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How the Philippines is planning for a brighter future

The Philippines has a booming economy, with enormous potential for further growth. *James Gavin* looks at the steps the Government and central bank have taken to make it an attractive destination for foreign investors.

The Philippines has emerged in recent years as one of the more dynamic Asia-Pacific economies, defying stereotypes with some impressive economic fundamentals. It is the world's 34th largest economy and the 13th largest in Asia, with the potential for considerable further growth. It is considered a "newly industrialized" country – one whose economy is transitioning from being based on agriculture to relying more on services and manufacturing.

The country has been one of Asia's fastest-growing economies in recent years. According to Government figures, gross domestic product (GDP) increased by 6.9% in 2016, 6.7% in 2017 and 6.2% in 2018. (By way of comparison, GDP in Emerging Asia grew by 6.5% in 2017 and 6.6% in 2018, according to OECD data.) Per capita income increased by 17% between 2016 and 2018.

Meanwhile, unemployment has fallen, partly as a result of the jobs created by foreign direct investment (FDI), which reached an all-time high of US$10.05b in 2017 (up from US$6.64b in 2015) according to central bank figures.

Analysts say the country has consigned its former reputation as the region's economic laggard to history. Indeed, by April 2019, Standard & Poor's and the Japan Credit Rating Agency had upgraded the Philippines' credit rating to just one step below an "A" territory rating.

There are challenges facing the Philippines, though, reflecting a more difficult regional environment in 2019. "The economy slowed down in the first quarter of 2019, and the trade war between the US and China is having an effect," says Joshua Kurlantzick, Senior Fellow for Southeast Asia at the Council on Foreign Relations, based in Washington, DC.

Strong demand

The World Bank (WB) highlights the Philippines' increasing urbanization, its growing middle-income class, and a large and youthful population. It's also worth noting that English is an official language and is taught in all the country's public schools.

The WB views the Philippines' economic dynamism as being rooted in strong consumer

Philippines fact file

Population: Estimated at 106,512,074 in 2018 (the 13th largest in the world)
Official languages: Filipino and English
Capital: Manila
Currency: Philippine Peso (PhP)
Land area: 298,170km²
Bordering countries: None
Natural resources: Timber, petroleum, nickel, cobalt, silver, gold, salt, copper
Nominal GDP: Estimated at US$354b for 2019
GDP growth: 6.2% YoY in 2018
Inflation rate: 3.3% YoY in March 2019 (2012-based CPI)

> "The Philippines is at the forefront in advancing reporting standards in the region, having adopted IFRS as early as 2005.

demand supported by improving real incomes and robust remittance inflows from expatriate workers. Business activities are buoyant – particularly in the services sector, and in industries including real estate, finance and insurance.

Such characteristics help put the Philippines squarely on investors' radar screens, helped along by a domestic market that is buoyed by rising population growth; in 2017 it grew by 1.4%, the same rate as Malaysia and higher than Indonesia.

President Rodrigo Duterte, who came to power in 2016, is committed to improving the country's infrastructure in order to create jobs and business opportunities, and boost economic growth. His "Build, Build, Build" program is made up of 75 major projects covering transportation, power, water supply and flood management. This mammoth endeavor envisages a total spend of at least 8t pesos (US$150b). The Government is planning to increase infrastructure spending to approximately 7% of GDP by 2022.

It has also focused on pushing through reforms, such as the 2017 Tax Reform for Acceleration and Inclusion Act. This revision of the tax code aims to make the system simple and fairer, and includes new revenue-raising measures that are designed to help fund the Government's infrastructure program.

"Duterte has courted foreign investors, particularly in infrastructure, as part of a broader attempt to strategically rebalance the Philippines economy," says Kurlantzick. "A lot of that investment has not come through yet, but they are clearly trying to woo more smart investment from China."

Bureaucratic obstacles

Despite the outreach to foreign investors, prominent investors active in the Philippines caution that some restrictions remain. They highlight issues in government effectiveness; for example, some Build Build Build projects have faced bureaucratic and procedural obstacles.

