

**Market Report
1Q2010
18 January 2010**

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ECONOMIC OVERVIEW

The global recovery continues to maintain momentum. Analysts are forecasting growth in 2010 of 2 – 4%, a marked improvement on the contraction of - 2.5% and - 0.8% for 2009. The economies of the Asian region are in general experiencing better growth than that of the rest of the world, reflecting more robust domestic demand which mitigates the impact of weakness in the more developed economies.

Existing government stimulus programmes remain central to the theme of the recovery and are expected to remain so for the majority of 2010. Monetary policy is also expected to remain accommodative as muted inflation in the developed world gives central banks the space they require to delay or minimize rate hikes. The US Federal Reserve, in particular, is likely to keep rates low, given the low inflationary outlook and the historically high level of unemployment (currently c.10%). While other central banks are likely to normalize rates during the course of the year, the degree of tightening is likely to be restrained by a reluctance to heighten the pressure on their currencies to appreciate relative to the Greenback. China's capacity to sustain government-mandated investment is another positive macro factor for global demand; in 2010, the flow-through effect of existing projects should serve to sustain high levels of Fixed Asset Investment. With only a 3% budget deficit and a 20% debt-to-GDP ratio, China has the room to move should further assistance be required.

While the economic picture is broadly encouraging, it is important to emphasize that it is not without risk and relies to a significant extent on the ability of the global economy to transit from government support to a mode which is more self sustaining; and at this point private demand-led growth is by no means assured. The US consumer, the traditional source of global demand, is facing several long-term structural issues, namely, household deleveraging, weak bank lending and high unemployment. This notwithstanding, marginal improvements may outweigh already-known structural problems in the short term as far as market sentiment is concerned. There are increasingly signs of such short-term stabilization, such as the bottoming out of household wealth as well as positive trends in initial jobless claims.

The very governmental actions that saved the global economy from collapse have also introduced new vulnerabilities into the global economic system. Many of the major developed economies are now facing double-digit fiscal deficits and are closing in on 100% of debt-to-GDP. This presents a major policy dilemma, as premature fiscal tightening could cause economic recovery to falter in the later part of 2010 after stimulus effects begin to fade, but failure to address debt sustainability could lead to sharply higher bond yields. On the monetary side, the massive expansion of central bank balance sheets and corresponding concerns over exit strategies could cause longer-term inflationary expectations to rise and/or major currencies to depreciate significantly over the long term.

In contrast to the developed world, the main risks in China are asset bubbles and associated policy risks. For now, China has some breathing room in terms of consumer price inflation because of excess capacity in the manufacturing sector. However, China already has most of the economic ingredients for a bubble, such as excess liquidity and excessive investment growth; a major saving grace is that private sector leverage in China is currently still low. On balance, our view is that the Chinese bubble is still in a formative stage, and the Chinese government is likely to maintain economic growth as a priority due to the overarching need to absorb the unemployed by way of economic growth. However, policy risks bear watching as authorities may take targeted measures to dampen asset prices, e.g. in the property market through controlling bank lending.

Our macro base case for 2010 is thus one of recovery with some tail risks. We expect risk assets to continue to benefit as the positive recovery momentum carries through into early 2010, supported by accommodative policy, acceptable market valuations and adequate liquidity. However, both the economy and markets remain vulnerable to setback because of continuing structural headwinds in US consumption, risks related to sovereign debt sustainability and growing asset bubbles in China.

EQUITIES

US

United States		31-Dec-09		
Market performance		Last close	%3M chg	%YTD
MSCI USA		2,600.7	5.9	26.3
S&P 500 INDEX		1,115.1	5.5	28.3
DOW JONES INDUS. AVG		10,428.1	7.4	22.9
NASDAQ COMPOSITE INDEX		2,269.2	6.9	50.2
Exchange rate		Last close	%3M chg	%YTD
US\$/¥		93.0	3.7	2.6
€/US\$		1.4	(2.2)	2.5
£/US\$		1.6	1.2	10.8
CHF/US\$		1.0	(0.1)	(3.1)
US\$/S\$		1.4	(0.3)	(1.8)
MSCI USA		2009E	2010E	2011E
EPS growth (%)		1.2	26.3	20.7
P/E (x)		18.3	14.5	12.0
P/B (x)		2.2	n/a	n/a
DY (x)		1.9	n/a	n/a

Source: Bloomberg, Citi, Credit Suisse, Thomson, CEIC, MSCI

Market Review

As the financial crisis abated, the US stock markets staged a strong rebound in 2009 on the back of better-than-expected corporate earnings and economic data. The S&P 500 index rallied 28.3% to deliver its best annual gain since 2003. However, even after this massive rally, the S&P 500 index is still not back to September 2008 level before Lehman filed for bankruptcy.

Most of the year's advance is the result of a consecutive three-quarter rally that has been underpinned by the strength in technology and natural resource shares, on expectations that the economic recovery will spur capital spending and increase demand for metals and other natural resources. The technology and materials sectors gained 59.9% and 45.2% respectively. Defensive sectors such as telecoms, utilities and consumer staples were the worst performing sectors. Mid-cap stocks outperformed both large and small cap stocks while growth was favored over value.

A low interest rate environment, coupled with brighter economic prospects, also spurred a rebound in M&A activities. Exxon Mobil paid \$41 billion for XTO Energy to gain access to natural gas production in shale formations. The pharmaceutical sector also saw two colossal deals with the acquisitions of Wyeth and Schering-Plough by Pfizer and Merck respectively as large pharmaceutical companies seek growth via acquisitions to offset patent challenges.

Outlook/Strategy

US GDP is expected to grow by low single digits in 2010 as economic momentum continues, led by inventory restocking, improvement in capital spending and fiscal stimulus. However, in the long term, the US macroeconomic outlook will be capped by both consumer and government deleveraging. Given benign inflation outlook, the Fed is unlikely to tighten monetary policy in 1H 2010.

The majority of the S&P 500 companies reported third quarter earnings ahead of expectations primarily due to aggressive cost cuts and provided constructive outlooks for the fourth quarter. We expect the corporate earnings outlook to continue to improve in the near term given rising industrial activity, tight cost controls and the benefit of operating leverage. Consensus expectations for S&P 500 earnings are growth of 26.4% in 2010 underwritten by productivity improvements pushing margins from 3Q09 cycle trough of 3.4% to near peak levels of 7.7% by 4Q10. Given this as a backdrop it is difficult to see that there is room for significant upward earnings revisions in the short term. Given the run seen in the market during 2009 investors are likely to look for supporting evidence of further progress before committing additional funds, they are also likely to be watchful of the potential for an unexpected development with regard to an upward move in interest rates as well as the impact of the withdrawal of government stimulus measures.

In terms of valuation, the US market is fairly valued with the S&P 500 trading at 14.5x consensus forward price earnings, in line with its long-term average of 14.1x. In order to advance higher, the market will require further earnings upside.

In general, we expect the producer and corporate sectors to outperform the consumer sector as utilization rates rebound and capital spending recovers. Unlike the consumer sector, the corporate sector is under-invested and under-leveraged. Recent rebound in business confidence indicators and capacity utilization rates also bode well for a recovery in capital spending. Capital goods and technology companies with exposure to enterprise IT spending such as Oracle, Cisco and IBM are beneficiaries of a recovery in capital spending.

We remain cautious on US commercial real estate (CRE) given the rapidly rising loan delinquencies, which are a leading indicator of loan losses. Regional banks have the largest exposure to CRE loans and as such, we maintain our underweight position in regional banks.

EUROPE

Europe		31-Dec-09		
Market performance		Last close	%3M chg	%YTD
MSCI EUROPE		3,381.5	4.0	27.7
DJ STOXX 600 €Pr		253.2	4.4	30.9
S&P EUROPE 350 INDEX		1,049.2	4.9	29.6
Exchange rate		Last close	%3M chg	%YTD
€/US\$		1.4	(2.2)	2.5
£/US\$		1.6	1.2	10.8
CHF/US\$		1.0	(0.1)	(3.1)
US\$/NOK		5.8	0.4	(16.7)
US\$/SEK		7.2	2.9	(8.6)
MSCI EUROPE		2009E	2010E	2011E
EPS growth (%)		(21.1)	26.7	21.5
P/E (x)		15.8	12.5	10.3
P/B (x)		1.7	n/a	n/a
DY (x)		3.2	n/a	n/a

Source: Bloomberg, Citi, Credit Suisse, Thomson, CEIC, MSCI

Market Review

MSCI Europe staged a strong recovery ending the year up 32.4%% in Singapore dollar terms after a shaky start to the year. European equity markets touched a 6-year low in early March, on expectations that a “depression like” economic scenario would pan out and as the financial crisis intensified. European equity markets subsequently recovered as the economic gloom lifted when governments announced unprecedented fiscal and monetary stimulus measures. In addition, concerns over the financial crisis faded as some European banks announced better-than expected results while others managed to raise capital to shore up their capital bases.

The Materials sector performed strongly during the year, rising 75% as metal prices rose with copper rising approximately 120% on resurgent demand from China. The Industrial sector also performed strongly rising 36.6% on expectations that the global economic recovery will result in a revival in capital expenditure.

