



Fund Houses Outlook 2011

Executive Summary

Key Macroeconomic Takeaways – Continued recovery is expected for 2011, but the pace of growth is likely to be slower than recent trends.

Asset Class Allocation – Increased risk appetite is observed with majority overweighting equities and underweighting developed market bonds.

Country Allocation – Consensus is towards overweighting Asia Pacific ex Japan and underweighting developed economies.

Sector Allocation – Information Technology and consumers related sectors are the top overweight sectors for 2011.

As you try to identify the economic outlook and investment opportunities for the new year, we conducted a questionnaire with 10 fund houses and share with you their take on 2011.

Key Macroeconomic Takeaways from Fund Houses

The general consensus of various fund houses is that global economic recovery is expected to continue next year, but at a slower pace than recent trends. Henderson Global Investors is “optimistic heading into 2011 that the recovery could progress against expectations” and feels that the recent slowdown seen in economic data is not uncommon as history shows that recovery usually slows in the second year following the recession.

Asia Pacific ex Japan is expected to remain the main driver of growth due to its solid government balance sheets, sustained fund inflows, improved earnings, and rising domestic consumption. Allianz Global Investors expects the much lower Debt/GDP ratio in the region, as compared to developed economies, to allow countries greater ability to implement stimulus programs and policies should any unforeseen shocks arise. In addition, improved earnings and rising domestic consumption are expected to result in robust growth momentum. Most see inflation as the primary concern in the region, and the challenge of governments will be to curb inflation through policy tightening without hindering growth.

The developed nations are likely to experience an extended period of subdued growth as “debt-laden economies are undergoing a long, drawn-out process of deleveraging”, according to Lion Global Investors. Quantitative easing and fiscal stimulus are expected to support liquidity and growth in the near term. However, most feel that fiscal health and sovereign debt financing issues, especially in Europe and UK, will continue to plague economies and limit investors’ confidence.

Moving into 2011, there are a few key risks that investors should keep in mind. Debt crisis in Europe could deteriorate and result in further contagion in Spain and Portugal and even the UK. The tug of war between inflation and tightening policies

The general consensus for 2011 is one of continuing growth but at a slower pace than recent trends.

Asia Pacific ex Japan is expected to remain the primary driver of growth.

Developed nations are likely to experience extended periods of sub-par growth..

Potential risks remain in 2011.



in Asia could pose downside risks to economies if policy tightening is inadequate or too much. It is also possible that a deflationary economy in the developed nations would occur and affect emerging economies negatively. Lastly, escalation of political tension between North and South Korea could further add on to the uncertainty of outlook.

Asset Class Allocation

Table 1: Asset Class Allocation by Fund Houses

Asset Class	Reasons
Equities (Overweight)	<ul style="list-style-type: none"> - Quantitative easing by developed economies supports risky assets - Economic recovery is on track - Corporate sector is in a healthy state to grow and invest - Equities appear to be fair value globally - Possible revival in merger and acquisitions activities - Offers higher yield relative to bonds
Commodities (Overweight)	<ul style="list-style-type: none"> - Growth in India and China likely to increase energy demand - Infrastructure demand supported by emerging economies
Developed Market Bonds (Underweight)	<ul style="list-style-type: none"> - Valuations are expensive - Europe debt crisis likely to persist and limit return - Low yield levels pose risk of sell off in bond markets

Source: Various Fund Houses, as of 22 Dec 2010

The general consensus for asset class allocation is towards overweighting equities and underweighting developed market bonds. Quantitative easing in the developed economies limits the downside potential for equities as the high liquidity and low interest rates environment supports risk appetite and asset prices. Coupled with the healthy corporate sector, potential for earnings growth, attractive valuation and expectations of continued economic recovery, it is no surprise that equity is the top overweight asset class for 2011.

In comparison, developed market bonds appear expensive on a historical basis and is the most underweight asset class. Although low rate is likely to be supported by major central banks in the near term, as Henderson Global Investors expect the first rate rise in the UK to be pushed back into the second half of 2011, many, including DBS Asset Management, expect persisting risk of the Europe debt crisis to impact bond price negatively.

Lastly, commodities are deemed as attractive by First State Investments due to increased risk appetite. In addition, demand from India and China, which are unable to produce enough coal to support their current energy needs, is expected to support coal prices in the next few quarters. Infrastructure development among

Equities generally favored as risk appetite increases due to liquidity and attractive fundamentals.

Developed market bonds appears expensive and can be negatively impacted by Europe debt crisis.

