| Standard Chartered Global Focus |

Monthly Analysis of Economic and Financial Market Developments – 07 September 2010

The risk of a double-dip

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Genuine, but not inevitable

Highlights of the month

- Fears about sovereign debt were overblown, and a resurgence of inflation is unlikely. While the risk of a double-dip is genuine, it is not our base case yet.

- Strong policy responses could save the US from suffering a Japan-style malaise. We believe the Fed will reactivate quantitative easing later this year, keeping GDP growth at 1.0% in 2011 and barely averting a technical recession.

- While we expect a G3-led slowdown in H2-2010 as fiscal stimulus wears off, this will be balanced by an improving outlook in 2011 driven by emerging markets, especially Asia, where strong fundamentals will support domestic demand.

- The global economic slowdown is causing a major asset allocation switch into bonds, which are increasingly correlated to Asian FX, favouring South East Asian currencies. African currencies like the ZAR that are sensitive to bond inflows have also benefited.

- Risk assets have been characterised by 'trendless volatility' during the summer. We believe UST strength may create upside but is a short-term risk, especially for high-grade bonds. Commodity index investing remains steady but could pick up.

Important disclosures can be found in the Disclosures Appendix

Global

Gerard Lyons, Chief Economist and Group Head of Global Research
Standard Chartered Bank, United Kingdom
+44 20 7885 6988, Gerard.Lyons@sc.com

- **Downside risks in the US need to be taken seriously; this is a weak recovery**
- **The risk of a double-dip is genuine, but not our base scenario**
- **It is a tale of two worlds: we expect Asia, led by China, to outperform**

The 64 million dollar question

What are the big issues that we should focus on in the remainder of 2010? In many respects, they are the same issues that have already dominated throughout this year, and which, over the course of the northern hemisphere summer, have led to a subtle but significant shift in market sentiment. The last sixteen months have seen the benefits of a pro-growth policy stance across much of the world. In recent months, monetary policy has admittedly been tightened slightly in a number of emerging economies, and worries about sovereign debt have hung over fiscal policy in the West since the turn of the year. Notwithstanding that, since the successful G20 London Summit of April 2009, global policy has been geared towards ending the financial crisis, minimising downside risks and restoring growth. However, given the scale of what went wrong before – high debt, excessive financial leverage and scale of the derivatives market – it would have been asking too much for all the policy aims to have been achieved. The most success was seen in minimising downside risks. There has also been some kick-starting of the recovery in the West, but only some.

What happens when the impact of policy stimulus wears off?

As a result, what would have once been called, in the US or UK, the ‘64 million dollar question’ remains to be answered. This is the make-or-break question where you get the big prize if you get it right, or risk walking away empty-handed if you get it wrong. In the current climate, the question is, what will happen in the West once the impact of the policy stimulus of the last year starts to wear off?

Normally, at this stage of a recovery, confidence would be rising and economic momentum would be gathering. Alas, in the West, this is not proving to be the case in all economies. In particular, the US looks weak, and the UK, whilst stronger, looks fragile. Meanwhile, a number of the ‘Club Med’ European economies face a tough time as fiscal policy is tightened. In contrast, the euro area’s core economy, Germany, looks in much better shape, benefiting from an export-led recovery driven by China.

It is important to differentiate between the advanced, emerging and frontier economies

This last point is perhaps the key. It is necessary to differentiate between the West and the East, as their underlying dynamics are different. But at the same time, it is important to appreciate the inter-connections between the advanced, emerging and frontier economies. Most of the advanced economies face only a modest recovery. The recovery in emerging economies is stronger, and the more it is driven by domestic demand, the stronger it can be. Meanwhile, the frontier economies still possess the greatest catch-up potential, which should be seen in even stronger rates of growth than current levels.

Global (cont)

None of these groups is fully decoupled from the others – indeed, quite the opposite. The crisis showed that emerging economies were not decoupled, but better insulated. The same line of reasoning is valid now. With the West accounting for two-thirds of the world economy, and given the export-focused nature of many countries across Asia and emerging regions, it is still important to recognise the inter-connections. That being said, the emerging economies are becoming more dominant and more important, as well as more resilient. In fact, led by China, they are driving more of global growth.

The risk of a double-dip is genuine

In our view, fears about sovereign debt were overblown and a resurgence of inflation is unlikely; however, the risk of a double-dip is genuine, even though it is not our main scenario

First, let's take the West. The big question is whether there will be a double-dip? This has now replaced market fears of a sovereign debt crisis, although the reality is that weak growth is the biggest threat to government finances. In many respects, the fears about sovereign debt were overblown. They were more specific than generic in that certain countries, like Greece, were far more exposed than others. Nevertheless, many countries already plan to take action to retain market confidence. This is likely to weigh on the recovery and reinforce pressure for monetary policy and interest rates to remain accommodative. In turn, there are some who worry that there will be a resurgence of inflation. This is unlikely, in our view.

But the risk of a double-dip is more genuine, even though it is not our main view. A double-dip could occur if one of a number of factors occurs. A policy mistake – in particular a premature tightening of monetary policy – would be the main concern, although the markets are also concerned about the impact of tighter fiscal and tougher regulatory policy. Other factors include an external shock that led to, say, a rise in oil prices, hitting Western economies at a time when the policy cupboard is bare; or a loss of confidence, given that the outlook depends upon the interaction between the fundamentals, policy and confidence.

Although we are very upbeat about prospects for the emerging economies, and expect that they will eventually pull Western economies up, the near-term outlook for the West is still tough. The scale of deleveraging still points to a sluggish recovery in the US and the UK, as well as parts of the euro area. This is despite the scale of the policy stimulus, which has included fiscal boosts, low interest rates, liquidity provision, national bailouts of parts of the financial sector, and currencies that are probably weaker than they would otherwise have been (this is certainly the case for sterling and the euro). Policy makers did a good job of bringing economies back from the brink. But as the policy stimulus wears off, the extent to which the private sector can take up the slack has been constrained, given the overhang of debt from the crisis.

Levels are key

While q/q annualised GDP data show that the US is heading for a double-dip, y/y data show that the US is in a V-shaped recovery

Fears of a double-dip have been reawakened by the latest US growth figures. According to Bloomberg, the market consensus is for 3.0% US growth this year and 2.8% next. In contrast, our view is for growth of 2.5% this year and only 1.0% in 2011. It is quite possible, indeed likely, that there could be a quarter of negative growth within this annual rate. This is also likely to trigger talk of a double-dip. But the real message is the same as the one we have stressed before: a very weak,

Global (cont)

below-trend recovery as debt is repaid and as the economy restructures. This will have a bearing on global growth, capping the scale of the rebound elsewhere.

The US reports its GDP figures in a particular way: quarter-on-quarter growth figures, which are then annualised. This is not necessarily the wrong way, or the right way, to report the data; it is just a different way. It should not make any difference, but it unfortunately seems to when it comes to the focus on whether there is a double-dip. The latest US GDP data showed US growth 'slowing' from 5.0% in Q4-2009 to 3.7% in Q1-2010 and 1.6% in Q2. In short, a weak recovery. But if the US reported its data on a year-on-year basis like the UK – and indeed many others – do, this would have shown growth picking up from 0.2% in Q4-2009 to 2.4% in Q1-2010 and 3.0% in Q2-2010. In fact, on a graph, it would have shown a traditional V-shaped recovery.

US output dropped more in the current recession than in previous ones, but the recovery is strong thanks to an aggressive policy response

Given all this confusion, I prefer to look at levels, and then compare recoveries. Let's take the last three US recessions. The early 1980s saw a genuine double-dip. The economy peaked in Q1-1980. It basically then fell in 1980, picked up in 1981 and fell again in 1982. The recession of the early 1990s was not a double-dip. Table 1 below allows a comparison. Economies usually grow. So at the bottom of the latest recession in 2009, the US economy was just over three-fifths bigger than it was at the bottom of the early-'90s recession. To allow a comparison of recessions and recoveries, the GDP data has been indexed with the bottom of each recession shown as 100 in the middle of the table. The previous peak (that is, the quarter when the economy peaked before it fell into recession) is shown in the second column. Thus, we can see that in the latest recession, the fall in the economy was more severe than in the early '80s and early '90s. But perhaps more interestingly for the present discussion about double-dips, one year into the recovery, the US economy is 3% above its floor. At the corresponding stage of the 1990s recession, it was 2.6% above its floor. In the early '80s recession, the economy hit bottom in Q3-1980; output then rebounded 4.4% in that first year, leaving GDP higher than its pre-recession peak (104.4 in Q3-1981 versus 102.3 in Q1-1980). Then trouble struck, and there was a double-dip. And after three years, the US economy in Q1-1983 was barely bigger than in Q1-1980 (102.9 versus 102.3).

Table 1: Various US recessions compared

Period	Previous peak	Bottom	1 year after bottom
1. Early '80s, 1st leg	102.3 (Q1-1980)	100.0 (Q3-1980)	104.4 (Q3-1981)
2. Early '80s, 2nd leg	103.0 (Q3-1981)	100.0 (Q1-1982)	101.4 (Q1-1983)
3. 1+2 combined	102.3 (Q1-1980)	100.0 (Q3-1980)	102.9 (Q1-1983)
4. Early '90s	101.4 (Q2-1990)	100.0 (Q1-1991)	102.6 (Q1-1992)
5. This recession	104.3 (Q4-2007)	100.0 (Q2-2009)	103.0 (Q2-2010)

Note: GDP at the bottom of each period is indexed to 100;

Source: Standard Chartered Research

Likewise, in the euro area and the UK, the recovery also has a V shape to it. The message is that the policy stimulus is allowing a recovery. But given the scale of the recession and the extent of the stimulus provided in the West, it is a weak recovery, and output has not returned to its pre-crisis level.

Global (cont)

Policy makes the difference between the US and Japan

The US is different from Japan

This has also triggered the question of whether the US could be like Japan. One similarity is that the recovery will be sluggish and that interest rates have to stay low for a prolonged period. Also, inflation is not a problem and deflation is a greater risk. There are, however, some meaningful differences. Japan's bubble burst in 1990, but it was not until 1997, not too long before Japan's financial crisis at the end of 1998, that employment peaked. Quantitative easing (QE) did not start until 2001, and even then it was less aggressive than seen in this financial crisis. The policy response in the US this time has been far more dramatic and focused – and, most importantly, timely and part of a consistent policy mix. In Japan, fiscal policy was tightened in 1997-98. In the US, the combined fiscal and monetary stance now is far more accommodative, and some of the fiscal boost – perhaps as much as one-quarter – has yet to feed through. The trouble is, at the state level, fiscal policy in some areas is being tightened to achieve balanced budgets. But perhaps of equal significance is that Japan – like the US – faced what I called both a demand-side and a supply-side problem. Japan focused solely on demand-side solutions, not on supply-side solutions. Yet demand- and supply-side problems required both demand- and supply-side solutions. Putting it another way, Japan never fully undertook the structural changes it needed to make. That is likely to be a big difference with the US. There, one can already see households and firms coming to terms with the need to change. It will still be a painful adjustment for the US – it couldn't be anything else – but this should prevent a 'lost decade' in the US. Perhaps just a few lost years instead.

Inflation is not an issue in the West

The bullish flattening of the US yield curve is fully justified

In this environment, the bullish flattening of the US yield curve is fully justified. Although yields may be low, the expected capital gains at low yields are a great attraction and explain the continued shift into Treasuries, and indeed many other government bonds. Moreover, supply is not the issue, the threat of deflation is. And yet there is little reason to worry about US inflation. There is no pricing power in the economy – wages are not rising, unemployment is a concern and there is spare capacity. Retailers and producers have to keep prices down to stay in business. This points to a difficult 2011, as workers will not see wages rise and firms may anticipate sluggish demand. As a result, private-sector investment may not only be small in scale, but it may also be aimed at enhancing productivity, not investing in new capacity. All in all, this suggests a difficult political period for the Obama administration, and not only justifies the Fed keeping interest rates low throughout 2011 and probably 2012-13, but should also point to further QE.

What does this mean for equities? There has been increased volatility and uncertainty in recent weeks. During Japan's 'lost decade', the equity market suffered badly. But in the US, it is a tale of two worlds: big firms and big banks are in better shape than small firms and small or regional banks. As US firms have taken action to address supply-side issues, employment has suffered, but productivity has risen sharply. Overall, despite the challenges, the US is recovering, though it is a slow, drawn-out process.

Global (cont)

China is not a bubble economy

The other big issue has been China. I continue to be surprised that more people do not ask me about the upside for China than about the downsides. The summer marked a high in the number of people asking, is China a bubble about to burst? There is nothing wrong with asking this question. My reply is no. In my view, China is not a bubble economy, but it is an economy prone to bubbles. And there is a big difference. That is, given the lack of depth of its capital markets, it will see bouts of asset-price inflation in property and equities. Indeed, this partly explains why the economy has slowed in recent months as the authorities took action to cap overheating. Now that the economy is slowing, we should be neither surprised nor alarmed. If anything, we should be pleased! It shows that the authorities are still able to control the economy through their policy levers. Thus, as we move into 2011, it would not be a surprise if policy were relaxed to give the economy another lease of life and avoid any additional deceleration.

Of course, when one visits China, one wonders why it ever needs to be given a lease of life. The place is buoyant. There was a big hit to exporting areas as the crisis unfolded. More recently, there has been upward pressure on wages in regions like the Pearl River Delta. But many other regions are still strong and are attracting new investment as businesses migrate from the coastal areas into the lower-cost interior. GDP growth was 10.3% in Q2-2010; exports were up 38% y/y in July, imports 23.2%. Loans are growing at 18.4%, retail sales at 23.3%, industrial production 13.4% and money supply 17.6%. So even though the authorities have engineered a slowdown, it is no more than that. And if growth does weaken further, we expect policy to be relaxed. Hence, we continue to be optimistic about prospects in China. This is significant for many other countries, both directly in terms of trade and indirectly in terms of the impact on confidence.

We are upbeat about growth prospects in 2011, especially across the emerging markets

In recent weeks it was announced that China had finally overtaken Japan as the world's second-largest economy. Although this in itself should not be a surprise, it is worth pointing out how sizeable the Asian region now is: the economies of China and Japan are both about USD 5trn in size, ASEAN about USD 1.5trn, and India USD 1.2trn; add in the other sizeable economies, such as South Korea and Pakistan, and one soon reaches an economic region almost the size of the US, which is about USD 14.2trn. And whilst the US is growing at a sluggish pace, Asia (even allowing for Japan) is growing at a much faster rate. Our forecasts suggest Asia (including Japan) will grow 5.3% in 2010 and 4.6% in 2011. The leaders will be China and India, both up 8.5% next year, with Indonesia up 6.5% and South Korea 4.1%. Given what is happening in the US, these are solid growth rates. They could yet be higher, but that would depend on robust confidence and domestic demand. We remain upbeat about Asia's prospects.

Global (con'd)

The fear of inflation triggers tightening in the East

What does this mean for policy? The tale of two worlds we have spoken of before remains very apparent in monetary policy. Whilst the West needs to keep rates low, across Asia, monetary policy is being tightened gradually in what is seen as a normalisation of rates. Although commodity price inflation is an ongoing focus – food and energy prices are always the main worry, and supply risks could push food prices even higher in the coming months – headline inflation rates paint a mixed picture. Rather than focus on the whole world, let's take Asia as an example. Using data for July, the latest month for which annual inflation rates are available across all countries, only three economies appear to have high inflation: India, at 10%; Vietnam, at 8.2% (although the rates for both of these countries are below recent highs of 11.2% in April and 9.5% in March, respectively); and Indonesia at 6.4% and rising. Elsewhere, the inflation numbers are not alarming: China 3.3%, Hong Kong 1.3%, Taiwan -0.5%, South Korea 2.6%, Malaysia 1.9%, the Philippines 3.9%, Singapore 3.1% and Thailand 3.3%.

In South East Asia, for instance, Malaysia held interest rates steady at its last meeting, after hiking in July along with Thailand and Vietnam. Singapore has become more hawkish on its currency. Indonesia, with creeping inflation, is under pressure to tighten. In the Philippines, rates are on hold given the balanced outlook as rising agricultural prices contrast with a recent weakening of imports, which suggests a slowdown in the processing trade sector.

A slowdown in H2-2010, led by the West, will be balanced by the improving outlook in 2011, driven by the emerging markets, especially Asia

In South Asia, meanwhile, India leads the way in hiking, but it probably has more to do. Inflation is stubborn. Yet recent economic data suggest that the central bank will move cautiously – slowing growth in household consumption sounds a note of caution, even as robust industrial and service-sector growth kept the economy growing at 8.8% in the April-June quarter, following 8.6% the previous quarter. Pakistan has also been hiking, but the horrific scale of the floods may weigh on future policy and prospects. Sri Lanka's central bank, in contrast, followed its July rate cut by cutting the reverse repo rate in August to a six-year low of 9% to spur lending and overall growth.

In North East Asia, Taiwan and South Korea have hiked, although rates remain relatively low. Concerns about a double-dip have caused Taiwan and Korea to avoid aggressive tightening, but strong exports and robust domestic demand justify further, albeit gradual, hikes. Meanwhile, Japan continues to battle a stronger yen. For China, domestic factors are very much dictating policy. This suggests fine-tuning, not aggressive tightening, in the months ahead.

Overall, the global slowdown that seemed likely in the second half of this year is materialising. But for now, it seems to be no more than that. And it is led by the West. Just as it is important not to be complacent about the downside risks, it is also important not to lose focus on the longer-term shifts. As we move into 2011, we expect better Asian fundamentals and recovering world trade to focus attention on the upside risks in many parts of the emerging world.

Asia

Tai Hui, Regional Head of Research, South East Asia
Standard Chartered Bank, Singapore
+65 6530 3414, Tai.Hui@sc.com

- **Asian exports to be tested again by slowdown in US and Europe**
- **Large swings in growth are likely to persist for small, open economies**
- **Consumption and fiscal tools should help to offset export weakness**

Adverse trade winds

Domestic demand is expected to come to Asia's rescue once more if export performance deteriorates

Domestic demand should help to break the fall

The global economy is slowing, and this will be of concern for Asian economies to varying degrees. US economic growth eased to 1.6% in Q2-2010, and further deceleration is on the cards. Europe is expected to go through a similar phase despite strength in its core economies. These developments reinforce our long-held view that the strongest phase of Asia's economic recovery is behind us, and that growth will return to trend in H2-2010 and 2011. This may prompt some central banks to take their foot off the monetary tightening brake temporarily. Asian governments also have the ammunition to implement another round of fiscal stimulus, if required.

With the global environment looking uncertain once more, we expect small, open economies such as Hong Kong, Singapore and Taiwan to experience a more volatile period than domestically oriented economies such as China, India and Indonesia.

Intra-regional trade is a friend indeed

So far in 2010, Asia's export recovery has been largely driven by intra-regional trade, with the US and Europe making limited contributions. Chart 1 illustrates that the US and Europe were directly responsible for less than 15% of Asian economies' export growth in H1-2010 (with the exception of China and the Philippines). 2010 is turning out to be another mediocre year for Asian exporters looking forward to the Christmas season, as demand from the West remains patchy at best and importers are unwilling to commit to large orders. For North East Asia, China has played a particularly important role in the export recovery. Hong Kong derived 71% of its export growth in H1-2010 directly from the mainland. China was also an important driver of export growth for Taiwan (37.8%) and South Korea (33.9%).

While North East Asian economies have depended on China for their export recovery, intra-regional trade within ASEAN has been the most prominent driver of export growth in ASEAN economies. Thailand has benefited the most, with other ASEAN markets accounting for 37% of its export growth in H1-2010. Singapore (36%), Malaysia (33%), Indonesia (27%) have also seen significant boosts from within the region. The Philippines was the exception, with intra-ASEAN trade explaining only 19% of its export growth in H1-2010.

In the event of a slowdown in the US, Europe or China, our analysis shows that North East Asian economies are more vulnerable than ASEAN countries. Hong

Asia (con'd)

Governments in the region are rolling back fiscal and monetary stimulus, but this can be reversed to support growth if required

Kong, Taiwan and South Korea all have high exposure to external trade relative to the size of their economies, so their trade and economic growth performance will be more synchronised with the global environment.

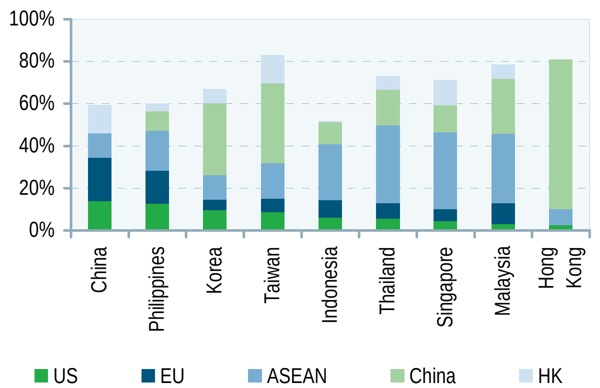
Counting on the big spenders and stimulus

With exports to the West likely to slow – and possibly stall – in late 2010 and early 2011, domestic demand will once again play a crucial role for Asia. As shown in Chart 2, private consumption and investment played an important role in driving economic growth across Asia in H1-2010. This was particularly apparent in India, the Philippines, Taiwan and Hong Kong. In Hong Kong, ample liquidity conditions are likely to continue to support the local real-estate sector and sustain domestic consumption. However, we are more cautious on investment in Taiwan, as the outlook for the tech sector remains cloudy, and capacity replacement and upgrades are probably not forthcoming. Singapore's performance shows that it has depended heavily on exports as a source of growth, leaving it vulnerable to a moderation in external demand.

In sum, we continue to believe that domestically driven economies with less export exposure are likely to outperform export-oriented economies as the global economy slows. This implies that Indonesia, China and India may see more stable, albeit easing, growth in H2-2010. Singapore, Taiwan and Hong Kong could see much larger swings in their growth performance.

