

Weekly Market Commentary

28 November 2011

The Public-Private Partnership Center recently released an updated list of projects for roll-out late this year and for 2012. This is the latest iteration of an initiative that was launched with much fanfare in late 2010. Unfortunately, up to now not a single project has been auctioned off. To be fair the govt. is exercising due diligence in the implementation of these multi-billion projects to ensure their proper implementation. Table 1 shows the latest list of projects from the PPP Center:

Table 1

PPP Projects for 2012 Rollout		
	Proponent	Cost (P mn)
Dec. 2011		
1 Daang Hari-SLEX Link Road (4 km)	DPWH	1,956
2 Classroom Project (9,623 units)	DECS	10,400
1H 2012 Rollout		
3 Puerto Princesa Airport Dev.	DOTC	4,200
4 NLEX-SLEX Connector (13.4 km)	DPWH	20,181
5 Vaccine Self-Sufficiency Project	DOH	900
6 Laguindingan Airport (O&M)	DOTC	7,800
7 Mactan Passenger Terminal	DOTC	10,200
8 Fare collection system (MM light railways)	DOTC	
9 Hydroelectric plants O&M (Angat & Macau)	DOE	
2H 2012 Rollout		
10 CALA Expressway	DPWH	11,790
11 New Bohol Airport Dev.	DOTC	8,000
12 LRT 2 Extension to Antipolo	DOTC	12,000
13 Dam & Water Treatment Plant for Metro Manila	MWSS	25,000
14 Cold Chain System	DA	1,500
15 Balara Water Hub	MWSS	20,000
16 Corn Bulk Handling Facility	DA	
17 Phil. Orthopedic Center Modernization	DOH	

Source: Presentation to the Financial Executives Institute of the Phil. (FINEX), by Cosette V. Canilao, PPP Center Executive Director, 23 Nov. 2011

Aside from these projects there are 43 other projects “in the pipeline”. Some projects which were earlier identified to be implemented under the PPP were taken off the list and will instead be undertaken directly by the govt. (e.g., rehabilitation of LRT 1 & 2 and new coaches for MRT 3).

Ms. Cosette V. Canilao, Executive Director of the state-run PPP Center stressed that the latest list is still “indicative” and would be reviewed “periodically”.

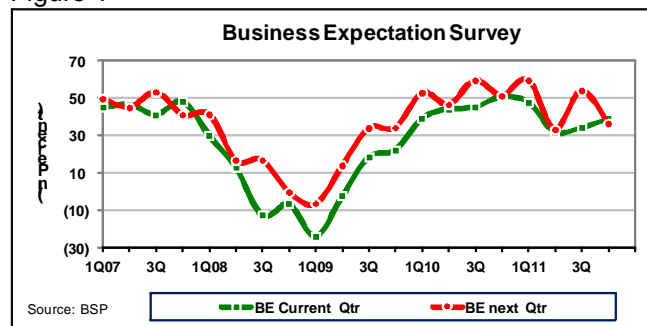
In a related development, the govt. plans to **privatize the New Bilibid Prison** in Mandaluyong City as well

as the construction of a new prison facility in the province.

Latest Business Expectation Survey sends mixed signals. Based on BSP data, respondents were generally optimistic for the current quarter (green line in Figure 1) on account of the following: (a) seasonal increase in consumer demand during the Christmas & harvest seasons; (b) implementation of govt. projects; (c) sound macroeconomic fundamentals; (d) business expansion arising from steady investment inflows; (e) introduction of new and enhanced business strategies; and (f) the steady stream of overseas remittances.

However, respondents were a bit skeptical on the business prospects for the next quarter (red line in Figure 1) due to (a) weak global economy; (b) geopolitical tensions in the Middle East & North Africa; (c) residual effects of the natural disasters in Japan and Thailand; (d) the adverse impact of recent typhoons on commodity prices.

Figure 1



3Q GDP weaker than expected. As we were finishing this news letter, 3Q GDP came out at 3.2%, weaker compared to the 3.4% growth during the 2Q and lower versus consensus estimate of 4.1%. This result should not come as a surprise given the absence of significant govt. spending during the quarter. More details next issue.

Corporate News:

Opposition to connector project. Citra, the operator and majority owner of the Skyway Road System, plans to oppose the connector road being proposed by Metro Pacific Investments (MPI). Citra claims that they have

the right to undertake this project as it was part of their original proposal to the govt. This objection could cause some delay to the scheduled Swiss Challenge on MPI's connector road project. The seriousness of Citra's proposal is in doubt though since the company has an overleveraged balance sheet.

Megaworld (MEG) and Clark Dev. Corp. is close to signing a deal that would allow the former to develop a 400-ha. area into a mixed-use facility featuring office, commercial, retail, leisure, residential, health and wellness components. Project cost is estimated at ₱7.0 bn.

Prime Metroline Transit Corp., a company controlled by Enrique Razon, bought 75% of Active Alliance, Inc. (AAI) for ₱200 mn. The deal will be finalized after the due diligence and the mandatory tender offer are completed. Investors believe that AAI will be used by Razon as the vehicle for his gaming interest Bloomsbury Hotels & Resorts. Razon is building a leisure and entertainment complex within the PAGCOR City which will feature a casino, hotels, retail shops, fine dining, health & wellness center.

