



MONEY MORNING

SPECIAL RESEARCH REPORT

The Three Markets You Can't Afford to Ignore

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If the wild stock-market swings and never-seeming-to-end financial crises of the past several years prove anything to investors, it's that the "tried-and-true" investing rules no longer all apply.

No longer is it enough to focus only on potential profits: Risk and the potential for loss are front-and-center as considerations to keep in mind. So is investment quality. It doesn't matter whether one's referring to a stock, a bond, an exchange-traded fund (ETF), or even an entire market (country), odds are that if the underlying investment is debt-laden, scandal-ridden and problem-plagued, then the "bargain" you think you got through bottom-fishing is likely to end up as a whole lot of investor heartache.

If you want to be successful in choosing the "next" hot market, keep these three rules in mind:

Rule No. 1: Countries that were stingy with their monetary and fiscal bailout plans during the worst part of the global financial crisis will now reap the benefits – and will easily distance themselves from the countries that slashed their interest rates to zero and allowed their deficits to soar.

Rule No. 2: Emerging economies will outgrow their richer, more-mature counterparts. There's simply more upside.

Rule No. 3: Global commodities prices will continue to move higher. The "haves" – those that control commodities – will outgrow the "have-nots."

Consider it a "good," "better," "best" type of scenario. Rule No. 1 is virtually a "no-exception" requirement in the new economic reality. An economy that doesn't fulfill that requirement most likely warrants a "pass." Countries that meet all three are top profit candidates.

Given these considerations, *Money Morning* has scoured the globe in search of the three markets we believe offer the best investment prospects in the months – and the years – to come.

The markets that we've chosen – and the reasons we've chosen them – may initially surprise you. But you'll quickly agree with our logic, as well as our analysis. The markets in question are:

- Singapore,
- Germany,
- and Chile.

All three are well-managed, growing economies – without the excesses in spending and debt that have wrecked markets as diverse as Greece and the United States. We’ve highlighted at least one investment from each.

With the introduction complete, let’s look at the markets. For a summary of the investment recommendations, check out **Chart III**, which appears at the end of this report.

Singapore: China’s Role Model

China’s economic model has been extraordinarily successful. But the Asian giant didn’t create it out of thin air.

It had a role model.

A generation before China began to take off, another smaller country - also dominated by an ethnic Chinese populace - demonstrated how rapid growth could be combined with political stability.

I’m talking, of course, about Singapore.

Just recently, Singapore demonstrated yet again that it might well have the answer to some of China’s current problems. The Asian island city-state said its economy grew at an annualized rate of 32% in the first quarter - and then it revalued its currency in order to prevent the Singapore economy from overheating.

As investors, we need to look at the mentor, as well as at the pupil.

A Global Leader Gets its Start

Singapore gained independence from Britain in 1959 and immediately elected Lee Kuan Yew as prime minister. He ruled the country for 31 years, after which his handpicked deputy ruled for 14 years. Lee’s son, Lee Hsien Loong, took over in 2004 as the third and current Singapore prime minister.

So essentially Singapore’s economic success is the work of one family, even one man (Lee Kuan Yew is still with us, in fact, serving as Singapore’s “Minister Mentor”).

Although Lee Kuan Yew had been elected in a loose alliance with the Communists, he followed a free-market economic policy, but one in which the overall direction of the economy was set by the government. Tax rates, in general, were low, government spending was kept at a remarkably low level - currently 15% - in terms of gross domestic product (GDP), and foreign investment was aggressively encouraged in most sectors.

Lee also solved the problem that is currently vexing the United States and other rich countries by privatizing both social-security and unemployment insurance: It forced employees to pay contributions into a “Central Provident Fund“ that operated individual accounts out of which unemployment payments, health-insurance premiums and, eventually, pensions were paid.

Thus, the area of the economy over which the state exercised direct control remained limited, while the Central Provident Fund exercised considerable influence on behalf of its account holders.

Overall, Singapore became the world’s leading trade *entrepot*, aggressively moving up the global value chain as its per-capita GDP increased and its citizens became richer and more educated. With per-capita GDP now estimated at \$50,300, Singapore is actually now richer than its U.S. counterpart.

And that’s not all the sovereign city-state has going for it. Singapore’s economic openness is actually quite

remarkable by world standards: It ranks second in the world on the Heritage Foundation's Index of Economic Freedom, and has also remained remarkably uncorrupt, ranking third on Transparency International's 2009 Corruption Perceptions Index [Please see Chart I].