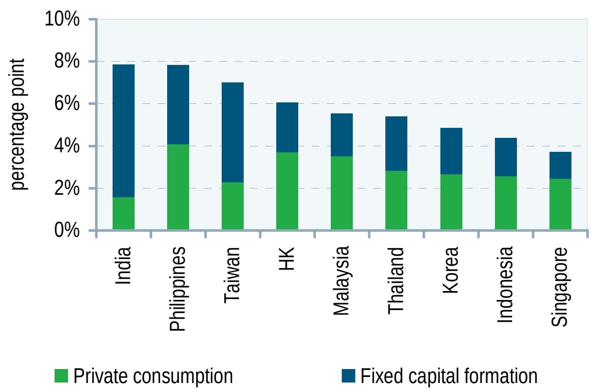
Asian authorities can opt to reduce such volatility through fiscal or monetary policy, and they have the means to do so. Governments in the region are still rolling back fiscal stimulus, and central banks are on the path to monetary tightening. While we do not expect a re-introduction of fiscal and/or monetary stimulus at this stage, Asian authorities certainly have the capacity to do so if required, thanks to their relatively low debt-to-GDP ratios and pre-emptive moves to normalise interest rates during the recovery phase. In addition to the consumption strength seen over the past two years, governments' ability to reflate their economies is another reason for investor optimism towards Asia.

Chart 1: Sources of Asian export growth



Sources: CEIC, Standard Chartered Research

Chart 2: Contributions to H1-2010 GDP growth



Sources: CEIC, Standard Chartered Research

Africa

Razia Khan, Head of Macroeconomic Research
Standard Chartered Bank, United Kingdom
+44 20 7885 6914, Razia.Khan@sc.com

- **Africa will not be spared the need for post-crisis fiscal adjustment**
- **Our analysis suggests that the impact on growth will vary widely**
- **Reforms and structural shifts may provide a sufficient offset to reduced spending**

Assessing the growth impact of fiscal adjustment

The mood of the moment is defined by the need for fiscal adjustment; as the S&P downgrade of Ghana shows, Africa will not be spared

Fiscal adjustment remains a key focus as risks to the global economy are assessed. The sharp reduction in deficits that will be required from the European periphery over the coming years is driving expectations of weak growth in these economies. In Africa, however, expansionary fiscal policy was identified as a key success of the crisis-response by policy makers. In the past, declines in global growth were always reflected in commodity-dependent Africa. This time around, the decline in aggregate GDP growth was less severe in Africa than elsewhere. Positive growth momentum before the crisis had something to do with it, but the expansionary fiscal stance in response to the crisis was credited as the main factor behind Africa's improved growth performance.

Expansionary fiscal policy was seen as one of the successes of Africa's post-crisis response; now, there is pressure to rebalance

However, post-crisis Africa will not be immune to the need for fiscal adjustment. This was brought home definitively by S&P's recent decision to downgrade Ghana's credit rating to B from B+; the rating agency cited reduced fiscal flexibility, notably the "cumulative effect of a large and erratic fiscal deficit", as the principal reason. Rating agencies do occasionally get things wrong – S&P downgraded Nigeria's rating from BB- to B+ last year following regulatory intervention in undercapitalised financial institutions, a move which has had minimal fiscal implications so far. Yet the downgrade of Ghana, even as its fundamentals have improved since the double-digit twin deficit crisis of 2008, serves as a reminder that fiscal positions in rapidly growing Sub-Saharan economies will be subject to greater scrutiny. After all, it is the mood of the moment that matters.

Although African economies generally have low levels of public debt, other constraints – revenue collection, ODA and access to international capital markets – are behind the urgency to cut deficits

While public debt ratios have generally been more favourable in African economies than elsewhere – the result of external debt forgiveness and relatively shallow domestic capital markets – reduced access to international capital markets for funding, potential declines in official development assistance (ODA), and generally lower revenue collection ratios are all seen as constraints. Therefore, even African economies will be pressured into reducing their fiscal deficits. It is worth considering the impact of steep fiscal adjustment on growth.

The picture is a mixed one at best. In Ghana, recently downgraded because of fiscal imbalances and substantial official arrears (thought to account for as much as 5% of currently measured GDP), significant expenditure reduction will be difficult. Much government spending reflects either pre-committed capex or politically sensitive expenditure items. Nonetheless, the authorities are committed to further fiscal consolidation, and with growth set to outperform as Ghana becomes an oil producer, the GDP impact of such consolidation is likely to be minimal. Exports should increase by at least 50% in 2011 as oil production gets

Africa (con'd)

underway. The growth impact is more difficult to quantify, as Ghana's GDP data is soon to be revised – but it will be substantial (officials suggest GDP growth of 20%).

Ghana's oil production should offset the GDP impact of fiscal adjustment; in Nigeria, the questionable quality of increased spending means any rebalancing will likely have a limited effect on growth

Nigeria will see substantial fiscal deterioration this year. Taking into account the revised 2010 budget and supplementary budgets, spending may rise by over 50%, and the deficit may exceed 6% of GDP. Nonetheless, given upcoming elections, such spending is seen as a one-off. Although the depletion of the country's excess crude earnings is a concern, plans to establish a sovereign wealth fund to save future oil windfalls may be a significant mitigant. Given the expected passage of the Petroleum Industry Bill, which will boost revenue even if a watered-down version is passed, the revenue outlook – based on expectations of future oil earnings – remains sound. Fiscal rebalancing will be required after the 2011 election, but the cutback in oil-revenue sharing between the three tiers of government is unlikely to have a severe effect on growth, as much of the spending of questionable quality in any case. Significantly, it may be offset by successful power-sector reforms.

Kenya, with its deeper domestic debt markets, has earned itself the space to increase spending, while Botswana will find itself more constrained

Not all African economies are feeling the pressure to rein in deficits. Despite an IMF recommendation for Kenya to remove its fiscal stimulus, the FY11 deficit is set to widen. With a revenue collection ratio that is comparable to more developed markets, and deeper domestic debt markets than other African frontier markets, Kenya has perhaps earned the fiscal space to increase spending. This contrasts sharply with Botswana, traditionally known for its fiscal conservatism. The global economic crisis and a slump in mining receipts saw Botswana's fiscal deficit balloon to an estimated 13% of GDP. Increased government spending prevented the crisis from having a more severe effect on the non-mining economy. Some development expenditure was redirected towards new export sectors (notably power) in the hope of expanding the country's narrow economic base and preventing similar crises in future. Even so, Botswana has promised a significant fiscal adjustment, with the restoration of a balanced budget by FY13. In an economy where government spending (traditionally 40% of GDP) has provided the main impetus to non-mining growth, the fiscal adjustment will be keenly felt. Diamonds may be seeing a recovery of sorts, but a recessionary feel may prevail for some time to come.

South Africa is set to see a steep rise in debt-servicing costs, but the outlook may not be as pessimistic as National Treasury forecasts suggest

Finally, in South Africa, the expansionary fiscal stance and the related increase in public debt levels will see spending on debt servicing rise faster than other components of expenditure in the years ahead. Given that the pre-crisis decline in debt-service costs allowed for higher expenditure on infrastructure and social grants, growth is likely to pay the price for any fiscal adjustment. For now, somewhat curiously, fiscal revenue continues to outperform despite an otherwise weak economic performance. The future may not be as bleak as officially projected.

MENA

Marios Maratheftis, Head of Research, West
Standard Chartered Bank, UAE
+9714 508 3311, Marios.Maratheftis@sc.com

Nancy Fahim, Economist, MENA
Standard Chartered Bank, UAE
+9714 508 3647, Nancy.Fahim@sc.com

- **Iraq is in the headlines, this time for more positive reasons**
- **Inflation should remain low in the region, with the exception of Saudi Arabia**
- **No significant improvement in credit growth seen in the GCC**

Iraq, inflation and GCC markets

Thin markets but important events

Iraq has reached two important milestones: high participation in free elections and the end of US military operations in the country

Summer is usually characterised by thin trading in the region, and this year has been no different. But the summer has been far from uneventful. Iraq is in the headlines, this time for positive news. Gulf Co-operation Council (GCC) economies have improved the availability of data, allowing us to make more accurate assessments of inflation and liquidity and their impact on markets.

Keeping an eye on Iraq

Iraq reached two important milestones this year: a free election and the end of US military operations in the country. The security situation still faces challenges, but Iraq is making progress.

Growth in Iraq will be high and will be driven by demographics, the oil sector and infrastructure investment

Iraq held parliamentary elections in March, deciding the 325 members of the Council of Representatives, who elect the prime minister and president. The Iraqi National Movement headed by former interim Prime Minister Ayad Alawi won 91 seats, marginally beating the opposition State of Law bloc (89 seats) headed by Prime Minister Nouri Al Maliki. With neither party enjoying an absolute majority and with no coalition having been formed, a deadlock has ensued.

The positive news is that the Iraqi public has passed the democracy test. Turnout for the parliamentary elections was 62%, and none of the ethnic groups staged boycotts. This is a positive development that reflects the progress made in recent years.

On 31 August, President Obama announced the end of US military operations in the country. This signals the end of the war, and while security challenges remain, this development has been welcomed by the Iraqi government.

We expect Iraq's economic growth to rebound to 7.0% in 2010. The three main medium-term growth drivers will be demographics, the oil sector and investment in infrastructure. In terms of demographics, Iraq has a population of 31.2mn people, 40% of them under the age of 40. Oil production has already returned to pre-war levels, and with proven oil reserves of 115bn barrels, the sector is attracting significant investment.

Inflation trends

The main drivers of inflation in the region are housing costs and food prices

Inflation in the region is driven by housing costs and food prices. Saudi Arabia and Jordan are experiencing rising inflationary pressures, the former mainly because of a tight housing market and the latter mainly driven by food prices. On

MENA (con'd)

the other hand, Qatar is in deflation and the UAE is experiencing disinflation as a result of housing-market corrections in both countries. Qatar recorded average deflation of 3.63% in the first seven months of 2010. In the UAE, inflation during the same period averaged 0.49%. Given the severity of the UAE's housing-market correction, we would have expected UAE inflation figures to be lower than, or at least to match, those of Qatar. Official UAE statistics likely underestimate deflationary pressures emanating from the housing market.

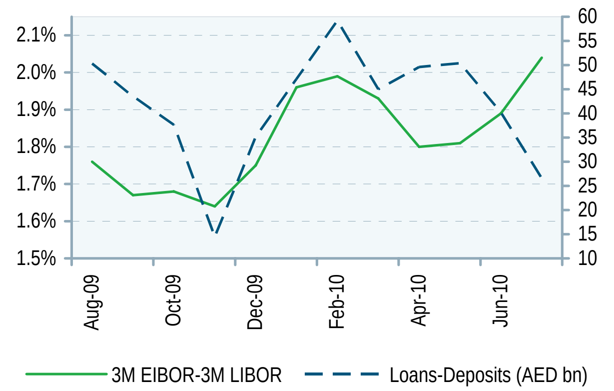
Credit growth and markets

UAE interbank rates have risen, despite the narrowing of the loan-deposit gap

Credit growth in the region is generally tight. Saudi Arabia's banking sector enjoys ample liquidity; the lack of private-sector credit growth there can be attributed to low confidence. Qatar's central bank reduced the overnight rate from 2% to a still-high 1.50% in August this year. Deflation suggests further scope to reduce the overnight rate to stimulate credit growth.

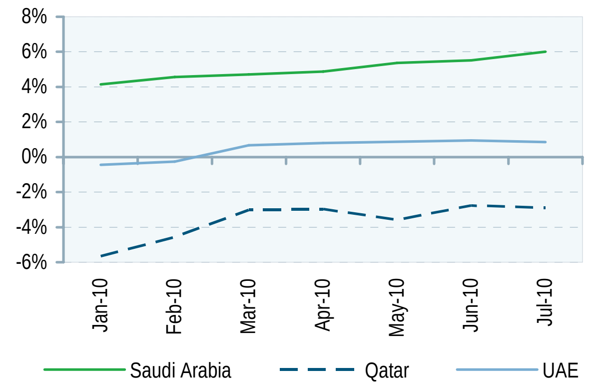
In the UAE, loans continue to exceed deposits, keeping interbank rates higher. It is interesting to note, however, that while the loan-to-deposit gap has been narrowing since April 2010, the disparity between UAE 3M EIBOR and US 3M LIBOR has persisted and even widened. The spread between EIBOR and LIBOR widened sharply following the surge in US LIBOR rates in March. US LIBOR rates have been coming off since July and have now normalised, but the EIBOR-LIBOR spread has not returned to pre-March levels. Domestic market sentiment in the UAE is expected to normalise, which should help to narrow the gap between EIBOR and LIBOR towards year-end.

Chart 1: EIBOR-LIBOR differential and loan-to-deposit gap



Source: Standard Chartered Research

Chart 2: Monthly inflation *(y/y %)*



Sources: Standard Chartered Research

Commodities

Michael Haigh, Head of Commodities Research
Standard Chartered Bank, Singapore
+65 6530 8113, Michael.Haigh@sc.com

- **Commodity and equity markets continue to be highly correlated**
- **Supply concerns in wheat show that fundamentals can prevail**
- **Commodity index investing remains steady but could pick up**

Correlations continue

Macro markets will provide direction

Until supply weakens or demand picks up, commodities and financial markets will move together

Equities and commodities continue to move along parallel tracks as macroeconomic variables influence commodity market sentiment. For most commodity markets – in particular oil – we believe that wider financial markets will continue to provide direction in the near term, especially given high inventory levels for crude and distillates, combined with modest growth prospects. Until the supply side weakens or demand picks up, the broad commodity markets may travel down a parallel track with the equity markets. Fundamentals may take a back seat.

Physical and financial markets influence correlations

With spikes in commodity prices, equities sell off as the threat of inflation looms

Physical markets can help explain the co-movement. Right up until the late 1990s, there was excess capacity for most commodities. This was brought about by advances in technology, as well as new discoveries that increased supply at a lower real cost. In such an environment, any significant rise in commodity prices could be attributed to supply-side shocks (the Gulf War, Arab oil embargoes, etc.) as opposed to fundamental shifts in the overall supply and demand balance. Such supply shocks resulted in commodity price increases, bringing the threat of inflation, which would ripple through to a decline in the equity markets – resulting in a negative correlation with commodity price movements.

By the late 1990s, years of underinvestment in the supply chain, combined with steady demand growth (particularly from Asia), meant most excess capacity had been absorbed. As such, changes in global economic activity have a deeper impact on commodity price cycles. While supply shocks may lead to periods of negative correlation, equity markets and commodity markets can be driven by a common factor, namely economic activity.

So do financial markets

If stock movements result in margin calls, commodities may sell off to raise cash for the calls

From the non-physical side, the impact of financial institutions on commodities has reduced the scope for cross-market arbitrage opportunities, in the process linking equity and commodity markets more closely. Moreover, because financial institutions may respond differently than commodity traders to stock-market fluctuations, prices may align. Specifically, if downward movements in the stock market force financial institutions to liquidate positions in commodity markets in order to raise cash for margin calls, markets may move in tandem.

Commodities (con'd)

Fundamentals prevail in wheat, sidelining macro influences

Uncertainty about the drought in Russia lifts wheat

For some commodities, macro drivers have been sidelined and fundamentals have prevailed in recent weeks. In the grains complex in particular, price stability followed by a recent noticeable price rise has illustrated the limited influence of other markets – such as crude oil and the US dollar (USD) – which can be significant macro drivers of the complex. Wheat prices especially have soared recently, resulting from uncertainty over the Russian wheat crop due to a drought. An export ban has meant that grain-exporting companies that have contracted to buy Russia grains have scrambled to source them elsewhere. Adding to the uncertainty have been recent weather concerns in Australia and Argentina. The price response to this (overdone, in our opinion) is a classic example of a supply shock that sends commodities and equities on different paths (see Chart 2).

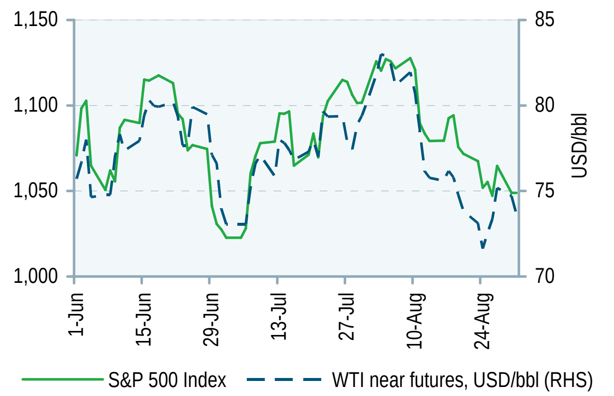
Commodity index investing remains steady but could pick up

Commodity index investing remains steady but could pick up

The release of the Commodity Futures Trading Commission (CFTC)'s report on index investments confirms that total index investments in commodities have remained steady. According to the data, total index investments stood at roughly USD 161bn as of the end of Q2-2010 (the most recent data available). This is almost exactly the same level reported at the end of Q1. The stability of the interest in commodities most likely reflects concerns about a double-dip for global economies – with investors sitting on the sidelines as a result.

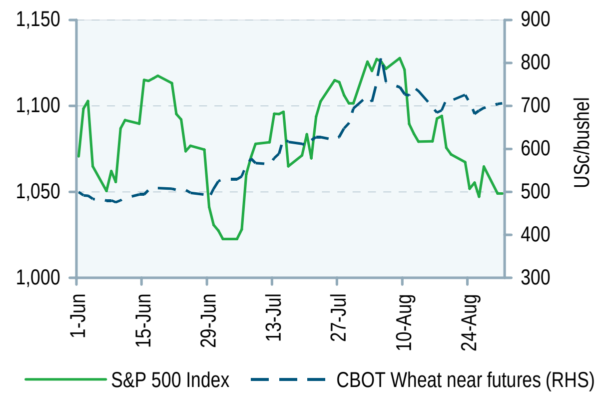
Going forward, we expect solid inflows into commodity via indexes to pick up in H2, as this provides exposure to stronger economic growth and can also provide a hedge against inflation. Long-only investments can only create upward pressure on the complex. While a plethora of alternative index products try to account for negative roll yield, contango and composition of index components (even going long/short at the same time), upward pressure on prices will prevail if inflows occur, regardless of these alternative products.

Chart 1: WTI vs. S&P 500



Sources: Bloomberg, Standard Chartered Research

Chart 2: Wheat vs. S&P 500



Sources: Bloomberg, Standard Chartered Research

Credit

Vijay Chander, Head of Credit Strategy
Standard Chartered Bank (Hong Kong) Limited
+852 3983 8569, Vijay.Chander@sc.com

- **Risk assets have been characterised by 'trendless volatility' all summer**
- **Weak macro conditions in the US have been offset by much stronger Asia/Europe**
- **UST strength may create upside but is a short-term risk, especially for HG bonds**

EM credit should benefit, despite volatile markets

Investor indifference, summer doldrums result in falling volumes

Retail investors are at their most bearish in several weeks, suggesting that the markets could rebound from here

As the summer draws to a close, the relative indifference of investors has caused asset markets to trade in wide ranges on declining volumes, without any clear signs of future direction. An element of risk aversion has appeared in recent days, causing us to adopt a slightly more cautious stance towards certain high-yield and bank Tier 1 issues that have performed well. However, asset markets are still within the broad range seen since at least the beginning of Q2-2010.

We remain constructive overall, given that a mix of technical indicators and relatively better macro conditions in emerging markets (EM) – in particular Asia, and more recently Europe – have offset the progressively weaker economic data out of the US. Turning to the technical indicators, retail investor sentiment, a contrarian indicator, is at its most bearish level in several weeks. According to the American Association of Individual Investors (AAII), bears outnumber bulls by nearly 30%, based on the results of its survey of 25 August 2010. This suggests that markets are set for a rebound, at least in the short to medium term.

Weak US macro data releases are offset by surprisingly strong European GDP growth figures

Regarding US macro data, the Philadelphia Manufacturing Index, which is considered a reliable indicator of current conditions in US factories, fell unexpectedly to -7.7 in the first half of August from +5.1 in early July (a negative figure implies a contraction). In contrast to the negative economic news from the US, several key euro-area economies recorded stronger-than-expected GDP growth – Germany's GDP rose by 2.2% in Q2-2010 and the Netherlands, Austria and France grew by 0.9%, 0.9% and 0.6%, respectively. In China, the Purchasing Managers' Index (PMI) rose to 51.7 in August from 51.2 in July. This was the 18th consecutive reading above 50, which suggests continued economic expansion. With macro data from Asia also showing considerable improvement, this should support markets going forward.

Flows into EM fixed income assets continue unabated

Despite heightened risk aversion to a range of risk assets, particularly equities, bond funds continue to attract considerable investor interest. According to the latest data from EPFR, inflows to higher-beta bond funds picked up considerably during the week ended 25 August from the previous week's levels. EM funds took in USD 1.07bn, while high-yield (HY) bond funds took in USD 603mn, up from USD 163mn the previous week. Bond funds overall saw cumulative inflows of USD 146.65bn during the week. The continuing attractiveness of bonds to investors should support credit as an asset class, particularly in the EM space, as

Credit (con'd)

this is one sector of the bond market that has enjoyed sustained inflows. (EM bond funds saw outflows in only two weeks since September 2009.)

Furthermore, it is worth noting that with money-market assets yielding close to 0%, the opportunity cost of not buying risk assets is significant and should cause a significant amount of cash to come off the sidelines. This also supports our constructive market stance.

Investors should exit fully valued Tier 1 names such as the ICICI perpetuals, and switch into the WOORIB Tier 1 paper

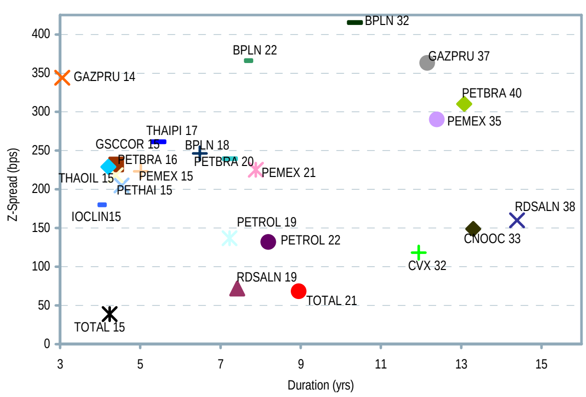
Limited room for spread compression, but Treasury rally is a plus

The strong rally in Treasuries seen in recent weeks, on the back of the expanded quantitative easing (QE) measures announced by the US Federal Reserve, should support credits at both the belly and the long end of the curve, even though Asia is trading at tight levels compared with other EM credits as well as corporates and banks in developed countries (see Charts 1 and 2 below).

