

24 May 2016

BUY

(Upgrade from HOLD)

PRICE TARGET(12-month)

P343.00

Manila Electric

Company

Bloomberg: MER PM /Reuters: MER.PS

Analyst

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Volume soars

- Upgrade to BUY, TP nudged higher to P343
- 1Q16 earnings in line with estimates
- Higher FY16F/17F figures on strong volume

Highlights

1Q16 net income up 2.9%; in line. MER reported net income of P4.5bn for 1Q16, +2.9% y-o-y. This is generally in line with our/consensus estimates. Net income growth was driven by strong volume growth (12.2%), higher revenues from non-electricity subsidiaries (+53.1%), gains from financial investments, as well as updated provisions. Costs and expenses sans purchased power costs, meanwhile, increased by 12.6% due mainly to the rise in operating costs in its non-electricity subsidiaries.

Robust volume growth lifts distribution revenues. As the country continues to experience warmer temperature and lower commodity prices persist, consequently pushing generation charges down, volume surged to 12.2% in 1Q16. With inflation remaining low, energy sales to residential customers jumped by 20% followed by the commercial segment at 12.7%. The industrial segment outpaced its FY15 performance of 3.4% with 1Q16 growth of 4.9%. This higher-than-expected volume growth more than offset the 8% decline in distribution tariff, thereby lifting distribution revenues by 2.4%.

Now at 100% payout. MER has also declared special cash dividends of P1.7 per share out of FY15 earnings. Together with the P15.1 per share declared earlier, total dividends declared out of FY15 earnings amount to P16.8 per share, equivalent to dividend payout of 100%.

Outlook

FY16F/17F earnings raised by 2%/3%. Following the robust volume growth in 1Q16, we raise our volume growth assumption for FY16F/17F to 7.1%/3.8% from 4.2%/3.5%. We believe that the current combination of higher average temperature and low inflation supports double-digit volume growth at least until 2Q, where management already mentioned a 12% growth in April. After adjusting for volume growth, we raise our FY16F/17F earnings by 2%/3%. From our initial estimate of a 4.6% decline, we now expect a milder 2.3% earnings decline for FY16F. Our FY16F still lags management guidance of P18.9bn earnings as our lower FY16F income is premised on lower distribution rate as well as absence of one-off items in FY15.

Recommendation

Upgrade to BUY; TP nudged to P343. Following our earnings revision and adjustments in MER's generation assets, we raise our SOP-derived TP to P343. Implied PE is at 21x FY16F. Together with the c.5% dividend yield from the revised payout assumption, MER offers a potential total return of 12%. Upgrade to BUY.

Forecasts and Financial Summary

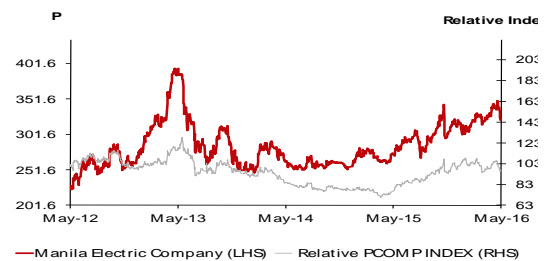
	2015A	2016F	2017F	2018F
Revenue	258,399	288,006	298,384	309,750
EBITDA	31,464	33,788	32,666	30,123
Net Pft (Pre Ex.)	19,098	18,663	18,361	16,468
EPS Pre Ex. (P)	16.9	16.6	16.3	14.6

Source of all data: Company, First Metro Securities, Bloomberg Finance L.P.

At A Glance

Shares out(m shrs)	1,127
Mkt. Cap(Pm/US\$m)	362,926 / 7,769
3m Avg. Daily Val.(US\$m)	1.9

Price Relative



Financial Ratios

	2015A	2016F	2017F	2018F
PE Pre Ex. (X)	19.0	19.4	19.8	22.0
EV/EBITDA (X)	10.9	9.8	10.0	10.8
Net Div Yield (%)	4.7	5.1	5.1	4.5
P/Book Value (X)	4.5	4.5	4.5	4.5
Net Debt/Equity	CASH	CASH	CASH	CASH
ROAE (%)	24.0	23.2	22.9	20.5

Rating System:

STRONG BUY (>20% total return over the next 3 months, with identifiable share price catalysts within this time frame)

BUY (>15% total return over the next 12 months for small caps, >10% for large caps)

HOLD (-10% to +15% total return over the next 12 months for small caps, -10% to +10% for large caps)

FULLY VALUED (negative total return i.e. > -10% over the next 12 months)

SELL (negative total return of > -20% over the next 3 months, with identifiable catalysts within this time frame)

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