Q209 Outlook
The Long Journey Back

Monthly Market Update: Special Edition
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- Strong cyclical stock market rebound is likely on oversold conditions
  - o Don't chase stocks
  - o Expect multiple mini-rallies and corrections before a more sustained rebound unfolds
  - o Cost average buying of stocks on the dips
  - o Continue to favour Asia ex-Japan

- Large spreads and high yields on corporate and emerging market sovereign debt
  - o Favour investment grade corporate and quality EM sovereign debt for income and eventual spread compression

- Rebound in commodities on recovery of emerging market growth
  - o Oil likely to be a key beneficiary

- USD weakening from H209
  - o Diversify USD holdings
  - o Favour Asian currencies and major currencies unlikely to engage in quantitative easing e.g. the Aussie

- Long-term uptrend in gold on concerns over aggressive global monetary stimulus
  - o Gold as a long-term hedge against USD weakness and financial turmoil
  - o Buy on the dips

Summary

Value emerging amidst the uncertainties. The recent rebound in stocks, commodities and commodity currencies should be seen as a part of a base building process – a process that could extend into the second half of the year given the ongoing uncertainties in the global economy and financial markets. Markets for risk assets are likely to correct again before we see a more sustainable rebound. Nevertheless, we do see value emerging in a range of assets and currencies. And we recognise that equities and other risk assets typically bottom before the economy recovers. We continue to expect a bottoming of the global economy end 2009/early 2010.

Plenty of problems ahead but financial market stresses have eased. We are of the view – indeed, developments of the past quarter have reaffirmed our belief – that the peak of the financial crisis has past. This is not to say that the financial sector is on the road to a rapid recovery. With an estimated $4 trillion in losses lurking in financial institutions and only a bit more than $1 trillion of that booked, the financial sector has a long journey ahead before it approaches anything near normality. And this is not to rule out periodic bouts of risk aversion. But credit and money market spreads have traded relatively flat over recent months notwithstanding all the bad news emerging over that period. Yes, banks are still reluctant to lend and capital remains scarce and costly. But the global economy has pulled back from the edge of an uncontrolled collapse under the weight of totally dysfunctional financial markets. In that sense, it appears to have gone through the worst of the financial crisis and now has to work through the recession.

The recession is severe but that too will past. Asset markets are now struggling to work past possibly the most severe global recession since the Second World War. But even there, it appears that we are already at, if not past, the worst of the global economic downturn. There are still many downside risks. And it will take many more months before there is greater clarity on the very early signs of rebound in the data seen early this year. But on balance, we still expect the US economy to bottom and stage a modest rebound end of this year.

Asset markets are likely to rebound ahead of the end of what is likely to be a 2-year US recession. Asset markets around the world, from stocks to commodities, have been "base building" since October-November last year. This confidence building process – involving testing the lows at which buyers are prepared to emerge – is likely to continue for some months ahead as global economies work through the recession and the US government works through its financial rescue operations. But typically, equities markets rebound before the end of recessions. In the case of the US, going back to and including the Great Depression, the average recession-linked bear market rebounds some three and a half months before the economy recovers.

Stock valuations have fallen way below previous cyclical lows and expectations have been beaten down. Earnings expectations have collapsed around the world In the US, S&P estimates are pricing in 26% y/y contraction for S&P 500 Q109 operating earnings. Meanwhile, economists' expectations have been also been beaten down in line with the dreadful data. Economic surprise indices, which measure the balance between economic data exceeding market expectations versus economic data disappointing the consensus, hit a peak of disappointment late last year and have been recovering steadily over recent months. In the US, the balance is now in favour of data releases exceeding market consensus estimates.

Meanwhile, stock valuations in the US have been beaten down to levels significantly below previous cyclical bear markets. There had only been two episodes in over 100 years when the price to earnings (PE) valuation for US equities had fallen lower than where they are now – during the Great Depression and the 1970s stagflationary bear market. While this arguably could be the worst global recession since the Second World War, it is unlikely to be of the magnitude of the Great Depression when the US economy contracted 26% in four years. The key is in the greater size of government in the US economy today compared to the Great Depression and the far greater policy flexibility today. In the early 1980s, that crucial discounting factor for valuation – interest rates – hit extreme highs (the Fed funds rate peaked at over 20%). In the current crisis, policy rates have been cut around the world to or close to zero.

The base building process is likely to see further pullbacks but the equities markets may have already put in the cycle's lows. The aggressive gains from trough to recent highs have seen the S&P500 rise more than 31% and the MSCI Emerging Markets pick up 38%. Such gains are unlikely to be sustained in a straight line. There will be new rounds of concerns over the global economy and the financial sector. There will be corrections in response. But on balance, we suspect that the corrections are unlikely to see new lows.

Commodities are likely to recover in tandem with equities. Commodities have been trading in close correlation with equities since the middle of last year. They were part of the deflation/risk aversion trade when stocks were plummeting. Now, commodities are pinning their hopes on the emergence of a "reflation trade". And they are "base building" along with equities – attempting to find a sustainable bottom from which to stage cyclical rebounds. The markets have priced in a lot of demand weakness. Meanwhile, supply has been cut back significantly in many areas. Although there could be pull backs in prices in coming weeks – as a correction to the rapid gains of recent months – we believe that the markets have already put in the lows. Oil in particular looks attractive on any pull backs below $50. We expect another surge in prices as data comes in later this year confirming a bottoming out of emerging market demand, particularly in China.

Gold remains attractive on pullbacks as a hedge against USD weakness. In recent months, gold appeared to have broken its inverse correlation with the USD. That is, instead of weakening when the USD is strengthening, gold has been positively correlated against the USD since Q408. The common factor here is risk aversion. The USD tends to strengthen during times of recession and financial crisis – witness the 1980s and 2000-2002. Investors also have a tendency to head for gold during times of uncertainty, whether it is a financial or political crisis. But the markets in more recent months may have also started to buy ahead of imminent USD weakness. The recent pullback in gold prices on easing risk aversion offers investors yet another opportunity to buy gold at lower levels. Gold should trade higher later in the year and in coming years on renewed USD weakness.

While there could be a sell off in US Treasuries when recession and risk aversion ease, recession/deflation and Federal Reserve purchases are likely to support the market for now. G7 government bonds are trading at historically very low yields at the moment. And with that comes vulnerability when recession and risk aversion ease. But that appears unlikely anytime soon. Notwithstanding the talk about "green shoots" showing in the global economy, the risks are towards deflation rather than inflation over the next 12 months. And Federal Reserve buying is also likely to put a floor on the US Treasury market for now. US Treasuries continue to have a place in diversified portfolios for hedging purposes.

Investors with greater tolerance for risk should consider investment grade corporate bonds and better quality emerging market sovereigns. Policy rates remain high in selected emerging market economies, offering high yields for their sovereigns. The possibility of further rate cuts in the event of more economic weakness is another plus for the outlook for sovereigns at the short-end. Given the deflationary environment, rates are unlikely to tick up over the course of the year. Beyond 2009, when risk aversion eases, spread compression should also kick in to lift prices.

Investment strategy implications – continue cost averaging risky assets on the dips and maintain a long-term view on these assets. We continue to recommend investors with longer investment horizons to cost average a range of risk assets on the dips. Given our expectations of further base building – with repeated failed rallies and multiple retests of the lows – we won't chase the rallies, we would buy the dips. Reflecting the uncertainties at this base building stage, we continue to underweight equities and overweight cash on a 3-month basis. But we are also maintaining a neutral weighting for stocks in our 12-month tactical asset allocation model, signaling that we do believe there are opportunities for stocks and other risk assets for longer term investors.

The tactical asset allocations for Q209 are as follows:

Q2-09 tactical asset allocation summary

Asset/Market	3-month	12-month
Cash	**Overweight**	**Neutral**
Equities	**Underweight**	**Neutral**
North America	Underweight	Underweight
Europe	Underweight	Neutral
Japan	Underweight	Underweight
Emerging Markets	Underweight	Overweight
Asia ex-Japan	Underweight	Overweight
Bonds	**Neutral**	**Neutral**
Global	Neutral	Underweight
Emerging	Neutral	Overweight
Asia	Neutral	Overweight
Alternatives	**Underweight**	**Neutral**
Hedge funds	Underweight	Neutral
Commodities	Neutral	Neutral
Property	Neutral	Neutral

Global Economic Outlook

"Green shoots" or "false spring"? In the midst of another sharp downturn in stock markets in March, Federal Reserve Chairman Ben Bernanke spoke of evidence of "green shoots" of economic recovery – making them some of the most popular two words amongst the economic/market "commentariat" over recent weeks. And this is absolutely crucial to the discussion on financial and asset markets. If these very early and tentative upticks in the economic data are indeed "green shoots" of recovery, then a more sustained rebound in asset markets should not be too far away. But if the data reverses and continues on its downtrend, the prices for risk assets are likely to bump along at or around the bottom for a lot longer.

