

TRIM Macro Thoughts

Hairline Cracks

Summary:

- ❑ **US** Hairline Cracks
- ❑ **EU** Weak Winner
- ❑ **ID** Betting on Decoupling
- ❑ **ID** Infrastructure Complains & Opportunity

The global recovery has met its headwind and is already slowing. One more month of data should be enough to make an accurate judgment of how things will pan out in the intermediate term. Central bankers are already on their toes right now. Investors should too, and be prepared of potential volatility that may create a window of opportunities for LT investors eyeing Indonesian assets. Buy On Weakness.

US Hairline Cracks

Leading indicators are showing signs of slowing end 2Q10. I argued to wait for Jul, Aug & 3Q10 data released by Oct to affirm the global recovery trajectory and adjust expectations accordingly going forward. Data released so far has been showing signs of what I call "hairline cracks", small weaknesses that is appearing in the data so far. However, the best move right now is to bet against the sustainability of the positive outlook for the US economy.

As such, US housing starts, building permits, weekly jobless claims and most importantly Philadelphia Fed Business Outlook Survey all come in weaker than expected. The combination of a weakening housing in the midst of a weakening manufacturing sector in the US will turn out to be a potent mix. Do remember that the manufacturing sector is the sub sector leading US out of recession, largely due to a weak USD. It is the only sector creating jobs in the past months.

US Economic Data

Date Time	Event		Survey	Actual	Prior	Revised
08/17/2010	Housing Starts	JUL	560K	546K	549K	537K
08/17/2010	Housing Starts MOM%	JUL	2.00%	1.70%	-5.00%	-8.70%
08/17/2010	Building Permits	JUL	580K	565K	586K	583K
08/17/2010	Building Permits MOM%	JUL	-0.50%	-3.10%	2.10%	1.60%
08/19/2010	Initial Jobless Claims	14-Agust	478K	500K	484K	488K
08/19/2010	Continuing Claims	07-Agust	4,500K	4,478K	4,452K	4,491K
08/19/2010	Philadelphia Fed.	AUG	7	-7,7	5,1	--
08/24/2010	Existing Home Sales	JUL	4,65M	3,83M	5,37M	5,26M
08/24/2010	Existing Home Sales MoM	JUL	-13.40%	-27.20%	-5.10%	-7.10%
08/25/2010	ABC Consumer Confidence	22-Agust	-46	-44	-45	--
08/25/2010	MBA Mortgage Applications	20-Agust	--	4.90%	13.00%	--
08/25/2010	Durable Goods Orders	JUL	3.00%	0.30%	-1.00%	-0.10%
08/25/2010	Durables Ex Transportation	JUL	0.50%	-3.80%	-0.60%	0.20%
08/25/2010	Cap Goods Orders Nondef Ex Air	JUL	--	-8.00%	0.20%	3.60%
08/25/2010	Cap Goods Ship Nondef Ex Air	JUL	--	-1.50%	0.50%	1.00%
08/25/2010	New Home Sales	JUL	330K	276K	330K	315K
08/25/2010	New Home Sales MoM	JUL	0.00%	-12.40%	23.60%	12.10%
08/25/2010	House Price Index MoM	JUN	0.10%	-0.30%	0.50%	0.40%

