BDO MONEY TALKS

Retail sector

For your convenience

By Marian Rose C. Ang

Retail channels include hypermarkets, supermarkets, discounters, mini-marts, convenience stores and *sari-sari* stores. In recent years, retailers have evolved their store formats in response to the ever-changing consumer lifestyle, which is heading towards modernity and convenience.

Per capita Gross Domestic Product (GDP) in the country has been increasing over the years and this has translated to higher consumer spending. The rise in income is mainly a result of the continued expansion of the Business Process Outsourcing (BPO) industry as well as the strong inflow of Overseas Filipino remittances. Those working for BPO companies are young, earn well and live a busy and fast-paced lifestyle which makes the ready-to-eat food offerings of convenience stores very appealing. Ready-to-eat food accounts for the largest percentage of convenience store sales, followed by beverages.

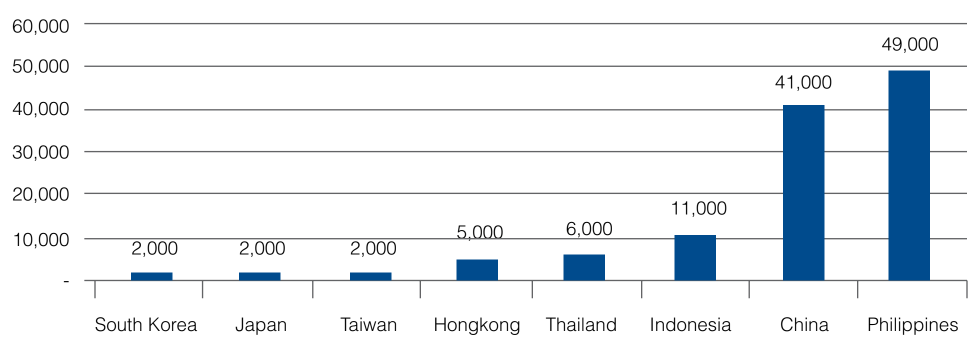
	Per Capita GDP	BPO Revenues (in billion USD)	BPO Employees	OFW Remittances (in billion USD)
2007	1,684.00	4.80	271,556	14.40
2008	1,919.00	6.10	355,135	16.40
2009	1,851.00	7.10	444,811	17.30
2010	2,155.00	8.90	536,128	20.56
2011	2,364.00	11.00	679,464	21.92
2012	2,591.00	13.00	769,932	23.35
2013	2,769.00	15.60	851,782	25.37
2014	2,851.00	18.40	1,000,000	26.97

Source: BSP

Population growth, changes in consumer lifestyle, urbanization and the influx of people from rural to urban areas have likewise fueled the growth of convenience stores. Companies are expanding not only in big but also small cities where BPOs are located as time-pressed consumers embrace convenience and proximity. At present, approximately 60% of convenience stores are located in Metro Manila, but operators are gradually moving to Visayas and Mindanao as these areas are still underpenetrated.

In terms of population per store, the Philippines has only one store for every 49,000 people, a far cry from that of South Korea, Taiwan, Japan (with 1 store for every 2,000) and Thailand (1 for every 6,000). Operators are scrambling to open as many stores to achieve market share, critical mass and profitability, making it likely that the number of convenience stores nationwide will double to 4,000 from 2,000 within 4 years.

Population per store (2014)



Source: Euromonitor

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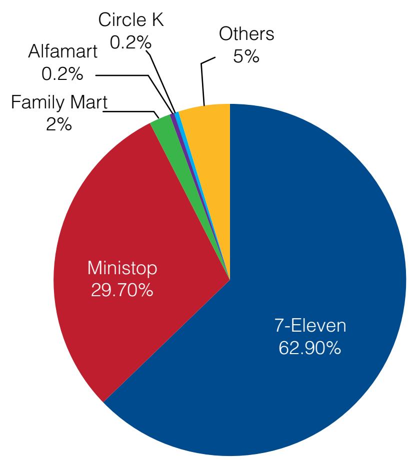
Market share of Philippine convenience stores (2014)



Source: Euromonitor

Based on a study by Kantar Worldpanel (Kantar), convenience store purchases from January 2014 to January 2015 rose by 45%, making it the fastest growing retail channel. This was followed by direct sales and drug stores which registered growth rates of 31% and 11%, respectively. Of the 3,000 homes in urban and rural areas surveyed, 18.50% of Filipino homes buy from convenience stores, up from 16.1% in 2014 - translating to an additional 560,000 customers. While majority of the buyers are from the National Capital Region (about 34% of homes purchase from convenience stores), the biggest spenders are located in Mindanao, with buyers shopping 9x a year versus those from the NCR who only purchase 5x a year.

For a time, the major players in the Philippines were only 7-Eleven, operated by Philippine Seven Corporation and Ministop, operated by Robinsons Retail Holdings, Inc. as it has been generally overlooked by international retailers. Of late however, the country has piqued the interest of these foreign brands because of the country's solid economic growth and favorable demographics. These retailers are hoping to gain a piece of the industry pie as *Euromonitor* estimates the Asia Pacific region to account for 39% of global convenience sales growth through 2019. Japan-based Family Mart has partnered with the Ayala and Rustan Groups, another Japan-based store, Lawson, has partnered with Puregold Price Club, Indonesia-based Alfamart has partnered with SM Investments Corporation, and US-based Circle K partnered with Super 8 Retail to operate convenience stores in the country.

The average size of convenience stores is around 100-150 square meters and are usually located in high traffic areas. Convenience stores have evolved from simply offering packaged food items to offering ready-to-eat meals, coffee, doughnuts and ice cream, among others, competing directly with quick service restaurants like Jollibee Foods and McDonalds. A small dining area and free internet connectively are also available to attract customers. This is in contrast to the traditional mom-and-pop / sari-sari stores that a lot of Filipinos are used to in many parts of the country.

7-Eleven and Ministop, which hold the top 2 spots, are strengthening their foothold in the industry, making sure that they are not left behind or overtaken by new players. The new players on the other hand, are playing catch-up with these industry incumbents – looking for ways and offering unique products to lure customers. The market leader, 7-Eleven is being very aggressive in its network expansion program as it aims to protect its market share in the industry. Network expansion however, is not just about gaining market share, equally important is the need to achieve economies of scale, buying buyer and operational efficiencies.

Store Tally	as of	Metro Manila	Luzon	Visayas	Mindanao	Total
7-Eleven	1H'15	620	643	133	2	**1,398**
Mini-stop	1Q'15	297	158	17	1	**473**
Family Mart	1Q'15	97	3	0	0	**100**
Alfamart	1H'15	1	51	0	0	**52**
Lawson	1H'15	4	0	0	0	**1**
Circle K	1H'15	2	0	0	0	**2**
Total		**1,017**	**856**	**150**	**3**	**2,026**

Source: Company Disclosures

A concern is the proximity of convenience stores with each other. In Metro Manila, it is normal to see several convenience stores located along one street. In some cases, you can find one particular retailer operating two convenience stores in one street. The retailer is probably cannibalizing the sales of the first shop that opened but this strategy will put off, if not, prevent another retailer from opening shop in the same street. Metro Manila therefore, appears saturated. That is why retailers are moving away from the Metro to other high-growth cities that remain underpenetrated like Cebu, Bacolod, Iloilo and Davao.

As competition for market share, sales and franchisees intensifies however, expect profitability to be hit. Operators of convenience stores also face competition from drug stores which have changed their store formats- increasing store areas and offering food, beverages and personal items. As competition gets keener therefore, market share is vital to compensate for the decline in margins.

