Trust Banking Group

United Coconut Planters Bank

Weekly Market Commentary

24 January 2012

Why 2012 will be a better year? In our January 09 newsletter, we noted that 2012 may surprise a lot of people in terms of growth. We believe that the Phil. economy will grow above the 4.7% Bloomberg consensus forecast. Table 1 below outlines why we believe growth in 2012 will be better compared to the previous year.

Table 1. Why 2012 will be a better year?

GDP Components	2011	2012
HH Final Consumption Exp.	Supported by remittances, IT/BPO revenues	
Govt. Final Consumption Exp.	Restrained govt. spending	Govt. spending to accelerate
Capital Formation	Limited infra proj;	Higher govt. spending from GAA;
	"Audit" periold for govt.	PPP starting to roll-out
Exports	Weak	Still weak
Imports	Weak	Still weak
GDP	4.7% forecast	Better than forecast

If viewed from the expenditure or demand side, GDP can be broken down into five components, namely (a) household consumption; (b) govt. consumption; (c) capital formation or investments; and (d) exports less imports.

As in the previous years, household consumption remained well supported last year due to remittances and the revenues we are getting from the IT/BPO sector.

Govt. consumption last year was restrained on purpose. 2011 may be viewed as an “audit year” wherein govt. reviewed existing and proposed projects to ascertain their economic and social importance as well as to determine that these projects are being implemented following the highest legal and ethical standards. This task was hard and tedious but certainly necessary. The govt. may not succeed 100% but it is a right step toward curbing rampant graft and corruption.

Investments, another vital component of GDP, declined in 2011 as the expected infra projects of the govt. (which would have attracted private capital) did not materialize.

Finally, our external sector (i.e., exports & imports) suffered severely last year given the global economic slowdown.

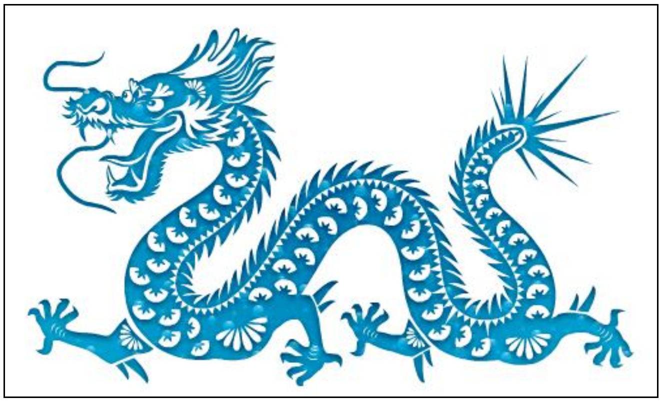
In short, only household consumption remained buoyant. The other sectors of the economy were either weak or contracted.

However, we believe that ***2012 will be different.*** This time the economy will be powered by three sectors, i.e., household consumption, govt. spending and investments. Consider the following (the data below has been slightly revised from the Jan. 09 version):

1. In Oct. 2011 the govt. implemented a ₱72.1 bn Disbursement Acceleration Plan (DAP) aimed at fast tracking project implementation. This program may be viewed as additional spending on top of what would have been spent in 2011. As of 09 January 2012, 95% or ₱69.3 bn of the DAP budget have been released to local governments, national agencies and govt.-owned & controlled corporations. Of the amount released, ₱53.8 bn have already been disbursed by the implementing units.
2. Early this month the govt. added another ₱13.4 bn to the DAP.
3. The economic component of the 2012 General Appropriations Act (GAA) is ₱439 bn or 24.2% of the ₱1.8 trillion national budget.
4. Out of the ₱439 bn, the infra component is ₱182 bn. of which ₱142 bn will be implemented starting Jan. 2012.
5. The ₱182 bn infra budget for 2012 is 25.6% higher vs. the 2011 budget.
6. 93% of the 2,187 line item infra projects in the 2012 GAA (or 2,025 line items) have already been bid out.
7. About 16 PPP projects worth approx. ₱152 bn are tentatively scheduled for bidding this year.

These are the reasons why we believe that 2012 will surprise us on the upside. We reckon that a lot of these developments have not been factored in by earlier GDP estimates.

Indeed, 2012 will be an auspicious year for the country and for us investors. **Gong Xi Fa Cai, or if you prefer, Kung Hei Fat Choi.**



What sectors will likely shine in 2012? We have identified several sectors that will likely outperform in 2012 given our macro assumptions.

1. **Infrastructure.** There are two reasons why we like this sector. First, the country has an infrastructure deficit which needs be addressed in the soonest possible time. Second, the govt. has recognized this problem and is focused on addressing it via the PPP. There are strong indications that the govt. would finally start rolling out the PPP program by early 2012.

