Vanguard Report

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Philippines Shows Potential for Cloud and Datacenter Growth

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451 Research

S&P Global Market Intelligence

Introduction

As the global hyperscale cloud providers and social media giants look to extend their reach farther into Asia, a number of countries have emerged as areas of interest: Indonesia, Malaysia, the Philippines, Thailand and Vietnam. Indonesia has already seen increased investment, while the rest are beginning to gain traction. Local telco and datacenter providers in the Philippines are bullish, while at the same time, the country is on the receiving end of new international connectivity in the form of undersea cables, as well as further development of domestic fiber. For its part, the Philippine government is working to make its energy sources more sustainable, and the country is home to several attractive customer segments, all of which creates an interesting landscape on which the hyperscalers could build.

The Take

As we look at the Philippines through the lens of digital transformation, many of the pieces are in place for the market to take off, and the country's datacenter industry is showing signs of a growth spurt in the wake of the COVID-19 pandemic. Growing hyperscale deployment has moved the needle in the datacenter scene in the Philippines, signaling demand for larger amounts of space and power. It is still early days to know where the market is headed, but the attention gives the local players a much-needed boost to carry out new developments.

Of course, there are many factors for companies to consider when entering a market or increasing investment in an existing market, not the least of which are the country's economic might and various strategic risks. In this view, the Philippines is on competitive footing with its peers, and in fact, it is likely that all five of the countries mentioned in the introduction will see further interest from hyperscalers and global enterprises. As it stands, we estimate the datacenter market in the Philippines, which can be an indicator of overall technology growth, to experience a CAGR of 13% in operational space between 2020 and 2025.

Macro Social and Economic Considerations

When evaluating whether to enter a new country, companies may consider any number of strategic factors, such as the current political climate, medium- and long-term economic outlook, current legal framework and proposed legislation. The tech industry specifically will also consider renewable energy availability, internet penetration rates, cloud readiness and availability/quality of connectivity options.

Strategic risk refers to any risk or collection of risks that may have material impact on a company's operational and investment decisions. The Philippines fares well among its peers in a comparison of the overall strategic risk of each country. When compared directly with Indonesia, which has received the lion's share of investment thus far, the Philippines scores slightly better in terms of economic factors.

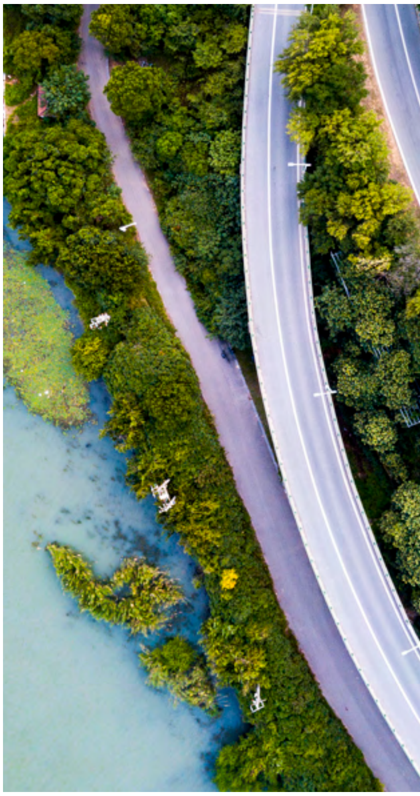


Figure 1: Comparison of strategic risk

Rank	Geography	ISO country code	Risk change date	Post 1 year outlook	Overall	Political	Economic	Legal	Tax	Operational	Security
29	Malaysia	MY	03 Nov 2022	→	1.4	1.5 →	1.5 ↘	1.2 →	1.6 →	1.4 ↗	1.2 →
62	Vietnam	VN	03 Nov 2022	→	1.7	1.1 →	1.8 ↘	1.9 →	1.6 →	2.7 →	1.3 ↗
98	Thailand	TH	03 Nov 2022	→	2.1	2.4 →	1.7 →	1.8 →	1.9 →	2.6 ↗	1.9 →
104	Indonesia	ID	03 Nov 2022	→	2.2	1.9 ↗	2.3 ↘	2.3 →	1.8 →	2.7 →	2.2 ↗
115	Philippines	PH	03 Nov 2022	→	2.3	2.0 →	1.7 →	2.4 ↗	2.0 ↘	2.9 →	2.7 →

Low			High			Extreme
0.7	1.5	2.3	3.1	4.3	6.4	10

Source: IHS Markit, part of S&P Global.