The Finance sector was initially plagued by concerns over capital adequacy and writedown of their legacy assets which resulted in the bailout of Anglo Irish Bank and Bank of Ireland by the Irish government, Royal Bank of Scotland and Lloyds by the UK government and Hypo Real Estate by the German government. Confidence in the sector subsequently improved as some of the better quality banks managed to shore-up their capital bases and also announced better-than-expected 1Q09 and 2Q09 results. News that ING Groep had agreed to EU demands that it sell its insurance units to secure approval for its bailout by the Dutch government so that it did not have an “unfair advantage” also had a negative impact on UK and Irish banks that had received large state bailouts, as the EU may also demand that these banks divest some of their assets. In addition, the downgrading of Greek sovereign credit ratings had a negative impact on Greek banks. The sector gave up some of its gains to eventually end the year up 40%.

The performance of the Utilities and Technology sectors lagged the market on the lack of a near-term catalyst, with Utilities suffering from its defensive characteristics.

There has been an uptick in M&A activity as companies seek to extract additional synergies through consolidation. Volkswagen announced that it had taken a 42% stake in Porsche AG, which

will eventually be merged into Volkswagen by 2011. Kraft Foods made an opportunistic takeover bid for Cadbury, which was rebuffed by the Cadbury Board. In the telecoms sector, Deutsche Telekom and France Telecom agreed to merge their UK mobile businesses creating the largest mobile operator in the UK. AXA SA has also teamed up with AMP to acquire AXA Asia Pacific with AXA SA gaining control of businesses outside Australia and New Zealand.

Outlook/Strategy

3Q09 earnings were generally positive with 58% of the companies reporting results that were ahead of analysts' expectations. The better-than-expected results were achieved as a result of cost cuts, as such, when revenue growth recovers, operating leverage will be higher and profitability will improve. Generally, companies have guided that 4Q09 business outlook is expected to see improvement on a sequential basis. As a result of the positive earnings surprises and guidance, the Financial, Consumer Discretionary and Material sectors saw earnings upgrades for 2010.

Looking ahead into 2010, we expect the cyclical economic recovery to support European equities underpinned by a rebound in earnings growth. MSCI Europe consensus earnings are expected to rise 27% in 2010. In terms of valuations, MSCI Europe trades at 12.5x consensus 2010 earnings, reasonable when compared to its long-term average of 13x. Following the sharp market re-rating and multiple expansion seen in 2009, we expect that further upside will be earnings-driven. While we remain neutral on the market overall, we continue to maintain our overweight position in the Materials sector as we expect it to continue to benefit from government fiscal spending programmes. We are also overweight the luxury goods sector as we believe that this sector has unique portfolio of strong brands that will benefit from the global recovery in consumption spending. Areas where we remain watchful include premature withdrawal of fiscal stimulus and monetary easing which could result in an economic slowdown. We also remain watchful over the possibility that a sharp rise in US commercial real estate delinquency rates may have a negative impact on the loan books of some banks.

JAPAN

Japan		31-Dec-09	
Market performance			
	Last close	%3M chg	%YTD
MSCI JAPAN	931.2	1.1	9.1
TOPIX INDEX (TOKYO)	907.6	(0.2)	6.2
NIKKEI 225	10,546.4	4.1	20.6
Exchange rate			
	Last close	%3M chg	%YTD
US\$/¥	93.0	3.7	2.6
MSCI JAPAN			
	2009E	2010E	2011E
EPS growth (%)	(116.1)	n/a	86.9
P/E (x)	(68.0)	33.2	17.8
P/B (x)	1.2	n/a	n/a
DY (x)	1.7	n/a	n/a

Source: Bloomberg, Citi, Credit Suisse, Thomson, CEIC, MSCI

Market Review

MSCI Japan finished the year up 9.1% after plumbing 25 year lows in March as concerns mounted over the deteriorating global economy and plunging corporate earnings. Thereafter, the market recovered on signs of stabilization in the global economy as the effects of worldwide government stimuli were felt. In this regard, the swift recovery of the Chinese economy was helpful for Japan. But the overall picture was not positive as Japan felt the full effect of a weak domestic economy which was undermined by a lack of consumer and corporate confidence; the effect of significant contraction in demand from the developed economies of the world which constitutes its major trading partners also took its toll.

During the year the Liberal Democratic Party (LDP) lost power for the first time since 1955 (save for a brief period in 1993) when the Democratic Party of Japan (DPJ) scored a landslide victory in the Lower House elections in August. Despite initial expectations of DPJ policies boosting domestic consumption, early moves by the new DPJ government were discouraging, including reversing some of ex-Prime Minister Koizumi's reform efforts such as to privatize Japan Post and adopting a sanguine attitude towards a strong yen. The newly-appointed Minister for Financial Services, Shizuka Kamei, also lashed out against Japanese companies' employment policies and capitalism in general while trying to implement a debt moratorium for small enterprises in Japan. This coupled with the strong yen, weak corporate profits and large capital-raising efforts by major companies, investor sentiment on the Japanese market was severely dampened and the market recovery lagged that of most global stock markets.

During the quarter, global cyclical sectors such as automobiles, electronics, machinery and industrial materials outperformed as these sectors rebounded from the sharp sell-off in 2008. While defensive sectors such as utilities, railways and telecoms that held up better in 2008 suffered reverses. Financials also did poorly, largely reflecting the capital raising done during the year and further capital raising expected in the coming year.

Outlook/Strategy

We expect current conditions of weak corporate profit and poor domestic consumption to persist in the short term. We also expect the strong yen and weak demand to increase deflationary pressures in Japan, and should spur the new government into more fiscal stimulus for 2010. The

Bank of Japan (BOJ) is also likely to be forced into more monetary easing measures to help contain deflation. Together, these measures may put a brake on the current down-cycle.

A potential upside surprise may come in the form of a sustained recovery in global demand, leading to a stronger export recovery for Japanese exporters and continued improvement in corporate profits. However, it still remains to be seen if the fiscal and monetary stimuli implemented by governments globally in 2009 will create a virtuous self-sustaining recovery in 2010.

Despite its underperformance relative to the rest of the global markets, the Japanese market is still not attractive on earnings-based valuations, mainly because of low profit expectations as exporters have to contend with both weak demand and a strong yen. However, asset-based valuation measures remain low when compared to historical averages and potential for re-rating is high if Japanese companies can demonstrate their ability to regain their profitability amidst adverse conditions.

We remain cautious on the market given the current negative operating environment for companies and the potential share overhang on the market from capital-raising exercises. Given the ongoing stagnation in the domestic economy we continue to focus our attention on those companies positioned to benefit from the recovery in the global economy. The strength in the yen is obviously a concern and as such we are seeking to identify those companies with an ability to improve their efficiency and operational gearing through cost containment or possibly earnings accretive corporate activity. We expect the long-term themes of exposure to the high growth economies such as China and India, alternative energy, environmental services and the services related to the demands of Japan's aging population to remain relevant. In the short term, the technology sector is interesting for its strong growth momentum and a wide range of growth themes such as LED lighting and Windows 7 adoption.

ASIA PACIFIC EX-JAPAN

Asia Pacific ex-Japan		31-Dec-09		
Market performance		Last close	%3M chg	%YTD
MSCI AC ASIA PACIFIC		130.2	3.3	32.5
MSCI AC ASIA x JAPAN		265.8	5.7	66.7
MSCI AC ASIA PAC EX JAPN		242.4	4.9	58.3
Exchange rate		Last close	%3M chg	%YTD
A\$/US\$		0.9	1.7	27.8
US\$/CNY		6.8	0.0	(0.0)
US\$/HK\$		7.8	0.1	0.1
US\$/INR		46.5	(3.3)	(4.7)
US\$/IDR		9,403.8	(2.7)	(15.4)
US\$/KRW		1,164.0	(1.2)	(7.6)
US\$/MYR		3.4	(1.0)	(1.2)
US\$/PHP		46.2	(2.5)	(2.9)
US\$/S\$		1.4	(0.3)	(1.8)
US\$/TW\$		32.0	(0.5)	(2.5)
US\$/THB		33.4	(0.2)	(3.9)
US\$/VND		18,479	3.6	5.7
MSCI AC ASIA PACIFIC		2009E	2010E	2011E
EPS growth (%)		75.7	40.3	20.7
P/E (x)		22.2	15.9	13.1
P/B (x)		1.6	n/a	n/a
DY (x)		2.1	n/a	n/a
MSCI AC ASIA x JAPAN		2009E	2010E	2011E
EPS growth (%)		17.2	28.6	15.9
P/E (x)		18.2	14.1	12.2
P/B (x)		2.1	n/a	n/a
DY (x)		1.9	n/a	n/a
MSCI AC ASIA PAC EX JAPN		2009E	2010E	2011E
EPS growth (%)		3.5	22.5	17.7
P/E (x)		18.3	14.9	12.7
P/B (x)		2.1	n/a	n/a
DY (x)		2.4	n/a	n/a

Source: Bloomberg, Citi, Credit Suisse, Thomson, CEIC, MSCI

Market Review

2009 saw an impressive rebound of Asian stock markets, thanks largely to an unprecedentedly loose monetary policy and massive fiscal stimuli by governments around the region and world. In local currency terms, the benchmark MSCI Asia Pacific ex-Japan registered a 58% gain for the year, outperforming MSCI AC World by 29%, and up 75% from its lows in March.

