What's *mine* is yours and vice versa

By Roxanne S.C. Olanday

The mineral wealth in the Philippines has long been touted as one of the richest in Asia with official estimates of mineral reserves ringing in at US$1.4 trillion. Of the 30 million hectares of total land area in the country, approximately 9 million are seen to have high mineral potential. According to the World Gold Council report, the country ranks 23rd in terms of gold reserves, while Bloomberg estimates place the country as the top producer of nickel. Despite all these however, the mining industry's contribution to the economy is kept at a dismal 1.1% in 2014, and 1.2% for the first quarter of 2015. In fact, as can be seen in Table 1, the gross value added in mining and quarrying last year was virtually the same level as in 2013, growing at an average of only 1.03% in the past five years.

Table 1: Gross Value Added In Mining & Quarrying at Current and Constant Prices, In Million Pesos (2010-2014)

	At Current Prices						At Constant 2000 Prices					
Industry/Industry Group	2014	2013	2012	2011	2010	CAGR (%)	**2014**	**2013**	**2012**	**2011**	**2010**	**CAGR (%)**
1. Copper mining	10,401	10,867	7,457	9,244	7,656	1.06	3,675	3,567	2,884	2,672	2,496	1.08
2. Gold mining	18,971	18,788	20,412	42,504	48,199	0.85	4,515	4,216	3,961	9,072	11,828	0.82
3. Chromium mining	249	130	165	108	92	1.18	113	72	94	40	32	1.29
4. Nickel mining	22,440	17,109	19,913	12,314	8,048	1.13	23,231	22,180	20,467	14,789	10,206	1.18
5. other metallic mining	843	1,878	2,961	3,113	1,250	0.77	206	562	668	500	297	0.93
6. Crude oil, natural gas & condensate	39,474	37,701	41,896	46,127	40,517	0.97	20,723	20,422	22,617	23,669	22,542	0.98
7. Stone quarrying, clay and sandpits	16,974	15,131	12,899	10,217	9,475	1.11	12,671	11,740	10,120	8,966	8,844	1.07
8. Other non-metallic mining	16,036	13,857	15,732	19,401	13,490	0.96	11,340	10,135	11,235	10,771	9,653	1.03
Gross Value Added in Mining & Quarrying	**125,388**	**115,461**	**121,435**	**143,028**	**128,727**	**0.97**	**76,474**	**72,894**	**72,406**	**70,479**	**65,898**	**1.03**

Source: NSCB

As though adding insult to injury, data gathered from the Mines &Geosciences Bureau of the Department of Environment and Natural Resources, show that total mining investment in 2014 only reached US$693.1 million, 52.3% lower from the prior year and well below projections of US$3 billion. This is said to have been largely driven by Executive Order 79 (EO 79) issued in 2012, which prohibits the government from granting new mineral agreements until a new revenue sharing scheme is in place. Approximately 1,800 mining applications (est. at Php528 billion worth of investments) was affected by EO 79. In addition, employment in the sector also fell to 235,000 from 250,000, with only a 0.6% contribution to total employment.

Meanwhile, total exports of minerals and mineral products grew 17.6% to US$4.01 billion in 2014, led by exports in copper, gold, and nickel, with Japan, Australia, Canada and China as the top destination countries. Total exports of non-metallic mineral manufacturers kept steady at US$244million.

The El Nino boost to nickel

Mining firms, however, find some comfort in the prevalent El Niño and the dryness that it brings, after a recent slump in global mineral and commodity prices. Typically, during the rainy season, around the third quarter of the year to the second quarter of the next, metal producers resort to halting field operation due to safety and technical issues. The weather makes the land wet and difficult to mine ore from. Now that the rainy season has moved further in the year, operations can continue for longer as well.

Nickel mining firms are particularly upbeat that their mining operations would continue until yearend, supporting company earnings and exports. Note, nickel is an important resource as it is a component of many consumer and industrial products like stainless steel, kitchen and laboratory sinks and plating material. The positive outlook of nickel miners is in stark contrast to farmers and agri-based producers whose output are severely damaged during the drought and dry spell that the El Niño carries with it. For instance, less rains from the first half of the year has already helped Nickel Asia Corporation, the largest mining firm in the country and global supplier of lateritic nickel ore, ship 9.68 million wet metric tonnes (WMT), 25% higher year-on-year. Meanwhile, the Philippines' third largest nickel producer Global Ferronickel Holdings, Inc., sees its shipments to grow by as much as 7 million WMT this year, a record by its books.

On the other hand, one deterrent to this is the aforementioned easing of commodity prices. London prices fell 27% in June to approximately US$11,980 due to warehoused nickel growing almost two times over in the past year and a half to 470,000 tonnes this June. Lagging demand also pushed Agata Mining Ventures to withdraw and cancel shipments in May. Nickel prices in the country have tumbled by 80% in value since its peak in 2007.

The Indonesian export ban; China inventories

Early last year, the Indonesian government banned the export of raw materials, including nickel, copper ore and bauxite, until mining companies construct metal-processing facilities (smelters) in order to add value to resources and generate jobs. 80 smelters are currently being built, with 25 finished and some 16 between 11% to 30% completion. This has already lost Indonesia billions of dollars worth of revenues to the benefit of the Philippines that has since then come out as the world's top nickel exporter and

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producer, contributing almost 20% of total global supply. Now the country is a major supplier of nickel ore to Japan and China. Almost all of China's nickel ores and concentrate imports came from the Philippines this January to June.

Still, concerns over the country's capacity to satisfy the demands of these two powerhouses remain. In particular, China's stockpiled volumes of nickel pig iron, used as a lower-quality substitute to refined nickel, are beginning to wane. Should inventories dangerously fall to 30%, the country would become completely reliant on supply from the Philippines, by which time China would be forced to consider importing from outside the Asia-Pacific area.

Inventories in China have already plunged to the level of 120,000 tons of pure nickel from 194,000 tons since the end of the first quarter this year. Remaining supply of nickel ore, including refined nickel and ferronickel, may run out in three months' time, according to Beijing Antaike Information Development Company. This could be a good thing for nickel investors as the declining supply could lift nickel prices on the London Metal Exchange back to US$16,000 per metric ton.

Coal and copper updates

Data from the BP Statistical Review of World Energy June 2015 revealed that in 2014, consumption of coal was globally unchanged, rising by a measly 0.4%, below the 10-year average annual growth of 2.9%. Similarly, the share of this resource in the primary energy consumption plummeted 30% worldwide. Beyond the Organisation for Economic Co-operation and Development (OECD), consumption only increased by about 1%, the slowest pace since 1998, on the back of declining consumption in China. Within the OECD, meanwhile, consumption also went down 1.5%, with the European Union sporting the largest fall at 6.5%. Production-wise, globally, coal posted laggard figures, thinning down to 0.7%, led by China, which also showed the world's largest decline in volume, and Ukraine.

Locally, this downward trend does not seem to follow as the Department of Energy claimed an additional 25 coal-fired power stations, with a total capacity of 12,200 megawatts (MW) are in the pipeline. Note, about a third of the Philippines' power capacity, close to 18,500 MW, utilizes coal as fuel. Supplies stem mainly from Semirara Mining and Power Corp.'s mines, though bulk of what is used is imported from Indonesia, with some trickling in from Australia, Vietnam and China. Last year, foreign coal imports leapt to a record 15.2 million tonnes.

