

The Philippines as a Regional Center for Shared Services

A combined paper by

Peter Wallace, EIU Philippines, Inc. and **Nigel Lucas**, Colliers Jardine

(Reprinted with permission from Business Review, the Business Digest of the European Chamber of Commerce of the Philippines, February 2000)

The almost frighteningly rapid change in the way business is being conducted is forcing companies to do a major rethink of their corporate strategies. Globalization and technological advances (particularly in the e-commerce field) are creating new ways to do business that were inconceivable less than a decade ago. And perhaps the most important concept to grasp is that change is now the constant. Ten years ago there were no centralized services in the Philippines-or anywhere else. Today, just from EIU's limited survey, we identified 14 companies that have moved some of their services into centralized operations in the Philippines. And the pace can only accelerate. McKinsey estimates global demand will reach US\$180B by 2010. But, it could well be higher. While Hong Kong and Singapore remain preferred locations for multinational companies' (MNCs) regional headquarters, the Philippines is fast becoming an attractive spot for back-office functions. Put simply, the cost-benefits to setting up remote or shared services centers in the Philippines are enormous, according to many already in the country. Wage costs for white-collar employees are estimated at 10%-20% of those in the United States, while the Philippine workforce is highly educated, proficient in English and easily adaptable-all important pluses in a rapidly changing global economy. Having missed out on previous Asia-Pacific booms, the Philippines is by now well aware of the benefits it has to offer MNCs seeking to gain from its abundant supply of quality, low-cost and skilled labour. On top of these benefits, the Philippine Government is providing attractive incentives to MNCs (such as tax holidays)-an added reason as to why a number of companies have already chosen to locate their call centers or shared services centers for time-consuming and labour-intensive functions in the country.

THE PHILIPPINES AS A LOCATION

The world-wide technological advancements of recent years mean remote or shared services centers no longer have to be located anywhere near a customer or a company's home base. They can also be set up elsewhere with relative ease once a location is selected.

Cost-effectiveness is perhaps the most important factor to consider when selecting a location. But the quality of a workforce, the availability of space, the stability of government, the regulatory environment, the taxsystem and the quality of telecommunications infrastructure are also key considerations.

While the Philippines has its share of disadvantages, most of the above are working in its favour and help place it far ahead of other regional countries competing for a share of this relatively new-found trend, such as Australia, China, Indonesia and Malaysia. And those factors that are not in the Philippines' favour are being worked on by the Government.

An annual survey of business executives by Hong Kong's Political & Economic Risk Consultancy has found the Philippines and Philippines to rank highest in the region for quality, cost and availability of skilled labour. Key advantages of locating in the Philippines as cited by foreign investors include:

- **Steady Economic Growth** -The Philippines has been one of the least affected by the regional financial crisis that started in the last quarter of 1997. After posting a 0.5% contraction in 1998, the Philippines is poised for a rebound with GDP growth of around 2.5% in 1999.
- **Competitive Labour Costs** - labour rates in the Philippines are among the most competitive in Asia, with the minimum daily wage rate currently pegged at P198 (US\$4.95). Wages for skilled labour are even more attractive.

- **Skilled Labour** - The Philippines offers skilled, educated and highly trainable manpower, and is a cost-effective producer of medium-andhigh-technology goods. The country's literacy rate is high and there exists a large pool of computer-literate manpower to draw from.
- **Multilingual Society** - Although Filipino is the national language of the country, English is widely used in education and business. The Philippines is the third-largest English-speaking country in the world. Moreover, the existence of a sizeable number of Chinese families in the country can meet the requirement for an understanding of various Chinese dialects, including Hokkien and Mandarin. Spanish is also spoken by many.
- **Liberal Business Environment** - Major monopolies and cartels have been abolished and various sectors have been liberalised, including banking, shipping, insurance, telecommunications and wholesale trade. Investment laws are opening more investment areas to 100% foreign equity. Retail trade liberalisation is in the process of legislative deliberation.
- **Incentives** - The Philippine Government has prepared a package of fiscal and non-fiscal incentives to attract foreign investors. Depending on the nature of business, incentives range from income tax holidays to duty-free importation of capital equipment. The corporate income tax was reduced to 33% from 35% in 1997 and will be further reduced to 32% in 2000. Companies in special economic/export zones are subject to an overall tax rate of only 5%.

