大華資產管理
UOB ASSET MANAGEMENT
United Behind You

Quarterly Strategy
1Q 2008

Content

1. SUMMARY 3

2. GLOBAL EQUITY STRATEGY
- Investment Outlook & Key Issues
- Market Returns
- US
- Europe
- Japan
- Asia Ex-Japan
- Singapore

4

3. GLOBAL FIXED INCOME STRATEGY

MARKET RETURNS
- Global Bonds
- Asia Bonds
- Singapore Bond

22

4. CURRENCIES 26

Introduction

The risks of a US recession have become uncomfortably high as the labour market has weakened to a worrying degree.

The Fed is likely to continue cutting interest rates to protect growth.

Volatility is however likely to remain high.

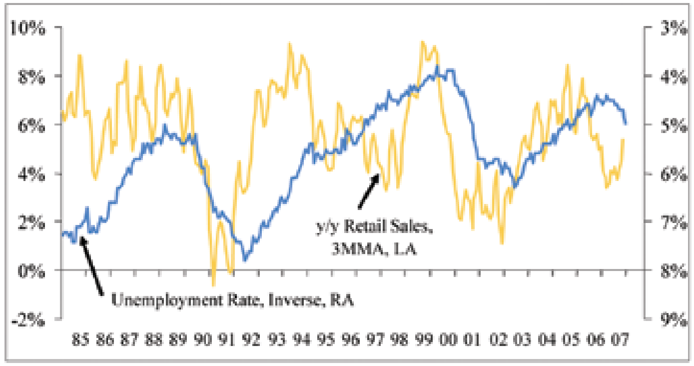
We move to an underweight position in equities and are neutral on bonds. Within equities we are still underweight in the US and now also Europe. We are neutral on Japan and stay overweight in Asia ex-Japan. We also like soft commodities and gold.

The risks of a US recession have become uncomfortably high. The persistent pressures in the interbank markets have meant that credit conditions have been deteriorating since August 2007 and the root of the problem, the US housing market, is also expected to worsen in 2008. The labour market has also weakened to a worrying degree.

The Fed is likely to continue cutting interest rates to protect growth. Mr. Bernanke's latest speech was dovish and although central banks continue to warn of inflation risk, more interest rate cuts are likely in the coming months.

Volatility is however likely to remain high in the near term. Equities are likely to stay under pressure until there is a sense that a recession will be averted in the US or if one does occur, that it will be brief and shallow. What is also needed for risk appetite to recover is more clarity on the full extent of subprime losses

We are underweight in equities and neutral on bonds. Within equities we are still underweight in the US and now also Europe. We are neutral on Japan and stay overweight in Asia ex-Japan. Within bonds, we are at neutral duration in G7 government bonds and increase our exposure to investment grade names. We also like soft commodities and gold.



US Unemployment Rate and US Retail Sales

Source: Morgan Stanley

01 investment outlook & key issues

INVESTMENT OUTLOOK

Volatility in financial markets remains high as we begin the new year. The recovery staged by equity markets in September and October crumbled in the final months of 2007 following another wave of subprime downgrades by the ratings agencies. The interbank market, which had hitherto been stabilizing, came under intense pressure again and the global central banks were forced to launch a major coordinated plan to inject more liquidity into the system. The main concern of financial markets as we move into 2008 is whether the US economy will enter a recession and how this will affect the global economy and financial markets. We highlight the key issues below:

KEY ISSUES

1. Will the US fall into a recession?

The risks of a US recession have become uncomfortably high. The persistent pressures in the interbank markets, the drying up of the commercial paper market and the widening of credit spreads have all meant that credit conditions have been deteriorating since August 2007. The immediate cause of the pressures in the interbank and credit market was the fresh downgrades by the ratings agencies on the US subprime mortgages. The downgrades have meant that funding for these securities has effectively disappeared and banks have had to take on even more of these assets onto their balance sheets, resulting in a hoarding of cash. Concerns about counterparty risk have also contributed to a wider reluctance to lend as the full extent and the location of the subprime losses remain unclear.

The interbank market improved following the coordinated injection of liquidity by the global central banks in mid-December but the market remains dislocated. The key funding rate, 3-month USD Libor was still elevated in the first weeks of January, at more than 60bps above 3-month US Treasuries Under normal circumstances, the spread is around 10bps.

Spreads in Interbank and Commercial Paper Markets

Source: UBS

Apart from interest rates being higher, borrowers are also facing tighter lending standards. As the Fed's latest Senior Loan Officer Survey indicated, the problems in the US housing market have spilled beyond the mortgage market and affected commercial, credit card and auto lending. Household consumption makes up about 70%[1] of the US economy and borrowing is an especially important driver of consumer spending in the US.

US Fed Senior Loan Officer Survey

Source: Haver, UBS

The root of all the problems, the US housing market, is expected to continue to worsen in 2008. Delinquency rates on all 1-4 unit US residential mortgages jumped to a 19-year high of 5.59% in the third quarter of 2007 and the foreclosure rate rose to a record 1.69%[2]. Many subprime mortgages taken out at the peak of the housing boom in 2005/2006 had very low 'teaser' interest rates. These rates are now being adjusted to higher levels and homeowners have not been able to meet the increased payments.

And more resets are due in 2008[3]. Roughly 1 of out 10 borrowers with an adjustable rate subprime mortgage is scheduled to have the first reset to a substantially higher rate in 2008. In the past, borrowers experiencing resets were able to avoid payment increases by refinancing their mortgages but falling home prices has taken away this option. The new plan by the US Treasury, Hope Now, to freeze resets will affect only an estimated 7% to 12% of adjustable rate mortgages as only those homeowners who are creditworthy but are unable to obtain financing will qualify for the scheme.

