▶AP's STEAM COST RISES

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Metro Pacific Investments' (MPI) Rail and Road Projects Take Off

Unfolding Infrastructure Portfolio. MPI's Public-Private Partnership (PPP)-oriented growth drivers, will kick in 2013, key of which is MPI's likely first light rail project. This is to be done by MPI's consortium with Ayala Corp., an unnamed local fund, an operator yet to be selected, which will collectively bid for the $650mn or Php28bn (project cost) 11-km LRT 1 South extension on Build Transfer Operate (BTO) arrangement with the government. The consortium is putting up 30% in equity or $200mn (Php8.6bn) while the balance will be on project financing, Php19.3bn. Internal rate of return eyed by the consortium is 13%, to be achieved through a revenue sharing with the government via subsidy and a tariff hike. LRT's daily traffic is 500k passengers or at an average fare of Php12/head, the company is estimated to generate Php2bn in yearly topline. Government adds about Php40/head in subsidy to keep the losing light rail company afloat.

Road and Rail projects Are Biggest Investments in Next 3-4 Years. MPI's next biggest capex for road projects is the Php21bn connector road linking North Luzon Expressway (NLEX) with South Luzon Expressway (SLEX). The others include the Php9bn Harbor Link road and the Php10bn Segment 9 connecting C5 to NLEX to begin construction by 4Q2012.

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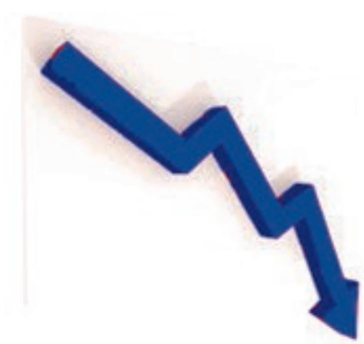
Market Stats

For the week ending September 7, 2012

Top Gainers			Top Losers		
Stock	Price	% w-o-w change	Stock	Price	% w-o-w change
AGI	12.22	3.74%	GLO	1,100.00	-3.93%
BEL	4.85	2.75%	JFC	96.30	-3.70%
CEB	60.00	2.04%	DMC	56.05	-3.20%
URC	62.10	1.97%	BPI	72.75	-3.00%
SM	719.00	1.41%	MWC	26.25	-2.96%

PSEi	Value	% w-o-w Change
Closing	5,201.32	0.10%
High	5,221.29	0.44%
Low	5,148.56	0.66%
Value T/O (in mn Php)	18,523.25	-3.20%
Foreign Buying (mn USD)	16.89	-122.19%

Interest Rates Still Down by Year-end



Interest rates are still predicted to drop toward year-end as last August's inflation rate spike to 3.8% is likely to be a blip. The inflation rate will begin to slow this month from what many economists consider to be this year's peak in the month of August. Higher inflation boosts the odds the BSP will keep its key policy rate steady. But should Philippine capital inflow pick up with the US doing a third round of quantitative easing toward yearend, the BSP may still opt to hold the rates steady to temper peso appreciation. Philippine bonds and the peso have both rallied on the view the BSP will keep its policy rate at record low of 3.75% and reduce borrowing costs further to protect the Southeast Asian nation's economy from a global slowdown.

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GSM PM CLOSE September 7, 2012
1.40yr 4.00% unchanged Dealt @ 2.40% for Php102Mn
4yr 4.175% (0.025 bps down)
4.83yr 4.30% (0.05 bps down)
9.22yr 4.75% (0.035 bps down) Dealt @ 4.725% to 4.715% for Php360Mn
9.37yr 4.75% (0.035 bps down) Dealt @ 4.715% for Php407Mn
18.9yr 5.60% (0.05 bps up) Dealt @ 5.525% to 5.56% for Php15.017Bn

GSM PM CLOSE September 7, 2012
23.3yr 5.64% (0.01 bps down) Dealt @ 5.645% to 5.62%for Php655Mn
25yr 5.65% (0.03 bps up) Dealt @ 5.60% for Php636Mn

RTB Tranche September 7, 2012
15:14.5yr 5.29% (0.01 bps down) Dealt @ 5.27% to 5.26% for Php1.019Bn
19.5yr 5.61% (0.02 bps up) Dealt @ 5.60% to 5.58% for Php4.803Bn

Note: GSM is Government Securities Market

(Rail and Road Projects…continued from page 1)

All these add up to Php41bn worth of capex, which may reduce to Php32bn depending on the configuration of the connector road, where a third of project cost or Php9bn-10bn will be taken up as equity by MPI and the rest of 70% (Php22bn-23bn) through project financing. The road project capex is predicted to be lumpy versus the more predictable yearly Php10bn of Maynilad (next 5 years) on which a 25% tariff hike next year is based and the Php1.7bn capex of the hospitals aimed at achieving a 3,000 bed capacity, inclusive of capex for Makati Med and Cardinal Santos.

