August 2010

Global Investment Perspective

34° S - Buenos Aires, Argentina

IN THIS ISSUE

Highlights

In July, an encouraging start to the US earnings season and better-than-expected European bank stress test results offset concerns over moderating economic indicators. For example, of the 351 companies in the S&P 500 Index which have reported second quarter earnings as at 31 July, roughly 75% have surprised on the upside. Meanwhile, European bank stress test results showed that all but seven of the 91 banks passed the tests. These encouraging results helped to improve investor sentiment and global equity markets rebounded in July as a result.

However, the easing in US and China GDP growth rates in the second quarter of 2010, as well as some disappointing economic data in other parts of the world, is fuelling the belief that the recovery is still subject to strong headwinds. Of particular concern is the ongoing weakness in employment and consumption for developed economies. In recognition of the slowdown in momentum, many companies — such as Kellogg in the retail sector and Nissan and Hyundai in manufacturing — are now cutting sales forecasts. This underscores our concern that earnings growth forecasts for this year and next are still elevated and, combined with the mixed prospects for consumption in developed economies, this could lead to disappointment in companies' earnings growth.

July Market Recap

Both developed and emerging market equity markets rebounded in July. US equities rose by 7%, whilst emerging markets gained 6.2%. The fact that US companies continued to post strong earnings results in the second quarter was a key driver of the rebound. That said, there were other factors behind the market rally. First, the European bank stress test results were generally received positively by investors, and secondly, there were several successful auctions of government debt in Eurozone countries. Both these items helped to boost European markets, with the MSCI Eurozone index rising by about 6% in July.

Outlook & Strategy

Our central scenario remains unchanged overall. The global economic recovery is making progress, but economic conditions continue to be challenging and global growth uncertainties remain. From a macroeconomic perspective, we anticipate positive but moderate growth in developed economies while, in emerging economies, growth should remain stronger. However, there is still a risk from the impact of further monetary tightening in emerging economies and indicators have already started to show that the rate of economic expansion there is slowing. Adding to concerns over the strength of the economic recovery, several major developed countries have also announced tough measures of fiscal tightening. These could pose risks to the sustainability of the economic rebound.

At the asset class level, in equity markets, forecasts for 2010 and 2011 earnings growth remain on the high side. Given the weakness in consumption in developed countries, we continue to believe that these growth forecasts could prove difficult to achieve. Therefore, despite an improvement in valuations following the market correction in May and June, and support from low interest rates, we maintain our moderately cautious stance on equities versus cash in this environment. Furthermore, at the sector level, we retain our preference for defensive sectors, such as utilities and healthcare, over more cyclical sectors and financial stocks. In the current economic environment, the more stable earnings profile of defensive companies is attractive, and the discount to cyclical sectors remains favourable, even as the valuations of defensive sectors have normalised somewhat.

At a regional level for equities, we maintain our preference for Latin America over Emerging Asia. Valuations remain supportive, despite the narrowing of the valuation gap between the two regions. At a country level, we reiterate a preference for Russian equities over broader emerging market equities. The valuation for Russian equities is attractive in absolute and relative terms. Furthermore, domestic demand has shown encouraging signs of recovery, while Russian inflation remains contained. However, longer term constraints remain meaningful, such as the country's fiscal deficit. There have been proposed asset sales in ten major state-run companies to raise revenue to reduce the deficit, so the longer-term risk is that the corporate sector may be used to finance the country's high social expenditure. Nevertheless, despite these longer-term risks, we see Russian equities as an attractive tactical opportunity in the short term.

In fixed income, with inflation under control in the developed world, central banks are likely to keep interest rates low, which is broadly supportive for fixed income markets. Within the asset class, we maintain our preference for developed market corporate bonds, as we see value on a total-return basis.

