THE NEXT BIG THING IN SOUTHEAST ASIA

Danny Yuan
Chief Operating Officer
ManpowerGroup Asia Pacific & Middle East
ASIA PACIFIC REGION ON THE RISE

In 2014, we are seeing a relatively new trend take hold in the Asia-Pacific region. Major companies, including Fortune Global 500s, are starting to locate their operations in Malaysia, Indonesia and the Philippines, the way they once flocked to China. Now, however, the reason for the move is different. Offshoring to China was largely driven by the availability of cheaper labor. While the cost of labor is one factor influencing why companies relocate to Southeast Asia, there are other considerations. Among them are demographic trends—mainly a steady supply of younger workers and the prospect of making in-roads into the region’s growing consumer markets.

WHY THESE COUNTRIES, ABOVE OTHERS?

Malaysia, Indonesia and the Philippines, referred to here as the “MIP” countries, have relatively large economies (ranking #16, 34 and 38, respectively out of 213 countries and territories). That speaks to large populations, high productivity and significant market potential. At the same time, wages are relatively low and education rates are high in relation to wages, especially in the Philippines and Malaysia. Combine these indicators with a projected influx of a large number of new workforce entrants and an emerging middle class, and it becomes apparent why forward-thinking companies are considering investments in the region.
Wages

Average wages in the MIP countries, are relatively low. In contrast, wages in other Asian countries have been rising to the point that relocating to, or remaining in these markets may no longer be as financially appealing. At the same time, China had the time and infrastructure to develop a sophisticated manufacturing capacity—something many other countries have yet to match. A recent special report in The Economist noted that “…wages in China and India have been going up by 10-20 percent per year for the past decade, whereas manufacturing pay in America and Europe has barely budged. Other countries, including Vietnam, Indonesia and the Philippines still offer low wages, but not China’s scale, efficiency and supply chains."

Given that companies are already relocating major operations to the MIP countries, it is reasonable to expect efficiencies will follow shortly.

<table>
<thead>
<tr>
<th>Wages: At-a-Glance</th>
<th>Malaysia</th>
<th>Indonesia</th>
<th>Philippines</th>
</tr>
</thead>
<tbody>
<tr>
<td>GDP (PPP, Current Int’l $, 2013)ii</td>
<td>$692.3 B</td>
<td>$2,388.4 B</td>
<td>$642.8 B</td>
</tr>
<tr>
<td>GDP Annual Growth (2010)i</td>
<td>7.2%</td>
<td>6.1%</td>
<td>7.6%</td>
</tr>
<tr>
<td>GDP Per Capita (Constant 2005 $)ii</td>
<td>$13,213</td>
<td>$3,880</td>
<td>$3,560</td>
</tr>
<tr>
<td>GDP Per Person Engaged (1990 $)i</td>
<td>$24,857</td>
<td>$11,461</td>
<td>$8,667</td>
</tr>
<tr>
<td>Real Avg Monthly Wages in USD (Aug. 2008)i,iv</td>
<td>$524.95</td>
<td>$90.00</td>
<td>$125.76</td>
</tr>
</tbody>
</table>

Demographics

Another significant driver of the increased relocation to MIP countries is demographics. The percentage of the population that is working-age in the “relocation triad” is comparable to the rest of the world, ranging from 61 percent to 66 percent of the population. Compared to China (at 73.5 percent), the percentage of the working-age population actually seems quite low, and may even be concerning. What matters most and makes the biggest difference, is what will happen in the next decade or so. The share of China’s population of young people, ages 0-14, is only 19.5 percent. Meanwhile, Malaysia, Indonesia and the Philippines enjoy much higher ratios of 29.1, 26.6 and 34.3 percent respectively, pointing to a demographic dividend in the MIP countries and a demographic deficit in China. The impact is clear: incoming talent will be far more available in the MIP countries than in China, which was the center of attention in years past.

