Philequity Corner (August 4, 2008)
By: Joseph Liao Ong

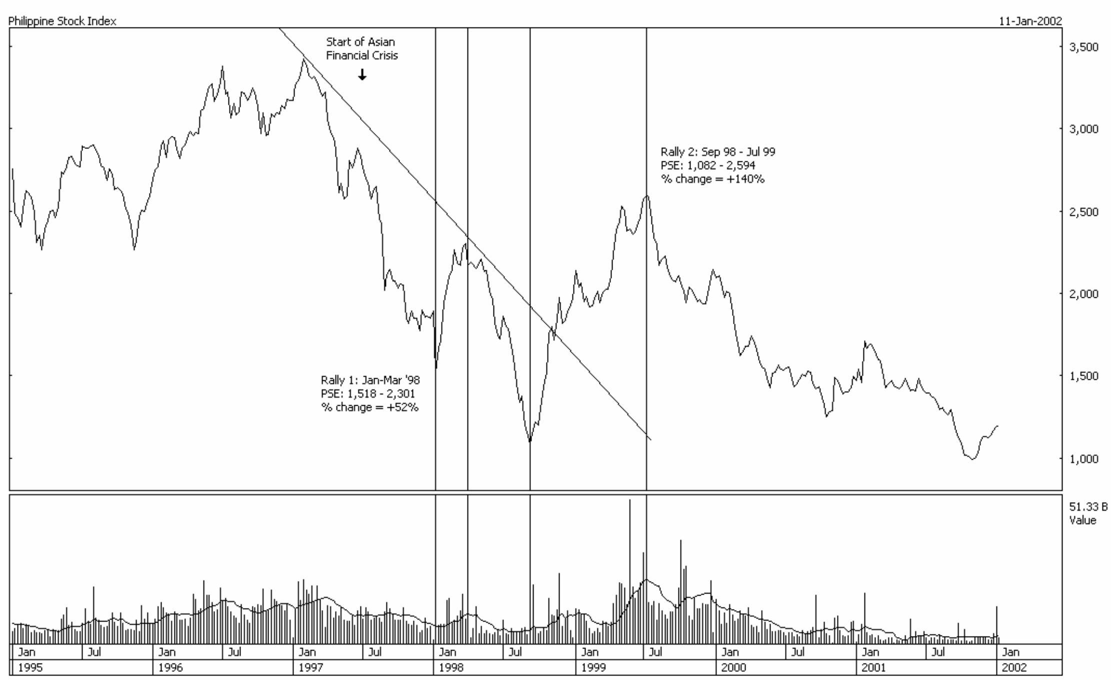
Bottoming out

Finding the stock market bottom is a difficult task. While logic dictates that a market's bottom is simply an inverse of a peak, a bottom is in fact more difficult to find. Bottom searching is oftentimes accompanied by fear as investors tend to panic during a downturn. Even the most savvy investors fail to pin down a market's lowest point. In the case of the Philippine stock market, the PSEi has already shed 29% of its value since the start of the year. After hitting 2,339.84 on July 3 (its lowest close year-to-date), the market has rebounded by 10.4%. This then begs the question: Has the PSEi already reached its bottom?

To say that the market has finally bottomed may be premature at this point. While the short-term backdrop is exhibiting positive signals that may help sustain the PSEi's current gain, the market remains tied to global events. Investors are still tentative as major economies remain fragile. Nevertheless, the key to smart investing is assessing if a stock's downside risk is low relative to its upside. Suffice to say, even in market downturns, investment opportunities are still present.

A flashback of the Asian Financial Crisis

Take for instance the bear market during the 1997 Asian Financial Crisis. It was not only highlighted by share price collapses but also market recoveries. The market encountered two major rallies. The first run-up was during the first quarter of 1998 which resulted in a 52% gain. The second rally, which started in September 1998, was much larger. It broke the major downtrend line and extended the PSEi's performance to 2,594 in July '99 – a return equivalent to 140%!