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Short-term Investment Outlook (6 - 12 months)

	ASSET CLASS	CURRENT VIEW	REASONING
EQUITY	Global Developed Market Equity	Neutral	• Despite some improvement over the recent months, valuation levels are not sending any strong signals. The outlook remains mixed with ongoing risks to growth on the one hand, and the support from interest rates, likely to stay low, on the other hand.
	US Equity	Neutral	• US economic activity is positive, but the pace of improvement is slowing down, while the risk from weak consumption and high unemployment persists. As such, the sustainability of US economic growth is in doubt.
	Europe Equity (including the UK)	Neutral	• While market liquidity support remains strong, high levels of unemployment, sovereign debt issues and potential reduction of economic stimulus in Europe add risk to the outlook for economic growth and corporate earnings.
	Japan Equity	Neutral	• Further JPY strength would add to Japan's deflation pressure, despite ongoing improvement in manufacturing and trade and low interest rates.
	Asia ex-Japan Equity	Neutral	• From a macroeconomic perspective, the outlook remains generally positive with strong performance in both manufacturing and consumer sectors. However, from a valuation perspective, market prices have largely reflected the positive news flow.
	Global Emerging Markets	Neutral	• Emerging markets are likely to continue to lead the recovery due to robust domestic consumption and strong intra-regional trade. That said, like developed markets, emerging market equities are exposed to the volatility stemming from the question marks around the sustainability of the global economic recovery.
	Latin America Equity	Positive	• Economic data remains strong in the region and there is the potential for positive surprises, especially from Brazil. Although the valuation discount to Emerging Asia has narrowed, it remains supportive on the whole.
	Middle East Equity	Neutral	• Economic data from the region has been highly encouraging and 2010-2011 forecasts are positive. In addition, valuations remain reasonable. Key risks include a slow down in US demand for oil and the potential deterioration of budget deficits among some of the countries in the region.
	Eastern Europe Equity	Neutral	• Similar to other emerging markets, manufacturing data has been encouraging. That said, weak labour market conditions, high levels of government debt and ongoing turmoil in Western European markets are weighing on the outlook for the broader region. However, at a country level, we have a preference for Russian equities on valuation grounds. Specifically, the valuation for Russian equities is attractive in both absolute and relative terms.
	Indonesia	Neutral	• Expectation of faster economic growth and stronger corporate earnings growth this year, may drive investors to continue accumulate local equities and may help the market to weather negative sentiment from rising pessimism on major economies recovery pace.
FIXED INCOME	US government bonds	Negative	• Despite heavy supply, macroeconomic headwinds have kept the demand for US government bonds fairly buoyant. However, within fixed income assets, we prefer to own corporate debt, where we see greater total return opportunities.
	EUR government bonds	Negative	• Sovereign risk and the impact of the deteriorating credit quality of several Southern European countries are likely to continue to generate volatility for this asset class. Overall, within fixed income, given the exceptionally low yields offered by government bonds, our preference remains for corporate debt on valuation grounds.
	Investment Grade Corporate	Positive	• Strong earnings results and a view that the major central banks will keep interest rates low for longer have seen demand for investment grade corporate bonds remain fairly robust.
	High Yield	Positive	• Given the recent volatility seen in other riskier asset classes, high-yield bonds continue to look attractive on a total-return basis.
	Sovereign USD-denominated Emerging Markets Debt	Negative	• Sovereign emerging market debt continues to look less attractive than high-yield corporate debt on valuation grounds. Whilst not directly involved, emerging market debt could suffer if the situation worsens in the Eurozone.
	Global Inflation-linked Bonds	Negative	• With break-even inflation levels up significantly since early 2009, the case for global developed inflation-linked bonds is less compelling than a year ago, from a valuation perspective. Therefore, we recommend a moderately negative allocation versus nominal bonds.

