

Aboitiz Power Corp (AP PM)

Greener pastures

Multi-year catalysts; re-initiate with BUY

We reinitiate coverage on AP with a BUY. Our SOTP-TP of PHP42 implies 27% upside potential (including FY22E dividend) and a trailing FY22E PER of 14.6x, slightly above its 5Y average of 13.8x but justified by growth prospects. We forecast FY22/23E earnings growth of 20%/19%, driven by profit streams from repaired and new coal capacities and its PHP190b plan to develop 3.7GW of renewable energy (RE) projects by FY30E. Our TP is based on the sum of the DCFs of AP's subsidiaries, using a dynamic WACC of 6.3-6.7% for RE and 6.1-7.0% for non-RE and distribution utility.

Beneficiary of power demand recovery

Maybank IBG Research expects the Philippines to post GDP growth of +7.0/+6.2% in FY22/23E, spurred by household spending and investment, which should drive electricity sales for both AP's generation and distribution units. We expect continued supply tightness in Luzon to bode well for AP's new capacity in FY22/23E.

Immediate earnings uplift from coal plants

Our FY22E earnings reflect the resumption of GMEC Unit 1 (316MW) operations, which had an unplanned outage during Jan-Oct 2021, in Feb 2022 but excludes the PHP911m (USD18m)/PHP500m (USD9.5m) GMEC/Manolo Fortich insurance claims proceeds, which AP expects to collect within FY22. Our forecast also factors in the start of GNP Unit 1's PSAs in Jan 2022 and commercial operations of the GNP Unit 2 by 4Q22. We estimate GMEC and GNP to cumulatively account for 26%/28% of our FY22E EBITDA/earnings. We estimate PHP3.3b additional net income from GMEC and GNP in FY22E, 16% of total FY22E earnings.

Strong RE pipeline until FY30E

AP is targeting a 50-50 traditional-RE generation portfolio mix by YE30E. To achieve this, we estimate it needs to deliver 3.7GW of new attributable RE capacity to balance out its 3.5MW of coal/oil assets and incoming 1GW LNG. We believe this aggressive 3.7GW RE pipeline is achievable given AP's successful track record, robust balance sheet and strong technical partners, such as JERA. Our forecasts only factor in 839MW disclosed RE projects for COD by FY25E, while we expect the rest in FY25-30E. This 3.7GW accounts for 10% of our TP.

| FYE Dec (PHP m) | FY19A | FY20A | FY21E | FY22E | FY23E |
|------------------------------|---------|---------|---------|---------|---------|
| Revenue | 125,635 | 110,377 | 124,974 | 129,819 | 132,508 |
| EBITDA | 38,752 | 37,853 | 39,311 | 41,843 | 46,292 |
| Core net profit | 15,820 | 11,715 | 17,732 | 21,213 | 25,324 |
| Core EPS (PHP) | 2.15 | 1.59 | 2.41 | 2.88 | 3.44 |
| Core EPS growth (%) | (27.1) | (25.9) | 51.4 | 19.6 | 19.4 |
| Net DPS (PHP) | 1.47 | 1.18 | 0.85 | 1.45 | 1.50 |
| Core P/E (x) | 15.9 | 16.7 | 14.2 | 11.9 | 10.0 |
| P/BV (x) | 2.0 | 1.5 | 1.8 | 1.6 | 1.5 |
| Net dividend yield (%) | 4.3 | 4.4 | 2.5 | 4.2 | 4.4 |
| ROAE (%) | 13.7 | 10.0 | 15.5 | 15.0 | 15.8 |
| ROAA (%) | 4.0 | 2.9 | 4.4 | 5.2 | 5.9 |
| EV/EBITDA (x) | 10.6 | 9.3 | 10.2 | 9.7 | 8.8 |
| Net gearing (%) (incl perps) | 112.9 | 111.7 | 92.1 | 86.4 | 74.8 |
| Consensus net profit | - | - | 20,837 | 20,505 | 22,467 |
| MKE vs. Consensus (%) | - | - | 0.0 | 7.9 | 12.7 |

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BUY

Share Price PHP 34.30
12m Price Target PHP 42.00 (+27%)

Company Description

Second largest power generation and distribution company in the Philippines

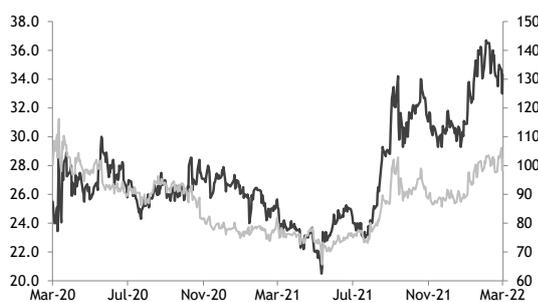
Statistics

| | |
|------------------------|----------------------|
| 52w high/low (PHP) | 36.70/20.50 |
| 3m avg turnover (USDm) | 1.4 |
| Free float (%) | 20.0 |
| Issued shares (m) | 7,359 |
| Market capitalisation | PHP252.4B USD4.8B |

Major shareholders:

| | |
|-------------------------|-------|
| Aboitiz Equity Ventures | 52.0% |
| JERA Asia Private Ltd. | 27.0% |
| Vanguard Group | 0.6% |

Price Performance



| | -1M | -3M | -12M |
|-----------------------|-----|-----|------|
| Absolute (%) | (4) | 8 | 37 |
| Relative to index (%) | 1 | 11 | 28 |

Source: FactSet

Acronyms used:

BSP - Bangko Sentral ng Pilipinas
CFB - Circulating Fluidized Bed
CSP - Competitive selection process
DOE - Department of Energy
DU - Distribution utility
ERC - Energy Regulatory Commission
FIT - Feed in tariff
GEAP - Green Energy Auction Program
GEOP - Green Energy Option Program
GMEC - GNPowr Mariveles (2x316MW; coal)
GNPD - GNPowr Dinginin (2x668MW; coal)
LNG - Liquefied natural gas
NERC - North American Electric Reliability Corporation
NGCP - National Grid Corp. of the Philippines
PSA - Power supply agreement
RE - Renewable energy
RES - Retail Electricity Supplier
RPS - Renewable Portfolio Standard
TLI - Therma Luzon Inc. (2x350MW; coal)
TSI - Therma South, Inc. (300MW; coal)
TVI - Therma Visayas, Inc. (340MW; coal)
WESM - Wholesale electricity spot market

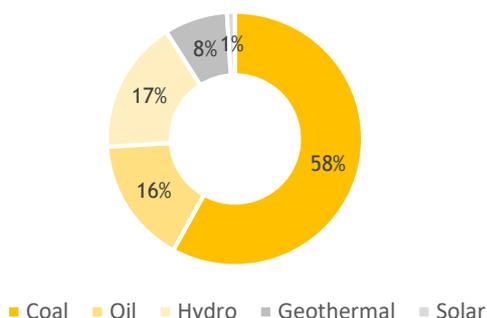
Stocks mentioned:

Aboitiz Equity Ventures (AEV PM, CP:PHP59.90, Not rated)
JERA Co Ltd (ticker, CP: ¥385.00, Not rated)
Meralco (MER PM, CP:PHP368.00, BUY, TP:PHP324.00)

Value Proposition

- AP is a vertically integrated power generation and distribution company with the Philippines' second-largest combined net attributable capacity of 3,495 MW in coal, oil, geothermal and hydro as of Dec 2021.
- AP also owns nine distribution utilities that operate across the country, including the second and third-largest ones.
- Portfolio scale and diversity will differentiate it from other generation companies in terms of reliability, flexibility, and its ability to offer RE-based generation.
- AP aspires to increase attributable capacity to 9.2GW with a 50/50 thermal to clean energy mix by FY30.

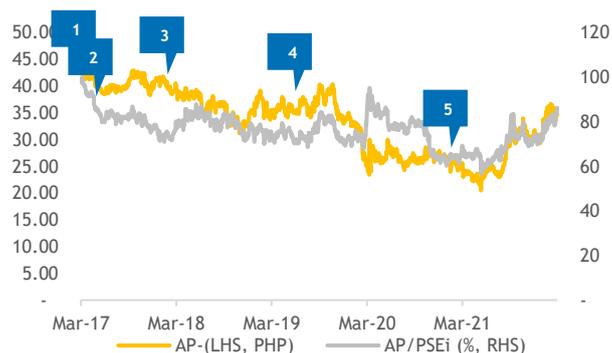
Attrib. Net Sellable Capacity (as of Dec 2021)



Source: Company

Price Drivers

Historical share price trend



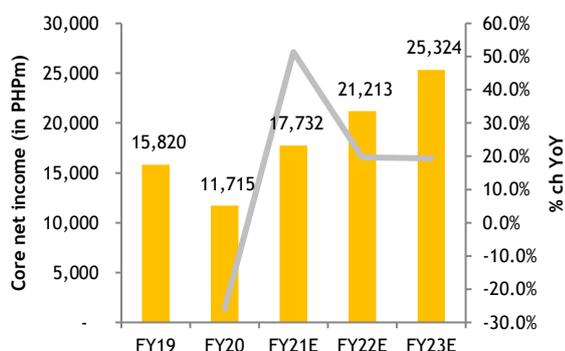
Source: Company, Maybank IBG Research

- AP inaugurates Therma South's 300 MW CFB coal fired power plant in Davao City on Jan 2016.
- AP acquired a 66.1% interest in 604 MW GMEC and 40% in 2x668 MW GNPD from Blackstone group for USD1.2b.
- AP acquired 59MWp SacaSun, its first venture into solar power generation.
- AP further acquired a 49% voting and 60% economic stake of Ayala Corp (AC PM) in AA Thermal for USD579.2m.
- JERA Asia Pte. Ltd. Share purchase agreement with AEW for 25.01% of AP for USD1.46b.

