19 out of 7 for infrastructure in the Global Competitiveness Report 2012-2013 released by the World Economic Forum. This lack of basic infrastructure such as roads, water and electricity has limited the flow of goods thus concentrating more than 60% of the country's economy in the 3 areas of Metro Manila (35.7%), Calabarzon (16.9%) and Central Luzon (9.1%). Standard & Poor's recently gave the Philippines a BBB- rating with a stable outlook, further boosting confidence.

Foreign direct investment (FDI) was a meager USD 2 billion (approximately 1% of GDP) in 2012. The prospect of it accelerating, since the Philippines obtained the investment grade rating from Fitch, is high. However, an investment grade rating may not necessarily equate to a significant increase in FDI because of the lack of perceived investment returns in locations without basic infrastructure.

Financing the growth of the country will thus largely be borne by the Government. Government spending needs to focus on integrating the geographies and spreading economic development across the country. The Government acknowledges this critical condition and has tapped on the private sector for support through Public-Private Partnerships.

The government continues to strive to revive the country's industrial sector, and manufacturing in particular, as this is seen as a key engine of long-term sustainable growth and employment for the significant number of unemployed Filipinos, particularly outside Manila. A recent report by the Asian Development Bank (ADB) showed that the services sector has contributed as much as 60% of total GDP growth in the last 30 years, in part thanks to the recent surge in BPO. The services sector provides over one-half of the Philippines output and employment but

Unemployed university graduates from 2009 to 2012



Source: NSO. Figures based on analysis by Deloitte labor productivity is well below that of the industrial sectors, which means that there may not be an opportunity to continue to provide well-paying jobs in the future. Indeed, for all its returns, the IT-BPO sector only employs just over 600,000 people of the labour force of 41 million in the Philippines-but is projected to grow to reach 1.3 million employees by 2016.

Based on the results of the Labor Force Survey of the National Statistics Office (NSO), approximately 490,000 individuals with university degrees are unemployed in 2012. This type of situation indicates a gap in job creation and a lack of employment opportunities for the higher-skilled workforce, which could result in a further 'brain drain'. Although these individuals would be able to seek employment opportunities abroad and spur the continuous growth of remittances, such a scenario is not sustainable. The improvement in 2012 is insufficient to reduce the country's reliance on OFW remittances and keep the talent in the country to generate innovations that would aid in sustaining the country's growth.

However, while unemployment is often cited as in the region of 7%, underemployment is considered to be as high as 20%.

Retail Industry

With a favorable outlook on the economy that is largely driven by consumption, the retail sector is expected to grow. Growth in 2013 in particular will tick even higher due to the impact of the elections and governance reforms. Although the majority of the population is in the low-income group, their combined annual earnings of USD 71 billion is still a significant force in the marketplace, particularly for basic goods and services. According to Business Monitor International, retail sales in the Philippines will grow from USD 32.17 billion in 2012 to USD 36.31 billion by 2016.

Retailers in the Philippines are interested in bringing in foreign brands that have been successful in Asia, especially in Southeast Asia, but not yet in the Philippines. These brands are mostly in the fashion and food and beverage sectors. This is due in part to the Filipino consumer's nature to be brand loyal, as supported by a study released by Neilsen in February 2013, and its Westernized culture which make the market more open and consumers fascinated by imported brands and concepts.

Growth in 2013 will be technology-driven. Retailers will be compelled to integrate technology in their marketing, sales, services and payment. As Philippine consumers become increasingly sophisticated, demand for higher quality products complemented with value-added services increases. The higher spending power of Filipinos would also require retailers to improve their payment systems to accommodate the increase in transactions.

Financial Services Industry

As with any developing market, a sound financial industry is essential in supporting the country's growth. There is a lot of liquidity in the system and interest rates remain low. This requires the financial industry and companies seeking to raise funds to appropriately manage its capital. Mismanagement of these funds may lead to undesirable consequences that would affect the country's overall growth.

Although there have been several mergers during the recent years, such as the one between two of the country's largest banks – the Philippine National Bank (PNB) and Allied Bank – these have still not resulted in a strong consolidation of the industry. According to the Economist Intelligence Unit, as of September 2012, the Philippines has approximately 700 banks, of which only 37 are considered as universal or commercial banks.

Regulations are also constantly changing due to the government's desire to increase governance and better regulate the industry: banks are now required to comply with Basel 3 by January 2014. Aggressive implementation of such regulations imposes pressure on smaller banks, which may potentially drive further consolidation.

Mobile Banking

According to a study released by Citigroup in April 2013, 75% of Filipinos are comfortable conducting banking transactions online. There is also significant usage of smart phones where, according to GFK in its July 2012 study, one in every three mobile phones sold in the Philippines is a smart phone. The increase in mobility at work and the faster pace of life, in combination with these trends, is an indication of the uptake of mobile banking among the Filipino consumers.

The country's reliance on remittances and money transfers gives rise to the threat of erroneous and/or inappropriate transactions. Mobile banking would be a viable platform for these services to address the potential lapses in control that may occur with physical transactions. Since the Philippine economy is concentrated in 3 main areas, mobile banking also allows the financial inclusion of regions that have minimal or no access to traditional banking facilities.

The unique state of the Philippine economy and the benefits of mobile banking provide a sound business case for mobile banking to take shape in the Philippines in the near future.

Find out more

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