There are, inevitably, some difficulties, but these are being worked on. They include:

- **Telecommunications** - The difficulty of inter-connectivity between competing telephone networks is now being addressed, and should lead to rapid growth in telephone density-which now has stands at nine lines per 100 persons. By way of comparison, telephone densities in Thailand and Malaysia are four to eight times higher. Five cellular telephone providers are tapping the pent-up demand, the largest having a subscriber base of some 900,000.
- **Air pollution** - Long criticised for its air pollution, the problem is being rectified with the recent passage of the Clean Air Act. The bill requires oil firms to bring down the aromatic content in unleaded gasoline and prohibits the import and sale of leaded gasoline and engines requiring its use.
- **Infrastructure** - Traffic congestion has long been a fixture of Philippine roads and highways. Recognising its detriment to economic growth, the Government has initiated a massive infrastructure program that includes mass rail systems, new airports, elevated highways and highway extensions.

SOME POSSIBLE SERVICES THAT COULD BE CENTRALIZED

Accounting	Application Development
Training	Inventory Control
Customer Services	Technology Support
Programming	Marketing Services
Call Centers	Server Management
Web site design	Data Processing
Human Resources	Management Information
Engineering Drawing	Systems
Administration	Animation

LANGUAGE REQUIREMENT

There's clearly benefit in centralizing services as a number of companies have now shown. For now it will be in English. But later it well might not be. There's a company in Flanders, Lermont and Harispie (H&P) that is well on the way to making voice recognition, in any language, part of a computers capability. The Economist recently revealed that there was a new "black box" that can accept something like 42,000 characters and convert them into the 1's and 0's computers need. The impact of this? The thousands of Chinese characters needed to speak Chinese will be now input table into computers. English will no longer be the essential input medium. Computers will even be able to talk back. So automatic call centers, computerized operator services, messaging, and so on will all be handling able by machine in the not too distant future.

That means there's a window of opportunity for the Philippines and Philippines that will soon be eroded. It already is on data entry-where the Chinese are now beginning to do it. Customer service, telemarketing etc will remain somewhat longer (unless you are targeting the Chinese market), but even there it wouldn't be surprising if automatic translation by another speaking "black box" takes that advantage away, humans are still needed and the western world likes not only their own language-more and more this is English-but also their own accent. That's one reason why the Philippines is generally preferred to Philippines for customer service centers. Americans resist talking to someone on the phone with an Philippinesn accent "It sounds foreign". And getting rid of idioms is harder for Philippinesns than for Filipinos. But Philippinesns can, and do, learn other accents.

Where will that leave the Philippines?

The recent Asiaweek survey on this subject mentioned 23,000 Philippinesns now working for MNC's in Philippines that they identified, with a forecast demand of 1.1 million by 2008. That's the competition. That's what the Philippines must face, and face-down. Nonetheless, for now the economies of scale and mass production techniques that revolutionized manufacturing are now revolutionizing services.

Centralizing services reduces total head count (economies of scale) and can now be done because of computers and their interconnection (mass production). So, backroom services will seek lower-cost, English-speaking, computer-trainable people. It all sounds very exciting but the Philippines has missed the boat on two revolutions (agriculture and industrial) now. For it not to miss this one too it will need to move faster, more boldly, more imaginatively. A reality the government has recognised, and has promised to address.

CHOICE OF LOCATION

Some of the parameters needed in choOutsource-Philippinesng where to locate a backroom center include

1. An English-speaking workforce
2. A computer literate (or trainable) workforce
3. A relatively low-cost workforce
4. A productive workforce
5. Enough of them to meet (future) demand
6. Excellent telephone lines (or equivalent)
7. Competitive telecom toll rates
8. Convergence
9. Competitive office support costs (rent, electricity, services, supplies, equipment etc, etc)
10. Decent living conditions

But perhaps the most important criterion is that everybody is happy. And, in this regard, there's been no one who wishes they hadn't moved their services here. The frustrations are more than offset by the satisfaction over the work performed. And that, of course, is what business is all about Doing a good job.

Of the parameters mentioned the Philippines has the first 6 equal to or better than anyone else. But number 7 is sporadic, and 8 has PLDT being dragged kicking and screaming into today's modern reality (volume is the name of the game). While 9 has the Philippine government totally nonplussed as to what it's all about-and how to do it. Does it violate the constitution by not discriminating about what's on the line-or the airwaves (wireless communications is the other revolution).

Because at the core of the Information Revolution is telecoms, not the computer, important as it is. It's the interconnection that's doing it. The Philippines is still mostly stuck in archaic rules and regulations, in inhibiting franchises, in separation of services that can no longer be separated, and

in stultifying bureaucracy (not that the Philippines bureaucracy is much better, in fact, probably worse). The private sector is making the changes. It's the Philippine government that will make or break this chance. And it will have to move swiftly if the chance is not to be lost.

As to 11, expats rank Manila up near the top.

Another attraction of the Philippines is company loyalty. Employees tend to stay. That means less training cost, fewer errors, better productivity. At TIMEX some years ago worker turnover was 1% per year. In their Bangkok plant it was 2% per month. They moved all the production to the Philippines.