Financial Metrics

- We expect FY22E core income to grow 20% due to improvement in revenue contribution of both its power generation and distribution businesses while both GNPD Units 1 and 2 (equitized) become operational within FY22.
- On top of potential capital appreciation, AP offers a yield of 4.2%/4.4% in FY22/23E.
- Our TP of PHP42.0 is based on the discounted cashflow of AP's subsidiaries, using a dynamic WACC of 6.3-6.7% for RE and 6.1-7.0% for non-RE and distribution utility.

Core Net Income (in PHPm)



Source: Company, Maybank IBG Research

Swing Factors

Upside

- Securing portions of MER's future CSPs due to tight baseload supply in Luzon could mitigate offtake risk while providing predictable cash flows.
- Higher WESM prices may be beneficial to earnings if AP's uncontracted capacities are net sellers to spot market.
- Strategic partnership with JERA resulting in faster and higher-quality execution of future RE/LNG pipeline.
- Expanding market share in the RES market.

Downside

- Prolonged forced outages of its power plants.
- Oversupply situation could expose gencos that sell at the spot market to increased off-take risk and soft spot prices.
- Inability of GNPD Unit 2 and new RE projects to secure contracted capacity.

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| | |
|--|------------------|
| Risk Rating & Score ¹ | 33.4 (High risk) |
| Score Momentum ² | -0.5 |
| Last Updated | 11 Feb 2022 |
| Controversy Score ³ (Updated: 30 Jul 2021) | 2 (Moderate) |

Business Model & Industry Issues

- Aboitiz Power's balanced portfolio of thermal assets, in addition to its aggressive RE target of 3.7GW, positions it to benefit both on a short-term and long-term horizon.
- While members of the Aboitiz family feature heavily in both the BOD and Executive Committee, AP is the only constituent of the FTSE4Good Index from the Philippine power sector, which is a testament to its strong ESG practices. It has been in the index since 2018, allowing it to capture investments from funds tracking the index.
- Currently, AP has the highest Philippine-based operating attributable RE capacity at 928 MW, ahead of FGEN and ACEN. AP strives to maintain a balanced portfolio and has set a target of increasing attributable capacity to 9,200MW with a 50-50 thermal-clean energy mix by 2030.
- AP garnered a Sustainalytics score of 33.4 in 2022, considered High Risk due to inherent exposure to coal-fired power plants (57% of total portfolio in 2021). Nevertheless, it garnered the highest Sustainalytics ESG management score so far among Philippine power companies in 2022 on the back of its ISO-certified asset and environmental management systems, highly-transparent and timely disclosure processes and aggressive 3.7GW RE pipeline.

Material E issues

- AP was the first in Asia to issue a green/climate bond, raising PHP12.5b in 2016 to refinance the loans used for the rehabilitation of the Tiwi-Makban geothermal facilities and free up cash for other RE investments.
- AP spent PHP231m in 2020 (1% of pre-tax profit) for CSR efforts with the bulk going towards environmental efforts. AP, together with the rest of the Aboitiz group, has planted a total of 11.7m trees to date, with 4.5m trees planted in 2020, in a bid to offset its carbon emissions.

As part of the Aboitiz group, AP participates in AEV's Apark program, various coastal and river clean-up activities, and biodiversity initiatives. Key initiatives for the group include (i) the Aboitiz Cleanergy Park, a mangrove reforestation site, nursery and botanical garden for 29 native tree species and 100 species of birds, (ii) the Balabag Wetland Park rehabilitation in Aklan, (iii) the San Juan river rehabilitation and (iv) the Calubcub II: Pawikan Conservation.

Material S issues

- AP reported 0 fatalities among its employees since 2016 but accounted for 11 deaths among contractors (2016- 2019) who are under its "prevailing influence."
- The group spent PHP423m on CSR initiatives in 2020. In total, the Aboitiz group served 445,697 beneficiaries through 1,519 projects amidst the pandemic.
- In compliance with Energy Regulations No. 1-94 (ER 1-94) which stipulates that host communities will get a share of one centavo for every kilowatt-hour (PHP0.01/kWh) generated by power plants operating in its area. AP has remitted PHP153m in 2020, in addition to around PHP504m outstanding funds to its host beneficiaries.
- There are 2,940 employees as of 2020, the majority of whom are male (72%). Males account for 70% of AVP and higher management positions.

Key G metrics and issues

- The Board of Directors (BOD) is composed of an all-male team of 9 members. Six out of the nine members of the BOD are part of the extended Aboitiz family, while the remaining three are independent directors. In terms of background, five have business backgrounds, 3 engineering backgrounds and 1 social science background.
- Six out of the nine members of the board are part of the extended Aboitiz family. Nevertheless, in Jan 2020, Emmanuel Rubio, AP's long-time Chief Operating Officer who has a background in industrial engineering, was appointed as the President and Chief Executive Officer effective 01 Jan 2020, making him the first president & CEO not related to the Aboitiz family.
- Compensation of AP's officers and directors totalled PHP220m, accounting for 1% of FY20 pre-tax profit.
- Related party revenue transactions, as part of the Aboitiz group, remained insignificant. Even so, AP has a RPT Committee which oversees material RPTs.
- SyCip Gorres Velayo & Co., a member firm of Ernst & Young, has been AP's external auditor for at least the past 10 years. Audit fees in FY20 totalled PHP8.7m, accounting for just 0.04% of FY20 pre-tax profits.

¹**Risk Rating & Score** - derived by Sustainalytics and assesses the company's exposure to unmanaged ESG risks. Scores range between 0 - 50 in order of increasing severity with low/high scores & ratings representing negligible/significant risk to the company's enterprise value, respectively, from ESG-driven financial impacts. ²**Score Momentum** - indicates changes to the company's score since the last update - a **negative** integer indicates a company's improving risk score; a **positive** integer indicates a deterioration. ³**Controversy Score** - reported periodically by Sustainalytics in the event of material ESG-related incident(s), with the impact severity scores of these events ranging from Category 0-5 (0 - no reports; 1 - negligible risks; ...; 5 - poses serious risks & indicative of potential structural deficiencies at the company).

1. Investment thesis

1.1 Diversified power giant has strong track record

Aboitiz Power Corp. (AP) is a well-diversified power holdings company with a strong track record given extensive experience operating several of the largest power generation and distribution firms in the Philippines. Its largest shareholder is Aboitiz Equity Ventures (AEV PM), a listed holding company which houses the Aboitiz family's diversified holdings in power as well as in banking, food, real estate, and infrastructure. As of 14 March 2022, Japan-based power giant JERA Co, Inc. (JERA) was AP's second-largest investor, with a 27% economic stake, after a block sale on 16 Dec 2021.

AP's power generation business is the second-largest in the country in terms of installed capacity, with 4,653MW net sellable capacity (3,494MW attributable capacity) as of Dec 2021. This comprises 18% of the 26,286MW of installed capacity in the Philippines (2020).

Fig 1: Power generation portfolio

| Power Source | Plant Name | Net Sellable Capacity (MW) | Ownership | Attributable Capacity (MW) |
|----------------------|-------------------------------|----------------------------|-----------|----------------------------|
| Hydro | Ambuklao | 105 | 50% | 53 |
| | Bakun | 75 | 100% | 75 |
| | Benguet | 53 | 100% | 53 |
| | Binga | 140 | 50% | 70 |
| | Davao 1-5 | 5 | 100% | 5 |
| | Magat | 388 | 50% | 194 |
| | Manolo Fortich | 69 | 100% | 69 |
| | Sibulan (A, B and Tudaya A) | 49 | 100% | 49 |
| | Sabangan | 14 | 100% | 14 |
| | Maris Main Canal 1 Tudaya (B) | 9 | 50% | 4 |
| | | 7 | 100% | 7 |
| Geothermal | Tiwi-MakBan | 290 | 100% | 290 |
| Solar | San Carlos | 46 | 100% | 46 |
| Total RE | | 1,248 | | 928 |
| Coal | Mindanao (STEAG) | 210 | 34% | 71 |
| | GNPower Mariveles | 632 | 78% | 495 |
| | GNPower Dinginin* | 1,336 | 70% | 935 |
| | Davao (TSI) | 260 | 100% | 260 |
| | Pagbilao (TLI) | 700 | 100% | 700 |
| | Pagbilao 3 | 388 | 50% | 194 |
| | Toledo | 216 | 26% | 57 |
| | Cebu (TVI) | 300 | 80% | 240 |
| Total Coal | | 4,042 | | 2,953 |
| Oil | Cebu | 64 | 60% | 38 |
| | Cotabato | 4 | 100% | 4 |
| | General Santos | 55 | 20% | 11 |
| | Mactan | 44 | 100% | 44 |
| | Mobile 1 | 96 | 100% | 96 |
| | Mobile 2 | 96 | 100% | 96 |
| | Mobile 3-6 | 200 | 100% | 200 |
| | Naga | 39 | 100% | 39 |
| Zamboanga | 100 | 20% | 20 | |
| Total Oil | | 698 | | 549 |
| Total Thermal | | 4,741 | | 3,501 |
| Total | | 5,989 | | 4,429 |

AP has the most operational attributable RE in the Philippines among peers at 928MW. However, current mix is skewed to coal, at 67% of its total capacity.

AP's portfolio is 18% of total installed capacity in the Philippines as of 2020.