Table 2: Gross Value Added In Mining & Quarrying at Constant Prices, In Million Pesos (1H14 Vs. 1H15)

	At Constant 2000 Prices		
Industry/Industry Group	**1H15**	**1H14**	**Growth Rate%**
1. Copper mining	2,436	2,546	(4.32)
2. Gold mining	2,407	2,115	13.81
3. Chromium mining	22	47	(53.19)
4. Nickel mining	16,707	15,467	8.02
5. Other metallic mining	63	95	(33.68)
6. Crude oil, natural gas & condensate	15,389	13,630	12.91
7. Stone quarrying, clay and sandpits	5,931	5,720	3.69
8. Other non-metallic mining	7,200	8,433	(14.62)
Gross Value Added in Mining & Quarrying	**50,155**	**48,053**	**4.37**

Source: NSCB

Although Table 2 shows that gold mining grew 13.81% from January to June this year versus last year, the commodity's price has since dropped 37%. Likewise, the price of copper fell to technically bearish levels of 48% since its peak four years ago, with the sub-sector declining also 4.32% in the first semester of 2015 compared to the same period last year. This could also be attributed to the withdrawal of resources giant and global commodities trader, Glencore PLC, from the 23,571 hectare Tampakan copper-gold mine in Mindanao. Glencore PLC sold its controlling stake in Sagittarius Mines Inc.to Alsons Prime Investments Corp. This mine was said to have been home to an estimated 2.94 billion tons of mineral resource, including 15 million tons of copper and 17.6 million ounces of gold, based on estimates of Sagittarius Mines Inc.

Figure 1: Falling Commodity Prices (Gold, Nickel, Copper, Coal)

Source: Bloomberg

Table 3: Global Metal Price Forecast

Metal/Commodity	Spot	Q3 15	Q4 15	Q1 16	Q2 16	2016	2017	2018	2019
Gold $/t oz	**1108**	**1118**	**1102**	**1103**	**1104**	**1105**	**1114**	**1128**	**1146**
Forecast (Median)		1137	1145	1125	1167	1180	1225	1250	1250
Diff (Median - Curr)		19	43	22	63	75	111	122	104
Copper $/mt	**5347**	**5309**	**5349**	**5337**	**5331**	**5331**	**5327**	**5326**	**5336**
Forecast (Median)		5319	5475	5525	5700	5800	6200	6777	6875
Diff (Median - Curr)		10	126	188	369	469	873	1451	1539
Nickel $/mt	**10095**	**10635**	**10088**	**10111**	**10129**	**10140**	**10219**	**10243**	**10243**
Forecast (Median)		11075	12237	12500	13250	15000	14500	20518	18170
Diff (Median - Curr)		440	2149	2389	3121	4860	4281	10275	7927
Coal CIF ARA $/MT	**53.55**	**56.25**	**51.94**	**50.52**	**50.12**	**50.5**	**50.72**	**51.35**	**52.46**
Forecast (Median)		62	57.5	58.5	59	58.65	60	60	60.1
Diff (Median - Curr)		5.75	5.56	7.97	8.88	8.14	9.28	8.64	7.64

Source: Bloomberg

In summary, there remains to be a dark cloud over the mining sector in the Philippines, especially considering the fall of commodity prices (Figure 1), from sluggish demand from China as its economy slows dramatically to 6% growth and on-going political and legislative issues dampen revenues and foreign investment in the sector. On the bright side, severe dry weather brought about by the El Niño phenomenon keeps mining firms optimistic that operations and thus earnings could extend further into the year. Meanwhile, the prolonged Indonesia export ban serves as both a blessing and a curse by pushing Philippine nickel exports and at the same time, putting pressure on miners and producers to meet the large demand from key importers. Like in any business cycle, metal prices will recover and the Philippine mining sector could benefit from a more conducive regulatory but sustainable and balanced-approach environment-focused government policies.

Atlas Consolidated Mining and Development Corporation (Atlas)

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Company Background

Atlas Consolidated Mining and Development Corporation (Atlas) is engaged in the mining, exploration, and development of mineral and metallic properties in the Philippines, primarily producing nickel, copper concentrates, and gold with silver, magnetite, and pyrites as by-products.

Atlas holds interests in the Lutopan underground mine, Lutopan open pit mine, Greater Biga mine, Carmen mine, and Carmen copper concentrator in Toledo City, Cebu, and Palawan Nickel projects located in Quezon, Aborlan, and Puerto Princesa.

The company is also involved in the supply of wholesale or bulk water to local water districts and other customers, and provides professional services, including management services to individual or corporate entities.

Share Data

PSEi Code	AT
Rating	**Outperform**
52-wk range (Php)	4.19-16.00
Current Price (Php)	4.90
12-month Target Price (Php)	7.01
Price Yield (%)	43.0
Dividend Yield (%)	0.0
Total Return (%)	43.0

Review of Share Price Performance

In our Aug 2014 issue of Money Talks, we expected Atlas to UNDERPERFORM the PSEi with a target price of Php15.89 per share. At Php4.90 as of Sep 14, AT's price is down 71% from the Aug 20, 2014 price of Php16.92 per share versus the PSEi's 0.38% comparative slide. The current rout in commodities (which include base and precious metals like copper and gold) prices caused primarily by expectations of weaker demand from China weighed on miners' revenues, and consequently, income and valuations.

AT vs PSEi (3-Year Performance)

Source: Bloomberg

EQUITY RESEARCH

Equity Valuation

Comparative Valuation	Closing Price (Php)	Market Cap (Php bn)	2015 P/B (x)	2015 P/E (x)	2015 ROE (%)	Dividend Yield (%)	Free Float* (%)
SCC	137.50	142.46	5.40	16.34	36.60	2.91	27.31
NIKL	7.38	56.83	1.76	10.39	19.06	5.92	19.16
PX	4.97	25.15	1.00	19.88	5.16	1.01	32.99
AT	**4.90**	**9.50**	**--**	**--**	**-0.89**	**4.90**	**42.27**

*Sources: Bloomberg; * Philippine Stock Exchange*
Note: SCC – Semirara Mining Corp.; NIKL – Nickel Asia Corporation; PX – Philex Mining Corp.

▶ **Weak metal prices drag 1H 2015 results.** Atlas Mining (AT) reported a Php611 million net loss for 1H 2015 because of: 1) a 39% y/y decline in revenues (refer to Operational Highlights table below) on weaker copper and gold prices and lower production volume due to unusually heavy rainfall; and 2) net unrealized foreign exchange (forex) loss of Php220 million recorded for the period primarily from the restatement of US dollar-denominated debt versus forex gain of Php285 million in1H 2014 as the Peso weakened against the US dollar to Php45.09 as of end-June 2015 from Php43.65 in end-June 2014.

▶ **Copper prices: quo vadis?** Copper price levels are currently at five-year lows, but Glencore's (one of the top copper producers in the world) Sep 7 announcement to cut copper cathode production by 400,000 tons over the next 18 months at its Katanga Mining (Democratic Republic of Congo) and Mopani (Zambia) Copper Mines as part of a debt-reduction drive has changed the outlook for the copper market in 2016-17. While this development may not significantly lift prices, it may help stem further drops in the short term.

Operational Highlights (Php millions)

	2013	2014	% chg	1H'14	1H'15	% chg
Copper prod'n ('000 lbs)	91,510	105,480	15%	53,482	46,400	-13%
Gold prod'n ('ozs)	21,430	26,310	23%	12,200	12,986	6%
Copper prices (US$/lb)	3.23	2.98	-8%	3.15	2.67	-15%
Gold prices (US$/oz)	1,368	1,248	-9%	1,295	1,201	-7%
Gross Revenue	14,451	16,181	12%	8,669	5,262	-39%
Core Net Income**	2,856	807	-72%	950	(604)	-164%
Net Income	1,896	397	-79%	989	(611)	-162%
Core NI margin %	19.76	4.99		10.96	-11.47	

*Sources: AT; ** BDO PB estimates*

Our View and Recommendation:

Short-term (less than 2 years): Assuming flat copper prices and metal recovery combined with a moderate increase in production, our 12-month fair value estimate for AT is at Php7.01 per share based on valuations of 12x P/E and 1.0x P/B. Potential price upside is at 43% largely because of the huge discount to book value. We do not expect AT to pay out dividends in the short term since we are forecasting a net loss in 2015 and minimal income in 2016. Moreover, it has a significant debt maturity in 2017. **Outperform.***

Medium-term (beyond 2 years): For the medium term, we expect AT's price to reach Php11.84 per share by 2017, for an average annual price yield of 47% versus our expected 10% gain for the PSEi. Metal prices volatility and regulatory environment continue to pose risks, which can go for or against miners depending on various factors. Nonetheless, AT's about 298 million tons in proved reserves at 0.32% to 0.36% copper yield for its Toledo mine alone could prove worthwhile to long-term investors, even at current copper prices. **Outperform.***

***Outperform** These are stocks whose share prices are going to outperform or beat the return of the Philippine Stock Exchange Index over a 12-month period.

