

Is First Gen an overlooked power play that deserves a re- rating?



Valuation Master Class

CASE  STUDY
VALUATION MASTER CLASS
by
A. Stoltz INVESTMENT
RESEARCH



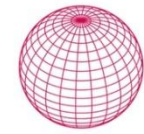
This information is for
learning purposes only.

***This is not
investment advice or a
recommendation.***



Ask
Ajarn
Andrew

Is First Gen an overlooked power play that deserves a re-rating?



VALUATION MASTER CLASS



Sector: Utilities



*Philippine's largest natural gas power producer
and leader in renewable energy with a total
installed capacity of 3,500 MW*

My value estimate:

PHP39
(Upside 40%)

BUY



3 things to know about this company

- ★ Resolving gas supply issues ensures longevity
- ★ A pioneer in renewable energy should be future proof
- ★ Undemanding valuation could lead to re-rating

Key statistics

Analyst consensus (6)

PHP35
(Upside 26%)

BUY

PE ratio

7x

Dividend yield

2.5%



Sales

Story

FVMR

Value

WCB

Risks

Natural gas 58%



Geothermal, wind, solar 39%



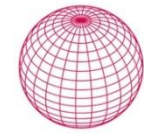
Hydro 2%



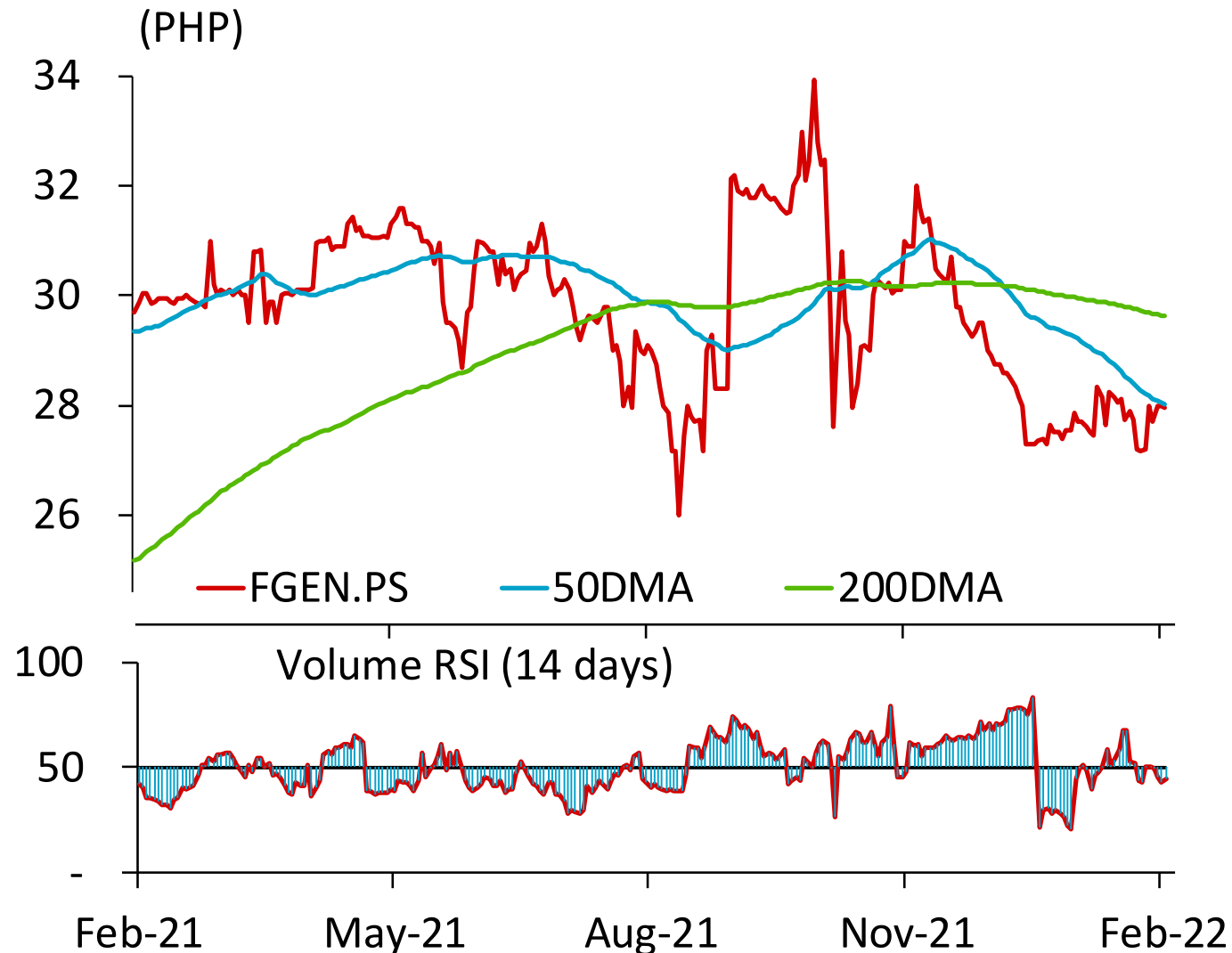
Others 1%



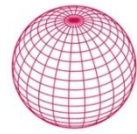
Price and volume turned bearish



VALUATION MASTER CLASS



- ★ Throughout the past year, the share price fluctuated around PHP30
 - Recently, the 50DMA has fallen below the 200DMA, suggesting a bearish signal
- ★ Volume RSI has fallen below the 50%-line; hence, not providing a support for a turnaround