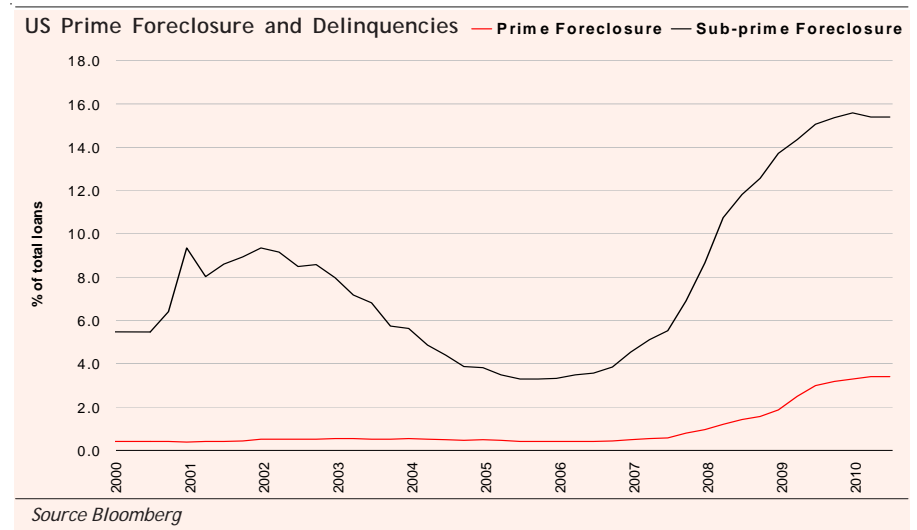
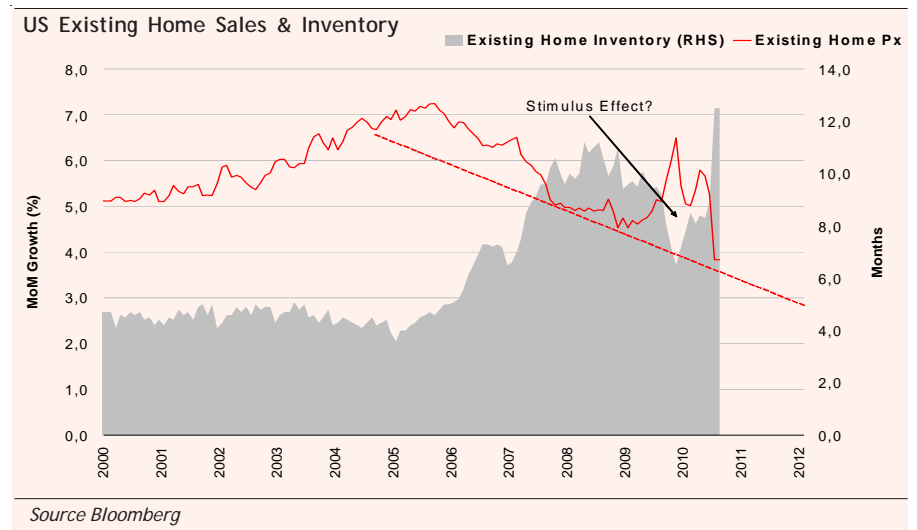
Source: Bloomberg

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The talk on the street now is that weak US housing may come back and haunt the US economy. The more bullish economists are arguing that US housing are already on its knees, and that its contributions have dwindled from 15% of GDP in 2006 to about 5% in 2009. The point here is not GDP contributions the weak housing sector is contributing, but rather the impact to bank's balance sheet if US housing prices were to re-enter a downtrend. We can see that mortgage delinquencies and foreclosures are still going to record levels, even for those prime mortgages.



Along that thought, Bisnis Indonesia reported an interesting article from Bloomberg on 20th Aug. The paper reported that US housing is still weak; as such, FED have asked 4 major banks Citi, Morgan, BoA, and Wells to buy back as much as USD180bn from Fannie Mae and Freddie Mac. Depending on the buy back amount and the recovery ratio, the four banks may suffer as much as USD17bn-USD27bn in losses. Mr. Ben maybe slowly passing back mortgage derivatives in really bad shape back to their respective originators. This is essentially bad news for the banking sector and potentially maybe destabilizing as the move puts banker's capital at risk and hence may shake market's confidence in them.

Fed's recent move may also be proof that both Mr. Obama and Mr. Ben Bernanke are growing desperate that their stimulus commitments are not working. Slowing growth is happening when FED stance is still loose, and that US continue to run mind-boggling budget deficits to sustain the economy. If we take out the immediate impacts of these policy interventions, then the underlying economy should reflect one that is undergoing massive deleveraging. This economic offset provided through the aggressive policy stimulus is not sustainable in the long run, and will provide the reason for investors to be massively short risk assets sometime later in the future.

