Recommendation: Subscribe - Trading Buy

CHP: Third largest cement producer (20% market share), to increase capacity by 26% to 7.2mn tonnes by 2019; cites short-term margin compression before new capacity

- CHP is the third largest producer in the Philippines with 20% market share, operating 2 cement plants with aggregate installed annual capacity of 5.7 million tonnes of cement. CHP markets cement and cement products through direct sales using an extensive marine and land distribution network; and aims to be a construction solution provider. The company is set to increase capacity by another 1.5 million tonnes (+26% to 7.2 million tonnes) by 2019. The company however cited possible margin compression due to importation, having supplied 5 million tonnes in FY15, close to capacity.

High valuation concern addressed with IPO priced at lower end of range - 10.75/sh;
CHP P/E higher than local peer, but lower than regional peer average

- Previous IPO price at 17/sh garnered concerns regarding lofty valuation CHP provides exposure to the local cement industry with only one available listed comparative: HLCM yields a lower 2016 est. P/E at 15.67x at but also has illiquidity concerns due to a low public float at only 14.26%, despite a larger market cap at P97 billion.
- Our regional peer comparative shows that at 10.75/sh, CHP 2016 est. P/E at 18.67x is lower than average 22.94x.

Net Proceeds est. of P20.12 billion to pare down Net Debt/EBITDA to 2.6x

- Gross Proceeds P21.85 billion, Est. Net Proceeds P20.12 billion to pay off short-term loan with CEMEX subsidiary NSH.
- Pay outstanding amounts under short-term loan from CEMEX subsidiary NSH of up to $504 million or P23.77 billion; or any debt used to refinance the short-term loan as partial payment for the long-term loan from NSH of P353 million or P16.65 billion.

Debt Incurred at favorable terms from subsidiary of parent; related to beneficial re-organization
Parent deleveraging / divesting via IPO

- Debt incurred at favorable terms from subsidiary of parent (no penalties) - $504 million or P23.77 billion short-term (5.21%, due July 9, 2016) and $353 million or P16.57 billion long-term (7.53% due 2020-2023) - was in connection with its "Re-rganization" which resulted to a combined benefit of P3 billion, improving EBITDA margin to 25% (proforma) from 12.2%.
- The re-organization involved (a) Restructure of royalty arrangements with CEMEX, lowered from 12-13% of sales to 5%. (b) Implement planned insurance strategy.
- Last year, Cemex SAB with an est. Debt/EBITDA of 5.17x as of 1Q16 said it would sell as much as $1.5 billion assets to cut debt and restore investment-grade capital structure. Post-IPO Cemex SAB will retain 55% stake.

IPO: CEMEX Holdings Philippines, Inc.	
Ticker	CHP
Offer Shares	2,337,927,954 (45% of Outstanding Shares)
Offer Price	10.75/sh
Par Value	1.00/sh
Minimum Subscription	100 shares; multiples of 100 thereafter
Issue & Outstanding Shares Post-Offer	5,195,395,454
Market Capitalisation (IPO)	55,850,501,130.50
Authorized Capital Stock	5,195,395,454
Gross Proceeds	21,854,543,922.50
Est. Net Proceeds	20.12 billion
Offer Period	July 4 - 11
Tentative Listing Date	July 18

Regional Peer Comparative (as of end-1Q16)

Company	Ticker	MKT CAP (Php)	P/E est. 2016
HOLCIM PHILIPPINES INC.	HLCM PM	97.43	15.67
SHAANXI QINLING CEMENT	600217 C	72.16	30.60
LAFARGE SURMA CEMENT LT	LAFCEM BD	55.31	26.82
CEMEX HOLDINGS PHL	CHP PM	55.85	18.67
AVERAGE		70.18	22.94

Scenario for the long-term investor: Increased capacity amid supply deficit by 2019; but no dividend policy in place

- A boost in capacity by 2019 and as a deficit emerges in the industry will be favourable to prices/margins. Notably, however, the company currently has no dividend policy in place.
- The cement industry is estimated to grow by CAGR 8.4% from 2015 - 2020. GDP to infrastructure spend is estimated to grow to 5% by 2018 or possibly 7% as targeted by the new administration. Philippines has one of the lowest cement consumption per capita at 215kg.
- Current industry capacity is in surplus of 2.2 million tons but is estimated to swing to a deficit of 3.2 million by 2019, even as 4.6mn tonnes of known new capacity is expected to be installed.

Income Statement					
in millions	2013	2014	2015	Proforma 2015	1Q16
Net Sales	16,776	19,496	23,937	23,937	6,328
Cost of Sales	-9,075	-10,391	-12,022	-12,268	-3,231
Gross Profit	**7,701**	**9,104**	**11,914**	**11,668**	**3,096**
Operating Expenses	-6,911	-8,214	-9,861	-6,732	-2,563
Operating Income before other expenses, net	**789**	**890**	**2,053**	**4,936**	**533**
Other income (expenses), net	-129	-59	787	787	8
Financial expenses and other financial expenses, net	-24	-58	-65	-1,359	-20
Foreign Exchange gain (loss)	277	-17	69	-763	-196
Earnings before income tax	**914**	**755**	**2,844**	**3,600**	**323**
Income Tax	-461	-249	-661	-587	-109
Net Income	**453**	**506**	**2,183**	**3,013**	**214**

Financials from 2013-2015

- Sales CAGR 19%, P23.93bn (2015), EBITDA CAGR 43%, P6.04bn (2015), Net Income CAGR 76%, P2.2bn (2015)
- Sales of cement and cement products accounted for 97.9% of combined net sales before eliminations resulting from combinations for fiscal 2015 and 98.1% of consolidated net sales for 1Q16. As of end-2015, bag cement accounted for over 80% of combined cement sales. As of 1Q16, bag cement accounted for 78% of consolidated cement sales. Net Income for 2015, improved from P506.6 million to P2.2bn primarily due to an improved gross profit margin and the re-organization (read more below).