Source: Company

Note: Includes 2x668-MW GNPower Dinginin with Unit 1 operational, Unit 2 COD by 2Q22*

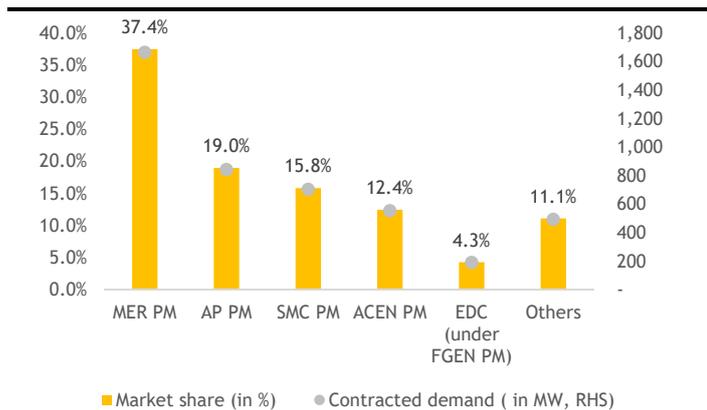
The group's initial foray into power generation was in 1978, via Hydro-Electric Development Corp. (Hedcor), a pioneer investor and industry leader in small to medium hydroelectric plants. 64% of AP's RE capacity is

hydroelectric. Furthermore, its retail electricity supplier (RES) unit has been a market leader since 2013.

Due to the group’s aggressive expansion into power generation, including other RE and baseload coal power, the bulk of AP’s revenues (FY21/22E: 65%/65%) is estimated to be from its power generation/RES segment.

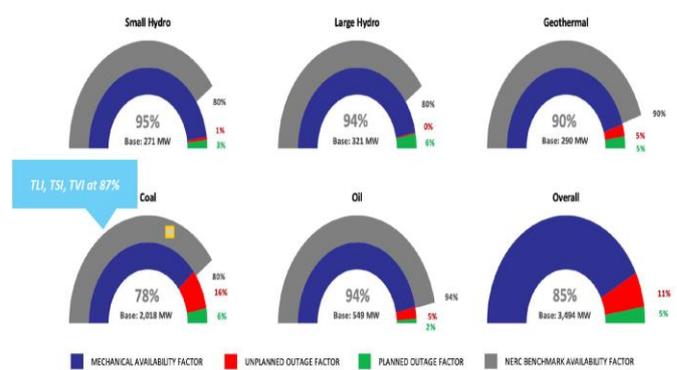
AP also owns nine distribution utility (DU) companies, including the second and third largest ones (Fig 3). The Aboitiz group’s earliest involvement in power involved the Aboitiz family’s acquisition of a 20% interest in the Visayan Electric DU in the 1900s.

Fig 2: AP is second-largest RES player (as of Dec 2021)



Source: Competitive Retail Electricity Market, ERC

Fig 3: Plant availability versus NERC benchmark (as of Dec 2021)



Source: Company

Fig 4: Recent plant outages (as of Feb 2022)

| Power plant | Capacity (in MW) | Type | Start | End |
|-----------------|------------------|---------|-----------|-----------|
| GMEC Unit 1 | 325.8 | Forced | 8-Jan-21 | 18-Oct-21 |
| TVI Unit 2 | 170 | Planned | 24-Jan-21 | 24-Feb-21 |
| TVI Unit 1 | 150 | Planned | 24-Feb-21 | 19-Mar-21 |
| GMEC Unit 2 | 325.8 | Planned | 20-Mar-21 | 3-May-21 |
| CEDC | | Planned | 21-Mar-21 | 10-Apr-21 |
| TSI Unit 2 | 150 | Planned | 10-Apr-21 | 7-May-21 |
| TSI Unit 1 | 150 | Forced | 12-Apr-21 | 18-Apr-21 |
| TSI Unit 1 | 150 | Planned | 12-May-21 | 6-Jun-21 |
| GMEC Unit 2 | 325.8 | Forced | 1-Jun-21 | 8-Jun-21 |
| Pagbilao Unit 2 | 382 | Forced | 2-Jun-21 | 5-Jun-21 |
| TVI Unit 1 | 150 | Forced | 16-Dec-21 | 9-Jan-22 |
| TSI Unit 2 | 150 | Forced | 25-Dec-21 | 12-Jan-22 |
| Pagbilao Unit 3 | 382 | Planned | 8-Jan-22 | 11-Feb-22 |
| GMEC Unit 1 | 325.8 | Forced | 11-Jan-22 | 3-Feb-22 |
| TVI Unit 2 | 170 | Forced | 12-Jan-22 | 17-Jan-22 |
| TVI Unit 1 | 150 | Planned | 15-Jan-22 | 31-Jan-22 |
| GMEC Unit 2 | 325.8 | Forced | 22-Jan-22 | 6-Feb-22 |
| GMEC Unit 1 | 325.8 | Forced | 9-Feb-22 | 14-Feb-22 |
| GMEC Unit 2 | 325.8 | Forced | 10-Feb-22 | 12-Feb-22 |
| GMEC Unit 2 | 325.8 | Forced | 17-Feb-22 | 20-Feb-22 |
| GMEC Unit 1 | 325.8 | Forced | 18-Feb-22 | 25-Feb-22 |

Source: Company, IEMOP*

Fig 5: AP’s DU franchises

| Distribution Group | Franchise Area | Franchise Expiry | Ownership |
|-------------------------|---|------------------|-----------|
| Davao Light | Davao City, Panabo City, others | 2050 | 99.93% |
| Cotabato Light | Cotabato City, portions of Datu Odin Sinsuat and Sultan Kudarat | 2039 | 99.94% |
| Visayan Electric | Cebu City, Mandaue City, Talisay City, others | 2030 | 55.26% |
| San Fernando (SFELAPCO) | San Fernando City, others | 2035 | 43.78% |
| SEZC | Subic Bay Freeport Zone | 2028 | 99.98% |
| MEZC | MEPZ 2 export processing zone | Zone life | 100.00% |
| BEZC | West Cebu Industrial Park | Zone life | 100.00% |
| LEZC | Lima Technology Center, Batangas | Zone life | 100.00% |

Source: Company

AP has a long history of successfully operating power assets within international quality standards:

- All of AP’s generation facilities achieved asset management certifications based on ISO 55001:2014 standard. This implies it has the ability to undertake power supply contracts and guard against regulatory risk and fines. 89% of AP’s 3,753MW capacity sales during FY21 were contracted, either to bilateral or ancillary service contracts, with the balance sold to the WESM;
- DU network availability and reliability targets are aligned with the performance bond standards set by the ERC as part of the Rules

for Setting Distribution Wheeling Rates (RDWR). Visayan Electric and Davao Light, were also among the first few Dus to be certified with an ISO 14000:2015 and ISO 45000:2018 for Occupational Health and Safety, and Environmental Management.

Despite strong asset management programs, AP's power assets must still manage impacts of forced outages due to unforeseen critical equipment issues or natural calamities. As of Dec 2021, most of AP's generation remained compliant with the reliability performance indices set by the ERC by virtue of Resolution No. 10 Series of 2020. Excluding GMEC, the availability of AP's other coal plants stood at 87% (as of Dec 2021), above the 80% NERC benchmark availability factor. This indicates that AP's plant availability across different technologies was generally at par when benchmarked against the historical availability performances, with coal outperforming in FY21. As a secondary mitigant, all generation assets have stand-alone or group insurance coverage, which is designed for each assets' unique risk profiles. DU assets are largely covered by Industrial All Risks (IAR) group insurance.

1.1 Beneficiary of recovering power demand

As an industry leader in the power utilities space, AP stands to be a major beneficiary of positive long-term power market fundamentals. In our view, current supply-demand dynamics are favourable for AP. Peak demand is expected to continue to rebound given its positive directional relationship with macroeconomic drivers, which remain sound, while near-term supply tightness may mean less competition for new supply contracts.

As improving vaccinations have limited the resurgence of severe COVID-19 cases, we expect lockdown restrictions to remain moderate (Alert Level 4 or below) until 1H22, when we expect that at least 70% of the population will have been vaccinated (See *Keeping on Course* report for more).

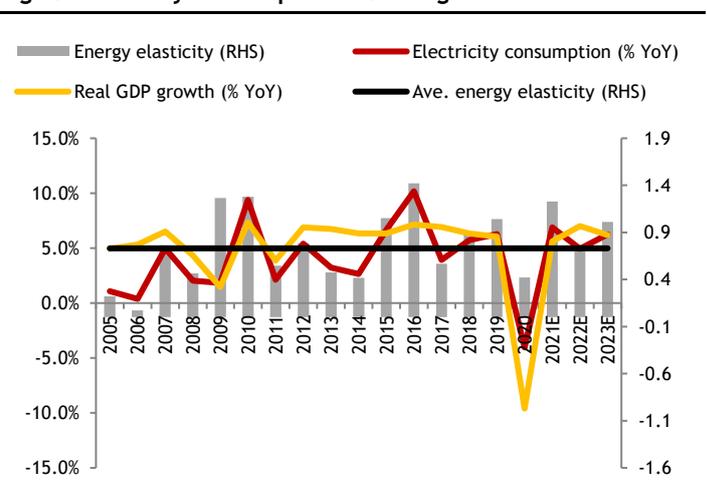
This reopening trajectory should spur household spending and business investment, which is directionally related to electricity consumption. This continued peak demand growth should bode well for both generation/RES and DU segments.