EU Weak Winner

The only major continent that is seeing relief in the recent months is the Europeans. Germany, the largest EU member grew the fastest in 2Q10 since the 2008 crisis. Obviously, the weak EUR against the USD is helping German exporters in their income. Hence, the ECB most influential council member, Axel Webber, seems to be talking down the EUR. He said that ECB should help banks through end-of-year liquidity tensions, before deciding if such emergency lending measures should be withdrawn in 1Q11. Axel Webber is famous to be hawkish, always very dutiful in fighting inflation. Markets are red on the comment. EURUSD fell almost a full cent to 1.2664 five week low on the comment.



Two conclusions to consider from such market actions are that (1) ECB themselves are still not confident of EU's growth. (2) European banking sector health is also still questionable.

That is why EURUSD, and European stocks traded in the red on early Wednesday trade, when ECB announces that they may be stress testing the banking sector on a regular basis. Olli Rehn, EU commissioner for economic and monetary affairs, said that further discussions with various EU member finance ministers are still needed to decide on the frequency of such stress testing.

The July stress test was widely criticized for being too lenient and unreliable. If the intention is to reinforce transparency and confidence in the system, then the "marketing gimmick" should stop. Only government bonds in bank's trading books are exposed to capital loss in July stress test. Only private sector loss is accounted in the event of a sovereign debt crisis, as it is still widely assumed that EU will bail out members in the end of the day. These are just simply unrealistic assumptions.

Going forward, a re-weakening of EUR is worth watching. EUR has been a good risk proxy for 2010. The market is already taking the cue from weaker EUR in the past weeks to reignite concerns of the EU economy due to its austerity programmes. S&P recent downgrade of Ireland long-term debt outlook from AA (flat) to AA- is not helping at all.

ID Betting on Decoupling

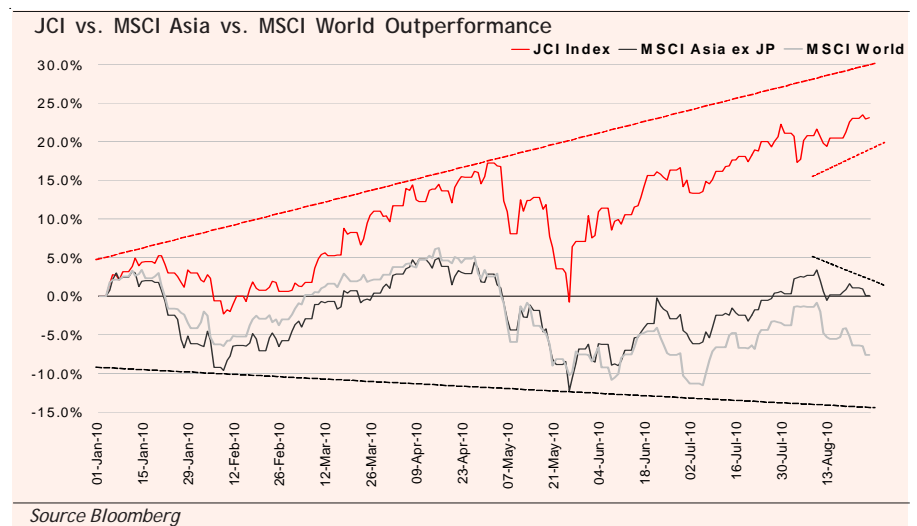
The thought here is that the only way to justify our persistent outperformance relative to regional indices is the acknowledgement that Indonesia can decouple from the world. Fundamentally, this is justifiable. While everyone is busy worrying about disinflation turning into deflation, Indonesia is fighting food and season induced inflation. Our core inflation is also at a "healthy" 4.5%. Government in US, EU, JP and China are guiding lower GDP growth next year, while Indonesia is guiding higher GDP.