Bulk Water Supply in Bulacan. Outside of the West Zone concession area, Maynilad is tapping the bulk water supply opportunities in Bulacan, with estimated potential demand of 180m liters daily (water supply solely from Angat dam), 20m liters daily of which is supplied by the existing local water districts. Maynilad's capex for this is Php4bn, to plug the demand supply gap over a period of four years. Tariffs for bulk water are a lot lower than the Php35/cubic meter (m^3) in the concession area and are unregulated, thus tariff setting and capex recovery would be on a negotiated basis. There is currently no regulatory framework for the water supply business outside of the East and West Zone concession areas, a reason behind Manila Water's offshore bulk water supply ventures viewed as less risky, i.e. in Vietnam.

Two More Hospitals. MPI is in the midst of acquisition talks for two more hospitals, one in Metro Manila and the other one in Northern Luzon. The 3,000 bed capacity target of MPI for its hospital business is the scale of operations deemed sufficient to justify an eventual IPO. Regional hospital price earnings multiple (PE) is Asia, according to company guidance, hover close to 33x.

MPTC Delisting. MPI's toll road company MPTC will be delisted, as issuance of new shares to comply with the 10% listing requirement by yearend is not consistent with stepped-up road investments still at their gestation period. The next two years will be capex-heavy for the PPP-oriented subsidiaries involved in roads, rail projects.

Cash Raising. Based on company guidance, MPI's sale of about 4% of the Maynilad (leaving it still with a controlling 54%) was a form of "cashing-in" aimed at partly funding the above PPP project related capex with no gains to be booked. MPI's consolidated cash position is Php10bn; it is underleveraged with 0.10x gross debt to equity and net debt of 0.06x, thus it has room for borrowing.

Broader Investors Base. MPI is also floating 100m ADR shares, seen to broaden the investor base offshore (US) and a move likely to raise share prices in step with foreign demand, according to company guidance. There is no dilutive consequence arising from the ADRs as shares backing up the demand for the ADRs will not require new issuance but sourced from the already existing shares.

Stock Data	
Price (Php)	4.19
Market Cap (Php Bn)	103.07
Outstanding shares (Bn)	24.60
PE 2012E (X)	15.11
Price to Book (X)	1.34
Source: Bloomberg	

PSEi Boosted by Global Optimism over ECB's Bond Buying Program

In the week ending September 7, 2012, the Philippine bourse edged higher, rallying back to the 5,200-level, boosted by global optimism over the ECB's bond buying program. The PSE index added just 5.13 points (+0.10%) to finish at 5,201.32. Foreigners were net buyers by Php704mn. In developed markets, US equities soared higher, ending at multi-year highs again on the ECB's detailed bond-buying program as well as hopes for another round of monetary stimulus (i.e. QE3) by the Fed. For the week, the Dow gained 1.7%, the S&P rose 2.2%, and the Nasdaq jumped 2.3%.

Moving forward, central bank actions (of both the US and the PHL) are seen to influence stock movements this week. Investors will watch out for the EU ruling on the bailout program as well as on a speculated QE3 announcement from the Federal Reserve. Foreign news flows due for the week include US trade balance, jobless claims, consumer sentiment, and PPI. On the local front, the Monetary Board will convene on Thursday to discuss policy rates; consensus sees no change in the current overnight borrowing rate which is at 3.75%.

(Interest Rates...continued from page 1)

Philippine bonds rose before a government debt auction while the peso rallied for a fifth day, the longest run of gains in two months. The currency reached a four-year high before a Federal Reserve meeting that may lead to a third round of asset purchases, boosting the supply of dollars. The two-day meeting concludes tomorrow, Sept. 13, 2012. The peso advanced 0.3 percent to 41.465 per dollar (Sept. 12, 2012), touching Php41.445, the strongest level since April 2008. On other hand, Philippine benchmark 10-year yields fell this month to the lowest since at least 2000 as demand surged at a debt sale, allowing government to borrow for a decade at the cheapest cost since the Asian financial crisis.

