

Global Investment Perspective

9° N - Bocas del Toro Island, Panama

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Highlights

On the whole, data has remained soft, reinforcing the view that the global economy is experiencing a weak patch. That said, after sharp drops in the previous month, US data releases were marginally better, though still mixed, in September. Manufacturing activity for the month and industrial production for August beat expectations, while annualised quarter-on-quarter Gross Domestic Product (GDP) for the April to June period was revised upwards. Conversely, key forecasts for GDP in 2011 and 2012 were downgraded again, while inflation, as measured by the US all items Consumer Price Index (CPI), was up by more than had been anticipated, hitting a two-year high. Nonetheless, the month saw some cheer as the US Federal Reserve (Fed) launched 'Operation Twist', a policy designed to lower yields on long-term bonds.

The picture was more downbeat in the eurozone, where economic figures were once again discouraging. Manufacturing and services activity in the region moved into contractionary territory. Unemployment remains high, while July retail sales for the eurozone were down, and consumer confidence fell. In spite of better-than-expected industrial production data from Germany and France, the mood remained sombre. Although Germany and France have continued to back Greece publicly, the debt situation in the country continues to cause concern. While the European Central Bank (ECB) kept interest rates at 1.50%, a rate cut is now looking more likely against a backdrop of weak growth, even though inflation across the region remains high. Meanwhile, in the UK, though economic data was once again disappointing, there were some signs of a recovery.

Elsewhere, after promising signs of a pick-up in activity in August, economic data from Japan has started to suffer from the deteriorating global outlook. In contrast, emerging markets have continued to register healthy economic performance, albeit with some moderation as well as variation across the bloc. For example, though year-on-year industrial production numbers in China (August figures) and India (July) have fallen, in Russia, industrial data beat expectations in August.

Market Recap

September proved to be another poor month for equities. Although stocks began promisingly amid speculation that President Barack Obama was planning significant economic stimuli next year, they subsequently resumed their downward trajectory, most of all in Europe, after ECB President Jean-Claude Trichet said downside risks to the eurozone economy had intensified. This engendered increased efforts by policy makers to contain the eurozone's sovereign debt crisis; Germany's parliament voted to back a euro rescue package and the ECB announced a further extension of its policy of providing unlimited liquidity to eurozone banks, saying it would include 12 month loans this month and 13 month loans from December that will bridge two crucial year-end periods. It also unveiled a EUR 40 billion programme to buy 'covered bonds' (ultra safe investments issued by banks). In the UK, the BOE announced that they would provide further monetary stimulus on a greater scale than had been expected increasing its stock purchase of gilts by £75 billion over the next 4 months. Meanwhile, in the US, the Fed also launched Operation Twist. However, it was the Fed's pessimistic assessment of the economy that became a catalyst for 'risk-off' behaviour in the markets this month. The Fed noted "significant downside risks to the economic outlook, including strains in the global financial markets". Overall, equities were down in September to end one of the most dismal third quarters in ten years. The S&P 500 fell by 7.0%, one of the worst-performing developed equity markets. European equities dropped by 5.8%, amid ongoing fiscal concerns and lacklustre economic data. Concerns over growth and eurozone debt weighed on Asia ex-Japan equities, which dropped by 9.2%. Emerging markets were also down, underperforming developed equities over the month; although economic numbers remain robust, signs of a slowdown are clearly emerging. However, Japanese equities were relatively resilient in September; the MSCI Japan index fell by only 0.8%.

Against this backdrop, US Treasuries performed strongly, rising by 1.76% over the month, contributing to their largest quarterly gain since the fourth quarter of 2008. As in the previous month, eurozone government bonds, except Greece, were up in September.

Outlook & Strategy

Although macroeconomic data remains weak, we continue to hold a constructive view with respect to risky assets. Nonetheless, we are aware that increasing signals of a slowdown in the global economy make the outlook an uncertain one. The on-going eurozone debt crisis is of particular concern. On a positive note, equities remain attractively valued and markets have already priced in high levels of risk. As such, we are confident with our moderate exposure to risky assets, although we continue to stress the need to diversify portfolios, given the considerable volatility that has plagued risk markets in recent months.

Against this backdrop, our central scenario is largely unchanged. We still expect lacklustre growth figures across the key developed markets, but anticipate growth from the emerging market bloc to be more robust, in spite of some moderation. This view now seems to be shared by the market. Although economic data releases have continued disappointed in some regions, we remain optimistic that any global downturn will be soft rather than a full-blown and lasting recession. Interest rates remain low and monetary easing steps to stimulate growth are now in place. However, we recognise that the downside risks are perhaps greater than they were earlier in the year.

The extreme volatility we have seen in markets stems from a plethora of fundamental and long-term concerns. In the short run, volatility is likely to remain. Nonetheless, despite greater risks, valuations have adjusted accordingly. Government bond yields in developed countries remain very low and reflect both the weak economic environment and low interest rates. Given these levels, it is hard to envisage further value. However, the same is not true for corporate issues, most of all at the higher-yielding end of the spectrum and we favour these over government bonds. Conversely, equities are, on the whole, trading at forward price/earnings (PE) ratios of 15 or under, with some countries, such as Europe, Russia, China, seeing ratios below 10. As the outlook for earnings growth remains robust for 2012, these valuations, in particular when compared to bonds and cash, are undoubtedly attractive in the long term.

Among developed market equities, we continue to prefer Japanese stocks on a currency-hedged basis. Short-term volatility aside, the current PE ratio is below its historic average and we feel the Japanese equity market still provides a number of attractive opportunities. In the emerging markets, Russia's compelling equity valuations, both on a relative and absolute basis, as well as signs of resilient economic conditions, make it our favoured market. Nevertheless, we remain aware that a further fall in oil prices amid declining global demand, poses a significant risk to Russian equities, although this is not our central view. We have also maintained a tactically overweight exposure to Chinese equities, which appear particularly attractive and are trading at a discount both relative to other emerging markets and historically. Furthermore, tighter monetary policy seems to be having a dampening impact on rampant inflation in China. As such, an end to the inflationary cycle may prove the impetus for supportive inflows.

In other fixed income, US dollar-denominated emerging market debt continues to look attractive, versus government bonds in developed nations. However, the asset class remains less compelling than developed market corporate debt, notably high-yield bonds. Meanwhile, our attitude to global developed inflation-linked bonds has become more optimistic, believing that their relative value versus government bonds has improved.

