

Vantage Point

A WEEKLY PUBLICATION FROM THE FUND MANAGERS AND ANALYSTS OF PHILEQUITY MANAGEMENT, INC.

MARKET OUTLOOK: CAUTIOUS

SECTOR PICKS: CYCLICAL STOCKS WITH EFFECTIVE RECOVERY PLANS AND FORTRESS BALANCE SHEETS, STOCKS WITH LOW VALUATIONS, COMPANIES WITH LESS DOMESTIC EXPOSURE

TECHNICALS: SUPPORT AT 6500 FOLLOWED BY 6200, RESISTANCE AT 6800 FOLLOWED BY 7000

With US inflation hitting its highest since 1981, it seems the signs of peaking were false. The May CPI print of 8.6% indicates what other regions are experiencing - that inflation is still heading higher and will likely plateau instead of peak. Unfortunately, even if it does peak or plateau, it will be doing so at a very high level that is already causing demand destruction. This has significant implications for the economic cycle we are in now.

With oil trading within 10% of the highs it set in March, we are seeing an unprecedented rise in fuel prices, which feeds into other commodities. This will likely prompt central banks to hike rates even more decisively - with a corresponding negative impact on growth.

Another consequence would be the weakening of currencies against the euro and dollar. With the Japanese yen going parabolic, some economists have raised warning bells. Last week, economist Jim O'Neil warned of a crisis in Asia if the yen depreciates beyond 150 against the dollar. "If the yen keeps weakening, China will see this as an unfair competitive advantage, so the parallels to the Asian financial crisis is perfectly obvious," said O'Neill who was a former Chief Strategist at Goldman Sachs and Chairman of Goldman Sachs Asset Management.

Currently, the yen is down 17% YTD and is trading around 135/\$. Even if the peso can remain relatively strong versus other Asian currencies, it is very difficult to buck the trend if all its neighbors are depreciating. This will have negative consequences for equities. We revert back to our cautious stance.

Philippine Stock Exchange Index (PSEi) 1-year chart



TRADING STRATEGY



With oil trading back near its highs, it is not a surprise that both the US and Europe reported above forecast inflation. The resulting plunge in global equities and a depreciating peso will weigh on the stock market. We shift back to our cautious stance as it seems markets are not yet ready to move higher.