Sales

Story

FVMR

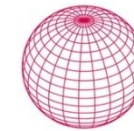
Value

WCB

Risks

- ★ Natural gas is widely accepted as the transition fuel for the mid-term future
 - **FGEN derives 58% of its revenue from gas**
- ★ The main problem is that the country's only gas field Malampaya is about to deplete over the next 3 years
 - **Hence, the market raised huge concerns about the longevity and profitability of FGEN's business to compensate for the lack of gas supply**

*Malampaya gas field*



Sales

Story

FVMR

Value

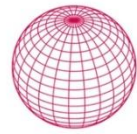
WCB

Risks

- ★ FGEN currently constructs the country's first liquefied natural gas (LNG) terminal with a capacity of 5.2m metric tons
 - **The terminal allows to store imported LNG and turn it back to gaseous form to generate energy**
- ★ So far, the construction progress is on track and the terminal could start operations by late 2022 already
 - **By resolving the supply issue, FGEN dispels any doubts about its longevity**



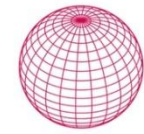
Tokyo Gas is the largest natural gas provider in Japan and holds a 20% stake in the LNG terminal that FGEN develops



Installed capacity Philippines

Fuel	2017	2018	2019	2020	%
Coal	8,049	8,844	9,313	10,944	42
Oil-based	4,153	4,292	3,779	4,237	16
Natural Gas	3,447	3,453	3,453	3,453	13
Renewables	7,079	7,226	7,214	7,617	29
Total	22,728	23,815	23,759	26,251	100

- ★ For now, the Philippine gov't still has a high tolerance for coal-fueled energy generation
 - Cheap coal is likely to remain the dominant fuel source in the near term
- ★ However, the gov't rewards the usage of renewable sources through long-term contracts with favorable prices
 - Philippine energy companies are required to start green transition soon



Sales

Story

FVMR

Value

WCB

Risks

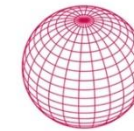
Installed capacity Philippines

Fuel	2017	2018	2019	2020	%
Coal	8,049	8,844	9,313	10,944	42
Oil-based	4,153	4,292	3,779	4,237	16
Natural Gas	3,447	3,453	3,453	3,453	13
Renewables	7,079	7,226	7,214	7,617	29
Total	22,728	23,815	23,759	26,251	100

Installed capacity FGEN

Fuel	2017	2018	2019	2020	%
Natural gas	2,135	2,162	2,147	2,017	58
Renewables	1,475	1,475	1,475	1,475	42
Total	3,610	3,637	3,622	3,492	100

- ★ It makes up 20% of the country's total renewable energy capacity
 - The company runs indigenous renewable sources like geothermal, wind, and solar
- ★ Its early shift towards renewable energy gives the company a timing advantage
 - Therefore, I expect a stable and strong gross margin over the next few years