The Philippines is home to more than 111 million people, making it the 13th-most-populous country in the world, and second only to Indonesia among the emerging countries discussed above. In 2021, the Philippines' GDP was $394 billion, representing 5.5% year-on-year growth. S&P Global Market Intelligence expects GDP growth of 7.1% in 2022 as the Philippine economy recovers from the COVID-19 pandemic and normalcy gradually resumes, and an average of 6.1% growth during 2023-2025. The outlook is supported by economic reopening, economic reforms, a large and young population, a growing middle class and increasing urbanization. The Philippines' real GDP growth is expected to be competitive among other Southeast Asian economies, slightly behind that of Vietnam but ahead of Indonesia, Malaysia and Singapore.

The Philippines has stepped up efforts to enhance its attractiveness and promote foreign investment with the passage of landmark reform bills in the past two years. The major reform bills include amendments to the Foreign Investment Act, Public Service Act, Retail Trade Liberalization Act, and Corporate Recovery and Tax Incentives for Enterprises. These changes will promote greater economic liberalization and boost investor sentiment. Already, foreign direct investment surged 81.9% in 2021, reversing a 21.3% decline in 2020. Furthermore, the Philippines joins 13 other countries as a member of the Indo-Pacific Economic Framework for Prosperity, an economic initiative launched by the United States to support fair and resilient trade, among other goals.

Beyond its economy, the Philippines is at the forefront in Southeast Asia for renewable energy policy. The country was the first to implement a renewable portfolio standard (RPS) to support the continued growth of renewables. The Department of Energy signed into effect the RPS rules and guidelines in December 2017, requiring distribution companies to procure a percentage of their energy sales from renewable sources. Since that time, renewable energy development has been inhibited by the fact that foreign ownership of renewable projects has been capped at 40% (except for biomass). As of September 2022, however, that limitation has been lifted.

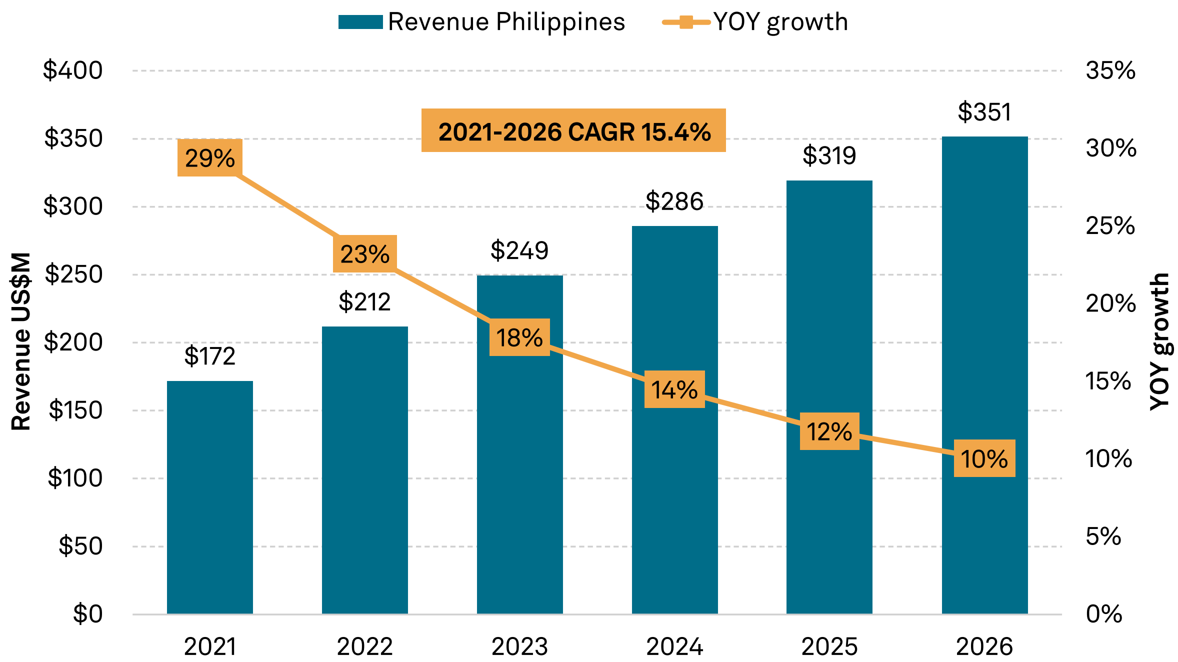
The Department of Justice (DOJ) issued a legal opinion that full foreign ownership in the renewable sector is permitted under the 1987 Philippine Constitution. The DOJ said "inexhaustible" sources of energy such as wind, hydro and solar are not covered by the 40% foreign ownership limit under the Constitution. The Department of Energy has sought the DOJ's opinion as the administration of President Ferdinand Marcos Jr. plans to increase the share of renewables in the Philippines' energy mix from 23.4% in 2021 to 35.0% by 2030 and 50.0% by 2040. Currently, distribution companies are only required to source 2.52% of their annual electricity supply from renewable sources. Marcos emphasized the need for additional power supply from renewables and nuclear energy in his first State of the Nation Address in July 2022 and met with executives of renewable energy firms during his working visit to the United States in September 2022. To date, renewables account for approximately 29% of the country's generation capacity, roughly half of which comes from hydroelectric.

