



The Standard Chartered
Private Bank

1Q09 Outlook Recovery In Waiting



- 1Q09 is likely to see more turbulence in the markets for “risky assets”
- Expect more bad news surrounding financial institutions and economies
- But credit and money market indicators suggest that the financial crisis may have already peaked
- Equities – which appear technically oversold – could stage a cyclical rebound later this year despite the structural economic problems
- Typically, US equity bear markets trough 3-5 months before the end of US recessions – we expect the US recession to end sometime middle of this year
- But the necessary workouts of the housing, credit and consumer bubbles will take time and are likely to limit the gains from any cyclical stock market rebound
- Commodities have been sold back to the levels of 4-5 years ago and could rebound on a return of risk appetite and an end to the global recession
- Investment grade debt spreads could remain high in the midst of capital scarcity – avoid high yielders as default rates are likely to soar
- USD and Yen are likely to remain supported in 1Q09 on continued financial market jitters, de-leveraging and risk aversion
- But the USD should weaken as risk appetite recovers
- Gold could correct further near-term on USD resilience but is likely to rally when the USD starts to weaken later in the year

Summary

This will be another “ugly” quarter for risk assets.

2009 is likely to be another difficult year for asset markets around the world. The early part of the year will see continued volatility, with renewed downside risks for equities. Stocks are likely to retest 2008 lows as: 1) the full extent of the damage inflicted by the credit crisis on financial institutions becomes more apparent; 2) a sharp downturn in cash-flow exposes corporate malfeasance; 3) incoming data reveals the depth of the recessions in the developed economies; 4) emerging market economies grapple with possibly sharper than previously expected slowdowns; and 5) the problems of Wall Street spill over to non-financial sector companies. There is a danger of equities even breaking the prior lows registered in 4Q08. Commodities – already severely oversold – could remain under pressure as risk aversion continues to dominate. Meanwhile on the currency front, continued risk aversion and de-leveraging are likely to support US Dollar and Yen strength in the early months of the year.

But the financial crisis may have peaked. If 2008 will be remembered as the year of financial crisis, 2009 is likely to play out as the year of the global recession. They are both painful adjustment processes that the markets have to work through. But even in the midst of renewed volatility early in the year on continued bad news from financial institutions and the economy, key money market indicators such as the TED spread and the Libor-OIS spread have remained stable at the recent lows. Easing spreads in the credit and money markets suggest the financial crisis may have peaked. But the financial sector around the world remains fragile and we do not rule out periodic rises in these spreads through the course of the year. However, the dominant theme for 2009 is likely to be volatility rather than the extreme risk aversion that characterized the period after the collapse of Lehman Brothers. The later part of 2009 could see a more sustainable return of risk appetites and more “normality” to markets.

Developed economies likely to remain in recession to the middle or late 2009.

The widely publicized financial distress of US automakers highlights the spilling over of the problems of Wall Street into “Main Street”. A new wave of debt defaults is likely to emerge in 2009 – this time from non-financial sector corporations. US commer-

cial and industrial loan delinquencies are likely to surge from the recent lows of 1-2%, possibly to above the 6-7% level recorded at the last cyclical peak – during the Savings & Loans (S&L) Crisis of the late 1980s/early 1990s. Amidst the turmoil in the financial system, the economies of the United States, Euro zone and Japan are likely to contract further through the first half of the year. The UK is likely to suffer a longer recession than the US and the Euro zone.

Emerging market economies will suffer sharp slow-downs but should generally rebound faster. While the emerging market economies are generally stronger than those of the developed world, growth rates have slowed dramatically and will ease further in 1H09. Emerging Asia's direct exports to the US may have declined over the past decade. However, with indirect exports, most Asia ex-Japan economies actually increased their trade exposures, as a percentage of their respective GDP, to the US and Euro zone. The globalization of trade has intensified inter-dependencies. And over the course of the bull market, there had been tremendous growth in net flows into emerging market equity funds and emerging market debt. That means instant financial contagion during bouts of risk aversion, de-leveraging and liquidation. The above means that emerging market economies' fortunes remain tied to the global business cycle. And their asset markets have indeed been damaged even more than their economies given the indiscriminate liquidation of risk assets during bouts of financial market fear.

The most trade-exposed economies of Asia ex-Japan are likely suffer recessions but regional governments generally have more policy ammunition than those in the developed world. The most trade exposed economies of Singapore, Hong Kong, Taiwan and Korea are either already in recession or are likely to officially register one in coming months. Nevertheless, Asia ex-Japan generally has more fiscal and monetary policy ammunition at its disposal to deal with the crisis than other regions. Emerging Europe's dependency on external financing has left its economies and financial institutions more exposed to stress and crisis.

Latam – along with Asia ex-Japan – should rebound more sharply than the developed economies. While Latin America is in a far better shape than the economies

of emerging Europe, sharply lower commodity prices and relatively high inflation have complicated the task of economic management. Generally however, Latin America and those Asia ex-Japan economies with larger domestic demand bases are likely to avoid recession and they should rebound faster than the developed world.

But high expectations of China could disappoint markets. A note of caution: the markets' high expectations of China's and India's supposed resilience leave them exposed to the risk of disappointment in the event of sharper than expected slowdowns in these two countries. The media will focus intense scrutiny on these two economies – in particular China – in coming months for every little sign of fragility.

Peaks of pessimism often coincide with points of greatest opportunities. The outlook is not all gloomy. Along with the uncertainties, there are likely to be investment opportunities. Indeed, peaks of pessimism are often also points of greatest opportunity.

Financial markets have possibly seen the highest level of fear second only to the Great Depression. A range of market signals suggest that we are probably at a level of pessimism second only to the Great Depression. The S&P 500 equities volatility index VIX at its recent peak was nearly double anything seen in its 18-year history. Similarly, the TED spread, which measures the risk premiums over US Treasury yields for uncollateralized lending in money markets, was also nearly double the levels seen during the height of the S&L crisis of the late 1980s. In credit markets, spreads have surged way above the peaks of the late 1980s and in many cases, are at their highest levels since the Great Depression. Meanwhile, the 10-year US Treasury yield is now at its lowest since 1955. The yield on 2-year US Treasury bills had fallen to a record low.

Equities – cyclical rebounds are possible amidst structural woes. Equities have already priced in a lot of bad news. They are technically oversold and could rebound in the latter part of the year. US mutual fund redemptions have exceeded the levels at the 2002 bottom of the last bear market. Indeed, the Dow Jones Industrial Average had lost more in the first 12 months of this bear market than in any other bear market since – and includ-

ing – the Great Depression. From their 2007 peaks to recent troughs, the S&P500 had fallen 52% and the MSCI Emerging Market Index 66%, with some markets down by around 70%.

While we expect a retest of 2008 lows and cannot rule out further downside in equities beyond that on another surge in risk aversion, valuations have already come down very substantially from their 2007 peaks. Asia ex-Japan markets are now trading around their book value – with the Hang Seng at 1.3x, Singapore's FTSTI on par with book value, and Korea's KOSPI at a 16% discount to book. Trailing price to earnings (PE) ratios have fallen into single digits in many emerging markets. And it is worth noting that bear markets typically end 3 to 5 months before the end of recessions. Eventually, the global recession will end. For the world's largest economies, we expect this to happen sometime middle to late 2009.

But structural economic overhangs will limit the gains. There are many structural overhangs, particularly in the developed economies, which are likely to limit any rebound in global equities. That is, we are unlikely to see equities make new highs or indeed even retest the prior (late 2007) highs. The US housing, credit and consumer bubbles have built up over a decade and will take time to work through. Meanwhile, there are housing bubbles in many other developed economies – for e.g. UK, Spain and Ireland – that have to be worked through as well. And the credit crisis has engulfed the financial sectors of Europe and UK as well.

Commodities – a lot of froth has been removed and prices should recover with risk appetites. For commodities, the overshoot of prices on financial flows has reversed savagely into what looks like an “undershoot” on de-leveraging, flight for safety, and Dollar strength. Here again, an easing of risk aversion and the end of the global recession should see the return of funds and higher prices. Although we expect generally firmer prices across the commodities complex in 2009, the first half of the year could be more volatile as markets search for signals of an end to the global recession. But generally, for commodities as for equities, the flipside of the current risk aversion could be opportunities as financial panic eases. A range of commodities, from base metals to oil, have seen massive price declines recently. The prices of many base metals

have given back almost all the gains of the past four to five years. Oil prices have gone back to the levels of 2004. And while gold could correct again on renewed financial market jitters and USD strength in 1Q09, the longer-term outlook is positive against a likely renewed downturn in the USD later in the year.

Bonds – avoid high yielders and stick to quality. US Treasuries are likely to remain well supported in the early months of the year as financial market jitters continue. But with the 2-year yield having hit unprecedented lows and the 10-year yield back to the mid-1950s, US Treasuries should be treated as portfolio hedges rather than tactical trades. With interest rates on the way down, high quality Emerging Market sovereigns are worthy of consideration. But to be clear, 2009 will remain a year of capital scarcity as banks de-leverage and financial institutions seek to raise funds to repair their balance sheets. Commercial and industrial borrowers will find it difficult to refinance their loans and spreads are likely to remain high. So, even those in investment grade corporate bonds have to be patient. Against the backdrop of an almost certain surge in the default rate, we would avoid high yielders.

Currencies – USD resilience amidst risk aversion should give way eventually to weakness when capital flight ends. The US dollar and the Yen, which have been strengthening on risk aversion, a flight to safety and de-leveraging are likely to correct on an easing of the fear gripping financial markets. Even if the USD remains resilient in the early months of the year on continued risk aversion, the eventual return of risk appetites should see renewed USD weakness. Certainly, the US Federal Reserve's aggressive “quantitative easing” – a euphemism for “printing money” – is likely to impose a price on the USD longer-term.

1Q09 tactical asset allocation summary

Asset class	3-month (4Q08)	12-month (4Q08)
Cash	Overweight (Overweight)	Neutral (Neutral)
Equities	Underweight (Underweight)	Neutral (Neutral)
Bonds	Neutral (Neutral)	Neutral (Neutral)
Alternatives	Underweight (Neutral)	Neutral (Neutral)

Global Economic Outlook

The US recession is likely to be long and deep but some improvement should be coming through by the second half of 2009. US recessions since the Second World War have typically lasted 10-11 months but recessions preceded by banking crises have historically lasted twice as long. 4Q08 real GDP growth was likely to have crashed around 7% pa as households and businesses cut spending following the Lehman collapse and the subsequent equities meltdown. The US recession, officially dated as starting in December 2007, will probably continue through to middle of 2009.


Aggressive policy responses. The public policy response has been dramatically stepped up around the world – led by the United States in the West and China in the East. The Fed has cut rates close to zero and aggressively expanded its balance sheet through so-called quantitative easing measures designed to boost bank lending and to ensure market rates stay low. The Obama Administration will also hit the ground running as it takes over and will quickly implement more fiscal stimulus measures. Meanwhile, China has announced a fiscal stimulus package equivalent to around 16% of its GDP, with the possibility of more to come.

Meanwhile, economies will adjust – painfully. The necessary private sector adjustment is happening. In the US, falling house prices and rising unemployment – clear trends over the past 2-3 years that have gained momentum over the past 12 months – will force household de-leveraging. And while US real GDP growth should be positive again in the second half of this year, the recovery will be sluggish. The “work out” of the housing, consumer and credit bubbles – not just in the US but in many developed economies – will restrain consumer confidence well into 2010. Meanwhile, the equities, credit and commodities markets have also adjusted – very sharply – in some cases feeding back into the economy through the wealth effect and shocks to consumer confidence.

Japan is likely to suffer less of a shock than the US but its recovery will be sluggish. Japan’s recession will deepen into 2009 as the global financial crisis hits exports, industrial output, and investment. But Japan’s banks have relatively low exposures to the global credit crisis. Meanwhile, the property market there – having deflated from the early 1990s – had hardly picked up before the crisis hit. And private sector debt levels have come down dramatically over the past 1-2 decades. Companies today carry much lower debt-to-equity ratios. So there are not the same structural problems of housing, credit and consumer bubbles as in the US and UK. Japan has a business cycle problem flowing from its dependence on exports for growth. Unfortunately, its government suffers a high fiscal deficit and debt relative to GDP. And the Bank of Japan’s policy rates were at 0.5% even before the economic crisis started. All of these leave little room for policy manoeuvre. Although Japan will probably not suffer as deep a recession as the US, its recovery is likely to be lacklustre.

The Euro zone is not going to do all that much better than the US. The financial crisis and global recession have hit the Euro zone hard, via tighter lending standards and weaker exports. There are wide differences within the Euro zone. Household debt levels are relatively modest in Germany, France, and in Italy. And they do not have to deal with burst housing bubbles ala US and UK. But some of the other Euro zone economies however, most notably Portugal, Ireland, Greece and Spain, face their own structural adjustments. They too have their own housing slumps to work through. They are likely to suffer continued economic pressures through to 2010. Netting out the pluses and the minuses, the Euro zone is still likely to go through a difficult recession. We are expecting a full year contraction of 2% for the Euro zone economy against 2.6% for the US.

UK recession is likely to be even more severe than the Euro zone. The UK looks set to suffer a long and deep recession, similar to the US. The now aggressive UK



policy response should avert an even worse outcome but the combination of a housing slump, an over-sized banking sector that has to retrench, and high household debt levels, could prolong the recession into 2010

The slowdowns in Asia and the Emerging Market economies will be severe but many will avoid recessions and the recoveries should be more robust than the US and Europe. Confidence plunged in the final months of 2008 and exports and industrial output crashed as new orders from the US and Europe dried up and the credit crisis squeezed trade finance. But inflation has collapsed as well and all the big countries are now aggressively cutting interest rates, have improved financial sector liquidity, and have implemented major fiscal stimulus programmes to help revive economic growth. Further, the key countries still retain the policy ammunition to do more, if necessary, whilst international supports for the most vulnerable (from the Fed, friendly governments, the IMF) have also come through. We expect the economic slowdowns to last for a couple more quarters but only those countries heavily dependent on external trade should suffer recessions. China, India, most of Asia, as well as the Middle East and Latin America, should be on a recovery path in the second half of 2009. Emerging Europe will take longer to recover given its high dependence on external financing and the weakness in its financial sector. But elsewhere there is scope for domestic demand to provide support. Banking systems are generally sound and there is no need for countries to suffer the household and financial sector de-leveraging that will hold back the high-income economies.

