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Market Outlook for the Last Lap of 2010.....




Kevin Scully, 23 October 2010



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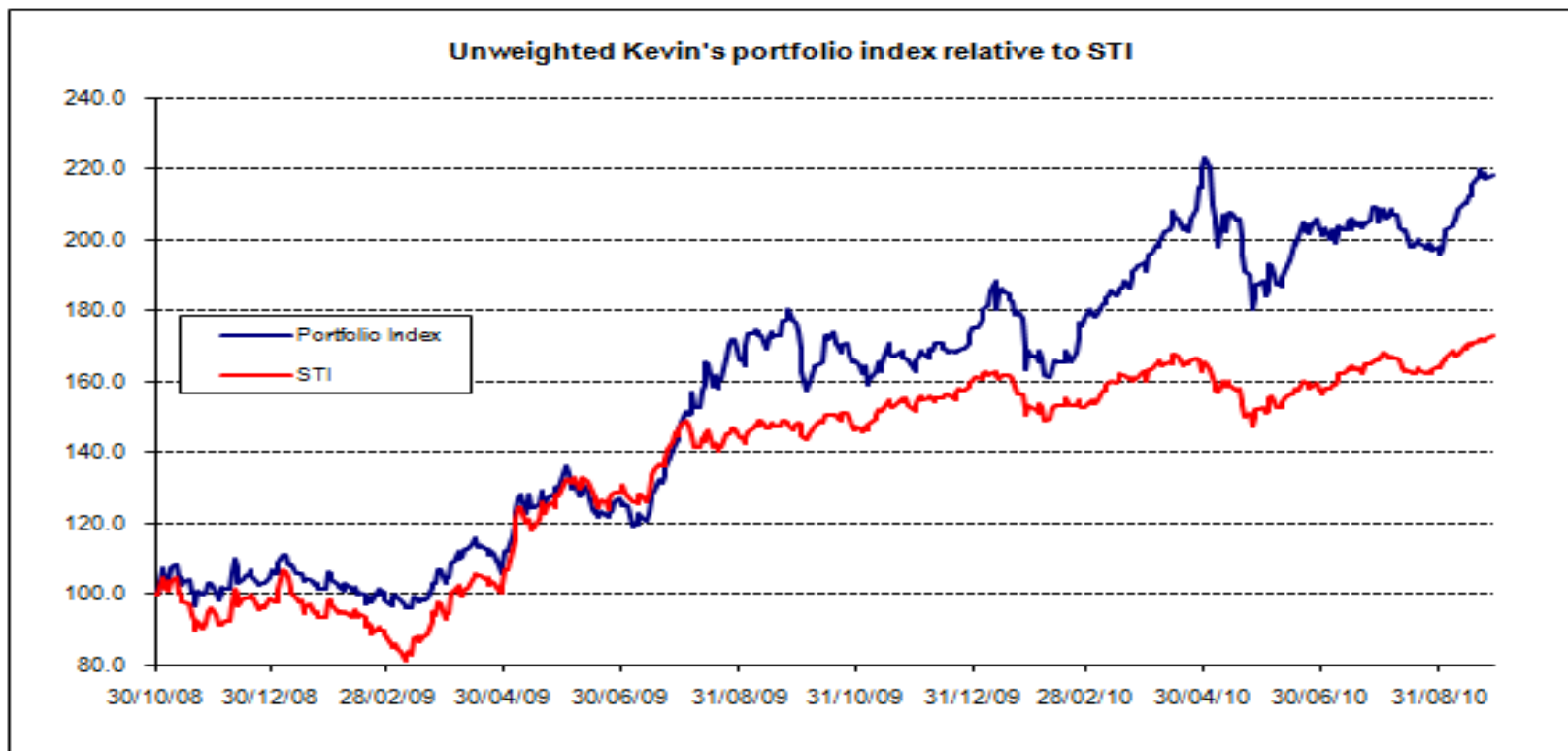


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For access to my Stock Picks (growth) and (yield) portfolios....



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At the InvestFair on August 21,
2010

I was bullish on stocks and said
that the STI Index would reach
3300 to 3500 before the end of
2010.....no change in the
target levels



A quick review of what has
happened in 2010 so far....

Stock markets have rebounded from their Q2-PIGS weakness....

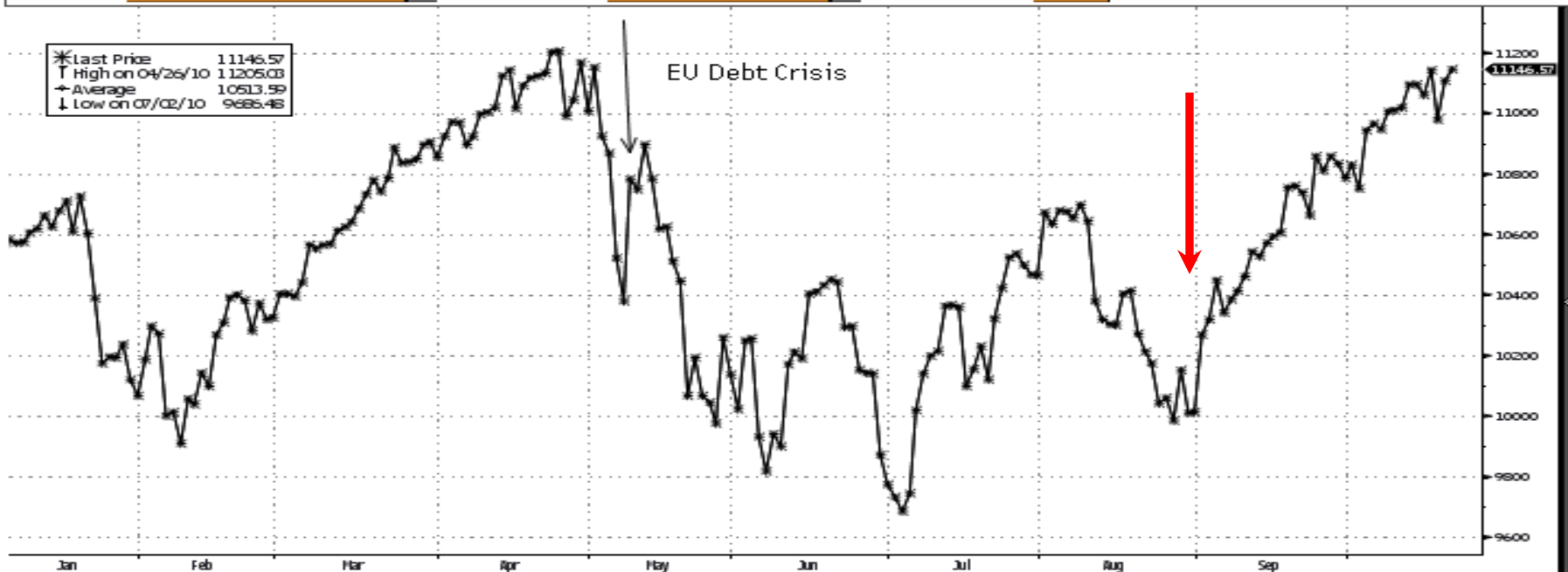
	Jan 1 2009	31-Dec- 09	% change	16-Jul- 10	% change	22Oct- 10	% change
Dow Jones	9034.7	10428.1	15.4%	10359.3	-0.7%	11132.6	6.8%
Nikkei 225	9043.1	10546.4	16.6%	9530.5	-9.6%	9426.7	-10.6%
Hang Seng Index	15042.8	21872.5	45.4%	20208.0	-7.6%	23612.7	8.0%
Shanghai Composite	1880.7	3277.1	74.2%	2392.5	-27.0%	2995.6	-8.6%
STI	1829.7	2897.6	58.4%	2947.2	1.7%	3158.4	9.0%

Dow in 2010.....