AboitizPower
A Better Future

Aboitiz Power Corporation's

Steam Cost Rises

Lower than Expected Steam Reserve Extraction or Lower Steam Reserves? Tiwi Macban's lower-than-expected steam reserve extraction rate is holding back Aboitiz Power Corp.'s (AP) power supply contracting ability. AP's Tiwi-Macban is not renewing a 200MW Power Supply Agreement (PSA) with Meralco, which ends this year, until AP is able to conclude a steam sales agreement with Chevron. Chevron is the steam field operator and steam fuel supplier of AP's geothermal plant 747MW Tiwi-Macban.

SSA with Chevron Hanging. Talking points of the currently being negotiated steam sales agreement between AP and Chevron included higher fuel cost due to a coal price indexation contract feature. There is the question about who will bear the burden of Tiwi-Macban's "resource improvement." That "resource improvement" involved, among others, the "make-up well drilling/steam extraction."

Capex on Make-up Well. AP had spent an undisclosed amount on the said drilling of make-up wells in Chevron's steam field this year on hopes it could boost the steam fuel capacity by another 30MW of equivalent power for Tiwi-Macban's existing 467MW running capacity. That additional 30MW didn't happen.

Tiwi-Macban Hit by Lower EBITDA. Tiwi-Macban suffered a Php669mn drop in 1H2012 EBITDA to Php4.1bn. The EBITDA downtrend in that plant contrasted with the rising EBITDAs across AP's renewable, coal-based plants, (except for the oil-based due to a provision for a likely lower tariff). In particular, Tiwi-Macban's EBITDA share to the overall power generation business EBITDA of Php15.7bn in 1H2012 dropped from a larger third in 2011 to just a quarter. The plant's EBITDA was squeezed by flat sales volume, up only by 1% to 1,706GWh, on steady load factor of 80% year-on-year. Fuel cost rose by almost 50% to Php1.46/kwh as AP was charged by Chevron with the steam field capex.

Lost Opportunity in Tight WESM. AP was unable to fully take advantage of the strong spot prices in the WESM in terms of sales volume maximization. At the time that spot prices were high in 1H2012, up 47% for peak average price of Php6.32/kwh, AP's spot sales dropped 13% to 589GWh from last year's 680GWh. Tiwi-Macban's traditionally huge sales volume contribution had gone missing. The geothermal plant suffered a drop of 83% in spot market sales to 55GWh in 1H2012 from 332GWh last year.

No to Coal Price Indexation. AP prefers not to come under GRSC, which will kick in 2013 and allow Chevron to benchmark its steam cost on the more expensive global coal price index.

No New Wells. AP is not drilling new wells, the company is estimating it would require 16 new ones at a cost of $8mn each, to generate more steam. AP may, instead, push for the extension of the existing contract with Chevron whose steam cost is a cheap Php1.00/kwh. That contract with Chevron ends next year.

Stock Data	
Price (Php)	33.55
Market Cap (Php Bn)	246.88
Outstanding shares (Bn)	7.36
PE 2012E (X)	11.28
Price to Book (X)	3.48

Source: Bloomberg

Tiwi-Macban is Important. Tiwi-Macban is one of AP's two largest plants and biggest EBITDA contributors. It accounted for almost half of AP's EBITDA in 2011, but is now down to a quarter of total 1H2012 EBITDA of Php15.7bn. The other one is coal-fired 700MW Pagbilao, 494MW of which is contracted with Meralco, 100MW contracted with others and the rest, merchant capacity.

Taking a Step Backward. Should negotiations with Chevron drag past the 2012 expiry of the 200MW Meralco off-take, AP will turn to the WESM. AP will sell the 200MW capacity to the spot market. We think that would be taking a step backward from AP's strategy to reduce merchant risk, which at one point last year reached a low of 12% of energy sales. The non-Meralco contracts of Tiwi-Macban were already indexed to coal.

