Driving fund penetration in the Philippines

Regulatory changes, investor education and use of technology are seen as critical to the growth of the country's mutual fund industry.

Like many other developing economies in Asia, the share of financial products among Filipino households remains very low.

However, with growing affluence and favourable demographics, and a maturing market, it's also clear that it is a matter of time before financial products adoption becomes more commonplace.

After a series of high-level conversations with leading product gatekeepers and asset management executives in the Philippines, it seems the role of the regulator will be one of the determining factors in how quickly the products industry evolves.

LEVEL PLAYING FIELD NEEDED

One regulation that has been pending for over a decade – but which would provide a big boost to the funds industry – is the Collective Investment Scheme (CIS) Law.

This proposes to create a much-needed level playing field.

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Currently, the most popular kinds of collective investment schemes in the country are unit investment trust funds (UITFs), mutual funds (MFs) and variable universal life insurance policies (VULs).

The UITF industry is estimated at around PHP 800 billion (USD16 billion), with about PHP 600 billion accounted for by money market funds. The MF industry, meanwhile, is estimated at around PHP250 billion.

At the moment, all three schemes – MF, UITFs and VULs – are governed by different regulators: the securities watchdog, central bank and insurance authority, respectively.

Because tax implications on each scheme are different, there is considerable tax and regulatory arbitrage among these investment products.

UITFs, for instance, are allowed to have feeder fund structures while MFs aren't. Yet MFs can be a fund of funds. VULs, meanwhile, can invest in other types of assets as well.

The tax treatment is also very different for each scheme. In particular, the tax regime for MFs is considered the most repressive. To give one example, MFs are subject to documentary stamp tax and corporate income tax due to its legal structure, while UITFs are not.

A common CIS Law would clearly help the situation by providing a uniform regulatory framework.

And the securities regulator is, under the CIS Law, expected to take charge of UITFs and MFs.

PUSHING THE PRODUCT ENVELOPE

This is also expected to lay the legal framework for new investment products such as ETFs, real estate investment trusts (REITs) and special purpose entities or trusts to raise capital for infrastructure projects.

Currently, both UITFs and MFs offer equity, bond, balanced and money market funds. Given the volatility in equity markets over the past 12 to 8 months, however, market practitioners believe that money will be predominantly parked in money market funds.

Some practitioners suggested that one way to further enhance the appeal of UITFs, for example, is to link them with bank accounts.

And with the launch of feeder funds investing in US and Japanese markets in recent years, investors also have an avenue to diversify.

When it comes to VULs, although there is some investor interest in the Philippines, one of the concerns about these products that some market participants share is that they are being promoted as investment, not insurance-led, solutions. As a result, VUL sales have become highly-dependent on the state of equity markets.

COUNTING ON PERA

A recent development that product and investment specialists in the Philippines expect to give a fillip to the asset management industry is PERA (Personal Equity and Retirement Account Law).

In short, this is a long-term investment savings plan designed to help Filipinos with their retirement planning. It will achieve this by channeling these funds into appropriate financial products.

> **"Another way to drive broader investment participation is by ensuring mandatory pension schemes through the PERA platform."**

Another way to drive broader investment participation is by ensuring mandatory pension schemes through the PERA platform. Indeed, market participants believe that this is essential.

BETTER UNDERSTANDING

This all relies on the country overcoming a fundamental hurdle that plays its part in holding the market back – the low financial literacy levels of Filipino investors in general. This needs to change, say practitioners, if the wealth management industry wants to have a chance of increasing fund penetration. In the current landscape, the UITF market, by far the most popular collective investment scheme, is dominated by institutional money.

There is a consensus among market practitioners, therefore, that one way to drive more funds to be bought is to embark on a large-scale financial literacy programme.

This could be jointly sponsored by the government and the industry.

DIGITAL DRIVE

This is not to say that efforts are absent entirely. Many institutions already engage in investor training sessions through their branches, for example, with the help of seminars and even webinars.

Digital channels are also growing in popularity as a way to offer investment solutions online to new – and especially younger – customers.

Increasingly, online platforms not only offer product information but also comparison data to help investors weigh up different financial products and assess their risk appetites.

Some firms are also using social media networks such as Facebook to reach out to younger audiences. ■