INDU 11146.57Y as of close 10/21

Index **GP**

INDU INDEX Advanced Hide GP - Line Chart Page 1/6
 Range 01/04/10 - 10/21/10 Upper Line Chart Mov. Avgs Currency USD
 Period Daily Lower None Mov. Avg 15 Events



Australia 61 2 9777 8600 Brazil 5511 3048 4500 Europe 44 20 7330 7500 Germany 49 69 9204 1210 Hong Kong 852 2977 6000
 Japan 81 3 3201 8900 Singapore 65 6212 1000 U.S. 1 212 318 2000

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Shanghai Composite in 2010

SHCOMP ↓ 2989.204 +5.671 Index **GP**
 DELAY 13:32 Vol 93,700 Op 2976.754 Hi 2993.908 Lo 2954.619 Prev 2983.532

SHCOMP INDEX Advanced Hide GP - Line Chart Page 1/6
 Range 01/04/10 - 10/22/10 Upper Line Chart Mov. Avgs Currency CNY
 Period Daily Lower None Mov. Avg 15 Events



Australia 61 2 9777 8600 Brazil 5511 3048 4500 Europe 44 20 7330 7500 Germany 49 69 9204 1210 Hong Kong 852 2977 6000
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STI Index in 2010

FSSTI ↑ **3159.15** -4.38 Index **GP**
 DELAY 13:28 Op 3163.60 Hi 3166.35 Lo 3154.58 Prev 3163.53
FSSTI INDEX Advanced Hide GP - Line Chart Page 1/6
 Range 01/04/10 - 10/22/10 Upper Line Chart Mov. Avgs Currency SGD
 Period Daily Lower None Mov. Avg 15 Events



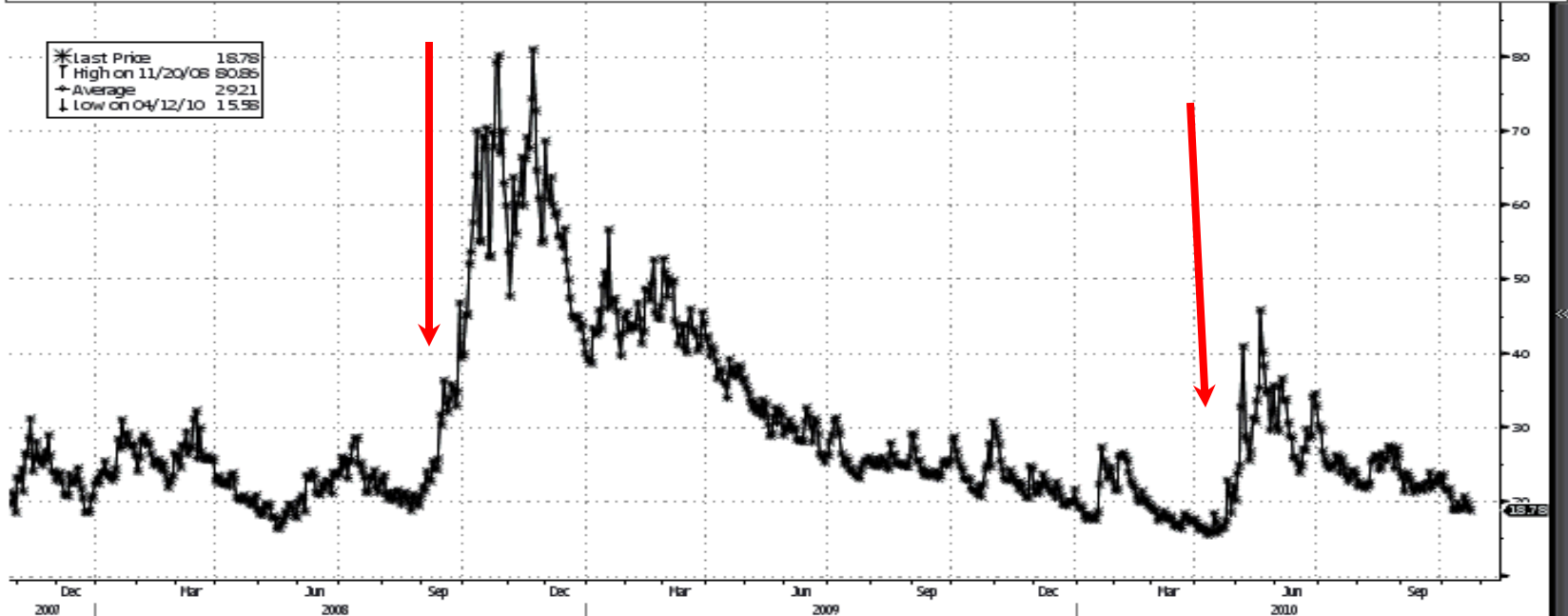
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VIX index which turned up during EU debt crisis has returned to normal levels


VIX 18.78Y as of close 10/22

Index GP

VIX INDEX Advanced Hide GP - Line Chart Page 1/19
Range 10/26/07 - 10/22/10 Upper Line Chart Mov. Avgs Currency USD
Period Daily Lower None Mov. Avg 15 Events



Australia 61 2 9777 8600 Brazil 5511 3048 4500 Europe 44 20 7330 7500 Germany 49 69 9204 1210 Hong Kong 852 2977 6000
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EU Debt Problems now manageable
but expect some problems in 2011 as
Governments struggle with Fiscal cuts
to reduce deficits

