

# Emerging Markets Daily

## Asia Edition

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**Yiping Huang**  
Head of Asia Pacific  
Economic & Market Analysis  
(852) 2501-2735  
yiping.huang@citi.com

**Don Hanna**  
Head of Emerging Markets  
Economic & Market Analysis  
(212) 816-7919  
don.hanna@citi.com

See Disclosure Appendix A1 for the  
Analyst Certification and Other  
Disclosures.

## Focus on India

- **India.** Outcome of election in Uttar Pradesh is positive, as it is the state's first unambiguous verdict since 1991, thus making way for political stability (p. 2).

## Highlights

- **China.** The growth of industrial output continues, easing the worry of overcapacity problems (p. 3).
- **Korea.** Current job market conditions appear fairly weak, supporting our view of moderating consumption growth (p. 3).
- **Malaysia.** The relatively benign inflation was largely attributable to the fading effects of fuel price hike and the continuous strengthening of ringgit (p. 3).
- **Taiwan.** We expect bond yields to continue trending up in the near future, but may not reach the same high level last year (p. 4).

## Market Drivers

- **US.** The Leading Indicators Index likely declined in April on softer employment and capital goods orders. The improvement in the national business monitor suggests a slight rebound in the Philly outlook survey.
- **Japan.** Despite weak industrial production, the economy likely advanced solidly in the first quarter.
- **China.** Record high profit growth and excess liquidity in banking sector likely generated more new investment.
- **Hong Kong.** Less robust demand for labor may prevent the jobless rate from falling again.
- **Singapore.** Non-oil domestic exports are expected to recover more decisively in April, growing 5.1% from a year ago.

## Data Calendar

Date	Day	Local Time	Country	Indicator	For	Citi Fcst	Mkt Fcst	Prev.
17-May	Thu	10:00 PM	US	Leading Indicators (%)	Apr	-0.3	0.0	0.1
18-May	Fri	12:00 AM	US	Philly Outlook Survey	May	5.0	3.0	0.2
17-May	Thu	7:50 AM	Japan	Gross Domestic Product (%QoQ sa)	1Q P	0.6	0.7	1.3
17-May	Thu	10:00 AM	China	Fixed Asset Investment (% yoy, YTD)	Apr	25.9	25.0	25.3
17-May	Thu	4:15 PM	Hong Kong	Unemployment Rate (%SA)	Apr	4.3	—	4.3
17-May	Thu	1:00 PM	Singapore	Non-Oil Domestic Exports (% YoY)	Apr	5.1	—	1.6

Source: Bloomberg, CEIC Data Company Limited, Citigroup estimates.

# Focus on India

**Rohini Malkani**  
+91-22- 6631-9876

**Anushka Shah**

## India: Spotlight on the UP Elections

**Uttar Pradesh (UP)<sup>1</sup> elections resulted in an unexpected but significant verdict.**

Over the weekend, Mayawati was sworn in as the Chief Minister of UP, after the Bahujan Samaj Party (BSP) that she leads beat all expectations, garnering a majority of 206 seats in a house of 403 (vs. 97 in 2002). The incumbent Samajwadi Party (SP), led by Mulayam Singh Yadav managed to secure 97 seats (vs. 143 earlier), while the BJP saw its tally drop to 50 (from 88 earlier). The Congress garnered a mere 22 seats (from 24 in the 2002 elections). This is the UP's first unambiguous verdict since 1991. This is positive since it makes way for political stability, as in the past no party has been able to secure a majority, thereby resulting in various coalitions that made governing difficult.

**The poll outcome will likely be positive for the central government.** With the SP supporting the UPA government at the centre from outside, there were talks that a strong result for the SP could have resulted in the formation of a Third Front. We believe that the poll outcome is positive as it removes the possibility of the formation of a Third Front. This bodes well for the UPA government completing its full term till early 2009.