Analyst Attributed Estimates

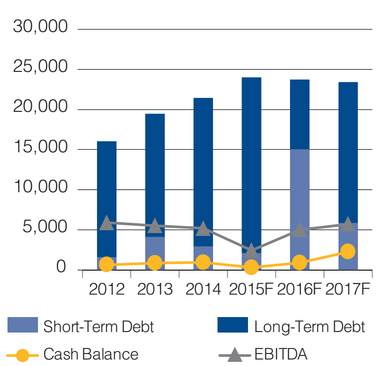
Internal	2015F	2016F	2017F
Net Inc. (Php Mn)	(585)	786	1,276
ROE %	-1.61%	2.16%	3.41%
EPS (Php)	-0.26	0.35	0.57
BV / Sh (Php)	15.98	16.33	16.89
Div / Sh (Php)	0.00	0.00	0.00
Div Yd %	0.00%	0.00%	0.00%
P/E (x)	-18.9	14.1	8.7
P/B (x)	0.3	0.3	0.3

Source: BDO Private Bank Research

Major Shareholders	% Stake
SM Investments Corp.	28.88
Alakor Corporation	21.75
Anglo Philippine Holdings Corp.	8.36
BDO Unibank, Inc.	6.28
Isidro A. Consunji	4.6
Martin C. Buckingham	1.06
Norges Bank Investment Management	0.89
Dimensional Fund Advisors	0.79
Alfredo Ramos	0.48
Primebridge Holdings, Inc.	0.45
Others	26.46
TOTAL	**100.00**

Source: Bloomberg

Debt Capacity Chart (Php millions)



We have downgraded our medium term rating for AT to BB- from BBB, assuming that there is no significant improvement in the industry's current situation. Otherwise, the score could still be upgraded. We also note that our rating system does not price in qualitative factors such as the support of strong equity investor groups.

CREDIT RESEARCH

Financial Highlights (Php millions)

	2012	2013	2014	2015F	2016F	2017F
Cash	654	866	951	304	896	2,267
Other Liquid Assets	7,598	4,745	3,287	3,093	3,341	3,446
Total Assets	57,953	63,205	65,915	67,362	68,236	69,427
Current Liabilities	4,646	8,078	8,123	6,371	19,740	10,749
Long Term Liabilities	17,839	18,276	21,394	24,958	11,677	20,583
Total Liabilities	22,486	26,354	29,516	31,329	31,417	31,332
Total Equity	35,467	36,852	36,399	36,033	36,819	38,094
Short-term Debt	1,585	4,143	2,960	2,122	15,049	5,874
Long-term Debt	14,473	15,349	18,472	21,912	8,680	17,552
Total Debt	16,059	19,492	21,432	24,033	23,729	23,426
Debt to Equity (%)	45.3%	52.9%	58.9%	66.7%	64.4%	61.5%
Net Debt to Equity (%)	43.4%	50.5%	56.3%	65.9%	62.0%	55.5%
Debt to Assets (%)	27.7%	30.8%	32.5%	35.7%	34.8%	33.7%
Net Interest Expense	1,003	830	1,383	1,224	1,323	1,191
EBITDA	5,923	5,540	5,210	2,470	5,019	5,733
EBITDA % Increase	419.2%	-6.5%	-6.0%	-52.6%	103.2%	14.2%

Sources: AT; F – BDO Private Bank Research

- **Lower spending in line with challenging environment...** Atlas Mining's capital expenditures (capex) of Php2.748 billion for 1H 2015 is lower than 1H 2014's Php4.3 billion, a prudent move considering the prevailing difficult environment for miners. Until the situation improves, we expect Atlas' capital spending to be subdued at around Php2 billion annually.

- **...but additional funds still needed for liquidity.** AT's interim 2015 financial statements showed additional net borrowings of Php2.875 billion, close to our full year estimate to help the company maintain liquid operations. With higher debt and lower retained earnings expected for 2015, AT's debt to equity ratio will rise to about 70% from under 60% in 2014 and 2013.

Our View and Recommendation:

Feeble prices mean tight cash situation. Weak metal prices translate to lower operating cash flows or EBITDA (earnings before interest, taxes, depreciation and amortization), averaging around Php4.6 billion annually. This can cover maintenance capex, but under a very tight cash scenario.

Refinancing likely for maturing debt. While AT's annual EBITDA flows look decent despite the odds, these are not enough to cover maturing debt of about Php15 billion in 2017. Thus, AT will have to refinance the debt or raise additional capital from equity sources to keep operations stable.

***BB (Lower Medium Grade)** Judged to have speculative elements. The issuer's capability to pay for such issues cannot be considered as well assured. Often, the protection of interest and principal payments may be very moderate and thereby not well safeguarded during both good and bad times over the future.

Nickel Asia Corporation (NAC)

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EQUITY RESEARCH

Company Background

Nickel Asia Corporation (NAC) is a holding company of various corporations that operate nickel mines in the Philippines. It is the largest nickel mining company in the country and is among the top lateritic nickel ore suppliers worldwide. It currently owns majority shares in four operating mines (Rio Tuba in Palawan, and Taganito, Cagdianao and Taganaan in Mindanao) and also has a 6% equity interest in the Coral Bay High Pressure Acid Leach (HPAL) facility at Rio Tuba and a 22.5% equity interest in the HPAL facility currently being built adjacent to the Taganito mine. In addition, it owns seven exploration properties, some of which are in the vicinity of its existing sites. The company has also expressed an interest to diversify to gold and copper mining, as evidenced by its recent acquisition of Cordillera Exploration Company Inc (CEXCI).

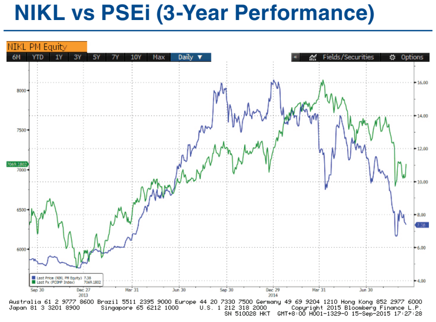
Share Data

PSEi Code	NIKL
Rating	**Outperform**
52-wk range (Php)	6.40-16.43
Current Price (Php)	7.38
12-month Target Price (Php)	9.60
Price Yield (%)	30.1
Dividend Yield (%)	7.7
Total Return (%)	37.8

Review of Share Price Performance

In our August 2014 issue of Money Talks, we expected NIKL to outperform the PSEi with a target price of Php15.11 per share (adjusted for a 50% stock dividend in January this year and another 100% in July). This view was supported by strong nickel prices in 2014 in contrast with other commodities (LME average of US$7.64 per pound for said period) and even stronger consensus price forecasts for 2015 and 2016 after Indonesia announced a ban on exports of nickel ore – though downside risks remained. A series of poor economic indicators from China, coupled with a stronger US dollar in 2015 finally weighed on nickel prices. After peaking at Php16.43 (adjusted) on Jan 14, 2015, NIKL's price is now down to Php7.38 per share. From our last report (Aug 20, 2014) to Sep 14, 2015, NIKL's price slid by 44%, much worse than the PSEi's 0.38% decline for the same period.