Current market focus is weak US
economic data



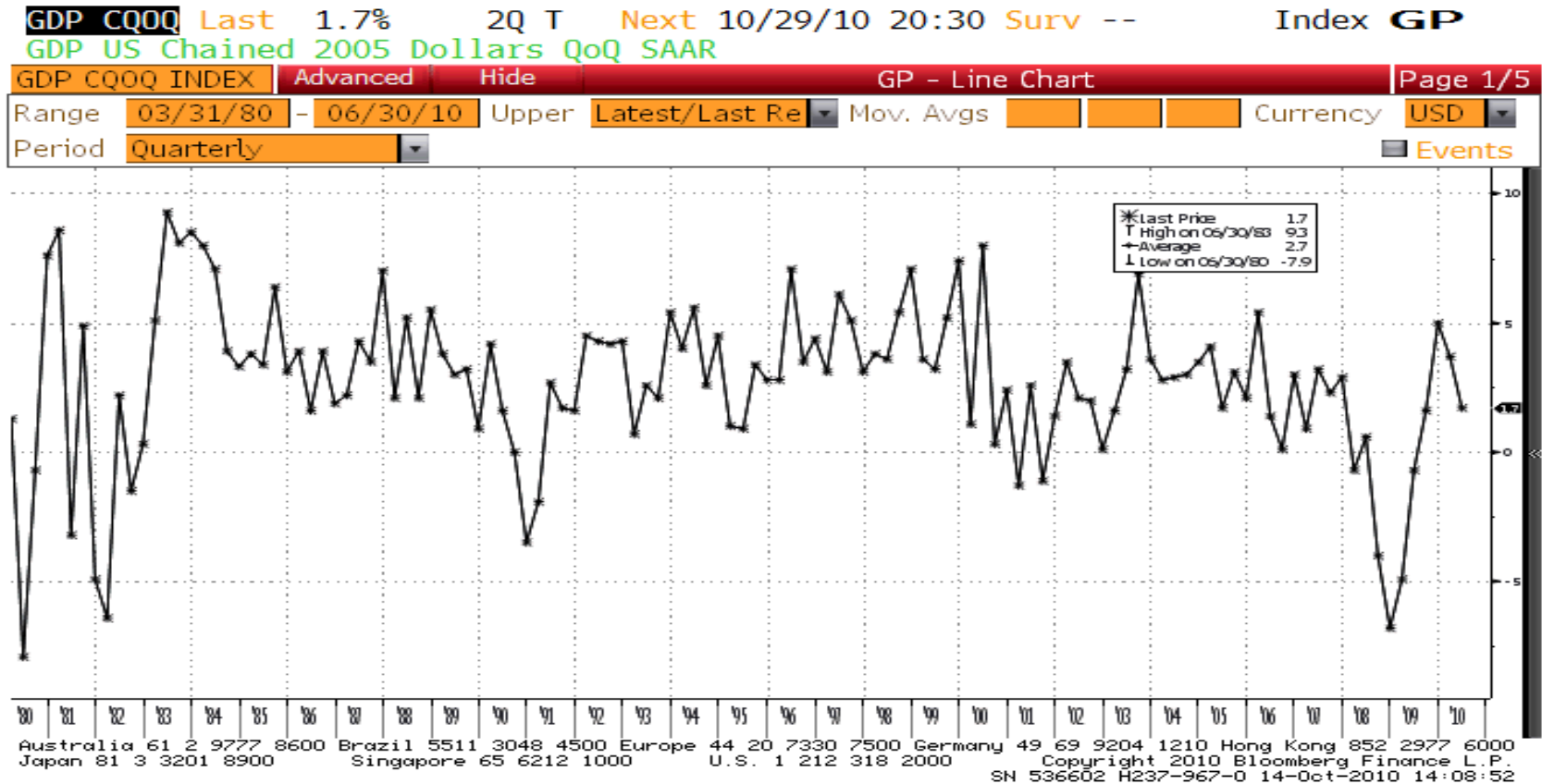
Economic recovery in the US is
faltering.....

But stock markets are
rallying....why !!!!??????

Global economy recovering nicely from 2009 led by developing economies

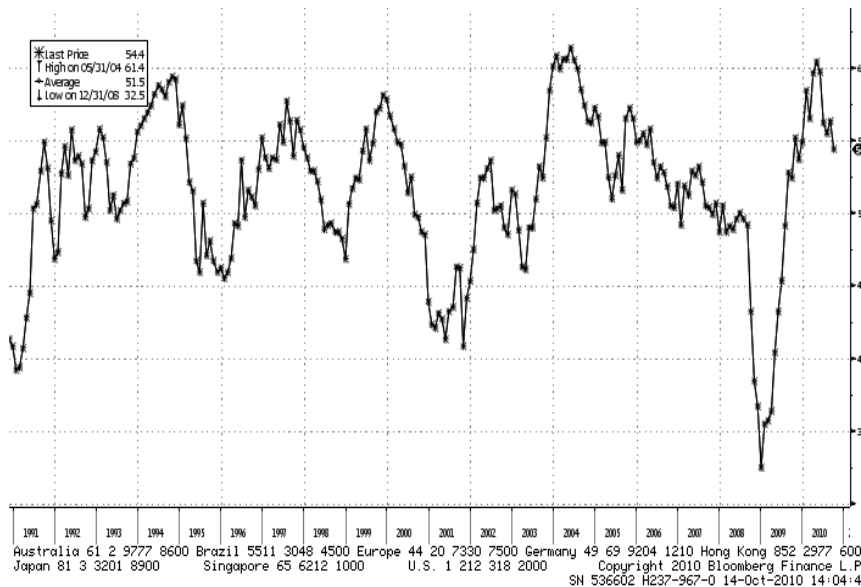
- World Bank – Global economy contracted by 2.1% in 2009 but forecasted to grow by 3.3% in 2010 and 3.3% in 2011
- US economy shrank 2.4% in 2009, but is expected to grow 3.3% in 2010 and 2.9% in 2011
- China grew 8.7% in 2009 and forecasted to expand 9.5% and 8.5% in 2010 and 2011 respectively
- But US economic forecasts are now too bullish – Q1 was 3.7%, Q2 was 1.7% and H2 now likely to be 1.5% giving full year growth of 2.1% or even less than 2%

US GDP growth starts to falter

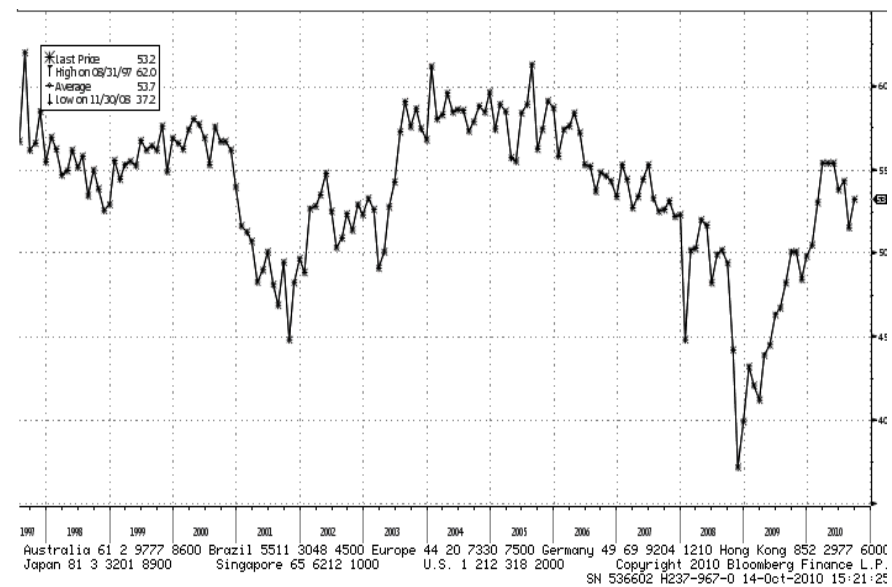


US economy both manufacturing & services sectors have started to falter...

