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# GUILD INVESTMENT MANAGEMENT INC.

## Guild Investment Global Market Commentary

**Written: June 30, 2009**

### INDIA

India is planning to invite foreign investors to participate in a plan to increase road building ten-fold. A *Financial Times* article titled "India Seeks Foreign Investment in Roads" discusses this plan.

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#### FINANCIAL TIMES

#### **India seeks foreign investment in roads**

By Joe Leahy in Mumbai

Published: June 23 2009

India's Congress party-led coalition government is planning to invite foreign investors to participate in an ambitious move to increase road construction 10-fold as the country seeks to boost much needed infrastructure development....

"The roads are in a mess," Mr Nath told the Financial Times in an interview.

"At the moment, we've been struggling with [building] 2km a day - I've set a target for 20km a day . . . we are going to work towards that."

## ABOUT THE AUTHORS



Monty Guild  
CEO

Mr. Guild founded Guild Investment Management in 1971. Mr. Guild is a recognized expert in the

Bureaucracy and land disputes have so far curbed India's efforts to improve its crumbling road network, even as its neighbour across the Himalayas, China, has built superhighways criss-crossing the country.

However, the return last month of the Congress party-led ruling coalition with an overwhelming majority has created the opportunity for an infrastructure programme of historic proportions, similar to the prewar highway construction boom of the US.

PwC, in a report titled "Infrastructure in India - a vast land of construction opportunity", says India is targeting investment in roads of \$92bn in the five years to 2012....

Analysts said that, while the programme was laudable, the key was implementation.

India's road-building programme in recent times has been disrupted by factors such as frequent changes of leadership at the National Highways Authority.

"They need to be ambitious and, more importantly, they need to focus on execution," said Arvind Mahajan, infrastructure and government national industry director at KPMG.

Mr Nath said the new roads finance company would be able to draw on the government's Rs100bn (\$2.1bn, €1.5bn, £1.3bn) in annual earnings from a tax on fuel sales as well as budgetary allocations of about Rs40bn and other income of about Rs60bn.

He said the government would raise international financing for the corporation as well as investment from pension funds and others interested in the long-term returns offered by infrastructure.

"I will do a roadshow in the next two months, all over the world, to attract funds for this," he said.

While land acquisition can be a challenge, he said people would be willing to sell because roads usually raised the value of their adjacent property.

The problem in the past was that roads did not get built, leading to dis-illusionment among the sellers.

areas of international investing and economics. He has been a writer and speaker on economic issues for 30 plus years and has been widely quoted in the world media. Mr. Guild supervises the investment and research functions at Guild Investment Management. He holds a BA in economics and an MBA with highest honors.



Anthony Danaher  
PRESIDENT

Anthony Danaher joined Guild in 1990. Mr. Danaher supervises the client service, accounting, and administration function. Mr. Danaher holds a BA in Business

India remains one of our favorite countries for global investment. India's underdeveloped infrastructure is one of the things keeping India from enjoying the 8% annual growth that we project for China over the next five years. We project India to have about 6% per annum GDP growth.

It is very encouraging to see the above mentioned approaches, which could be of importance to the prosperity of all Indians. The Indian market is currently experiencing a pull back after a strong upward march in prices. We will be buyers on the correction.

## **PROTECTIONISM**

Protectionism still remains a global threat. I have been generally encouraged by the dignity shown by many governments who could have played the protectionism card more aggressively, or engaged in a unilateral collapse of their currency in order to increase exports. Perhaps due to banking concerns, the latter has not happened...yet.

On the trade front, all the news is not good however. This week the U.S. and European Union lodged a case with the World Trade Organization accusing China of export quotas. The trend is positive thus far, but we cannot lose focus on the fact that protectionism can still increase even more than it has so far during the depression in the developed world. Politicians usually find a way to do the politically expedient and often economically unwise thing; and during a period of high unemployment and low economic activity, they are under more pressure to be more short-sighted and do dumb things.

## **U.S. IS TURNING INTO A NATION OF SAVERS AT LEAST TEMPORARILY**

Administration, with an emphasis in accounting and an MBA.

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The U.S. savings rate is at 5.7%, a multi year high. This is a positive as Americans must stop their wild spending and start saving and creating capital so the economy can return to a growth footing.

