ING Investment Management Asia Pacific

September/October 2009

HOUSEVIEW

Global Economic Outlook

World

- Industrial production, business confidence and real estate markets continue to show improvements.
- However, unemployment trends continue to worsen in many G7 countries and any turnaround would be protracted.
- Abundant liquidity and refusal of central banks to tighten monetary policy have led to a substantial rise in asset prices.
- With greater risk appetite and abundant liquidity, the US dollar continues to weaken against major currencies and commodities.

United States

- September's ISM non-manufacturing index rose to 50.9, marking the expansion of the service sector for the first time since the bankruptcy of Lehman Brothers.
- The unemployment rate continued to inch up, registering 9.8% in the month of September. The US lost 175,000 jobs in the month of September and while the pace of decline is abating, it will nevertheless be a long time before the unemployment rate reverses.
- The deep freeze of the US housing market continues to thaw with pending home sales increasing 12.1% compared to year ago in August.

Europe

- The ECB kept interest rates unchanged at 1% and there is little expectation of a rate hike in the near future.
- While Euro-zone industrial production improved 0.9% MoM in August, it remains 15.4% lower than previous year's level.
- The Euro-zone unemployment rate stood at 9.6%

Japan

- The Tankan index while still at -33, indicating that manufacturers are less pessimistic relative to June when the index was -48.
- The housing situation in Japan remains difficult as witnessed by the 38.3% fall in housing starts for August. Construction orders also fell 25.2% compared to the previous year.
- The unemployment rate unexpectedly improved to 5.5% in August as the number of employed increased by 290,000 compared to July. The job to applicant ratio also stopped worsening for the first time since January 2008 at 0.42.

Global Market Insights

Equities

- Global equity markets remain buoyant with abundant liquidity helping to push asset values higher.
- Optimism towards third quarter earnings remain high though third quarter earnings have so far provided more positive surprises.
- Unemployment trends remain difficult and we would expect the eventual turnaround in the labour market to be slow and incremental.
- Despite the substantial market rally, Asian and global emerging markets continued to receive substantial fund inflows helped by large size IPOs.
- The substantial outperformance of developing markets vs. developed markets can potentially reverse as economic recoveries in G7 countries continue to gain traction.

Bonds

- Global macro data continues to remain strong. The combination of inventory, fiscal policy and credit/financial conditions has temporarily boosted growth momentum significantly from Q2'09 onwards. However, the more than expected rise in the US unemployment rate in September serves as a reminder of the distinct possibility of another jobless recovery in the US.
- Underlying disinflation trends are still present and expected to persist. However, this may only come to the forefront again in 2010. We expect the Fed to keep interest rates in the 0-0.25% range until Q3'10 and to modestly increase them thereafter.
- Asset markets are being driven by the "liquidity-trade", as ample central bank liquidity and cash positions available in money market funds has started to flow into all asset classes that provide a yield that is in excess of cash.
- A sharp sell off in bond markets is unlikely. Beyond the sharp stimulus and inventory driven rebound, we expect bonds to perform relatively well as financial markets transition into a slower, broader recovery, where demand-pull inflation is not a near-term problem.

Returns

- Equity markets continued to climb in Sepember, as abundant liquidity and optimism towards third quarter earnings kept equity prices well bid.
- Global government bonds had another good month on the back of a sharply weaker USD, and also somewhat lower yields, in spite of an improved macro backdrop.

Equities Benchmark	September	Year-to-Date	12 Months
MSCI World (USD terms)	3.99%	24.90%	-2.29%

Bond Benchmark	September	Year-to-Date	12 Months
World Govt Bond Index (USD terms, unhedged)	2.29%	4.57%	13.78%

Asia Pacific Economic Outlook

Overview

- While Australia has begun to tighten interest rate, other central banks are likely to adopt wait and see approach.
- Meanwhile, economic improvements continues and accomodative fiscal and monetary policy is likely to remain in place in the near term..
- Optimism towards third quarter earnings is high with market to focus on business outlook rather than current earnings.
- Recent bout of US dollar weakness is likely to benefit Asian currencies due to faster economic growth, low financial leverage and asset value appreciation potential.

