PrimeEquity Research

Meridian Securities INCORPORATED

Member: Philippine Stock Exchange

DAILY MARKET PRIMER

13 August 2018

PSEi	Value Turnover (US$)	Net Foreign Flow (US$)	PHI:US (PLDT ADR)	US$ 1.00
7,804.98 (-0.20%)	156,847,513.42	(9,714,074.24)	25.29 (-2.77%) = 1,343.08	53.107

MARKET OUTLOOK

- The stock market will likely keep trading lower as investors continue to digest last week's growth and inflation surprises and the latest central bank rate hike.
- The PSEi is currently up 1.7% for the month and after trading sideways last week, there is strong indication of a pullback this week. Investors will continue to factor in the disappointing economic numbers from last week that fell short of most analysts' expectations.
- The Philippine Statistics Authority (PSA) reported on Tuesday that inflation accelerated to 5.7% in July, higher than June's 5.2% and the fastest in more than five years. Year to date, inflation is now at 4.5%, well beyond the central bank's 2% to 4% target.
- Last week also saw the release of latest economic growth data which showed that the Philippine economy, as measured by gross domestic product (GDP), grew by 6% in Q2 of 2018. This is the slowest pace since Q2 of 2015, when GDP expanded by 5.6%.
- Household spending, which accounts for 60% of GDP, slowed to 0.2% in Q2 of 2018 compared to 6.3% in the same period a year ago.
- As such, the lagged effect might be visible for the remaining quarters, as consumers and investors alike, adjust to the initial phase of the Tax Reform for Acceleration and Inclusion (TRAIN) law.
- Meanwhile, the central bank last week hiked interest rates by 50 basis points, marking the third consecutive tightening move by the Monetary Board this year in a bid to temper inflation. Benchmark interest rates now range from 3.5% to 4.5%.
- Majority of well-run listed firms have proper risk management governance that should be able to absorb any sequel changes that might take place.
- On the upside, investors should see market declines as an opportunity to shop.
- The property sector has been bullish since the beginning of the year and is expected to continue to perform well. Conglomerates that were laggards last year are also in favor as investors have found it easier to make money from them as compared to their peers.
- Investors are advised to watch out for opportunities and hunt for undervalued stocks.
- Contrarians in a ghost month believe in opportunities on lulls or in dips. There have been discussions on the probability for weakness, but it pays to be alert too when opportunities arise than chase the boat later on.
- The PSEi's support is placed from 7,530 to 7,660, with resistance from 7,880 to 7,960.

ECONOMIC HIGHLIGHTS

IMF on Q2 Growth

- Economic growth remains "respectable" despite slowing sharply in Q2, the International Monetary Fund (IMF) said over the weekend, welcoming last week's aggressive interest rate hike as a necessary policy step.
- IMF said the Philippines' growth momentum remains intact, even as economic expansion slowed to 6% in April-June.

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

Wednesday, August 22
• Budget balance (JULY)

ECONOMIC HIGHLIGHTS (continued)

IMF on Q2 Growth (continued)

