Philequity Corner (August 27, 2012)
By Valentino Sy

Whatever It Takes

"*The ECB is ready to do whatever it takes to preserve the euro. And believe me, it will be enough*." – ECB President Mario Draghi

This is the pledge of ECB President Mario Draghi. His words caused financial markets to rally strongly the past month. Draghi raised expectations last July 26 that the ECB will step in and buy massive amounts of Spanish and Italian debt to help lower borrowing costs and preserve the euro.

As a result, the yields on the 10-year Spanish bonds fell from a high of 7.75% in July 25 to 6.41% last August 24. Meanwhile, the yields on the 10-year Italian bonds declined from 6.71% to 5.71% over the same period.

Draghi's remark also triggered a rally in the euro from a two-year low of 1.2042 against the US dollar registered in July 24 to close at 1.2513 last Friday.

Euro

Source: Yahoo Finance

Risk "on"

Stocks took the cue from the declining Spanish and Italian bond yields as a signal that "risk" is now back "on." Battered European stock markets, such as that of Spain and Italy, rallied sharply.

		Price as of		
Country	**Index**	**25-Jul**	**24-Aug**	**%Change**
Spain	IBEX	6,004.9	7,310.3	21.7%
Italy	Mibtel	12,506.7	14,880.7	19.0%
France	CAC	3,081.7	3,433.2	11.4%
Greece	Athex	588.1	644.0	9.5%
Germany	DAX	6,406.5	6,971.1	8.8%
US	S&P 500	1,337.9	1,411.1	5.5%

Source: Bloomberg, Wealth Research

Similarly, the markets of export-oriented East Asian countries (which are the most economic sensitive and the most battered) such as South Korea, Japan, Taiwan and Hong Kong rallied strongly. Meanwhile, the domestic-oriented countries such as the Philippines and Malaysia (which are considered defensive) lagged.

Country	Index	Price as of 25-Jul	24-Aug	% Change
South Korea	KOSPI	1,769.3	1,919.8	8.5%
Japan	Nikkei	8,365.9	9,070.8	8.4%
Taiwan	TWSE	6,979.1	7,477.5	7.1%
Hong Kong	HIS	18,877.3	19,880.0	5.3%
Thailand	SET	1,188.6	1,237.2	4.1%
Indonesia	JCI	4,000.8	4,145.4	3.6%
Singapore	STI	2,990.9	3,050.5	2.0%
Malaysia	KLSE	1,635.1	1,648.2	0.8%
Philippines	PSEi	5,161.8	5,143.4	-0.4%
China	SSE	2,136.2	2,092.1	-2.1%

Source: Bloomberg, Wealth Research

Sectoral rotation

Other trades that signify "risk on" have been playing out too. In the US markets, investors shifted toward cyclicals and out of defensive sectors. Financials like Citigroup and Bank of America rallied strongly. Cisco, a tech bell-weather, surprised to the upside. Meanwhile, copper producer Freeport McMoran and casino operator Las Vegas Sands likewise rallied sharply the past month.

Meanwhile, the consumer staples such as Coca-cola Hershey Foods and retail stocks such as Walmart and Costco (which performed strongly in the 2nd quarter of 2012) lagged. High-yield stocks such as Verizon and Abbott Laboratories similarly stayed flat.

	Company	Symbol	Price as of 25-Jul	24-Aug	% Change
	Citigroup	C	25.79	29.83	15.7%
Cyclicals	Bank of America	BAC	7.07	8.16	15.4%
	Cisco	CSCO	15.42	19.20	24.5%
	Freeport Mcmoran	FCX	31.43	36.13	15.0%
	Las Vegas Sands	LVS	37.51	42.63	13.6%
	Coca Cola	KO	38.51	38.47	-0.1%
	Hershey Foods	HSY	69.96	72.61	3.8%
Defensives	Walmart	WMT	71.67	72.11	0.6%
	Costco	COST	93.48	96.25	3.0%
	Verizon	V	121.99	126.66	3.8%
	Abbott Lab	ABT	64.12	65.84	2.7%

Source: Bloomberg, Wealth Research

All eyes on Jackson Hole

After rallying strongly the past month, global stock markets are now facing resistance and are now correcting. All eyes are now on Jackson Hole as investors await the Fed's next move. Located in the State of Wyoming, Jackson Hole is where the US Federal Reserve holds its annual symposium. The much anticipated event is attended by the world's central bankers, policy experts and leading economists.

Jackson Hole gives investors a "peep" at how central bankers currently view the global economy. Particularly, investors are keeping an eye on the Bernanke's keynote speech on August 31which should offer clues whether another round of quantitative easing (QE3) is in the pipeline. On September 1, Mario Draghi will be the speaker and will also indicate what the ECB is planning to do.

Who will win? Who will prevail?

Will the world's central banks be able turn the global economy up from a slowdown or recession? Or will the global economy continue to stagnate?

We, in Philequity, believe that in due time the world's central banks will be able to turn the global economy around because they have a lot of tools in their arsenal. The Fed and the ECB are ready to provide more easing if need arises. Draghi said last month that the ECB is "willing to do whatever it takes to save the euro." Meanwhile, Bernanke promised last week that "there is scope for further action by the Fed to ease financial conditions and strengthen the recovery."

Moreover, we are confident that the central banks will prevail because most of them are all-out to provide stimulus and are now working together to save the global economy. Aside from the Fed and the ECB, other central banks have joined in. Taiwan, South Korea, China and even the Philippines have recently cut rates. Meanwhile, Brazil has cut policy rates for a record eight times. Remember the wise saying: "*Don't fight the Fed*."

Philippine stocks are consolidating

As global markets were rallying strongly last month, the Philippine market remained flat. The reasons why the Philippine market is consolidating are the following:

1) **Overnight secondary placements** – In one of our articles last month, we mentioned the negative effects of overnight secondary placements as it saps market liquidity. In July alone, a total of Php26.55 billion was raised by Ayala Land, Ayala Corp. and Pure Gold. This month, Tanduay announced plans to sell up to 3 billion shares which could potentially raise Php38.16 billion based on last Friday's closing price of 12.72 per share. And just as we had predicted in our previous article (see *An Avalanche of Secondary Placements,* July 23, 2012), SM Investments Corp. announced a Php 6.3 billion placement.

2) **Ghost month** – In last week's article, we mentioned that Philippine stocks tend to pull back during the months of August and September (see *The Friendly Ghost*, August 20, 2012). Investors, especially the Chinese, avoid making investments during the Chinese ghost month which started last August 17 and will end September 15. This period also typically coincide with the summer holidays of American and European fund managers which partly explain the decline in market liquidity during this time.

3) **Switch to "risk on"-** Lastly, foreign investors sold Philippine stocks which are considered "defensive" as the market switched to "risk on" last month. Similar to what happened to telecoms, pharmaceuticals and consumer staples in the US, investors sold their "defensive" positions and shifted to battered "cyclical" stocks and countries. Local retail investors and local institutions absorbed the selling of foreign investors in Philippine stocks.

Window of opportunity

As the Philippine market consolidates, we view this as a window of opportunity to buy Philippine stocks at lower prices. Going forward, we remain bullish on the Philippine economy and the stock market. The earnings of listed Philippine companies is one of the very few which exceeded expectations. While short-term players and hedge funds take profit, we believe that economic and corporate fundamentals will prevail at the end. Long-term investors will reap the rewards of staying long in the Philippine economy and in the Philippine stock market.

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