



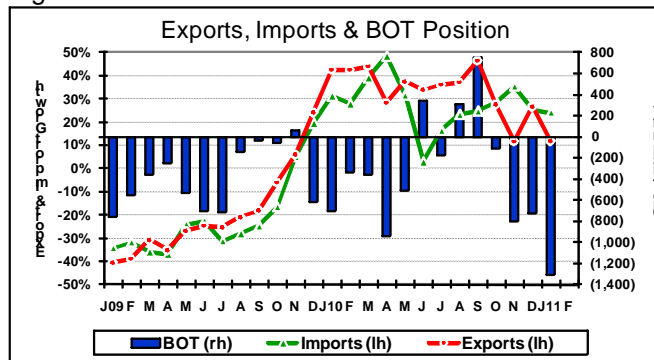
# Weekly Market Commentary

18 April 2011

**Three important news flows** caught our attention last week. These are (1) merchandise exports; (2) inflation; and (3) remittances.

**Merchandise exports eased in Feb.** as it grew by only 8.2% to USD3,864 mn, slower than the 11.8% growth in Jan. The slowdown in exports was principally due to the 2.7% contraction of electronics. The country's electronic exports account for the bulk or 54% of total export receipts. The slowdown in Phil. exports is not surprising as global growth is being weighed down by rising commodity prices and exacerbated by the crisis in the Middle East & North Africa (MENA). The govt. is looking at a 10% export growth this year but this target could be subject to a downward revision given inflationary pressures, turmoil in the MENA region and a slowdown in Japan.

Figure 1



BOT: Balance of Trade (i.e., exports less imports)

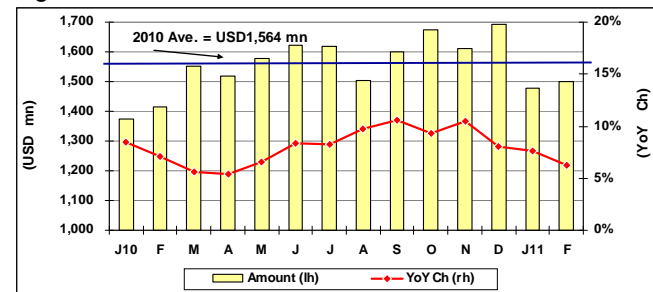
**Inflation.** Wages are likely to rise soon following the instructions of the Dept. of Labor & Employment (DOLE) for regional wage boards to start public hearings on minimum wage increases in their respective areas.

While organized labor is demanding for a legislated P125/day across-the-board increase, we believe that daily wage earners will instead get a combination of cash and non-cash benefits, with the cash component being lower than what is being sought for.

**Remittances remain strong . . . for now** as it grew by 6.2% year-on-year to USD1,501. While the absolute figure is still significant, we note that remittance growth has been easing since Dec. last year. It is still early to say whether this development is a result of the ongoing

crisis in the MENA region. Nevertheless, we will closely watch remittance flows as these account for a substantial portion of the economy.

Figure 2



**Public Private Partnership (PPP) projects as growth driver . . .** The govt. has been aggressively seeking private sector participation in large infrastructure projects to be undertaken under the PPP arrangement. The Aquino administration views PPP projects as the cornerstone in its economic development objectives.

**. . . But hitting speed bumps.** Since first unveiled nine months ago, not a single project has been auctioned off. An initial set of projects has been announced but the original timetable has been pushed forward since bid documents are still being completed. We understand that the first bidding is just a month or two from now.

We do share the government's belief on PPP projects as growth driver . . . provided it takes off.

Table 1

PPP Projects for 2011 Rollout	Proponent	Cost (P mn)
Privatization of LRT 1 (O&M)	DOTC	7,700
Privatization of MRT 3 (O&M)	DOTC	6,300
Daang Hari-SLEX Link Road (4 km)	DTI	1,500
NAIA Expressway (Phase 2)	DPWH	11,800
NLEX-SLEX Connector	DPWH	21,000
LRT 1 South Extension Project	DOTC	70,000
LRT Line 2 East Extension Project	DOTC	11,300
New Bohol Airport Development	DOTC	7,600
Puerto Princesa Airport Development	DOTC	4,400
New Legaspi (DARAGA) Airport Dev.	DOTC	3,200
Privatization of Laguindingan Airport (O&M)	DOTC	1,500
CALA Expressway (Cavite section, 27.5 km)	DPWH	11,790
<b>Total</b>		<b>158,090</b>

