PrimeEquity Research

Meridian Securities INCORPORATED
Member: Philippine Stock Exchange

DAILY MARKET PRIMER

10 August 2018

PSEi	Value Turnover (US$)	Net Foreign Flow (US$)	PHI:US (PLDT ADR)	US$ 1.00
7,820.71 (-0.39%)	119,398,618.08	6,090,902.27	26.01 (+0.15%) = 1,379.18	53.025

MARKET OUTLOOK

- Share prices retreated on Thursday as investors sold off positions following disappointing second-quarter gross domestic product (GDP) data and an expected central bank rate hike.
- The loss was blamed on the slower-than-expected GDP growth of 6%, which was down from 6.6% three months earlier and way below the government's 7% to 8% target for the year.
- Investors also expected the raising of interest rates which may cause some shift from equities to fixed-income markets, making it attractive this time.
- Shortly after market close, the central bank's policymaking Monetary Board decided to raise interest rates for a third time this year, this time by 50 basis points, (bps) from 25bps previously, to help temper rising inflation.
- This brought the central bank's overnight borrowing, lending and deposit rates to 4%, 4.50% and 3.50%, respectively.
- It remains to be seen how the market will react today to the central bank's decision to raise interest rates by 50bps. This move is in line with expectations which called for more aggressive moves especially with July's high 5.7% inflation figure.
- The PSEi may not have overreacted to the slower Q2 GDP (gross domestic product) since some of the biggest blue-chip stocks have reported positive earnings. So these companies are weathering the slowing GDP figures and rising inflation rate.
- Investor mindset has been predicated on a strong economy and a longer-term perspective.
- However, the market is expected to continue digesting the disappointing GDP news.

ECONOMIC HIGHLIGHTS

Policy Rate Hike

- The central bank raised rates anew yesterday in a more aggressive move as expected, to temper inflation amid signals that prices could remain elevated until next year.
- The Monetary Board raised policy rates by 50 basis points (bp) on Thursday, marking the third consecutive tightening move this year as policy makers wanted to rein in price expectations.
- This is also the central bank's strongest response in a decade. The last time the central bank raised rates by 50bp in one go was in July 2008, which saw inflation surge to a 17-year high at 12.2% against a 3% to 5% target that year.
- Rates now stand at 4.5% for the overnight lending rate, 4% for the overnight reverse repurchase rate, and 3.5% for the overnight deposit rate.
- In deciding to raise the central bank's policy rate anew, the Monetary Board noted that latest baseline forecasts have shifted higher over the policy horizon, indicating some risk of inflation exceeding the target in 2019.
- The central bank tightened rates by 25bp each during its May and June meetings, at a time when monthly inflation started to log beyond 4%.
- Inflation expectations — which play a huge part in terms of price movements — remain "elevated" as of now. The stronger adjustment is likewise seen to "prevent sustained supply-side price pressures," even after previous tightening moves.

ECONOMIC INDICATORS					
GDP Growth Rate	6.0% (Q2 2018)	Unemployment Rate	5.5%% (April 2018)	GIR	US$76.892-B (July 2018)
Fiscal Surplus / (Deficit)	(P54.3-B) (June 2018)	Exports Growth Rate	(0.1%) (June 2018)	BOP	(US$1.177-B) (June 2018)
Inflation	5.7% (2012 BY) (July 2018)	Imports Growth Rate	24.2% (June 2018)	O/N RP	4.50% (as of August 9, 2018)
91-day T-Bill Rate	3.219(as of July 23, 2018)	Cash Remittances	US$2.469-B (May 2018)	O/N RRP	4.00% (as of August 9, 2018)

ECONOMIC CALENDAR

Friday, August 10
- Industrial production (JUNE)

Wednesday, August 22
- Budget balance (JULY)

ECONOMIC HIGHLIGHTS (continued)

Policy Rate Hike (continued)