Short-term Investment Outlook (6 - 12 months)



	ASSET CLASS	CURRENT VIEW*	REASONING
EQUITY	Global Developed Market Equity	Neutral	<ul style="list-style-type: none"> Equity valuations relative to cash and especially government debt remain attractive, plus liquidity remains supportive. There continue to be risks to the economic recovery, but our core scenario is for positive, although sub-trend growth.
	US Equity	Neutral	<ul style="list-style-type: none"> Corporate earnings have been encouraging. Unemployment remains elevated at over 9%, although recent payroll figures have shown improvements.
	Europe Equity (including the UK)	Neutral	<ul style="list-style-type: none"> Although valuations look cheap, economic conditions remain fragile. UK growth has slowed, while the economic health of peripheral eurozone countries remains uncertain. That said, policy action has been favourable with major central banks agreeing to measures to help deal with the ongoing eurozone debt problems.
	Japan Equity	Positive	<ul style="list-style-type: none"> We maintain our overweight exposure to Japanese equities, which we believe offer attractive opportunities in spite of signs that the economy is beginning to suffer from the deteriorating global outlook. In addition, the current price-to-earnings ratio is still trading far below the historic average.
	Asia ex-Japan Equity	Neutral	<ul style="list-style-type: none"> In spite of a slowdown in global demand, Asia ex Japan countries still carry more favourable economic prospects than other developed nations. At a country level, we prefer Chinese equities relative to other Asian emerging markets. Valuations are favourable and inflation is exhibiting early signs of peaking amid further central bank tightening.
	Global Emerging Markets	Neutral	<ul style="list-style-type: none"> Emerging countries are likely to continue to lead the economic recovery, due to robust domestic consumption and strong intra-regional trade. That said, like developed markets, emerging market equities are exposed to volatility stemming from the question marks around the sustainability of the global economic recovery, exacerbated by the monetary tightening cycle that has already begun in a number of key emerging economies.
	Latin America Equity	Neutral	<ul style="list-style-type: none"> The economic performance of Latin American countries remains strong and earnings growth estimates for 2011 look reasonable. Nonetheless, the good news seems to be well reflected in market prices and relative valuation measures show no strong signals. We, therefore, retain our neutral stance.
	Middle East Equity	Neutral	<ul style="list-style-type: none"> Given the political unrest within the region, in the short-term we expect volatility to persist affecting the overall performance. The investment potential will be largely dependent on oil prices and supply uncertainties.
	Eastern Europe Equity	Neutral	<ul style="list-style-type: none"> Manufacturing data has varied within the different countries. At a country level, we favour Russian equities. Russia's economic activity has been encouraging, while valuations for Russian equities are attractive in both absolute and relative terms.
Indonesia Equity	Neutral	<ul style="list-style-type: none"> Amid volatile regional sentiment, local sentiment remains cautious while earning season arrives in October, giving the market a good sentiment combined with the lowered interest rate by the central bank. 	
FIXED INCOME	US government bonds	Negative	<ul style="list-style-type: none"> Excess capacity in developed markets and the commitment of the Fed to remain accommodative are generally supportive for low yields. However, the market is still offering little value relative to history and, downside risks remain, particularly in relation to fiscal policy. Within fixed income, we prefer to own corporate debt, where we see greater total return opportunities.
	EUR government bonds	Negative	<ul style="list-style-type: none"> We have a negative stance on eurozone government bonds relative to cash. This is due to uncertainties regarding the economic health of eurozone peripheral countries. In addition, valuations of these bonds do not look particularly attractive; they offer limited protection against negative surprises.
	Investment Grade Corporate	Positive	<ul style="list-style-type: none"> Strong corporate earnings results, the view that major central banks will keep interest rates low and strong demand for yield have boosted investment grade corporate bonds. We continue to be positive on the asset class
	High Yield	Positive	<ul style="list-style-type: none"> High-yield bonds continue to look attractive on a total return basis. We have retained our positive view on the asset class given robust corporate results, declining default rates and low interest rates.
	Sovereign USD-denominated Emerging Markets Debt	Neutral	<ul style="list-style-type: none"> While sovereign US dollar-denominated emerging market debt continues to look less attractive on valuation grounds than developed market corporate debt, and high yield in particular – they remain more attractive relative to government bonds.

Short-term Investment Outlook (6 - 12 months)



	ASSET CLASS	CURRENT VIEW*	REASONING
FIXED INCOME	Global Developed Inflation-linked Bonds	Negative	<ul style="list-style-type: none"> The value of global inflation-linked bonds relative to government issues has improved recently, and we have increased our stance from underweight to neutral.
	Indonesian Bonds	Positive	<ul style="list-style-type: none"> Strong macroeconomic numbers amid global fears are showing positive sentiment towards Indonesia's economic potential. Lowered interest rates also provide positive signs to the bonds market for Indonesia.
OTHER INVESTMENTS	Oil	Between the range of US\$90 to US\$110 per barrel	<ul style="list-style-type: none"> Our target range for the oil price remains US\$ 90 - US\$ 110. We maintain this forecast as supply and demand forces appear reasonably balanced at present. However, short-term volatility is expected while economic growth uncertainty persists.
	Gold	Neutral Between the range of US\$1,250 to US\$1,400 per troy ounce	<ul style="list-style-type: none"> We maintain our neutral stance on gold. Quantitative easing combined with ongoing macroeconomic uncertainty, remain supportive factors for this precious metal. That said, although recent data releases have been disappointing, the economic recovery remains in place. Balancing these factors, We expect gold will trade in a range of US\$ 1.500 to US\$ 1.600 per troy ounce in the medium-term.
	Commercial Real Estate (unlisted markets)	Neutral	<ul style="list-style-type: none"> We expect property to continue to be volatile in the near term, as macroeconomic and sovereign risks persist. However, the asset class offers an attractive yield, particularly relative to government bonds.
CURRENCY	Euro, British pound sterling, Japanese yen and the US dollar	Neutral	<ul style="list-style-type: none"> Valuation indicators are not sending any clear signals at present. We see both event-driven and sentiment-driven risks contributing to ongoing volatility. We thus continue to have a neutral view on currency exposures.
	Indonesia Rupiah against USD	Neutral	<ul style="list-style-type: none"> While the central bank is actively providing intervention to the financial market, the Rupiah stability is maintained. However the dovish moves by the central bank may further pressure Rupiah for a weakening sentiment.

*within the broad asset class

Summary

We have maintained a moderately overweight allocation to global equities overall relative to both government bonds and cash. In developed market equities, we continue to be moderately positive on Japan, where we continue to see valuations and policy support providing a favourable backdrop for the country's equities. Within emerging market equities, we continue to prefer China and Russia as their valuations are more attractive.

Within fixed income, our negative view on government bonds relative to cash remains. We maintain our positive stance on corporate issues in the light of attractive valuations and favourable issuer fundamentals. Within corporate debt, we favour high yield bonds as their extra yield should provide some protection should government bond yields rise. Our central economic scenario remains: slow but positive growth in the major developed markets. This environment is typically positive for credit markets.

Regarding the four major developed market currencies, we believe that heightened levels of volatility are likely to persist. Valuation measures are not sending strong signals at present and, as a result, we maintain our neutral stance on currency positions.

Given the backdrop of heightened uncertainty with respect to global growth and assuming the continuation of volatility in the markets, our key recommendation is to be well diversified.

Macro Assessment

Data remains soft, reinforcing the view that the global economy is experiencing a weak patch. The sovereign debt crisis in the eurozone and fiscal concerns in other developed markets are among some of the major worries for investors. Co-ordinated central bank action to try and ease the gloom did little to lift sentiment.

US

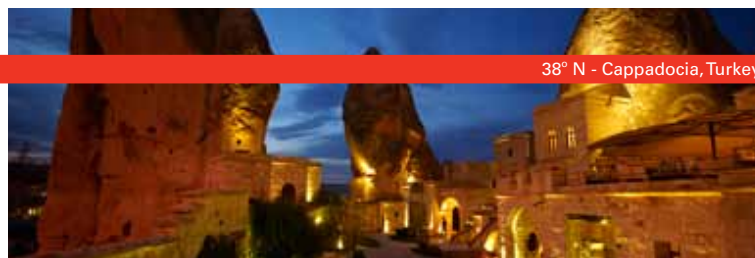
Economic data releases were mixed but remained at low levels following sharp drops last month.

