FIRST METRO INVESTMENT CORPORATION
Metrobank Group

30 August 2013
Volume 1 No. 31

The Bellwether

Fortnightly on Market Action and Outlook

STOCK WATCH

AboitizPower

- AP CLINCHES 120 MW ANCILLARY CONTRACT, WORKS OUT LOWER STEAM PRICING WITH CHEVRON

MARCVENTURES HOLDINGS INC.

- DESPITE THE MINING GLOOM, MARC OVERHAULS AND DELIVERS

D&L

- DNL ON TRACK WITH FULL YEAR PHP1.38BN EARNINGS GUIDANCE; WE EST. A MIN. 15% 2014 EARNINGS GROWTH

U.S. Fed QE3 Exit Increasingly for Real

End of asset purchases

The sharp drops in Asian stock markets and upticks in 10-year U.S. Treasuries post a detailed Fed's view of an expanding U.S. economy signals one thing: that the end of Fed's asset purchases is in sight, whether it happens sooner or later—September, October, November of 2013.

It now does not seem to matter whether the Fed's tapering isn't a tightening or whether the U.S. Fed has been successful at bringing about a U.S. recovery through a lax money policy.

That is why even if some economists believe that the September QE tapering is less likely since the U.S. economic recovery has been uneven, the taper timing makes little relevance to market practitioners who continue to wind down positions in emerging market (EM) equities.

Higher much higher rates?

The truth that higher interest rates are staring markets in the face makes the earlier Fed statement that a "tapering must not be construed as a tightening" harder and harder to believe by the day. The perception is that the Fed thinks the risks of a prolonged monetary expansion are greater than the benefits. As markets digest that view, the result is more market volatility.

Global repercussions on EM financing

As U.S. economic data improves and the chances of a taper rise, the global repercussions are seen to be strong. U.S. interest rates, which help to set the cost of capital globally, if they rise dramatically, with yields on the U.S. 10-year bond up sharply since early May, to 2.90 percent could make it harder and more expensive for emerging markets in need of cash to finance themselves, according to Bloomberg.

Continued on page 2

2Q2013 GDP Growth Breaks Away from Decade Trend of Philippine Election Years

The 2Q2013 slowdown to 7.5% from 1Q2013's 7.8% (revised to 7.7%) highlights a potential break from a decade-long trend growth as there was not an instance in Philippine election years since 2004 that 2Q GDP has slowed relative to 1Q. In 2004, 2007 and 2010, the second quarter GDP growth were above the 1Q13 by 0.4%, 1.3% and 0.5% , respectively, and were also more than 1% above the year ago's 1Q and 2Q growth levels. See Figure 1 on page 4.

Philippine consumption, which is three quarters of GDP, slowed to 5.2% in 2Q2013 y-o-y from 5.5% in 1Q2013 even as election spending was expected to heat up in 2Q, theoretically driving disposable incomes and spending. Also, spending for durables sharply slowed to 5.7% from 10%, defying past trends. NSCB statistics showed in election years 2004, 2007 and 2010, 2Q growth of spending on durables surged four-fold to 3.6%, tripled to 6% and almost double to 29%, respectively, y-o-y.

Was it the peso's strength against the USD in 2Q2013 that crimped the purchasing power of the OFW remittance-driven disposable income of households? The peso had in fact depreciated by 5.6% to Php43.13 on the dollar in 2Q, which should enhance the local purchasing power and spending. OFW remittances are seasonally up also in 2Qs. And this peso drop didn't just happen in June. The peso shed 1%, 2.61% and 2.74% of its value against the USD in April, May and June (end of period from months' start), respectively. There was no comparable currency movement in 1Q. The peso was steady all throughout on the dollar, starting the year at Php40.85 and ended last March at Php40.81, yet 1Q2013 consumption surged 5.5% in the same period.

Construction also slowed dramatically to 15% from 30.1%, led by public construction moderating to 31% from 45% and private construction slacking to a growth of 9% from 26%. Historically, this was not the case in election years 07 and 2010. Construction growth in 07 and 2010 were up strongly, doubled to 23% and swung to positive 11% from negative 3.83% in the previous year, respectively. The private sector's slowdown was critical as it accounted for 66% of the total construction output.

