**Philequity Corner (June 25, 2012)**
**By Valentino Sy**

## Greece is the Word

"Greece is the word." All eyes were on Greece as the financial world was counting down to June 17, the date of Greek elections. With the victory of the pro-bailout New Democracy party, the world averted a possible financial armageddon. A win by the leftist anti-bailout party, Syriza, would have been disastrous since they signalled that they would not honor the agreements which were part of the bailout package. This spectre of an immediate and disorderly Greek exit would have such far-reaching consequences that all central banks geared up for it in case it happens. Although austerity measures are still expected to be renegotiated, a sudden Greek removal from the European Union has temporarily been averted.

## Not Out of the Woods

Compounding a Greek economy that is shrinking, Spanish long term bond yields have gone up to unsustainably high level. As deposit flight continues in bailout recipients Greece and Spain, Italy may be the next country asking for a bailout. Amidst all this, some countries are already ring fencing their own economies. The Swiss central bank has instructed Credit Suisse and UBS to increase their capital reserves in order to cope with a full-blown Euro region crisis. However, European leaders have already begun drawing a roadmap out of the crisis. As early as last year, it was clear that the EU would have to take steps towards forming a banking union and a fiscal union. While we are not out of the woods yet, the victory of the pro-bailout party in Greece is a step in the right direction.

## A Long Journey

In a recent trip to Greece, one of our directors noted that there are very deep-seated problems in Greece. For instance, as he was talking with some Greek workers, he could not help but notice their anger against their own politicians. Another eye-opener was the disparity in salaries. While corporate employees in the private sector get taxed, government employees are able to work tax-free even though the nature of their job is the same. In addition, the Greek Orthodox church seems to have significant influence on government affairs which leads to preferential treatment. Like a welfare state, people are not incentivized to be as productive as they can because the government will provide for them even when they are unemployed. These structural issues are present in Italy, Spain and other socialist countries as well. Given that it will take years to undo all of these, Euro region as a whole has a long journey ahead of itself before it is able to reinvent itself as a stable fiscal and monetary union.

## Philippines Remains Resilient

With Greece and Spain taking the spotlight, stock markets have experienced increased volatility and significant drawdowns. Although the PSEi did go through a corrective phase, this is just a hiccup compared to the dismal YTD performance of most major markets. For instance, Greece and Spain are down 11% and 20%, respectively. Last Friday, all Asian markets were down except for the Philippines and Malaysia, which both have strong domestic economies. In fact, the Philippines is up 17.1% YTD while our Philequity fund is up 18.4% over the same period. If we examine the performance of the PSEi since the market bottom in March 17, 2009, we will see that the PSEi had risen 290%. On the other hand, our Philequity fund outperformed the market, rising an enormous 320% over the same time frame. Even over the past 18 months, the Philippine economy weathered crisis after crisis, from civil revolts in the Middle East to a Japanese earthquake. Through all these, the Philippines has remained resilient.

There are many reasons for the country's strength amidst adversity, some of which we will enumerate below:

1. Strong trust in President Noynoy Aquino's government
2. Lower prices for crude oil and major agricultural commodities
3. High GDP growth relative to the rest of the world
4. Soon-to-be launched PPP program to boost our infrastructure
5. Robust domestic consumption
6. Booming BPO sector
7. Growing OFW remittances
8. Strong Philippine peso
9. Ratings upgrade to a positive outlook, bringing us closer to the coveted investment grade rating
10. Positive current account balance and shrinking budget deficit

**From Debtor to Creditor**

For the past 40 years, the Philippines has been a net borrower from the IMF, especially as a result of the 1997 Asian financial crisis. In 2006, the country was finally able to pay off all its loans to the IMF as implementation of continuing reforms made our economy stronger. Last week, the BSP announced that from being a borrower from the IMF, we are now lending them a whopping $1 billion. This event is so significant since the Philippine economy is now robust enough to help the more troubled nations. Unfortunately, this shift from being a debtor to a creditor was not treated with much importance by the media, which had chosen to relegate it to a short article in the inside pages of the business section. Given how significant this paradigm shift is, we believe that this event deserves no less than a frontpage headline article in every newspaper.

**Buy Philippines**

With these in mind, we think it best to focus on what is right with the Philippines than what is wrong in other countries. Although the Philippines is not immune from any global crisis, it is at least partially insulated because of the factors mentioned earlier. Using the same logic, we advise investors not only to focus on the Philippines but also on stocks exposed mostly to our own economy. Utilities come to mind because whether or not Spain defaults will not affect electricity or water consumption in the country. Other stocks with domestic revenue streams, such as retail and infrastructure companies which have most, if not all, of their business here will also be able to grow their earnings even if the problems in the rest of the world escalate. Just as we have reiterated in previous articles, we suggest that investors stick with companies that have growing earnings and good business models.

**Greece and Grease**

To end this article, we leave you with a portion of the song "Grease is the Word." Composed by Barry Gibb of the Bee Gees, the song was inspired by the 1971 stage production "Grease" that is one of the longest running Broadway musicals of all time. This song was the centerpiece of a blockbuster musical movie of the same name in 1978 starring John Travolta and Olivia Newton-John. Although the song tackled adolescent and social issues, surprisingly enough if you change the word "grease" to "Greece", the words in the song are very relevant to what is happening in that country right now. So, we want to dedicate the following stanzas of the song to our readers and our friends in Greece.

Grease is the word, is the word that you heard
It's got a groove, it's got a meaning.

We solve our problems and We see the light
We got a lovin' thing, we've got to feed it right
There is a danger we can make it so far
We start believin' now that we can be who we are.

Grease is the word.
It's got a groove, it's got a meaning
Grease is the time, is the place, is the motion.
Grease is the way we are feeling.

We take the pressure and we throw away
Conventionality belongs to yesterday
There is a chance that we can make it so far
We start believin' now that we can be who we are - grease is the word.

Grease is the word, is the word, is the word...

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