September 16, 2010

TRIM Macro Thoughts

Pleasant Surprise

Summary:

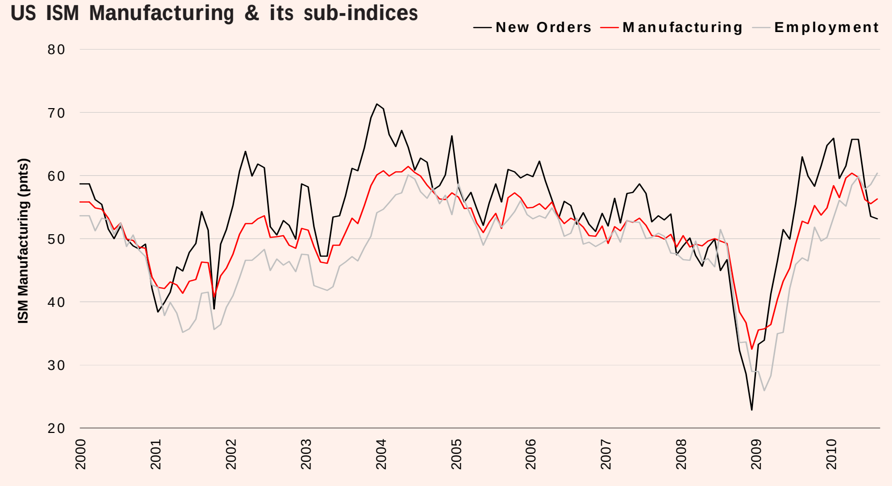
- US Celebrated Data
- CN Decent Data
- ID Inflation and policy response

October will be the important month, as Sept & 3Q10 data should decide the fate of the global economy going into 2011. Data so far seems to concur with our view that growth will slow, and that the world will avoid a double dip recession. Easy credit is the key to sustaining Indonesia's current growth model credit driven consumption. Bank Indonesia has responded well to the rising risks of inflation. Buy on Weakness for LT Indonesian Asset Investors.

US Celebrated Data

The fight between bulls and bears continues. S&P500 is back on a positive trend since 25th Aug, up 8.2% to 1125 yesterday on good data flow relative to a low expectation. Worthy of discussions here is the change in private payroll and retail sales; however let's take a look at ISM numbers first.

US ISM manufacturing surprised almost everybody, strengthening to 56.3 in Aug from 55.5 in Jul, way above 52.8 weakening expected. The figure sparked this 8.2% S&P500 rally. However, looking deeper into the figure reveals more. ISM manufacturing new orders index has declined from May peak at 65.7 to 53.1 in Aug. This historically has been a good leading indicator for the ISM manufacturing index. The only 1 sub-indicator that is still showing signs of uptrend and it is the employment index.



Source Bloomberg

This lagging indicator explains why the bull has a case in terms of employment outlook, as highlighted by the euphoria in when Aug non-farm payroll numbers of -54k, which beat expectations of -105k. Excluding census hiring distortions, private payrolls grew 67k, versus expectation of 40k, slower than last months reading of 107k. The bet here is still for activities in the US to slow. The bears argue that many stimulus programmes available in the 1H10 such as FED bond purchase, cash for clunkers and first time home purchase tax credit will stop in the 2H10, on top of an already disappointingly low 2Q10 GDP growth of 1.6%.

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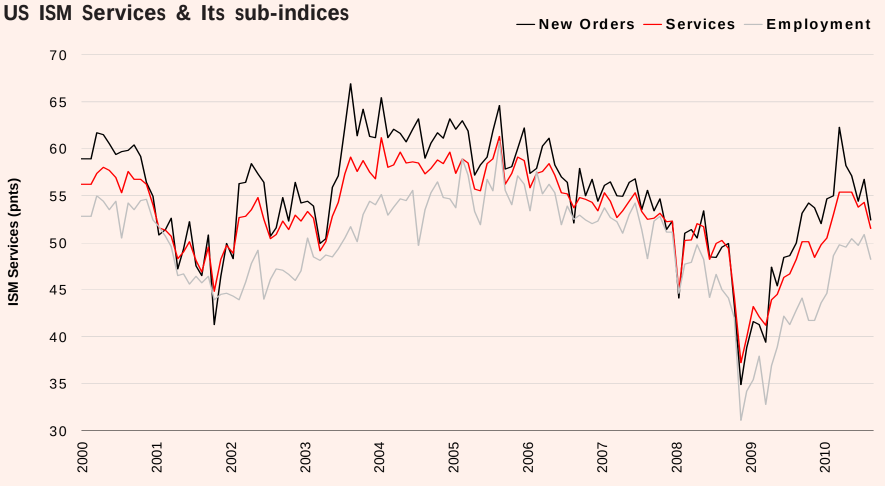
What the market ignored, which in my opinion is more important than ISM Manufacturing is ISM Services which represents more than 90% of the US economy. As such, ISM services slowed further in Aug to 51.5 from 54.3 in Jul, a level considerably below expectations of 53.2. New orders index declined to 52.4 in Aug, from its recovery high of 62.3 back in Mar'10. Employment in the services ISM show even more bearish reading, only showing very weak employment expectations (above 50 reading) twice in May and Jul in 2010, since the reading collapse to its series low of 31.1 in Nov'08. The reading has pointed to negative growth since Dec'07 and is now showing signs of peaking again despite remaining in negative growth territory.