Short-term Investment Outlook (6 - 12 months)

	ASSET CLASS	CURRENT VIEW	REASONING
FIXED INCOME	Indonesia	Positive	• Highest yield among Asian government bonds, strong and stable rupiah, and expectation of positive fundamental outlook, all may drive demand for local bonds to rise further and support the market.
OTHER INVESTMENTS	Oil	Range of between US$65 - US$85 per barrel	• We expect the oil price to keep fluctuating in the US$65-US$85 range, as improved demand is balanced out by the clouded economic growth outlook. Fluctuation in risk appetite will also contribute to oil price volatility.
	Gold	Neutral Range of between US$1,000 - US$1,200 per troy ounce	• Inflation pressure and concern over the USD as a reserve currency make gold an investable long-term theme. But in the near term, the gold price could be constrained by relative USD strength and supply concerns as the IMF intends to sell some of its gold reserves.
	Commercial Real Estate	Neutral	• High unemployment, falling occupancy rates and declining rental values in the US and Europe warrant a cautious/ negative outlook for these two markets in general. But, within Europe, we have a positive view on the UK relative to other direct markets due to the increase in investors' interest in UK properties and the lack of quality supply. The outlook for Asia Pacific is improving, although there is regional divergence and concern that price bubbles could be forming in markets like Hong Kong and China.
CURRENCY	Rp vs US$	Positive	• Positive fundamental background and high yield/return offered by Indonesian assets, may drive overseas investors to continue accumulating Indonesian equities and bonds, providing support to rupiah. • The euro is susceptible to both positive and negative surprises depending on how the resolution of the 'PIGS' (Portugal, Italy, Greece, Spain) fiscal difficulties unfolds. Valuation indicators are not sending any signals at present so, in the short term, we recommend a neutral EUR position overall. The GBP is also susceptible to event risk from the resolution of the UK's budget deficit.
	EUR vs US$	Neutral	
	GBP vs US$	Neutral	
	JPY vs US$	Neutral	

Summary

In developed market equities, we maintain our preference for defensive sectors, such as healthcare and telecommunication services, over financial stocks and cyclical sectors. At the regional level, we maintain our preference for Latin America over Emerging Asia, although the valuation gap between the regions has narrowed. At a country level, we have a preference for Russian equities over broader emerging market equities. The valuation for Russian equities is attractive in absolute and relative terms. Furthermore, domestic demand has improved, while Russian inflation remains contained. However, longer term constraints remain meaningful, such as the country's fiscal deficit. There have been proposed asset sales in ten major state-run companies to raise revenue to reduce the deficit, so the longer-term risk is that the corporate sector may be used to finance the country's high social expenditure. Nevertheless, despite these longer-term risks, we see Russian equities as an attractive tactical opportunity in the short term.

In fixed income, we continue to favour a neutral position on government bonds relative to cash. However, within other segments in the asset class, we prefer corporate debt, where we see greater value opportunities.

For currencies, it is likely that heightened volatility will continue. Valuation measures are not currently providing any strong signal, therefore our currency recommendation continues to be for neutral positions, as we prefer to take active positions where we have greater conviction.

Macro Assessment

28° N - Delhi, India

While the economic recovery is progressing, the slowdown in the pace of improvement is becoming more prevalent, fuelled by concerns about consumption and fiscal challenges in developed countries.

US

While the recovery is underway, economic data highlighted a moderation in improvements.

- For 2Q, US GDP growth eased to 2.4% q-o-q from a revised 3.7% q-o-q in 1Q. Likewise, the ISM manufacturing index declined by more than expected, to 56.2 in June, from 59.7 in May.
- Other reports disappointed, fuelling the belief that the sustainability of the recovery is still subject to strong headwinds from unemployment and fragile consumption.
- Reflecting the slowdown in momentum, the US Federal Reserve cut its 2010 GDP growth forecast for the US.
- Given the disappointing data, Consensus Economics also lowered its forecast for 2010 GDP growth by 0.2% to 3.1%, and reduced it by 0.1% to 3.0% for 2011.
- Turning to inflation, in June, the all-items CPI fell to 1.1% y-o-y, which was significantly lower than the May reading of 2.0% and below the consensus estimate.

Europe

The economic outlook for the region is improving, but concerns remain for the medium term.

