FIRST METRO INVESTMENT CORPORATION
Metrobank Group

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The Bellwether

Fortnightly on Market Action and Outlook

STOCK WATCH

▶ 6% NET PROFIT GROWTH IN 2014

▶ HIGHER INDUSTRIAL ENERGY SALES IN 1Q14

Market Outlook

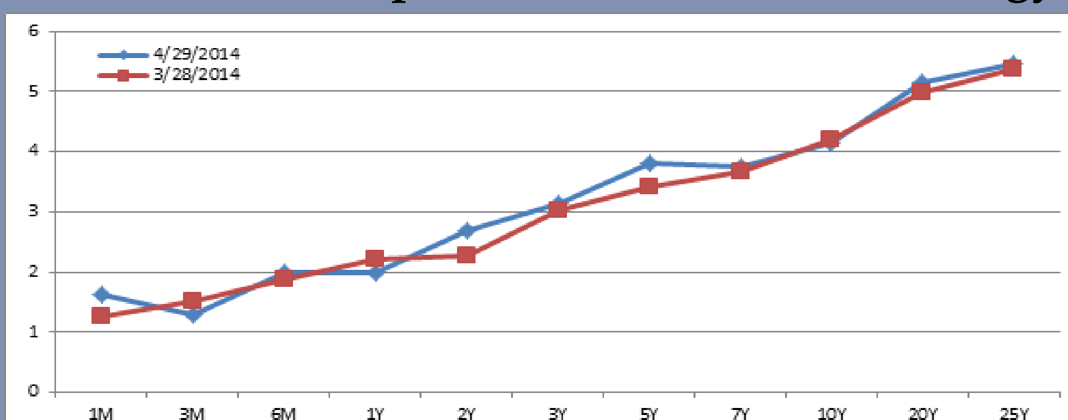
PSEi Target

PSEi will achieve 6900 - 7000 by yearend. The Philippine market remains on solid ground, backed by strong fundamentals and reasonable valuation at forward PE (2015) of 16x. We believe in investors' differentiating the Philippine market versus 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.

Market Drivers

Three factors will drive the market to these range level: (1) corporate earnings (2) excess system liquidity, strong M3 growth (3) return of foreign funds. This range based on a 15% -18% for the 6900-7000. We think the economic fundamentals are rightly placed to support such earnings growth, to name a few -- low inflation and still low interest rates (whose rise -we think- will be tempered by the still excess system liquidity), GDP growth momentum forecasted at 7% by gov't authorities in 1Q14 and the much talked about Phil fundamental merit for a credit rating upgrade by a still a notch higher. Fitch

Yields to Inch Up as the Market Remains Edgy



Source: PDS

Quiet trading in April as market seeks clarity of central banks' monetary stance here and abroad, damping trading volume to a shallow Php184.6 B from Php517bn and Php625bn, a 64.3% and 70.5% m-o-m and y-o-y decline, respectively. Most market participants maintained overall short duration position and pricing was generally range-bound. Month-on-month basis, largest yield movement was seen at the belly of the curve, increasing by an average of 24.7 bps as participants unloaded in favor of the short-end. The 91-day bill rally produced small cut in losses sustained from the belly. The secondary rate of 3-month bills dropped to 1.3%--14 bps lower than the 1.44% yield we saw during auction. Flattening of the yield curve and rising short-term rates indicate market's sensitivity to monetary stance.

Towards the end of April, BSP Gov. Tetangco signaled that the Board is not as aggressive, and had opted to be careful not to prematurely change policy rates to avoid backlash to the economic growth momentum. Unless the BSP and the FOMC change their position on the schedule of policy rate increase, we expect weak trading to continue in May, as the market remains apprehensive. We expect liquidity to be raised in the short-end on short duration strategy because of a potential 10-15 bps uptick in yields due to higher inflation expectation for May because higher food prices, from a lower 4.1% in April. Market will be generally edgy and on a wait-and-see towards the 1Q 2014 GDP announcement. Note that supply of t-bills will be tighter with the rejection of bids for the 6-month and 1-year debt (May 5 auction). Apparently, National Government has a better cash position due to the seasonally high tax collection period in April.

BPI Make the best happen.

Bank of the Philippine Islands (BPI):

Php20bn Net income or 6% Growth for 2014

BPI Stock Data	
Price (PHP)	90.80
Market Cap (PHP Bn)	356.76
Outstanding shares (Bn)	3.93
2014E PE (X)	16.95
Price to Book (X)	3.15

Source: Bloomberg

Lighter Securities Portfolio

In the first quarter of 2014, earnings fell to Php3.6bn (from Php8.4bn in 1Q13) due to the drop in trading gains. Non-interest income (ex-securities trading) climbed by 16% to Php4.26bn. Due to the more volatile trading environment, the bank decreased the securities portfolio size to Php48.1bn (from Php92.1bn in end-Dec. 2013) and shortened the duration of the trading securities portfolio.

Double-digit loan growth

In spite of reduced trading, net interest income (NII) stood at Php8.1bn in 1Q14, 15% higher YoY. Core lending business remained robust resulting in a 25% growth of net loans to Php641.7bn, driven by corporate and consumer loans. Metro Manila middle market segment grew 30%, while the provincial areas improved 20%. Auto loans grew 40% growth, faster than the industry average of 20-24%. Car sales grew 21.4% to 32,470, year-to-date Feb. 2014 However, housing loans slowed down at the low-teens compared to the same period last year, while business loans under its Ka-Negosyo program expanded 15%.