But the outlook risks are to the downside. Central banks and governments are now aggressively responding to the global recession but it is difficult to predict how effective all the stimulus measures will be and when they will start to revive economic activity. We are cautious on the economic outlook and on recovery in the banking and credit markets. Although on balance we expect modest recoveries in 2009, we cannot rule out risks of a prolonged period of economic contraction if financial markets remain “broken” despite the policy measures already underway.

Equities

3M: Underweight

12M: Neutral

Cyclical rallies are possible amidst structural problems. Equities are likely to put in a cyclical bottom in 2009 but not before continued high volatility particularly in the earlier part of the year.

This is a year that will pit: 1) deflation against government intervention; 2) negative news flow against massive discounting of that bad news; 3) secular versus cyclical factors.

The economic and financial market overhang from the bursting of three simultaneous bubbles – housing, credit and equities – will take years to resolve. However, the sharp decline in share prices against a backdrop of aggressive government fiscal and monetary intervention all over the world has possibly set the scene for a powerful cyclical rally.

Deflation versus government intervention: Global economy under assault on multiple fronts. US consumers are tightening their wallets under the pressure of two years of falling house prices. Simultaneously, a catastrophic drop in the value of credit derivatives is forcing banks around the world to write off assets and deleverage.

And while the US is the epicenter of the ongoing economic and financial market turmoil, similar housing, consumer and credit bubbles have burst in the UK, many parts of Europe, Australia and New Zealand.

Synchronised recessions. The US, Euro zone and Japan are in synchronized recessions. Economies with large exposures to the international trade and finance cycle such as Singapore, Hong Kong, Taiwan and Korea have either followed into or are on the brink of recessions. Meanwhile, developing economies – including China – are now suffering sharper than previously expected slowdowns. Inflation is rapidly easing, under the weight of falling oil/commodity prices, declining house prices/rentals

and diminishing spending power. Deflation is now looming as a threat.

Aggressive government intervention all over the world – monetary, fiscal and “unconventional” measures. Against the backdrop of recession, governments all over the world are aggressively “reflating” their economies with fiscal, monetary and “unconventional” measures. The US government in particular has escalated its interventions from interest rate cuts to the provision of liquidity to financial institutions through the Federal Reserve and the nationalization of troubled financial institutions. The Fed has also been buying credit market assets including mortgage-backed securities and commercial paper. In the process, it expanded Fed bank credit 151%, from \$892 billion to \$2,241 billion over the course of 2008. And with policy rates now close to zero, the Fed is pushing aggressively into “quantitative easing”, which means flooding the banking system with reserves. (Exhibit 1)

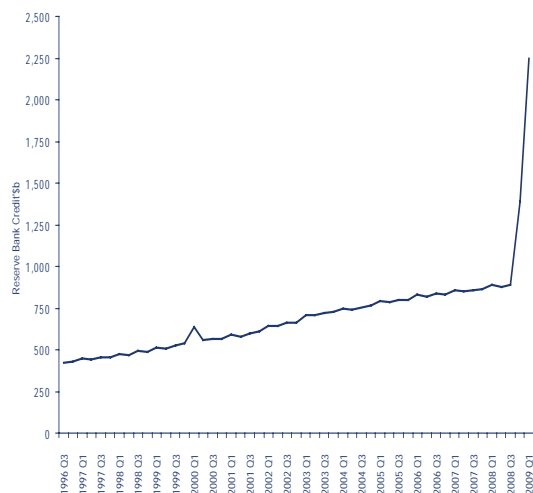
Meanwhile, China has announced a CNY4 trillion (approximately \$600 billion) fiscal stimulus package, with the possibility of more to come early in 2009 if the Chinese economy slows more sharply than expected. This is approximately 16% of the Chinese GDP – fiscal stimulus on a grand scale and comparable to President Franklin De-lano Roosevelt’s “New Deal” during the Great Depression.

While considerably more modest, governments elsewhere in the world have also been engaging in fiscal stimulus. And central banks have been following the lead of the US Fed in cutting rates aggressively.

If government intervention prevails over the threat of deflation – as we expect it should eventually – the global economy will avoid a “depression”, or a multi-year recession. The US economy should bottom sometime middle of 2009, with equities hitting a cyclical bottom some months before that.

Much of the bad news may already be in the price: This first year of this bear market has been worse than even the Great Depression. Clearly, the news flow in coming months on both the economic and financial fronts will be awful. But global markets have on average fallen by nearly 50% from their 2007 peaks to the 2008 troughs, with some markets registering declines of approximately 70%. The Dow Jones Industrial Average

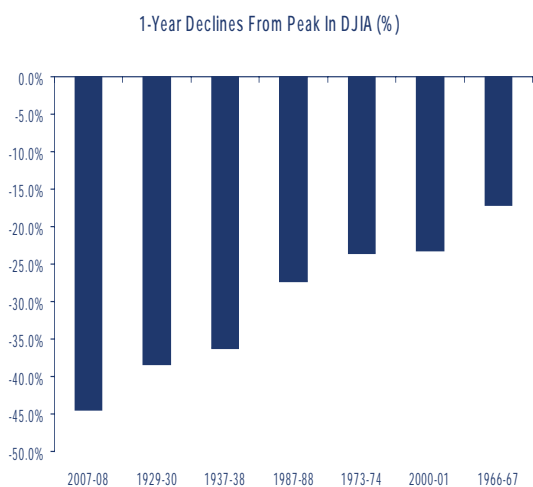
Exhibit 1: US government “money machines” hard at work



Source: US Federal Reserve

(DJIA) declined more in the first 12 months of this bear market than in any other bear market since and including the Great Depression. (Exhibit 2)

Exhibit 2: First year of this bear market worse than the Great Depression



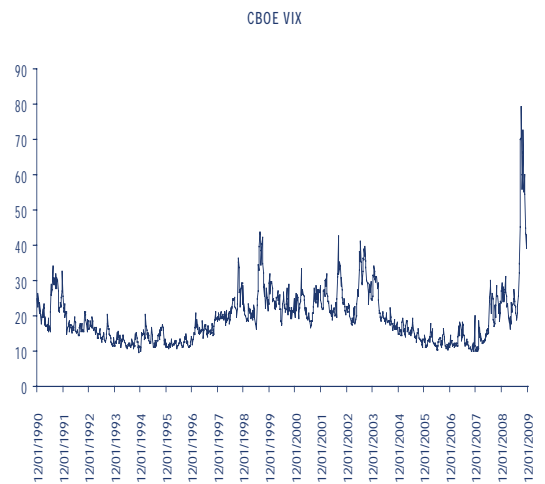
Source: Bloomberg



Equities volatility and money market/credit spreads have hit multi-decade highs and are tentatively easing. Financial market panic is at multi-decade highs, with the TED spread at its recent high almost double the level at the peak of the Savings & Loans crisis in the late 1980s. Similarly, the equities volatility index, VIX, at its recent high, was also nearly double the highs recorded over the past 18 years.

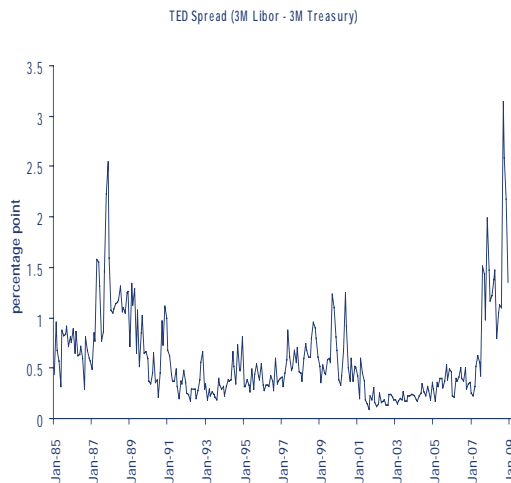
Corporate bond spreads have reached multi-decade highs, pricing in levels of debt default not seen since the Great Depression; the yield on the 10-year US Treasury has fallen to lows not seen since the mid-1950s; and the yield on the 2-year Treasury bill has hit a record low. Meanwhile, the credit default swap spreads on a range of financials have eased sharply from the extreme peaks following the collapse of Lehman Brothers – a sign that the financial panic that had been a constant feature of 2H08 may have peaked. (Exhibits 3-6)

Exhibit 4: CBOE VIX has hit record high



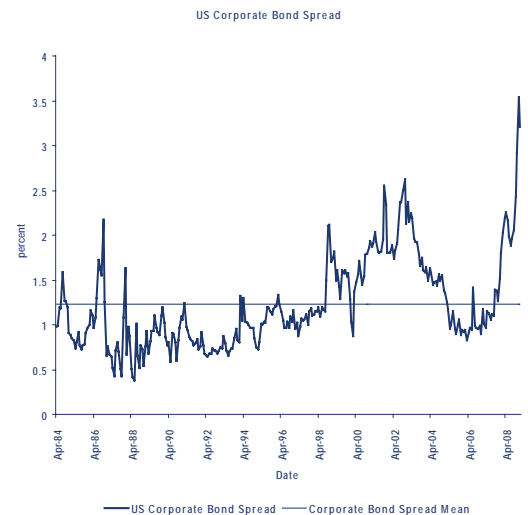
Source: Bloomberg

Exhibit 3: TED spread vastly exceeded peak in late 1980s



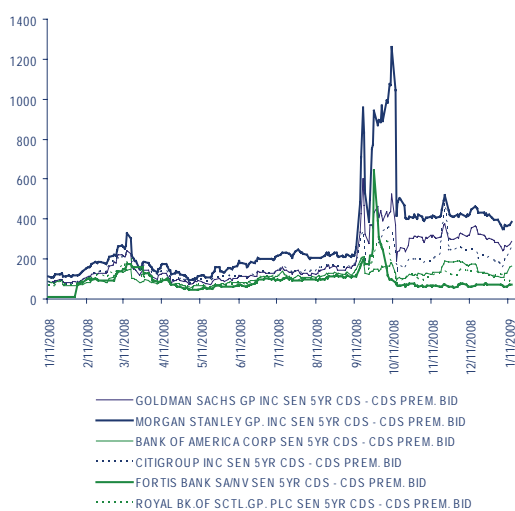
Source: Bloomberg

Exhibit 5: Corporate spreads at multi-decade highs



Source: Datastream

Exhibit 6: Credit default swap spreads for financials are easing



Source: Datastream

The downside risk is a protracted recession – a “depression”. The credit and equities markets – led to some extent by recent economic indicators – have priced in a severe recession and more financial distress in 2009.

The downside risk which may not have been fully factored into prices is the possibility of this ending up a protracted recession – something akin to a “depression”.

Valuations have gone past cyclical lows but not anywhere near the lows of the secular bear markets of the Great Depression or the late 1970s/early 80s. Valuations have yet to hit the lows of the Great Depression and the stagflation bear market of the late 1970s-early 1980s. In those two episodes, the trailing price to earnings (PE) ratio for US equities went into single digits of between 6 to 8 times. The equivalent ratio is currently still around 18x historic earnings – leaving a frightening valuation gap yet to be closed if this is as bad as those two bear markets. But valuations on both PE and price to book measures have gone significantly below the lows of the last cyclical bottom in 2001.

Why this is neither a New Great Depression nor a stagflationary bear market. Two factors argue against a drastic “compression” of valuation multiples similar to the 1930s and 1970s/1980s. The gold standard for the USD and many other developed world currencies during the Great Depression prevented stimulatory government policies. And in the late 1970s/early 1980s, Vietnam War and oil shock-induced inflation forced the US Fed into policy rates of over 20%.

Quantitative easing today versus the deflationary impact of the gold standard during the Great Depression. During the Great Depression, the US and many other developed economies linked their currencies to a gold standard. This resulted in monetary tightening in economies that had insufficient gold. Governments ended up with deflationary policies during the downturn as they raised interest rates to defend their currencies against demands for gold. However, this time, the Fed has no such restriction and is effectively “printing money” through so-called “quantitative easing”.

Fed funds rates now at the zero boundary while they were punitively high in the late 1970s/early 1980s. The single digit PE ratio recorded during the late 1970s/early 1980s, was set against the backdrop of Fed funds rates surging to a peak of around 20%. This is important as interest rates provide the discount factor for valuations. OPEC-imposed oil price shocks and the flight of capital away from a weakened USD were important contributors to the problems of the period. This time, oil prices have slumped along with the global recession, the Fed funds rate has been cut to nearly zero, and there has been a flight of capital into US Treasuries.

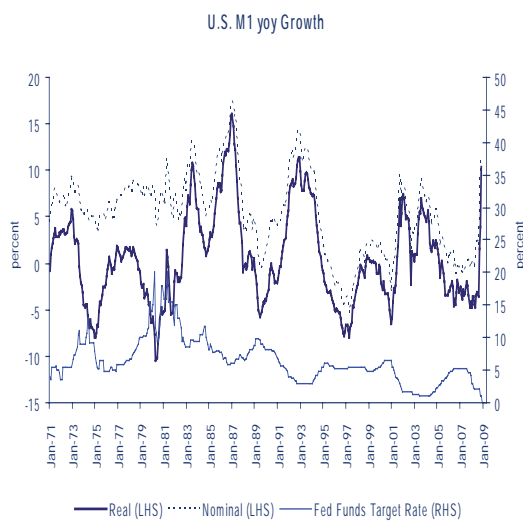
Secular versus cyclical factors: Long-term structural economic problems in the US will overhang global equities markets. We do not underestimate the economic challenges ahead for the global economy, particularly the US. The housing bubble and the resultant sub-prime mortgage crisis are arguably the final denouement of massive consumer and credit booms that accelerated from the mid-1990s.