**Several companies are likely to benefit under the new regime.** A key reason behind the success of the BSP (originally a party for the Dalits - the lower caste) was Mayawati's strategy of fielding 86 Brahmins (the upper caste) as well as Muslims. This indicates that caste was no longer an issue and that the main objective was to dethrone the SP. While the BSP has issued no pre-election manifesto on its economic policies, news reports indicate that the new UP government is expected to focus on small and micro enterprises - one of their main vote-banks. Another likely beneficiary is the Taj Expressway Project of the Jaypee Group, which got its approval during Mayawati's previous regime. Though there are no permanent friends or enemies in politics, some of the long-time supporters of the earlier government include the Reliance Dhirubhai Ambani Group, Bajaj Hindustan, the Sahara and Ansal Group, as well as Flexi and HPCL.<sup>2</sup>

### Uttar Pradesh Election Results

	2007	2002
BSP	206	97
SP	97	143
BJP	50	88
Congress	22	24
Others	27	49
<b>Total Seats</b>	<b>402</b>	<b>402</b>

### Structure of the Government at the Centre. Total Elective Seats are 543; 272 seats are required to form a majority

TOTAL UPA= 224+96=320				TOTAL OPPOSITION=221	
Congress + Allies		Outside Support		NDA	
Congress	145	CPI-M	43	BJP	138
RJD	21	CPI	10	BJD	11
DMK	16	Other Left	7	Others	32
NCP	9	Samajwadi Party	36	<b>Total</b>	<b>185</b>
PMK	6			<b>Other Opposition</b>	
TRS	5			BSP	19
Others	22			Others	19
<b>Total</b>	<b>224</b>	<b>Total</b>	<b>96</b>	<b>Total</b>	<b>36</b>

Source: Election Commission

<sup>1</sup> UP is the most populous and fifth largest state in India, with state politics thus having a crucial impact on politics at the centre

<sup>2</sup> For details please see *Times of India*, dated May 12, 2007

## News in Brief

Yiping Huang  
(852) 2501-2735

### China

**The growth of industrial output remained on trend in April, at 17.4%yoy, easing the worries of overcapacity problems.** Those industries that led the growth of industrial outputs are mining and processing of ferrous metal ores (25.8%) and non-metal ores (23.2%), transportation equipment (22.8%), and chemicals (20.3%). Production of vehicles increased 18.6%. **Positive:** This could largely be due to continuously growing exports and gradually improving domestic demand (including both investment and consumption). Industrial productivity could further be boosted alongside the steadily rising world manufacturing center in China. A profit squeeze is unlikely in the near term, even though currency appreciation could accelerate a bit, as expected. *(Minggao Shen)*

### Malaysia

**April CPI rose by 1.5% yoy, in line with the market's and our expectations.** The relatively benign inflation was largely attributable to the fading effects of the fuel price increases in early 2006 and the continuous strengthening of the ringgit, which lowered import costs. Consumer price inflation was on average 2.4% yoy in the first four months of 2007, led by increases in food and beverages, tobacco, fuels and transport. The mild inflation continues to allow the central bank to maintain its accommodative monetary policy to support economic growth. We continue to expect BNM to maintain the OPR at the current 3.5% level until the end of the year. Our year-end CPI forecast remains at 2.3%. *(Leon Hiew)*

### South Korea

**Current job market conditions appear fairly weak,** as the number of jobs rebounded by only 10,000 after two consecutive monthly declines. Unemployment rate rose by 0.1%p, and the pace of employment growth became the lowest since October last year. The employment conditions in sectors like construction, transportation, telecom and business service are relatively strong while the ones like agriculture, manufacturing, wholesale and retail, and education

service are weak. On job status breakdown, we watched relatively strong growth in non-salary family workers and daily workers, which may not be a favorable change.

Current softness in job market seems to support our view that consumption would moderate or "normalized" from the annualized 5.5% growth in 1Q07. *(Suktae Oh)*

**Corporate profit margin declined in 2006 again, to 5.2% from 5.9% in 2005, due to continued won appreciation and the worsening of terms of trade.**

The decline in profit margin was seen for both export-oriented (4.9%) and domestic market-oriented firms (5.7%), which suggests that the impact of higher energy and raw material prices was quite significant. We watched narrowing of profit margins in key sectors like electronics, metals and chemicals, while the auto sector preserved its margin despite the widely-known concerns on a strong Korean won. Other transportation equipment (mainly shipbuilding) showed the most pronounced margin expansion, though the level of operating margin itself (3.6% in 2006) does not look impressive.