China, the engine of growth in Asia continues to gain prominence with no signs of slowing down and has become the largest export market for the regional economies. Indeed, it is expected to have overtaken Germany as the largest export market globally in 2009. Meanwhile, the investment revival in India provides a positive backdrop to Indian corporates and the economy. Regional corporate earnings were boosted by the inventory restocking cycle as well as cost cutting measures. By and large, reported earnings continued to surprise on the upside while earnings estimate revisions maintained their positive momentum for the last eight consecutive months. By the close of the year, earnings per

share growth for year 2009 was projected in positive territory ($\approx 3\%$) compared with a negative 8% at the start of the year, while 2010 growth is expected to exceed 20%; the highest in the world.

The accelerating growth (macro and corporate) in the region continued to attract foreign fund inflows, particularly from the re-allocation of funds away from developed markets as investors' risk appetite normalized. The net inflow for Asia ex-Japan was US\$19 billion for the year, offsetting the net outflow in 2008. The key beneficiaries were Korea, Taiwan and India with a net inflow of US\$25.7 billion, US\$15.6 billion, and US\$15.3 billion respectively.

For the year, all the Asia Pacific ex-Japan markets registered gains in local currency terms, led by Indonesia (+95%), India (+94%), Taiwan (+75%) and Singapore (+70%). The Vietnamese market was impacted by the 5% devaluation of the Dong in early December, as the country's trade deficit swelled and the market retreated 15% to close the year 60% higher. By sector, the return was positive for all with the cyclicals outperforming the defensive sectors. Information technology sector topped the chart, up 103%, followed by consumer discretionary (+93%), materials (+68%), and financials (+60%). Telecommunication services sector was the laggard (+5%) as it was affected by more intense competition.

Outlook/Strategy

With the steep recovery of the Asian markets, valuations have risen from their distressed levels in 1Q09 to around mid-range of historical valuations. On forward 2010 price to earnings, it is 14.9x compared to long term average (20-year) of 16x while on price-to-book, it trades on 2.1x vs historic average of 1.6x. However, for the region as a whole, returns on equity have been on a rising trend reflecting the region's positive economic momentum and productivity improvements. Balance sheets have been strengthened, with average net gearing of 26% compared with 42% pre-Asian crisis in 1997.

As the markets have fairly priced in the expected earnings for 2010, fulfilment of earnings expectations and confidence in 2011 earnings expectations are essential catalysts for further market upside. China's announcement in mid-December that year-on-year inflation has turned positive is a signal that rising inflation is likely to be a key theme regionally in 2010. We believe that this is likely to incentivize the private sector to increase capital expenditure as well as provide pricing power to suppliers.

In view of our base case for low growth in the global economy, we believe that central banks are likely to keep interest rates low in the near term. Upside inflation risks through rising commodity prices are the major risk factor. However, we believe that governments are more likely to normalize rates as the year unfolds rather than attempt to manage the economy through artificial measures. As such, we expect investors' risk appetite to remain high in a low-rate environment, further supported by re-allocation of funds to emerging Asia.

Our strategy is to be fully invested, and be selective on sectors and markets. Apart from our constructive view on China and India, for their long term structural growth, we are sanguine on Taiwan as we expect that improvement in cross-strait ties culminating in the Economic Co-operation Framework Agreement (ECFA) will set the stage for a secular re-rating of the market. Increased confidence in the long-term prospects of Taiwan has already seen capital repatriation.

Within the region, we view the consumer and healthcare sectors as long-term themes in Asia. Rising middle class and affluence, coupled with China's change in growth model to one that is domestic-driven will directly benefit these sectors. With more infrastructure being rolled out as a result of the stimulus programme, the resource/upstream sectors are also beneficiaries. We like the upstream oil, cement, steel and gold sectors. The financials sector, including real estate, will also continue to benefit from asset reflation as real rates stay low.

- **AUSTRALIA**

Australia		31-Dec-09		
Market performance		Last close	%3M chg	%YTD
MSCI AUSTRALIA		3,216.4	3.0	36.8
S&P/ASX 200 INDEX		4,870.6	2.7	34.5
Exchange rate		Last close	%3M chg	%YTD
A\$/US\$		0.9	1.7	27.8
MSCI AUSTRALIA		2009E	2010E	2011E
EPS growth (%)		(19.9)	0.6	20.8
P/E (x)		17.2	17.1	14.1
P/B (x)		2.1	n/a	n/a
DY (x)		3.7	n/a	n/a

Source: Bloomberg, Citi, Credit Suisse, Thomson, CEIC, MSCI

Market Review

While 2008 saw a record decline in the Australian market, 2009 witnessed one of the strongest rebounds of the past twenty years. Leading indicators at this time last year suggested that Australia could not escape a recession. What eventuated was that Australia managed to avoid serious damage in the global downturn, aided by quick and aggressive fiscal stimulus and an unprecedentedly relaxed monetary policy. Australian corporates also did their part, raising capital quickly and avoiding large scale job cuts. In Singapore dollar terms, the market's return was one of the strongest in recent years, returning 72%, helped by a sharp rally of the Australian dollar. Materials performed strongly within the market, followed by consumer discretionary and financials as investors unanimously preferred cyclical exposure over defensive ones.

Interest rates and the currency were a major focus during the year. The strong Australian currency proved to be an accurate leading indicator of the global and domestic economy. Once momentum in the domestic economy became increasingly clear, the Reserve Bank of Australia surprised the market with interest rate hikes, beginning in 4Q09. Over the second half, the trend in economic data remained positive, supporting the momentum seen in the markets. The employment data was the standout with the unemployment rate declining from 5.8% to 5.7%; with about 100,000 jobs added.

Portfolio Positioning

The portfolio is overweight in materials, consumer discretionary and healthcare stocks. Within materials, we prefer stocks in the bulk commodities and precious metals spaces, which in our view should benefit from low global interest rates and economic recovery. Our holdings in the consumer discretionary sector comprise stocks with exposure to media and non-domestic consumer spending. We are wary of domestic consumer spending stocks given strong outperformance in 2009 and rising interest rates. Healthcare stocks continue to look interesting to us, not only because of underperformance in 2009, but also because of the possibility of a stronger US dollar. We have gone to an underweight position in the financial sector following a strong run in the shares across the sector.

Outlook/Strategy

Growth momentum intact

The first half next year should see a sequential acceleration in GDP growth, supported by a bounce in dwelling investment and rising consumption volumes. The second half should then experience some sequential moderation reflecting the lagged impacts of tightening financial conditions, fiscal fade and some slowing in the contribution from the housing rebuild. Recent earnings upgrades have been broad based across cyclically exposed sectors and stocks, both domestic and increasingly global. Into February 2010's reporting season, we expect to see negative effects of the strong AUD becoming a headwind, although earnings momentum for much of 2010 should be on an improving trend.

Merger and acquisitions to re-emerge

Aggressive capital raisings in the midst of the global financial crisis have resulted in the financial leverage of Australian companies declining to below long-term averages. Given that an anticipated drastic slowdown in the domestic economy did not emerge, Australian corporates appear to be sitting on too much capital. With the economy and earnings outlook recovering strongly, and capital becoming more available, potentially the excess capital will be used for merger and acquisitions. Domestically, this process has begun with the announcement of a number of takeover bids, and increasingly we should see Australian companies active in making offshore acquisitions to capitalize on the still-strong Australian dollar. On balance, we believe that the liquidity boost from increased M&A activity will be a positive driver for equity markets.

Looking for value

Investors remain focused on the length and duration of the recovery phase with a specific focus on how much earnings leverage will emerge in FY11 and what is being priced into shares. The recent outperformance of the cyclical stocks has resulted in the majority now demanding a premium rating, suggesting current forecasts will need to surprise on the upside to justify any further outperformance. As such, it makes sense to look at what has been left behind in this rally of cyclical sectors and stocks and examine closely the drivers and assumptions being made in their valuations. Primarily, the media, leisure, telco and healthcare sectors look attractive on both a price-to-book and PER basis.

- **CHINA/HONG KONG**

China/Hong Kong		31-Dec-09	
Market performance	Last close	%3M chg	%YTD
MSCI CHINA	357.3	9.6	62.4
SHANGHAI SE COMPOSITE IX	3,277.1	19.0	77.1
SHENZHEN SE COMPOSITE IX	1,201.3	28.2	112.6
MSCI HONG KONG	40,056.3	3.6	60.2
HANG SENG INDEX	21,872.5	4.1	52.7
Exchange rate	Last close	%3M chg	%YTD
US\$/CNY	6.8	0.0	(0.0)
US\$/HK\$	7.8	0.1	0.1
MSCI CHINA	2009E	2010E	2011E
EPS growth (%)	14.8	22.1	16.2
P/E (x)	17.1	14.0	12.0
P/B (x)	2.7	n/a	n/a
DY (x)	1.9	n/a	n/a
MSCI HONG KONG	2009E	2010E	2011E
EPS growth (%)	(6.7)	15.9	15.0
P/E (x)	20.0	17.3	15.0
P/B (x)	1.6	n/a	n/a
DY (x)	2.6	n/a	n/a

Source: Bloomberg, Citi, Credit Suisse, Thomson, CEIC, MSCI

Market Review

MSCI China and the China A-shares rebounded more than 62% and 97% respectively in 2009 on aggressive government stimulus and the deep retrenchment of 2008, which represents one of the largest trough-to-peak swings in recent years. For MSCI China, information technology and consumer stocks were amongst the best performing sectors while the worst performing sectors were telecom services and utilities. In the A-share universe, the consumer and energy sectors were the best performing while utilities was the worst. Likewise, MSCI Hong Kong rose 60% in 2009, with telecommunication services, information technology and financials being the best performing sectors, and utilities/industrials being the worst.

