

Asia Pacific region



Overview

Asian equity markets fell in May to their lowest level in 10 months before clawing back some of the lost ground. The MSCI Asia Pacific index ended more than 9% lower in US dollar terms, while that excluding Japan fell almost 11%. Net foreign sales of Asian equities were the highest in more than a decade. Risk aversion rose sharply amid ongoing fears the European debt crisis would spread and subsequent rumours that Beijing may review its debt holdings in the Continent. Although the Chinese authorities refuted these claims, Germany's controversial ban on naked short selling, coupled with the Spanish central bank's takeover of several regional lenders, intensified worries that the tentative global economic recovery may be derailed. Adding to the gloom were additional moves by China to cool the property market and heightened political tensions on the Korean peninsula.

Investors largely ignored the robust first-quarter economic growth data, which continued to exceed expectations across most of Asia. The large economies of China, India and Indonesia, as well as the more export-oriented ones, such as Hong Kong, Korea, Taiwan and Singapore, saw GDP growth accelerate, while election spending and overseas remittances drove the Philippine economy. Japan also saw growth quicken because of strong auto and high-tech exports, but consumer prices fell for a thirteenth consecutive month.

Consumer price inflation in the region rose, particularly in Australia during the first quarter as wages rose; China, where consumer and property prices accelerated in April; India, where food prices advanced; and Singapore, where transport and housing costs climbed. In contrast, Korea and Indonesia saw price inflation fall. Most central banks opted to leave interest rates unchanged but Australia and Malaysia hiked rates, while India announced it would gradually unwind monetary stimulus. China increased banks' reserve ratios for the third time this year, and introduced further measures to cool the property market. India proposed a US\$11 billion fund for infrastructure needs. Hong Kong and Singapore will release more land to dampen rising home prices, while Malaysia plans to cut subsidies of petrol, gas and education.

On the political front, Indonesia's embattled finance minister Sri Mulyani Indrawati quit to join the World Bank; Philippine senator Benigno Aquino won the presidential election by a landslide; and Thailand extended a nationwide curfew as anti-government protests spread to the provinces despite ending in Bangkok. An arrest warrant on charges of terrorism was issued for former prime minister Thaksin Shinawatra.

Looking ahead, equity investors are becoming increasingly nervous amid fears that Europe's financially troubled periphery may dim the Continent's prospects and possibly trigger a relapse in the global economy as a whole. In Asia, there are worries that China's moves to cool its runaway property market may not be sufficient to prevent inflationary pressures rising, while political instability has been exacerbated by the escalating row between the two Koreas as well as Japan's revolving door politics that has seen four prime ministers resign in the last four years. Japan's prime minister Yukio Hatoyama quit in early June after less than nine months in office amid waning public support.

Over the short term, we remain cautious about the prospects for corporate earnings growth, as rising input prices, in combination with stagnating top line growth, threaten to hurt margins. There are also doubts about the sustainability of recoveries once economies are weaned off government stimulus measures. However, Asia's strong fiscal position give governments the option to extend pump priming should the need arise. As such, long-term fundamentals for the region remain robust, with rising intra-regional trade and domestic consumerism underpinning the region's growing self-reliance.

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Corporate news

Australia: The government proposed a new levy on resource companies' profits, which will at face value have a dramatic impact. However, this is only the initial proposal and there will be a period of consultation with various hurdles to be cleared before it is ratified. **BHP Billiton** said the proposed 40% tax on profits will increase its tax rate from the current 43% to 57% from 2013, while **Rio Tinto** is reviewing the potential impact on its domestic operations. Elsewhere, **QBE Insurance** raised US\$850 million in bonds to reduce bank borrowings.

China/Hong Kong: Swire Pacific shelved the initial public offering of its property division owing to weak market demand. **ASM Pacific** reinforced its market leadership with stronger orders across most applications in the first quarter. Higher interest margin and fee income helped **China Merchants Bank**, while a recovery in crude oil prices boosted **PetroChina's** profits. Its parent, CNPC, will acquire a 35% stake in Shell's Syrian oil and gas unit.