<table>
<thead>
<tr>
<th>Demographics: At-a-Glance</th>
<th>Malaysia</th>
<th>Indonesia</th>
<th>Philippines</th>
</tr>
</thead>
<tbody>
<tr>
<td>Population (2014)i</td>
<td>30.01 MM</td>
<td>253.6 MM</td>
<td>107.7 MM</td>
</tr>
<tr>
<td>Working Age Population (15-64) (2014)i</td>
<td>65.7%</td>
<td>67.3%</td>
<td>61.8%</td>
</tr>
<tr>
<td>Youth Population 0-14 (2013)i</td>
<td>29.1%</td>
<td>26.6%</td>
<td>34.3%</td>
</tr>
<tr>
<td>Employment to Population Ratio (2012)i</td>
<td>58.6%</td>
<td>63.1%</td>
<td>60.1%</td>
</tr>
<tr>
<td>Unemployment Rate (2010, 2011, 2012)i</td>
<td>3.4%</td>
<td>6.6%</td>
<td>7.0%</td>
</tr>
<tr>
<td>Labor Force by Education – Secondary (2008, 2010)i</td>
<td>55.7%</td>
<td>22.3%</td>
<td>39.2%</td>
</tr>
<tr>
<td>Labor Force by Education – Tertiary (2008, 2010)i</td>
<td>24.2%</td>
<td>7.1%</td>
<td>28.0%</td>
</tr>
</tbody>
</table>
Market Presence

The reasons companies and industries enter a market may differ. In some cases, an industry may choose to enter a market solely for the sake of establishing its presence there. This is especially true in markets with a rising middle class, such as Southeast Asia. That explains why, for example, automakers have invested considerably in Russia despite the relatively higher cost of wages there. Since the country has one of the fastest growth rates of car ownership per capita in the world, manufacturers have a lot to gain. We are seeing similar examples in Southeast Asia. For example:

**Motor Vehicles:** In some Southeast Asian countries, there is limited tax on the import of automotive parts as compared to the import of fully manufactured cars. That is to say, importing parts and assembling vehicles in country is far less expensive than importing fully assembled motor vehicles. Add to this rapid growth in vehicle ownership in a particular country, and it is easy to see why manufacturers might consider locating their assembly plants there. In fact, a recent Boston Consulting Group report argues that the MIP countries are among the most promising for this type of investment.⁴

**Consumer Goods:** White goods (e.g., appliances, linens), air conditioning, luxury goods and brand-name products will likely see rapid uptake in MIP countries and throughout Southeast Asia as the region’s middle class continues to expand. These items typically come with high import taxes, so the confluence of a growing middle class and relatively low wages makes the MIP market appealing for manufacturers.

**Fast-Moving Consumer Goods:** Non-durable goods like pre-packaged food, toiletries, consumables and household products are also likely to see increased production and consumption in MIP countries as the middle class continues to expand. These are items that are often inefficient to import regardless of tax, especially when manufacturing in-country is a viable option.

MIP countries are also attractive destinations for fulfilment and distribution given the higher education/lower cost factors already noted.

With the exception of outsourced call centers in the Philippines, which are credited with contributing to the country’s economic growth,⁴ there is no single industry driving investment in the MIP countries. Unique local economic factors and the availability of natural and human resources likely contribute to the presence of manufacturing in these countries. At the same time, global companies from technology to health care, retail and pharmaceuticals and many others are seeing opportunities in the triad.
IS RELOCATION TO MIP COUNTRIES INEVITABLE?

Companies are already moving into the MIP triad, and it is not just a matter of labor arbitrage. The fact that relocating companies are developing new markets, while accessing less costly labor pools, demonstrates their increased sophistication.

“It is no longer about moving somewhere just for cost savings, but about the total opportunity.”

In addition to the factors already mentioned, investment in MIP countries is also being stimulated by favorable regulatory, political and practical considerations. For example:

- **Malaysia** is politically stable and considered geographically appealing, with easy access to north Asia and a well-developed infrastructure. The country’s public policy is favorable to foreign investors with no limitations on where investments originate. Many tax stimuli (such as incentives for setting up operational headquarters in the country and double deduction of certain expenses) and protections are also available to foreign investors, so the overall environment is an attractive one. Shared services, such as global administration support, financial services, and IT help desks are increasingly popular and provide added motivation for investment.

- **Indonesia’s** economy is the largest in Southeast Asia. It also offers political stability. Recent reforms, including favorable tax and customs reforms, have contributed to the country’s economic surge and stimulated significant amounts of investment.