China's stimulus package has fed through to the economy. Market consensus expects China's GDP to grow by 8.7% in 2009, exceeding the 8% official target. With the benefit of hindsight, the Chinese economy has been recovering from a relatively brief below-trend growth period and has begun a new expansion cycle. The recovery has been led by domestic demand, and in particular infrastructure investment. Real estate investment also surprised on the upside, as property developers have responded aggressively to the strong recovery in the property market. Retail sales growth has remained resilient. The export sector has experienced sequential improvement, suggesting that the worst in the export sector could be behind us. The Purchasing Managers Index (PMI) has stood firmly above the 50 mark over the past few months, indicating a solid expansion in industrial activity. The employment component has picked up to above 50 in the latest National Bureau of Statistics PMI series, suggesting improvement in employment and consistent with recovery of the labour-intensive manufacturing sector. Inflationary pressure remained subdued throughout the year, providing ample flexibility for accommodative fiscal and monetary policies.

The recent macroeconomic data from Hong Kong indicated that the economy is recovering; 3Q 2009 GDP reveals a smaller year-on-year contraction of 2.4%. The government upgraded its 2009 GDP forecast from the -3.5% to -4.5% which was set in August, to -3.3%. Both exports and imports showed a slight improvement of 1.3% and 6.5% respectively after 11 consecutive months of contraction. Unemployment continues to fall, from a peak of 5.4% in August, to 5.1% in November. Tourist arrivals have turned positive since July while retail sales growth picked up from September. Since June, Hong Kong's hotel occupancies continued to recover with room rate declines moderating. Property transactions remained buoyant due to low interest rates and the recovering economy.

Outlook/Strategy

China's economy is likely to return to trend growth in 2010 with consensus forecasts of GDP growth in 2010 at c.9.8%, and is expected to remain the bright spot globally in terms of growth prospects in the medium to longer term. China's growth is underwritten by a combination of the potential for further productivity gains from a low base, a strong external financial position, a relatively robust financial/banking system which will facilitate economic growth, and an effective policy transmission mechanism.

There have been concerns about policy normalization/tightening efforts by the Chinese government for example, increased capital requirements in the banking sector, administrative measures targeting the real estate market, and to a lesser extent, slower credit growth. We believe that China's banking system remains fundamentally sound. The risk of a full-blown credit bubble is minimal in the near term given that domestic leverage remains relatively low. The Banking sector's capital replenishment pipeline is more of a response to the regulator's prudent requirement on capital adequacy, and only represents short-term overhang in the market. The overall scale of new loans growth is likely to be smaller in 2010 than in 2009, but should remain at a robust level. While there are signs of overheating in the property sector in the first-tier cities, there does not seem to be a nationwide property bubble. We applaud the government's timely efforts to tighten credit and various measures aimed at cooling down the property sector, as over-reliance on expansionary policy can lead to undesired consequences such as inflation overshoot, overcapacity and a full-blown asset bubble. A prudent and timely exit strategy by the government is crucial for China to prolong its cycle and realize its secular growth potential.

The MSCI China index is now trading at around 14x P/E for 2010 against consensus forecast of 22% 2010 EPS growth, which is marginally higher than the long-term, mid-cycle level of 13x but remains attractive relative to the region. Likewise, the aggregate A-share market, trading at 20x P/E for 2010, is largely priced at mid-cycle valuations. We remain positive on the market, and will look for opportunities to add positions in domestic demand plays and buy laggards on dips. In terms of investment themes for China, we believe that domestic demand should remain as a secular growth driver for China in the foreseeable future, particularly against a backdrop of subdued external demand. Although opportunities exist in most sectors, we believe the key beneficiaries include consumption-related players, upstream resource players and banks, and our China portfolio is overweight in these sectors.

We remain neutral on the Hong Kong market. FY2009 earnings have been upgraded but FY2010 remains almost unchanged. After a 60% increase in 2009, MSCI Hong Kong has become slightly overvalued. It now trades at a 17.3x P/E for 2010, a standard deviation higher than its historical mean, while its dividend yield of 2.6% is a standard deviation below historical mean. The market continues to be at risk from asset inflation driven by high levels of liquidity in the financial system and no structural oversupply in any real estate segment. Capital values have risen driven by sharp cap rate compression, while the residential and prime retail market is seeing rental increases. Our Hong Kong portfolio is invested across four sectors – industrials, technology, financials and properties, being overweight on the latter two. For the Hong Kong market, we like brand leaders. We also like Hong Kong-listed China companies as they are exposed to the growth of China.

- **INDIA**

India		31-Dec-09		
Market performance		Last close	%3M chg	%YTD
MSCI INDIA		472.7	4.2	93.7
BSE SENSEX 30 INDEX		17,464.8	2.0	83.2
Exchange rate		Last close	%3M chg	%YTD
US\$/INR		46.5	(3.3)	(4.7)
MSCI INDIA		2009E	2010E	2011E
EPS growth (%)		10.7	28.2	19.4
P/E (x)		21.7	16.9	14.2
P/B (x)		3.8	n/a	n/a
DY (x)		0.9	n/a	n/a

Source: Bloomberg, Citi, Credit Suisse, Thomson, CEIC, MSCI

Market Review

The Indian market rallied 97.6% in Singapore dollar terms over 2009.

Investor confidence in India started the year on a weak footing, undermined by the fast deteriorating global economic outlook, dismal corporate governance developments and the lingering effects of the terrorist attacks in November 2008. From oversold levels in February, the market rallied hard from March, in line with recovering global sentiment. Boosting the market further was the positive surprise in the general elections results in May and the consequent formation of a stable government focused on growth. This was seen as a structural change that should bode well for India's economic growth for the next five years. News of a drought in July and disappointment over the measures announced in the Budget began to hurt investor sentiment. In particular, investors were unsettled by a larger-than-expected fiscal deficit and the lack of concrete measures to address it. However, as the earnings reporting season commenced, companies reported better-than-expected earnings performance for the June quarter, led by IT services, autos and cement companies which sparked a return of confidence across the market. Encouragingly, earnings growth for the September quarter continued to be strong, with margins being the key driver while revenues were down.

The Reserve Bank of India (RBI) acknowledged the pervasive effects of the global financial crisis early and acted aggressively. In an attempt to normalize liquidity in the banking system, which has seen sharp tightening primarily due to capital outflows, the RBI cut the benchmark repo rate by a significant 2.5% to 6.5%. Broad-based fiscal measures were also announced by the government, amounting to about 0.7% of GDP. The concerted efforts by the RBI and the government enabled India to escape a drastic economic slowdown.

On the macroeconomic front, India's industrial production resumed its growth trend, registering a strong 10.3% in October led by an improvement in almost all the reported industry segments. Year-to-October growth in IIP stands at healthy 7.1% while Q2FY10 GDP growth accelerated sharply by 7.9%, helped by manufacturing and a surprisingly positive growth agriculture sector.

Portfolio

The portfolio is overweight in materials, utilities and consumer discretionary stocks. Within the materials sector, we prefer steel, iron ore and fertilizer stocks, all of which should benefit from low global interest rates and economic recovery. We are positive on utilities as the power requirements of this fast developing country will create power deficits for a number of years. Within the consumer discretionary sector, we own a number of auto stocks which we believe provide excellent exposure to the rural as well as urban consumption theme.

Outlook/Strategy

Positive changes in the infrastructure space

While the infrastructure spending theme has been a permanent feature in India, recent announcements by the Indian government have again shown how seriously it is pushing infrastructure spending. Key developments include permitting infrastructure developers to gain access to secured loans from banks, rather than only unsecured loans; and easing land-acquisition related delays by ensuring that a project is opened up for bidding only after 80% of the necessary land is acquired. Both of these measures, amongst many others, indicate the government's seriousness about accelerating infrastructure build-out and should result in faster implementation – with emphasis on roads, power (generation and T&D) and in rural infrastructure.

Reforms to be a constant feature in future

As a consequence of the strong election mandate, reforms are likely to occur as an avenue to address the significant budget deficits as well as other regulatory reforms to level the playing field particularly for foreign investors. The Divestment Secretary indicated that the department is discussing minority stake sales in 60 central state-owned units. In terms of priority, state-owned listed companies with less than 10% free-float and state-owned unlisted profitable firms are likely to be the first to be subjected to this divestment mandate. Importantly, these divestments alone are expected to lower the fiscal deficit by c.1.5% of GDP by FY11, and lead to a higher free-float in the market – essential for a country that is dependent on foreign capital inflows to grow.

Consumption resilient in both rural and urban areas

For India to continue to grow at the government's target of 8 – 9% annually, it is estimated that the rural economy needs to grow by at least 5% per annum. The government is clearly aware of this as can be seen by the number of measures aimed at supporting the rural economy (e.g. The National rural employment guarantee scheme, minimum support prices for agricultural products, etc). As such, it is likely that the rural economy will stay reasonably firm. At the same time, in the urban areas, recent human resources surveys indicate that wage increases in Indian urban areas are likely to be highest in the Asia Pacific region, even surpassing China's wage growth for 2009 and 2010. Additionally, companies surveyed indicated their intention to expand their labour forces, which will serve to underpin the urban economy. As such, both the rural and urban consumers are likely to be a significant force in India's economic growth, thereby reinforcing the domestic economy as the key driver of India's economic expansion. Key beneficiaries would include the Fast Moving Consumer Goods sector, as well as those manufacturing and or distributing 2 and 4 wheelers.

