Philequity Corner (September 23, 2013)
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No Taper!

Last September 18, Fed Chairman Ben Bernanke again took center stage and surprised everyone. Coming from the Fed's Open Market Committee meeting, Bernanke announced that there will be no tapering of the Fed's quantitative easing (QE) program for now. Bernanke's announcement was made against a backdrop of investor and economist expectations that the Fed will reduce its bond purchases by $10B per month. The surprise announcement therefore became a big positive boost for the markets. This drove the US stock market to reach new all-time highs and caused emerging market (EM) stock indices and exchange-traded funds (ETFs) to jump sharply.

Unprecedented Monetary Easing

In past articles and presentations, we talked about Bernanke's bold moves and unprecedented policy actions. What he is doing with the Fed's QE has never been done before and was never a major part of what is written in economic textbooks.

His policy toolkit includes driving interest rates to ultra low levels and purchasing government and mortgage bonds in order to inject more liquidity into the economy. These drove investors out of less risky and low-yielding assets and forced them into riskier assets like stocks or property. Bernanke's QE program has therefore created a "wealth effect" which was driven by rising asset prices. In turn, it inspired business and consumer confidence and led to increased economic activity.

As this was happening, the Fed's QE program also encouraged other global central banks to do something similar for their respective economies (*The Great Global Monetary Easing*, October 12, 2012). Moreover, the Fed's QE initiatives drove investors to take risk-on trades, giving rise to a global bull market in stocks (*Global Bull Market*, January 7, 2013).

The Tale of the Taper

QE tapering refers to the gradual reduction in the Fed's monthly bond purchases or liquidity injections into the economy. It will mark the start of the transition from an aggressive monetary easing stance to one that is more moderate.

Since QE drove a higher level of risk-taking, talks of QE tapering triggered the opposite: large scale unwinding, deleveraging and repatriation. Bernanke's May 22 speech, which hinted about the possibility of QE tapering within the next few months, sparked off vicious corrections in EM bonds, currencies and stocks (*The Tale of the Taper*, July 22, 2013). As the markets have since priced-in the prospect of QE tapering, it came as a positive surprise that the Fed has refrained from tapering for now.

Easier for Longer

The Fed's QE program has gone a long way in helping the US economy improve and recover from the 2008 subprime mortgage crisis. However, various economic indicators give a mixed picture about the strength and sustainability of the US economy's growth. Moreover, the current set of economic data does not provide enough evidence that the economy is growing in line with the Fed's expectations.

The Fed's decision to delay QE tapering clearly shows that its primary concern is the strength and sustainability of US economic growth. Given that the US economic recovery is still not very strong, the Fed opted to choose the conservative stance. The Fed does not want what it has done in the last few years to be put to waste. For now, it wants to eliminate the risks to economic growth before it starts tapering its QE program. It also wants to ensure that economic growth continues and does not get derailed.

Engines of Growth

While the US economy is growing gradually, other developed markets are improving as well. As Europe is quietly fixing its house, its manufacturing output, as measured by the Purchasing Managers Index (PMI), surged to a 2-year high. Japan is in the middle of its economic turnaround as Prime Minister Shinzo Abe and Bank of Japan Governor Haruhiko Kuroda implement the 3 arrows of Abenomics (*Out of the Sandtrap*, April 15, 2013). Meanwhile, it appears that China has stabilized and would be able to avert a hard-landing for its economy. As the world's bigger economies all show promising signs of improvement, it becomes more apparent that global economic growth will only continue, if not accelerate, moving forward. This will ultimately strengthen the economic growth of EM countries like the Philippines.

The Bad Neighborhood Improves

Although the talks about QE tapering did not affect the Philippine economy directly, it exposed vulnerabilities in our Asian neighbors, most notably India and Indonesia (*Best House in a Bad Neighborhood*, September 2, 2013). As a result, global investors sold down Asian stocks, thereby causing steep corrections in EM indices.

Recently, however, things have started to turn for the better. Driven by the improvements in the US, Europe, Japan and China, EM equities have shown signs of bottoming (*The Bad Neighborhood Improves*, September 16, 2013). As EM stocks had been gradually recovering, the Fed's decision to delay QE tapering caused sharp up-moves in EM ETFs. The table below shows the eye-popping 1-day gain of EM ETFs on September 18, the day of the Fed's "no taper" announcement.

1-Day Gain of EM ETFs on September 18

ETF	Ticker	1-Day Gain
MSCI Emerging Markets	EEM	4.2%
MSCI Philippines	EPHE	7.2%
MSCI Malaysia	EWM	4.6%
MSCI Singapore	EWS	2.9%
MSCI Thailand	THD	5.7%
MSCI Korea	EWY	4.1%
MSCI Indonesia	EIDO	9.5%
MSCI India	INDA	4.9%

Sources: Bloomberg, Wealth Securities

Weaker Dollar, Stronger Peso

Along with Asian stocks, Asian currencies have been battered because of the possibility of QE tapering and the problems in India and Indonesia. Since QE tapering is off the table for now and since a possible crisis in Asia has been averted, Asian currencies have started to strengthen. The table below shows the strong moves of Asian currencies since August 28.

% Change of Asian Currencies since August 28		
Country	**Currency**	**% Change**
Philippines	Peso	3.8%
Malaysia	Ringgit	5.1%
Singapore	Dollar	2.0%
Thailand	Baht	3.3%
Korea	Won	3.6%
Indonesia	Rupiah	2.0%
India	Rupee	9.5%

Sources: Bloomberg, Wealth Securities

The peso has strengthened along with its regional counterparts. After closing at 44.73 on August 28, it closed at 43.05 on September 20 and gained 3.8% within that period. Given the peso's recent strength, it stands to reason that the local stock market will also continue to move strongly in the next few days or weeks.

Double Bottom

The last few months have been a rollercoaster ride for local investors. In the last 4 months, the PSE Index reached an all-time high of 7,404, corrected to as low as 5,678, rallied back to as high as 6,830, only to correct again and touch an intraday low of 5,562.

The intraday bottom of 5,678, which was established last June 25 (*5-6-7-8*, July 1, 2013) was slightly breached and successfully retested when the index bounced off the intraday low of 5,562 on August 28. Given this, it appears that a double bottom has been forming for the PSE Index. In technical parlance, a double bottom is a powerful chart formation that signals a strong bullish reversal.

As EM equities continue to show signs of strength, the charts of other EM indices and ETFs show similarly strong bottoming formations that may also precipitate bullish reversals. Considering this, it appears that the PSE Index, along with our EM neighbors, has weathered the storm for now. Moreover, the Fed's "no taper" decision provides a strong tailwind for our index to move higher and retest its previous highs.

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