Bloomsbury will occupy 8.3 ha. of the proposed 120 ha. PAGCOR City. Aside from Bloomsbury, three other companies are obliged to set-up their own gaming complexes as part of their license agreement with the govt. These companies are Travellers Int'l. (jointly owned by AGI and Genting of Malaysia), Belle Corp. (majority owned by the SM group) and Aruze (Japanese owned).

Sale of Shares. Three companies are planning to sell its shares soon:

1. **Tanduay Holdings**, via an IPO to increase free float to at least 10%
2. **Eton Properties**, via an IPO to increase free float to at least 10%
3. **SMC Global Power.** Possibly via a private placement after its USD850 mn IPO was deferred. SMC Global Power is the country's largest Independent Power Producer (IPP) by virtue of its right to sell the output of the 1,000 MW Sual coal plant, 345 MW San Roque Hydro and 1,200 MW Ilijan natural gas plant.

Investors continue to be battered by strong headwinds coming from Europe. What was originally viewed as a problem in Europe's periphery has now moved dangerously into its center. The reason why the problem has festered is due to Europe's refusal to take drastic steps to address the creeping contagion. In order to calm markets, investors would like to see:

1. A more robust European Financial Stability Facility (EFSF). This has been partly accomplished when Europe's leaders agreed to leverage the EFSF.
2. A more pro-active role of the European Central Bank (ECB). This would mean, among other things, allowing the ECB to raise funds via the issuance of Euro bonds. The funds would then be used to buy distressed sovereign bonds with the aim of keep Euro bond yields low. This strategy is very similar to the Fed's quantitative easing program.

Largely due to political reasons, the second proposal is strongly being opposed by German Chancellor Angela Merkel. Frau Merkel said that the Euro bonds are "not needed and not appropriate". She said Euro bonds would "level the difference" in euro region interest rates. "It would be a completely wrong signal to ignore those diverging interest rates because they're an indicator of where work still needs to be done".

In other words Germany (the Eurozone's largest economy) does not want to further foot the bill until substantial reforms are underway in Europe's profligate governments. Moreover Germany remains reluctant to further open its purse unless fiscal integration is enhanced. These are the quid pro quo being demanded by Germany.

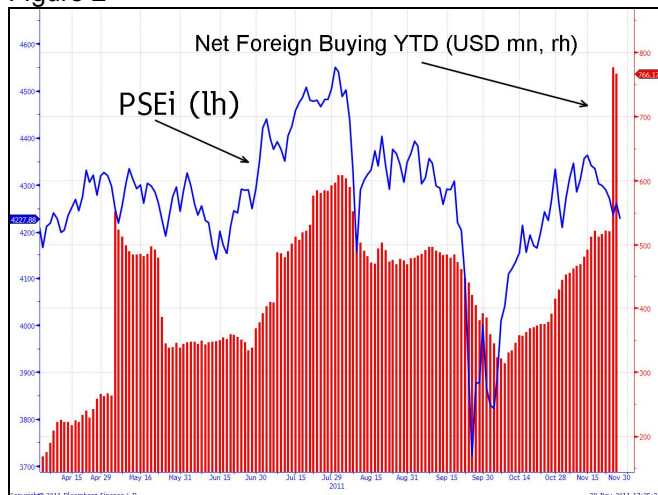
While Germany's position is understandable there is a clear danger to this approach. The longer Germany procrastinates, the deeper the problem becomes which could ultimately threaten the stability of Germany itself.

Not our problem but . . . These may not be our problems but we continue to suffer from their ripple effects given the interconnectedness of financial markets. Fortunately for the Phil. the negative impact on our markets is being mitigated by improving domestic fundamentals.

Foreign buying remains positive throughout the year. Figure 2 below shows the level of foreign buying in the local bourse. While the daily flows fluctuate the trend continues to be net foreign inflows. During the last two trading sessions though foreign buying was extremely high on account of the MSCI rebalancing. As reported in our previous newsletter four stocks made it to MSCI's indices. These are San Miguel Corp. (+1.7% to ₱128.00), Int'l. Container Terminal Services (-1.9% to ₱56.90), Universal Robina (+1.9% to ₱51.45) and Lepanto Consolidated "B" (+7.5% to ₱1.71).

We expect MSCI-related trades to continue this week and next as the official rebalancing will only occur on Nov. 30.

Figure 2



Local bonds ended mixed last week but yields were mostly higher (Table 1). Improving fundamentals, indications that the BSP will likely keep rates steady until the end of the year and a high liquidity level have kept rates at record lows. The weak 3Q GDP may even prompt the BSP to undertake monetary easing as early as 1Q 2012.

