PrimeEquity Research

Meridian Securities Incorporated
Member: Philippine Stock Exchange

DAILY MARKET PRIMER

21 September 2018

PSEi	Value Turnover (US$)	Net Foreign Flow (US$)	PHI:US (PLDT ADR)	US$ 1.00
7,134.73 (-1.20%)	84,872,257.17	(7,134,750.45)	25.69 (-1.04%) = 1,388.80	54.060

MARKET OUTLOOK

- The main index sank deeper into bear territory on Thursday, as investors favored international markets versus placing their investments in the country.
- There seems to be no end in sight for the sell-down as the Philippines is still viewed as a riskier asset class versus the more developed US economy. In fact, US stocks closed higher overnight as investors took escalating trade tensions in stride to instead focus on improving economic fundamentals.
- Analysts also warned of the inflationary pressures seen from the effects of typhoon Ompong, which ravaged parts of Northern Luzon last weekend. Agricultural damage reportedly now reached P14-bil, which may hamper economic managers' expectations of inflation slowing in Q4.
- The balance of payments (BOP) surplus data which came in Wednesday afternoon is clearly not enough to calm investors into buying back into the market.
- The country's BOP position reverted to a huge surplus in August as the Philippines raised fresh funds from yen-denominated bonds, although the eight-month tally still remained negative.
- The Philippines' external position settled at a $1.272-bil surplus last month, turning around from the $455-mil deficit in July and the $7-mil deficit logged in August 2017, the central bank reported on Wednesday.
- Despite the positive print last month, the year-to-date BOP tally still ended at a $2.44-bil deficit. This is wider than the $1.391-bil shortfall posted as of August 2017, and is still wider than the $1.5-bil deficit expected for the entire 2018.
- Wall Street gained overnight as continued relief that fresh U.S. and China tariffs were less damaging than feared.
- After having slapped new tariffs on each other's goods this week, China now hopes that Washington will show sincerity and take steps to correct its behavior. This, in turn, is hoped to provide local stocks some respite from further sell-offs.

ECONOMIC HIGHLIGHTS

CIT Cuts

- Lower corporate income tax (CIT) rates are unlikely to provide a big boost to inbound investments, Fitch Solutions said, noting that a weak business environment hounded by red tape still deters investors from making big bets in the Philippines.
- Fitch Solutions, the research unit of Fitch Ratings, said the second tax reform package now awaiting legislative approval will not be a source of additional state revenues and is unlikely to lead to a deluge of foreign direct investments (FDIs).
- Earlier this month, the House of Representatives approved House Bill No. 8083, or the Tax Reform for Attracting Better and High-quality Opportunities (TRABAHO) Act, which gradually reduces the corporate income tax (CIT) rate to 20% from the current 30% by two percentage points every other year starting 2021.
- This will come alongside a new one-size-fits-all scheme for tax incentives, which will replace various types granted by investment promotion agencies and likewise put a cap on the number of years in which a company can enjoy such perks.
- Under the bill, incentives will consist of a three-year income tax holiday (ITH) as well as allowable deductions up to five years for "labor, training, infrastructure building, and research and development expenditures." This is a far cry from the current regime which grants ITH for up to nine years, with a 5% tax on gross income.

ECONOMIC INDICATORS					
GDP Growth Rate	6.0% (Q2 2018)	Unemployment Rate	5.4%% (July 2018)	GIR	US$77.829-B (August 2018)
Fiscal Surplus / (Deficit)	(P86.4-B) (July 2018)	Exports Growth Rate	0.3% (July 2018)	BOP	US$1.272-B (August 2018)
Inflation	6.4% (2012 BY) (August 2018)	Imports Growth Rate	31.6% (July 2018)	O/N RP	4.50% (as of August 9, 2018)
91-day T-Bill Rate	3.549 (as of September 10, 2018)	Cash Remittances	US$2.401-B (July 2018)	O/N RRP	4.00% (as of August 9, 2018)

ECONOMIC CALENDAR

Monday, September 24
- Budget Balance (August)

Thursday, September 27
- Monetary Board Policy Meeting

ECONOMIC HIGHLIGHTS (continued)

CIT Cuts (continued)

- The House approval puts the ball in the Senate's court, although lawmakers there are studying a different version that would immediately cut the CIT rate to 25% in the first year of implementation.
- However, the Fitch unit said the country is unlikely to see much fiscal gain from the TRABAHO bill. The think tank believes that the impact on the government's fiscal position is negligible. The government expects a loss of P62-bil in revenue upon the lowering of CIT in 2021 and, according to Fitch's forecast, this will represent just 1.5% of the expected revenue collection that year. Moreover, the TRABAHO also seeks to trim tax incentives that are offered to investors, making them more selective and less encompassing, and this will likely offset some of the loss in revenue from lower corporate taxes.
- The Department of Finance (DOF) had originally designed the second tax package to be revenue-neutral, meaning it was not to yield additional tax collections unlike Republic Act No. 10963, or the Tax Reform for Acceleration and Inclusion Act, that took effect this year. But since CIT cuts are no longer pegged to annual revenue increments from removal of redundant fiscal perks under the bills in Congress, this measure is now expected to yield more foregone revenues.
- Fitch Solutions is also unsure that the lower tax rates will improve the Philippines' attractiveness as an investment destination.
- On the investment front, Fitch is unconvinced that the lowering of CIT rates will provide a significant boost, in the absence of accompanying improvements to the business environment.
- While CIT rates are one of the considerations of potential investors when they look to relocate their businesses, Fitch believes that more of them are deterred by the poor business environment caused by red tape and corruption, as well as poor infrastructure conditions.
- Moreover, the lowering of CIT rate is so gradual that it will take until at least 2025 before they fall in line with regional levels, the think tank added, noting that it will take years before the tax rate actually becomes competitive.
- Not all tax reforms proposed by the Executive can be approved by yearend, a House leader has said, contrary to President Rodrigo R. Duterte's request in his State of the Nation Address last July in hopes of securing legislative approval before lawmakers shift attention to preparations for the May 2019 mid-term elections.