Going Forward

Prospects for the retailing sector remain bright and the upward trend is seen to continue. In a study done by Euromonitor, consumer spending is expected to take-off when per capita GDP reaches $3,000. In the case of the Philippines, this is seen to happen in the next year or so. The country is also about to enter the demographic sweet spot whereby a big part of the population is of working age which means more people with spending power. Lastly, the overall penetration rate in the country is very low compared to Thailand and other Asian countries which leaves ample room for retailers to expand their businesses.

In spite of the boom in the convenience store industry, we do not expect a significant impact on other food retailing channels such as supermarkets and hypermarkets. Convenience stores have their own niche market and can only offer a limited number of products due to the limited shelf space. The first to be hit by the expansion of branded convenience stores are probably the mom-and-pop and *sari-sari* stores that are located in major thoroughfares. Branded stores are able to offer more variety and better customer experience. Nevertheless, *sari-sari* stores will remain an important sector and will continue to grow, albeit at a slower pace. *Sari-sari* stores will continue to thrive in rural and far flung areas as it will not be profitable for big retailers to open shop there. Note that in small towns, the *"palista"* system that is available in *sari-sari* stores very much appeals to class CDE. ♦

Puregold Price Club, Inc.

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Company Background

Puregold Price Club, Inc. (PGOLD) was incorporated on September 8, 1998, as a company engaged in the business of buying, selling, distributing, and marketing wholesale or retail goods and commodities.

The Company conducts its operations through three retail formats and store brands: (i) hypermarkets, through Puregold Price Club; (ii) supermarkets, through Puregold Junior; and (iii) discounters, through Puregold Extra, which offers a limited number of goods, comprising of the Company's top-selling stock-keeping units, that are intended to be sold quickly at prices lower than Puregold Price Club or Puregold Junior.

In 2012, Puregold acquired Kareila Management Corporation (also owned by the Co family), operator of S&R; and the Gant Group of Companies, owner of 19 Parco supermarkets. S&R is the only warehouse membership club in the Philippines, and targets middle to upper class customers offering high quality international and local brands through its stores in the Philippines.

In 2013, acquired Company E Corporation, operator of 4 Eunilane food marts and 11 Grocer E supermarkets.

In 2014, PGOLD announced a joint venture with Lawson Asia Pacific, with the aim of building Lawson convenience stores nationwide.

Puregold has grown significantly since it commenced operations, expanding from 1 store in 1998 to 254 stores in 52 cities and 56 municipalities as of end-March 2015.

Share Data

PSEi Code	PGOLD
Rating	Outperform
52-wk range (Php)	31.45-43.95
Closing Price (Php)	36.00
12-mo. Tgt Price (Php)	41.30
Price Yield (%)	7.13
Dividend Yield (%)	0.98
Total Return (%)	8.11

Review of Share Price Performance

PGOLD's price slid from over Php40 per share to under Php35 in August 2014 following news of a 6.6% decline in 1H 2014 earnings. The stock's price recovered towards the end of 2014 in tandem with better results for the last two quarters of that year. At its July 13, 2015 closing price of Php36 per share, however, PGOLD underperformed the PSEI with its price down by 15.8% from a year ago compared with a 9.7% increase in the equity benchmark for the same period.

Price Performance

PGOLD —— PCOMP ——

Source: Bloomberg

EQUITY RESEARCH

Equity Valuation

Comparative Valuation	Closing Price (Php)	Mkt Cap (Php bn)	2015 P/B (x)	2015 P/E (x)	2015 ROE (%)	Div Yield (%)	Free Float* (%)
SM	897.00	720.34	2.64	22.65	11.47	1.44	45.98
PGOLD	**36.00**	**99.58**	**2.62**	**19.73**	**14.00**	**1.07**	**32.63**
RRHI	70.65	97.85	2.25	22.06	10.55	0.75	37.55
SEVN**	107.00	49.05	11.97	49.53	26.81	0.37	32.37
SSI	8.43	27.93	2.92	22.01	13.38	0.98	29.63

*Sources: Bloomberg; * Philippine Stock Exchange; **BDO PB estimates*
Notes: SM – SM Investments; RRHI – Robinsons Retail Holdings, Inc.; SEVN – Philippine Seven Corp.; SSI – Store Specialists, Inc.

- **Double-digit growths in 1Q net profit, sales.** Puregold Price Club's (PGOLD) 1Q 2015 results showed that net profit stood at Php1.054 billion (+11.8% y/y) as net sales reached Php20.689 billion (+12.5% y/y). Sales growth was supported by an almost 13% y/y increase in number of stores to 254 from 225 in 1Q 2014. Other operating income likewise improved to Php742 million (+10.1% y/y), driven by earnings from promotional activities, rent and membership fees.
- **Lower EBITDA margin.** Meanwhile, continued expansion led to a faster growth in cash operating expenses (+12.8% y/y to Php2.528 billion) relative to sales, particularly those associated with new store openings such as rent and salaries. This resulted in a deterioration in 1Q 2015 EBITDA margin to 9.1%. Nonetheless, we expect the situation to improve towards the end of the year as new stores gain foot traffic and sales volume, aided by seasonality factors.

Earnings Results: Full Year 2014; First Quarter 2015

	2013	2014	Chg (%)	1Q'14	1Q'15	Chg (%)
No. of stores	215	248	15.35%	225	254	12.89%
Same stores sales growth	2.80%	3.50%		-0.10%	3.70%	
Net Sales (Php Mn)	73,177	84,697	15.74%	18,385	20,689	12.53%
Gross profit (Php Mn)	12,699	14,484	14.06%	3,204	3,563	11.20%
EBITDA (Php Mn)	6,877	8,133	18.26%	1,737	1,881	8.29%
Net Income (Php Mn)	3,959	4,520	14.17%	943	1,054	11.75%
Gross profit (%)	17.35%	17.10%		17.43%	17.22%	
EBITDA (%)	9.40%	9.60%		9.45%	9.09%	
Net Income (%)	5.41%	5.34%		5.13%	5.10%	

Source: PGOLD

Our View and Recommendation:

Short-term (less than 2 years): At Php36.00, PGOLD's P/E (price-to-earnings) ratio of 19.73x and P/B (price-to-book) ratio of 2.62x consensus 2015 estimates make it the cheapest among selected retail peers. The stock also has the second-highest dividend yield (1.07%) in our basket of retailers. Our 12-month fair value estimate for PGOLD is at Php41.30 per share, based on a blended metric of P/E at 22x (factoring in a low premium to the company's 2015 return-on-equity or ROE of 14%), and P/B at 2.5x. With a possible price upside of 7.13%, PGOLD may outperform the PSEi's 5% to 6% growth expectations. **Outperform.***

Medium-term (beyond 2 years): Assuming that the company: 1) meets its goal of adding 25 new Puregold and 2 S&R stores annually; and 2) maintains net income margins of close to 5.0% through our forecast period, we expect PGOLD's price to reach Php46.55 per share by 2017, for a price yield of 11.0%. Plus an estimated dividend yield of 1.2%, the stock can give a total return of 12.2%, versus the PSEi's expected growth of 6% in the medium term. **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)	5,437	5,863	6,223
ROE %	14.1%	13.5%	12.9%
EPS (Php)	1.97	2.12	2.25
BV / Sh (Php)	13.96	15.66	17.44
Div / Sh (Php)	0.30	0.39	0.42
Div Yd %	0.83%	1.09%	1.18%
P/E (x)	18.32	16.99	16.00
P/B (x)	2.58	2.30	2.06

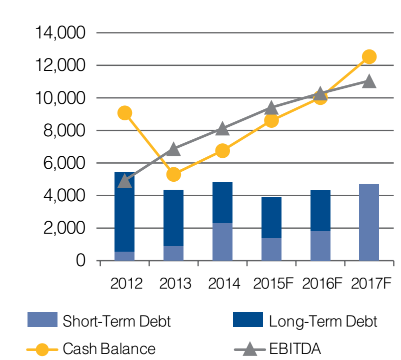
Source: BDO Private Bank Research

Major Shareholders

	% Stake
Cosco Capital, Inc.	51.01
Lucio L. Co	7.63
Susan P. Co	6.44
Capital Research Global Investor	4.79
Ameriprise Fin Group	1.66
Thornburg Inv. Mgmt Inc.	1.22
Others	27.25
Total	**100.00**

Source: Bloomberg

Debt Capacity Chart (Php millions)



Source: Bloomberg, BDOPB Research

Overall, PGOLD garnered a credit rating of **A+*** for the medium term, backed by its cash-rich operations, healthy capitalization, hefty interest cover and favorable maturity profile.