We expect that corporate profit margin will stabilize in 2007 after two years of decline thanks to stable currency and the margin expansion of transportation equipments sector (auto and shipbuilding), though sustained weakness in high-tech sector (at least until mid-year) remains a key negative factor. *(Suktae Oh)*

**Weakness in large store sales suggests corrections in consumption.** Large store sales in April, at -5.5% yoy, showed a significant weakness, which raises the chance of correction in retail sales or consumption spending after the strength in 1Q. We expect that total consumption goods sales will also be weak in April, considering the softness in auto sales and large store sales. *(Suktae Oh)*

**Terms of trade rebounded for the second consecutive quarter in 1Q07, mainly thanks to the decline in oil prices.** We expect that terms of trade will decline again in 2Q, as high-tech export prices

(especially the memory chips) continue to fall while crude oil prices have rebounded. *(Suktae Oh)*

## Taiwan

**We expect bond yields to continue trending up in the near future, but they may not reach the same high level last year.** Benchmark 10-Year government bond yields rebounded sharply on news that the central bank (CBC) will auction another NT\$50bn 364-day negotiable certificate of deposit (NCDs) on May 21. Last time when the CBC auctioned the long-dated NCD twice in a month was in April last year, triggering a rebound in the benchmark 10-year government yields from 1.80% to 2.37% one month later. This year, the central bank has again resorted to the auction of 364-day NCDs to boost bond yields, besides an audit check on major bond traders and asking the post office not to buy government bonds.

On-the-run 10-year bond yields closed at 2.1048%, up 4.73bp from previous trading closing. In April, the CBC surprised the markets by offering 364-day NCDs at a fixed rate of 1.88%, a day after the auction of same tenure NCD resulted in 1.901%. On May 8, the central bank used the same tactics by offering 364-day NCDs at a fixed rate of 1.90%, after the 1.94% of auction result from the previous day. But with the passage of the bill to lift insurance companies' overseas investment cap from current 35% to 45%, bond markets finally felt that the bearish sentiment has run its course and staged a comeback rally, which saw benchmark 10-year bond yields drop to 2.046% on May 11. The higher-than-expected auction result of 2-year government at 1.9320% did not have a significant impact on bond yields. *(Cheng Mount Cheng/Renee Chen)*

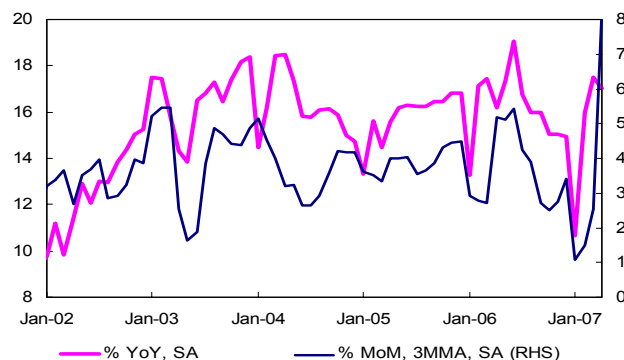
# Data Review

Announcement	Release Date	HK/SG- Time	For	Actual	Citi Fcst	Mkt Fcst	Prev
<b>China</b>							
Value Added Industry (% YoY, real)	16-May	10:00 AM	Apr	17.4	17.9	17.5	17.6
<b>Korea</b>							
Unemployment Rate (% SA)	16-May	12:30 PM	Apr	3.3	3.3	--	3.2
<b>Malaysia</b>							
CPI (% YoY)	16-May	5:00 PM	Apr	1.5	1.6	1.6	1.5

Source: Bloomberg, CEIC Data Company Limited, Citi estimates.