2. **Gaming.** The govt. has recognized the potential of this sector. PAGCOR has issued gaming licenses to four companies: (a) Travellers Int'l. (a JV between Alliance Global & Genting of Malaysia); (b) Belle Corp. (60%-owned by the SM group); (c) Bloomberry Hotels & Resorts (owned by ICTSI Chair Ricky Razon); & (d) Universal Entertainment of Japan. Travellers has already one operating casino Resorts World Manila while Belle and Bloomberry are about to finish theirs by end 2012.

3. **Energy.** Supply tightness will still be a concern in the next 2 years before the new baseload plants are on stream. Generating companies which have finished their plant rehabilitation or expansion should benefit from higher output.

4. **Retail.** Consumer spending will continue grow on the back of strong remittances and increasing income from the IT/BPO sector. These are the main drivers for these sector.

5. **Mining.** The facts of this sector are well known: (a) the country is highly mineralized; (b) the sector is still underdeveloped; (c) there are only a few large scale mining operations; (d) the govt. has recognized mining as a growth sector; and (e) foreign firms are seriously looking into the industry. Expect volatility given the nature of commodity prices and concerns over the environment.

Economic & Corporate News:

Monetary easing starts. As expected, the BSP cut its policy rates by 25 basis points to 4.25% for its overnight borrowing rate and 6.25% for its overnight lending rate. The Monetary Board of the BSP believed that a benign inflation outlook has *allowed some scope for a reduction in policy rates to help boost economic activity and support market confidence*.

The SDA rate has likewise been reduced to 4.375% and 4.4375% for the 14-day and one month tenors, respectively.

Fiscal expansion. The DBM announced that as of 15 January, the department has already released 72.3% of the 2012 budget allocation for govt. agencies. Interestingly 72.1% of capital outlays have already been released. This should enable agencies to immediately implement their respective infra projects before that start of the rainy season.

This aggressive stance of the govt. is in sharp contrast to its restrained spending posture especially during the first half of last year.

Investments should greatly benefit from the twin impact of monetary easing and higher govt. spending. These developments support our bullish view for 2012.

Table 2. 2012 National Budget

Items	Budget	Released[1]	
	(mn)	(mn)	(%)
Department Budget			
Salaries & wages	426,162	424,442	99.6%
Maintenance & Other Oprtg. Exp.	234,415	211,859	90.4%
Capital Outlay	208,342	150,286	72.1%
Others	223,452	2,671	1.2%
Sub-Total	1,092,371	789,258	72.3%
Automatic Appropriations[2]	723,629	69,528	9.6%
Total	1,816,000	858,786	47.3%

1/ As of 15 January 2012
2/ Internal Revenue Allotments, interest payments, retirement & insurance premiums
Source: DBM

Broadcaster GMA Network (GMA7 & GMAP) expects 2012 profits to reach ₱3.0 bn or 67% higher compared to the ₱1.8 bn profits last year. Felipe Gozon, GMA Chair and CEO is confident that the target will be achieved as 70% of their revenue target for the year have been covered by advertising commitments. GMA is also expecting political placements late this year as 2013 will be a mid-term election year.

SMC Global Power IPO may push through early this year. The IPO was originally slated late last year but was later deferred due to weak market conditions. SMC Global Power is the largest independent power producer (IPP) in the country.

SM Land's offer for the Bonifacio South property to be decided soon. The Bases Conversion Dev. Authority (BCDA) will submit to Pres. Aquino its recommendation with regard the unsolicited offer of SM Land for the 33.1 ha. Bonifacio South property. The original offer (recently revised) was made in 2010 but the deal never fell through. To protect the govt. and investors, details of the offer are not made public. What we only know are its general terms: upfront cash payment of ₱2.0 bn and assured annual revenue of ₱25.9 bn over a period of 20 years. SM Land also committed to invest at least ₱20 bn for this property. Once approved by Pres. Aquino, the BCDA will proceed with the Swiss Challenge.

If SM Land wins this deal, it will join Megaworld and Ayala Land as the three biggest landlords in the Fort Bonifacio/Nichols area.

Global stocks continue to rally amid signs that the U.S. recovery is gaining traction and Europe's debt crisis is slowly being addressed. Speculation that China will ease lending restrictions has also contributed to a rebound in the prices of base metals.

The PSEi is not to be left behind. The index has already risen by 8.6% to 4,748 since the start of the year. While the gains were generally across all sectors, the main driver was the unexpected rally of PLDT. Apparently, PLDT is being bought by foreign funds as a yield play. Based on an estimated dividend of ₱180/share, PLDT's dividend yield for this year is about 6.% - 7.0%. It is definitely an attractive alternative to low yielding U.S. bonds.