CREDIT RESEARCH

Financial Highlights (Php millions):

	2012	2013	2014	2015F	2016F	2017F
Cash	9,084	5,299	6,759	8,614	10,015	12,526
Receivables – net	7,610	10,687	13,150	16,332	20,033	23,932
Total Assets	45,444	49,626	53,666	60,822	67,268	74,946
Current Liabilities	10,777	12,882	13,835	15,909	17,005	21,512
Long Term Liabilities	7,241	6,157	5,598	6,282	6,949	5,176
Total Liabilities	18,018	19,039	19,433	22,192	23,954	26,688
Total Equity	27,426	30,586	34,233	38,631	43,315	48,258
Short-term Debt	552	884	2,326	1,380	1,810	4,717
Long-term Debt	4,909	3,452	2,493	2,493	2,493	0
Total Debt	5,461	4,335	4,820	3,873	4,303	4,717
Debt to Equity (%)	19.9%	14.2%	14.1%	10.0%	9.9%	9.8%
Net Debt to Equity (%)	-13.2%	-3.2%	-5.7%	-12.3%	-13.2%	-16.2%
Debt to Assets (%)	12.0%	8.7%	9.0%	6.4%	6.4%	6.3%
Net Interest Expense	(15)	21	129	16	1	23
EBITDA	4,924	6,877	8,133	9,412	10,291	11,051
EBITDA % Increase	75%	40%	18%	16%	9%	7%

Sources: PGOLD; F – BDO Private Bank Research

- **Growth spurt.** An initial public offering (IPO) in 2011 strengthened Puregold Price Club Inc.'s (PGOLD) balance sheet and paved the way for expansion – both organically and by way of acquisitions. The wider equity base allowed PGOLD to significantly improve its credit rating and avail of long-term loans (in addition to IPO proceeds) for capital expenditure (capex) needs. Expansion resulted in EBITDA (earnings before interest, taxes, depreciation and amortization) growing from less than Php2 billion in 2010 to over Php8 billion by 2014.
- **Far from complacent.** Despite its accomplishments in the past four years, PGOLD continues to be on expansion mode. Last February, Puregold announced that it acquired from Nueva Ecija-based retailer NE, Inc. nine supermarkets located in Nueva Ecija, Bulacan, Baler, Aurora and Isabela. PGOLD's capex guidance for 2015 is at Php5.5 billion broken down as follows: Php2.5 billion for 25 new Puregold stores; Php1 billion for 2 new S&R stores; Php500 million for 50 to 100 Lawson stores; and Php1.5 billion for possible acquisitions.

Our View and Recommendation:

Robust cash flows can cover capex needs… Our estimated 2015 EBITDA of about Php9.4 billion for Puregold can cover the company's planned capex of Php5.5 billion as well as 2-year debt of Php3.7 billion. As such, we don't expect the company to require much external funding support and continue to maintain a low leverage profile.

…and support liquid operations. Annual forecasted EBITDA flows ranging between Php9.0 billion to over Php11 billion for the years 2015-17, can cover annual capital expenditures of Php3 billion (organic) to Php6 billion (with acquisitions). The company also has a workable dividend payout ratio of around 20%, which allows it to plow back most of its earnings to the business either for expansion or cash accumulation. Hence, we expect liquidity to stay fluid and maintain a comfortable working capital ratio of 1.7x in the next 3 years, with days receivable (or the length of time to collect receivables) & inventory turnover at only less than 5 and 60, respectively.

***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.

Robinsons Retail Holdings, Inc.

Company Background

Robinsons Retail Holdings, Inc. (RRHI) is the country's second largest Multi-Format Retailer. Since opening its first Robinsons Department Store in Metro Manila in 1980, the company now operates in 6 business segments: supermarkets (Robinsons Supermarket and its 2 new sub-formats – Robinsons Easymart and Robinsons Selections), department stores (Robinsons Department Store), DIY stores (Handyman Do it Best, True Value, and the newly acquaried big box hardware subformat – A.M. builders' Depot), convenience stores (Ministop), drug stores (South Star Drug and Manson Drug) and specialty stores (Robinsons Appliances, Toys "R" Us, Daiso Japan, Topshop, Topman, Dorothy Perkins, Shiseido, Benefit).

RRHI, through its wholly-owned subsidiary Robinsons Gourmet Food and Beverage, Inc., also recently signed an International Distribution Agreement for the supply of Costa Coffee beans and operations of Costa Coffee shops in the Philippines.

As of March 31, 2015, RRHI has a portfolio of 1,356 stores nationwide (587 in Metro Manila, 584 in Luzon – outside of M.M., 126 in Visayas, and 59 in Mindanao).

RRHI is separate from and is not intended to be folded into the umbrella of JG Summit Holdings, Inc. Nonetheless, it enjoys synergistic benefits with affiliate firms within the Gokongwei Group, like site locations (Robinsons Land Corp.), products (Universal Robina Corp.), and advertising publications (Summit Media), among others.

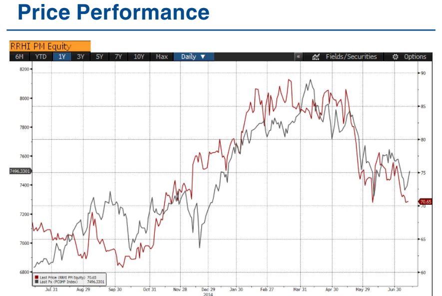
Share Data

PSEi Code	RRHI
Rating	Outperform
52-wk range (Php)	60.55-90.10
Current Price (Php)	70.65
Target Price (Php)	83.56
Price Upside (%)	18.30
Dividend Yield (%)	0.70
Total Return (5)	19.00

Review of Share Price Performance

RRHI peaked at Php90 last March, ahead of PSEi's breaching the 8,000 level by April, but has since been on a general downtrend along with most local equities on concerns of: 1) the PSEi's relatively high P/E valuation compared with other regional markets; 2) the impending interest rate hike by the US; 3) the lingering debt crisis of Greece; and 4) China's slumping stock market and decelerating economy. Market sentiment may improve moving forward, depending on news that will come out from the US, Greece and China, and on whether our GDP growth and corporate earnings improve from lower-than-expected first quarter results.

Price Performance



RRHI —— PCOMP ——

Source: Bloomberg

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EQUITY RESEARCH

Equity Valuation

Comparative Valuation	Closing Price (Php)	Mkt Cap (Php bn)	2015 P/B (x)	2015 P/E (x)	2015 ROE (%)	Div Yield (%)	Free Float* (%)
SM	897.00	720.34	2.64	22.65	11.47%	1.44%	45.98
PGOLD	36.00	99.58	2.62	19.73	14.00%	1.07%	32.63
RRHI	**70.65**	**97.85**	**2.25**	**22.06**	**10.55%**	**0.75%**	**37.55**
SEVN**	107.00	49.05	11.97	49.53	26.81%	0.37%	32.37
SSI	8.43	27.93	2.92	22.01	13.38%	0.98%	29.63

*Sources: Bloomberg; * Philippine Stock Exchange; **BDO PB estimates*
Note: SM – SM Investments, Inc.; PGOLD – Puregold Price Club, Inc.; SEVN – Philippine Seven Corp.; SSI – SSI Group, Inc.

