Weekly Investment Bulletin

[24th] September 2012

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Market Roundup:

Global indices were little changed and where European markets may have given up gains mid week, they ended in ascendancy. US markets also rose as well as their Japanese and Chinese counterparts.

Indeed for the latter two, it was a big week.

The Japanese central bank has expanded its stimulus program to try to boost the country's sluggish economy, joining its counterparts in the U.S. and Europe in easing the flow of money.

The Bank of Japan Wednesday added $126 billion to its asset-purchase fund, pushing it to $695 billion, in an effort to advance the world's third largest economy. The bank said the move was necessary as economic activity in Japan had “come to a pause.”

This comes after the US Federal Reserve, took aggressive action last week in an attempt to improve hiring in the American labour market and cut the country's stubbornly high jobless rate. The Fed said that each month it would buy $40 billion worth of securities to spur more lending by banks and spending by businesses and consumers.

Earlier, the European Central Bank said it would buy the bonds being sold by the debt-ridden countries in the 17-nation euro currency bloc to ease their borrowing costs, the latest effort to resolve the continent's three-year governmental debt crisis.

Finally in China, a $156 billion stimulus package was announced where the focus of the spending will be on infrastructure projects internally. That initiative balances out the efforts of Beijing to further develop the service sector in the country. The goal is to create a consumption economy, lessening the export dependence that now exists.

Market Data (12 month):

S&P 500:

FTSE100:

FTSE Eurofirst 300:

Nikkei 225:

Shanghai Composite:

Source: www.ft.com

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Emerged:

After three decades of GDP growth of year on year 10% growth, China is coming to reality from a miracle economy to normal powerhouse. The past quarter has seen a coming wave of fiscal stimulus measures and easing from the People's Bank of China, (PBoC), as China enters a new era in which a narrowing of the output gap and a relatively strong labour market will make Beijing more prudent.

This means less aggressive stimulus stabilising growth downward to between 7% and 8%.

Over the last couple of weeks, central bankers have been in the spotlight, doing what they can to support growth. The European Central Bank unleashed its open-ended bond buying program after Mario Draghi promised to do all he can to save monetary union, and Fed chief Ben Bernanke announced QE3.

Markets have rallied in stupor, and look now to Beijing to provide the next risk asset catalyst via stimulus.

As we've previously reported, China has been unveiling a series of simulative measures from all fronts to tackle its economic slowdown. From the central government and the PBoC to regional governments, the latest spending plans are worth approximately more than 11 trillion RMB ($1.74 trillion).

Indeed some are expecting Chinese GDP to stunt at 7.7% in Q3 but rebound strongly to 8.8% in the final quarter of 2012. There are reasons to be sceptical of such growth expectations, as China's collection of stimulus plans will force both structural and cyclical changes that will limit their individual impact.

China GDP:

China Business Confidence:

China Stock Market Performance:

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In contrast to their American counterparts, China's job markets have held up well, adding 8.2 million jobs through July (about 80% of their year-long target) and seeing wage rates rising.

As a result, inflation has also begun to tick up, which can be attributed to the shrinking of the output gap (which started narrowing in Q3 2011). CPI inflation has rebounded from recent lows and is moving up both on a monthly and a yearly basis. This rise in inflationary pressures is occurring at similar rates of economic growth, which in turn suggests a structural change in potential growth rates is taking place.

Still, as China transitions to this "new normal" of growth in the 7% to 8% range, an active policy stance will be needed to ensure a smooth transition. The most troubling statistic of all is the marked slowdown in export growth, which went from 7% in the second quarter to a near standstill in July and August. China's economy depends on external demand for growth, making it key to support exports in order to stabilize the economy.

Stimulus, they suggest, is warranted. And indeed it has been announced. In order to "stabilize" GDP growth, the NDRC (Beijing's planning agency) has approved a slew of highway and subway projects, along with power stations, wind farms, airports and other things, worth an estimated one trillion RMB ($158 billion) or 2.1% of GDP.

Also, different regional governments have announced investment projects probably worth more than ten trillion RMB ($1.58 trillion). At the same time, the PBoC has eased reserve requirement rations (RRR) and could probably do so twice more this year, and pushed commercial banks to lend. Housing purchase restrictions, which since April 2011 have substantially slowed real estate investment, are being eased as well.

Cont:

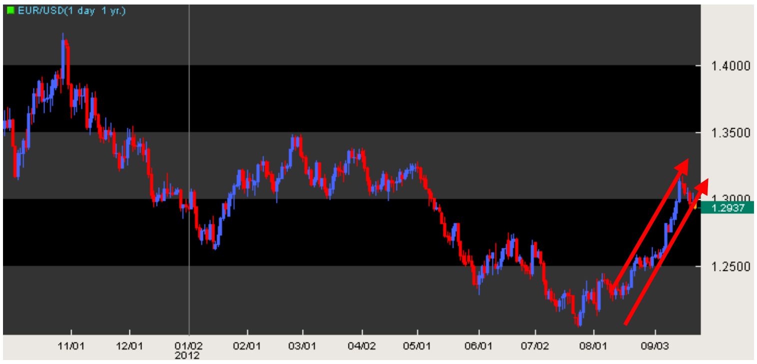
Those expecting these projects to spark a steep rebound in output growth will need to be patient. While the 2009 stimulus projects had an average completion time of 2 years, the newly proposed projects have a life span of three to five years, while the regional government plans could be completed within eight years furthermore several of these plans still have no funding plan.