- News on the fiscal situation of countries in the region improved in July. There were a number of successful bond auctions, including Greece's six-month treasury bills.
- The European Central Bank kept its main policy rate at 1.0%.
- European Central Bank (ECB) President Trichet stated that global gloom over the region's prospects was "overdone" and he confirmed that the ECB would continue to support banks with the provision of liquidity.
- In addition, the Purchasing Managers' Index readings for July surprised on the upside as the services, manufacturing and overall composite readings all beat forecasts, reducing fears about economic fragility in the region. Likewise, retail sales also improved, rising by 0.3% m-o-m in May following a 1.5% decline in April.
- However, labour conditions were a concern. Eurozone unemployment remained elevated at 10% in June.

UK

Economic data was encouraging, but the fiscal austerity plan continues to cloud the outlook for growth.

- In June the UK released the details of its "austerity budget" aimed at cutting public spending and increasing taxes. This should reduce the UK's budget deficit to 6.3% of GDP by 2014-15.
- In encouraging economic news, 2Q GDP increased by 1.1% q-o-q, the fastest pace in four years and far stronger than expectations. The pick-up was widespread across all sectors with service activity and manufacturing output increasing.
- However, unemployment remained at 7.8% in May, while the Purchasing Managers' Index and service index readings fell in June, although they remained in expansionary territory.
- Overall, Consensus Economics forecast for 2010 GDP growth was left at 1.3%, but the 2011 forecast was lowered by 0.2% to 2.1%, given the difficulty in assessing the impact of fiscal austerity on future growth.
- The core CPI actually rose to 3.1% y-o-y in June from 2.9% y-o-y in May, which was already well above the Bank of England (BoE)'s 2% target. While the BoE maintained interest rates at 0.5%, one Monetary Policy Committee member explicitly stated inflation concerns.

Japan

July economic reports disappointed, confirming a slowdown in the pace of economic recovery.

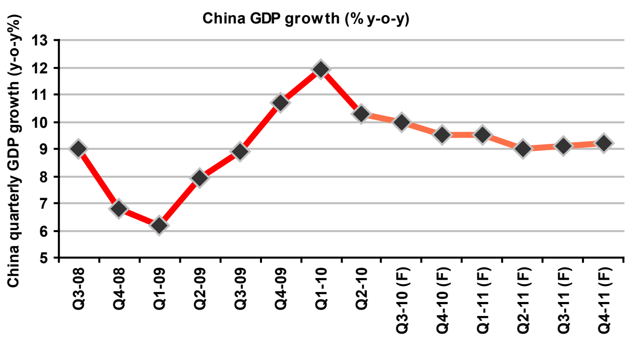
- Recent data suggested that the export and industrial-led recovery could be running out of steam.
- For example, industrial production, despite growing by 20.4% y-o-y in June, rose only marginally m-o-m, by 0.1%, versus a rise of 1.3% m-o-m in May.
- Data showed a cooling of exports, from a growth of 32.1% y-o-y in May to 27.7% y-o-y in June. Exports have been the main driver of the nation's economic rebound.
- In the consumer sector, data continued to be mixed, confirming the belief that domestic demand is unlikely to take over from exports. For example, nationwide department store sales declined sharply in June, by 6.0% y-o-y versus a drop of 2.1% y-o-y in May.
- However, the pace of deflation eased, with the all-items CPI coming in at -0.7% y-o-y in July (- 0.9% in June), while the y-o-y core CPI rate moved to -1.5% y-o-y in July, from -1.6% y-o-y a month earlier.

Macro Assessment

Emerging Markets

Economic data here remained strong in July, but was less impressive than previously, suggesting that the pace of recovery may be easing, especially given ongoing monetary tightening.