Industry and Other Players

- Other significant cement players include Holcim Philippines and Republic Cement & Building Materials Incorporated (formerly Lafarge Republic Inc.), now owned by AEV-CRH Holdings Incorporated.
- Total industry capacity 29.5 million tonnes but effective capacity (90%) is at 26.6 million tonnes. In 2015, cement sales rose 14.3% to P24.4 million. Currently, companies are expanding capacity which usually takes 3 years to build. By 2019, an additional 4.6 million tonnes are expected to total 34.1 million tonnes, but with an effective capacity (90%) of 30.7 million tonnes, resulting to an est. deficit of 3.2 million tonnes.
- Over the past 10 years the cement industry has outpaced GDP with an average growth 7.8% vs. 5.4%. Cement has grown 11.6% to 24.4%, GDP 4.5% to 7.6%.
- GDP to Infrastructure spending has grown form 1.8% (2010) to 5% (2016) to est. 5.4% (2018), maybe soon it could increase to 7% under new administration.
- Cement consumption has grown a CAGR 9.1% form 2009-2015, estimated to grow a CAGR 8.4% from 2015 - 2020. And yet Philippines has one of the lowest cement consumption per capita at 215kg vis-a-vis Indonesia 230kg, Cambodia 240kg, Laos 430kg, Vietnam 560kg, Thai 600kg.

Cemex Holdings (Ticker: CHP) is the newly-formed subsidiary of Cemex Asian South East Corp., a wholly-owned indirect united of Cemex España, S.A., which in turn is indirectly owned by Cemex, S.A.B. de C.V. based in Monterey Mexico, one of the largest cement companies in the world.

- Last year, Cemex SAB said it would sell as much as $1.5 billion assets to cut debt and restore investment-grade capital structure. Cemex SAB agreed to sell $400 million of US properties in May following a $53 million million agreement to dispose of its Bangladesh and Thailand operations announced in March.
- Post-IPO Cemex SAB will retain 55% stake.

CHP is one of the leading cement producers in the Philippines with 20% market share, operating 2 cement plants with aggregate installed annual capacity of 5.7 million tonnes of cement as of 1Q16. Markets cement and cement products through direct sales using an extensive marine and land distribution network. CHP aims to be a construction solution provider.

Cement subsidiaries have been operating in the Philippines for over 17 years with well-established brands "APO," "Island" and "Rizal"

- APO Cement plant in Cebu has three grinding lines and has an installed annual capacity of 3.8 million tonnes of cement,serving customers in the Visayas and Mindanao.
- Solid Cement plant in Rizal currently has three grinding lines and an installed annual capacity of 1.9 million tonnes of cement, plans to install a new integrated cement production line to provide approximately 1.5 million tonnes of additional capacity per year by 2019, serving the NCR. Come also has one ready-mix plant located in Manila and an admixtures facility located in Parañaque.

Distribution infrastructure includes 4 marine distribution terminals and 16 land distribution centers across the Philippine. Uses own fleet and third party transport to distribute.

- Leased 850 trucks for the distribution of bag and bulk cement, 23 ready-mix concrete mixer trucks; chartered 57 marine vessels for the waterborne distribution of bag cement; contracted 5 marine vessels to augment fleet of 2 owned marine vessels for the distribution of bulk cement

Background on Cemex in the Philippines

- Cemex Initially entered the Philippine market in 1997 with a minority investment of 30% in Rizal Cement Company (est. 1930). Solid Cement, a subsidiary of Rizal Cement at the time, was eventually merged with parent Solid Cement.
- In 1999, Cemex, together with another investor, bought an aggregate 99.9% interest in APO Cement.
- In May 2015, Cemex announced it was undertaking a new $300 million investment in the Philippines, including the construction of a new 1.5-million-ton, integrated cement-production line at the Solid Cement plant in Luzon and representing 25% increase in the company's cement capacity in the Philippines.
- In January 2016, acquired, directly and indirectly through intermediate holding companies, a 100% equity interest in each of Solid Cement and APO Cement.

Strengths

- Leading cement producer in the Philippines anchored by well-regarded brands
- Customer-centric direct sales approach supported by extensive distribution infrastructure
- Track record of innovation with a broad product offering
- Strategically located plants and infrastructure
- Cost-effective producer with highly efficient operations
- Benefit from synergies with CEMEX, a world-class operator
- Experienced and dedicated management team

Strategies

Core elements include Health and Safety, Customer-Centricity, Increasing Efficiencies, Cost Reduction and Pricing Initiatives.

- Expand capacity to capture growth opportunities in the attractive markets of the Philippines
- Continue to enhance profitability by increasing operational efficiency at our plants
- Further strengthen our distribution network
- Continue developing and introducing innovative solutions for our customers
- Foster sustainable and socially responsible development