

Global: Economic Recovery?




Microscope

Recently, the easing credit from banks to mortgage-related market, especially for “jumbo” loan, is a positive signal. The collapse of the market without government support last year forced lenders to hold on to most of the jumbo mortgages they made. Issuance of bonds backed by new prime-jumbo, subprime or Alt-A loans plummeted 98% last year to \$11.1 billion, according to Inside Mortgage Finance. While, the US financial system are improving and the TARP has funded billions of dollars in government investments for faltering banks, all these helped rescue the US property market through helping homeowners with mortgage refinancing. JPMorgan Chase & Co. and Citigroup Inc. are expanding in jumbo mortgages used to buy the most expensive homes, helping revive a market that shriveled amid a three-year jump in homeowner defaults. The two New York-based banks are signaling new interest in a market hobbled since 2007, when record-breaking defaults on home loans caused investors to flee securities backed by mortgages. No matter how they price, the increasing supply of jumbo loan will translate into more credit easing in coming months. 

The global recession is showing signs of easing as financial markets thaw. Government reports last week showed that Europe’s manufacturing and service industries contracted at the slowest pace in nine months in June, while US consumer spending rose in May, according to Bloomberg. The Organization for Economic Cooperation and Development also raised its forecast for the economy of its 30 member nations for the first time in two years last week. In addition, although the process of restructuring and strengthening bank balance sheets is not yet completed, banks have successfully raised capital from the private sector. During this financial tsunami, financial institutions around the world have amassed losses of more than \$1.4 trillion, according to Bloomberg. In Europe, governments and central banks are on the hook for more than 3.7 trillion euros (\$5.2 trillion) of guarantees and funding. UBS

AG, the European bank with the biggest losses from the credit crisis, said on June 25 it expects a second-quarter loss. Meanwhile, governments and central banks are tightening banking rules to strengthen the global financial system. US President Barack Obama this month also proposed new rules to tighten oversight, while European leaders agreed on a sweeping overhaul of their regulations. Figure-wise, unemployment in the US was expected to rise at a slower pace and the manufacturing slump eased this month, according to the Bloomberg’s survey last week. The jobless rate rose 0.2% to 9.6%, the highest level in 26 years, according to the median of 58 estimates in a Bloomberg News survey. The gain would be the smallest since November 2008. A survey of purchasing managers may show manufacturing shrank at the mildest pace in 10 months. In

fact, government’s measures to stabilize housing and consumer spending for the past few months are only now starting to pay off, indicating it will take months before a recovery develops. The job market will remain a big threat to the emerging rebound as companies from GM Corp. to Kimberly-Clark Corp. focus on cutting costs by trimming payrolls. Employers have eliminated 6m jobs since the recession began in December 2007, the most of any economic slump in the post-World War II era. The payrolls report may also show manufacturers slashed workers this month. The job reductions and plant shutdowns may persist, reflecting the fallout from the bankruptcies of GM and Chrysler. Beside autos, the downturn may be easing. But the economic status will convince the Fed to keep rates unchanged for some time. 

MARKET BRIEFING


YTD % (local curr)

US DJ	8,438 (-3.9%)
Nasdaq	1,838 (16.6%)
Euro Stoxx 50	2,389 (-2.5%)
HSI	18,600 (29.3%)
Japan NK225	9,877 (11.5%)
China Shanghai Composite	2,928 (60.8%)
Singapore	2,317 (31.6%)
India BSE30	14,764 (53.0%)
Brazil BOVESPA	51,485 (37.1%)
Aus All Ord	3,899 (6.6%)
US-10yr Bond	Yield 3.54%


As at 26/06/09

Insight: “Carry Trade”

Carry trade is a popular trading strategy used in the past decade, especially in currencies market. Traders buy high interest currencies and sell currencies with low interest rates. A trader using this strategy attempts to capture the difference between the rates, which can often be substantial, depending on the amount of leverage the investor chooses to use. These positions ensure that each trading day rollover-interest will be posted to the trader’s account. Thus the carry trade has the potential to significantly enhance a trader’s return. Here’s an example of a “yen carry trade”: a trader borrows 10,000 yen from a Japanese bank, converts the

funds into US dollars and buys a bond for the equivalent amount. Let’s assume that the bond pays 3% and the Japanese interest rate is set at 0%. The trader stands to make a profit of 3% as long as the exchange rate between the countries does not change. Many professional traders use this trade because the gains can become very large when leverage is taken into consideration. If the trader in our example uses a common leverage factor of 10:1, then she can stand to make a profit of 30%. The big risk in a carry trade is the uncertainty of exchange rates. Using the example above, if the US dollar was to fall in value relative to the Japanese yen, then the trader would run the risk of losing money. It’s also a very bad idea for tens of thousands of traders to make the same bet; if it goes wrong for them all at once, it would be very nasty. 

A-Z Financial Tools

A **zero-beta portfolio** is referred to a portfolio of assets constructed by including a variety of assets that move independently of each other. The portfolio could have a risk profile similar to a risk-free asset. At the same time, changes in the value of the portfolio are uncorrelated with the stock market. Consequently, it might pave the way for stable portfolio performance. 



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