- **KOREA**

Korea		31-Dec-09		
Market performance		Last close	%3M chg	%YTD
MSCI KOREA		434.3	1.1	58.4
KOSPI INDEX		1,682.8	0.6	50.6
Exchange rate		Last close	%3M chg	%YTD
US\$/KRW		1,164.0	(1.2)	(7.6)
MSCI KOREA		2009E	2010E	2011E
EPS growth (%)		54.9	33.4	11.2
P/E (x)		13.8	10.3	9.3
P/B (x)		1.5	n/a	n/a
DY (x)		1.0	n/a	n/a

Source: Bloomberg, Citi, Credit Suisse, Thomson, CEIC, MSCI

Market Review

Due to February's US\$4 billion current account surplus, the government's US\$14 billion economic stimulus measures for 2009 and some tentative positive indicators for the global economy, sentiment turned positive in March. Better-than-expected 1Q09 GDP and the improved current account balance boosted investors' risk appetite in April. As foreign investors turned net buyers of US\$4 billion worth of Korean equities, the MSCI Korea index rallied 28% in just two months.

The market's appreciation was underwritten by 2Q09 earnings reports which showed signs of recovery, improving fundamentals of the Korean economy and better-than-expected economic recovery across the region. During 3Q an additional US\$16 billion worth of foreign investment pushed MSCI Korea another 27% higher.

In October and November, share prices corrected 7% as recovery trades lost some steam on the expectation of a strengthening Korean Won. Nonetheless, strong export shipments and a rebound in construction completion suggested that economic indicators remained firm; foreign investors invested another US\$2 billion in December, pushing the MSCI Korea up 8% in the last month of the year.

During the year, foreigner investors were net buyers of US\$26 billion worth of Korean equities, resulting in 8% appreciation of KRW against USD and 58% rise in MSCI Korea. Consumer Discretionary was the best performing sector, followed by Information Technology and Materials. Consumer Discretionary stocks led the rally due to improved domestic consumer sentiment and better-than-expected results for 1Q and 2Q09. Information Technology stocks also rallied with the news of Qimonda's bankruptcy, the rebound in the prices of DRAM and NAND flash, a weaker Korean Won, the tentative signs of a recovery in demand in 1Q09, and the better-than-expected results for 2Q09. For the major exporters, larger-than-expected sales growth played a big role in lifting share prices too.

Outlook/Strategy

Korea's economic indicators still point to a firm recovery but the momentum seen previously in the upward revision of earnings is slowing. Following a strong run the equity market is delicately positioned and could see a correction due to excessive earnings expectations and overvaluation. In our opinion, the consensus expectation for 2010 EPS

growth to be 27% higher than 2007, may be too aggressive. In terms of valuation Korean equities are not attractive with the index (MSCI Korea) trading on a P/E of 10.3x and P/B of 1.5x both of which are above historical averages.

With earnings visibility as the top priority, our strategy emphasizes two key themes:

1. Banks' Profit Recovery. Banks' earnings will recover in 2010, benefiting from net interest margin improvement, credit costs coming off a high base and an improving economic backdrop. We expect net interest margins to improve given a more liquid environment supported by deposit growth outstripping loan growth and the rolling over of high cost deposits at lower rates and new lending spreads being significantly higher than that of existing loans. We also expect to see credit costs decrease significantly on the back of a substantial drop in new non-performing loans and the reduction in the overall level of non-performing loans by end 2009. In addition, the anticipated increase in interest rates in 2010 will further buffer earnings. The banks which we like include Daegu Bank, KB Financial Group and Korea Exchange Bank.

2. Non-life Insurers' Sustainable Growth. Non-life insurers will benefit from structural growth in private healthcare insurance business propelled by increasing demand from an aging population. Their earnings will also rise as the economic and interest rate outlook improves. A recovery in the economy will result in a higher persistency ratio while a rise in interest rates will be positive for interest income. Moreover, strong new premium growth will strengthen the outlook for growth in embedded value. The Non-life insurers which we like include Dongbu Insurance and Samsung Fire & Marine Insurance.

In the longer term we expect Korean equities will be positively driven by the multi-year structural themes of exposure to China's growth consumption and the increase in global market share by Korea's leading exporters. China's private consumption growth will substantially exceed its GDP growth in the next ten years as the authorities aim to rebalance the country's economic mix by boosting private consumption as a portion of the economy. Korea is well positioned to benefit from China's growth in consumption given that China is already Korea's largest export market; additionally the depreciation of Korean Won against the RMB and JPY provides a competitive edge to exporters. Moreover, improvement in technology, product quality, pricing and brand equity will ensure that the current trend of global market share gain at the expense of US/Japanese companies in handset, flat-panel television set, Dynamic Random Access Memory and automobile businesses will be a multi-year phenomenon.

- **TAIWAN**

Taiwan		31-Dec-09		
Market performance		Last close	%3M chg	%YTD
MSCI TAIWAN		164.5	7.5	74.7
TAIWAN TAIEX INDEX		8,188.1	9.0	85.4
Exchange rate		Last close	%3M chg	%YTD
US\$/TW\$		32.0	(0.5)	(2.5)
MSCI TAIWAN		2009E	2010E	2011E
EPS growth (%)		46.1	67.7	25.4
P/E (x)		28.6	17.1	13.7
P/B (x)		2.1	n/a	n/a
DY (x)		2.5	n/a	n/a

Source: Bloomberg, Citi, Credit Suisse, Thomson, CEIC, MSCI

Market Review

As a result of several government initiatives that saw among other things the extension of the total bank deposit guarantee to 2010, the lowering of the discount rate by the Central Bank of China and the Financial Supervisory Commission's new policies to help companies facing financing pressure, sentiment started improving in February. Foreign investors were drawn back to the market having taken a measure of confidence from a stream of good news such as the successful conclusion of the third cross-strait negotiations between China and Taiwan which resulted in the signing of a number of agreements, the conclusion of an alliance between Taiwan's Far Eastone Telecommunications with China Mobile whereby the latter would take a 12% stake in the former making it the largest foreign investor in the business; and news that export order growth turned positive in April. In all foreign investors committed US\$5 billion to the market and underwrote a rally in the MSCI Taiwan of 58% in just four months.

Although share prices pulled back 7% in June due to a disappointing turnout at Taipei Computex, a confluence of positive cross-strait news and an additional US\$10 billion worth of foreign institutional investors' buying sent MSCI Taiwan another 29% higher in 2H09. Among the good news was the decision of the Ministry of Economic Affairs to ease certain rules which restricted investment in Taiwanese businesses by Chinese companies. The China Banking Regulatory Commission also sought to lay the ground work for closer co-operation by suggesting that Taiwanese banks would be able to apply for branch status once the relevant regulatory authorities signed the Financial Memorandum of Understanding. Other positive news included the third Chinese procurement group's US\$4 billion orders from Taiwan and the Central Bank of China's announcement that Taiwanese banks' Hong Kong-based branches would be allowed to handle RMB deposit and exchange business by year end. In addition, export orders recorded a solid 37% year-on-year expansion in November.

During the year, foreign institutional investors bought a net US\$16 billion worth of Taiwanese equities, contributing to a 3% appreciation in the Taiwanese Dollar against the USD and a 75% rise in the MSCI Taiwan. In terms of performance at the sector level, Consumer Discretionary was the best, followed by Information Technology and Materials. Whilst Consumer Discretionary stocks were mostly China consumption plays, Information Technology stocks rose on the back of improving guidance for 1Q09 sales growth and operating profits as well as better-than-expected 2Q09 earnings results.

Outlook/Strategy

Continued strength in export demand from China, an improvement in the inventory cycle in the US and a recovery in global demand for personal computers will reinforce export recovery in Taiwan. Cross-strait negotiations for the Economic Co-operation Framework Agreement which will include an early harvest program where corporate Taiwan will enjoy preferential treatment in addressing the mainland market will form a basis for decision making during 2010.

Having done well in 2009 there are now risks developing such as peaking earnings momentum and potentially falling liquidity. However despite these risks we believe that Taiwanese equities remain attractively valued with the MSCI Taiwan's on a P/B of 2.1x which is below the historical average and a P/E of 17.1x which is close to the historical average. We see any pull-back in prices as a good buying opportunity.

With export recovery and improving domestic confidence in mind, our strategy emphasizes two key themes:

1. Global Personal Computer Shipment Recovery. Global PC shipment is forecast to grow 12% per annum in the next two years. Emerging markets will be a key growth driver for 2010 as PC shipments to the emerging markets is forecast to grow 20% on falling system prices, improving consumer confidence and upgrade demand. Furthermore, recent recovery in US corporate profit is a good leading indicator that corporate information technology spending and PC replacement will follow in 2011. Hence, notebook PC related names – including Cyberlink, Delta Electronics and Shin Zu Shing - remain in a sweet spot benefiting from emerging market demand, a new product cycle (e.g. slim/power-saving notebook) and the corporate replacement cycle following a period of underspend.