- > In manufacturing, the US Institute for Supply Management (ISM) manufacturing index rose to 51.6 in September (versus 50.6 last month), higher than the expected level of 50.5. Industrial production also beat expectations, rising 0.2% month-on-month in August, while the University of Michigan Consumer Confidence index rose to 59.4 in September.
- > In addition, the US ISM non-manufacturing index beat expectations in September, coming in at 53.0 against expectations of 52.8.
- > Second-quarter GDP growth was revised up to an annualised 1.3% quarter-on-quarter from 1.0% quarter-on-quarter and personal consumption was revised up to 0.7% from 0.4% in the second quarter of the year. However personal spending rose only 0.2% month-on-month in August from a revised 0.7% month-on-month in July.
- > Labour market data was encouraging. US payrolls climbed by 103k in September following a revised 57k increase the prior month, beating expectations. The median forecast had been for a rise of 60k. However, overall the unemployment rate remains elevated at 9.1%. In a separate release, the Bureau of Labor statistics announced an annual revision to the March 2011 total payroll figure, adding 192,000.
- > President Obama announced a US dollar 447 billion jobs plan (approximately 3% of GDP), combining tax cuts and infrastructure spending in order to spur economic growth and improve the poor employment situation.
- > In addition, the Fed launched 'Operation Twist' in an attempt to drive down long-term interest rates by purchasing US\$ 400 billion of long-dated securities financed by the sale of an equal amount of bonds with a maturity less than three years.
- > The US all items CPI increased to a new two-year high of 3.8% year-on-year in August, higher than expected. The core consumer price index, excluding food and energy related goods, came in at 2.0% year-on-year in August from 1.8% year-on-year in the previous month.
- > Consensus Economics forecasts for GDP growth in 2011 and 2012 were downgraded again to 1.6% (-0.2%) and 2.1% (-0.3%), respectively.
- > International Monetary Fund (IMF) forecasts were also downgraded significantly from previous forecasts in June. The 2011 forecast has fallen by 1.0% to 1.5%, while the 2012 has fallen by 0.9% to 1.8%.

Europe ex-UK

Economic data in the eurozone continued to disappoint.

- > Manufacturing and services activity moved into contractionary territory in the region. The eurozone Purchasing Managers Index (PMI) for manufacturing dropped to 48.5 in September from 49.0 in August, while the PMI services number fell to 49.1 from 51.5.
- > In addition, the unemployment rate remains high, remaining at 10.0% in August.
- > On the consumption front, eurozone retail sales dropped to 0.2% month-on-month in July from a revised 0.7% month-on-month earlier.
- > With disappointing news across several sectors, eurozone consumer confidence fell again to -18.9 in August from -11.2 in July.
- > However, in more encouraging news, industrial production numbers beat expectations in July. In Germany, it increased by 4.0% month-on-month, while, in France, it rose by 1.5% month-on-month.
- > Regarding the deteriorating debt situation in Greece, Merkel and Sarkozy continue publicly to back Greece and remain adamant over the country's future in the eurozone. The statement provided a boost to sentiment although the Greek situation continues to be concerning.



- > As expected, the ECB maintained interest rates at 1.50% and announced a further extension of its policy of providing unlimited liquidity to eurozone banks, saying it would include 12 months loans this month and 13 months loans from December that will bridge two crucial year-end periods. It also unveiled a EUR 40 billion programme to buy 'covered bonds' (ultra safe investments issued by banks).
- > The eurozone CPI rate remained at 2.5% year-on-year in August although the initial estimate for September suggests inflation has risen to 3.0%, which would be the highest level in three years. Core CPI year-on-year also remained unchanged at 1.2% in August.
- > The Consensus Economics inflation forecast for 2011 remains unchanged at 2.6% while the 2012 forecast has fallen slightly to 1.8% (down 0.1%) in September.
- > The Consensus forecasts for 2011 and 2012 eurozone GDP growth were both revised down to 1.7% (-0.2%) and 1.0% (-0.5%) respectively in September.

UK

Data within the UK was generally disappointing although there were some signs of recovery.

- > In manufacturing activity, the ISM manufacturing index unexpectedly moved into expansionary territory, coming in at 51.1 in September from a revised 49.4 in August.
- > Industrial production was less encouraging, coming in at -0.2% month-on-month in August. Furthermore, the PMI Services index fell to 51.1 in August from 55.4 in July, the biggest drop in the measure in a decade.
- > Elsewhere, retail sales fell by 0.2% year-on-year in July, showing stagnant consumer spending over the last year.
- > In the labour market, the unemployment rate remained at 7.9% in July, but monthly jobless claims came in lower than expected.
- > In the housing market, house prices fell by 1.2% month-on-month in August, having risen 0.3% month-on-month in July.
- > UK inflation increased in August to 4.5% year-on-year from 4.4% year-on-year in July. The core CPI was unchanged at 3.1% year-on-year in August.
- > The Monetary Policy Committee (MPC) was unanimous in maintaining rates at all-time lows of 0.5% in September and announced that they would provide further monetary stimulus on a greater scale than had been expected. The Bank's MPC voted to increase its stock purchase of gilts by £75 billion over the next 4 months.
- > Consensus Economics September inflation forecasts for 2011 and 2012 were unchanged at 4.4% and 2.7%, respectively.
- > The Consensus Economics 2011 GDP growth forecast was revised downwards to 1.2% (-0.1%) while the 2012 forecast was revised down to 1.8% (-0.2%) in September.

Macro Assessment

Japan

Economic data from Japan is starting to suffer from the deteriorating global outlook

- > Second-quarter GDP growth was revised down to -0.5% quarter-on-quarter from the initial estimate of -0.3% quarter-on-quarter.
- > During the second quarter, private consumption was flat, business investment fell by 0.9% and exports declined by 4.9%. A separate report showed second-quarter capital spending fell by 7.8% year-on-year, its first drop in a year.
- > Japanese industrial production for August came in lower than expected at 0.8% month-on-month (against an expected figure of 1.5% month-on-month), but still illustrates a continued recovery.
- > However, September's PMI manufacturing index fell into contractionary territory, coming in at 49.3 from 51.9 in August.
- > Machine orders were disappointing, falling by 8.2% month-on-month in July following a 7.7% rise last month. Exports were more encouraging, expanding by 2.8% year-on-year in August, having fallen by a revised 3.4% year-on-year in July. Global uncertainty and the strong Japanese yen remain a threat to the external outlook.
- > In consumer activity, real household spending fell by 2.1% year-on-year in July, while nationwide department sales fell 1.7% year-on-year in August. In the labour market, the jobless rate fell to 4.3% in August, from 4.7% in July.
- > Japan's CPI rose by 0.2% year-on-year in August following a 0.2% rise in July while the core CPI (excluding fresh food and energy) fell by 0.5% year-on-year, slightly less than expectations.
- > In September, the Consensus Economics forecasts for inflation in 2011 and 2012 have both fallen to -0.2%. The September Consensus GDP growth forecast for 2011 has increased to -0.5% but the 2012 forecast has fallen significantly to 2.4% (-0.8%).

Emerging Markets

Emerging markets continue to display robust economic performance, despite signs of moderation and variation across regions.