China

- China's PMI stood at 54.3 in September further improving from the 54.0 figure reported in August.
- Industrial production was up 12.3% in August bring the year to date total to up 8.1%.
- Fixed assets investment grew 33.0% year to date to August fueled by strong loan growth.

North Asia

- Hong Kong's unemployment rate remained constant at 5.4% in August
- Korea's depart store sales rose 7.6% in August pointing towards improvements in domestic consumption.
- Taiwan's Leading indexx showed 1.9% improvement on month on month basis.

South Asia

- Consistent with an improving economy, Indonesia saw cement consumption reach above 4mt in August for the first time in 15 months.
- Malaysia's economy remained in difficulty with industrial production dropping by 8.4% in the month of July.
- Philippines' OFW remittance rose a higher than expected 9.3% to US$1.49 billion in July.

Pacific

- Australia raised its benchmark rate by 25bps to 3.25% signalling the central bank's confidence in the economy.

Asia Pacific Market Insights

Equities

- Post G20 meeting, the market is currently factoring monetary and fiscal policy would not see dramatic tightening in the near term as most governments deem their respective economies too fragile to sustain shocks.
- Abundant liquidity for long periods is likely to create asset bubbles where Asian real estate and equity prices can overshoot fair value.
- US dollar weakenss will cause the market to reexamine the prospect of exporters that on one hand benefit from better G7 demand but on the other hand see their products become less competitive.
- Third quarter earnings will provide a glimpse into 2010 outlook which the market is likely to place greater emphasis than current earnings.
- Asia Pacific's 2010 estimated PE stands at 14.6X with an estimated earnings growth of +19.2% and 3 months earnings revision of +7.0%.
- Given the considerable optimism and complacency imbued into the third quarter earning season, the market will show slim tolerance for disappointments.

Bonds

- In contrast to the benign outlook for G3 bonds, the significantly higher resilience shown by Asian economies is likely to result in an earlier withdrawal of the accommodative monetary stance in the region.
- Headline inflation will continue to drift higher in Asia, fuelled initially by supply side factors and low base effects, and is likely to force liquidity sterilization measures in some of the Asian economies, although diminished supply concerns and ample liquidity are likely to provide some comfort to local bonds.
- We expect the amount of rate hikes to be modest, and believe the degree of tightening priced into most yield curves is exaggerated as the longer term growth outlook, and final demand from the developed world remains uncertain.
- While we are cautious in our outlook on bond markets, we remain fundamentally bullish on Asian currencies medium term and expect a majority of returns to be driven by currency strength.

Returns

- Asian markets resumed thier uptrend with another very strong month in September. Asian assets continue to garner interest in light of faster economic growth and weak USD.
- Asian local currency bonds had a strong month, with bulk of the gains coming from Asian FX appreciation

Equities Benchmark	September	Year-to-Date	12 Months
MSCI Asia Pacific Ex Japan (USD terms)	8.84%	61.44%	26.74%

Bond Benchmark	September	Year-to-Date	12 Months
HSBC Asia Local Bond Index (USD terms)	3.04%	4.41%	9.62%

Recommended Asset Exposures	
International Equities	Neutral
Asian Equities	Underweight
International Bonds	Overweight
Asian Bonds	Neutral
Cash	Neutral

ING IMAP Houseview

	Key Drivers	Key Risks	Risk Rating
World Economy	• Deleveraging of consumer, financial and corporate sectors • Continued co-ordinated approach to the financial and economic crises	• Emerging markets decline into recession • Protectionism emerges	High Low
Global Equities	• Prospects for economic growth • Earnings growth and the extent of revision	• Earnings downgrades surprise on the downside • Availability of credit diminishes	High Medium
Global Bonds	• Accomodative monetary stance • Deficit spending and bond supply • Muted core inflation and weak consumer demand	• Return of risk appettite/ demand for risky assets • Exit of accomodative monetary policies • Inflation worries escalating • Increasing fiscal deficits, rising public debt	Medium Low Low Low
Asian Equities	• Extent Asia is impacted by the global economic slowdown • International investors appetite for risk	• Earnings revisions surprise to the downside • Valuations fail to halt market slide	High High
Asian Bonds	• Bond supply and fiscal stance • Excess liquidity • Extent of growth rebound	• Higher G3 bond yields • Increased inflation and higher commodity prices • Premature and excessive monetary policy tightenng	Low Medium Low