Fig 6: Macroeconomic forecasts

| | FY19 | FY20 | FY21E | FY22E | FY23E |
|------------------------------------|------|-------|-------|-------|-------|
| Real GDP (%) | 6.1 | -9.6 | 5.6 | 7.0 | 6.2 |
| Private Consumption (%) | 5.9 | -7.9 | 4.2 | 6.3 | 6.4 |
| Government Consumption (%) | 9.1 | 10.5 | 7.0 | 5.2 | 4.3 |
| Gross Fixed Capital Formation (%) | 3.9 | -27.5 | 9.6 | 12.8 | 12.7 |
| Exports of Goods & Services (%) | 2.6 | -16.3 | 7.8 | 9.7 | 10.0 |
| Imports of Goods & Services (%) | 2.3 | -21.6 | 12.9 | 11.6 | 12.5 |
| Current Account Balance (% of GDP) | -0.8 | 3.6 | -0.5 | -0.8 | -1.3 |
| Fiscal Balance (% of GDP) | -3.4 | -7.6 | -8.3 | -7.0 | -6.0 |
| Inflation Rate (%) | 2.5 | 2.6 | 3.9 | 3.4 | 2.7 |
| Unemployment Rate (%) | 5.1 | 10.4 | 7.8 | 6.3 | 5.4 |

Source: Maybank IBG Research

Fig 7: Electricity consumption vs. GDP growth



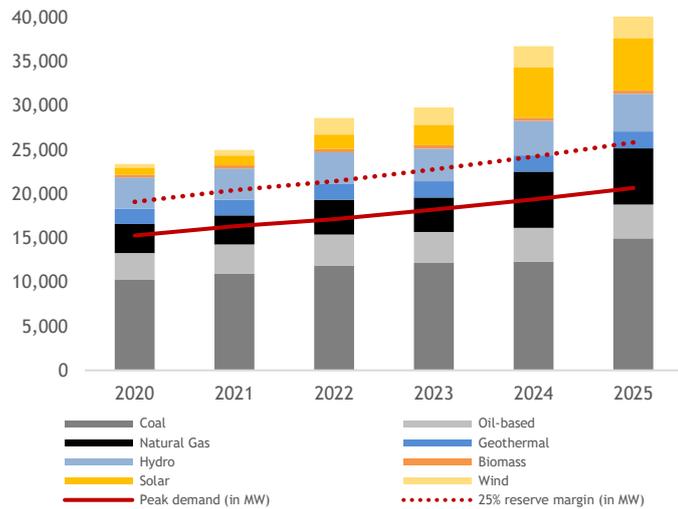
Source: DOE, Maybank IBG Research

We forecast electricity consumption for the Philippines to grow by 6.0% pa from FY21-23E, in line with the forecasts of power grid operator NGCP, which expects national power demand to grow at an average annual

compounded growth rate (AACGR) of 6.23% for FY21E-25E, 6.73% for FY26E-30E and 6.49% for FY31E-40E.

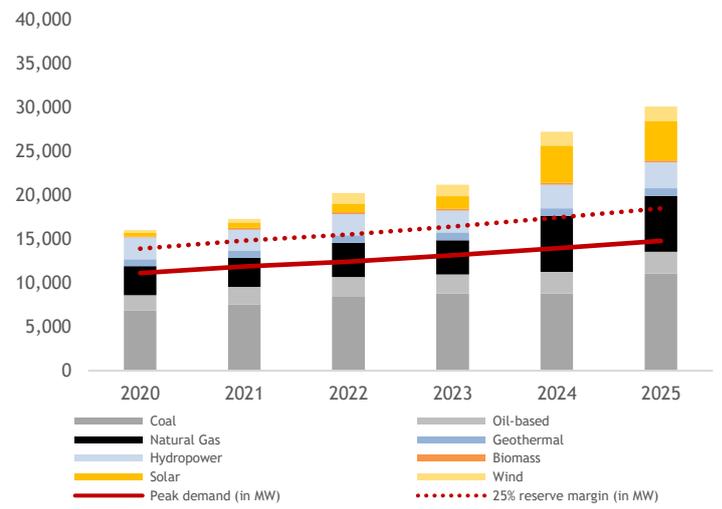
Going into FY22, we expect continued supply tightness in the Luzon power grid – the largest one – which we expect to persist until FY24E. This should ease offtake risks for uncontracted capacities and open opportunities for baseload plants, such as AP’s uncontracted 668MW GNPD Unit 2.

Fig 8: Philippine supply-demand situation manageable...



Source: DOE, NGCP, Maybank IBG Research

Fig 9: ...but near-term Luzon supply tightness seen ...



Source: DOE, NGCP, Maybank IBG Research

1.2 Immediate earnings uplift from coal plants

Despite the ongoing regulatory push to develop new RE capacity in lieu of coal, we expect AP’s existing baseload coal capacity to remain relevant over the next couple of decades given:

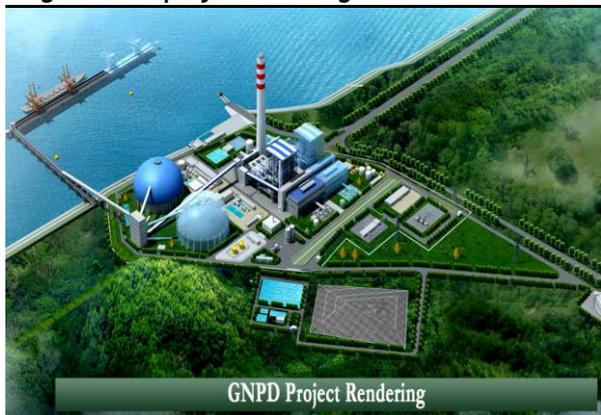
- There is still limited regulatory support for RE, hindering the pace of domestic expansion. Major DUs such as MER and AP’s own DUs remain compliant with RPS until 2024. There has been no active solar and wind FIT regime in the Philippines since 2016 and the market is still finalizing other mechanisms such as Green Energy Auction Program (GEAP);
- Malampaya, the country’s sole domestic source of LNG, an alternate baseload fuel, is set to be depleted sometime between 2024-27, posing energy security concerns if import terminal assets do not start on schedule by 2H22; and
- In the case of AP, the higher returns and stable cashflows from its coal operations enable AP to internally fund and pursue RE projects, ahead of the finalization of further regulatory support framework.

For FY22-23E, coal will be the immediate growth catalyst for AP as we estimate coal to account for c.67% of its generation mix, inclusive of GNPD (2x668 MW), which we expect full commercial operations starting Jan 2022 for Unit 1 after COVID-19-related delays. Our numbers also factor in the resumption of Unit 1 of GMEC (2x316MW), which returned from forced outage last Feb from forced outage for most of 2021. Before GNPD, GMEC was considered the largest greenfield project built in Luzon Island post-EPIRA enactment in 2001.

We estimate GMEC and GNPD to cumulatively account for 26%/28% of our FY22E EBITDA/earnings. We estimate PHP3.3b additional net income from GMEC and GNPD in FY22E, 16% of total FY22E earnings.

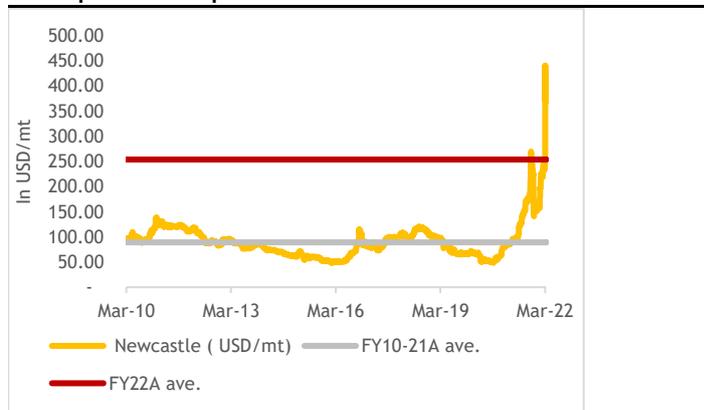
- Given pass-through mechanism of its PSAs, the coal price surge due to the Russian-Ukraine conflict should be neutral for its coal plants' EBITDA margins. AP also covers its coal exposure with commodity swap contracts, after signing fixed price contracts, as added margin protection.
- The higher efficiencies of supercritical coal plants imply less expensive coal requirements for same amount of power output, enabling GNPD to bid competitively for PSAs. Should spot prices average PHP9/kWh for three months and trigger the secondary price cap (SPC) of PHP6.50/kWh, AP estimates that its competitors using high kcal Newcastle at USD470/MT will only be breaking even, while its major plants (TLI, TVI, GMEC, and GNPD) using lower calorific coal at USD245/MT would still net profits. For FY22/23E, we expect spot prices to climb to an average of PHP6/kWh and PHP5/kwh, respectively, which will still be manageable for AP.

Fig 10: GNPower Dinginin is AP's last coal plant after DOE's ban on greenfield projects starting Oct-20



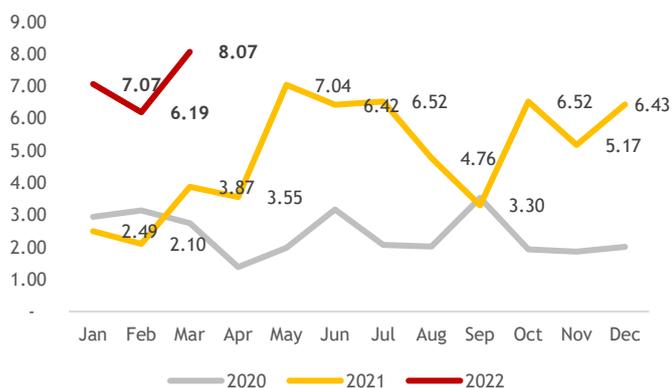
Source: GN Power

Fig 11: Coal cash costs are pass-through or hedged at Newcastle index price assumption for fixed contract



Source: Bloomberg

Fig 12: Spot prices (LWAP) rebounded post-2020



Source: Company, IEMOP

Fig 13: Securing CSP of MER is a key catalyst to watch

| | Min. MWh/yr | PSA- Start | PSA- End | Publication |
|--------------------|-------------|------------|----------|-------------|
| Baseload 70MW | 537,600 | Aug-21 | Jan-37 | Aug-21 |
| Baseload 1,000MW | 7,680,000 | Mar-26 | Feb-46 | Jan-22 |
| Baseload 1,200MW | 9,216,000 | Jan-30 | Dec-49 | TBD |
| RE Baseload 100MW | 657,000 | Mar-25 | Feb-45 | Jul-22 |
| RE Baseload 300MW | 1,971,000 | Mar-24 | Feb-44 | Aug-21 |
| RE Mid-merit 850MW | 3,350,700 | Mar-26 | Feb-46 | Aug-21 |
| RE Mid-merit 500MW | 1,971,000 | Mar-26 | Feb-46 | Aug-21 |
| Peaking | | March | July | TBD |

Source: MER Power Supply Procurement Plan 2021

Of GNPD Unit 1's 668MW capacity, 89% has already been contracted as of Mar 2022. However, its Unit 2 remains uncontracted and is set to be allocated to spot market after its grid synchronization by 2Q22. This could potentially expose GNPD Unit 2 to offtake risk and price volatility over the near term. This market risk exposure is limited to Unit 2 and even so, we expect this to be partially mitigated by the supply shortness in Luzon arising from the expected normalization of peak demand and momentary de-rating of LNG capacities (due to impending Malampaya depletion), which should keep WESM prices elevated (c. PHP6 in FY22E). Nevertheless, winning MER's competitive selection process (CSP) of Dus for portions of baseload PSAs

could be a potential catalyst for AP. There is at least one CSP scheduled in FY22 for at least 1,000MW of baseload capacity.