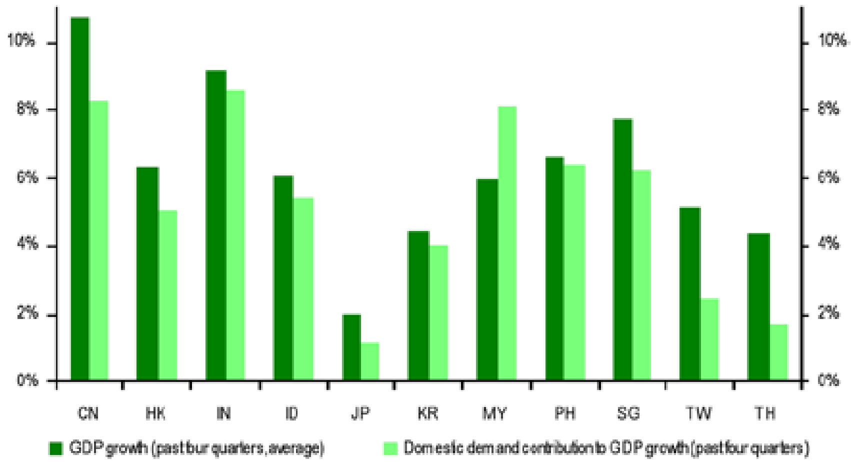
The labour market has also weakened to a worrying degree. The latest unemployment rate in US has jumped from 4.7% to 5%. Abrupt changes in the unemployment rate have in the past, signaled the onset of a recession. December non-farm payrolls was also a very weak 18,000. The labour market is probably the most important determinant of consumer spending. Consumer spending held up in October and November but expectations are it to be weaker. On the business front, the latest ISM manufacturing dropped sharply below the boom/bust line of 50 although the non-manufacturing ISM, which captures conditions in the bigger service sector, was 53.9.

[1] Source: US Bureau of Economic Analysis
[2] Source: US Economics, 10 December 2007 Morgan Stanley
[3] Source: US Federal Reserve Governor Randall Kroszner, Testimony to the Committee on Financial Services, U.S. House of Representatives 6 December 2007

2. Is the rest of the global economy also slowing down?

Although there was a measure of successful decoupling of the global economy from the US in 2007, leading indicators are pointing to both a **slowing Europe and Japan in 2008.** While both these regions are not as dependent as the US on credit for their growth, the adverse events in the financial markets have taken their toll on business and consumer confidence. Their important export sectors are also facing headwinds because their currencies have appreciated. In the second half of 2007, the euro strengthened by about 10%[4] against the US dollar,as the US Fed has been cutting interest rates while the ECB still sounded hawkish. The Japanese yen has also strengthened as carry trades do not flourish when financial conditions are volatile.

Among emerging economies, the most important one, China, is set on a tightening course as inflation remains high. China's growth is still however expected to be around 10% in 2008. In the other **emerging economies, the export sectors are weakening but domestic demand appears resilient,** particularly in the form of infrastructure spending. Most of the countries furthermore have healthy trade balances and as a result, their currencies are not under pressure. The risk of higher interest rates comes from inflation, as oil and food prices remain high.



Asia – Domestic Demand & GDP

Source: Haver, UBS

[4] Source: Bloomberg

3. Are central banks behind the curve?

Against this background of a weakening global economy, the **risk of policy error has risen.** Although the dovish speech by Mr. Bernanke on 10 January 2008 indicated clearly that the Fed was fully aware of the risks to growth, the concern of the markets is that any forthcoming interest rate cuts could be too late to stop the US economy from falling into a recession. Furthermore, it is only the Fed, the Bank of England and the Bank of Canada which have eased monetary policy. The ECB has maintained its hawkish position while the Bank of Japan realistically has no room to ease as policy interest rates are still at an abnormally low level.

Central banks are apprehensive about inflation. Although globally core inflation enery prices – remains benign which excludes volatile food and energy prices remains benign, central banks are still worried that the high food and energy prices will feed into the overall price level. This is particularly the case for the ECB which, in its policy making, gives more weight to headline rather than core inflation. Headline inflation in Europe has risen above 3%, well above the ECB's target of 2%. So far however, there appears to be no significant pass-through of higher food and energy prices into wage costs in the G7 countries.

G7 Unit Wage Cost

Source: UBS

ASSESSMENT

We recently wrote, in our Asset Allocation Report, that although growth in the US was expected to slow sharply given the tightening credit conditions and the damage wrought to business and consumer confidence, we felt that a full-blown recession would be unlikely as long as the labour market held up. Since then, the data has shown a sharp jump in the unemployment rate from 4.7% to 5%. This has further increased the risk of a recession although we continue to believe that one will be avoided.

We expect the Fed, to continue to ease interest rates to protect growth. In the words of Mr. Bernanke, "We stand ready to take substantive additional action as needed to support growth and to provide adequate insurance against downside risks." We believe inflation fears are misplaced. Although headline inflation is high, core inflation and long term inflation expectations remain benign. A weakening labour market will also reduce wage pressures, the key driver of core inflation in developed economies.

However we expect volatility to stay high until there is a sense that a recession will be averted in the US or if one does occur, it will be brief and shallow. But monetary policy works with a lag and US economic data could get worse before it gets better. What is also missing for risk appetite is more clarity on the full extent of the subprime losses. About US$100bn has been written off so far but estimates of the losses range from US$150-$500bn.

ASSET ALLOCATION

We move to an **underweight position in equities.** Since 2003, equities have been driven by earnings growth and the risk of earnings downgrades is high in an environment of slowing global growth. Although multiples can typically expand when earnings slow and interest rates are being cut, the current low level of risk appetite makes this unlikely in the near term. Equity valuations are however not demanding with trailing global PE at 16x, against an average of 21.6x over the last 20 years, or 20x if the TMT bubble years of 1998-2000 are excluded. This should provide some support for the market.

Within equities, we are underweight in the US and Europe where we see the greatest risk of earnings downgrades. We are neutral on Japan as the market has fallen to a highly attractive level, with the dividend yield now exceeding the yield on 10-year JGBs. In recent years, similar developments have heralded strong rallies in Japanese equities. Although it is debatable whether the Japan market is ready to take off in the near term, we believe that the downside should at least be limited. We continue to be positive on Asia ex-Japan markets where earnings have on the whole been more resilient. We focus on domestic demand names and avoid the global exporters.