NIKL vs PSEi (3-Year Performance)



Source: Bloomberg

Equity Valuation

Comparative Valuation	Closing Price (Php)	Market Cap (Php bn)	2015 P/B (x)	2015 P/E (x)	2015 ROE (%)	Dividend Yield (%)	Free Float* (%)
SCC	137.50	142.46	5.40	16.34	36.60	2.91	27.31
NIKL	**7.38**	**56.83**	**1.76**	**10.39**	**19.06**	**5.92**	**19.16**
PX	4.97	25.15	1.00	19.88	5.16	1.01	32.99
AT	4.90	9.50	--	--	-0.89	4.90	42.27

*Sources: Bloomberg; * Philippine Stock Exchange*
Note: SCC – Semirara Mining Corp.; PX – Philex Mining Corp.; AT – Atlas Cons. Mining & Dev't Corp.

▶ **Consensus P/E multiple at only 10.4x.** Bloomberg consensus estimates show that NIKL has a P/E multiple of only 10.4x versus an ROE of 19.1%. While BDO PB's lower 2015 net income estimate resulted in a higher P/E (16.3x) and lower ROE (13.4%) compared with consensus figures, NIKL still has the lowest P/E and highest ROE (excluding SCC, whose power generation operations account for close to 70% of its bottomline) either way. Among listed productive miners, NIKL is also tops in terms of dividend yield.

▶ **Drop in nickel prices drag 1H revenues, income.** For 1H 2015, Nickel Asia's revenues slid by 15% y/y to Php7.971 billion as weaker nickel prices offset a 24% y/y growth in volume (refer to Operational Highlights table below). The Indonesian ore export ban more than doubled non-LME (London Metal Exchange) nickel prices in 2014, but the negative outlook for commodities in general finally caught up with nickel in 2015 as China's economic indicators continued to point to a slowdown, and the US dollar maintained its strength on rate hike expectations. Meanwhile, the company's net income declined at a faster pace (-46% y/y to Php2.174 billion) as: 1) increased production volume translated to higher operating costs (+23% y/y to Php5.221 billion); and 2) lower nickel prices likewise dragged net income of associates Coral Bay Nickel Corporation and Taganito HPAL Nickel Corporation to Php60.2 million (-85% y/y from Php400.1 million in 1H 2014).

Operational Highlights (Php millions)

	2013	2014	% chg	1H'14	1H'15	% chg
Nickel ore sold ('000 WMT)	16,542	21,791	32%	7,772	9,672	24%
LME ave. price (US$/lb)	6.91	7.60	10%	7.57	6.22	-18%
Non-LME (US$/WMT)	20.65	44.63	116%	41.52	23.10	-44%
Gross Revenue (Php M)	11,110	24,746	123%	9,338	7,971	-15%
Net Income	2,586	11,008	326%	4,032	2,174	-46%
Attributable Net Income	2,054	8,552	316%	2,714	1,490	-45%
Attr. NI Margin %	18.49	34.56		29.06	18.70	

Source: NIKL

Our View and Recommendation:

Short-term (less than 2 years): While base metal prices have so far remained weak, nickel supply and demand data from the World Bureau of Metal Statistics show a small net deficit as of June 2015. If this becomes a trend, nickel prices will likely recover in the next few months. Assuming that prices will indeed improve in 2016, we estimate NIKL's 12-month fair value at Php9.60 per share based on a weighted P/E metric of 16x and P/B ratio of 2.0x. This can give investors a potential price yield of 30.1%. We note that strong operating cashflows have allowed NIKL to pay out more than its dividend policy of up to 30% of previous year's attributable net income for the past 5 years, or an average dividend yield of 8.06%. Thus, long-term investors can still earn a decent yield from NIKL dividends even if metal prices stay weak. **Outperform.***

Medium-term (beyond 2 years): Given the present state of commodities prices, consensus forecasts for average nickel prices were downgraded to US$16,625 to US$18,000 per ton (approximately US$7.54 to US$8.16 per pound) for 2016 and 2017, respectively. With these price assumptions, we estimate NIKL's 2017 fair value at Php10.99 per share, for a price upside of 18.63%. Plus a possible dividend yield of 12.05%, total return may reach 30.68%. **Outperform.***

***Outperform** These are stocks whose share prices are going to outperform or beat the return of the Philippine Stock Exchange Index over a 12-month period.

Analyst Attributed Estimates

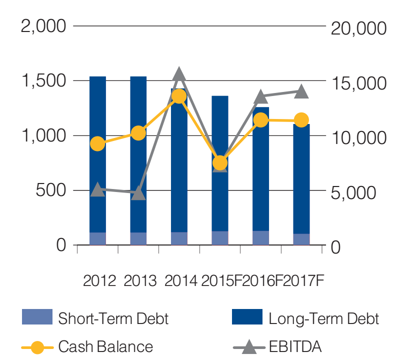
Internal	2015F	2016F	2017F
Net Inc. (Php'mn)	4,434	8,679	8,945
ROE %	13.40%	26.08%	25.16%
EPS	0.45	0.89	0.92
BV / Sh	3.19	3.63	3.66
Div / Sh	0.85	0.45	0.89
Div Yd %	11.47%	6.16%	12.05%
P/E (x)	16.29	8.32	8.07
P/B (x)	2.32	2.04	2.02

Source: BDO Private Bank Research

Major Shareholders	% Stake
Sumitomo Metal Mining Philippine Holdings Corporation	25.91
Mantra Resources Corporation	25.60
Ni Capital Corporation	13.38
Luis J. L. Virata	12.78
Pacific Metals Co. Ltd.	2.77
Teachers Advisors Inc.	0.37
Philequity Management, Inc.	0.35
Schroder Investment Mgmt Ltd.	0.30
Vanguard Group, Inc.	0.23
Eaton Vance Management	0.23
Others	18.08
Total	**100.00**

Source: Bloomberg

Debt Capacity Chart (Php millions)



We maintain our **A+** medium-term credit score for NIKL. This strong investment-grade rating is hinged on healthy cash flows from operations, minimal debt, comfortable debt maturity profile and fluid liquidity.

CREDIT RESEARCH

Financial Highlights (Php millions)

	2012	2013	2014	2015F	2016F	2017F
Cash	9,263	10,234	13,562	7,538	11,423	11,358
Receivables – net	938	839	1,431	1,316	1,981	2,052
Total Assets	27,179	28,914	35,184	32,736	38,213	40,395
Current Liabilities	1,276	1,309	2,115	1,737	2,185	2,296
Long Term Liabilities	2,322	2,393	2,167	2,075	1,883	1,711
Total Liabilities	3,598	3,702	4,282	3,812	4,068	4,007
Total Equity	23,582	25,212	30,902	28,924	34,145	36,388
Short-term Debt	117	117	118	128	131	106
Long-term Debt	1,423	1,421	1,313	1,233	1,129	1,000
Total Debt	1,539	1,539	1,432	1,361	1,260	1,106
Debt to Equity (%)	6.5%	6.1%	4.6%	4.7%	3.7%	3.0%
Net Debt to Equity (%)	-32.8%	-34.5%	-39.3%	-21.4%	-29.8%	-28.2%
Debt to Assets (%)	5.7%	5.3%	4.1%	4.2%	3.3%	2.7%
Net Interest Expense	(210)	(146)	(144)	(202)	(107)	(170)
EBITDA	5,131	4,810	15,673	7,336	13,600	14,078
EBITDA % Increase	-28.7%	-6.3%	225.9%	-53.2%	85.4%	3.5%

Sources: NIKL; F – BDO Private Bank Research

- **Still no major expansion plans.** With no major acquisitions or ongoing expansion, Nickel Asia Corporation's (NIKL) capital expenditures (capex) for 2014 slid further to Php1.56 billion from Php1.93 billion in 2013 and Php2.72 billion in 2012. We expect maintenance capex to range between Php1.5 to Php2.0 billion annually from 2015 to 2017. As of end-June 2015, NIKL has spent around Php950 million.