Benguet Corporation Restructures

Corporate Restructuring. The country's fourth largest primary gold producer Benguet Corp. (BC), with 1H2012 gold output of 188kg, is adopting a corporate restructuring that will markedly delineate mining activities from other allied and non-allied businesses where it may soon engage. BC has both a nickel and a gold tailings dam project subsidiary, Benguet Nickel Mining Inc. (BNMI) and Balatoc Gold Resources Inc., respectively. This move followed a balance sheet clean-up last year that had seen a debt buy-back deal cut BC's leverage. On the other hand, capital infusions and improving profits plugged a capital deficit.

Inspired by DMCI Holdings Inc (DMC), BC to Do Contract Mining. BC also had set its eyes on doing contract mining, inspired by DMC' success in BC's own Sta. Cruz Nickel mining project in the province of Zambales. DMC, who's due to end said contract mining in the so-called 100 hectare Area 1 of the Sta. Cruz Nickel Project contract this yearend, made almost Php1bn in 2011 from its share of BC's nickel shipments. That amount was not only 63% higher than the Php563mn earnings achieved in 2010 but also comprised a tenth of its 2011 audited core earnings of Php9.6bn. Out of BNMI's 710k ton nickel ore shipment in 1H2012, DMC had a share of 520k tons. BC shares have long been listed in the US stockmarket.

Nickel Processing Plant. There's a plan for a nickel processing plant and capital raising at the nickel unit BNMI. More specifically, BC is looking for a partner that could put up a processing plant for BNMI and do a nickel supply off-take agreement.

Shipments In Line With Target. Benguet's 1H2012 earnings of Php185mn were 320% higher than the comparable figure a year ago. But this figure is still a long way off the target for the year of Php500mn. Benguet plans to ship 7k oz of gold (to the Bangko Sentral ng Pilipinas, its key buyer) and 600k tons of nickel ore or 11-12 boatloads. In 1H2012, it already shipped 198k tons of its own nickel ore (excluding shipments attributable to DMC totalling 500k tons). BNMI has a remaining stock pile of 7 boatloads, which almost seals the entire year's target shipments as "done." Nickel ore grade ranged from 1.5%-1.8%/ton with selling prices from $20-$35/ton of ore.

Acupan's gold output were 188 kg based on the report of the DENR for 1H2012, equivalent to 6,580 oz., already 94% of the target for the year. But the company reported in a 17-Q SEC filing that it only sold 3,045 oz in 1H2012 at an average price of $1,614/oz, 10% above last year.

Earnings to Gain Speed as Project Investments Pay Off. Both gold and the nickel shipments were in line with delivery targets. Earnings lag the target only because of the investments made for the Acupan's tonnage ramp-up (seen to reach 1,000 TPD in 2013) and nickel mine site infrastructure development, enabling BC to take over DMC and achieve full control of the nickel shipments and profits. Since the 2Q results were indicative of the quarterly performance and not the 1Q2012 earnings of just Php27mn given the capex drag of the nickel mine development during that period, management is confident the Php500mn earnings target is "do-able." PE is 7.6x based on this year's earnings.

Stock Data	
Price (Php)	23.95
Market Cap (Php Bn)	3.91
Outstanding shares (Mn)	102.30
PE (X)	3.6
Price to Book (X)	1.68

Source: Bloomberg

Doubling of Earnings in 2013? We expect a doubling of this year's earnings in 2013 should the tailings dam project take off next year (as early as January, 2012), which will raise overall gold shipments to 12,000 oz. That assumed also that the daily tonnage at the core gold mine site Acupan will reach 300 tons per day (TPD) by yearend 2012 from the current 142 TPD with grade at 2.5g/ton and rise further to 1,000 TPD in 2013. Additional shipments from the nickel unit in 2013 on top of this year's 12 boatloads and improvement in prices from the 2Q bottom of 15k/ton LME spot will count as bonuses. We estimate 2013 earnings at a minimum of Php1bn, yielding a PE of 3.6x.

Tanduay Holdings Inc. Converts to LT Group

Float Rises

Public Float to Rise to 29% Post Overseas Share Sale. Tanduay Holdings Inc.'s (TDY) public float (that of the LT Group Inc.) will rise to 29%, initially, after the overseas share sale of Lucio Tan's Tangent Holdings' (Tangent) maximum 3bn existing shares. Tangent's share ownership of Tanduay then drops to 71%, assuming 3bn shares are actually sold. The 3bn is just the maximum, TDY has not confirmed a definite amount nor a price for these shares, to be set during a book build.

