

Emerging Markets Daily

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Focus on India

- **India.** The growing use of bio fuels as a substitute of petroleum is taking its toll on food price inflation (p. 2).

Highlights

- **Singapore.** NODX in May expanded 3.7%yoy on non-tech sector strength (p. 3).

Market Drivers

- **US.** May housing starts likely fell to reflect the sharp decline in permits last month and decreasing buyer traffic. Permits, however, probably recovered somewhat after April's outsized drop.
- **Germany.** We expect a seventh consecutive monthly gain in ZEW business expectations in June, in line with the increase in Sentix business expectations.

Data Calendar

Date	Day	Local Time	Country	Indicator	For	Citi Fcst	Mkt Fcst	Prev.
19-Jun	Tue	5:00 PM	Germany	ZEW Survey (Econ. Sentiment)	Jun	28.5	--	24.0
19-Jun	Tue	8:30 PM	US	Housing Starts (Mn)	May	1.47	1.47	1.53
19-Jun	Tue	8:30 PM	US	Building Permits (Mn)	May	1.52	1.47	1.46

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

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

Focus on India

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India: Bio Fuels and the impact on food prices

Bio Fuels are fast-becoming a substitute of petroleum as transport fuels. Faced with the challenge of growing energy dependence and curbing green house gas emissions (GHG), a number of countries have begun to implement the use of alternative fuel sources, specifically bio-fuels- to substitute petroleum for transport. While benefits are plentiful, the growing use of bio-fuels has one serious disadvantage: it is driving up the prices of agricultural commodities and thus taking its toll on food price inflation.

Government initiatives include setting targets for conversion to alternative fuels and providing farmers with rebates for crop development. In order to encourage the use of bio-fuels, a number of countries have imposed regulations requiring a shift towards greener fuel. The EU recently approved a directive requiring member countries to use 10% bio-fuels for transport by 2020, while the US is required to use 132bn liters of bio-fuel by 2017. In India, the government has proposed a rise in ethanol blend with petrol to 20% by 2012 though there is little progress on this front as the oil and sugar companies have failed to arrive at a consensus on pricing. To augment supply, many countries, including Brazil and the EU, are providing subsidies to farmers to encourage them to grow crops that will aid the development of alternate fuels. A point worth noting is that India proposes to use bio-diesel produced from jatropha which is grown on waste-lands

However, a key trade-off to this is an uptrend in food prices. While benefits abound, the growing use of bio-fuels is driving up the prices of agricultural commodities with prices of corn and wheat – the key feedstock for ethanol - have reached their highest levels in over a decade this year. This is despite expectations of strong global grain production in FY08 which in turn has impacted prices of processed goods. Satisfying the EU's new regulations would require the entire region's rapeseed oil production as feedstock as well as put immense pressure on production of wheat and sugar beet which in turn will keep up the pressure on prices of wheat, edible oils and oilseeds.

To this end, we could see primary product prices in India continue to face pressures unless adequate measures to ramp up production are taken. To compensate the shortfall in domestic wheat production, India resorted to wheat imports after a gap of nearly six years. Higher food prices remain one of the key reasons for the rise in primary product inflation which has a weightage of 22% in India's WPI basket. While the latest headline inflation number has come in at 4.8%, primary product inflation remains high at 8.2% with wheat prices (weightage of 1.4%) rising 8.5% while oil-seeds (weightage of 2.7%) rising 28% YoY. Thus to minimize the domestic impact of rising global prices, India would need to enhance agricultural production and productivity to minimize imports of primary articles.

News in Brief

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Japan

Contrary to some market participants' expectations, **Bank of Japan Governor Toshihiko Fukui kept a restrained tone, hardly anxious to move early**, in his press conference Friday, June 15. That said, his restrained tone is not surprising at all given the current situation. If he had made a hawkish comment implying a willingness to move early when financial markets have almost fully priced in an August rate hike in the past few weeks, the markets could have started to discount an even earlier July hike. A rate hike just before the upper house election (currently scheduled on July 22) could drive the central bankers into an awkward position. It is only natural that they avoided such a situation.