Thus, there is not a whole lot of value here, at least based on credit spreads. However, even if spreads do not compress further, the continuing rally in Treasuries should support a number of cash bonds that have lagged in price terms – particularly high-grade (HG), select HY sovereign and quasi-sovereign issues. Thus, we believe that investors should focus on select names that meet these criteria.

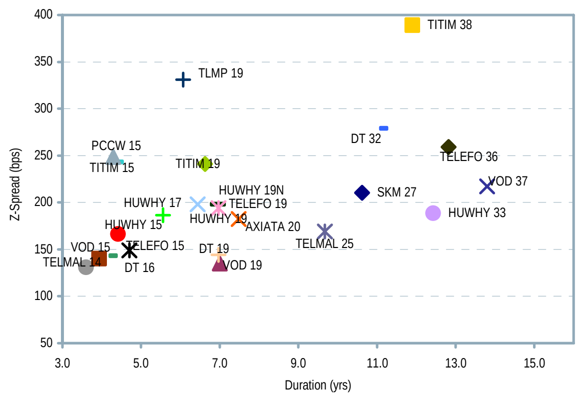
In particular, the PLNIJ benchmarks out of Indonesia, which have lagged the compression seen in PSALM relative to the Philippines sovereign, should outperform. Elsewhere, we recommend that investors exit positions in certain banking-sector Tier 1 issues, such as the 7.25% of ICICI 2049s, which appear fully valued, and other HY names with limited upside, such as the PRKSN '11s and the CFGINV '13s. On the other hand, investors should consider the higher-beta Tier 1 issues such as the WOORIB '37-17s and hold on to positions in Chinese property-sector names such as HPDLF and EVERRE, and Indonesian resources issuers such as BUMIIJ.

Chart 1: Asian oil and gas names look expensive



Sources: Bloomberg, Standard Chartered Research

Chart 2: Asian telecom benchmarks are also costly



Sources: Bloomberg, Standard Chartered Research

FX

Callum Henderson, Global Head of FX Research
Standard Chartered Bank, Singapore
+65 6530 3282, Name.callum.henderson@sc.com

- **The global economy is slowing, causing a major asset allocation switch into bonds**
- **Asian FX correlations with bonds have been increasing, favouring South East Asia**
- **African currencies such as ZAR that are also sensitive to bond inflows have gained**

Global slowdown and asset allocation

The hunt for yield is an increasingly important driver of FX

The global slowdown has led to a major asset allocation switch in favour of bonds

Global FX markets were choppy and trendless for much of August given the ‘unusually uncertain’ economic backdrop, and have reacted to each headline and piece of data. Stepping back a bit, it is clear that the global economy is decelerating rather than collapsing. Within this, there is some divergence. For instance, the US economy grew strongly in Q4-2009 and Q1-2010 but decelerated in Q2-2010. On the other hand, both the euro area and the UK saw stronger growth in Q2-2010. Overall, however, the story in the G4 is one of gradual deceleration after the initial post-crisis recovery.

Given the need for deleveraging in the US and Europe, the multi-year outlook for the G4 remains for weak growth, disinflation and very low yields. This is clearly a much more positive backdrop for fixed income than for equities, which is why we have seen a major asset allocation switch in favour of bonds this year. In our view, this is as much a secular as a cyclical trend, as pension funds are underinvested in fixed income relative to equities in the context of the 'new normal' of multi-year low growth. This has important implications for currency versus asset-market correlations.

AXJ currencies have typically been more sensitive to equities, but old correlations are breaking down

Asia ex-Japan (AXJ) is the emerging market (EM) region most sensitive to the global trade cycle. AXJ currencies have typically rallied during periods of global expansion and fallen in downturns. From a flow perspective, this is largely because foreign inflows into AXJ equities have typically had high correlations with AXJ currency performance. However, in the ‘new normal’, the hunt for yield is dominating the hunt for growth. Moreover, global investors continue to allocate increasingly to AXJ local debt markets, where they have historically been underinvested. As such, the correlations of foreign inflows to fixed income and AXJ currency performance have been rising, albeit to varying extents.

Foreign ownership of the Indonesian and Malaysian government debt markets has risen to 27% and 24%, respectively. Note that the Malaysian ringgit (MYR) and the Indonesian rupiah (IDR) are two of the three best-performing AXJ currencies so far this year. The other is the Thai baht (THB), which was up more than 3% in August alone. Having been as underweight the THB as they could get earlier in the year due to political tensions in Bangkok, asset managers are clearly moving back to neutral at the very least, even in the face of monetary tightening. In the near term, this outperformance is likely to continue.

FX (con'd)

South East Asian currencies offer relative value in Asia

Long South East Asia versus North Asia

The top-performing AXJ currencies this year have not only been more bond-related rather than equity-related currencies, they have also all been from South East Asia. Year-to-date to 1 September, the top five currencies against the USD are the MYR (+9.41%), THB (+6.80%), IDR (+4.41%), SGD (+3.93%) and PHP +2.47%). The Chinese yuan (CNY) is only up 0.22%. The Taiwan dollar (TWD), Hong Kong dollar (HKD) and Korean won (KRW) are all weaker on the year.

In our view, there are two reasons for this massive outperformance by South East Asia. First, as discussed above, higher nominal interest rates and bond inflows have been an increasingly important driver of currency performance. Second, due to trade ties, the economic slowdown in China has had a more negative impact on Greater China and South Korea than on South East Asia. Moreover, Taiwan is a very externally reliant economy, while South Korea is vulnerable to shifts in risk appetite because of its high leverage.

While North Asian authorities have generally been interventionist against currency strength, Indonesia, Malaysia and Singapore have all encouraged currency strength – albeit to varying degrees – to temper imported inflation. As the slowdown in China intensifies in H2, we expect this outperformance of South East Asian currencies to continue. Investor clients should respond by maintaining overweight allocations in South East Asia, while taking a more defensive stance on North Asia.

ZAR is benefiting from booming bond inflows; correlation with EUR-USD breaks down

African currencies have also benefited in the hunt for yield

The increasing importance of bond-market inflows has also been seen in Africa. The South African rand (ZAR) has in the past tended to be a typically cyclical currency, depreciating sharply when there is a slowdown in the global economy – more specifically, in key export destinations such as Europe and Asia – and appreciating as the global economy expands. However, this rather basic correlation has become more nuanced in recent years given the increasing importance of foreign inflows into South African government bonds (SAGBs).

On an absolute basis, the ZAR is only up 1.36% against the USD year-to-date, but this still makes it the top currency in Africa. Note that this outperformance has occurred at a time when the DXY (USD) index has strengthened on the year and EUR-USD is down 11.15%. Typically, USD-ZAR has been highly correlated with the DXY index – and inversely correlated with EUR-USD. The fact that USD-ZAR is lower on the year despite EUR-USD losing over 11% shows that this relationship has broken down. This is clearly due to bond inflows. So far this year, foreigners have bought a net ZAR 67bn of South African bonds – more than in any full year since the financial rand was abolished in 1995. Indeed, 2009 was the second-highest year for South African bond-buying since 1995, at ZAR 26.54bn.

The fundamental backdrop of high policy rates, low growth and declining inflation has been supportive of bond inflows, and thus of the ZAR. The near-term risk to this would be a rebound in inflation, but that does not appear likely for now.

Rates

Will Oswald, Head of Fixed Income Research
Standard Chartered Bank, Singapore
+65 6307 1527, Will.Oswald@sc.com

Christophe Duval-Kieffer, Head of Quantitative Strategies
Standard Chartered Bank, United Kingdom
+44 207 885 5149, Christophe.DuvalKieffer@sc.com

Edward Lee, Regional Head of Rates Strategy, Asia
Standard Chartered Bank, Singapore
+65 6530 3188, Lee.Wee-Kok@sc.com

- **US growth outlook is still weak, but risk/return in long UST positions has declined**
- **Pension fund demand may drive further long-term fixed income performance**
- **Many Asian markets now offer positive carry versus USTs**

Risk/return in long UST positions diminishes

Risk/return for USTs is deteriorating as recent economic growth data surprises less to the downside

The slowdown in the US economy has triggered a significant rally in bond markets, initiated between May and July by negative economic data surprises – particularly the slowdown in manufacturing highlighted by the June ISM manufacturing index.

The more recent rally between August and September has been driven by the pricing in of sharp disinflation/deflation fears, as reflected in the collapse in inflation breakevens. ‘New’ policies, such as the reinvestment of repaid GSE bonds or prepaid MBS in the Fed’s portfolio, have played only an indirect, signalling role in the rally, especially as far as disinflation is concerned. By contrast, lower mortgage rates and re-mortgaging have resulted in lower long-dated Treasury yields, once again proving the key role of ‘negative convexity’.

More recent economic data releases, notably the August ISM and payroll numbers, have driven a back-up in yields. While the fundamental factors underpinning long positions –- a sluggish recovery and weak inflation – remain, the risk/return profile of large long positions has deteriorated, also as a result of higher realised volatility. Uncertainty remains, and long/flattening positions have to be scaled down for now.

Demand also driven by pension funds’ secular rotation to fixed income

Pension funds’ rotation into fixed income assets is exacerbating UST curve flattening and adding to demand for Asian fixed income

Structural problems in US pension funds have also contributed. According to *Pensions & Investments*, the average allocation to global equities among the 200 largest US defined benefit schemes (dominated by state pension funds) is 51%, with fixed income allocations at just 29%. State pension funds are now facing the twin problems of no or limited inflows (as the poor quality of state finances has led Congress to approve postponement of inward payments), and an increasing number of retirees as demographics start to deteriorate. These factors will generate a switch into assets with higher current yields.

Private-sector pension funding ratios are also under stress. While the fixed income allocation is higher than that of state pension funds, at 38%, the equity bias is still high, at 51%. Under the Pension Protection Act of 2006 (PPA), liabilities must be discounted by AA yields. However, pension funds are allowed to use the high point from Q4-2008 as their discount rate until the end of 2010, reducing the mark-to-market loss. According to estimates from Mercer, a global consulting firm, the funding ratio of the 1,500 largest US-listed pension funds reached an all-time low of 71% at end-August 2010 if the AA yield were used (the previous low was 75% in December 2008).

Rates (con’d)

We believe that pension funds are now accelerating a long-overdue rotation into fixed income assets, creating a feedback loop in the breakdown in the historical correlation between USTs and equities. Given weak yield and duration availability in the US, the result has been continued flattening further out the yield curve and a search for yield and duration in a broader range of markets, including Asia.

Asian bond-UST correlation picks up amid improving carry differentials

Asia/UST correlation rises; many markets now offer positive carry

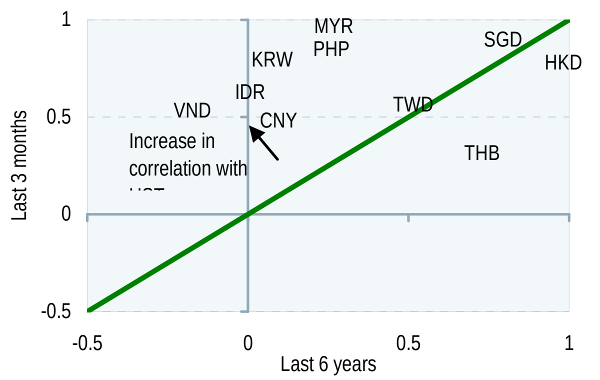
The correlation between Asian local-currency government bonds and USTs has picked up sharply over the past three months relative to historical trends (Chart 1). While the SGD and HKD markets have long had a close relationship with USTs, the IDR, PHP, MYR and KRW markets have shifted to a much stronger correlation.

This is partly explained by an increase in rates market correlations, but the higher carry (or, in some cases, the move from negative to positive carry) in Asian bond markets versus USTs has contributed to foreign demand (Chart 2). THB, MYR and CNY 10Y government bonds have switched from negative carry pre-credit crunch to positive carry, while even 10Y SGS are only 55bps below UST yields. This improved carry, and a bias towards longer-term Asian FX strength, have driven a sharp pick-up in inflows; in Thailand, this duration demand has occurred even as the Bank of Thailand (BoT) continues to hike rates. We see value in Asian domestic government bonds towards the longer end, where the flattening has not been as pronounced as in core markets or at the shorter end of domestic rate curves.

Idiosyncratic stories do remain, however, most notably in India and China. In India, foreign access to domestic government bonds is severely limited, while the Reserve Bank of India (RBI) has remained hawkish (although recent GDP data suggests that it might be cautious near-term, given the weak contribution from consumption). We look for 10Y GoISecs to underperform further.

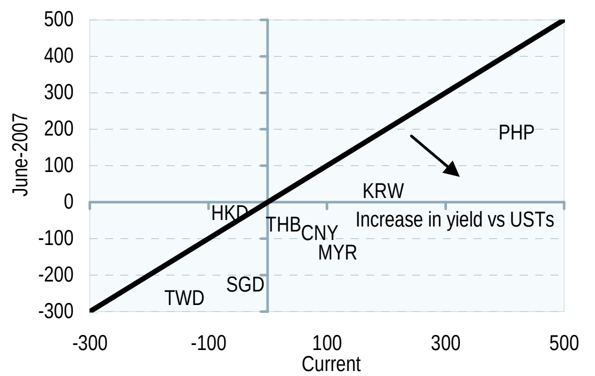
In China, we recommend receiving 5Y NDIRS, as the economy appears to have cooled recently, while banking-sector liquidity has risen. However, we prefer NDIRS exposure to bonds, as the shift in bank assets towards lower risk-weighted assets could be offset by recapitalisation needs.

Chart 1: Asian bonds’ correlation with USTs rises



Correlation of 10Y UST with 10Y Asian bond;
Source: Standard Chartered Research

Chart 2: Asian bonds offering more attractive carry



10Y Asian bond yield minus 10Y UST, in bps terms;
Source: Standard Chartered Research

Australia

Simon Wong, Regional Economist
Standard Chartered Bank (Hong Kong) Limited
+852 3983 8559, Simon.Wong@sc.com

- **Q2 GDP surged on export income; terms-of-trade gains are still the key story for H2**
- **Political deadlock has a short-term silver lining but breeds longer-term policy risks**
- **Renewed global weakness and wide credit spreads to push next RBA hike to 2011**

Trade windfall masks uncertainties

Export surge propels mid-year growth

Growth hit a three-year high in Q2 on exports, and terms of trade hit a new record

Against a backdrop of rising interest rates and waning fiscal stimulus, headline GDP growth in Q2 quickened to a three-year high of 1.2% q/q (see Chart 1). Echoing the quarter's streak of record-breaking trade surpluses, net exports were the unmistakable growth driver, making their first positive contribution to headline growth since Q2-2009. Yet the real surprise was consumption growth, which accelerated to its strongest pace since late 2007, suggesting a strong trickle-down effect from export earnings to the household sector thanks to a robust labour market.

While the headline GDP price deflator surged by an alarming 2.8% q/q, this was due to a jump in the export component. Local prices, as measured by the domestic final demand deflator, gained a modest 0.3% q/q. Sharply higher export prices are also captured in a 12.7% q/q jump in Australia's terms of trade (the relative price of exports versus imports), a gain that exceeded the previous peak in 2008.

Outlook hinges on persistent gains in terms of trade

A sustained gain in terms of trade could provide an income boost of 1% per quarter

The Q2 GDP report confirmed that a trade windfall has again come to dominate the cyclical outlook. This creates both upside and downside risks for the Australian economy. On the one hand, we estimate that the current gains, if sustained, could provide a boost of 1% to national income in each of the coming quarters – hardly a trivial sum.

Downside risks are likely to keep the RBA on hold this year

Yet on the other hand, renewed weakness in the global economy, if it materialises, threatens to cut short Australia's export boom. Recently reported declines in full-time employment and the trade surplus in July are a reminder of the potential volatility that lies ahead. Another worry for the financial markets is a prolonged period of risk aversion driven by banking-sector funding costs: Australian banks saw their credit spreads narrow in July but re-widen in August as concerns over Europe's debt crisis were replaced with concerns over renewed weakness in the US economy. Our view is that the 'fear factor' will be a recurring theme in coming months, and will keep the Reserve Bank of Australia (RBA) on hold for the rest of this year, notwithstanding the strong Q2 GDP performance.

Hung parliament opens era of reduced policy visibility

Adding to rising uncertainty over the global outlook, policy visibility has also deteriorated at home. Already, the Q2 GDP report alluded to a drag on growth from policy interference. The first instance of this was a marked slowdown in

Australia (con'd)

fiscal spending growth, the direct result of the government's unwinding of earlier stimulus. More importantly, the unfavourable reception of the proposed mining tax caused business investment to remain subdued; a sharp drawdown in inventories during the quarter echoed earlier reports of production stoppages by mining companies at the peak of the controversy over the tax.

A minority government could add to near-term policy risks

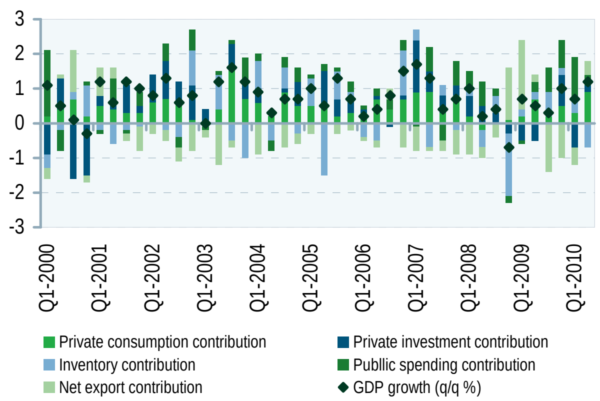
Unfortunately, the deadlock that resulted from the August federal election raises the risk of a prolonged period of policy uncertainty. Both the incumbent Labor Party and the main opposition Liberal/National coalition failed to secure the 76 seats in the House of Representatives needed to form a majority government. While negotiations continue, the country will likely have its first minority government in more than seven decades. This may be mildly supportive of near-term growth, as the new administration is likely to back down from the controversial mining tax and other draconian cost-cutting measures. The price will be a less convincing path towards fiscal consolidation.

Mixed lending trends underpin two-speed economy

The RBA could resume tightening in 2011

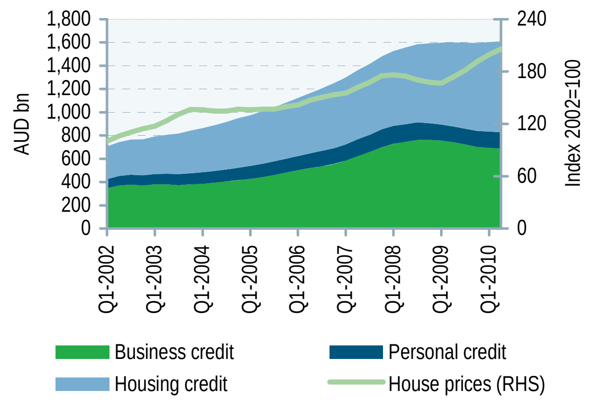
Beyond immediate fiscal performance, our main concern arising from the current political situation is the heightened risk of policy paralysis, which would prevent the new government from addressing more fundamental economic issues. In particular, the current resurgence in export income could rekindle fears of a surge in housing prices, potentially creating a 'Dutch disease'-type asset bubble (see Chart 2). Recent private-sector lending data also suggests that, while business borrowing dropped for an eighth straight quarter in Q2, housing loans continued to rise to a new high, highlighting the dichotomy in the current recovery. Unfortunately, given the previous administration's ill-fated mining tax proposal, the new government is unlikely to introduce further measures to address the structural imbalance. This would put an additional burden on the RBA to safeguard financial stability in the medium term. In our view, these developments argue for a more vigilant stance from the central bank once current external uncertainties recede. We expect the RBA to resume tightening next year.

Chart 1: Breakdown of GDP growth



Sources: ABS, Standard Chartered Research

Chart 2: House prices and credit



Sources: ABS, RBA, Standard Chartered Research

Brazil

Douglas Smith, Regional Head of Research, Latin America
Standard Chartered Bank, United States
+1 212 667 0564, Douglas.Smith@sc.com

- **Government candidate Dilma Rousseff is likely to win the election in the first round**
- **We do not expect any policy departure from the Lula government**
- **This means that fiscal challenges will remain a moderate concern**

The election will bring more of the same

Background

Much of the federal government and all state governors are up for re-election in October

On 3 October 2010, Brazilians go to the polls to vote for president, all 513 seats of the Lower House, two-thirds of the Senate (54 of 81 seats), governors of all 26 states and the federal district, and state legislatures. The winners will take office on 1 January 2011. In the run-up to the October 2002 election, two terms ago, the market was very concerned about the rise in the polls of candidate Lula da Silva of the Workers' Party (PT), who had espoused anti-market policies in the past.

Two terms and eight years later, President Lula enjoys very high popularity (76%), but he cannot run again because of term limits. His chosen successor is Dilma Rousseff (PT), who was Chief of Staff and Minister of Energy in Lula's government. The opposition candidate is José Serra, who has held many high-profile roles, including Governor of São Paulo state, Mayor of São Paulo, and Minister of Health and Minister of Planning in the previous administration.

The continuity candidate

There is a strong chance that Dilma will win in the first round, giving her a strong mandate

The popularity of Lula and his government is a huge advantage for Dilma. So too is the booming economy, with growth of over 6% this year. The latest polls show Dilma leading Serra by 24ppt, with 51% of voting intentions in the first-round vote, up from a 17ppt lead recently. While the market prefers Serra for president, Dilma's wide and growing lead has not hurt asset prices. Indeed, there is a strong likelihood that she will win in the first round if she obtains 50% plus 1 of the valid votes. Otherwise, the two leading candidates have a run-off on 31 October.