We are **neutral on bonds.** Following the strong rally in recent months, G7 government bonds are no longer cheap. However they are likely to continue to benefit from heightened risk aversion and a flight to safety.

Within G7 government bonds, we are overweight in the UK and Australia, which are advanced in their interest rate cycles, neutral weight in the US, Europe and Canada, and underweight Japan where yields are still extremely low. In duration terms, we are long in the UK, short in Australia and neutral on the US, Europe and Canada.

In Asia, we are positioned cautiously at the start of 2008, preferring high grade to high yield. We focus on defensive issuers and underweight sectors with expected technical headwinds.

We will also increase our exposure to Asian currencies and go long in duration in the US on expectations that the US dollar will weaken further and that more Fed rate cuts are forthcoming.

We introduce commodities into the portfolio. As an asset class, commodities have a low correlation with equities and bonds and are also typically an inflation hedge. For this quarter, we prefer exposure to soft commodities and gold. The growing movement for clean energy has meant the conversion of crops into bio-fuels and there has been an overall upward pressure on prices, as many crops are to some extent substitutes for each other. Gold prices have been moving closely with oil prices and are also enjoying an additional boost from the weak US dollar.

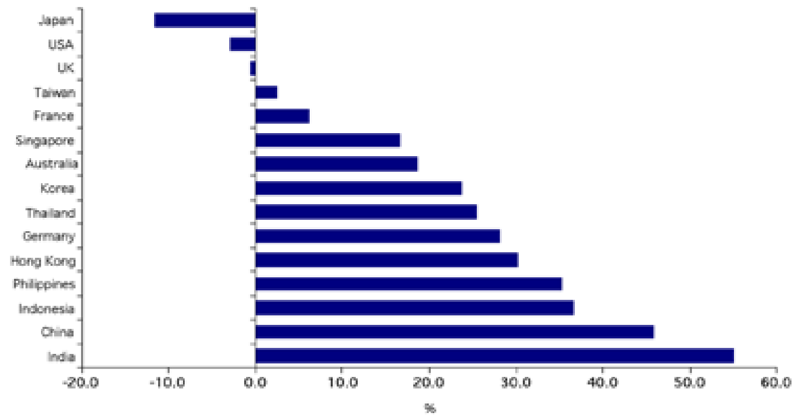
	Conservative	Change from 4Q	Moderate	Change from 4Q	Growth	Change from 4Q
Equities	25%	-10%	45%	-10%	65%	-10%
Bonds	55%	-2.5%	35%	-2.5%	15%	-2.5%
Commodities	10%	+10%	15%	+15%	15%	+15%
Cash	10%	+2.5%	5%	-2.5%	5%	-2.5%

Note: The neutral Moderate benchmark weights are Equities (55%), Bonds (35%). Commodities (5%) and Cash (5%)

GLOBAL EQUITY STRATEGY

Market Returns

Ranked Returns: Equity Indices
YTD as at 31 December 2007, SGD adjusted



US

Earnings Outlook

S&P earnings in 3Q dropped 5% due to declines in Financials, Energy and Consumer Cyclicals. The fall in Financials was driven by subprime writedowns and we are likely to see more charges in 4Q as Banks clear the deck for a stronger 2008.

The key question now is whether there will be a profit contagion to the other sectors. Analysts expect a 13% gain in 4Q for Non-Financials but we believe results could fall short of these forecasts. We are equally concerned about 2008 estimates, which until recently, had not been revised to any great extent despite the leading indicators pointing to a sharply slowing economy. Earnings are currently in the process of being revised as we head into the start of the reporting season.

Valuation

At 14.7x FY2008 estimates. the S&P 500 is beginning to look cheap compared to its own history but as mentioned, we believe there is a risk to 2008 earnings. In relative terms, the recent decline in bond yields have made US equities more attractive with the earnings yield on the S&P 500 300bp above 10-year Treasuries.

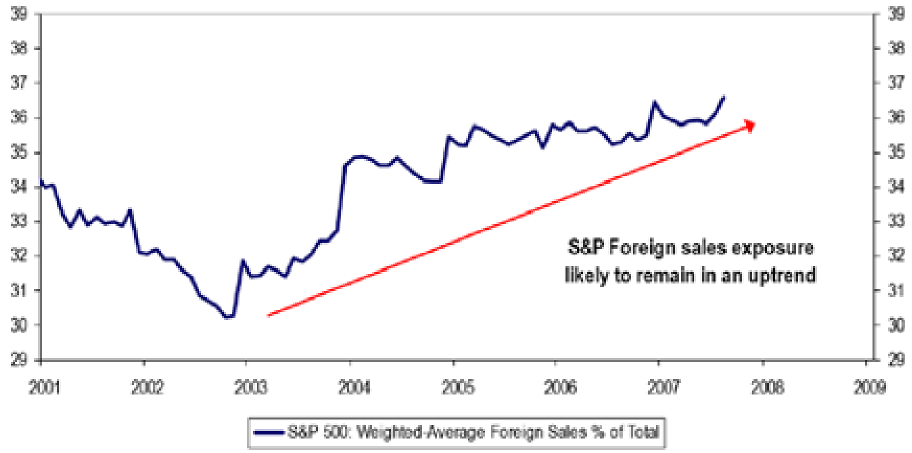
Strategy

The S&P 500 is not representative of the US economy. The foreign exposure of S&P 500 companies is on a clear uptrend and this provides good fundamental opportunities. For some time now we have been favouring the large-cap, globally diversified companies. We continue to stick to this theme and now also favour the sectors which are inflation beneficiaries. Our focus areas are in Healthcare, IT, Energy and Consumer Staples. The earnings of Healthcare and IT are driven by non-US demand, which is enjoying an added boost from a weak US dollar.