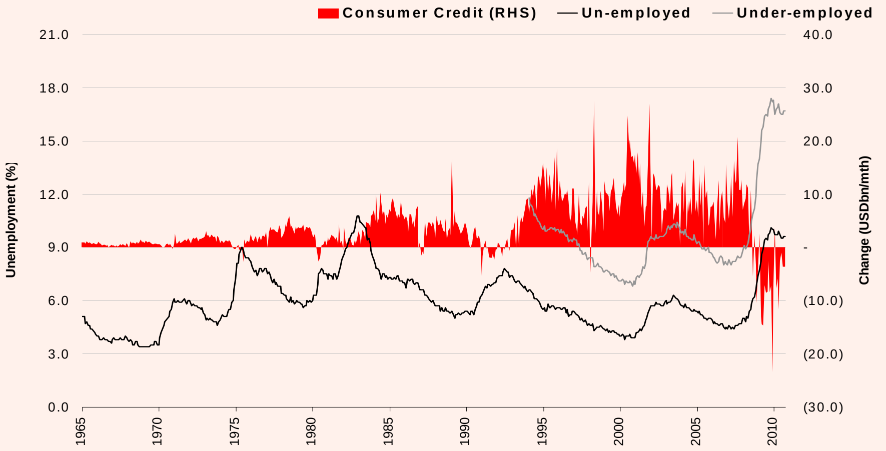
US ISM Services & Its sub-indices



Source Bloomberg

The other data point that the market celebrates is the Aug retail sales. Ex auto & gas retail sales jumped from -0.1% in Jul to 0.5% growth in Aug. The point about consumers is that consumers continue to deleveraging, paying off more debt than they borrow, as unemployment (as well as underemployment readings) continue to disappoint the real sector. The only other time in recent history when unemployment rose >9.0% was back in 1982 during the S&L crisis. Unemployment rose above 9.0% and stayed there for 15 months before steadily decline, supported by a US economic recovery that reached as high as 4.5% in 1983 and 7.2% in 1984. Unemployment has hovered 9.0% for 15 months already coming this Sept, however unemployment remains stubborn at 9.6% and is expected to remain so until 2011 in a bearish case scenario. The biggest question remains if consumption can pick up structurally in the US, despite the recent retail sales numbers. As such, inline with the stubborn employment outlook, US consumers has been consistently paying their debt since 24 months ago, when the sub-prime crisis first appear between mid 2007 - early 2008. Whether this is a structural shift or not is yet to be told, and is the key to our future expectations in growth.

US unemployment & consumer debt changes



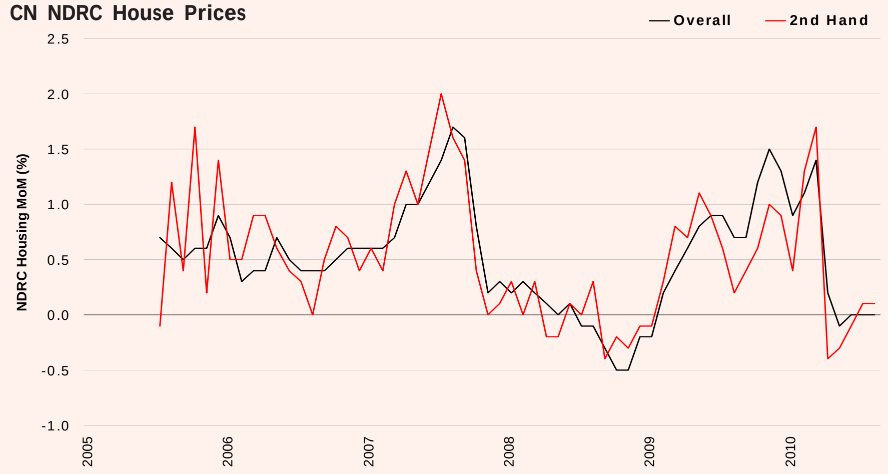
Source Bloomberg

CN Decent Data

Market recently celebrated CN success in sustaining clean and stable data. Bank lending remains at a stimulated RMB500bn/month in Aug. Imports which "collapsed" to a 22.7% YoY recovered back to 34.4% YoY in Aug, suggesting Chinese will continue to sustain its support for global growth through imports demand. What the market really celebrated was its retail sales numbers which improved further to currently at 18.4% YoY from its crisis "low" of 11.6% YoY. Such growth suggests consumption is doubling every 4 years, a number not to joke around because the base includes >1.3bn people, of which 57% are still rural population.