Between Lula's popularity and the positive economic outlook, Dilma is the natural beneficiary of the 'continuity' vote. In the not-too-distant past, Brazil experienced volatile growth and frequent boom-and-bust cycles owing to poor policies (Chart 1). Recently, volatility has been lower, and income and other measures of social well-being, such as health and purchasing power, have risen steadily (Chart 2). In fact, the economy only experienced a brief recession during the recent global financial crisis. By 2011, Brazil will be a USD 2trn economy, a doubling in five years.

This period of macro stability has boosted the ranks of Brazil's middle class. This has been compounded by the various social and income transfer programmes during the Lula administration, for example *Bolsa Familia* and *Minha Casa, Minha Vida*. Increases in the minimum wage have been important too, since benefits such as social security are indexed to the minimum wage. This progress has changed the dynamics of Brazil's politics and boosted the popularity of the PT.

Brazil (con'd)

No reason to expect significant policy changes

On a broad level, Dilma (or Serra) is unlikely to break much from the policies of the Lula administration, which have brought huge popularity to the government. Both candidates believe in active state involvement in the economy. Neither Dilma nor Serra would advocate legal independence of the central bank board or fixed terms for its directors. In fact, we would not be surprised to see criticism of central bank policies if interest rates were not cut quickly enough. Both candidates would also try to prevent the Brazilian real (BRL) from appreciating too strongly.

Furthermore, we do not expect any major initiatives on energy, labour, or public expenditure/tax reform. Lula did not move forward on these contentious issues even with very high approval ratings. Neither the Dilma nor Serra campaign has advocated any major changes. Dilma believes that the key source of growth will be consumption via social programmes and income transfers, which the public banks can facilitate via credit extension. She seems to have little appetite for reforms or measures to increase the economy's long-term potential growth rate.

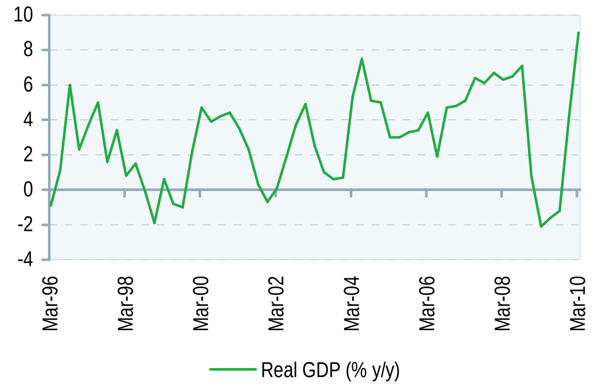
Implications for monetary policy and markets

Given the high popularity of Lula's income and social policies, they are unlikely to undergo major changes, despite the pressure they put on the fiscal accounts

Fiscal policy will be a key challenge. At 41.7% of GDP, net government debt is still high for an investment-grade country. Plus, the government's interest payments exceed 5% of GDP per year. This calls for tighter fiscal policy to reduce the debt, but we expect only minimal progress there. The problem is that the rigidity of the fiscal accounts leaves very little room to cut discretionary expenditure.

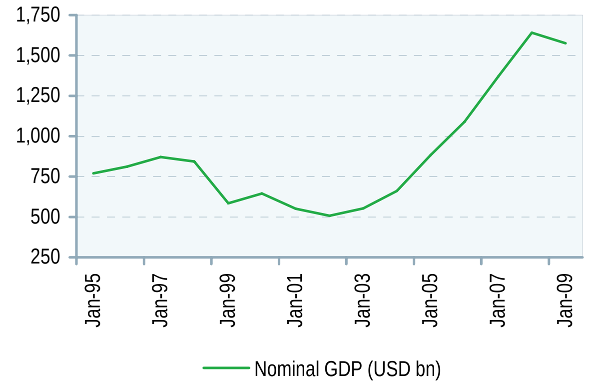
This also means that monetary policy will continue to do the heavy lifting when it comes to controlling inflation. For this reason, the credibility of appointments to the central bank board and the finance ministry will be key determinants of how the market reacts to the new government – particularly if Dilma is elected, as the polls strongly suggest.

Chart 1: In the past, the economy experienced boom-bust cycles of volatile growth



Sources: Bloomberg, Standard Chartered Research

Chart 2: More recently, income gains have been steadier and sustained, boosting Lula's approval



Sources: Bloomberg, Standard Chartered Research

China

Stephen Green, Regional Head of Research, Greater China
Standard Chartered Bank (China) Limited
+86 21 3851 5018, Stephen.Green@sc.com

- **China's economy seems to have hit a moderate growth plateau**
- **Further weakness is possible in Q3 on housing construction and export slowdown**
- **There are plenty of stimulus tools Beijing could use; we expect mild loosening in Q4**

Economy has stabilised

Steady PMI readings suggest that China's economy is currently on a plateau of moderate growth

From April to July this year, we saw clear signs of a slowdown in the breakneck pace of China's economic recovery. This, we argue, was the result of quiet government tightening moves which began at the end of 2009. These measures included fewer infrastructure project approvals, less fiscal spending and the CNY 7.5trn bank loan quota for the year. The government attack on the real-estate sector which began in April concentrated fears that, at worst, China's bubble would burst, and at best, its slowdown would intensify in Q3-2010 and trigger the need for a second round of stimulus at the end of the year. Markets were also nervous about a continuing pick-up in China's inflation, which would have forced the authorities to double down on their tightening measures, causing a right royal mess. Commodities sold off in Q2 partly on fears of this China slowdown.

In the last month, however, we have seen a number of signs that the economy has stabilised at a moderate rate of expansion. A key factor supporting this view was the August PMI, which we show in Chart 1. The seasonally adjusted (SA) PMI was at 53.4, and the new orders reading (SA) hit 56.4. Other signs of renewed dynamism included an uptick in apartment and car sales, as well as bigger-than-expected fixed investment spending. Although onshore investor sentiment has yet to turn (the stock market is still in the doldrums), the worst of the slowdown may already be over.

There are still some negative trends in place which could weaken growth in next three months

Fears of a collapse in China's economy were always overdone, we believe, but we have been surprised by how early the apparent stabilisation has taken place. As a result, we are still cautious. Real-estate construction activity should slow in Q3 as the number of new project starts falls. Our recent survey of developers suggests that construction activity will not collapse, but we still expect most developers to hold off on new starts until after Q3. That is when we expect a wave of new pre-sales to hit the market, bringing some price weakness (see **Special Report, 3 August 2010, 'China – Our big real-estate survey, Phase 1'**). We expect low-income housing construction to be more of a 2011 phenomenon than a 2010 one, given that government targets and heavy political pressure only started in April-May. This year is all about local governments allocating land for low-income housing, brow-beating developers to help, organising funding, and breaking ground in order to meet the target of 5.8mn new units. Next year, construction should start in earnest. Most of the funding will have to come from banks, given less-than-generous support from the Ministry of Finance (MoF) so far (CNY 60bn allocated, compared with the total annual cost of CNY 400bn).

China (con'd)

Guidance to the banks on lending to developers and infrastructure projects still seems to be tight, and this could still drag on growth in Q3. Exports are also likely to weaken a bit after the Christmas shipping season ends in October. A recent chat with a shipping client suggested that freight traffic on the China-US route is running above capacity, with no signs of a slowdown yet, while China-Europe traffic is at about 90%, having weakened a tad since April.

No reason to worry – there is plenty of stimulus left if needed

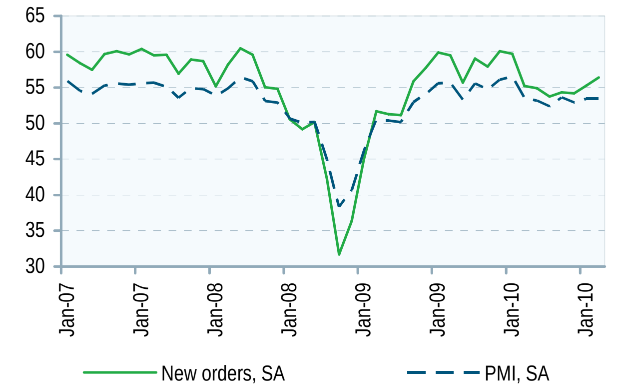
There is still plenty in the cupboard if needed

So China appears to have reached a plateau of steady growth. Exports and housing may lead to some weakness, but everything else appears to be ticking along nicely. Moreover, inflationary pressures still appear contained (although there was a sharp uptick in the manufacturing input price component of the PMI in August). Policy is on hold for the moment, as we have been saying for a while. Even the Chinese yuan (CNY) is flat against the US dollar (USD), despite the June de-peg, as Chart 2 shows.

We do expect the slowdown in the US economy to unnerve Beijing by Q4. At the same time, housing prices may have corrected by October, and confidence may suffer a little. Under these circumstances, we would expect moderate policy loosening. An added consideration is that if US pressure on China to let the CNY appreciate ramps up again, Beijing might again deflect this pressure by stimulating domestic demand and supporting the global economy in that way.

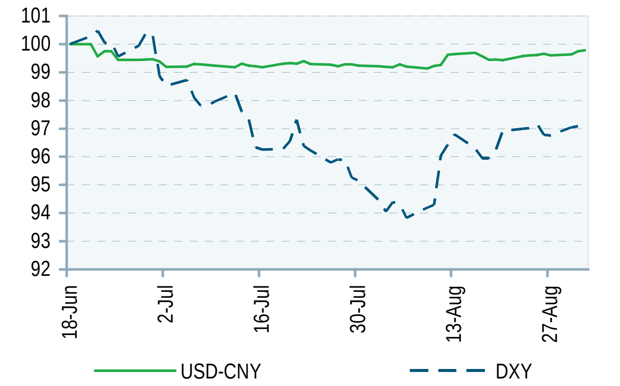
In contrast to G7 governments, the authorities in Beijing have plenty of additional stimulus tools if they need them. We visited Zhejiang province a couple of months ago and were told that no big infrastructure projects had been approved since September, suggesting that there are still thousands of projects which could be started if Beijing felt the need. Bumper fiscal revenues piled up in the MoF's bank account in H1 and are crying out to be spent, possibly on low-income housing as well as education and health care. And for all the worry about the banks' balance sheets, the capital-raisings they are currently involved in should give them more capacity to lend if needed.

Chart 1: PMI and new orders, SA



Sources: CEIC, Standard Chartered Research

Chart 2: USD-CNY central parity fixings and DXY
June 18 2010 = 100



Sources: Bloomberg, Standard Chartered Research

EU

Sarah Hewin, Senior Economist
Standard Chartered Bank, United Kingdom
+44 20 7885 6251, Sarah.Hewin@sc.com

- **The recovery in global trade has helped to drive euro-area growth**
- **Asia and Latin America have been the most dynamic markets for euro-area exports**
- **Stronger euro-area demand has also driven rapid import growth from these regions**

Asia more significant than US for euro-area trade

China and the 'dynamic Asian' economies – Hong Kong, Singapore, South Korea, Malaysia, Taiwan and Thailand – are the destination for some 12% of euro-area exports, and Asia overall buys a larger share of euro-area exports than the US

Broad Europe remains key export market, but less dynamic than EM

Euro-area trade activity has been buoyant since Q3-2009, reflecting the recovery in global trade as economies have emerged from recession and begun to rebuild inventories. After falling by 18.2% in 2009, euro-area exports rose by 15.9% in the first five months of 2010 versus a year earlier. Similarly strong growth in imports has limited the net contribution of trade to GDP growth during the economic recovery, though in the case of Germany, foreign trade contributed 0.8ppt to Q2-2010 growth.

Germany is leading the way in the euro area's export boom, with its exports to markets outside the region up 23.4% in the first five months of 2010. The country's total exports are now back to near pre-recession levels, helped by sales of high-technology machinery to rapidly growing emerging markets, especially in Asia. Among other key euro-area economies, Spain and the Netherlands have also experienced strong export growth, with their exports to non-euro-area markets rising by more than 20%. France and Italy have lagged, with exports outside the euro area growing by around 10% y/y in the first five months of 2010.

The euro area has benefited from rising demand across broader Europe: in addition to the UK, key export destinations include Switzerland, Sweden, Norway and emerging Europe. While these markets are still more significant export destinations for the euro area than China, other major Asian economies and Latin America, Asia and Latin America lead the way in terms of the pace of export growth. Exports to these regions from the EU as a whole and the euro area rose by 30-40% y/y in the first five months of 2010.

In terms of European markets outside the euro area, while euro-area exports to Sweden were up 23.2% during the January-May period, export growth to the UK and Switzerland has been more subdued, at some 11-12% y/y during January-May. Euro-area export growth to key emerging European countries (Russia, Poland, the Czech Republic and Turkey) was 19% y/y during the same period.

Rapid export growth to Asia and Latin America

The UK and the US are still the euro area's largest single-country export markets outside the region (accounting for some 25% of the total). But China and the 'dynamic Asian' economies (Hong Kong, Singapore, South Korea, Malaysia, Taiwan and Thailand) absorb a combined 12% of the region's exports to non-euro-area markets – similar to the US – and Asia overall is a more significant destination than the US. Latin America accounts for some 5% of euro-area

EU (con'd)

Emerging markets in Asia and Latin America have been the most dynamic markets for euro-area exports so far this year

exports. Moreover, emerging markets in Asia and Latin America have been the most dynamic markets for euro-area exports so far this year. Exports to the US recorded single-digit y/y growth in January-May 2010 (although this was better than US exports to the euro area, which fell by 5.2%). By contrast, euro-area exports to 'dynamic Asia' grew by 32.3% during the same period, and exports to Latin America rose by 35.5%.

While the euro area experienced a sharp decline in exports to virtually every country in 2009, its export growth to China remained positive, at 4.4% last year. Growth in the region's exports to China has accelerated markedly this year, to 43.5% y/y in the first five months of 2010.

Euro-area recovery underpins strong EM imports

The pick-up in the euro-area economy is also supporting buoyant import growth. For example, the latest German data showed that imports rose by 17% in H1-2010 as Germany's economic recovery became more broad-based and domestic demand picked up. Having fallen sharply during the crisis, euro-area import volumes recovered from mid-2009 and showed positive y/y growth in Q1-2010.

In the first five months of 2010, euro-area imports from 'dynamic Asia' rose by 16.3% y/y, and those from Latin America were up 17.2%. Imports from China, which slumped by 14.4% in 2009, rose by 17.5% y/y in January-May 2010. China is the euro area's most important source of imports, accounting for some 13% of the total in January-May 2010, but import growth has been strongest from commodity-producing economies, including Russia and the Gulf states.

Table 1: Euro-area trade by region

Euro area, 2009	Exports as	Imports as
	% of total exports	% of total imports
Dynamic Asian economies	5.8	5.9
China	6.2	12.7
Latin America	4.7	4.7
Key emerging Europe	15.5	16.9
US	11.8	8.4

Source: Eurostat

Table 2: Euro-area trade, % change

% change, y/y	Euro-area exports		Euro-area imports	
	2009	Jan-May 2010	2009	Jan - May 2010
Dynamic Asian economies	-11.5	32.3	-19.4	16.3
China	4.4	43.5	-14.4	17.5
Latin America	-20.6	35.5	-27.6	17.2
Key emerging Europe	-24.3	19.0	-20.7	29.7
US	-19.1	9.9	-15.1	-5.2

Source: Eurostat

Note: 'Dynamic Asian economies' consist of Hong Kong, Singapore, South Korea, Malaysia, Taiwan and Thailand;.'Key emerging Europe' consists of Russia, Poland, Czech Republic and Turkey.

Hong Kong

Kelvin Lau, Regional Economist
Standard Chartered Bank (Hong Kong) Limited
+852 3983 8565, Kelvin.KH.Lau@sc.com

- **Recent Fed reassurance suggests HIBOR will stay low throughout next year**
- **Property-market measures short on immediate impact, long on pre-emptive value**
- **We revise 2010 and 2011 inflation forecasts to 2.5% and 4.0%, 2010 growth to 6.0%**

Implications of sustained low HIBOR

Subdued HIBOR trajectory

3M HIBOR should trade around 0.30% until end-2011, barring transitory spikes running up to period-ends

US Federal Reserve Chairman Bernanke's recent reassurance that the Fed is ready to act should growth weaken sufficiently, either by further expanding quantitative easing or through other means, reinforces our view that the Fed will not hike rates until Q2-2012. This means HIBOR is also unlikely to head significantly higher anytime soon, in our view.

Because of Hong Kong's Linked Exchange Rate System, HIBOR looks set to mirror the subdued trajectory of its USD counterpart over the next 18 months (see Chart 1). The risk that sizeable capital outflows will push HIBOR higher also appears low for now, thanks to Hong Kong's still-attractive growth story, the continued structural increase in capital inflows from mainland China, and the low likelihood that the USD-HKD spot rate will test the 7.85 weak-side convertibility threshold again anytime soon. A re-test towards the 7.85 mark would be needed for the Hong Kong Monetary Authority (HKMA) to intervene to buy HKD and sell USD; only then would the Aggregate Balance start to shrink. With this gauge of interbank liquidity still standing close to HKD 150bn (versus a norm of less than HKD 5bn), HIBOR appears well capped on the upside.

Near-term, 3M HIBOR appears to have found a floor near 0.25% since late August. This is roughly in line with our view that, barring transitory spikes running up to period-ends, it should trade around 0.30% all the way to end-2011. Beyond that, the longer end should lead the initial stages of the uptrend, and spreads between HIBOR and USD LIBOR should start to normalise across the curve. Ultra-low US interest rates have compressed these spreads since the outbreak of the global crisis (especially at the short end), and only a resumption of the USD LIBOR uptrend would begin in reverse this. The anticipated climb in HIBOR in 2012 should therefore lag somewhat behind that of USD LIBOR.

Spotlight still on property

Do not write off the latest property-market cooling measures; they should help to limit leverage and speculation going forward

Given the lack of autonomous monetary policy or tools to manage interest rate expectations, the Hong Kong government has resorted to macro-prudential measures to rein in property prices. Among other measures, the government recently banned the resale of unfinished new homes in order to curb speculation and introduced three new sites for auction to increase supply; the HKMA also tightened rules on residential mortgage loans to limit leverage (see **On the Ground, 13 August, 'Hong Kong – New property cooling measures'**).

Hong Kong (con'd)

Although many believe these new measures have had a limited effect given subsequent strong land auction results, we believe some of them will help to pre-empt excessive leverage and speculation down the road, especially now that interest rates are set to stay low for longer. We continue to take comfort in the fact that the mortgage debt-servicing ratio, at 41.5% as of end-Q2, remains below its 20-year (1989-2008) historical average of 53.0%, and that confirmor cases (buyers reselling flats to sub-purchasers before the legal completion of the original sale) account for less than 2% of total transactions (see Chart 2).

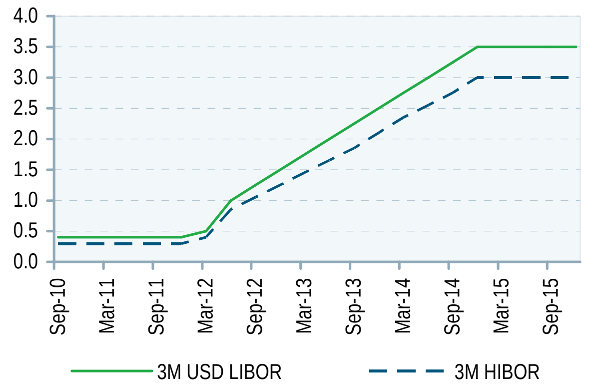
Expectations are that the government will need to deliver more measures not just to defuse a potential bubble, but also to make properties more affordable to lower-income households. The top priority is still to address the perceived uncertainty of future land supply; meanwhile, the debate over whether to restart the Home Ownership Scheme (and, if so, by how many flats a year) appears due for a conclusion. Dealing with the likely continuation of capital inflows chasing local (mainly luxury) property prices higher will be much trickier – recent calls to limit property ownership by foreigners appear overdone for a free and open economy like Hong Kong. We also doubt the credibility and effectiveness of the recently reported removal of property investments from the list of eligible assets under the Capital Investment Entrance Scheme.

Prolonged low interest rates, rising public transport fares and the impending introduction of a minimum wage pose upside risks to inflation and growth

Revised inflation and GDP forecasts

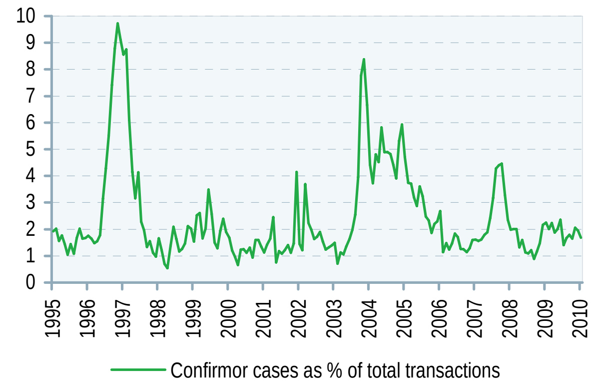
We have long argued that the lagged effect of higher residential rents since early 2009 will finally start to impact CPI inflation next year. But given (1) likely prolonged low interest rates, (2) an impending rise in some public transport fares, and (3) uncertainty surrounding the introduction of a minimum wage, we revise up our 2011 inflation forecast to 4.0% from 3.5%. While this is higher than the pre-crisis, post-deflation norm of 2-3%, we do not believe it is alarming enough to derail our 5.0% growth forecast for 2011. We also raise our 2010 inflation forecast to 2.5% (from 2.0%) and our GDP growth forecast to 6.0% (from 5.4%) to reflect the further extension of already ample liquidity, and possible mild policy loosening in China in Q4-2010.