We continue to expect an upswing in corporate IT spending as it is now eight years since the last capex replacement cycle. In the Energy space, we prefer the service providers to the oil producers, as the rise in exploration demand and the global shortage of rigs continue to give pricing power to the former. Finally, we also like Consumer Staples and Healthcare, which are traditionally defensive sectors, and in the last 10 years, have been the sectors showing the highest correlation with the VIX.

MODEL PORTFOLIO

Sector	Weight	Top Picks
Consumer	Underweight	Altria Group,Coke
Energy	Neutral	Exxon Mobild
Financials	Neutral	US Bancorp
Healthcare	Overweight	Merck, Gilead Sciences
Industrials	Neutral	General Electric
Information Technology	Overweight	Adobe, Apple
Materials	Neutral	Freeport McMoran
Telecom Services	Overweight	America Movil
Utilities	Underweight	-



S&P 500 Foreign Sales Exposure

Source: ISI

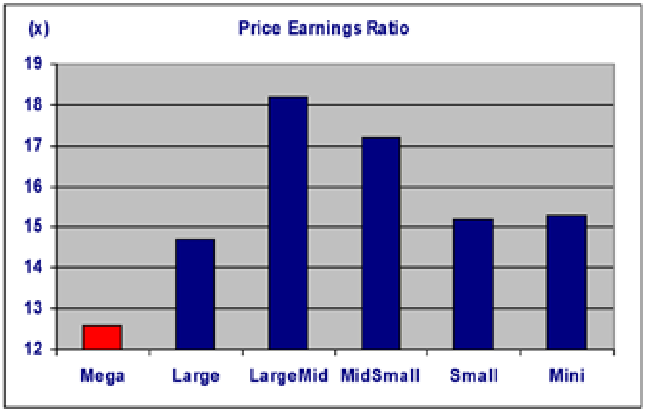
EUROPE

Earnings Outlook

Both the macro-economic backdrop and earnings momentum have deteriorated since the previous quarter. According to Consensus Economics, projections for 2008 GDP growth in the Eurozone have been revised down to 1.9%, from 2.2% in September. The ongoing US subprime crisis have caused credit spreads to continue widening and liquidity has been squeezed in the European financial markets. Banks, in turn, have tightened their lending standards across Europe thus hurting credit-sensitive demand particularly housing investment. There were steep declines in important sentiment indicators like the IFO Economic Climate for the Euro Area and the ZEW Indicator of Economic Sentiment (Germany) during the final quarter of 2007. The rapidly weakening US economy coupled with slowing consumer spending in Europe implies more economic downgrades ahead in 2008. On the corporate front, European earnings momentum turned negative in the final quarter. But at 9% consensus earnings for 2008 remains too high in view of the deteriorating global economic fundamentals. Our estimates for earnings growth in 2008 is around 6.8%, based on the historical pattern that nominal sales growth tends to grow in line with nominal GDP, assuming an operational leverage of 1.3x. Other headwinds for European earnings are currency hedges rolling off and raw material prices and labour costs potentially continuing to climb through 2008.

Valuation

Valuations, however, are not demanding in Europe reflecting a fundamentally strong corporate sector. The current forward PE of around 12x is close to the lows seen in the early 1990s. Similarly, both the nominal and real equity risk premium in Europe also suggest that equities are not expensive relative to bonds. Our Discounted Cash Flow model, likewise, indicates that the market is undervalued even after using our below-market consensus 2008 earnings growth assumption of 6.8%.



Source: SG Equity Research

Strategy

Despite the undemanding valuations, it would be difficult for the European equity market to outperform amid downgrades in both GDP growth rates and corporate earnings estimates. But it is worth noting that European non-financial companies are well-positioned for an impending slowdown in 2008. They are generating free cash flow with a yield of 4% and many have reduced the net debt/EBITDA ratio from over 2.0x to below 1.5x. Moreover, the high-gearing sectors like Construction and Materials, Utilities as well as Telecoms have interest cover well above 2x.

MODEL PORTFOLIO

Sector	Weight	Top Picks
Basic Materials	Neutral	Rio Tinto (UK)
Industrials	Neutral	ABB and Schneider Electric
Financials	Underweight	HSBC
Energy	Neutral	Shell
Telecom Services	Overweight	Telefonica and Telenor
Consumer	Neutral	Reckitt Benckiser, British American Tobacco
Utilities	Overweight	EDF, Suez and Iberdrola
Healthcare	Neutral	Roche and Novartis
Technology	Overweight	Nokia, Temenos

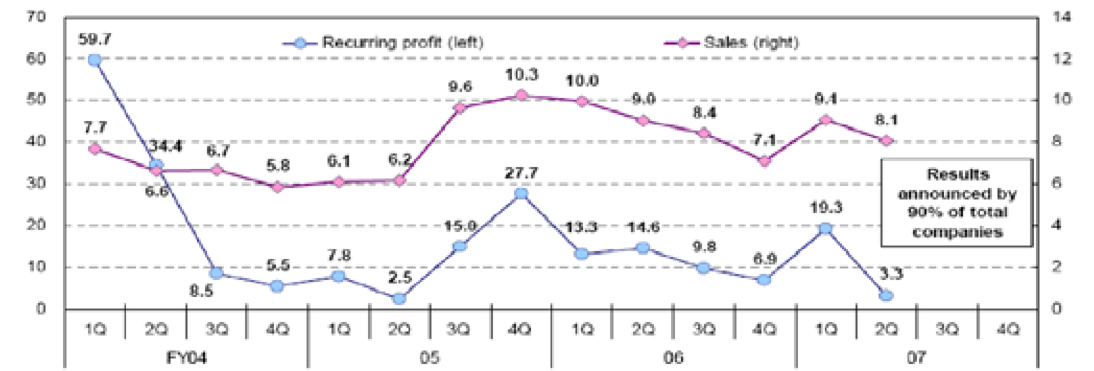
We see opportunities in four main areas. Firstly, mega cap stocks are still more cheaply priced than their mid-cap to small-cap peers on both the P/E and price/book multiples. Moreover, the mega-cap stocks tend to be in the more defensive sectors like Telecoms, Food & Beverage and Utilities. These include stocks like Telefonica, EDF, Suez and Nestlé. Moreover, the dividend yield on the mega-cap stocks is about 1.5x that of mid-cap and small-cap stocks. Secondly, we expect more interest rate cuts not only in the US but also in the UK and eventually in Continental Europe. We expect the Bank of England's Repo rate to come down by another 50bp, by mid-2008. As such, we favour interest-rate sensitive sectors like Healthcare, Utilities, Consumer and Banks. Thirdly, Climate Change catalysts will remain at the forefront in 2008 with an increasing drive towards the production of cleaner energy and growing legislation worldwide to cut carbon dioxide emissions. Specific materials and segments are expected to prosper from these trends including the producers of wind turbine engines (Gamesa and Vestas System) as well as companies benefiting from greater usage of fertilisers and polysilicon. Finally, we plan to invest in Russia which enters 2008 with strong fundamentals (Russia's foreign exchange reserves are one of the largest in the world). In particular, we prefer segments which leverage on Russia's comparative advantage in natural resources like potash. We also like its telecom sector which offers stronger growth potential relative to its more developed European peers.