A Role Model for China

This combination - a free-market economy under a high degree of direction by a government that retains firm political control (though Singapore was - and remains - a democracy) - was highly attractive to China's leaders, particularly the late Deng Xiaoping, as they sought ways to open up their economy from the 1980s.

The Chinese leadership has maintained tighter political control than the Singapore government, imprisoning - and even executing - dissidents, and not allowing free elections. Mainland China also retained a high degree of state control of industries it considered strategic, such as oil, steel and anything related to defense. However, like Singapore, China has welcomed foreign investment - and at least on the surface has pursued a policy of relatively free trade, low taxation and relatively low public spending.

Apart from its lack of democratic freedoms, China's principal failure to match Singapore has come in the areas of economic freedom (including secure property rights) and corruption - the Asian giant ranks only 140th out of 179 countries on the Index of Economic Freedom and 79th out of 180 countries on the Corruption Perceptions Index.

Still, China has labor costs that are nowhere near as high as those of Singapore, meaning the larger country retains considerable room for inefficiency. Nevertheless, as it gets richer, moving up the Heritage Foundation and Transparency International lists should be a top priority for China.

How to Play Singapore for Profit

Singapore's recovery from the 2008-2009 recession has been rapid. By advancing at an annualized rate of 32%, Singapore's economic growth for the 2010 first quarter outpaced the same measure for the first three months of 2009 by a stunning 13.1%.

The Monetary Authority of Singapore (MAS) - the nation's central bank - raised its exchange-rate target for the Singapore dollar by an undisclosed amount of 2% to 3%. The objective: To keep the Singapore economy from overheating and boiling over.

Needless to say, rapid economic growth and danger of overheating is a problem for China, too, and a modest revaluation of the yuan may well prevent economic overheating and inflation (not to mention also

Chart I: Steady Singapore

In each of the last three years, Singapore has ranked second out of 183 countries in the "Index of Economic Freedom" that's published annually by The Wall Street Journal and The Heritage Foundation, a top Washington think tank. The Index measures 10 "freedoms" - from property rights to entrepreneurship - as a way of gauging just how competitive the economy of a particular nation is likely to be.

Not surprisingly, given that the global financial crisis that struck with full force in 2008, the United States saw its standing slip in each of the last several years: It was No. 5 on the 2008 list, No. 6 on the 2009 list and No. 8 on this year's list.

Rank	Country	Score	Change (From Last Year)
1.	Hong Kong	89.7	(-0.3)
2.	Singapore	86.1	(-1.0)
3.	Australia	82.6	0.0
4.	New Zealand	82.1	0.1
5.	Ireland	81.3	(-0.9)
6.	Switzerland	81.1	1.7
7.	Canada	80.4	(-0.1)
8.	United States	78	(-2.7)
9.	Denmark	77.9	(-1.7)
10.	Chile	77.2	(-1.1)

Sources: The Heritage Foundation, Money Morning Staff Research

making the U.S. Congress happy. For all those reasons, China is believed to be carefully watching the results of the MAS' reaction to Singapore's torrid growth.

While Singapore is a relatively small economy - with a GDP of only \$165 billion in 2009 - its exalted positions in wealth, economic freedom, clean government and clean business make it a highly attractive place in which to invest. Of course, the rest of the world is aware of this, so the Singapore stock market normally trades at a fairly steep valuation.

Still, its recent valuation of 19 times earnings make it an absolute bargain when compared with its much-slower-growing U.S. counterpart (the Standard & Poor's 500 Index is currently trading at an almost-equally-lofty Price/Earnings (P/E) ratio of 21).

The problem with Singapore investments is that the Sarbanes-Oxley mess has deterred Singapore companies from obtaining New York listings, so there are now no companies with U.S. listings beyond the so-called "Pink Sheets." If you have a broker that allows you to invest directly on the Singapore Stock Exchange, that is not a problem.

For those who don't have such a broker, take a look at the iShares Trust MSCI Singapore Index Exchange-Traded Fund (NYSE: EWS), which has net assets of \$1.6 billion and an expense ratio of only 0.55%.

