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Rescue package need to move quicker.

Fighting depression is undoubtedly the most important task for the new US administration. Thus, Obama moved as quickly as possible to put his plan onto the table. The plan consists of 3 parts. They are the American Recovery and Reinvestment Plan (ARRP), Financial Stability Plan (FSP) and Homeowner Affordability and Stability Plan (HASP). Each of them target at reviving a specific area, ARRP is for general economy, FSP for the financial system and HASP for housing market.

ARRP moved on quickly. It had been approved by Congress and Senate, and signed by Obama to become legislation. So, the US government can now start to put it into work. The helps from the USD 78 billion tax cuts and government spending under ARRP is expected to show in 2-3 quarters time. Still, it would be insufficient to reviving the downward spiral in US economy. Let's take the job market as an example, Obama planned to create 4 million jobs in the next 2 years. But, non-farm payroll statistics showed that US had lost 2.5 million jobs in the 5 months to Jan 2009.

But, FSP only made baby steps. The suggestion for setting up a bad bank made a come back. Still, asset valuation remained an unmovable obstacle. The US government turned to public-private partnership for the bad asset buyer. Under the new ownership structure, the government can leverage on the capital and expertise of the private partners to help closing the valuation gap. Moreover, the political risk would be lower as the prices are negotiated by market participants. However, the new suggestion cannot insulate the banks from losses arising from the bad assets completely. The private partners under the new plan shall be financial institutions e.g. hedge funds, private equity funds. They usually borrow from banks to fund their investment. If they ran into problem after buying the bad assets, the banks would still suffer from losses on loans to them. But, if the prices of the troubled assets recover, the banks were deprived of the gains. In other words, the risk and reward for the banks are tilted toward losses. It seems that the new plan is not an attractive option for banks. We think that the US government needs another plan, which gives the bank more protection from the bad assets. Bad bank and nationalization should be on the list of choices.

In sum, the new administration pushed the rescue package a step forward, which is an achievement. ARRP is expected to help US economy later in the year. But, FSP does not make enough progress. Without a viable plan to restore the health of the financial system, it is unlikely the rescue package will manage to turn US economy around. The general economy and the financial system rely on each other for their prosperity. So, US economy can not flourish if the problems in the banking sector is not taken care of.

US: Negative

DJIA dropped by 11.72%, S&P500 lost 10.99% and NASDAQ went down by 12.20% in Feb 2009. Financial companies are still in danger. We can tell in 2 ways. First, aids by government were still needed. AIG called for capital injection again. This time it got USD 30 billion. Second, progress of FSP is trivial. The government is now conducting stress test for 19 largest financial companies. But, there is no concrete plan to due with the problems for companies scoring poorly in the stress test. They can only rely on urgent capital injection to stay afloat. As for the equities market, DJIA and S&P 500 had already broken the lowest level since 1997. Though that it may have occasional rebound, it would only be short-lived.

EU: Negative

DAX lost by 6.68%, CAC lowered by 9.11% while FTSE100 fell by 7.70%. Lately, the banking crisis in Eastern Europe caused concerns about stability of Euro. Banks from West

Europe expanded aggressively in Eastern Europe in the bloom years and lured the locals with low interest loans denominated in Euro or Swiss Franc. However, Eastern Europe experienced huge capital outflow and their currencies depreciated severely against Euro since the later half of 2008. The borrowers in East Europe found their Euro-denominated debt swelled in local currencies, but their assets and income did not grow at the same pace. Servicing the debt became a sore. At the same time, defaults in the region became a problem to the banks from the West. What made it more worrying is the attitude of Continental Europe. German Prime Minister Merkel turned down Hungary's request for a EUR 180 billion aids to countries in the region. It showed that West Europe did not want to have their fate tied to the Eastern Europe countries. They still want to retain the right to back off from helping the Eastern counterparts. Although EUR 24.5 billion help was offered by World Bank, Europe Investment Bank and European Reconstruction and Development Bank. But it was just a small number compare to the EUR 1 trillion lending by West Europe banks in the region. Without full support from the West, the banking system in Eastern Europe will still be in danger and remain a threat to Continental Europe.

Japan: Negative

Last month, Nikkei 225 index lost 5.29%. Recent data showed that Japanese exports and industrial production plummeted. But, it was not unique to Japan. Exports for Korea, China, Singapore, Germany, UK and Italy all diminished. Clearly, vanishing demand was the cause for contraction in exports. So, weakening Yen is not going to help. We remain negative on Japan.

China: Negative

HSCEI ended Feb 2009 with a 3.21% drop. Stimulation policy for the 10 highlighted industries had all been announced. Now, the market is speculating that Chinese government will announce more policies to prop-up the economy during the Communist Party meeting early March. Still, the global economy is not improving. Even if there is more policy to boost the economy, we do not expect the impact on equities market to last long.

Hong Kong: Negative

Hang Seng Index also dropped by 3.51%. Earnings season started with the banks reports. In general, their results were not good, but expected. HSBC brought a negative surprise, earnings was much poorer than forecast. Thus, share price plunged and dragged on Hang Seng Index. For the earnings reports to come, the Chinese enterprises are the ones that can move the market. But, the impact is more likely to be negative as many of them had already issued profits warnings earlier in the year.

Emerging Markets: Negative

Eastern Europe was the market in spotlight. Since the conditions Eastern Europe is linked to Europe, we have our comments in the paragraph for Europe this month. Please refer to our comments for Europe for details.

Bonds: Neutral

The threat of bubbles in Treasuries issue went down further. Although equities market plummeted lately, it did not drive up prices of Treasuries again. On the other hand, the Treasuries fell gradually. 30 years Treasuries bonds fell 15% from peak and now the price is very close to the level before it shot up last year. For 10 years Treasuries note, the trend is very similar. Just that the ups and downs are less obvious compare with 30 years issues.

Commodities: Slightly positive

Commodities are still in range trading. Gold approached USD 1,000/ounce when investors fled Treasuries for safe heaven. But, as the decline in Treasuries issue slowed down, gold pulled back very quickly. Now, it is again hovering around USD 900/ounce. It has not break away from range trading. For crude oil, it had moved between USD 30-40/barrel and tested the bottom several times in the last 3 months. So, USD 30/barrel had become a strong support for oil prices.

Hedge funds: Slightly negative

HFRX Global Hedge Fund index lost 0.37% last month. Strategies with better performance were convertible arbitrage, relative value arbitrage and merger arbitrage. They made 2.15%, 0.49% and 0.44% gain respectively.

Advices for investors

The rescue package by US government did not move on smoothly. So far, progress for FSP, which aims at stabilizing and re-vitalizing the financial system, is disappointing. Although ARRP, the plan for protection jobs and general economy, is ready for kick-off, it is not sufficient to bring US economy back to track without the helps of banking system. So, US government needs to work out a viable plan to bring banking system back to work.

Our suggestion to investors is to continue accumulating assets with discipline and patience.

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