Data releases are still not good – just less bad. To keep things in perspective, a broad sweep of the economic data still makes depressing reading. The world remains in a deep, synchronized recession, with the structural problems of the English-speaking world and parts of the Euro zone spilling over to the exporter nations of the world – most notably Asia. What Mr. Bernanke and the market are presumably cheering is a collection of recent data points which are arguably "less bad".

For example, the February US durable goods orders grew 3.4% against the market expectation of a contraction of 2.5%. And US February home sales came out at 337,000 against the consensus of 300,000. US factory orders, the ISM manufacturing new orders index and retail sales also ticked up.

Hopes rest with success of government intervention. Governments all over the world are aggressively intervening on both fiscal and monetary fronts to cushion and shorten the economic downturn. The US, UK and Japan have pushed into "quantitative easing", buying credit securities and pumping credit into the hands of banks. The Federal Reserve has expanded bank credit from around $800 billion middle of last year to over $2 trillion end of last year. With the latest round of commitments to buy US Treasuries and Mortgage Backed Securities (MBS), the figure is likely to blow out to around $3 trillion. And it is not just in the US – money supply growth has surged throughout the developed world.

The most optimistic signals are coming out of China. Outside the US, data flowing out from China stood out in recent months in terms of early signs of possible recovery. The surge in money supply (M2 was up 19% y/y in January) appears to have flowed through to a sharp rise in lending (up 21% y/y in nominal terms in January). China's manufacturing PMI (purchasing managers' index) has been on an unbroken upturn from October of last year. And although industrial production eased slightly in March, after turning up from October last year, the growth rate was still encouraging, at 8.3% y/y. Although it came off from the 11% recorded the previous month, this was still higher than the consensus estimate of 6.3%. (Exhibit 1)

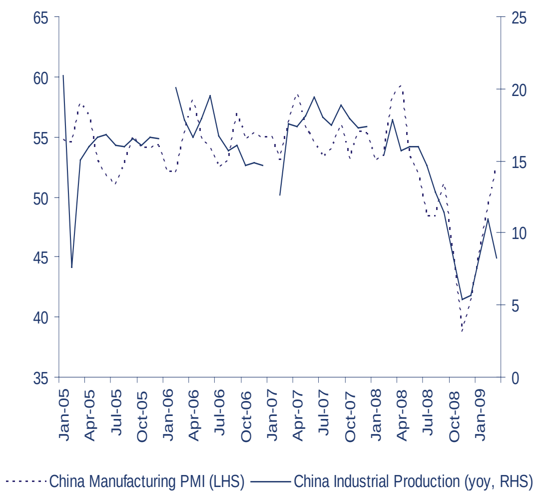
Part of the "base building" process. Economic data are still in that very tentative phase of attempting to find a bottom. The markets for risky assets have been "base building" for some time in anticipation of economic recovery. But as with the process in asset markets, a successful "base build" for global economies will likely be a prolonged and choppy affair. Indeed the burst of optimism over US economic data early in the year has now been followed by some disappointment over March figures.

For example, US housing starts and building permits ticked down again after February's surprise jump. March housing starts came in at 510,000 against an expected 540,000 and the previous month's 572,000 (downwardly revised from 583,000). Similarly, March building permits came in at 513,000 against the consensus expectation of 549,000 and the previous month's 564,000 (upwardly revised from 547,000). And headline retail sales came in -1.1% m/m in March, from the consensus estimate of 0.3% and the previous month's figure of 0.3% (upwardly revised from -0.1%). (Exhibit 2)

But eventually, the recession will end. Governments have aggressively raised expenditures. At some point, consumers will reach a point at which they won't or can't cut back any further on spending. And inventories are showing signs of bottoming, with restocking unavoidable even in this dismal environment. We expect the US economy to bottom Q309 and rebound Q409. And emerging market economies should generally start recovering around or slightly ahead of the US economic rebound.

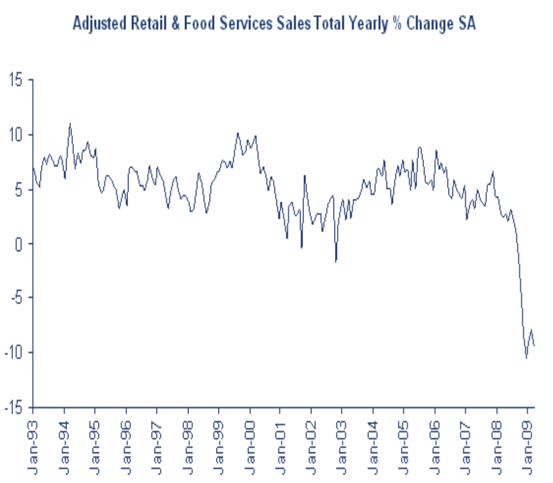
Beyond the rebound, a period of sluggish growth. However, the structural overhangs in the United States, the UK and parts of the Euro zone – from the property, credit and consumer bubbles – will combine with the "dead weight" from an estimated $4 trillion of troubled assets in the financial sector to limit the size the economic rebound around the world. US unemployment is set to surge to 10% and possibly a bit beyond that. Meanwhile, US house prices are likely to fall another 10-15% over the coming year. The erosion of household net worth and uncertainties of surging unemployment have already curbed consumption and forced US households to start saving more. Investors have to prepare themselves for a period of slower consumer expenditure growth off an already lowered base.

Exhibit 1: China's industrial production and PMI – on the mend



Source: Bloomberg

Exhibit 2: US retail sales – an example of the bumpy process of base building



Source: Bloomberg

Equities

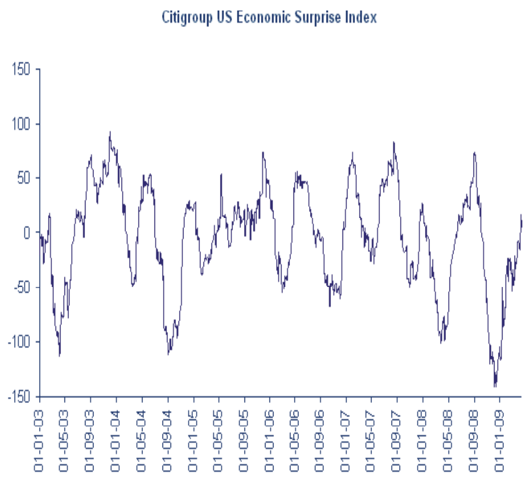
3M: Underweight
12M: Neutral

Indicators suggest equities may have past the point of maximum pessimism. Our call last quarter – that financial market stress had peaked – has been validated by subsequent developments on money and credit markets. Money market indicators such as the Libor-OIS and TED spreads have traded relatively flat even in the midst of the March sell off in stocks. Similarly, credit default swap spreads have traded largely sideways over recent months. The peaks of the post-Lehman period are unlikely to be repeated anytime soon. In the equities market, the S&P500 volatility index VIX also traded flat even while stocks were being aggressively dumped in March – suggesting a measure of calm had returned to the stock market.

Base building could continue for a few more months but the lows are likely to hold. Equities markets around the world have rebounded from their March lows. From the lows to the recent highs, the S&P500 had rebounded some 31% and the MSCI Emerging Markets put on some 37%. These are huge rebounds in a very short period of time. And with the ongoing stress tests on US banks, lagging economic data showing a deepening recession, and with huge uncertainties on the earnings front, this rebound is likely to correct again. There are likely to be several failed mini-rallies before a more sustainable rebound emerges. But we suspect that the lows will survive retests in coming weeks and months.

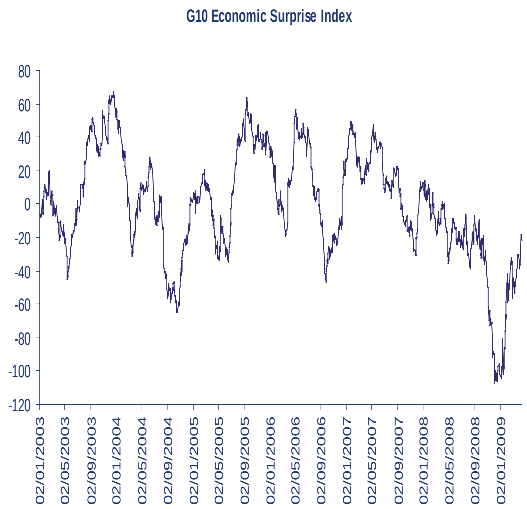
Disappointment over economic data has eased. The economic surprise indices for the US and the G7 – which measure the balance between economic data releases which exceeded the consensus versus those which came in worse than market expectations – bottomed late last year. And they have been turning up since then. That suggests that disappointment over economic data had peaked and is easing. Indeed, in the US, the balance has now turned in favour of data releases exceeding market expectations. (Exhibits 3, 4) So a lot of the bad news appears to have been factored into the market's calculations.