Chart 1: 3M interbank rate forecast *(%)*



Sources: Standard Chartered Research

Chart 2: Residential property not speculation-prone



Sources: CEIC, Standard Chartered Research

India

Anubhuti Sahay, Economist
Standard Chartered Bank, India
+91 22 2268 3182, Anubhuti.Sahay@sc.com

- **Revised draft of direct tax code waters down radical changes planned earlier**
- **Delayed implementation leaves room for further changes**
- **When implemented, the new code will be a step towards a better tax regime**

Tax reform is not radical enough

The Indian tax system is set for a major overhaul. The Goods and Services Tax (GST) is expected to reform the indirect tax structure (though implementation might miss the April 2011 deadline), and the new direct tax code (DTC) is set to replace the country's archaic direct tax laws by April 2012. These laws have not been significantly modified in 48 years.

Tax rates have been more or less maintained at current levels, while various exemptions and tax holidays have been retained, defeating the purpose of simplifying the direct tax regime

The intent behind reforming the direct tax is noble. India's tax rates are among the highest in the world, and the DTC seeks to simplify direct tax laws for both corporates and individuals. It envisages a meaningful reduction in tax rates, with a clear focus on increasing the tax base and abolishing the myriad tax exemptions prevalent under the current law. As mentioned by the finance minister, the DTC will seek to give India a competitive edge by lowering the tax burden and closing loopholes related to international taxation.

However, the curse of democracy has probably already taken its toll on the DTC proposals. The first DTC draft, submitted in August 2009, included several contentious proposals that evoked mixed reactions from stakeholders including corporates and foreign investors. However, the revised bill tabled in Parliament in August 2010 seems to have lost most of the initial intent and does not look much different from the current tax regime. For instance, the effective corporate tax rate is now proposed to be reduced from 33% to 30%, versus the initial proposal of 25%. In fact, the proposed minimum alternative tax (MAT) rate of 20% on book profits is slightly higher than the current all-inclusive rate of 19.9%, although companies will be allowed to carry forward MAT credits for 15 years instead of the current 10 years. For individuals, while some changes to tax brackets have been proposed, tax rates have been maintained at the same level.

Likewise, a plethora of tax exemptions and holidays initially slated for withdrawal have been retained, defeating the purpose of simplification. Under the current regime, tax holidays offered in Special Economic Zones (SEZ) have encouraged companies to set up industrial units despite weak economic rationale. While such tax holidays would have been virtually eliminated under the first draft, they are grandfathered under the revised proposal. A lack of measures to improve tax compliance and administration remains another sore point. While the first draft also lacked explicit measures on this front, it contained other recommendations to address the problem, which are absent from the revised proposal.

India (con'd)

Further changes to the DTC are still possible, as implementation is not expected until April 2012

The revised code may also fail to achieve the original intent of reducing tax litigation. For instance, international taxation was one of the most contentious issues in the first draft of the DTC. The draft implied that in case of a conflict between a double taxation avoidance treaty and the DTC, the most recent treaty would prevail. Given that the draft code was expected to come into force only by 1 April 2011, it would have post-dated – and overridden – all other tax treaties. India has tax treaties with about 75 countries, including Mauritius, which accounts for more than 40% of FDI into India (any transaction related to the transfer of shares in an Indian company by a Mauritius holding company is untaxed). Thus, the implementation of the originally proposed DTC was clearly a concern for corporates already invested via this route. The revised draft saves investors from such a sweeping change, specifying that neither the tax treaty nor the DTC shall have preferential status. However, any tax treaty benefit will now be subject to a general anti-avoidance rule, with the onus shifting to the taxpayer to prove that the transaction was not done with the intent of avoiding taxation. This might lead to more litigation.

Overall, while the revised DTC has disappointed tax experts and stakeholders on several counts, it contains some bright spots. Although tax reductions for domestic corporates have been watered down, foreign investors should still gain significantly, as the proposed 30% tax rate – while still higher than the originally proposed 25% – is significantly lower than the current 42.23%. Investors have welcomed the decision to keep the long-term capital gains tax at 0% and reduce the short-term capital gains tax. The application of MAT to book profits rather than gross assets, as initially suggested, also gives more breathing room to capital-intensive industries, especially infrastructure companies.

It is important to note that these are still proposals. As implementation has been pushed back by a year to April 2012, more changes are still possible as key stakeholders express concerns over various facets of the DTC. It is therefore too early to assess its macroeconomic impact. Whatever the outcome, India has at least begun its journey towards a tax system more comparable with global norms.

Table 1 : Spot the difference

Category	Existing rate	First DTC draft	Revised DTC draft
Corporate tax	33.2% (including surcharge and cess)	25% (all-inclusive)	30% (all-inclusive)
Corporate tax for foreign company	42.23% (including surcharge and cess)	25% (all-inclusive)	30% (all-inclusive)
Personal income tax		New tax brackets to be introduced to reduce the tax burden for individuals. Peak rate of 30% applicable for income above INR 2.5mn	New tax brackets to be introduced to reduce individual tax burden, but peak rate of 30% is applicable for income above INR 1.0mn.
Capital gains	0% on long-term gains, 15% on short-term	Eliminate the difference between short- and long term-capital gains tax	0% on long-term capital gains; graded 5-10-15% short-term capital gains tax rates proposed
Special Economic Zones (SEZ)	SEZ enjoy profit-linked deductions	Eliminate profit-linked deductions	Profit-linked deductions continued for existing SEZs, if notified before 2012 production started by 2014
Minimum alternative tax	18% of book profits (19.9% with surcharge)	2% of gross assets, 0.25% for banking companies	20% of book profits (no surcharge applicable)

Sources: Press releases, DTC draft

Kenya

Razia Khan, Head of Macroeconomic Research
Standard Chartered Bank, United Kingdom
+44 20 7885 6914, Razia.Khan@sc.com

- **USD-KES price action has indicated a susceptibility to global recovery sentiment**
- **But Kenya's growth impetus is increasingly domestic or sub-regional**
- **Confidence has received an important boost following the referendum**

All set for growth

While the KES has demonstrated greater vulnerability to global risk appetite, the key drivers of growth are domestic and regional

Following the successful passage of Kenya's constitutional referendum in August, the first key political test since the post-election fallout at the end of 2007, confidence in the country's economic prospects is growing. Kenya was one of the few African economies to grow faster in 2009 than in 2008, mostly reflecting the dislocation that followed its political crisis in 2008. While the recovery has been gradual and interrupted by drought, most indicators have turned more positive. Nonetheless, the vulnerability of the Kenyan shilling (KES) to recent euro (EUR) volatility and changes in risk appetite has raised new concerns about the susceptibility of Kenya's recovery to a renewed global downturn. In our view, however, most of the factors supporting growth are domestic and regional, giving the economy some degree of resilience.

In recent months, more than USD 1bn has been raised from the domestic bond market for infrastructure spending. Oil-related developments in East Africa, and increasing reliance on Kenyan ports for access to export markets, should lead to further infrastructure gains. (The transport and communications sector contributes 9.8% of GDP, and this is set to rise with Kenya's growing relevance as a regional hub.) The impact of earlier monetary and fiscal easing is yet to manifest itself fully in the real economy, with the bank rate cut by 75bps to 6% as recently as July.

The evidence so far

Sectoral growth rates for Q1-2010 show post-drought gains in agriculture (up 4.6% y/y), mining (9%), manufacturing (7.8%), wholesale and retail trade (3.7%), and perhaps most impressively, the financial sector (11.9%). While the drought took a greater toll on electricity, which declined by 2.1%, manufacturing should receive a renewed boost from improved HEP supply, lower tariffs and robust regional demand. The volume of cargo throughput handled at Kenyan ports rose by 7.8% y/y in January-April 2010, while cement consumption rose by 14.3%. Despite ash-cloud disruptions, tourism has also done well.

Public debt ratios are not a big concern; there has been minimal overshooting of interest rates, and innovative domestic borrowing has prevented crowding-out of the private sector

While Kenya's expansionary fiscal stance has provided a significant counter-cyclical boost to growth (the FY11 deficit is projected to be even wider than the 6% of GDP achieved in FY10), public debt ratios do not pose an imminent threat to the growth outlook. Public and publicly guaranteed debt stood at 47% of GDP in May 2010, up from 44% a year earlier, with domestic debt – currently at 25.7% – increasing by 4ppt of GDP. However, careful management of the domestic borrowing requirement has prevented significant interest rate overshooting, While short rates may have bottomed, longer-dated Treasury bonds, with maturities of between 10-20Y, now account for almost 30% of outstanding

Kenya (con'd)

government securities. With the central bank easing interest rates late in the cycle, the recovery is unlikely to pose much threat to government bond yields. Indeed, the most recent infrastructure bond auction was oversubscribed.

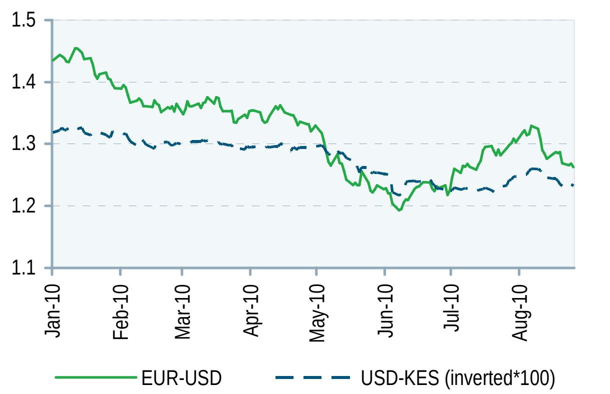
Kenya's banking sector is in good shape, and the outlook for credit growth is healthy

Money supply growth is healthy, with broad money M2 (M3 excluding foreign-currency deposits) growing 25.6% y/y in May, double the rate only a year earlier. The aggregate balance sheet of the banking sector grew by 24.7% over the same period, funded mainly by customer deposits (77.8%). The banking sector is in good shape and is poised for further asset growth. Tier 1 capital grew by 24.8% in the last year, reflecting a combination of new capital injections and retained earnings. With 41.5% growth in pre-tax profits in Jan-May 2010, it is not surprising that private-sector growth continues to accelerate.

Regional developments, including rapid infrastructure improvements, will be the big driver of Kenyan growth in the years ahead

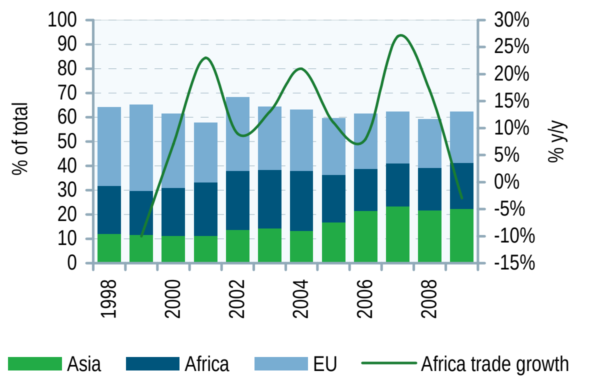
Bank credit to the private sector has been broad-based, channelled to trade (29.5%), private households (26.5%), real estate (26%), transport and communications (10.3%), consumer durables (9%), manufacturing (6%), finance and insurance (5.9%), and agriculture (5.1%). The credit growth pattern is telling, indicating either rising domestic activity or a correlation with regional trade. As Chart 2 shows, Kenya's trade with regional partners – and, more recently, Asia – has gained importance at the expense of trade with its traditional partner, the EU. While Kenya's top export markets – Uganda (11.4%), the UK (10.3%), Tanzania (7.6%) and the Netherlands (6.7%) – are still fairly mixed, there is little doubt that as East African regional economies grow faster, their share of Kenyan trade is likely to outperform. Within Africa, economic growth in this sub-region was the most resilient to the global crisis; Ethiopia led the way, with a 9.9% GDP growth rate in 2009. Given the recent establishment of the East African Protocol, which allows for the (theoretical) free movement of goods and labour within established East African Community borders, and strong growth in Ethiopia and Southern Sudan just beyond, regional influences remain overwhelmingly positive. Whatever the FX market's fears over a potential global double-dip, the sympathetic depreciation of the KES appears overdone.

Chart 1: USD-KES has been more susceptible to global risk aversion, tracking the EUR-USD recently



Sources: Reuters, Standard Chartered Research

Chart 2: But regional and Asian trade have grown in importance



Sources: IMF DoTS, Standard Chartered Research

Mexico

Douglas Smith, Regional Head of Research, Latin America
Standard Chartered Bank, United States
+1 212 667 0564, Douglas.Smith@sc.com

- **The external boost to manufacturing has had little effect on domestic demand**
- **More uncertainty over the US outlook means that growth will be delayed further**
- **The central bank will remain on hold through Q3-2011; receiving rates is attractive**

The slow road to recovery

Growth to slow in H2

Q2 growth was flattered by base effects; we expect more slowing ahead

Mexico's GDP grew 7.6% y/y in Q2-2010, in line with consensus. This sounds like impressive growth, but it came on the back of a 10% y/y decline in Q2-2009, so the base effect was significant. We expect growth in H2 to be less robust and continue to look for a modest 4.5% growth rate in 2010 after the 6.5% contraction last year, followed by a slower 4.0% in 2011. If there is a risk for 2011 growth, it is to the downside, in our view.

Still-weak domestic demand

After a period of recession, Mexico's growth is typically first boosted by external demand, which drives industrial production; then, this expansion spreads to domestic demand with a lag. This, at least, was the case following the 1994-95 recession, which was the last one of similar magnitude to the downturn Mexico has experienced in the past two years.

The boost to manufacturing from US demand has done little to help the domestic economy

The first part of the pattern described above appears to be intact. The bulk of Mexico's growth this year has been driven by external factors. For example, the rebuilding of inventories in the US and demand for auto-related exports led to a surge in Mexico's non-oil exports to the US. In seasonally adjusted terms, real GDP grew 3.2% in Q2. The industrial component rose 1.7% q/q in Q2, with a strong contribution from manufacturing (+2.1% q/q). Growth in the service sector, which is more indicative of domestic demand, was a more modest 0.9% q/q in Q2. The third component of the supply side, agricultural output, rose 6.8% q/q after a 2% contraction in Q1.

The rebound in industrial production has been weaker than in the 1994-95 recession

Note that in the current recovery, industrial production is rebounding more slowly than in 1994-95. Chart 1 shows the seasonally adjusted index of industrial production and how many months it took for industrial production to recover to its pre-crisis peak. Here, we use October 1994 and March 2008 for the starting dates. After October 1994, it took 24 months for industrial production to return to the pre-crisis level. In the current rebound, 26 months have passed and industrial production remains 4ppt below the March 2008 pre-crisis peak.

Besides the relatively slow recovery in industrial production in this cycle, a second concern for growth is that the external environment is becoming more uncertain, particularly in the case of the US. This risks derailing the recovery in Mexico even before we see any pick-up in domestic demand; hence our outlook for mediocre growth ahead compared to, say, Brazil, Chile or Peru.

Mexico (con'd)

No rate hikes are expected through at least Q3-2011

The central bank is on hold for the foreseeable future

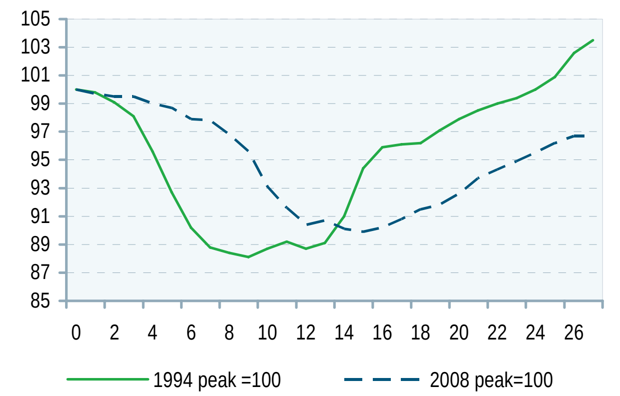
The central bank of Mexico (Banxico) has kept the overnight rate on hold at 4.50% for 13 consecutive months. Aside from the central bank in Colombia, Banxico is the only one in the region not tightening monetary policy. In its post-meeting statement for August, Banxico cited the deterioration in the US economic outlook as a source of downside risk for Mexico. This was new, and added a dovish spin to the outlook. We maintain our view that the central bank will stay on hold through Q3-2011, and if there is a risk to this view, it is that rate hikes will be delayed even further.

The TIIE futures market has steadily pushed out its expectations of the first rate hike. At present, there are about 26bps of tightening priced in for June 2011, 31bps priced in by September and 41bps priced in by December. We expect that the futures will move further in the direction of our view as more weak data are released.

Lacklustre growth performance, as reflected in the long period taken for industrial production to regain its pre-crisis high, plus the uncertain outlook are key reasons for this. Furthermore, core consumer prices are moving in the right direction, and real wage growth is only slightly positive. This economic backdrop is consistent with low inflation expectations. At the same time, it is no surprise to see weak consumer confidence, which remains well below pre-crisis levels, even if it is off the May 2009 lows (Chart 2). The unemployment rate is also still high: the July 2010 level of 5.40% on a seasonally adjusted basis was 11bps higher than the December 2009 rate.

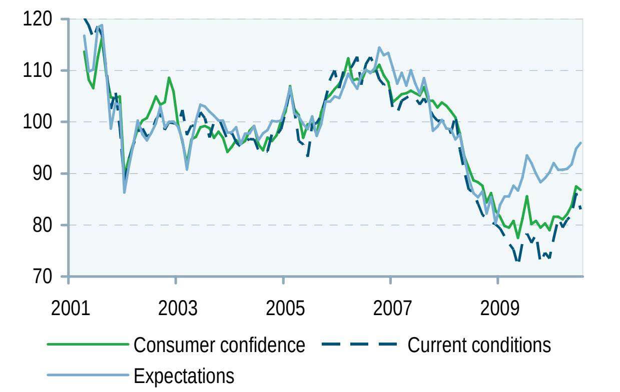
With US rates low and expected to be so for some time, Mexico's rates look attractive. The 10Y TIIE rate is 6.675% as of this writing. The yield has risen about 35bps in the past two weeks, and we will be looking for entry points to receive rates.

Chart 1: The long rebound in industrial production
Months to return to peak level, IP Index, 3mma SA basis



Sources: Bloomberg, Standard Chartered Research

Chart 2: Consumer confidence in the doldrums
CC Index, sa basis, national survey



Sources: Bloomberg, Standard Chartered Research

Pakistan

Sayem Ali, Economist
Standard Chartered Bank (Pakistan) Limited
+92 3245 7839, Sayem.Ali@sc.com

- **Floods have hit economy hard, with losses estimated at USD 4bn (2% of GDP)**
- **We lower our FY11 GDP growth forecast to 2.5% from 4.5%, raise inflation to 15%**
- **Deficit may jump to 6.5% of GDP vs. 4% target; IMF funds are critical to stability**

Counting the costs of the floods

Floods cause widespread damage

Economy has suffered widespread damage due to heavy floods; we revise down our FY11 growth forecast to 2.5% and raise our inflation forecast to 15%

Heavy floods in the Indus River resulting from monsoon rains have caused widespread damage to the economy. Nearly 20mn people have been displaced, making this one of the worst natural disasters in history. Nearly 1.25mn houses have been completely destroyed, leaving most of the affected households without shelter. Losses to the economy are estimated at close to USD 4bn (2% of GDP). We now expect a significant slowdown in GDP growth in FY11 (ends June 2011) and lower our growth forecast to 2.5% from 4.5%; this would follow growth of 4.1% in FY10. We also now expect FY11 inflation to jump sharply to 15%, versus our earlier forecast of 12%, depending on the extent of the damage and the measures taken by the government to reconstruct and rebuild the affected areas. However, the details will be known only after the completion of a damage assessment report jointly initiated by the World Bank and the Asian Development Bank (ADB), due in October.

Severe damage to crops and infrastructure

30% of cultivable land submerged in floods and main cash crops destroyed; key road and bridges washed away, with food security of millions at risk

The floods have caused widespread damage to the standing crop, the backbone of the economy, with nearly 30% of cultivable land destroyed by the flooding. The Ministry of Food, Agriculture and Livestock estimates losses to the agriculture sector at USD 2.8bn, and another USD 450mn in losses in the livestock sector. The country's main cash crops – including cotton, sugar and rice – have been badly damaged. This could snowball into significant losses for value-added manufacturing and more bad assets for banks. The UN Food & Agriculture Organization (FAO) has warned that the food security of millions is at risk if the next wheat crop is not salvaged, with the sowing season scheduled to start this month.

The floods have also damaged public infrastructure, with road links cut off, power stations shut down, and gas and petroleum supplies suspended. More than 2,500 schools, 175 health centres and 1,000 water-supply facilities have been damaged, according to the National Disaster Management Agency. The National Highway Authority estimates that nearly 1,000 bridges and more than 400km of road infrastructure have been destroyed, severely hampering supply of essential food commodities to villages and towns. The power infrastructure has also been badly damaged, with supply of 1,500MW disrupted due to damage to power plants, exacerbating the existing energy crisis and further stalling growth.

Pakistan (con'd)

Government will need to raise taxes and cut subsidies to fund reconstruction spending and limit the build-up of public debt

Fiscal reforms are needed to fund reconstruction spending

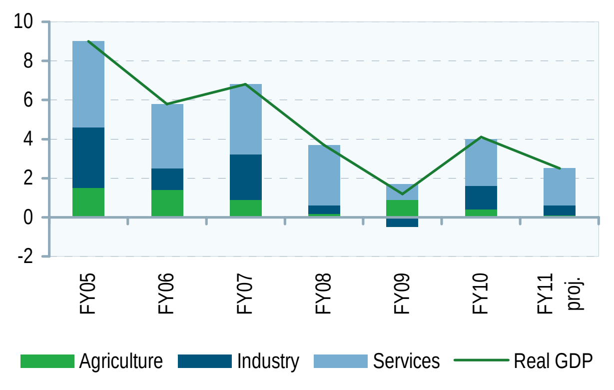
The FY11 budget initially targeted a deficit of 4% of GDP, but the costs of relief, rehabilitation and reconstruction will be significant. We now expect the fiscal deficit to rise to 6.5% of GDP in FY11, depending on the scale of the damage and the inflow of foreign grants. The government will need to create fiscal space to pay for relief and reconstruction expenditures and limit the build-up of public debt. The immediate measures announced by the government include freezing investment spending at FY10 levels and allocating PKR 153bn (0.9% of GDP) for flood-related spending. However, the government will need to undertake significant fiscal reforms to fund reconstruction activity, including reforming the sales tax regime to boost tax revenues by PKR 86bn. Power-sector subsidies are also expected to be phased out, bringing additional savings of PKR 127bn (0.7% of GDP).