Bank credit and consumer credit as percentages of GDP surged from the mid-1990s. Running in tandem, the capitalization of the US stock market as a percentage of GDP also accelerated from the mid-1990s and finally house prices took off in the early part of this decade. The problems that developed over a decade will take more than a few months to stabilize.

Notwithstanding the structural economic problems that have yet to be worked through – and hence likely to overhang equities in coming years – there are market signals that a cyclical rally in stocks could unfold in 2009 even amidst the secular or long-term de-leveraging necessary to restore equilibrium.

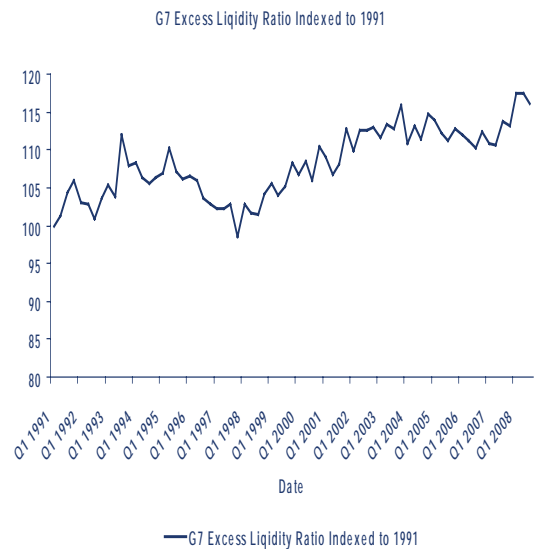
But the acute stage of the crisis appears to be passing. The financial market crisis appears to be easing. As a result of policy actions, money market spreads and credit default swap spreads for financials have dropped sharply. M1 money supply growth in the US has accelerated upwards in recent months. Similarly, money supply in the G7 has been growing faster than their sluggish economies. When banks start to lend again, stock markets could revive in response. (Exhibits 7, 8)

Exhibit 7: Money supply growth surges



Source: Bloomberg

Exhibit 8: G7 money supply growth starts exceeding economic growth



Source: Datastream

Markets usually rebound ahead of the end of recessions. Significantly, we are expecting the US economy to begin a modest recovery by mid-2009. On average, from (and including) the Great Depression through to the “tech wreck” of the early 2000s, US bear markets end 3.5 months before the end of the underlying recessions. Excluding 2000-2003 – which was aggravated by September 11 and subsequent wars and where the recession ended way before the bear market – the average is 4.8 months. (Exhibit 9)

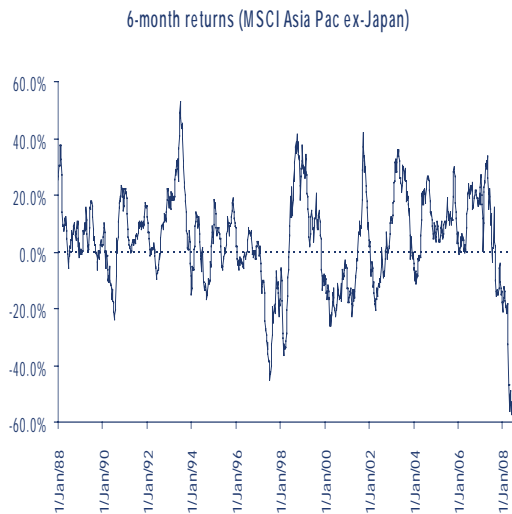
And technically, the markets appear to be oversold. 6-month returns for the MSCI Asia ex-Japan index have fallen past the lows of the Asian Financial Crisis and the 5-year rate of change for the S&P500 is also approaching cyclical lows at which there had previously been tradable rallies. (Exhibits 10, 11)

Exhibit 9: US equities bear markets usually trough ahead of the end of recession

Recession start	Recession end	Bear Market Trough	Lead time (No. of weeks)
Aug-29	Mar-33	7/8/1932	34
May-37	Jun-38	4/1/1938	9
Feb-45	Oct-45	No bear market	NA
Nov-48	Oct-49	6/10/1949	16
Jul-53	May-54	9/18/1953	32
Aug-57	Apr-58	12/20/1957	15
Apr-60	Feb-61	10/21/1960	15
Dec-69	Nov-70	5/22/1970	23
Nov-73	Mar-75	10/4/1974	21
Jan-80	Jul-80	3/28/1980	14
Jul-81	Nov-82	8/6/1982	12
Jul-90	Mar-91	10/12/1990	20
Mar-01	Nov-01	10/4/2002	-48
Mean including 2001			14
Mean excluding 2001			19
Median			15

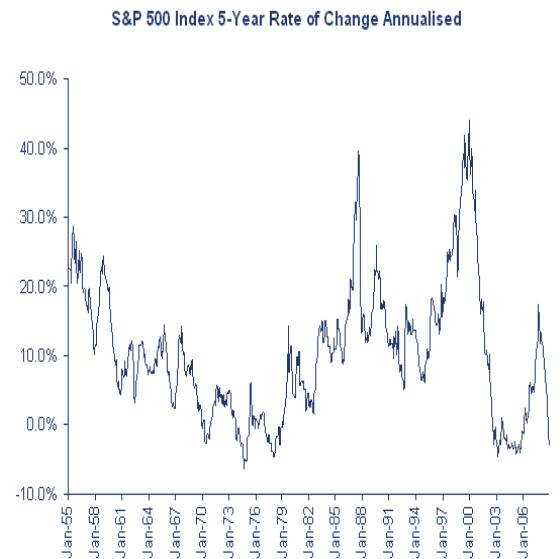
Source: NBER, Bloomberg

Exhibit 10: Asia ex-Japan – at cyclical turning point?



Source: Bloomberg

Exhibit 11: S&P500 – approaching cyclical turning point?



Source: Bloomberg

But this is not going to be a new bull market. Given the structural economic overhangs in the US and other developed economies from the debt binge of past years, it is difficult to see a new bull market unfolding. That is, any cyclical rebound is unlikely to break above the peaks of early 2000 and late 2007.

And a tradable rally is more likely from 2Q than in the early months of the year. Easing spreads in the credit and money markets suggest the financial crisis may have peaked. But the financial sector around the world remains fragile and risk aversion could spike again on another round of bad news surrounding financial institutions.

Spillover of the problems of Wall Street to ‘Main Street’ will keep markets on edge in coming months. Meanwhile, the financial distress of US automakers highlights the spilling over of the problems of Wall Street into ‘Main Street’. We are likely to see the markets focusing in the early months of the year on a new wave of debt defaults – this time from non-financial sector corporations.

Economic contraction likely to deepen in 1H09. Amidst continued turbulence in the financial system, the recessions in the United States, Eurozone, Japan, and the United Kingdom are likely to continue through the first half of the year. And while the emerging market economies are generally stronger than those in the developed world, growth rates have slowed dramatically and will ease further in 1H09.

Underweight equities over 3-months but more optimistic over 12-months. The markets are likely to remain on the edge in the early months of the year as it attempts to figure out whether governments and central banks have got a measure of the massive problems confronting the global economy. Further, there is a danger of more secondary shocks from the financial crisis, with the possibility of more of the sort of scandals that typically emerge when markets slump and liquidity dries up.

Until the markets gain more confidence in the effectiveness of government measures in containing the global recession and financial crisis, there will continue to be a lot of turbulence for equities. In technical terms, this is the “base building” needed for the markets to establish the lows at which buying support kicks in. However, beyond 1Q09, as government intervention gains more traction in both financial markets and economic indicators, equities are likely to rebound.

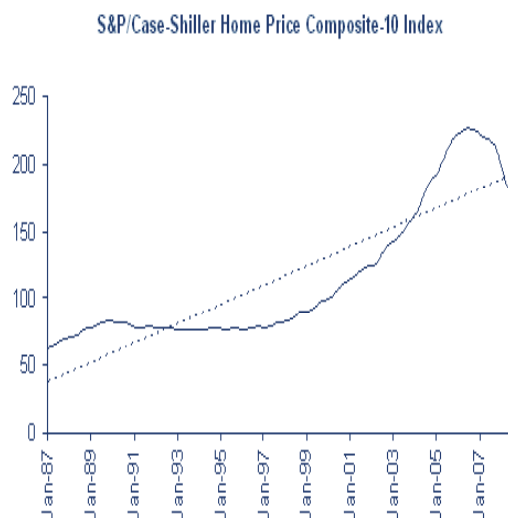
Regional Outlook

North America
3M: Underweight
12M: Underweight

Structural overhangs are likely to limit US stock market performance on the rebound. While there are signals that a cyclical rebound is likely this year for US equities, the upside is likely to be constrained by structural economic concerns. Clearly, what the US is going through is not just a cyclical economic downturn. It is the unwinding of bubbles in property and credit built up over 1-2 decades. (Exhibits 12-14)

The US consumer will be severely constrained by the erosion of household net wealth and growing job insecurity. Notwithstanding the fiscal stimulus promised by the incoming Obama administration, the US consumer is almost certain to be very restrained through 2009 in the face of continued falls in house prices and rising unemployment. Indeed, the process of repairing the household balance sheet is likely to last well beyond 2009. (Exhibit 15)

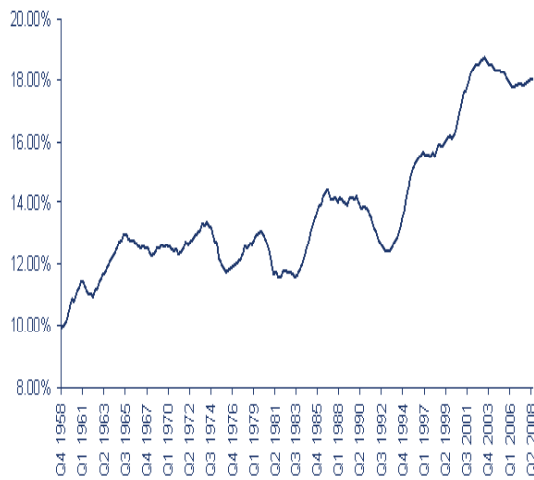
Exhibit 12: Deflating the property bubble



Source: S&P/Case-Schiller

Exhibit 13: Unwinding 15 years of consumer credit expansion

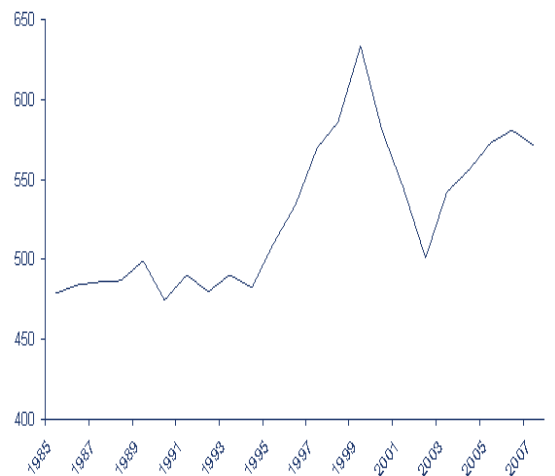
Consumer credit outstanding as percentage of GDP (nominal prices, SA)



Source: Datastream

Exhibit 15: Household net worth will continue to shrink

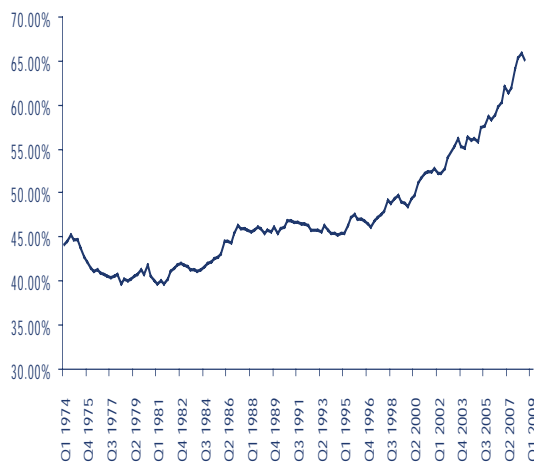
US HOUSEHOLD NET WEALTH RATIO(% DISPOSABLE HOUSEHOLD INCOME)



Source: Datastream

Exhibit 14: Working off the excesses of the credit boom will take time

US Commercial Bank Credit Relative to GDP



Source: Datastream

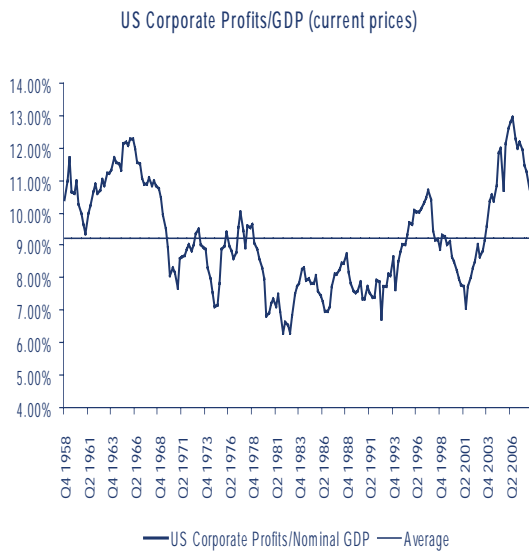
Corporate earnings are likely to shrink sharply.

