



## Market Commentary

October 2008

GLOBAL EQUITY

EQUITIES	1 Mth	3 Mth	YTD	12 Mth
MSCI AC World	-11.7	-12.6	-27.1	-30.9
MSCI World	-11.1	-11.1	-25.8	-30.0
MSCI USA	-8.4	-4.7	-20.7	-26.0
MSCI Europe	-14.2	-16.9	-32.7	-35.3
MSCI Japan	-10.7	-13.8	-23.5	-30.8
MSCI AC Asia ex-Japan	-15.8	-19.8	-40.9	-42.3
MSCI Emerging Markets	-16.8	-23.7	-37.0	-36.9

Returns in Singapore dollars  
Source: Bloomberg

World equity markets fell sharply in September as concerns over liquidity led to the failure of Lehman Brothers and the near failure of several significant financial institutions. This unprecedented shift in liquidity conditions has raised significant concerns over growth prospects for the broader economy and corporate sector. This change in outlook weighed most heavily on Emerging Markets, Asian and European equity performance, although all regions registered declines. Investor behavior continues to be driven by fear, fear over the housing market, fear over the growth outlook, and fear of contagion risk. Financial stability became a key focus of policy makers in the US as well as Europe, with the eventual passing of the Troubled Asset Relief Program (TARP) in the US and emergency government action in Ireland and Germany to guarantee deposits in an effort to stabilise funding. In the span of just over a month, with the collapse of Lehman, the near failure of Merrill Lynch and the conversion of Goldman Sachs and Morgan Stanley to bank holding company licensed entities, investors bore witness to the end of the broker-dealer model.

### OUTLOOK AND STRATEGY

EQUITIES	Policy	Change	Comment
US	Slight Overweight	↑	Policy responses has been the most aggressive. GSE support measures should help to ensure an orderly clearing process. A still weak dollar is helping export-oriented sectors. Having underperformed for several years, valuations are now supportive, and relative expectations are low.
Europe	Underweight	-	We see greater risks to earnings and have tempered our previously positive view on Europe. We are somewhat concerned that policy response has been slow to adjust to the shift in liquidity and note the increased leverage of European financials and the risks of ongoing deleveraging.
Asia ex-Japan	Neutral	↓	The sharp deterioration in external factors has led us to reduce our allocation to Asia. We are concerned that the deterioration in exports will weigh on domestic confidence and pose further risk to earnings expectations.
Japan	Neutral	↑	In the face of softening external demand, it is difficult to overweight Japan. While valuations appear more attractive at the moment, Japan remains a heavily export-oriented market.

We continue to closely monitor financial conditions in both the US and Europe in search of signs of stabilisation. The passing of the TARP in the US is a first step in what we expect will be a gradual recovery process. We fear that the recovery timeline in Europe may prove more protracted. We remain concerned that tighter financial conditions in Europe will have an adverse impact on economic performance into 2009. The defensive posture in terms of the types of companies that we are targeting prevails, as does our decision to underweight consumer discretionary and mid-cycle industrial companies. We have started to deploy incremental capital to the US. We remained concerned about Europe and are slightly less positive on both Asia ex-Japan, as well as Latin America. Our strategy is to continue to focus on the less cyclical sectors including consumer staples, healthcare and telecommunications.

We have lifted our exposure to the US to slightly overweight and may further increase our exposure there. Expectations in the US have already been lowered significantly, and the prospects of downward revisions outside of the housing, consumer discretionary and financial sectors are somewhat contained, with the still weak dollar providing a boost to the export Industrial sector. The Fed is likely to continue to provide an accommodative monetary stance should downside risks build.

Continued headwinds in the form of tight credit conditions, declining asset prices, higher debt service costs, and rising savings rates will likely exert downward pressure on medium term growth and represent a risk to our soft landing hypothesis.

As we write, there is increasing concern over a global recession. The acute shift in financial conditions, and consumer and business confidence appear to make a sharp global slowing all but unavoidable. We had previously commented on the diminished visibility over earnings as a clear concern and because of this we remain extremely defensive in our investment approach. While valuations do provide some support, we do not believe they will prove a catalyst over the short term.

We keep our underweight in **Europe** as the valuation argument, when superimposed against the sharp deterioration in financial and economic conditions appears very tenuous. Weaknesses in the financial system is adversely impacting the real economy. We see significant need for de-leveraging across many of the largest financial institutions in Europe. This will likely be accompanied by an extended period of upward re-pricing of risk for borrowers, which will exert a drag on growth.

We have tempered our earlier optimism in **Asia ex-Japan**. Growth appears to be slowing faster than previously feared. As such, we have adopted an increasingly defensive strategy in terms of the type of companies targeted, with domestic demand plays featuring prominently.

We are neutral in Japan. Corporate sector profit growth is uninspiring, particularly in the export sectors that are dependent on a robust global economy to drive growth. Whilst Japan has held up as a risk aversion trading market we view the medium term earnings growth prospects as uninspired.

Current conditions are negative for the equity markets, and will likely continue to dampen performance for the next couple of quarters. We continue to focus on high-quality bottom-up investments which will perform better in an environment of rising volatility.

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