This is also the reason why a number of high dividend paying counters like Globe, Semirara Mining and GMA remain well supported.

Moreover, we expect a correction in the short-term given the sharp rally in the last two weeks.

Table 1. PDSTF Rates

PDST-F	YIELD (%)		Change
	13-Jan-12	20-Jan-12	(bps)
1 Month	1.96	1.93	(3.55)
3 Months	1.72	1.67	(4.92)
6 Months	2.18	2.14	(4.46)
1 Year	2.22	2.22	(0.15)
2 Years	2.88	2.65	(23.42)
3 Years	3.87	3.86	(1.46)
4 Years	4.88	4.98	10.00
5 Years	4.99	5.11	11.35
7 Years	5.28	5.34	5.73
10 Years	5.34	5.37	3.29
20 Years	6.72	6.66	(5.96)
25 Years	6.41	6.38	(2.64)

Source: Bloomberg

Table 2. SDA Rates

Tenor	YIELD (%)		Change
	13-Jan-12	20-Jan-12	(bps)
1 Month	4.6875%	4.4375%	(0.25)
14 Days	4.6250%	4.3750%	(0.25)

Source: BSP

Table 3. Indicative ROP Prices

Series	Coupon	Maturity	Yrs to Maturity	PRICE 20-Jan-12	Yield to Maturity
ROP 13	9.000	15-Feb-13	1.1	107.50	1.9%
ROP 14	8.250	15-Jan-14	2.0	111.78	2.2%
ROP 15	8.875	17-Mar-15	3.2	120.53	2.1%
ROP 16 n	8.000	15-Jan-16	4.0	120.52	2.6%
ROP 16	8.750	07-Oct-16	4.7	126.27	2.8%
ROP 17	9.375	18-Jan-18	6.0	129.23	3.9%
ROP 19	9.875	15-Jan-19	7.0	139.25	3.5%
ROP 19 n	8.375	17-Jun-19	7.4	131.86	3.5%
ROP 20	6.500	20-Jan-20	8.0	119.61	3.7%
ROP 21 n	4.000	15-Jan-21	9.0	102.67	3.6%
ROP 21	4.950	15-Jan-21	9.0	102.25	4.6%
ROP 24 n	7.500	25-Sep-24	12.7	128.65	4.5%
ROP 24	9.500	21-Oct-24	12.8	145.64	4.7%
ROP 25	10.625	16-Mar-25	13.2	158.63	4.6%
ROP 26	5.500	30-Mar-26	14.2	112.05	4.4%
BSP 27	8.600	15-Jun-27	15.4	133.19	5.4%
ROP 30	9.500	02-Feb-30	18.0	155.01	4.9%
ROP 31	7.750	14-Jan-31	19.0	135.19	4.9%
ROP 32	6.375	15-Jan-32	20.0	118.82	4.9%
ROP 34	6.375	23-Oct-34	22.8	119.80	4.9%
ROP 36	6.250	14-Jan-36	24.0	102.25	6.1%
ROP 37	5.000	13-Jan-37	25.0	101.30	4.9%

Source: Bloomberg

UITF Performance

Table 4. UITF Performance

UITF (PhP)	31-Dec-11	13-Jan-12	20-Jan-12	Change Wk-on-Wk	Change Yr-to-Date
UCF	1.6013	1.6212	1.6188	-0.14%	1.10%
U$MMF	1.2649	1.2650	1.2651	0.00%	0.01%
UCMF	1.1769	1.1783	1.1789	0.06%	0.17%
UBF	1.9234	1.9797	1.9957	0.81%	3.76%
UEF	2.5150	2.6103	2.6463	1.38%	5.22%

UCF United Conservative Fund
U$MMF United USD Money Market Fund
UCMF United Cash Management Fund
UBF United Balanced Fund
UEF United Equity Fund

Table 5. Market Indicators

Indicator		Level 2011 Yr. End	Level 13-Jan-12	Level 20-Jan-12	Change Wk-on-Wk	Change % Ch	Change YTD	Change % YTD
Peso	1	43.84	43.77	43.32	-0.45	-1.03%	-0.53	-1.20%
Stocks	2	4,372	4,614	4,748	134.07	2.91%	375.94	8.60%
3-mo. PDSTF (ch in bps)	3	1.6581	1.7165	1.6673	-0.05	(4.92)	0.01	0.92
Peso Bonds	4	347	348	348	0.23	0.07%	1.18	0.34%
3-mo. USD LIBOR (ch in bps)	5	0.5810	0.5670	0.5611	-0.01	(0.59)	-0.02	(1.99)
Rep. of the Phil. bonds (ROP)	6	196	196	197	0.91	0.46%	0.92	0.47%
Crude Oil (USD/bbl)	7	98.83	99	98	-0.37	-0.37%	-0.50	-0.51%
Gold (USD/troy oz)	8	1,564	1,639	1,667	27.65	1.69%	102.95	6.58%
DXY (USD Index)	9	80	82	80	-1.29	-1.58%	0.05	0.06%
ADXY (Asian Currencies)	10	115	116	116	0.81	0.70%	1.18	1.02%
VIX	11	23	21	18	-2.63	-12.58%	-5.12	-21.88%
V2X	12	32	29	25	-3.88	-13.43%	-6.80	-21.37%