Table 1. PDSTF Rates

PDST-F	YIELD (%)		Change (bps)
	18-Nov-11	25-Nov-11	
1 Month	2.22	2.31	9.81
3 Months	1.39	1.89	49.92
6 Months	1.40	1.74	34.75
1 Year	1.40	1.72	32.66
2 Years	2.83	2.70	(12.70)
3 Years	3.70	3.69	(1.84)
4 Years	4.99	5.11	11.54
5 Years	5.18	5.23	5.77
7 Years	5.32	5.39	7.46
10 Years	5.90	5.93	3.38
20 Years	7.33	7.28	(4.65)
25 Years	7.32	7.19	(13.05)

Source: Bloomberg

UITF Performance

Some of our funds (UEF, UBF) took advantage of MSCI-related trades. It was a good week for equities with our UEF and UBF higher by 1.5% and 0.9% for the week, respectively.

Table 2. SDA Rates

Tenor	YIELD (%)		Change (bps)
	18-Nov-11	25-Nov-11	
1 Month	4.6875%	4.6875%	0.00
14 Days	4.6250%	4.6250%	0.00

Source: BSP

ROPs were slightly on the defensive last week as investors turned cautious in the light of Europe's still unresolved problems. Any further weakness should be a buying opportunity.

Table 3. Indicative ROP Prices

Series	Coupon	Maturity	Yrs to Maturity	PRICE	Yield to Maturity
				25-Nov-11	
ROP 13	9.000	15-Feb-13	1.2	108.50	1.9%
ROP 14	8.250	15-Jan-14	2.1	113.21	1.9%
ROP 15	8.875	17-Mar-15	3.3	121.41	2.1%
ROP 16 n	8.000	15-Jan-16	4.1	121.27	2.6%
ROP 16	8.750	07-Oct-16	4.9	126.73	2.8%
ROP 17	9.375	18-Jan-18	6.1	130.14	3.8%
ROP 19	9.875	15-Jan-19	7.1	138.56	3.7%
ROP 19 n	8.375	17-Jun-19	7.6	130.89	3.7%
ROP 20	6.500	20-Jan-20	8.2	118.87	3.8%
ROP 21 n	4.000	15-Jan-21	9.1	101.17	3.8%
ROP 21	4.950	15-Jan-21	9.1	97.50	5.3%
ROP 24 n	7.500	25-Sep-24	12.8	126.58	4.7%
ROP 24	9.500	21-Oct-24	12.9	143.53	4.9%
ROP 25	10.625	16-Mar-25	13.3	156.06	4.9%
ROP 26	5.500	30-Mar-26	14.3	108.70	4.7%
BSP 27	8.600	15-Jun-27	15.6	129.63	5.7%
ROP 30	9.500	02-Feb-30	18.2	150.72	5.2%
ROP 31	7.750	14-Jan-31	19.1	130.81	5.2%
ROP 32	6.375	15-Jan-32	20.1	116.41	5.1%
ROP 34	6.375	23-Oct-34	22.9	117.96	5.0%
ROP 36	6.250	14-Jan-36	24.1	97.00	6.5%

Source: Bloomberg

Table 4. UITF Performance

UITF (PhP)	31-Dec-10	18-Nov-11	25-Nov-11	Change	
				Wk-on-Wk	Yr-to-Date
UCF	1.4839	1.5558	1.5532	-0.17%	4.67%
USMMF	1.2462	1.2620	1.2678	0.46%	1.73%
UCMF	1.1451	1.1738	1.1731	-0.06%	2.44%
UBF	1.7428	1.8790	1.8961	0.91%	8.80%
UEF	2.2666	2.4709	2.5075	1.48%	10.63%
UCF	United Conservative Fund				
USMMF	United USD Money Market Fund				
UCMF	United Cash Management Fund				
UBF	United Balanced Fund				
UEF	United Equity Fund				

Table 5. Market Indicators

Indicator	Level			Change			
	2010 Yr. End	23-Sep-11	30-Sep-11	Wk-on-Wk	% Ch	YTD	% YTD
Peso	43.80	42.73	42.74	0.01	0.03%	-1.06	-2.42%
Stocks	4,201	3,886	4,000	113.69	2.93%	-201.49	-4.80%
3-mo. PDSTF (ch in bps)	1.2917	4.1944	2.9627	-1.23 ¹	(123.17)	1.67 ¹	167.10
Peso Bonds	307	323	326	3.06	0.95%	18.65	6.07%
3-mo. USD LIBOR (ch in bps)	0.3028	0.3602	0.3743	0.01 ²	1.41	0.07 ²	7.15
USD Bonds (ROPs)	178	186	186	-0.69	-0.37%	8.03	4.52%
Crude Oil (USD/bbl)	91.38	79.85	90.26	10.41	13.04%	-1.12	-1.22%
Gold (USD/troy oz)	1,420.78	1,656.80	1,623.97	-32.83	-1.98%	203.19	14.30%
DXY (USD Index)	79.03	79	79	0.05	0.07%	-0.48	-0.60%
ADXY (Asian Currencies)	116.46	115	115	-0.52	-0.45%	-1.82	-1.56%
VIX	17.75	41	43	1.71	4.15%	25.21	142.03%
V2X	23.92	49	47	-1.86	-3.83%	22.76	95.18%

Sources:

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