▶ **Valuation multiples in range with peers...** RRHI's current market price of Php70.65 per share translates to fair P/E and P/B multiples of 22x and 2.2x respectively, which is within range of listed retail peers. The company however, has a relatively lower ROE figure as a result of an equity boost from its Php28.6 billion IPO back in 2013.

▶ **...amid new store additions and steady SSSG.** RRHI sustained robust double-digit growths in both top and bottom line results for the first quarter, driven by the company's ongoing store expansion (+211 stores) and steady overall same store sales growth (SSSG) of 3.4% on higher basket size purchases. The supermarket (+15 stores, +11% revenues, +14% EBITDA), DIY (+27 stores, +21% revenues, +12% EBITDA) and department stores (+22 stores, +10% revenues, +8% EBITDA) segments continue to drive growth as they contribute 47%, 18%, and 14% of the group's EBITDA respectively. Meanwhile, the convenience stores segment added 71 outlets and posted a 19% jump in revenues, but higher operating expenses (+30%) pushed the segment's EBITDA down by 15% to Php59 million. The drugstores segment on the other hand, added 65 outlets, recorded a 12% increase in revenues and an 11% hike in EBITDA to Php87 million. The specialty stores segment also added 31 stores, grew revenues by 24% and recorded a 70% surge in EBITDA to Php100 million.

Earnings Results: Full Year 2014; First Quarter 2015

	2013	2014	% chg	1Q'14	1Q'15	% chg
No. of stores	1,064	1,327	24.7%	1,145	1,356	18.4%
Same stores sales growth	2.6%	3.6%		2.4%	3.4%	
Revenues (Php Mn)	68,575	81,834	19.3%	17,750	20,112	13.3%
Gross profit (Php Mn)	15,632	18,862	20.7%	3,989	4,649	16.5%
EBITDA (Php Mn)	5,063	5,768	13.9%	1,043	1,189	14.1%
Net Income (Php Mn)	3,117	3,933	26.2%	643	822	28.0%
Gross profit (%)	22.8%	23.0%		22.5%	23.1%	
EBITDA (%)	7.4%	7.0%		5.9%	5.9%	
Net Income (%)	4.5%	4.8%		3.6%	4.1%	

Source: RRHI

Our View and Recommendation:

Short-term (less than 2 years): RRHI share price has pulled back by almost 7% to Php70.65 from its 2014 close of Php75.70, resulting in more attractive multiples of 22x P/E and 2.2x P/B. The stock however, has a target price of Php83.56 (based on modified valuations of 25x P/E and 2.5x P/B) for a possible price upside of 18.3% in the next 12 months, on assumptions that the company is able to expand its top line by 20% and improve its EBITDA margin to 7.4%. As such, RRHI will likely outpace the PSEi's expected return of 5%-6% during the same period. **Outperform.***

Medium-term (beyond 2 years): Considering a projected annual EPS growth of 16%, as the company adds between150-280 stores each year, RRHI may be valued at Php98.50 by 2017 using the same valuation factors of 25x P/E and 2.5x P/B. With a potential annualized price appreciation of 14.2%, RRHI may thus continue to outperform against most stocks in the PSEi, as supported by its more diverse and extensive portfolio of retail formats. **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)	4,208.3	5,031.8	5,677.6
ROE %	10.2%	11.1%	11.4%
Div / Sh	0.51	0.61	0.73
Div Yd %	0.7%	0.9%	1.0%
BV / Sh	31.20	34.28	37.72
EPS	3.04	3.63	4.10
P/B (x)	2.26	2.06	1.87
P/E (x)	23.25	19.45	17.23

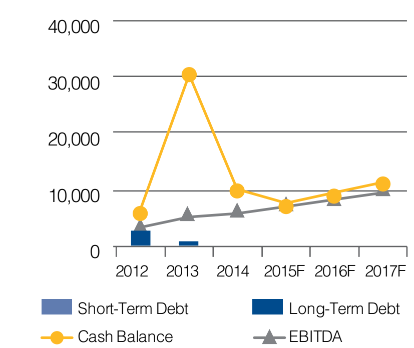
Source: BDO Private Bank Research

Major Shareholders

Major Shareholders	% Stake
JE Holdings, Inc.	35.00
Lance Y. Gokongwei	11.70
Robina Y. Gokongwei-Pe	7.65
James L. Go	3.00
Lisa Y. Gokongwei-Cheng	2.55
Faith Y. Gokongwei- Lim	2.55
Ameriprise Fin Grp	1.92
Norges Bank Investment	1.65
TIAA CREF Investment	1.33
Fidelity International	0.77
Others	31.88
Total	**100.00**

Source: Bloomberg

Debt Capacity Chart (Php millions)



Source: Bloomberg, BDOPB Research

Overall, RRHI retained its high quality AA* rating. Credit is supported by its robust earnings outlook, adequate liquidity and negligible leverage position. However, its rating hinges on the company's capability to effectively execute and implement its network expansion plans by identifying suitable sites for its target market. RRHI faces market saturation risk amid increasing competition in several business segments. Its key competitors (i.e. SM, Puregold) also have their respective expansion programs, which may coincide with the locations of the company's existing and prospective stores, and thus affect its sales volume and earnings. Some geographical areas may have also reached or may be close to reaching their point of saturation (where the size of local demand is not large enough to accommodate new stores).

FIXED INCOME RESEARCH

Financial Highlights (Php millions):

	2012	2013	2014	2015F	2016F	2017F
Cash	6,052	30,129	9,970	7,103	9,001	11,119
Receivables - net	7,180	8,479	12,376	15,208	17,499	18,985
Total Assets	24,232	52,351	57,494	62,835	71,625	78,868
Current Liabilities	13,302	13,375	15,022	16,339	20,296	22,199
Long Term Liabilities	2,872	993	1,235	1,323	1,439	1,515
Total Liabilities	16,174	14,368	16,258	17,662	21,735	23,713
Total Equity	8,057	37,982	41,236	45,173	49,890	55,155
Short-term Debt	412	396	56	56	0	0
Long-term Debt	2,117	112	56	0	0	0
Total Debt	2,528	507	112	56	0	0
Debt to Equity (%)	31.4%	1.3%	0.3%	0.1%	0.0%	0.0%
Net Debt to Equity (%)	-43.7%	-78.0%	-23.9%	-15.6%	-18.0%	-20.2%
Debt to Assets (%)	10.4%	1.0%	0.2%	0.1%	0.0%	0.0%
Net Interest Expense	58	77	12	21	0	0
EBITDA	3,040	5,063	5,768	7,132	8,463	9,524
EBITDA % Increase	69%	67%	14%	24%	19%	13%

Source: RRHI; F – BDO Private Bank Research

▶ **Minimal debt...** RRHI holds little debt after repaying most of its borrowings from proceeds of its Php28 billion IPO back in 2013. Excess funds from the IPO were also deployed for its aggressive store portfolio expansion and to also augment the company's working capital for its day-to-day operations. With EBITDA sizeable enough to fund majority of the company's capital spending needs, we expect the company to maintain robust working capital ratios of 1.3x on average.

▶ **...on cash-generative operations.** RRHI also cited that its cash conversion cycle remains at negative 2 days as of the first quarter of 2015, with trade receivables at 3.3 days, inventory at 56.7 days and payables at 62.0 days.