In 2014, wholesale and retail lending business units are expected to jump by a fifth. Furthermore, the growth in revenues and net income this year will be driven by higher loans and increase in non-interest income, which may come more from fees and commissions and less in trading.

On-line Loan Availment Platform

Online Loan Availment Platform. In addition, BPI launched its one-stop online platform (www.bpiloans.com) to provide convenience to consumers in making purchases of big-ticket items (i.e. a car or house) nationwide, with over 100k properties and gallery of vehicles posted in the website. As part of its growth strategy, this online platform was already used by about 10% of its total loan applications and expects to improve this to at least 50% in a couple of years.

On Track to Meet Guidance Profit Guidance

BPI expects a 6% jump in net income to Php20bn. However, ROE may decline to 15% (from 18.1%) driven by its recent Php25bn stock rights offering, which increased its capital by almost 25%. But through this share sale, BPI's tier 1 CAR will expand to 18.6% (from 14.7%), which shows a high level of loss absorption capacity and making it one of the well capitalized bank in the industry.

No Acquisitions, So Far

BPI's new CEO is emphasizing organic growth with the PNB deal shelved for now. According to management, there are no ongoing discussions about potential acquisitions.

Branch Expansion

As restrictions in bank branch expansion expire in July, BPI plans to add 40-50 new branches this year (a total of 865-875, from 825 branches in end-2013). ▲

(Market Outlook.. continued from page 1)

had affirmed the investment grade rating and that will reinforce the current standing of Phil vs. peer investment grade countries. Thirdly, we note especially the return of foreign funds whose net inflow from early last Feb (Feb 4, 2014) up to last (April 25, 2014) reached Php35bn, surpassing last year's total net funds outflow of Php28bn. The flow will support our target PSEi range.

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 benign 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. ▲

Manila Electric Company (MER):

1Q14 Industrial Energy Sales up +5.2%, But Core Income Flat on Lower Tariff and +2% Overall Volume

MER Stock Data	
Price (PHP)	280.80
Market Cap (PHP Bn)	314.69
Outstanding shares (Bn)	1.13
2014E PE (X)	16.20
Price to Book (X)	4.21

Source: Bloomberg

Industrial Sector Stands Out

Meralco posted core net income of Php4.1bn in 1Q14, flat vs year ago's Php4.0bn while overall sales volume improved by 2%. But industrial energy sales were notably higher, +5.7% year-on-year (yoy), with strong demand from the manufacturing sector, basic metals, rubber and plastics. Commercial demand was also higher, +2.2% due to the hotel, mall, hospital expansions. The drop in residential sales was the swing factor that led to the overall 1.7% growth in 1Q14 energy sales, dropping to a historic low of residential share of the sales mix to just 27.9% from 30%. See table 1 below. That has never happened in the past based on management recollection, attributing it to a combination of colder 1Q14, perceived high electricity prices due to the generation charge TRO controversy. Distribution tariff was also lower at Php1.63/kwh from Php1.65/kwh a year ago due to the sales mix being more of industrial. Industrial customers are billed cheaper than residential and commercial accounts based on the regulatory framework performance base rate system (PBR). Overall customer count grew 3.5% to 5.4m. Php45m were realized from equity in earnings of the 20% investment in Global Busines Power. Management won't give the extent of income from 28%-owned Singapore-based genco Pacific Light. Consolidated expenses were up 9% yoy due to manpower hiring by subsidiaries, project expansions entailing taxes and licenses: (San Buenaventura's 450MW coal-fired plant in Mauban, Quezon in partnership with EGCO of Thailand), EPC and other permits for Redondo Peninsula Energy. Cash is a robust Php60bn. Debt is Php35bn. Gearing is 0.40.

Seasonality

IQ is seasonally down in terms of energy sales due to the weather cycle and post-holiday season, but the stronger quarters such as the summer months in 2Q and late 3Q up to 4Q holiday will compensate. 1Q is definitely not representative of the entire year, management clarified. MER's 2014 full year net profit earnings growth consensus forecast is 14.7% to Php19.5bn. Forward PE is 15.81x, below market of 18.4x.
There is no profit guidance yet.

Outlook

There is a base 11MW consumption of Solaire to which will add Belle Corp's City of Dreams' hotel casino's 3Q opening and that of Solaire's expansion involving 300 more VIP hotel rooms, same period, for an expected energy sales of 35MW in 4Q14. Tiger Hotel's Manila Bay Resorts, a hotel and casino project, one in the four located in Pagcor City, will add to next year's demand for electricity. JGS' Petrochemical plant will connect to the Meralco grid with 35MW demand late in the year. The industrial sector will continue to drive energy sales based on management view. On the other hand, the newly contracted interim power supply should keep electricity rates affordable in the summer months and improve the electricity price perception of the residential sector leading to segment recovery back to its 30% share in the sales mix.

We think increasing demand for retail space, housing, residential high-rise due to Phil demographic trends, rising affluence and growing urbanization point to increased energy sales. Meralco is building 3,000 MW power generation capacity to meet that demand by 2018-2020, which is within the 30% ownership limit of the Luzon grid. The huge surge of electricity demand expected in the hotter summer months this year given the El Nino forecast will be met with 474MW of contracted interim power supply at peaking rates of Php11-12/kwh (four months only this year) from Pan Asia, Toledo Power, and two more suppliers, ensuring sales volume support. ▲

Energy Sales Mix by Sector

Sector	Energy sales mix	Energy sales growth
Commercial	39.4%	+2.2%
Industrial	32.2%	+5.7%
Residential	27.9%	-3.3%

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