Exhibit 3: Balance of US data now in favour of upside surprises



Source: Bloomberg

Exhibit 4: G10 – data disappointment easing



Source: Bloomberg

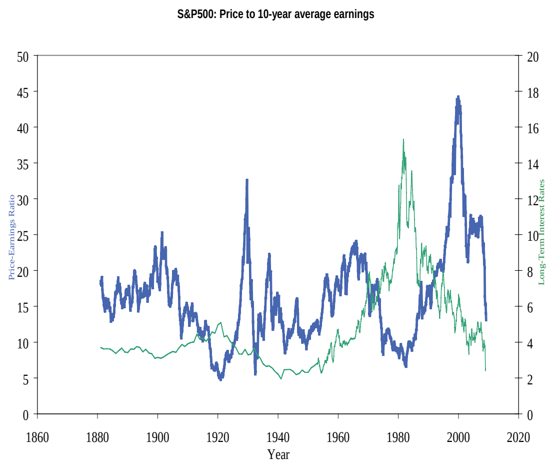
Earnings expectations have "capitulated". In stark contrast to the situation a year ago when analysts were still expecting some earnings resilience, forward earnings estimates have collapsed, with forecasts for the S&P500's Q109 operating earnings down 26% y/y.

Valuations have been severely compressed. As a result of collapsing historic earnings and forward earnings estimates, price to earnings ratios have been severely "compressed". Using both 1-year trailing and 10-year average earnings, there have only been two episodes over the last 100 years during which PE valuations have fallen significantly below where we are currently. That is, during the Great Depression and the stagflationary bear market of the 1970s and early 1980s. (Exhibit 5)

This is arguably the worst recession in post-War history but this is not a new Great Depression. The differences between the situation today and the conditions during the Great Depression are stark. During the Great Depression, the US economy shrank 26% over four years. This is equivalent to 7% contraction in the GDP over four consecutive years. And as bad as things have been, the US economy actually grew 1.1% last year and is likely to contract by around 3.4% in 2009. And of course, the US government contributes a lot more to GDP today than during the Great Depression – around one-third compared to 8% at the start of the Great Depression. Finally, the gold standard greatly constrained government monetary policy. Indeed, it resulted in higher government policy rates at a time when lower rates were required.

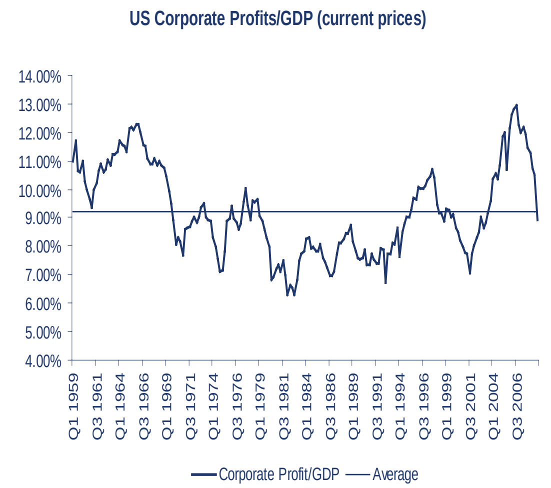
Why valuations should not dip to the levels of the late 1970s/early 1980s. The stagflationary 1970s resulted in then Federal Reserve Chairman Paul Volcker raising the policy rate to 20% by 1981. And along with that, market rates also soared. This is important because interest rates represent the opportunity cost of money and is the discount factor in valuation estimates. Today, the Fed's policy rate is effectively zero.

Exhibit 5: PE valuations have been lower only during the Great Depression and the 1970s/early 1980s stagflationary bear market



Source: Robert J. Shiller

Exhibit 6: Mean reversion in earnings likely to curb stock price gains



Source: Datastream

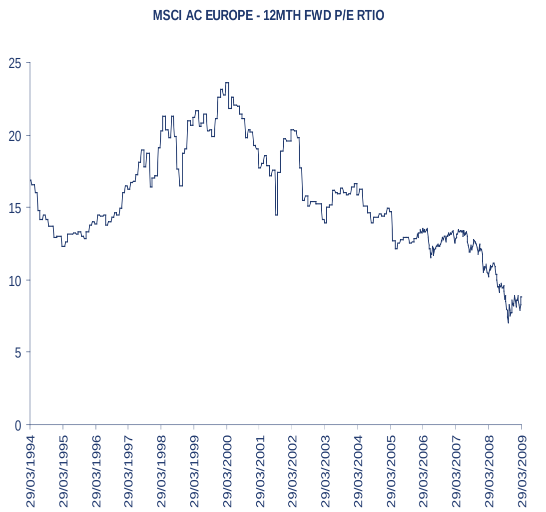
Money supply growth – a sea of liquidity behind a dam of fear? Money supply growth in the US has surged past previous cyclical peaks. This has not been limited to the US. In the G7, excess liquidity – defined as money supply growth over GDP growth – has also ticked up sharply in recent months. However, to date, this monetary expansion has yet to show up in bank lending. But all this liquidity should eventually flow over to more lending, greater economic activity, and higher asset prices.

US market will enjoy the rebound but longer term, suffer from structural overhangs. The US equities market – along with other global markets – is technically oversold. And the economy is likely to bottom out before year end and stage a modest recovery in Q409. Ahead of that, the US stock market is likely to rebound when there is greater visibility on earnings and financial institution stress.
But the structural overhangs from the property bubble, household debt, and financial institution balance sheet problems are likely to limit the market's relative performance. Property prices are likely to continue deflating until 2010, with further losses of around 15% quite possible. Unemployment could well surge past the previous cyclical peak of around 10%. As a result, the household savings rate is likely to continue to edge up, suggesting a muted recovery in consumer spending. There is also likely to be mean reversion in corporate earnings, which hit historic highs before the bursting of the credit bubble. (Exhibit 6)

Euro zone market is cheap by historical standards but it too will struggle with its own structural issues. Price to earnings valuations – both trailing and forward – have fallen to single digits in the European market. (Exhibit 7) Indeed, top to bottom, some Euro zone stock markets have fallen by levels that appear to be pricing a catastrophe – a new Great Depression rather than just a severe recession. MSCI Ireland fell 85% from 2007 peak to 2009 trough; MSCI Austria had fallen 79%; and MSCI Greece 74%.

Pan-European indices are registering trailing and forward PE ratios in the range of 8-10 times. They are on average trading with no premium over book value. The valuations reflect not just the economic outlook for 2009, which are just as grim in the Euro zone as they are in the US. They also appear to be pricing in structural issues peculiar to the Euro zone. Key among the issues is the structural rigidity of a single currency in a bloc which contains economies with vastly different characteristics. Equally, there are serious concerns over the loan exposures of Western European banks to emerging Europe which have been estimated in the region of $1 trillion.

Exhibit 7: Collapse of European share valuations



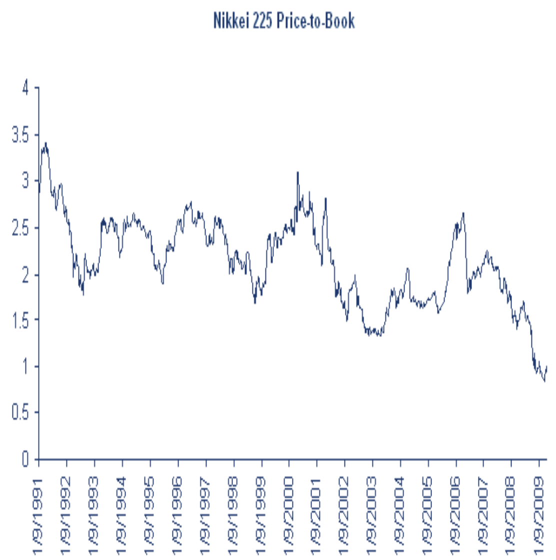
Source: Bloomberg

But the biggest Euro zone economies are in better shape than the US. Some Euro zone economies – for example Ireland, Greece and Spain – face a difficult period ahead unwinding their own "bubbles". They had enjoyed and are now paying the price of surging property prices, high inflation, strong wages growth, high household indebtedness (relative to disposable income) and large current account deficits. But the largest Euro zone economies Germany and France had not experienced similar "boom" conditions. Indeed, German property prices traded flat through the course of the past decade and actually fell in real terms at certain points. And they do not suffer the problems of high household indebtedness and current account deficits.

Japanese exports will eventually recover but the country's chronic demographic, domestic demand and cost competitiveness problems will limit its stock market's performance. Japanese economic data makes depressing reading. By February, the decline in exports peaked at around -50% y/y. Even with the slight "improvement" in March, the contraction continues at -46% y/y. And with that, industrial production has been falling over recent months by 30-40% y/y, investments have gone deeply negative and retail spending is also contracting. Indeed, the close correlation between the Nikkei 225 index with the USD/JPY is an eloquent statement of Japan's reliance on external demand and currency competitiveness for growth.

Nikkei is trading below book value. But even with these structural issues, there will be opportunities even in the Japanese market. Japanese equities are now trading on average below book value – something not seen even during the so-called "Lost Decade" following the bubble economy of 1986-1990. (Exhibit 8)

Exhibit 8: Nikkei trading below book value



Source: Bloomberg

Favour Asia ex-Japan within Emerging Markets for their stronger fundamentals. When the US economy stabilizes, it will be the emerging market economies, particularly Asia ex-Japan, which will recover faster. Asia ex-Japan enjoys stronger economic fundamentals – budget and current account surpluses or small deficits, large international reserves, and relatively low levels of household debt. Further, their financial systems have relatively low exposures to the troubled credit securities that are now weighing down US and European banks.