India: **ABB India's** parent will buy the company's shares at a significant premium, offering 900 rupees a share to lift its stake in the Indian unit to 75%. **Piramal Healthcare** plans to sell its domestic formulations business to US-based Abbott Labs for US\$3.7 billion to focus on contract manufacturing and anaesthetics. **Godrej Consumer Products** completed the acquisition of the 51% of Godrej Sara Lee it did not own from its joint venture partner, consolidating its position in the Indian fast-moving consumer goods space. **ICICI Bank** will buy Bank of Rajasthan in a move that will add over 460 branches to its network. Our holdings posted positive results: **HDFC** full-year results benefited from solid loan growth and **Grasim** gained from healthy cement demand.

Indonesia: **Unilever Indonesia** enjoyed stronger first-quarter sales. It will invest US\$430 million over the next three years to double its size in five years.

Japan: **Toyota Motor** will recall four Lexus models over a steering problem. The carmaker also partnered US-based Tesla Motors to build electric cars, a marked departure from its growth strategy. Meanwhile, its global vehicle production rose in April and sales jumped 21.3% year-on-year. **Honda Motor** restored managerial salary cut last year following a rebound in earnings; it had planned to expand capacity in China but subsequently suspended production at all its Chinese plants because of strikes. A recovery in global demand boosted **Canon's** shipments this year; separately, it abandoned the development of televisions with its costly SED (surface-conduction electron-emitter display) technology. **Unicharm** announced a ¥65.7 billion buyout of pet food affiliate Unicharm Petcare. **Mitsubishi Estate** will supply more condominiums amid signs that the market segment is bottoming. In earnings news, **Shin-Etsu Chemical's** results were helped by recovering demand and good cost control; Canon's earnings improved partly because of a rebound in spending by makers of chips and LCD panels; while better cost controls improved the profitability and cash flow of Toyota and **Takeda Pharmaceutical**.

Korea: **Samsung Electronics'** first-quarter results impressed as supply constraints and better-than-expected sales drove memory prices; it is investing more to address the supply shortage and widen the technology gap with its rivals by increasing capital expenditure to 18 trillion won this year. **Daegu Bank's** net interest income grew but its asset quality deteriorated.

Malaysia: **CIMB Group** is boosting its presence in Asia: it is seeking a secondary listing in Indonesia to enhance its brand and expand its operations. The lender is also increasing its stake in Indonesian subsidiary CIMB-Niaga by buying a 19.67% stake from state investment agency Khazanah, which it will fund via a new issue of up to 134 million shares at M\$14.50 each. In Cambodia, it obtained a banking licence to set up a wholly-owned subsidiary. On the earnings front, the group's first-quarter net profits rose on lower provisions and higher non-interest income.

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Philippines: In first-quarter results, **Ayala Land's** increase in net income was driven by higher home sales but the **Bank of the Philippine Island's** net profits fell because of higher expenses and provisions for income tax.

Singapore: First-quarter results were generally favourable: **ST Engineering** was helped by good performances across most divisions. Lower provisions boosted both **UOB**, which also benefited from the sale of its life assurance business, as well as **OCBC**, which posted the best loan growth among domestic banks. Enhanced operating margins drove **Venture Corp's** net profits. **City Developments** was driven by property sales and its hotel subsidiary. For the full year, **SingTel's** earnings were buoyed by stronger contributions from its regional associates, while **Singapore Airlines** remained profitable as second-half earnings offset first-half losses.