1.2 Strong RE pipeline until FY30E

AP's strategy is centred on raising its total attributable capacity to 9.2GW by 2030, by:

- targeting an energy mix of 50:50 between RE and non-RE capacities, of which an undetermined portion of pipeline potentially developed overseas;
- adding 3.7GW of additional RE capacity to bring total RE to 4.6GW (50% of total), diluting coal to just 32% of the portfolio in the process;
- adding one baseload 1GW LNG plant with capacity of 1GW; and
- committing to add no new coal capacities after GNPD Units 1 and 2.

Given the DOE's industry roadmap (Philippine Energy Plan 2020-40), which indicates increased regulatory policy support towards RE and its moratorium on greenfield coal power asset development, AP's strategy to roll out 3.7GW of RE is timely and repositions the company for long-term growth with a more sustainable platform.

Fig 14: RE power generation pipeline

| Project/COD | Stake | Total Capacity (in MW) | Attributable Cap (in MW) | Technology |
|--------------------------------------|-------|------------------------|--------------------------|------------|
| Maco BESS | 100% | 49 | 49 | BESS |
| Cayanga/4Q22 | 100% | 75 (94MWp) | 75 | Solar |
| Laoag/3Q23 | 100% | 130 (160MWp) | 130 | Solar |
| Magat BESS/ 1H24 | 50% | 20 | 10 | BESS |
| Tarlac/3Q24 | 100% | 35 (44MWp) | 35 | Solar |
| Calatrava/4Q24 | 100% | 120 (150MWp) | 120 | Solar |
| San Manuel/ 4Q24 | 100% | 67 (84MWp) | 67 | Solar |
| Magat Floating/ FY25 | 50% | 120 (150MWp) | 60 | Solar |
| Gamu/3Q25 | 100% | 40 (50MWp) | 40 | Solar |
| Olongapo/3Q25 | 100% | 169 (212MWp) | 169 | Solar |
| Ramon/3Q25 | 100% | 45 (56MWp) | 45 | Solar |
| Committed/indicative-Solar | | 869 | 799 | |
| Kibungan/2Q25 | 100% | 40 | 40 | Mini Hydro |
| 9ncillary/indicative- Hydro | | 40 | 40 | |
| Total RE pipeline until FY25E | | 909 | 839 | |
| Necessary RE from FY25E-FY30E | | 2,861 | 2,861 | Various |
| New RE capacity from FY22-30E | | 3,770 | 3,700 | |

Given 839MW committed/ indicative total pipeline for RE until FY25E, we estimate AP will need to roll out 477MW new capacity per year starting FY25 to hit the 3.7GW pipeline target.

This would entail PHP24b annual capex between FY25E-30E for RE development alone.

Source: Company

Note: Includes 323MW new RE projects from latest AP bond prospectus

Despite the absence of a solar and wind FIT regime since 2016, leveled costs for RE are improving (a result of more efficient technologies and growing scale economies which reduce RE component unit costs) and the introduction of regulatory mechanisms, such as the Renewable Portfolio Standard (RPS), Green Energy Auction Program (GEAP), and Green Energy Option Program (GEOP) should further raise demand for RE.

- RPS is a market-based policy mechanism that mandates Dus, electric cooperatives, and RES to source a percentage of power from RE. The program requires an annual 1% increase to the mandatory RE sourcing with the goal of reaching 35% RE mix by 2030.
- GEAP will consist of two components: (i) the Green Energy Auction to determine RE facilities eligibility under GEAP, and 2) the Green Energy Tariff which will provide pricing signals for electricity generated from RE facilities resulting from a competitive process and set the benchmark price for Dus under the Opt-in Mechanism. AP confirmed GEAP will be one of the planned offtakers for its RE project pipeline, while it is waiting on the GEAR price to be assigned by ERC.
- GEOP is a voluntary policy mechanism that allows users of over 100kW of power to source from eligible RES that source power from RE. AP

intends to use 1.24GW of hydro, geothermal, and solar capacity to supply GEOP, with participation via its existing RES firms. The DOE declared AP's subsidiaries, Aboitiz Energy Solutions, Inc., Prism Energy, Inc., and Adventenergy, Inc. as eligible to participate in GEOP.

These will be necessary to push renewables to the aspirational 35%/50% of power generation mix by 2030/2040, respectively. See *Year Ahead 2022 Powering up the reopening economy report for more.*

Since MER and AP-led Dus are compliant with RPS until 2024, we expect RE contracting to accelerate only by FY25. Besides bilateral RE contracts and RES, we expect GEOP and GEAP to further facilitate contracting of RE.

Currently, we estimate AP's RE pipeline to be at 839MW, including 799MW solar/BESS and 40MW hydro. Including this initial 839MW, AP has identified 3.5GW of RE projects across the country in various stages of development, the bulk of which are likely to be developed between FY25-30E and will require PHP143b in additional capex. AP targets to contract as much of its pipeline as it can (c.700MW of 3.7GW pipeline RE have service contracts) to produce IRRs at low-teen levels, assuming a 70:30 debt to equity funding mix.

For baseload, AP is only looking at LNG will conduct feasibility studies for two potential sites in Luzon and Cebu. AP is in no rush to pursue LNG as it is confident that GNPD's capacities are enough to fill the near-term baseload capacity gaps. Given this, our forecasts assume LNG will not be in play until FY30E.

AP's balance sheet is primed for this kind of aggressive expansion. Its balance sheet is underlevered (gross debt/EBITDA of 3.5x, as of Sep 2021) and the predictable operating cashflows from its current generation and DU portfolios, which is expected to increase by 8% p.a. over FY20A-FY23E, should support increased debt to fund capex. Further, AP's collaboration with JERA furthers opens synergistic opportunities for, not only technology transfer, but also access to capital. Lastly, we believe listing AP's RE subsidiary, Aboitiz Renewables Inc. (ARI, Unlisted), could be a back-pocket for raising funds for its 3.7GW RE pipeline as the market has an increasing appetite for green stocks.

We estimate that AP has an investment capacity of nearly PHP388b, which should be more than sufficient to fund its projects.

2. Financial analysis

2.1 FY21 earnings snapshot

In a limited press release, AP reported 4Q21 net income of PHP5.2b (-8% YoY; -6% QoQ) due to higher steam costs for APRI and lower water inflow for hydro plants. Nonetheless, this still brought AP's FY21 net income to PHP20.8b, up 66% YoY. Excluding non-recurring expenses of PHP228m for impairment losses of TVI and Redondo Peninsula Energy Inc, FX gains and c.PHP3.3b tax adjusted BI claims/liquidated damages from outages of GMEC and GNPD, we estimate FY21E core net income of PHP17.7b, up 51% YoY.

- Beneficial generation/RES EBITDA of PHP43.4b was 15% higher YoY due to (i) commissioning revenue from GNPD Unit 1; (ii) higher availability of TLI, TSI and TVI facilities (67-85% in FY20 vs 87% in FY21); (iii) higher water inflows for hydro plants; and (iv) higher WESM dispatch 1,801GWh (8% of total) in FY20 vs 3,630GWh (14% of total) in FY21). These were partially offset by the GMEC outage in Jan-Oct 2021. Capacity sold in FY21 increased by 10% to 3,753MW while energy sold increased 14% to 26,031GWh.
- Beneficial DU EBITDA was PHP7.5b, up 5% YoY. Energy sales increased 4% to 5,584 GWh on higher energy consumption as Residential, Commercial, and Industrial customer segment demand increased due to less stringent community quarantines and the resumption of operations of commercial and industrial customers.

ROE recovered to 14.1% from 9.9% in FY20. As of end Dec-2021, current ratio stood at 1.5x, versus year-end 2020's 1.4x, while its net-debt-to-equity ratio was at 1.1x, versus year-end 2020's 1.4x.