Cloud Growth

The Philippines has an early-stage cloud computing market with an expected CAGR of 15.4% for 2021-2026, according to 451 Research's Cloud Computing Market Monitor. The Philippine government has been among the earliest in the region to initiate cloud transition, starting in 2013. The Department of Information and Communications Technology followed up with an amendment to its Cloud First policy in June 2020 to emphasize the guidelines on cloud computing in the public sector.

Beyond this initiative, the pandemic has been a catalyst for cloud adoption in the Philippines, a situation that is familiar in many markets across the world.

Figure 2: Aggregate cloud computing market forecast: Philippines



Source: 451 Research's Market Monitor, Cloud Computing.

Amazon Web Services (AWS) launched its office in Manila in May 2016, soon after those in Bangkok and Kuala Lumpur. At present, AWS has content delivery network and edge points of presence in the Philippines. AWS Outposts, which extend AWS infrastructure, services and APIs to customer premises, have been available in the market since 2021. Earlier in 2022, however, Manila was named as one of the metros for the AWS Local Zones, along with other cities in the region, including Bangkok and Hanoi.

– Similarly, Microsoft has CDN POP, as well as a Front Door edge location in Manila. Microsoft has worked on the digitalization of the public sector since 2017. Among the government departments that use Azure services are finance, education, science and technology, justice, social security, internal revenue and municipal governments, as well as the central bank BSP.

– Google has a smaller presence in the Philippine market compared to AWS and Azure. The company set up its Manila office in 2018 and is expected to roll out its Transfer Appliance service soon in the Philippines.

Of the Chinese cloud providers, Alibaba Cloud went ahead of the pack when it launched its first datacenter in October 2021. The Chinese hyperscaler, which says it serves more than 200 companies, has recently indicated plans to step up investment in the Philippines. Meanwhile, Tencent Cloud has been available in the Philippines since 2022 through resellers including ClinkIT Solutions and Acclivis.

Customer Segments

Until the recent expansion of the hyperscalers, the financial services sector was the largest customer vertical for datacenters, followed by the business process outsourcing sector and other multinational firms. Overall, nearly three-quarters of the customer base in the Philippines is represented by multinational or foreign firms.

Content and OTT providers, meanwhile, mostly leverage the connectivity services at the datacenters. Market dynamics are shifting as more companies embark on digitalization of their IT infrastructure, many with a hybrid cloud approach.