- **The Philippines** offers significant tax incentives and simplified import/export procedures. From a geographic standpoint, its port-based economic zones provide advantages in shipping across the Pacific. Finally, industry investments—particularly in the area of business process outsourcing—are driven by the fact that the country has one of the largest English-speaking populations in the world.
### SAMPLE INVESTMENTS IN MIP COUNTRIES

Investment in MIP countries is also stimulated by favorable regulatory, political and practical considerations. Below are brief examples how companies leverage the workforce opportunities in these countries.

**Malaysia**
- Largely due to geographic advantages, Huawei Technologies, a global ICT solutions provider, recently established a data-hosting and logistics hub in Malaysia.\(^x\)
- Halliburton is expanding its existing manufacturing and technology center in Malaysia, growing its current space by nearly one-third and adding 350 jobs.\(^{xii}\)
- India’s largest drug manufacturer, Ranbaxy Labs, announced it will establish a new manufacturing facility. Access to the local health care market as well as other Eastern Hemisphere markets was cited as key rationale.\(^{xvi}\)
- Japanese technology firm NTT Communications established a data center in Malaysia to take advantage of a growing market, low electricity rates and a stable infrastructure.\(^{xvi}\)

**Indonesia**
- Hankook Tire is investing $1.17 million in a new tire factory, selecting Indonesia over Thailand and Vietnam due to its large domestic market.\(^{xi}\)
- Austria’s Lenzing AG is opening its fourth viscose fiber factory in Indonesia with its total investment worth $146.77 million.\(^{xiv}\)
- Japanese electronics manufacturers Panasonic, Sanyo and Toshiba have either expanded their investments or shifted factories from other countries to Indonesia for better access to the domestic market.

**Philippines**
- Many Japanese electronics companies—including Canon, Brother, Furukawa Automotive, FujiFilm—have opened manufacturing operations in the Philippines.\(^{xi}\)
- In 2012, adhesives manufacturer Cemedine announced plans to establish a wholly owned subsidiary in the Philippines.\(^{xv}\)
- The Japanese Chamber of Commerce and Industry of the Philippines Inc. estimates that the number of Japanese firms operating in the Philippines could increase by 200-300 businesses by 2017.\(^{xiv}\)
- Philippine conglomerate Ayala Group is betting on strong domestic growth with investments on promising sectors such as supermarkets, hospitals and power plants.\(^{xix}\)
- In the financial sector, Canada’s Manulife Financial and Sun Life Financial have become among the top foreign insurance companies in the country.
CHALLENGES WITH RELOCATING TO THE MIP COUNTRIES

As the saying goes, if it were that easy, everyone would do it. While we are seeing growing numbers of companies entering these markets, they do face numerous risks and challenges that must be considered and, to the extent possible, mitigated. A brief summary of these considerations is provided here.

**Malaysia**

Only 52.8 percent of the local graduates are employed 6 months after finishing their studies. Not unlike many countries in the world, this is due to the mismatch in the skills university graduates have versus what employers need.\textsuperscript{xx}

The skilled talent pool in Malaysia is low at 27 percent compared to regional peers like Singapore, Taiwan and Korea.\textsuperscript{xxi} Malaysia has set forth a national agenda to make the country a high-income nation by 2020,\textsuperscript{xxii} but according to estimates, it will require at least 45 percent of the workforce to be highly skilled. Clearly, there is much work to be done. To compound matters, the country has faced problems with low levels of students passing English exams—only 16 percent scored highly in 2012.\textsuperscript{xxiii} This may become a challenge as multinationals consider relocating their operations to the country.

**Indonesia**

While labor arbitrage is available, there is high workforce mobility and turnover due to the lack of the right talent available at the right time. Anecdotally speaking, we hear of companies offering 12 month sign-on bonuses for talent, and salaries are increasing quickly.

Bribery and corruption have also presented problems. A 2011 Gallup Poll found that 9 of 10 Indonesians believed government corruption to be widespread. This poses a unique problem for multinational companies that seek assurance from global suppliers regarding their ethical business practices. Finally, natural disasters, including earthquakes and the 2004 tsunami, are present in the minds of companies looking to locate in the country.