Fig 15: 4Q21/FY21 earnings review

| PHP m | 4Q21 | 4Q20 | % YoY | 3Q21 | % QoQ | FY21 | FY20 | % YoY |
|-----------------------------------|----------|----------|-------|----------|-------|-----------|-----------|-------|
| EBITDA | 12,554.0 | 14,051.0 | -10.7 | 13,087.0 | -4.1 | 50,401.0 | 43,452.0 | 16.0 |
| Net interest expense | -3,292.0 | -3,586.0 | -8.2 | -3,150.0 | 4.5 | -13,542.0 | -13,765.0 | -1.6) |
| Depreciation/Amortization | -2,864.0 | -2,861.0 | 0.1 | -2,928.0 | -2.2 | -11,286.0 | -11,026.0 | 2.4 |
| Net income to common shareholders | 5,150.0 | 5,572.0 | -8.0 | 5,553.2 | -7.3 | 20,837.0 | 12,577.7 | 65.7 |

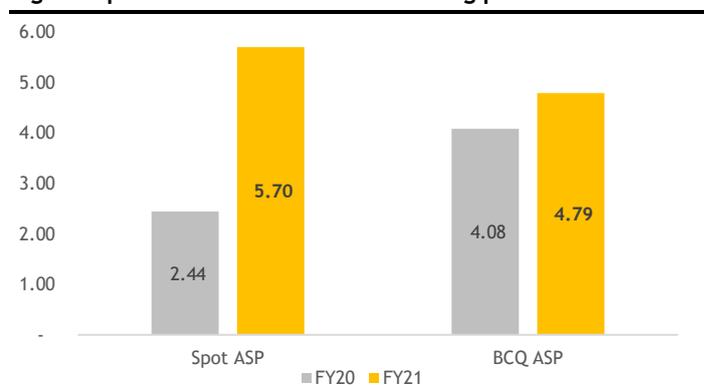
Source: Company, Maybank IBG Research

Fig 16: Energy sold (in GWh)

| In GWh | FY21 | % to total | FY20 | % ch YoY |
|---------------------|--------|------------|--------|----------|
| BCQ | 18,568 | 71% | 18562 | 0% |
| 11ncillary Services | 3,833 | 15% | 2392 | 60% |
| WESM | 3,630 | 14% | 1801 | 102% |
| Total | 26,031 | 100% | 22,754 | 14% |

Source: Company

Fig 17: Spot and bilateral contract selling price



Source: Company

Fig 18: DU electricity sales- beneficial

| In GWh | FY21 | FY20 | % ch YoY |
|--------------------------------|--------------|--------------|-----------|
| Residential | 1,709 | 1,680 | 2% |
| Commercial/industrial | 3,875 | 3,688 | 5% |
| Total electricity sales | 5,584 | 5,368 | 4% |

Source: Company

Fig 19: Beneficial EBITDA per segment

| In PHPm | FY21 | FY20 | % ch YoY |
|---------------------|---------------|---------------|------------|
| Genco/RES | 45,375 | 37,875 | 20% |
| DU | 6,390 | 6,165 | 4% |
| Parent | -1,364 | -587 | 132% |
| Total EBITDA | 50,401 | 43,452 | 16% |

Source: Company

2.2 FY22/23 earnings growth of 20%/19%

We project AP to sustain a double-digit earnings growth trajectory in FY22/23E, at +20%/+19% YoY to PHP21.2b/25.3b. Earnings growth over the medium term will be largely expansion driven, arising from incremental income from new capacities (booked under revenues and equity income).

In the FY21 briefing, AP disclosed that it intends to add c.1.8GW of new attributable capacity in FY22-25E from:

- GNDP Unit 1 and 2: 2x468MW;
- 799MW total solar capacity (including 150MWp Magat floating); and
- 40MW Kibungan Hydro plant.

Complementing these capacities are the Maco (49MW) and Magat (20MW) battery projects, which AP intends to launch between FY22-24. Given the expected COD of these capacities, we forecast AP's FY23E beneficial energy sales to hit 31,242GWh, implying a FY20-23E CAGR of 10.9%.

Fig 20: Consolidated Income Statement (FY20A-23E)

| in PHP m | FY20A | FY21E | YoY | FY22E | YoY | FY23E | YoY | Notes |
|-------------------------------|----------------|----------------|------------|----------------|------------|----------------|------------|---|
| Revenues | 110,377 | 124,974 | 13% | 129,819 | 4% | 132,508 | 2% | |
| Generation | 51,751 | 61,630 | 19% | 63,671 | 3% | 63,422 | 0% | Growth is attributable to contributions from additional 1,010/130MW new capacities for FY22/23 and 10-month contributions from GMEC, which should sufficiently offset the normalized utilization factor for TLI and TVI (85% in FY22-23E, from c.90% in FY21E). |
| Distribution | 41,872 | 43,710 | 4% | 45,345 | 4% | 47,044 | 4% | FY22/23E average annual volume growth of 6% from steady electricity sales recovery as both commercial/industrial and household segments benefit from economic reopening. We expect the DU segment to surpass its pre-COVID-19 volumes (FY19 at 5,849GWh) by YE23E. |
| RES | 16,477 | 19,345 | 17% | 20,506 | 6% | 21,736 | 6% | FY21/22/23E sales growth of 17%/6%/6% as we expect more contestable customers to join RES as economy reopens while AP's RES units are also GEAP participant. |
| Other fees | 277 | 289 | 4% | 297 | 3% | 306 | 3% | |
| Cost & expenses | -83,497 | -96,522 | 16% | -98,720 | 2% | -97,604 | -1% | We expect more moderate purchased power increase of 3% in FY22E as GMEC resumes in Feb-2022 after long 2021 outage. |
| Income from operations | 26,880 | 28,452 | 6% | 31,099 | 9% | 34,904 | 12% | |
| Operating margin | 24.35% | 22.77% | | 23.96% | | 26.34% | | Improvement driven by slower costs versus revenue growth. |
| Finance cost | -14,254 | -13,013 | -9% | -12,348 | -5% | -11,987 | -3% | Lower interest accretion from lease liabilities offset by rising debt after FY22E. We assumed an effective interest rate of 5% |
| Finance income | 653 | 774 | 19% | 803 | 4% | 814 | 1% | Higher average cash balance from increased plant output. |
| Equitized income | 2,675 | 9,271 | 247% | 7,841 | -15% | 10,704 | 37% | Full year earnings contribution of GNPD by FY23E after initial sync of Unit 1 in FY21 and Unit 2 in FY22. |
| Other income (loss) | 4,929 | 757 | -85% | 1,214 | 60% | - | -100% | |
| Pre-tax income | 20,883 | 26,241 | 26% | 28,610 | 9% | 34,435 | 20% | |
| Income tax | -6,062 | -2,731 | -55% | -4,154 | 52% | -5,458 | 31% | Lower ETR due to CREATE Act, absence of reversal of deferred tax on NOLCO |
| Effective tax rate | -33.29% | -16.09% | | -20.00% | | -23.00% | | |
| Net income | 14,821 | 23,510 | 59% | 24,456 | 4% | 28,977 | 18% | |
| To minority | -2,244 | -2,673 | 19% | -2,333 | -13% | -3,653 | 57% | |
| To common shareholders | 12,578 | 20,837 | 66% | 22,123 | 6% | 25,324 | 14% | |
| Non-recurring items | 863 | 3,106 | 260% | 911 | -71% | 0 | -100% | Excludes FX, insurance claims, and impairment. |
| Core net income | 11,715 | 17,732 | 51% | 21,213 | 20% | 25,324 | 19% | |

Source: Company, Maybank IBG Research

Note: Using FY21E while audited 17-A is not available.

2.3 Impact of RE push starting to reflect on FY23E

We expect AP's gearing levels to rise, alongside its capacity expansions. While its improving operating cashflows should be sufficient to cover working capital and the equity component of its expansion, we expect AP to borrow at least 70% of its project costs to optimize project-level returns and, more importantly, keep its balance sheet flexible for potential acquisitions and/or opportunistic partnerships for its 3.7GW RE target.

We expect long-term debt to rise to PHP302b by FY30E, from PHP167b as of Sep 2021. Despite this, consolidated DE ratio and debt-to-EBITDA should remain healthy at 0.9x and c.3.5x by FY30E, as more capacities come onstream.

Fig 21: Consolidated balance sheet (FY20A-23E)

| in PHP m | FY20A | FY21E | FY22E | FY23E | Notes |
|-----------------------------------|----------------|----------------|----------------|----------------|---|
| Cash and cash equivalents | 38,700 | 40,161 | 40,713 | 57,676 | |
| Receivables | 22,017 | 23,993 | 24,923 | 25,439 | |
| Inventories | 6,308 | 7,583 | 7,755 | 7,668 | |
| Property, plant, and equipment | 203,451 | 197,345 | 203,409 | 209,503 | We assume direct capex (ex. JV) of PHP16/17/46b, which represents the 75/130/222MW additions in FY22/23/24E |
| Other assets | 127,449 | 133,495 | 139,995 | 141,995 | |
| Total Assets | 397,925 | 402,576 | 416,794 | 442,281 | |
| Accounts Payable | 18,372 | 20,602 | 21,071 | 20,833 | |
| Short term debt | 11,743 | 11,743 | 11,743 | 11,743 | |
| Long term debt | 177,321 | 168,191 | 172,044 | 183,294 | We expect new projects to be financed with 70% debt and 30% internally generated equity. |
| Other Liabilities | 55,904 | 50,199 | 46,309 | 42,868 | |
| Total Liabilities | 263,340 | 250,736 | 251,168 | 258,739 | |
| Capital stock | 19,947 | 19,947 | 19,947 | 19,947 | |
| Retained earnings | 118,650 | 133,232 | 144,685 | 158,947 | |
| Other equity | -4,012 | -1,339 | 994 | 4,647 | |
| Total Equity | 134,585 | 151,840 | 165,626 | 183,542 | |
| Total Liabilities + Equity | 397,925 | 402,576 | 416,794 | 442,281 | |

Source: Company, Maybank IBG Research

2.4 Improving operating cashflow

The improvement in AP's cashflows is largely the result of contributions from its expanded coal portfolio. While operating cashflows appear sufficient to fund AP's initial RE capex, we expect it to continue to borrow at least 70% of its upcoming project costs.

Fig 22: Consolidated Cash Flow (FY20-23E)

| in PHP m | FY20A | FY21E | FY22E | FY23E | Notes |
|-------------------------------|---------|---------|---------|---------|--|
| Cash from operations | 31,782 | 35,982 | 38,270 | 40,167 | Improvement is from increased output from GNPD and new RE capacities. |
| Capital expenditures | -5,429 | -5,917 | -16,378 | -17,035 | Capex is mainly for AP's RE pipeline and maintenance of other generation and DU assets. |
| Cash for investing activities | -4,527 | -754 | -14,664 | -7,964 | |
| Cash for financing activities | -25,914 | -33,767 | -23,054 | -15,239 | Amid AP's improving operating cashflows and the presumed ring-fenced funding structure for its RE expansions, we conservatively forecast AP's dividend payout to remain at 50% of previous year's net income in FY22/23E, same as FY21E. |

Source: Company, Maybank IBG Research

3. Valuation

3.1 Initiate with BUY; SOTP-TP of PHP42

Our 12-month forward valuation of AP is based on the sum of the individual discounted cashflows of its various thermal, RE and distribution subsidiaries.