Asian economies with large domestic demand bases have been relatively resilient. The more export-dependent economies of Asia are in recession. But China, India and Indonesia – three economies with the same hallmark of having large sources of domestic demand – have been relatively resilient. India should turn in growth of around 5% this year and Indonesia should still achieve 4% expansion.

And while there are downside risks to our forecasts, we expect China on balance to emerge with 6.8% GDP growth for 2009. Indeed, the 6.1% y/y growth recorded by China in Q109 is likely to mark the bottom of the downturn for China. Commercial bank-financed infrastructure projects and government fiscal stimulus, and expansion of money supply have all helped. It is still early days but the upticks in a range of data/indicators are encouraging. They range from the manufacturing PMI (purchasing managers index) to industrial production to car sales. Even housing sales has just about stopped declining.

The China factor could benefit selected Asian economies. Although clearly China's consumption is too small to pull the world out of recession, its trade links with Asia should help boost regional economic activity when the global economic cycle turns. Hong Kong, Taiwan, and Singapore stand out as beneficiaries.

Can emerging markets outperform even while US equities struggle with structural overhangs? When the economies of the G7 stop contracting, it is likely that emerging market equities will outperform those of the high income countries. From 2000-2002, even while the US was in the midst of a recession and bear market, emerging markets' relative performance traded sideways. More importantly, their relative performance vis-à-vis the US bottomed out from their long period of underperformance from when the US economy and stockmarket were in boom and bull mode from 1995-2000. And on US economic recovery and USD weakening from 2002 onwards, emerging market equities greatly outperformed US stocks. (Exhibit 9) Once again, when the US economy stabilizes, we expect the USD to weaken. There is a strong possibility that emerging markets will then resume their outperformance.

Exhibit 9: Emerging markets to outperform on economic recovery and USD weakness?

Source: Bloomberg

Exhibit 10: Summary

Markets	3-month	12-month
North America	Underweight	Underweight
Europe	Underweight	Neutral
Japan	Underweight	Underweight
Emerging Markets	Underweight	Overweight
Asia ex-Japan	Underweight	Overweight

Country	Comments	Weighting
China	* Some positive economic data/indicators have emerged in the first quarter of this year, suggesting that the prompt implementation of fiscal stimulus is taking effect: i) Manufacturing PMI turned up for 4 consecutive months to Mar 09 into expansionary territory; ii) Fixed asset investment rose an average of 26.5% y/y in Jan and Feb, and 28.6% in Mar. iii) Industrial production rose 6.8% y/y in Mar, up from the 3.8% average in Jan/Feb. * Chinese banks largely unscathed by the credit crisis. Hence, despite the global credit crunch, domestic credit continued to register strong growth, averaging around 22% y/y in Jan and Feb and 29% in Mar 09. * Export contraction eased to -17.1% y/y from -25.7% y/y in Feb and an average of around -21% in Jan/Feb. * Government has reaffirmed its commitment to the target of 8% growth in 2009. While it may be a challenging target (SCB forecast: 6.8% growth in 2009), Premier Wen Jiabao has stated that China has the capacity for further stimulus to the economy and this could well occur if there is no clear sign of a pick-up in Q2. * There is room for further easing of monetary policy given that inflation has fallen off, with CPI and PPI rates at -1.2% and -6.0% y/y in Mar. SCB looks for another 81 bps to be taken off the 1-year loan rate, bringing it down to 4.5% from the current 5.31% by the end of the year. * Overall positive fundamentals suggest the outlook for Chinese equities is improving. * Downside risk is that the Shanghai Composite Index has picked up 33% year to 23 April and there could be some correction before a more sustainable rebound. * State-owned heavy industrial and construction firms are the main beneficiaries of the central government's stimulus package and there is still risk that companies outside this group may disappoint on the earnings front.	3M: Neutral (Neutral) 12M: Overweight (Overweight)
Hong Kong	* Exports fell 21.8% y/y in Jan and 23% y/y in Feb. Trade remains a large factor in the economy, with exports at 160% of GDP in 2008. *Re-exports dominate trade activities (97% of exports), with China (near 50% of re-exports), US and Japan being the top 3 trading partners * Given the outlook of depressed demand from developed economies near term, the export sector is likely to remain under substantial pressure in Q209. * SCB forecast is for GDP to contract 5.2% and 5% in Q109 and Q209 respectively. * Announced budget was generally viewed as conservative and with a longer term focus. Less spending was targeted at addressing the current crisis compared to regional peers such as Singapore. * But aggressive monetary easing from the Federal Reserve has depressed interest rates and induced strong liquidity growth in Hong Kong through the HKD-USD peg, creating a reflationary environment * We expect a weaker USD (and by extension a weaker HKD) moving into the year will benefit the export sector. * In the longer term, the economy has potential to benefit from a China-led recovery in Asia – through tourist arrivals and direct investments from China – once economic conditions in the developed world stabilize and move towards recovery.	3M: Neutral (Neutral) 12M: Neutral (Neutral)
Taiwan	* Economy is highly exposed to external demand – exports are 64% of 2008 GDP * With the collapse in external demand, the economic data has been dismal. Q408 GDP fell 8.36% y/y, the biggest decline on record, with exports contracting by over 40% y/y for each of the months of Dec 08 and Jan 09. * Signs of improvement were seen in Feb, with the decline in exports, export orders and industrial production easing to between -20% and -30% y/y from -40% and -50% in Jan (though the Lunar New Year holiday effect had inflated the improvements). *But it is clearly still too early to declare a recovery. Recent Mar export data had turned down again, contracting 35.7% y/y * Semi-conductor and electronic goods production turned and rose in Q109. * De-stocking of inventory in semi-conductor industry is well advanced and general market expectations are for some recovery in capacity utilization in the Taiwan tech sector in Q209, with some possibility of this performance continuing into Q309. * But much of the positive expectations for Q2 may have been priced in, with Taiwan equities posting one of the strongest year-to-date performances in Asia (TAIEX: +28% ytd as of 23 April). Rotational play out of Taiwan may result in less impressive relative performance this quarter. * But there are signs that the tech sector may have bottomed (e.g. the semi-conductor book-to-bill ratio had hit the previous 2001 low and rush orders were seen from China). Recovery, albeit at a slow pace, could sustain into H209 as the sharp plunge in capacity utilization rebounds to meet demand after inventories are worked through. * Inflationary pressures are also nearly non-existent, allowing the government to maintain a loose monetary policy stance. * Improving cross straits ties should be a medium/long term positive for domestic economy.	3M: Neutral (Neutral) 12M: Overweight (Overweight)

Note: Bracket denotes last quarter's weighting

Country	Comments	Weighting
Korea	* In line with its regional peers, Korean exports have also been severely impacted, with Jan-Feb combined exports around -26% y/y, with some bottoming seen on an easing of the decline to -21% yoy in Mar * As with Taiwan, production in the tech sector saw similar signs of rebound in Q109 (+21.8% m/m in Jan and +12.6% m/m in Feb) * The non-tech sector showed signs of a moderate rebound (from -4.0% m/m in Jan to + 4.4% m/m in Feb) * Consumption-related data also picked up in Feb (consumer goods sales were up 5.0% m/m). * An extra budget of 29 trillion won (3% of GDP) has been approved to be spent this year to shore up jobs and the economy * Export-related sectors should benefit from a weak won (relative to early 2008 levels) near term, suggesting a more positive outlook for the tech and industrials sectors * Concerns over Korea's short term foreign currency debt have eased from the earlier part of March and the point of maximum stress on its external payment situation has likely passed. The recent step-up in global efforts to contain the credit crisis and steps that Korea had taken to relieve its funding problems (e.g. the successful issuance of 3 billion USD in sovereign bonds) have reduced the risk of another market panic on such concerns. * Its improving current account position (+US$3.6 bn in Feb 09 from -US$1.7 bn in Jan 09 and -US$2.3 bn in Feb 08) is helping with sentiment as well. * But high household debt levels and a vulnerable housing market means continued downside risk to domestic spending. * SCB forecasts significant GDP contraction (-2.5% y/y for 2009) and this poses downside risks on earnings.	3M: Underweight (Underweight) 12M: Neutral (Neutral)
India	* There has been recent stabilization in economic and industrial production indicators such cement production and auto production but economic activity remains at depressed levels. * Weak external demand is expected to weigh on export-oriented production * A wide fiscal deficit (projected by government at 6% of GDP in 2009) means there is government limited fiscal capacity to boost demand, leaving the burden to monetary policy. * With some deflationary pressures looming, (the wholesale price inflation is currently below 0.5% and is expected to average negative over the next 6 months) there is room for more accommodative monetary policy – this will be beneficial for stocks. * Reverse repo and repo rates are expected to go down further to 3.0% and 4.0% respectively by mid-year. Policy ammunition is ample for more cuts if necessary. * RBI and government are facilitating financing for needy firms, relieving the pressure from the depressed offshore funding market. But credit flow to the real sector is far from the trend from recent years, with non-food credit growth at its lowest level since 2004. * The improving current account balance on lower oil import prices and resilient remittances should also be positive for the INR and sentiment on the domestic equity market. * However, the fiscal strains on India are likely to continue, with SCB projecting a fiscal deficit of 6.5% of GDP in 2009 and 6.3% in 2010 – a negative that the market may have not yet fully priced in. * Limited visibility on the outcome of the election in April/May – posing some political risk in the coming quarter.	3M: Underweight (Underweight) 12M: Overweight (Overweight)