Continued on page 4

(US Fed QE3 exit... continued from page 1)

Regional slowdown

There is also little inspiration coming from much of Asian economies on a slowdown mode. While the Philippines remains an exception with a still solid external account positions (+2% current account surplus relative to GDP and record-high gross international reserves of $82bn as of last June 2013) the negative news flow about neighboring countries tend to reinforce the sell down on emerging markets' equities and currencies.

$900mn equity outflow in just one week

The combination of Indonesia's record current-account gap, Thailand's economic contraction and increased speculation that the Federal Reserve will pare stimulus has spurred foreigners to sell $909 million of shares in the two Southeast Asian nations the third week of August 2013.

Philippine rates rising. Would the SDA phase-out still be a mitigant?

For its part, the yield on the Philippines' 5.875 percent bond due March 2032 rose 20 basis points, or 0.20 percentage point, to 4.75 percent last August 22, the highest level since July 16, according to Tradition Financial Services. On the other hand, the PSEi plunged as much as 6.9 percent last August 22, its biggest intraday drop since October 2008. The peso fell 1 percent to 44.085 per dollar, according to data from Tullet Prebon Plc. last August 22.

How deep is the slowdown?

Malaysia's economy grew 4.3 percent in the second quarter, slowing considerably on a year-on-year basis and prompting the central bank to lower its full-year growth forecast. The pace of growth announced by Bank Negara fell short of analysts' forecasts, and was down from 5.4 percent growth in the second quarter of 2012. Bank Negara blamed slack external demand for Malaysian goods due to global economic weakness and said it had revised its growth projection for the year to 4.5-5.0 percent.

Thailand left its benchmark interest rate at 2.5 percent amid concerns over sluggish economic growth. The move, which follows a trim to interest rates in May, comes after official figures showed persistent weakness in the kingdom's economy in the first two quarters of the year. Thailand has suffered two consecutive quarterly economic contractions this year, with figures Monday showing the economy shrank 0.3 percent in the three months to June compared to the previous quarter. This followed the revised 1.7 percent contraction in the three months to March. Manufacturing output eased 1.0 percent on a year-on-year basis, with manufacturers hit by slowing domestic demand and ongoing global weakness, the National Economic and Social Development Board said in a statement, as the U.S. and China struggle to get up to speed.

Are capital controls making a big comeback?

According to James Saft, a Reuter's columnist, India's imposition of capital controls shows how the prospect of a rollback of U.S. monetary policy is already starting a global war for capital. India has rolled out a series of capital controls to help support the partially convertible rupee, which has been hammered 13 percent lower so far this year and stands at an all-time low against the dollar. Besides limits on the amounts Indian individuals and business can shift out of the country, India banned the duty-free import of flat-screen televisions by airline passengers, a move that has the feel of clutching at straws. Although India has large reserves of foreign currency – more than $270 bn – it also must sell or refinance bonds of about $250bn over the next year, leaving it highly vulnerable to strong outflows of capital. India is not alone. Brazil, South Africa and Indonesia have also seen their currencies come under pressure. All this is happening when the Fed taper is at best a rumor. How much worse when the taper becomes for real?▲

AboitizPower
A Better Future

Aboitiz Power Corporation (AP)

Clinches 120MW Ancillary Contract, Works Out Lower Steam Pricing with Chevron

AP Stock Data	
Price (Php)	32.50
Market Cap (Php Bn)	239.15
Outstanding shares (Bn)	7.36
PE (X)	12
Price to Book (X)	3.05

Source: Bloomberg

AEV's core net income were up 4% to Php11.6bn. Quarter-on-quarter (q-o-q), earnings were 12% higher to Php6.2bn. Net debt to equity was higher at 0.6x by end-2Q2013 versus 0.4x as at end-2012. Capex will be biggest for power, Php125bn (beneficial) for 1,197MW additional beneficial capacity in the next five years to secure long-term growth.

Income boosters for the 1H13 results were: Pilmico, earnings up 21% to Php630mn in 1H2013 year-on-year (y-o-y).

Union Bank earnings were also higher 52% to Php6.2bn in 1H2013 y-o-y, largely on trading income, that were 69% higher versus year ago to Php5.6bn. Net interest income (NII)

Continued on page 3

(Aboitiz Power... continued from page 2)

flat at Php3.7bn. Net interest margin fell 41bps to 4.59% versus 5.4% y-o-y, largely led by drop in average yield, down 43 bps bigger than the drop in funding cost of 39 bps to 1.43%

The narrow NIM might improve with the interest outlook bottoming out. Accrual income from the reduced peso HTM intended to be replenished will compensate for low yielding Treasury investments left in UBP's books. The strong peso deposit generation, a quarter of the Php214bn in low-cost CASA and up 26% q-o-q will go to loans. Deposits were up 13% in 1H2013, overtaking loan growth of 7% that were heavily placed in corporates, preferreds and bonds.

