PrimeEquity Research

Meridian Securities INCORPORATED Member: Philippine Stock Exchange

MARKET RECAP

03 August 2018

PSEi	Value Turnover (US$)	Net Foreign Flow (US$)	PHI:US (PLDT ADR)	US$ 1.00
7,819.39 (+0.77%)	107,849,438.57	125,371.00	25.00 (-1.11%) = 1,327.88	53.008

Market Recap

- Philippine share prices rebounded following a tech-led rise on Wall Street, although the latest exchange of trade threats between Beijing and Washington capped gains and kept investors on edge.
- The benchmark PSEi gained 59.84 points or 0.77% to close at 7,819.39. The broader All Shares index added 23.61 points or 0.51% to 4,668.29 at the closing bell.
- Shares, which have fluctuated this week owing to the increasingly heated trade row, took another hit when the White House said it was considering more than doubling threatened tariffs on $200-bil of Chinese imports.
- Beijing responded by saying it would not give into "blackmail".
- There are genuine concerns about this trade war underlying markets, which makes any genuine retaliation from China, rather than the current rhetorical approach, an issue for markets.
- However, while the risks of escalation remain high, the market still thinks the latest US threat is just a negotiating tactic.
- The equity markets now have time to regroup and settle down after yesterday's slide. But the US-China trade conflict involves the epicenter of the region and this will continue to weigh psychologically on Asian equities.
- Investors also remain cautious ahead of the July US jobs report due later on Friday, which will give a reading on the health of the world's largest economy and possible clues about the pace of Federal Reserve interest rate rises.
- More than 1.715-bil shares, valued at P5.716-bil, changed hands. Market breadth was positive, with advancers trumping decliners, 126 to 67, with 51 issues unchanged.
- Gainers: MBT (+3.68%), AEV (+3.27%), DMC (+2.48%), JGS (+2.15%), AC (+2.10%)
- Laggards: MER (-2.63%), EDC (-2.14%), ALI (-1.82%), ICT (-1.72%), SMC (-0.29%)

Tax Reform and Inflation

- The Department of Finance said rising inflation, which has been partly stoked by a new tax law, has been "politicized," making it hard for the Duterte administration's succeeding tax reforms to breeze through Congress.
- Inflation spiked to a fresh five-year high of 5.2% in June from May's 4.6%, putting the year-to-date figure at 4.3%, or above the central bank's 2% to 4% target range. The central bank has responded by delivering back-to-back rate hikes.
- People have blamed soaring prices on the Tax Reform for Acceleration and Inclusion law, which raised excise levies on fuel, "sin" products and sugary beverages, among others.
- Supply-side factors like higher global oil prices—exacerbated by the continuing depreciation of the peso—are also pushing up commodity prices. The country's economic managers, meanwhile, have pointed out that elevated inflation was typical of a rapidly expanding economy.
- "Unfortunately, the inflationary episode has been politicized. Tax reform was blamed for causing inflation," Finance Secretary Carlos Dominguez III said.
- "What should otherwise be understood as an economic phenomenon normally accompanying high growth has been skewed to pin blame on our reformist policies," Dominguez added.
- According to the Finance chief, tax rates imposed on "sin" products and sugary drinks—which have been driving up inflation—were intentionally punitive to improve the health of Filipinos.
- He then said the remaining tax reforms might hit snags in Congress due to "more political resistance."
- "Part of the reason for this resistance is the proximity of elections. Tax policy, as we know, is never the best way to be re-elected," Dominguez said. "Nevertheless, we are committed to seeing the entire comprehensive tax reform program enacted this year."
- Also known as TRAIN 2, the second package of the government's Comprehensive Tax Reform Program seeks to reduce corporate income tax rates and streamline fiscal incentives to grant them only to those who need them.
- Despite President Rodrigo Duterte's public popularity and the super-majority he holds in Congress, Senate majority leader Juan Miguel Zubiri earlier said the proposed corporate tax reform has "very little support" from senators amid fears that the measure could slow investments and fan inflation.

MARKET RECAP

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Tax Reform and Inflation (continued)

- The DOF is targeting to introduce in July this year the rest of the tax reform packages that mainly cover property and capital income taxation.
- Since the start of 2018, the DOF has submitted Package 2, as well as the reforms on taxes on alcohol and mining, while supporting the bill of Sen. Manny Pacquiao on tobacco excise taxes.

Mining

- The government plans to slap royalty on all mining operations under the proposed tax package 2 Plus.
- The Department of Finance (DOF) had proposed to impose royalty on mining contractors for all metallic and nonmetallic mining operations, whether small- or large-scale.
- At present, a royalty is imposed only on mine sites that were declared mineral reservations.
- For operations within mineral reservations, the plan is to levy royalty equivalent to 5% of the market value of the gross output of the mineral products extracted or produced, exclusive of all other taxes.
- For mining operations outside mineral reservations, the proposal sets the royalty at 3% yearly during the first three years, 45 on the fourth year and 5% beginning the fifth year onward.
- Mining contractors will also pay an “additional government share” when the basic government share consisting of direct taxes, royalties, fees and other related payments amount to less than 50% of their net mining revenues.
- Based on the DOF proposal, the additional government share would be equivalent to “the difference between the 50% of net mining revenue and the basic government share during the calendar year.”
- The net mining revenue is derived by deducting expenses from gross output.
- Also, the new mining tax regime will impose limitations on mining contractors’ interest expense deductions, depending on the debt-to-equity ratio.
- A debt-to-equity ratio of 1.5:1 for an income year will not allow a deduction for the interest paid on the part of the debt that exceeded the ratio.
- For a ratio exceeding 1.5:1 for a taxable year, meanwhile, the deduction will be disallowed if the amount of a contractor’s debt does not surpass the “arm’s length debt value.”

ECONOMIC INDICATORS					
GDP Growth Rate	6.8% (Q1 2018)	Unemployment Rate	5.5% (April 2018)	GIR	US$77.675-B (June 2018)
Fiscal Surplus / (Deficit)	(P54.3-B) (June 2018)	Exports Growth Rate	(3.8%) (May 2018)	BOP	(US$1.177-B) (June 2018)
Inflation	5.2% (2012 BY) (June 2018)	Imports Growth Rate	11.4% (May 2018)	O/N RP	4.00% (as of June 20, 2018)
91-day T-Bill Rate	3.219 (as of July 23, 2018)	Cash Remittances	US$2.469-B (May 2018)	O/N RRP	3.50% (as of June 20, 2018)

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