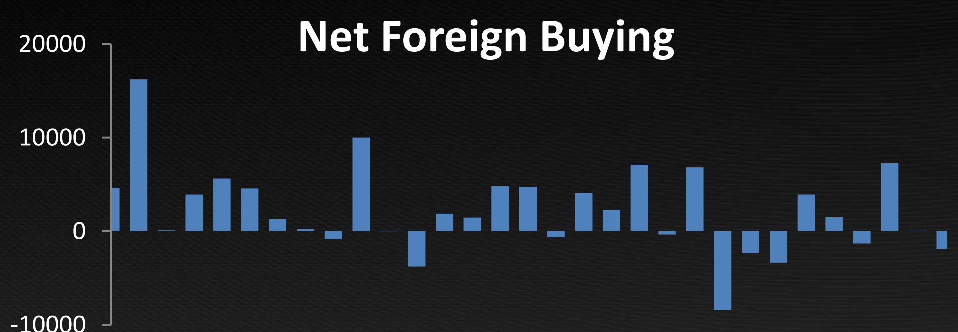

THE TIDES OF OPPORTUNITY
2013 COL-MID YEAR MARKET BRIEFING
APRIL LYNN TAN, CFA
VP & HEAD OF RESEARCH
COL FINANCIAL
PHILIPPINES

Fund Flows Cause Significant Market Volatility



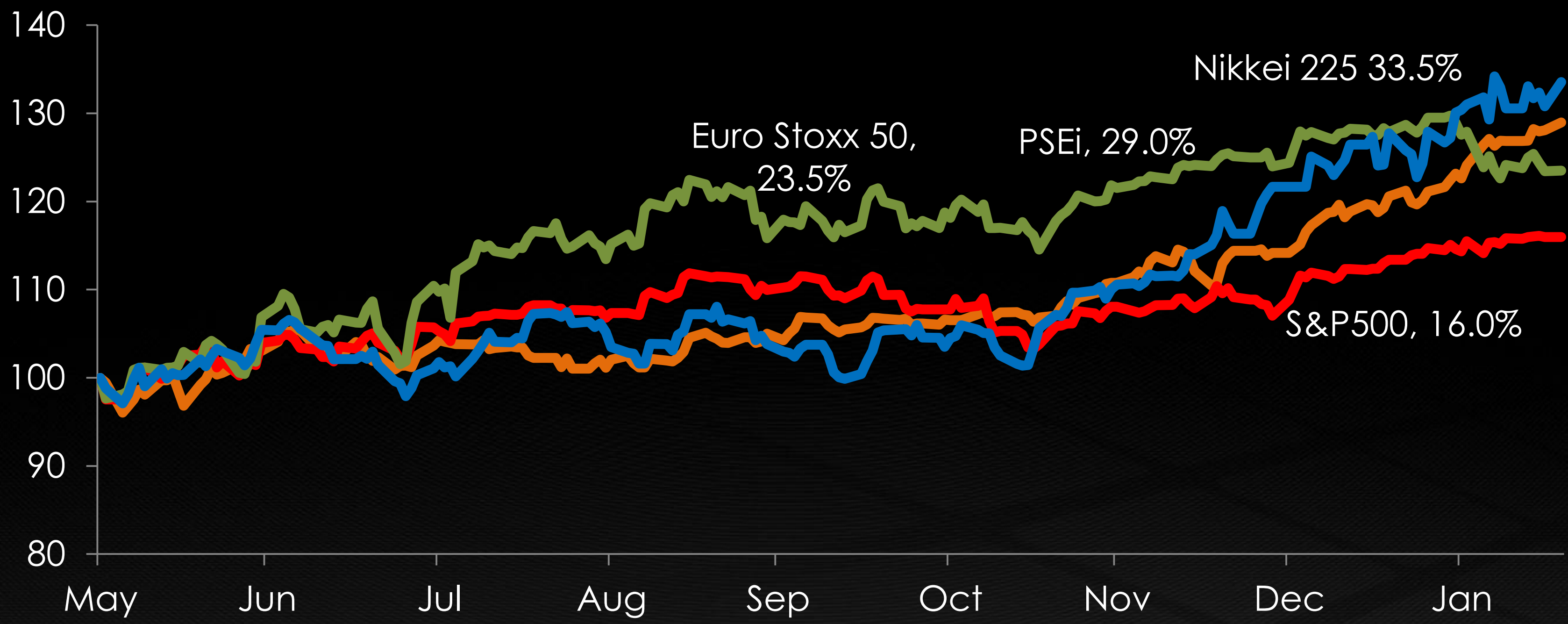
PSEi is up by 14% for the year to date period, after rising by as much 27% and falling by almost 1%, as foreign funds flowed in and out of the market

Source: Bloomberg

In the business of trust.

“High Tide Lifts all Boats”

Performance of Global Markets (June 2012 to April 2013)



Source: Bloomberg

Liquidity drove equity markets higher from mid 2012 to April 2013

“High Tide Lifts all Boats”

Examples of Liquidity Enhancing Measures

Europe: Outright Monetary Transaction or OMT (Aug 2012)

USA: QE 3 (Sept 2012), Add’l bond buying program from US$40 Bil to US$85 Bil (Dec 2012)

Japan: Abenomics (Dec 2012)

Philippines: SDA rate cuts – 100 bps (2012), 150 bps (2013)

Prospects of Reduced Liquidity Trigger Global Sell-off in May and June

Timeline of News on Tapering of US Fed Bond Buying Program

May 22: Fed minutes noted that a number of participants expressed willingness to reduce QE as early as June

June 19: Bernanke said the Fed may begin reducing the pace of purchases "later this year" and may end the program about the middle of 2014, assuming the economy performs as forecast by the Fed