- Prices of widely used goods surged to 5.7% in July, beating market expectations which brought the seven-month average to 4.5%, well above the 2% to 4% target range.
- All 14 economists polled last week were sure that the central bank will raise interest rates this week, but were torn as to whether it will involve a typical 25bp increase or stronger. More analysts bet on a 50bp hike following the release of July inflation data on Tuesday.
- The Monetary Board believed that the series of policy rate adjustments thus far in 2018 will help reduce further the risks to inflation. Favorable conditions arising from sustained domestic growth also suggest that the economy can accommodate a further tightening of monetary policy settings.
- Thursday's move is also in keeping with the central bank chief's hints of a "strong policy response," versus a "measured" approach previously.
- Meanwhile, the central bank has let go of plans to reduce bank reserves, saying that the 200bps cut introduced this year is sufficient for now. The central bank will introduce fresh reserve cuts by next year, or when inflation returns to within target.
- The central bank also expects further price spikes over the coming months.
- The central bank sees inflation averaging 4.9% this year, versus a 4.5% estimate during its June meeting. The pickup is due to the P1 provisional increase in jeepney fares, higher water rates, the scheduled increase in tobacco excise tax, and higher Dubai oil prices.
- By 2019, inflation will ease to 3.7%, although faster than the previous 3.3% forecast. Inflation is also seen to average 3.2% by 2020, against a 2% to 4% target range.
- The central bank also noted the need for other government agencies to implement "non-monetary measures" to soften future price increases. The latest estimates do not factor in the passage of the rice tariffication bill, which the central bank said could bring down inflation by 0.2% if implemented during Q4.
- The measure can also trim inflation down by 0.6% for 2019 once cheaper rice is imported to augment dwindling supply of the staple. Rice accounts for nearly a tenth of the consumer basket used in measuring inflation.
- While inflation is currently "on the high side," authorities are carefully watching developments and is ready to take necessary actions "as needed."
- Central bank officials are confident the tightening moves — which cumulatively raised rates by 100bps so far this year — will not stunt overall economic growth.
- The central bank argues that focusing on inflation right now is not necessarily anti-growth. One can argue it will sustain growth over the medium term.
- The Philippine economy expanded by 6% during Q2, well below market expectations and the state's 7% to 8% goal. Still, the central bank said the Philippine economy "continues to be strong" and can weather higher borrowing rates.
- The central bank noted there are signs that lending rates "have started rising" to mirror upward adjustments in the benchmark rate, although pointed out that money supply remains "adequate."
- Still, bank analysts said this might not be the last tightening move from the central bank.

Full-year Growth Target

- The Philippine economy grew to its slowest pace in three years in Q2, leading some analysts to downgrade their forecasts despite the country remaining as one of Asia's fastest-growing economies.
- Gross domestic product (GDP) — the total amount of final goods and services produced within the country — grew 6% in the three months to June, lower than the revised 6.6% growth recorded in the same period in 2017, according to data released by the Philippine Statistics Authority yesterday.

ECONOMIC HIGHLIGHTS (continued)

Full-year Growth Target (continued)

- The Q2 result was also below the revised 6.6% in Q1 and the 6.8% median estimate in a poll last week.
- This is the slowest pace since the second quarter of 2015 when it recorded a 5.6% growth.
- Year-to-date, GDP in H1 by 6.3%, which is also below the government's 7% to 8% target band for 2018.
- Gross national income — the sum of the nation's GDP and net income received from overseas — recorded a growth of 5.8% in Q2, down from 6.6% previously.
- Socioeconomic Planning Secretary Ernesto M. Pernia said the economy would have to grow "by at least 7.7%" in H2 to reach the low-end of the government's growth target for this year.
- Mr. Pernia cited "policy decisions" in contributing partly to the economic slowdown such as the temporary closure of Boracay Island, and regulations affecting the mining industry such as excise tax on metallic and non-metallic minerals.
- Services — the country's mainstay that accounted for almost half of GDP — led growth among major sectors at 6.6%, faster than the 6.4% recorded in the same period last year.
- Meanwhile, industry posted a 6.3% growth, slower than the 7.1% print in 2017.
- Manufacturing remained the top contributor to industry growth even as it slowed down to 5.6% from the 7.6% growth in Q1 and 8% in Q2 of 2017, chipping in 3.7 percentage points to the 6.3% industry growth.
- The construction sector grew by 13.5% in Q2 compared to last year's 4.3% and 8.8% in Q1.
- Mining and quarrying, meanwhile, went the other direction as it declined by 10.9% versus the 6.9% expansion seen in Q1 and the 19.2% growth in Q2 of 2017.
- Agriculture also grew albeit marginally at 0.2% versus the 6.3% growth posted a year ago.
- On the expenditure side, household spending — which made up roughly 56% of Q2 GDP — was up 5.6% in Q2, slower than the 6% growth logged in Q2 of 2017.
- Exports of goods and services expanded at a slower pace of 13% compared to 2017's 21.4%. Imports, meanwhile, grew 19.7% from 18.6%.
- On the other hand, government spending went up by 11.9%, slower than the 13.6% in Q1, but faster than the 7.6% in Q2 of 2017.
- Capital formation, which is a measure of private investment, posted faster growth at 20.7% compared to 12.4% in Q1 and 7.6% last year.
- Market players now expect a slower full-year expansion for the country this year following Q2 growth turnout, noting that times have turned more "challenging" for the economy amid rising prices.
- Bank economists said they now see full-year GDP growth to be slower than their initial forecasts, leaving slimmer chances to hit the government's 7% to 8% goal and could even settle below the 6.7% pace logged in 2017.
- ANZ Research has scaled down its forecast to 6.6% from 6.8% following the first semester print, amid concerns on the trend for domestic demand as well as net exports.
- ING Bank N.V. Manila was likewise of the same sentiment: Downward revisions of 2018 GDP forecast are necessary not only as a result of the downside surprise of Q2 and the downward revision of Q1 GDP growth.
- Previously, ING expects full-year growth at 6.8%.
- The weaker peso — which has traded above P53 versus the dollar since June — has "not encouraged" significant investments in the export sector. It has likewise failed to lift outbound shipments of goods despite bigger valuations during H1 of the year.
- A widening trade imbalance and soft farm output have dragged overall economic activity, aggravated by high inflation which "could have dampened household spending.
- Nomura also flagged a possible scaling down of their 6.9% growth estimate for 2018 given dismal turnout for agriculture, mining, manufacturing and services.
- Still, it expects an acceleration of growth in H2, led by investment spending as the government makes more progress in implementing infrastructure projects, which should crowd-in private sector spending.
- Looking ahead, Capital Economics expects the slowdown in GDP growth to continue over H2 of this year as tighter monetary policy and higher inflation weighed on consumer spending.