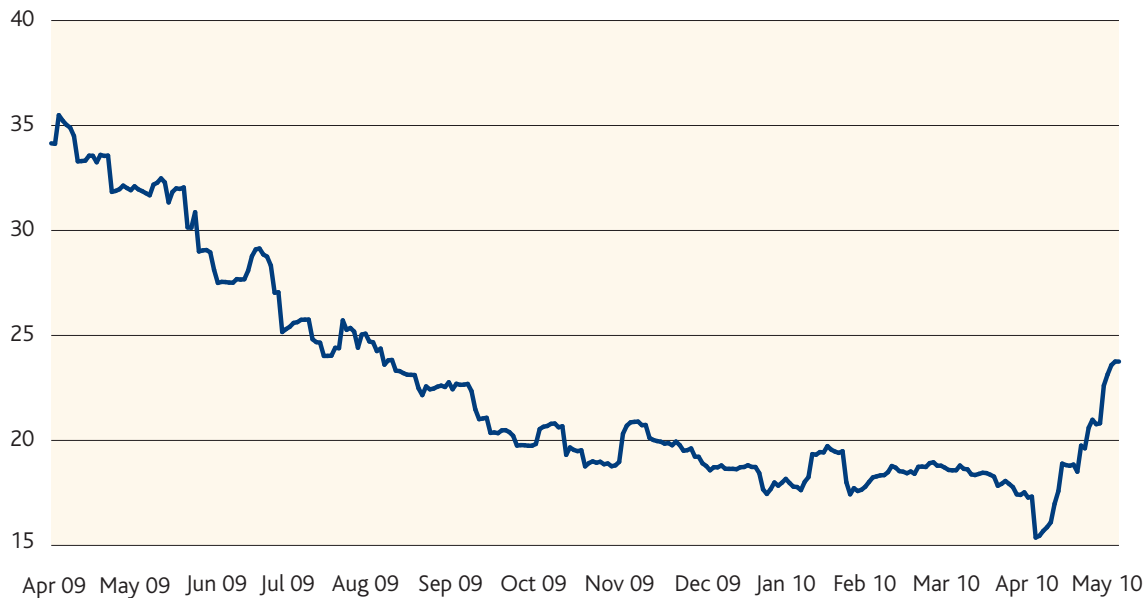
Taiwan: **Taiwan Mobile** posted resilient first-quarter earnings though management warned that price cuts and elevated costs could impact second-quarter performance. Nevertheless, it proposed a dividend payout of NT\$5.03 per share. **TSMC's** results were boosted by strong demand and margin improvement.

Thailand: **Siam Cement's** results were underpinned by its chemicals and paper divisions. **PTT Exploration and Production's** earnings rose on higher selling prices, lower costs and a one-off tax gain.

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Focus: Back with a vengeance

Historical volatility (60 days) of the MSCI Asia Pacific ex Japan Index



Source: Bloomberg, 31 May 2010

Market volatility had been gradually declining over the past 12 months, slowly reaching its lowest level for the period in April. All it took was for the European debt crisis to worsen in May and suddenly, nervous investors' confidence evaporated.

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Performance of Asia Pacific stock markets

	31/05/10 Index	1 month (%)			Year to date (%)		
		Local currency	US\$	£	Local currency	US\$	£
MSCI AC Asia Pacific	95.78	-8.60	-9.84	-5.02	-5.62	-5.79	4.71
Australia ASX All Ordinaries	4453.60	-7.87	-16.98	-12.54	-8.79	-14.93	-5.46
China Shanghai Se B-Share	207.54	-16.08	-16.08	-11.59	-17.78	-17.78	-8.62
Hong Kong - Hang Seng	19765.19	-6.36	-6.64	-1.65	-9.63	-10.02	0.01
India Bse Sensex 30	16944.63	-3.50	-7.67	-2.73	-2.98	-2.62	8.23
Indonesia Jakarta Composite	2796.96	-5.87	-7.52	-2.57	10.36	13.01	25.60
Japan Topix	880.46	-10.80	-7.88	-2.96	-2.99	-0.79	10.26
Korea Kospic Composite	1641.25	-5.76	-13.10	-8.46	-2.47	-5.51	5.02
FTSE Bursa Malaysia	1285.01	-4.56	-6.81	-1.83	0.96	5.99	17.80
NZSE All Share	719.24	-6.57	-13.85	-9.25	-6.96	-13.87	-4.27
Pakistan KSE100	9326.42	-10.56	-11.89	-7.17	-0.64	-1.73	9.22
Philippines PSEi Composite	3272.73	-0.53	-4.42	0.69	7.21	7.12	19.05
Sri Lanka CSE Colombo All-Share	4237.16	1.15	1.29	6.70	25.15	25.81	39.83
Taiwan TAIEX	7373.98	-7.87	-9.70	-4.87	-9.94	-9.90	0.14
Thailand Bangkok SET	750.43	-1.71	-2.18	3.05	2.16	4.77	16.45
MSCI India	690.21	-4.01	-8.16	-3.25	-2.39	-2.03	8.89
MSCI Singapore	326.76	-7.51	-9.46	-4.61	-6.47	-6.20	4.25

Source: Factset.