Prospects of Reduced Liquidity Trigger Global Sell-off in May and June

Global Indices Correction from Peak to Trough

Country/Index	Index		% Change
	Peak	Trough	
Philippines (PSEi)	7,403	5,679	-23
Thailand (SET)	1,650	1,339	-19
Indonesia (JCI)	5,295	4,289	-18
Japan (Nikkei 225)	15,943	10,375	-35
USA (S&P 500)	1,687	1,573	-7
Europe (Euro Stoxx 50)	2,851	2,495	-13

Source: Bloomberg

Prospects of Reduced Liquidity Trigger Global Sell-off in May and June

July 17: Bernanke Clarifies his Statement on Tapering of Bond Buy Back Program

"Our asset purchases depend on economic and financial developments, but they are by no means on a preset course"

Source: Kingdom Economics

Improving Relative Growth Outlook of DM Leading to Shift in Fund Flows

Relative Performance of Global Markets (July M/M)

Country/Index	% Change
Philippines (PSEi)	2.7
Thailand (SET)	-3.1
Indonesia (JCI)	-5.0
Japan (Nikkei 225)	-0.1
USA (S&P 500)	5.0
Europe (Euro Stoxx 50)	6.0

Source: Bloomberg

Improving Relative Growth Outlook of DM Leading to Shift in Fund Flows

ST Risks in EM Asia

- GDP growth slows as exports are hurt by China's slow down
- Currencies weaken due to deteriorating current account position and foreign fund outflows
- Interest rates increase due to rising inflation, and the need to defend the currency

ST Opportunities in DM

- US GDP growth outlook improving due to recovery of housing market and favorable liquidity conditions
- "Green shoots" of economic recovery in Europe
- Dollar to strengthening due to stronger economic outlook, expected tapering of Fed QE

Strong Philippine Fundamentals to Justify Continuous Increase of PSEi

- Favorable Economic Growth Outlook
- Less Vulnerable to Risks Facing EM Asian Economies
- BSP to Limit Access to SDA

Favorable GDP Growth Outlook

Strong and Resilient GDP Growth

	Philippines	World
2008	4.2	1.5
2009	1.1	-2.4
2010	7.6	4.0
2011	3.9	2.9
2012	6.6	2.3
1Q13	7.8	2.7

Source: Bloomberg, IMF

Favorable GDP Growth Outlook

1Q13 GDP Growth

Expenditure	Growth
Consumer	5.1
Government	13.2
Capital Formation	47.7
Fixed capital	16.8
Construction	33.7
Durable Equipment	9.4
Others	83.3
Net Exports	-95.7
GDP	7.8
GNI	7.1

Source: NSCB

- Better than expected
- Fastest in Asia
- Robust growth of capital formation to pave the way for a more sustainable increase in GDP

Favorable GDP Growth Outlook

Strong Performance to be Sustained

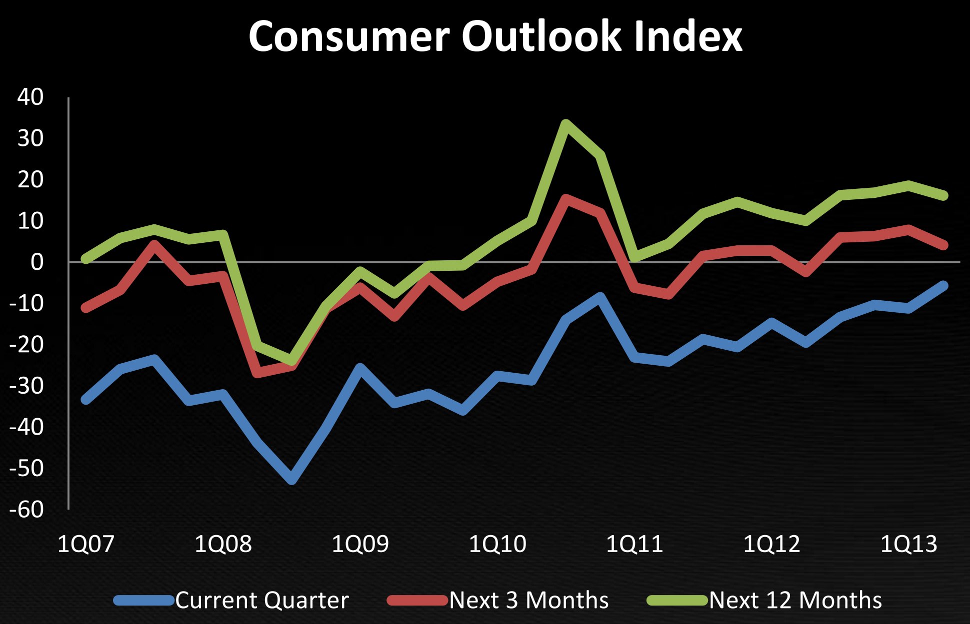
Consumer Spending (+)	Investment Spending (+)
Government Spending (+)	Exports (-)

Drivers of Consumer Spending

- Strong consumer confidence
- Resilient OFW Remittances and BPO sector
- Weaker peso and benign inflation
- Philippines to enter demographic window