Our View and Recommendation:

Comfortable liquidity... The company's substantial liquidity, aided by proceeds from its IPO and robust operating cash flows should be sufficient to support RRHI's expansion program with minimal need for external funding support. The retailer has budgeted Php6 billion for capex spending this year as it targets a store network 1,600 by yearend

...and upbeat earnings outlook. An upbeat earnings outlook with operating cash flows estimated to expand at a CAGR (compounded annual growth rate) of 18% through 2017, also strengthens its credit profile. EBITDA growth will likely be aided by margin improvements from 7.0% last year to possibly 7.7% by 2017, as the company continues to optimize its sales mix and varied store formats.

***AA (High Quality)** Margins of protection may not be as large as in Aaa issues. Fluctuations of protective elements may be of greater amplitude or there may be other elements present which make the long-term risk appear somewhat larger for Aaa-rated securities.

Philippine Seven Corporation

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Company Background

SEVN was incorporated on November 23, 1982 and acquired the license to operate 7-Eleven (7-11) stores in the Philippines on December 13, 1982 from Seven Eleven, Inc. (formerly Southland Corporation) of Dallas, Texas. In July 1988, SEVN transferred its Philippine area license to operate 7-11 stores to its affiliate, Phil-Seven Properties Corporation (PSPC), together with some of its store properties, in exchange for shares of stock of PSPC. In May 1996, the stockholders of both SEVN and PSPC approved the merger of the two companies, with the Securities and Exchange Commission (SEC) subsequently approving of the merger in October 1996. PSPC was then absorbed by SEVN as the surviving entity.

SEVN and its subsidiaries are primarily engaged in the business of retailing, merchandising, buying, selling, marketing, importing, exporting, franchising, acquiring, holding, distributing, warehousing, trading, exchanging, or otherwise dealing in all kinds of grocery items, dry goods, food or foodstuffs, beverages, drinks, and all kinds of consumer needs or requirements and in connection therewith, operating or maintaining warehouses, storages, delivery vehicles and similar or incidental facilities. They're also engaged in the management, development, sale, exchange, and holding for investment or otherwise of real estate of all kinds, including buildings, houses, and apartments and other structures.

As of end 2014, SEVN is operating 1,281 stores, 563 of which are franchise stores, 180 franchise store service agreements, and the remaining 538 are company-owned stores.

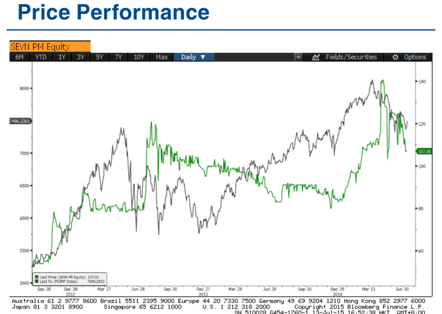
Share Data

PSEi Code	SEVN
Rating	Underperform
52-wk range (Php)	79.00 – 185.00
Current Price (Php)	107.00
Target Price (Php)	82.67
Price Upside (%)	-22.7
Dividend Yield (%)	0.4
Total Return (%)	-22.4

Review of Share Price Performance

SEVN is currently up by 26.6% to Php107.00 from its 2014 closing price of Php84.50. The share price surged by 118.9% to Php185.00 on May 6, 2015 due to: 1) an aggressive expansion plan to widen store network by 25% annually to protect market share; and 2) projected benign inflation in 2015, which increases purchasing power of consumers. The price declined by 42.2% to Php107.00 from its recent peak on investor concerns over the on-going Greek crisis and uncertainty in timing of the US Federal Reserve's policy rate hike.

Price Performance



SEVN —— PCOMP ——

Source: Bloomberg

EQUITY RESEARCH

Equity Valuation

Comparative Valuation	Closing Price (Php)	Mkt Cap (Php bn)	2015 P/B (x)	2015 P/E (x)	2015 ROE (%)	Div Yield (%)	Free Float* (%)
SM	897.00	720.34	2.64	22.65	11.47%	1.44%	45.98
PGOLD	36.00	99.58	2.62	19.73	14.00%	1.07%	32.63
RRHI	70.65	97.85	2.25	22.06	10.55%	0.75%	37.55
SEVN**	**107.00**	**49.05**	**11.97**	**49.53**	**26.81%**	**0.37%**	**32.37**
SSI	8.43	27.93	2.92	22.01	13.38%	0.98%	29.63

*Sources: Bloomberg; * Philippine Stock Exchange; **BDO PB estimates*
Notes: SM – SM Investments; PGOLD –Puregold Price Club Inc; RRHI – Robinson's Retail Holdings Inc; SEVN – Philippine Seven Corp; SSI – SSI Group Inc

- **Expensive P/E but highest ROE.** SEVN with P/E of 49.5x is the most expensive among its peers and more than twice (2x) their multiples of 19.7x – 22.7x. However, it provides the highest ROE at 26.8% which is more than double (2x) its rivals that register an ROE range of 10.6% - 13.4%.
- **Store expansion to be main growth driver.** SEVN grew net income by 12.8% in 1Q 2015 as they expanded their footprint by 27.8% to 1,341 stores in response to increased competition for market share in the convenience store sector. Despite fierce rivalry from existing (i.e., Mercury Drug, MiniStop) and new entrants (i.e., FamilyMart, Alfamart), SEVN remains the leader with 49% market share in 2014. They seek to retain this dominant position by targeting a network of 2,000 stores by 2019 and further strengthen their foothold as the leading convenience store chain in the country.

Earnings Results: Full Year 2014, First Quarter 2015

	2013	2014	% chg	1Q'14	1Q'15	% chg
No of Stores	1,008	1,281	27.1%	1,049	1,341	27.8%
Revenues (Php Mn)	14,134	17,107	21.0%	3,611	4,543	25.8%
Gross Profit (Php Mn)	3,472	4,246	22.3%	842	1,091	29.5%
EBITDA (Php Mn)	1,702	2,128	25.1%	340	415	22.1%
Net Income (Php Mn)	683	873	27.9%	100	113	12.8%
Gross Margin (%)	24.6%	24.8%		23.3%	24.0%	
EBITDA Margin (%)	12.0%	12.4%		9.4%	9.1%	
Net Margin (%)	4.8%	5.1%		2.8%	2.5%	

Source: SEVN

Our View and Recommendation:

Short-term (less than 2 years): Given SEVN stock price may have already reached its peak at Php185 on May 6, 2015, it is currently in its correction phase with price lower by 42.2% to Php107. Assuming adjusted valuation multiples of 35x P/E and 8.0x P/B, we expect the share price to further decline by 22.7% to Php82.67 as it faces stiffer competition from other convenience store operators who also want to take advantage of the country's resilient consumer spending. **Underperform.***

Medium-term (beyond 2 years): The projected annual EPS growth of 18.3% through 2018 is possible if they are able to achieve their aspirational 25% annual store growth over the next three (3) years. This could allow their share price to reach Php132.32 by 2018 giving an annualized price return of 6.4% along with a possible dividend yield of 0.6% for a total return of 7.0%, which may outperform most stocks in the PSEi, though only marginally. **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)	990	1,179	1,471
ROE (%)	26.8%	25.7%	25.9%
Div / Sh (%)	0.40	0.46	0.55
Div Yd (%)	0.37%	0.43%	0.51%
BV / Sh	8.94	11.04	13.70
EPS	2.16	2.57	3.21
P/B (x)	11.97	9.69	7.81
P/E (x)	49.53	41.61	33.36

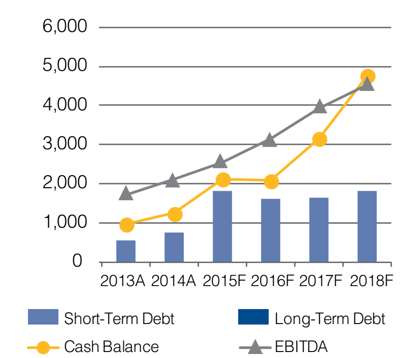
Source: BDO Private Bank Research

Major Shareholders

	% Stake
President Chain Store (Labuan) Holdings Ltd	51.56
PCD Nominee (Foreign)	24.51
Asian Holdings Corporation	6.69
PCD Nominee (Filipino)	4.76
Agus Development Corporation	2.69
Jose Victor P. Paterno	2.59
Ma Cristina P. Paterno	1.75
Others	5.45
Total	**100.00**

Source: List of Top 100 Stockholders (As of March 31, 2015)

Debt Capacity Chart (Php millions)



Source: Bloomberg, BDOPB Research

Overall, SEVN achieves an **A*** rating or an upper medium credit grade.