Note: Bracket denotes last quarter's weighting

Standard Chartered

Country	Comments	Weighting
Indonesia	* Suffered less from the collapse in external demand compared to regional peers. Domestic consumption generates around 70% of GDP. * SCB is forecasting 2009 growth at 4.0%, down from 6.1% in 2008. * But it is still in that small, elite league of positive growth economies. * Payment position has been under pressure with its current account deteriorating as a result of the recent slump in exports and lower commodity prices, and with its capital account hit by de-leveraging flows and outflows from stock market. *Indonesia appears to have regained confidence in its financial markets which had suffered along with a rise in its sovereign CDS and a slump in the IDR – the currency has strengthened significantly recently. * Concerns over Indonesia's external liquidity position appears overdone and the current external debt position should still be comfortable. * As the financial crisis plays out over the course of the year, credit concerns should ease and portfolio capital flows should return – this will be positive for both the domestic equity market and the IDR. The IDR has already gained around 11% against the USD and the JCI has risen 18% ytd (as of 23 Apr). * Inflationary pressures are easing with Mar CPI at 7.92% from over 12% mid-2008. * More monetary policy easing is expected (to bottom at 7.0% in Q209 from 7.5% currently), but corresponding declines in the bank lending rate has not been forthcoming. * Onshore US liquidity remains somewhat tight, restricting corporate capital expenditure. * Fiscal policy still faces headwinds from cumbersome processes between central and regional governments and may limit the effectiveness of announced fiscal stimulus of around IDR 73 trillion (US$6.5 billion). * While political risk from the ongoing elections is perceived to be small, there is still the possibility of some uncertainty if Golkar forms an alliance with PDI-P to upstage President Yudhoyono despite his Demokrat party's lead in the vote count.	3M: Underweight (Underweight) 12M: Neutral (Neutral)
Thailand	* Political instability remains the key negative for the Thai stock market. * After a brief period of calm in the political environment following the formation of the Democrat Party-led government, demonstrations and even violent protests by pro-Thaksin supporters have broken out. * A state of emergency was declared recently in Bangkok and 5 cities around the capital, on violent unrest followed by an assassination attempt on one of the leaders of the anti-Thaksin movement. * Investor confidence is likely to be undermined by the repeated episodes of disruptive protests, and with no sign of a quick resolution to the core problems of class and region-based politics, constitutional change and the future shape of Thailand's political structure. * Thailand's export-led economy (exports are around 60% of GDP) has also been hit by the global downturn, with exports at -26.5% y/y in Jan and -11.3% y/y in Feb. * Thai banks have been conservative and are in comparatively healthy positions. But banks are maintaining a cautious lending stance due to the rise in non-performing loans and transmission of loose monetary policy appears hampered by the decline in personal and other loans. * Inflation is tame with the likelihood of the economy slipping into deflation in Q209 * Policy interest rate is expected to be lowered to 1.0% in Q209 from the current 1.5%. * In terms of valuation, the Stock Exchange of Thailand (SET) Index stands out with a price-to-book value of 1x. But its trailing PE of 12x is about average.	3M: Underweight (Underweight) 12M: Underweight (Underweight)
Malaysia	* Exports are under pressure from the collapse in external demand. Core exports include crude oil, palm oil and electronics. Jan exports were down 27.8% y/y and down 15.9% y/y in Feb. * But the overall impact of this external demand decline on growth is expected to be less than on countries such as Singapore and Hong Kong. * Domestic demand in Malaysia has been a more significant growth driver for the economy, given its larger population and infrastructure demands. But this segment will also see slower growth given stagnant income growth and a more cautious economic outlook. * The second fiscal stimulus of MYR 60 billion (to be spent over 2 years) is sizeable but it has raised concerns about the fiscal health of the country. * The fiscal deficit is expected to rise to 7.6% of GDP (from the government's previous expectation of 4.8% in Nov 08). The rise in the deficit should be manageable given the country's significant forex reserves and current account surplus. * But there are downside risks (i.e. lower than expected petroleum tax revenue and sluggish economic growth) and a surge in the deficit could risk a sovereign rating downgrade, dampening market sentiments. * The policy interest rate is expected to bottom at 1.5% from the current 2%. * The recent stabilization of commodity prices should be positive for exports and sentiment towards the stock market.	3M: Neutral (Neutral) 12M: Neutral (Neutral)

Note: Bracket denotes last quarter's weighting

Country	Comments	Weighting
Singapore	* One of the worst hit economies in Asia as a result of the collapse in external demand and global trade. But gradual improvements have been seen, with the contraction in non-oil domestic exports easing to -17% y/y in Mar from the Jan/Feb average of around -29%. Industrial production contraction eased to 22.4% y/y in Feb from -29.8% in Jan. * There has been substantial impact on the economy given that the exports-to-GDP ratio is around 185% and total trade amounts to around 350% of GDP. * A SGD 20.5 billion fiscal stimulus package should help support households and businesses but significant import leakage and the significance of external demand (which accounts for 75% of GDP growth) means substantial contraction is still likely this year. * The outlook for H109 remains poor, with growth expected at -11.5% y/y for Q109 and SCB's forecast is -9.9% for Q209. * The central bank re-centered the policy band for the SGD in April but retained a neutral stance on currency appreciation. * Valuation of the FSSTI is one of the lowest in the region in terms of trailing PE (9.3x) and book value of 1.1x. But its forward PE at 12 to 13x is about average relative to regional peers.* The stable political environment and its pro-active government remain core positives for the economy. * Performance has lagged other Asia ex-Japan markets year-to-date given the country's reliance on external demand for growth. Confirmation that global trade has stabilized in April/May data could lift sentiments towards the Singapore market.	3M: Neutral (Neutral) 12M: Neutral (Neutral)
Australia	* Australia is weathering the global financial crisis better than most developed economies, with the depreciation of the AUD cushioning the effects of the downturn. * It also has relatively more monetary policy ammunition, with its policy interest rate at 3% compared to zero or near zero levels in most other developed economies. * Further monetary easing is expected to bring the policy rate to 2.5% by mid-year. * Fiscal policy easing is also notable, with stimulus packages worth around 7% of GDP (AUD 44.7 billion announced Sep 08 and AUD 42 billion announced Feb 09). * Stabilizing commodity prices, signs of recovery in China and China's interest in resource assets should prove supportive of commodity-related stocks.	3M: Neutral (Neutral) 12M: Neutral (Neutral)
Saudi Arabia	* GDP growth, traditionally low for the MENA region, will slow to around 2% pa in 2009. * But oil prices have stabilised comfortably above government budget stress levels, and should rise further in the second half of 2009. * Slower GDP growth will also lower inflation; we forecast it down to 7% this year from 11% in 2008. * Valuations are reasonable rather than cheap; with a PE ratio of 13x, and a price-to-book of 1.6x. * A restricted market for outside-MENA investors.	3M: Underweight (Underweight) 12M: Neutral (Neutral)
Kuwait	* GDP growth is likely to slow to around 3% from 4% in 2008, but government support measures should prevent a hard-landing. * Oil prices should also be supportive. * Inflation as elsewhere is now slowing, whilst the government comfortably retains the financial resources to support the economy, as well as any major company that gets into trouble. * Kuwait has an FX rate that is more flexible than elsewhere in the Gulf region. * The market's dividend yield is high at 5-6% but valuations are far above the regional average – at a PE ratio of 30x.	3M: Neutral (Neutral) 12M: Neutral (Neutral)
UAE	* Oil prices should continue to rise and government fiscal and liquidity supports should lift the non-oil sector from the second half of 2009. * Dubai property prices are likely to fall further but supply restrictions and Abu Dhabi financial support should avert major problems amongst the banks and real estate developers. * GDP growth is forecast to slow to 0.0-1.0% pa in 2009 from 2008's 7.4%. But this will at least bring a big drop in inflation; down to 2-3% pa from 20%. * Valuations are low - a PE ratio of 5x in Dubai and 7x in Abu Dhabi. The price-to-book ratio in Dubai is 0.7x and 1.2x in Abu Dhabi.	3M: Neutral (Neutral) 12M: Neutral (Neutral)
Brazil	* Economic growth will slow sharply in 2009. * But the banking system is strong and a Fed swap facility should avert any further liquidity strains. * Monetary easing should continue, taking the policy interest rate down to 9.25% by end 2009, from 11.25% now. * Overall debt levels are sustainable and the FX rate should rise having fallen far. * It has been relatively insulated from the global recession, compared to the more export dependent economies of Asia, and higher commodity prices should further boost its outlook. * Valuations have moved up but remain reasonable – at a PE ratio of 14x, a price-to-book of 1.5x.	3M: Underweight (Underweight) 12M: Neutral (Neutral)

