



August 15, 2011  
World Markets Feel U.S. Woes



**Q: What a week! Looking back the trigger was really the political deadlock in Washington, about the US debt ceiling, and then the S&P downgrade on Friday after the market close. Then, it just snowballed from there with Europe and then that snowballed into Latin America and Asia. Now looking forward what's the medium term impact of all of these in your view?**

One thing we should be clear is that the US has been living beyond its means for a very long time. The downgrade is really a reality check, that the US policy makers should take some swift action to take some expenditure reduction plans and the whole debate politically in US was a mess, in the sense that it shows that no concrete action is likely till after the election in 2013. What does that mean? That means we are going to remain in sub-par growth environment for a very long time to come.

**Q: So, you don't think that's enough?**

It's not enough. Balancing the budget is not the issue here. The issue here is taking the bitter pill and taking concrete expenditure cuts. That has not happened. That is where the political divide is, and that needs to happen before the market can believe again that this is a sustainable recovery.

**Q: This is the criticism that we're hearing from a lot of people, that Washington really didn't take the tough decisions this time around. Let's look at the US economy. We still have a 9.1% unemployment, very sluggish growth, a lot of economists are saying this is going to take years not months for the US to get back on track. In your view, is the US another Japan?**

I think the probability of it becoming another Japan has become higher and higher by the day, by the delay in the policy making. The fact that the policy makers in the US have said that interest rates are going to remain low for a long time is practically public admission of the fact that

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economic growth is going to remain sub-par. The problem is that the corporates in the US is actually very profitable and they are very flexible.

**Q: We have seen great corporate earnings.**

Exactly. So in an environment where the macro economy is very weak, corporate America is still going to cut jobs to retain profitability and that means unemployment is going to remain very high.

**Q: Let's look at a couple of different strengths here as a result of what happened last week. We saw the Chinese Yuan appreciate significantly and for the year it's up about 3.1%. Now for a very long time, American politicians have criticized China for undervaluing the Yuan. Now we see it's rising. What's the impact? Is it good for China since it helps trim down the inflation? Is it good for the US?**

China is having its own balancing act. You're right absolutely about by appreciating the RMB, they prevent inflation spiking further, and it prevents higher domestic rates inside China. But it does hurt the exporters which have been the key to economic success in China. And make no mistake, China's going to do what's right to China, not necessarily what's best for the US. And what that does mean is gradual appreciation. We should rule out the possibility of any sudden revaluation of RMB. But I think what will speed up very fast is that the RMB is going to become a global reserve currency probably within the next 2 years.

**Q: In the next 2 years? Because I heard other people said oh it's going to take a decade or so. But you're more optimistic about the RMB beating the Dollar as a reserve currency.**

I think the one fact that has changed the last one week is that people are now going to look at the USD and say - it used to be a safe haven, it still is a safe haven for the major of my assets, but I can't depend upon it for the next ten years. I need to buy something else.

**Q: So, what does all of this do for investor sentiment here in Asia?**

I think unfortunately Asia is a kind of recipient of all these policies in Europe, the US and Japan. So you can hide in Asia in local currency bonds, in local interest rates but investor sentiment is now plunging back. Sentiment surveys show that people are much more risk averse.

**Q: In certain countries, you are seeing a little bit more optimism like Indonesia and India. Is that right?**

Yes. Any country which is more reliant on domestic demand like Indonesia and India is obviously sustaining itself not on exports to the US or to Europe; it's sustaining itself on what the local people do. And even though they're getting hurt by higher inflationary pressures, they are still relatively buoyant in terms of domestic demand and the economy is doing relatively well.

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