


Global Economy: Market-led recovery in the making!



Microscope

The IMF last week said the global economy this year would be stronger than it previously forecast, driven by emerging markets. Emerging and developing economies is expected to grow 6% this year, almost triple the 2.1% pace forecast for advanced economies. For the largest economy, the US, the 4th quarter GDP growth indicated that consumption and inventories were big contributors to growth, along with exports due to the weak dollar. One area that didn't contribute to the 5.7% GDP growth was government. In fact, government's contribution to Q4 GDP actually acted as a drag, as the marginal contribution from the Federal side was more than offset by the drag of state and local governments. In addition, commercial activities recovered in recent months. US companies have disclosed an increase in transactions of about 22% over the past two months as firms revive deals that were shelved or postponed during the credit crunch. It is widely expected that a reasonable number of large, conservatively capitalized companies are eyeing both domestic and cross-border opportunities. This indicates that the market-driven recovery is in the making. 

Besides China, the Reserve Bank of India last Friday told lenders to set aside more deposits as reserves than economists predicted after raising its growth and inflation forecasts. Governor increased the cash reserve ratio to 5.75% from 5%, exceeding the median forecast for a half-point move in a Bloomberg News survey, while the bank kept benchmark interest rates unchanged. In fact, India took a big step toward tightening monetary policy as inflation and asset-bubble concerns reverberate across Asia. China, Malaysia and the Philippines moved closer toward raising rates this month and Australia and Vietnam have already done so, spurring a sell-off in stocks in the region. However, India's benchmark stock index gained after the report, on optimism that the economic growth could gain momentum over the next year. In China, the central bank ordered some banks to pare lending, raised the ratio for

deposits banks must set aside as reserves and guided bill yields higher this month after loan growth surged. On the other hand, Malaysia kept borrowing costs unchanged on Jan. 26, while warning that rates cannot be kept too low for too long because of the need to prevent a build-up of financial imbalances. Meanwhile, the Philippines increased its so-called rediscounting rate, one of the interest rates it charges lenders for borrowing money from the central bank, as it began unwinding stimulus measures. Certainly, the excess liquidity in the market will be affected in the short term. However, all these official announcements and measures indicated that the economic activities are coming back. As growth accelerates and the output gap closes, excess liquidity, if allowed to persist, may exacerbate inflation expectations. Though the

inflationary pressures stem predominantly from the supply side, the consolidating recovery increases the risks of these spilling over into a wider inflationary process. The pre-emptive moves are wise to prevent another financial crisis. Company-wise, Infineon, Europe's second-largest semiconductor maker, posted a second consecutive quarterly profit. The chipmaker reported first-quarter net income of 66 million euros from a net loss of 404 million euros a year earlier, buoyed by demand from its auto and telecommunications customers. The CEO is raising its guidance for the full 2010 fiscal year, looking for revenue growth in excess of 20% with a high single-digit combined segment result margin. As such, we may see increasing capital expenditure for corporations during 1H 2010. 

MARKET BRIEFING


YTD % (local curr)

US DJ	10,067 (-3.5%)
Nasdaq	2,147 (-5.4%)
Euro Stoxx 50	2,776 (-6.4%)
HSI	20,121 (-8.0%)
Japan NK225	10,198 (-3.3%)
China Shanghai Composite	2,989 (-8.8%)
Singapore	2,745 (-5.3%)
India BSE30	16,357 (-6.3%)
Brazil BOVESPA	65,401 (-4.6%)
Aus All Ord	4,596 (-5.9%)
US-10yr Bond	Yield 3.58%
As at 29/01/10	

Insight: "TIPS"


Treasury Inflation-Protected Securities (or TIPS) are the inflation-indexed bonds issued by the US Treasury. The notional amount of the securities is adjusted to the Consumer Price Index, the commonly used measure of inflation. Therefore, the coupon rate is constant, but generates a different amount of interest when multiplied by the inflation-adjusted principal, thus protecting the holder against inflation. Inflation reflects the increases in the cost of consumer goods and services over time. Because the cost of goods is steadily rising, especially after an extended period of loosening monetary

policy, investment returns must be adjusted for inflation, which means the only returns that help investors increase their purchasing power are "real" returns—or those returns left over after subtracting inflation.

Therefore, choosing investments that will earn a return above the rate of inflation can protect an investor's future purchasing power. The inflation protection built into TIPS is designed to provide investors with predictable real returns and an explicit hedge against inflation. Including TIPS in a portfolio of stocks and traditional bonds may provide investors with benefits in addition to inflation protection, including enhanced diversification and capital preservation. Together with removing the uncertainty associated with inflation risk, TIPS tend to be less volatile than nominal bonds and significantly less volatile than equities. 

Financial "In & Out"

IN: Developed markets are likely to enjoy the return of capital from overseas after over 1 year's recessionary period since the collapse of Lehman.

OUT: Emerging markets may face profit-taking pressure because of the possible capital outflow after the period of appreciating value in both currencies and underlying assets. 



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Next Insight
"Currency-linked Investment"