Drivers of Consumer Spending

Consumer Confidence Hits All-Time High



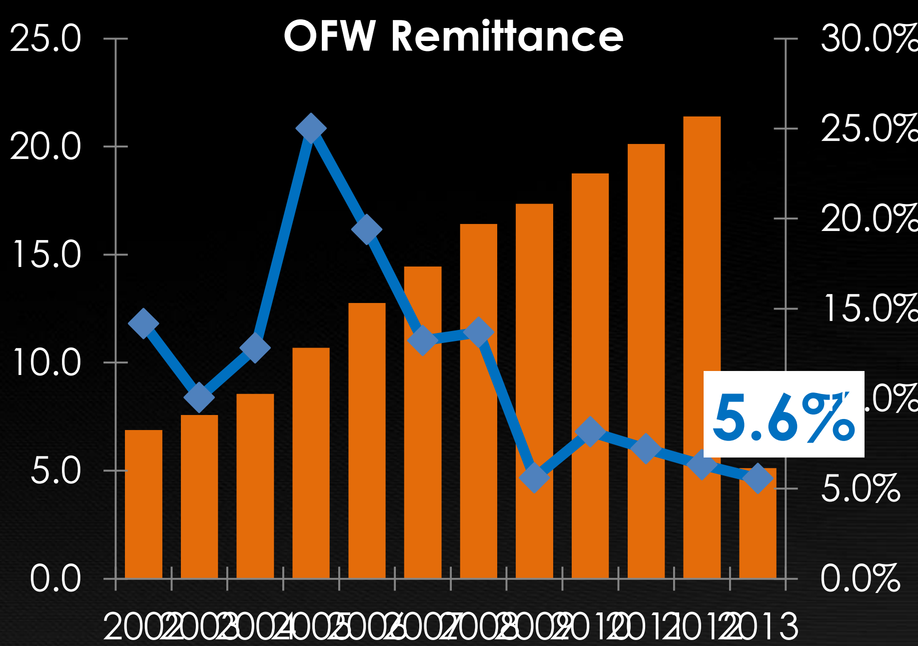
Source: BSP

Reasons for Improvement in Consumer Confidence

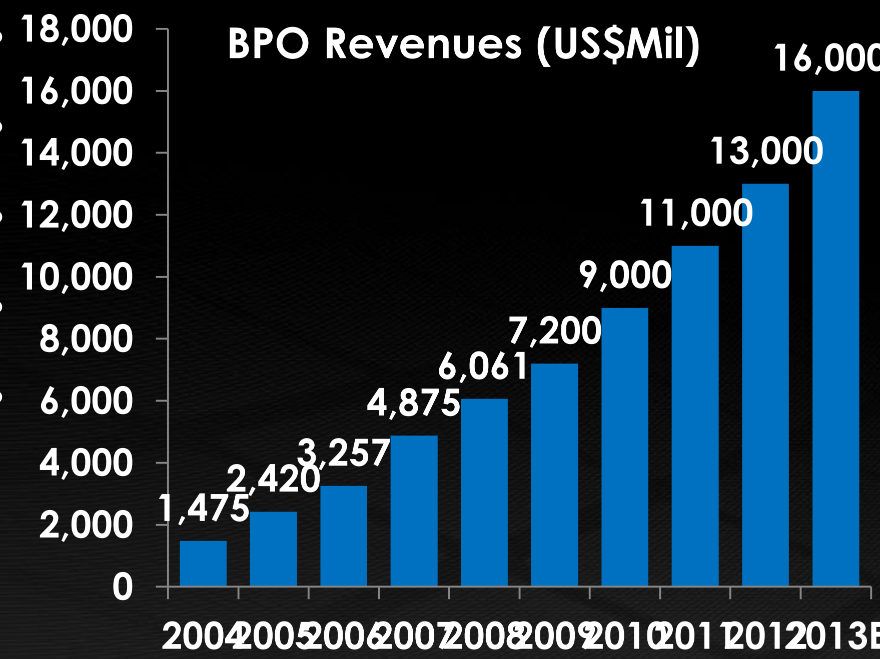
- Better job opportunities
- Increased investment inflows
- Salary increases

Drivers of Consumer Spending

OFW Remittances and BPO Revenues Continue to Increase



Source: BSP



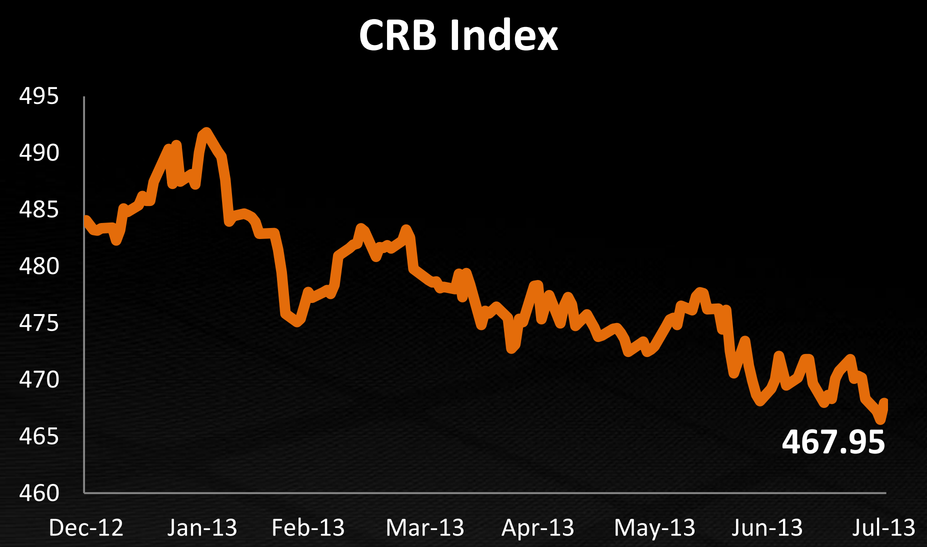
Source: BPAP

COL FINANCIAL PHILIPPINES

In the business of trust.

