FIRST METRO
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The Bellwether

Fortnightly on Market Action and Outlook

STOCK WATCH

ABS-CBN

▶ 7% EARNINGS GROWTH IN 1Q14

D&L

▶ KEEPING UP THE POSITIVE TRENDS

FILINVEST LAND INCORPORATED

▶ RIDES THE PROPERTY UPTURN

Market Outlook II

Revised PSEi Target

PSEi looks poised to breach 6900 - 7000 range which we earlier predicted as our yearend target. Positive statements from the third major credit rating agency, Moody's Investors Service Inc., that Philippine reforms are sustainable beyond 2018 is raising the probability of a breakout above 7,000 to a possible 7,200-7,400 territory by yearend. The Philippine market remains on solid ground and has risen 17% year-to-date on double-digit corporate earnings growth in 1Q14, a big positive surprise that defied the consensus bet of single digit growth for the entire year.

Drivers

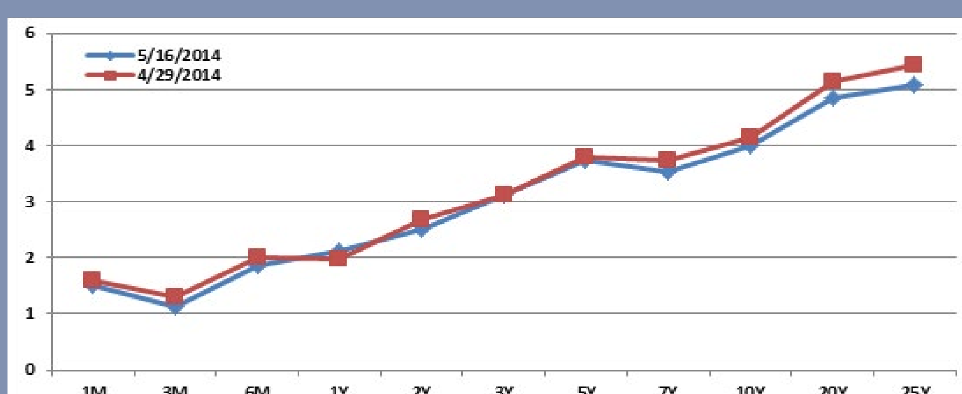
If and when the 1Q14 GDP growth rate hits 7%, which is likely given the strong industrial sector performance -- energy sales of 5.7% to industrial sector recorded by Meralco in 1Q14, 10% energy sales of Aboitiz Power Corp. and export growth of 6.5% in 1Q14 versus negative -6.18% in the comparable period last year -- the PSEi revisiting the highs achieved last May 2013 is not a long shot .

The financial markets are flashing confidence in the continuing liquidity that has began to flatten the yield curve, signalling further that inflation pressures will be kept at bay. Forward PE is reasonable at 16x and backed by strong fundamentals. All these are come-ons to investors' differentiating the Phil. market vs. weaker neighboring economies in Asia such as Indonesia faced with a hugely depreciated rupiah and an upcoming election; a less attractive Thailand due to political uncertainties despite reasonable valuation; slowdown in China, structurally weak India with GDP at around 5% from 10% two years ago and near term elections.

The foreign funds has, in fact, returned, whose net inflow last Feb (Feb 4, 2014) up to last (April 25, 2014) reached Php35bn and surpassed last year's total net funds outflow of Php28bn. The momentum of such flow will support our revised target PSEi range of 7200-7400.

Surprise Credit Rating Upgrade Led to Treasury Rally

Peso Yield Curve



A surprise one-notch rating upgrade by S&P led to unexpected Philippine treasury rally, pushing average daily volume for the first half of May to Php 16.11 bn, coming from only Php 8.38 bn in April. After the upgrade was announced, the trade volume reached Php 30.32 bn. The market was controlled by buyers, settling the long-end to 6-week lowest level (10-yr @ 4.0%, 20-yr @ 4.846, 25-yr @ 5.097%). Gains in the US treasury slightly contributed to this, as the US 10-yr rate broke below the 2.60-2.75% band to 2.52%, end of second week of May (May 16, 2014). Despite tight supply of short-term papers, the front end rates eased by an average of 27.7 bps.