Sources:
1/ Phil. Dealing System
2/ Phil Stock Exchange Index
3/ Phil. Deal. & Exch. Corp.; change in basis points
4/ HSBC Local Bond Index
5/ Bloomberg; change in basis points
6/ JP Morgan Asia Credit Index
7/ West Texas Intermediate
8/ Bloomberg
9/ DXY = USD spot index
10/ ADXY = Asian currencies vs. USD index
11/ CBOE volatility index
12/ Eurozone volatility index

Annex A
Explanatory notes on our Market Indicators.

In general, market indicators are used to assess the pulse and health of our economy. It is very similar to how doctors check our heartbeat, the color of our eyes, our cholesterol level or the sugar content of our blood to initially assess how healthy (or unhealthy) we are.

Since we are generally concerned with investments, the appropriate measures to look at are economic and market indicators. As investors, we want to know where these indicators are headed so we can make the appropriate decisions. These indicators are as follows:

Peso. *This is our currency and its current level and direction normally indicate the general health of the economy.*

Stocks. *A strong or robust stock market reflects a strong and growing economy or vice versa. Our stock market cannot be strong if our economy is weak. And the opposite is equally true. After all, corporate earnings and prospects reflect the overall outlook of the economy. The index we are using is the Phil. Stock Exchange Index (PSEi).*

3-month PDSTF Rate. *This is the indicator we use for domestic interest rates. It used to be the 90-day Treasury Bill rate but this instrument has lost its appeal since it is not very liquid and may not truly reflect market levels. PDSTF rates are better indicators of where interest rates are since these are based on actual rates of highly liquid instruments.*

Peso Bonds. *The HSBC Local Bond Index (Phil.) tracks the average price movements of local bonds and is a good indicator of how expensive (or cheap) bonds are. The index should also provide an indication of where bond yields are headed since bond prices and bond yields move in the opposite direction.*

3-month USD LIBOR. *This is the US dollar counterpart of the 3-month PDSTF rate. LIBOR means London Interbank Offer Rate, the rate at which banks lend to each other and used as a benchmark for commercial lending.*

USD Bonds (ROPs). *This index tracks the price movements of Phil. bonds denominated in US dollars. The index we are using is the JPMorgan Asia Credit Index (Phil.).*

Since the indices we use for stocks, peso bonds and USD bonds (ROPs) are based on price movements, the higher the level of the index, the better it is for investors.

Crude Oil. *At least in our lifetime, oil will always be one of the most important economic indicators since it is a basic feedstock of economies worldwide. The benchmark that we are using is the West Texas Intermediate (WTI) as it is the most common and widely used crude oil index.*

Gold. *This is our proxy for uncertainty. The price of gold normally goes up during uncertain or difficult times. This is because gold is the ultimate store of value. Paper currencies could lose their value but gold will always retain its value whether as an ornament or as a unit of exchange.*

DXY. *It is a spot index of the USD based on a basket of five currencies, Euro (57.6%), Japanese Yen (13.6%), British Pound Sterling (11.9%), Canadian Dollar (9.1%), Swedish Krona (4.2%) and Swiss Franc (3.6%). The DXY does not reflect the trade position of the US in the global economy. It is being used for convenience as its value is updated on a daily basis.*

ADXY. *It is a spot index of emerging Asian currencies versus the USD. It is composed of ten currencies, Renminbi (33.9%), South Korean Won (14.2%), Hong Kong Dollar (11.4%), Singapore Dollar (10.3%), Taiwan Dollar (8.2%), Indian Rupee (6.3%), Malaysian Ringgit (5.2%), Thai Baht (4.9%), Indonesian Rupiah (3.3%) and Phil. Peso (2.3%). The index is constructed based on two considerations, trade performance (75%) and liquidity (25%).*

Finally, note that there will always be a speculative element in the movement of these indicators. But speculation is not their main driver. The most important driver that normally sustains the movement of an indicator over the long-run is its fundamentals. For example, the movement of the peso is dictated by the following fundamental factors: (a) the health of our economy; (b) the amount of US dollars remitted by Filipinos working and living abroad; (c) the level of our exports; and (d) the amount of foreign direct investments we receive.

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