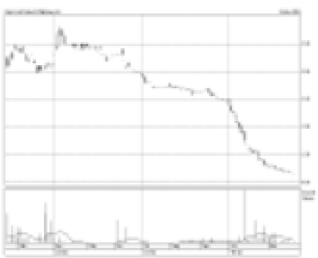
AB Capital Securities, Inc.

November 25, 2008

Pepsi Cola Philippines (PIP)

BUY

Price (Nov.21)	0.65
Target Price	1.50
52 week high	3.30
52 week low	0.65
Shares O/S (M)	3,694
Freefloat (M)	1,330
Market Cap (B)	2.40
Daily Turnover (M)	15.92
Dividend Yield	6.50%



	PIP	Industry	Market
3 mos	-69.63%	-31.60%	-33.53%
6 mos	-76.79%	-41.19%	-38.52%
YTD	-77.19%	-52.91%	-51.24%

Tapping a New Market

Summary

Investing in Pepsi-Cola Philippines Inc. (PIP) is to be considered due to its growth prospects in the Non-Carbonated Beverage (NCB) market and its sizeable share in the broad Carbonated Softdrink (CSD) market. Among other comparable companies, the cost of investing in Pepsi-Cola Philippines is relatively cheap.

• PIP is a licensed bottler of PepsiCo beverages in the Philippines. Carrying a strong brand name, Pepsi-Cola Philippines will remain in one of the top spots in the beverage industry.

• Pepsi-Cola will remain a defensive investment as demand for beverages will stay strong. Growth is driven by its emerging NCB segment while its CSD products will continue to contribute a steady share of revenues.

• The company is virtually debt free with a 0.03 Debt-to-Equity ratio. They gave out dividends of Php0.10 this November. In the succeeding years, up to 50% of annual net income will be paid out as dividends. Both P/E and P/B ratios of Pepsi-Cola are attractive compared to its comparable companies. Its return on equity is significantly higher than the beverage industry and market average.

• In the long run, revenues from the CSD segment will remain steady due to the maturity of the market. Growth will be fueled by the NCB segment.

• With a discount of 131% to its fair value, PIP would be a cheap investment. Trading at a price of Php0.65 per share and with a WACC of 11.20%, the fair value arrived for PIP is Php1.50 per share. Compared to an average P/E of 16.4x for its peer companies in the region, the company has a P/E ratio of 3.1x. Its ROE is high at 14.41% against an average of 8.17% to 12.9% for both the beverage industry and the market.

• Gross profit margin for fiscal year 2008 declined slightly due to factors such as rising costs, competition, and weather disturbances. But as inflation levels temper, cost of goods sold and expenses will drop.

Maria Arlysa E. Narciso
Equities Analyst
898-7584

AB Capital Securities Inc.
8th Floor, Phinma Plaza
39 Plaza Drive, Rockwell Center,
Makati City, Philippines
Tel: 898-7555
Fax: 898-7595, 898-7597

email: abcsi@abcapital.com.ph
website: www.abcapitalonline.com

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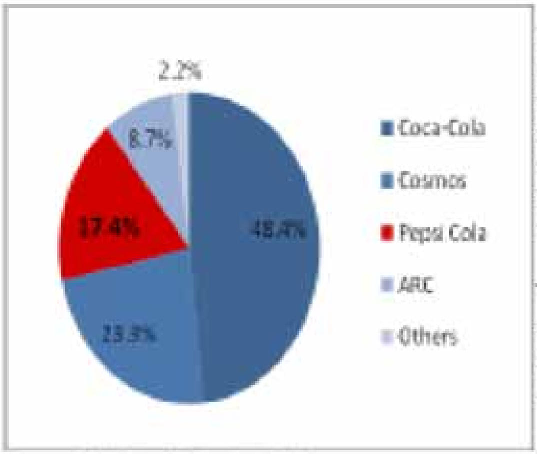
Pepsi Cola Philippines (PIP) BUY

Figure 1: CSD Market Share



Source: AC Nielsen (September 2007)

in P millions	2006	2007	2008
Assets	5,716.30	6,785.30	8,044.79
Liabilities	2,993.00	3,461.60	2,765.40
Equity	2,723.30	3,323.70	5,279.39

Strong Foundation

With strength in its brand name and a wide range of products under its wings, Pepsi retains a strategic hold in the beverage market. The growth potential of its NCB segment will be its main driver in revenues. PIP currently manufactures tea, juice, and sports drink products in its Non-Carbonated Beverage segment. Known brands under this are Lipton, Tropicana, and Gatorade.