However, power generation and distribution arm Aboitiz Power (AP) core earnings were 6% lower to Php10.9bn. Inclusive of Php1.4bn fx losses and debt prepayments costs, reported net income were sharply lower at 22% to Php9.5bn. While energy sales were up 5% to 5,360 GWh, other negative factors were at play. See below.

AP's selling prices were lower, both bilateral contracts, (-10.4% to Php4.75/kwh) and spot, (-19% to Php5.15/kwh). Recall spot prices last year were higher due to higher forced outage in Luzon grid. Bilateral contract selling prices move in the same direction as fuel prices, e.g. lower coal prices this year.

Ancillary revenues were dramatically lower also, -62% to Php2.6bn from Php7bn, blamed on NGCP's low acceptance rate of AP's nominated energy at only a quarter to half of the latter or high of 180GWh each month (in May and June), respectively. GWh sales were 63% lower to 557 from 1,494 a year ago.

AP was unable to sell to WESM the same capacity nominated for NGCP (but unaccepted) either because water level of Magat didn't permit it or WESM prices were not profitable. Still, the hydros managed a 14% increase in GWh sales. But the price effect of both the spot and contracted energy of the hydro portfolio had a more powerful impact on EBITDA.

The weakness of ancillary (selling prices steady at Php4.63 and lower volume) where the hydros are dependent for much for their sales also helped to shave the hydros' EBITDA which dropped 39% to Php2.9bn from Php4.8bn a year ago. The load factor of Magat dropped to 39% from 102% as contracted energy sales of Magat sharply dropped to 102GwH from 199 a year ago. The hydro's EBITDA contribution dropped to 18% share of total AP generation EBITDA of Php15bn from last year's 30% share.

Together with the geothermal's pricey fuel (coal price indexation kicking in) that had reduced dispatch (volume down 13% largely led by contracted energy) because selling prices have become uncompetitive during non-peak hours, the renewable energy (inclusive of hydros) EBITDA dropped 18%. Tiwi-Macban's steam had to be vented consequently. Steam field operator Chevron's bill on geothermal fuel (under GRSC) was Php2.30/kwh in May, higher than the Php1.70/kwh a year ago and actual steam cost of Php1.21/kwh. Tiwi Macban's 400MW running capacity was way below the installed of 600MW. Load factor steady at 85%. Revenue sharing contract under negotiation between AP and Chevron to address the pricey fuel and steam well drilling/well work over. The oil and coal plants sold higher volumes, +48% at +10%, respectively, helping to boost generation EBITDA by 14% to Php7.7bn. Coal plant Pagbilao is 47% of EBITDA, the oils only 5% of EBITDA while Tiwi Macban is 29% share of EBITDA and the hydros, 19%.

The distribution business was up, with +16% increase in EBITDA to Php2.6bn, even with flat power sales of 2% to 1,997GWHr. Thanks to higher gross margin/kwh sale to Php1.71 year-to-date versus Php1.44 a year ago.

The ancillary business is expected to improve volume-wise with 120MW approved by NGCP for Magat and Pagbilao in 2H2013. Open access will see some 258MW available to big users (reclassified under open access) of 1MW/year but it is not clear if this will make additional income for AP margin-wise. Volume-wise, this does not represent incremental sales.

AP is a dividend play and a bet on earnings recovery near term on the back of a new ancillary contract and revenue sharing scheme with Chevron lowering steam fuel cost for AP's geothermal unit. Near term earnings upside also arises from more capacity based contracts (60% of contracted energy) replacing expiring energy contracts for earnings and cashflow stability. AP also has a Php125bn long-term expansion by half of existing 2,300MW capacity in five years. (Capacity based contracts require that off-takers pay AP a fixed capacity fee (return on investment) whether AP dispatches or not. Energy contracts require that AP dispatches and gets paid only based on the dispatch). PE is 12x. Dividend yield 4.8% gross.▲

(2Q2013 GDP Growth... continued from page 1)

Yet cement company earnings growth were at an all-time high. Holcim +52% in 1H2013, LRI was up 55%, same period. Y-o-y 2Q2013 earnings growth were 32% and 76% for HLCM and LRI, respectively, better than 1Q2013. Y-o-y 1Q2013 earnings growth were 77% and 33% for HLCM and LRI, respectively.