Mining Tax Reform

- A proposal to give government a bigger share in mining revenues goes back to square one, as House Speaker Gloria M. Arroyo on Thursday asked the Department of Finance (DOF) to submit a new draft that would consider inputs from miners.
- The panel was scheduled to discuss the still-unnumbered substitute bill that consolidated House Bills 7994 and 422, titled: "An Act Establishing the Fiscal Regime for Mining Industry" and authored by committee chairman Rep. Estrellita B. Suansing of Nueva Ecija's first district and committee member Rep. Romero S. Quimbo of Marikina City's second district, respectively.
- Ms. Arroyo recalled that when Gloria L. Tan-Climaco, director of Filminera Resources Corp. and member of the Chamber of Mines of the Philippines (COMP) board of trustees, had approached her "two days ago" to say "that the measure, as you are preparing it, is going to kill the industry," she told the official: "Do not tell me that. This is an administration measure. Tell it to the DOF."
- Ms. Suansing then asked DOF officials attending Thursday's hearing to "Please clarify and inform the Speaker that this is not his (Mr. Dominguez's) priority officially."
- Sought for comment, Mr. Dominguez downplayed the issue as "a misunderstanding."
- "If the mining (bill) is ready to be passed then we respect House decision to pass it," Mr. Dominguez said.

ECONOMIC HIGHLIGHTS (continued)

Mining Tax Reform (continued)

- “Then next priority is tax amnesty, further increases in alcohol, tobacco, MVUC (Motor Vehicle Users Charge), financial taxes and uniform property validation in that order.”
- Mining tax restructuring was one of the tax reforms the DoF submitted to Congress in late July in hopes of securing legislative approval by yearend, before lawmakers turn their attention to preparations for the May 2019 mid-term elections.
- Asked whether the DOF would consider miners’ suggestions to take into consideration the varied cost structures of extracting various ores, Finance Undersecretary Karl Kendrick T. Chua told reporters late Wednesday on the sidelines of plenary House discussions on the DOF’s budget for 2019: “If there are better suggestions, we’ll review and study the proposals.”
- Among others, DoF-backed HB 7994 proposes a three percent royalty based on the market value of gross output of mines outside mineral reservations in the first three years of the effectivity of the measure, increasing to 4% in the fourth year and then 5% in the fifth year onward, on top of all other national and local taxes.
- COMP has said that the government should first regulate illegal small-scale miners, arguing that they account for bulk of uncollected industry revenues.
- Ms. Arroyo said on Thursday that she supports the phased royalty scheme, and that she has “a proposed provision that says ‘open-pit mining, as defined here in this Act, is prohibited and any mining tenement that will not comply with DAO (Department Administrative Order) shall take steps to comply with the DAO within a period allowed by the DENR (Department of Environment and Natural Resources).”

CORPORATE NEWS

FB

- San Miguel Food and Beverage, Inc. (SMFB) has completed the share-swap transaction consolidating the traditional units of parent San Miguel Corp. (SMC) under its portfolio.
- SMFB said it had completed the P336.35-bil transaction involving its issuance of 4.24 billion new shares to SMC, in exchange for the company’s 7.86-bil common shares in San Miguel Brewery, Inc. (SMB) and 216.97-mil shares in Ginebra San Miguel, Inc. (GSMI).
- SMFB now serves as the holding company for SMC’s food and beverage, liquor, and brewery businesses, with SMB and GSMI as its subsidiaries. It now holds an ownership of 51.16% and 78.26% in SMB and GSMI, respectively, while SMC’s stake in SMFB will increase to 95.87% from 85.37% as of September last year.
- Following the completion of the share swap, SMFB said it had filed an application with the Philippine Stock Exchange (PSE) to list the new shares it had issued to SMC.
- The share-swap transaction is part of the San Miguel group’s internal restructuring, in a bid to create a “significant consumer food and beverage vertical market under SMC.” The company also expects the restructuring to enhance its trading liquidity and broaden the shareholder base to institutional and retail investors.
- SMFB’s public float now stands at 4.12%, less than half of the minimum public ownership rule of 10% set by the Securities and Exchange Commission (SEC). The company targets to conduct a follow-on offering worth up to P142-bil by year-end to meet this requirement, filing with the SEC last August a registration statement to sell up to 1.02-bil common shares at up to P140 each.

GOLD BUYING / Troy Oz.	COPPER BUYING / lb.
US$1,203.80	US$2.765