The company is a defensive player as consumption or demand will be relatively resilient. Despite a slow down in the economy, the industry and the company itself will remain strong.

Growth and expansion will be achieved by tapping the emerging NCB market. The NCB market share is to be improved by widening the distribution network and outlet reach. Other planned investments include in-store refrigeration equipment and trucks, and larger warehouse spaces for storage.

Financial Strength

in P millions	2006	2007	2008	2009F	2010F
Total Sales	10,992.81	12,916.21	12,980.89	13,596.00	14,331.08
Gross Margin	38.44%	36.52%	36.75%	37.24%	37.24%
Net Income	868.75	1,011.39	760.70	782.21	735.08
NI Margin	7.90%	7.83%	5.86%	5.75%	5.13%
EPS	0.24	0.27	0.21	0.21	0.20
ROE	31.90%	30.43%	14.41%	12.90%	10.82%

Future performance will be driven by the fast growth of NCBs as the company capitalizes on this growing market. Margins are assumed maintained for the next years. Constant improvements in its market reach and product distribution contributes to this revenue growth.

The high inflation figures caused operating expenses to balloon, slightly outpacing revenue growth. This also led to a drop in the 2008 Net Income Margin by almost 2 pecentage points and lowered the Net Income by more than Php200 million. Revenue share of NCBs to net sales will grow by at least 4 percentage points while CSD's share slightly diminishes. With the mature CSD market, PIP intends to keep its current market share in the said segment while utilizing the high potential of the NCB market.

Risks

CSD market has reached its maturity with an expected steady future sales. Consumers have shown preference for NCBs leading to growing sales from this segment. This may likely be the revenue driver of the company.

The increase in prices of raw materials significantly affects operating costs. In its 2006 and 2007 fiscal years, the company's expenses for sugar and beverage concentrates made up 26% of their Cost of Goods Sold. With slowing inflation levels, the company's Net Income may improve.

Distribution covers only 46% of the market.

Figure 2: Sales in Php thousands

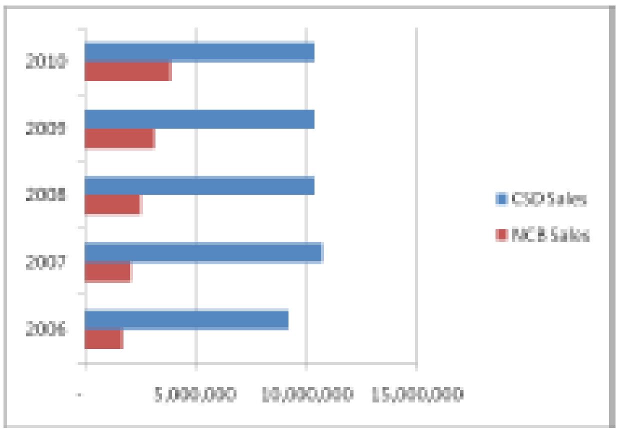
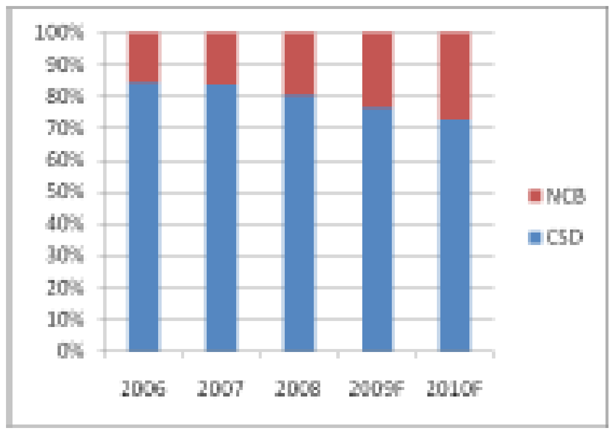


Figure 3: Share in Net Sales



Valuation

A modest growth in sales is expected for the company in the next few years. This is due to the fact that the CSD market is nearing its maturity while the NCB market is just beginning to grow. Though revenues from CSDs turn out to be flat or steady, the segment will still contribute a sizeable amount of revenues to the company. Sales growth in the next few years is to be driven by the NCB segment.

Using a WACC of 11.20%, PIP's fair value was seen at Php1.50 per share. At a current price of Php0.65, this a 131% discount. As such, the company is deemed undervalued.

Assumptions

The growth rate for CSD sales is forecast to drop and was kept at a constant level in the next years. This is to account for the mature CSD market and the growing market for NCBs. Conversely, we assumed a moderate NCB sales growth as this segment continues to develop.