Meanwhile, corporate profits are shrinking in the midst of the ongoing recession. Profitability – using earnings as a percentage of GDP as a proxy for profit margin – had hit unprecedented levels in recent years and now appears to be mean reverting. (Exhibit 16)

The “cure” is likely to be tomorrow’s “ailment”. The justifiable response of the US government to the current economic and financial problems is to spend its way out of trouble – and in the process, metaphorically run its money “printing presses” at full speed. This has already worked in easing money market spreads down from their recent peaks. And eventually, it should ease spreads and rates across credit and mortgage markets. But in the process, it is likely to worsen the government debt and current account deficit situation in the US. The markets would already be anticipating the future cost of the bailouts and the fiscal and monetary interventions. This is likely to limit its exuberance on the rebound. (Exhibit 17)



Exhibit 16: Profitability has peaked and is declining



Source: Datastream

Valuations are not particularly compelling either.

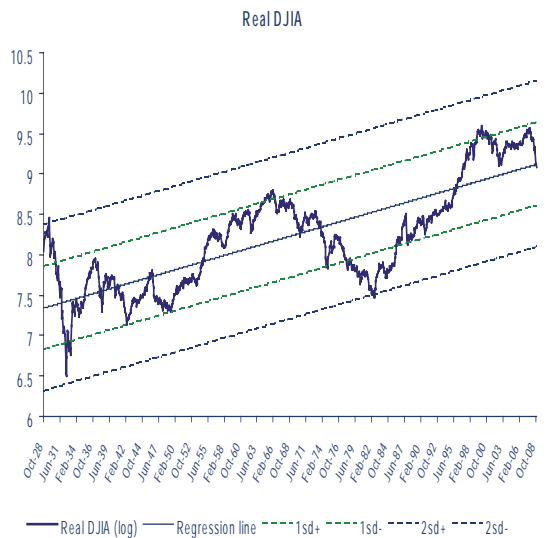
Given all the above structural issues, the valuations for US equities do not look particularly compelling. While it is argued that US equities are cheap relative to recent history, they are not cheap relative to more severe bear markets or even relative to other markets today. They do not appear to offer a sufficient pricing buffer against the uncertainties that will continue to dog the US economy in coming years. At the bottom of the secular bear markets of the 1930s and 1970s, the trailing PE for US equities fell to single digits of between 6 and 8 times. The S&P500, for all the losses recorded since October 2007, is still trading at a trailing PE of 18 times. We do not expect a re-run of the lows of 1930s and 1970s. But this is likely to be the worst recession in the US since the 1970s and a cyclical low PE of 18 times does not appear to have built in sufficient downside protection for worse-than-expected possibilities. (Exhibits 18-20)

Exhibit 17: US Treasury issuance likely to spike



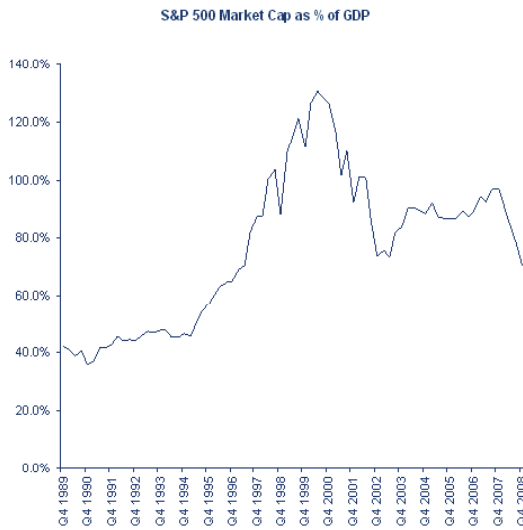
Source: Datastream

Exhibit 18: Dow Jones deflated by CPI - still not "cheap" by secular bear market standards



Source: Bloomberg

Exhibit 19: S&P500 market capitalization as a percentage of GDP has only reverted back to 2001



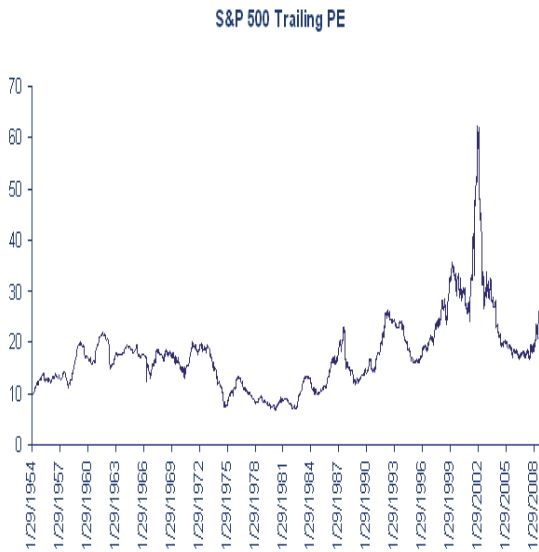
Source: Bloomberg

Europe
3M: Underweight
12M: Neutral

The economic outlook is grim – Germany leads the way down. The difficulties facing Europe’s largest economy, Germany, highlight the downside pressures facing the Euro zone. The year opened with the German government offering a \$66 billion fiscal stimulus package amidst dismal economic data that point to a deepening recession. (Exhibits 21-22)

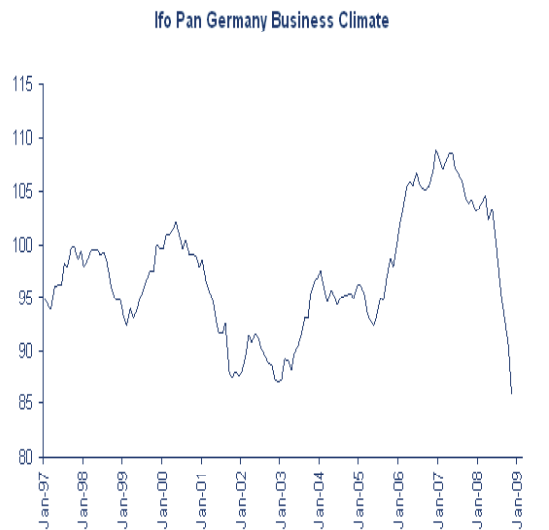
Recession feeds back into consumer spending and exports amidst financial sector de-leveraging. Meanwhile, Euro zone banks face the same de-leveraging and capital raising pressures that will hold down lending in the US and in UK. Unemployment is also likely to rise across the Euro-zone which, combined with all the other outlook uncertainties, will keep consumers and businesses cautious on spending for a prolonged period. The global recession and the lagged impact of a strong Euro have also hurt exports and production.

Exhibit 20: S&P500 trailing PE still in the high teens



Source: Datastream

Exhibit 21: German business confidence plummets



Source: Bloomberg



A more timid fiscal response. In addition, given widely differing government debt burdens and institutional constraints (i.e. the Growth and Stability Pact), the Euro zone is likely to stay more cautious on fiscal stimulus measures to support the economy than the US, UK, and parts of Asia.

But there are fewer structural overhangs to work through in the largest Euro zone economies. Some Euro zone countries, notably Portugal, Ireland, Greece and Spain, have their own property bubbles and household de-leveraging to work through. But the big Euro zone economies do not need to suffer the massive structural de-leveraging that could overhang the US and the UK for possibly years. Household debt in Germany, France, and Italy is relatively low, non-financial sector debt is moderate, and property slumps remain unlikely because house prices did not climb so much in the good years.

Rate cuts to continue. Inflation should continue to fall further and then stay low into 2010. Interest rates have already been cut and although the ECB will likely be less aggressive on the pace of further rate cuts and on quantitative easing than the UK and the US, ECB rates still look set to fall further. We expect them to fall to 1% by 2Q09.

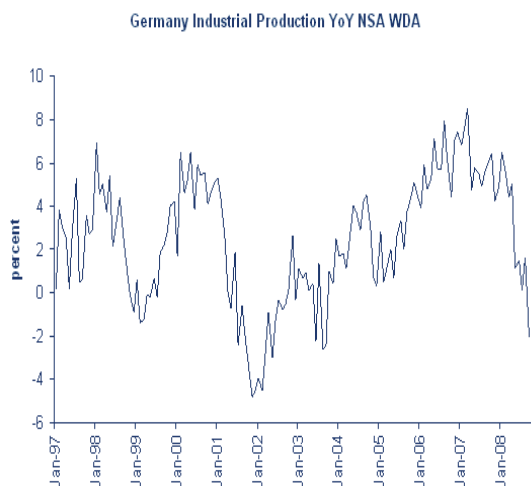
Euro zone valuations have priced in a lot of bad news. More than the US, stocks in the Euro zone have fallen to levels that appear to be pricing in a severe recession. The trailing and forward price to earnings (PE) ratios for the

Dow Jones Euro Stoxx 50 have fallen to 7.5 times and 8.5 times respectively. (Exhibit 23) And the price to book ratio has fallen to around 1.3 times. Compare this against the S&P 500's 18-19 times trailing PE ratio and 11 times forward PE ratio (if you believe the expected earnings side of the equation).

European PE ratios are where US stocks were during the Great Depression. These European equities valuations – which are comparable to where the US stock market's trailing PE ratio had declined to during the Great Depression and the 1970s/early 1980s stagflationary bear market – suggest a great deal of corporate profit stress may have been discounted. Indeed, even in terms of its own history, the average European market trailing PE ratio has already been compressed back to the levels of the late 1970s and early 1980s.

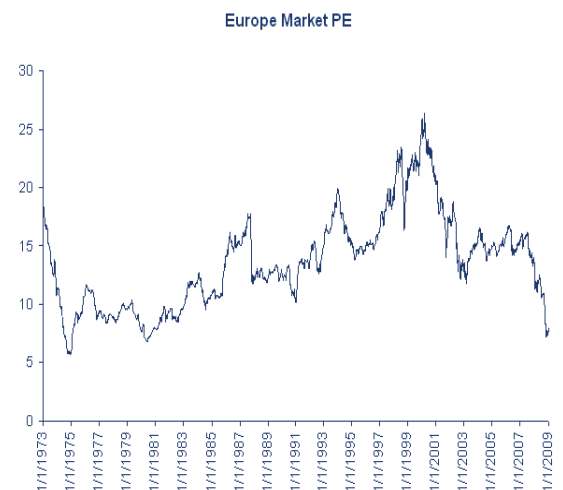
Dividend yields amongst the highest in the world. In addition, the market dividend yield is among the highest in the world at 5-6 per cent. Of course, as elsewhere, there is uncertainty about the security of dividends as the recession squeezes earnings and balance sheets. But dividends for European equities are less biased towards the financial sector than in the US and UK. The major Euro zone dividend payers are in telecoms and the technology sector where debt levels are relatively low, and in the defensive areas such as utilities and consumer staples. The European market dividend yield, as it now stands, is significantly higher than government bond yields.

Exhibit 22: Global economic downturn and lagged impact of a high Euro damages exports and industrial production



Source: Bloomberg

Exhibit 23: Stock valuations in Europe have been compressed further than in the US



Source: Bloomberg

Japan
3M: Underweight
12M: Underweight

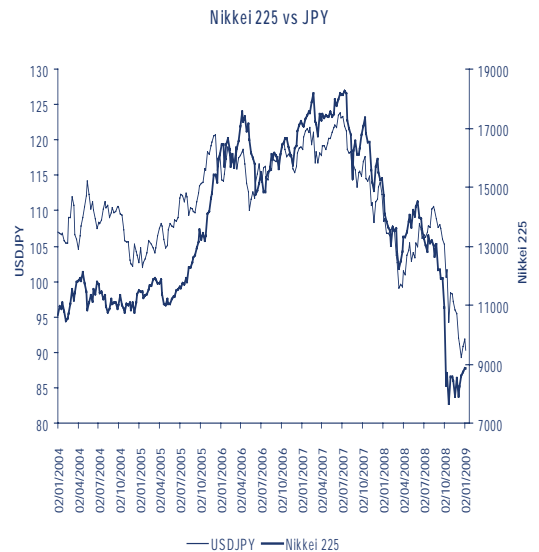
Trading below book value but there is little earnings growth momentum. Notwithstanding the arguments from “Japan bulls” about valuations – the Nikkei 225 is at around 0.9 times book value and the trailing PE is around 10 times– there is little immediate urgency to upgrade our weighting for Japan. The price to book ratio appears to simply reflect a poor earnings and return on equity (ROE) outlook. According to Bloomberg, publicly-listed Japanese companies posted an average ROE of 8.5% for fiscal year 2008-2009 against 18.7% for US companies.

The earnings outlook for 2009 remains grim – export dependence and strong Yen are a toxic mix. Much has been written about the impact of the global recession on Japanese export manufacturers – including Toyota’s much publicised production shutdowns in Japan planned for February and March. But for us, the most eloquent statement of the Japanese economic and corporate earnings dilemma in this crisis remains the overlay of the Nikkei 225 chart against the USD/JPY – and how closely the two charts track one another. (Exhibit 24) The Japanese economy lacks a domestic growth driver, is dependent on external demand and remains hostage to a competitive Yen. With the risk of continued de-leveraging and periodic spikes in volatility, we are unlikely to see any significant weakening of the Yen in 1Q09.

Structural factors continue to overhang Japanese equities. The Japanese government has little monetary and fiscal ammunition to cushion the international downturn. The government is running a fiscal deficit equivalent to around 4% of GDP, it has the highest government debt to

GDP ratio in the OECD, and the Bank of Japan’s policy rate is down to 0.1%. Longer-term, its declining demographics mean continued concerns around taxes, social security, and government fiscal balances. And these in turn have fed back into chronic political instability, with successive Prime Ministers struggling to get on top of these issues. Japan has had four Prime Ministers in two years and Prime Minister Aso Taro, only four months into the job, is also now struggling to retain his popularity.