Drivers of Consumer Spending

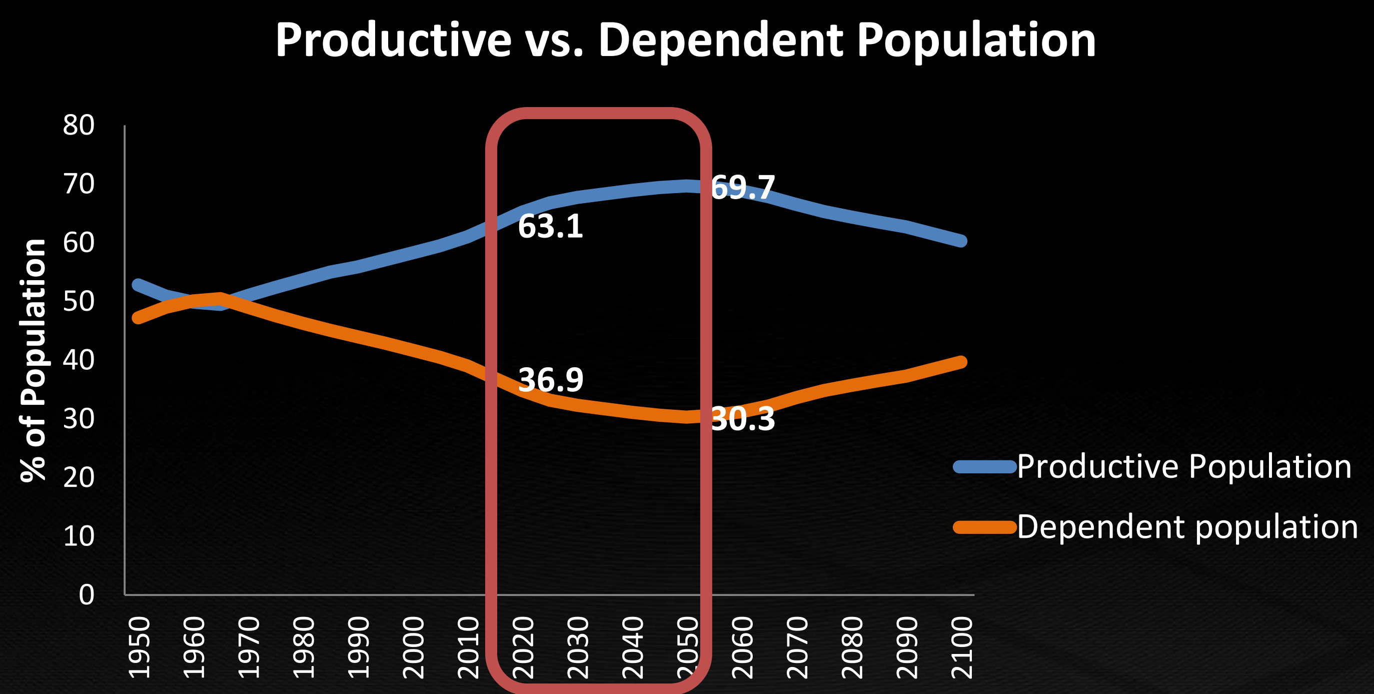
Weaker Peso and Benign Inflation to Boost Spending Power



Peso weaker by 5.6%, while CRB index down by 3.3%

Source: Bloomberg

Drivers of Consumer Spending



Source: UN

Philippines about to enter "demographic window"

Drivers of Consumer Spending

What is “Demographic Window”?

- Period of high economic growth brought about by a growing number of people entering the productive ages of 15 to 64
- Children below 15 <30%, Elderly above 64 <15%
- Economies of countries that had entered the demographic window grew by an average of 7.3% in the first decade alone
- Demographic window expected to open in 2015, and last until 2050, as the working population reaches 63% in 2015 and peaks at 69% by 2040-2055

Drivers of Consumer Spending

Philippine Population Statistics				
Population Growth	1.8%			
Median Age	23.3			
Age	**% of Population**			**Growth**
	2013	**2015**	**2055**	**2015-2055**
0 – 14	34.0%	**32.8%**	19.5%	-19.8%
15 – 64	61.6%	63.1%	**69.7%**	**48.0%**
65 & Above	4.4%	4.1%	10.8%	252.1%

Source: CIA World Fact Book, UN

- Population below 15 to drop below 30% after 2015
- From 2015-55, productive population will grow by 48% while dependent population will grow by only 11%
- Productive population will peak at 69.7% in 2055

Drivers of Investment Spending

- Credit Ratings Upgrade
- Strong Business Confidence
- Strong and Liquid Banking System
- Favorable Regional Developments
- Growing Pipeline of PPP Projects

Drivers of Investment Spending

Fitch & S&P Upgrade Philippines Rating to Investment Grade; Moody's to Follow Suit

Ratings Agency	Rating	Upgrade Date
Fitch	BB+	Jun-11
	BBB-	Mar-13
S&P	BB	Nov-10
	BB+	Jul-12
	Outlook from "stable" to "positive"	Dec-12
	BBB-	Apr-13
Moody's	Ba2	Jun-11
	Ba1	Oct-12
	Review for possible upgrade	Jul-13

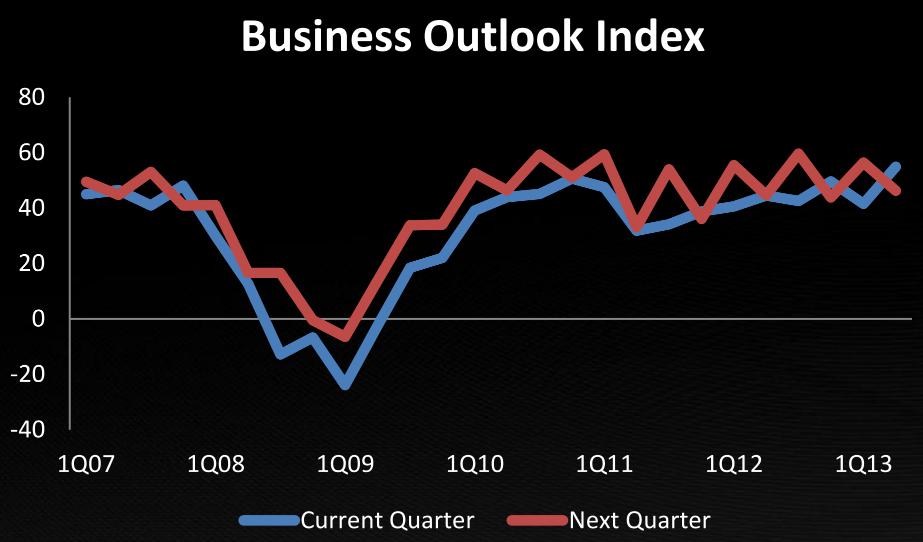
Drivers of Investment Spending

Implications of the Ratings Upgrade

- Philippines now radar screen of more foreigner investors
- To help ensure that funding cost stays low
- To lead to more investments, higher GDP growth, higher stock market