- **Strong net cash position.** Thanks to improved nickel prices in 2014, NIKL closed 2014 with a higher cash balance of Php13.562 billion versus 2013's Php10 billion, even after paying out over Php5.5 billion in dividends. Cash balance as of end-June 2015 slid to Php7.750 billion after the company bought additional AFS (available-for-sale) investments and gave common shareholders Php3.798 billion in dividends on the interim. With minimal debt in its books, NIKL is seen to maintain its strong net cash position through 2017.

- **Scaling down?** In early September, NIKL disclosed that subsidiary Hinatuan Mining Corp. (HMC) will scale down operations in Eastern Samar beginning Sep 15 after the Mines and Geosciences Bureau (MGB) Region 8 office refused to release the Mineral Ore Transport Permit (MOEP) for the removal of ore stockpile (from mining prior to suspension in early 2000s) on the island despite endorsements from the Office of the Presidential Assistant for Rehabilitation and Recovery and MGB Director Leo B. Jasareno. The scale-down will result in the laying-off of 200 employees, who are residents of Manicani Island. This should have minimal impact on NIKL as HMC's current mining activities are in Surigao del Norte.

Our View and Recommendation:

Low production costs support profitability and liquidity. Relatively low production costs enable NIKL to continue to operate profitably during times of unfavorably low metal prices. Thus, despite an expected drop in 2015 projected EBITDA (earnings before interest, depreciation and amortization or operating cash flows) to Php7.3 billion, the amount is still healthy – enough to fundworking capital needs, capex, taxes, debt service and dividend payments.

Diversification, expansion options. Strong cash flows from current operations will help NIKL pursue expansion and diversification into other metals (e.g., gold and copper) in the future. A solid balance sheet will also allow the company to easily tap the debt market for additional capital should the need arise.

***A (Upper Medium Grade)** With favorable investment attributes and are considered upper-medium grade obligations. Factors giving security to principal and interest are considered adequate but elements may be present which suggest a susceptibility to impairment sometime in the future.

Philex Mining Corporation (PX)

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EQUITY RESEARCH

Company Background

Philex Mining Corporation (PX) and its subsidiaries are organized into 2 main business groupings: the metals business directly under PX, Philex Gold Philippines, Inc. (PGP), and Silangan Mindanao Mining Co., Inc. (SMM) and the energy and hydrocarbon business under Philex Petroleum Corporation (PXP).

PX was incorporated in the Philippines in 1955 and has been listed on the Philippine Stock Exchange since November 23, 1956. PX is primarily engaged in large-scale exploration, development and utilization of mineral resources.

PXP on the other hand, a 64.78%-owned subsidiary of PX, is a Philippine corporation organized in December 2007 and is also listed on the Philippine Stock Exchange. It has interests in various petroleum service contracts in the Philippines and Peru held directly and through its subsidiaries, Pitkin Petroleum Plc ("Pitkin", where it holds a 53.07% stake), and Forum Energy Plc ("FEP", where it holds a 60.49% stake).

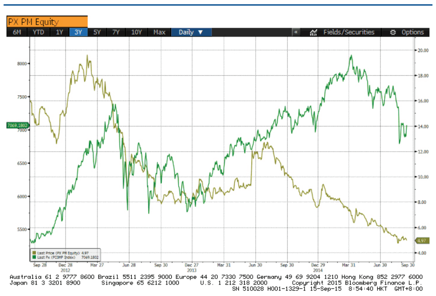
Share Data

PSEi Code	PX
Rating	**Neutral**
52-wk range (Php)	4.64-10.94
Current Price (Php)	4.97
Target Price (Php)	5.48
Price Upside (%)	10.2%
Dividend Yield (%)	0.7%
Total Return (%)	11.0%

Review of Share Price Performance

PX has slumped 45% from its peak level of Php11 last September, when the miner was allowed to resume normal operations upon satisfaction of rehabilitation works and settlement of penalties imposed by the government for the tailings spill accident in 2012. Since then, the miner's stock went downhill, dragged by sliding commodity prices, as investors agonize over China's weakening economy and demand.

PX vs PSEi (3-Year Performance)



Source: Bloomberg

Equity Valuation

Comparative Valuation	Price (Php)	Market Cap (Php bn)	2015 P/B (x)	2015 P/E (x)	2015 ROE (%)	Dividend Yield (%)	Free Float* (%)
SCC	137.50	142.46	5.40	16.34	36.60	2.91	27.31
NIKL	7.38	56.83	1.76	10.39	19.06	5.92	19.16
PX	**4.97**	**25.15**	**1.00**	**19.88**	**5.16**	**1.01**	**32.99**
AT	4.90	9.50	--	--	-0.89	4.90	42.27

*Sources: Bloomberg; * Philippine Stock Exchange*
Note: SCC – Semirara Mining Corp.; PX – Philex Mining Corp.; AT – Atlas Cons. Mining & Dev't Corp.

▶ **Expensive mining stock relative to earnings...** PX is presently trading at book value, but with relatively high P/E of 20x compared to peers since its denominator earnings were hit by declining gold and copper prices. As such, the company's valuation multiples would only improve if and when the demand and supply dynamics for commodities get better. This however, is largely dependent on data coming out of China. Meanwhile, PX will probably post flat earnings of about Php1 billion in the near term, while it carries on with the Silangan mine development.

▶ **...amid prospects for Silangan mine.** The Silangan project has estimated reserves of 5 billion pounds of copper and 9 million ounces of gold in its 25-year mine life, which is worth US$26.7 billion (or Php1.2 trillion) even with today's subdued metal prices. Assuming a 10% income margin, then the prospective mine has a potential to generate an annual income of Php4.8 billion, which is higher than the Php3.9 billion average annual income of PX for the years 2006-2011, prior to Padcal's tailings leak accident in 2012. As such, its EPS could also improve to Php0.70 by 2018 even with an assumed 36% dilution in outstanding shares to 6.74 billion taking into account a likely share offering next year. Modest multiple assumptions of 10x-15x P/E would then value PX at Php7.0-10.50 per share, if the estimated reserves of Silangan are monetized.

Operational Highlights (Php millions)

	2013	2014	% chg	1H'14	1H'15	% chg
Gold prod'n ('ozs)	99,802	105,008	5%	52,286	53,689	3%
Copper prod'n ('000 lbs)	32,495	35,391	9%	18,197	16,891	-7%
Gold prices (US$/oz)	1,297	1,270	-2%	1,341	1,190	-11%
Copper prices (US$/lb)	3.3	3.0	-9%	3.1	2.6	-16%
Gross Revenue	10,462	10,898	4%	5,782	4,886	-15%
Core Net Income	1,081	1,122	4%	559	520	-7%
Net Income	312	703	125%	600	565	-6%
Core Net Income %	10.3%	10.3%		9.7%	10.6%	

Source: PX

Our View and Recommendation:

Short-term (less than 2 years): PX has fallen near its 12-month low, tracking the movement of gold and copper prices. The miner's stock is now down to its book value amid continuing weak metal prices and uncertain recovery given slowing economic growth for China and its consequence to emerging markets. Using adjusted valuation multiples of 15x P/E and 1.5x P/B, PX has a target price of Php5.48 in the next 12 months, for a potential price upside of 10.2%. As such, the miner will probably track the local index, as investors focus on recurrent earnings out of Padcal's operations. **Neutral.***

Medium-term (beyond 2 years): Over the next 2 years however, PX will probably just hover at the Php5.5-5.6 levels on flat income prospects of around Php1.1 billion until it commences operations for Silangan sometime in 2018. **Underperform.****

***Neutral** These are stocks whose share prices are going to move in tandem or within the PSEi movement as a benchmark over a 12-month period.
****Underperform** These are stocks whose share prices are going to underperform or lag the return of the PSEi as a benchmark over a 12-month period.