## China. The growth of industrial output has remained on trend in April

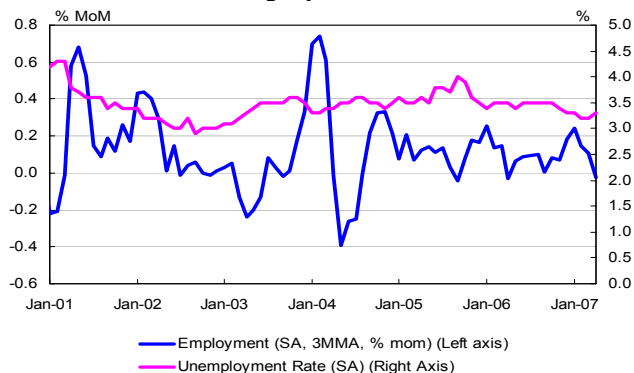
### Value Added of Industry



Source: CEIC Data Company Limited

## Korea. Job market appears fairly weak

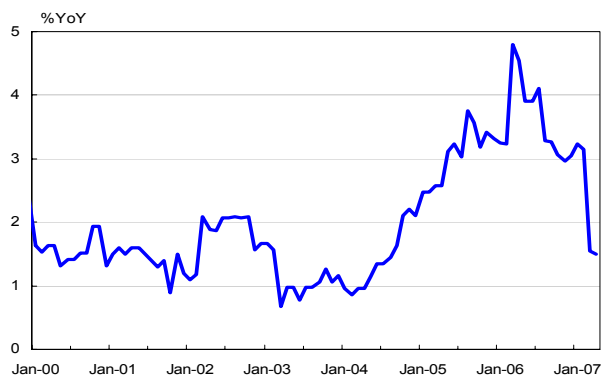
### Unemployment Rate



Source: CEIC Data Company Limited

## Malaysia. CPI expansion averaged 2.4%yoy in the first four months of 2007

### CPI Inflation



Source: CEIC Data Company Limited

# Selected Market Indicators

Policy Rates				
	Spot	Change (ppt)		
		1 Day	1 Mo	1 Yr
China - 1-year lending rate	6.39	-	-	0.54
Hong Kong - 3-Month Interbank Rate	4.41	0.01	0.13	(0.19)
India - Overnight Reverse Repo Rate	6.00	-	-	0.50
Indonesia - BI Rate	8.75	-	(0.25)	(3.75)
Malaysia - Overnight Policy Rate	3.50	-	-	-
Philippines - O/N Rate	7.50	-	-	-
Singapore - 3-Month Interbank Rate	2.44	(0.08)	(0.38)	(1.00)
South Korea - Overnight Rate	4.50	-	-	0.50
Taiwan - Overnight Rate	1.72	-	(0.00)	0.21
Thailand - 14-Day Repo Rate	3.81	(0.06)	(0.22)	(0.94)
Long Term Bond Yield				
	Spot	Change (ppt)		
		1 Day	1 Mo	1 Yr
China - Government bond yield (5-Year)	3.17	-	0.26	0.66
Hong Kong - 5-Year Exchange Fund Note	4.03	0.02	(0.11)	(0.62)
India - 10-Year Gilt	8.15	-	0.05	0.57
Indonesia - FR26	8.95	(0.04)	(0.51)	(3.08)
Malaysia - MGS 1/05	3.18	-	(0.24)	(1.41)
Philippines - 5-Year T Bond	5.93	-	-	(1.26)
Singapore - 10-Year SGS	2.66	-	(0.12)	(0.89)
South Korea - 5-Year Treasury	5.11	-	0.11	0.14
Taiwan - 10-Year Government Bond	2.06	-	0.04	(0.20)
Thailand - 10 Year Government Bond	3.60	0.03	(0.59)	(1.91)
Vietnam - 5-Year Government Bond	7.28	(0.05)	0.18	
Other Indicators				
	Last	Change		
	Index Level	1 Day	1 Mo	1 Yr
Fed Funds	5.31	-	-	0.38
6 month LIBOR	5.37	-	(0.01)	0.09
10 Yr UST	4.69	(0.02)	(0.05)	(0.41)
10 Yr Bund	4.294	(0.01)	0.09	0.28
Eurostoxx	3860	-0.18%	0.80%	10.60%
10 Yr JGB	1.670	(0.01)	(0.03)	(0.30)
10 Yr Swap	5.23	(0.02)	(0.04)	(0.38)
HY BB Index	464	0.00%	1.16%	9.78%
HY B Index	509	0.00%	1.26%	11.10%
VIX	14.01	-	2.03	0.66
DJIA	13384	0.00%	4.96%	14.67%
SPX	1501	0.00%	2.18%	13.93%
TPX	1712	-0.04%	-0.80%	3.91%
NASDAQ	1872	0.00%	2.02%	13.25%
Oil, WTI	63	-0.03%	-0.73%	-10.10%
Copper Index	350.50	-0.81%	-0.98%	-11.75%
JPY/USD	120	0.09%	0.54%	8.83%
USD/EUR	1.3596	0.04%	0.45%	5.42%
ECB Marginal Lending	4.75	-	-	1.25
BOJ	0.53	0.01	(0.51)	(0.51)
Palm Oil Future	2,390	1.84%	5.86%	
Gold	671	-0.23%	-2.93%	-2.96%
DRAM Benchmark Value Weighted Index	2,906	-0.18%	-13.21%	-14.43%