Regional vs. ID GDP Growth					
GDP (%)	2008	2009	2010	2011	2012
Developed Asia					
Hong Kong	2.2	-0.2	2.9	1.5	1.4
Singapore	1.9	1.4	7.8	2.2	--
South Korea	2.3	2.8	3.0	1.8	1.8
Taiwan	0.7	0.7	--	--	--
ASEAN					
Thailand	2.5	0.4	4.4	1.7	1.9
Vietnam	6.2	7.9	--	--	--
Malaysia	4.7	0.9	3.8	2.4	2.2
Philippines	3.9	3.6	2.3	2.0	1.9
China	9.6	11.7	7.0	6.1	--
India	7.5	9.3	--	--	--
Indonesia	6.3	6.0	6.0	6.3	6.5

Source: Bloomberg

The bet on this decoupling is perhaps the big call to make for investors going forward. The Financial Crisis 2008, and recent issue of a global double dip will continue to contrast the great shape Indonesia is in. We will continue to grow, no matter what happens to global growth, thanks to our large domestic market dependence, low consumer and government leverage, healthy banking and private sector. One big catalyst looms in the corner to fully detach Indonesia from the global drag, and that is our very own, long delayed public sector fix asset investment cycle.

As such under such scenario, our relative premium should continue to grow. Our growing economic momentum will result in a higher Index EPS at the end of every year. As such, it is not puzzling that there are already analysts betting on Index reaching 4000 by end 2011 and 4800 by end 2012. Interesting to note, this decoupling can already be observed in JCI outperformance against regional peers underperformance in the absence of major macro or micro news in Indonesia, in both the past week and YTD performance.



One huge catalyst to support this macro story is the pool of investment money waiting to enter Indonesia when we attain our investment grade in the next 1 to 2 years. As such, one criterion that is hindering our goal is the accumulation of reserves. But personally, a bigger story that investors should be more focused on is the potential successful infrastructure story can unlock. This has been discussed extensively in previous thoughts, and we will continue to focus on this other bigger fundamental catalyst.

Investment Grade Criteria

	Actual	Investment Grade Criteria
Debt of GDP (%)	26%	< 50.0%
Budget Deficit (%)	2.10%	< 3.0%
Reserves	US\$80bn	>USD100bn
GDP Growth (%)	6.50%	

Source: Investor Daily 2010 08 23

ID Infrastructure Complains & Opportunity

Investors Daily wrote in a report on 23rd Aug 2010, that there is as much as Rp27tr or 0.3% of 2010est GDP of private sector investments that has been held up because of the undeveloped infrastructure in Indonesia.

Industries and Its Complains

Sector	Remarks
Electronics	road & port congestion
CPO secondary & tertiary industries	minimal facilities to facilitate operations
Textile, Sugar	limited choice of suitable space for expansion
F&B	road congestion
Ceramics	Gas shortage
Steel	minimal facilities to facilitate operations

Source: Investor Daily 2010 08 23

Market Strategy

ST "Hot money" euphoria has driven JCI index to trade along its uptrend channel and sustained its momentum in breaking new highs in the last 3 consecutive trading days. As such, JCI index returned 2.0% in the last three days, versus YTD returns of 22.9%. In view of a potential symmetrical triangle, we see room for JCI index to continue its uptrend, at least testing 3,198 - 3,200 levels.

Nevertheless, ST oscillator is nearing its 4th Jan peak (99.2) on 23rd Aug at 95.3. This has been a good early indicator of an intermediate term Index weakness is two other occurrences this year namely 23rd Apr (97.9) and 22nd Jul (94.5). JCI subsequently peaked on 4th May and 30th Jul respectively. We continue call ST traders to sell on strength, locking in gains and preparing for potential JCI weakness in the coming month.



LT The global recovery has met its headwind and is already slowing. One more month of data should be enough to make an accurate judgment of how things will pan out in the intermediate term. Central bankers are already on their toes right now. Investors should too, and be prepared of potential volatility that may create a window of opportunities for LT investors eyeing Indonesian assets. Buy On Weakness.

Happy Investing,

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