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During the month we met the following companies:

Australia: ARB, Austereo, Austar, Australand, Australia & New Zealand Banking, BHP Billiton, Brickworks, Campbell Brothers, carsales.com, CFS Retail Trust, Clough Engineering, Commonwealth Bank of Australia, Commonwealth Property Office Fund, CSG, Customers, David Jones, Incitec Pivot, InvoCare, IOOF, Iress Market Technology, JB Hi-Fi, Leighton, Monadelphous, Myer, National Australia Bank, Navitas, Newcrest Mining, Orica, PaperlinX, Programmed Maintenance Services, SAI Global, Seek, Sonic Healthcare, SP Ausnet, Suncorp Metway, Super Cheap, Tower Australia Group, Wesfarmers, Westfield Group, Westpac Banking, Wotif.com

China/Hong Kong: Agricultural Bank of China, Anta Sports Products, Asia Satellite Telecommunications, Baidu.com, Cheung Kong, China Fire & Security Group, China Life Insurance, China Mengnui Dairy, China Mobile, China Petroleum & Chemical, China Resources Land, China Resources Enterprise, China South Locomotive & Rolling Stock, CLP Power, Digital China, Dongfeng Motor Group, Green Dragon Gas, Guangdong Alpha Animation & Culture, Li & Fung (Trading), Li Ning, PetroChina, Stella International, Tencent, Tsingtao Brewery, Towngas China, Uni-President, Wharf, Wumart Stores, Xinjiang Goldwind Science & Technology, Yangzijiang Shipbuilding, Zhuzhou CSR Times Electric

India: ABB India, Ashok Leyland, Eicher Limited, Gas Authority of India, Godrej Consumer Products, Grasim Industries, ING Vysya Bank, Oberoi Realty, Shopper's Shop

Indonesia: ACE Hardware, Delta Dunia, Indika Energy, Indosat, International Nickel, M.P. Evans Group, Petra Foods, PT Energi Mega Persada, Ramayana Lestari Sentosa, Telekomunikasi Indonesia

Japan: Accordia Golf, East Japan Railways, Fast Retailing, GMB, Honda Motor, Ikyu, Macromill, Mandom, McDonald's Holdings, Mitsubishi Estate, Omron, Parco, Resorttrust, Start Today, Takara Bio, Takara Printing

Korea: Busan Bank, Korea Telecom, LG Electronics, Samsung Electronics

Malaysia: Aeon Co. (Msia), Allianz, Bursa, Hong Leong Bank, Shin Yang Shipping, TA Global

New Zealand: Millennium & Copthorne New Zealand

Pakistan: Unilever Pakistan

Philippines: Ginebra San Miguel

Singapore: CDL Hospitality Trusts, Chi-X Asia Pacific, City Developments, Fraser and Neave, Noble Group, Olam International, Singapore Airlines, Singapore Airport Terminal Services, Singapore Exchange, Singapore Press, SMRT, ST Engineering, Tiger Airways, United Overseas Bank, United Overseas Land

Sri Lanka: Central Bank of Sri Lanka, John Keells

Taiwan: Giant Manufacturing, Taiwan Semiconductor Manufacturing, Uni-President Enterprises, United Microelectronics

Thailand: BEC World, Bumrungrad Hospital, Hana Microelectronics, Home Product Center, Kasikornbank, Minor International, Prinsiri, PTT Exploration and Production, Serm Suk, Siam Commercial Bank, Tisco Bank, Total Access Communication

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