Philequity Corner (June 4, 2012)
By Valentino Sy

Philippines: One of the few bright spots left

The Philippine stock market remained one of the few bright spots left as most markets suffered deep declines last month on worries over the European debt situation. Following inconclusive Greek elections, growing risk of a Greek exit from the Eurozone and escalating woes in Spain and Italy, investors fled to safe havens. Furthermore, the impact of the European crisis on the real economy has begun to emerge as countries around the world begin to record slower growth – and some slide into recession.

In contrast, the Philippines reported strong economic growth during the 1st quarter of 2012 of 6.4 percent, far exceeding expectations. This came a day after Moody's upgraded the country's credit outlook of Ba2 from "stable" to "positive." As a result, the PSE index managed to close strong for the month, declining by only 2.1 percent in May even as markets around the global suffered a bloodbath.

Yet another twist in the Greek Drama

For the first four months of the year, the problems in Europe seemed reasonably well contained after Greece passed the unpopular austerity bill in February and the EU backed a 2nd Greek bailout of 130 billion euros in March. This view, however, was shattered last month after the radical left Syriza coalition came in 2nd during the May 6th Greek elections, dashing hopes for the formation of a coalition government.

The rise of Syriza supported by a growing number of angry, jobless Greeks who prefers less austerity increased the danger of a Greek exit from the Eurozone. While a second general election is slated on June 17th to settle the impasse, investors and the markets (which declined heavily in May) remain pessimistic. Fitch Ratings downgraded Greece's credit ratings two notches further into junk territory.

European banks plunge

Aside from Greek news weighing on stocks last month, the weakness of European banks, especially the Spanish bank Bankia, also added to the selling pressure. Bankia, which lost 60 percent of its market value in May, is asking the Spanish government for a 19 billion euro bailout. This is in addition to the 4.5 billion euros already injected, the biggest in Spanish banking history.

Moody's downgraded 16 Spanish banks, 26 Italian banks and Santander UK in May. The credit rating agency is set to review banks in Germany, France, Austria and the Netherlands this month and most of these banks are likely to see their credit rating cut by the end of June.

Global growth is slowing

The impact of the crisis in Europe is becoming more evident around the world as global manufacturing growth expanded at its weakest pace in five months. Eurozone's manufacturing PMI slipped to 45.1 (where a reading below 50 means a contraction), marking the lowest level in 35 months. Similarly, UK's manufacturing PMI fell sharply to 45.9 in May from 50.2 in April, which is the lowest reading since May 2009. What surprised most investors, however, was the drop in China's manufacturing PMI which fell sharply to 50.4 from 53.3 the previous month.

Other emerging market leaders such as Brazil and India showed similar dismal economic results. Brazil's economy expanded a measly 0.2 percent in the 1st quarter of 2012, the slowest pace since the 3rd quarter of 2009. And while India still managed a 5.3 percent growth, it pales in comparison to the 9.2 percent growth the previous quarter. It also marked India's weakest growth in nine years.

Philippine growth is surging

In contrast to the sharp economic slowdown in most countries, the Philippine economy expanded at a faster pace backed by a recovery in manufacturing and services. The National Statistical Coordination Board (NSCB) reported last week that 1st quarter 2012 GDP rose 6.4 percent, which was well ahead of consensus estimates of

4.3 percent. The 4th quarter 2011 GDP numbers were likewise revised higher to 4 percent from the 3.7 percent growth reported initially.

Note that the strong 1st quarter 2012 GDP growth was achieved despite the absence of public private partnership (PPP) projects that will be launched only this 2nd half of 2012. Also, government spending grew 12.1 percent in the 1st quarter of 2012. We expect this pace of growth to be sustained given the government's healthy revenue growth and its manageable fiscal deficit.

Global stocks sold down in May

The proverbial saying "Sell in May and go away" proved correct this year. European stock markets such Greece, Spain and Italy led the bloodbath in May as expected, declining 24.9 percent, 13.1 percent and 11.9 percent, respectively. Meanwhile, the German DAX index fell 7.3 percent as the region struggled to find a solution to their financial and political crisis.

The US markets likewise fell sharply last month. The Nasdaq Composite index was down 7.2 percent following Facebook's dismal IPO performance. Facebook stock is already down 27 percent from its IPO of $38 per share. Meanwhile, the Dow Jones Industrial Average was down 6.2 percent in May, totally erasing all its gains for the year.

US & Europe	Index	Last Price	%Chg May	%Chg Ytd
US	Nasdaq Comp	2,747.5	(7.2)	5.5
Germany	DAX	6,050.3	(7.3)	2.6
US	S&P 500	1,278.0	(6.3)	1.6
US	DJIA	12,118.6	(6.2)	(0.8)
Switzerland	SMI Index	5,777.5	(4.0)	(2.7)
Canada	TSX Comp	11,361.2	(6.3)	(5.0)
UK	FTSE	5,260.2	(7.5)	(5.6)
France	CAC 40	2,950.5	(6.1)	(6.6)
Italy	MIB Index	12,740.0	(11.9)	(15.6)
Greece	Athex	501.9	(24.9)	(26.2)
Spain	IBEX 35	6,065.0	(13.1)	(29.2)

Source: Bloomberg, Philequity Research

Philippine stocks, no. 1 in Asia

Shielded by good economic numbers and strong corporate performance in the 1st quarter of 2012, the Philippine market performed relatively well last month despite the problems in Europe and concerns of slowing global growth. The market declined by only 2.1 percent in May and continues to lead Asia and most global stock markets year-to-date with a 15.6 percent return (see table below).

Asia Pacific	Index	Last Price	%Chg May	%Chg Ytd
Philippines	PSEi	5,062.4	(2.1)	15.8
Thailand	SET	1,115.2	(7.1)	8.8
China	Shanghai Comp	2,373.4	(1.0)	7.9
Singapore	STI	2,745.7	(6.9)	3.8
India	SENSEX	15,965.2	(6.4)	3.3
Malaysia	KLCI	1,573.6	0.6	2.8
Hong Kong	Hang Seng	18,558.3	(11.7)	0.7
South Korea	KOSPI	1,834.5	(7.0)	0.5
Taiwan	TWSE Index	7,106.1	(2.7)	0.5
Australia	All Ordinaries	4,116.9	(7.5)	0.1
Japan	Nikkei 225	8,440.3	(10.3)	(0.2)
Indonesia	JCI	3,799.8	(8.3)	(0.6)

Source: Bloomberg, Philequity Research

Back to business

One of our concerns in early May was that the issue with China regarding the Scarborough Shoal would escalate militarily or in a trade war (see our article *Bananas, Pineapples & the Stock Market*, May 13, 2012). We said that this conflict should be resolved quietly and diplomatically, away from the media. So far, steps have been made to diffuse the situation. And the media hoopla over the situation appears to have died down which is positive.

Meanwhile, another event which has created so much frenzy in the media - the impeachment trial of Chief Justice Corona – has ended. The distraction from this impeachment has now ended and our legislators can now go back to their regular business, passing important legislative agendas.

PSEi relatively unscathed but remains in consolidation

While there remains to be a high degree of near-term risk arising from the turmoil in Europe and uncertainty over the slowdown in China, India and other emerging markets, we remain bullish over the prospects of the Philippine economy and Philippine stocks in the long run.

However, after reaching our end-2012 target of 5,300 well ahead of time, we expect the PSEi to remain in consolidation mode as further news coming out of Europe is digested. During this time, we remind investors to review their asset allocation and adjust them accordingly given the current investment environment. Also remember to stick to companies with good business models and sustainable earnings growth.

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