Note: Bracket denotes last quarter's weighting

Country	Comments	Weighting
Mexico	* The economy will suffer recession in 2009, with GDP likely to contract 1-2% after climbing 1.3% in 2008. * Inflation is sticky and the central bank is more cautious on rate cuts than is the case elsewhere in LATAM. * But Mexico has more scope, if needed, to ease fiscal policy to help its economy than is the case in Brazil. * The FX rate has fallen far and, we expect, should rise. * Corporate earnings are well-supported by low debt levels and large cash cushions. * Valuations are reasonable rather than low – at a PE ratio of 13x, a price-to-book of 2.0x.	3M: Underweight (Underweight) 12M: Neutral (Neutral)
Argentina	* A severe economic downturn is underway. * High debt levels and high inflation limit the scope to credibly ease fiscal and monetary policies. * The history of default and government intervention continues to limit foreign support. * Commodity prices should improve further during 2009, but domestic political uncertainties will climb as well with key mid-term elections set for the second half of this year. * Valuations are very low, with a PE ratio of 6x, a price-to-book of 0.7x. But the risks are high.	3M: Underweight (Underweight) 12M: Underweight (Underweight)
Russia	* Banking sector consolidation is underway but it could be messy. * There are continued corporate governance issues which will hold back foreign investment. * The economy is likely to suffer recession in 2009 but inflation and interest rates look set to stay relatively high. * Firmer commodity prices should help over the next 12 months but net exports are a small part of Russia's overall economy. * The authorities should be able to hold the rouble relatively stable but further devaluation is a risk. Devaluation would lift inflation even more, and stress corporates which face large foreign debt repayments. * But valuations are very low – a PE ratio of 4x and a price-to-book of 0.7x .	3M: Neutral (Neutral) 12M: Overweight (Overweight)
Turkey	* The economy will suffer recession this year, and recovery, likely from late 2009, will probably be sluggish. * Inflation and interest rates should fall further over the next few months but will bottom out at relatively high levels; inflation around 6-7% and rates around 10%. * Politics remain potentially volatile but should stay generally stable. * An IMF agreement is close and should bring fiscal policy back on track. * The external deficit is narrowing sharply and foreign financing needs look manageable. * The lira should rally provided global risk appetite continues to improve. * Valuations are low – a PE ratio of 7x and a price-to-book of 0.9x.	3M: Underweight (Underweight) 12M: Neutral (Neutral)
Hungary	* The economy is adjusting the painful way to the bursting of credit and asset price "bubbles"; via deep recession, large currency devaluation, and sharply higher unemployment. * The FX rate crash has lifted the foreign debt burden and Hungary's work-out is likely to be prolonged. * The recession is unlikely to lift before end-2009 and any recovery in 2010 will likely to very sluggish. * But the IMF is providing support. * Hungry is unlikely to lead the regional recovery. * Valuations, appropriately, are still low – the PE ratio is 5x and price-to-book is 0.8x.	3M: Underweight (Underweight) 12M: Neutral (Neutral)

Note: Bracket denotes last quarter's weighting

Global Bonds
3M: Neutral
12M: Neutral

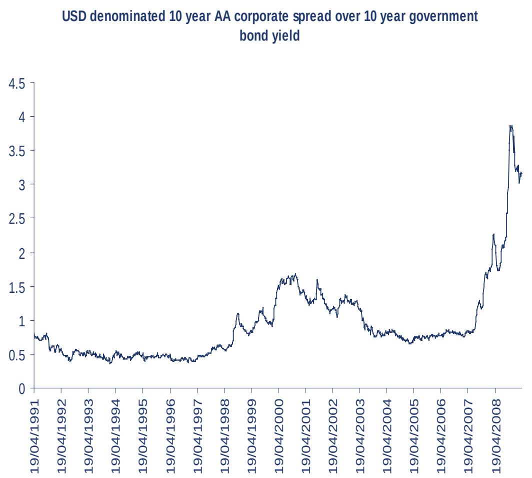
Low inflation should support government bonds for a few more months. Despite market worries over the massive increase in debt issuance, and the occasional bond auction "failure" in Europe, government debt markets rallied in Q1 2009 on safe-haven buying, falling inflation, and as Central Banks cut official rates close to zero. In addition, central banks in the US and UK have also started to buy government debt as part of "quantitative easing" programmes. The rally is well-advanced but probably still has further to go. Headline inflation in the US and Europe is likely to turn negative during the second half of 2009 as rising unemployment hits wages and recessions open up more excess capacity, which will further curb corporate pricing power. In addition, dysfunctional banking systems mean that it will take quite some time before quantitative easing threatens an imminent inflation pick up. Yield curves should also flatten further over the next three months as shorter duration rates stay low and longer duration bond yields move down.

Government bonds will sell-off when economic recovery kicks in. Deflation should be temporary and will eventually be replaced by renewed inflation worries. Investors are also likely to switch to riskier assets, curbing safe-haven inflows. In addition, worries over debt issuance will linger and will eventually pull yields higher especially when government buying tapers off. The weak economic recoveries we expect in the US, Europe, and Japan will mean that the fiscal deficits opened up by all the recent stimulus programmes and bank rescue packages will take a long time to work down. Finally, once the credit markets are clearly functioning better, central banks will be more pro-active in lifting policy interest rates than was the case in the early phase of previous economic upswings to ensure that asset market "bubbles" and unacceptably high inflation do not develop quickly.

The emerging debt rally should continue. USD sovereign debt spreads narrowed in Q1 2009, as emerging equities rose and as low interest rates in the US and Europe encouraged investors to stretch for yield. We expect emerging debt to perform well over the next 12 months. Capital inflows have crashed and all the key emerging markets are either in severe economic slowdowns or recessions. As a result, credit rating downgrades remain a threat. But yield spreads remain wide and probably discount too pessimistic an outlook for the key borrowers. The key countries have lower foreign debt burdens than was the case in the 1990s, lower foreign financing needs, and better macro-economic management. This is particularly true in emerging Asia. We also expect that commodity prices will continue to improve. In addition, most countries retain sufficient domestic policy flexibility, or will get external help (from the IMF etc), to avoid major debt servicing problems even if 2009 turns out to be even more difficult than we expect. But of course, there will be big variations in country performances and risks. Emerging Europe, which needs to work through the bursting of asset price and credit bubbles, and where foreign financing needs are large, will underperform. Those countries where debt burdens remain high and where economic policies are still poor (e.g. Ecuador, Ukraine) will also underperform. But there are opportunities in countries with generally sound economies and interest rate/spread downside possibilities – they include Brazil, the Philippines and Indonesia. Local currency emerging sovereign debt is another opportunity as Asian and emerging currencies appreciate against the US dollar over the second half of 2009 and as risk appetite improves.

There are also opportunities in investment grade corporate debt. Investment grade corporate debt and high yield (non-investment grade) debt sold off in March but rose in Q1 2009 as a whole. Investors, given the very low US Treasury yields, have become more prepared to take on some credit risk in return for potentially higher returns. We expect that corporate debt spreads will continue to decline, lifting prices. But investors should be selective as recessions continue and as bank lending even for creditworthy borrowers remains constrained. Investment grade bonds are likely to outperform near term. (Exhibit 11) High yielders remain high risk propositions but could do better when economies and financial markets recover. But note that ratings agencies expect the default rate for high yielders to reach 15-20% in 2009-2010 – levels last seen in the 1930s Great Depression. This compares with a default rate in the 5-6% region currently. (Exhibit 12) But even with investment grade corporate debt, the default rate is expected to hit 8%.

Exhibit 11: Investment grade corporate bonds offer long-term opportunities as spreads narrow



Source: Bloomberg

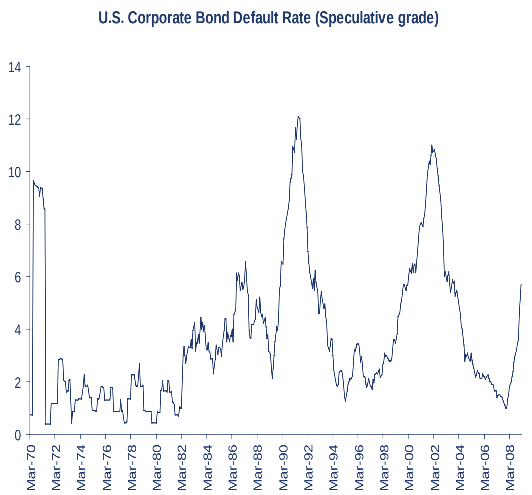
Commodities

3M: Neutral
12M: Neutral

The reflation trade – betting on global economic recovery. From an overshoot early last year – even while stocks were already correcting sharply– commodities traded in tight correlation with equities from July to November 2008. They crashed in tandem. But they are both now "base building" – trading sideways – awaiting signs of an end to the global recession and the return of the so-called "reflation trade".