Sales

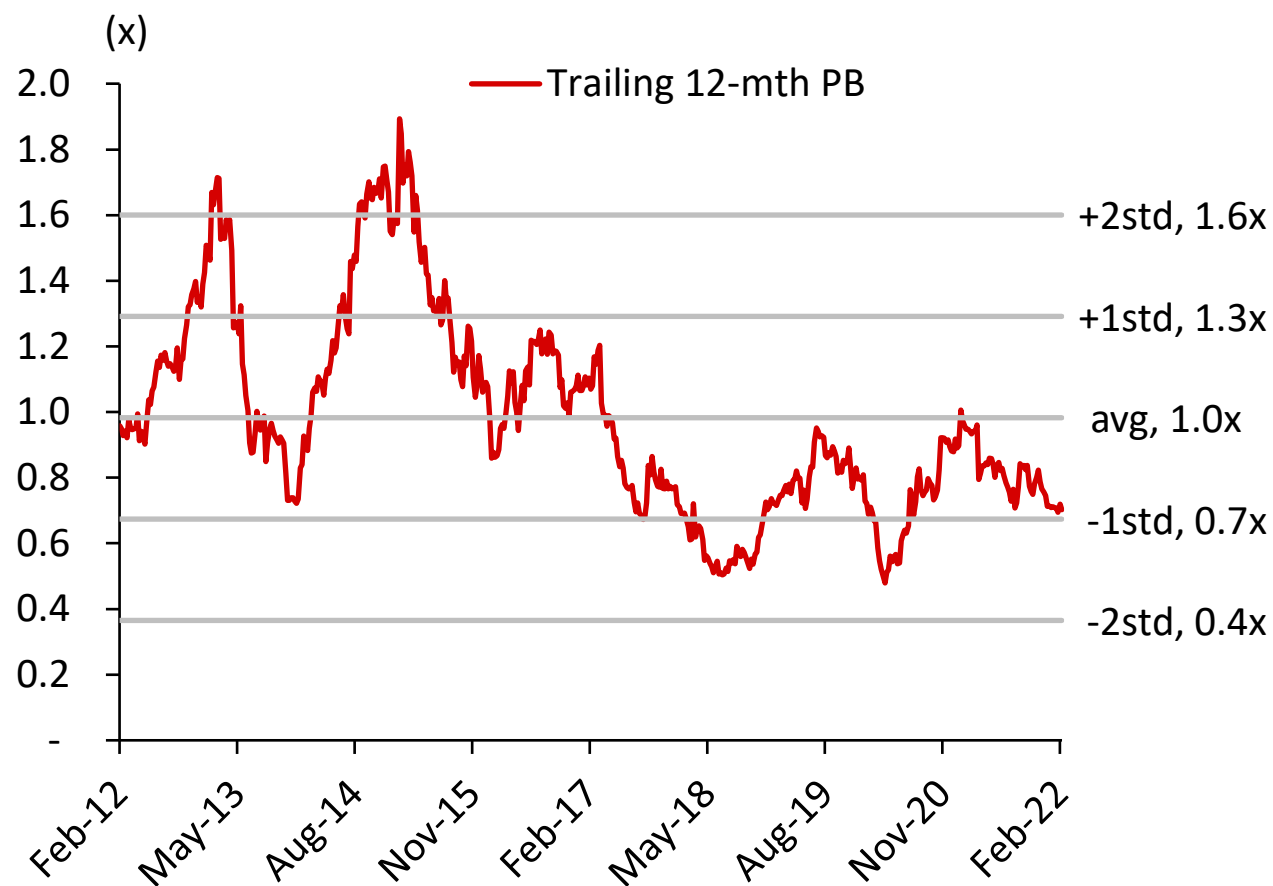
Story

FVMR

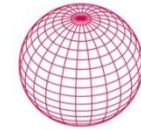
Value

WCB

Risks



- ★ The stock currently trades more than one standard deviation below its historical average on PB
- ★ FGEN regularly has beaten analysts' forecasts in the past
 - **With the LNG terminal, FGEN does not only solve supply issues, but might also sell excess LNG, creating additional revenue**



Sales

Story

FVMR

Value

WCB

Risks

- ★ In 2020, the US-based investment company KKR acquired a 12.6% stake in FGEN
- ★ In October 2021, KKR announced to acquire another 7.3% stake for PHP33 per share, which is a 20% premium to market price
 - **I consider the follow-on investment of KKR as a positive signal that the share price could provide further upside**



KKR is a leading investment firm with total assets under management of US\$459bn



What Is Going to Happen with Inflation?

By Valuation Master Class Student

Many forces at work impact inflation. There are current trends that cause both inflationary and deflationary measures. Whether we'll see inflation or deflation in the future depends on which of these forces dominate.

[Read More](#)



How to Value a Startup

By Andrew Stotz

This story started when Dan, a podcast listener, replied to my recent weekly email with this question, "How do you value a startup, especially if there is no revenue?"

[Read More](#)



How to Fight Back When Your Dreams Are Crushed

By Andrew Stotz

The trouble you face is not your fault, and I'm gonna show you how you can fight back. I challenge you to recommit to your dreams today!

[Read More](#)

ValuationMasterClass.com



What Does It Mean to Be Financially World Class?



What Is Liabilities To Assets Ratio?



What Is Growth Year Over Year?

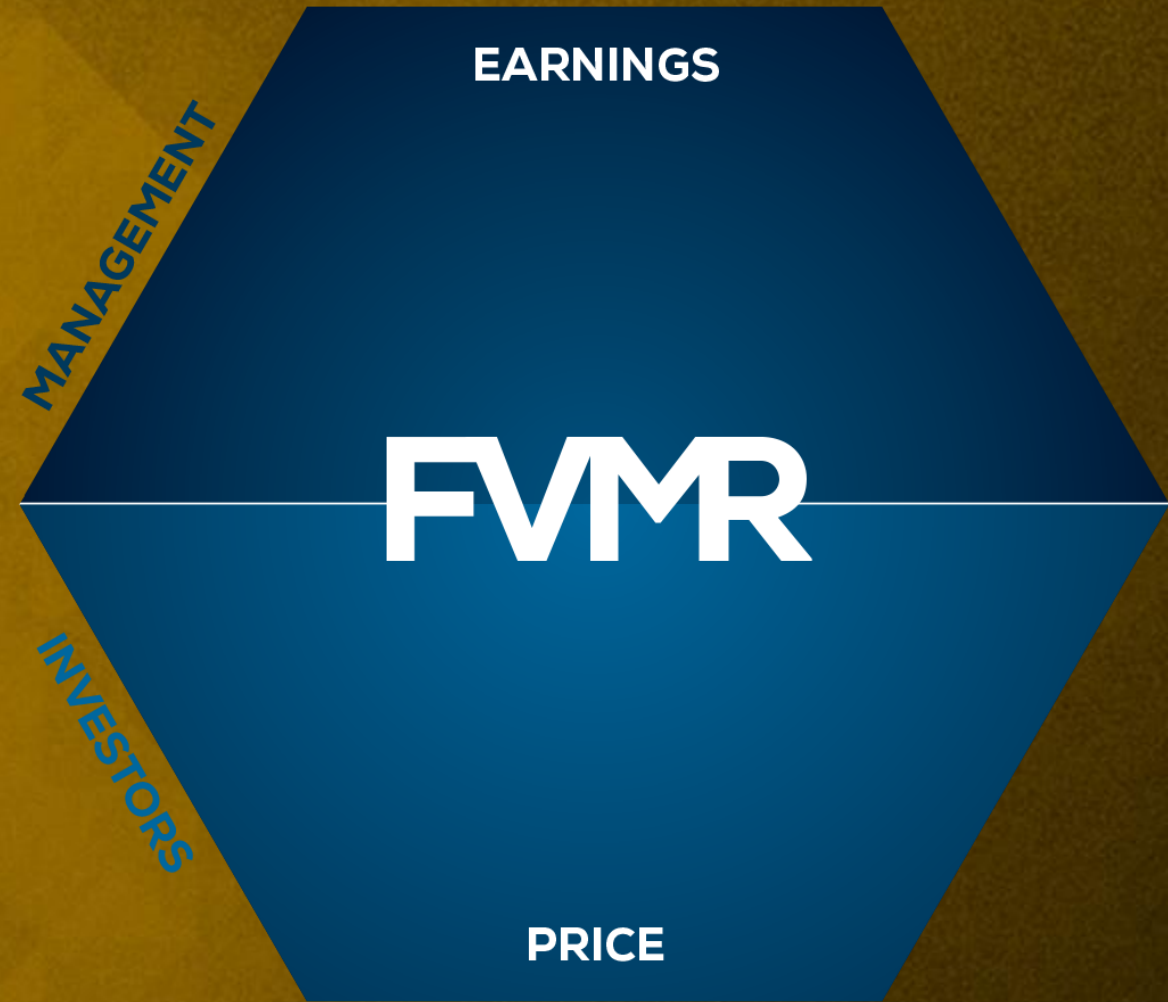
Scan this QR code
to go to the
ValuationMasterClass.com
blog to download all full
Case Study reports for free.

