

Bubble... Trouble ...Bubble?




MicroCope


Experienced the property market bubble during 2002-05, the US got trouble due to the 'Subprime' concern afterward. The recent dose of the Federal Reserve's 50-basis point cut in overnight rates to 4.75% seemed to let the financial market take a breath. Many stock markets (except the US market) and commodity prices surged to new highs. Will the bull run last for a while, or few years?

While the Fed lowered rates, central banks in Europe, the UK, Canada, South Korea and Australia have held off raising rates. Even the Bank of Japan, which has been chomping at the bit to normalize monetary policy, she chose to leave its overnight lending rate at 0.5% with only one of nine board members dissenting. For investors, they would like to seek guidance on the way markets are heading. Back to early 1997, markets were abuzz

with speculation about Thailand's ability to defend its currency and service its debts. Analysts mostly ignored the issue. By early 1998, Thailand had morphed into an Asia problem and begun to hurt the stock prices of US banks. Then Russia defaulted and in the fall of 1998, hedge fund Long-Term Capital Management had to be bailed out. The Standard & Poor's 500 Index fell 15% in six weeks, the Nasdaq Composite Index tumbled 30% in less than three months. The Fed responded by cutting rates three times in September, October and November of 1998. Concerns about the year 2000 computer bug also prompted the Fed to pump liquidity into markets. The result was the "Tech Bubble". The late 1990s show that investors can make money in aging bull markets that become bubbles. Where is the "Bull" now heading?

Less likely for the US! The latest government data shows unexpected job losses in August, sagging core retail sales and no relief in sight for the moribund housing market. Now that US gross domestic product probably is growing at an annualized rate of less than 2%, speculation is rampant that another Fed rate cut is assured before January. What's more, many investors see the Fed reacting to rising oil prices by cutting interest rates to preserve growth and the European Central Bank by raising rates to ward off inflation. Since the start of 1993, the dollar has been the worst performer among the world's 10 major currencies when oil-price growth is stronger than usual. That is bad news for the dollar, let alone the US stockmarket. 

Gold prices at one point topped \$746 an ounce, a 28-year high in response to the dollar's decline. Since gold is priced in terms of US\$, the rise and fall of our fiat paper currency may prove to be the most powerful catalyst that changes the direction of gold price. Although gold has largely lost its role as a form of currency, the central banks still use it as an international trading currency and a safe haven in time of crisis.

The Dow/Gold Ratio is a powerful measure of the gold value relative to the stockmarket. Now the ratio is 19x, which is higher than the long-term average of 16 for 1901-2007. Gold is the most unbiased form of money in existence. Fake government paper money comes and goes, but gold has been money for thousands of years. It is the ultimate store of wealth. Paper assets excel when everyone is fixated on growth. When the growth phase ends, and preservation of wealth becomes the paramount concern, gold tends to excel. When paper burns, gold shines. Assume the Dow remains at 14,000 level, the ratio of 16x implies gold prices can hit as high as US\$875/ounce next year. 

MARKET BRIEFING

YTD % (local curr)

US DJ	13,820 (+10.9%)
Nasdaq	2,671 (+10.6%)
Euro Stoxx 50	4,370 (+6.1%)
HSI	25,843 (+29.4%)
Japan NK225	16,312 (-5.3%)
China Shanghai Composite	5,454 (+103.9%)
Singapore	3,542 (+18.6%)
India BSE30	16,564 (+20.1%)
Brazil BOVESPA	57,798 (+30.0%)
Aus All Ord	6,371 (+12.9%)
US-10yr Bond Yield	4.69%
As at 21/9/07	


Insight:

"Mirror Fund vs. Direct Fund"


One-stop Service?

Mirror funds invest in other funds – the underlying funds – and will invest exclusively in the underlying fund, managed by fund management companies external to the mirror fund operator, usually insurance companies. The mirror fund may also hold a small amount of cash, in addition to investment in the underlying fund. As such, the unit price of the mirror fund will differ from the price of the underlying fund. Generally speaking, mirror funds keep 5% to 10% of their portfolios in cash as a cushion for buying opportunities and redemptions,

sometimes more when markets look uncertain. In a market with an upward bias, this creates a drag on performance. A fund's ability to handle cash flow

also affect performance. Cash drag occurs when new money to the fund is not invested in a timely fashion, resulting in stocks being purchased at higher prices. In a rising market even a one-day delay can impact returns. However, the mechanism of mirror fund facilitates asset allocation with the flexibility to switch between one mirror fund and the other without substantial transaction costs, especially when there involve fund switching between different fund houses. Accordingly, consumers should analyze their needs first before choosing the appropriate plan. 

A-Z Financial Tools

Beta measures the risk of a share or mutual fund relative to the market (or benchmark) risk. If the benchmark goes up by 20%, a share with a beta of 1.5 would increase by approximately by 30%. High beta mutual funds would on average outperform in a bull market, or underperform when the market falls. They are quite simply more sensitive to a benchmark move. 



IBC Group

Comprehensive Financial Planning
Wealth Management Advisory
International Business Advisory
Call 2268 6688
Email: insider@ibccapital.com

Next Insight

"Myth of Retirement Planning"