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ABS-CBN Corporation (ABS):

7% earnings growth in 1Q14

ABS Stock Data	
Price (PHP)	38.90
Market Cap (PHP Bn)	33.34
Outstanding shares (Bn)	0.86
2014E PE (X)	20.99
Price to Book (X)	1.42

Source: Bloomberg

We expect recurring net income to post 25% growth to Php 2.0 bn this year. We remain bullish for the Company until the medium-term, as its aggressiveness in market and product development strategy results to brighter 2015 prospects. Its revenue mix target is 25%-75% in the next 5-10 years, in favor of non-broadcast businesses.

ABS-CBN recurring net income grew by 39.7% from Php 385 m to Php 535 m in 1Q 2014. The company was able to take advantage of diversifying its businesses, shifting from advertising revenues to consumer sales. Growth for ABS was fueled by its film and global distribution businesses. Its domestic peer GMA7 reported 46% net income decline to Php 326 m and 4% decline in recurring ad revenue.

Three STAR cinema movies generated more than Php 300 m theatrical sales each, pushing segment's net revenue to Php 660 m (25.2% growth). In terms of broadcast viewership, it has the highest audience share both in the total day (44%) and primetime slots (48%) for the whole Philippines, and at par with GMA 7 for the Metro Manila audience. As for the global distribution, net revenues increased by 22.1% to Php 1.515 bn due to improvement in theatrical and events, via international release of movies ASAP Dubai.

ABS-CBN is committed to expand its consumer sales businesses. Its capital expenditure for this quarter is consistent with this strategy, as the Company spent Php 1.072 bn—only 17.35% (Php 186 m) is for Program Rights. The same period last year, the CAPEX for program rights was at Php 311 m (29.37% of total). For this quarter, Php 497 m and Php 389 m were spent for the pay TV and Digital TV, Maintenance and Others, respectively. As for this year, the capital expenditure might reach Php 6 bn, only Php 750 m (12.5%) is for acquiring Program Rights.

Outlook:

We are bullish for ABS-CBN, now that it is expanding its consumers and tapping on different markets. The film business will continue to boost income growth, as the Company plans to release about 20 movies in 2014, higher than its usual 12-16 releases per year. Capital expenditure for this year might reach Php 6 bn, only Php 750 mn (12.5%) is for acquiring Program Rights. The O Shopping and ABS-CBN Mobile will likely reach break-even numbers in 2015. ▲

Net Income by Segment (Php mn)

	1Q 2014	1Q 2013	% Change
TV and Studio Operations	895	617	45.1
Pay TV Networks	41	80	-48.8
New Business	-398	-194	105.2
Total	**538**	**503**	**7.0**

Source: Company data

(Market Outlook. continued from page 1)

Risks

We identify near-term key risks (but low probability risks) to be the ff:
• El Nino;

• An aggressive policy rate hike by the BSP which is unlikely given the low inflation;

• Inflation rising much faster than forecasted;

• Earnings don't deliver, but which is showing an average of 15%-19% for cement and consumer companies like Holcim, Emperador.
• US unwinding its stimulus much faster than widely anticipated, that is US Fed rates might move up from the current near 0 to 25% range even before 1Q15 or as early as late this year, weakening the peso and reversing anew the money flow back to the developed market. ▲

Filinvest Land, Inc. (FLI):
Rides the Property Upturn

FLI Stock Data	
Price (PHP)	1.62
Market Cap (PHP Bn)	38.80
Outstanding shares (Bn)	24.25
2014E PE (X)	9.25
Price to Book (X)	0.80