**It's usually up within 24h.*

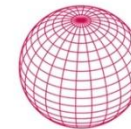


FVMR Scorecard

- ★ Measures a stock's attractiveness relative to all other companies
- ★ Attractiveness is based on four elements
 - Fundamentals, Valuation, Momentum, and Risk
- ★ Scale from 1 (Best) to 10 (Worst)



Weak momentum, but price suggest cheap opportunity to buy



VALUATION MASTER CLASS

Sales

Story

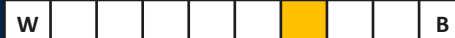
FVMR

Value

WCB

Risks

Fundamentals



(%)	Dec-17	Dec-18	Dec-19	Dec-20	PTM**
Operating profit margin	25.5	24.5	24.3	29.4	26.2
Recurring net margin	7.3	9.8	12.9	15.2	14.1
Asset turnover	31.7	37.5	41.9	33.5	37.8
Return on assets	2.3	3.7	5.4	5.1	5.3
Recurring return on equity	7.1	10.4	14.0	12.3	12.3

Valuation



(x)	Dec-17	Dec-18	Dec-19	Dec-20	PTM**
Price-to-sales	0.7	0.8	0.5	1.2	1.0
Price-to-earnings	9.7	8.1	4.2	7.6	6.9
Price-to-book	0.7	0.9	0.5	0.9	0.9
PE-to-EPS growth (PEG)	nm	0.2	0.1	9.1	0.6
EV/EBIT	8.2	7.1	5.1	6.1	5.3

Momentum



(%)	Dec-17	Dec-18	Dec-19	Dec-20	PTM**
Revenue growth	9.4	15.8	8.7	(14.9)	9.2
Recurring EPS growth	(31.2)	53.4	46.2	0.8	10.8
Operating profit margin chg. (bps)	(691)	(95)	(25)	511	103
	6mth	3mth	1mth	3wk	1wk
Price change	(7.1)	(9.9)	(7.0)	(5.7)	(2.0)