- This, however, could prompt revisions to the IMF's current forecasts.
- Gross domestic product (GDP) growth slowed from the downward-revised 6.6% pace in Q1 due to slower expansion in consumer spending and exports, although this was offset by a surge in state spending.
- After its latest annual health check on the economy in July, the IMF projected Philippine GDP expanding by 6.7% this year, matching the pace clocked in 2017 but settling below the government's 7% to 8% target.
- The multilateral lender said the Philippines has been "performing well" but flagged rising inflation and a changing external environment as key sources of risks.
- In separate commentaries late last week, ING Bank N.V. Manila and Fitch Solutions (formerly BMI Research) trimmed their growth forecasts to 6.3% following the soft Q2 figures, coming from previous estimates of 6.8% and 6.5%, respectively.
- To accelerate GDP growth, the IMF said significant structural reforms are needed to increase productivity, alongside scaling up infrastructure investments and on social services, particularly health and education.
- The IMF has expressed support for succeeding tax reform packages, opening up more industries to foreign investments by relaxing the "negative list" of sectors restricted to foreign participation, as well as replacing import quotas for rice with regular tariffs — a step that is expected to slash retail prices by about P7 per kilogram.
- The IMF has backed the Executive's proposal to overhaul the current tax incentives regime, saying that the Philippines "does not need to resort" to giving away such perks just to invite companies to invest here.
- On the other hand, it also said that the government should work to maintain the fiscal deficit at 2.4% of GDP this year — versus the state's programmed 3% — noting that the lower ratio will help contain inflationary pressures which have been hurting the economy in recent months.
- The central bank fired off its strongest policy adjustment in a decade as inflation remains elevated, having hit a fresh multiyear high of 5.7% in July. Prices of widely used goods have surged by 4.5% for the first seven months, and central bank officials last Thursday hinted that inflation could remain elevated even until 2019.
- The IMF had suggested the "further tightening" of policy rates to rein in inflation expectations.
- The IMF sees inflation averaging 4.7% this year, which is lower than the 4.9% full-year forecast which the central bank announced last week. Both are well above the central bank's 2% to 4% target range.
- Several economists are betting that this might not be the last tightening move from the central bank.
- The central bank has kept the door open for further rate hikes, ANZ Research said, as it bet another 25bp increase when the central bank's Monetary Board convenes for its sixth policy review this year on Sept. 27.

Monetary Policy Outlook

- Monetary authorities will likely continue to raise interest rates given the need to temper inflation and despite a softening economy, analysts said.
- IHS Markit, Japan's Nomura, and Fitch Solutions all said an additional policy rate hike could be announced before the year ends, and also possibly in 2019, following last Thursday's 50-basis point (bps) adjustment — the largest in 10 years.
- Inflation hit yet another five-year high of 5.7% in July, prompting the central bank's policymaking Monetary Board to shift from the 25-bps adjustments ordered in May and June.

ECONOMIC HIGHLIGHTS (continued)

Monetary Policy Outlook (continued)

- The Monetary Board also raised its inflation forecasts for 2018 and 2019 to 4.9% and 3.7%, respectively, from 4.5% and 3.3% previously, and also issued a 3.2% inflation forecast for 2020.
- Philippine monetary authorities, IHS Markit said, are facing the challenge of having to deal with a softening economy and rising inflation.
- With the central bank having hiked the policy rate by 100 bps altogether since May this year, the impact of higher policy rates will also be a moderate drag on GDP (gross domestic product) growth over coming quarters.
- A key risk to the near-term inflation outlook is from the risk of further rises in world oil prices, which could push inflation higher and force more central bank rate hikes during H2 2018 and in 2019, IHS Markit added.
- Across the Asia-Pacific central banking landscape, the combination of US Federal Reserve rate increases and external account pressures would ensure a continued shift away from accommodative monetary policy settings during the next 12–18 months.
- Through the end of 2019, IHS Markit expects the most aggressive monetary policy tightening among Asean (Association of Southeast Asian Nations) central banks to be from the BSP and Bank Indonesia.
- Nomura, meanwhile, said the central bank had clearly left the door open to more rate hikes.
- Nomura subsequently cut its 2018 Philippine growth forecast to 6.5% from 6.9% but at the same time maintained its view of another 50-bps increase for the rest of the year.
- Fitch Solutions, which also slashed its 2018 outlook to 6.3% from 6.5%, also said that the Monetary Board was not done with hiking key interest rates.
- Rising inflation expectations and risk aversion were said to be causing the peso to weaken, and while the central bank can intervene to help stabilize the currency, negative real interest rates and a tightening US Fed suggest that further interest rate hikes will likely be needed over the coming quarters to safeguard macroeconomic stability, and this is likely to come at the expense of growth.