- > Taking year-on-year industrial production as an example, China (13.5% in August versus 14.0% in July) and India (3.3% in July against 8.8% in June) reported a slowdown, below expectations, while Russia reported a higher year-on-year number, above expectations (6.2% in August versus 5.2% in July).
- > Despite the slowdown in China's manufacturing activity, consumer spending and external trade remain buoyant. Chinese retail sales increased by 17.0% year-on-year in August, compared to 17.2% year-on-year in July, in line with expectations, while exports (24.5% year-on-year in August compared to 20.4% year-on-year in July) and imports (30.2% year-on-year in August versus 22.9% year-on-year in July) both increased, beating expectations.
- > In addition, Indian year-on-year exports remained at impressive levels, coming in at 44.3% in August following an all-time high of 81.8% in July.
- > China's PMI manufacturing index rose to 51.2 in September from 50.9 in August and remains in expansionary territory. However, the HSBC manufacturing PMI for September remains in contractionary territory at 49.9.
- > In Brazil, in an unexpected move the Brazilian Central Bank (BCB) reduced its policy rate by 50 basis points to 12.0%, citing the effects of the global slowdown on the domestic economy.
- > Brazil's PMI manufacturing fell for a third straight month to 46.0 in August, whilst retail sales (7.1% year-on-year in July) and unemployment (6.0% in August) remain flat.



- > In Eastern Europe, Russian economic activity stood out in comparison to the rest of the emerging markets, with increasing real wages (3.9% year-on-year in August versus 2.4% year-on-year in July), retail sales (7.8% year-on-year in Aug against 5.7% year-on-year in July) and falling unemployment (6.1% in August compared with 6.5% in July).
- > In emerging markets inflation has started to come off from its peak. In China, the CPI dropped to 6.2% year-on-year in August down from its three-year peak of 6.5% year-on-year, in line with consensus forecasts. India's August Wholesale Price Index headline inflation rose to 9.8% year-on-year (versus 9.2% in July), above consensus, and core inflation continued to rise.
- > Despite global economic weakness, the primary concern of the Reserve Bank of India (RBI) remains inflation and they continue to tighten their policy rate with the most recent round coming from the tightening of reverse repo rate by 25bps to 7.25%.
- > In line with other positive Russian economic data, Russia's year-on-year CPI dropped to 8.2% in August from 9.0% in July. In Brazil, year-on-year CPI increased slightly to 7.2% (+0.4%) year-on-year in August.
- > Overall, the consensus economic forecasts for GDP growth for emerging markets remained solid but moderated slightly in Asia.

Macro Assessment

Indonesia

Strong domestic sentiment shows a resilient economy. Foreign reserve was hit as the central bank struggled to absorb volatile regional market sentiment towards Rupiah.

- > Overall, the macroeconomic indication showed a strong economic resilience against the global crisis. However, having a stance to maintain strong growth in Indonesia's economy, the central bank decided to lower BI rate as much as 25bps to 6.50%.
- > The room for BI rate to be lowered was due to the fact that inflation is showing good progress where September inflation year-on-year is at 4.61% down from prior reading at 4.79%
- > The measure on consumer confidence also showed good progress, signalling that Indonesian domestic consumption can absorb Indonesia's economic supply. Bank Indonesia consumer confidence rose from 110.6 to 115.
- > Foreign Reserve declined to US\$ 114 billion from US\$ 124.6 billion as Bank Indonesia strived to maintain Rupiah stability on the negative sentiment from regional volatility.
- > Exports remain robust as it declined to 37% growth. The prior reading suggested growth to be 39.5%. The number is a positive surprise as surveyed estimates displayed 28.4% growth in September's business. The strong export translated into a positive trade balance at US\$ 3.76 billion though trade with China, Korea and Japan declined. This was a result of stronger business partnership with India.



Equity Markets



Global Developed Markets

US

- > S&P 500 declined by 7.0% in September, one of the worst-performing developed equity markets, with the decline led by financial and material stocks.
- > This was against a backdrop of mixed economic data. Second-quarter GDP figures were revised upward, while manufacturing and industrial production numbers beat expectations. However, labour market data disappointed, prompting President Obama to announce a significant jobs plan.
- > Furthermore, the Fed launched 'Operation Twist' in an attempt to drive down long term interest rates.
- > Earnings growth estimates at 16.2% for 2011 and 13.6% for 2012 for US companies remain attractive and earnings results for the second quarter of 2011 were stronger compared to the first quarter.
- > US equity valuation measures - such as the 12-months forward PE ratio of approximately 11.1x - continue to look undemanding.
- > Most of the economic data in the US points to a stagnant economy. After the August declines, manufacturing surveys and consumer sentiments have stabilised at low levels.
- > However, it was the Fed's pessimistic assessment of the economy that became a catalyst for 'risk-off' behaviour in the markets this month. The Fed noted "significant downside risks to the economic outlook, including strains in the global financial markets".
- > Investors are reluctant to look at PE valuations, given concerns on earnings revisions. However, about 39% of the S&P 500 stocks with positive earnings, and for which data is available on Bloomberg (around 99%), are trading below the 12x level versus 23% at end September last year.
- > Given the nature of the current economic environment, leading indicators that capture shifts in confidence are particularly useful. Though consumer surveys indicate a drop in confidence, the business surveys are yet to indicate a similar fall, reflecting a more positive outlook among the business community.
- > Overall, we maintain a modest overweight allocation to the US and other equity markets relative to government bonds and cash (based on the attractive valuation measures) while we remain neutral on the US versus other equity markets.

Europe

- > equities suffered alongside other risky assets in September. Eurozone equities fell by 5.8%, due to fiscal concerns and weak economic data. Meanwhile, UK equities were down 4.7%.
- > Within the eurozone, concerns over member countries' debt and growth potential continue to mount and drive equity performance. Ratings agency S&P downgraded Italy's long-term and short-term sovereign ratings by one notch to A/A-1.
- > On the political front, the agency thinks that Italy's fragile governing coalition will continue to limit the government's ability to respond decisively to the challenging domestic and external macroeconomic headwinds.
- > In more encouraging news, policy action was favourable. Major central banks across the developed world announced that they will provide additional US dollar funding to their respective banking systems in coordination with the Fed.
- > The ECB has scheduled three separate US dollar liquidity operations, starting from 12 October, with maturities of approximately three months, in full allotments (i.e. unlimited), which are designed to cover banks' funding needs.
- > In addition, the German parliament showed overwhelming support in extending the German guarantee to an expanded European Financial Stability Facility (EFSF). The decision was greeted in Brussels as a removal of a big potential road block for taking further action on the debt turmoil of the eurozone.
- > Although peripheral fiscal eurozone issues remain a concern and recent economic data releases have been weaker, overall, economic activity remains mildly positive. Whilst the possibility of a technical recession in Europe has increased, we do not expect it to be deep.
- > The growth figures do not indicate a significant enough slowdown to warrant the major earnings downgrades implied by global equity market prices at the moment. Valuations for riskier asset classes, especially equities are unusually compelling, yet they are not driving market performance. For example, a dividend yield of 5.05% (MSCI Eurozone) is attractive relative to 10-years eurozone bond yields, which have dipped below 2%.
- > In addition, our central view is still for rates to remain accommodative in 2011 and 2012 due to the potential impact on fragile growth in the region.
- > Therefore, with earnings growth still looking positive next year, these valuations, particularly relative to bonds and cash, are compelling, and we still favour equities as a long-term investment.

