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Mart bogged down by fears of slowing US economy

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LAST week, the KLSE was the worst amongst all Asian bourses. The benchmark Kuala Lumpur Stock Exchange Composite Index (KLCI) fell 21.79 points or 3.26 per cent to close at 647.48. The Emas Index was next in line with a fall of 4.66 points or 3.03 per cent to close at 149.15.

The Dow's technical rebound of 294 points to 9,799 last Thursday did not help at all. Instead our bourse continued to be bogged down by fears of a slowing US economy that will likely affect our own economy.

Investors remained sidelined in reaction to these fears - and the low average daily volume of 75 million shares done reflects the current bearish mood.

Prime Minister Datuk Seri Dr Mahathir Mohamad's announcement of a stimulus plan to pump-prime the Malaysian economy to cushion any impact of a US economic slowdown had little positive effect on the local bourse.

Some of the Government's measures include an additional RM3 billion in fiscal spending to boost the construction sector. He also touched on steps to boost local consumption by reducing employees' contribution to the Employees' Provident Fund (EPF) from 11 per cent to 9 per cent and a relaxation of rules on foreign equity and property ownership to redress the current property overhang, but unfortunately, these measures were not seen by investors to be sufficient to change the market's perception to lift it out of the doldrums.

Perhaps, a lowering of Bank Negara's intervention rate and a re-pegging of the ringgit against the US dollar might have done the trick to jump-start a rebound - but it is anybody's guess how far the market would have gone even if these two measures were announced.

Very clearly, the "tide" of the market is still receding. Even if a whole string of goodies were announced, the most we can see is a knee-jerk reaction from the market - only to fall back again.

This "tide" is something that Malaysia alone cannot control. I am referring to the flow of foreign funds. It is rather unfortunate that foreign funds look at Indonesia and Thailand's economy and politics to judge Malaysia.

We all know it is not right to compare apples and oranges. Compared with Indonesia and Thailand, we have done much since 1998 in restructuring our banks, insurance and public companies through Danaharta and Danamodal. Their success in turning around sick and virtually "dead" companies are now emulated by some Asian countries.

Meanwhile, the Securities Commission and the KLSE have also worked hard on improving Malaysia's corporate governance and transparency, including stricter rules on corporate reporting, disclosures, remisiers and investor education and so on.

Malaysia did all these without the help of the International Monetary Fund - yet these factors are overlooked by foreign funds principally because they see Malaysia as part of South-East Asia or even Asia.

One day, the "tide" will turn in Asia's favour. Sooner or later, US and European funds will start flowing in again because they are now awakening to the reality that the US stock market cannot go on rising forever.

Perhaps, the Fed's decision on March 20, of not cutting interest rates by 75 basis points but instead by only 50 basis points, has unwittingly triggered what could well be the beginning of a big bear market for the US.

The Dow is now at its two-year lows. The Nasdaq's parabolic rise from 250 points in Oct 1984 to a high of over 5,000 by March 2000 is now a pathetic shadow of itself, having suffered by more than a 62 per cent plunge within just one year - when it took Nasdaq 16 years to climb that mountain to 5,000!

Having fallen so much, further falls will likely be limited on the Nasdaq. But the Dow is a different story. It is just about to roll over the cliff. The Dow has formed a "diamond" reversal pattern and has broken through major supports. This rare "diamond formation" spells a market reversal. Charts are a reflection of the market's sentiment and it has turned bearish.

My guess is, it may be too late even for Federal Reserve Chairman Alan Greenspan to keep the US\$10 trillion (US\$1 = RM3.80) US economy from going bust because on March 20, he could well have unknowingly turned the US stock "tide" around.

"Six months ago, many on Wall Street took it on faith that Greenspan could pull off (a bust) with ease. But as the US economy's course has wavered, so has the trust of some of his followers. Criticism of Greenspan, all but non-existent while Americans are basking in the stocks bull-run and blockbuster economic growth of the late 1990s, is starting to crop up on newspaper editorial pages", according to a foreign news agency report.

Federal Reserve officials defended that if the US economy continues to remain weak, its central bank will "stand ready" to cut interest rates further. Talks are of another 100 basis points rate cut.

Even so, my view is, the FOMC decision on March 20 has inflicted great psychological damage to the market's confidence. As a result, the herd is now talking about "selling" rather than "buying".

Because of this loss in confidence, a 100 basis point cut, if any, will most probably only result in a "dead-cat-bounce" after which I expect the Dow to fall further. Dow rose in a similar parabolic fashion with the Nasdaq, from 600 points in 1974 to over 11,000 by the year 2000.

A 38 per cent correction will peg the Dow at 7,500, its 1998 support level. It looks like the market is going this way. It is hard to stop the freight train - of mass psychology.

Mass psychology works both ways. Remember when the US market was on a super bull-run in 1998 from the 8,000 leve? Greenspan used the phrase "irrational exuberance" to warn investors about getting too gung-ho on stocks. His words fell on deaf ears. The Dow went on for two years to 11,000 while Nasdaq rose from 1,500 to 5,000 in the same period. This is the hallmark of a runaway bullish mass psychology. Investors throw caution to the wind.

Now I fear the US investor is behaving differently from 1998. Let not the crowds' fears turn into a mass of negativity and even hysteria. If so, the US stock market may well be manifesting "irrational exuberance" - but of a negative kind, regardless of the amount of damage-control the Fed may introduce. In the end, I believe it is the power of the herd that moves markets. Once this market confidence evaporates, there is very little that any government can do to turn it around - except time.

If the US stock markets do continue to fall, I believe funds now in America will begin to look for new frontiers to invest their money. Asia-Pacific countries have a lot to offer to the institutional investor. They have great growth prospects but the choice of country will determine the extent of the fund managers' returns.

In this respect I believe Malaysia is still one of the better countries in Asia for foreign funds to invest their money, for in spite of our imperfections, we have come a long way since the financial crisis of 1998

in redressing many of our mistakes and weaknesses.
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