Fig 23: Target price computation for AP

| | Equity Value (PHPm) | Attributable Value (PHPm) | Value per Share (PHP) | Notes |
|--|------------------------|------------------------------|--------------------------|---|
| Projects existing/under construction | | | | |
| Coal/LNG | 220,193 | 172,788 | 23.5 | Reflects 40 years plant life. |
| Geothermal | 29,558 | 29,558 | 4 | Reflects 20 more years of operations. |
| Hydro/Solar | 115,733 | 76,159 | 10.3 | Reflects 25 years average plant life for solar, 20 years for hydro. |
| Oil | 26,093 | 19,714 | 2.7 | Reflects 20 years of operations. |
| Distribution | 58,299 | 47,323 | 6.4 | Assumed renewal of DU franchises with a 2% terminal growth rate. |
| Total operational/ under construction | 449,876 | 345,543 | 47 | |
| Post-FY24 RE pipeline | 15,243 | 15,243 | 2.1 | 2.9GW RE starting FY25 to FY30 to reach 50:50 target. |
| Asset Value | 465,120 | 360,786 | 49 | |
| Net (debt)/cash | -54,055 | -54,055 | -7.3 | |
| Net asset value | 411,065 | 306,731 | 41.7 | |

Source: Company, Maybank IBG Research

For thermal non-RE capacities and Dus, we used a dynamic WACC between 6.1-7.0% based on the following assumptions:

- Risk-free rate of 4.0% and market-risk premium of 6.0%;
- Asset beta of 0.82x, which is justified given that baseload coal plants are less cyclical
- Debt to equity split of 59%/41%
- After-tax cost of debt between 4.2-5.4%.

For existing RE capacities and those under construction, we used a dynamic WACC between 6.3-6.7% based on the following assumptions.

- Risk-free rate of 4.0% and market-risk premium of 6.0%;
- Asset beta of 1.1x, which is justified given RE capacities typically service peaking demand requirements which have more cyclical drivers.
- Debt to equity split of 70%/30%
- After-tax cost of debt between 4.5-5.0%.

We did not assume terminal growth for power generation assets given limited asset lives but used a 2% terminal growth rate for the DU assets, which is our long-term assumption for volume growth demand for the Philippines.

Finally, our forward valuations include AP's c.3.0GW RE pipeline after FY24E, which we expect to have an average project cost of USD1m/MW and to come onstream from FY25E-30E. For this, we used an IRR method, which assumes an equity return of 12%, under the following assumptions:

- Risk-free rate of 4.0% and market-risk premium of 6.0%;
- Asset beta of 1.1x, which is justified given RE capacities typically service peaking demand requirements which have more cyclical drivers.
- Debt to equity split of 70%/30%
- After-tax cost of debt between 4.5-5.0%.

These altogether translated to a net asset value of PHP306.7b or PHP41.7 per share, rounding up to our TP of PHP42.0.

3.2 Stock performance

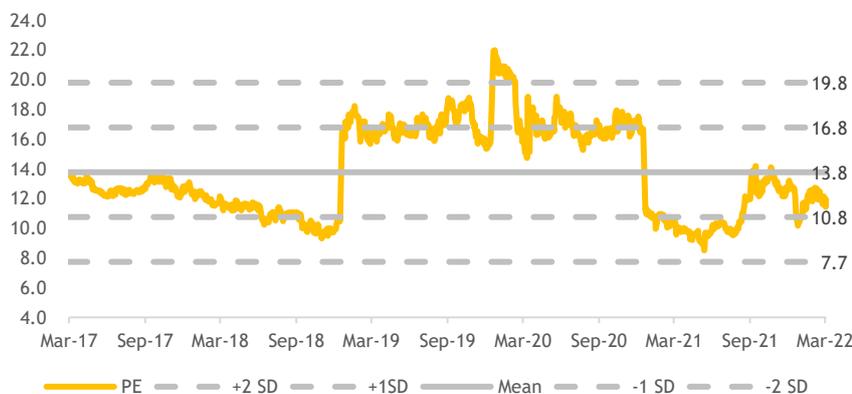
AP is trading at a trailing FY22E PER of 11.9x, still below its 5Y average PER of 13.8x. At our PHP42.0 TP, the FY22E implied trailing PER is 14.6x, slightly above the 5Y PER but justified by the company's growth prospects. Moreover, AP's ROE and dividend yield compare favourably against the median metrics of its peers, strengthening our BUY call on the stock.

Fig 24: Peer comparison

| Name | Ticker | CP | TP | Upside | Rec | PER | | ROE | | Div Yld |
|------------------------------|--------------|-------------|-----------|-------------|------------|-------------|-------------|-------------|-------------|------------|
| | | | | | | FY21E | FY22E | FY21E | FY22E | FY22E |
| Median | | | | | | 11.6 | 10.5 | 8.8 | 13.6 | 1.7 |
| Aboitiz Power Corp.* | AP PM | 34.3 | 42 | 22.4 | BUY | 12.3 | 11.9 | 14.7 | 14.4 | 4.1 |
| AC Energy Corp.* | ACEN PM | 8.15 | 5.4 | -34.2 | SELL | 58.3 | 45.4 | 4.3 | 5.3 | 0.4 |
| First Gen Corp.* | FGEN PM | 26.75 | 33 | 21.5 | HOLD | 6.3 | 5.4 | 13.1 | 13.5 | 2.6 |
| Manila Electric Co.* | MER PM | 380 | 324 | -11.2 | BUY | 18.5 | 23.1 | 23.6 | 21.6 | 3.6 |
| Semirara Mining * | SCC PM | 29.5 | 23.5 | -6 | BUY | 9.6 | 11.9 | 30.7 | 23.4 | 6.3 |
| Jilin Electric Power-A | 000875 CH | 8.69 | na | na | na | 30.4 | 20 | 6.7 | 10.1 | 0.3 |
| Shenergy Company Limited-A | 600642 CH | 6 | na | na | na | 11.2 | 9.2 | 7.6 | 8.6 | 5.2 |
| Shanghai Electric Power Co-A | 600021 CH | 10.55 | na | na | na | 46 | 10.5 | 4 | 14.2 | - |
| Gd Power Development Co -A | 600795 CH | 2.52 | na | na | na | 11.6 | - | na | na | - |
| Jiangsu Guoxin Corp Ltd-A | 002608 CH | 5.67 | na | na | na | 10.3 | 7.6 | na | na | - |
| Fujian Funeng Co Ltd-A | 600483 CH | 10.7 | na | na | na | 10.5 | 7.2 | 10 | 13.7 | 1.7 |
| Hubei Energy Group Co Ltd-A | 000883 CH | 4.12 | na | na | na | 10.3 | 9.6 | na | na | - |
| Ytl Corp Bhd. | YTL MK | 0.52 | na | na | na | 91.8 | 26.6 | 0.6 | 1.1 | 4.6 |

Source: Bloomberg, Maybank IBG Research

Fig 25: AP's 5-year historical PER band



AP exhibited lower PER in FY21 and FY22 due to EPS recovery post-2020.

Positive narratives such as strong ESG risk mitigation and aggressive RE expansion are possible rerating factors to consider.

Source: Bloomberg, Maybank Research

4. Risks

4.1 Execution risk

While some RE technologies are straight forward, such as solar and hydro, these (including LNG) lie outside of AP's core competencies and exposes AP to execution risks, which could be exacerbated by its aggressive pipeline. We estimate that our PHP42 valuation of AP could reduce by up to 5% (or PHP2.1) should AP fall short of delivering 2.9GW of RE capacities post-2024.

Nevertheless, we believe that AP's exposure to execution risk could be mitigated by the fact that technical expertise in the RE space can be easily and widely outsourced. Further, its partnership with JERA offers added comfort given JERA's longer and wider experience in both the RE and LNG space.

4.2 Merchant risk for uncontracted RE and GNPD Unit 2

AP's new capacities (5,168MW including new RE, LNG, and GNPD Unit 2) face merchant risk. GNPD Unit 2 is still uncontracted, while its future RE capacities could be without FIT. Nevertheless, AP has a few options:

- GNPD Unit 2 should be eligible in the next baseload CSP, which we expect to be in FY22E; and
- RE capacities, which should further develop under the GEOP and GEAP, could be sold to DUs or RES.

Even if GNPD Unit 2 remains uncontracted, AP's spot exposure would only be 16% of sold capacity, which should remain manageable.

We expect this to be partially mitigated by spot prices which will be buoyed by the supply shortness in Luzon. We assumed FY22/23E spot price will climb but remain manageable at PHP6/kWh and PHP5/kWh, respectively. Even in the extreme case that the secondary price cap (SPC) of PHP6.50 is triggered, AP's major coal plants such as TLI, TVI, GMEC, and GNPD run on low calorific coal and would still be able to maintain margins considering their lower equivalent fuel cost versus plants using high calorific coal.

Nevertheless, winning MER's competitive selection process (CSP) of DUs for portions of baseload PSAs could be a potential catalyst for AP. There is at least one CSP scheduled in FY22 for at least 1,000MW of baseload capacity.

4.3 Potentially limited access to funding due to coal exposure

Although there is no indication from the government that coal will be phased out, is the government already imposed a moratorium on greenfield coal plant development. Some big banks worldwide and even locally have already announced they will halt funding of new coal plants by 2033. As more financial institutions join the net zero movement internationally, local creditors may be pressured to limit AP's access to funding.

