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New hopes for Taiwan

Kuomintang (KMT) made 2 very significant victories in elections held in Taiwan this year. Mr Ma Ying-Jeou, candidate-to-election from KMT won the presidential election on 24 March. The party also took control of the Legislative Yuan after elections earlier in January. After those 2 elections, KMT regained control over Taiwanese government.

The shift in political power brought about hopes about business and investment in Taiwan. Unlike the ruling Democratic Progress Party, KMT had forged forward to build a closer tie with mainland China. It is likely that economic ties across the strait will be improved under the rule of GMT. Moreover, Mr Ma put forward the I-Taiwan 12 projects to revitalize the stalling Taiwanese economy.

Let see what they means to Taiwan.

Better cross strait relationship shall help to unlock plenty of business opportunities. First, Mr Ma had vowed to push forward the re-opening of the direct connection by air, ship and posts with mainland China and he also planned to allow mainland tourist groups to visit Taiwan. More convenient traffic and bringing in tourist group shall benefit tourism, hotel and catering as well as retails business. Moreover, barrier for Taiwanese banks to tag into the business opportunities in mainland China is being tore down. The Taiwanese regulator approved the plan of Fubon Financials to acquire a 19.9% stake in Xiangmen Commercial Bank. It is likely that other financial institutions will follow suit. In the past, they were not able to do business with Taiwanese companies in China. But now, it becomes a new opportunities for them.

For domestic economic development, Mr Ma also put forward the I-Taiwan 12 projects. The projects include investment in transportation infrastructure such as railroad, ports and airports and development of new industrial parks for innovative industries. Theses would also create jobs and business opportunities for the construction industry.

Undoubtedly, the change in the Island would open up a lot of opportunities. But the change in external environment brings along challenges. US economy is slowing down, consumption and imports growth shown weakness in recent months. It shall be a headwind for the Taiwanese electronic industry. Since the electronic industry the dominant to Taiwan stock market (it represents around 60% of the MSCI Taiwan index), risk to this sector should not be overlooked.

Overall, we remain neutral to Taiwan for now. We believe that the shift in political power shall help to unlock business opportunities and improve economy conditions in Taiwan. But, it will take time for Mr Ma and his new government to push through their plans and the slowdown in US would hurt Taiwan electronic industry. It is likely that Taiwan stocks performance shall diverge. The domestic driven sectors e.g. real estate, financials are where good performance stay with.

US: Negative

DJIA was up by 4.54%, S&P 500 rose 4.75% and NASDAQ moved up by 5.87%. The Fed's interest rate decision was in the spotlight again. It cut the interest rate by 0.25%. It was the smallest move since Jan 2008. Investors interpreted it as a signal for the rate cut cycle the end soon. It also showed that the Fed believed aggressive rate cut is no longer needed to quench panic selling in the financial markets. Equities markets responded with a strong rebound. Still, we think that the change in investors' attitude was just a short-term stimulus. Fundamental factors e.g. corporate profits, economic conditions shall drive the market afterwards. As US economy is still sliding down, we remain cautious to US equities.

EU: Negative

European markets rebound also. DAX was up by 6.33%, CAC gained 6.15% and FTSE100 moved up by 6.92%. Market performance had continued to trail that of US. For the underlying economy, the UK housing market data is most concerning to us. House prices reported the first year on year decline in 12 years and mortgage loans default rate jumped. It showed that UK housing market is under pressure. It would be a major risk factor for EU in coming months.

Japan: Negative

NIKKEI jumped by 10.57%. However, we still rate it behind other markets both in terms of economy and stock market performance. The reason is that Japan had yet to re-emerged from export led growth and remained reliant on other markets for its economy.

China: Slightly negative

HSCEI surged by 17.78% in Apr. A share market got a jolt from the Chinese government. It has cut the stamp duties from 0.3% to 0.1% and announced the requirement for preciously non-tradable shares. Although the stamp duties had always been a tiny transaction cost, investors perceived that as a move to prevent further decline. The A share markets rebound strongly and gave the Hong Kong listed counterparts a push, especially for the insurers.

Hong Kong: Slightly negative

HSI also jumped by 12.72% last month. The domestic enterprises are relatively slower mover compare to mainland Chinese companies. As the mainland enterprises were having better earnings, it is expected that the local companies will continue to lag behind.

Emerging Markets: Slightly negative

Most of the emerging markets followed the major markets in recent month. Still, Brazil stock market remained an exception. It had stayed close to the peak despite nearly every market dropped. The credit rating agency S&P lifted the credit rating for sovereign debt of the country to investment grade. The stock market jumped on that and broken new high. It proved that the market had not entered bear market. However, the advantage in valuations compared to other emerging markets had been eroded.

Bonds: Slightly positive

As mentioned earlier, the Fed had signaled that its rate cut action is coming to the end. The yield for both 2 years and 10 years Treasury bonds rose. However, the US economy is still fragile and we believe that the Fed still needs to keep rate low. For Europe and UK, the interest rate trends remained unchanged. ECB kept its interest rate at 4% on inflation concerns. Bank of England cut by 0.25% due to the threat of slowing housing market. Overall, the interest rate trend became less favourable on Fed action.

Commodities: Positive

The change in expectations about future course of US interest rate was also the driving force in commodities market. As US interest rate is expected to be near the bottom, it led to a strong rebound of USD. In turn, commodities prices dropped. Gold dropped more than 150 USD/ounce to around USD 840/ounce. However, the Fed shall continue to keep rate low and US economy is still heading down. The USD should just be having a rebound and it is not expected to last. Thereby, we still suggest investors to accumulate commodities related investment when it pulls back.

Hedge funds: Neutral

The HFRX Global Hedge Fund Index rose 1.20% in April. HFRX Equity Arbitrage Index, HFRX Relative Value Arbitrage Index and HFRX Event Driven Index were the performance leaders. Their month gains were 2.40%, 1.55% and 1.61% respectively.

Advices for investors

Equities market finally became stable and investors' sentiment was no longer overwhelmed with sub prime related problem. Now that investors seem calmed down, we think that fundamental factors e.g. corporate profit, economic prospect would drive investors decisions. As US and EU both shown signs for further economic slowdown, they shall weigh on the economy of other countries. Thereby, we remain cautious towards equities investment.

Change in interest rate expectation triggered a rebound in USD, it, in turn, led to a pull back in commodities prices. We reiterate the view that investors should accumulate commodities investments as they consolidate.

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