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A healthy bout of profit-taking

Correction seen temporary; longer-term direction hinges on US economic risks

By GRACE CHONG

After the market plunge this week, BT speaks with various players - the fund manager, the economist, the technical analyst, and the research analyst - on their views of the situation and the stocks worth watching

MOST fund managers believe that the recent stockmarket plunge was more a temporary correction, and remain optimistic about the region's growth prospects, which will be driven by rising consumption in Asia.

After rocketing to all-time highs recently, the benchmark Straits Times Index (STI) suffered its biggest one-day plunge in almost five years on Monday, wiping a staggering \$16 billion off the total value of its shares. Still, DBS Asset Management equity strategist Peter Chiang says the correction in global equity markets was not unexpected.

'The markets were making multi-year highs despite the combined headwinds of high oil prices and rising bond yields in the US,' said Mr Chiang.

'The trigger for the correction was the US government report on inflation which fuelled concerns that the Fed (the US Federal Reserve) may have to keep raising interest rates to restrain the US economy. The extent and the duration of the correction will therefore depend on the unwinding of these headwinds.'

However, Mr Chiang also felt that the US economy's leading indicators are pointing to a growth slowdown, which makes the correction in global stock prices more like a healthy bout of profit-taking.

The STI has fallen 127 points, or around 4.8 per cent, from Monday. Since the all-time high of 2,659 on May 3, the loss has been 167 points, or around 6.2 per cent. Said Michael Koh, managing director of JF Asset Management: 'Conditions were ripe for a correction with investors sitting on good profits and the trigger was provided by weakness in overseas equity markets.'

Moving ahead, Mr Koh feels that the economic backdrop remains positive - growth prospects are good, market valuations in terms of price to earning ratios and dividend yields are not particularly stretched, and corporate earnings and balance sheets are sound. 'However, one will need to watch whether earnings will be adversely impacted by a slower US economy as interest rates continue to rise due to inflationary concerns; and margin pressures arising from higher input costs,' he added.

Most fund managers are inclined to believe that the near-term direction of the Singapore stock market will be determined by global macro considerations like US interest rates and investors' perception of the inflation outlook.

'The economic risks from the US will dictate the longer term direction not just for the Singapore market, but for most financial markets in general,' says Schroder Investment Management's portfolio manager Seok Teoh. 'Ultimately, it is a question of whether interest rates are rising faster than inflation to compensate holders of US assets for the risks of currency depreciation and inflation surprises.'

With US consumers being so highly geared, the concern is that consumption may not hold up if rates rise too fast,' she added.

Domestic demand is increasing in importance, and the focus is shifting to funds that will benefit from Asia's rising consumption.

'Under these conditions, our favoured sectors include beneficiaries of capex cycles, office and retail property, and companies oriented to improving domestic consumption in Singapore and Asia,' said Ms Seok Teoh.

Prudential also shares this strategy of focusing on Asia: 'Under this mantle, regional banks are a large overweighting as are the telecoms,' says Prudential Asset Management (Hong Kong) Limited's head of investment services, Robert Rountree.

Mr Chiang from DBS Asset Management recommends: 'Investors should focus on absolute returns. We suggest staying in equities relative to bonds.'

'The stock markets are expected to be more volatile, and stock prices have moved into oversold territory. Buying into bargains in such conditions will probably yield a good return six to twelve months down the road,' he added.

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