JAPAN

Earnings Outlook

2QFY07 earnings growth moderated from 1QFY07, although it was above expectations. TSE 1st section stocks show sales up 8.1% yoy and recurring profit (RP) up just 3.3%. Prospects for corporate profitability are becoming less clear with macro economic conditions worsening not only globally but also within Japan. Based on consensus forecasts, FY07 sales and RP are expected to rise by 6.3% and 7.4% respectively.

Quarterly Sales and Recurring Profit at TSE1 Companies (y/y %) — **Chart 1**



Source: Compiled by DIR.
Note: Universe = TSE1 companies (excl. financials and listed subsidiaries). Business results for Mar and non-Mar companies were divided into quarterly increments and plotted on a y/y% change basis. Data for 2Q FY07 aggregate quarterly business results for companies whose quarter ended between Jul and Sep. 2Q FY07 data includes results released through 15 Nov.

Valuation

Valuations of Japan equities appear attractive. Prospective PER of 15.8x is at a 33-year low. The equity dividend yield of 1.6% now exceeds the 10-year JGB yield of 1.49%, which has historically suggested downside support for the market.

Strategy

Global equity market conditions are likely to remain challenging given the overall tightening of credit in global markets as well as the heightened risk of a US recession. Protracted weakness in the Japan's domestic economy makes it particularly vulnerable to external shocks.

We have moved our strategy to be positioned more defensively, adding to our holdings in stocks from Communications and Consumer Staples. We have reduced our weights in economically-sensitive sectors such as Real Estate and Technology. Financial stocks are trading at historical low valuations.

However, the fundamental picture remains sluggish given muted loan growth, and the strong likelihood that the Bank of Japan's next rate hike will be delayed. We continue to favour structural growth stocks, and companies benefiting from the urbanisation occurring in the emerging economies.

MODEL PORTFOLIO

Sector	Weight	Top Picks
Autos	Neutral	Toyota, Exedy, Denso
Real Estate	Neutral	Sumitomo Realty, Mitsui Fudosan
Financials	Neutral	Mizuho, SMFG, T&D
Materials	Neutral	Nippon Electric Glass, Toray, Nippon Steel, JFE
Industrials	Overweight	Komatsu, Sumitomo Heavy, Fanuc, Mitsui & Co
Healthcare	Neutral	Takeda, Astellas
Consumer	Neutral	Seven & I, Unicharm, Toyo Suisan
Technology	Neutral	Nintendo, Ricoh, Ibiden
InfoComm	Neutral	KDDI, NTT, Capcom

ASIA EX-JAPAN

Outlook and Strategy

We believe that growth will be maintained in Asia ex-Japan, led by the resilient economies of China and India. The domestic-driven economies like Indonesia, Thailand and Malaysia should also stay firm. An expected faster appreciation of the Chinese renminbi will be positive for Asian currencies as well as financial markets, as will expected further Fed rate cuts. Rising inflation continues to be a key risk in Asia with the accompanying risk of higher interest rates, as the bias of Asian central banks will be towards taming rising prices.

Although Asian corporates saw upgrades in their earnings expectations in the fourth quarter of 2007, we believe that risks have increased in the Asian markets given the continued uncertainty over the fallout from sub-prime mortgages and the heightened risk of a US recession. Hence, we move our strategy to be positioned more defensively, favouring defensive growth stocks, which are reasonably valued. We tactically reduce our weight in China from overweight to neutral given the Chinese policy-makers' stated aim of moving towards a tightening stance, which will create headwinds for the market. There could be potentially more negative newsflow as corporates start to feel the pinch, We raise Hong Kong to overweight, as we view the market to be a key beneficiary of lower US interest rates. We also move Thailand, Indonesia and Malaysia to overweight. We tactically reduce our underweight position in South Korea due to its attractive valuations. There is a potential for downgrades in earnings in export-dependent economies such as Taiwan, where we are underweight.

In terms of our sector strategy, we raise our weights in Utilities to overweight, in line with our strategy to go defensive. We remain overweight in Consumer Staples as the domestic sector offers more resilient growth in the face of the slowing external sector. We maintain an overweight in Industrials as infrastructure spending by Asian governments will underpin demand in the construction sector. We continue to be overweight Property, but move towards the Hong Kong market, which is a key beneficiary of falling interest rates. We remain underweight in Financials as our view is that concerns over banks' CDO exposures will linger. We continue to underweight Technology as we expect it to be most impacted by a slowdown in export markets.