Agricultural Output Growth Outlook

- The Department of Agriculture (DA) is sticking with the official 4% growth target for farm production output in 2018 despite the H1 growth rate of 0.58%.
- The DA is still confident that the sector can exceed the target by year's end, after the Philippine Statistics Authority (PSA) forecast a bumper harvest for a number of crops this year.
- First half output "is not reflective of the sector for the whole year because even PSA is saying that it is projecting a bumper harvest for this year."
- Despite storms, both the DA and the agriculture industry expect some boost from the rains in some areas where irrigation is poor.
- However, fisheries output is still expected to post lower output as the closed fishing season starts in November.
- Farm output in 2017 was 3.97%. The 2017-2022 Philippine Development Plan sets a 2.5% to 3.5% target range for farm output growth.
- In Q1, growth was 1.47%, slowing from 2.2% in Q4 of 2017.
- Last week, PSA reported that Q2 growth further slowed to 0.07% due to the drop in the crops subsector's output.
- The IBON Foundation said on Friday that agriculture cannot grow due to the government's neglect of the sector.
- The Duterte administration only pays lip service to improving agricultural productivity amid this severe crisis of agriculture in the countryside. The administration also continues the government's long-standing neglect of the sector, it added.
- IBON Foundation in its statement noted that the DA received a lower budget in 2019.
- IBON Foundation warned that food prices will rise as farm workers shift to other jobs, depressing production.
- IBON Foundation said imports, which the DA is resorting ahead of the yearend holidays, should be temporary.
- With importation, uncompetitive domestic producers not given enough support by the government will be displaced if trade protection for them is removed, it added.
- Importation could also tend to worsen the trade deficit and add to pressure on the peso to depreciate.

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CORPORATE NEWS

MER / AC

- Meralco PowerGen Corp. (MGen) is not keen on acquiring the coal-fired power plants being offered by Ayala-led AC Energy, Inc., saying the company's thrust is towards developing renewable energy.
- In May this year, AC Energy announced it was looking for buyers for as much as half of its thermal energy platform and possibly raise up to $1-bil in part to support its regional expansion.
- MGen's decision was in part because AC Energy does not hold a controlling stake in the thermal projects.
- MGen remains keen on developing renewable power sources, including solar and wind.

JGS

- JG Summit Holdings, Inc.'s attributable profit dropped by a third in Q2 of 2018, as the weaker peso, higher fuel prices, as well as rising prices of raw materials for its food, airline, and chemical units tempered the double-digit increase in revenues.
- The listed conglomerate said net income attributable to equity holders of the parent went down to P5.02-bil in the April to June period, against the P7.13-bil it generated in the same period a year ago.
- In contrast, revenues climbed 11.4% to P74.6-bil, thanks to the performance of Universal Robina Corp. (URC)'s branded consumer foods and agro-industrial units, the growth in Robinsons Land Corp. (RLC), and higher average selling prices of products under JG Petrochemcial Group.
- On a six-month basis, JG Summit's attributable profit went down 32.8% to P9.84-bil, while revenues rose 8% to P145.3-bil.
- For the food and beverage unit, URC reported a 23.1% decline in attributable profit to P4.81-bil during H1. This was due to higher costs of raw materials and foreign exchange gains.
- URC's consolidates sales of goods and services amounted to P64.37-bil by end-June, 5.9% higher year-on-year.
- Meanwhile, RLC's attributable profit went up by 14% to P3.33-bil for the period, driven by higher sales of residential properties, leases of commercial spaces, and more malls operated from January to June. Revenues from the property business rose by 19% to P13.1-bil
- Cebu Air, Inc., which operates low budget carrier Cebu Pacific, saw a 23.6% drop in earnings to P3.31-bil, despite a 6.1% uptick in revenues to P37.83-bil. The airline recorded a 6.3% increase in passenger revenues to P28.3-bil for the period, alongside a 28.1% increase in cargo revenues to P2.65-bil.
- Operating expenses of Cebu Pacific however grew 14% to P33.06-bil, due to the rise in fuel prices during the year. The airline also recorded net foreign exchange losses of P1.58-bil as a result of the weaker peso. Cebu Pacific currently has long term dollar-denominated debt used to fund its aircraft acquisitions.
- Earnings of the petrochemical business meanwhile slumped by 50.2% to P1.6-bil, amid an 8.9% climb in revenues to P21.18-bil.
- JG Summit's banking unit, Robinsons Bank Corp., delivered a 31.1% profit increase to P211.43-mil, as banking revenues likewise went up 32.2% to P2.73-bil.