Equity Markets

Japan

- > Japan's equity market remained stagnant in September, as lingering eurozone debt problems and weakening global growth continued to keep investors away from risky assets. Japanese equities actually stayed resilient and decreased by only 0.8% during the month, outperforming other developed countries (the MSCI World declined by 6.0% in September).
- > Recent data suggests that the pace of recovery in Japan may slow as a result of the gloomy global economic outlook.
- > Industrial production continued to improve on a month-on-month basis, rising 0.8% in August. However, the improvement was below expectations of 1.5%, raising concerns of a less robust recovery.
- > Export growth was negatively impacted by a higher yen and lower external demand. Merchandise trade exports grew 2.8% year-on-year in August, missing expectations of 8% year-on-year. The country's trade balance turned negative from 72.5 billion yen in July to -775.3 billion yen in August due to large growth in imports.
- > Retail trade came out softer in August at -2.6% year-on-year (versus 0.7% in July) as consumer sentiment was weakened by a worse global economic outlook.
- > The risk of deflation remained with core CPI unchanged at -0.5% year-on-year in August.
- > The Bank of Japan (BoJ) kept its target rate at 0.1%, as expected, after the September meeting.
- > Risk aversion has continued to drive equities lower while the developments in the eurozone have done little to reverse weak sentiment.
- > We expect equity markets to continue to be volatile and our strategy remains concentrated on the investment value over a longer-time horizon.
- > While we acknowledge the short-term volatility in the stock market, we are confident that Japan will perform relatively better given support from the government's recovery plan.
- > Economic data, such as export growth and industrial production, will inevitably be impacted by slower external demand. However, local demand and retail consumption could help the economy resist falling into a deep recession.
- > We expect that the BoJ will maintain its accommodative monetary policy.
- > The 12-months forward PE ratio is trading at around 11.4x as at the end of September for Japanese equities; this attractive valuation supports our overweight position in Japanese equities, as we seek long-term investment value.
- > Overall, we continue to prefer equities over government bonds and cash because the returns of the latter in real terms are heading towards zero or even negative territory. We also favour Japan within equities due to the support provided by the government's recovery plan and attractive valuations.
- > The continuous strength of the yen could lead to further central bank intervention. Thus, it is reasonable to keep the position on a hedged basis.

Global-Emerging markets

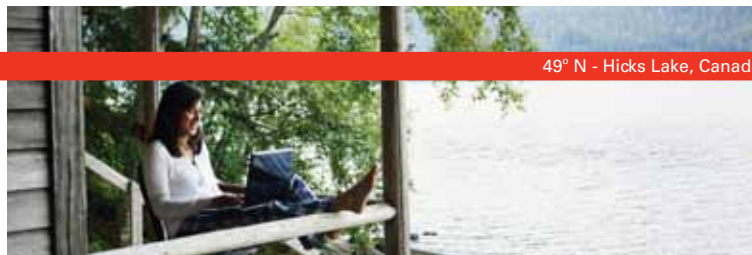
Emerging markets closed the month with negative performance of -7.4% on a total return basis, underperforming developed equities by 1.4%.

Latin America was the relative outperformer, returning -5.3%, with negative performance from Brazil (-4.6%) and Mexico (-5.3%). Asia and Eastern Europe were the relative laggards, returning -8.4% and -10.0%, respectively. Within Asia, negative performance from China, Thailand and Indonesia were the main detractors, while Russia and Hungary provided the main drag on returns in Europe.



- > Economic data over the past month has been mixed. For example, year-on-year industrial production slowed down in China (from 14.0% to 13.5% in August), although this was offset by a marginal increase in the PMI (from 50.9 in Aug to 51.2 in September). Consumer spending also increased by 17% year-on-year in August (from 17.2% in July), as did external trade, with imports and exports (30.2% year-on-year and 24.5% year-on-year in August, respectively) both beating expectations.
- > India fared less well with a decline in both industrial production (3.3% in July versus 8.8% in June) and export growth. Year-on-year exports fell significantly after a record increase last month (81.8% year-on-year in Jul versus 44.3% year-on-year in August).
- > In Brazil, a marginal increase in year-on-year retail sales (from 7.07% in June to 7.11% in July) was offset by a declining PMI (which fell to 46.0 in August, from 47.8 the previous month), prompting an unexpected 50 basis-point cut in policy rates by Brazil's central bank.
- > In Russia, a 2% decline in year-on-year exports (44.7% in June against 42.6% in July) was offset by a greater-than-expected increase in industrial production (6.2% in August versus 5.2% in July). Domestic consumption also remains buoyant, with year-on-year retail sales increasing to 7.8% in August (compared to 5.7% in Jul).
- > Overall, the consensus economic forecasts for GDP growth for emerging markets remain solid, albeit at slightly moderated levels.
- > The decline in emerging market equities has led to a decline in both trailing and forward PE ratios (excluding Brazil, India and Russia). The 12-months forward PE ratio currently stands at 9x, which represents a 20% discount to the five-year average (broadly similar to last month). Relative to the 10-year average valuations, current levels represent a 15% discount.
- > Inflation has started to decline across most major emerging economies, reflecting the impact of recent tightening in monetary conditions and a continuing slowdown in global growth. A breakdown of the data suggests that non-food inflation remains stable, while food inflation is beginning to ease on the back of softening commodity prices.

Equity Markets



- > While fundamentals remain strong, valuations are still attractive and interest rates in the developed world are at multi-year lows, emerging market equities continue to look favourable on a longer-term view. As with other equity markets, we maintain our modestly overweight position and remain neutral between developed and emerging markets.
- > At a country level, we keep our preference for Chinese and Russian equities relative to other emerging markets on valuation grounds. Relative to their five-year average, Russia and China equities' 12-months forward PE ratios are trading at -36% and -38%, respectively, the largest discounts in the emerging market universe.

Asia ex-Japan

- > Asia ex-Japan equities took another hit in September as investors' concerns over growth and eurozone debt intensified. The MSCI Asia ex Japan index slid 9.2% over the month.
- > Industrial production growth moderated in China, falling from 14.0% year-on-year in July to 13.5% in August. Retail sales were largely unchanged at 17.0% year-on-year in August (17.2% in July). However, China's exports in August expanded and exceeded expectations, rising by 24.5% year-on-year (against an expected figure of 21.9%).
- > Export growth in South Korea remained upbeat in August, up 27.1% year-on-year (27.3% in July). However, export growth in Taiwan slowed to 7.2% year-on-year in August, below the 15.5% estimate.
- > China's consumer price index started to fall in August, down to 6.2% year-on-year from 6.5% last month. This is an integral element for the People's Bank of China to slow its pace of tightening in the months ahead.
- > In India, monthly wholesale prices bounced back to 9.78% year-on-year in August after a revised measure of 9.22% last month (compared with 9.44% in June). The RBI subsequently stepped in to raise interest rates by 0.25% to 8.25%.
- > We expect equity markets to continue to be affected by higher volatility while investment sentiment will also be driven considerably by various uncertainties. However, it is not our base case to expect the world to enter into a deep recession and, hence, the lower equity prices we are seeing do offer exceptional investment value over a longer-time horizon.
- > Since a deep recession is not expected, we therefore do not anticipate significant adverse earnings revisions. Besides, earnings expectations have already discounted the current slower growth scenario.
- > We reiterate that Asia ex-Japan equities remain very attractive in terms of their valuation. The 12-months forward PE ratio is trading at 10.1x as at the end of September, which is well below the historical average.
- > Given that equity valuations are close to all-time low levels, we suggest equities will offer a better risk-reward trade-off against low-yield government bonds and cash. Within equities, we continue to favour Chinese equities because of the supportive economic fundamentals.

