

# Philippines

The economy avoided recession owing to resilient domestic industries and stable overseas remittances which continue to fuel domestic demand; deal values managed a slight increase in the first half of 2009 as a result of domestic transactions. Deal activity in 2010 is expected from delayed IPOs and possible consolidation in the business process outsourcing industry.



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## Current Environment

GDP growth slowed to 0.4% in the first quarter of 2009 as the Philippines felt the impact of the global financial crisis. The industrial and manufacturing sector contracted by 6.6%, exports contracted sharply by 18.2% and investments in durable equipment declined by 17.9%. In response, the Philippine government increased spending on infrastructure projects from 2.6% of GDP to 3.8%.

The country's fiscal position however is in a delicate situation as revenue-generating agencies have showed declining performance in the first five months of the year. Collections from the Bureau of Internal Revenue and Bureau of Customs have declined by 6.6% and 7.4% respectively. The government has continuously raised the budget deficit ceiling for 2009, and now it is at Php250 billion or approximately 3.2% of GDP. Prior ceilings were 2.5% and 1.2%. Before the onset of the global downturn, the 2009 estimate was 0.5%.

The slump in the country's top export, electronics, is believed to have bottomed out after a 33.2% slump in April. Despite the big drop from the prior year, month-on-month figures show a 3.9% growth in April to US\$1.62 billion, indicating some recovery in the sector. Industry organisation officials from Semiconductor and Electronics Industries in the Philippines, Inc., believe that the second quarter of 2009 will be stronger than the first quarter.

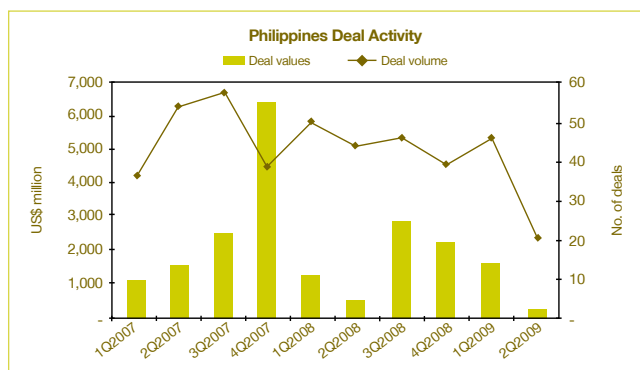
Despite the slowdown, the Philippines has been identified as one of the few countries to have not been severely impacted by the global financial crisis. Sectors that have continued to be resilient and contribute to growing the economy include construction, agriculture, transportation, communications and storage, mining, and business process outsourcing.

Inflation levels have come down significantly from the multi-year high that was reached in 2008. The Central Bank expects June inflation levels at 1.2% to 2.1%. This is a significant decrease from 3.3% recorded in May, and the 12.5% peak in August of last year. Inflation levels are targeted to fall within 2.5% to 4.5% for 2009, and are expected to remain subdued into 2010. Once a global economic recovery begins, stronger inflation is expected to return.

Inward remittances grew 2.6% to US\$5.5 billion for the first four months of the year as there was continued demand for Filipino workers in the global market. Remittances from abroad supported domestic consumption and kept the economy buoyant.

The composite index of the PSE has improved to 2,431.4 points as of 3 July 2009, an increase of 30% from the 31 December 2008 closing of 1,872.85 points. The Philippine peso to US dollar exchange rate remained stable with the rate ranging between Php47.390 to Php48.371 per US dollar.

## Deal Activity



Source: Thomson Reuters, based on total domestic, inbound and outbound deals announced as of 30 June 2009.

Deal values in the first half of 2009 increased by 5% to US\$1.81 billion, compared to the same period in 2008. This came on the back of a 144% increase in domestic deal value (US\$1.57 billion), largely related to deals in the banking and telecommunications sectors.

Total value for inbound deals shrank 78% to US\$211 million, while total value for outbound deals shrank 80% to US\$26.5 million.

The number of deals in the first half of 2009 shrank 30% to 66 deals, compared to 94 deals in the first half of 2008.



## San Miguel Corporation

As indicated in prior issues of this bulletin, San Miguel Corporation (SMC) continues to be an active participant in the Philippine deal landscape, as it disposes of its holdings in the food and beverage industry and explores opportunities in other industries.

Most significantly, Q-Tech Alliance Holdings Inc. acquired a 19.91% stake in SMC from Kirin Holdings Co Ltd, for Php39.6 billion (US\$823.4 million), which was the biggest transaction in the Philippines during the first half of 2009.