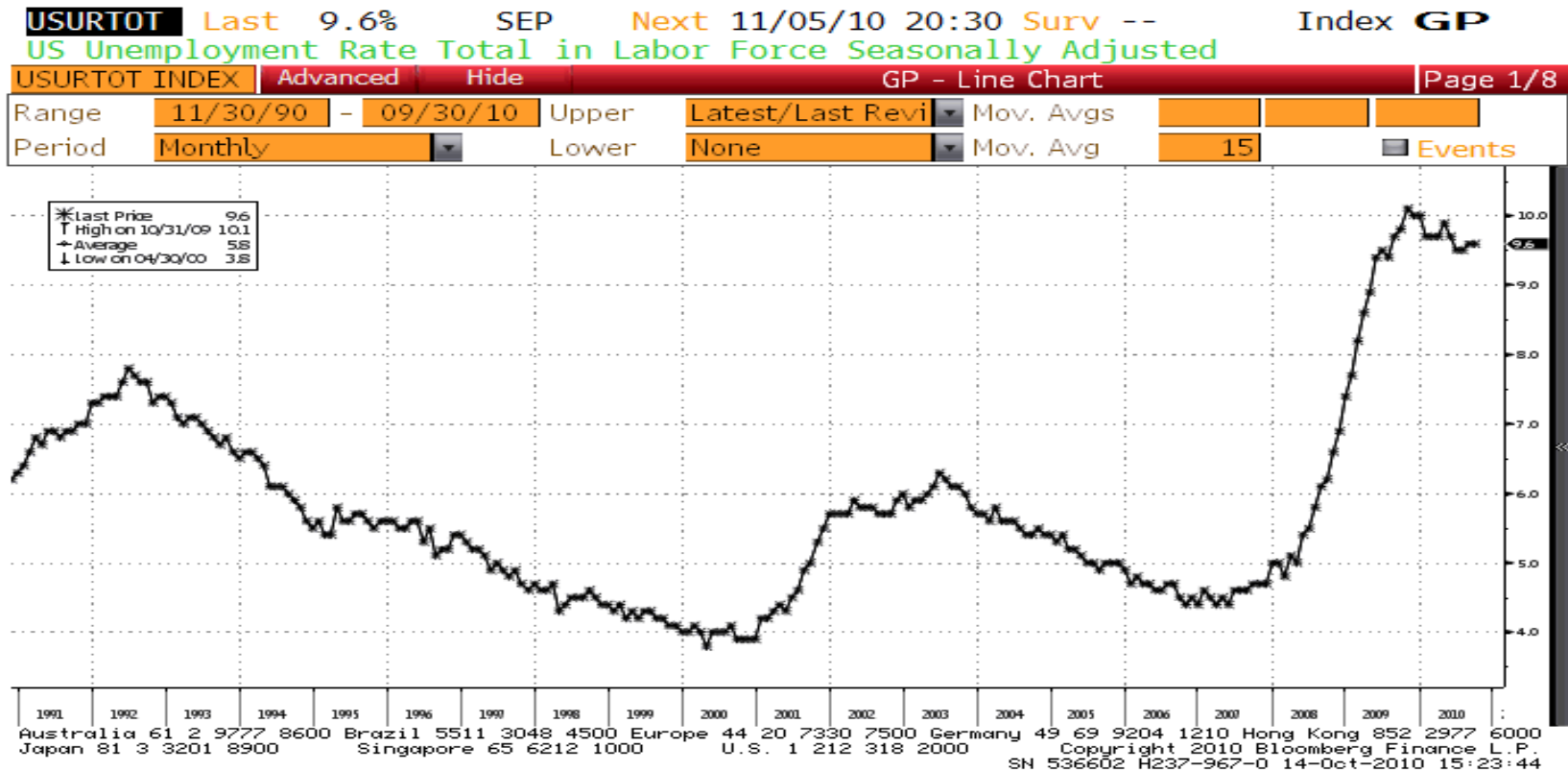
ISM Manufacturing



ISM Non-Manufacturing



US unemployment remains high




US Trade Deficit continues to widen

USTBTOT Last -\$42.8B JUL Next 10/14/10 20:30 Surv -\$44.0B Index **GP**
 US Trade Balance Balance Of Payments SA

USTBTOT INDEX Advanced Hide GP - Line Chart Page 1/8
 Range 01/31/92 - 07/31/10 Upper Latest/Last Re Mov. Avgs Currency USD
 Period Monthly Lower None Mov. Avg 15 Events



1992 1993 1994 1995 1996 1997 1998 1999 2000 2001 2002 2003 2004 2005 2006 2007 2008 2009 2010
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US Government and Federal Reserve now talking about QE 2 (quantitative easing 2)

.....expect an announcement on November 2, 2010

I think QE2 is the wrong strategy because.....

- US interest rates are already at an all time low.....its not high interest rates that is deterring consumption
- Banks are flushed with money and want to lend but nobody wants to borrow....so pouring more money into the banking system will also make the surplus cash worse
- What is probably needed is more fiscal spending but the US Government is already up to its eye balls in debt....so they don't have a choice
- QE2 is likely to lead to more volatility ahead

Short term QE2 will lead to a short term liquidity bull run !!!



the question you must ask is how much of this expected liquidity is already in stock prices and how long it will last

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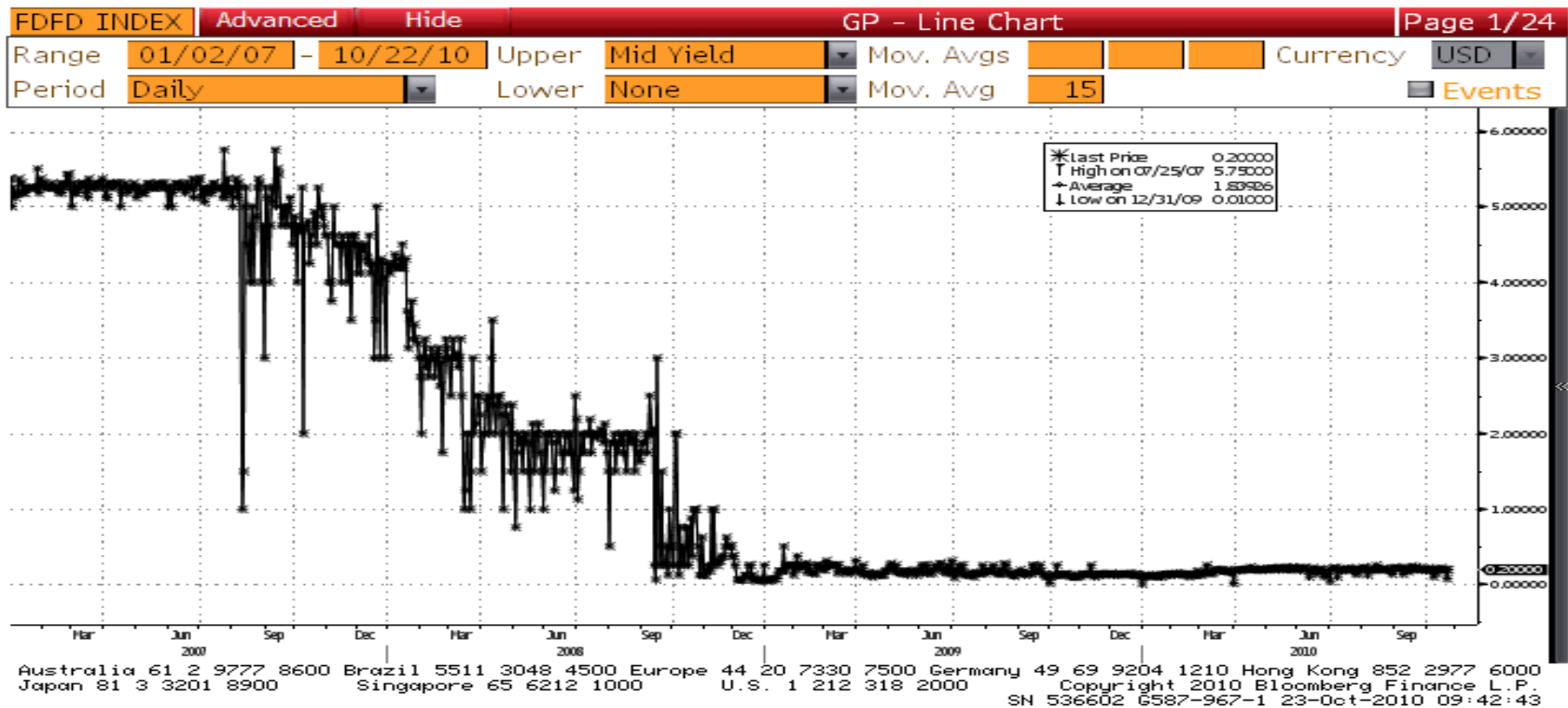
Lessons of 2007/2008