Analyst Attributed Estimates

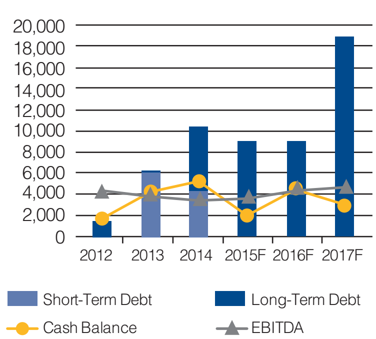
Internal	2015F	2016F	2017F
Net Inc. (Php'mn)	1,025	1,153	1,137
ROE %	4.3%	3.7%	2.9%
Div / Sh	0.04	0.04	0.04
Div Yd %	0.7%	0.7%	0.8%
BV / Sh	4.97	5.68	5.81
EPS	0.21	0.17	0.17
P/B (x)	1.00	0.87	0.86
P/E (x)	23.95	29.05	29.45

Source: BDO Private Bank Research

Major Shareholders	% of total
Asia Link BV	20.71
Social Security System	20.59
Two Rivers Pacific Holding	14.96
First Pacific Company Ltd	10.51
Norges Bank Investment	2.52
Vanguard Group Inc	0.27
Eaton Vance Management	0.24
Pangilinan Manuel Velez	0.09
Tortorici Edward Anthony	0.07
State Street Corp	0.06
Others	29.98
Total	**100.00**

Source: Bloomberg

Debt Capacity Chart (Php millions)



Overall, PX maintained its medium-grade BBB- rating. Credit is supported by its prudent capital structure and adequate operational liquidity. However, the mining sector continues to face declining metal prices amid China's slowing economy, and the uncertain outcome of an ongoing regulatory review on taxation. Developments on these factors could hurt the miner's profitability in the interim. PX has been operating at EBITDA margins of 33%-34% at present, much lower than the 54%-56% levels when metal prices were at their peak during the years 2011-2012. Meanwhile, execution risks could also deter or delay its Silangan project.

CREDIT RESEARCH

Financial Highlights (Php millions)

	2012	2013	2014	2015F	2016F	2017F
Cash	1,670	4,081	5,232	1,887	4,365	3,014
Receivables - net	208	295	1,056	1,015	1,115	1,174
Total Assets	29,272	39,921	44,640	45,340	59,930	70,871
Current Liabilities	4,618	9,775	7,523	2,921	3,093	3,249
Long Term Liabilities	2,563	4,228	10,076	14,442	15,099	25,019
Total Liabilities	7,181	14,003	17,599	17,363	18,192	28,267
Total Equity	22,091	25,917	27,042	27,978	41,739	42,603
Short-term Debt	1,450	6,176	4,308	0	0	0
Long-term Debt	0	55	5,947	8,947	8,947	18,947
Total Debt	1,450	6,231	10,255	8,947	8,947	18,947
Debt to Equity (%)	7%	24%	38%	32%	21%	44%
Net Debt to Equity (%)	-1%	8%	19%	25%	11%	37%
Debt to Assets (%)	5%	16%	23%	20%	15%	27%
Net Interest Expense	(14)	390	338	204	205	461
EBITDA	4,207	3,770	3,324	3,625	4,270	4,660
EBITDA % Increase	-52%	-10%	-12%	9%	18%	9%

Source: PX; F – BDO Private Bank Research

- **Conservative capital structure...** PX has a low leverage capital structure with a conservative debt-to-equity ratio of 38% as of end 2014 given its sizeable equity base of Php27 billion. As such, the miner has ample capacity to tap new borrowings to pursue its Silangan mine development and other exploration projects.

- **...support resource development.** Silangan's definitive feasibility study will be completed this year and will be the basis for its financing plan. The new gold and copper mine is estimated to require US$1.2 billion (or Php56 billion) in developmental funding, and PX has so far spent more than Php13 billion as of end 2014. Overall, the company intends to fund 70% of the Silangan project through debt with the balance via equity, and is open to strategic partnerships to help secure capital.

Our View and Recommendation:

Existing mine sustains operational liquidity... Given additional ore reserves that extended Padcal's mine life and improved efficiencies, PX is projected to produce decent operating cash flows or EBITDA of Php3.6 billion to Php4.7 billion despite the current weakness in metal prices. As such, the miner is able to pay off some debt, with its total borrowings down to Php9.7 billion as of June 2015.

...while new mine development prepares funding plan. Moving forward, PX intends to "improve liquidity and strengthen capital base" as it is in the process of evaluating potential partners and assessing market conditions for Silangan's fund raising.

***BBB (Medium Grade)** Neither highly protected nor poorly secured. Interest payments and principal security appear adequate for the present but certain protective elements may be lacking or may be characteristically unreliable over any great length of time. Such issues lack outstanding investment characteristics and in fact have speculative characteristics as well.

Semirara Mining & Power Corp (SCC)

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Company Background

Semirara Mining and Power Corporation (SCC) was incorporated on February 26, 1980 and initially engaged in the exploration, development and mining of coal resources in Semirara Island in Caluya, Antique. It is a majority-owned subsidiary of publicly-listed DMCI Holdings, Inc. (DMC), its parent company.

On August 18, 2014 the company changed their name from Semirara Mining Corporation to reflect their forward integration to power generation from just being purely a coal producer and supplier.

It is the only large-scale coal producer in the Philippines, with an estimated maximum annual coal production of 7.5 Million metric tons (MT) and coal reserve of about 150 Million MTs. It is engaged in surface open-cut mining of thermal coal in its mine site as well as production and sale of sub-bituminous coal. It serves the power generation sector, cement and other industries, and also exports coal products.

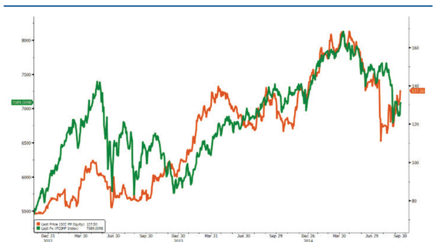
Share Data

PSEi Code	SCC
Rating	**Underperform**
52-wk range (Php)	110.80 – 169.60
Current Price (Php)	137.50
Target Price (Php)	144.19
Price Upside (%)	4.9
Dividend Yield (%)	2.9
Total Return (%)	7.8

Review of Share Price Performance

From our Nov 7, 2014 report (not published in Money Talks), SCC's stock price has surged 41.3% to a peak of Php169.60 on April 7, 2015 as it was perceived to benefit from the foreseen power supply shortage during the summer months. Its uptrend reversed beginning April, dragged by general market concerns on high equity valuations. The stock hit a 52-week low of Php110.80 (-34.0% from the high) on July 22, 2015 after the Department of Energy (DOE) issued a suspension order on SCC's coal mining operations when the north portion of the Panian coal mine, due to heavy monsoon rains, collapsed causing a landslide and burying ten (10) people. The price has since recovered to Php137.50 as of Sep 14, 2015 after the Department of Environment and Natural Resources (DENR) lifted the suspension on their Environmental Compliance Certificate (ECC). DOE has also recently completed its investigation on the mining incident expressing willingness to lift SCC's suspension order once they comply with their recommended preventive measures.