SCC

- Semirara Mining and Power Corp. (SMPC)'s net income stood at P8.1-bil by end-June, 3% higher than what it generated a year ago, as its coal business cushioned the effects of the plant shutdowns of its power unit.
- The Consunji-led firm said the coal business posted improved margins year-on-year due to a recovery in global coal prices last June.
- Coal sales went up 9% to 6.9-mil metric tons (MT), as demand from domestic customers increased by 11%, alongside the 6% increase from coal exports.
- This led to a 35% jump in core profits for the coal business in H1 to P7.2-bil, compared to the P5.3-bil recorded in the same period in 2017.
- Production, however, dropped by 2% year-on-year to 7.2-mil MT. On a quarterly basis, production declined by around 1-mil MT.
- The power unit, SEM Calaca Power Corp. (SCPC), recorded a core profit of P373-mil for the period, down 60% from the P1.15-bil it reported in H1 of 2017.
- Meanwhile, Southwest Luzon Power Generation Corp. (SLPGC) posted a 66% decline in core profit to P478-mil.

CORPORATE NEWS (continued)

PAL

- The listed operator of Philippine Airlines (PAL) saw a 16.79% cut in its losses in Q2 driven by higher passenger volumes and other revenues.
- PAL Holdings, Inc. saw its net attributable loss down to P290.817-mil from last year's P349.5-mil despite recording higher expenses.
- It's total revenue reached P38.34-bil, up 13.9% from the P33.66-bil it posted last year. The growth is "primarily due to the increase in passengers and cargoes carried as a result of the increase in number of flights operated as well as improvement in yields."
- The flag carrier's total expenses grew to P38.67-bil from last year's P33.21-bil, surging 16.4% because of the additional flights PAL opened.
- The rising price of fuel continues to affect the company's business, hitting it with a 32.8% increase — P3.2-bil — in flying operations expenses. It said that the per-barrel price of fuel surged to $93.92 this year from $73.89 last year.
- PAL saw its net attributable loss from January to June go up 7.19% to P1.398-bil from last year's P1.304-bil due to higher losses in Q1.
- PAL reported a net loss of P7.3-bil in 2017 due to higher expenses brought by rising fuel prices and aircraft and passenger expenses. It sank further in Q1 of 2018, to P1.1-bil from P954-mil year on year.

AGI

- Alliance Global Group, Inc. grew its attributable profit by 17% in H1 of 2018, driven by the double-digit growth across its property, liquor, and fastfood businesses, alongside the recovery in its gaming unit.
- The holding firm of tycoon Andrew L. Tan reported a net income attributable to equity holders of the parent of P7.9-bil, versus the P6.9-bil it realized in the same period a year ago.
- This was supported by a 9% increase in revenues to P73.2-bil for the first semester.
- Megaworld Corp., AGI's property unit, saw its attributable profit rise 13% to P7.3-bil in H1. The residential and rental units pushed consolidated revenues 10% higher to P26.8-bil.
- Megaworld also noted that its hotel business saw significant growth at 10% to P715-mil for the period, following the addition of more hotel rooms under its portfolio.
- Emperador, Inc. delivered an 18% uptick in attributable profit to P3.3-bil, helped by an 8% increase in consolidate revenues to P19.5-bil.
- The whiskey business — which accounts for 27% of total profit — posted a 77% increase to P890-mil, as sales from brands The Dalmore and Jura boosted revenues by 16% to P6.2-bil.
- The whiskey business supported the slower growth of the brandy business, which grew by 4% in terms of revenues to P13.6-bil.
- The attributable profit of Travellers International Hotel Group, Inc. (TIHGI) stood at P1.7-bil in H1, recovering from the P375-mil it generated in the same period a year ago.
- Gaming revenues slipped 3% to P4.5-bil, although TIHGI said gross gaming revenues have seen improvements on a quarterly basis.
- Meanwhile, Golden Arches Development Corp. booked a net income of P741-mil, 26% higher year-on-year. The local franchisee of the McDonald's brand benefited from the addition of 19 stores to its portfolio, ending June with 585 stores.
- Sales revenues then expanded 11% to P13.5-bil, with same-store sales growth at 5.7%.

GOLD BUYING / Troy Oz.	COPPER BUYING / lb.
US$1,213.05	US$2.745