We also have not seen property companies' earnings growth of the following magnitude in the past:

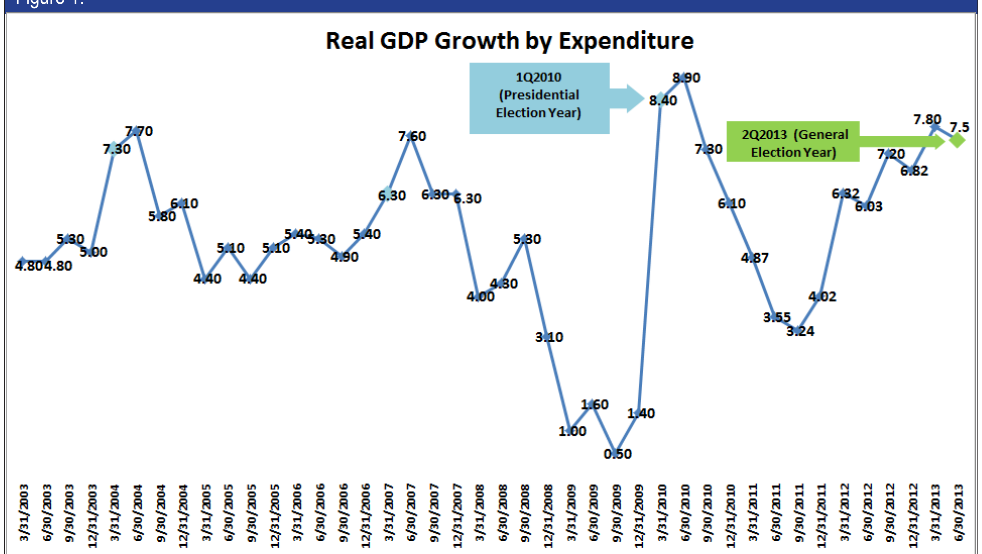
ALI, VLL and FLI raked in y-o-y 1H2013 earnings growth of 30%, 30% and 25%, respectively, same period. ALI maintained its 2Q earnings growth y-o-y of 30%. National income accounts are computed based on big industry player' revenues deflated for inflation, according to NSCB's National Accounts Head Fe Talento with whom we had a chat about the 2Q2013 results this morning.

If industry players were doing so great, then why the sharp slowdown in construction activities? Was it the weather, a property bubble threat, the BSP real estate lending cap or peaking of the property development cycle? 2Q had the summer months, seasonally the peak of construction activities in the country, also the time when Meralco energy sales seasonally rise, which it did. The latter was up 7% compared to the 1Q2013's flat growth of 1.2%.

Because construction and durables fell, gross capital formation decelerated to 13.2% in 2Q2013 from 44.5% in 1Q2013. This was the biggest growth killer from the demand side, aside from exports which slid -6.5%. Gross capital formation accounted for 17% of GDP, with construction and durables each chipping in shares of 9% each.

From the supply side, manufacturing was buoyant, rising 10.3% from 9.5%, yet exports shrank. Manufacturing is 22% of GDP and is part of the Industry Sector, whose growth was marred also by the moderation of construction activities. Industry slipped to 10.3% from 10.9%. Industry is 33% of GDP. The growth driver was services, up +7.4% from 6.8%, helped by real estate, transportation and trade. Services is 57% of GDP from the production side. But agriculture shrank -0.3% from 3.1% in 1Q2013 due to what NSCB said was an early harvest in 1Q as farms hedge vs. climate change.

Figure 1.