CORPORATE NEWS

TEL

- A group of foreign private equity investors is looking to acquire a majority stake in Voyager Innovations, Inc., according to PLDT.
- The telecommunications giant has four weeks to finalize deal with the foreign group over the Voyager investment.
- The sale of Voyager, which registered a P1.3-bil loss in the first six months of 2018, is expected to have a positive impact on PLDT's financials.
- The company declined to name the investors, except to say they are involved in financial technology.
- PLDT is likely to remain the single largest investor in Voyager with its investment of P9-bil to P10-bil so far, but the foreign investors as a group would take a majority share when the deal is done. PLDT will retain a 45% stake in Voyager.
- On Thursday, the telecommunications giant reported its attributable net income dropped 58% to P4.862-bil in Q2, from P11.56-bil during the same period a year ago. Last year's figure included proceeds from the sale of its equity interest in Beacon Electric Asset Holdings, Inc.
- For H1, attributable net income fell 29% to P11.76-bil, "primarily due to lower net income from wireless and other businesses, partly offset by higher net income from fixed line business."
- Excluding non-recurring items, the six-month core profit dropped 25% to P13.13-bil. PLDT maintained a full-year core income guidance of P23-bil to P24-bil, excluding Voyager.
- Revenues rose 5% to P41.73-bil in the April to June period, bringing the six-month tally 4% higher to P82.2-bil.
- The company said this was "primarily due to higher revenues from data services in the fixed line business, as well as higher non-service revenues from the wireless and fixed line businesses, partially offset by lower revenues from mobile and home broadband services in the wireless business."
- For H1, data/broadband and digital services accounted for P39.6-bil in revenues, representing 54% of the total service revenues.
- Fixed broadband revenues grew 58% to P13.2-bil; mobile internet rose 29% to P12.3-bil; and corporate data and data center generated P10.9-bil in revenues, up 13%.
- By business unit, PLDT Home recorded a 14% increase in revenue during the January to June period to P18-bil, fueled by a strong demand for fiber-powered broadband service.
- PLDT Enterprise revenues went up 9% to P18.7-bil in H1, driven by higher wireless data, cloud and other services.
- The Individual Wireless business group's revenues jumped 2% to P29.9-bil, as mobile data revenues grew.

