


When US recovers, can Asia rebound?



Microscope

Asia has the third largest nominal GDP of all continents, after North America and Europe. As of 2007, the largest national economy within Asia, in terms of gross domestic product, is that of China followed by that of India and that of Japan. Historically, Japan has had the largest economy in Asia and second-largest of any single nation in the world, after surpassing the Soviet Union in 1986 and Germany in 1968. In the late 1980s and early 1990s, Japan's GDP was almost as large (current exchange rate method) as that of the rest of Asia combined. In 1995, Japan's economy nearly equalled that of the USA to tie as the largest economy in the world for a day, after the Japanese currency reached a record high of yen. Economic growth in Asia since World War II to the 1990s had been concentrated in quite a few countries of the Pacific Rim (Philippines, Thailand, Malaysia, Singapore, Hong Kong, Taiwan, Japan, and S.Korea). In the long run, it is forecasted that the People's Republic of China will surpass Japan to have the largest nominal and PPP-adjusted GDP in Asia within a decade. India is also forecasted to overtake Japan in terms of Nominal GDP by 2020. 

During the last six months when US sank, Asia could not swim. The correlation of performance between Asia countries and the US is high, primarily because the US represents almost half of global demand. After the announcement of US economic figures recently, including employment rates and business indicators, many analysts expect a broad, sustained recovery in both the economy and the financial markets coming in second half of this year. At the same time, policy makers are echoing the mood on Wall Street. Things appear to have improved in the financial sector, especially on the aggressive write-off of bad debt for the last quarter and that significantly reduces the risk of a financial meltdown in the future. According to Bloomberg, US Treasury Secretary Henry Paulson said on last Thursday that the US was closer to the end of this problem than they were to the beginning. In addition, a report from the Bank

of England concluded that mortgage securities, which have been at the heart of the financial troubles, probably have fallen too far. The central bank also said prices of such securities should improve gradually in the coming months. Furthermore, the costs of insuring against the failure of banks and other companies have fallen sharply since the end of March. According to Bloomberg, pressures on financial firms also appear to have eased somewhat because banks have tended to borrow less from the Fed in recent weeks than they did in March and early April. The cost of interbank borrowing has also fallen. Although optimism on the global stockmarkets is premature, the recovery of sentiment and increasing risk appetite is reflecting on rising asset prices. As such, capital flow to Asia may soon happen once there are further confirmations about the fact

that subprime crisis is fading out. In fact, Asian economies still have growth momentum even as the US faces a slowdown. Last month, the Monetary Authority of Singapore said the city-state could still achieve full-year gross domestic growth of 4-6%, barring a sharp downturn in the US economy. Company-wise, Japan Airlines Corp had roughly doubled its 2007/08 profit estimates to above market expectations, thanks to strong business travel demand on its international routes. International demand has been showing a strong recovery with an improvement in Japanese companies' earnings and an export-backed upswing in the country's economy increasing the appetite for business travel. This earnings result confirmed the solid growth in economy in this region. 

MARKET BRIEFING

YTD % (local curr)


US DJ	13,058 (-1.6%)
Nasdaq	2,476 (-6.6%)
Euro Stoxx 50	3,877 (-11.9%)
HSI	26,241 (-5.7%)
Japan NK225	14,049 (-8.2%)
China Shanghai Composite	3,693 (-29.8%)
Singapore	3,236 (-6.6%)
India BSE30	17,600 (-13.2%)
Brazil BOVESPA	69,366 (+8.6%)
Aus All Ord	5,760 (-10.3%)
US-10yr Bond	Yield 3.86%

As at 02/05/08


Insight: "Hedge against Stagflation"

Over the past 25 years, stagflation – inflation combined with a recession – has been avoided. Traders are buying commodities as a hedge against inflation and thus, implicitly, predicting stagflation. In the past, headline inflation in the US started from 5.5% in 1970, peaked at 12.2% in 1974 and again at 13.3% in 1979. For the '70s as a whole, inflation averaged 7.4% annually. Real economic growth tumbled. Subtracting for inflation, the US economy grew by just 3.27% on average from 1970 to 1979, quite a drop from the 4.44% average annual growth in real gross domestic product recorded from 1960 to 1969. And in two

years during the 1970s, after subtracting for inflation, the American economy actually declined in size -- by 0.5% in 1974 and 0.2% in 1975. In fact, the 1970s weren't a great time for investors. S&P 500 index

returned a compound annual 5.9% from 1970 to 1979. With inflation running at an annual 7.4%, an investor in the stock market was losing ground every year to inflation. Bond investors had it even worse. So, what can we do in 2008? Remember that stagflation is possible but not certain. Moreover, many investment tools should work pretty well in 2008. Commodities, energy, gold and growth stocks in sectors of the economy that will grow even if the economy slows. And any defensive growth stock with enough pricing power to raise its prices fast enough to stay ahead of inflation. 

A-Z Financial Tools

Return on Equity (ROE) is an indicator of corporate profitability, determined by dividing net income for the past 12 months by common stockholder equity (adjusted for stock splits). Investors use ROE as a measure of how a company is using its money. ROE may be decomposed into return on assets (ROA) multiplied by financial leverage (total assets/total equity). 



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