Currency						
		Change (%)				
	Spot	1 Day	1 Mo	1 Yr		
Bangladesh Taka	68.975	0.00%	-0.22%	0.36%		
China Renminbi	7.683	0.13%	0.64%	4.17%		
Hong Kong Dollar	7.8177	-0.04%	-0.07%	-0.83%		
Indian Rupee	40.88	0.21%	2.51%	11.34%		
Indonesian Rupiah	8792	-0.10%	3.41%	4.58%		
Malaysian Ringgit	3.4005	-0.04%	1.19%	5.94%		
Philippine Peso	46.95	0.10%	1.44%	11.50%		
Singaporean Dollar	1.5198	-0.24%	-0.36%	3.59%		
South Korean Won	924.0	0.02%	0.71%	2.27%		
Taiwan Dollar	33.331	0.07%	-0.44%	-4.58%		
Thai Baht (onshore)	34.575	-0.13%	1.08%	9.91%		
Thai Baht (offshore)	33.450	-0.60%	-2.54%	13.60%		
Vietnam Dong	16035	0.05%	0.01%	-0.42%		
Equities						
	Last	Change (%)				
	Index Level	1 Day	1 Mo	1 Yr		
Bangladesh DHAKA	1843	0.00%	8.52%	23.94%		
China (H Shares)	10950	0.52%	5.81%	35.81%		
China (Shanghai SE Composite)	3986	2.18%	9.77%	59.53%		
Hong Kong Hang Seng	20937	0.33%	0.86%	21.70%		
India NIFTY	4153	0.78%	3.35%	15.15%		
Indonesia Jakarta	2064	1.26%	4.84%	30.82%		
Korea KOSPI	1601	0.70%	4.28%	13.65%		
Malaysia Kuala Lumpur	1352	0.47%	2.18%	29.02%		
Philippines Composite	3409	0.01%	4.15%	27.84%		
Singapore Straits Times	3501	0.75%	2.49%	28.20%		
Taiwan Taiex	7989	0.17%	-0.69%	11.50%		
Thailand SET	722	1.26%	4.14%	-5.46%		
Vietnam Ho Chi Minh	1041	-1.32%	5.57%	45.77%		
EM CDS (5Yr)						
	Prev	Change				
Spread (in bp)	Close	1 Day	1 Mo	1 Yr	5s-2s	10s-5s
China	12	0	1	-9	6	8
India	45	0	-3	-13	-	-
Indonesia	108	0	-4	-50	60	76
Korea	15	0	-1	-8	5	6
Malaysia	14	0	-1	-12	7	9
Philippines	109	0	-4	-64	62	77
Thailand	38	0	-2	0	17	23
Volatility						
		Last	ATMF	1 Day	1 Mo	1 Yr
China	1M Vol		1.35	0.05	0.05	-1.50
	3M Vol		1.70	0.20	0.30	-1.40
Hong Kong	1M Vol		0.83	0.00	0.13	0.40
	3M Vol		0.78	0.00	0.08	0.13
India	1M Vol		7.51	-0.04	1.16	1.56
	3M Vol		6.47	0.07	0.72	0.97
Korea	1M Vol		3.65	0.00	-0.25	-3.70
	3M Vol		3.80	0.00	-0.20	-3.05
Singapore	1M Vol		3.25	0.00	-0.10	-2.25
	3M Vol					
Taiwan	3M Vol		3.30	0.00	-0.15	-1.75
	1M Vol		2.65	0.00	-0.18	-3.70
	3M Vol		2.88	0.00	-0.38	-3.08
Thailand	1M Vol		12.50	0.00	-2.91	5.20
	3M Vol		10.50	1.00	-1.00	3.50