PSE

- There will be no changes in the 30 companies comprising the Philippine Stock Exchange index (PSEi), the bourse operator said on Thursday.
- The Philippine Stock Exchange, Inc. (PSE) said the result was derived from its review covering the July 2017 to June 2018 period.
- Considered a local barometer for investor confidence, the PSEi should be composed of top companies based on liquidity and full market capitalization, and have a free float level of at least 15%.
- Among the sub-indices, the financial index was the lone sector that remained unchanged after the review. Three firms will be added to the industrial index, namely Ginebra San Miguel, Inc., PetroEnergy Resources Corp., and Pepsi-Cola Products Philippines, Inc. They replace Alsons Consolidated Resources, Inc., San Miguel Food and Beverage, Inc., and Phinma Energy Corporation.
- The PSE has increased the number of companies under the holding firms index to 15, adding Prime Orion Philippines, Inc. and Solid Group, Inc. For property, Cebu Landmasters, Inc and Philippine Estates Corp. have been added, while Sta. Lucia Land, Inc. was removed.
- Boulevard Holdings, Inc., Golden Bria Holdings, Inc., and IPM Holdings, Inc. have been dropped from the Services Index, with Philippine Seven Corp. and Wilcon Depot, Inc. added in their place.
- Lastly, the PSE removed Atlas Consolidated Mining and Development Corp. and Lepanto Consolidated Mining Co. from the mining and oil index.
- The changes will be implemented starting Aug. 20.

CORPORATE NEWS (continued)

SMC

- Diversified conglomerate San Miguel Corp. (SMC) grew its recurring profit by 29% in the first six months of 2018, following higher volumes and favorable selling prices across its units.
- SMC reported a recurring net income of P35.5-bil as of end-June, supported by a 27% jump in consolidated revenues to P499-bil.
- The listed company said that including the impacts of mark-to-market losses due to foreign exchange translation, net income would have stood at P27.6-bil, 6% higher year-on-year.
- SMC's core interests are in food and beverage, power, fuel and oil, and infrastructure.
- The newly consolidated food and beverage arm under San Miguel Food and Beverage, Inc. (SMFB) delivered a 20% increase in net income to P15.4-bil. This followed a 15% uptick in combined sales revenues to P137.4-bil.
- The food business alone generated a profit of P3.1-bil, as consolidated revenues went up 12.4% to P62.9-bil due to the strength of its agro-industrial and branded value-added businesses.
- The beer unit through San Miguel Brewery, Inc. expanded its revenues by 18% to P62.5-bil. Its net income accordingly grew by 26% to P11.3-bil for the first semester.
- Ginebra San Miguel, Inc. posted a net income of P506-mil, after revenues went up 19% to P12-bil due to the growth of its Ginebra San Miguel and Vino Kulafu brands.
- Petron Corp. exhibited profit growth of 16% to P9.5-bil from January to June, fueled by the sales volumes from both Philippine and Malaysian operations. The company also benefited from the rising prices of crude oil and finished products.
- Petron's consolidated revenues reached P273.5-bil, 32% higher than the P207-bil it logged in the same period a year ago.
- Meanwhile, SMC Global Power Holdings Corp. saw its consolidated revenues climb by 41% to 57.4-bil.
- The power unit's operating income stood at P17-bil for H1, 28% higher than the P13.3-bil it posted in the same period a year ago.
- For the packaging business, the San Miguel Yamamura Packaging Group expanded its operating income by 17% to P1.6-bil in the first semester. Sales revenues went up by a fourth to P17.6-bil following strong sales from the glass, plastics, and metal products. The company also noted the positive performance of its Australian operations.
- The infrastructure business also recorded an 11% increase in consolidated revenues to P12.1-bil, as the company saw higher traffic volume from its operating toll roads. These include the South Luzon Expressway, Skyway Stage 1 and 2, and the Ninoy Aquino International Airport Expressway. Its operating income likewise gained 19% to P6.2-bil.

CEB

- Cebu Air, Inc. reported a 39% drop in net profit to P1.87-bil in Q2, weighed down by rising fuel prices and weakening of the peso.
- The listed operator of Cebu Pacific said its net income for the first six months fell 24% to P3.309-bil, from P4.334-bil recorded in the same period last year.
- Q2 revenues went up 4% to P19.57-bil, while H1 tally increased 6% to P35.65-bil. Passenger revenues rose by 2% to P14.6-bil in the April to June, and by 6% to P28.3-bil in the six-month period.
- However, expenses grew at a faster clip, jumping by 16% to P17.06-bil in Q2, and by 14% to P33.06-bil in H1.
- The bulk of expenses came from flying operations, which soared by 21% to P7.61-bil in Q2, and by 18% to P14.53-bil in the six months ending June.

GOLD BUYING / Troy Oz.	COPPER BUYING / lb.
US$1,214.20	US$2.764

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