Exhibit 24: Nikkei 225 versus USD/JPY – a story of export dependency



Source: Bloomberg



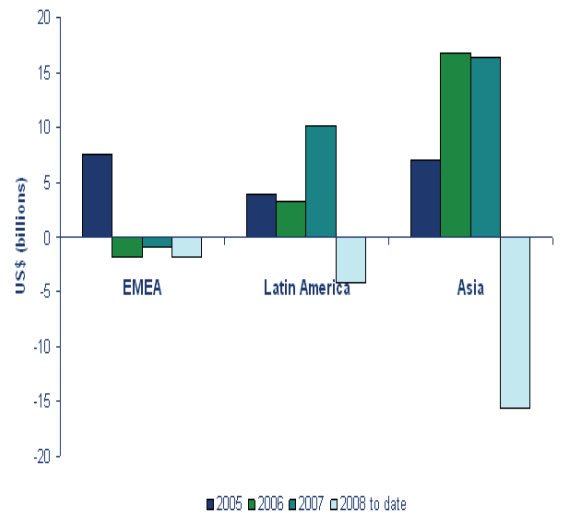
Emerging Markets/Asia ex-Japan
3M: Underweight
12M: Overweight

Emerging market assets require a return of financial market stability to recover. The fortunes of emerging market (EM) assets will continue to be dictated by the ebb and flow of global risk appetites/risk aversion. And here it is important to distinguish between emerging market assets and emerging market economies. In many emerging market economies – particularly in developing Asia – the higher growth base, stronger economic fundamentals and greater policy flexibility have provided some cushion for the economy in the midst of a deep recession in the developed world. But global financial flows have resulted in instant contagion, pushing EM asset prices down more sharply than those in the US – hence the characterisation of Asia ex-Japan as “innocent bystanders” and “collateral damage” amidst credit distress and unwinding of leverage that started amongst developed country financial institutions.

Victims of globalised financial flows. Emerging markets assets that had been beneficiaries of large inflows in recent years have been hit with a reverse of those flows in 2008. The unwinding of leverage and risk positions has been indiscriminate. While Asia ex-Japan may have strong economic fundamentals relative to the developed world and Eastern Europe, this economic advantage has not stopped it from suffering the largest outflows in the EM world. (Exhibit 25) Flows into emerging markets – and asset prices – have a negative correlation to risk aversion and volatility. Spikes in volatility/risk aversion in the developed world have resulted in outflows of funds and drops in asset prices. (Exhibit 26)

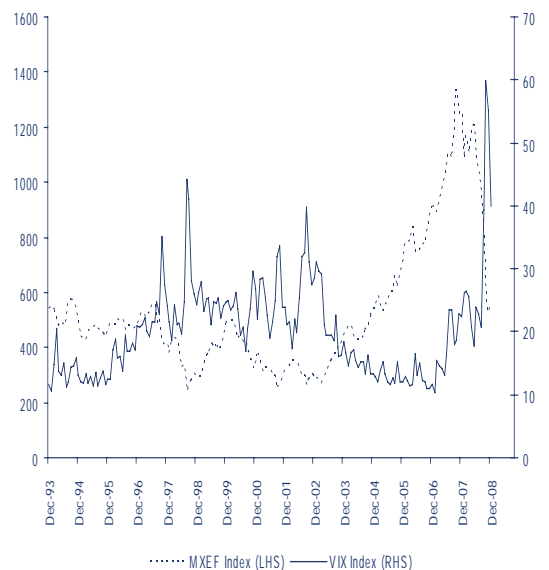
Both economies and asset markets should bounce back faster than those in the developed world. While the developed world is in the midst of adjusting to major structural problems associated with the bursting of housing, credit and consumer bubbles, the EM economies could scrape through with only a cyclical downturn. The EM economies, particularly developing Asia, generally have stronger fundamentals – current account and fiscal surpluses or small deficits; large international reserves; relatively low financial sector leverage; and high household savings. They should rebound faster when the cycle turns. And the higher volatility emerging markets should also enjoy a stronger rebound on an easing in volatility and a return of fund flows into risk assets.

Exhibit 25: Inflows turn into outflows on risk aversion
Net Flows to Emerging Market Equity Funds



Source: IMF

Exhibit 26: Emerging market stock prices versus volatility in the developed world



Source: Bloomberg

Need to be discriminating about emerging markets – favour Asia over Emerging Europe. De-leveraging and capital flight had threatened emerging markets with the possibility of a financial crisis akin to the late 1990s. Economies with large external financing needs have again found themselves threatened with a dangerous downward spiral of falling currencies, rising interest rates, and declining economic activity. Even the relatively sound economies of South Korea and Indonesia have been given scares over their currencies. But there are greater vulnerabilities in emerging Europe which could periodically re-emerge as threats in 2009.

Emerging Europe paying the price for its dependence on external financing. Several eastern European countries have already gone to the International Monetary Fund (IMF) and the European Union (EU) for financial assistance. In recent months, the IMF has given emergency loans to Hungary, Ukraine, Iceland, Belarus and Latvia. Serbia has also asked for IMF help. Emerging Europe faces a dangerous combination of a global recession, large current account deficits, and tight external financing conditions. Some of the Emerging Europe economies have a high dependence on the foreign parents of

subsidiary banks operating in their territories to fund credit expansion. But many of the foreign parents of these banks have their own difficulties either stemming from their own balance sheet problems or in obtaining funds from a tight international wholesale market. Intertwined with that is the risk of a loss of confidence in some emerging European banks. The lack of policy ammunition – as a result of fiscal and current account deficits – will turn into a policy squeeze as the IMF forces fiscal restraint as part of its assistance packages. All this could constraint these economies in any global rebound.

LATAM economic management complicated by inflation and falling commodity prices. Latin America is in better shape than emerging Europe but it generally enjoys less policy flexibility than Asia. On one hand, it suffers relatively high inflation, high interest rates, and current account deficits. Meanwhile, economic growth is slowing as a result of high trade exposure to the US and sharply lower commodity prices. But recovery in commodity prices later this year could offer some respite. And an eventual easing of inflation could give LATAM economies – particularly Brazil and Mexico - room to cut rates in 2009.

Country	Comments	Weighting
China	<p>* The key attractions for Chinese equities are the economy's strong internal and external balances; its high growth base; its demographics; and the massive 70% decline in stock prices (Shanghai Composite Index) from 2007 peak to 2008 trough</p> <p>* The government should be relatively well-positioned to provide fiscal stimulus to the economy, having achieved a budget surplus in 2007, FX reserves equivalent to 45% of GDP and government debt of only around 16%-18% of GDP. * The Central government announced spending of CNY4 trillion (16% of 2007 GDP) November last year, while provincial governments appear to have lined up CNY18 trillion of public spending over 2009-10, (though the source of funding remains unclear and is questionable whether all projects can materialize within the proposed time frame). * Lower corporate profitability, peaking of labor demand (especially in export sectors) suggests lower wage growth and lower domestic demand. The weak housing market will also be a drag on household expenditure. * However, private consumption should not correct sharply as in the developed world given the high savings rate in China. * Other than fiscal pump-priming, monetary policy has been moving towards supporting growth: The PBoC has slashed its benchmark one-year lending rate 216 bps from its September high to 5.31% and has brought reserve requirements for smaller banks down by 400 bps so far. More monetary policy easing may be possible due to easing inflation. * Gradual recovery seen in 2H09, with GDP expected at 7.5% yoy in 2009. * Chinese equities are in an advanced stage of deflating the bubble from 2007. The average trailing PE ratios (for the MSCI China and the H-share Index, respectively) are 9 and 10 times. The forward PE for both indices is around 8 times. These are cheap relative to Chinese equities' valuation history and reasonable relative to current international valuations.</p>	<p>3M: Neutral (Neutral) 12M: Overweight (Overweight)</p>
Hong Kong	<p>* Hong Kong's small, open economy is exposed to the global economic downturn given its dependence on exports and financial services. * Exports fell 5.3% yoy in November, its first decline in 5 months. Exports to Asia, United States and mainland China dropped across the board. * We do not underestimate the threat facing HK. The recession will deepen into 2009 and is likely to last to the end of the year. * The risk is that earnings contracts more sharply than the market consensus of flat growth. * But Hong Kong is well positioned to exploit trade and business opportunities in China, whose domestic demand should hold up better than U.S., Europe and the smaller, open economies in Asia. * Its pro-active government is likely to take nimble steps to mitigate adverse economic effects during this slow growth period, though the HKD peg to USD compromises some policy flexibility. The Government is expected to move into a bigger budget deficit in 2009 on implementation of larger fiscal stimulus (likely to include tax cuts and public spending to cushion slowdown).</p>	<p>3M: Neutral (Neutral) 12M: Neutral (Neutral)</p>
Taiwan	<p>* An export dependent economy with a high proportion of companies reliant on discretionary technology products * The Taiwan stock market is likely to be weighed down as global discretionary consumption slows. * Exports have collapsed (fell 41.9% yoy in December, and contracted 19.5% yoy in 4Q08) on weak external demand. A weakening trend is seen for exports to the US, Euro zone and mainland China. * Business spending could scale back as corporate earnings come under pressure, while consumer spending is likely to fall on weaker wage growth and rising unemployment.* But there are five positives for Taiwan – 1) monetary easing 2) fiscal stimulus 3) very low burden of earnings expectations 4) low valuations and high dividend yields 5) the longer-term China story. * Monetary policy easing is well underway. The central bank slashed its policy rate four times by 25 bps from mid-September to mid-November and followed with aggressive cuts of 75 bps in December and 50 bps in January 09, bringing the policy rate to 1.5%. * Rapidly easing inflation (headline CPI at 1.2% yoy in December) suggests room for more rate cuts (we expect another 50 bps in 1H09). * Government has announced fiscal measures include TWD83 billion (0.64% of GDP) in shopping vouchers in early 2009 and a special budget of TWD400-500 billion in public investment and expenditures for 2009-2012. * The market has built in a reasonable buffer for downside risk in expecting 14% earnings contraction. This is one of the most hard nosed consensus figures in the region. * The forward PE ratio on this sharply lower earnings figure is 12 times and the market's estimated forward dividend yield is still 7% notwithstanding the expected earnings contraction.</p>	<p>3M: Neutral (Neutral) 12M: Overweight (Overweight)</p>

Note: Bracket denotes last quarter's weighting

Country	Comments	Weighting
Korea	<p>* A significant number of South Korean corporations are exposed to global cyclical sectors. Exports account for around 46% percent of GDP, of which about 22% goes to G3 countries. Reflecting the exposure to the global economic environment, industrial production plunged 14.1% yoy and exports fell 18.3% yoy in November.</p> <p>* Besides high foreign currency borrowings by financial institutions, households are also highly leveraged, suggesting that spending will likely be impacted by the credit crunch. Outstanding household credit-to-annual disposable income has risen from nearly 40% in 1996 to 70% in 2007. * SME investment is likely to slow due to de-leveraging and the weak Won * The deteriorating economic outlook and the risk of continued tight USD liquidity conditions could continue to undermine currency and equity market sentiment in 1Q09. * But further improvement in US credit spreads and global liquidity conditions following the aggressive reflation efforts by the Fed and other central banks could provide support for the Won and reverse bearish sentiment on a more sustainable basis later in the year. * Inflationary pressures are abating. Headline CPI inflation peaked at 5.9% yoy in July and has since then moderated to 4.5% yoy in November. * The Government is in aggressive interest rate easing mode, with the benchmark rate down to 2.5% in January from 5.25% in September (100 bps cut in December and 50 bps cut in January). * Notwithstanding the above positives, our bottom line concerns are Korean banks' high foreign currency borrowings, the country's relatively high household leverage, continued tight USD funding conditions, uncomfortably high consensus earnings growth expectations, and consequently unreliable PE valuation ratios.</p>	<p>3M: Underweight (Underweight) 12M: Neutral (Neutral)</p>
India	<p>* The manufacturing sector outlook remains bleak * Export growth has fallen into negative territory. * We have revised down our 2008 forecast to 6.3% and 5% for 2009, from 7% and 6.3% previously * The turmoil in global markets will continue to impact on the availability of funds in 2009 – causing investments to ease. *Investments have been surging as a percentage of GDP over the past decade and have been a major driver of growth. *Risk aversion in the midst of the financial turmoil will limit investments as a driver near-term. *Credit spreads are still wide even after RBI rate cuts, suggesting credit market stress. * But rapidly falling inflation gives room to the RBI to cut rates more aggressively. SCB expects the repo rate to fall to 4% by mid-2009 from 5.5% currently, the reverse repo rate to fall to 3% from 4% currently and the cash reserve ratio to fall to 3.5% from 5% currently. * The announcement of a fiscal package worth INR320 billion (US\$6.5 billion or 0.54% of GDP), and the intention to ensure that the US\$60 billion budget expenditure for the remainder of the year is fully spent, should support growth. *Lower oil prices should help improve external balances, supporting a rebound in INR in 2009. *India's external financing needs – relatively small though they are – could be a cause for some volatility in this risk averse environment. *We would like to see valuations compressed a little more in light of this.</p>	<p>3M: Underweight (Underweight) 12M: Overweight (Overweight)</p>
Indonesia	<p>* Fragile market sentiment could keep the IDR volatile in 1Q09. * Falling commodity prices is a near-term negative for the commodity exporter. Main exports include palm oil, copper, coal and gas, prices of which have fallen substantially in past months. * But US\$6.5 billion fiscal stimulus announced early January and a large domestic market should provide some cushion. * Another positive is that domestic consumption accounts for around 65% of GDP compared to 9% from net exports in 2007. * However, fixed investment is under pressure from credit crunch and economic crisis. * There is a danger of a vicious cycle combining slowing growth, tight international liquidity conditions, a weakened IDR contributing to inflationary pressures, and relatively high interest rates to control inflation and defend the currency. * Upcoming elections should see campaign spending, helping the economy. * Bank Indonesia has moved into an easing cycle, cutting the BI rate by 25 bps in December and another 50 bps early January to 8.75%. Further rate cuts should follow* SCB sees the BI rate reaching 7.0% by end 3Q09. Inflation is near 11% yoy in December, but SCB expects it to fall to 5.5% by end 2009. * But the danger is that lower rates may encourage further weakness in the IDR.</p>	<p>3M: Underweight (Underweight) 12M: Neutral (Neutral)</p>