BUSINESS ENVIRONMENT

As to the general business environment, a survey by EIU-Philippines Inc. of some 45 MNC's in September summarises it pretty well.

1. Inefficient infrastructure
2. Corruption
3. Convoluted bureaucracy
4. "Crony" competition
5. Rigid labor environment
6. High (comparative) cost
7. Dealing with the court system
8. Small market
9. Crime
10. Unfair competition
11. Slow processing of goods (BOC, etc)
12. Land ownership
13. Globalization, as barriers come down
14. Obsolete plants (vs elsewhere)

Most of these apply equally well to service companies. The government must not only address these in the priority listed but also must provide the necessary support systems and effect actions that include

- Sending a clear message of stability and consistency
- Providing adequate infrastructure (particularly telecoms)
- Lowering telecoms costs
- Providing a competitive incentive structure
- Educating Filipinos
- Reducing red tape
- Removing archaic rules and regulations

COMPANY EXAMPLES

Apart from freely allowing the entry of foreign investments into almost all areas of the economy, the Philippine Government grants incentives for projects that it considers highly desirable. Major incentives include those granted by the Board of Investments, the Philippine Economic Zone Authority, the Subic Bay Metropolitan Authority and the Clark Development Corporation.

To better describe how many are taking advantage of the benefits and incentives the Philippines has to offer, a handful of case studies are offered below

American Online (AOL)

AOL, the giant US-based Internet Service Provider, has facilities in the Clark Special Economic Zone, a former US airbase about 80 kilometers north-west of Manila. AOL has a workforce of 600

Filipinos who receive 10,000-12,000 e-mail inquiries per day, of which 80% originate from the United States.

Caltex Shared Services

The US-based oil company has moved its world headquarters to Singapore but has located accounting functions in Manila's alternative financial district, Ortigas Centre, handling five regional countries. Its center is also starting to absorb human resources work. Employing 60, the number is expected to double by the end of the year.

Andersen Consulting

Andersen Consulting has a solutions center in the Makati CBD, the country's financial hub, which is the biggest of its 40 centers around the world. Started in 1989 with 12 employees, the Manila operation currently employs 515 developing and customising software for US-based clients in the financial-services and utilities fields.

Sealand

Sealand Asia has been executing its regional administrative functions at Wynsum Corporate Plaza in Ortigas since 1998. Citibank has just started work at its new regional call center in Eastwood City, a 15-hectare master planned community along E. Rodriguez Avenue, near the Ortigas business district. Citibank Square has been built to service primarily its credit card operations.

Procter & Gamble

Procter & Gamble recently established a regional center in the Makati CBD focusing on Accounting Services for its Asia Pacific Operations.

Fluor Daniel and Bechtel

A substantial part of Fluor Daniel's regional design work is carried out at its center in the Asian Star Building in Filinvest Corporate City (FCC), Alabang. FCC is located approximately 30 kilometers south of Makati. Bechtel has some 1000 engineers doing engineering drawings for its worldwide affiliates

CATEGORY OF SERVICES	EXAMPLE	LOCATION	DESCRIPTION
Corporate Back Office	Caltex	Ortigas	Treasury, human resources
Data Processing	Sealand UPS	Ortigas Alabang	Shipping documents Shipping documents
Data Processing	SPI Technologies	In close proximity to the International Airport	Digitize library card catalogues, Digitize technical manuals, Maintain UK voters' lists, Digitize archive for US Dept. of Justice
Engineering	Bechtel Fluor Danie Parsons	Makati Alabang Makati	Blueprints, engineering designs Blueprints, engineering designs Blueprints, engineering designs
Internet Service Center	Barnes & Noble AOL	Eastwood City Clark Special Economic Zone	Process Internet orders Answer customer e-mail
Medical Transcription	Kumar	Makati	Transcribe doctors' dictation
Software	Andersen Consulting	Makati	Developing and customising software
Corporate Shared Services	Procter & Gamble	Makati	Shared accounting functions
Corporate Technology Support	Citibank	Eastwood City	Systems Development and Support
Website Center	Asian Sources Media	Fort Bonifacio	Maintain large website

CONCLUSION

As is evident from the advantages listed above, the Philippines has much to offer the MNC seeking a cost-effective location for back-office functions—a fast-growing business trend in the Asia-Pacific area. While Hong Kong and Singapore will remain prime locations for regional head offices, they are simultaneously outsourcing out in the areas of customer support and accounting. Emerging countries like the Philippines offer a viable alternative. With its highly educated, English-proficient and low-cost workforce, coupled with a sound economy, liberal business environment and attractive government incentives, the Philippines is poised to take a significant share of the market for regional shared service centers. It may have missed out on previous booms, but it is not likely to let it happen again.