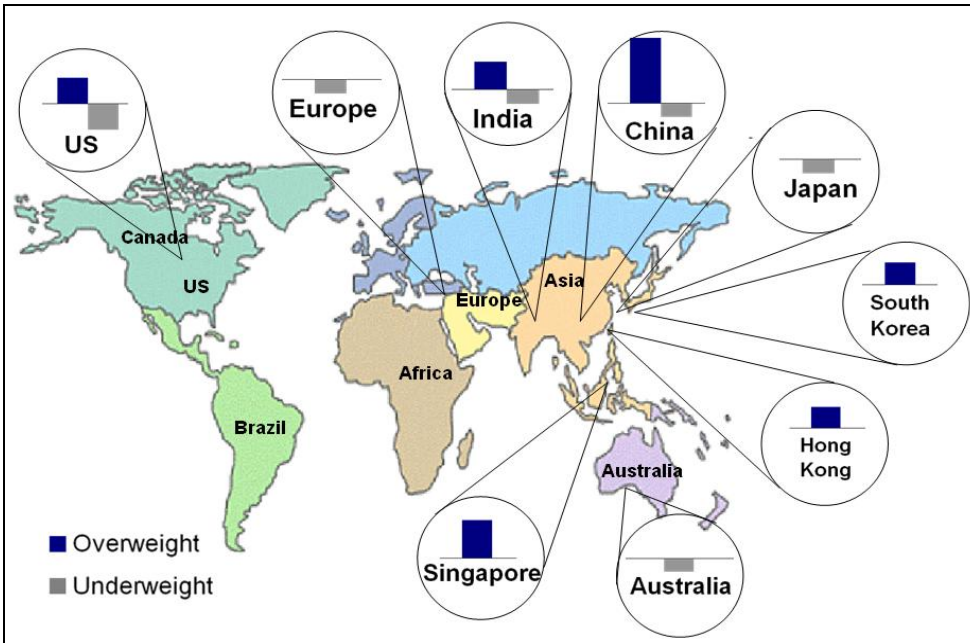
Commodities are likely to gain on the back of increasing demand from emerging economies.



emerging economies should also create strong demand for commodities. However, it is useful to note that Aberdeen Asset Management is wary of the sustainability of the commodity price cycle.

Country Allocation

Figure 1: Country Allocation by Fund Houses



Consensus is towards overweighting Asia Pacific ex Japan and underweighting developed countries.

Source: UT Research Team and responses from Various Fund Houses, as of 22 Dec 2010

We tallied a summary of the various fund houses' views on country allocation and the consensus is towards overweighting Asia Pacific ex Japan and underweighting mainly developed countries for the reasons mentioned under the "Key Macroeconomic Takeaways from Fund Houses" section.

However, three particular areas for debate lie in China, India and US. Advocates of China argue on its attractive valuation, large growth potential and favorable macro fundamentals, while antagonists of China are fearful of corporate management quality and government's reach in strategic industries.

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As for India, DBS Asset Management feels that the valuations have run ahead of fundamentals. Prudential Asset Management however feels that investors will "continue to attach importance to India's muted sensitivity to the global market despite the valuation premium" and remains positive on the medium-term outlook for India.

Lastly for US, Deutsche Asset Management expects its growth to surprise markets, but Allianz Global Investors remain cautious due to macroeconomic challenges. Fullerton Fund Management Company expects US equities to rally initially, but upside to be capped by structural headwinds eventually.



Sector Allocation

Table 2: Sector Allocation by Fund Houses

Overweight	Underweight
Information Technology	Asian Utilities
Consumer discretionary and staples	Financials
Energy	Industrials

Source: Various Fund Houses, as of 22 Dec 2010

For sector allocation, information technology and consumers related sectors are two popular areas for overweight. Fund Houses overweight the information technology sector due to its healthy balance sheet, strong free cash flow generations and attractive valuation.

As for consumers related sectors, Lion Global Investors and Aberdeen Asset Management expect them to benefit from the growth in emerging markets. Fullerton Fund Management Company however feels that consumers staple stocks are too expensive and are vulnerable to price controls due to recent rising inflation.

Conclusion:

In sum, fund houses are generally positive on the outlook for 2011 and overweight equities and the Asia Pacific ex Japan region. Our (UT Research Team) view is mostly aligned with fund houses' consensus as we have overweight emerging Asia and equities as well. For equities, we are overweight on South East Asia but neutral on China due to their overhanging policy and inflation risks. As for fixed income, we overweight corporate and Asia bonds and underweight Europe bonds. For more details, please refer to our "Investment Outlook 2011" report.

Brought to you by UT Research Team

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* We would like to give special thanks to respondents for our questionnaire and their valuable opinions.



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3 Jan 2011

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