Source: Bloomberg

Filinvest Land Inc.'s 1Q14 earnings growth was 15% to Php1.1bn, while sales take up grew 11% over last year, same period. It made Php3.9bn in earnings last year, up 11% year-on-year. The sales mix for the period was more of locals, 60% from 50% versus those of OFWs at 40%, the latter used to be a bigger half, underscoring the buoyant domestic demand. FLI, a low-cost to middle-income housing developer in the price points of Php2m-5m/unit, is boosting recurring income comprising 30% of total revenues by more than doubling its BPO office space to 870k sqm by 2018. Its housing development portfolio remains a big chunk of revenues at 70%. This year, FLI is adding 100k sqm to its existing office gross leasable area (GLA) of 210k sqm with three buildings, one in Cebu and two in Quezon City. Its retail leasing is also expanding, with additional 50k and 25k sqms of leasable space, respectively, for the Festival Mall in Filinvest Corporate City, two more malls in Molino, Cavite and in Tagaytay City. FLI is also building a mall in South Road Property in Cebu by the end of next year. Landbank stands at 2,356 hectares. Capex this year is Php20bn and it is raising Php10bn in debt. Debt to equity ratio stood at 0.72:1 as of 1Q14.

2013 was the first time Filinvest had positive operating cashflow since 2011 worth Php2.5bn as real estate inventories grew by only Php262m last year and in-house financing was streamlined in favor of more bank financing. FLI is one of the cheapest in the property counter with PE of just 9.65x, but also a laggard (up only by 17% in price appreciation ytd May 14 vs average of 24% for peers) despite the 32% equity float. The share's average daily value traded fluctuates from a low Php3m three months ago to a high of Php64m lately compared with Robinsons Land Corp's (RLC) Php87m and Ayala Land, Inc.'s (ALI) Php127m. FLI share prices may begin to move as soon as the campaign of investor conferences hit the road.

FLI has the ff view on the Phil Real Estate Market.

I. That the residential real estate market will continue to be very strong given the demographics, population growth and housing backlog of the Philippines. The continued flow of remittances from overseas Filipino workers (OFWs), along with historically low interest rates, are key drivers for the residential real estate sector. The banking system is also very liquid, and many banks are aggressively cultivating their residential mortgage portfolios. As a result, homebuyers are finding it easier to finance their housing purchases. This increased liquidity will continue to give further impetus to the residential property market. It sees the largest potential in the affordable to middle-income housing segments for families.

Key risk is the oversupply in selected areas geared toward the investment market, rather than the more stable end-user market. The Philippines is seeing more luxury developments and high-rise buildings than ever before, but the market for such properties may be limited. Much of the demand for these types of properties may be more speculative and investment-driven. These segments will be the first to be affected should there be an economic slowdown.

II. Demand in the businesses process outsourcing (BPO) and office construction sectors continue to be quite strong, and is expected to remain as such over the next few years. While there were some concerns that the global economic slowdown would undercut demand for BPO services in the Philippines, this has proved to be unfounded and demand has actually increased to a point where it now actually outstrips current supply in the market.

III. Furthermore, the tourism industry is beginning to take off and more developers are interested in getting involved in tourism projects. As the government continues to prioritise growth in the tourism industry, and as more developers realise the potential offered by such projects.

Key risk. Activity is anticipated to increase, though the lack of transport infrastructure may slow such developments.

IV. The retail market will remain quite strong as long as remittances from OFWs continue to grow. Growth in this sector is a direct result of consumption and consumer spending fuelled by the remittances of OFWs to their families in the Philippines. While some shopping centres in the country have been overbuilt, and it may sometimes take malls a number of years to reach full occupancy, these commercial centres are popular with the populations in their communities. While there is sufficient demand to keep such projects profitable, development will continue.