- Its 2010 and investors seem to have forgotten the financial crisis of 2007/2008.
- The recent financial crisis started in mid 2007 with the collapse of a small British Bank – Northern Rock in the US this was followed by the collapse of another 25 subprime lenders.
- The Fed responded through quantitative easing (QE) and lowered the Fed Funds Rate which was 5.25% in August 2007 down to 1% in October 2008. Interest rates are near zero now.
- Where did the liquidity go ?!

Fed fund rates in 2007 to 2008 from 5.6% down to less than 1% and almost zero now

FDFD .200000Y as of close 10/22

Index GP





US\$ weakened against most
unpegged currencies

EU strengthened against US\$ for about 12 months in 2007/08 hitting high of 1.60

EUR ↑ 1.3959 +.0021 WBFX 1.3958/1.3959 AEFX
 At 14:08 Op 1.3939 Hi 1.3970 Lo 1.3889 Prev 1.3938 Value 10/26/10

EUR CMPL CURRENCY Advanced Hide GP - Line Chart Page 1/24

Range 01/01/07 - 10/22/10 Upper Market Price Mov. Avgs Currency USD

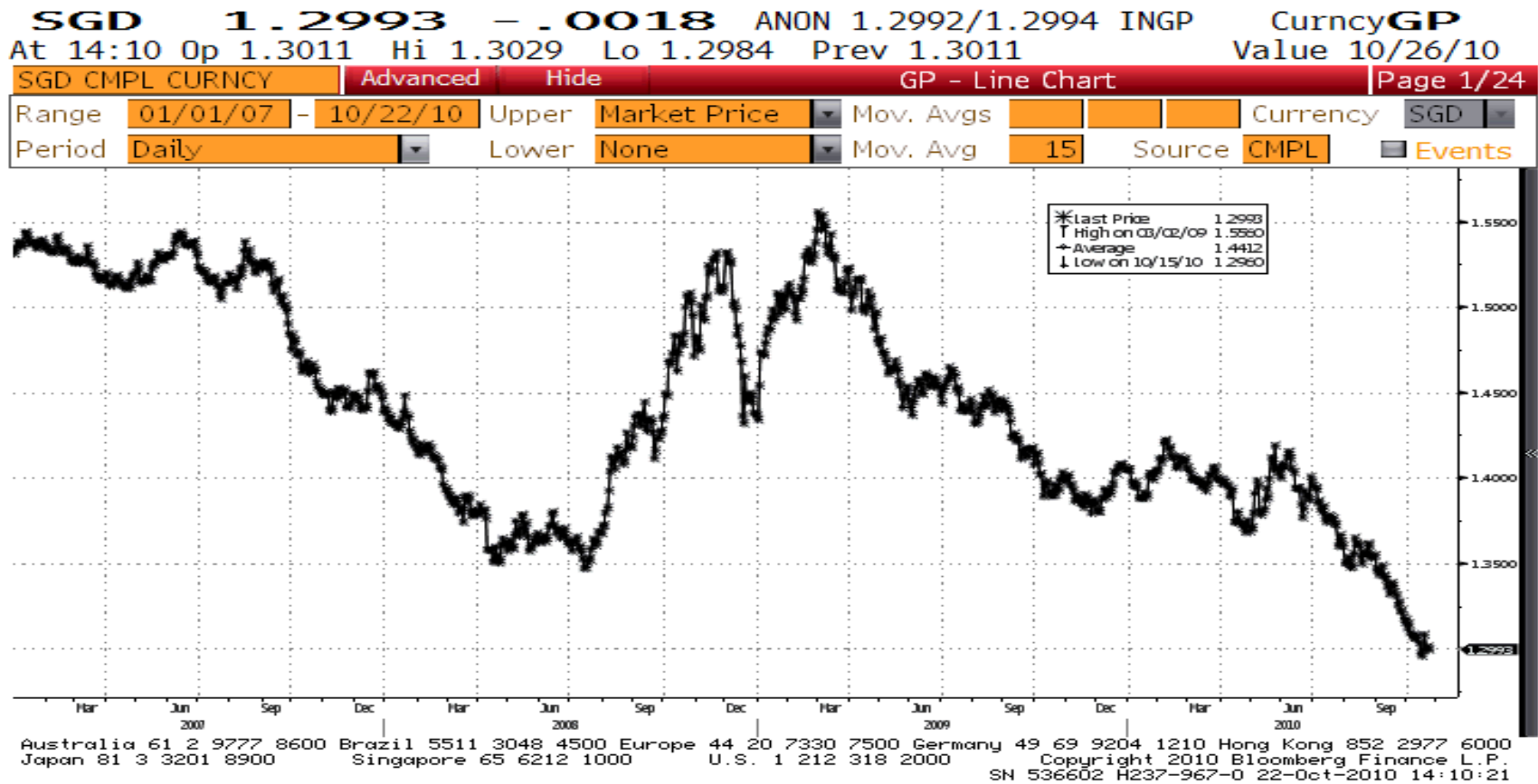
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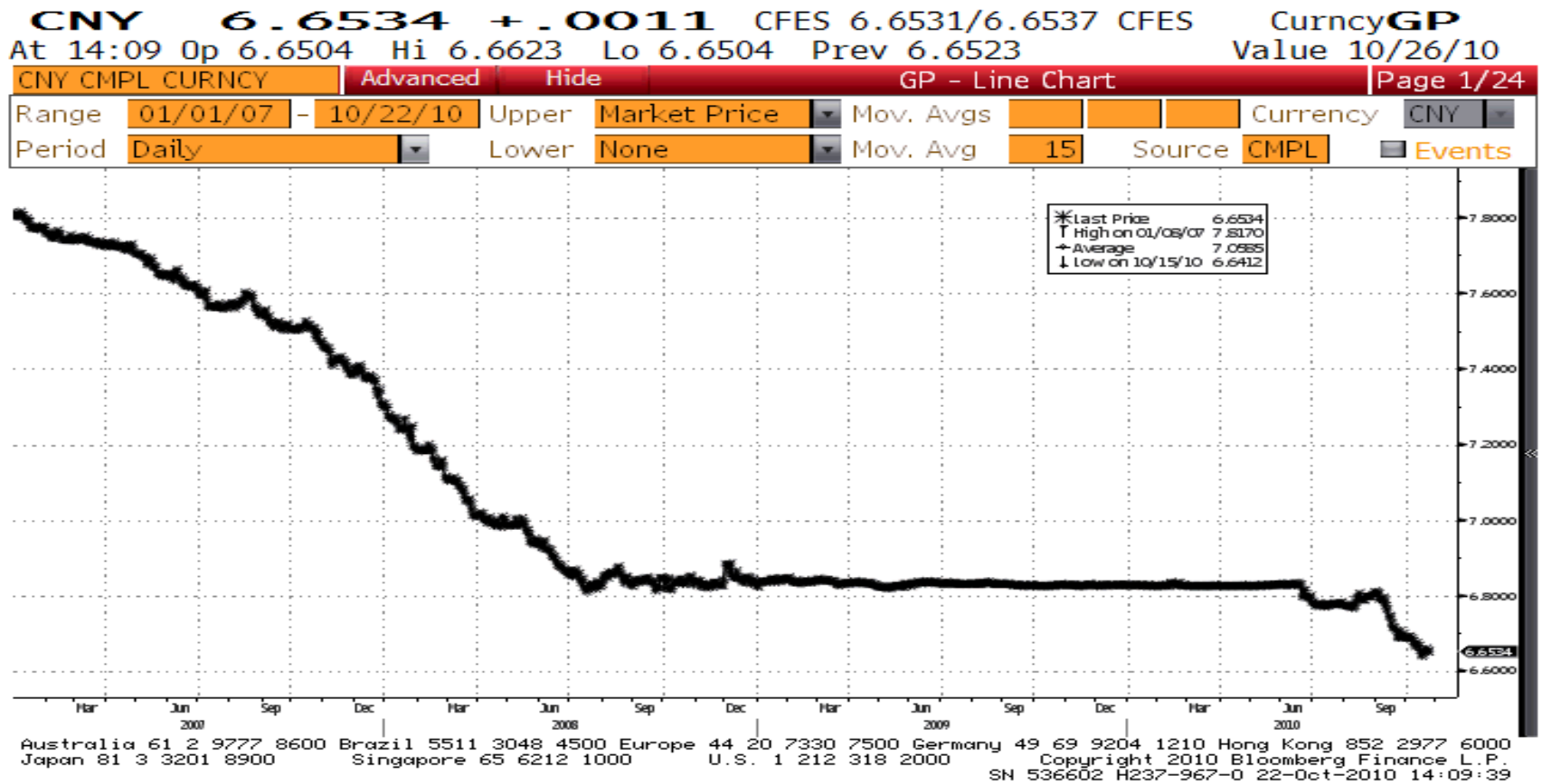
Australia 61 2 9777 8600 Brazil 5511 3048 4500 Europe 44 20 7330 7500 Germany 49 69 9204 1210 Hong Kong 852 2977 6000
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S\$ strengthened against the US\$ in 2007/2008 for nine months