Risk

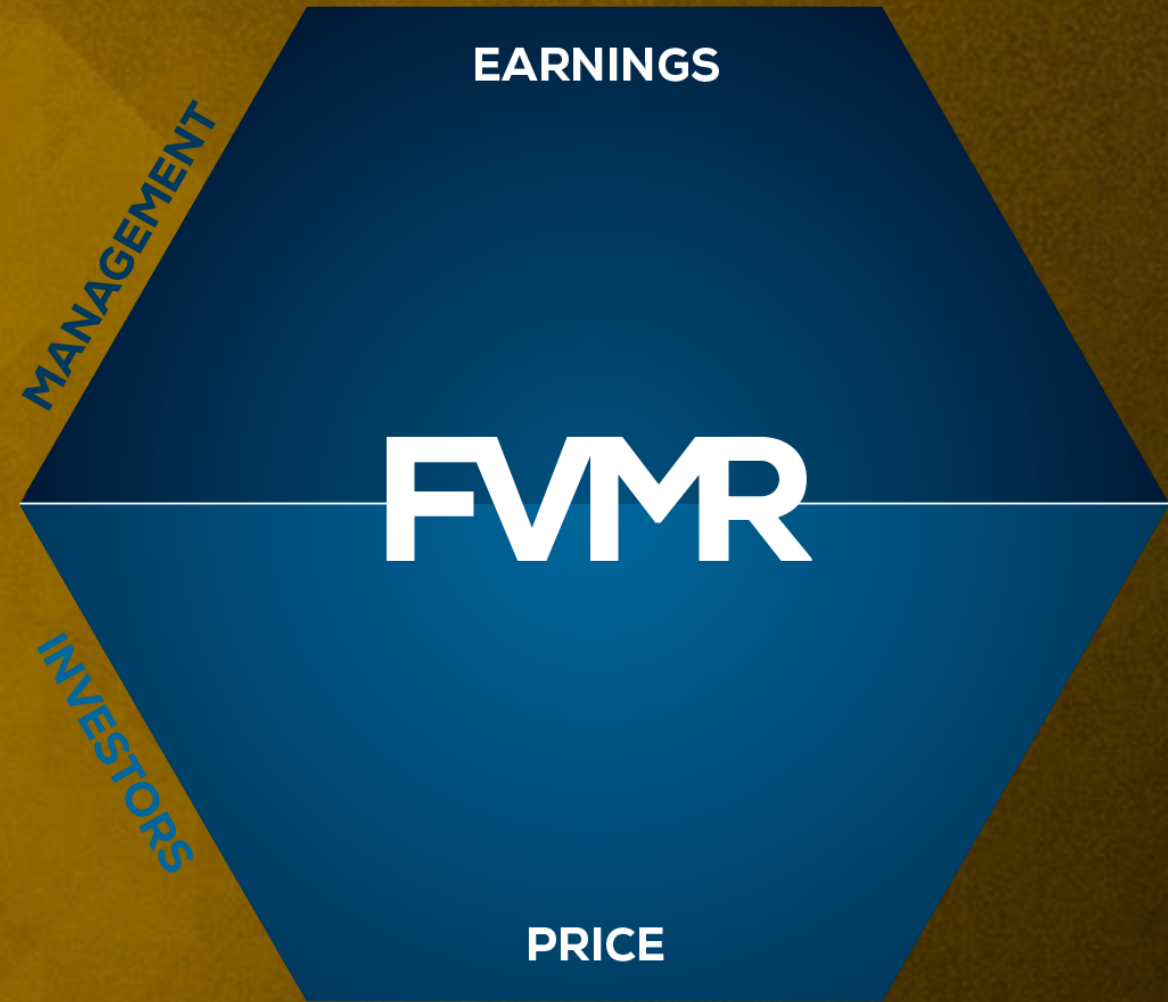


(x)	Dec-17	Dec-18	Dec-19	Dec-20	PTM**
Current ratio	1.8	1.7	1.5	1.5	1.6
Net debt-to-equity (%)	125.1	101.3	69.9	48.7	34.1
Times-interest-earned	2.9	3.9	4.8	5.6	6.5
	5yr	3yr	1yr	6mth	3mth
Beta	0.4	0.4	0.3	0.4	0.5

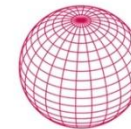
Note: Benchmarking against 120 non-financial companies in Philippines.

Recently, I created a short
online course explaining my
FVMR investing approach

I usually sell it
for \$97 but for
a limited time
I am offering
it for FREE



Analysts see strong upside



Sales

Story

FVMR

Value

WCB

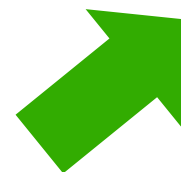
Risks

Analyst consensus valuation

Recommendation	Oct-21	Nov-21	Dec-21	Current
Strong buy	3	3	3	3
Buy	1	1	2	2
Hold	1	2	1	1
Sell	-	-	-	-
Strong sell	-	-	-	-
Average score	1.6	1.8	1.7	1.7

Price target	Oct-21	Nov-21	Dec-21	Current
Median	34	34	35	35
Mean	36	37	37	38

6
analysts

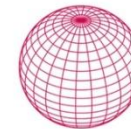


Upside: 28%

Analyst consensus 3-year forecast

(%)	18	19	20	21E	22E	23E
Revenue growth	2.5	8.7	(14.9)	11.8	2.3	7.0
Gross margin	34.6	35.3	39.6	na	na	na
EBIT margin	25.4	25.2	29.0	29.4	30.2	28.4
Net margin	11.2	13.8	15.1	13.8	14.2	15.4

- ★ Almost all analysts have a BUY recommendation, with only 1 analyst staying on HOLD
- ★ Consensus expects solid revenue growth for the future given the growing demand for energy
 - Also, margins are expected to stay stable at a high level, meaning that analysts are positive about the LNG substitution



Sales

Story

FVMR

Value

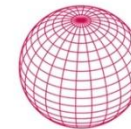
WCB

Risks

(YE Dec, US\$ m)	2019A	2020A	2021E	2022E
Revenue	2,151	1,830	2,050	2,091
Cost of goods & services	(1,392)	(1,105)	(1,250)	(1,275)
Gross profit	760	726	799	815
SG&A	(217)	(194)	(205)	(209)
Other operating (exp)/inc	0	0	(40)	(40)
EBIT	543	532	554	566
Interest expense (net)	(93)	(87)	(74)	(69)
Other non-operating inc/(exp)	27	28	28	29
Earnings before taxes (EBT)	478	472	508	526
Income tax	(67)	(85)	(107)	(110)
Earnings after taxes (EAT)	411	387	402	416
Equity income/Minority interest	(118)	(118)	(120)	(125)
Earnings from cont. operations	293	269	281	291
Forex/Exceptionals before tax	4	7	-	-
Net profit	296	276	281	291