V. Areas to Take Off. More than ever, developers are looking to regional growth centres as they seek to establish themselves in markets outside of Metro Manila and other traditional growth regions. While urban centres including Cebu and Davao continue to see heavy competition and many developments, non-traditional markets like Cagayan del Oro, Iloilo and Zamboanga are also experiencing increased interest. Some developers are even trying out high-rise condominiums in these alternative markets, though such projects remain experimental. Filipinos typically favour individual houses, and to date these high-rise projects have only been successful in the cosmopolitan centres of Manila and Cebu. In the past, such buildings have usually struggled to reach full capacity. ▲

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D&L Industries, Inc. (DNL):

Keeping up the positive trends

DNL Stock Data	
Price (PHP)	9.39
Market Cap (PHP Bn)	32.79
Outstanding shares (Bn)	3.57
2014E PE (X)	20.26
Price to Book (X)	4.18

Source: Bloomberg

Rising volumes boost revenues and net income

For the first quarter of 2014, D&L Industries, Inc. (DNL) posted revenue growth of 34% and net income growth of 20%, driven by double-digit volume growth across all segments. Revenues and net income hit PHP1.3bn and PHP377.0mn, respectively. The charge was led equally by DNL's two biggest businesses – food ingredients and specialty plastics – both posting volume growth of 25%.

The food ingredients segment, which contributed 74% of revenues and 38% of net income, grew revenues by 40% to PHP2.3bn and net income to PHP143mn. Overall gross profit margin (GPM) fell 1.1% to 13.4% mainly due to higher sales volume from low-margin products relative to high-margin products. The higher volume resulted from recovered market share stemming from a significant decrease in smuggling activities.

The specialty plastics segment, which boasts of the highest margins among DNL's businesses, grew its revenues 16% to PHP163mn. This is a reversal of the decline in volume and sales in 2013. As a result, net income increased 16% to PHP163mn. Overall GPM rose 0.3ppt to 31.1%. The segment contributed 22% of the group's revenues and 43% of net income.

Equitized earnings from Chemrez jump 38%

Affiliate Chemrez Technologies, Inc. (COAT) contributed PHP33mn to DNL's 1Q14 earnings. Revenues and net income increased by 16% to PHP1.2bn and 39% to PHP97mn, respectively, driven by strong demand for its environment-friendly non-biodiesel oleochemical products, especially in the export market. Overseas sales, comprising 22% of COAT's revenues, rose 32% YoY. Overall GPM rose 4.7ppts to 15.3%.

Recovery in volume from low-margin products lower margins

DNL's low-margin products (refined coconut oil) have recovered as smuggling abated. This brought its revenue contribution to 36% from 32% in 2013.

Balance sheet remains stable

DNL has kept its balance sheet unlevered. While borrowings climbed to PHP2.0bn from PHP1.7bn in 2013, its debt-to-equity ratio remained at 0.29x. Finance costs decreased substanially, falling 62% to PHP7.8mn from PHP20.8mn in 1Q13.

Cost efficiency maintained

Raw materials comprise 84% of DNL's total costs. Palm oil and coconut oil comprise 45% and 21%, respectively, of raw materials costs. Both are volatile commodities in terms of price; coconut oil in particular has seen massive spikes over 2013. These spikes, coupled with a weaker peso (70% of raw materials are exported), drove costs up 35%. DNL, however, successfully maintaned its margins due to their ability to pass on price increases to their clients.

Valuation

DNL is currently trading at 24.4x P/E, still below the peer average of 26.6x. This is much more favorable than the high P/E ratios of Jollibee (JFC) at 38.5x, PureGold (PGOLD) at 32.8x, and Universal Robina (URC) at 31.3x. DNL's 1Q14 earnings growth also exceeded those of its peers, excluding Pure Foods (PF) which increased 24%. ▲

(Yield Curve.. continued from page 1)

We see downward trend across the board generally persisting until the end of May, as the market expects Moody's and Fitch to follow S&P in recognizing Philippine strong macroeconomic fundamentals, and BSP indicating that it doesn't plan additional prudential measures to aggressively siphon liquidity at this time. Also, government fiscal position, inflation expectation and forex rates will remain favorable for GS market rates. This will be indicated by the upcoming 3-year auction, which we see to be oversubscribed to 2.8-3.0 tendered/offer ratio, with yield estimated to follow downward trend in the secondary market. On one note, we will see pockets of slight profit-taking to realize gains and recover Treasury losses. ▲

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