EDC, FGEN, FPH:
Market overreacts to Bacman failure, upgrade to BUY

We lowered our 2013E and 2014E earnings forecast for EDC by 14.3% and 6.1%, respectively, to Php8.3Bil and Php9.1Bil, after we reduced our revenue contribution estimates for the Bacman due to the disruption in the operations of the plant and damages sustained by unit 2. We reduced our FV estimate on EDC by 6% to Php8.0/sh, but upgraded our rating from HOLD to BUY given that we believe the recent decline in share price almost reflects the worst case scenario for the Bacman already.

EDC – Share price almost reflects worst case scenario for Bacman

Since announcing that the Bacman's operation would be halted again last March 1, EDC's share price dropped by a total of 15.3% to only Php6.37/sh . While EDC's profitability would be negatively affected by this development, we think the market over reacted due to the following reasons:

- The Bacman geothermal plant is comprised of three units, with two 55MW units (unit 1 and 2) plus a smaller 20MW unit 3. Although both 55MW units were shut down, only unit 2 was damaged. Unit 1 was shut down only as a precautionary measure. After the favorable outcome of tests by third party engineers, EDC plans to resume operating unit 1 later this month. Although the unit will operate at a de-rated basis for at least a year, the amount of foregone revenues is only Php830Mil in 2013 and Php380Mil in 2014. This is equivalent to only 2.8% and 1.2% of our revenue forecast for the two years respectively.

- As far as unit 2 is concerned, it is still uncertain when the damaged turbine will be replaced. However, EDC has an insurance claim for business interruption with a maximum coverage of Php2.3 Bil applicable after the first 45 days of unit 2's shutdown. Based on our estimates, the insurance claim is enough to offset 14 months of foregone revenues resulting from the non-operation of unit 2.

Forecast Summary (PhpMil)

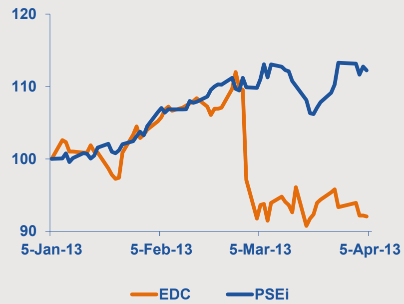
Year to Dec. 31	2010	2011	2012	2013E	2014E
Sales	**24,902**	**25,263**	**28,369**	**29,292**	**31,434**
% change y/y	*12.8*	*1.5*	*12.3*	*3.3*	*7.3*
EBIT	**10,243**	**9,218**	**13,462**	**12,620**	**14,001**
% change y/y	*9.3*	*-10.0*	*46.0*	*-6.3*	*10.9*
EBIT Margin (%)	*41.1*	*36.5*	*47.5*	*43.1*	*44.5*
EBITDA	**13,688**	**12,660**	**17,022**	**16,332**	**17,909**
% change y/y	*29.3*	*-7.5*	*34.5*	*-4.1*	*9.7*
EBITDA Margin (%)	*55.0*	*50.1*	*60.0*	*55.8*	*57.0*
Net Profits	**4,116**	**-166**	**8,659**	**8,341**	**9,095**
% change y/y	*24.3*	*N/A*	*N/A*	*-3.7*	*9.0*
NPM (%)	*16.5*	*-0.7*	*30.5*	*28.5*	*28.9*
EPS (cents)	**0.22**	**-0.01**	**0.46**	**0.44**	**0.49**
% change y/y	*24.34*	*N/A*	*N/A*	*-3.68*	*9.05*
RELATIVE VALUE					
P/E(X)	28.8	-711.7	13.7	14.2	13.0
P/BV(X)	3.7	4.0	3.3	2.8	2.4
ROE(%)	*12.8*	*-0.6*	*24.4*	*20.0*	*18.6*
BVPS(P)	1.7	1.6	1.9	2.2	2.6
Dividend yield(%)	*1.9*	*1.6*	*1.2*	*2.2*	*0.0*

**Source: COL estimates*

SHARE DATA

Rating	**BUY**
Ticker	EDC
Fair Value (Php)	8.00
Current Price	6.30
Upside (%)	34.92

SHARE PRICE MOVEMENT



ABSOLUTE PERFORMANCE

	1M	3M	YTD
EDC	-2.78	-8.30	-6.67
PSEi	0.20	12.62	15.70

MARKET DATA

Market Cap	118,125.00Mil
Outstanding Shares	18,750.00Mil
52 Wk Range	5.55 - 7.90
3Mo Ave Daily T/O	219.89Mil

GEORGE CHING
george.ching@colfinancial.com

- Assuming that Bacman will operate at a de-rated capacity for one year beginning 2Q13 for uni1 and 4Q13 for unit 2, and that the long term load factor of the Bacman drops from our original assumption of 80% to 70%, our net income forecast for EDC would drop by only 14.3% to Php8.3 Bil for 2013 and 6.1% to Php9.1 Bil for 2014. Meanwhile, our fair value estimate for EDC would drop by only 6.0% to Php8.00/sh, much less than the 15.3% decline registered by the share price.