**Philippines**

Businesses in the Philippines are limited by nationality requirements. For example, procurement requirements for the public sector mandate that providers of goods and services must be 60 percent Filipino-owned, while infrastructure services must be 75 percent Filipino-owned.\textsuperscript{xxiv}

Another challenge is the cost of doing business in the market. Infrastructure can be particularly costly in the Philippines, largely because of the price of electricity, the highest in all of Asia.
TAKING ADVANTAGE OF THE OPPORTUNITIES, WHILE MITIGATING THE RISKS AND CHALLENGES

Moving operations into a new market is hardly a turnkey operation. It is essential to have the right people in place, on the ground, including experts who can navigate local markets, regulatory environments and cultural nuances. Companies should also have access to the right talent communities—both local and global to understand what is needed and when.

While the challenges in MIP countries are considerable, there are many opportunities for forward-thinking companies to mitigate them. Following are a few examples of approaches that ManpowerGroup has developed to enable its clients to leverage opportunity in Southeast Asia. For example:

• Given the magnitude of the talent shortage in Malaysia, a customized Manpower Academy solution was developed for the Malaysia unit of a leading global computer systems consulting firm. Sourcing Manpower Academy students, the “Recruit, Train, Deploy, Manage” program provides extensive technical training in high demand help-desk technologies. The result is a 94 percent retention rate.

• In Malaysia, a shortage of English-speaking technical talent poses a serious challenge. Frequently, candidates will have one skill, but not the other. To close the gap between the skills taught in schools and the skills required on the job, Manpower Academy was launched to enable high-potential candidates to boost either language or technical skills. The Academy includes a language “boot camp,” on-campus training for university students, and a program to reach untapped talent. Since the program was first piloted in 2010, more than 9,500 ICT candidates have been placed with Manpower Malaysia clients.

• During a business reorganization, a leading global provider of information, financial and media services required 200+ immediate hires and had no internal capacity to manage volume HR requirements in its Philippine operations. With extensive knowledge of the local market, ManpowerGroup’s recruiters were able to implement a sourcing, assessment and interview strategy that outperformed the client’s days-to-hire performance metrics. Another challenge ManpowerGroup is able to mitigate is attrition. Business process outsourcing attrition in the Philippines is as high as 50 percent. Through continuous client and candidate engagement and the development of feedback loops, attrition can be reduced significantly, in this case to a mere 2 percent.

9,500 Candidates placed with additional training from Manpower Academy

94% Retention rate following implementation of “recruit, train, deploy, manage” program

2% Attrition Rate
Candidate engagement programs helped reduce attrition rates by 96%
IT IS TIME TO CAPITALIZE ON NEW OPPORTUNITIES

If the metrics are any indication, opportunities abound in Southeast Asia. The vast majority of companies moving into the region are well aware of the regulatory and environmental challenges as well as of the opportunities. In the Human Age, talent is the biggest differentiator, and MIP countries offer a unique and advantageous environment. Companies able to find ways to fully understand the markets will be several steps ahead of their competition when it comes to their greatest asset—talent.

In times of compressed margins, faster time-to-value and pervasive economic uncertainty, the worst business decision that an organization can make is to continue business as usual.

At ManpowerGroup Solutions, we are looking for markets that offer the infrastructure and demographics to provide a sustainable platform that enable businesses to grow and employees to thrive. That is our barometer. In the MIP countries, we have spent years making in-roads into those markets and developing communities of talent. As a result, we are uniquely poised to support companies as they seek to compete in this region and around the globe.

ABOUT THE AUTHOR

Danny Yuan joined ManpowerGroup China in 2003. Danny has held several senior management positions, including Commercial Director, Practice Head, Corporate Affairs Director, and Operations Director, leading the company’s service network development, government relations, financial management, professional practice organization and other related operations. In December 2012, he was promoted to Chief Operating Officer overseeing business operations within Asia Pacific & Middle East.
REFERENCES

ManpowerGroup Solutions prides itself on the ability to analyze and forecast trends impacting the world of work and the marketplace. As skills and available talent change and marketplace priorities shift, it is critical for organizations to have timely, relevant, and accurate insights into the global workforce. With this in mind, we make significant investments to understand and share observations around macro-trends (e.g., demographics, employment, economics) and their likely impact on talent sustainability.

Join the conversation on ManpowerGroup Solutions’ social media channels:

LinkedIn ManpowerGroup
Twitter @MpGrpSolutions