Drivers of Investment Spending

Business Sentiment Hits an All-Time High



Source: BSP

Reasons for Improvement in Business Sentiment (ex Seasonal Factors)

- Expansion of businesses
- Country's strong macroeconomic fundamentals
- Credit rating upgrade

Drivers of Investment Spending

Strong and Liquid Financial System to Fund Investment Spending Growth

Banking Statistics (Universal & Commercial Banks)				
	NPL Ratio	**Provision/ NPL**	**Loans/ Deposit**	**Loans/ Deposit + SDA**
2010	2.9%	118.3%	62.6%	49.1%
2011	2.2%	126.4%	68.4%	50.9%
2012	1.9%	141.5%	71.6%	53.9%

Capital Adequacy Ratio		
Minimum Requirement	BSP	10.0%
	Basel III (2014)	10.0%
Philippine Banks (2012)		17.3%

Source: BSP

Drivers of Investment Spending

Favorable Regional Developments

- Significant increase in minimum wages
    - *China, Thailand and Indonesia*
- Floods in Thailand
- Growing tension between China and Japan

- *FDI in Philippines +54% in 2012 to US$2.8 Bil; alreadyUS$1.3 Bil during first four months of 2013*
- *Investment pledges +39% in 1H13*

Drivers of Investment Spending

Growing Pipeline of PPP Projects

Value of PPP Projects Awarded So Far

Awarded Projects	Value (PhpBil)	Date Awarded
Daang Hari-SLEx Link Road	2.0	2011
PPP for School Infrastructure Project (Phase I)	16.4	2012
NAIA Expressway Project	15.5	2013

Source: PPP Center

Drivers of Investment Spending

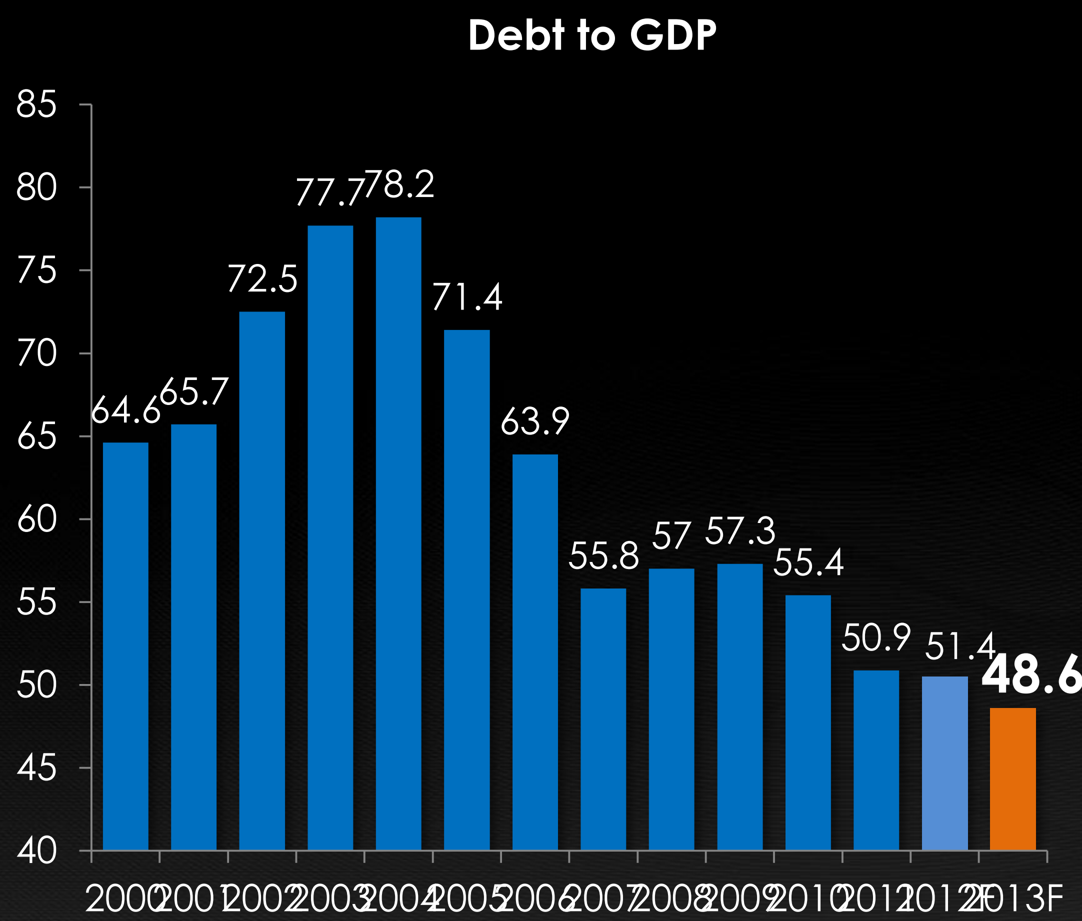
Growing Pipeline of PPP Projects

Value of PPP Projects to be Awarded Soon

Projects	Value (PhpBil)	Status
Projects with Live Bidding		Currently undergoing bidder due diligence whereby requalification documents or bidding documents are being prepared by the prospective bidders. Around 6.5 months to project award.
Modernization of the Philippine Orthopedic Center	5.7	
Talisay City Plaza Complex Restoration and Redevelopment	0.2	
LRT Line 1 Cavite Extension and O&M	60.6	
PPP for School Infrastrucutre Project (Phase II)	8.8	
Automatic Fare Collecton System (AFCS)	1.7	
Mactan-Cebu International Airport Passenger Terminal Bldg.	17.5	
Cavite-Laguna Expresway (CALAX)	35.0	
Rehabilitation, Operation & Maintenance of Angat Hydro Electric Power Plant Auxilliary Turbines 4&5	1.2	
Total	**130.7**	
NEDA Boar-Approved/LDC-Approved Projects		Invitation to prequalify and bid to be released soon
NLEx-SLEx Connector Road	25.6	

Source: PPP Center

Government Ready and Willing to Spend



Source: DBM

Improving government finances pave the way for higher spending

Government Ready and Willing to Spend

2Q13 Government Spending

In PhpBil	2Q12	2Q13	% Change
Revenues	400.0	475.1	18.8%
Expenditures	400.4	459.9	14.9%

Source: BTr

Government spending remained strong during the second quarter of the year. . .