Note: Bracket denotes last quarter's weighting

Country	Comments	Weighting
Thailand	<p>* Relatively low foreign debt and large foreign exchange reserves have helped insulate the Thai economy and currency from the worst of the global credit crisis. As of September 2008, foreign debt was at US\$67 billion, of which only 37% is short-term debt and the foreign exchange reserve to debt ratio is 140%. * Aggressive monetary policy (100 bps rate cut to 2.75% in December) reflects the focus on growth. * However, the political situation remains fragile. While the anti-Thaksin PAD now leads the ruling coalition, the country's political divisions – between urban and rural, north and south, middle class and poor – remain unresolved and increasingly bitter. *No reconciliation between the opposing forces is imminent and this could continue to limit government effectiveness in 2009. * Meanwhile, exports and manufacturing output are expected to decline further (US, Europe and Japan account for one third of exports), while tourism is likely to slump after the damage to the country's reputation from the year-end closure of Bangkok's international airport. * There is always the possibility of contagion if other emerging market currencies come under assault – such an event will complicate interest rate policies and economic management.</p>	<p>3M: Underweight (Underweight) 12M: Underweight (Underweight)</p>
Malaysia	<p>* Malaysia had enjoyed some buffer from the global credit crisis relative to some other regional markets – as a result of from the low leverage and high savings of its consumers, government and corporations. * Property gains have been relatively modest from 2003. There has been an absence of the negative effects associated with burst property bubbles. * But the economy is still likely to be hit by slowing global growth. It is the third-most open economy in Asia ex-Japan with exports-to-GDP at around 94%. Slower external demand and lower commodity prices (especially lower crude oil and palm oil) will hit the economy in 2009 – it is likely to enter a recession early in the year but rebound in 2H09. * Bank Negara has embarked on preemptive monetary policy easing. It lowered its policy rate in November by 25 bps from 3.5% to 3.25%. Banks' statutory reserve requirements have also been brought down to 3.5% from 4%. SCB expects further policy rate easing, with the rate expected to be cut to 2.5% by the end of 1Q09. * MYR7 billion fiscal stimulus proposed in early November should also help the economy. * SCB expects GDP to stay positive with a 0.5% yoy growth in 2009.</p>	<p>3M: Neutral (Neutral) 12M: Neutral (Neutral)</p>
Singapore	<p>* As a small, open and largely export dependent economy, there is little standing between Singapore and the global recession – it is highly correlated to the global business cycle. * Exports-to-GDP ratio is around 185% while financial sector makes up 12% of GDP. * A sharp drop in exports and industrial production has already been seen in recent months. Manufacturing (around 25% of GDP) contracted 9% yoy in 4Q08 and is expected to remain under pressure from lower external demand. * Government GDP forecast revised down to -2% to 1% range for 2009. * Domestic consumption will take a hit in 2009 as job losses, wage freeze and pay cuts start to set in. * Weaker property market and fall in stock market expected to add to the downward pressure on domestic spending. * Government poised to announce fiscal stimulus (budget due January 22), but the impact may be limited given high trade exposure and low domestic spending in relation to GDP. * SCB forecasts GDP growth at -2.5% in 2009. * Earnings expectations have gone negative but profits could shrink even more sharply than the single digit contraction expected by the market. * Dividend yields – if sustained – are relatively high at over 5%. * A big attraction is that the market is currently trading close to book value.</p>	<p>3M: Neutral (Neutral) 12M: Neutral (Neutral)</p>
Australia	<p>* Household and corporate sector de-leveraging is likely to limit domestic consumption and investment. * Falling commodity prices are sapping the terms-of-trade advantage that had buoyed the economy in recent years. * SCB forecasts GDP to shrink 1.2% in 2009. * Aggressive monetary policy easing will partly offset the drag on growth. So far the policy rate has been slashed by 300 bps. SCB expects the RBA to cut another 125 bps in 1Q09. * Inflation is easing, but likely at a slower rate compared to other economies such as the U.S. and Euro zone due to its weak currency. * Fiscal stimulus of around 0.8% of GDP should have started taking effect in December. Australia's net asset position puts it in a strong position for further fiscal stimulus and infrastructure spending in 2009. The government had indicated that it may even contemplate deficit spending to help the Australian economy avert recession. * An eventual rebound in commodity prices will take pressure off both the economy and stock market. * But earnings growth expectations are suspiciously high in the midst of contracting global demand, a likely recession in Australia and a deep slump in commodity prices.</p>	<p>3M: Neutral (Neutral) 12M: Neutral (Neutral)</p>

Note: Bracket denotes last quarter's weighting

Country	Comments	Weighting
Saudi Arabia	* GDP growth, traditionally low for the MENA region, will slow to around 2% pa in 2009. * Oil prices have dropped to levels around \$40/bl which, if sustained, would stress the government budget. But prices should be up by end 2009. * Inflation should slow to around 7% this year, from 11% in 2008. * Valuations are not cheap by either world or regional standards, with a PE ratio of around 12x. * A restricted market for outside-MENA investors.	3M: Underweight (Underweight) 12M: Neutral (Neutral)
Kuwait	* GDP growth likely to slow, to around 3% from 4% in 2008. * Oil prices for a time will stay close to levels that stress the budget but should rise later in 2009. * Inflation as elsewhere is now slowing, whilst the government retains the financial resources to support the economy, as well as any major company that gets into trouble. * FX rate is more flexible than elsewhere in the Gulf region. * Valuations remain below the regional average - a PE ratio of 9x, price-to-book of 1.7.	3M: Neutral (Neutral) 12M: Neutral (Neutral)
UAE	* Oil prices should stabilise above Abu Dhabi break-even levels, and rise later in 2009. * The non-oil sector is slowing sharply but government fiscal and liquidity supports should head-off an economic slump. * Dubai property prices are likely to fall further but restrictions on new supply should avert a prolonged slump. * Local banks will be hit by the property downturn and reduced wholesale market funding. * But valuations are broadly in line with global comparables and cheap by regional standards – at a PE ratio of 7x (for the top 40 UAE companies) and a price-to-book of 1.5.	3M: Neutral (Neutral) 12M: Neutral (Neutral)
Brazil	* Economic growth will slow sharply in 2009 but the banking system was strong entering the downturn. * High interest rates (13.75% early January) provide plenty of scope for monetary easing. We forecast that rates will fall from early 2009 as inflation moves lower. * Overall debt levels are sustainable and the FX rate has fallen far. * Lower rates should bolster Brazil's resilience to the global recession. * Valuations are moderate by EM standards – with a PE ratio of 9x. * Commodity prices are expected to rise in 2009 – offering some respite.	3M: Underweight (Underweight) 12M: Neutral (Neutral)
Mexico	* The economy has weakened sharply but remains more resilient than in the past to US recessions. * Inflation has slowed and rates should be falling soon. * Mexico also has more scope to ease fiscal policy to help the economy, if needed, than is the case in Brazil. * The FX rate has fallen far. * Corporate earnings are well-supported by relatively low debt levels and large cash cushions. * Valuations are reasonable at a PE ratio of 10x.	3M: Underweight (Underweight) 12M: Neutral (Neutral)
Argentina	* A severe economic downturn is underway and looks set to continue throughout 2009. * High debt levels and high inflation limit the scope for fiscal and monetary easing, whilst the history of default and government intervention will limit foreign support. * But commodity prices should improve during 2009. * At face value, PE valuations are cheap – at a market PE ratio around 6x - but the risks are high.	3M: Underweight (Underweight) 12M: Underweight (Underweight)
Russia	* Russia suffers from banking sector problems, a large corporate foreign debt exposure, and governance issues. Further, oil prices have dropped to levels which could stress the external balance and the budget. * But the government is providing fiscal and liquidity support and still has the ammunition to do more. * Inflation should fall, and the FX rate has dropped and should drop further. * Recession is likely in 2009, which will bring more corporate stresses. * But expectations have collapsed and the market is expecting 25% earnings contraction – one of the most downbeat consensus in the world today. * And valuations are very low, at a trailing PE ratio of 3x and a forward PE of between 4 and 5x.	3M: Neutral (Neutral) 12M: Overweight (Overweight)
Turkey	* A severe economic slowdown is underway but the economy should stabilise from mid-2009. * Inflation is collapsing and interest rates should continue to fall sharply. * External support is coming through, domestic economic management should remain good, EU accession talks will continue, and political risks are low. * Deficit financing issues should ease if, as we expect, global investor risk appetite improves during the course of 2009. * Valuations are attractive – at a PE ratio of 5x.	3M: Underweight (Underweight) 12M: Neutral (Neutral)
Hungary	* The economy crashed in late 2008, as the gradual correction to earlier foreign debt, inflation, and external deficit blow-outs, was overwhelmed by the global crisis. * Recession is likely in 2009 but inflation has crashed too and more rate cuts are likely. * The IMF is also providing help. * A long workout looks inevitable but, as elsewhere in the region, valuations are (perhaps appropriately) cheap - the PE ratio is 4x.	3M: Underweight (Underweight) 12M: Neutral (Neutral)

Note: Bracket denotes last quarter's weighting



Global Bonds

3M: Neutral

12M: Neutral

Continued risk aversion could support government securities for a bit longer. Government bonds in the US, Europe, and Japan have rallied strongly on safe-haven buying, the fall in headline annual inflation, and as central banks aggressively cut official policy rates. And the rally should continue for at least a few more months. Headline inflation in the high-income countries will likely slow towards zero, or even below zero in some cases, through the course of 2009. The Federal Reserve is likely to keep US rates close to zero into 2010 and official rates in the Europe are likely to move down to 1% or possibly even lower by mid-2009. Further, the recessions will be deep and unemployment should rise sharply. Significant spare capacity will open up, which will take a long time to close. Inflation is likely to stay low for some time after the economy begins to revive, keeping government bonds well-supported.

Government bonds as a hedge rather than a tactical play. US Treasuries have priced in a tremendous amount of fear. The yield on the 2-year US Treasury had hit unprecedented lows recently and the yield on the 10-year had hit lows not seen since the mid-1950s. So while ongoing financial turmoil and the immediate threat of deflation could support prices, the better part of the price move appears to be over. And government bonds will be vulnerable when economic activity revives. Current deflation fears could eventually be replaced by renewed inflation worries given the aggressive quantitative easing in the US – which is simply a euphemism for “printing money”. Investors could also quickly switch to riskier assets, curbing safe-haven inflows. In addition, the weak economic recoveries we expect in the US, Europe, and Japan will mean that the fiscal deficits opened up by recent economic stimulus packages will likely take a long time to move back towards balance or surplus. Finally, debt issuance is set to soar in the US and Europe to cover bank bail-out packages and the fiscal stimulus programmes. When financial markets and economies stabilise, government bond yields in the US and elsewhere are likely move up again, pulling down bond prices and hitting investor returns. Government bonds should remain part of diversified portfolios but as

strategic hedges against bouts of financial turbulence rather than for their trading/tactical value.

Better quality emerging market sovereigns should recover. Foreign currency emerging debt remained under stress in 4Q08 as investors liquidated portfolios to cover redemptions and losses elsewhere. The combination of global recession, crashing commodity prices, and aggressive investor de-leveraging also triggered country-specific crises (mainly in Emerging Europe but also in Ecuador, Argentina, and Pakistan). Emerging debt will only rally when global investor risk appetites improve. But yield spreads have climbed sharply and are probably discounting too pessimistic an outlook for the key borrowers. Credit availability will stay constrained but the key countries have lower foreign debt burdens and better macro-economic management than in the 1990s. In addition, most countries probably retain sufficient financial resources, including foreign exchange reserves, to avoid major problems even if the economic slowdowns last far longer than we expect. Local currency emerging market debt should also rally during the course of 2009 as domestic inflation moves down sharply and central banks cut interest rates further. We also expect Asia and emerging market currencies to eventually rise in 2009 against the US dollar as risk appetite improves. But as with emerging market equities, investors should be discriminating and stick to the higher quality sovereigns.

The improvement in the corporate debt market is likely to be slow. Default rates are expected to move sharply higher during the course of 2009 as the global recession works through and funding problems deepen. Moody's expects a rise from 3-4% at the end of 2008 to 10-11% in the US by end 2009, and to 12-13% in Europe. Corporate credit spreads over US Treasuries have ballooned out to 15-16% for High Yield (non-investment grade corporates) and 2-3% for Investment Grade. Notwithstanding those spreads, we would avoid high yield debt – the default rates are almost certain to soar. And continued redemptions could keep hedge funds on the sidelines for some time while other investors are likely to wait until economic activity revives. In addition, there are fears that the recovery rates on bonds in default may be especially low this time around. And even with Investment Grade debt, the scarcity of capital in 2009 is likely to keep spreads high. Investors will have to be patient.

Commodities

3M: Neutral

12M: Neutral

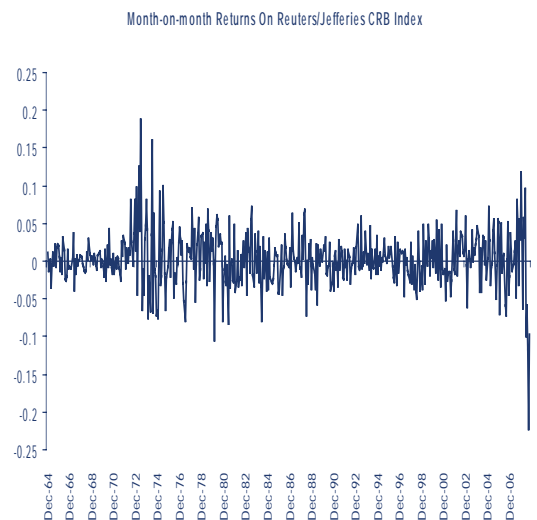
1Q09 is likely to see continued tight liquidity/de-leveraging, weak economic data and a resilient USD tussle with oversold conditions. Liquidity is expected to remain tight for at least a few more months, with the de-leveraging that lifted the US dollar in the second half of 2008 likely to continue for a bit longer. These factors are likely to restrain movements in commodity prices early in the year. In addition, the global recession still has to be worked through. The coming months are likely to see news of a deepening recession in the US, Euro zone and Japan. More importantly, there is a risk of a sharper than expected slowdown in the Emerging Market economies. This will have knock-on effects for commodities demand. But against that, many commodities are, technically, oversold.