Impact of floods can be cushioned by support from IMF and other donor agencies; new IMF loan is critical to medium-term stability

Relations with the IMF are critical to medium-term stability

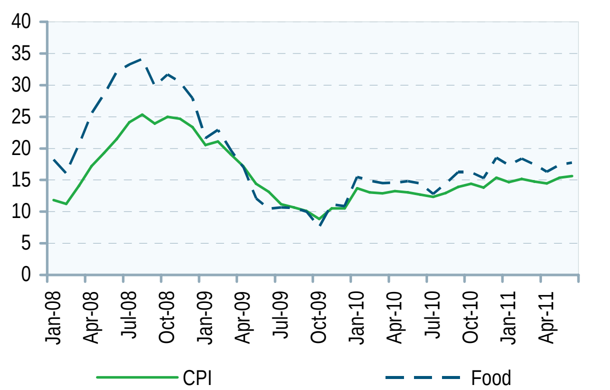
Relations with the IMF hit a road block in June 2010, after the government missed key performance targets in areas including the fiscal deficit, borrowing from the central bank and implementation of the value added tax (VAT). However, in the aftermath of the floods, the IMF is expected to relax some of its targets and release the next tranche of USD 1.3bn. This will provide short-term support to the Pakistani rupee (PKR), but a new IMF loan facility will be badly needed to provide medium-term support for the currency. In this regard, the IMF has offered Pakistan access to the Emergency Financing facility for natural disasters, with a limit of 20% of the country's Special Drawing Rights (SDR) quota. This comes out at close to USD 600mn, given the country's quota of 1.85bn SDRs. While Pakistan's short-term economic prospects are worrisome, reconstruction spending over the medium term will provide a significant boost to domestic output. This was the case in the aftermath of the 2005 earthquake, which caused an estimated USD 6.4bn loss to the economy. The short-term impact on growth was negative, with growth slowing to 5.8% in FY06 from 9% in FY05. However, the economy received a boost in the subsequent two years, expanding by an average of 6% per annum, primarily owing to reconstruction spending.

Chart 1: GDP growth projected to slow to 2.5%



Sources: Ministry of Finance, Standard Chartered Research

Chart 2: Inflation projected to increase to 15% *(% y/y)*



Sources: State Bank of Pakistan, Standard Chartered Research

Singapore

Alvin Liew, Economist
Standard Chartered Bank, Singapore
+65 6427 5229, Alvin.Liew@sc.com

- **Latest property-market cooling measures announced on 30 August may not work**
- **Low interest rates globally and domestically may keep property market hot**
- **More measures likely in Q4; repeat of 1996 correction is unlikely but not ruled out**

Mind that property

End of dizzy heights? Maybe not

Record-high property prices led to a third round of cooling measures, but these may not stop the price increases

Singapore announced its latest series of cooling measures for the private and public residential property market on 30 August – the third batch since November 2009. The measures are aimed at both curtailing demand and expanding supply. The private residential property price index rose by 11% in H1-2010 to 184.2, breaching the previous record, although deflating the index shows that its real level remains some way off the 1996 peak (Chart 1). Meanwhile, the public housing resale price index rose by nearly 7% in H1 to 161.3, the highest since the data was made available in March 1994. While we believe property price appreciation is in Singapore's interest, and that the government likely shares this view (home ownership is high, at 90%, and households have significant amounts of their retirement savings invested in their homes), policy makers want to avoid sharp and volatile price moves. Sharp price rises could turn real home buyers into speculators, encourage over-leveraging and raising affordability issues, especially for first-time home buyers. Sharply lower prices lead to negative equity and erode the retirement funds invested in homes.

Singapore's domestic bank lending grew by 7% y/y in the first seven months of 2010, adding nearly SGD 17.4bn worth of new loans. Unsurprisingly, mortgages accounted for most of the growth, accounting for 70% of all newly added loans. The banking sector's housing loan book has been growing since June 2006, in spite of the global credit crisis and the 'Great Recession' of 2008-09. While the central bank already has a regulation (Section 35) limiting banks' exposure to the (non-owner-occupied) property sector to 35% of their loan books, the latest cooling measures are another backstop to protect the banking sector, and the broader economy, from a property-market correction. Market expectations are for transaction volumes to fall and price increases to slow following the latest measures. But what if prices continue to reach even dizzier heights? We believe this could happen for one key reason: low interest rates.

Where would the money go?

Low interest rates, both externally and domestically, will be the key driver of the Singapore property market

We expect interest rates to remain depressed until mid-2012. With Singapore's domestic interest rates priced off of global rates, we expect very low rates during this period. This extraordinarily low interest-rate environment will continue to drive foreign funds into Singapore seeking property investment opportunities, while locals may continue to add exposure to mortgages. The Monetary Authority of Singapore's (MAS) Singapore dollar (SGD) appreciation policy makes domestic property assets even more attractive.

Singapore (con'd)

Funds going into residential property are largely from individuals. While the latest measures may prompt some funds originally destined for residential property to be diverted to commercial real estate (via portfolio investment in listed commercial property developers or real-estate funds), it is unlikely individuals will buy commercial buildings. We therefore expect funds to continue to flow into residential property.

Unabated property price increases are likely to prompt a fourth wave of measures; we see downside for the property market in 2011

Looking for the possible fourth wave

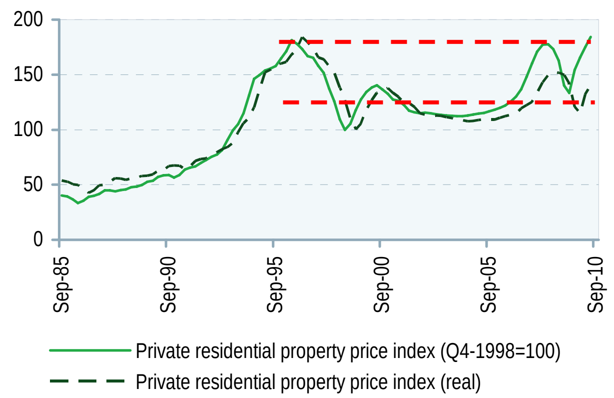
As noted above, we believe foreign capital flows into Singapore are likely to persist. It is worth noting that during the previous property up-cycle (2005-08), sharp price increases were initially limited mostly to the high-end segment before spreading to other segments. This time around, price increases have been faster and more broad-based, spanning from the top end of the market to the public housing resale market.

Hong Kong also recently implemented property-market cooling measures, but they have not impacted subsequent land auctions. If Singapore's property prices continue to rise, we believe the Singapore government may introduce a fourth wave of measures, likely in November 2010. Recalling the market correction of 1996, we believe the final regulatory straws (that could break the property market's back) would be:

1. Limiting permanent residents to one mortgage loan
2. Not allowing foreigners to take out mortgages
3. Implementing a capital gains tax

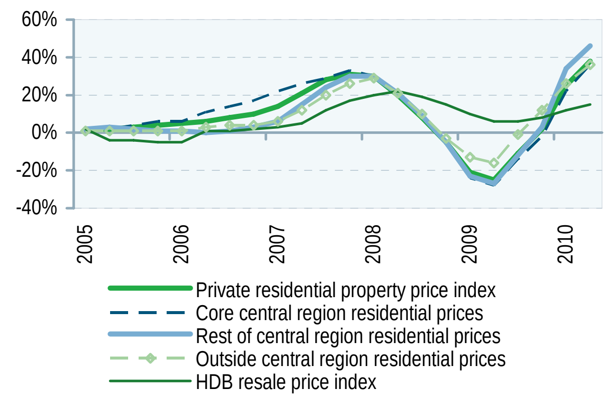
While we now expect property prices to rise by 10-15% in 2010 (versus our previous forecast of 5-10%), declines are likely in 2011. During the 1996-98 period, private property prices corrected by 40% amid the Asian financial crisis and draconian anti-speculative property measures. While this is not our core scenario this time, we cannot rule it out just yet.

Chart 1: Nominal property price index rose to a record in Q2-2010; real index did not



Sources: CEIC, Standard Chartered Research

Chart 2: Price increases are faster and more broad-based now than in 2005-08



Sources: CEIC , Standard Chartered Research

South Africa

Razia Khan, Head of Macroeconomic Research
Standard Chartered Bank, United Kingdom
+44 20 7885 6914, Razia.Khan@sc.com

- **Pre-crisis, South Africa's consumption boom reflected highly imbalanced growth**
- **Household debt has not corrected meaningfully, and arrears are substantial**
- **Continued household rebalancing suggests output gap will remain in place**

The still-elusive consumer

Private-sector balance sheets and economic growth

In terms of GDP levels, other emerging markets have seen real gains since the crisis, while the difference in South Africa is barely perceptible

Despite 550bps of interest rate easing in this cycle, South Africa's economic recovery remains weak and highly dependent on the external environment. While the sharpest y/y decline in South African GDP (2.7% in Q2-2009, according to Bloomberg data) was less dramatic than in many other economies, especially other emerging markets, South African growth since the global crisis has been unexciting. In absolute terms, GDP has only just managed to pull ahead of its pre-crisis level, while most other emerging markets have seen their GDP levels soar. Growth has compensated for the contraction seen during the crisis, but has not added much more. This is a big concern for an economy hoping to undergo deep structural changes, reduce poverty levels, and lessen income inequality.

Pre-crisis growth was marked by considerable imbalances, with consumption in overdrive and the external sector underperforming

South Africa's pre-crisis boom years were marked by remarkably unbalanced growth. Although the economy became more open during this time, which coincided with a significant commodity price boom, South Africa's share of global exports nonetheless declined. It was the domestic economy that outperformed. The strength of the South African rand (ZAR), its beneficial impact on inflation, and resulting multi-decade lows in interest rates, brought about a step change in trend growth. The emergence of a new middle class and the easy availability of credit prior to the June 2007 introduction of the National Credit Act gave rise to a credit-fuelled rise in consumption.

South Africa's current account deficit narrowed a bit during the recession before widening again; however, its counterpoint, domestic consumption, remains subdued

While the growing imbalance between domestic savings and consumption contributed to a significant widening of the current account deficit (its quarterly peak was over 9% of GDP), growth at least benefited. South Africa's recession saw a short-lived narrowing of the current account deficit, but consumption – accounting for 60% of GDP – has yet to show signs of life. Even though South Africa's well-regulated banks made it through the crisis largely unscathed (there was a brief cyclical rise in NPLs as past credit excesses caught up with the banks), y/y growth in private-sector credit extension has only just nudged its way back into positive territory. Household consumption, although growing, remains subdued relative to pre-crisis levels. South Africa's high unemployment rate (25.3% in Q1, and most likely still rising) and high levels of household indebtedness explain why. The household debt-to-disposable income ratio has risen meaningfully in recent decades, from 42% in 1980 to 52% prior to the recent growth upswing in 2002 and over 80% at the peak of the cycle. At 78.4% in Q1-2010 (the latest available data), it has barely corrected. Given this, what will it take to achieve higher consumption growth?

South Africa (con'd)

There is little to suggest that improved retail sales performance is sustainable; narrow focus on union wage demands misses the point, and formal-sector jobs are not being created fast enough

Since the publication of our earlier piece on this subject (**'In search of the South African consumer', Global Focus, February 2010**), little has changed. Retail sales have received a boost from the adoption of a lower deflator and from the World Cup, but neither factor points to sustainable growth. Major retailers continue to report heightened price sensitivity among consumers, a key factor keeping inflationary pressures in check. Even as PPI has moved higher, there is a disconnect with consumer price inflation. In recent months, CPI inflation has surprised to the downside. CPI inflation for low-income earners is the most subdued. This may be because of lower food inflation, as food is more prominent in low-income consumption baskets. Alternatively, it may indicate where the pain really lies: with low income earners facing the highest real interest rates.

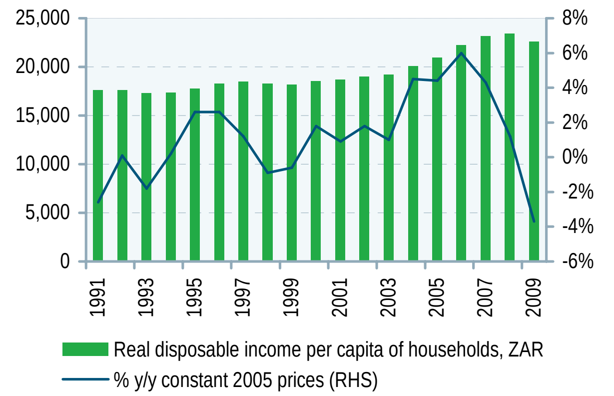
Because almost half of South Africa's credit-active consumers now have impaired credit records, any interest rate relief is likely to be used to pay down old debts

Although South African interest rates are currently at their lowest in 30 years and may be eased further, high debt has prevented households from responding more vigorously to monetary easing. In other economies, there is evidence of more rapid consumer rebalancing. In South Africa, anecdotal evidence suggests that consumers are borrowing more in order to repay debt. Data from the Credit Bureau Monitor suggests that over 60% of South Africans with credit agreements are now in arrears. According to the National Credit Regulator, almost half of South Africa's 18.21 'credit active consumers' now have impaired credit records.

With consumption under-performing relative to trend, South Africa can ill afford a renewed deterioration in the global economy

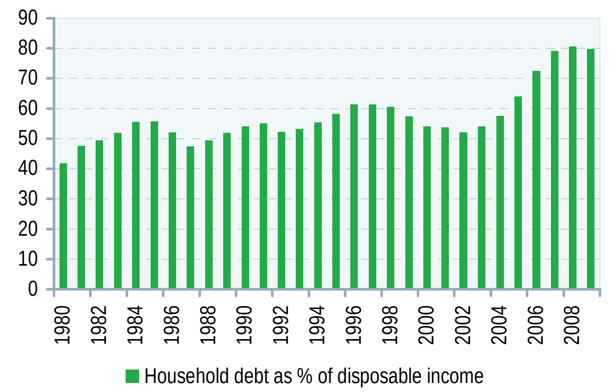
The macroeconomic implications are clear. Further interest rate relief is more likely to be used to repay existing debt than to run up new, unsustainable levels of borrowing that might threaten macroeconomic stability. While much analysis has focused on higher-than-inflation union wage demands, and the inferred rise in real disposable income growth that should feed into higher consumption, insufficient attention has been paid to credit conditions, the terms of credit availability, and the risk of rising joblessness. Most significantly, with the domestic economy failing to fire on all cylinders, South Africa's susceptibility to a renewed global downturn would be heightened. Given the structural poverty reduction that the authorities hope for, even temporarily weak growth may be more than the country can afford.

Chart 1: Sharp decline in disposable income growth



Sources: SARB, Standard Chartered Research

Chart 2: Elevated debt levels constrain credit demand



Sources: SARB, Standard Chartered Research

South Korea

Suktae Oh, Regional Head of Research, Korea
SC First Bank Korea Limited
+82 2 3702 5011, Suktae.Oh@sc.com

- **BoK emphasises rise in inflation pressures resulting from strong GDP growth**
- **But most factors suggest that inflation is not likely to rise significantly near-term**
- **Stable inflation will lead to a gradual normalisation of policy interest rates**

Inflation in check

BoK warns against demand-pull inflation pressures

BoK started its rate-hiking cycle based on a potential rise in inflation pressures due to strong GDP growth

The Bank of Korea (BoK) started its rate-hiking cycle with a warning about demand-pull inflation pressures. It has repeated the phrase “demand-pull inflation pressures will gradually increase due to the economic recovery” in its monthly policy statements since May, and finally started hiking rates in July. In its official economic outlook released in July, the BoK forecast that headline CPI inflation would rise to 3.0% in H2-2010 and 3.5% in H1-2011 as the output gap (the difference between actual and potential GDP) turns positive in H2-2010. BoK Governor Kim has taken every opportunity to emphasise the anticipated turnaround in the output gap recently. The upside surprises in June and July industrial production support the BoK’s view that demand-pull inflation pressures are at work. We expect an additional 25bps rate hike at the monetary policy meeting on 9 September.

Output gap may not be an accurate indicator of slack in economy

Output gap may vary according to estimates of potential GDP, and the labour market still has room to improve

However, the output gap may not be an accurate indicator of demand-pull inflation pressures or slack in the economy. Admittedly, Korea’s recovery from the global financial crisis has been very strong. One can conclude that the level of Korea’s GDP will return to trend soon if the recovery continues (see Chart 1). The return to trend can be defined as the closing of the output gap, because the simplest way to estimate potential GDP is to derive the trend. But there are many other ways to estimate potential GDP, such as the production function approach, which may produce different results. No country has a single, official data series for potential GDP, and the BoK does not disclose its own estimates.

Labour-market indicators still show some slack in the economy. Here, we use the rate of employment (the ratio of the number of jobs to the population over age 15) as the key labour-market indicator, since the more widely used unemployment rate does not cover ‘disappointed jobless people’ who have stopped looking for jobs. Chart 1 shows that the employment rate was around 59% in Q2-2010, after the labour-market recovery – still lower than the pre-crisis level of 60%. While the BoK is concerned about the recent pick-up in wage growth (to 6.0% y/y in Q1-2010), last year’s low base effect contributed to this, Wages declined by 1.9% in Q1-2009, and two-year average wage growth rate in Q1-2010 was only 2.0%.

Other factors do not support a significant rise in inflation

Money and credit indicators do not point to a significant rise in inflation, as they are stable these days. We believe that the steep rise in inflation in 2008 was related to the acceleration in money and credit growth in 2004-08. Broad money

South Korea (con'd)

(M2) growth picked up from 2.4% in January 2004 to 15.8% in May 2008, and bank loan growth rose from 3.3% in March 2005 to 17.0% in July 2008. Headline inflation reached 5.9% in July 2008, and core inflation peaked at 5.6% in December 2008. M2 growth and bank loan growth are now holding steady at 10% and 3%, respectively, which suggests stable inflation.

Money and credit growth, the property market, commodity prices and the CPI data itself do not support a significant rise in inflation

Ongoing weakness in the real-estate market is also inconsistent with rising inflation pressures. The CPI is directly linked to the housing market through rents (weighting of 9.8%), and may also be indirectly related to the commercial real estate market, as rents are an important part of the cost of services, in particular the price of eating out. Consumers' expected inflation rate has risen to 3.2% from 3.0% in recent months, but this should be offset by the decline in suppliers' pricing power indicated in the business survey. Finally, we are not worried about commodity price-driven supply-push inflation pressures as long as concerns about a global double-dip recession persist.

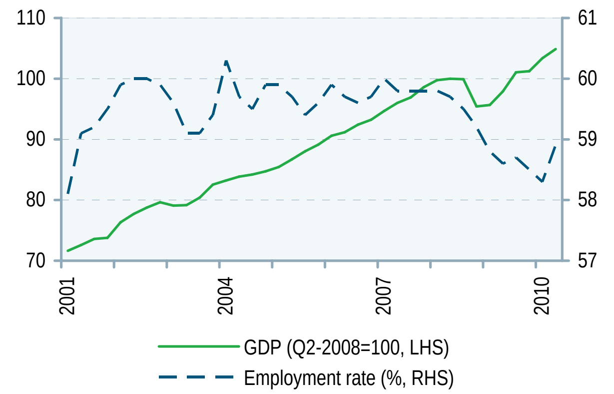
The actual CPI inflation data does not support the BoK's base-case scenario that headline inflation will accelerate to 3.5% in H1-2011. The wide gap between headline and core inflation indicates that headline inflation is currently driven by food and energy prices (see Chart 2). Considering that fresh food inflation is at historically high levels (20.0% in August 2010) and that energy prices are likely to remain stable in the near future, food and energy inflation is expected to slow from the current level of 9.0%. In order for the BoK's base-case scenario of 3.5% headline inflation to materialise, core inflation may have to rise above 3% within six months as food and energy inflation slow. This is unlikely, considering the remaining slack in the economy and the inherent stability of core inflation.

Stable inflation will lead to a gradual hike in policy rates throughout 2011, in our view

Stable inflation means gradual rate hikes

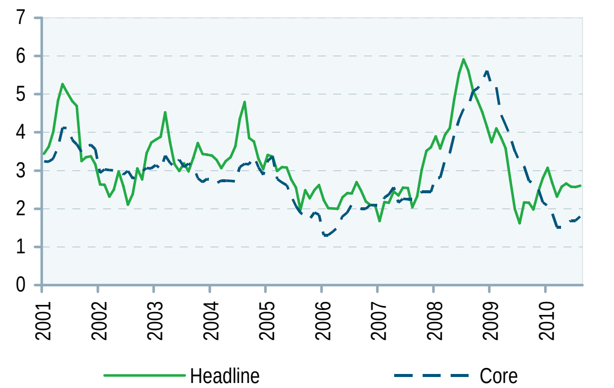
Based on the factors outlined above, we believe that headline inflation will stay within the current range of 2.5-3.0% well into 2011. Stable inflation will lead to gradual hikes in policy rates for the time being. Concerns about growth clearly outweigh concerns about the domestic and global economies, in our opinion.