Government Ready and Willing to Spend

2014 Proposed Government Budget (In Php Bil)

Expenditure	2013	2014	% Change
Social Services	699.4	842.8	*20.5%*
Economic Services	509.2	590.2	*15.9%*
General Public Services	347.3	364.5	*5.0%*
Debt Service	333.9	352.7	*5.6%*
Defense	89.5	92.9	*3.8%*
Net Lending	26.5	25.0	*-5.7%*
Total	2,005.8	2,268.1	*13.1%*

. . . And should remain strong in 2014, with spending on social and economic services to grow faster than total spending

Source: DBM

Less Vulnerable to Risks Facing EM Economies

GDP Growth Forecast of EM Asia

	OLD	NEW
Thailand	5.10%	4.20%
Indonesia	6.20%	5.90%
Philippines	6.00%	7.00%

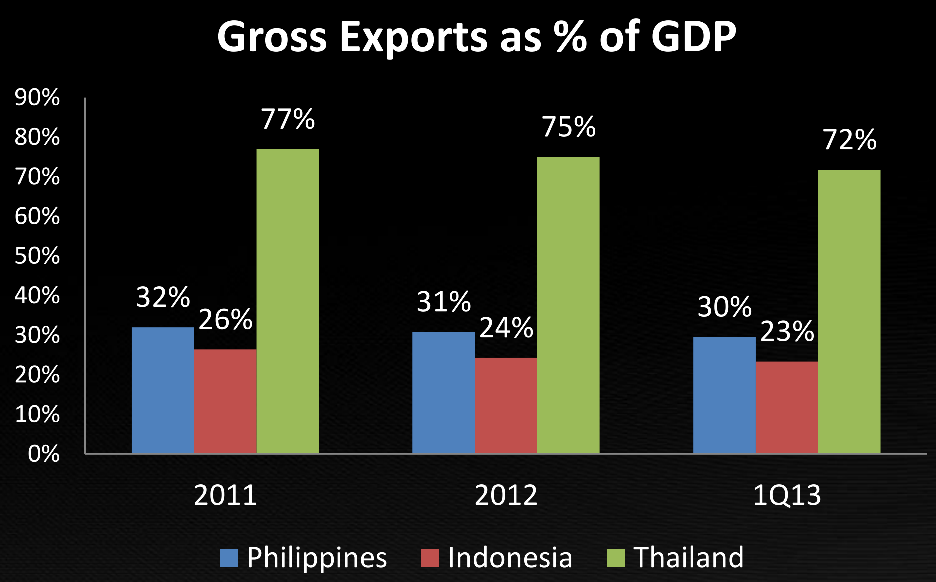
Source: Thailand – Bank of Thailand, Indonesia - World Bank, Philippines – IMF

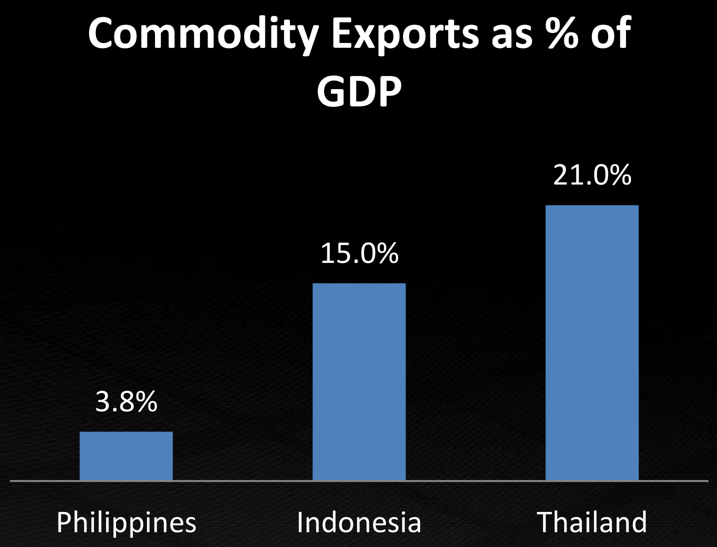
Thailand and Indonesia suffer from downgrades while Philippines enjoys upgrade

In the business of trust.