- Economic activity in Asian and Latin American economies remained buoyant in July. Industrial production and exports, which are key drivers of Asia's economic activity, continued to display double-digit growth in South Korea, Taiwan, India and China.
- Furthermore, domestic demand remained upbeat, particularly in China and Brazil, with retail sales up 18.3% y-o-y in the former and 10.2% y-o-y in June in the latter.
- Nevertheless, other key reports suggested that the strength of the recovery may be easing. For instance, China's GDP growth cooled to 10.3% q-o-q in 2Q, from 11.9 % q-o-q in 1Q.
- Of further concern, ongoing inflationary pressures in both Asia and Latin America continued to support a normalisation of interest rates.
- In Eastern Europe, however, the growth story is less buoyant. This is largely due to uncertainty about the economic situation in the Eurozone and concerns about slower-than-expected growth in the US and China.



Source: Consensus Economics, Bloomberg, 30th July 2010. F = Forecast

Indonesia

Inflation started to accelerate but remain within central bank's target range and fundamental continued showing positive numbers

- Inflation accelerated by 5.05% in June from a year earlier, faster than previous month as the end of harvest season drove food supply to be limited. However, central bank viewed that as long as inflation remain between its target range of 4% to 6%, then it still has room to keep interest rates low in order to boost credit growth. Indeed, Bank Indonesia maintained BI rate at 6.5% for the 11th month.
- Exports remain healthy particularly to other Asian markets where trade balance grew higher than analysts expectation at $ 2.47 bn in May.
- The rise in commodity prices has been helping foreign reserve to stay near record high at $ 76.3 bn, providing enough ammunition for the central bank to do currency intervention if needed, in order to guard rupiah's stability.
- Higher motorcycle sales and credit growth, add to evidence that domestic consumption remain strong and increase expectation that corporate earnings may show positive results.

Equity Markets

Global Developed Markets

We retain a moderately cautious view on equity markets relative to cash. On the whole, the commitment from policymakers in the developed world to keep interest rates at the current low levels is good news for equity markets. However, given analysts' ambitious forecasts for earnings growth in 2010, the risk of negative earnings surprises continues to weigh on the outlook for the asset class, particularly if measures of fiscal austerity lead to a slowdown growth in the second half of 2010.

US

- While a recovery in economic activity is taking place in the US and elsewhere, the pace of improvement is generally slowing down.
- Earnings growth forecasts for 2010 and 2011 are still elevated and, combined with the mixed prospects for consumer demand for developed economies, this is likely to create more room for disappointment in earnings growth.
- Turning to valuations, the US equity market's 12-month forward PE has been relatively unchanged since June, at 12x. While the valuation level appears to be lower than the long-term average, ongoing risks to earnings and uncertainty regarding economic growth continue to justify a moderately cautious view on equities in the US and elsewhere.
- At the sector level, we maintain our preference for defensive sectors such as healthcare and telecommunication services against the more cyclical sectors and financial stocks.

Europe

- While economic activity has started to slow, it is still positive in both the UK and the Eurozone. However, concerns over government debts and the impact of austerity measures are ongoing.
- In addition, unemployment remained high and consumer demand mixed, supporting our view of only moderate economic growth in 2010.
- From a valuation perspective, while Eurozone and UK equities are trading at reasonably undemanding levels (12-month forward PEs of 10.2x and 9.5x respectively), we are still concerned about the forecasts for earnings growth for these regions, as we are elsewhere.
- Overall, we retain our moderately cautious stance on European equities and favour being moderately underweight equities versus cash.

Japan

- While, on the whole, the Japanese economy is recovering, recent data suggested that the risk over the sustainability and strength of the rebound remains high.
- As with many other developed markets, the expectations for company earnings growth in 2010 and 2011 still seem to be on the high side, which creates the potential for negative company earnings surprises, should the global economic rebound lose momentum.
- The valuations for Japanese equities are not excessive relative to history (the market was trading at a 12-month forward PE of 13.9x, at end July) and are in neutral territory relative to other developed equity markets.
- Therefore, given the risk to earnings from a softening of the pace of recovery, we reiterate a moderately cautious stance on Japanese equities relative to cash, as we do for other major developed equity markets.