FIXED INCOME RESEARCH

Financial Highlights (Php millions):

	2013	2014	2015F	2016F	2017F	2018F
Cash	973	1,242	2,127	2,080	3,163	4,773
Receivables – net	1,381	1,765	2,322	2,867	3,500	4,090
Total Assets	6,025	7,882	10,747	12,583	15,082	17,796
Current Liabilities	3,177	4,225	6,157	6,917	8,069	9,264
Long Term Liabilities	307	367	493	604	732	851
Total Liabilities	3,483	4,593	6,650	7,520	8,801	10,114
Total Equity	2,541	3,290	4,097	5,063	6,281	7,681
Short-term Debt	560	750	1,828	1,617	1,655	1,811
Long-term Debt	–	–	–	–	–	–
Total Debt	560	750	1,828	1,617	1,655	1,811
Debt to Equity (%)	22.0%	22.8%	44.6%	31.9%	26.4%	23.6%
Net Debt to Equity (%)	-16.3%	-14.9%	-7.3%	-9.1%	-24.0%	-38.6%
Debt to Assets (%)	9.3%	9.5%	17.0%	12.8%	11.0%	10.2%
Net Interest Expense	9	10	27	41	40	45
EBITDA	1,702	2,128	2,559	3,163	3,914	4,525
EBITDA % Increase	40.1%	25.1%	20.2%	24%	24%	16%
Net Income	683	873	990	1,179	1,471	1,711
ROE %	30.7%	30.0%	26.8%	25.7%	25.9%	24.5%

Source: SEVN; F – BDO Private Bank Research

- **Boosting capital budget...** SEVN has allotted Php3.5 billion (+75% y/y) for its 2015 capital expenditures with almost Php2.5 billion (or 71% ot total) earmarked to achieve their target yearend store count of 1,600 (+319). The remaining Php1 billion will be for equipment replacement & new product line, store remodeling, warehouse expansion, and other corporate purposes. Their long-term aspiration is to expand store network to 2,000 in the next 3 – 4 years or by 2018 while maintaining their ideal ownership mix of 60:40 franchise and company owned.
- **...to protect market leadership.** Increased competition from a number of new convenience store-chain brands also prompted the company to venture outside Luzon (Cebu and Iloilo). The strategic entry into new territories is seen as an opportunity to establish a strong first-mover advantage into unchartered markets. Fierce rivalry for market position is being felt from local convenience store businesses forming joint ventures with foreign store brands (e.g., MiniStop, FamilyMart, AlfaMart, Lawson, All Day Chain).

Our View and Recommendation:

EBITDA can support capex spending. With SEVN's intensive campaign to safeguard market position, net income is seen to register a compounded annuall growth rate (CAGR) of 16.2% for the next two (2) years. Despite having an aggressive expansion strategy, two-year average operating cash flow of Php2.8 billion is adequate to internally fund its annual capital expenditures, which we estimate to range between Php2.0-2.4 billion.

Prudent leverage sustained by equity buildup. Over the medium-term, the estimated yearly net income growth of 18.3% through 2018 and stable profit margins, will help SEVN accumulate retained earnings and cause its D/E ratios to remain within a conservative range of 20%-45%. Sizeable and growing operating cash flows of Php2.5 billion to Php4.5 billion also have the ability to cover interest and dividend payouts by around 12.7x over the next four (4) years.

***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.

SSI Group, Inc.

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EQUITY RESEARCH

Company Background

Established in 1987, Store Specialists, Inc. (SSI) is the leading specialty retailer in the Philippines with an extensive portfolio of established international brands that are supported by a nationwide strategic retail presence. As of March 31, 2015, their retail network consists of 746 stores across the Philippines, including Metro Manila, Luzon, Visayas and Mindanao, with a total gross selling space of 137,746 sqm.

The merchandise sold in their store network covers a broad range of categories and brands, from luxury and bridge apparel to casual wear and fast fashion, footwear, accessories and luggage, food, home and décor, and beauty and personal care. SSI represents 112 brands as of March 31, 2015.

The company has also expanded its retail format offerings with new joint ventures in convenience stores under the "Family Mart" franchise and department stores under the "Wellworth" brand. Family Mart has opened 100 stores as of March 31, 2015, while Wellworth has opened its second store in UP Town Center last May.

Share Data

PSEi Code	SSI
Rating	Outperform
52-wk range (Php)	7.50-11.60
Current Price (Php)	8.43
Target Price (Php)	10.04
Price Upside (%)	19.10
Dividend Yield (%)	0.00
Total Return (5)	19.10

Review of Share Price Performance

SSI surged to a high of Php11.60 at the start of 2015 following solid quarterly earnings results for 2014. The stock however, has sank back to Php8.43 (-37.6%), faster than the PSEi's 9% pull back from its peak of 8,137 on concerns of the potential impact of a weakening euro and a strengthening dollar to its cost of merchandise from Europe and US, as gross profit margins noticeably narrowed to 55.5% for the first 3 months of 2015 from 56.2% in the same period last year. The company however, believes it will not post mark-to-market losses for its inventory from Europe. SSI also clarified that the lower gross margins reflect the higher contribution of the Fast Fashion segment (38% from 36% LY), which has lower margins relative to other categories, but is more efficient in terms of operating expenses. As such, the company showed better EBITDA margins for 1Q'15.

Price Performance

SSI —— PCOMP ——

Source: Bloomberg

Equity Valuation

Comparative Valuation	Closing Price (Php)	Mkt Cap (Php bn)	2015 P/B (x)	2015 P/E (x)	2015 ROE (%)	Div Yield (%)	Free Float* (%)
SM	897.00	720.34	2.64	22.65	11.47%	1.44%	45.98
PGOLD	36.00	99.58	2.62	19.73	14.00%	1.07%	32.63
RRHI	70.65	97.85	2.25	22.06	10.55%	0.75%	37.55
SEVN**	107.00	49.05	11.97	49.53	26.81%	0.37%	32.37
SSI	**8.43**	**27.93**	**2.92**	**22.01**	**13.38%**	**0.98%**	**29.63**

*Sources: Bloomberg; * Philippine Stock Exchange; **BDO PB estimates*
Note: SM – SM Investments, Inc.; PGOLD – Puregold Price Club, Inc.; RRHI – Robinsons Retail Holdings, Inc.; SEVN – Philippine Seven Corp.

▶ **Reasonable valuations...** SSI's current market price of Php8.43 per share translates to reasonable P/E and P/B multiples of 22x and 2.9x respectively, which are comparable with larger-cap peers. SSI however, caters more to the upper to mid-income segments of the retail market, and realizes better net income margins of around 7%-8% compared to the usual 4%-5% of listed local retail players.