Web site Print

China – We continue to be positive on the China market for the longer term given the resilient domestic economy with urbanisation driving domestic consumption and infrastructure spending. More Qualified Domestic Institutional Investors (QDII) funds – an estimated US$90bn – are expected to leave China by the end of 2008, of which one-third is expected to be invested in Hong Kong-listed Chinese companies. That will be positive for China 'H' share companies as 'H; share still trade at a large discount to 'A' shares and their valuation should converge. On the flip side, the key risk for the Chinese economy is high inflation, which could become persistent. The Government is pursuing more serious tightening measures in an attempt to control inflation and have instituted outright price controls on energy and food. We view that this tightening stance could potentially dampen corporate profits as rising cost pressures lead to margins being squeezed and if external demand collapses, overcapacity will also result. The Chinese export sector is also at risk of being affected by a sharp US slowdown. Hence our strategy for this quarter is to tactically reduce our weight in China from overweight to neutral.

Hong Kong – We further upgrade Hong Kong to overweight from neutral as we view the market to be the most direct beneficiary of US Fed rate cuts with asset inflation providing a boost to markets. Near negative real interest rates, a fall in unsold inventory and rising wages have revitalized the Hong Kong physical property market, which is in turn supportive of property stocks. Banks are also expected to benefit from a pick-up in mortgage loans. The key risk for the Hong Kong market is companies outside the property sector seeing earnings downgrades on rising cost pressures.

Taiwan – We maintain our underweight position in Taiwan as we view the tech-heavy market to be most vulnerable to a sharp US slowdown. In addition, banks are now vulnerable to further write-downs from holdings in collaterised debt obligations (CDOs) and the market in general lacks catalysts. With the strong showing by the Koumintang in the legislative elections, expectations for a KMT victory in the presidential elections have increased and Financials and Consumer stocks are likely to benefit if cross-straits relations improve.

Korea – We raise our weight in Korea from underweight to neutral as there are some signs of a pick-up in domestic consumption that could mitigate the impact of a US slowdown on the external sector. There is scope for capital management among Korean corporates and the election of a pro-business President is expected to be positive for the market.

Indonesia – We raise our neutral weight to overweight as we expect low interest rates to fuel domestic growth. Private investment is also expected to be a growth driver following favourable government policy towards the infrastructure sector with spending on power plants and toll roads expected to add substantially to GDP. The market is also expected to benefit from higher commodity prices such as coal and palm oil.

Malaysia – We raise our weight in Malaysia from neutral to a slight overweight as we expect the internal economy to be one of robust consumption-led growth on the back of liberalization in the use of employee provident funds (EPFs) and civil servants' pay increase. The market is also expected to benefit from the high palm oil prices while a pre-election rally may be on the cards with elections potentially being held early in the year.

The Philippines – We maintain our underweight in line with our defensive stance. Overseas foreign workers (OFW) remittances remain strong and the government is committed to privatising state-owned assets to cover the budget deficit. The key risks include a mismanagement of monetary policy and political volatility.

Thailand – We upgrade our neutral weight to overweight as there are early signs of a recovery in private investment via higher SME loans growth and domestic consumption. Following the December elections, we expect to see some return to normalcy for Thailand that could spur a positive re-rating to Asia's cheapest equity market. The key risk is political as a coalition government led by the People's Power Party (PPP) formed by the former Thaksin-led Thai Rak Thai (TRT) party members could face resistance from the military and may be ineffective.

India – We upgrade India from underweight to overweight as the market has shown to be one of the most resilient in the face of volatility in global markets. GDP growth is still robust at 8-9% and we expect the liquidity environment in India to improve and there is a possibility that interest rates are peaking. Indian companies are also delivering strong earnings growth and industrial production is accelerating.

MODEL PORTFOLIO

Sector	Weight	Top Picks
Banking	Underweight	Kasikornbank, Bank Rakyat Indonesia
Consumer	Overweight	Anta Sports, Sime Darby, Astra Agro
Energy	Neutral	PetroChina
Industrials	Overweight	Hyundai Development, Sembcorp Industries
Materials	Underweight	China Bluechemical
Property	Overweight	Sun Hung Kai Properties, Kerry Properties
Technology	Underweight	Innolux, Hon Hai Precision
Telecoms	Neutral	China Mobile
Utilities	Overweight	Beijing Enterprises

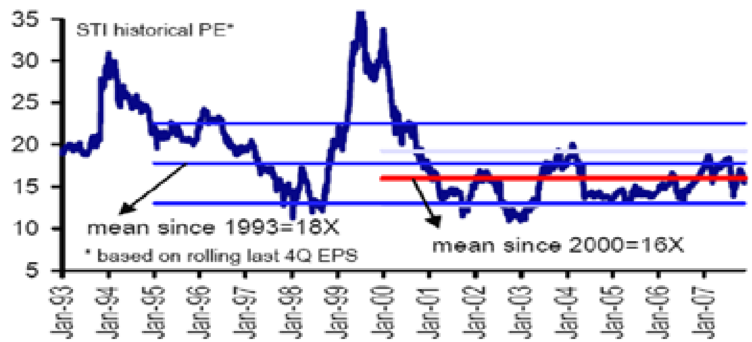
SINGAPORE

Earnings Outlook

The expected earnings growth of 12% in 2008 is likely to be driven by the banks, with property and conglomerates still contributing strongly. For the banks, draw-downs on record property transaction values in the previous years will help drive loan growth while for the property companies, development profit recognition from sales over the past two years will continue to drive earnings. Similarly, record order backlogs for the conglomerates sector provide earnings visibility on a 1-2 year view. The key risk to earnings growth for FY08 is a sharp slowdown in the economy driven by a recession in the US.

Valuation

In the first week of 2008, the STI was back to the level just prior to the 50bp initial Fed rate cut on 18 September 2007. While the odds of a US recession have increased, our base case assumption is for sub-par growth in the US but no recession. Singapore's GDP should remain robust in 2008 given the powerful upswing in the domestic investment cycle, which in turn is now boosting consumption growth via a fully employed job market. Market valuation stands at a relatively undemanding 15x trailing FY07 P/E – versus a 14-year mean of 18x – but the risk to 2008 earnings has risen from 3 months ago. Other valuation metric such as comparing Price/Book against ROE suggests that the STI remains undervalued.