- Assuming the worst case scenario where the Bacman plants would be totally scrapped, EDC's fair value would drop to Php6.03/sh, almost at par with its current price. However, we believe that this scenario would be highly unlikely. Management already said that if the rehabilitation fails, it could just replace the turbines of the Bacman plants to improve their reliability over the long-term.

FGEN & FPH – Savings on interest expense to offset negative impact of Bacman shutdown on profitability

Both FPH and FGEN will also be negatively affected by the Bacman shutdown. Recall that FGEN owns 49.5% of EDC, while FPH indirectly owns 33% of EDC through its 66% stake in FGEN. Following the news that Bacman's operations would be halted again, FGEN's share price fell by a total of 7% to Php24.45/sh, while FPH's share price dropped by 5.1% to Php109.7/sh. However, the negative impact of Bacman's shutdown on profitability will be more than offset by the savings that both will incur from paying lower interest expenses starting this year.

Late last year, FGEN refinanced ~ US$400Mil worth of long term debt to take advantage of lower interest rates. As a result, interest expense is expected to drop by 24% from US$91 Mil in 2012 to US$29 Mil in 2013. Meanwhile, FPH also reduced its debts at the parent company level last year given its highly liquid position. Coupled with the drop in FGEN's interest expense, FPH's consolidated interest expense is expected to drop by 11.4% from Php3.9in 2012 to Php3.5Bil in 2013.

As a result, despite the negative impact of Bacman's shutdown, our net income forecast for FGEN still increased by 0.8% to US$119 Mil in 2013 and by 8.0% to US$123 Mil for 2014. Our net income forecast for FPH also increased by 2.0% to Php2.3 Bil in 2013 and by 6.3% to Php2.3 Bil for 2014.

Exhibit 1: Summary of changes in forecast

		2013E			2014E	
in PhpMil	**Old**	**New**	**% change**	**Old**	**New**	**% change**
Net profit forecast						
EDC	9,738	8,341	*-14.3*	9,689	9,095	*-6.1*
FGEN (in US$Mil)	118	119	*0.8*	113.80	123	*8.0*
FPH	2,222	2,266	*2.0*	2,171	2,307	*6.3*

Source: COL estimates

Upgrading EDC and FGEN to BUY, maintain BUY rating on FPH

Given the larger than warranted drop in EDC and FGEN's share price, we are upgrading our rating on both stocks to BUY from HOLD. Meanwhile, we are maintaining our BUY rating on FPH.

As discussed earlier, assuming the highly unlikely scenario where the Bacman plants would be fully written off, our fair value estimate of EDC would drop to Php6.03/sh, implying a possible downside of only 6% based on its current price. Based on our base case fair value estimate of Php8.00/sh, which already a factor in a more conservative outlook for Bacman, upside potential is significant at 24.4%.

Our revised fair value estimate of FGEN is Php29.50/sh, down 4.3% from our original fair value estimate. In our computation, we only factored in the negative impact of a decline in EDC's fair value and ignored the positive impact of a drop in interest expense. Despite the drop, upside potential based on FGEN's current price of Php24.45/sh is significant at 20.6%. Outside of Bacman, we continue to like FGEN given its Sta. Rita and San Lorenzo gas plants, which have long term take-or-pay contracts for all of their generation capacities. EDC also remains attractive despite Bacman, with around 80% of its power generation capacity secured with long-term take-or-pay contracts. It is also a pure play on renewable energy.

We are maintaining our BUY rating on FPH. Despite rising by 20.1% for the year to date period, FPH still trades at a 19.6% discount to our revised fair value estimate of Php134.40/sh which already factors in the negative impact of a decline in EDC's fair value. The stock also trades at a steep 24.7% discount to its market based NAV of Php143.60/sh. Fundamentally, we like FPH because it is a cheaper way to gain exposure to the country's power industry given the Company's 66% stake in FGEN and its 3.9% stake in Meralco, the country's largest power distributor.

Exhibit 2: Summary of changes in FV estimates

FV estimate (Php)	Old	New	% change
EDC	8.5	8.0	*-6.0*
FGEN	30.8	29.5	*-4.3*
FPH	139.0	134.4	*-3.3*

Source: COL estimates

Investment Rating Definitions

BUY	HOLD	SELL
Stocks that have a **BUY** rating have attractive fundamentals and valuations, based on our analysis. We expect the share price to outperform the market in the next six to twelve months.	Stocks that have a **HOLD** rating have either 1.) attractive fundamentals but expensive valuations; 2.) attractive valuations but near term earnings outlook might be poor or vulnerable to numerous risks. Given the said factors, the share price of the stock may perform merely inline or underperform the market in the next six to twelve months.	We dislike both the valuations and fundamentals of stocks with a **SELL** rating. We expect the share price to underperform in the next six to twelve months.

Important Disclaimers

2401-B East Tower, Philippine Stock Exchange Centre, Exchange Road, Ortigas Center, Pasig City, 1605 Philippines
Tel: +632 636-5411 Fax: +632 635-4632 Website: http://www.colfinancial.com