Germany: The Surprising "Must-Invest" Economy

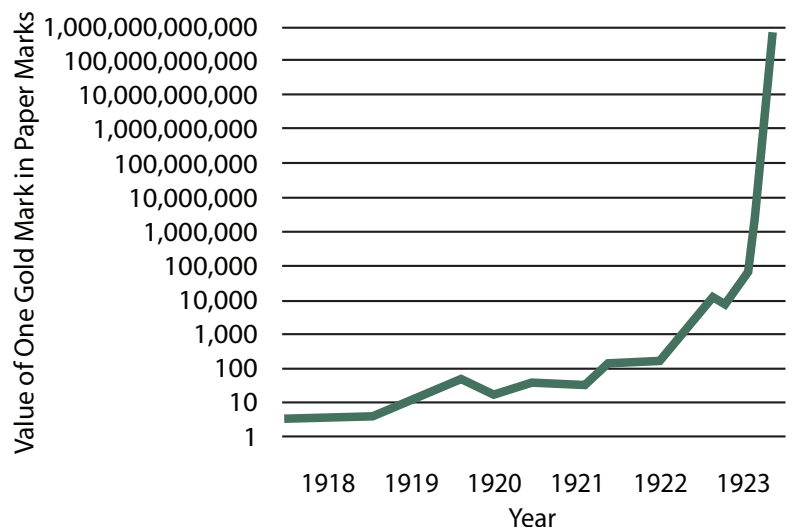
If you're a U.S. investor, you can't be happy about the prospects for your portfolio. After all, you're mostly trapped in an economy with a gigantic and dangerous financial-services sector, a central bank that can't stop itself from printing money and a government that overspends wildly.

But there is an answer: You should consider allocating some of that "at-risk" capital to a country that has none of those problems: Germany.

Germany has a banking system, of course, but that banking system is not the overgrown financial-services monster that we have here in the United States (or, for that matter, in Great Britain). It's impossible to get a subprime mortgage in Germany: Even now - and even after mortgage levels have crept up in recent years - the average down payment for the purchase of a new home in this key Eurozone nation is 50%.

Chart II: A Grim Reminder

For those who wonder about the damage that could be caused by a period of so-called "hyperinflation," just look at what happened in Germany's Weimar Republic from 1921 to 1923 – the scene of perhaps the best-documented cases of hyperinflation in modern history. Although the government blamed the massive runup in prices on the hefty war reparations due as a result of the treaty that ended World War I, many experts say those payments accounted for only a third of that country's deficit. Bankers and foreign speculators exacerbated the price escalation, which during the last half of 1922 saw the country's cost-of-living index soar from 41 to 685 – an increase of more than 16 times. The German mark fell from about 60 marks to the U.S. dollar in early 1921 to 8,000 marks to the dollar in December 1922. Overall, as the chart shows, the paper mark/gold mark ratio rose from one in 1921 to 1 trillion in 1923.



Sources: Wikipedia, The Economics of Inflation, Money Morning Staff Research

As a result, the homeownership rate in Germany is only 43%, the lowest rate in the European Union.

That's actually healthy: Far less of Germany's capital is tied up in unproductive housing and the savings rate is correspondingly higher. (Let's face it, most Americans don't accumulate 50% of the cost of a house in savings over their lifetimes - unless forced to do so in a company-pension scheme).

What's more, this more-modest home-ownership rate lessens the impact of speculative bubbles, since the wealth of most folks isn't tied up in rapidly escalating housing prices. So while the German banking system had its own real estate problems in the late 1990s, the only parts of it that got in trouble in 2008 were those banks that had rashly ventured overseas and got caught up in the U.S. disaster.

Up until 1999, Germany had the most admirable central bank in the world - the Bundesbank. This was a much better set up than the U.S. Federal Reserve. It was owned by the states instead of by the national government, so political interference was much more difficult. It was a single institution, instead of a collection of regional banks, so it was much easier to manage. And it had the single objective of avoiding inflation (Germany having bad memories of the Weimar hyperinflation of the 1920s) so did not get sidetracked into attempting Keynesian management of employment. As a result, Germany's currency - the Deutsche Mark - was a beacon of stability during the inflation-ridden 1970s **[Please See Chart II]**.