Growth is still above the 7.5% target, labour markets remain stable, and the uptick in inflation could be exacerbated by QE3 and Draghi's OMT.

Recent monetary and fiscal stimulus should help stabilize the Chinese economy. But Beijing will be cautious. As the economy transitions to a new phase of slower economic growth, China's leadership will have to manage growth as they reduce their exposure to foreign demand and increase the share of domestic consumption to find stability, focusing possibly more on inflation than growth.

Currencies:

EURUSD

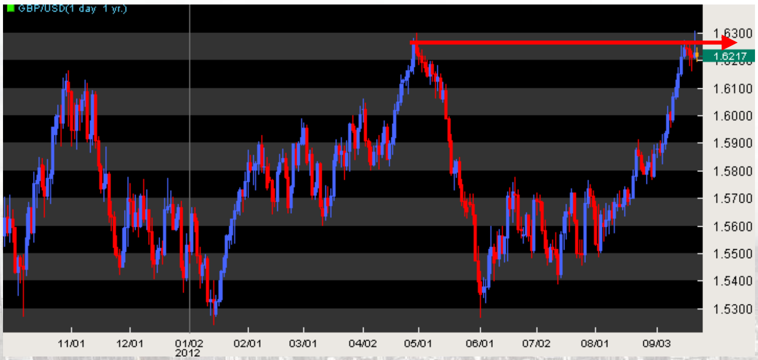


EURUSD remains in uptrend from 1.2042. Range trading between 1.2800 and 1.3171 is expected over the next several days. Another rise could be seen, and a break above 1.3171 resistance could trigger another rise towards 1.3500.

EURGBP

EURGBP's retreat from 0.8114 extended further last week and dipped to as low as 0.7974 so far. While a deeper fall might be seen initially this week, we'd expect downside to be contained by 0.7962 resistance.

GBPUSD



GBPUSD's upward movement from 1.5268 extends to as high as 1.6309. Further rise is still possible after a minor pullback, and next target would be at 1.6500 area. Support is at 1.6050, as long as this level holds, the uptrend will continue.

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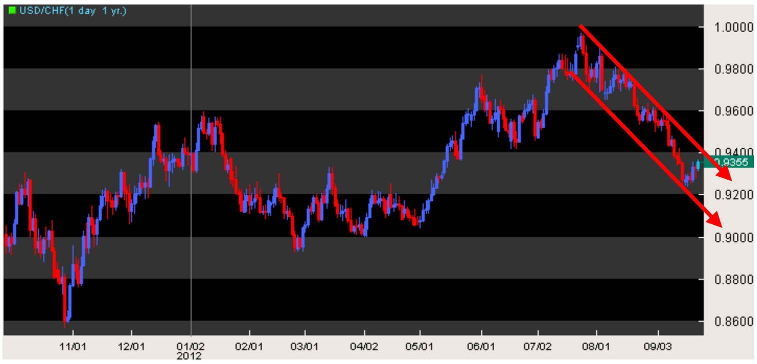
USDCHF



USDCHF remains in downtrend from 0.9971, the rise from 0.9239 is treated as consolidation of the downtrend. Range trading between 0.9239 and 0.9500 would likely be seen over the next several days. A breakdown below 0.9239 will trigger another fall towards 0.9000.

USDJPY

Being contained by the resistance at 80.61 USDJPY pulled back from 79.21. A rise to test the trend line resistance would likely be seen and a clear break above will target towards the 82.00-83.00 area. On the downside, as long as the trend line resistance holds, the price action from 77.66 (Jun 1 low) could be treated as consolidation of the downtrend, and further decline towards 76.00 is still possible.

USD Weighted Index

All four components gained ground against the USD, led by a 0.34% rally in the Australian dollar, while the British Pound gained 0.20% even as the U.K. saw a record GBP 14.4B budget deficit in August. It seems as though the Bank of England is becoming upbeat towards the economy as the Funding for Lending scheme is expected to boost private sector activity, and we may see the Monetary Policy Committee slowly move away from its easing cycle.

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Gold:

Gold Futures saw some selling pressure due to the weak China data yesterday. The much-anticipated HSBC China manufacturing PMI was released Thursday and came in at a reading of 47.8 in the latest month, which was the eleventh straight month of contraction in China's manufacturing sector. Gold's 14-day relative-strength index is at 76.5 today, above the level of 70 that generally indicates a pullback in Gold Futures prices may be imminent.

Crude:

Oil traded near a six-week low after US stockpiles climbed the most since March, Chinese manufacturing shrank and Japanese exports fell, signalling fuel demand may be slowing among the world's biggest crude users. Futures were little changed after declining as much as 1.4% last week. US oil inventories surged 8.5 mln barrels last week as Gulf of Mexico production resumed after Hurricane Isaac.

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Summary:

Despite more recent actions from Japan, China and US, the market just can't shake off Europe. Even Draghi's 'sterilisation' of European bond markets do not detract from the wider picture.

Greece returns to the spotlight after it reportedly faced a budget shortfall of €20bln to satisfy the minimum conditions for international aid. This is almost double previous estimates. With euro zone officials admitting that the €173bln bailout offered to Athens in 2010 being sorely wide of the mark, Greece now needs to plug the gap, if it's to receive the next tranche of €31bln. This was due in July.

Spain is now reportedly working on further economic reforms, which is set to pave the way for a formal request for international assistance.

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