

Global Jitters - Investing in Growing US?

Global markets which went into dizzy in 2009, after getting encouragement from the Government have come into action again. Global interest rates are low and so are bond yields. The Government driven packages have brought in new cash into the system, which is waiting to be pumped into the markets. Low yield bonds and low interest rates are driving FIIs' to invest in emerging market and, thus, driving these markets up. This write-up makes a journey through some markets worth investing. According to the author, FII flows are the key triggers driving Indian stock markets; and one can recommend investors who have invested into Indian equities to start booking profits. He opines that with other global economies trailed down with laggards and crisis like Europe, Japan and China already at higher levels, US economy has started throwing some easing numbers and one can think that FII's flows in equities would INCREMENTALLY REVERSE back to the green pack in second half of the year 2011.



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Introduction

1. Global markets which went into dizzy in 2009, after getting encouragement from the Government have come into action again. Global interest rates are low and so are the bond yields. This is more western oriented wherein GDP growth rates are less than 3 per cent *versus* more than 6 per cent GDP growth in emerging markets. Hence, investors are investing in emerging markets, which are growth oriented as also having higher valuations. The Government driven packages have brought in new cash into the system, which is waiting to be pumped into the markets. Low yield bonds and low interest rates are driving FIIs' to invest in emerging markets and, thus, driving these markets up.

Some major markets

2. One can have a look on the following major markets:

- ◆ **US:** Stock markets in the US are more mature to performance. They perform 6 months ahead due to anticipation of events over the actual events. Stocks and gold are moving now and then suggesting a change in the economy. This week, the National Bureau of Economic Research in the US announced that the recession ended in June 2009.

Based on August 2010 data, fear of double dip recession has reduced, which has been felt across the board from private sector jobs to retail sales. The central bank has pumped

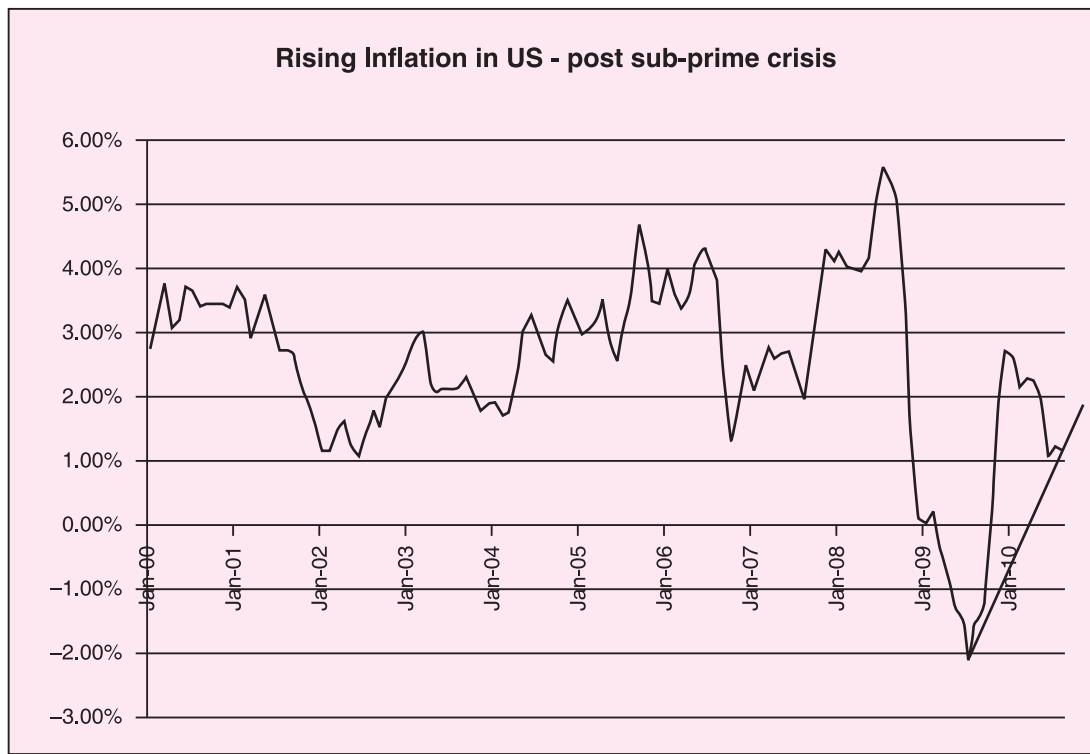
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more than \$1.7 trillion into the economy with purchases of treasury and mortgage-related debt. Although the recession ended in June last year, yet the unemployment rate is at a stubbornly higher rate of 9.6 per cent and there is an oversupply of homes in the market. Residential construction and sales are improving, but they are on their way too soon to assume a sustained growth. However, it is understandably better since this activity will creep higher interest as great affordability pulls people into the market.

Dow Jones Industrial index moved up a bit and appreciated by more than 5 per cent from 1st week of September to mid-September. Gold prices have been moving up since quite a while now. This is due to many investors moving out of US denominated bonds and stocks earlier : because of the belief that the Government has spent away too much money; that borrowing is out of control; and that the US dollar will not hold

its value against other currencies. To avoid that potential loss, they are moving into gold. Due to the Government's pumping in so much money into the system and with the anticipation of people getting pulled back into the markets, inflation has to be just around the corner. There's a lot of money waiting to be spent between all the savings from consumers and businesses clutching tightly to their cash. When investors psychology changes from fear to at least comfortable (not even greed), a torrent of money will flow into goods and services. Prices will inevitably go higher as demand exceeds supply.