2. Capital Repatriation and Asset Reflation. Taiwan has been experiencing capital inflows by the private sector with US\$41 billion in accumulated capital (12% of GDP) since 3Q08. The continuing trend of capital repatriation and the Financial MOU which allows for ease of capital flows between China and Taiwan will help facilitate cross-strait investment and benefit the Taiwanese property sector. The appetite for Taiwanese property is likely to expand for both the residential and commercial sectors as assets are revalued in line with an increase in economic confidence. In addition, Chinese state-owned entities or private corporations will set up their Taiwan offices. Due to a lack of investment in the past, property prices should rise on the back of increasing demand. In this environment, property and land owners like Cathay Financial Holdings, Taiwan Fertilizer and well capitalized banks like Chinatrust Financial Holdings will be the key beneficiaries.

From a longer-term perspective, Taiwan is moving in the right direction. The signing of the Financial MOU is a positive step for cross-strait relations as it shows both sides' ability to set aside political differences and focus on economic issues. Positive developments on closer economic ties with the mainland will help support Taiwan's growth and competitiveness, positioning Taiwan to better capitalize on the recovery in China's growth. These will lead to structural changes in Taiwan's economy; help boost confidence and capital repatriation, thereby bringing about a re-rating of Taiwanese equities.

- **SINGAPORE**

Singapore		31-Dec-09		
Market performance		Last close	%3M chg	%YTD
MSCI SINGAPORE		3,932.8	9.4	69.5
STRAITS TIMES INDEX		2,897.6	8.4	62.7
Exchange rate		Last close	%3M chg	%YTD
US\$/S\$		1.4	(0.3)	(1.8)
MSCI SINGAPORE		2009E	2010E	2011E
EPS growth (%)		(14.3)	17.7	10.2
P/E (x)		18.2	15.4	14.0
P/B (x)		1.9	n/a	n/a
DY (x)		2.9	n/a	n/a

Source: Bloomberg, Citi, Credit Suisse, Thomson, CEIC, MSCI

Market Review

2009 has gone down in history as an extraordinary year. Driven by the global financial crisis which started in late 2008, the STI plunged to 1,456.95 on 9 March 2009 – a six-year trough – amid market fears of a global depression. By December, however, the index had climbed to close at 2,897.62, on the back of a recovery triggered by a series of global quantitative easing measures to inject liquidity to revive the financial markets.

The collapse in global trade in the wake of the global financial meltdown has led to Singapore's open economy reaching a bottom in 1Q09, with a year-on-year contraction of -10.1% vs -4.2% in 4Q08. In light of the dismal growth numbers, the Monetary Authority of Singapore (MAS) eased monetary policy by re-centering the exchange rate's intervention band. In addition, the Singapore government unveiled a S\$20.5 billion fiscal stimulus package aimed at helping businesses and individuals through the recession.

With the growing signs of an economic recovery lifted by the coordinated stimulus measures around the world, Singapore's GDP rose 21.6% quarter-on-quarter (-3.2% year-on-year) in 2Q09 on the back of a sharp rebound in the biomedical industry and improving export activities. The economic growth momentum continued through the 3Q with a 14.9% quarter-on-quarter (+0.9% year-on-year) expansion. The 4Q flash estimates highlighted a contraction of 6.8% quarter-on-quarter, but an expansion of 3.5% year-on-year, indicating that while the momentum outside the biomedical sector has slowed relative to the exceptional growth in Q2 and Q3, the economic recovery trend remains intact.

While the economic and stock market recovery gained traction, the real estate sector saw a sharp increase in prices driven by increased buyer confidence and an exceptionally low interest rate environment. This led to the introduction of new cooling measures by the government, such as increasing the supply of land available and the removal of the interest absorption scheme and interest-only loans.

Outlook/Strategy

During the year, the STI and the MSCI Singapore rose 63% and 70%, respectively. In contrast to 2008, cyclical stocks including commodities, offshore and marine, and property were out-performers in 2009, while defensive high-yield sectors such as telecommunications and land transportation underperformed. In terms of capitalization it was large cap stocks leading the recovery, with small and mid cap stocks lagging. In

particular, the S-shares suffered a massive blow to their reputation as certain Chinese listings ran into corporate governance, accounting scandals and going concern issues.

Heading into 2010, equities appear to be in a sweet spot, with low interest rates and a weak USD fuelling liquidity, the economic recovery on track and corporate earnings rebounding to pre-crisis levels. After the strong rally in the last nine months, the equities market should offer a more normalized return scenario going forward, as corporate earnings expectations appear to be largely priced into stocks. In Singapore, the government has projected 2010 GDP growth at 3.0-5.0%, and maintained their 2009 forecast at -2.5 to -2.0%. CPI inflation forecast for 2010 has been revised upwards to 2.5-3.5% from 1.0-2.0%.

In the near to medium term, we believe the low interest rate environment should continue to be supportive of asset markets. However, the government is also concerned by the rapidly rising property market and hence announced measures to cool the market.

Earnings upgrades should continue, albeit at a slower pace. We would look for a more positive top-line and improving margins over the next year, supported by operational efficiencies and a benign interest rate environment.

Longer term, we expect a higher population base and the two integrated resorts to drive tourism, generate more domestic consumption and create a more vibrant services sector. We expect job creation and investment spending to continue, driven by the government's expenditure and foreign direct investments. Domestic services like financials (banks & real estate), telecoms, healthcare, consumer and land transport sectors will benefit from the ongoing economic recovery.

The market is trading at P/E of 18x (FY09) and 15x (FY10), which is around the historical mean. We see valuations fair at current levels although believe that domestic catalysts and strong liquidity will lift markets higher throughout 2010.

In view of improving economic fundamentals, we would be positioned in banks for a 2010 recovery as interest rates are expected to trend up and loan growth to stabilize. In our view, banks are also attractive on valuations versus the market. For a major re-rating to take place, ROE needs to expand from current levels.

The REIT sector remains undervalued and offers an attractive risk-reward proposition over the next 3-6 months. Domestic segments like hotels and business travel-related services could benefit from a stronger Singapore brand as a business and holiday destination. The telecoms and healthcare sectors remain stable on earnings consistency. The poor earnings outlook in the transportation and office sectors could drag down market earnings for 2009 as well as 2010. But we see these sectors as potentially profitable investments from a global trade recovery perspective, given the low consensus earnings expectations.

- **ASEAN - Malaysia/Indonesia/Philippines/Thailand/Vietnam ex Singapore**

ASEAN ex Singapore		31-Dec-09		
Maket performance				
	Last close	%3M chg	%YTD	
MSCI MALAYSIA	250.0	5.5	50.5	
FTSE Bursa Malaysia KLCI	1,272.8	5.9	46.7	
MSCI INDONESIA	1,012.8	2.2	95.0	
JAKARTA COMPOSITE INDEX	2,534.4	2.7	89.0	
MSCI PHILIPPINES	200.2	7.0	61.0	
PSEi - PHILIPPINE SE IDX	3,052.7	9.0	63.0	
MSCI THAILAND	396.4	0.8	69.3	
STOCK EXCH OF THAI INDEX	734.5	2.4	64.4	
HO CHI MINH STOCK INDEX	494.8	(14.8)	60.3	
Exchange rate				
	Last close	%3M chg	%YTD	
US\$/IDR	9,403.8	(2.7)	(15.4)	
US\$/MYR	3.4	(1.0)	(1.2)	
US\$/PHP	46.2	(2.5)	(2.9)	
US\$/THB	33.4	(0.2)	(3.9)	
US\$/VND	18,479.0	3.6	5.7	
MSCI MALAYSIA				
	2009E	2010E	2011E	
EPS growth (%)	(19.5)	21.9	14.0	
P/E (x)	18.8	15.4	13.5	
P/B (x)	2.1	n/a	n/a	
DY (x)	2.4	n/a	n/a	
MSCI INDONESIA				
	2009E	2010E	2011E	
EPS growth (%)	8.2	13.0	18.2	
P/E (x)	15.6	13.8	11.7	
P/B (x)	3.9	n/a	n/a	
DY (x)	1.7	n/a	n/a	
MSCI PHILIPPINES				
	2009E	2010E	2011E	
EPS growth (%)	19.2	14.9	13.7	
P/E (x)	16.8	14.6	12.9	
P/B (x)	2.5	n/a	n/a	
DY (x)	2.2	n/a	n/a	
MSCI THAILAND				
	2009E	2010E	2011E	
EPS growth (%)	20.8	13.8	17.8	
P/E (x)	12.9	11.3	9.6	
P/B (x)	1.9	n/a	n/a	
DY (x)	2.9	n/a	n/a	
HO CHI MINH STOCK INDEX				
	2009E	2010E	2011E	
EPS growth (%)	n/a	10.6	n/a	
P/E (x)	13.9	12.6	n/a	
P/B (x)	1.9	n/a	n/a	
DY (x)	1.4	n/a	n/a	

Source: Bloomberg, Citi, Credit Suisse, Thomson, CEIC, MSCI

Market Review

Regional markets surged after touching lows in March. The ferocity of the regional markets' rallies initially took investors by surprise, as the economic outlook was still fragile. Nevertheless, improving economic data led by rebounds in industrial production and exports reinforced prospects of economic recovery. By end of 2009, Indonesia was the best performing market, followed by Thailand, Philippines, Vietnam and Malaysia. Amongst the regional currencies, the Indonesian Rupiah appreciated 15.4% against the

US Dollar while the Thai Baht and Philippine Peso appreciated by 3.9% and 2.9% respectively. The Vietnamese Dong depreciated by 5.7%.