Source: Bloomberg (as of 5/16/2007 5:14 PM).

# Economic & Market Analysis

## ECONOMIC AND MARKET ANALYSIS — Asia Pacific

### Yiping Huang

Head of Asia Pacific  
Economic & Market Analysis  
(852) 2501-2735  
[yiping.huang@citi.com](mailto:yiping.huang@citi.com)

### Don Hanna

Head of Emerging Markets  
Economic & Market Analysis  
(212) 816-7919  
[don.hanna@citi.com](mailto:don.hanna@citi.com)

### Hak Bin Chua

Asia Equity Themes and  
Singapore  
+65 6432-2057  
[hak.bin.chua@citi.com](mailto:hak.bin.chua@citi.com)

### Moh Siong Sim

Asia Currency and Interest Rate,  
and Malaysia  
+65 6328-5721  
[moh.siong.sim@citi.com](mailto:moh.siong.sim@citi.com)

### Adrienne Lui

Asia  
+852 2501-2753  
[adrienne.lui@citi.com](mailto:adrienne.lui@citi.com)

### Michael Luk

Asia  
+852 2501-2775  
[michael.y.luk@citi.com](mailto:michael.y.luk@citi.com)

### Leon Hiew

Asia  
+65 6432-1166  
[leon.hiew@citi.com](mailto:leon.hiew@citi.com)

### Rohini Malkani

Bangladesh and India  
+91 22 5631-9876  
[rohini.malkani@citi.com](mailto:rohini.malkani@citi.com)

### Anushka Shah

Bangladesh and India  
+91 22 5631-9878  
[anushka.shah@citi.com](mailto:anushka.shah@citi.com)

### Minggao Shen

China  
+86 10 6510-2933 x71068  
[minggao.shen@citi.com](mailto:minggao.shen@citi.com)

### Joe Lo

Hong Kong  
+852 2868-8442  
[joe.lo@citi.com](mailto:joe.lo@citi.com)

### Patricia Pong

Hong Kong and China  
+852 2868-8449  
[patricia.pong@citi.com](mailto:patricia.pong@citi.com)

### Anton H. Gunawan

Indonesia  
+62 21 5290-8423  
[anton.gunawan@citi.com](mailto:anton.gunawan@citi.com)

### Suktae Oh

Korea  
+82 2 2077-4014  
[suktae.oh@citi.com](mailto:suktae.oh@citi.com)

### Jun Trinidad

Philippines and Thailand  
+63 2 894-7270  
[jun.trinidad@citi.com](mailto:jun.trinidad@citi.com)

### Cheng Mount Cheng

Taiwan  
+886 2 2777-7070  
[chengmount.cheng@citi.com](mailto:chengmount.cheng@citi.com)

### Renee Chen

Taiwan and Vietnam  
+886 2 2777-7063  
[renee.chen@citi.com](mailto:renee.chen@citi.com)

## ECONOMIC AND MARKET ANALYSIS

### David P. Lubin

Head of CEEMEA  
Economic & Market Analysis  
+44 20 7986-3302  
[david.p.lubin@citi.com](mailto:david.p.lubin@citi.com)

### Alberto Ades

Head of Latin America  
Economic & Market Analysis  
+212 816-2735  
[alberto.ades@citi.com](mailto:alberto.ades@citi.com)

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