Following chart shows the rising inflation in the US post sub-prime crisis to 1.15 per cent in August 2010, hitting deflation at 2.10 per cent in July 2009 and going all the way up to an inflation of 2.72 per cent in December 2009. This rebound of 4.82 per cent in 5 months seems just the beginning of a smoother ride going forward.



Source: www.inflationdata.com

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- ◆ **Europe:** A lot has been written on Europe. It is observed that it always tides with the US economy, but with a lag period. The widely known Greece crisis and the stimulus package started the run spreading to other European nations. However, Greece cannot unilaterally stimulate its economy with monetary policy like the US who printed new money and injected a total package of more than US\$1.3trillion into the system by purchasing outstanding debt and has, thus, expanded its balance sheet size since the global financial crisis began.
- ◆ **Japan:** It is going through deflation, triggered by an asset bubble which has collapsed. Japan has an aging population, over-presentation of older voters and trade surplus-funded fiscal deficits. Many older people in Japan live on fixed income, so they favour falling prices and are against loose monetary policy. Japan has one of the most acute cases of an aging population in the world with about 22 per cent of population being over 65 years old as compared to 20 per cent in Germany and the U.S. and about 8 per cent in China.

US have big trade and the Government budget deficit with a substantial portion of debt being held by foreigners while Japan has a large trade surplus, but also has a budget deficit. Japan has public debt like the US, but with the vast majority of it being held domestically.

Japan announced an \$11 billion stimulus package to tackle deflation and a rising yen, which has hit a 15-year against the dollar. The Central bank has kept interest rate at 0.1 per cent with GDP growing at an annualised 1.5 per cent in the April-June 2010 quarter.

- ◆ **India:** The BSE-30 index crossed the sentimental 20,000 mark this week, in line with improved outlook on Indian economy. Good monsoons improved outlook for the farm sector. Planning commission is estimating 6 per cent growth in farm production. Strong growth in manufacturing sector with 12.2 per cent growth during April-July 2010 has raised improved outlook for overall GDP to grow beyond current projections of 8.5 per cent.

Following figure presents annual and monthly checks with booming outlook on agriculture:

<i>Annual figures</i>				
% growth	FY 2007	FY 2008	FY 2009	FY 2010
GDP growth	9.7	9.2	6.7	7.4
Credit Growth	28.1	22.3	17.5	16.7
WPI avg inflation	6.5	4.8	8	3.6
Exports \$ bn	129	166	189	182
Imports \$ bn	191	256	308	299
<i>Monthly checks</i>				
% growth	May-10	Jun-10	Jul-10	Aug-10
Industrial production	11.3	5.8	13.8 na	
WPI inflation	10.6	10.3	9.8	8.5
Exports	31	30	13	22
Imports	37	23	35	32
FDI \$ mn	2,213	1,380	1,785 na	

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Booming Agriculture - Kharif estimates				
Fig in MT	2009-10	2010-11		
Rice	75.9	80.4		
Cereals	99.5	108.6		
Total pulses	4.3	6.0		
Total foodgrain	103.8	114.6		
Oilseeds	15.7	17.3		
Sugarcane	277.7	324.9		
Cotton*	23.9	33.5		

*in mn bales of 170kgs each

Foreign funds rush to India

3. The difference in bond yields between the west and India has brought in US\$16 bn foreign funds in bonds till date with US\$9.1 bn FII's exposure to debt instrument this year. The Indian Government has eased ceiling for foreigners to invest in Government securities from US\$5 bn to US\$10 bn and in corporate bonds from US\$15 bn to US\$20 bn. This move would ease pressure on banks to raise interest rates as the credit growth is picking up. However, this would increase volatility in market when interest rate rises in the west since investors would incrementally go back to the green pack.

Upcoming IPO: The run in BSE-30 Index has brought in cheer for new players to get listed. There are more than 10 IPO's coming up who are looking for retail and HNI participation to continue. In the recent past, some of the companies have had some gains post-listing which has brought in interest back from retail and HNI's. Companies which came out with new issues in April, May and July have done badly on current price. However, August and up to Mid-September, wherein 4 issues were announced, more than 10 per cent gains are witnessed over issue price.

Conclusion

4. FII flows are the key triggers driving Indian stock markets. One can recommend investors, who have invested into Indian equities to start booking profits. Though it is not a hurried situation since the 15 per cent corporate earnings growth for BSE-30 cos in India would make the same kind of returns to the investor. However, since Indian equities strongly move along the lines of global asset allocation which determines FII flows, in relative terms, US market is going to be the next asset that these FIIs' would like to invest in the coming calendar year onwards. Overall, Indian numbers stand good as they are forecasted with strong GDP growth reflecting into steady corporate earnings growth going forward. Many investors who did not get a chance to enter in the recent Indian stock market rally and who are still holding stocks purchased at higher levels during the previous highs, need to book losses and move on. With other global economies trailed down with laggards and crisis like Europe, Japan and China already at higher levels, US economy has started throwing some easing numbers and one can think that FIIs' flows in equities would INCREMENTALLY REVERSE back to the green pack in second-half of the year 2011.

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