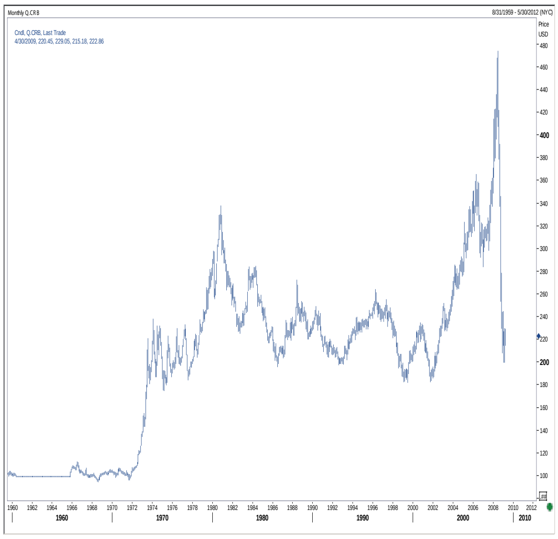
Collapse in commodity prices has discounted a lot of bad news. While we can never know when markets fully price in all the bad news – not least because there are many events which are not easily given to analysis – it is worth noting that the CRB Index has already fallen some 58% in just six months from its 2008 peak. It has corrected deeper than equities in a much shorter space of time. Indeed, this was the most severe correction in the four-decade history of the CRB index. (Exhibit 13)

Exhibit 12: Non-investment grade bond defaults are likely to surge way past previous cyclical highs



Source: Datastream

Exhibit 13: CRB Index – sharp decline has priced in a severe recession



Source: Thomson Reuters

Market has responded to the price signals and supply has been cut back. Both metals and oil producers have responded to the sharp decline in prices by cutting back supply. Most of the demand weakness appears to have been reflected in both the price and in supply responses. And going forward, we expect the sideways trading typical of the base building phase is likely to continue as markets are buffeted between the stronger economic data coming out from China and the likelihood of disappointment over the so-called signs of “green shoots” emerging from the high income economies of US, UK, Euro zone and Japan. But on balance, the aggressive fiscal and monetary stimulus pursued around the world should deliver a modest recovery late this year. And we expect commodities – along with equities – to recover ahead of that.

Metal prices to push higher after some consolidation – the cyclical lows are unlikely to be revisited. Base metals bounced in March and April, broadly in tandem with equities as risk appetites recovered. Apart from sentiment and financial flows, there were also fundamentals behind the move – supply has been cut back significantly, the PMI and industrial production data in China have been steadily improving, and there had been restocking in China. But prices could correct again, along with equities weakness and renewed risk aversion, before a more sustained rally emerges.

Oil is likely to have past the cycle low. Oil prices have rebounded strongly from the lows of around $35/barrel. Indeed, prices have been trading on a gentle upward trend in recent months, with higher highs and lows forming. Barring another major systemic shock, oil is unlikely to revisit the cycle lows again. The demand data is clearly awful. For example, China’s net crude imports had fallen by as much as 22% y/y. But on the other side of the equation, supply has also been cut. OPEC has cut supply by 13% from last July while non-OPEC output is expected to remain flat y/y. And even more importantly, much of the demand weakness appears to have already been reflected in the price. With some rebound in global growth likely late in the year and against the strong possibility of renewed USD weakness, oil should put on further gains in coming months.

Gold remains a valid hedge against crisis and USD weakness. Since November last year, gold appeared to have diverged from its negative correlation against the USD. That is, it had been going up together with the USD from November 2008 to March this year. An obvious reason for this is safe haven flows. That is, funds have been flowing into both the USD and gold on risk aversion. But there might also have been an element of the market for gold moving ahead of and in anticipation of a weaker USD in the second half of the year. Given the huge amount of monetary stimulus and quantitative easing in the US, it is difficult to see the fundamentals for sustained USD strength beyond this episode of risk aversion. On the dips, gold offers an investment opportunity for diversified portfolios.

Currencies

USD strength is unlikely to sustain – use the window of opportunity to diversify currency holdings. The amount of fiscal stimulus and quantitative easing undertaken by the Federal Reserve is likely to limit the extent of the cyclical rebound in the USD. To some extent, the rebound in the USD was not surprising – there was a cyclical element and a global deleveraging element in the strength of the USD seen since middle of last year. The USD has tended to do well during times of crisis, recession and financial stress. This happened during the Nasdaq crash/recession of 2000-2001 and the geopolitical crisis that followed September 11. (Exhibit 14)

The irony of USD strength in the midst of a US-centric crisis. In this particular episode, banks deleveraged, causing a shortage of US Dollars around the world. At the same time, fund managers sold out of risk assets everywhere around the world, resulting in financial flows back into USD. And risk-averse investors also rushed for US Treasuries, pushing the USD even higher. Note that we had been through, in recent years, a period of unprecedented corporate profitability in the US, suggesting there were huge amounts of funds in corporate treasury operations to be pulled back into the safety of US Treasuries when fear and crisis emerged.

Exhibit 14: The USD index (DXY) – strength in times of stress unlikely to sustain beyond the crisis

Source: Thomson Reuters

Near-term, the USD could make further gains. In Asia ex-Japan, the ongoing global recession is likely to put continued downside pressure on the currencies. Similarly, on another bout of risk aversion, U.K.'s ballooning public sector debt and the economic pain from ECB's reluctance to move into aggressive easing could reverse some of the gains made recently by the sterling and the euro. And fresh doubts over China's economic recovery and a correction in the commodities markets could force the Aussie dollar to retrace some of its strong gains off the year's lows.

But the many and serious structural problems will limit the USD rebound. Beyond this period of global deleveraging, risk aversion and safe haven flows, the fundamentals facing the USD are grim. The structural overhangs are many and serious. They include the impact on household wealth from the bursting of the housing bubble, the likelihood of structurally higher unemployment going forward, the likely long-term reversal of the household savings rate, the impact of massive government spending on the twin deficits, and the zero policy rates. These will all weigh heavily on the USD. Indeed, they are likely to limit the size of the rebound in the USD compared to what was seen in 2000-2002. Certainly, there is little possibility of a re-run of the early 1980s – US interest rates were then extremely high with the policy rate peaking at around 20%.

Asia ex-Japan (AXJ) currencies are likely to rebound when fund flows return to the region. AXJ currencies are so-called "cyclical currencies" – tending to do well in times of economic expansion and poorly in downturns. While the year-to-date data shows that institutional investors have been net sellers of the Asia ex-Japan equities markets, this is likely to quickly reverse when risk aversion eases. Indeed, in recent weeks, we have seen outperformance from the emerging markets off the March lows. We expect outperformance from emerging, particularly Asia ex-Japan, stock markets over the course of the next 12 months. On that, the money flows are likely to return, boosting AXJ currencies against the USD.

FX Forecasts

Note: Forecasts are valid as of 24 Apr 2009

	Q1-09a	Q2-09f	Q3-09f	Q4-09f	Q1-10f	Q2-10f	2008a	2009f	2010f
Majors									
Europe	1.33	1.45	1.50	1.55	1.50	1.46	1.40	1.55	1.49
Japan	97.3	93.0	92.0	88.0	95.0	101.0	90.6	88.0	105.0
UK	1.43	1.45	1.48	1.63	1.62	1.60	1.46	1.63	1.67
Canada	1.25	1.25	1.20	1.15	1.10	1.17	1.22	1.15	1.15
Switzerland	1.15	1.08	1.04	1.00	1.05	1.08	1.07	1.00	1.10
Australia	0.68	0.75	0.80	0.85	0.80	0.75	0.72	0.72	0.85
New Zealand	0.55	0.60	0.64	0.69	0.65	0.62	0.60	0.57	0.71
Asia									
China	6.83	6.85	6.87	6.86	6.85	6.82	6.82	6.86	6.70
Hong Kong	7.75	7.76	7.79	7.82	7.81	7.79	7.75	7.82	7.80
Indonesia	11700	11300	10500	9800	9300	9300	11120	9800	9100
India	49.72	50.00	49.00	48.00	47.00	45.50	50.50	47.00	43.50
Korea	1398.35	1300.00	1180.00	1150.00	1180.00	1110.00	1259.50	1150.00	1000.00
Malaysia	3.65	3.75	3.65	3.55	3.45	3.45	3.45	3.55	3.25
Philippines	48.17	48.00	46.50	45.00	44.50	45.50	46.45	45.00	43.00
Pakistan	80.52	80.00	81.00	82.00	84.00	86.00	77.80	82.00	87.80
Vietnam	17545	18000	18500	18500	18600	18100	17483	18500	17800
Singapore	1.52	1.52	1.48	1.45	1.44	1.40	1.43	1.48	1.34
Thailand	35.53	37.00	36.50	35.50	35.00	34.50	34.80	35.50	34.00
Taiwan	33.82	34.80	34.60	34.30	34.00	33.70	32.98	34.30	32.90
Other Emerging Markets									
Brazil	2.27	2.18	2.00	1.90	1.85	1.95	2.33	1.90	1.85
Mexico	14.26	14.00	13.20	12.50	11.40	12.20	13.40	12.50	11.75
Chile	582.98	550	540	525	490	510	633	525	480
Turkey	1.66	1.65	1.60	1.45	1.40	1.35	1.54	1.45	1.42
South Africa	9.61	9.20	8.90	9.10	9.30	8.50	10.00	9.10	9.10