For instance, digitalization of the banking sector signals some potential headroom for hyperscalers in the Philippines over the near term. As of mid-2021, more than 41 banks in the Philippines had received approval from Bangko Sentral ng Pilipinas, the central bank, to switch to cloud-based core banking, according to data from the Asian Development Bank. Security Bank, UnionBank and Bank of the Philippine Islands are among the financial institutions that have adopted cloud infrastructure. Likewise, most fintech and digital payment startups — the largest segment of the startup ecosystem in the Philippines — are running on cloud platforms.

Cloud Readiness

The Philippines has a growing leased datacenter market. Providers ePLDT, the enterprise arm of PLDT, and Globe Telecom, through its joint venture with STT GDC and Ayala Corp., are the two largest operators in the market, maintaining 10 and six facilities, respectively, nationwide.

Almost all of the providers in the market offer services beyond colocation, such as managed hosting services, web hosting, application hosting and, increasingly, more managed cloud services. Wholesale offerings are limited because the majority of the facilities available are inadequate to meet the requirements of hyperscale customers. Existing providers are anticipating sustained interest from hyperscalers in this market. Growing hyperscale deployment could very well lead to further development of the wholesale datacenter segment.

The growing profile of the Philippine market has also drawn the attention of other datacenter operators. In 2021 and 2022, the entry of Digital Edge, SpaceDC, EdgeConneX and Bee Information Technology PH affirms that the Philippines is on the right track for growth.

Subsea Cables

Eleven subsea cable networks run through the Philippines, and nine of them are either fully or partially owned by PLDT or Globe Telecom. The current pipeline shows that the Philippines will have two more international subsea cables by 2024: Apricot, funded by Meta Platforms (Facebook), and Google CAP-1, funded by Amazon and Meta.

Notably, Indonesia and the Philippines have become hotbeds of subsea cable investment in Southeast Asia. The multiple undersea cable projects have certainly contributed to the growth of the datacenter markets in these two countries. Tech companies have largely skipped Malaysia due to its unfavorable cabotage policy that does not allow foreign vessels to repair cables in its waters.

Furthermore, the east coast of the Philippines — the eastern seaboard of Mindanao, in particular — is considered a strategic neutral territory for operators to avoid the South China Sea, which remains a contested area for China and a few Southeast Asian nations including the Philippines.

Meanwhile, market leader PLDT has made a few large investments in submarine network cables in its bid to boost connectivity speed of its services: namely, the Asia Direct Cable system ($75 million investment, to go live in 2023), the Apricot cable system ($80 million investment, to go live in mid-2025), and the Jupiter cable system ($137 million investment, came online in 2021).

The 9,400 km Asia Direct Cable is a partnership between several telecom providers including China Telecom, China Unicom, National Telecom, PLDT, Singtel, SoftBank, Tata Communications and the Viettel Group. The submarine cable connects China, Japan, the Philippines, Singapore, Hong Kong, Thailand and Vietnam. PLDT, as part of a consortium with Google and Meta, developed the 12,000 km Apricot submarine cable that will connect seven international landing points, namely the Philippines (Davao & Baler), Japan, Taiwan, Guam, Singapore and Indonesia. A separate consortium including Amazon, Meta, SoftBank, PCCW Global, PLDT and NTT Communications developed the 14,000 km Jupiter cable that spans from Japan to the Philippines and the United States.

PLDT is the Philippines' largest fully integrated telecommunications company that offers a wide range of digital services across the country's most extensive fiber optic backbone, subsea cable systems, cellular networks, internet exchanges, and world-class data center facilities, including the Philippine's largest hyperscale data center in Sta. Rosa City rising by end-2023.

Catering to over 76M network subscribers and 200,000 enterprise customers, PLDT operates robust, world-class digital infrastructures to power the digital future of every Filipino. Invest in the Philippines today with PLDT.
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About the Author

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As a Principal Research Analyst for 451 Research, a part of S&P Global Market Intelligence, Dan Thompson provides insight into the multi-tenant datacenter (MTDC) market space. He currently leads the research in APAC and Latin America, while also assisting in the coverage of North America. Dan is particularly focused on MTDCs that are trying to move up the stack to offer additional services beyond colocation and connectivity. These services may include disaster recovery, security, various forms of cloud and other managed services. He also assists the 451 Research Information Security group when their interests overlap.

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