Global conditions should eventually become more supportive over the course of 2009. The economic stimulus measures put in place by policy-makers around the world will eventually gain traction and economies should then stabilise and revive. We expect this from around mid-2009 in Asia and the big emerging markets. As this becomes more apparent, there is likely to be a more sustained rise in commodity prices.

The commodity markets have already priced in a lot of bad news. Commodities had their worst month in October at least since 1964 on slowing global economic activity and expectations of further reduction in demand. Total return on the Reuters/Jefferies CRB Index clocked its biggest one-month decline in four decades. Much of the downside is arguably already in the price with investors generally holding net "short" positions on the major US exchanges. (Exhibit 27)

Sharp price falls have resulted in big supply cuts. The dramatic price falls since mid-2008 have also brought big supply cuts across most sectors, which should limit the near term downside for prices and, over the longer term, should accentuate any upward move once demand bottoms out. Prices at the end of 2008 for many commodi-

Exhibit 27: Commodities – pricing in a lot of bad news



Source: Thomson Reuters

ties had fallen far below production costs. In addition, the financial crisis has curbed credit availability, accentuating the squeeze on supply.

USD strength on de-leveraging and flight for safety has limits.

The US dollar should weaken again later in 2009 as de-leveraging comes to an end, risk appetites improve, and the FX markets refocus on the structural problems in the US which should keep US rates low for longer than elsewhere.

Oil – flat demand growth has forced OPEC to cut supply.

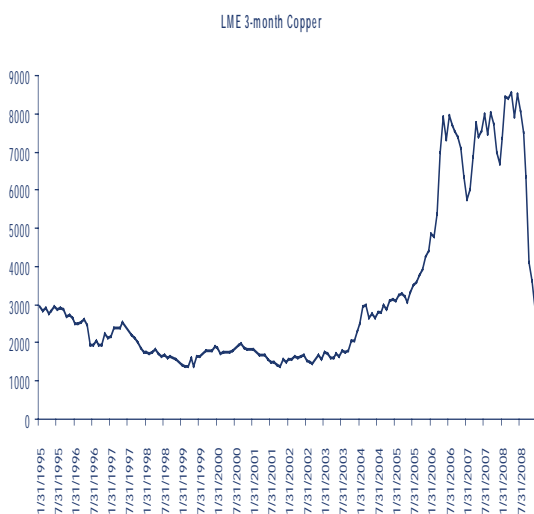
Demand for oil should come in flat for the full year 2009, as demand expansion in Asia and the emerging markets is offset by a second year of demand decline in the high-income economies. On the supply side, OPEC has agreed to cut output by 4.2 million barrels per day (bpd) from September levels. This is a cut of another 2.2million bpd further to those made in October and November. At this time, it appears that OPEC is holding its discipline and output is coming down.



Oil prices should rebound on a recovery in the global economy and risk appetites. Once the global economy starts to revive, energy demand should pick up and structural supply constraints should quickly kick-in. Continuous oil industry investment is needed to keep production levels constant. But the oil price collapse from the middle of 2008 and the financial crisis have stalled new projects. Also, we do not underestimate the role of risk appetites in oil prices. Much of the rally in oil prices to record highs in mid-2008 was associated with a build up in large speculative positions. As it was massively (technically) overbought then, it appears oversold today. Return of risk appetites and financial flows would be supportive.

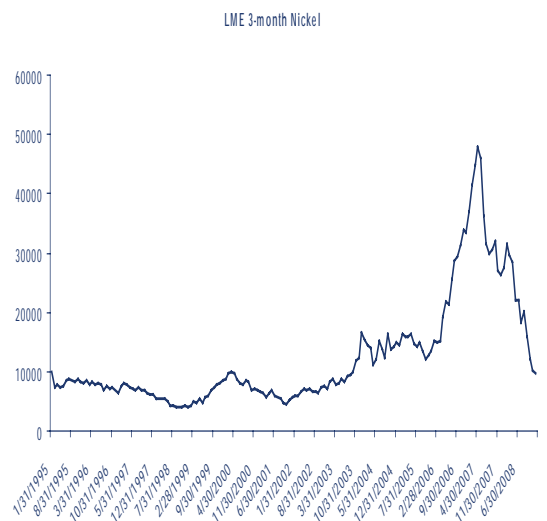
Base metal prices should rise once economic growth in China recovers. The sell-off in the second half of 2008 was indiscriminate and all metals prices fell sharply. Prices for some base metals had hit four-year lows. (Exhibits 28, 29) But we expect more divergence in performance in 2009 as supply and demand specifics assume a higher profile. Demand should also gradually pick up this year as the economic slowdowns in China and the other big emerging markets bottom out. Also note that prices have fallen toward or below cost levels in some cases. The sharp price falls and the dramatic erosion of profitability – with losses for many producers – have provoked aggressive output cuts. So the downside is not unlimited.

Exhibit 28: Metals – a lot of froth has been removed



Source: Thomson Reuters

Exhibit 29: Metals – a lot of froth has been removed



Source: Thomson Reuters

Indeed, all these factors suggest there is a bottoming out of base metals underway.

Gold prices should move up as the US dollar weakens again. Gold is expected to range-trade in the early months of 2009. But once de-leveraging comes to an end, which we expect could happen sometime in the first half of 2009, the US dollar should weaken again and send gold prices higher. In addition, low global interest rates should improve the opportunity cost of holding gold relative to other investments, new gold mine supply will stay constrained, and jewellery demand should pick up if, as we expect, economic growth revives in the key consuming regions (India, China, and the Middle East). We expect significantly stronger gold prices towards late 2009.

Agricultural commodity prices have probably bottomed. The final months of 2008 were likely the low point, and prices should rise this year on improved investor sentiment and continued supply concerns. The global recession has hit demand but lower prices and the credit crunch have also brought a quicker pull back in supply than has generally been the case with metals and energy. In addition, agricultural commodities, especially grains, are relatively more insulated from the economic cycle than metals and energy. Supply constraints are likely to kick in quickly once demand revives.

Hedge Funds

3M: Underweight

12M: Neutral

A difficult end to a difficult year. 2008 has been a difficult year for financial markets in general and hedge funds have gone through the most difficult year on record. With the notable exceptions of Macro Managers, Commodity Trading Advisors (CTAs) and dedicated short sellers that have been able to achieve positive performance numbers, all other strategies posted double digit losses.

Recent developments involving investigations into the activities of Bernard L. Madoff Investment Securities LLC could further undermine confidence in hedge funds, resulting in more redemptions and an accelerated decline in assets under management. Meanwhile, global economic conditions will almost certainly deteriorate in coming months. And trading conditions in financial markets will remain difficult, with the possibility of more stresses on the entire finance sector, including hedge funds.

Liquidity conditions could worsen. All of this could worsen the liquidity problem facing the hedge fund industry – something that had already been escalating through the course of 2008. Faced with rising redemptions, many fund managers have invoked “gate provisions” to limit the amount of redemptions at any one time. Others have put illiquid assets into so-called “side pockets”, segregating them from liquid assets in the event of redemptions. At the extreme end, there have also been suspensions of redemptions.

While the number of hedge funds that are imposing “gates” or halting redemptions is a minority of the industry, this development nevertheless affects funds of hedge funds investors either through delayed redemptions or higher fees for redemptions.

Investors with high or imminent liquidity needs should note this deterioration in liquidity conditions affecting even funds of hedge funds.

Downgrading our 3-month asset allocation weighting for hedge funds. In addition to the above, we also recognize the uncertainties facing financial markets in general. We have cut the 3-month weighting of hedge funds in our tactical asset allocation from “overweight” to

“underweight”. Our 12-month tactical asset allocation view remains “neutral”.

But hedge funds, as an asset class, remain valid tools for portfolios diversification long-term.

To avoid the risk of “throwing the baby out with the bath water”, it is also important to stress the role of hedge funds for portfolio diversification – specifically their role in providing better risk adjusted returns and cushioning the downside during bear markets. The chart below, which compares the HFRI Fund Weighted Composite index against the MSCI World index from Dec 96 to Nov 08, shows how hedge funds, as an asset class, function as risk diversifiers. (Exhibit 30) More recently, in the very difficult year to December 2008, hedge funds as an asset class were again able to significantly outperform long-only indices and mutual funds and offer investors some downside protection.

Need to be discriminating about the different types of hedge funds.

It is important to note that the term “hedge funds” applies to a broad range of non-traditional investment funds with sometimes very different risk and returns characteristics. For example, while the HFRX Global Hedge Fund Index declined by 23% in the year to 16 December, with the Macro Index actually up 5%, the Convertible Arbitrage Index was down 58%.

Exhibit 30: Hedge funds for portfolio diversification



Source: Bloomberg

Currencies

Volatility is likely to remain a key feature in currency markets this year – why the USD is likely to resist early correction. The steep USD slide in December, driven by improvements in risk appetite and aggressive Fed easing in the month, highlighted the volatility we are likely to see in currency markets in the first quarter of 2009. Indeed, in the first half of the year, we have already seen fluctuations of 6.4 per cent in the GBP/USD and 5.3 percent in the EUR/USD. In this quarter, negative economic surprises should prove frequent, equity markets will remain fragile and sentiment could turn quickly. So volatility is likely to stay with us and the Dollar should trade in a broad range against most majors. A clear directional trend is unlikely in the first half of the year, as the USD finds itself buffeted by the following cross currents: 1) Upside support from flows as global de-leveraging works through and 2) downside pressure from concerns on the languishing U.S. economy and an ultra-loose monetary policy.

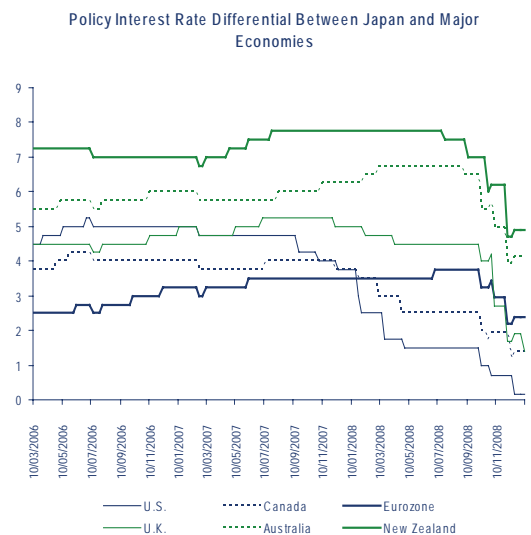
But USD weakness is expected to set in later in the year. However, we do expect the Dollar to weaken eventually. The level of de-leveraging flows should ease over time, while quantitative easing measures will build up a sustained supply of USD, supporting bearish sentiment towards the Greenback. We suspect more pronounced Dollar weakness is likely to be seen around the second half of this year.

Further monetary easing is likely to continue to drag down the Sterling and Euro. Recent economic data is indicating rapid deterioration of economic activity in Europe. Industrial production has fallen substantially across U.K., Germany and France while the sharp decline in new orders suggests that the down trend is likely to continue. Unemployment rising as companies scale back and embark on cost-cutting measures. Inflation has plunged below the ECB's target rate of 2 per cent, with headline CPI estimated for December at 1.6 per cent. Policy makers in Europe are expected to drive interest rates down further. Indeed, the Bank of England is expected to drive interest rates to nearly zero and follow in the footsteps of the U.S. Federal Reserve into quantitative easing. While

the ECB is not expected to move into quantitative easing anytime soon, its policy rate is likely to be slashed down to 1 per cent by the first half of the year. These actions are bearish for both the Sterling and the Euro and should restrain these currencies in the first quarter.

Yen remains supported on de-leveraging. De-leveraging and the flow of domestic savings back into Japan should continue to support the Yen in the earlier part of the year. The interest rate differentials between Japan and other developed countries – which resulted in carry trades for most of the decade – have shrunk rapidly as central banks race to slash rates. But de-leveraging flows should have eased from last quarter, suggesting the likelihood of more subdued support and gains in the Yen. Further, the market would be wary of possible intervention in the currency markets, as the Japanese government is unlikely to tolerate a much lower USD/JPY given its negative impact on Japanese exports. But risk aversion could return on corporate earnings shocks and this could in turn result in temporary spikes in Yen strength in the quarter. (Exhibit 31)

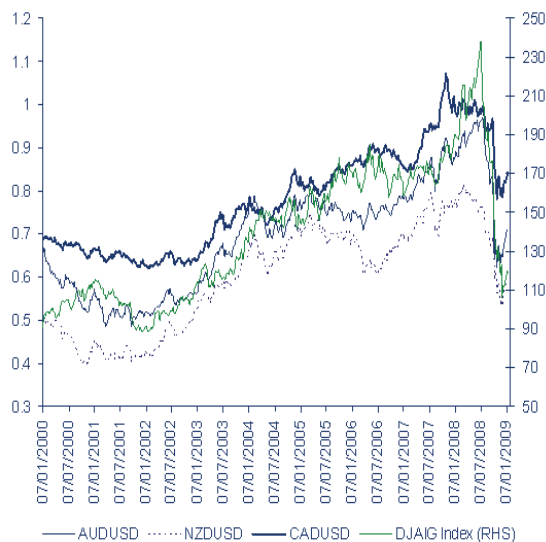
Exhibit 31: Unwinding of carry trades on narrowing interest rate differentials



Source: Bloomberg

Commodity currency strength likely to continue to be contained by lower interest rates and weak commodity prices. A number of negative fundamental factors we pointed out last quarter still plague the major commodity currencies. Despite the deep cuts we have seen so far, policy interest rates in Canada, Australia and New Zealand will likely head even lower and currently weak commodity prices are expected to reverse past years positive terms-of-trade gains in these economies. This suggests the CAD, AUD and NZD could still be kept on the defensive against the dollar in 1Q09. But the stabilizing of commodity prices after the steep slide last year could help with sentiment towards these currencies, as will the likely bottoming of interest rates by the end of the quarter. The above should help limit further significant downside from current depressed levels. (Exhibit 32)

Exhibit 32: The commodity currencies trade tightly against commodity indices



Source: Bloomberg

CAD – catching up with the global recession. As with the rest of the developed world, the economic situation in Canada appears to be worsening faster than initially expected. The collapse in employment numbers and the slump in consumer confidence suggest that the Canadian economy is playing catch-up with the severe downturn in the rest of the world. We anticipate more interest rate cuts by the Bank of Canada this quarter, and sustained strengthening of the CAD is unlikely near term.