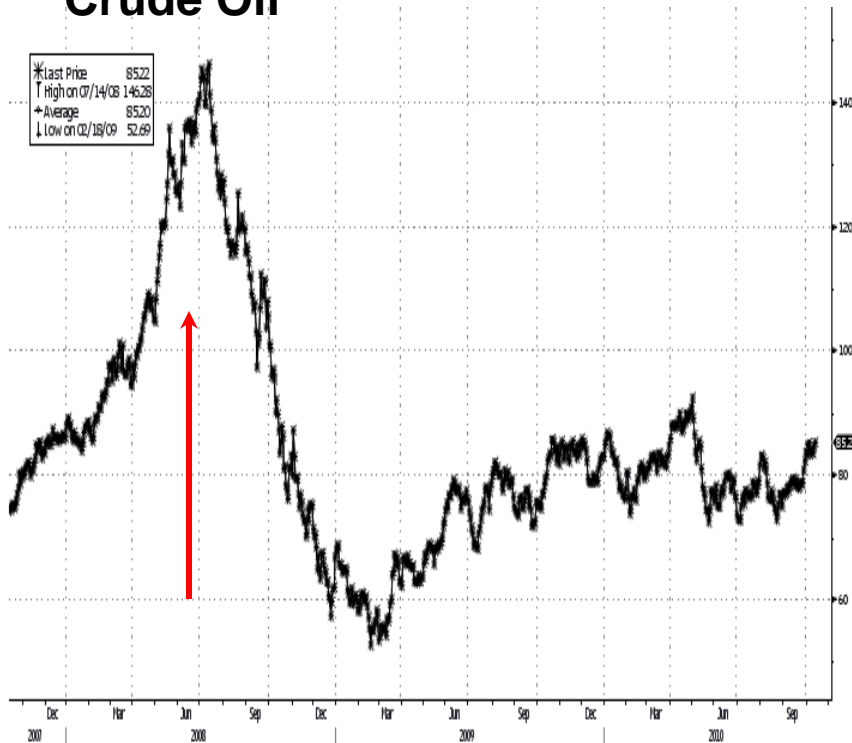


RMB in a controlled appreciation against US\$ in 2007/2008 for 9 months



Commodities - Crude oil, palm oil !!

Crude Oil



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 Japan 81 3 3201 8900 Singapore 65 6212 1000 U.S. 1 212 318 2000
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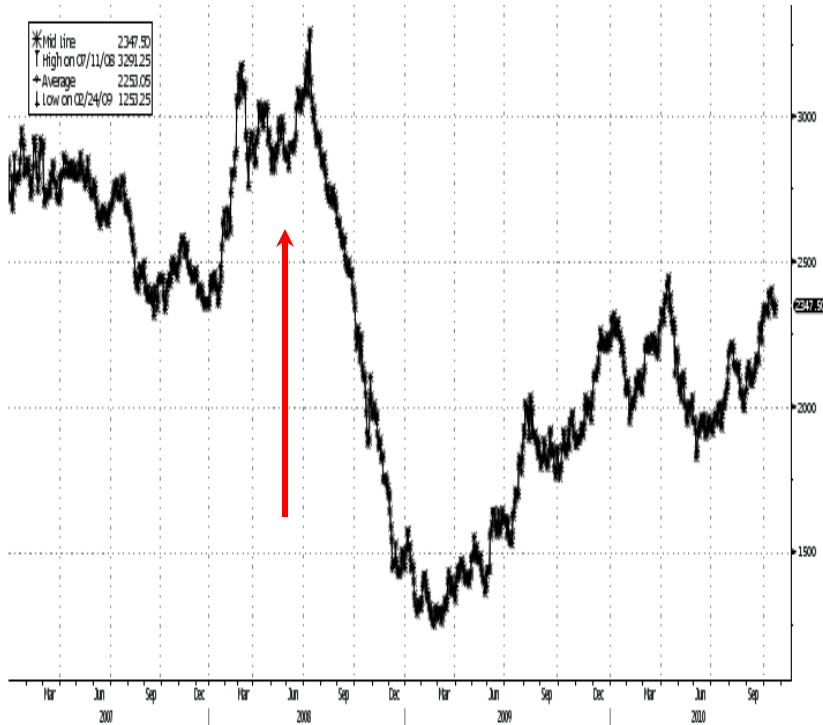
Crude Palm Oil