We believe that chances of a July hike have now been almost completely eliminated. Even a strong Tankan result (released July 2) will have an only limited impact on the policy decision. Even if the BoJ seriously considers an August rate hike (at the August 22-23 policy meeting), quite a few important economic indicators are slated for release before that date including the second-quarter GDP (around August 13). As we cannot rule out the possibility of softness from these data, the BoJ had little pressing need to imply a specific date for the next rate hike. The BoJ most likely adopts a 'natural attitude' i.e., a rate hike will depend on upcoming economic indicators. (*Kiichi Murashima*)

Singapore

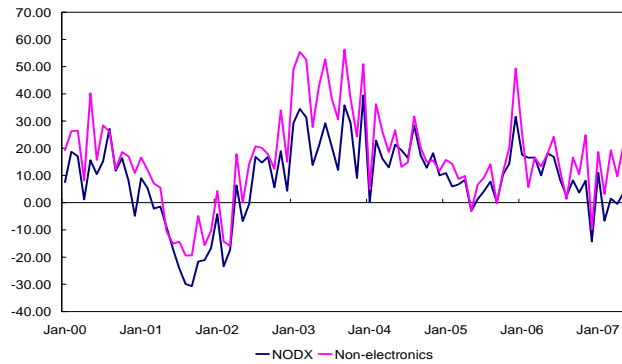
NODX for the month of May expanded a higher-than-expected 3.7%yoy due to strength in the non-electronics sector, which offset the decline in the electronics sector. The electronics sector continued to contract for the fourth month in a row due to the decrease in domestic exports of ICs, disk drives, telecommunications equipments, and diodes and transistors. Weaker overseas sales especially from weaker US demand are hurting the electronics sector. The non-electronics sector on the other hand, gained 22%yoy in May, up from the 9.6%yoy expansion in the previous month. The strong performance of the non-electronics sector is due largely to the solid recover from the pharmaceuticals sector, which expanded by 76%yoy in May versus a 17.2%yoy contraction in the previous month. Going forward, we expect the electronics sector to pick-up in 2H07 as some leading tech indicators are suggesting that the tech slump could already be past its worst. (*Hak Bin Chua*)

Data Review

Announcement	Release Date	HK/SG- Time	For	Actual	Citi Fcst	Mkt Fcst	Prev
Singapore							
Non-Oil Domestic Exports (% YoY)	18-Jun	1:00 PM	May	3.7	1.5	2.4	-0.4