Global-Emerging markets

- Many economists believe the weaker growth numbers from China indicate 'a slowdown, not a meltdown', a view we currently share. Nevertheless, Chinese growth numbers will be a key focus in the near term as any indications that the slowdown is more pronounced could be met with equity market weakness.
- Equity valuation measures are not giving any strong signals, either in emerging markets or developed markets, and, given our continuing modest concern over the levels of earnings forecasts, we favour a moderately cautious position in equity markets overall.
- Within emerging markets, we continue to favour Latin American markets versus those of Emerging Asia, albeit with less conviction as the valuation advantage of the former has lessened in recent months.
- Furthermore, we favour Russian equities versus the wider emerging markets universe, as we continue to believe that Russian stock valuations are attractive in absolute terms relative to other emerging market equities.

19° N - Mexico City, Mexico

Equity Markets

Asia ex-Japan

- So far, economic releases have confirmed a robust macro-economic backdrop for the economies of Asia-ex Japan, while indicators for domestic demand continue to impress, underscoring our central scenario for solid positive growth for the region.
- However, we continue to expect further monetary tightening in Asia-ex Japan, as underlying price pressures remain a concern, particularly in food items, and overall this is a risk for equity investors.
- Valuations are not overly-demanding and the 12-month forward PE level is similar to that of June. However, we are more concerned about the high levels of earnings' growth forecasts, which could prove too optimistic given the ongoing risks to a sustainable global recovery.
- Therefore, in line with other equity markets, we are modestly cautious on the outlook for Asia ex-Japan.

Latin America

- Performance for equities across Latin America was strong in July (with Brazil being the largest market), with a rise of 9.2% as measured by the MSCI index
- Overall, while buoyant economic activity in Latin America is positive for global economic growth, it increases the risk of further monetary tightening.
- In general, economic data in Latin America continued to be strong but the levels of inflation provided some cause for concern. Monetary policy was being tightened to prevent economic overheating. For example, in July, Brazil raised its reference interest rate by 0.50%, taking it to 10.75%.
- On the whole, given our expectation for potential positive surprises in macroeconomic performance for the region and relatively supportive valuation levels, we continue to prefer Latin American to emerging Asian equities.

Middle East

- Middle East and North Africa (MENA) have, in fact, been outperforming international equity markets in recent months, despite low volumes.
- Looking between now and year-end, while, on the one hand, a better global environment and an encouraging macro picture should support equity markets, on the other hand, valuation levels are not showing any strong signals relative to other equity markets.
- The region is not immune from the ongoing uncertainty surrounding the sustainability of the global recovery.

Eastern Europe

- Good performance from Russian equities, up 8.6%, contributed positively to the Eastern European region as a whole, which rose by 8.3% in July.
- In Eastern Europe, however, the growth story is less buoyant than in other emerging markets. This is largely due to uncertainty regarding the economic situation in the Eurozone and the concerns about a potential slowdown in growth in US and China.
- For example, while Russia and Turkey displayed strong economic readings in July, in other areas, such as the Baltics, countries are still struggling to emerge from their economic contraction.
- Overall, this could hurt the sustainability of the economic recovery in Eastern Europe.

Equity Markets

28° N - Delhi, India

Indonesia

- Bank Indonesia's decision in keeping interest rates at low level of 6.5%, increased expectation lending growth may rise further and support the economy, sending positive sentiment to banking shares last month.

- Positive earnings results from several big-cap companies in second quarter, added to evidence of strong consumption level. This increased investors' appeal toward Indonesian equities and drove market to reach a new record high at 3096 at the end of last month.

- Higher commodity prices and positive earnings results from US and European companies, drove risk appetite to rise and added support to JCI last month.

- The appointment of new Bank Mandiri's president director, ended market uncertainty on who will lead the nation's biggest bank and added positive sentiment to banking shares. Former Bank Mandiri's president director, Mr Agus Martowardjojo was elected as the new Finance Minister, replacing Ibu Sri Mulyani who took a new role in the World Bank in June.

- Looking through positive fundamental background mentioned above, we remain positive on Indonesian equities' outlook.