Less Vulnerable to Risks Facing EM Economies

Philippines Less Dependent on Exports, Sale of Commodities



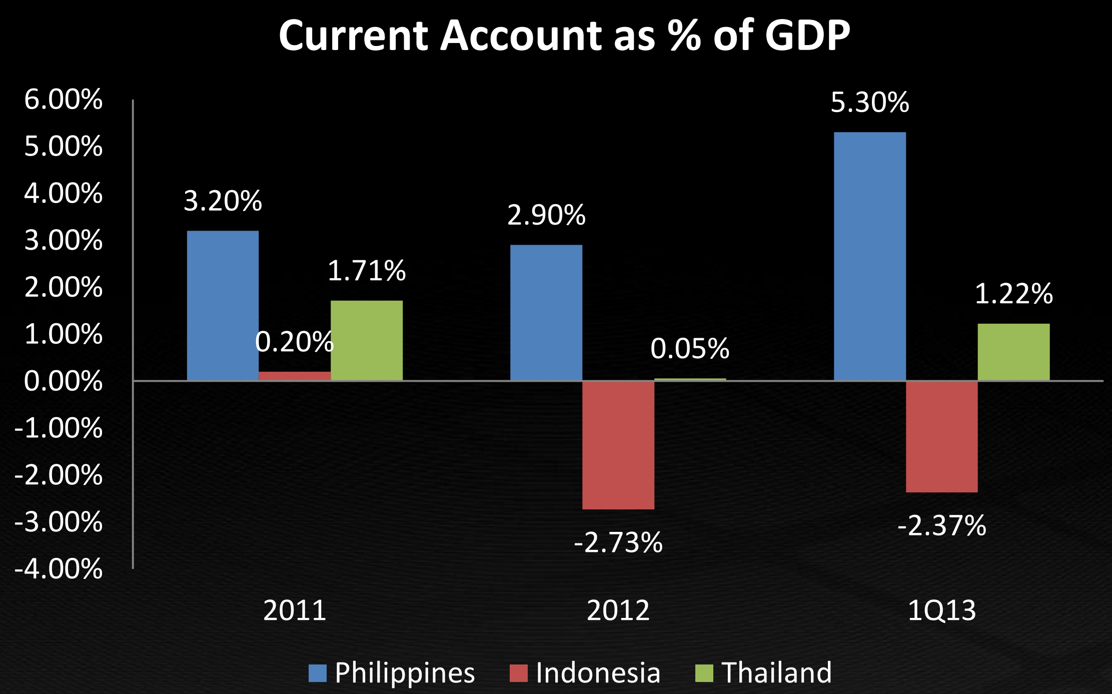


Philippines is more resilient to global economic weakness, rebalancing of Chinese economy

Source: Central Banks of TIP

Less Vulnerable to Risks Facing EM Economies

Philippines Boasts of a Very Strong Current Account Position



Strong current account position minimizes the threat of a sharp depreciation of the peso

Source: Central Banks of TIP

Less Vulnerable to Risks Facing EM Economies

Potential Increase in Interest Rates is Expected to be Minimal

- Benign inflation
- Minimal threat of a significantly weaker peso
- Release of funds from SDA to ensure ample liquidity

BSP to Limit Access to SDA

- Trust entities offering SDA exposure via "Investment Management Accounts" to be phased out by November 2013
  - *More than 50% of Php1.9 Tril worth of SDA placements suspected to be of this form*
  - *30% reduction mandated by end July*
- More funds to go into riskier assets looking for higher yields
- To help mitigate the negative impact of foreign fund outflow

COL FINANCIAL PHILIPPINES
In the business of trust.

Challenges and Risks

- Expensive Relative Valuation of the PSEi
- Earnings Growth to Slow in 2014
- Investor Sentiment Remains Poor
- Contagion
    - *Weaker currency*
    - *Rising interest rates*
    - *Volatile stock market*

Relative Valuation of Composite and Sector Indices

Relative Valuation & Index Comparison Across TIP

2013 Relative Valuation	Thailand	Indonesia	Philippines
Composite (P/E)	11.9	12.8	17.7
Consumer (P/E)	13.0	24.0	32.4
Banks (P/BV)	1.5	1.9	2.0
Property (P/E)	12.1	10.7	22.2
Power (P/E)	8.8	14.8	14.2
Telco (P/E)	19.1	16.5	17.5
Index Weight	**Thailand**	**Indonesia**	**Philippines**
Commodity Cos.	19.8%	11.2%	<1.0%

Source: Bloomberg, COL Estimates

Expensive relative valuation of the PSEi somewhat justifiable by index composition, better economic outlook

Equities Still Cheap Relative to Other Domestic Asset Classes

Comparative Yield of Different Asset Classes

Stocks	Time Deposit	SDA	10-Yr-T-Bond
5.6%	1.7% to 2.0%	2.0%	3.4%

** The PSEi's earnings yield based on 6,500*

Due to low interest rates, stocks remain the most attractive asset class even though valuations are expensive based on historical averages

Earnings Growth to Slow in 2014

2014 EPS Growth

Sector	EPS Growth
PSEi Composite	5.9%
Consumer	15.6%
Banks	0.1%
Property	13.7%
Power	3.5%
Telco	2.6%
Conglomerate	7.9%

Source: Bloomberg, COL Estimates

Focus on sectors and stocks that will continue to deliver growth

Contagion – Winners and Losers

- Philippine corporates not too vulnerable
  - *Not highly leveraged*
  - *No large refinancing requirements in the near term*
  - *Minimal exposure to dollar loans*

- Banks and airlines are most vulnerable
  - *Rising interest rates and volatile markets to hurt trading portfolio of banks*
  - *Oil prices are currently elevated and cost is denominated in US dollar*

- Telcos are major beneficiaries
  - *Weaker peso to result to higher international long distance revenues*

PSEi Scenario Analysis

PSEi Targets Under Different Scenarios

PSEi Target	Base Case*	Bear Case**
End 2013	7,500	7,250
% Upside from 6,500	15.4%	11.5%
End June 2014	7,700	7,450
% Upside from 6,500	18.5%	14.6%

**Base Case, 10-yr T-bond rate at 4.0%*

***Bear Case, 10-yr T-bond rate at 4.5%*

Strategy

- The Philippine stock market's long term uptrend remains intact given the country's solid ST and LT fundamentals, resilience to risks facing EM Asia, and the increase in liquidity that will result from the BSP's move to limit access to SDAs.
- Nevertheless, the performance of the stock market for the rest of the year could be challenging given the prevailing risk of contagion and poor investor sentiment.
- Moreover, notwithstanding the positive general outlook for the economy, not all sectors are expected to perform strongly in 2014.

Strategy

- Focus on buying companies whose earnings growth are expected to remain strong next year and who are less vulnerable to the prevailing risk of contagion.

- A staggered approach in buying stocks over the next few months should be adopted to increase the likelihood of getting a better average purchase price.