★ FGEN has delivered remarkably stable profits and there is no reason to assume differently in the future

- **Long-term take-off agreements ensure stable margins**



Sales

Story

FVMR

Value

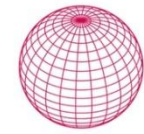
WCB

Risks

(YE Dec, US\$ m)	2019A	2020A	2021E	2022E
Cash & short-term investments	682	992	1,025	1,341
Accounts receivable	433	443	393	401
Inventories	129	178	174	177
Other current assets	57	54	59	61
Total current assets	1,300	1,666	1,651	1,979
Long-term investments	-	-	-	-
Net fixed assets	2,611	2,679	2,709	2,741
Intangible assets	46	36	32	28
Goodwill	955	1,005	965	965
Other long-term assets	297	322	306	309
Total assets	5,210	5,708	5,663	6,022

- ★ Currently, there are no concrete expansion plans in place
 - I believe that FGEN might add a few smaller renewable energy projects over time but does not undergo aggressive acquisitions

Balance sheet - liabilities



VALUATION MASTER CLASS

Sales

Story

FVMR

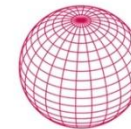
Value

WCB

Risks

(YE Dec, US\$ m)	2019A	2020A	2021E	2022E
Overdrafts & short-term loans	317	466	401	397
Accounts payable	320	371	340	347
Other current liabilities	206	246	205	209
Total current liabilities	842	1,083	946	953
Long-term debt	1,631	1,491	1,342	1,329
Other long-term liabilities	145	178	180	182
Total liabilities	2,618	2,752	2,469	2,464
Minority interest	467	533	653	778
Paid-up capital - Common shares	1,317	1,387	1,387	1,387
Paid-up capital - Preferred shares	78	86	86	86
Retained earnings	1,478	1,696	1,926	2,165
Revaluation/Forex/Others	(749)	(745)	(858)	(858)
Total equity	2,125	2,423	2,541	2,780
Total liab & shareholders' equity	5,210	5,708	5,663	6,022

- ★ Its strong cash flow generation allows FGEN to reduce its debt over time and fund CAPEX internally



Sales

Story

FVMR

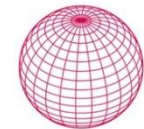
Value

WCB

Risks

(YE Dec)	2019A	2020A	2021E	2022E
General growth (YoY, %)				
Revenue	8.7	(14.9)	12.0	2.0
Assets	3.0	9.6	(0.8)	6.3
Gross profit	11.0	(4.5)	10.2	2.0
Operating profit	8.1	(2.1)	4.3	2.1
Attributable profit	33.9	(6.9)	2.0	3.5
EPS	35.7	(5.5)	2.1	3.5
Recurring EPS	26.8	(7.9)	11.3	3.5
Du Pont analysis (%)				
Net profit margin	13.8	15.1	13.7	13.9
Revenue per PHP100 of assets	41.9	33.5	36.1	35.8
Assets/equity (x)	2.3	2.1	2.0	1.9
Return on equity	13.5	10.8	9.8	9.4
Others (%)				
Effective tax rate	13.9	17.8	21.0	21.0
Dividend payout ratio	12.5	14.3	12.5	12.5

- ★ FGEN paid out stable and growing dividends
 - The small payout ratio of less than 15% still delivers a dividend yield of around 3%, which is above Philippine average
 - There is potential to pay out more and it could turn into a dividend play over the next few years



Sales

Story

FVMR

Value

WCB

Risks

(YE Dec)	2019A	2020A	2021E	2022E
Internal liquidity (x)				
Current ratio	1.5	1.5	1.7	2.1
Quick, or acid test ratio	1.4	1.4	1.6	1.9
Working cap. mgmt (Days)				
Inventory conversion period	31	50	51	50
Receivables collection period	68	86	73	68
Days from raw mat to coll	98	136	124	118
Payables deferral period	83	113	102	97
Cash conversion cycle	16	24	22	21
Profitability ratios (%)				
Gross profit margin	35.3	39.6	39.0	39.0
EBIT margin	25.2	29.0	27.0	27.1
EBIT return on avg assets	10.6	9.7	9.7	9.7
Return on average assets	5.8	5.1	4.9	5.0
Financial risk (x)				
Liabilities-to-assets (%)	50.3	48.2	43.6	40.9
Debt-to-equity	0.8	0.7	0.6	0.5
Net debt-to-equity	0.5	0.4	0.2	0.1
Times-interest-earned	7.0	8.0	10.5	11.6
Effective interest rate (%)	5.3	4.9	4.2	4.2

★ Strong margins translate into stable return on assets

If you want to learn how to value companies, check out my 6-week, **online Valuation Master Class Boot Camp**

- 🌐 **PRACTICAL** – Learn practical stock valuation skills and apply them to value actual companies
- 🌐 **FOCUSED** – Access the tools, tips, and tricks I used to become a #1 financial analyst
- 🌐 **INSPIRING** – Join a group of inspiring, like-minded financial professionals
- 🌐 **NETWORK** – Get a job through my network of thousands of financial industry leaders



**Class starts
March 7th!**

Save US\$402 until February 28th!