Latin America

- > Among the emerging markets, Latin American bourses were the best performing, although they still fell by 5.3% overall in September. Brazil slightly bettered the regional average (-4.6%) while Mexico matched the region's return, falling by 5.3%.
- > Equity market performance was set against a backdrop of mixed data. In Brazil, a slight improvement in year-on-year retail sales (up from 7.07% in June to 7.11% in July) was offset by a dip in the purchasing managers index (which fell to 46 in August, from 47.8), prompting an unanticipated cut of 0.5% in policy rates by the Brazilian Central Bank.

- > On the whole, however, the economic performance of Latin American countries remains robust amid encouraging earnings growth estimates for 2011.
- > Moreover, there has already been some progress in the fight against inflation although this is not likely to be fully under control until the final quarter of this year.
- > As such, the economic news seems to be reflected in market prices and relative valuation measures show no strong signals.

Middle East

- > The situation in the Middle East and North Africa remains unsettled, amid ongoing civil unrest in many countries across the region.
- > In the post-revolution states, there is still no clarity on the economic outlook. For example, in Egypt, the economy continues to struggle despite the country agreeing its 2011/12 budget and terms for an International Monetary Fund financing deal.
- > However, where political pressures have been negligible, such as in the United Arab Emirates, Kuwait and Qatar, the economic ramifications of unrest have been positive. This is due to the partial shift in economic activity from the troubled nations to the neighboring Middle Eastern countries, less affected or not affected at all by the turmoil. We continue to monitor events in the region closely.
- > Against this backdrop, valuations remain undemanding and 12-months forward PE ratios are compelling on an historical basis.

Equity Markets

Indonesia

- > Earning season is expected to produce positive surprise in the Indonesian equity market, as exports remained to grow higher than estimates due to the strong business with India.
- > As the central bank took a dovish stance in October's monetary policy, expectation on "cheap funds" showed a good tendency that the government is pro-growth and tolerate inflation. As the inflation are relatively lowered compared to previous months readings, the move from central bank is considered the market to be "ahead of the curve" hence can provide a positive sentiment to the equities.
- > The strong consumption pattern and the consumer confidence index reading in the September's data may support the sentiment towards domestic-oriented stocks such as consumer sectors and local banks. Banks also has big weighting on Jakarta Composite Index, the Indonesian main composite index.
- > As stock-to-earning ratio valuation remains below 15. Sentiment towards Indonesian stocks may remain attractive with another fact that the export-to-GDP ratio is also considered low around 25% (compared to the regional peers' dependency to export as a foundation of GDP growth).

Eastern Europe

- > Eastern European bourses suffered a weak month with Russia and Hungary proving to be the worst-performing markets.
- > Economic data offered a mixed bag. In Russia, a small fall in year-on-year exports for July was countered by a larger-than-anticipated rise in industrial production for August. Meanwhile, domestic consumption continued to rise, with August year-on-year retail sales registering small but not insignificant improvement.
- > From a regional perspective, though economic activity has clearly moderated, encouraging data continues to emanate from the broader Eastern European region.
- > At a country level, we maintain our preference for Russian equities relative to other emerging markets. Russia's economic activity remains robust, while valuations for Russian equities are attractive in both absolute and relative terms.



Fixed Income



US dollar Government Bonds

- > US Treasuries returned 1.76% during September, achieving their biggest quarterly gain (6.73%) since the fourth quarter of 2008.
- > Ongoing concerns surrounding the possibility of a recession, coupled with further action from the Fed, combined to push US government bond yields to fresh lows. The yield on 10-years US Treasuries dropped well below 2%, hitting lows of 1.67% on 23 September.
- > Following their two-day meeting, the Federal Open Market Committee announced that it intends to purchase US\$ 400 billion of longer-dated US Treasuries (maturities between six to thirty years) and sell an equal amount of shorter-dated US Treasuries (maturities of three years or less), by the end of June 2012.
- > The 'Operation Twist' program is designed to lower long-term interest rates to support the economy. The yield curve responded accordingly, with the 30-years Treasury yield dropping by 0.69% over the month as a whole, to end September at only 2.92%.
- > Also, in a positive surprise move, the Fed announced that it will reinvest principal payments from its agency debt and mortgage securities back into debt issued by mortgage financiers (e.g. Fannie Mae), in order to support the mortgage market.
- > The Fed provided a rather pessimistic assessment of the US economy, noting "significant downside risks to the economic outlook, including strains in the global financial markets".
- > Although a 'twist' was widely expected by the market, it was more aggressive than the bond market had been expecting, particularly given the size of the purchases and the emphasis on the longer end of the maturity spectrum (29% of the US\$ 400 billion will be reinvested in 20-30 years maturities, buying nearly all of the planned 30-years issuance until June 2012).
- > While balance sheet expansion is on hold for now, the Fed intends regularly to review the size and composition of its securities holdings and is prepared to adjust those holdings as appropriate.
- > From a fiscal perspective, the ongoing withdrawal of stimulus in the US is likely to continue to restrain economic growth, keeping it at rather anaemic low levels. This is in line with our central scenario for the major developed economies as they deal with gradual debt reduction and greater fiscal restraint.
- > Despite a slowdown in the pace of economic recovery and an anaemic growth outlook, US Treasury yields still appear unattractive both relative to history and to other asset classes. Government bond yields are at extremely low levels and are already pricing in a very weak economic scenario. It is difficult to see much value at these levels. Therefore, we re-iterate our cautious view on the asset class and maintain our preference for corporate bonds within fixed income.
- > As expected, the ECB maintained interest rates at 1.50%. The market is now pricing in a cut of 25 basis points next month with risks to the economy skewed to the downside.
- > However, the initial consumer price index year-on-year estimate for September suggests inflation has risen to 3.0%, which would be the highest level in three years. This has placed additional pressure on the ECB, which aims to keep inflation below 2% to manage stagnant growth and rising inflation effectively.
- > Reflecting the 'risk-off' environment, the German yield curve shifted down significantly across all maturities in September. For example, the 10-years German bond yield fell from 2.22% to 1.89% (a fall of 0.33%).
- > The Consensus forecasts for 2011 and 2012 eurozone GDP growth were both revised down to 1.7% (-0.2%) and 1.0% (-0.5%) respectively in September.
- > The overriding mood in the financial markets is still volatile and long-term uncertainties regarding the economic health of eurozone peripheral countries remain. We do not believe we have seen the last of market volatility resulting from peripheral eurozone fiscal difficulties.
- > Government bond yields are at very low levels (10-years yields are 1.89% in Germany, 1.92% in the US, 1.03% in Japan) and are already pricing in a weak economic scenario. It is difficult to see much value at these levels.
- > Therefore, against this backdrop, we maintain a cautious outlook for eurozone government bonds against cash. Overall, within fixed income, we believe corporate bonds offer better value and are preferred over government bonds.

Eurozone Government Bonds

- > Eurozone government bonds were positive in September, posting returns of 0.8% for the month.
- > There was notable divergence in performance across the region. Greek bonds continued to fall, down 19.9% amid continued speculation over a possible default, while relative safe havens, such as Germany and France, were up by 2.3% and 2.0%, respectively.
- > In a largely expected move, the German parliament showed overwhelming support in extending the German guarantee to an expanded EFSF. The decision was greeted in Brussels as a removal of a big potential road block for taking further action in the debt turmoil of the eurozone.
- > S&P downgraded Italy's long-term and short-term sovereign ratings by one notch to A/A-1 citing the limited ability of the coalition government to respond decisively to the challenging domestic and external macroeconomic headwinds. The yield on 10-years Italian bonds increased to 5.54% from 5.14% at the start of the month.