Fixed Income

USD Government Bonds

- Recent economic data has reinforced the downside risk to growth, and also suggests that inflation is likely to remain benign.
- The consensus view on inflation has shifted significantly over the last year as many market participants were expecting higher inflation in the medium term, due to accommodative policy from the US Federal Reserve, but now such concerns seem a lot less prevalent.
- Overall, we expect US interest rates to remain on hold for the rest of the year and, in all likelihood, for longer, due to weaker economic data, a very slowly-improving employment picture, an absence of inflationary pressures and well-anchored inflation expectations.
- We retain our neutral position in US Treasuries relative to cash. Within fixed income assets, we retain our preference for corporate bonds, where we see greater total-return opportunities.

Eurozone Government Bonds

- We retain our neutral allocation in Eurozone government bonds relative to cash. The market has reacted positively to the extended liquidity measures put in place by the European Central Bank and the encouraging bank stress test results. However, the mood in the financial markets is still volatile.
- Elevated unemployment is keeping a lid on consumption, which remains stifled at best. The July Consensus Economics 2010 forecast for consumption growth in the Eurozone has fallen to a weak 0.1%.
- However, this should contain inflation and enable the low interest rate environment to be maintained, which is supportive for government bonds.
- Overall, given the low yields offered by government bonds and ongoing fiscal concerns in the eurozone, our preference remains for corporate debt within fixed income.

Investment Grade Corporate

- In the absence of inflationary pressure in developed markets, central banks can continue to maintain low interest rates for the foreseeable future.
- Spread-implied default levels, versus average and highest actual default levels seen over the past 40 years, seem to more than adequately compensate investors for corporate bond risk.
- Furthermore, in the US, 2Q corporate earnings results have so far exceeded analyst estimates in aggregate, which is a further supportive factor for corporate bonds.
- Overall, despite some concerns surrounding the sustainability of the global recovery, we do not hold a possible "double-dip" scenario as our central view. We remain constructive on the opportunities in credit markets and, as such, maintain our positive view on investment grade corporate bonds.

High Yield

- Our positive view on high yield bonds would have been profitable year to date. Furthermore, corporate earnings remain supportive for credit and second quarter earnings results reported so far have been better than expected, in aggregate.
- Our central scenario of subdued inflation is a positive factor for corporate bonds, as it helps keep government bond yields at low levels. Income is also in demand in this environment of low interest rates, thus encouraging flows into high-yielding asset classes.
- Currently, declining default rates further support the case for corporate bonds.

Sovereign USD-denominated Emerging Markets

- With interest rates in developed markets low and expected to remain low, assets with a reasonable yield are likely to find support with investors.
- As such, this suggests ongoing demand for USD-denominated emerging market debt from both domestic and global investors.
- From a valuation perspective, the asset class looks interesting on a stand-alone basis, but developed markets' debt continues to offer a better risk/return trade-off.

Global Inflation-Linked Bonds

- In developed economies, inflation is expected to be relatively contained in the near term, as high unemployment and tighter fiscal policies are likely to weigh on growth.
- For inflation-linked bonds in developed markets, from a valuation perspective, break-even inflation levels have risen significantly since early 2009, so the case for the asset class is less compelling than a year ago. Therefore, we recommend a moderately negative allocation versus nominal bonds.

Indonesia

- Interest rates that was kept at lowest level since July 2005 and stable rupiah, continued providing positive sentiment to the nation's bond market last month.
- The new regulation on investing in short-term debt instruments implemented by the government aimed for preventing too much hot money flow to Indonesian markets, increased demand for longer tenor government bonds (tenor longer than 1 year bond) and helped support the market.
- Higher yield offered by this instruments combined with positive fundamental outlook and optimism that credit rating may reach investment grade in near future after Moody's upgraded the nation's credit outlook from stable to positive, may drive demand to remain robust on this instrument and therefore we maintain our positive view on this asset class.