Increased savings means that spending is not rising, thus retail sales are weak. We believe that the situation is such that employment must rise substantially before retail sales will rise meaningfully. The economy in the U.S. remains weak. We are still several quarters away from the bottom in unemployment, and there is reason for caution as businesses want to improve profits by cutting headcount.

## **U.S. AND EUROPEAN STOCK MARKETS**

The fact is that the U.S. and European stock market has rallied in spite of weak U.S. and European economic data. The U.S. market is about even for the first six months of 2009; after a terrible drubbing in 2008. World economies in Europe, Japan and the U.S. continue to be under pressure and the economies of exporting countries in general have weakened. If this is the case, why are we bullish on stock markets in China, India, Hong Kong and Brazil?

## **THE GROWING COUNTRIES**

These countries are benefiting from a several factors.

1. They did not buy into the derivative madness. They did not pollute their banking systems with massive amounts of derivatives on leverage that later were sold for a fraction of their cost.
2. They did not put pressure on their national treasury to bail out banks with newly printed cash and they did not have gargantuan new lending to bankrupt banks and investment banks to keep them solid.

3. Their money supplies have grown as new money is coming into the system in the form of private direct investment and government investment in infrastructure.
4. The velocity of money is growing because their banks are not required to cut lending and bail out bad loans, so they are free to expand lending to enterprises that will grow.
5. With GDP growing corporate profits will grow; and with corporate profits growing, stock valuations in these countries will grow. Numerous academic research papers and much subjective observation reinforce the notion that stocks will rise when corporate profits rise.

In other words, these countries' banking regulators did their job, and the banks were investing conservatively. At the same time in Europe and the U.S. banks and banking institutions were gambling...ultimately with the taxpayer's money.

### **THE ISSUE OF A NEW MULTI-POLAR CURRENCY WORLD IS JUST GETTING TRACTION**

In the developing world, we see a strong and continuing campaign (that we have mentioned from time to time in these pages) to add other currencies and currency trade agreements into the world financial structure. The purpose of this campaign is to gradually supplant (we imagine that it will take decades) the U.S. dollar with a new world reserve currency, probably the Chinese Yuan. As an intermediate step, many nations are proposing using a basket of currencies for trade and lending status...close to a reserve currency status.

The issue is complicated, but we will attempt to simplify. The proposal of a group of currencies

has been tried before in SDR (Special Drawing Rights) and other forms, and it is unwieldy and did not work well. This time however, as an intermediate step from the U.S. dollar to the Yuan, the SDR scheme might work for a limited period of time.

### **WHY DO MANY COUNTRIES WANT TO EVENTUALLY REMOVE THE U.S. DOLLAR AS THE WORLD CURRENCY?**

Countries around the world hold much of their reserves in U.S. dollars. They believe that the U.S. has acted irresponsibly and diluted the value of the dollar by unwise spending and deficit creation.

They believe that the U.S. has enjoyed a large amount of political and military advantage due the fact that the U.S. dollar has been the world reserve currency for decades. They do not approve of many of the choices that the U.S. has made such as bailing out inefficient industries and wild banking excesses on the back of taxpayers. They do not see an end to the huge deficits projected for the U.S. Thus, the dollar has lost the confidence of many nations.

For generations, the U.S. provided a defense umbrella to many nations such as Japan, Korea, Saudi Arabia, and many others. This has not changed. In addition, the U.S. was a destination for export goods from many emerging countries. Many of these goods were turned into machines and other finished products that were then resold to the world. Today, the U.S is not importing as much, its consumers are forced into becoming savers [and wisely so], and U.S. manufacturing has become less competitive (although the U.S. still exports many technology products and many foodstuffs to the world).

In general, the dollar is gradually being replaced. This will be a multi-year process. We will watch

the world gradually come to accept the assertion that we should have a multi-currency world, and then probably a one reserve currency world...led by the Chinese Yuan.

All of the current talk is just part of a long term process as described in a Reuters News story this past weekend.