▶ **...amid moderating pace of expansion.** After a landmark 2014 that saw SSI go public and spend over Php3 billion to increase its store network by 21% to 723, the company now plans to moderate the pace of its expansion with lower capital expenditure budgets of Php2 billion this year and Php1.6 billion next year. SSI has also cited that store site selection has become more difficult as more retail players compete for commercial space. For the first quarter, the company posted a slower income growth of 22.5% (from 62.5% last year), given its reduced store expansion rate. EBITDA margins however, improved to 21% (from 18%), despite higher merchandise cost given slower escalations for key operating expenses such as rental and personnel costs.

Earnings Results: Full Year 2014, First Quarter 2015

	2013	2014	% chg	1Q'14	1Q'15	% chg
No. of brands	91	106	16.5%	85	112	31.8%
No. of stores	597	723	21.1%	639	746	16.7%
Revenues (Php Mn)	12,788	15,213	19.0%	3,389	4,034	19.0%
Gross profit (Php Mn)	6,292	8,532	35.6%	1,906	2,239	17.5%
EBITDA (Php Mn)	1,551	2,920	88.3%	611	848	38.8%
Net Income (Php Mn)	614	998	62.5%	218	267	22.5%
Gross profit (%)	49.2%	56.1%		56.2%	55.5%	
EBITDA (%)	12.1%	19.2%		18.0%	21.0%	
Net Income (%)	4.8%	6.6%		6.4%	6.6%	

Source: SSI

Our View and Recommendation:

Short-term (less than 2 years): For full year 2015, SSI expects both revenues and profits to grow between 19%-22% on the back of rising consumer affluence. Having established a strong presence in Metro Manila, SSI is also looking to expand its footprint in other developed cities in the country such as Cebu and Iloilo. And based on valuation multiples of 21x P/E and 3x P/B, we derive a target price of Php10.04 in the next 12 months, which translates to a worthwhile potential price upside of 19.1%. **Outperform.***

Medium-term (beyond 2 years): Assuming SSI gradually slows down its store expansion from over 100 new outlets this year to over 60 branches by 2017, earnings growth will correspondingly decelerate from over 20% to probably 16% to 8% in the next 3 to 4 years. Nonetheless, SSI is still expected to outperform most stocks in the PSEi with an estimated annualized price yield of 17.6% considering our target price of Php12.63 by 2017 (based on the same pricing multiples of 21x P/E and 3x P/B). By then, the company may also establish a dividend policy and start paying out dividends to shareholders. For now, we assume that SSI has zero payouts since it has yet to declare dividends as a publicly listed firm. **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)	1,347.1	1,719.6	1,995.2
ROE %	13.2%	14.4%	14.3%
Div / Sh	-	-	-
Div Yd %	-	-	-
BV / Sh	3.1	3.6	4.2
EPS	0.4	0.5	0.6
P/B (x)	2.73	2.34	2.00
P/E (x)	20.73	16.24	14.00

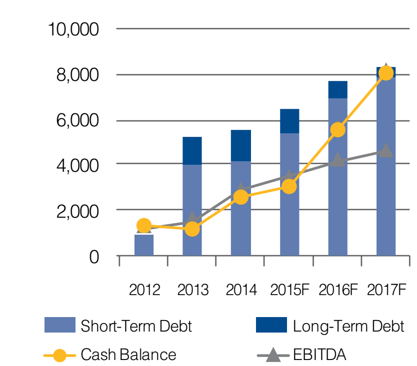
Source: BDO Private Bank Research

Major Shareholders

Major Shareholders	% Stake
Wellborn Trading & Investment	14.10
Marjorisca Incorporated	13.11
Birdseyeview Inc	13.11
Educar Holdings Corp	12.55
Bordeaux Holdings Inc	12.53
Tantoco Sr Bienvenido R	1.81
RBS Luxemburg SA	1.72
Norges Bank Investment	1.26
Baring International Inv	1.12
R Tantoco Ma Teresa	0.98
Others	27.71
Total	**100.00**

Source: Bloomberg

Debt Capacity Chart (Php billions)



Source: Bloomberg, BDOPB Research

Overall, SSI retained its upper medium-grade A rating. Credit is supported by its: 1) positive earnings outlook with EBITDA flows growing from Php3.5 billion to Php4.5 billion in the next 3 years; 2) adequate liquidity with working capital ratios of 1.4x on average; and 3) prudent leverage position with D/E ratios below 65%. Nevertheless, the company has to manage and constantly monitor: 1) execution risks of new brand launches considering the very dynamic and competitive retail landscape; and 2) increasing holding costs in case of rising inventory levels.

FIXED INCOME RESEARCH

Financial Highlights (Php millions):

	2012	2013	2014	2015F	2016F	2017F
Cash	1,256	1,135	2,528	2,981	5,518	8,061
Receivables - net	5,770	6,398	8,565	9,207	9,987	10,273
Total Assets	9,562	11,878	18,060	20,541	24,121	27,263
Current Liabilities	7,418	7,650	7,390	8,791	10,929	12,354
Long Term Liabilities	754	1,462	1,798	1,531	1,254	975
Total Liabilities	8,172	9,111	9,188	10,322	12,183	13,329
Total Equity	1,390	2,767	8,872	10,219	11,939	13,934
Short-term Debt	673	3,919	3,925	5,193	6,779	7,763
Long-term Debt	0	1,174	1,492	1,163	835	506
Total Debt	673	5,094	5,417	6,356	7,614	8,270
Debt to Equity (%)	48.4%	184.1%	61.1%	62.2%	63.8%	59.3%
Net Debt to Equity (%)	-42.0%	143.1%	32.6%	33.0%	17.6%	1.5%
Debt to Assets (%)	7.0%	42.9%	30.0%	30.9%	31.6%	30.3%
Net Interest Expense	8	88	277	301	375	442
EBITDA	1,223	1,551	2,920	3,535	4,137	4,569
EBITDA % Increase	51%	27%	88%	21%	17%	10%

Source: SSI; F – BDO Private Bank Research

▶ **Increasing short-term debt to fund inventory purchases...** SSI has increased its short-term loans payable by 14% to Php4.1 billion as of end-March 2015 from end December 2014 level, proceeds from which supported the purchase of inventory, which correspondingly grew 12% to almost Php9 billion during the same period. The company normally maintains an inventory level of 11 to 14 months depending on the season and line-up of brand or store launches that typically require a higher stock level.

▶ **...as SSI builds up brand portfolio.** SSI added 15 brands and 126 stores in 2014, which increased its inventory level to almost 13 months from 11 months in 2013. Stock buffering due to Manila's port congestion may have also contributed to the company's higher inventory. Meanwhile, SSI added 7 new brands during the first quarter - bridge brand Max & Co; accessories brands Charming Charlie and Radley; and footwear brands Amazonas, Jelly Bunny, Kurt Geiger and Lipault. SSI president Anton T. Huang said "Most of them will open early next year due to the cycle of ordering. Some of them, about 3 or 4, will open by the second half of the year."

Our View and Recommendation:

Steady EBITDA growth and equity accumulation... We expect SSI to produce double-digit EBITDA growth through 2017, with projected operating cash flows of Php3.5 billion to Php4.5 billion sizeable enough to internally fund its planned annual capex of Php1.5 billion to Php3 billion and support working capital needs. As such, we expect the company to maintain a conservative leverage profile with a projected D/E range of 60%-65% as it continues to accumulate retained earnings and entails little incremental debt.

...sustains operational liquidity and a sound balance sheet. Ample operating cash flows also generate healthy interest coverage ratios of over 10x, and sustain adequate working capital ratios of 1.4x on average.