After the 5bn new share issuance to Tangent at Php1.0 par value by Tanduay, announced last week and to be completed by Sept., 2012, Tangent's share ownership of TDY will rise back to 95% from the current 89.7%. It is from that 95% level that Tangent ownership will fall to 71%, post the 3bn share equity placement.

Tangent is the majority owner of TDY with a 90% stake before the corporate restructuring into a holding company. Recall that the abovementioned Php5bn cash subscription by Tangent to TDY's newly issued 5bn shares were intended to fund the LT Group's purchase of the Tan companies to consolidate them under the holding firm (LT Group Inc.). Please see table below.

Acquisitions at Book; Php5bn was sufficient. Majority of the companies --Asia Brewery, Philippine National Bank (PNB), Allied Bank (ABC), Fortune Tobacco, Eton Properties, PAL Holdings Inc (PAL), AirPhil Express (AirPhil) -- were acquired at book that is why the Php5bn cash subscription of Tangent was sufficient to complete the consolidation under the LT Group Inc., according to company guidance. Valuation was "fair" as Tanduay acquired loss-making holding companies that owned shares of most of the 7 companies and at the same time TDY assumed their liabilities. These include, among others, Bona Sorte, Cosmic Holdings, which own the shares of PAL and AirPhil, respectively; 11 holding companies that own shares of PNB; 2 holding companies that own shares of Allied Bank (Solar Holdings and Caravan Holdings). For companies like Asia Brewery and Fortune Tobacco, the purchase was via TDY's cash subscription to their newly issued shares at par value of Php1.0bn, worth Php1.8 and Php1.6bn, respectively.

Industry observers say Tanduay may only get an exemptive relief from a tender offer if it is able to get the majority approval (for a waiver) of the minority shareholders in a special stockholders' meeting. PSE rules require a tender offer for an equity placement that exceeds the 10% share ownership limit. Right now there is no price or any valuation range being indicated by TDY for the two-step equity placement, which is seen to mimmick last year's secondary offering. That was when Tangent sold existing shares of 398m and bought back the same (but now on lock-up), generating almost Php2bn worth of proceeds for the holding firm's capex requirements.

Proceeds of the Equity Placement Will be for Increasing Stakes in Existing Companies and for other Ventures. We think it is also possible that Mr. Tan is increasing his stake in the merged PNB Allied Bank to 60%, the maximum limit for a single group ownership in a bank, from the current plan for LT Group's ownership of 35% of PNB and 28% of Allied Bank, respectively. The PAL and Airphil contracted ownerships will stay, he said, without detailing the prospects for Eton and Fortune Tobacco.

Synergies in Liquor. We note some synergies in the liquor business under the restructuring as follows:

Asia Brewery's earnings will now accrue to the holding firm. There are benefits from increased coordination in the liquor business strategy: expanded Tanduay's distribution reach together with Asia Brewery, with 7 more distributors being added by Tanduay to the combined network, to improve market share in Luzon. Luzon is largely a brandy market (not a rum market which is the Visayan region where Tanduay holds a 99% market share) held in large part by Alliance Global Inc.'s (AGI) Emperador, Emperador Light and Matador brands. AGI's alco-mix drink, "The Bar," is TDY's key competitor in Luzon's growing alco-mix drinks market. TDY expects to reach the 20m cases rum sales volume, (the world's largest sales volume held by Bacardi), next year with its export foray and stepped up local demand in an election year, 2013.

Stock Data	
Price (Php)	11.84
Market Cap (Php Bn)	47.14
Outstanding shares (Bn)	3.98
PE (X)	-
Price to Book (X)	5.21
Source: Bloomberg	

TDY's Corporate Restructuring Events	TDY Shares in mn	Tangent Ownership of TDY	Tangent's Shares in mn	Public float
TDY outstanding shares prior to asset transfer	3,981	89.70%	3,571	10%
1) TDY's new share issuance to Tangent	5,000			
Total Post-Asset Transfer	8,981	94.63%	8,498	5%
2) Tangent Divestment/Overseas Equity Placement				
Max of 3bn shares (assumption)	3,000			
Fully Diluted Shares post Secondary offering	11,981	70.93%	8,498	29%