

Global Equity

EQUITIES	1 Mth	3 Mth	YTD	12 Mth
MSCI AC World	-1.6	-2.0	1.2	10.7
MSCI World	-1.5	-2.7	1.8	10.6
MSCI Emerging Markets	-2.1	2.4	-2.4	11.2
MSCI USA	-0.3	-1.4	3.1	9.1
MSCI Canada	-2.3	-5.3	1.0	9.9
MSCI Europe	-3.2	-1.1	4.9	17.9
MSCI Japan	-0.8	-14.0	-10.5	-5.7
MSCI Australia	-4.6	-1.3	-0.8	17.9
MSCI AC Asia Ex-Japan	-0.7	5.0	-1.2	13.0
MSCI Latin America	-2.3	-2.9	-6.5	5.0
MSCI EMEA	-5.5	-1.2	-2.1	14.5

Returns in Singapore dollars. Source: Bloomberg, 31 May 2011

Equity markets declined in May as concerns over the peripheral Europe resurfaced, while economic data rolled over. Investors became preoccupied with trying to distil the effect of the Japan earthquake and tsunami from the softening of other broad indicators. Consequently, Europe and the more cyclically exposed markets including EMEA and Australia registered the sharper declines. All regions posted negative returns in US dollar terms in May.

The dominant feature of market performance during the month of May was concern over the strength of the recovery and fiscal challenges. In particular, there was renewed focus on Greece's need for further support, as Greece's credit rating was downgraded to sub-investment grade. Meanwhile, credit spreads for all of the peripheral countries widened, reflecting the structural challenges that have to be dealt with into the future.

Also, emerging market inflation concerns linger. Indeed, China's headline CPI came in at 5.5% in May, with producer prices up 6.8%. Recent surges in food and energy prices only exacerbated the challenge, and pointed to an upward bias in expectation and the need for additional tightening measures. Economists are now expecting up to 75 basis points in further tightening.

India, too, is facing inflationary challenges. CPI in April rose to 9.4%. Meanwhile the RBI Bank Rate remained at 6%, leaving real interest rates in negative territory.

Brazil CPI inflation came in at 6.55% in May, up from 6.5% in April. Brazil's central bank continues to maintain positive real interest rates, but inflation remains stubbornly high. Expectations are for inflation to gradually moderate into the year.

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OUTLOOK AND STRATEGY

	Policy	Change	Comment
US	Overweight	–	The corporate sector is in solid shape and a weaker dollar is adding upside to profit estimates over the medium term. Meanwhile, employment data has picked up and consumption data has been favourable, suggesting that the recovery is pretty well entrenched. The corporate sector is in a strong position to grow into recovery. We continue to favour the US over other developed regions. OVERWEIGHT.
Europe	Underweight	↓	The outlook in Europe is increasingly divergent, with the peripheral countries' problems weighing on the broader region and the Euro. While employment in the core has held up favourably, the situation in the periphery looks increasingly dire. We have, nonetheless, increased our exposure to the region given its attractive valuations and opportunities outside of the financial sector. UNDERWEIGHT.
Asia (ex-Japan)	Neutral	↓	Inflation data in Asia is a problem, and further policy tightening is inevitable, especially in China and India. The shift in policy bias is coming at a time when the cyclical recovery is moderating due to base effects. Although the longer term growth outlook still remains favourable, the policy shift could pose a significant headwind to market performance. We remain more defensive, focused on sectors where pricing power should be stronger. NEUTRAL.
Japan	Underweight	↓	The sharp pull back in Japan's markets has created a tactical buying opportunity. However, longer term headwinds have been exacerbated by the earthquake and subsequent power crisis. Furthermore the strong Yen continues to be a challenge for exporters. We have looked for opportunities in more defensive sectors like consumer staples and capital goods. UNDERWEIGHT.
Latin America	Overweight	–	Inflation is a challenge in Brazil, and we have moved incremental capital to Mexico and other countries. The region's need to replenish and enhance its capital stock is both a positive and a negative and may put additional pressure on inflation in the near term before long term productivity gains can be realized. We still like the region but have reduced the OVERWEIGHT.

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	Policy	Change	Comment
EMEA	Underweight	↓	EMEA (Eastern Europe, Middle East & Africa) outlook varies by region. Growth prospects in Eastern Europe remain favourable, while the outlook in Africa is deteriorating. The outlook for the more industrialised parts of Eastern Europe (Czech Republic and Poland) remain favourable as do prospects for resource rich Russia. UNDERWEIGHT.

The growth outlook deteriorated appreciably over the past few months. The trajectory of the global economy has been further clouded by supply chain disruptions arising from the Japan earthquake. However, the start of a multi-year fiscal adjustment process suggests that the below potential growth will likely persist in the developed world for some time. The outlook for Europe continues to be clouded by the challenges of the periphery and the risk of contagion via the European banks. We continue to prefer the US over Europe given the vulnerability of the European banking system.

The slowdown in global growth should help to allay some of the inflation concerns in the emerging world. However, this does not imply that central bankers should become any less vigilant. With expectation that inflation will abate later this year, we have stepped up our exposure to emerging markets..

Macro-economic and operating conditions present multiple challenges and pose several risks that are difficult to predict due to the political dynamics at play. Against this backdrop, we are broadly “de-risking” our investment portfolios and focusing on less cyclical sectors. While equity valuations remain very attractive, there is increased earnings risk given the environment of decelerating growth and persistent inflation. We continue to focus on high quality franchises that have sufficient pricing power to manage in an environment where input costs may rise.

Contact Details

Address 80 Raffles Place UOB Plaza 2 Level 3 Singapore 048624

24-hour Hotline 1800 222 2228 (Local) • (65) 6222 2228 (International)

Fax (65) 6532 3868

Email uobam@uobgroup.com

Website uobam.com.sg

Business Offices

Singapore

Institutional Business

Dennis Siew

Senior Director

Retail Business

Norman Wu

Senior Director

New Strategic Markets & Private Banks

Rachel Ong

Director

Structured Investments

Chong Jiun Yeh

Executive Director

Brunei

Kamal Muhd

General Manager

Japan

Masashi Ohmatsu

Chief Executive Officer

Malaysia

Lim Suet Ling

Chief Executive Officer

Taiwan

Juang San Tay

General Manager

Thailand

Vana Bulbon

Chief Executive Officer

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