As mandated by R.A.9337 which took effect November of 2005, the Corporate Income Tax Rate that will be used is 35% of net taxable income. This will be reduced to 30% starting January 1, 2009.

The high inflation figures for the past months are expected to have an impact to the company's FY 2008 expenses. The lagged effects will likely be carried over on the first half expenses of FY 2009. This will ease in the next fiscal years as inflation starts to temper.

Pepsi Cola Philippines (PIP)

BUY

Figure 4: P/E Ratio

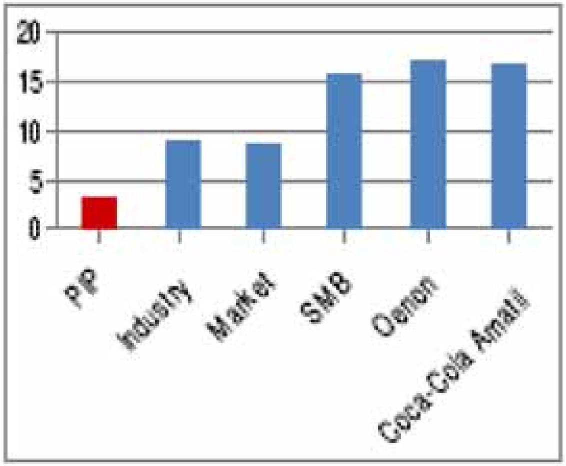


Figure 5: P/B Ratio

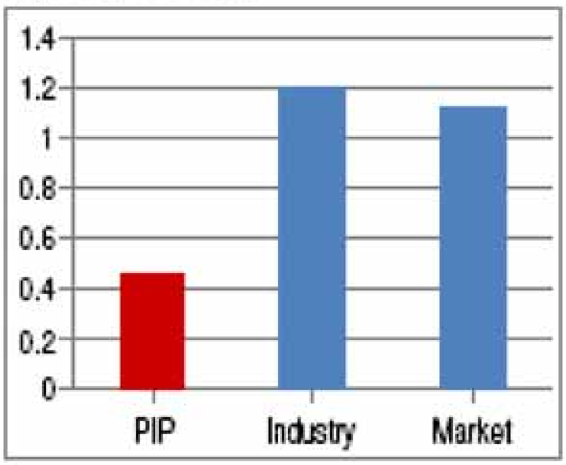
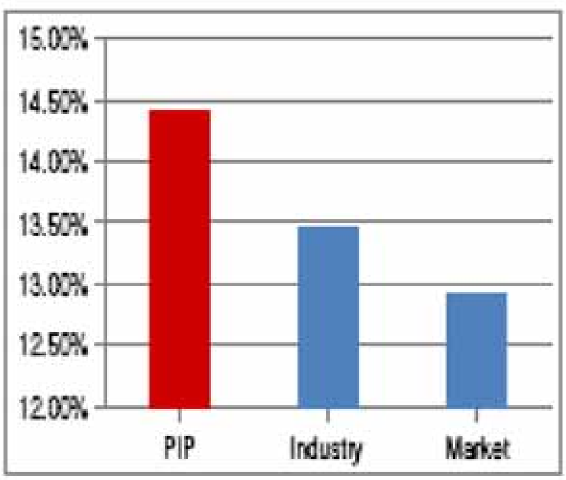


Figure 6: Return on Equity



Cheap Investment, High Return

Pepsi-Cola's P/E ratio is 3.1x. This is significantly cheaper than the 7.36x average P/E of the beverage industry and the 8.67x P/E of the market. For a current price of Php0.65 per share, a dividend yield of 6.5% is expected.

PIP has a P/B of 0.45x compared to the beverage industry average of 0.55x and the market's 1.12x. Its cheap P/B assures a 14.41% Return on Equity which is more attractive than the industry's 8.17% return and the market's 12.91% ROE.

A Good Buy

The strong foothold and demand for the beverage sector in the market will remain robust and growing in the future.

In the succeeding years, Pepsi's growth opportunity lies in developing its NCB segment. Growing demand for non-carbonated beverages would be Pepsi's driver for higher revenues.

As of 2007, PIP's distribution covers only 46% of the market. With a very low debt, the company can afford new borrowings for the expansion of its distribution channels. This would translate to higher sales and wider market reach for the company.

Pepsi-Cola is a more attractive investment than other comparable companies. Its expected return and dividend yield with such low valuations makes PIP a cheap investment. Given its growth potential in the NCB market, its cheap valuation, and strong brand name and market hold, Pepsi-Cola Philippines is rated as a Buy.