The majority of the regional markets benefited from prospects of economic recovery; Indonesia's stellar stock market performance was helped by the successful re-election of President Susilo Bambang Yudhoyono, as well as its resilient domestic economy which grew by 4.3% in 2009 when many economies were suffering from recession. Sectoral performances across the region were divergent with cyclical sectors such as Consumer Discretionary, Financial, Energy and Material sectors outperforming while the Telecommunication Services and Utility sectors underperformed.

Outlook/Strategy

Following the dramatic turnaround in stock market performances in 2009, the outlook for 2010 is for a return to trend growth. All regional economies are expected to post positive GDP growth in 2010 although the extent of recovery would vary across the region. Regional stock markets are likely to continue rising in 2010, buoyed by flush liquidity, further signs of economic recovery and corporate earnings growth.

Interest rates are likely to remain low in most regional markets as inflation, although muted is expected to rise. Nevertheless, countries which are more vulnerable to sharp rises in inflation such as Vietnam and Indonesia, could see policy moves to rein in inflationary pressures.

Political risks are likely to rise in Thailand in 2010. Key political events include the Supreme Court's decision on the seizure of Thaksin's assets worth Baht 76 billion (US\$2.3 billion), a no-confidence motion against the Prime Minister in 1Q 2010, as well as the state of King Bhumibol's health. The Philippines will be holding a Presidential election in May 2010, which together with buoyant OFW remittances, are combining to underwrite a positive outlook for domestic consumption and infrastructure stocks. In Indonesia the key issues for 2010 are economic reform as well as the implementation of key infrastructure projects. In Malaysia the economy is expected to improve, helped by domestic demand and government infrastructure projects. Vietnam represents something of a contrast as the economy remains fragile with concerns over deteriorating fiscal and trade deficits.

Within our regional portfolios, we are underweight the Malaysian, Indonesian and Vietnamese stock markets. Both Malaysian and Indonesian markets are underweight on valuation concerns while risks of macro instability in Vietnam weigh on our view of the market.

We have adopted a strategy of investing in core companies with strong balance sheets and cash flows while maintaining exposure to cyclicals which should benefit from a recovering global economy. We are positive on financials given the low interest rate environment and resilient domestic economies in Asean. Key themes for banks across the region include moderate loan growth, rising net interest margins, and falling credit costs. The real estate sectors in most regional countries have seen a recovery as pent-up demand saw encouraging developer sales. We are neutral on the transportation sector where we feel that the worst is behind us. Amongst the energy sector, we prefer the upstream E&P companies which closely track crude oil prices as well as coal companies which will likely see demand surprises from China and India.

FIXED INCOME

US/EUROPE/ASIA/SINGAPORE

Market Review

In 2009, global interest rates stayed at historically low levels as central banks kept monetary policies loose to allow the economic recovery time to gain traction. In developed markets of the US, Europe and Japan, government bond yields in shorter-dated maturities were close to zero. This led to a rotation into risky assets including credit papers as investors sought to pick up yield. Against this backdrop, interest rate markets posted flat returns (+0.66% JPMorgan Government Bond Index Global) whilst credit markets turned in a remarkable performance of +28.3% in USD terms (based on JP Morgan Asia Credit Index) for the year.

In 2H09, improving economic data suggesting a recovery in momentum triggered a gradual rise in interest rates in most markets. Yield curves showed a general steepening bias, with short-dated maturities anchored by low policy rates and longer-dated maturities moving higher in tandem with the stabilizing economy and less headwinds in the financial markets. Within the developed markets for government bonds, US treasuries underperformed selling off -3.77% in 2009 when interest rates moved higher across the yield curve. Australian government bonds sold off -2.61% on the back of consecutive hikes in the cash rate to 3.75% to bring the policy rate to more neutral levels and moderate the pick up in the housing sector. Returns in most other interest rate markets were fairly flat: Germany +1.84%, Singapore +0.33%. In Asia, interest rate markets had a more mixed performance. Using the HSBC Asian Local Index as a proxy, the out-performers were Indonesia (+22.4%) and Philippines (+8.2%) while the under-performer was India (-4.9%). The performance of the remaining Asian country indices ranged from -2.9% to +2.1% (in local currency terms).

Credit spreads in Asia tightened from historical extremes in October 2008 and ended 2009 tighter than pre-Lehman levels. Asian credit papers performed well due to the high yield sector which posted a return of +43.2%, almost double the high grade papers which registered a return of +22.1%. On the supply front, 2009 issuance recovered remarkably, pushing the total primary issuance to US\$50 billion, almost 3x that of 2008. High grade issuers dominated the primary market and made up about three quarters of new issues. The bulk of the 2009 new issuance came from Korean issuers (39%) followed by Hong Kong (16%) and Singapore (7%).

Overweight positioning in credit markets was the key contributor to bond portfolios in 2009. In particular the issuers in Korea, Singapore and Malaysia, saw credit spread tightening giving returns in excess of 15%. The bond portfolios also benefited from small exposures in selective names in the Asian high yield sector. We also maintained a slight underweight duration position through most of the year, with neutral impact on returns.

Outlook/Strategy

Against a backdrop of gradual recovery and accommodative monetary policy in 1Q2010, we expect government bond yields to trade within a range, each range to move higher, in measured steps, until there is further evidence of the economic recovery becoming more sustainable. We expect yield curves generally to flatten as short rates normalize from historically low levels and subsequently to bear steepen on supply pressure and economic recovery. The recommended positioning for bond portfolios in 2010 is to stay underweight duration against benchmarks.

In the developed markets, the large output gaps leave plenty of room for a rebound in economic activity without significantly stoking inflationary pressures. This paints the scenario for a gradual, rather than sharp, normalization of interest rates from current low levels. We are, however, less sanguine on inflationary pressures for Asian markets, and expect bond yields in Asia to move higher in tandem with US interest rates, but note that the rise could potentially be more

pronounced given Asia's higher sensitivity to food and commodity inflation. We expect Asian policymakers to remain vigilant on inflationary pressures but will seek to balance any upward move in rates with an eye to the consequences for both exports and currency. We think that where necessary, Asian policymakers are likely to choose targeted administrative measures over interest rate tools to deal with any unwelcome asset price inflation. For Asian interest rate markets, we maintain a neutral duration stance near term and look to move to underweight if inflationary pressures and economic growth were much stronger than expected. Closer to home, for Singapore interest rates, we expect yields to creep up gradually until the next shift in policy in April 2010. If the recovery looks sustainable, the bias is for MAS to shift to tightening stance at that time.

In the credit markets, we remain constructive on Asian USD credits on supportive fundamentals, valuation and technical factors. After a remarkable year, we think there is still some room for credit spreads to grind in as fundamentals, valuation and technicals are still supportive for Asian USD-denominated bonds. Nonetheless, the degree of spread tightening in 2010 is more limited than in 2009. There are a number of factors working in favor of Asian credits, which include the improving economic and credit fundamental outlook, healthy fund flows and steady market technicals. We think credit spreads are currently still pricing in excessive default risks and a higher premium to US credits compared to historical levels. We expect credit spreads to tighten further in 2010 though the potential upside will be more limited compared to that of 2009, given the significant tightening achieved last year. We see value in Asian Quasi-sovereigns, High Grade and Bank debts. Within the high yield space, we prefer the high-quality issuers which have stronger fundamentals and better corporate governance. We will look out for opportunities in the primary market which can provide further diversification.

The combination of economic recovery and cessation of buyback programs by the US Federal Reserve/US Treasury and Bank of England and the draining of liquidity by the European Central Bank will be a catalyst for interest rate markets to normalize and move higher in 2010. Real interest rates have to increase to attract capital and encourage domestic savings. How much higher interest rates will move will be determined by how key macro developments intersect, specifically: (1) the forces of the business cycle and output gap, which tend to drive the economy at the outset of the recovery; (2) the severity of financial headwinds, including consumer indebtedness, commercial real estate problems, and most importantly the prospect of a state and local government sector fiscal crisis; (3) the timing and appropriateness of the central banks' exit strategies; and (4) the rising private-sector savings rate which would create demand for government bonds. Against this backdrop, we recommend to stay underweight duration for bond portfolios and a continued focus on investment grade Asian USD credit papers in 2010.