Chart 1: GDP and the employment rate



Sources: Bank of Korea, Statistics Korea

Chart 2: Headline and core CPI inflation *(% y/y)*



Source: Statistics Korea

Sri Lanka

Samantha Amerasinghe, Economist
Standard Chartered Bank, Sri Lanka
+94 11 2480015, Samantha.Amerasinghe@sc.com

- **Board of Investment estimates FDI inflows will reach USD 0.6bn by year-end**
- **FDI inflows may be a critical indicator of the country's growth prospects**
- **Bureaucratic processes are the main stumbling block to attracting FDI**

FDI inflows need to gather pace in H2

Attracting FDI is critical to growth

A 16.8% drop in inflows in H1-2010 versus the year-earlier period, when the country was still at war, does not bode well

Sri Lanka may fall short of the government's USD 1bn FDI target in 2010. The H1-2010 FDI statistics released by the state-run Board of Investment (BOI), which promotes industrial investment in Sri Lanka, has sparked much debate, as the numbers were far below expectations. The BOI has estimated 2010 FDI inflows at USD 0.6bn, equal to what the country received during the war-ravaged year of 2009. Given the improved economic environment in 2010, FDI inflows should have been much stronger. Investment in the real economy is what matters most, and the 16.8% drop in inflows in H1-2010 versus H1-2009, when the country was still at war, is not promising. Inflows for the first six months of 2010 were only USD 0.2bn (down from USD 0.25bn in 2009), although USD 2bn worth of FDI projects had been approved by the BOI up to end-June.

While global FDI flows declined by 14% in 2008 and dropped by an even larger 29% in 2009 (according to UNCTAD figures), FDI inflows into Sri Lanka rose to a record USD 0.89bn in 2008, then slowed in 2009 to USD 0.6bn. While flows to Sri Lanka were not immune to the global financial crisis, the reasons for the decline in FDI in 2009 were two-fold: (1) a non-conducive business environment due to both domestic factors and the global crisis, and (2) the high fiscal deficit, which triggered investor concerns about the structural soundness of the economy.

Ease of doing business cited as key driver of FDI

Significant efforts are needed to revamp the overly bureaucratic FDI approval process, which appears to be the main stumbling block

Historically, sluggish investment growth has been attributed to Sri Lanka's cumbersome FDI approval process. The ease of doing business has been cited as a key driver of foreign investment, and the country's ranking slipped to 105 in the World Bank's 2010 'Doing Business' report from 97 a year earlier. While the war obviously impeded Sri Lanka's ability to realise its potential for attracting FDI, excessive bureaucracy appears to be an even bigger stumbling block. As Sri Lanka's buoyant growth drives increasing capital requirements (our 2010 growth estimate is 6.8%) and a need to expedite infrastructure development, a significant shift towards investment-friendly policies and an acceleration of the liberalisation process are needed to attract further investment. The creation of a cabinet committee last month to look into easing the FDI approval process is encouraging. According to provisional figures for H1-2010, the bulk of foreign investment (almost 60%, or USD 120mn) was channelled into the infrastructure sector, while the manufacturing sector attracted 27% of flows, agriculture attracted 12.5%, and the services sector – which contributes almost 60% of GDP and includes the booming tourism sector – received just USD 2mn, or 1% of flows.

Sri Lanka (con'd)

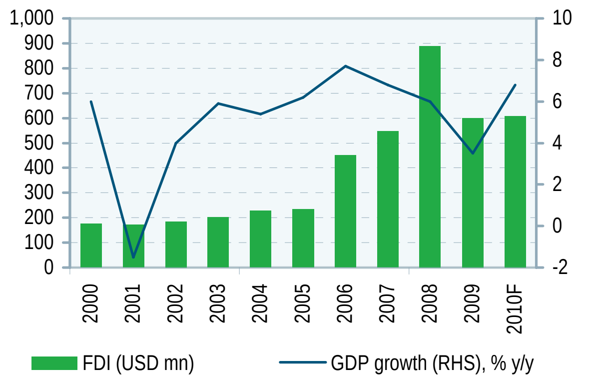
IMF board has endorsed the government's progress in implementing key fiscal reforms

Longer-term investors may adopt a 'wait and see' approach

We expect FDI inflows to gather pace in H2-2010 based on the usual seasonal pattern. Our forecast for longer-term net FDI inflows, at USD 0.6bn, is similar to the BOI forecast. We expect Sri Lanka's USD 1bn sovereign bond issue in September to be oversubscribed, boosting foreign investor sentiment. However, in our view, longer-term investors are likely to remain cautious towards starting large projects as they assess whether Sri Lanka can sustain its current macroeconomic stability. On the upside, we have observed a positive change in investors' mindset, thanks to the post-war economic recovery and the robust growth outlook for H2-2010, driven by strong fundamentals. The awarding of a contract in August for the USD 0.5bn Colombo South Port project to a China-Sri Lanka shipping consortium with a 55% stake in the deal is likely to add further impetus to FDI flows by year-end. Furthermore, the IMF board has endorsed the government's progress in implementing key fiscal reforms following the successful fourth IMF staff review under the USD 2.6bn Stand-by-Arrangement in mid-August. The IMF said that the "economy is getting on track, gaining momentum and being built on strong fundamentals". It is confident that the target of reducing the budget deficit to 8% of GDP in 2010 will be achieved, and has approved the September release of the fourth tranche of USD 0.2bn.

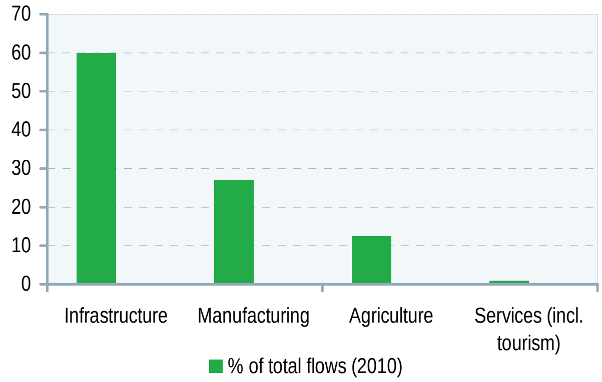
Sri Lanka's move towards fiscal consolidation is on track, with the latest central bank data showing that the budget deficit narrowed by 15.49% y/y in H1-2010 to LKR 215bn as government revenues rose sharply. Tax revenues increased by almost 16% after the effective tax rate on vehicle imports was slashed by about 50% in June. Tax revenue from vehicles soared by 240% m/m to LKR 1.7bn in July due to increased purchases of imported cars. This has helped the government to stick to its fiscal targets, shoring up investor confidence. The successful implementation of reforms helped Sri Lanka build up its FX reserves to a record USD 5.8bn in July, which should provide added comfort to investors. While we are confident that Sri Lanka will become an increasingly attractive destination for FDI, it is imperative that FDI inflows are strong enough to support the country's post-war economic growth potential.

Chart 1: FDI growth needs to gather pace in H2



Sources: CBSL, Standard Chartered Research

Chart 2: Sectors attracting highest FDI flows



Sources: Standard Chartered Research

Thailand

Usara Wilaipich, Senior Economist, Thailand
Standard Chartered Bank (Thai) PCL
+662 724 8878, Usara.Wilaipich@sc.com

- **Economic growth was buoyant in Q2-2010, despite political turmoil**
- **Resilient fundamentals should bring Thailand back into focus for foreign investors**
- **We expect more portfolio inflows, leading to a monetary policy dilemma**

Bulletproof economy

Solid fundamentals and exports lead to resilience

Thai economy has shown considerable resilience to the political turmoil in Q2-2010

Despite the worst political turmoil in years, Thailand has managed to keep its economic performance broadly in line with the region's. This is evident in healthy real GDP growth of 10.5% in H1-2010 – the fastest since 1995. The country's economic resilience to the political turmoil was supported by sound macroeconomic fundamentals including healthy household savings, low corporate indebtedness, a prudent fiscal position, limited asset-price inflation and a robust external payments position (for more details, see **Special Report, 23 August 2010,** '**Thailand – Economic resilience amid political turbulence**'). Separately, the Thai economy benefited from strong 36% y/y export growth in H1-2010, driven by global inventory restocking.

Portfolio inflows set to return

Buoyant growth performance is luring foreign investors back to the country

Buoyant economic growth should bring Thailand back onto foreign investors' radar screens. Since 2000, foreign investors appear to have been underweight Thai stocks, as indicated by sluggish foreign net buying (shown in Chart 1). This is understandable given foreign investors' concerns about ongoing political instability.

The silver lining of foreign investors' underweight position in Thai stocks is that there is less downside risk from foreign selling going forward. It also points to significant potential for investors to return to Thailand once they recognise the country's solid and resilient economic fundamentals.

Against this backdrop, potential portfolio inflows into Thailand could put further appreciation pressure on the Thai baht (THB). Although political uncertainty remains, the country's economic performance in recent quarters suggests that the political unrest has had only a limited market impact.

The political environment on the ground has gradually improved since the end of the violent anti-government protests in Bangkok in April and May, although ongoing tensions between the ruling Democrat Party and supporters of former Prime Minister Thaksin Shinawatra continue to cloud the long-term political outlook. Recently, Fitch Ratings commented that it may upgrade its outlook on Thailand's A- local-currency rating from negative to stable.

A monetary policy dilemma

Given the strong recovery in H1-2010, the Bank of Thailand (BoT) started normalising policy rates in June. Following a 25bps policy rate hike at the June

Thailand (con'd)

BoT is likely to maintain a gradual approach to interest rate normalisation

Monetary Policy Committee (MPC) meeting, the BoT hiked by another 25bps in August, raising the benchmark 1-day repo rate to 1.75%.

Based on the BoT's recent hawkish post-meeting statements, the rate normalisation process is likely to continue. We expect one more 25bps hike at the next MPC meeting on 20 October, taking the benchmark rate to 2.0%. Thereafter, we expect the BoT to stay put until the end of Q3-2011. Our forecast is based on the belief that the BoT needs to balance inflation risks with the potentially rapid THB appreciation arising from higher interest rates, which would undermine Thailand's exports.

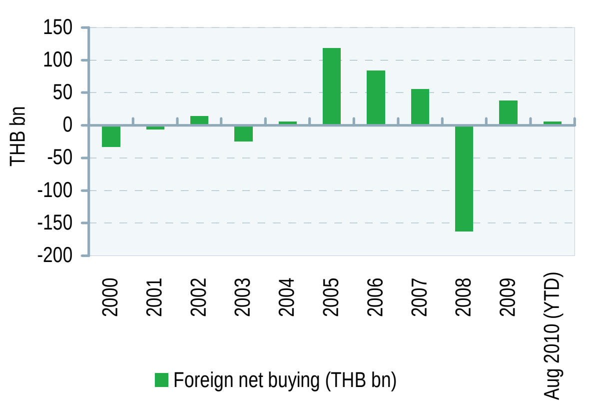
A strong THB hurts and helps

As of 30 August 2010, the THB had strengthened by 6.6% against the US dollar (USD) this year. This was faster than most other Asian currencies – including the Chinese yuan, Korean won, Taiwan dollar, Singapore dollar, Philippine peso, Indonesian rupiah, Indian rupee and Vietnamese dong – despite the political unrest in Q2-2010.

Given the potential for rising portfolio inflows in coming quarters, THB appreciation may accelerate. This would undermine Thailand's export competitiveness, slowing the key engine of the recovery. This is particularly worrisome given that there are already growing signs of a slowdown in export growth in H2-2010.

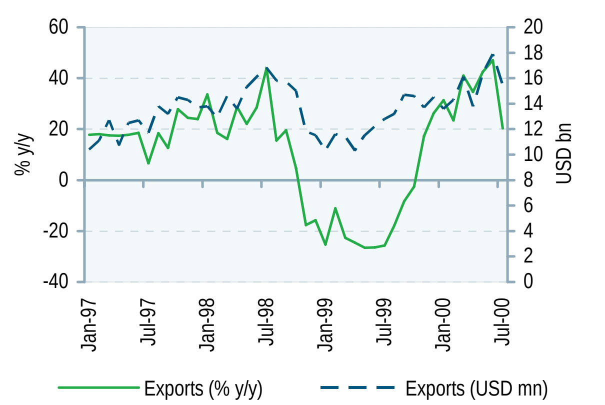
On a positive note, THB appreciation thus far should help to contain import prices and inflation down the road. Also, with interest rates in the US and other major economies likely to stay exceptionally low for an extended period, this should allow the BoT to keep its policy rate unchanged until there are clear signs of a more stable THB.

Chart 1: Foreign net buying in Thai stock market



Sources: SET, Standard Chartered Research

Chart 2: Thai export growth *(% y/y)*



Sources: BoT, Standard Chartered Research

UAE

Shady Shaher, Economist, MENA
Standard Chartered Bank, Dubai
+9714 508 3647, Shady.Shaher@sc.com

- **Economic growth outlook for 2010 improves on pick-up in non-oil growth**
- **Oil sector stabilises after contracting in 2009**
- **Credit conditions remain extremely difficult, highlighting challenging conditions**

Growth, liquidity and the markets

UAE outlook

We forecast 2010 growth at 3.0% on the improved outlook for non-oil sectors

Sultan Mansouri, the UAE economy minister, says he expects clear skies ahead, compared with the overcast conditions of last year. We forecast positive growth of 3.0% this year, despite uncertainties and risks such as weak credit growth. Inflation is low, and this is unlikely to change; in fact we believe the official numbers may overestimate inflationary pressures. However, with bank loans still exceeding deposits, credit conditions are likely to remain tight.

Where is growth coming from?

Oil production is stabilising in 2010 after dropping by 12% in 2009

Growth is finding support from both the oil and non-oil sectors. The oil sector makes up close to 30% of the UAE economy. In 2009, the oil sector was one of the biggest drags on growth as the UAE cut production by close to 12% versus 2008 levels. In addition, oil prices dropped from an average of USD 99/barrel in 2008 to about USD 62/barrel in 2009, making expansionary spending more challenging. Higher oil prices and stable production should allow the oil sector to make a positive contribution to growth in 2010.

There is also positive news from the non-oil sectors of the economy. The trade sector is significant for Dubai, with the ‘trade & wholesale’ component making up close to 40% of Dubai’s GDP. Official figures show that Dubai’s non-oil trade increased by 18% y/y in H1-2010 to USD 76 bn. Exports from Dubai rose by 38% to USD 8.93bn, and imports climbed by 13% to USD 48.3bn. More importantly, re-exports rose by 20% to USD 18.78bn. The re-export sector is of particular significance, as Dubai is the world’s third-largest re-export hub. While the increase in imports is detracting from growth dynamics, it is consistent with a pick-up in domestic economic activity and demand.

Dubai’s aviation sector is also showing strength, with the number of passengers travelling through Dubai International Airport hitting 4.3mn in July this year, up 14.3% from a year earlier. Year-to-date through July, passenger numbers were up 16% to 26.8mn. Air traffic cargo is also picking up – the emirate handled 197,845 tonnes in July, a 23.5% increase over the same month last year, while the year-to-date figure was 1.3mn tonnes, up 25.5% from last year. Abu Dhabi’s aviation sector is also growing, with passenger numbers rising by 9.2% y/y in July, while air cargo traffic increased by 12.3%. Hotel occupancy rates in Dubai had bounced back to 80% by June 2010, after plunging to close to 50% in January, according to government statements. Abu Dhabi reported a 16% y/y rise in the number of hotel guests in July, the ninth consecutive month of double-digit growth. Meanwhile, the Dubai Chamber of Commerce predicts that the value of retail

UAE (con'd)

sales will increase by 3.5% this year, pointing to a subdued pick-up in consumer spending.

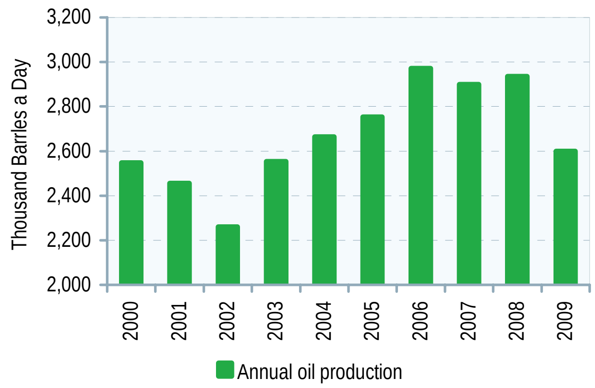
Inflation is probably lower than statistics suggest

Inflation in the UAE has remained subdued, at 0.9% y/y and 0.3% m/m in July, as higher fuel prices resulting from local gasoline price hikes caused the transport component (9.9% weighting in the CPI basket) to rise by 3.5% m/m. Housing costs continue to fall, with the housing and energy component (39% of the basket) dropping by 0.2% m/m in July. However, we believe that the housing component of the CPI does not accurately reflect deflationary dynamics in the UAE housing market – last year, this component rose by 0.42%, lifting the overall index by 1.56%, which surprised us given the sharp property-market correction during the year. We believe this component of the CPI basket is likely to face further disinflationary pressures, keeping UAE inflation subdued in 2010.

Credit growth is non-existent

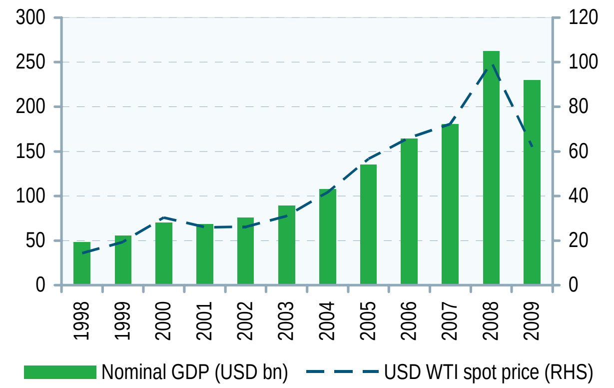
UAE credit growth is very weak, with private-sector credit falling 3.2% y/y and rising 0.6% m/m in June. A key reason for this is that bank loans still exceed deposits. The gap narrowed from AED 40.2bn in June to AED 26.6bn in July, but this was solely the result of increased deposits and flat credit growth on a m/m basis. The lack of credit growth is draining liquidity from the system. It is also interesting to note that interbank rates in the UAE remain significantly higher than US LIBOR, despite the fact that the UAE dirham (AED) is pegged to the USD; 3M EIBOR is currently at 2.337%. The loan-deposit gap is one factor keeping EIBOR higher, but it is not the only reason. While the gap has been narrowing since April 2010, the spread between 3M EIBOR and 3M LIBOR rates has widened during the period. This could be partly because of a risk premium in the UAE, but also because of inefficiencies in the fixing process for interbank rates in the UAE.

Chart 1: UAE oil production trended lower in 2009



Sources: BP Statistical Review of World Energy 2010

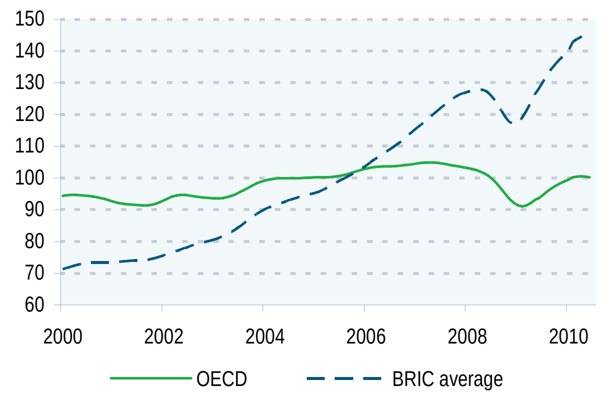
Chart 2: UAE nominal GDP vs. oil price



Sources: UAE central bank, Standard Chartered Research

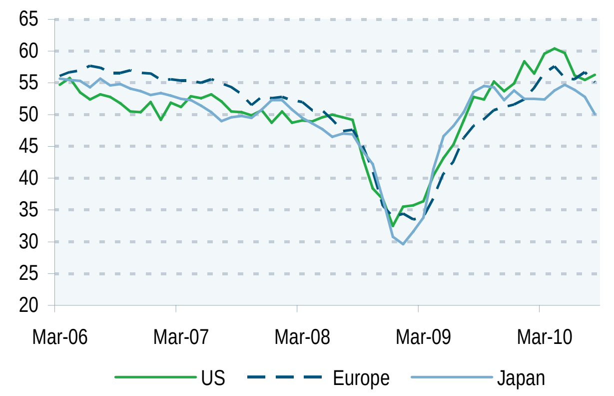
Market snapshots – Global and G3 economies

Chart 1: Emerging markets lead global recovery
OECD and BRIC leading Indices



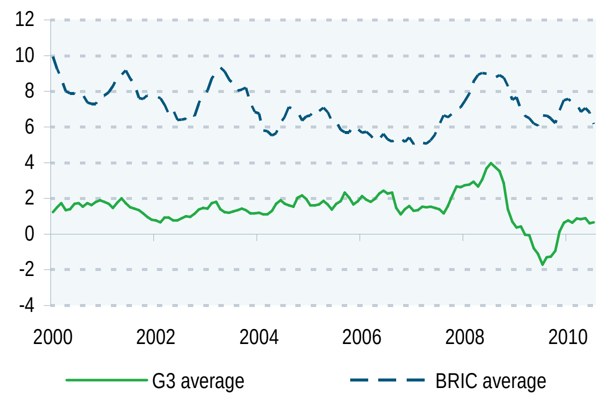
Sources: Bloomberg, Standard Chartered Research

Chart 4: Recovery in G3 economies is plateauing
PMIs



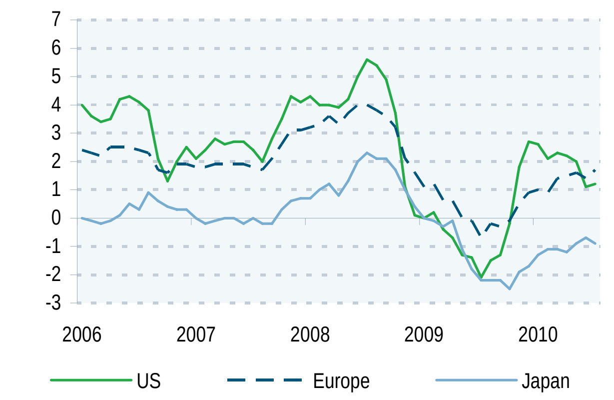
Sources: Bloomberg, Standard Chartered Research