### *Telecommunications, Real Estate, Packaging*

- SMC plans to acquire Express Telecommunications Inc., a mobile cellular phones wholesaler.
- In July 2009, SMC signed a subscription agreement with Liberty Telecoms Holdings Inc. to increase subscription from 20% to 53% in Liberty Telecoms for Php1.8 billion.
- San Miguel Properties Inc., a majority-owned unit of SMC, acquired Maison 17 Properties Inc., a real estate development firm, from Wallmasters Inc. for Php300 million (US\$6.38 million).

SMC plans to acquire the remaining 30% stake in San Miguel Rengo Packaging Corp. from Rengo Co. Ltd for Php250 million (US\$5.20 million). SMC also plans to raise its stake by a further 6.7% in Mindanao Corrugated Fibreboard, Inc.

### *Food and Beverage Disposals*

- SMC will be disposing its international beer operations and domestic beer brands to San Miguel Brewery, Inc., a 94.25%-owned unit of SMC.

### *Banking*

- East West Banking Corp fully acquired AIG Philam Savings Bank, as well as Primus Finance & Leasing Inc. These two transactions were estimated to have a total value of Php2 billion (US\$42.3 million). East West Banking Corp. also agreed to acquire Philam Auto Finance & Leasing Inc. from American International Group Inc.
- In April, GT Capital Holdings Inc. acquired a 25.01% stake in Metropolitan Bank & Trust Co. from Grand Titan Capital Holdings Inc.

- In May, Banco de Oro Universal Bank Inc. and GE Capital signed a definitive agreement to transfer GE Money Bank into Banco de Oro. GE Capital will also acquire a 1.5% stake in Banco de Oro with an option to increase its stake up to 10%.

Other significant transactions include:

- In July, Pilipino Telephone Corp., a subsidiary of Smart Communications, Inc., completed the acquisition of 223 million common shares of Manila Electric Co (MERALCO) from First Philippine Utilities Corporation, formerly known as First Philippine Union Fenosa, Inc., for Php20.07 billion.
- Metro Pacific Investments Corp. agreed to acquire a 10.17% stake in MERALCO from PLDT Beneficial Trust Fund.
- Abacus Securities Corp. was granted an option to acquire a 4.82% stake in Atlas Consolidated Mining & Development Corp. for Php500 million (US\$10.6 million).
- In March, state-owned Development Bank of the Philippines and Land Bank of the Philippines jointly acquired a 56% interest in Metro Rail Transit Corp. (MRT). Both banks are planning to raise their interest in MRT from 56% to 76%.

## Outlook

### *IPO Activity and Elections*

IPO activity remained absent in the market during the first six months of the year, which is similar to the second half of 2008. We expect that activity will pick up towards the second half of 2010 at the earliest, when the economy is estimated to have recovered and the political and regulatory uncertainty that will come prior to the June 2010 national elections will have dissipated.

The sole exception to the expected postponement of IPOs could be the Pilipinas Shell Petroleum Corp.'s IPO, which is due to occur in the third quarter of this year. Shell has long been asked by the Energy Department to list at least one tenth of their shares, in compliance with the 1998 Oil Deregulation Act.



### Energy Privatisation

The state-owned Power Sector Assets and Liabilities Management Corporation (PSALM) had scheduled the bidding of two large power assets, the coal-fired Sual (1000 MW) and Pagbilao (700 MW) in May and June this year. The offers from the participating bidders, San Miguel Energy Corporation and Therma Luzon Inc., did not meet PSALM's reserve price for the assets. A new round of bidding will take place later this year.

### Contact Center Companies

Despite the global downturn, the business process outsourcing industry continues to do well in the Philippines. A recent PwC survey of major players in the contact center industry showed that in 2008, industry revenues grew by more than 20% and agent headcount by 13%. However, the survey also showed that operating margins have weakened, especially among companies with less than US\$10 million in annual revenue or those with under 600 agents. The industry may be ripe for consolidation among smaller players, who need scale to better manage their operating expenses.

### Growth in bank lending

Bank lending in the Philippines continued to grow with the support of the Bangko Sentral ng Pilipinas (BSP). Loans of commercial banks for use in economic activity grew by 3.1% to Php1.78 trillion (US\$37.5 billion) in May 2009 from Php1.748 trillion (US\$36.3 billion) in December 2008. The key sectors of the economy where there was growth in lending include fishing, electricity, gas and water, transportation, storage and communication, financial intermediation, public administration and defense, health and social work, and other community, social and personal services.

Further, the BSP has reduced key policy interest rates by 200 basis points since December 2008 to spur economic activity. ■