In 1999, control of Germany's monetary policy passed to the European Central Bank (ECB). The ECB is not as solid as the Bundesbank, but it still beats the Fed. The ECB expanded the money supply much less than did the Fed from 2002-07, and it has issued much less monetary stimulus since the crash. Consequently, there is far less danger of inflation in Germany and the Eurozone in general than there is in the United States. Yes, there's the possibility that German taxpayers might have to bail out Greece, but the same possibility exists in the United States with respect to California, which is much larger.

However, the most important advantage for Germany over the United States - in fact, over all the other major industrial economies - is its superior fiscal policy. When the talk of "stimulus" first appeared in late 2008, Peer Steinbrück - a Social Democrat who was then serving as Germany's finance minister - rudely described it as "crass Keynesianism." As a result, Germany did very little stimulus, and so still has a budget deficit of less than 5% of GDP, in spite of the recession.

Last September, the German electorate decided that even Steinbrück was too socialist, and so elected a coalition between Angela Merkel's Christian Democrats and the Free Democrats, a free-market party that is even more opposed to public spending than Merkel. The effect of this has been to push Germany even more firmly into the fiscal-retrenchment camp - the German parliament lopped an extra 5.8 billion euros (\$8 billion) off public spending before finalizing the 2010 budget - no pork barrel waste there!

The result has been a very brisk economic recovery, with no inflation and no significant risk of "crowding out" the private sector. Manufacturing orders were up a strong 4.3% in January, far more than had been expected, and are now 19.6% ahead of where they were a year ago. Unemployment is 8.2%, well below the U.S. level, while Germany's current-account surplus is a massive 5.2% of GDP.

With competitive manufacturing, a business-friendly government and plenty of domestic capital, Germany is about as healthy an economy as there is in the world today and is thoroughly underrated by U.S. and British analysts. Its stock market is trading at a fairly demanding 19.7 times earnings, according to *The Financial Times* database. But that's lower than the U.S. market multiple of 21.0 times earnings. And Germany has better near-term prospects.

You should think about owning some of Germany's promise, even if it's only through the iShares MSCI Germany Index Fund ETF (NYSE: EWG).

Chile: The World's Shrewdest Government

As we noted at the outset, three powerful investment trends will separate the winners from the losers in the post-financial crisis new economic reality:

- The countries that were stingy with their monetary and fiscal bailout plans will now reap the benefits; they will outpace the countries that slashed their interest rates to zero and allowed their deficits to soar.
- Emerging economies will outgrow their richer, more-mature counterparts.
- Global commodities prices will continue to move higher.

One country is poised to profit from all three of those trends. What's more, the political worries that always seem to diminish its allure to investors are ready to recede, making this emerging-southern-hemisphere heavyweight one of the premiere profit opportunities for 2010.

We're talking about Chile.

Political Changes Pack a Profit Punch

The politics are the most recent development. Chile held the first round of its presidential election on Dec. 13, and right-wing candidate Sebastian Piñera won 44% of the vote. More importantly, the two furthest-left candidates were knocked out, meaning the Jan. 17 run-off was between the conservative Piñera and the center-left Eduardo Frei.

Piñera ended up as the winner: He vowed to promise a tough law-and-order program and vowed to use his business know-how to boost the economy. He also promised to continue some of the popular social programs of outgoing President Michelle Bachelet. So Chile's politics are likely to become at least mildly more pro-business and possibly much more so.

Since the country - even under President Bachelet - was already the best-run country in Latin America (you can sensibly argue for Alvaro Uribe's Colombia, but not really Luiz Inácio Lula da Silva's Brazil when you look closely), that's really very good news, indeed.

But here's the real kicker: If just a few other factors shift from neutral to favorable, it could lead to some stellar growth as global investors choose Chile as their Latin American base.

The World's Shrewdest Government?

Chile is the world's largest producer of copper, accounting for a full third - and perhaps a bit more - of the world's total output. Since the price of copper zoomed more than 100% in 2009, that translated into a strong year for Chile.

A year ago, the spot price of copper was just over \$2 a pound. Prices soared to better than \$3.50 a pound in April and fallen back a bit since - but only to about \$3.20 a pound. That's still well above where the price was a year ago.

Naturally, Chile's dominance in copper makes the country vulnerable if copper prices drop. So during the years of boom and high copper prices before 2008, the country and its leadership shrewdly and wisely created a "rainy day" fund it could use when copper prices slump.

That fund is worth \$19.5 billion - the equivalent of 10.5% of Chile's gross domestic product (GDP). And it's already paying dividends.

