



Philippines

As the economy takes off, so too does M&A activity

Current Environment

The government's initial estimate of Gross Domestic Product (GDP) for 2007 indicates solid growth of 6 percent and 6.9 percent in the first and second quarters, respectively. This was way above the National Economic and Development Authority's estimate of 5.3 - 6.1 percent. Historically, GDP growth hovered around 5.5 percent or lower. Accordingly, the 2007 full year GDP forecast is estimated at 6.1 - 6.7 percent.

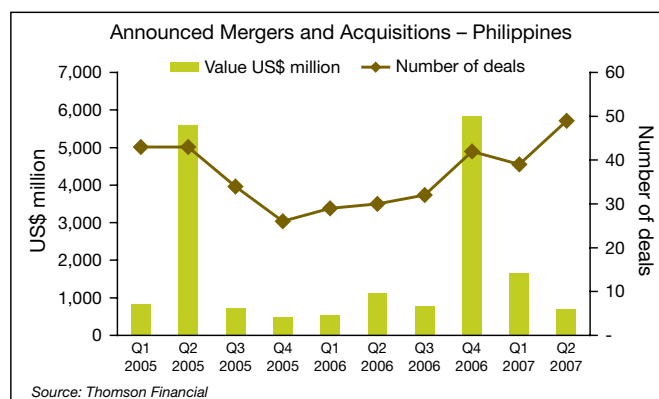
For the first half of 2007, the service sector fuelled the growth on the supply side. The service sector grew by 9.1 percent for the first quarter with transport, communication and storage, business process outsourcing (BPO) and call centres leading the pack. Activity in the real estate sector has also been ticking up, partly driven by the demand for office space from the BPOs. On the demand side, growth was boosted by substantial government spending in the May 2007 elections, high export performance and solid private consumption.

Investors' renewed sense of optimism in the Philippine economy is reflected in the buoyant stock market. The Philippine Stock Exchange index reached new highs, closing at 3,665 at the end of June, an 18 percent growth from December 2006. Companies are actively engaged in stock rights offerings and initial public offerings (IPOs). These include the US\$370 million stock rights offering of the Alliance Global Group, and the IPOs of National Reinsurance Corporation and Pacific Online Systems Corporation, raising US\$52.3 million and US\$7.6 million respectively. This positive sentiment is also mirrored in higher foreign portfolio investments of US\$1,673 million for the first five months of 2007, which was 152 percent higher than the same period in 2006.

The price environment continues to be stable in the aftermath of the mid-term elections, with inflation contained at an average of 2.7 percent. On the other hand, interest rates have started to climb slightly, with the 91, 182 and 364-day papers averaging higher at 3.02 percent, 3.998 percent and 5.174 percent in the primary market. The Philippine Peso however continues to appreciate against the US dollar. At the end of June 2007, the Peso closed at Php46.24 to the US dollar from Php49.03 as of the end of December 2006. The strengthening of the Peso is largely due to the continued remittance from the overseas Filipino workers (OFW), averaging at least US\$1 billion per month.

As for government fiscal performance, the government targets tax collection of US\$16.6 billion for 2007. However, for the period January to May 2007, tax collection is already short by US \$979.7 million, leading to the resignation of the Bureau of Internal Revenue Chief in June 2007. The government plans to cover the shortfall by raising US\$2.3 billion from privatisation proceeds. This may be a tall order for the government to reach the budget deficit target of US\$1.4 billion for the year.

Deal Activity



The value of announced deals was up by 42 percent to US\$2.3 billion for the first half of 2007, with deal volume increasing to 88 as compared to the 59 for the first half of 2006.

The increase in deal volume, specifically in inbound investments, can be attributed to increased optimism with respect to the economic and political environment of the country.

Major deals that transpired include the following:

Food and beverage sector

San Miguel Corporation (SMC) has announced plans to divest its majority stake in National Foods Australia to Kirin Brewery. SMC disclosed that it is planning to explore other industries, such as mining and utilities.

In line with these divestment plans, SMC finalised the sale of its 65 percent interest in Coca-Cola Bottlers Philippines, Inc. for US\$590 million. SMC also sold its stake in Del Monte Pacific Limited in Singapore for US\$150 million in April 2007.

Also in the beverage industry, Singapore-based Nassim Fund acquired a minority stake in Pepsi-Cola Products Philippines, Inc. for US\$21.6 million. The company plans to do an IPO by 2008 and thereby raise approximately US\$150 million.

Utilities sector

Davao Oriental Electric Cooperative acquired the sub-transmission assets of the state-owned National Transmission Corporation for US\$1.4 million in June 2007.