***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.

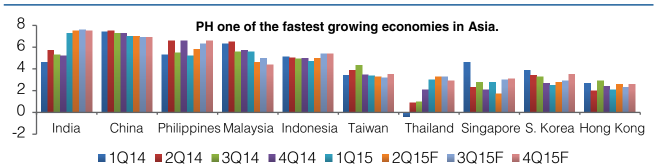
Retailing in the deep

By Roxanne Olanday

The year was 2010 — It was the best of times. It was the worst of times. The world was still reeling from the financial crisis that struck the United States of America, much of Europe, Japan and China. Meanwhile, a tiny archipelago in the Pacific was preparing for the 15th general elections of its country. A politician, whose family name was well-known nationwide, soon assumed presidency of the Philippines. In that same year, foreign brands like BonChon, Muji and Forever21 took the Philippine retail industry by storm, becoming the second batch of international names to set up shop in the country.

It is little wonder why global mid-range brands such as H&M and UNIQLO and luxury brands like Jimmy Choo and Hermès alike seek to set up shop in the country once dubbed as the Pearl of the Orient. An estimated 200 international brands have set foot on Philippine soil since 2008 with about 45 newbies entering just last year. Among its regional peers, the Philippines remains one of the fastest growing countries, posting an average economic growth of 6.28% over the past 5 years, with its per capita income rising 49% from US$1,919 in 2008 to US$2,851 in 2014.

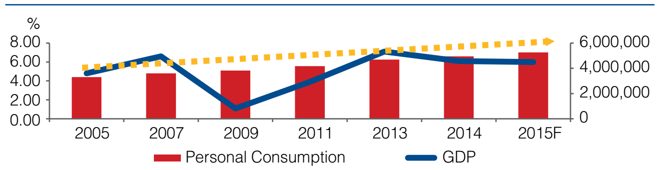
2014-2015 Quarterly GDP Growth Comparison of Key Asian Countries



Source: Bloomberg LP, BDO estimates

Meanwhile, consumer spending remains the lifeblood of the Philippine economy, steadily expanding by 5.6% on average from 2010-2014, and consistently contributing an estimated 70% of the gross domestic product. On top of this, the country has garnered investment grade ratings from premier credit agencies over the years, attracting foreign investors left and right. In fact, advisory firm CB Richard Ellis (CBRE) Philippines ranks the country 13th among the world's target cities for international retail brands. With these in consideration, Philippine Retailers Association expects that in a decade, the retail sector's contributions to the gross domestic product would grow to 20% from 13% in 2014.

Philippines GDP Growth and Personal Consumption 2005-2014



Source: Bloomberg LP

According to population reports by the Philippine Statistics Authority (PSA), the local working age population of 15 to 64 years old made up 63% of all Filipinos in 2010 and bulk of this, at 60% share, were within the 20 to 44 age group. Slated to jump 50% to 53 million people by 2040, we see this young group as the driving force of retail consumption.

Philippines Population Projection 2000-2040 (In Thousands)

Year	Working Age Population (15-64 Yrs. Old)	20-44 Yrs. Old.	Under 30 Yrs. Old.	Total Population
2000	45,453	27,904	26,838	76,947
2005	51,869	35,202	26,353	85,263
2010	58,798	35,202	26,353	94,014
2015	65,286	39,051	28,099	102,968
2020	71,717	42,563	29,476	111,783
2025	78,019	45,683	30,743	120,226
2030	84,088	48,526	32,255	128,110
2035	89,683	50,874	33,387	135,302
2040	94,731	52,697	33,912	141,671

Source: PSA

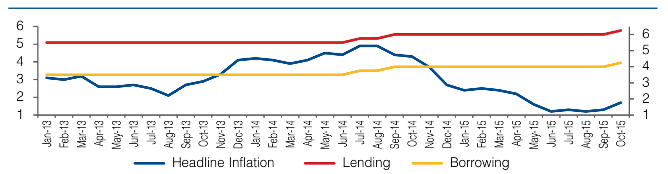
This is important to note given the rise and continued growth of the business process outsourcing (BPO) industry and overseas Filipino worker (OFW) remittances. Both have invariably nurtured the middle class — families whose per capita income range between Php65,787 to Php805,582 — and increased their capacity and propensity to spend. An estimated 2.3 million OFWs sent home cash remittances totaling US$26.97 billion last year. Meanwhile, the BPO sector has also continued to expand at a compounded annual growth rate of 30% from 2010-2014 to contribute revenues of US$18.40 billion in 2014. The BPO workforce responsible for this has likewise swelled from 536,128 people in 2010 to an estimated 1.00 million in 2014 and is even eyed by the Information Technology and Business Process Association of the Philippines (IBPAP) to grow 20% this year to 1.2 million BPO employees nationwide.

Real estate developers and retailers alike appear to be making the most of this steadily growing middle class as can be seen by the proliferation of shopping malls in the metro and nationwide. While Metro Manila leads with a cumulative 6.5 million square meter shopping area that may grow by another half million in 2 years' time from ongoing mall and housing development projects, cities like Cebu, Davao, Bacolod and Clark are becoming preferred areas for commercial developments.

These developments have seen a drastic change in strategy and design as developers seek to accommodate the shift in consumer dynamics due to the gradually expanding middle class. City centers are now littered with high rise condominiums as BPO workers like call center agents, given their unconventional working hours, prefer to live nearer their place of work. In other cases, especially for the upper middle class, the congestion and heavy traffic in the metro drive them to live either in nearby provinces or the suburbs. Consumers here are more focused on their 'quality of life', deciding for a less chaotic environment to raise their families. For both instances, we would find the new trend of integrated development projects also known as 'self-contained communities' where residential properties, offices, schools and shopping centers surround each other and create convenient pocket communities where everything is near each other and function around that proximity aspect. For instance, Ayala Land Inc.'s Arca South is a 74-hectare development near Bonifacio Global City, Taguig. It has 3.6 million square meters of commercial and residential floor space to accommodate 60,000 residents and around 400,000 officer workers, as well as 260,000 square meters of shopping mall space. Similarly, shopping malls nowadays not only house clothing shops and restaurants, but also contain bowling lanes, cinemas, skating rinks, playgrounds and food courts. Larger malls like the SM Group's SM North EDSA in Quezon City and SM Mall of Asia in Pasay City, see over half a million people (on weekends) and about 300,000-400,000 (on weekdays) visit them daily to enjoy all these mall amenities and facilities.

Aside from the solidly growing BPO sector and OFW cash remittances, other striking points to consider are the current low interest rates and low inflation. The Bangko Sentral ng Pilipinas (BSP), the Philippines' central bank, has kept overnight borrowing and lending rates at 4.0%and 6.0% respectively, since September last year. Initially, the monetary board gradually raised interest rates to curb the slowly rising inflation, which stayed on the 4.0% level for over 9 months, from December 2013 to September 2014, and peaked at 4.9% in July and August. At that time, inflation was driven by global supply pressures that began to ease shortly after the collapse of oil prices, and to this day remains low and is expected to stay that way in coming months. A low inflation environment is significant to the retail discussion because of its 'wealth effect', or the change in spending behavior that accompanies a change in perceived wealth. Basically, low inflation means low overall prices. This subliminally pushes consumers to spend more because it makes people feel 'wealthier' when goods and services are more affordable.

Philippine Inflation and Overnight Lending And Borrowing Rates 2012-2015



Source: BSP, Bloomberg, BDO estimates

All in all, the Philippines is seen to be reaching a 'demographic sweet spot' or a situation in which most of the population is employable, thus making for a larger labor force that could drive the economy. Should both cash remittances and the BPO sector continue on its growth trajectory, coupled with the low-interest rate and inflationary environment, we can expect an ever expanding and flourishing retail sector. This would be even more evident upon the completion of the ASEAN Economic Integration in the coming years as there may be more foreign retailers and brands lining our malls and shopping centers.