Source: National Statistical Coordination Board

Table 1. Real GDP Breakdown

Real GDP growth (2000 prices)	1Q2013	2Q2013	% of GDP
Demand side			
Private Consumption	5.5%	5.2%	67
Gov't Consumption	13.2%	17.0%	13
Capital Formation	44.5%	13.2%	17
Fixed Capital	15.6%	9.7%	19
Construction	30.1%	15.6%	9
Durable Equipment	9.6%	5.7%	9
Breeding and orchard dev't	0.6%	-1.1%	1
Intellectual Property Products	10.4%	16.3%	0
Changes in stocks	-48.6%	-19.0%	-2
Exports	-7.6%	-6.5%	47
Imports	2.0%	-3.0%	46
GDP	7.7%	7.5%	
Net factor income	8.2%	2.7%	
GNP	7.8%	6.8%	
Supply side			
Agri, Fishery & Forestry	3.1%	-0.3%	9
Agri & Fishery	2.5%	-1.1%	8
Fishery	5.8%	3.3%	2
Industry Sector	10.9%	10.3%	33
Mining and Quarrying	-1.9%	-2.7%	2
Manufacturing	9.5%	10.3%	22
Construction	29.3%	17.4%	6
Elec, Gas & Water	0.3%	5.5%	3
Service Sector	6.8%	7.4%	58
Transpo, Comm and Storage	2.8%	3.5%	8
Trade & repair of goods	5.5%	7.3%	16
Finance	18.0%	9.6%	7
Real Estate, Renting & Business	5.8%	9.5%	11
Gov't services	8.3%	5.9%	5
Other services	5.3%	7.4%	11

Source: National Statistical Coordination Board

Marcventures Holdings, Inc.

Despite the Mining Gloom, MARC Overhauls and Delivers

MARC Stock Data	
Price (Php)	1.80
Market Cap (Php Bn)	3.12
Outstanding shares (Bn)	1.73
PE (X)	-
Price to Book (X)	1.45

Source: Bloomberg

What MARC had dreamt of in 2011, a bottomline of close to a billion pesos, it now seems to be achieving and fast. Earnings to date—up to the third week of August 2013—above expectation and bound to rise with the 9-month topline push up. Mining operations has just started in May, the seasonal pattern for most Surigao-based nickel miners, yet shipments of nickel ore were past the 700k ton level, already, and cash on hand is healthier. We think a bottomline of Php850mn looks like an easy target with shipments planned at 48 for the entire year equal to 2.6m tons of ore, reflecting volume-based mining amid weak metal prices. The planned shipments for 2013 are triple the previous year's 637k tons or 11.5 shipments. 1H2013 earnings were Php330mn, more than double the whole of last year and above the Php265mn in 2011.

That this feat is happening at a time when industry peers are struggling with collapsing limonite selling prices (but not necessarily weak sales volume) makes the MARC's earnings story an industry aberration. In 1H2013, Oriental Peninsula and Nickel Asia Corp.'s (NIKL) earnings both disappointed, flat for ORE and down to half of the previous year's level for NIKL. These results were notwithstanding record high shipments for ORE and NIKL that apparently didn't compensate for the fall in nickel selling prices.

Confidence in the nickel miner seems to be at its highest point when a thrift bank recently lent it Php200mn. Government last April also granted it an expanded Environmental Compliance Certifcate (ECC). MARC's ore resource is estimated at 45m tons, (based on a CP report to the Mines and Geosciences Bureau-MGB) up from previously 11m tons. This new estimate was after drillings made under the amended ECC that expanded commercialization up to 300 hectares or an additional 180 has on top of the existing 120 has. MARC's mineral production sharing agreement (MPSA) has a contract area of 4,799 has.

A big part of the secret is in MARC's newly opened low-cost mine Pili and the ramped-up mode of iron ore mining under the new management's strategy. What this low-cost mine enables MARC to sell and its string of huge Chinese off-takers worked wonders on operating results. The mine site is close to the pier, 8km only from previously 24km at its father Cabangahan mine, also in Surigao province. The new location halved operating cost and doubled the net profit margin per ton to 47%. MARC sells iron ore of 51% grade at \$20-21/ton contained in limonite ore with grade of 0.7 - 0.8 g per ton ore, a departure from the high grade saprolite it was selling two years ago for as much as \$75/ton. That was prior to the collapse of China's steel industry and the metal price slump that went with it.▲

D&L

D&L Industries, Inc. (DNL)

on Track with Full Year Php1.38bn Earnings Guidance; We Estimate a Minimum 15% 2014 Earnings Growth

DNL Stock Data	
Price (Php)	6.40
Market Cap (Php Bn)	22.86
Outstanding shares (Bn)	3.57
PE (X)	17.78
Price to Book (X)	2.85

Source: Bloomberg

DNL's 1H2013 earnings were up +16% to Php655mn on track with 2013 full year guidance of Php1.38bn.

1H2013 earnings was 64% of full year 2012 earnings of Php1.03bn.