Source Bloomberg

One tail that bugs me albeit minor is CN's National Development and Reform Commission (NDRC) house prices. As such, MoM price growth of Chinese new and 2nd hand homes, compiled by NDRC show signs that the housing sector is cooling. This is exactly what the policies in China aim to achieve. Although the path is right, tightening bias should remain, as housing prices fail to fall at a speed and size expected by that of market and the government. As such, 15% to 20% decline is still the baseline scenario most analysts are looking at, and at this consolidation rate, tight policy may remain well into 4Q10 and perhaps early 1Q11. Nevertheless, anymore aggressive policy tightening should be sidelined, especially in view of a weakening macro picture. As such, maintaining 8.0% real GDP growth for CN as a worst case scenario investment assumption still seems highly visible at this moment.



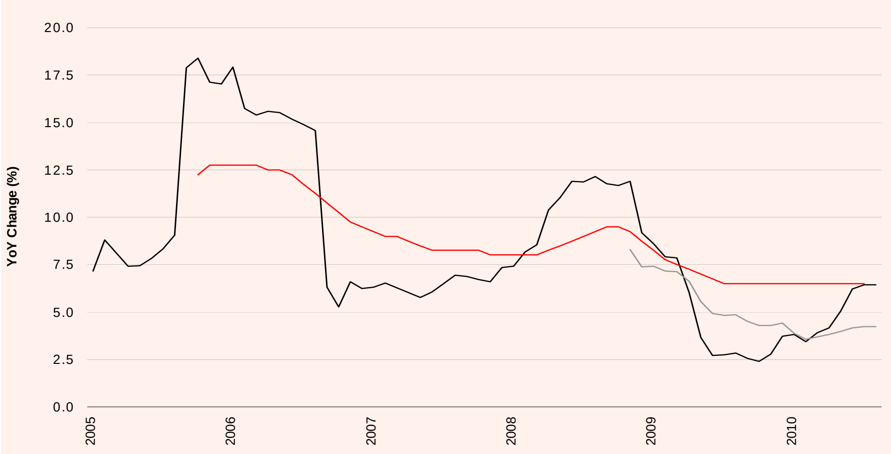
Source Bloomberg

ID Inflation and policy response

The Indonesian policy response to the rising inflationary risks is ideal in my view. As such, Bank Indonesia announced that banks must raise their cash reserve requirement by 300bps from 5.0% to 8.0%. The second rule, regarding bank LDR outside the range of 78% to 100%, will require banks top up 0.1% reserve for every 1.0% short from 78% LDR and 0.2% reserve for every 1% excess of 100% LDR.

The last inflation number has poised some concerns on my side. MoM reading came in at 0.76% MoM, lower than prior month at 1.57% and expectations of 1.00%. The worrying bit is the increasing core inflation, which rose 4.53% in Aug, higher than 4.15% in July and 4.26% expected. This paints more than a food / soft commodity supply side issue that everybody thinks its driving inflation in Indonesia. Unexpected trade deficit in Jul also reinforces this concern that demand side is much stronger than many anticipated.

ID Inflation



Source Bloomberg

However, BI's policy response is expected to address the following concerns, which at the same time moderate longer term risks that may arise from Indonesia's current growth model of credit driven consumption. (1) Raising cash reserve requirements effectively raises cost of funds for banks by 25bps to 50bps, depending on previous asset use and yields from the various banks. This will force banks to be at least more careful with lending, assuming they are not going to pass on the increased costs to borrowers due to the lower net interest margin / profitability from future lending. These should somewhat address demand side pressures in the economy, while not risking increased cost of lending directly if BI has chose to move its BI reference rates instead. (2) The punishing banks with LDR ratios outside the 78% to 100% ranges will force banks with lower LDR to be more effective in lending and smooth the money intermediation and multiplication within the economy; and banks with higher LDR to de-risk and grow loans while not risking their respective balance sheets.