Liquigaz Philippines Corporation acquired the commercial and industrial liquefied petroleum gas business of Chevron Philippines Inc. in May 2007.

The 360 megawatt government-owned Magat hydro plant was also successfully sold to Norway's SN Power and Aboitiz Power Corporation in January 2007.



Mining sector

There were a number of movements in the mining industry. These included an increase in the stake of Anglo Investments BV in the Kalayaan Copper Gold Resources, Inc. from 40 percent to 60 percent for US\$21 million.

Another is Indophil Resources NL's acquisition of an additional 5 percent in Tampakan Copper-Gold Project, raising its stake in the project to 37.5 percent. The Project is also 62.5 percent owned by Xstrata PLC. The 5 percent stake was bought from Alsons Corporation for US\$23.8 million.

Manufacturing sector

In April 2007, Nihon Yamamura Glass Co Ltd acquired a 35 percent stake in San Miguel Packaging International Ltd.

TKC Steel Corporation acquired 100 percent of Treasure Steelworks Corp, a steel manufacturer, for US\$2.2 million.

Banking and insurance sector

China Bank acquired the Puyat Family's 87.5 percent stake in Manila Bank for US\$34.6 million in June 2007.

In March 2007, First Metro Investment Corporation announced plans to acquire a 16.67 percent stake in Philippine Charter Insurance Corporation, a majority-owned unit of Metrobank.

Danvil Holdings Inc. acquired Berkley International Philippines from WR Berkley Corporation for US\$27 million.

BPO sector

Global E-business Solutions Inc. announced plans to acquire a 90 percent interest in E-Performax Contact Centres Corporation from Easycall Communications Philippines Inc, for US\$1.5 million in June 2007.

Outlook

The Philippine macroeconomic fundamentals have been showing strength as evidenced by higher than expected 2007 half-year growth, low interest rates and a strong Peso. Investors remain bullish on the economy, with the mining and BPO sectors expected to spearhead the growth.

Mining sector

The Philippines being one of the world's largest deposits of metallic and non-metallic mineral sources, mining is expected to grow significantly. It was reported that some 300 firms have already positioned themselves for the mining boom. In retrospect, the Supreme Court of the Philippines ruled that the 1995 Mining Act was constitutional, thus confirming the permissibility of 100 percent foreign-owned mining contracts.

BPO sector

Despite the cost impact of the strengthening Peso, BPO projects continue to spread across the country. This sector of

contact centres, medical transcription, software development and other IT-enabled services receives high inflows of overseas funds reportedly estimated to reach US\$10 billion by 2010.

Property sector

There is also renewed confidence in the property sector. Property demand is seen to be driven by BPOs, tourism and housing demand from OFWs. This is reflected in the consolidation of the property companies of Villar-owned Vista Land, Lifescapes and C&P Homes.

The President's trip to China in April 2007 resulted in a property development deal of the Fort Bonifacio property estimated at US\$2-4 billion. The proponents for this project will be Shimao Group of China and the Bases Conversion Development Authority.

Alliance Global Group, likewise consolidated its interest in Megaworld, another major property firm in the Philippines specialising in office spaces for BPOs by increasing its stake in the latter by 25 percent in February 2007.

Privatisation of government assets

Given the Philippine fiscal situation, the main thrust of the government is to raise money via selling government assets. The government-owned National Power Corporation was a major contributor to the deficit and thus has been put up for sale. The government is expected to raise at least US\$1,081 million from the privatisation of power plants. Targeted for privatisation are the 600MW Calaca power plant and 600MW Tiwi Makban geothermal plant and the 25-year National Transmission Corporation concession.

Also, the country's major seaports and airports have been up for auction. These include Laguindingan airport in Misamis Oriental, Northern Mindanao, where Korean heavyweights Daewoo, Samsung and Hanjin have all expressed interest.

The North Harbour in Tondo and the Batangas port have also registered interest from major listed companies. North Harbor in Tondo is a 35 percent-65 percent joint venture between Metro Pacific Investments Corp. and Harbour Centre. In June 2007, International Container Terminal Services, Inc. won the right to operate the Subic Bay Freeport.

The Department of Finance (DOF) put the Iloilo airport privatisation out for bids. However, the bids submitted were below the US\$26 million minimum set by the DOF. The DOF gave the bidders a second chance to improve their bids.

In line with the government's plan to raise revenues by selling its stake in listed companies, the government is including for sale its 29 percent stake in Meralco and the Lopez group is readying itself for the purchase.

Despite the deficit target, the government will continue its spending, allocating US\$3.1 billion for infrastructure projects in 2007. These government-led activities, coupled with the promising outlook for the economy as a whole, will continue to feed the increased M&A trend for the foreseeable future.