Source: Phil. Eco. Briefing, 23 March 2011

**Tourism getting a boost.** The draft Implementing Rules & Regulations (IRR) on open skies policy has effectively dropped the reciprocity arrangement. This means that foreign carriers can bring visitors into the Phil. without a quid pro quo similar privilege granted our own airlines. This unilateral action on our part may look disadvantageous on the surface but is actually net positive for the economy. First, open skies has been proven to boost tourism (e.g., Singapore, Malaysia). Second, domestic airlines should benefit from this policy as tourists arriving in the Phil. will still need local carriers (like Cebu Pacific & PAL) to bring them to their final destination such as Boracay or Palawan.

**Building a war chest?** Two weeks ago, **Alliance Global, Inc. (AGI)** sold 550.1 million treasury shares at P11.16/share via a private placement. During the same exercise, **Megaworld (MEG)**, a subsidiary of AGI, also sold 321.9 million AGI shares it owns at the same price. The placement generated P6.1 billion and P3.6 billion for AGI and MEG, respectively. Both companies do not really need the cash at the moment but this recent fund raising could mean another major move into tourism related projects.

In another development, MEG plans to issue a 7-year, US dollar denominated corporate notes. The notes will be used to partly refinance MEG's USD100 million bond obligation.

**Local bonds** staged a minor rally driven mainly by liquidity and a possible 1Q 2011 fiscal outperformance by the government. However, we remain cautious about this rally as inflationary threat is still very real considering the elevated level of crude oil.

Table 1. PDSTF Rates

PDST-F	YIELD		Change (bps)
	08-Apr-11	15-Apr-11	
1 Month	1.35	1.18	(17.12)
3 Months	1.10	0.99	(11.47)
6 Months	1.22	1.08	(13.85)
1 Year	2.26	2.11	(15.19)
2 Years	4.28	4.09	(18.88)
3 Years	5.13	5.00	(12.65)
4 Years	5.63	5.52	(10.85)
5 Years	5.76	5.65	(11.00)
7 Years	6.48	6.37	(10.97)
10 Years	6.91	6.85	(6.15)
20 Years	8.13	8.12	(0.96)
25 Years	8.09	8.03	(6.69)
HSBC ALBI*	308	310	0.6%

\*The HSBC Asia Local Bond Index (Phil.) tracks the price movement of Phil. sovereign bonds. A positive change means that bond prices moved higher & yields lower or vice versa.

**ROP** prices eased last week as investors turned cautious in the light of renewed concerns over Europe's debt problems. The possibility of Greece restructuring its debt, the 2-notch downgrade on Ireland by Moody's and Portugal's coming elections have spooked investors and dampened risk taking.

We believe that while strong economic fundamentals remain supportive for ROPs, external concerns (e.g., Europe's debt problems, crisis in the MENA region) will create volatility in the ROP market.

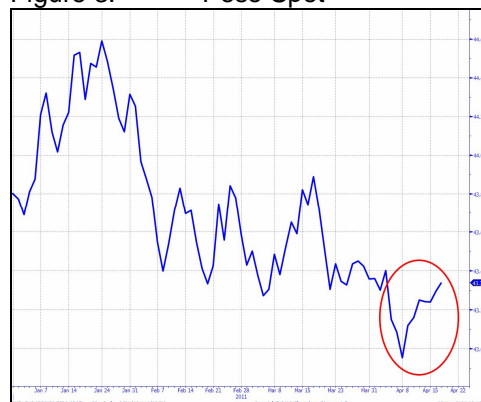
Table 2. Indicative ROP Prices

Series	Coupon	PRICE		Change (bps)
		08-Apr-11	15-Apr-11	
ROP 13	9.000	112.75	112.75	0.00
ROP 14	8.250	115.75	115.75	0.00
ROP 15	8.875	123.00	122.88	(12.50)
ROP 16 n	8.000	121.13	120.75	(37.50)
ROP 16	8.750	127.50	127.25	(25.00)
ROP 17	9.375	127.75	127.00	(75.00)
ROP 19	9.875	134.75	133.75	(100.00)
ROP 19 n	8.375	125.75	125.00	(75.00)
ROP 20	6.500	113.00	112.38	(62.50)
ROP 21	4.950	98.00	98.00	0.00
ROP 24 n	7.500	118.75	117.50	(125.00)
ROP 24	9.500	136.50	135.25	(125.00)
ROP 25	10.625	148.13	146.63	(150.00)
ROP 26	5.500	97.75	97.13	(62.50)
ROP 30	9.500	139.75	137.50	(225.00)
ROP 31	7.750	120.00	118.50	(150.00)
ROP 32	6.375	104.50	102.25	(225.00)
ROP 34	6.375	104.50	102.50	(200.00)
JACI Phil*		177	176	-0.7%