STI Trailing Price/Earnings

Source: Datastream, UBS estimates

Strategy

We remain cautious in the near term and advocate a defensive portfolio in the first quarter of 2008 when uncertainties over growth are likely to be at their highest. Furthermore, credit markets have not returned to normalcy as evidenced by the still elevated spreads in the money markets. However, past episodes of Fed easing when the Singapore economy remained resilient pointed to a positive return to the STI 12 months into the initial Fed rate cut. We would view large falls as buying opportunities.

Corporate earnings remain healthy and interest rates remain low in Singapore. We overweight the Banking, Consumer Discretionary and Industrials sectors. In the Consumer Discretionary sector we see stock-specific catalysts, while in the Banking sector we are slightly overweight due to our positive view of the asset reflation theme in Singapore, which will be positive for loan growth, coupled with the relatively small CDO exposure for the local banks. We also overweight the Industrial sector as the conglomerates continue to ride on the still buoyant offshore and marine industry.

MODEL PORTFOLIO

Sector	Weight	Top Picks
Consumer Discretionary	Overweight	Singapore Press Holdings, Jardine C&C
Consumer Staples	Underweight	-
Energy	Underweight	-
Financials (Banks)	Overweight	DBS
Financials (Real Estate)	Neutral	CDL Hospitality Trust, Bukit Sembawang, Hiap Hoe
Healthcare	Underweight	-
Industrials (Capital Goods)	Overweight	Keppel Corp, SembCorp Industries, ST Engineering
Industrials (Commerical Services & Supplies)	Overweight	Zagro Asia
Industrials (Transportation)	Overweight	SMRT, SingPost
Information Technology	Underweight	-
Telecommunications	Underweight	SingTel
Utilities	Overweight	CitySpring Infrastructure Trust

02 global fixed income strategy

Web site
Print

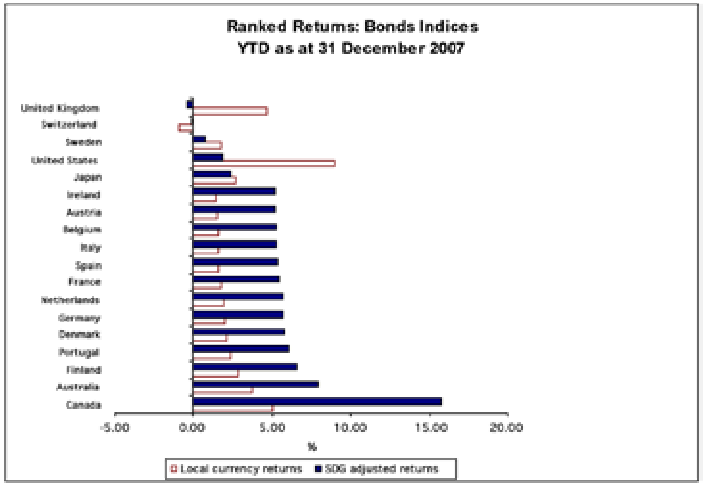
MARKET RETURNS

Global Bonds

Economic data continued to soften further in the last quarter of 2007. The slowdown appeared to be across the G3, with the US declining the most. Forward looking indicators such as the OECD leading indicators are pointing to a further deceleration in the coming six months, with weakness especially pronounced in Japan. The leading indicators for Europe are also showing signs of economic moderation, though to a lesser extent.

The slowdown appears to be broad-based. Employment growth in the developed economies is losing momentum and with this, retail sales are also moderating. Consumer confidence surveys have also weakened. In the business sector, both surveys and actual data appear to have peaked and are likely to slow further; though the services managers' surveys are holding up relatively better than the manufacturing managers' surveys. Further moderation is likely for both sectors because of the poor conditions in the financial markets and the resultant tightening of credit.

Although the economic data is signaling a moderation in activity, headline inflation is moving higher, primarily because of food and energy prices. This is a function of supply disruptions and geopolitical problems but consumer inflation is nonetheless being pushed up in an environment of softening growth. So far, there are few signs of the higher food and energy prices penetrating into core inflation and inflation expectations, as priced by financial markets, are showing a benign outlook. Although it is likely that commodity inflation could moderate as the global economy moderates, geopolitical risks remain high and there is a chance that this does not actually occur.



Please refer to the last page for important notice & disclaimer

The high degree of uncertainty to the economic outlook and the continued stress in financial markets have resulted in a weak performance for risky assets over the recent weeks and correspondingly strong performance in risk-free assets. This has resulted in a low absolute yield in the risk-free markets and even lower yields in the short end of many yield curves, especially in the US. Without an aggressive reduction of the interest rates, the front end of yield curves appears to be quite expensive compared to policy rates. But given the unusually high degree of uncertainty, the short end of yield curves is likely to remain fairly well-bid and could remain expensive for an extended period of time.

The interest rate cuts by the US Federal Open Market Committee and the liquidity injections by the major central banks show a commitment by central banks to counter this imminent slowdown. Although the issue of how much to cut and when to cut will remain debated by the market, the actions clearly demonstrate an intention to moderate the impact from the slow-down. The exception is perhaps the European Central Bank which continues to sport a hawkish rhetoric despite the recent softening in economic data as headline inflation in the Eurozone remains high.

We expect economic conditions to continue to be challenging and believe this will force the main central banks to continue to reduce official interest rates at the cost of a temporary neglect of inflation. This will be supportive of risk-free interest rate positions. We propose a neutral posture with a bias to add on market weakness.

Asian Bonds

Asia's credit markets ended 2007 on a weak note with near-term valuations across the region remaining vulnerable in 2008 given the headwinds from the global credit markets and the rising risks of a US recession. Asian credit spreads have widened across the board with the high yield and financial sectors being hardest hit. The new issuance market has also been affected with many companies delaying their bond issuance as investor appetite has waned.

We do not see an immediate end to this current malaise and expect 2008 to present itself as a game of two halves. The first part of the year is likely to be of a stop-start nature, with the market being plagued by the bad news. The second half is likely to be better flowing as risks are quantified and the appetite for credit returns. While Asia fundamentals remain intact on the back of resilient investment and consumption, we continue to debate the timing of the recovery and the eventual return of stability to our markets in 2008.