Market Valuations

Valuation as of date 31 Dec 2009	EPS Growth (%)			3-mth chg. In EPS est. (%)		P/E (x)			P/B (x)	DY (%)
	2009E	2010E	2011E	2009E	2010E	2009E	2010E	2011E	current	current
Asia/Pacific										
Japan	(116.1)	nm	86.9	n/a	6.9	(68.0)	33.2	17.8	1.2	1.7
Topix Index		85.0	46.6			38.4	20.8	14.2	1.1	1.7
Nikkei 225		86.6	43.0			44.0	23.6	16.5	1.4	1.5
Australia	(19.9)	0.6	20.8	n/a	2.1	17.2	17.1	14.1	2.1	3.7
S&P/ASX 200 Index		21.1	15.7			17.4	14.3	12.4	0.5	3.8
China	14.8	22.1	16.2	1.5	3.0	17.1	14.0	12.0	2.7	1.9
Shanghai SE Composite Index		26.9	20.5			24.1	19.0	15.8	3.4	1.4
Shenzhen SE Composite Index		41.4	25.0			34.5	24.4	19.5	4.5	0.6
Hong Kong	(6.7)	15.9	15.0	1.2	2.0	20.0	17.3	15.0	1.6	2.6
Hang Seng Index		19.7	18.7			17.1	14.3	12.1	2.1	2.9
India	10.7	28.2	19.4	(1.7)	1.2	21.7	16.9	14.2	3.8	0.9
BSE Sensex 30 Index		28.8	20.1			21.1	16.4	13.6	3.5	1.1
Indonesia	8.2	13.0	18.2	3.2	4.1	15.6	13.8	11.7	3.9	1.7
Jakarta Composite Index		17.9	19.7			16.0	13.6	11.3	2.7	2.1
Korea	54.9	33.4	11.2	4.2	4.3	13.8	10.3	9.3	1.5	1.0
KOSPI Index		29.5	13.0			14.1	10.9	9.7	1.3	1.3
Malaysia	(19.5)	21.9	14.0	1.6	3.3	18.8	15.4	13.5	2.1	2.4
FTSE Bursa Malaysia KLCI		12.6	14.5			16.8	14.9	13.0	2.2	3.3
Philippines	19.2	14.9	13.7	1.6	0.9	16.8	14.6	12.9	2.5	2.2
PSEi - Philippine SE Idx		12.0	12.1			14.3	12.8	11.4	2.1	3.3
Singapore	(14.3)	17.7	10.2	6.7	6.4	18.2	15.4	14.0	1.9	2.9
Straits Times Index		16.0	10.3			17.4	15.0	13.6	1.8	2.9
Taiwan	46.1	67.7	25.4	17.3	13.3	28.6	17.1	13.7	2.1	2.5
Taiwan Taiex Index		44.7	12.8			24.8	17.2	15.2	2.2	2.5
Thailand	20.8	13.8	17.8	2.8	0.7	12.9	11.3	9.6	1.9	2.9
Stock exchange of Thai Index		13.6	14.3			12.6	11.1	9.7	1.6	3.6
Vietnam		10.6	-	n/a	n/a	13.9	12.6	-	1.9	1.4
Asia Pacific	75.7	40.3	20.7	4.6	3.0	22.2	15.9	13.1	1.6	2.1
Asia ex Japan	17.2	28.6	15.9	3.8	4.5	18.2	14.1	12.2	2.1	1.9
Asia Pac ex Japan	3.5	22.5	17.7	3.5	3.8	18.3	14.9	12.7	2.1	2.4
Europe	(21.1)	26.7	21.5	2.9	2.1	15.8	12.5	10.3	1.7	3.2
DJ Stoxx 600 € Pr		25.3	20.5			16.0	12.7	10.6	1.7	3.3
S&P Europe 350 Index		25.9	19.7			15.7	12.5	10.4	1.7	3.4
United States	1.2	26.3	20.7	0.6	2.5	18.3	14.5	12.0	2.2	1.9
S&P 500		27.3	20.5			18.1	14.2	11.8	2.2	2.0
Dow Jones Industrial Average		22.4	16.2			16.2	13.2	11.4	2.8	2.6
NASDAQ Composite Index		42.0	22.4			26.1	18.4	15.0	2.8	0.8

Source: Credit Suisse, Bloomberg, MSCI, Thomson

APPENDIX 2

31-Dec-09

Economic data	Real GDP % YoY			CPI % YoY			Current Official policy rate (%)	Government bond yield (%)				Exchange rates			Unemployment (% of labor force)	Current account balance (% GDP)	Fiscal balance (% GDP)	Business confidence		Consumer confidence				
	2008	2009E	2010E	2008	2009E	2010E		2 yr	5 yr	10 yr	10-2yr	Spot	% 3M chg	%12M chg				2009E	2009E	2009E	latest	% 3M chg	latest	% 3M chg
Asia/Pacific																								
Japan	n/a	-5.3	1.5	n/a	-1.3	-1.5	0.100	0.2	0.5	1.3	1.1	US\$/¥	93.0	3.7	2.6	5.2	2.7	-9.3	-32.0	6.0	39.9	-0.5		
Australia	n/a	1.1	3.3	n/a	1.9	2.3	3.750	4.4	5.2	5.6	1.2	A\$/US\$	0.9	1.7	27.8	5.7	-4.2	-2.3	n/a	n/a	n/a	n/a		
China	9.0	8.7	9.8	1.2	1.6	3.7	5.310	1.6	2.9	3.5	1.9	US\$/CNY	6.8	0.0	0.0	4.3	6.6	-3.0	124.4	8.5	88.5	1.0		
Hong Kong**	2.4	-3.2	4.0	2.1	0.9	1.4	0.500	0.6	1.9	2.6	2.0	US\$/HK\$	7.8	0.1	0.1	5.4	8.5	-1.5	n/a	n/a	n/a	n/a		
India*	6.7	6.2	7.8	0.3	6.0	5.0	4.750	5.6	7.3	7.6	2.0	US\$/INR	46.5	-3.3	-4.7	n/a	-0.8	-7.0	143.7	25.1	n/a	n/a		
Indonesia	6.1	4.3	5.5	11.1	3.7	6.7	6.500	7.8	9.0	10.0	2.2	US\$/IDR	9,403.8	-2.7	-15.4	9.0	1.7	-2.0	20.6	-7.3	111.0	-3.3		
Korea	2.2	-0.1	4.7	4.1	2.5	3.5	2.000	4.4	4.9	5.4	1.0	US\$/KRW	1,164.0	-1.2	-7.6	3.4	4.8	-2.5	112.1	1.1	113.0	-1.0		
Malaysia	4.6	-2.0	5.2	4.4	1.3	2.3	2.000	2.6	3.7	4.2	1.6	US\$/MYR	3.4	-1.0	-1.2	3.9	14.9	-7.4	113.7	8.4	105.4	-0.4		
Philippines	3.8	1.4	3.7	8.0	3.1	4.0	4.000	4.8	6.4	8.1	3.3	US\$/PHP	46.2	-2.5	-2.9	7.7	5.5	-4.5	n/a	n/a	n/a	n/a		
Singapore**	1.1	-1.3	6.5	4.3	0.8	2.4	0.375	0.6	1.4	2.5	1.9	US\$/S\$	1.4	-0.3	-1.8	3.4	12.0	-4.0	24.0	28.0	n/a	n/a		
Taiwan	0.1	-3.5	4.3	1.2	1.0	0.8	1.250	0.4	0.8	1.4	1.0	US\$/TW\$	32.0	-0.5	-2.5	5.9	11.9	-3.9	n/a	n/a	65.4	8.9		
Thailand	2.5	-3.3	4.2	0.4	2.6	3.0	1.250	2.0	3.3	4.0	2.0	US\$/THB	33.4	-0.2	-3.9	1.8	8.0	-4.9	49.0	2.9	68.0	2.6		
Vietnam**	6.1	4.7	6.0	19.9	5.8	9.8	8.000	11.5	11.7	11.5	0.0	US\$/VND	18,479.0	3.6	5.7	5.3	-8.6	-8.2	n/a	n/a	n/a	n/a		
Europe																								
Euro Area	n/a	-3.8	1.5	n/a	0.3	1.2	1.000	1.3	2.4	3.4	2.1	€/US\$	1.4	-2.2	2.5	9.4	-0.2	-6.6	-1.6	0.6	-17.3	4.7		
UK	n/a	-4.7	1.5	n/a	2.1	3.5	0.500	1.3	2.8	4.0	2.7	£/US\$	1.6	1.2	10.8	8.3	-2.7	-12.3	n/a	n/a	n/a	n/a		
Switzerland	n/a	-1.4	1.1	n/a	-0.5	-0.1	0.250	0.3	1.0	1.9	1.6	CHF/US\$	1.0	-0.1	-3.1	3.7	8.0	-0.7	n/a	n/a	n/a	n/a		
Sweden	n/a	-4.5	2.5	n/a	-0.4	0.9	0.250	1.7	2.4	3.3	1.6	US\$/SEK	7.2	2.9	-8.6	8.6	6.8	-2.1	n/a	n/a	n/a	n/a		
Norway	n/a	-1.1	2.8	n/a	2.3	1.9	1.750	2.3	3.2	4.1	1.8	US\$/NOK	5.8	0.4	-16.7	3.3	15.6	7.4	n/a	n/a	n/a	n/a		
United States	n/a	-2.6	2.7	n/a	-0.3	2.0	0.130	1.1	2.7	3.8	2.7	-	-	-	-	9.3	-3.1	-10.0	53.6	0.7	52.9	-0.5		

* India: Wholesale price index (WPI) is used to measure inflation
 ** Hong Kong: Hong Kong base rate (HKBASE Index) is used as official policy rate
 Singapore: 3-month SIBOR is used as official policy rate
 Vietnam: Base lending rate is used as official policy rate
 *** Government bond yields are as of 31 Dec 2009
 Source: Bloomberg, CEIC, CIRA Estimates

31-Dec-09	Spot	% chg 3M	% chg 12M
VIX	21.7	-15.3	-45.8
Gold (US\$/ounce)	1,097.0	8.9	24.4
WTI Crude oil (US\$/barrel)	79.4	10.7	31.7

Source: Bloomberg

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