Price Performance SCC vs PSEi



Source: Bloomberg

EQUITY RESEARCH

Equity Valuation

Comparative Valuation	Price (Php)	Market Cap (Php bn)	2015 P/B (x)	2015 P/E (x)	2015 ROE (%)	Dividend Yield (%)	Free Float* (%)
SCC	**137.50**	**142.46**	**5.40**	**16.34**	**36.60**	**2.91**	**27.31**
NIKL	7.38	56.83	1.76	10.39	19.06	5.92	19.16
PX	4.97	25.15	1.00	19.88	5.16	1.01	32.99
AT	4.90	9.50	--	--	-0.89	4.90	42.27

*Sources: Bloomberg; *Philippine Stock Exchange*
Notes: NIKL – Nickel Asia Corporation; PX –Philex Mining Corporation; AT – Atlas Cons. Mining and Dev't Corporation

- **Modest consensus P/E with highest ROE.** Despite having the highest P/B at 5.4x, SCC's P/E is middling at 16.3x and exhibits the highest ROE at 37.4%, almost twice NIKL's and more than 7x PX's. The disproportionate P/B and ROE is because of SCC's utilization of more debt capital with higher D/E ratio of 85.5% versus its peers (AT – 58.9%; PX – 37.9%; NIKL – 4.3%). Although its consensus dividend yield pales in comparison with AT's (4.9%) and NIKL's (5.9%), it's still decent at 2.9% and better than PX's 1.0%. SCC's significantly higher ROE is due to its growing power business, which gives better margins compared to its mining segment.

- **New power plants to help achieve 2015 profit target.** SCC's 1H 2015 net income grew 78% y/y to Php4.7 billion driven by power revenues that surged 46% to Php7.2 billion with Calaca Units 1 & 2 improving collective average capacity by 29% to 551 MW and capacity factor of 83% from just 34% in 1H 2014. The new power plants (Units 3 & 4) with combined capacity of 300 MW is expected to contribute Php1 billion to net income during 2H 2015 and help SCC achieve its full year profit target of Php9 to Php10 billion.

Our View and Recommendation:

Short-term (less than 2 years): Assuming valuation multiples of 15.0x P/E and 4.5x P/B, we expect SCC's share price to reach Php144.19 over the next 12 months, providing a price upside of 4.9%. The price surge is expected to be limited given the possible lag time before SCC is able to comply with regulatory requirements to resume mining operations in Panian. In the event that coal stock piles run out, SCC could incur additional costs to import coal from Indonesia. Meanwhile, the company is channeling some equipment to a new mining site (Narra) as they expect Panian to exhaust its mine life by mid-2016. The transition could post a challenge to SCC given that it has to dig deeper into the new mine before the needed coal is extracted. **Underperform.***

Medium-term (beyond 2 years): The projected annual EPS growth of 18.7% through 2018 can be achieved if the rehabilitated plants (Units 1 & 2) and new plants (Units 3 & 4) reliably maintain their capacities. On the basis of their expanding power portfolio, SCC's share price could reach Php201.73 by 2018 giving an annualized total return of 15.4% inclusive of the possible 2.9% dividend yield. **Outperform.****

***Underperform** These are stocks whose share prices are going to underperform or lag the return of the PSEi as a benchmark over a 12-month period.
****Outperform** These are stocks whose share prices are going to outperform or beat the return of the Philippine Stock Exchange Index over a 12-month period.

Analyst Attributed Estimates

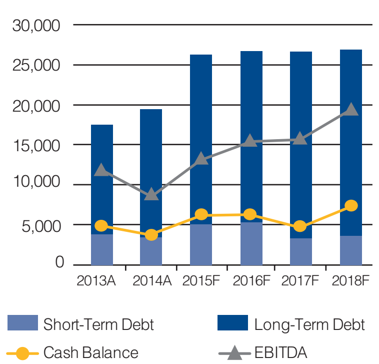
Internal	2015F	2016F	2017F
Net Inc.(Php Mn)	9,452	11,058	10,699
ROE (%)	37.4%	35.4%	28.2%
Div / Sh (%)	4.00	4.00	4.00
Div Yd (%)	2.91%	2.91%	2.91%
BV / Sh	26.09	32.44	38.45
EPS	8.84	10.35	10.01
P/B (x)	15.55	13.29	13.74
P/E (x)	5.27	4.24	3.58

Source: BDO Private Bank Research

Major Shareholders	% Stake
DMCI Holdings Inc	56.3
PCD Nominee (Filipino)	12.6
Dacon Corporation	12.2
PCD Nominee (Foreign)	12.2
National Development Company	3.2
DFC Holdings	1.9
Others	1.6
Total	**100.0**

Source: PSE

Debt Capacity Chart (Php millions)



Overall, from **BB** last November 7, 2014, we have upgraded SCC's credit score to a medium investment grade credit rating of BBB-

FIXED INCOME RESEARCH

Financial Highlights (Php millions)

	2013	2014	2015F	2016F	2017F	2018F
Cash	4,819	3,683	6,195	6,253	4,810	7,310
Receivables – net	4,032	4,128	4,727	5,231	5,178	6,466
Total Assets	44,727	51,901	64,277	72,170	78,550	90,022
Current Liabilities	9,991	12,138	14,630	15,241	13,272	15,355
Long Term Liabilities	14,609	17,057	21,764	22,263	24,188	24,236
Total Liabilities	24,600	29,195	36,394	37,503	37,460	39,591
Total Equity	20,128	22,706	27,883	34,666	41,089	50,431
Short-term Debt	3,806	3,333	5,174	5,198	3,261	3,503
Long-term Debt	13,657	16,089	21,088	21,523	23,415	23,415
Total Debt	17,464	19,421	26,262	26,721	26,676	26,918
Debt to Equity (%)	86.8%	85.5%	94.2%	77.1%	64.9%	53.4%
Net Debt to Equity (%)	62.8%	69.3%	72.0%	59.0%	53.2%	38.9%
Debt to Assets (%)	39.0%	37.4%	40.9%	37.0%	34.0%	29.9%
Net Interest Expense	354	282	863	947	956	846
EBITDA	11,658	8,574	13,206	15,499	15,639	19,290
EBITDA % Increase	20.4%	-26.4%	54.0%	17.4%	0.9%	23.3%

Sources: SCC; F – BDO Private Bank Research

- **Completion of Phase 1 expansion...** SCC has just completed the Phase 1 expansion of the Calaca energy project last end-June 2015 involving 2 x 150 MW coal-fired power plants costing US$450 million (Php20 billion) over the last two (2) years (since 2013). In the next 2 years, we still see capital expenditures (capex) to average Php10 billion as SCC proceeds with its phase 2 expansion.
- **...and onwards to Phase 2.** SCC has signed a joint venture (JV) agreement with an undisclosed local partner to build Unit 5 with 350 MW capacity and estimated cost of Php22 billion. The decision to collaborate with a business partner was a strategic move to accelerate plant construction which will increase total power portfolio to 1,250 MW in the next 3 – 4 years or by 2018 at the earliest. Over time, SCC's goal is to add 700 MW (2 x 350 MW) and reach gross installed capacity of 1,600 MW.

Our View and Recommendation:

Extra capacity to boost EBITDA. Additional earnings from Phase 1's commercial operation is projected to propel EBITDA higher by 54% to Php13.2 billion this 2015, more than the estimated business spending of Php11.0 billion. Although D/E ratio will rise to 94.2% this 2015, it will significantly decline to 77.1% in 2016 as full year earnings contribution of Units 3 and 4 is realized. This will translate to higher retained earnings and a wider equity base.

Earnings from power business to trim D/E. Over the medium-term, net income is projected to grow at an annualized rate of 18.7%, building up retained earnings and causing D/E to fall further to 53.4% by 2018 when Unit 5 is expected to be commissioned. By then, power is expected to replace coal mining as the main revenue driver, increasing its topline contribution to 63% in 2018 from just 43% in 2014. This gives SCC a more reliable revenue source as energy demand increases over time in line with demographics. With operating cash flows increasing at an annualized pace of 22.5% through 2018, it is expected to more than double to Php19.3 billion by 2018 from just Php8.6 billion in 2014. As such, internally generated funds can cover about 3.0x SCC's annual obligation on interest expense and dividend payments. The excess can be redirected to support capex requirements effectively reducing borrowing needs.

***BBB (Medium Grade)** Neither highly protected nor poorly secured. Interest payments and principal security appear adequate for the present but certain protective elements may be lacking or may be characteristically unreliable over any great length of time. Such issues lack outstanding investment characteristics and in fact have speculative characteristics as well.