Australia 61 2 9777 8600 Brazil 5511 3048 4500 Europe 44 20 7330 7500 Germany 49 69 9204 1210 Hong Kong 852 2977 6000
 Japan 81 3 3201 8900 Singapore 65 6212 1000 U.S. 1 212 318 2000
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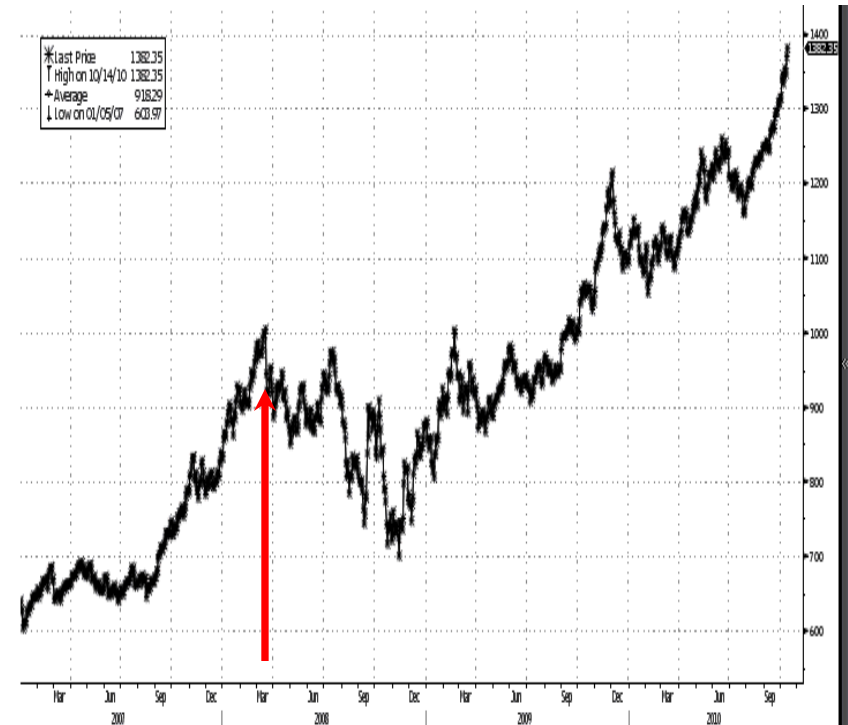
Commodities - Aluminium, Gold!!

Aluminium LME



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 Japan 81 3 3201 8900 Singapore 65 6212 1000 U.S. 1 212 318 2000
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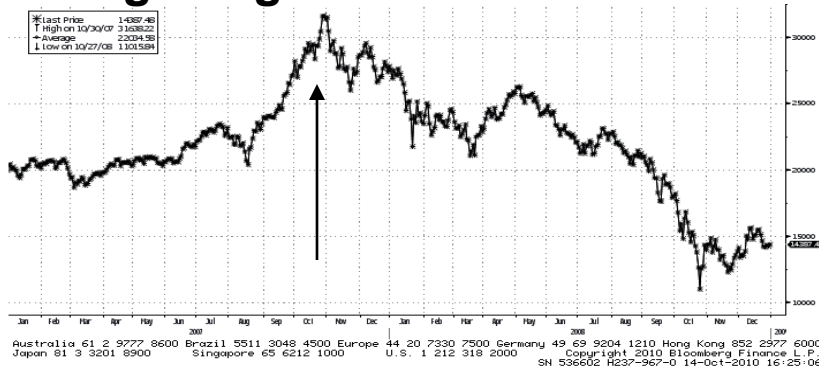
Gold



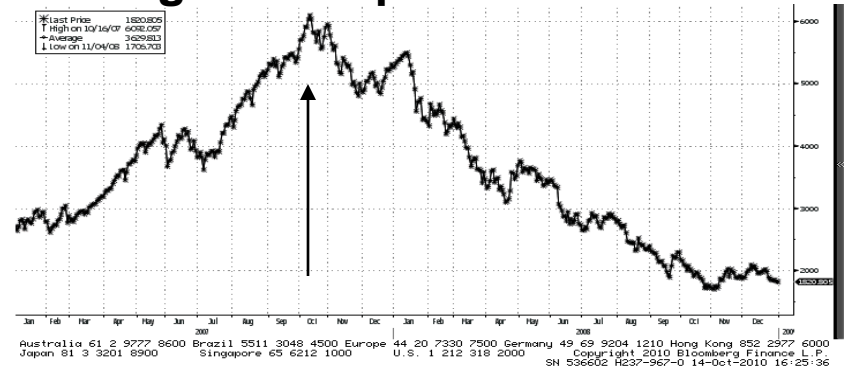
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Stocks

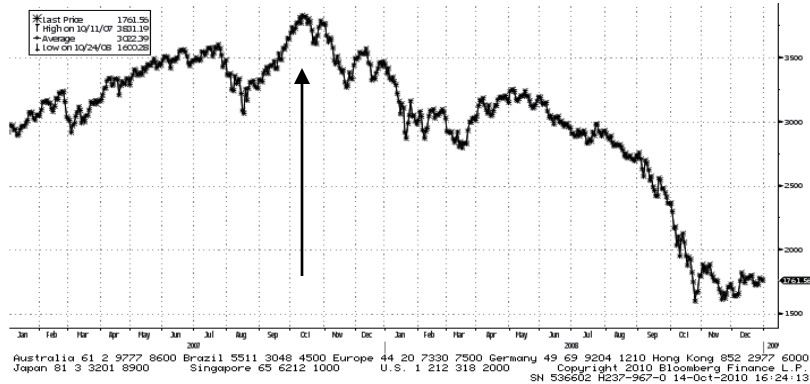
Hang Seng



Shanghai Comp Index



STI Index





QE1 liquidity BULL in
2007/2008....lasted between 9-12
months

QE2 BULL probably had preemptive
run and **started in August**
2010.....assuming it lasts 6-9
months.....

should end in Q2-2011



What could shorten or derail the
Liquidity Bull ???!

Trade war or currency war.....

Earnings disappointment

Premature raising of interest rates in
the face of inflation



Currency or trade war looming between the US and China

US President Obama under a lot of pressure to reduce trade deficit

- High unemployment, weak GDP and rising trade deficits – could lead to unilateral trade sanctions and a currency war
- Under a new US Currency Manipulation Bill passed by Congress in early October, if the US classifies China as a currency manipulator – it can impose tariffs on imports from China.
- US has already imposed import tariffs on China steel and China has imposed import duties on US food (chicken)
- Is this just rhetoric or is the threat real !!??

US pressured Japan to strengthen its currency in 1985 by 40% in 2 years

- The famous Plaza Accord saw the US force Japan to strengthen its currency when Japan was running a huge trade surplus with the US.
- It created the huge asset bubble in Japan and the asset deflation that we still see today some 30 years later.



