PHILEQUITY CORNER

Elephant in the Room
By ARSamson

There was to be no "Pacquiao Rally" last week, the irrational conviction that a victory (albeit a close one on points) by the national idol was to usher in such exuberance as to strengthen the peso and perk up the falling stock market. Chartists swear to having previously observed such irrational behavior after each victory by the boxing icon, along with a brief drop in crime rates, traffic violations, and lower mall sales.

This absent Pacquiao Rally follows the discrediting too of that other tightly held belief that the American sub-prime woes should not have any ripple effect on these shores. This conviction arises from the simple fact that we don't have those newfangled financial weapons of mass destruction in our local portfolios. This so-called "Decoupling Theory" (what happens in America does not concern us) was embraced by other economies including Europe and the two other financial behemoths China and India. All these economies maintained they have a strong domestic economy driven by local consumption. And all too briefly the hold of the decoupling theory on the financial mind left nary a trace, no fingerprints even as all the markets followed the lead of the thirteen-trillion-dollar economy to affect the rest of the world.

I propose the "Elephant-in-the Room" theory in moving our local markets. Forget the impact of exports and the rising peso vis-à-vis the dollar in the share of the local economy, or the impact of the inward remittance of dollars from our hardworking OFWs. The elephant theory shows how size (and influence) matters. And we premise this analysis on the fact that we speak English and understand what the analysts are saying, just as they understand our scandals faithfully reported by our media.

Here are the reasons why elephants (rather than bulls, bears, and pigs) rule.

The cable channels have opened up our interpretation of events towards the American perspective. The news channels have introduced us to familiarity in American sports and the race for the MVP honors in the NBA. When looking for explanations to what's happening in the equities, commodities, and currencies markets, we are guided by Bloomberg or CNBC and their selection of doomsayers and analysts giving their opinions on what's happening. We pick up the terminology as well (including sub-prime woes and housing starts) and have a greater familiarity with the travails of the financial sector in Wall Street than in Ayala Avenue—their graphics are more compelling.

The foreign funds are a factor in the local market. In a small playground like Manila (one year's transaction value is less than HK's one-week transaction, and half a day in Wall Street) sell-offs by the foreign funds, albeit with Manila already small in their portfolio, even for emerging markets, have a disproportionate impact on the prices of the listed stocks.

The biggest market cap stock (TEL) is also listed in the New York Stock exchange and with its PSE index weight at 20%, the roller coaster movements in the Dow also impact this single stock and again unduly affect market sentiment.

The New York market closes about six hours before the Manila market opens. This time and zonal difference dictates the opening market sentiment of the PSE, along with the closing price of local stocks listed in the US. Additional clues come from the earlier opening New Zealand and Australia and the first hour of the Tokyo market. These three early Asian markets are likewise affected by the mood of Wall Street and how it closed.

The metaphor of the elephant in the room demonstrates that this beast does not even have to be rampaging to make its presence (and mood) felt by others in the enclosed space. True, one may not even be looking at the behemoth or depending much on its goodwill. It's mere presence and the space it occupies leaves little room for freedom of choice.

It is said that the coming US elections will affect two-thirds of the world even if indirectly. Still only a fraction of that (US voters) gets to vote. The proxy excitement or even support for specific candidates (I like Hillary, even if I can't possibly vote for her) goes beyond a spectator sport and the professional interest in a political contest and the effects of spin on even the most harmless statements like those of Ferraro. No, this unhealthy attention affects how this other half of the world lives.

Optimism in the markets is driven not just by hard numbers. One only has to be reminded of the lack of excitement three days after each of the Fed rate cuts on general market sentiment. Optimism is not purely an emotional high. There is a need to explain its basis in some positive news.

Pessimism, on the other hand, seems to have the benefit of a perfect storm. The Iraq war, said in a new book by Joseph Stiglitz, a Nobel laureate in economics, to cost upwards of three *trillion* dollars including contractors, arms and the rehabilitation of the returning veterans, heads the list of bad news. From here, add the price of crude oil, lowest housing starts in seventeen years, rising unemployment and the near-death experience of financial services companies, what's left to cheer about?

Today is Easter Monday. And we know from the tale of the passion (sacrilege alert) that the Stations of the Cross feature three falls with the cross before…the crucifixion. Optimists of the equities market unite—you have nothing to lose but your margin calls. This particular story of Easter ends with a stone rolled away from the mouth of the cave and the announcement of One who has risen from the grave.

Monday after a long Easter break is a good day to hope for a similar recovery from death.

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