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ASSET MANAGEMENT



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## The tigers return

Prompt action from Asia's relatively debt free governments, combined with resilient underlying domestic demand helped the region escape the worst of the global economic contraction, despite the deterioration in its export markets.

Unlike the stance adopted by the West, where government spending was directed towards funding bank bailouts, Asian governments took active steps to boost domestic consumption directly through infrastructure spend and subsidies. At the same time, high savings rates across the region, supplemented by interest rates falling to all time lows, helped to sustain consumption, as did the increase in disposable income. With export sectors now recovering, Asia looks to have weathered the storm.

Recent GDP data confirms the continuation of this 'V'-shaped recovery, not only in developing but also in developed Asian markets such as Singapore, Hong Kong and Korea; the former 'Asian Tigers'. These countries saw their governments allocate a much higher percentage of GDP to fiscal stimulus. In Korea, the KRW22 trillion Four Rivers project is a good example of such spending, as are Singapore's job credit subsidies.

Such markets are also well placed to take advantage of a recovery in global trade. As beneficiaries of growth in China, they also stood to gain from the economic recovery driven by the RMB4 trillion fiscal stimulus

package. Whether their comeback will last into 2010 - the 'Year of the Tiger' - however, remains to be seen. Elsewhere, Japan, having been through its worst post-war recession, saw a recovery driven largely by inventory restocking following overly aggressive initial cuts in production. We expect a steady economic improvement into 2010, however, there is little sign of a sustained recovery.

### The end of loose policy

Much uncertainty surrounds what will happen when stimulus measures are withdrawn, and when loose monetary policy from governments around the world comes to an end. Authorities everywhere are faced with the conflicting needs of supporting growth while avoiding inflationary pressures.

Asia will inevitably be less accommodative on monetary policy, given the strength of its recovery, and will lead the US in tightening policy. However, rising interest rates will be less damning to the relatively unleveraged balance sheets of Asian consumers and businesses than they will to their western peers.

Although we are cautious on the potential consequences of the unconventional policy responses seen over the past year, we are confident that Asia's strong fundamentals will help sustain economic growth momentum, as structural forces such as industrialisation and urbanisation continue apace.

Australia has already begun to tighten policy, and other countries such as Korea and India should be next in line. In Singapore, the government is slowly withdrawing its jobs credit subsidies, while Hong Kong is devising new ways to quell the property price bubble, given that its interest rate policy is tied to the US on account of the Hong Kong dollar peg.

Singapore should remain well placed with the opening of various gambling resorts next year, while Hong Kong will continue to benefit from its proximity to China. It is Korea which will see the greatest impact from rising interest rates, given that it has the highest household debt to GDP ratio in Asia. It is also, to a large extent, dependent on the western consumer for its export-driven economy.

### China's spending spree

With a vast number of Asian companies now cash rich, we expect merger and acquisition activity to continue, which may provide further support to share price valuations. We expect a pick-up in activity –

domestic, intra-regional, inbound and outbound – both by multinational companies anxious to establish firmer footprints in the growth markets of Asia, and by Asian companies attempting to establish a global presence.

China has been particularly active on this front; overseas direct investment jumped 190% in the third quarter of 2009 to US\$20.5 billion as China took the opportunity to acquire resources while alleviating pressure on its currency. High profile examples include the investments made by China Investment Corporation in Noble Group, PT Bumi Resources and Astana. We see further opportunities in resources, especially within energy, and companies with strong consumer brands and distribution networks.

However, we believe that cash poor companies with incoherent strategies and a history of poor corporate governance will struggle, as these types of business tend to place their egos ahead of shareholder interests.

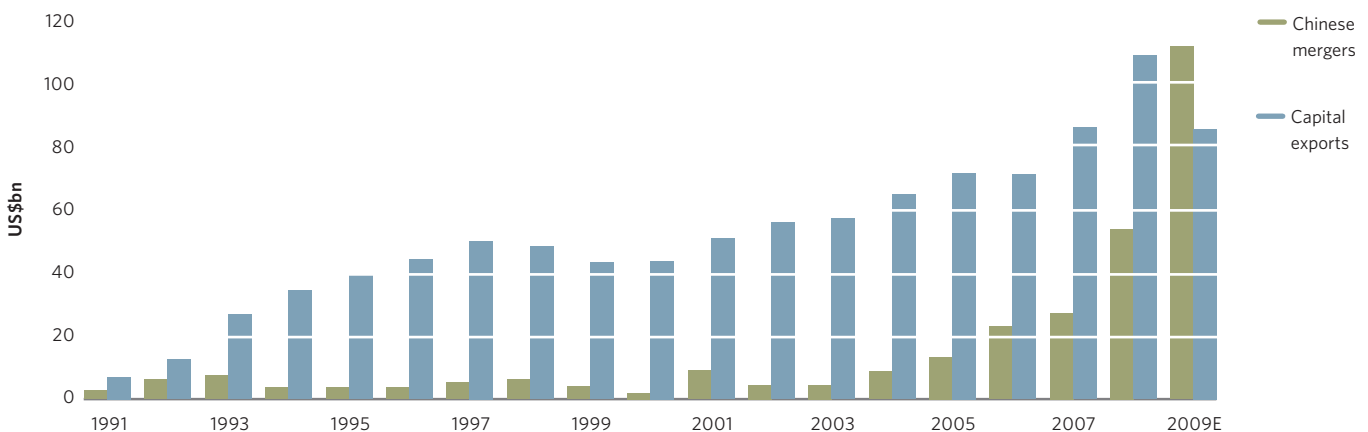
### A bright future

Although economic conditions will continue to remain challenging in the near term, over the longer term, Asia remains well placed in the global rebalancing process, thanks to better fundamentals for sustainable growth beyond policy-driven economic growth.

Financials remain supportive at the country, corporate and consumer level, and although fiscal balances will be under pressure this year and next, Asia is in much better shape than its developed nation counterparts. The outlook for income from developed Asian markets, where payout ratios are already higher than in western markets, looks particularly favourable in an uncertain world, especially when compared to government bond yields.

Currency appreciation from the region will be another driver of investment returns given our view on the US dollar. For these reasons, we remain upbeat on the medium to long-term outlook for Asia, where the growth paradigm remains unchallenged despite the uncertainties facing the global economy.

## CHINESE MERGERS AND ACQUISITIONS



Source: HSBC, Bloomberg, CEIC as at 16 July 2009

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