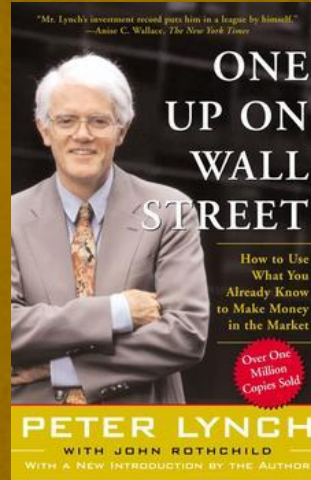


Scan this QR code to learn more & register to get the full curriculum or just go to
ValuationMasterClass.com
/bootcamp

A. Stotz Investment Research Stock Picking Checklist

Inspired by

Peter Lynch's book



- ★ Where he talked about "ten baggers", stocks that go up 10x
- ★ We did extensive research on ten baggers and found...
- ★ 9 factors that drive long-term share price performance



Long-term share price performance potential



Sales

Story

FVMR

WCB

Ratios

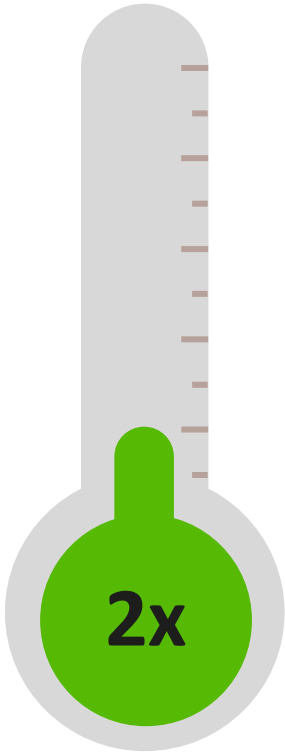
Value

Risks

A. Stotz Investment Research Stock Picking Checklist

	Potential	Comment
1. Management – Commitment to growth	Weak	Flat revenue in the past as FGEN did not add much further capacity over time
2. Growth – Can grow at double-digits	Moderate	Demand for energy might grow in line with population growth
3. Margin – High gross margin	Good	90% of its energy generation is covered by long-term contracts, ensuring stable profits
4. Predictability – Minimal non-core expenses	Good	Non-core items are relatively small
5. Intensity – Sales grow faster than assets	Weak	Heavy fixed investments required to grow; asset turnover is with 33% very low
6. Conversion – Low cash conversion cycle	Moderate	Cash conversion cycle is moderate and stood at 24 days as of 2020
7. Cash flow – Consistently positive cash flow	Good	Consistent and strong operating cash flows were able to cover investing outflows
8. Capital – Access to capital	Moderate	Leverage is moderate. Net debt-to-equity stood at 0.4x in 2020
9. Valuation – Reasonable valuation	Good	Trades lower on both 21E PE and PB compared to Philippine Telecoms, but higher ROE

10x Bagger Potential





Sales

Story

FVMR

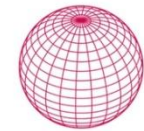
Value

WCB

Risks

(YE Dec, US\$ m)	2019A	2020A	2021E	2022E
EBIT	543	532	554	566
<i>Est tax rate (%)</i>	<i>14</i>	<i>18</i>	<i>21</i>	<i>21</i>
NOPAT	467	437	438	447
Add: Depre & amort	225	233	265	280
Less: CAPEX	(116)	(147)	(273)	(288)
Chg in A/R	(58)	(10)	50	(8)
Chg in inventory	(21)	(49)	4	(3)
Chg in oth curr assets	8	3	(6)	(1)
Chg in A/P	1	51	(30)	7
Chg in oth curr liabs	83	41	(41)	4
Less: Chg in working cap	14	36	(24)	(2)
Less: Chg in invest cap				
Free cash flow to firm	590	560	406	437

- ★ FGEN cash flows on a consistent basis and the market might not have appreciated that fact yet



Sales

Story

FVMR

Value

WCB

Risks

Forecast assumptions

3-year average	Consensus	My assumptions
Revenue growth (CAGR)	7.0	6.6
Gross margin	na	38.8
EBIT margin	29.3	25.0
Net margin	14.5	14.0

My valuation method

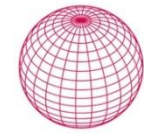
Market: Philippines

Market risk-free rate	5.0
Market equity risk premium	8.0
Market return	13.0
Company beta (x)	0.8
COE	11.0

WACC	9.3
Terminal growth rate	2.0

Valuation Method:
FCFF

- ★ My short-term outlook is roughly in line with consensus
- ★ I am bit more optimistic on the long-term future and believe the company to maintain a great ROIC of 10-12% over time



Sales

Story

FVMR

WCB

Ratios

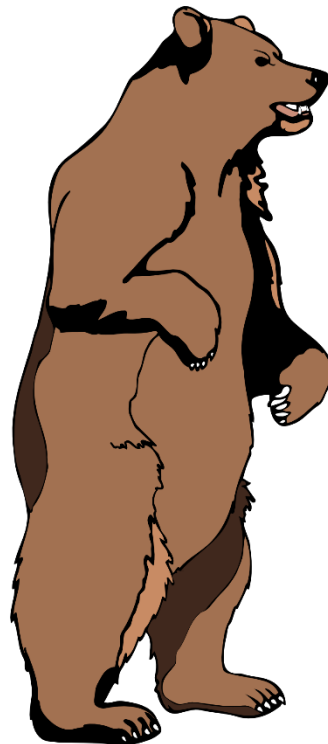
Value

Risks

Bear

PHP35

(Upside 27%)