Source: SCB Global Research

Government Bond Forecasts

Note: Forecasts are valid as of 2 April 2009

Country	Tenor	Q2-09f	Q3-09f	Q4-09f	Q1-10f
China	2-year	1.25	1.20	1.15	1.60
	5-year	2.70	2.80	2.80	3.00
	10-year	3.40	3.50	3.50	3.60
Hong Kong	2-year	0.90	1.30	1.60	1.80
	5-year	1.60	2.20	2.60	2.80
	10-year	2.00	2.40	2.80	3.10
India	2-year	5.00	5.00	5.00	5.25
	5-year	6.60	6.75	7.00	7.25
	10-year	6.85	7.00	7.25	7.75
Indonesia	3-year	9.50	8.75	8.50	8.75
	5-year	10.00	9.25	9.00	9.50
	10-year	11.50	10.50	10.25	10.50
Malaysia	3-year	2.20	2.30	2.30	2.50
	5-year	3.10	3.20	3.30	3.50
	10-year	3.60	3.65	3.75	4.00
Pakistan	3-year	13.00	12.50	12.00	12.20
	5-year	13.30	12.90	12.50	12.70
	10-year	13.50	13.30	12.90	13.10
Philippines	2-year	4.75	4.25	4.50	5.00
	5-year	5.50	5.00	5.50	6.00
	10-year	7.25	6.75	7.00	7.25
Singapore	2-year	0.70	0.90	1.10	1.30
	5-year	1.45	1.60	1.90	2.20
	10-year	2.05	2.30	2.60	2.90
South Korea	3-year	3.50	3.70	4.00	4.20
	5-year	4.30	4.50	4.70	4.90
	10-year	4.80	5.00	5.10	5.20
Taiwan	2-year	0.70	1.10	1.40	1.50
	5-year	1.35	1.60	1.80	2.00
	10-year	1.80	2.20	2.40	2.50
Thailand	2-year	1.20	1.40	1.80	2.10
	5-year	2.10	2.30	2.70	2.90
	10-year	3.40	3.50	3.80	4.00
United States	2-year	0.80	0.90	1.10	1.30
	5-year	1.60	1.75	2.00	2.30
	10-year	2.40	2.65	3.00	3.30
Vietnam	2-year	7.00	7.50	8.00	8.50
	5-year	7.20	7.80	8.50	9.00
	10-year	8.20	8.50	9.00	9.75

(End of period, % yield)

Source: SCB Global Research

Commodity Forecasts

Note: Forecasts are valid as of 23 April 2009

	Q1-09a	Q2-09f	Q3-09f	Q4-09f	2008a	2009f	2010f
Energy							
Crude oil (near future, USD/b)							
NYMEX WTI	43	50	60	70	100	56	80
ICE Brent	46	50	57	67	98	55	77
Dubai spot	44	48	55	65	94	53	75
Refined oil products							
Singapore fuel oil 180 (USD/t)	253	267	293	345	511	289	393
Singapore gasoil (USD/b)	53	56	65	80	119	64	91
Singapore jet kerosene (USD/b)	55	57	66	82	121	65	93
Singapore naphtha (USD/b)	45	49	55	66	88	54	76
Europe gasoil (USD/t)	420	447	514	596	917	494	687
Europe jet (USD/t)	446	467	549	660	997	530	758
Europe naphtha (USD/t)	381	427	498	592	788	475	685
Coal (USD/t)							
API4	68	60	70	75	121	68	88
API2	71	64	75	81	147	73	96
globalCOAL NEWC*	74	65	80	90	129	77	103
Metals							
Base metals (LME 3m, USD/tonne)							
Aluminium	1,403	1,450	1,500	1,550	2,619	1,476	1,750
Copper	3,488	3,800	3,400	3,500	6,876	3,547	4,000
Lead	1,170	1,200	1,100	1,200	2,092	1,167	1,238
Nickel	10,641	11,000	11,000	11,000	21,243	10,910	12,000
Tin	10,935	10,000	11,000	12,000	18,395	10,984	12,250
Zinc	1,208	1,250	1,200	1,300	1,902	1,239	1,325
Steel** (CRU assessment, USD/t)							
HRC, US	561	500	545	540	947	536	545
HRC, Europe	541	490	530	525	927	522	526
HRC, Japan	902	760	745	730	985	784	679
HRC, China	539	475	515	510	729	510	525
Precious metals (spot, USD/oz)							
Gold (spot)	909	925	975	1,050	872	965	1,100
Palladium (spot)	200	200	215	225	351	210	275
Platinum (spot)	1,026	1,100	1,050	1,100	1,574	1,069	1,200
Silver (spot)	12.65	12.50	12.60	12.70	14.97	12.60	13.00

*Forecasts are period averages; *weekly quote **monthly average*

Source: Bloomberg, Platts, CRU, SCB Global Research

Commodity Forecasts (cont'd)

Note: Forecasts are valid as of 23 April 2009

	Q1-09a	Q2-09f	Q3-09f	Q4-09f	2008a	2009f	2010f
Agricultural products							
Softs (near future)							
NYBOT cocoa, USD/tonne	2,556	2,600	2,700	2,650	2,556	2,627	2,850
LIFFE coffee, USD/tonne	1,588	1,700	1,700	1,725	2,144	1,678	1,689
NYBOT coffee, USc/lb	113	120	125	130	132	122	138
NYBOT sugar, USc/lb	12.7	14.5	15.0	15.0	12.1	14.3	15.0
Fibres							
Cotton (Cotlook A index, USC/lb)	54.8	60.0	62.0	65.0	71	60	75
Grains & oilseeds (nr future)							
CBOT corn (maize), USc/bushel	377	375	510	510	527	443	499
CBOT Soybeans, USc/bushel	944	1,000	1,015	1,150	1,233	1,027	1,208
CBOT wheat, USc/bushel	549	625	650	650	796	618	703
CBOT rice, USc/cwt	12.8	12.8	13.0	13.2	17.6	12.9	14.0
Thai B rice 100%, USD/tonne*	586	605	625	610	687	606	603
Edible oils (3m future)							
Palm oil (MDV,MYR/tonne)	1,892	2,000	2,250	2,500	2,840	2,161	3,125
Soyoil (CBOT, USc/lb)	33	38	40	40	52	38	47

*Forecasts are period averages; *weekly quote **monthly average*

Source: Bloomberg, Platts, CRU, SCB Global Research

SCB Tactical Asset Allocation Q2-09

3M Weighting					
	TAA Weighting	**Conservative**	**Moderate**	**Aggressive**	**Very Aggressive**
Cash	USD Cash	Over	Over	Over	Over
Bonds	Global Bonds	Neutral	Neutral	Neutral	Neutral
	Asia Bonds	Neutral	Neutral	Neutral	Neutral
	Emerging Market	Neutral	Neutral	Neutral	Neutral
Equities	North America Equities	Under	Under	Under	Under
	Europe Equities	Under	Under	Under	Under
	Japan Equities	Under	Under	Under	Under
	Asia ex-Japan Equities	Under	Under	Under	Under
	Emerging Market Equities	Under	Under	Under	Under
Alternatives	Funds of Hedge Funds	Under	Under	Under	Neutral
	Properties	Neutral	Neutral	Neutral	Neutral
	Commodities	Neutral	Neutral	Neutral	Neutral
Summary	**Total Cash**	Over	Over	Over	Over
	Total Bonds	Neutral	Neutral	Neutral	Neutral
	Total Equities	Under	Under	Under	Under
	Total Alternatives	Under	Under	Under	Neutral

Source: SCB Group Wealth Management

12M Weighting					
	TAA Weighting	**Conservative**	**Moderate**	**Aggressive**	**Very Aggressive**
Cash	USD Cash	Neutral	Neutral	Neutral	Neutral
Bonds	Global Bonds	Under	Under	Neutral	Neutral
	Asia Bonds	Over	Over	Neutral	Neutral
	Emerging Market	Over	Over	Neutral	Neutral
Equities	North America Equities	Under	Under	Under	Under
	Europe Equities	Neutral	Neutral	Neutral	Neutral
	Japan Equities	Under	Under	Under	Under
	Asia ex-Japan Equities	Over	Over	Over	Over
	Emerging Market Equities	Over	Over	Over	Over
Alternatives	Funds of Hedge Funds	Neutral	Neutral	Neutral	Neutral
	Properties	Neutral	Neutral	Neutral	Neutral
	Commodities	Neutral	Neutral	Neutral	Neutral
Summary	**Total Cash**	Neutral	Neutral	Neutral	Neutral
	Total Bonds	Neutral	Neutral	Neutral	Neutral
	Total Equities	Neutral	Neutral	Neutral	Neutral
	Total Alternatives	Neutral	Neutral	Neutral	Neutral

Source: SCB Group Wealth Management

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