AUD – downside pressure could resume beyond recent near term upside. With the 75 basis point reduction off the cash rate last month, the Reserve Bank of Australia (RBA) had brought the benchmark interest rate down by 3 per cent since September 2008. As with most other developed economies, Australia is facing severe headwinds on a drop in global demand. It faces a fast falling housing market, and a reversal of the positive terms-of-trade gains from buoyant commodity prices in recent years. Inflation is falling, though its pace could lag other countries due to its weak currency. Further interest rate cuts are likely to be seen in 1Q09.

Emerging Market (EM) currencies : Export-dependent economies to take their turn under pressure. Currencies of countries with current account deficits, notably the Korean Won and the Indian Rupee in Asia, had remained under pressure for the most part of last quarter with some respite only seen recently. However, this trend should change as the economic crisis runs its course in 2009. Contraction in consumption from developed economies suggests weakness is likely to shift to currencies of countries with higher growth dependence on exports, such as Taiwan, Singapore, Malaysia and Hong Kong. Sentiment towards the KRW and INR should improve over the year as lower fuel prices help with the current account balances of these countries and as the credit crisis plays out.

FX Forecasts

Note: Forecasts are valid as of 22 Jan 2009

	4Q08a	1Q09f	2Q09f	3Q09f	4Q09f	1Q10f	2007a	2008a	2009f
Majors									
Europe	1.40	1.34	1.38	1.45	1.55	1.60	1.46	1.40	1.55
Japan	93.00	90.00	95.00	92.00	88.00	85.00	111.71	93.00	88.00
UK	1.46	1.45	1.38	1.48	1.63	1.68	1.98	1.46	1.63
Canada	1.22	1.21	1.25	1.20	1.15	1.10	1.00	1.22	1.15
Switzerland	1.07	1.12	1.08	1.04	1.00	0.98	1.13	1.07	1.00
Australia	0.72	0.70	0.72	0.77	0.80	0.85	0.88	0.72	0.80
New Zealand	0.60	0.61	0.64	0.66	0.68	0.72	0.77	0.60	0.68
Asia									
China	6.82	6.90	6.95	6.95	6.90	6.85	7.30	6.82	6.90
Hong Kong	7.75	7.78	7.85	7.83	7.81	7.81	7.80	7.75	7.81
Indonesia	10700	11500	10800	10000	9300	9300	9400	10700	9300
India	49.00	49.00	48.25	47.00	46.00	45.00	40.07	49.00	46.00
Korea	1259.50	1300.00	1250.00	1180.00	1150.00	1180.00	936.00	1259.50	1150.00
Malaysia	3.45	3.70	3.75	3.65	3.55	3.45	3.31	3.45	3.55
Philippines	46.45	46.50	48.00	46.50	45.00	44.50	41.60	46.45	45.00
Pakistan	77.80	80.00	80.00	81.00	82.00	82.00	61.85	77.80	82.00
Vietnam	17483	17600	18000	18500	18500	18600	16017	17483	18500
Singapore	1.43	1.54	1.57	1.52	1.48	1.44	1.44	1.43	1.48
Thailand	34.80	35.25	37.00	36.50	35.50	35.00	33.72	34.80	35.50
Taiwan	32.98	34.10	34.80	34.60	34.30	34.00	32.43	32.98	34.30
Other Emerging Markets									
Brazil	2.17	2.40	2.18	2.00	1.90	1.85	1.78	2.17	1.90
Mexico	13.40	13.80	12.60	12.00	11.55	11.40	10.90	13.40	11.55
Chile	633	640	610	600	525	490	437.00	633.00	525.00
Turkey	1.54	1.57	1.50	1.35	1.20	1.13	1.17	1.54	1.20
South Africa	10.00	8.80	9.20	8.90	9.10	9.30	7.04	10.00	9.10

Source: SCB Global Research

Government Bond Forecasts

Note: Forecasts are valid as of 22 Jan 2009

Country	Tenor	1Q09f	2Q09f	3Q09f	4Q09f
China	2-year	1.80	2.00	2.30	2.50
	5-year	2.35	2.55	2.90	3.10
	10-year	2.80	3.25	3.55	3.75
Hong Kong	2-year	0.90	1.10	1.50	1.90
	5-year	1.70	2.00	2.50	2.85
	10-year	2.00	2.30	2.70	3.05
India	2-year	6.25	5.50	5.65	6.00
	5-year	6.75	6.25	6.35	6.75
	10-year	7.00	6.50	6.75	7.15
Indonesia	3-year	14.00	12.50	12.25	11.75
	5-year	14.50	13.25	13.00	12.50
	10-year	15.00	14.00	13.75	13.25
Malaysia	3-year	3.00	3.10	3.20	3.40
	5-year	3.40	3.50	3.55	3.70
	10-year	3.70	3.85	3.90	4.05
Pakistan	3-year	15.60	14.80	13.80	13.30
	5-year	16.20	15.40	14.40	13.80
	10-year	16.90	16.20	15.20	14.60
Philippines	2-year	6.50	6.25	6.35	6.50
	5-year	7.15	6.85	7.00	7.25
	10-year	7.80	7.35	7.50	7.75
Singapore	2-year	0.90	0.95	1.20	1.50
	5-year	1.50	1.65	2.00	2.35
	10-year	2.30	2.50	2.85	3.25
South Korea	3-year	3.60	3.25	3.40	3.70
	5-year	3.75	3.40	3.55	3.85
	10-year	4.50	4.25	4.35	4.60
Taiwan	2-year	1.50	1.60	1.80	1.80
	5-year	1.60	1.70	1.90	2.00
	10-year	1.70	1.85	2.05	2.15
Thailand	2-year	2.70	2.50	2.85	3.20
	5-year	2.90	2.75	3.15	3.50
	10-year	3.65	3.50	3.80	4.00
United States	2-year	1.15	1.25	1.40	1.90
	5-year	2.10	2.30	2.50	2.90
	10-year	3.40	3.50	3.65	3.90
Vietnam	2-year	10.00	9.50	9.25	9.75
	5-year	10.00	9.75	9.50	10.00
	10-year	10.50	10.25	10.00	10.50

(End of period, % yield)

Source: SCB Global Research

Commodity Forecasts

Note: Forecasts are valid as of 22 Jan 2009

	4Q08a	1Q09f	2Q09f	3Q09f	4Q09f	2008f	2009f	2010f
Energy								
Crude oil (near future, USD/b)								
NYMEX WTI	59	50	53	60	70	100	58	80
ICE Brent	57	47	50	57	67	98	55	77
Dubai spot	54	45	48	55	65	94	53	75
Refined oil products								
Singapore fuel oil 180 (USD/t)	296	195	228	273	325	504	255	393
Singapore gasoil (USD/b)	62	60	66	69	80	118	69	91
Singapore jet kerosene (USD/b)	75	62	68	71	82	120	71	93
Singapore naphtha (USD/b)	38	39	45	55	66	87	51	76
Europe gasoil (USD/t)	591	484	484	522	596	907	522	689
Europe jet (USD/t)	634	564	568	606	684	986	605	788
Europe naphtha (USD/t)	370	392	436	507	596	792	483	685
Coal (USD/t)								
API4	96	80	85	100	110	122	94	115
API2	102	90	100	120	130	147	110	138
globalCOAL NEWC*	93	80	85	100	110	129	94	115
Metals								
Base metals (LME 3m, USD/tonne)								
Aluminium	1,875	1,500	1,650	1,750	1,800	2,620	1,675	2,000
Copper	3,915	3,000	3,300	3,800	4,000	6,876	3,525	4,500
Lead	1,253	1,200	1,200	1,250	1,300	2,092	1,238	1,050
Nickel	11,073	9,300	10,000	10,500	10,500	21,224	10,075	12,000
Tin	12,881	11,000	12,000	13,000	14,000	18,395	12,500	13,500
Zinc	1,217	1,100	1,200	1,350	1,400	1,900	1,263	1,575
Steel** (CRU assessment, USD/t)								
HRC, US	787	600	580	575	570	946	581	575
HRC, Europe	743	585	565	550	540	927	560	541
HRC, Japan	1,091	1,050	850	795	780	985	869	739
HRC, China	549	529	509	499	493	729	508	511
Precious metals (spot, USD/oz)								
Gold (spot)	798	885	950	1,000	1,050	872	971	1,100
Palladium (spot)	190	170	200	215	225	351	203	275
Platinum (spot)	869	950	1,000	1,050	1,100	1,574	1,025	1,200
Silver (spot)	10.23	10.50	10.50	11.00	12.00	14.97	11.00	13.00

Forecasts are period averages; *weekly quote **monthly average

Source: Bloomberg, Platts, CRU, SCB Global Research

Commodity Forecasts (cont'd)

Note: Forecasts are valid as of 22 Jan 2009

	4Q08a	1Q09f	2Q09f	3Q09f	4Q09f	2008f	2009f	2010f
Agricultural products								
Softs (near future)								
NYBOT cocoa, USD/tonne	2,259	2,500	2,600	2,700	2,650	2,558	2,613	2,850
LIFFE coffee, USD/tonne	1,786	1,900	2,000	1,900	1,900	2,145	1,925	1,994
NYBOT coffee, USc/lb	112	120	125	130	130	132	126	138
NYBOT sugar, USc/lb	11.6	13.0	15.0	15.5	16.5	12.1	15.0	16.0
Fibres								
Cotton (Cotlook A index, USc/lb)	57.7	62.0	63.0	65.0	72.0	71	66	76
Grains & oilseeds (nr future)								
CBOT corn (maize), USc/bushel	384	500	550	610	610	527	568	561
CBOT Soybeans, USc/bushel	896	1,015	1,050	1,100	1,150	1,233	1,079	1,208
CBOT wheat, USc/bushel	547	600	625	650	650	796	631	703
CBOT rice, USc/cwt	15.0	14.0	16.0	16.5	16.5	17.6	15.8	16.0
Thai B rice 100%, USD/tonne*	592	600	605	625	610	687	610	603
Edible oils (3m future)								
Palm oil (MDV,MYR/tonne)	1,611	1,850	2,250	2,500	3,000	2,839	2,400	3,125
Soyoil (CBOT, USc/lb)	34	38	40	44	45	52	42	47

Forecasts are period averages; *weekly quote **monthly average

Source: Bloomberg, Platts, CRU, SCB Global Research

SCB Tactical Asset Allocation 1Q09

3M Weighting					
	TAA Weighting	Conservative	Moderate	Aggressive	Very Aggressive
Cash	USD Cash	Over	Over	Over	Over
Bonds	Global Bonds	Neutral	Neutral	Neutral	Neutral
	Asia Bonds	Neutral	Neutral	Neutral	Neutral
	Emerging Market	Neutral	Neutral	Neutral	Neutral
Equities	North America Equities	Under	Under	Under	Under
	Europe Equities	Under	Under	Under	Under
	Japan Equities	Under	Under	Under	Under
	Asia ex-Japan Equities	Under	Under	Under	Under
	Emerging Market Equities	Under	Under	Under	Under
Alternatives	Funds of Hedge Funds	Under	Under	Under	Neutral
	Properties	Neutral	Neutral	Neutral	Neutral
	Commodities	Neutral	Neutral	Neutral	Neutral
Summary	Total Cash	Over	Over	Over	Over
	Total Bonds	Neutral	Neutral	Neutral	Neutral
	Total Equities	Under	Under	Under	Under
	Total Alternatives	Under	Under	Under	Neutral

Source: SCB Group Wealth Management

12M Weighting					
	TAA Weighting	Conservative	Moderate	Aggressive	Very Aggressive
Cash	USD Cash	Neutral	Neutral	Neutral	Neutral
Bonds	Global Bonds	Under	Under	Neutral	Neutral
	Asia Bonds	Over	Over	Neutral	Neutral
	Emerging Market	Over	Over	Neutral	Neutral
Equities	North America Equities	Under	Under	Under	Under
	Europe Equities	Neutral	Neutral	Neutral	Neutral
	Japan Equities	Under	Under	Under	Under
	Asia ex-Japan Equities	Over	Over	Over	Over
	Emerging Market Equities	Over	Over	Over	Over
Alternatives	Funds of Hedge Funds	Neutral	Neutral	Neutral	Neutral
	Properties	Neutral	Neutral	Neutral	Neutral
	Commodities	Neutral	Neutral	Neutral	Neutral
Summary	Total Cash	Neutral	Neutral	Neutral	Neutral
	Total Bonds	Neutral	Neutral	Neutral	Neutral
	Total Equities	Neutral	Neutral	Neutral	Neutral
	Total Alternatives	Neutral	Neutral	Neutral	Neutral

Source: SCB Group Wealth Management

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