Base

PHP38

(Upside 40%)



Bull

PHP42

(Upside 54%)



World Class Benchmarking Scorecard

- ★ We identify a company's competitive position relative to global peers
- ★ We use a composite rank of profitability and growth, called "Profitable Growth"
- ★ Scale from 1 (Best) to 10 (Worst)



Strong profitability but average growth



Sales

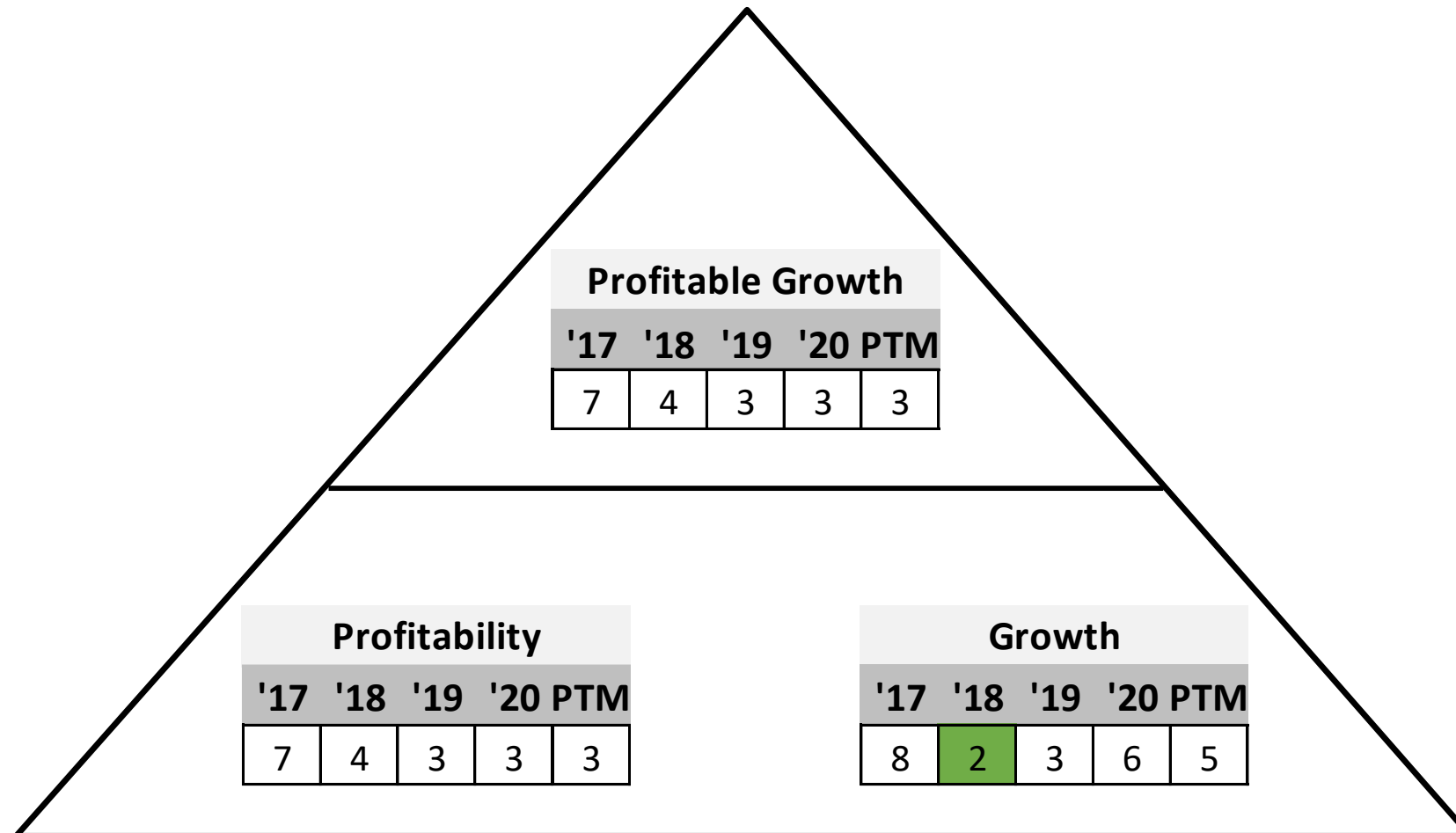
Story

FVMR

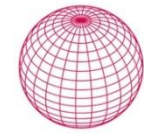
Value

WCB

Risks



Benchmarked against 320 large Utilities companies worldwide.



Sales

Story

FVMR

Value

WCB

Risks

- ★ Delay in building the LNG terminal could disrupt its gas production
- ★ Unexpected outages of production (e.g., weather conditions, transmission constraints)
- ★ High dependency on Meralco, which makes up 50% of its revenue

CONCLUSION

- FGEN to remain a cash flow machine as supply problem seems to be resolved
- Early shift to green energy gives it a timing advantage in a coal-dominant country
- Valuation is cheap; institutional interest could unlock upside



Is First Gen an
**overlooked power
play** that deserves
a **re-rating?**