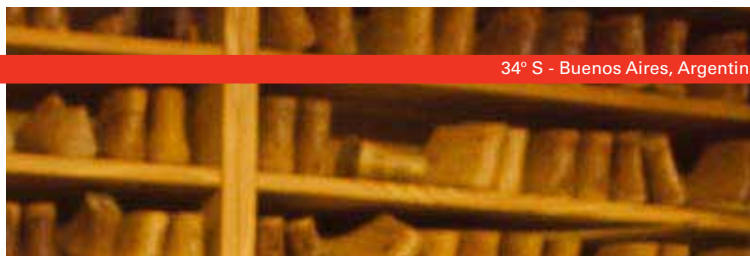
Fixed Income

Investment Grade Corporate

- > Global investment grade corporate debt returned -0.36% during September according to Bank of America Merrill Lynch index data. As in recent months, the performance was driven by an increase in credit spreads as major developed market government bond yields fell over the month.
- > For the year-to-date, investment grade credit is lagging government bond returns, but has still achieved a positive absolute return of 3.50%, given the underlying fixed income rally.
- > The option-adjusted credit spread increased over the month from 2.27% at the end of August to 2.64% at the end of September (according to Bank of America Merrill Lynch data), as risk aversion remained high, reflecting ongoing concerns regarding slowing economic momentum.
- > However, investment grade corporate fundamentals continue to look strong and stable. Credit quality is still seeing positive momentum, with upgrades outnumbering downgrades over the last 12 months, despite the growth concerns over the economy.
- > Companies are still continuing to take advantage of historically low financing rates by issuing significant amounts of debt. For example, US investment grade companies have raised over US\$ 704 billion in bond issues year-to-date, versus a total of US\$ 664 billion during the same period in 2010. Hewlett-Packard raised US\$ 4.6 billion of debt during September, in a four-part offering. However, the company is paying a higher yield compared with bonds of a similar maturity sold four months earlier.
- > Further volatility in risky asset prices seems unavoidable given the unfinished nature of the European peripheral debt crisis, rising global economic challenges and the depletion of fiscal and monetary tools authorities have at their disposal.
- > However, investment grade corporate bonds are not dependent upon a strong cyclical growth outlook for performance, but traditionally have performed well in environments of low or negligible growth.
- > The backdrop of low interest rates is likely to continue to fuel investor demand for yield. The current yield of 4.02% for a diversified index of global investment grade corporate bonds (as measured by Bank of America Merrill Lynch data as at 30 September) remains attractive in comparison to cash or government bonds.
- > Furthermore, valuations in the credit markets are more compelling than at any time since mid-2009 and credit spreads more than adequately compensate for the current default risk.
- > Overall, we believe that the current environment and valuation backdrop are still favourable for credit and, therefore, we continue to prefer investment grade corporate bonds relative to government bonds.



Fixed Income



Sovereign USD-denominated Emerging Markets

- > US dollar-denominated emerging market debt returned negative performance (-4.0%) after seven positive months.
- > The Merrill Lynch US Dollar Emerging Market Sovereign Plus index option-adjusted spread rose steadily over the month. It reached a high of 437 basis points at the end of the month, reaching levels not seen since April 2009, on the back of the on-going sovereign debt crisis in the eurozone and mounting fears of a Greek default.
- > The cost of insuring against default for certain emerging markets remains at similar (or lower) levels to many European developed countries, as the latter continue to be plagued by their debt troubles and emerging markets are rewarded for their fiscal health and resilient growth prospects. For example, the cost of insuring against Portuguese sovereign debt default over the next five years is comparable to that for Venezuela and Argentina, and far exceeds that of Brazil and China.
- > The worsening sovereign debt crisis in Greece continues to stress the markets as a credible solution remains elusive.
- > The persistent slowdown in global growth and strict austerity measures imposed by developed economies continue to haunt investors and underscore the relative strength of emerging economies' balance sheets and their improved credit worthiness.
- > Even so, substantial net outflows are already evident in emerging market government bond markets as investors start to adopt a more cautious stance and confidence in the asset class wanes. That said, funds denominated in local currency (rather than US dollars) have seen the largest outflows due, in part, to the recent currency weakness in emerging markets.
- > Long-term trends of structural fundamentals remain favourable and while spreads on emerging market debt are low by historical standards, they still appear attractive relative to yields available in alternative investments such as developed market government bonds.
- > Although we have a mildly constructive stance on the asset class relative to cash and developed market government bonds, we continue to prefer developed market corporate debt (particularly high yield) to US dollar-denominated emerging market sovereign debt and hence have a neutral recommendation.

High Yield

- > In September, global high-yield corporate bonds posted another monthly negative performance (-3.7%). This takes the year-to-date return down to -2.5% in September, from +1.2% in August.
- > The negative performance was caused by spread widening due to increased risk aversion. Global high-yield option-adjusted credit spreads increased to 8.65% in September, from 7.48% at the end of August, reaching their highest level since the financial crisis of 2008-09. This marks another rise above the 800 basis-point level, usually accompanied by weak economic growth and an upturn in defaults.
- > High-yield issuance increased slightly from last month. However, the US\$ 7 billion of high-yield debt issued in September was much lower than the US\$ 47 billion issued during the same time last year. Although, the year-to-date figures continue to indicate a better issuance this year (US\$ 270 billion) compared to the issuance (US\$ 255 billion) during the same period last year.
- > Increased risk of contagion from the eurozone and the lack of a concrete direction in the global economic slowdown continue to keep high-yield investors on the sidelines.
- > The global annualized speculative grade (i.e. high yield) default rate remains unchanged at 1.9% in September, as measured by Moody's. This remains very low relative to history and reinforces our positive view on the asset class.

- > Our central scenario for a low-inflation, modest-growth environment in developed economies is likely to keep interest rates in these countries low. Therefore, demand for high-yield bonds, which have attractive yields (9.8%), should remain high.
- > We believe high-yield bonds are a good relative investment given that the low default rates are accompanied by attractive yields, while companies remain conservative in their balance sheet management.
- > Overall, we retain our positive view on the asset class. This reflects our continued expectation that: global growth will be positive, albeit at low levels; monetary policy will remain accommodative; and yield-seeking fund flows will continue to be supportive.

Global Inflation-Linked Bonds

- > In developed economies, although it is at higher-than-desired levels, inflation is expected to be relatively contained in the near-term, although monetary easing programmes may stoke inflationary pressures in the longer run.
- > The value of global inflation-linked bonds relative to government issues has improved recently, and we have increased our stance from underweight to neutral.

Indonesia

- > Bank Indonesia surprisingly decided to reduce interest rate in October monetary policy. As this move signalled a stance to prepare against global crisis, the move can also provide positive sentiment to the Rupiah-based bonds.
- > The continuously strong business performance in the local economy is being supportive to grow the GDP as regional demand may weaken. This, combined with the strong local consumer confidence shall help Indonesia to maintain its resilience against global risk.
- > While foreign ownership on Indonesia bonds is signalled to be reduced, the government's strong intervention against the sell-pressure of short-term Indonesia bonds by foreign investors gave a stable price movement of the bonds market.
- > While yield curve is flattening, the sentiment towards short term bonds may be reduced while long term bonds may appear to be more attractive.