\*JACI Phil. tracks the price movement of Phil. USD sovereign bonds with maturity of at least 1 year. A positive change means bond prices moved higher or vice versa.

**Peso.** The peso has mildly depreciated last week in line with other Asian currencies (Fig. 3). In addition, the concern over weaker remittances may have contributed to slight bearishness on the peso.

Figure 3. Peso Spot\*

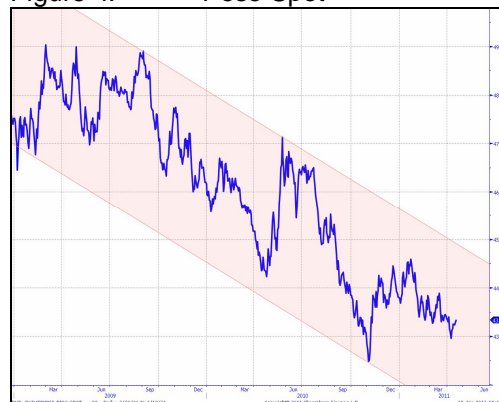


\*Jan. 2011 - present

Nevertheless, we still believe that this weakness is temporary as the peso is well supported. Remittances, even if slightly weaker, will still be huge in absolute terms (around USD20.0 bn for 2011). Aside from remittances, revenues from the Information Technology/Business Process Outsourcing sector will also contribute to US dollar inflows. This year, the Business Processing Association of the Phil. (BPAP) expects industry revenues to hit USD11.6 billion from USD9.1 billion last year.

Our year-end target for the peso is between ₱42.30 – ₱40.00

Figure 4. Peso Spot\*



\*Jan. 2009 - present

## UITF Performance

Table 3. UITF Performance

UITF (PhP)	31-Dec-10	08-Apr-11	15-Apr-11	Change	
				Wk-on-Wk	Yr-to-Date
UCF	1.4839	1.4935	1.4939	0.02%	0.67%
U\$MMF	1.2462	1.2509	1.2509	0.01%	0.38%
UCMF	1.1451	1.1531	1.1535	0.03%	0.73%
UBF	1.7428	1.7977	1.7984	0.04%	3.19%
UEF	2.2666	2.3785	2.3773	-0.05%	4.88%
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 4. Market Indicators

Indicator		Level			Change			
		2010 Yr. End	08-Apr-11	15-Apr-11	Wk-on-Wk	% Ch	YTD	% YTD
Peso	1	43.80	42.96	43.24	0.29	0.66%	-0.56	-1.28%
Stocks	2	4,201	4,241	4,252	10.63	0.25%	50.50	1.20%
3-mo. PDSTF (ch in bps)	3	1.2917	1.1012	0.9865	-0.11	(11.47)	-0.31	(30.52)
Peso Bonds	4	307	308	310	1.82	0.59%	2.35	0.76%
3-mo. USD LIBOR (ch in bps)	5	0.3028	0.2853	0.2748	-0.01	(1.05)	-0.03	(2.81)
USD Bonds (ROPs)	6	178	177	176	-1.15	-0.65%	-1.59	-0.90%
Crude Oil (USD/bbl)	7	91.38	113.37	110.22	-3.15	-2.78%	18.84	20.62%
Gold (USD/troy oz)	8	1,420.78	1,474.93	1,486.70	11.77	0.80%	65.92	4.64%
DXY	9	79.03	75	75	-0.23	-0.31%	-4.20	-5.31%
ADXY	10	116.46	118	118	-0.03	-0.03%	1.53	1.31%
VIX	11	17.75	18	15	-2.55	-14.27%	-2.43	-13.69%
V2X	12	23.92	20	19	-1.16	-5.80%	-5.11	-21.38%

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/ DX Y = 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.*

**ADX.** *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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