



AMG Market Commentary

September 2008

Rough Weather, Rough Market

Hong Kong had hoisted typhoon signal #9 in August. The last time was about 11 years ago. The weather was really rough, and same was the equity market. August, supposed to be a time when the sun is shining and people enjoying the summer holidays, but instead, it was stormy and gloomy. We are talking about the equity market here. We are currently encountering, probably the most difficult investing environment since 1998, when the Russian defaulted their liabilities.

We had no clear market direction. Investors are being caught by the discrepancy between market fundamentals and technical. Earnings for S&P 500 companies varies, but then the index actually performed relatively better than the SSE, which the financials reporting strong growth.

On a global level, value stocks (clear defensive plays); have underperformed growth stocks (clear aggressive plays).

We believe that most people have underestimated eagerness of governments to ignore moral hazard and defend markets at all costs, which will only bring in more uncertainties over the next few months.

US: Negative

US stocks have rebounded despite a stream of bearish news, including a weakening economy. Besides financial shares, stocks tied to consumer spending, such as auto makers and retailers, had their biggest monthly gain in August since 2003. (1)

Small caps reflecting by the Russell 2000 was outperforming than the DJIA.

Europe: Negative

The weak GDP figures published on August 14th have shown that the economy is expected to continue to shrink. The main reason is due to the weaker demand in the Euro zone's main foreign markets have at last started to hurt the economy. The Euro area had leant heavily on strong export growth to keep it moving. Upward wage pressure is also expected to push up unemployment.



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Asia: Neutral

MSCI Asia Pacific ex Japan, the fastest growing region in the world, is down -27.9% year to date, while the US, the source of problems with all the Mortgage-backed securities and financial institution meltdowns, is down about -10%. (2)

Japan: Neutral

Revised national accounts data show that Japan's economy grew more strongly in the first quarter of 2008 than the government initially thought. A censure motion against Mr. Fukuda has been passed in the House of Councillors, the upper house, and the first of its kind against a prime minister in Japanese history, but Mr. Fukuda was able to brush it off with relative ease. (Mr. Fukuda resigned as the Prime Minister of Japan in the evening of September 1st, 2008) (3)

Greater China: Positive

China's SSE Composite Index rebounded by a headline-grabbing 7.6 percent to 2522 on August 20th, reversing slightly more than half of the 14.9 percent plunge that the main index had suffered since the Olympics opening ceremony on August 8th. The stock surge brought with it a glimmer of hope that the worse might be over for what has been an epic collapse of China's stock prices over the past 10 months as measured by the roughly 60 percent decline in the SSE Composite Index from the intraday high of 6124 hit on October 16th, 2007. (4)

Hong Kong: Neutral

With the announcing of strong earnings from H shares, Hong Kong Market still suffered selling pressure as influenced by the A shares and also the US market. Hong Kong's daily trading also decreased to 2005/06 level. China mobile encountered heavy trading pressure and have gone back to the \$80's range. The post Olympics fear had caused the market to suffer losses especially after the market couldn't see how the Chinese government would bring in any new policies to stimulate capital market.

Emerging Markets: Negative to Neutral

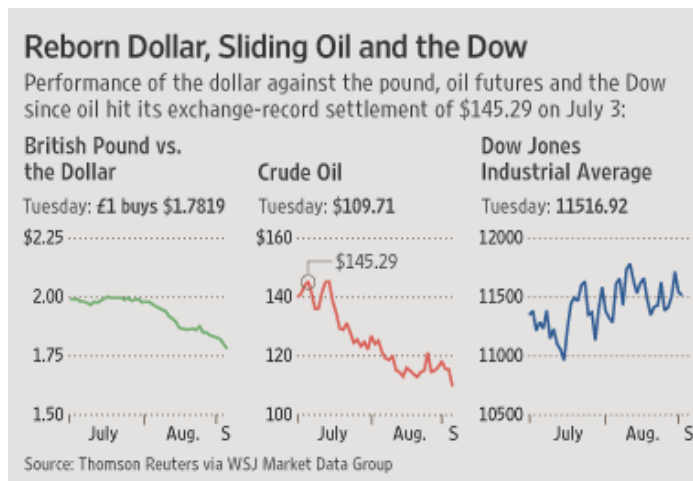
Rising tension with the West could damage foreign investor sentiment towards Russia, Fitch rates Russia as BBB+ with a stable outlook. The oil and gas rich country's vast foreign reserves made it less vulnerable, but that it could still suffer consequences from the fallout of its conflict with Georgia, according to the spoke person from the agency. (8) Latin America suffered capital outflow as the rising US dollar and falling global demand on commodities have caused capital to flow back to home.

India: Positive

The lowering of oil prices has helped to ease the pressure. The Sensex started August with strong performance, but then the performance retreated after the mid month when profit taking occurred.

Commodities: Neutral

Even as sentiment has turned negative on commodities, worries about the financial system have abated, despite continued problems on Wall Street and in the housing market. Oil is down nearly 25% since it peaked in intraday trading on July 11th, but US financial stocks have rebounded more than 16% in the same period. The dollar has strengthened, most dramatically against the British pound. (5) Many commodities' prices have slid in recent months, and the most recent to show weakness is steel. It's down as much as 30% in some markets as suppliers cut prices following a first-half surge to a June record. Signs shown that demands are slowing on a global basis. The recent decline in commodities has been



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driven by confirmed weakening global demand, it might not necessarily be good news for stocks or economies. But lower commodity prices could bring relief to businesses and consumers either directly or through lower interest rates, which are supported by inflation fears. Lower commodity prices ease those fears somewhat and help with the long term economical growth.

Hedge Funds: Positive

Hedge funds reined in their losses in July, as global financial markets witnessed sharp declines and reversals across major asset classes; the Dow Jones-AIG Commodity Index fell 12%, while the MSCI World Index, after shedding 5.6% intra-month, finished the month down 2.5%. By comparison, the EurekaHedge Hedge Fund Index declined by a relatively modest 2.5%, on the month. (7)

Currencies:

In August, RMB actually fell about 0.2% against the US dollar, a rare reversal of its mostly upward trend since the peg was dropped in July 2005. At the same time, the US dollar has rallied against other major currencies. Because the RMB hasn't moved much against the dollar, those gains also pushed RMB's value upward against other currencies, particularly like Euro and Sterling Pound. The yuan rose 6% against the euro during August, reversing a long decline. It also gained against the Japanese yen and the Korean won. (6)



Things to Look Forward:

How is the financial industry going to respond on future of Fannie Mae and Freddy Mac? What about investors? Earnings of companies are also on the watch list. Changes on unemployment will be the main focus as it is not a number that can be influenced by other factors. For political situations, Thailand, Japan, Korea, Taiwan and Eastern Europe are also critical. Most likely central banks will not adjust any rates this month for major currencies, but pressure is building up for Sterling.

- 1 and 2 from Bloomberg news September 1st, 2008
- 3 from Economist, August 27th, 2008
- 4 from China: No Time for Complacency, Asia Sentinel, August 28th 2008
- 5 and 6 from WSJ, August 29th, 2008
- 7 from www.eurekaHedge.com
- 8 from Reuters Alert, Reuters, August 26th, 2008

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