Other Investments



Oil

- > Oil prices declined over the month by about 10.8%, making September the second consecutive month with an oil price decline, amid concerns of significant downside risk to economic growth.
- > WTI Crude closed at US\$79.2 per barrel at the end of September, below our target range of US\$90-110.
- > Crude oil price weakness was triggered by the global economic slowdown and bleak prospects for financial markets over the course of September. Oil prices plunged to their lowest levels over the year in tandem with the large sell-off in financial and commodities markets.
- > Driven by both supply disruption to Brent oil and a glut of WTI oil, the price spread between WTI and Brent, the two most important oil benchmarks in the world, continued to widen, hitting record levels of over US\$26 per barrel.
- > If the current positive reports of preserved Libyan oil infrastructure are correct, domestic Libyan production rates could reach 1.3 million barrels per day by the end of the year, lifting supply and further easing price pressures.
- > An outlook of lower global gross domestic product growth has prompted the International Energy Agency to reduce again its forecast for 2011 global oil demand by 200 thousand barrels per day to 89.3 million barrels per day.
- > Global oil supply rose by 1.0 million barrels per day to 89.1 million barrels per day in August, with non-OPEC providing 80% of the total increase.
- > OECD industry stocks rose back again by 10.7 million barrels to 2.687 million barrels or 58.4 days of forward demand cover. However, the International Energy Agency notes that this is the first time total oil industry stocks have slipped below the five-year average since the economic recession of 2008.
- > The global growth outlook remains relatively subdued although our central forecast is for positive growth. Hence we maintain our expectation for oil to trade in a range of US\$90-110 per barrel, on a six- to 12-months view. The risks to this range lie on the downside.

Gold

- > Actions by the Fed are likely to continue to provide liquidity and potentially weaken the US dollar further, both of which are likely to drive commodity prices, including gold, higher.
- > Increased inflationary risks are adding to the attractiveness of holding the metal as well.
- > That said, although recent data releases have been disappointing, the economic recovery remains in place.
- > Balancing these factors, we expect gold will trade in a narrower range of US\$ 1,500 to US\$ 1,600 per troy ounce in the medium-term and maintain our neutral stance.

Commercial Real Estate (unlisted)

- > A delay in the UK economic recovery is likely due to deterioration in global economic conditions and persistent eurozone sovereign debt concerns. Accommodative monetary policy is likely to be prolonged, sustaining a substantial property yield margin relative to bond rates.
- > We believe Asia Pacific has the best long-term economic fundamentals among the regions. However, the heady pace of rental growth is likely to moderate in the event of a global economic slow-down. This is expected to prompt a correction in current aggressive pricing, particularly for prime retail property.
- > In the US, the sharp deceleration in GDP is expected to persist and unemployment will likely stay at elevated levels. Occupier markets are predicted to remain subdued and positive rental growth is unlikely to manifest until there is a substantial improvement in the economy.
- > With a worsening economic outlook in Continental Europe, we believe occupier markets would be challenged to continue the rental growth that started in the fourth quarter of 2010. However, limited new supply provides support for current rental levels, particularly for core markets where tenant demand should be relatively resilient.
- > Our outlook for property remains neutral. The risks from the impact of the economic slowdown are counteracted by the reduction in supply (given slowing bank funding) and property's attractive yield relative to government bonds.

Currency



- > The US dollar found favour from investors in September. Against the yen, it rose by just 0.5%, but gains were larger against sterling (+4.3%) and the crisis ridden euro (+7.7%). The driving force was the US dollar's perceived 'safe haven' status in a world with few other such options.
- > Many emerging market currencies suffered substantial falls against major currencies. The Brazilian real fell over 18% against US dollar and the Russian rouble by 11.6%. Concern in these economies is switching from inflation to slowing growth, suggesting the interest rate support that previously helped fuel currency appreciation will be reversed. Indeed, Brazil surprised the market with a 0.5% cut in interest rates.
- > The notable exception to this was the Chinese renminbi where the onshore currency was virtually unchanged against the US dollar. Further small steps have been taken by the Chinese authorities to increase the convertibility of the renminbi and officials have been talking about their aim of future full convertibility.
- > Safe haven currencies are becoming scarce. The Swiss National Bank has, so far at least, successfully capped the appreciation of the Swiss franc. The previously high-flying Australian dollar is now less attractive because of softening commodity prices and Norwegian krone liquidity was never sufficient for the major players. This leaves the US dollar, which, despite the rating downgrade of US sovereign debt by Standard & Poor's last month, despite the faltering economy and low interest rates and despite probably unsustainable levels of government debt, is finding support.
- > The euro will continue to be buffeted by the uneven process of finding a resolution to the debt crisis of the peripheral eurozone countries. Our central forecast is that this will occur, but will be protracted, and politics will play a large part, making the task of analysing the euro that much harder. Furthermore, the ECB is likely to ease monetary policy, a move that is not supportive for the currency.
- > The Japanese yen continues to be capped by the threat of intervention and sterling has little to recommend it, as interest rates will remain low, further quantitative easing is possible, if not probable, and growth remains anaemic. For now, the US dollar looks the winner of this 'ugly' contest but, with many risk factors and political dependencies, we maintain our recommendation for neutral currency positions.

Long-Term Investment Outlook (three to five years)



ASSET CLASS	CURRENT VIEW	REASONING
Developed market equities	Positive	<ul style="list-style-type: none"> Average rate of growth somewhat subdued in the developed world. Yet exposure to higher growth areas like emerging markets will benefit earnings growth and dividend growth and are likely to keep average nominal returns at high single digit levels.
Emerging market equities	Positive	<ul style="list-style-type: none"> Expected to outperform developed market equities thanks to a favourable structural backdrop including improved fiscal management and trade balances, labour force expansion and rapid urbanisation.
Developed market sovereign bonds	Negative	<ul style="list-style-type: none"> Comparatively low level of yield and issues around public debt are likely to keep average returns relatively subdued
Developed market credit	Positive	<ul style="list-style-type: none"> The level of spread continues to be attractive on a historical basis and corporate balance sheets in developed markets are generally in good shape. This is likely to keep average return for credit assets above respective government bonds.
High Yield	Positive	<ul style="list-style-type: none"> The level of spread continues to be attractive on a historical basis and corporate balance sheets in developed markets are generally in good shape. This is likely to keep average return for high yield credit assets above respective government bonds.
Emerging market debt	Positive	<ul style="list-style-type: none"> Structural improvements such as improved fiscal management and trade balances, labour force expansion and rapid urbanisation along with reasonable valuation levels are likely to lead to outperformance of emerging market debt relative to cash and developed market sovereign debt.
Developed market inflation-linked bonds	Neutral	<ul style="list-style-type: none"> Inflation expectations are likely to remain contained due to subdued growth in developed markets. In addition, independent central banks are focused on keeping price pressures under control. Furthermore, valuations for this asset class have deteriorated. However, if higher inflation in emerging markets is not dealt with effectively, it could feed through to developed markets over the medium-term.
Commodities	Positive	<ul style="list-style-type: none"> Growth in emerging markets likely to remain an element of support for this asset class.
Developed cash rates	Negative	<ul style="list-style-type: none"> Subdued economic growth and stimulus measures are likely to keep rates at low levels for the foreseeable future

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