

Philequity Corner (November 14, 2010)
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Is The Bull Run Over?

The PSE Index recorded a new all-time high of 4,413.42 last November 5, 2010. Since then, it has closed lower for six consecutive days, shedding 336.74 points or 7.6 percent. So far, this is the biggest decline we have experienced in this bull market which started in March 2009. This has prompted many of our readers and investors to raise questions whether this bull run is over or not. We are taking this opportunity to answer those queries, including inquiries regarding the Nickel Asia IPO.

1) Is the bull run over?

First of all, we would like to point out that this sell-off was long overdue. The market has been going up for five straight months without any meaningful correction. The PSE Index has gained 1,300 points since late May when it was still doing 3,100.

Secondly, we believe that the market is just experiencing a natural and healthy correction. Having reached 4,400 two weeks ago, the market clearly needed to work out its overbought condition after the strong rally. So while the 7.6 percent decline seems big, it is just a natural corrective move when viewed from context of where the market came from. In fact, the recent decline is just a fourth (1/4) of the rally from May to November (see chart below).



Source: www.stockcharts.com

Lastly, we do not believe that the bull run is over. The macroeconomic outlook of the Philippines is bright as attested by the credit rating upgrade we received from Standard & Poor's last Friday. S&P raised the country's long-term sovereign credit rating from BB- to BB with stable outlook.

On the corporate earnings standpoint, we forecast a 14.5 percent earnings growth in 2011, following the 26.9 percent growth we expect this year. While the market is fairly priced at 15x forward earnings, it is well below the 2007 peak valuation of 18x and the “bubble” levels it reached in the mid-1990s of 20x to 25x.

With respect to technicals, as long the trendline is not breached to the downside (in this case, as long as 3,800 holds), the PSE index remains in bullish mode.

2) Why did the market go down?

One reason why the market went down was simply because of profit taking. Note that when Bernanke first hinted of a QE2 in late August, equities worldwide went parabolic for the next two months. When the Fed finally laid out its plans for QE2 last November 4, that’s when the markets started to correct. The markets were expecting \$500 billion QE2, but the Fed did a little more with \$600 billion. Therefore the sell-off could not have been triggered by a disappointment over QE2. Clearly, it was a case of profit taking since the actual announcement of QE2 has already been discounted.

Another reason for the decline is that some investors have started to unwind their long emerging markets / short US market position. In fact last week, Goldman Sachs recommended closing out its suggested bet that emerging markets will outperform the S&P 500 index. Goldman cited improving US economic data, as well as inflation and policy tightening in emerging market nations.

With regard specifically to the Philippine market, the private banking division of Morgan Stanley and UBS recently repeated an underweight position in Philippine stocks. But actually, they missed much of the rise in Philippine stocks. Morgan Stanley was underweight Philippine stocks since last year and UBS private banking was underweight Philippines 3 to 4 months ago.

3) Should we bail out now?

While we see the current market setback as a pause and as a good buying opportunity, at the end of the day, it all boils down to one’s asset allocation and risk tolerance.

If you are overweight and overleveraged in Philippine stocks, it may be appropriate to lighten up on your positions. Holding the right amount of stocks will help you tolerate the huge swings prior to the market’s next move higher.

If you are underweight equities or you do not have any stock position at all, now is a good time to start accumulating blue chip names or buying a mutual fund. This correction gives you the opportunity to buy stocks at cheaper levels before the bull run resumes.

4) Should we invest outside the Philippines?

Investing in your own backyard has its advantages because this is your own country. You can invest in what you know and in the companies that you are familiar with. But if you have the

expertise and the means to invest outside the country, go ahead. Investing outside will give you diversification of assets. During this correction, for example, you can turn to defensive names like McDonalds (MCD), IBM, Yum Brands (YUM), growth companies like Apple (AAPL), Google (GOOG), copper giant Freeport McMoran (FCX) or turn around companies like Las Vegas Sands (LVS), Citicorp (C) and Ford (F). You can also buy ETFs for US (SPY), Hong Kong (EWH), Thailand (THD), etc.

You can also take advantage of the correction to accumulate precious metals thru exchange traded funds (ETFs) like the SPDR Gold Trust ETF (GLD), iShares Silver Trust ETF (SLV), or to buy agricultural commodities thru Powershares DB Agriculture Fund (DBA). Or you can also purchase a basket of mining companies thru Market Vectors Gold Miners ETF (GDX) or Market Vectors Junior Gold Miners ETF (GDXJ).

5) What is Nickel Asia?

Nickel Asia is the latest initial public offering (IPO) in the Philippines. The company is one of the largest global suppliers of laterite nickel ore, and the largest nickel mining company in the Philippines. It accounted for more than 50 percent of all nickel exports of the country in 2009. It currently operates four laterite nickel mines, namely: Rio Tuba, Taganito, Cagdianao, and Taganaan. The company sold 6.5 million WMT of saprolite ore and limonite ore in 2009, generating Php4.3 billion in revenues.

6) How is it priced?

Nickel Asia is being offered at Php15 per share or 12x P/E. Its initial public offer consisting of 304,500,000 primary shares with an over-allotment option of 45,675,000 shares is oversubscribed.

7) How do you get it?

The IPO has been heavily subscribed by clients of stockbrokers. Investors have up to 11 am today (November 15) to subscribe through the local small investors (LSI) program. Investors interested can call their stockbroker, the underwriters, or the PSE for help. If you do not have your own stockbroker, you can call Wealth Securities at 634-5038 for assistance.

The LSI program entitles the investor to invest up to a maximum of 1,600 shares. LSI applicants are required to submit a filled-up application form and a photocopy of any two valid government-issued IDs. Physical appearance is also required. Check payments should be payable to "NAC IPO".

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