Stock Picks – Removing the Banks, Adding RLC and AC

"COLing the Shots" Model Portfolio

	Current Price	FV	Buy Date	Buy Below Price
EEI	12.50	16.50	30-Mar-12	14.35
PGOLD	40.50	48.00	11-Jun-12	41.75
AGI	26.45	28.11	11-Jan-13	24.40
MEG	3.18	4.78	11-Jan-13	4.16
TEL	3,074.00	3,500.00	11-Jan-13	3,043.00
DNL	6.78	10.00	14-Feb-13	8.70
RLC	22.70	28.17	5-Aug-13	24.50
AC	600.00	753.00	5-Aug-13	654.78

Stock Picks – Removing Banks

- We are removing BDO and Metrobank from our "COLing the Shots" model portfolio.
- Over the long term, we still like the banks since we expect them to be major beneficiaries of the economy's favorable growth outlook. We also don't expect interest rates to go up substantially and permanently to significantly hurt their trading portfolios. Valuations have also become attractive in our view.

COL FINANCIAL PHILIPPINES
In the business of trust.

Stock Picks – Removing Banks

- However, banks could underperform in the near term due to the following reasons:
  - Highly vulnerable to contagion risk as potential increase in interest rates would hurt trading gains and value of stock holders' equity.
  - Earnings growth in 2014 expected to be flat due to the normalization of trading gains.

New Stock Picks - RLC (Php22.70, FV:Php28.17)

- RLC is one of the three largest mall operators in the country. It is also involved in office leasing, hotels and residential development.

- Bulk of revenues (64%) and profits (76%) come from leasing operations which have high visibility. Mall leasing revenues are also more resilient given the attractive competitive environment the mall leasing business.

- Operating profits from residential development business are also expected to rebound after the company became more aggressive in launching projects. During 1HFY13, reservation sales grew 61%.

New Stock Picks - RLC (Php22.70, FV:Php28.17)

- EPS growth of 12.3% in FY13 and 11.1% in FY14.
- Valuations have become very attractive, after the stock was sold off due to its removal from the MSCI small cap index and the breakdown of its talks with the Okada group. Potential upside to our FV is 24%.

New Stock Picks - AC (Php600.00, FV:Php753.00)

- AC is one of the oldest and largest conglomerates in the country, owning shares in market leaders such as Ayala Land, BPI, Globe Telecom, and Manila Water.

- Aside from the said businesses, the company is taking steps to expand into the power sector. So far it has already committed around US$466 Mil out of its US$600 Mil to US$700 Mil budget for power investments. The growing share of the privately owned power segment should give investors another reason to own the conglomerate.

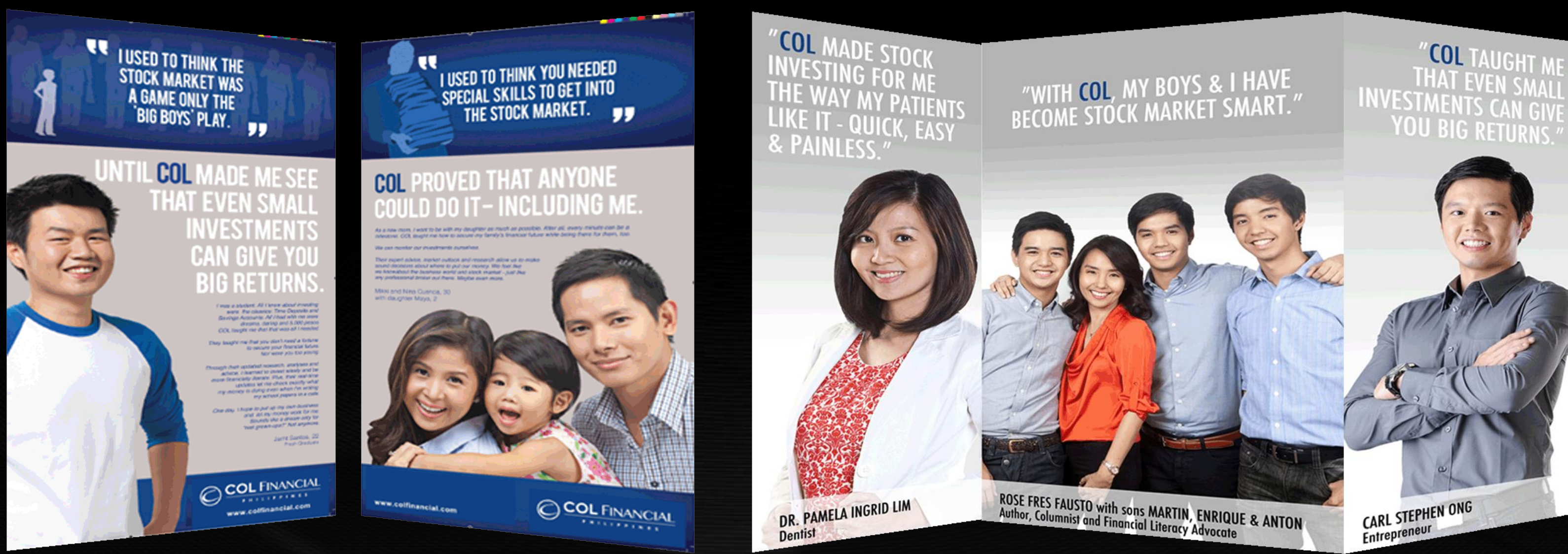
New Stock Picks - AC (Php600.00, FV:Php753.00)

- AC is also one of the major players in the bidding for PPP projects. In 2011, it won the bid for the Daang-Hari PPP project. It also expressed interest to bid for CALAx, LRT 1 extension, and the Mactan-Cebu International Airport projects.

- Potential upside to our FV is 25%.

COL FINANCIAL

HELPING YOU LIVE RICHER LIVES.



For more information visit www.colfinancial.com

COL FINANCIAL PHILIPPINES

In the business of trust.