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

Singapore. NODX Expands on Strength in Non-Electronics



Source: CEIC Data Company Limited

Selected Market Indicators

Policy Rates					Currency						
	Spot	Change (ppt)			Spot	Change (%)					
		1 Day	1 Mo	1 Yr		1 Day	1 Mo	1 Yr			
China - 1-year lending rate	6.57	-	0.18	0.72	Bangladesh Taka	68.775	0.00%	0.33%	1.03%		
Hong Kong - 3-Month Interbank Rate	4.42	(0.05)	(0.00)	(0.15)	China Renminbi	7.6294	-0.06%	0.53%	4.88%		
India - Overnight Reverse Repo Rate	6.00	-	-	0.25	Hong Kong Dollar	7.8195	-0.02%	-0.02%	-0.70%		
Indonesia - BI Rate	8.50	-	(0.25)	(4.00)	Indian Rupee	40.77	0.23%	-0.12%	12.45%		
Malaysia - Overnight Policy Rate	3.50	-	-	-	Indonesian Rupiah	8905	1.52%	-0.95%	4.36%		
Philippines - O/N Rate	7.50	-	-	-	Malaysian Ringgit	3.4245	0.96%	-0.93%	6.35%		
Singapore - 3-Month Interbank Rate	2.63	-	0.25	(0.83)	Phillipine Peso	45.895	0.33%	1.44%	15.81%		
South Korea - Overnight Rate	4.50	-	-	0.25	Singaporean Dollar	1.5377	0.03%	-0.80%	3.78%		
Taiwan - Overnight Rate	2.48	-	0.75	0.91	South Korean Won	927.9	-0.02%	0.66%	3.00%		
Thailand - O/N Repo Rate	3.53	-	(0.47)	(1.31)	Taiwan Dollar	33.146	0.13%	0.63%	-2.01%		
					Thai Baht (onshore)	34.585	0.16%	0.16%	11.23%		
					Thai Baht (offshore)	32.490	-0.15%	1.35%	18.41%		
					Vietnam Dong	16112.5	0.08%	-0.33%	-0.80%		
Long Term Bond Yield					Equities						
	Spot	Change (ppt)			Last Index Level	Change (%)					
		1 Day	1 Mo	1 Yr		1 Day	1 Mo	1 Yr			
China - Government bond yield (5-Year)	3.59	-	0.34	0.95	Bangladesh DHAKA	2029	0.00%	7.44%	36.22%		
Hong Kong - 5-Year Exchange Fund Note	4.64	(0.04)	0.54	(0.04)	China (H Shares)	11867	3.56%	8.49%	46.57%		
India - 10-Year Gilt	8.19	-	0.04	0.39	China (Shanghai SE Composite)	4253	2.83%	5.25%	62.98%		
Indonesia - FR26	8.66	(0.12)	(0.11)	(3.93)	Hong Kong Hang Seng	21583	2.62%	3.14%	26.60%		
Malaysia - MGS 1/05	3.57	-	0.47	(0.95)	India NIFTY	4147	-0.58%	-1.62%	30.31%		
Philippines - 5-Year T Bond	5.93	-	-	(4.77)	Indonesia Jakarta	2126	0.28%	2.95%	38.42%		
Singapore - 10-Year SGS	2.94	-	0.35	(0.46)	Korea KOSPI	1807	1.92%	10.77%	30.15%		
South Korea - 5-Year Treasury	5.36	(0.00)	0.17	0.33	Malaysia Kuala Lumpur	1372	0.85%	1.13%	34.89%		
Taiwan - 10-Year Government Bond	2.54	-	0.43	0.35	Philippines Composite	3681	0.25%	6.29%	42.36%		
Thailand - 10 Year Government Bond	4.52	0.06	0.97	(1.02)	Singapore Straits Times	3624	1.18%	3.07%	34.49%		
Vietnam - 5-Year Government Bond	7.26	0.00	(0.02)	-	Taiwan Taiex	8574	0.00%	6.29%	23.30%		
					Thailand SET	765	2.67%	4.70%	12.99%		
					Vietnam Ho Chi Minh	1044	-0.40%	-2.16%	49.84%		
Other Indicators					EM CDS (5Yr)						
	Last Index Level	1 Day	Change		Prev	Change					
			1 Mo	1 Yr		Close	1 Day	1 Mo	1 Yr	5s-2s	10s-5s
Fed Funds	5.25	-	-	0.31	India	48	0	3	-29	#VALUE!	#VALUE!
6 month LIBOR	5.41	-	0.04	(0.12)	Indonesia	97	0	-4	-110	59	69
10 Yr UST	5.14	(0.03)	0.33	0.01	Korea	15	0	0	-9	5	6
10 Yr Bund	4.633	(0.02)	0.32	0.69	Malaysia	14	0	0	-17	7	7
Eurostoxx	4019	1.34%	2.79%	19.21%	Philippines	97	0	-5	-125	51	67
10 Yr JGB	1.895	(0.05)	0.25	0.08	Thailand	35	0	-3	-6	16	21
10 Yr Swap	5.73	(0.03)	0.37	0.03							
HY BB Index	457	0.00%	-1.45%	9.01%							
HY B Index	506	0.00%	-0.82%	11.32%							
VIX	13.94	-	1.18	(3.31)							
DJIA	13639	0.00%	0.61%	19.25%							
SPX	1533	0.00%	0.66%	18.36%							
TPX	1788	0.86%	5.18%	14.18%							
NASDAQ	1942	0.00%	2.34%	19.54%							
Oil, WTI	68	-0.24%	4.27%	-3.01%							
Copper Index	345.55	0.97%	3.72%	4.75%							
JPY/USD	123	-0.01%	1.87%	6.67%							
USD/EUR	1.3402	0.10%	-0.80%	5.67%							
ECB Marginal Lending	5.00	-	0.25	1.25							
BOJ	0.53	0.04	(0.49)	(0.56)							
Palm Oil Future	2,503	3.12%	5.31%	11.63%							
Gold	658	0.35%	-0.62%	-8.19%							
DRAM Benchmark Value Weighted Index	3,073	0.00%	8.08%	-							

Source: Bloomberg (as of 6/18/2007 7:43 PM).

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