

June 2009 Review and Near-Term Outlook

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US stocks declined in June, halting the streak of gains which began in March. Even though the S&P 500 rose 15% percent quarter-on-quarter (QoQ), posting one of its best-ever quarterly advances, the rally stalled in June amid concerns that prices may already fully reflect the anticipated economic recovery. At its month-end closing level of 919.32, the S&P 500 was up 1.8% year-to-date (YTD). Meanwhile, the DJIA's 8,447.0 end-June level represents a 3.75% YTD decline.

In contrast, investors around the region remained optimistic about economic recovery prospects, and felt that Asian equities were still trading at a discount, particularly in the case of producers of commodities and electronics which would significantly benefit from a global rebound. Thus, stocks in the region continued climbing through the end of the June. The MSCI Asia Pacific Index closed the month at 103.81, or up 28% QoQ, marking the biggest quarterly rally since this index was launched in 1988.

Prices of crude oil fell from an eight-month high and gasoline slipped, as reports showed US consumer confidence declining unexpectedly in June. Crude oil for August delivery fell by US\$2.11 / bbl, or 3%, to US\$69.38 / bbl. Nonetheless, crude prices are up 56% YTD, and have touched a YTD high of US\$73.38 / bbl during trading. The overall rally in oil prices for the YTD period is the result of investors' search for alternative investments in light of rebounding world equity markets and a weaker US Dollar.

The Philippine Stock Exchange Index (PSEi) turned to profit taking towards the end of the June, after crossing the 2,600 level in mid-month. Despite a subdued closing level of 2,437.99, the local index still managed to gain 30.19% YTD and 2.03% month-on-month (MoM).

Last month, the Bangko Sentral ng Pilipinas (BSP) slashed the overnight rate for the fifth time since mid-December 2008 to a 17-year low of 4.25%, and signaled that this policy of monetary easing can be expected to continue. Benign inflation is one major reason for this stance: domestic headline inflation for June slowed further to 1.5%, which is a 22-year low. Meanwhile, the Philippine Peso strengthened in June to close at PHP48.122 / US\$, according to Tullett Prebon Plc. During the second quarter of 2009 (2Q09), the Peso appreciated by 0.4% – its first QoQ gain since the end of 2007.

Your Kabuhayan Fund made some modest advances, ending the month with a NAVps of PHP 1.0622, for a MoM rise of 1.63% and a YTD increase of 14.57%. Your ATR KimEng Equity Opportunity Fund closed June at NAVps of PHP 1.5735, up 2.43% MoM and up 22.38% YTD. Your MFMCP-Aizawa Trust Philippine Fund posted a NAVps of US\$ 60.25 at end-June, growing by 0.65% MoM and 19.81% YTD, both in US Dollar terms. Unlike last year, a more stable currency rate has helped the Aizawa fund's value.

We feel that the Philippine stock market is currently overbought. The PSEi's average P/E ratio is approximately at its all-time mean of 13X, coming from a low of 9X late in 1Q09. The massive run-up of 22.75% during 2Q09 was warranted by 1Q09 corporate results which were generally better than analysts' expectations. On the macroeconomic front, there is more concern today than there was earlier in the year. The budget deficit is now expected to be closer to 3% of GDP, compared to the 1.5% level expected at the beginning of this year. This is primarily due to low tax collections and higher public spending in the infrastructure arena. The Philippine Budget Secretary is not concerned with this development and recently commented that the country can operate efficiently with a budget deficit of up to 4% of GDP. With the Peso and inflation now stable, we expect GDP growth in the second half of 2009 (2H09) to exceed the dismal performance of 1H09. Official numbers have not yet been released but we expect to see 1H09 GDP at around 2%.

We have reduced our exposure to equities in all our managed portfolios because we expect the market to consolidate for 4-6 weeks. We continue to favor the energy sector for its value and the communications sector for its cash yield. We have reduced our exposure to the property sector, and are slowly increasing our exposure to the banking sector.