Other Investments

Oil

- Oil prices rose in July, as investors' risk appetite returned thanks to strong corporate earnings results in the US and elsewhere. Supply and demand dynamics remain balanced, in line with global growth prospects. However, uncertainty over the sustainability of economic recovery is likely to cause ongoing price fluctuations. Balancing, on one hand, the expected pick-up in demand and, on the other, the degree of spare capacity, we believe that the oil price is likely to keep trading in a range of US$65-85 per barrel on a 6 to 12-month view.

Gold

- The gold price fell by about 5% m-o-m in July, representing the first monthly decline since March. The price came under pressure last month due to improved sentiment, as concerns over the European sovereign debt crisis receded.
- Gold has now fallen by about 6% from its 21 June record high of US$1,266.50 an ounce.
- There are reasons to expect limited upside to the current gold price. Firstly, money supply growth remained generally low, especially in the US, at 1.6% y-o-y in April. Secondly, inflation in developed countries is generally muted.

Commercial Real Estate

- The UK remains the most attractive unlisted market, based on valuations and supportive investor demand. However, the rental growth outlook remains weak, albeit slightly improving.
- Given the recent performance of the segment, we have slightly trimmed our outlook of prospective returns. Nonetheless, the view of the UK remains positive in the short term due to valuations.
- In the Asia Pacific region, property markets are benefitting from relatively strong economic growth which, other things being equal, is good for real estate. The problem is that some markets may be experiencing oversupply.
- In the US, there is evidence that the unlisted market is at or close to the bottom, with wide variations from city to city, however.
- Finally, the picture for continental Europe continued to be mixed, with wide variations at the country level. For instance, France and the Nordic region look attractive, while the situation in Eastern Europe, Spain and Greece is more troublesome.

Currency

- The USD was weaker against major currencies during July, declining by 6.2% against the EUR, by 2.2% against the JPY and by 4.8% against the GBP.

- Not only were investors generally less risk averse during the month, which tends to favour currencies other than the 'safe-haven' USD, but concerns over the sustainability of the US economic recovery also reduced the USD's attraction.

- The USD continues to be heavily influenced by global risk attitudes. However, the recent focus has shifted more towards the sustainability of the US economic recovery, which may extend the recent weakness of the currency.

- We no longer hold the view that the UK's relatively poor fiscal position compared to some of the major Euro countries will favour the EUR over the GBP in the medium term as the new UK coalition government appears to have taken aggressive action to address the deficit.

- Positive fundamental outlook and high yield offered by Indonesian equities and bonds, combined with higher earnings results from corporation, continued driving overseas investors to enter the market and supporting rupiah further last month.

Long-Term Investment Outlook (three to five years)

ASSET CLASS	CURRENT VIEW	REASONING
Developed market equities	Positive	• Average rate of growth somewhat subdued in the developed world. Yet a combination of exposure to higher growth areas like emerging markets and dividend growth are likely to keep average nominal rates at high single digit levels.
Emerging market equities	Positive	• Expected to outperform developed market equities thanks to a favourable structural backdrop.
Developed market sovereign bonds	Negative	• Comparatively low level of yield and issues around public debt are likely to keep average returns relatively subdued.
Developed market credit	Positive	• The level of spread continues to be attractive on a historical basis and is likely to keep average returns for credit assets above respective government bonds.
High Yield	Positive	• The level of spread continues to be attractive on a historical basis and is likely to keep average returns for credit assets above respective government bonds.
Emerging market debt	Positive	• Structural improvement and reasonable valuation levels are likely to lead to an outperformance of emerging market debt relative to cash and developed market sovereign debt.
Developed market inflation-linked bonds	Neutral / Negative	• Inflation expectations are likely to remain contained over the medium term due to subdued growth expected in developed markets.
Commodities	Positive	• Growth in emerging markets likely to remain an element of support for this asset class.
Developed market cash rates	Negative	• Subdued economic growth and stimulus measures are likely to keep rates at subdued levels for the foreseeable future.

For further information please visit your local Premier website where you will find the contact details of our Premier Relationship Managers or www.hsbcpremier.com