In the last quarter of 2008 copper prices dropped, so Chile undertook a “stimulus” of 2.5% of GDP - an easily affordable bargain under the circumstances. The budget deficit is 4% of GDP because of the recession, but that’s easy to deal with: Thanks to the forward-thinking, there’s no budget problem to speak of.

Chart III: Top Profit Plays for the Three “Must Invest” Markets

Country	Investment	Exchange/Ticker	Attraction
Singapore	iShares Trust MSCI Singapore Index ETF	NYSE: EWS	Net assets of \$1.6 billion, expense ratio only 0.55%.
Germany	iShares MSCI Germany Index Fund ETF	NYSE: EWG	Germany has better growth prospects than the U.S.
Chile	Banco de Chile SA	NYSE ADR: BCH	Chile’s largest bank, 4% dividend.
Chile	CorpBanca SA	NYSE ADR: BCA	Chile’s most-profitable bank, 3.5% dividend.
Chile	Lan Airlines SA	NYSE ADR: LFL	Chile’s remoteness favors airlines; nice dividend.
Chile	Vina Concha y Toro SA	NYSE ADR: VCO	4.4% dividend.

If only all the governments around the world were this shrewd...

After advancing at a 0.55% clip in 2009, Chilean GDP should accelerate to a healthy 3.5% clip in 2010, a team of forecasters assembled by *The Economist* predicted. And with copper prices still high, that prediction would well be low.

Chile is sitting in the exact sweet spot of the current global recovery, and is well worth some investment. Because of the country’s relative stability, however, the market is not especially cheap, trading at 17.6 times earnings. But it is cheaper than the U.S. Standard & Poor’s 500 Index, and its P/E of 21.0.

Despite its small size - or perhaps because of it - Chile has tried to be as open as possible to foreign investment capital. That’s been true since the 1980s, which is why there are more than a dozen Chilean stocks that trade on the New York Stock Exchange as American Depository Receipts (ADRs).

Let’s look at four with the best outlooks:

- **Banco de Chile SA** (NYSE ADR: BCH): Banco de Chile is the country’s largest bank. It is controlled by Quiñenco SA, part of the Luksic Group of companies, and has branches in Argentina, Brazil, Mexico and the United States. The company trades at 14 times projected 2009 earnings, with a dividend yield of 4.0%. Since Chile hasn’t had a deep recession, banking remains a good business, although 2009 earnings were down.
- **CorpBanca SA** (NYSE ADR: BCA): Although CorpBanca is the fifth-largest bank in Chile, it is consistently the most profitable. Currently, CorpBanca’s ADRs trade at only nine times earnings, and feature a dividend yield of 3.5%. Third-quarter earnings were up 8% from the second quarter, so the shares seem very reasonably priced.
- **Lan Airlines SA** (NYSE ADR: LFL): Normally we’d suggest you were mad to invest in an airline (a business that has lost money worldwide over the entire 106 years since the Wright Brothers first flew at Kitty Hawk). In the near term, LFL shares remain pricey, trading at 30 times prospective earnings. But while it’s been a tough year for the airline, LFL does make money. And here’s the long-term kicker: Chile’s long, thin shape, remoteness and abundance of mountains figures to make air travel both within the country – and abroad – a most profitable business. Add in a healthy business climate and a robust commodities market, and Chile will become a destination

spot for the global commodity “have nots.” The ADRs recently featured a 2.6% dividend yield.

- **Vina Concha y Toro SA** (NYSE ADR: VCO): We can’t help this one – we like the product. Vina Concha is Chile’s largest wine producer. Chile was the only country in the world whose grapes were not infected by the Great Phylloxera Blight of 1873. Therefore, wine snobs can claim that Chilean wines - being made with pre-Blight grapes - are the best in the world. The market seems to buy this sales pitch, since the stock trades at 20 times projected 2009 earnings. But the shares also feature a nice 4.4% dividend.

Editor’s Note: This report was researched and written by Martin O. Hutchinson, a contributing editor for both Money Morning and The Money Map Report. Hutchinson is also the editor of The Permanent Wealth Investor, an advisory service that invests in gold, commodities and high-powered, dividend-paying stocks. A former merchant banker with more than 25 years experience in both New York and London, Hutchinson has more recently emerged as an award-winning columnist and a recognized expert on the global financial crisis.

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