We also expect uneven performance to be delivered across Asia's credit segments. A number of global and regional themes at play will, individually or in combination, impact credits to varying degrees. For example, we expect Asia's banking sector to continue to underperform in 2008 not only due to broader developments across the global banking sector but also owing to the expected deterioration in the sector's regional technicals on anticipated heavy supply from Korean and Indian banks.

As a result, we are positioned cautiously at the start of 2008, generally moving up the credit curve, focus on defensive issuers and underweight sectors with expected technical headwinds. We will also increase our exposure to Asian currencies and go long in duration in the US on expectations that the US dollar will weaken further and that more Fed rate cuts are forthcoming.

Singapore Bonds

Flash estimates of the Singapore economy indicate that GDP contracted in the final quarter of 2007. Full year growth is still expected to be above 7%, still a commendable performance and well above its potential output of 4% to 6%. The resilience of the economy, despite a weak electronics sector, is a testament to the successful efforts by the government to diversify into other industries.

While the restructuring efforts will continue to bear fruit into 2008, sentiment has been weighed down by the ongoing US sub-prime situation, and the spillover to the broader US economy. So far, the effect is clear in the financial sector, where there is evidence that banks are tightening lending standards to the corporate and consumer sectors. Whether this will blow up into a full-fledged credit crunch for the broader economy is perhaps too early to tell, as banks were well-capitalized prior to the recent shocks. The Singapore government has cautioned that this year's growth could potentially tilt towards the lower end of its 4.5% to 6.5% target range in 2008, if the US economy deteriorates further.

On a less positive note, Singapore inflation accelerated to 4.2% in November 2007 – the fastest pace of increase since 1982, the effect of stubbornly high commodities-related prices and global food inflation. This was also coupled with domestic factors including above-potential growth, a tight labour market and rising housing cost. For the January-November period, the Consumer Price Index (CPI) was up 1.9% year-on-year and looks to exceed MAS' expectation of 2% for all of 2007. These inflationary pressures are likely to persist till first half of 2008 and the CPI is projected to surge to 4% to 5% in first half of 2008 and eased subsequently to 1.5% by the end of 2008. Overall, the CPI is expected to average about 3.5% to 4.5% for the full year of 2008.

As a result of higher price pressures, MAS steepened the gradient of its SGD NEER (nominal effective exchange rate) policy band in October 2007, although it maintained its 'gradual and modest apprecia¬tion' position. However, should inflation escalate beyond expectation, MAS is expected to remove the word 'gradual' at the coming meeting in April 2008.

The environment over the next 3-6 months will be very challenging. The US subprime problem is still evolving and it is unclear what the full losses will be and also the impact of the credit crunch on the global economy. We expect the Fed to retain its easing stance into 2008, thus leading short term SGD rates lower as the short end is most sensitive to Fed cuts. However, in view of increasing domestic inflationary pressures, any weakening of long-term SGD interest rates may be limited. As such, we are positioned between the five to ten-year tenor of the curve.

Web site Print

CURRENCIES

The US dollar lost ground in the last quarter of 2007, with the Euro, Japanese yen, Swiss franc and Singapore dollar all benefiting from the broad US dollar weakness.

The growing risk to the US economy from the ongoing subprime crisis has continued to cast a dark shadow over the currency and the market is pricing in aggressive interest rate cuts by the US Federal Open Market Committee. Although there have been brief moments, typically upon sharp spikes in volatility, when the US dollar strengthens due to its historical status as a safe haven currency (in terms of liquidity), the currency has, in subsequent periods, declined further.

Most Asian currencies have benefited from the weak US dollar and will likely to continue to do so. Although the Asian economies are unlikely to be immune from a US economic slow-down, the economic fundamentals of most Asian economies have significantly improved compared to a decade ago. Economic growth continues to be relatively stronger compared to the US and there is policy flexibility in light of the huge growth in foreign reserves.

We continue to expect a softer US dollar in the coming year as the softening economic environment and still uncertain outlook of the US housing market put the risks for the currency on the downside.

CURRENCY FORECAST

Currency	Against USD End 4Q 2007	Forecast End 1Q 2008
Japanese Yen (JYP)	112	105
Euro (EUR)	1.47	1.50
Singapore dollar (SGD)	1.44	1.41

Important Notice & Disclaimers

This publication is strictly for information purposes only and should not be construed as accounting, legal, regulatory, tax, financial or other advice. This publication is not an offer, recommendation, solicitation or advice to buy or sell any investment product.

All information contained in this publication is based on facts, assumptions, forecasts and analysis as of the date of this publication and is subject to change at any time. Although care has been taken to ensure the accuracy of information contained in this publication, UOB Asset Management Ltd ("UOBAM") and its employees make no representation and accept no responsibility for its completeness or accuracy.

Past performance of any investment product, investment product manager, company or entity mentioned in this publication, and any forecasts on the economy or markets are not necessarily indicative of the future or likely performance of such product, manager, company or entity. Any extraordinary performance may be due to exceptional circumstances which may not be sustainable.

Units in funds are not deposits or obligations of, or guaranteed or insured by, United Overseas Bank Limited, UOBAM, UOB Group or any of their affiliates or distributors. United Overseas Bank Limited, UOBAM, any subsidiary or associate of the UOB Group or any of their affiliates may have interests in entities or funds mentioned in this publication and may also perform or seek to perform brokering and other investment or securities-related services for such entities or funds. Investments are subject to investment and foreign exchange risks including the possible loss of the principal amount invested. The value of units and any income from them may fall or rise. All application for units in any of the funds must be made on the application forms accompanying the prospectus for the fund (the "Prospectus"), which may be obtained from UOBAM or any of its appointed distributors. Investors should read the Prospectus carefully before deciding whether to subscribe for or purchase units in the fund. Investors may wish to consult a financial adviser before investing in any investment product.