Of mining and taxes

By Roxanne S.C. Olanday

Nothing is certain but death and taxes. However, in the case of the mining industry in the Philippines, uncertainty looms over the current tax policy and the proposed new revenue sharing scheme, sparking much debate in the past few years.

Under the Philippine Mining Act of 1995 (Republic Act 7942), discussions on the tax scheme focus on the Mineral Production Sharing Agreement (MPSA), typically awarded to local companies (with at least 60% local ownership) and the Financial Technical Assistance Agreement (FTAA) for foreign firms (with up to 100% foreign ownership). In the present policy, the government gets 2% excise tax on the actual market value of mining output, under MPSAs, and 50% of the profits of foreign contractors under FTAAs. While a 2% excise tax does not seem menacing, note that on top of this, under the National Internal Revenue code and other laws, miners must still pay a long list of taxes, duties and fees.

Though miners are required to surrender a hefty sum of their earnings via all these taxes and fees, this is purportedly not the main intention of the law. It is claimed to be toward sustainable development of the industry through focusing on environmental protection, social equity and mineral resource management. In fact, mining contractors are provided with some fiscal and non-fiscal incentives covering things like pollution control devises, income tax carry forward of losses, income tax accelerated depreciation of fixed assets, and investment guarantees (i.e. repatriation, earnings remittance, freedom from expropriation and requisition of investment, and confidentiality of information). FTAA contractors may also avail of an additional tax holiday incentive on national taxes within five years of the start of commercial operation, and even prior, during construction and development period.

Proposed new tax schemes

In spite of these however, proposals have been made to revise the existing revenue and tax scheme. The three proposals are as follows: a) House Bill 5367 (HB 5367), filed by the inter-agency Mining Industry Coordinating Council (MICC), in which the government as primary “owner of the minerals” is annually entitled to either 10% of the mining firm’s gross revenues, or 55% of adjusted net mining revenues, whichever is higher, and 60% of any windfall profit. Still, other levies and taxes such as corporate income tax, royalties to indigenous communities and capital gains, among many others, remain; b) House Bill 3586 (HB 3586), drafted by the 1-BAP party-list Rep. Silvestre H. Bello III and Taguig City Rep. Lino S. Cayetano (2nd District), which seeks to require mining contractors to give up 60% of its revenues to the national government and 15% to the “hosting” local government; and c) House Bill 5843 (HB 5843) by Deputy Speaker and Nueva Vizcaya Rep. Carlos M. Padilla levies a 5% royalty on mining, 10% cash flow surcharge and 5% ore export tax, aside from national and local taxes.

A recent hearing at the House of Representatives aired the Department of Finance’s simulation of the prevailing policy and the three measures, and revealed that the MICC proposal was the most favorable to the national government, yielding the biggest revenue-share among them. In terms of average effective tax rate (AETR), the current MPSA regime gives 47%; FTAA, 62%; HB 5367 (MCC proposal), 71%; HB 5843, 63%; and HB 3586 50%. However, using the internationally accepted AETR, the 60+% AETR of FTAAs is not considered ‘internationally competitive’ given that even top mining countries like Australia and the United States only submit an AETR between 40% to 45% to their governments. In summary, the proposed measures were largely opposed, with the MICC proposal receiving the most flak. So to raise money in taxes, business groups stressed the need to be competitive to attract investors to increase the base for taxes. However, at present, the Philippines’ foreign direct investment (FDI) is in the lower bracket compared to its ASEAN peers, raking in only US$6.2 billion in 2014, far behind Singapore who lead the bunch at US$72billion, Indonesia, Thailand, Malaysia and even Vietnam. Moreover, when looking at the contribution of FDI to the economy, the Philippines only made 1.4% in 2013, the lowest among all ASEAN member states.

Tax regimes in other countries

Unlike the Philippines, China does not have a specific tax scheme for mining, treating the industry as simply part of the general manufacturing industry. Miners however can avail of a reduced corporate income tax of 15%, from the standard 25% rate, for operations in western regions within the period of 2011 to 2020, especially if these activities meet certain categories, reliant on the regions involved. Additionally, there are specific taxes for the industry: the Resource Tax, based on the tonnage or volume, Compensation Fees for Mineral Resource at 0.5% to 4% on sales revenue of mineral exploitation-recycle ratio, and Royalty Fees of Exploration Right & Exploitation Right, based on the mining area. Incentives are available for foreign investors exploiting and exploring the Western China area. Mining contractors also need to pay a 17% VAT and local surcharge.

In the case of Australia, it similarly has taxes and royalty fees like China and the Philippines. However, as the mining industry has consistently been a large contributor to the lone landmass’ economy and has been known for its mineral resources, especially coal, iron ore, mineral sands, copper, gold and uranium, its mining taxes are more ironed out. The Asia-Pacific country requires mining contractors to pay the Australian State or Territory governments income tax mining royalties whose rates (either a set amount or fixed percentage of the volume of minerals extracted or the realized value of the mined minerals) depending on the commodity and location where the mineral was mined. Aside from this, specific to the industry, there is a “Mineral Resource Rent Tax” (MRRT) levied on iron ore and coal projects (i.e. 20% on the net value of the mine output in the Northern Territory). The paid MRRT is deductible for income tax purposes (note that corporate income tax is a flat rate of 30%). Additionally, there are license fees and community initiatives tax.

Similar to the reduced corporate income tax in China, mining tax payers in the United States of America usually are Alternative Minimum Tax payers due to regular deductions applied like percentage depletion. Still, there are exceptions to income tax such as in the state of Nevada where gaming and mining are huge businesses; in its place is the Nevada Net Proceeds Tax. However, the United States, in contrast to most developed countries, imposes taxes on its citizens and businesses on worldwide income. This generates tax profits on income earned in the United States and on foreign profits when repatriated. Unlike the Philippines, China or Australia however, the US government does not require a payment of mining royalties. Instead, there are severance taxes and for some states, a requirement for mines to bid at fair market value for access to certain minerals, both of which behave similar to royalties. The other applicable royalty is Federal Land Royalty that is based on the value at extraction for coal mining (12.5% for surface mining and 8% for underground mining), or a 2.5% to 5% royalty for mining of hard rock minerals.

In the case of Russia, mining operations are typically taxed under a general tax regime that includes the corporate income tax of 20% (2% paid to the federal budget and 13.5% to 18% to the constituent regions), mineral extraction tax (MRET) and other payments of VAT, payroll contributions, property and land taxes. The MRET in particular uses the value of the extracted mineral resource, established as a fixed amount per tonne, save for coal, as its tax base. Like the Philippines, Russia has incentives or certain benefits like a decreased tax burden for underground development of ferrous ores and reduced MRET for investors in Far East. In Russia, however, depreciation or amortization for taxing purposes does not apply to mineral resources.

And lastly, in South Africa, as with the United States, residents are taxed based on their worldwide income. Non-residents of South Africa are charged taxes on their income received or accrued to them from a South African source or deemed South African source. This may be subject to a tax treaty relief. Only gold mining companies are not charged a corporate tax rate of 28%, as there is a special taxation formula linked to profits. Furthermore, it was only in 2010 when South Africa applied mining royalties via the Mineral and Petroleum Resources Royalty Ace (MPRRA), a royalty percentage based on value rather than volume, specially based on whether the mineral is refined or unrefined.

Taking these into consideration, the Philippines should review and compare its other mining policies to other countries, within the region and worldwide, and assess which policies best fit our mining situation in the country and yet remain competitive against other global players. After all, a better tax regime could attract more foreign investors and help boost the very promising Philippine mining industry beyond its 1% contribution to the economy. Furthermore, the development of the local mining sector would benefit our economy if this is complemented with the re-emergence of basic industries to support and strengthen our manufacturing sector in the future.