Japan has never recovered from the asset inflation of that revaluation

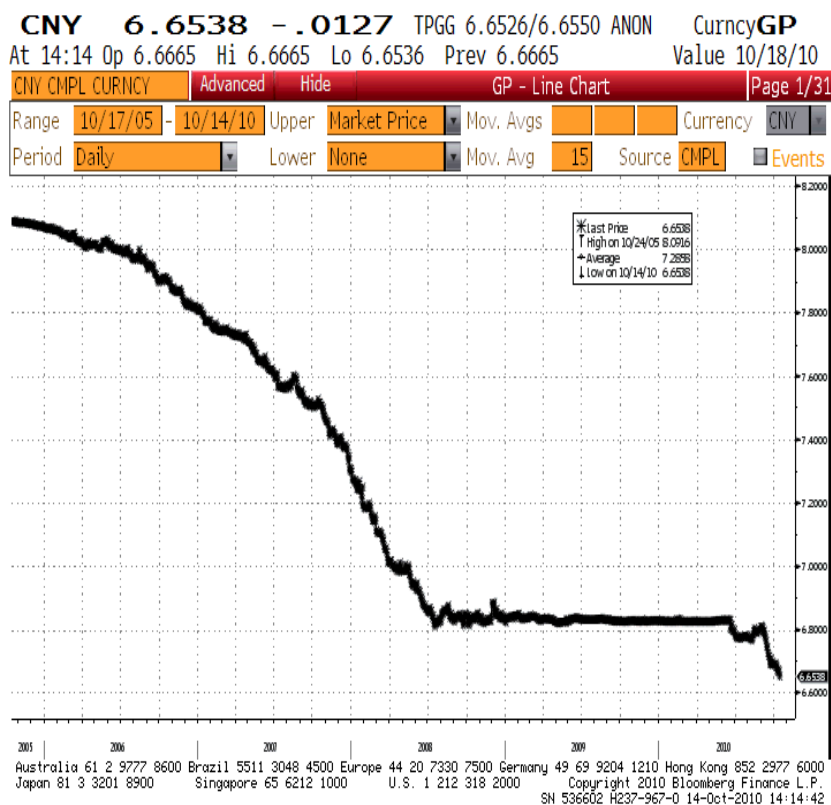
Nikkei 225 in 1984


- Revaluation of Yen caused huge influx of money pushed the Nikkei225 to 40000 and led to a massive property asset bubble.



China will never agree to such an Accord.....

- RMB will appreciate gradually.....but not at the rate as demanded by the US or Japan in the 1980s.
- China's PM has already warned of the economic effects of an excessive appreciation of the RMB.
- China also owns too much US Treasuries to undertake such a strengthening.





Undervalued Asian currencies
fuelling property asset bubbles as
there is pressure on them to
appreciate their currencies
or raise interest rates

Article in Straits Times today shows the trend of inflation and interest rates in Asia

Central banks in Asia are under pressure to tighten monetary policy to curb inflation, but not all have made moves yet.

	CPI Inflation (Sept)	Latest move by central bank	Date of last meeting
China	3.6%	Raised one year lending rate for first time in 3 years to 5.56%	Oct 19
India	8.6% ¹	Held at 6%. Raised interest rates 5 times since March.	Oct 21
Thailand	3%	Kept interest rates at 1.75% after hiking twice since July	Oct 20
Singapore	3.3%²	Allowed Singdollar to strengthen slightly faster, and widened exchange rate band	Oct 14
South Korea	3.6%	Held interest rates at 2.25% for third straight month	Oct 13
Indonesia	5.8%	Kept interest rates at record low 6.5% for 14th straight month	Oct 5
Australia	3.1% ³	Kept borrowing rates at 4.5%. Was first to raise interest rates among major economies	Oct 5
Taiwan	0.3%	Raised interest rates to 1.5%	Sept 30
Malaysia	2.1%	Held overnight rate at 2.75% after three consecutive rate hikes	Sept 2

NOTE: 1 Wholesale price inflation 2 September figures out next week 3 CPI is reported per quarter. September figures out next week

ST GRAPHICS

Hong Kong imposes property curbs

- 4 May 2010

HK's URA introduces new measures that include a restriction on corporate purchases of flats to 10 percent of total sales and a maximum limit of two units per buyer during the sale period

- 25 Oct 2010

Loans on properties valued at 20 million Hong Kong dollars (\$2.6 million) or more would be capped at 60 percent, down from 70 percent. For cheaper properties the maximum loan would remain 70 percent but would be capped at 12 million Hong Kong dollars.

Last week Henderson Land Development said it sold a duplex for a world record of 88,000 Hong Kong dollars per square foot.



Australia introduces curbs on foreign property buyers

- 24 April 2010

Australia clamped down on foreigners buying property after complaints that a rapid influx of Asian money had helped make its housing among the most expensive in the world.

The government reimposed tough rules relaxed in 2008 that say temporary residents need permission to buy homes and must sell when they leave, while foreigners investing from abroad can only buy new properties.

The rules are backed by stiff new penalties including compulsory sell orders, as well as expanded monitoring and a crackdown on real estate agents who help foreigners flout the rules.



Singapore imposes property curbs in late August 2010



Investment strategy for rest of 2010 into 2011



Ride the liquidity BULL into Q1-2011.....
Asian stock markets still cheap in PER
terms

Watch out for trade war related macro
changes such as currency appreciation
or import tariffs that may impact
margins and earnings

Most major stock markets are trading toward the low end of historic PER range

Index	Historic PER range	Current PER	Prospective PER	Earnings growth
Dow	10 to 25	13.6	13.2	3.0%
Shanghai Composite	12 to 60	19.8	16.9	17.2%
Hang Seng Index	7 to 23	14.8	14.9	-0.7%
STI Index	7 to 25	12.9	15.6	-17.3%

Summary

- EU Debt crisis concerns have abated.....but problems from cuts in Fiscal spending likely to surface in 2011
- Markets have rallied since August on expectation of QE2 which I expect will last till Q1-2011.....leading to a spike in stocks, commodities...this is probably half way through
- High unemployment in the US and huge trade deficits may result in currency or trade wars with the passing of the Currency Manipulation Bill
- Stock markets have gained 10-15% in Q3 and while not expensive on current forecasts may be vulnerable to rising interest rates in Asia and slower corporate earnings growth in 2011.

Which stocks contributed to the Q3-2010 rally in the STI Index ?

Index/Stocks	30-Aug	22-Oct	Change	% chng	Contribution to STI	% contribution
STI Index	2957.06	3173.6	216.5	7.3%		
DBS	13.86	14.50	0.64	4.6%	12.2	5.6%
OCBC	8.74	9.06	0.32	3.7%	8.8	4.1%
UOB	18.88	18.44	-0.44	-2.3%	-5.7	-2.6%
SGX	7.48	9.54	2.06	27.5%	24.6	11.3%
Genting	1.66	2.22	0.56	33.7%	37.8	17.5%
Jardine M	44.00	44.90	0.90	2.0%	3.4	1.6%
Jardine S	24.84	26.00	1.16	5%	3.7	1.7%
Jardine C&C	32.60	38.96	6.36	20%	10.2	4.7%
City Dev	11.46	13.14	1.68	15%	12.8	5.9%
Sub total					107.8	

My strategy.....

- Stay fully invested and ride the liquidity BULL into Q1/Q2 2011
- 50% in laggard Blue Chips such as banks which under-performed the Q3 rally (we prefer OCBC and UOB) and Telcos such as Sing Tel and Starhub are on undemanding PERs and offer decent dividend yields of 5-7%
- Property sector – sentiment likely to be neutral to negative in the wake of Government policy to cool prices. But property companies now have strong balance sheets – and are under no pressure to cut prices even those who have more expensive landbanks. Preference for the mid to high end not mass market – Allgreen, Wing Tai and Sing Holdings.
- Technology stocks still offer value and should have a good Q3-2010 but watch guidance closely especially into Q4-2010 and Q1-2011 as inventory restocking is now complete and we may see some slowdown in demand plus pressure on margins from weakness in US\$.....obvious weakness now in harddisk
- Construction stocks remain undervalued with many companies trading below NTA and some even below cash levels....worth a look for medium term investors if they increase their dividend payout



Thank You

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