ID Banks Matrix

		Mkt Cap (Rptr)	2Q10 LDR (%)	Asset (Rptr)
BBCA	BANK CENTRAL ASIA PT	156.6	52.69	298.6
BMRI	BANK MANDIRI TBK	139.5	67.63	402.1
BBRI	BANK RAKYAT INDONESIA	132.0	87.24	323.8
BBNI	BANK NEGARA INDONESIA PT	58.8	68.92	225.5
BDMN	BANK DANAMON INDONESIA TBK	48.0	106.03	100.4
BNGA	BANK CIMB NIAGA TBK PT	28.5	86.31	126.3
PNBN	BANK PAN INDONESIA TBK PT	26.5	80.19	88.8
BNII	BANK INTERNASIONAL INDONE PT	17.4	94.28	67.6
BBTN	BANK TABUNGAN NEGARA TBK PT	16.5	116.07	60.9
BNLI**	BANK PERMATA TBK PT	13.3	85.35	62.0
MEGA	BANK MEGA TBK PT	10.7	63.60	40.1
BTPN	BANK TABUNGAN PENSIUNAN NASL	9.6	88.26	28.0
BAEK	PT BANK EKONOMI RAHARJA TBK	8.0	50.46	22.1
NISP	BANK OCBC NISP TBK PT	6.7	77.54	39.1
BBKP	BANK BUKOPIN TBK PT	4.5	77.52	42.9
MAYA	BANK MAYAPADA INTL TBK PT	3.9	85.10	8.5
MCOR	BANK WINDU KENTJANA INTL TBK	0.6	83.79	3.2
AGRO	BANK AGRONIAGA TBK PT	0.6	79.69	3.1
SDRA	BANK HIMPUNAN SAUDARA PT	0.6	97.49	2.9
BEKS**	BANK EKSEKUTIF INTERNASIONAL	0.6	82.45	1.1
BABP	BANK ICB BUMIPUTERA TBK PT	0.6	94.05	7.3
INPC	BANK ARTHA GRAHA INTERNASION	0.5	83.36	15.8
BVIC	BANK VICTORIA INTERNATION PT	0.5	51.00	8.4
BKSW	BANK KESAWAN TBK PT	0.5	77.67	2.4
BBNP	BANK NUSANTARA PARAHYANGAN	0.4	75.87	4.5
BACA	BANK CAPITAL INDONESIA PT	0.4	43.08	4.0
BNBA	BANK BUMI ARTA TBK PT	0.3	64.85	2.2

*** using 1Q10 BS numbers*

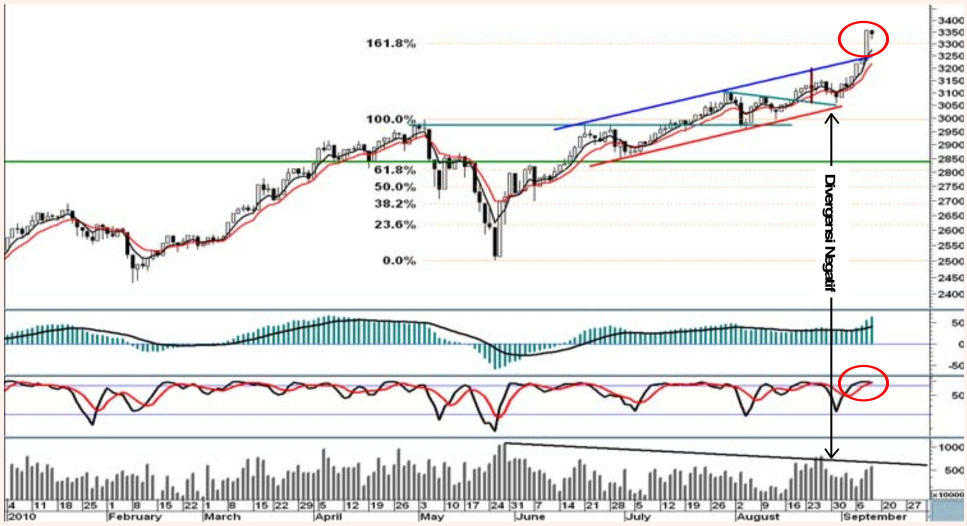
Source: Bloomberg

Market Strategy

ST Foreign funds flows continue to buoy JCI performance in the past weeks, breaking new record highs in the last 2 trading days pre- and post- Lebaran holidays, accumulating 2-day gains of 7.8% vs. 8.6% MTD. Penetration of trend resistance, at the same time clearing 161.8% retracement resistance clearly outlines JCI's momentum, potential of testing its next resistance at 3,380.

Nevertheless, negative divergence formed between higher prices and lower volumes in the weekly chart illustrated clearly shows JCI vulnerability to profit taking, potentially forming a dead-cross at the fast-moving oscillator in overbought areas (95.1). Such a price action will take JCI to test its strong fibbo ratio resistance turn support of 161.8% as well as trend support in the region of 3,250 - 3,300. We recommend ST clients to trade cautiously, and rebalance your portfolio into defensive stocks with strong, visible fundamentals.

JCI - Breaking Resistence



Source : Trim Research

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Happy Investing,

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