Source: Technistock

Oil is becoming more of *the* barometer

These days, performance of global economies is hinged on the price of oil. Black gold is becoming more the relevant barometer than gold, given its daunting ramifications on world inflation. After the wave caused by the US sub-prime issue, rising inflation rates across the globe due to skyrocketing crude oil prices has caused pessimism in stock markets, particularly for oil-importing countries like the Philippines. The view that the world economy is slowing down has softened crude oil prices in the recent weeks. If the downtrend continues, then the inflation peak projected by Bangko Sentral ng Pilipinas (BSP) may be realized. The stock market, as a result, should experience a valuation rebound.

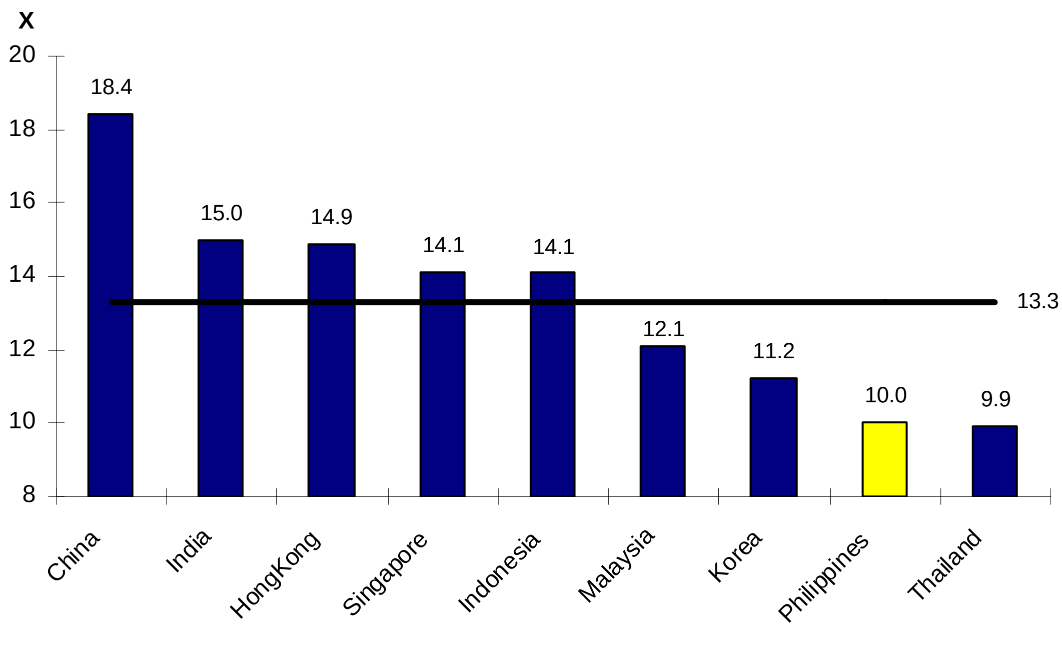
Closing Prices of Crude Oil Benchmarks

	Peak	Date	Current	% Change
WTI	$145.86	3-Jul-08	$125.10	-14.2%
Brent	$146.60	3-Jul-08	$124.18	-15.3%
Dubai	$141.33	15-Jul-08	$120.09	-15.0%

Source: Bloomberg

Valuation: Is the price right?

The PSEi is trading at 10x 2008 earnings, which is at the lower end of the trading range. These estimates are based on 2008 consensus earnings from Bloomberg. During the past three years, the PSEi traded between 10x to 17x forward earnings. In contrast to the region, the Philippines' valuation appears attractive as it trades below the region's 13.3x average. Even with possible earnings downgrades due to slowing world economies, Philippine valuation still looks cheap.



Source: Bloomberg

Downside protection

Dividend yields oftentimes provide share price cushion, which limits further downside of a stock. This is especially true when the yield is juxtaposed with a comparable government instrument. The 30-company PSEi constituents are projected to declare a little more than 50% of their 2008 earnings, thanks in large part to the telecom companies. The resulting average dividend yield, however, translates to 4.4% — lower than the 91-day T-bill of 5.699% and the 1-year MART of 7.285%. Although the yield from the stock market appears lower than risk-free investments, holding on to stocks which pay dividends gives an added boost. An investor can patiently earn the dividends of blue chips stocks while the bear lasts. When the bull market arrives, the patient investor can earn a handsome return together with the dividend he has earned.

For comments and inquiries, you can email us at info@philequity.net. You may also view our archived articles at www.philequity.net or www.yehey.com/finance.