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### **China, Brazil working on trade FX deal**

*Sunday, June 28, 2009 12:08:06*

*Provided by: Reuters News*

- \* China, Brazil want trade deals done in local currencies*
- \* Other central bankers question dollar's global role*

*By Krista Hughes and Tamora Vidaillet  
BASEL, Switzerland, June 28 (Reuters) - China and Brazil are working on a currency arrangement to allow exporters and importers to settle deals in their local currencies, bypassing the U.S. dollar, the countries' central banks said on Sunday.*

*Speaking on the sidelines of the Bank for International Settlement's annual general meeting in the Swiss city of Basel, other central bankers questioned the dollar's future role as the world's dominant reserve currency.*

*China's Central Bank Governor Zhou Xiaochuan and Brazil's Central Bank President Henrique Meirelles discussed the bilateral deal in a meeting at the BIS on Saturday.*

*"It is agreed in principle," a spokeswoman for the Brazilian central bank told Reuters. "They will start to study this."*

*No details were available on the size of the arrangement or the timeline for finalizing details.*

### **ALTERNATIVE TO DOLLAR**

*The debate of an alternative international currency to the dollar has heated up in recent months after the world's key reserve holders in emerging economies have expressed concern about the U.S. dollar remaining the dominant reserve currency.*

*As emerging nations gain more clout in the global economy, they also want to study how they might increase the use of local currencies in international trade.*

*China -- the world's top holder of foreign exchange reserves -- renewed its call on Friday for the creation of a super-sovereign reserve currency to reduce the dollar's global domination, which it said had worsened the financial crisis.*

*Russia, whose reserves are the world's third largest, has also called for the world to become less dependent on the dollar.*

*"You have China, Russia proposing we should think about a more international reserve currency other than the dollar," Jassem Al-Mannai, director general, Arab Monetary Fund said in a Reuters interview. "America, through this crisis, accumulated huge debts. It's a heavy burden on the dollar."*

*Argentina's central bank Governor Martin Redrado told Reuters that the dollar will have to share the global stage with strong regional currencies such as the Chinese yuan and Brazilian real in the future.*

*"The yuan will have a role in Asia with the yen; obviously the euro; in South America probably the real .. so we are looking at a world in which the dollar will continue to be the leading currency, but it will be a much more shared approach," he said.*

*Philippine central bank Governor Amando Tetangco also told Reuters in Basel that the recent trend of diversification away from the dollar is set to continue.*

*"(For) emerging central banks to shift out of the U.S. dollar, it has been always an option and this has happened to some extent in the form of diversification into foreign currencies ... This process will inevitably continue," he said.*

#### **YUAN'S INTERNATIONALIZATION**

*Zhou said a further step was for Brazilian President Luiz Inacio Lula da Silva and Chinese President Hu Jintao to discuss the arrangement, which he said would not necessarily involve a currency swap like those China has in place with other countries.*

*"What we are discussing is that Brazil's president Mr Lula and our president Mr Hu talk about the possibility and gradual development to use our local currency for some trade settlement and ... investment, that's the major thing," he told reporters. "It's not necessarily to use a currency swap."*

*The People's Bank of China has arranged six bilateral currency swaps, totaling 650 billion yuan (\$95.12 billion), since December with countries including Malaysia, Argentina and Hong Kong.*

*Under the arrangements, a central bank on the other side of the swap will be able to lend the yuan provided by the PBOC to domestic commercial entities to pay for imports.*

*Chinese exporters are thus paid in their home currency, eliminating exchange rate risks and reducing the cost of fund transfers. The same applies in the other direction of the swap.*

*Brazil is not afraid of slowly diversifying out of U.S. dollars in its investments and international trade, as long as the process is safe and not an "adventure," Foreign Minister Celso Amorim said on Friday.*

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## **INVESTMENT SUMMARY**

We continue to focus on China, and India (which is having a pull back making it somewhat more interesting), oil, and gold. Some U.S. stocks maybe interesting, but we see substantially bigger profits in the areas just mentioned. In our opinion, all investors below retirement age should structure a portfolio which includes at least 40% of assets in stocks of fast growing countries, oil, and gold. We recommend that you buy them on corrections and do not chase rallies. Only then do we believe that investors will they be able to protect themselves from a declining dollar and a mediocre investment environment in the U.S., Europe, and Japan.

Thanks for listening.

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