Key Earnings Drivers:

1) Gross profit margin (GPM) expansion to 19% from 14% (last year) as two high margin products food ingredients (FG) and plastics (PL) sustained their GPM rise to 16% and 25%, respectively, from previous year's 12% and 21%. Consolidated net profit margin rose to 13% from 10%. FG and PL accounted for 71% and 24% of topline and 41% and 38% of net income, respectively. Ninety percent of plastics revenue represents exports to Europe and Japan. DNL's exports were on the aggregate up 17% to Php811mn in 1H2013.

2) There was also sales volume growth across all product segments, except 10% drop in plastics which should be no cause for worry as it was largely due to base effect of clients' sourcing from DNL more instead of the regular suppliers. Growth is expected to normalize at the 15%-17% rate next year, having grown in 2012 by 25%.

Sales volumes were also up for food ingredients, +4%; refined vegetable oils, +3%; specialty fats and oils, +17%; aerosols, +27%. These growth rates are expected to be sustained next year, especially with GDP and Philippine consumption on the growth path.

Chemrez' earnings, a 36%-owned affiliate engaged in the biodiesel market, will grow 10% this year. Its 1H2013 earnings were ahead of last year by 10% to Php143mn. There is no guidance for Chemrez this year.

Petron is Chemrez' biggest client with share of 53% of total production of biodiesel which is about 2m liters a month. Chemrez rated capacity is 80m liters per year, with utilization of 40% and holding a 30% share in the 140m litre per year Philippine biodiesel market. Upside is biodiesel mandatory 2% blend rising to 5% in 2015. Debt to equity ratio was steady 0.51x versus 0.48x a year ago.▲

First Metro Investment Corporation
Metrobank Group

NICKEL ASIA CORP.

Nickel Asia Corp.'s (NIKL)

Pilot Plants to Expand Mining Operations for Other Metals

NIKL Stock Data	
Price (Php)	15.76
Market Cap (Php Bn)	39.70
Outstanding shares (Bn)	2.52
PE (X)	15.65
Price to Book (X)	1.67

Source: Bloomberg

1H2013 results

NIKL's 1H2013 shipment volume increased by 10.30% to 5.54 million wet metric tons (WMT) of nickel ore leading to Php4.38bn in revenues, 17.5% lower year-on-year due to weak nickel prices. Net income dropped by 50% to Php645.6mn. The company had a lower selling price of $7.54 per pound of pure nickel on 1.97mn WMT of ore sold in 1H2013 versus $8.60 per pound of payable nickel last 1H2012. Meanwhile, it realized an average selling price of $20.14 per WMT for the remaining balance of ore negotiated on a per shipment basis.

THPAL 2 still undergoing testing

THPAL 2 (Taganito high-pressure acid leach), 22.5%-owned by NIKL, is already completed but it is still undergoing test operations and will start commercial operations on 4Q2013. The facility will be at full capacity in 2014, generating 30,000 tons per year of contained nickel and 2,600 tons of mixed sulfide.

Iron pilot plant

Last June 3, 2013, Sumitomo Metal Mining Co., Ltd. (SMM) announced the construction of its pilot plant in Taganito, Surigao del Norte which will process the hematite tailing from nickel into higher grade iron ore of 60% from the current 30%-40% using SMM's HPAL technology.

Iron ore sells at $138/WMT based on the Australian benchmark and at a lower $90/WMT with impurities. If this becomes successful, it will be replicated in Coral Bay as it will be very beneficial in lowering the amount of tailings and maximizing the use of the nickel ore produced. The plant is currently under commissioning and will be completed by next year.

Scandium pilot plant

The plant for scandium oxide recovery at Coral Bay Nickel Corp. (6%-owned by NIKL) in Palawan will start the pilot plant construction next month (September 2013). The pilot plant will begin operations in 2014, with a capacity of 10kg per month. NIKL targets to start commercial operations in 2015 with a capacity of 10-15 MT per year, depending on the market.

Scandium's currently sells at $2,000/kg. The potential is still unclear because attributable earnings/revenue sharing has not been drawn yet.▲

Cristina S. Ulang	Basil Jason L. Go	Bianca P. Angala	Patricia L. Dalusung	Ignacio V. Pardo
Research Head	Research Analyst	Research Analyst	Research Associate	Research Associate

FIRST METRO INVESTMENT CORPORATION
Metrobank Group