There are also economic problems to deal with, including rising inflation, growing public debt and a trade deficit, with some commentators suggesting that the country needs to develop new industries to remain competitive internationally. There are also wide disparities in income and growth between the country's different regions and socioeconomic classes.

Nevertheless, investors see the direction the country is heading as positive. For example, efforts to make it easier to do business have garnered plaudits. The Ease of Doing Business Law was fast-tracked and is now on the statute book. It constitutes different types of application that commit the Government to act within three, seven or 20 days, depending on the complexity of the application. One feature of the law is that if these deadlines are not met, there is an escalation process that enables companies to report the issue to the appropriate government agency.

Driving good behavior

As for corporate governance, standards are rising, with scores on the Asean Corporate Governance Scorecard improving in recent years. Particularly strong improvements have been seen in two categories: disclosure and transparency, and the responsibilities of the board.

The central bank, Bangko Sentral ng Pilipinas (BSP), has implemented consumer and investor protection standards which are expected to be embedded into the corporate culture of BSP-supervised institutions. It also expects that these reforms will drive good behavior and greater market discipline, addressing conflicts that are inimical to the interests of financial consumers.

The Philippines is at the forefront in advancing financial reporting standards in the region, having adopted IFRS as early as 2005. This makes it attractive to multinational companies that prefer to use IFRS rather than multiple domestic standards.

The BSP is planning further steps to improve standards. It has also been strengthening its anti-money laundering and know your customer policies for financial institutions, given the involvement of a local bank in the hacking of Bangladesh's central bank in 2016. It has also increasingly made officers directly accountable for violations, with hefty fines imposed and the board replaced in that incident.

In May 2017, the BSP and the International Finance Corporation (IFC), a member of the World Bank Group, signed a Memorandum of Understanding to enhance capacity and raise environmental, social and corporate governance standards among Philippine banks. IFC will support the BSP in improving its assessment tools to promote good governance and effective risk management in the banking system. It will also contribute to the BSP's capacity-building initiatives, particularly in applying the proportionate legal and regulatory framework.

Such moves should help to improve investor confidence in a growth-oriented economy that intends to go on defying stereotypes. ■

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Viewpoint: A commitment to good corporate governance

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Over the last two decades, the Government, regulators and businesses in the Philippines have been increasingly focused on and committed to promoting corporate governance. Driven primarily by the Philippine Securities and Exchange Commission (SEC) and the central bank (BSP), corporate governance has become a significant matter for most boards, in particular for financial services companies.

The SEC mandated that companies exercise and report on corporate governance practices through the issuance of the Code of Corporate Governance in 2002. This was superseded by a revised code in 2009, with amendments in 2014. Additionally, the SEC released the Philippine Code of Corporate Governance Blueprint in 2015, which was followed by the new Code of Corporate Governance for Publicly Listed Companies in 2016. It has also announced its alignment with the ASEAN Corporate Governance Scorecard principles.

While the latest SEC guidelines apply to all listed companies, the financial sector has additional regulations promulgated by the BSP through its Manual of Regulations for Banks and Manual of Regulations for Non-Bank Financial Institutions, which are updated regularly to reflect improvements in regulatory requirements. These provide extensive guidance and compliance information to help financial institutions in the Philippines promote transparency and accountability.

In August 2017, the BSP issued a circular to provide enhanced corporate governance guidelines for BSP-supervised financial institutions, amending the Manual of Regulations for Non-Bank Financial Institutions. This raises the bar on what is expected from the board of directors and risk management systems, and provides term limits for independent directors.

In addition to its partnership with the BSP, the International Finance Corporation (IFC) has been working with the SEC in training 250 representatives of publicly-listed companies on best practices in implementing a new corporate governance code that took effect on 1 January 2017. The code, which aims to increase the board responsibilities, competence and commitment of company directors, is among the latest examples of IFC's contribution to the development of corporate governance policies and regulations in more than 30 countries worldwide.

While there is still much work to be done to truly achieve sustainable and effective corporate governance in the Philippine financial sector, all stakeholders have demonstrated their resolve and commitment to promote a strong, healthy and stable banking and financial system.

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