Nevertheless, we think AP has a few funding options available such as raising bonds, welcoming other strategic partners and/or listing its RE subsidiary.

| FYE 31 Dec | FY19A | FY20A | FY21E | FY22E | FY23E |
|-------------------------------------|------------------|------------------|------------------|------------------|------------------|
| Key Metrics | | | | | |
| P/E (reported) (x) | 15.4 | 16.2 | 12.1 | 11.4 | 10.0 |
| Core P/E (x) | 15.9 | 16.7 | 14.2 | 11.9 | 10.0 |
| P/BV (x) | 2.0 | 1.5 | 1.8 | 1.6 | 1.5 |
| P/NTA (x) | 2.0 | 1.5 | 1.8 | 1.6 | 1.5 |
| Net dividend yield (%) | 4.3 | 4.4 | 2.5 | 4.2 | 4.4 |
| FCF yield (%) | 11.8 | 13.5 | 12.2 | 8.7 | 9.2 |
| EV/EBITDA (x) | 10.6 | 9.3 | 10.2 | 9.7 | 8.8 |
| EV/EBIT (x) | 14.2 | 13.1 | 14.1 | 13.1 | 11.6 |
| INCOME STATEMENT (PHP m) | | | | | |
| Revenue | 125,635.2 | 110,376.6 | 124,973.8 | 129,819.1 | 132,508.5 |
| EBITDA | 38,751.6 | 37,853.3 | 39,311.1 | 41,843.4 | 46,292.1 |
| Depreciation | (9,895.7) | (10,973.4) | (10,859.3) | (10,744.5) | (11,387.9) |
| Amortisation | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 |
| EBIT | 28,855.9 | 26,879.9 | 28,451.8 | 31,098.9 | 34,904.3 |
| Net interest income / (exp) | (12,755.9) | (13,600.5) | (12,238.5) | (11,544.4) | (11,172.8) |
| Associates & JV | 3,814.0 | 2,675.1 | 9,271.0 | 7,841.4 | 10,703.7 |
| Exceptionals | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 |
| Other pretax income | 3,483.4 | 4,928.6 | 756.9 | 1,213.7 | 0.0 |
| Pretax profit | 23,397.3 | 20,883.1 | 26,241.3 | 28,609.5 | 34,435.2 |
| Income tax | (3,215.5) | (6,061.9) | (2,731.3) | (4,153.6) | (5,458.2) |
| Minorities | (2,859.1) | (2,243.5) | (2,673.0) | (2,333.0) | (3,653.0) |
| Discontinued operations | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 |
| Reported net profit | 17,322.7 | 12,577.7 | 20,837.0 | 22,122.9 | 25,323.9 |
| Core net profit | 15,819.6 | 11,715.0 | 17,731.5 | 21,212.6 | 25,323.9 |
| Distributable Income | 15,819.6 | 11,715.0 | 17,731.5 | 21,212.6 | 25,323.9 |
| BALANCE SHEET (PHP m) | | | | | |
| Cash & Short Term Investments | 37,433.9 | 38,699.5 | 40,161.2 | 40,712.7 | 57,676.0 |
| Accounts receivable | 21,747.4 | 22,017.3 | 23,992.7 | 24,922.9 | 25,439.2 |
| Inventory | 6,632.0 | 6,308.2 | 7,582.6 | 7,755.3 | 7,667.6 |
| Property, Plant & Equip (net) | 209,521.5 | 203,451.2 | 197,344.8 | 203,408.6 | 209,503.1 |
| Intangible assets | 46,712.5 | 44,279.4 | 46,448.2 | 46,448.2 | 46,448.2 |
| Investment in Associates & JVs | 60,878.5 | 61,828.8 | 61,828.8 | 68,328.8 | 70,328.8 |
| Other assets | 27,543.5 | 21,340.6 | 25,217.5 | 25,217.5 | 25,217.5 |
| Total assets | 410,469.4 | 397,925.1 | 402,575.8 | 416,794.0 | 442,280.5 |
| ST interest bearing debt | 20,721.7 | 28,997.6 | 29,548.3 | 13,247.6 | 15,278.7 |
| Accounts payable | 22,376.1 | 18,371.8 | 20,601.7 | 21,070.9 | 20,832.7 |
| LT interest bearing debt | 167,585.3 | 160,067.1 | 150,386.4 | 170,540.0 | 179,759.1 |
| Other liabilities | 66,143.0 | 55,904.0 | 50,199.0 | 46,309.0 | 42,868.0 |
| Total Liabilities | 276,826.3 | 263,340.0 | 250,735.6 | 251,167.9 | 258,738.9 |
| Shareholders Equity | 125,543.0 | 127,158.6 | 141,740.8 | 153,193.7 | 167,456.2 |
| Minority Interest | 8,100.0 | 7,426.5 | 10,099.5 | 12,432.5 | 16,085.5 |
| Total shareholder equity | 133,643.0 | 134,585.1 | 151,840.2 | 165,626.2 | 183,541.6 |
| Total liabilities and equity | 410,469.4 | 397,925.1 | 402,575.8 | 416,794.0 | 442,280.5 |
| CASH FLOW (PHP m) | | | | | |
| Pretax profit | 23,397.3 | 20,883.1 | 26,241.3 | 28,609.5 | 34,435.2 |
| Depreciation & amortisation | 9,895.7 | 10,973.4 | 10,859.3 | 10,744.5 | 11,387.9 |
| Adj net interest (income)/exp | 12,755.9 | 13,600.5 | 12,238.5 | 11,544.4 | 11,172.8 |
| Change in working capital | 2,778.0 | (4,356.7) | (676.4) | (633.7) | (666.8) |
| Cash taxes paid | (3,669.1) | (4,605.5) | (2,731.3) | (4,153.6) | (5,458.2) |
| Other operating cash flow | (3,814.0) | (2,675.1) | (9,271.0) | (7,841.4) | (10,703.7) |
| Cash flow from operations | 39,357.0 | 31,781.7 | 36,660.4 | 38,269.7 | 40,167.0 |
| Capex | (9,675.8) | (5,428.7) | (5,916.5) | (16,378.1) | (17,035.0) |
| Free cash flow | 29,681.1 | 26,352.9 | 30,743.9 | 21,891.6 | 23,132.1 |
| Dividends paid | (10,817.1) | (8,682.7) | (6,254.8) | (10,670.0) | (11,061.4) |
| Equity raised / (purchased) | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 |
| Change in Debt | 20,493.1 | 2,950.0 | (9,130.1) | 3,852.9 | 11,250.2 |
| Perpetual securities distribution | 3.0 | 4.0 | 5.0 | 5.0 | 5.0 |
| Other invest/financing cash flow | (41,663.7) | (19,279.5) | (12,321.2) | (14,523.0) | (6,357.5) |
| Effect of exch rate changes | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 |
| Net cash flow | (2,303.7) | 1,344.7 | 3,042.8 | 556.6 | 16,968.3 |

| FYE 31 Dec | FY19A | FY20A | FY21E | FY22E | FY23E |
|--|-----------|-----------|-----------|-----------|-----------|
| Key Ratios | | | | | |
| Growth ratios (%) | | | | | |
| Revenue growth | (4.5) | (12.1) | 13.2 | 3.9 | 2.1 |
| EBITDA growth | (14.2) | (2.3) | 3.9 | 6.4 | 10.6 |
| EBIT growth | (20.9) | (6.8) | 5.8 | 9.3 | 12.2 |
| Pretax growth | (17.5) | (10.7) | 25.7 | 9.0 | 20.4 |
| Reported net profit growth | (20.2) | (27.4) | 65.7 | 6.2 | 14.5 |
| Core net profit growth | (27.1) | (25.9) | 51.4 | 19.6 | 19.4 |
| Profitability ratios (%) | | | | | |
| EBITDA margin | 30.8 | 34.3 | 31.5 | 32.2 | 34.9 |
| EBIT margin | 23.0 | 24.4 | 22.8 | 24.0 | 26.3 |
| Pretax profit margin | 18.6 | 18.9 | 21.0 | 22.0 | 26.0 |
| Payout ratio | 62.4 | 69.0 | 30.0 | 48.2 | 43.7 |
| DuPont analysis | | | | | |
| Net profit margin (%) | 13.8 | 11.4 | 16.7 | 17.0 | 19.1 |
| Revenue/Assets (x) | 0.3 | 0.3 | 0.3 | 0.3 | 0.3 |
| Assets/Equity (x) | 3.3 | 3.1 | 2.8 | 2.7 | 2.6 |
| ROAE (%) | 13.7 | 10.0 | 15.5 | 15.0 | 15.8 |
| ROAA (%) | 4.0 | 2.9 | 4.4 | 5.2 | 5.9 |
| Liquidity & Efficiency | | | | | |
| Cash conversion cycle | (0.4) | 4.2 | 14.5 | 14.6 | 14.0 |
| Days receivable outstanding | 62.3 | 71.4 | 66.3 | 67.8 | 68.4 |
| Days inventory outstanding | 27.1 | 31.3 | 28.7 | 31.0 | 31.7 |
| Days payables outstanding | 89.7 | 98.4 | 80.5 | 84.2 | 86.0 |
| Dividend cover (x) | 1.6 | 1.4 | 3.3 | 2.1 | 2.3 |
| Current ratio (x) | 1.5 | 1.4 | 1.6 | 2.2 | 2.6 |
| Leverage & Expense Analysis | | | | | |
| Asset/Liability (x) | 1.5 | 1.5 | 1.6 | 1.7 | 1.7 |
| Net gearing (%) (incl perps) | 112.9 | 111.7 | 92.1 | 86.4 | 74.8 |
| Net gearing (%) (excl. perps) | 112.9 | 111.7 | 92.1 | 86.4 | 74.8 |
| Net interest cover (x) | 2.3 | 2.0 | 2.3 | 2.7 | 3.1 |
| Debt/EBITDA (x) | 4.9 | 5.0 | 4.6 | 4.4 | 4.2 |
| Capex/revenue (%) | 7.7 | 4.9 | 4.7 | 12.6 | 12.9 |
| Net debt/ (net cash) | 150,873.1 | 150,365.2 | 139,773.5 | 143,074.9 | 137,361.7 |

Source: Company; Maybank IBG Research

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