Chart 2: Inflation risk remains low
G3 and BRIC inflation, % y/y



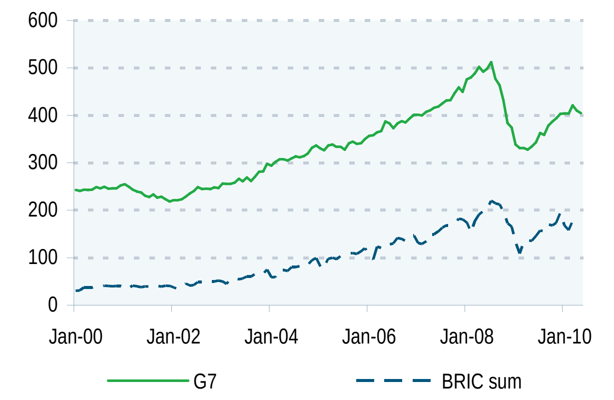
Sources: Bloomberg, Standard Chartered Research

Chart 5: G3 inflation is capped by spare capacity
Headline CPI, % y/y



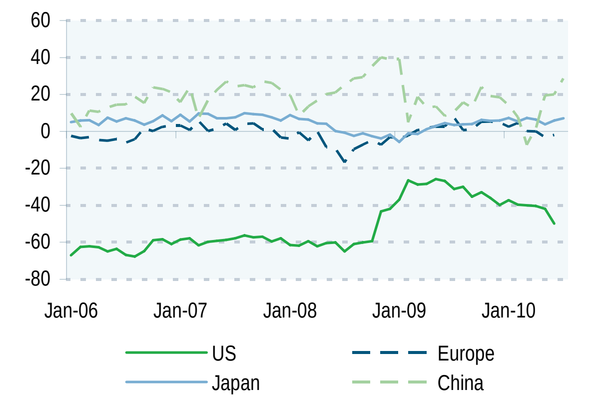
Sources: Bloomberg, Standard Chartered Research

Chart 3: Global exports edging towards the 2008 peak
OECD exports, BRIC exports (USD bn)



Sources: Bloomberg, Standard Chartered Research

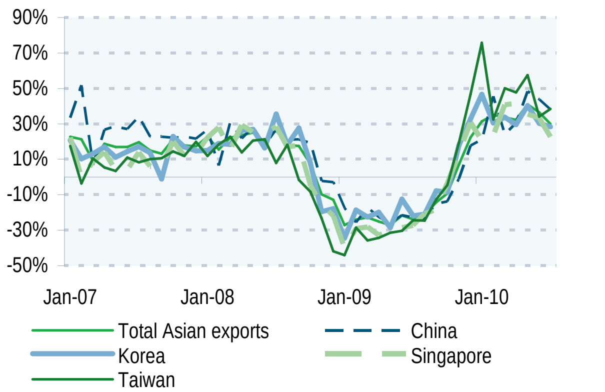
Chart 6: Trade imbalance is widening again
G3, China trade balances (USD bn)



Sources: Bloomberg, Standard Chartered Research

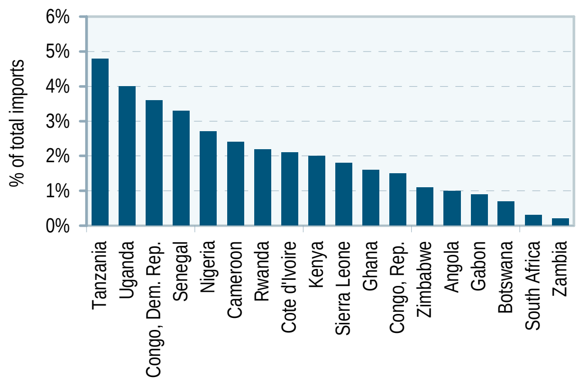
Market snapshots – Asia and Africa

Chart 7: Export recovery is reaching a plateau
% y/y



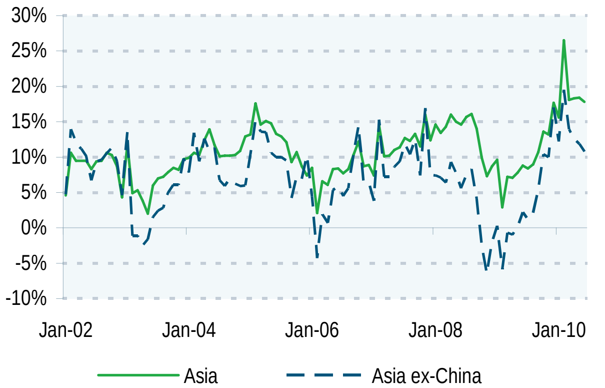
Sources: CEIC, Standard Chartered Research

Chart 10: Rising wheat prices appear manageable for most African countries
Wheat imports as % of total imports, 2007



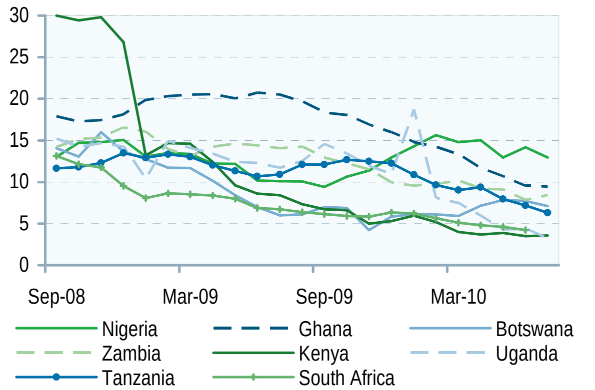
Sources: FAO, Standard Chartered Research

Chart 8: Asian consumers show resilience
Retail sales index, GDP-weighted, % y/y



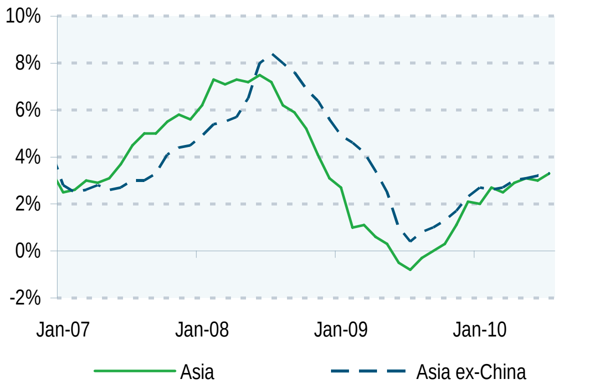
Sources: CEIC, Standard Chartered Research

Chart 11: CPI trends allow for easy monetary policy
'Frontier' Africa inflation by country, % y/y



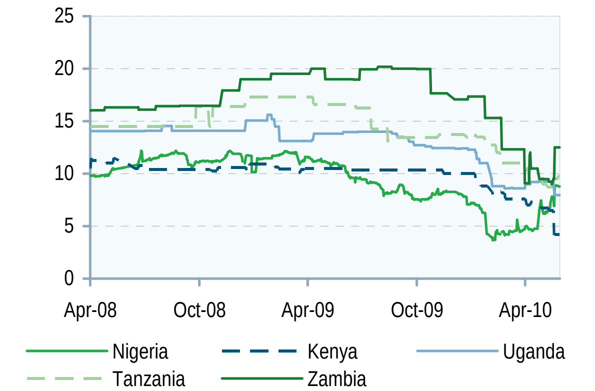
Sources: Datastream, Standard Chartered Research

Chart 9: Asian inflation to pick up in months ahead
CPI, % y/y



Sources: CEIC, Standard Chartered Research

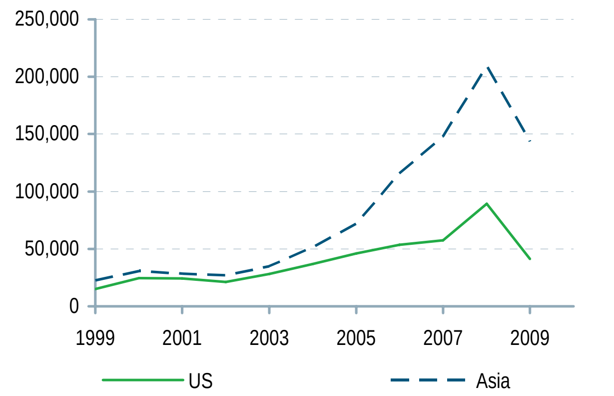
Chart 12: Increased supply, tighter liquidity could end rally in African bonds *(5Y yield since April 2008, %)*



Source: Standard Chartered Research

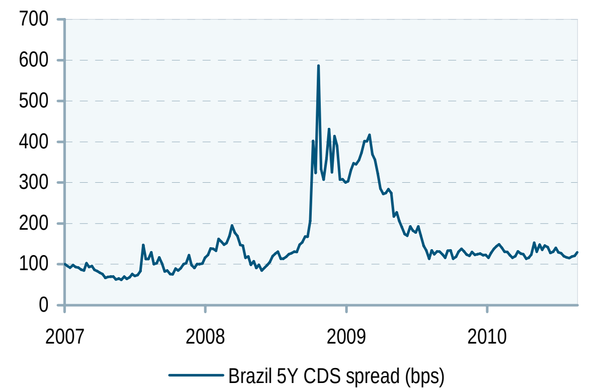
Market snapshots – MENA and Latam

Chart 13: MENA trade with Asia overtakes flows to US
USD



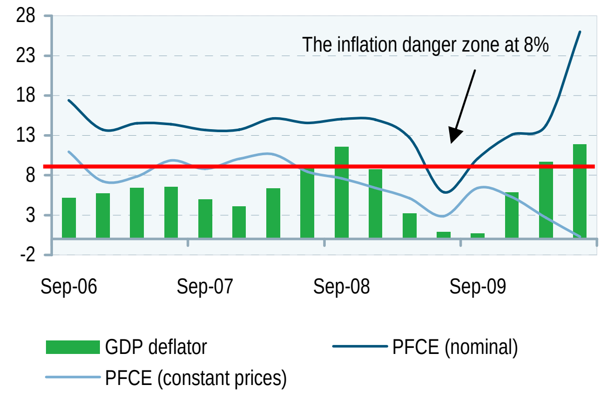
Sources: IMF DOTS, Standard Chartered Research

Chart 16: Market unconcerned about Brazil's October presidential elections



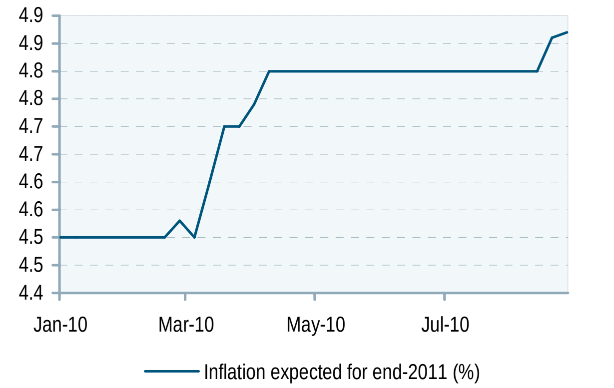
Sources: Bloomberg, Standard Chartered Research

Chart 14: India – high inflation hits real consumption
% y/y growth, base: 2004-05



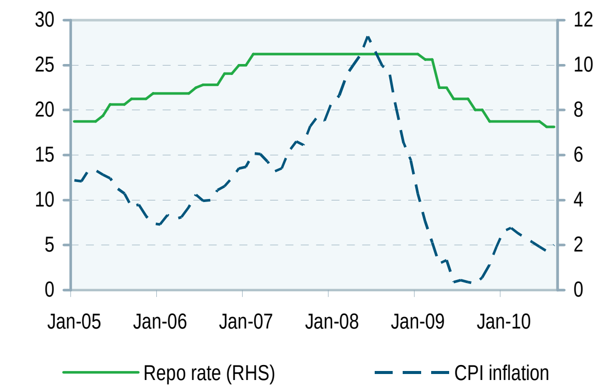
Sources: CSO, Standard Chartered Research

Chart 17: Brazil inflation expectations for 2011 are above the 4.5% inflation target



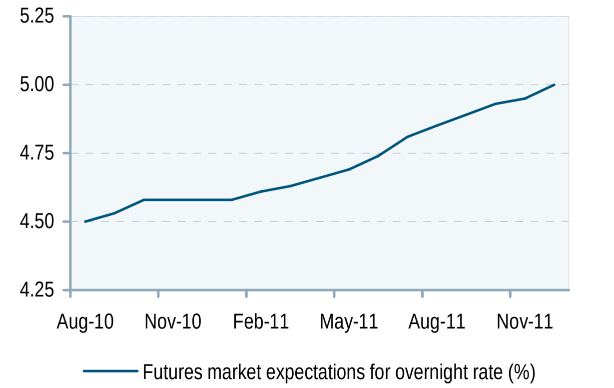
Sources: Bloomberg, Standard Chartered Research

Chart 15: Sri Lanka has room for further rate cuts
CPI inflation, % y/y; repo rate, %



Sources: CBSL, Standard Chartered Research

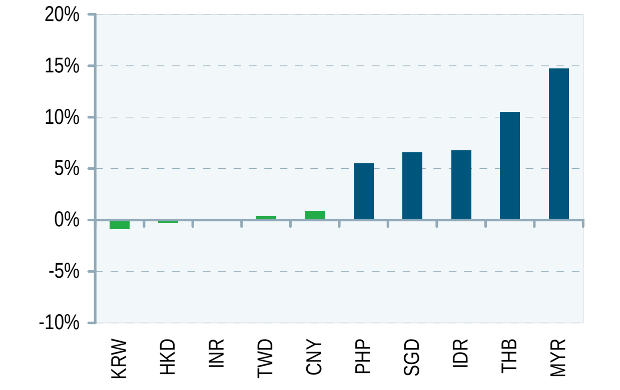
Chart 18: Mexico rate-hike expectations are very low



Sources: Bloomberg, Standard Chartered Research

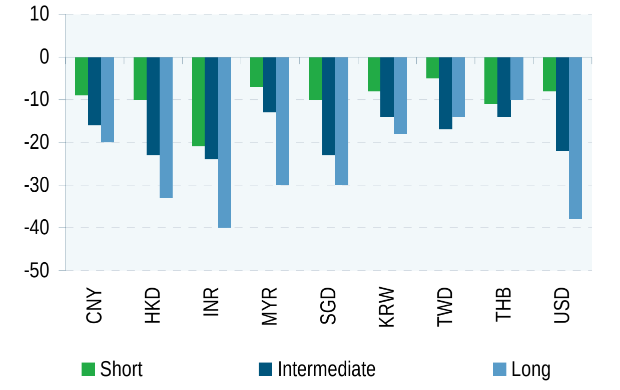
Market snapshots – FX and rates

Chart 19: SEA Currencies have outperformed NEA and SA currencies in 2010 *(changes from 01/01/2010)*



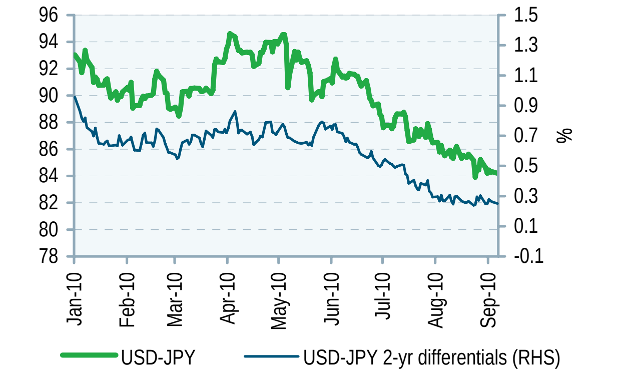
Sources: Bloomberg, Standard Chartered Research

Chart 22: Bullish sentiment prevails in Asian rates
Changes in IRS levels since 01-Aug-10 (bps)



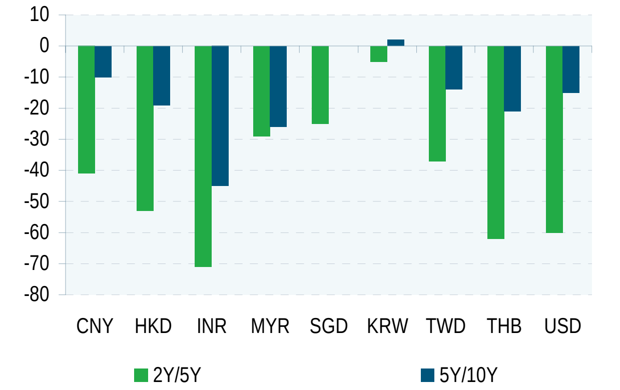
Sources: Bloomberg, Standard Chartered Research

Chart 20: Narrowing Interest differentials continue to drive USD-JPY downwards



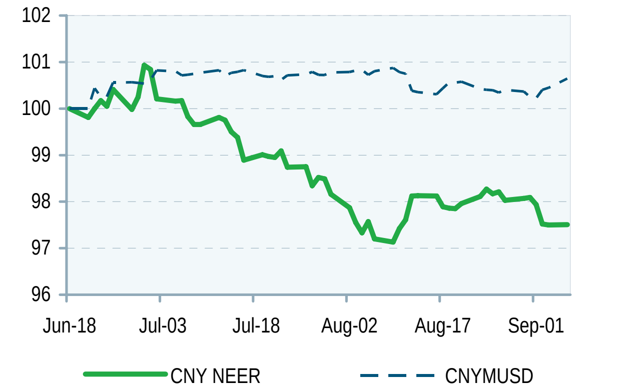
Sources: Bloomberg, Standard Chartered Research

Chart 23: Flattening to move out the maturity curve
Changes in IRS slopes since 01-Aug-10 (bps)



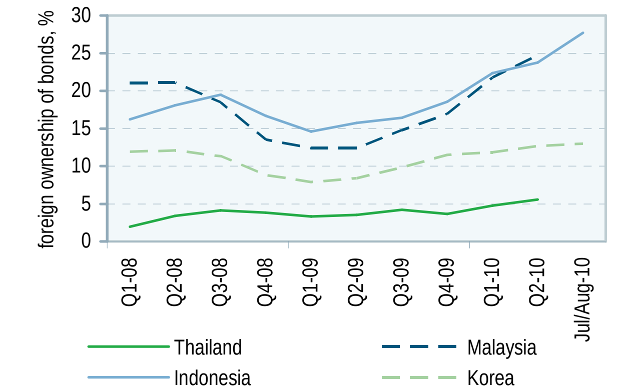
Sources: Bloomberg, Standard Chartered Research

Chart 21: Tentative signs of a correlation between the CNY fixes and a trade-weighted basket



Sources: Bloomberg, Standard Chartered Research

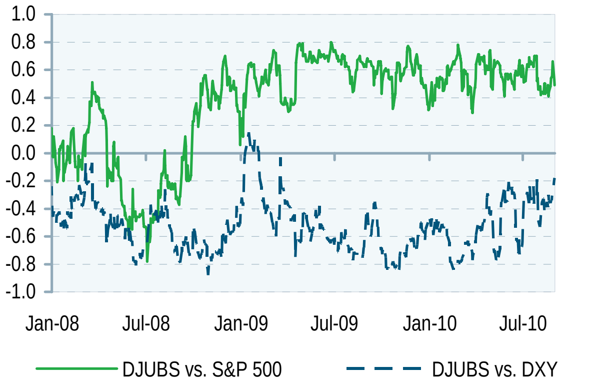
Chart 24: Hunt for yield pushes foreign ownership of Asian local-currency bonds to record highs



Sources: Bloomberg, Standard Chartered Research

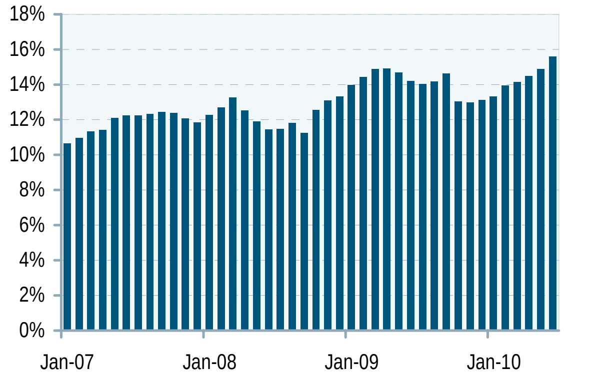
Market snapshots – Credit and commodities

Chart 25: DJUBS vs. DXY and S&P500
20-day rolling correlation



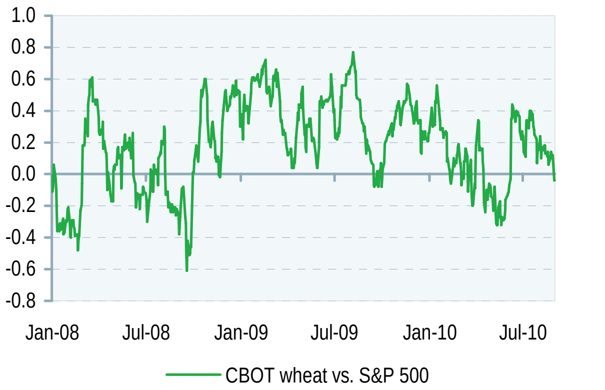
Sources: Bloomberg, Standard Chartered Research

Chart 28: EM bond funds increase allocations to Asia



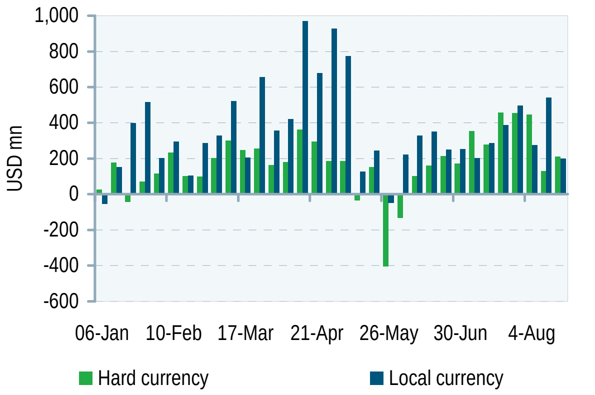
Sources: EPFR Global, Standard Chartered Research

Chart 26: CBOT wheat vs. S&P500
20-day rolling correlation



Sources: Bloomberg, Standard Chartered Research

Chart 29: Hard-currency and local-currency inflows into EM are running neck and neck

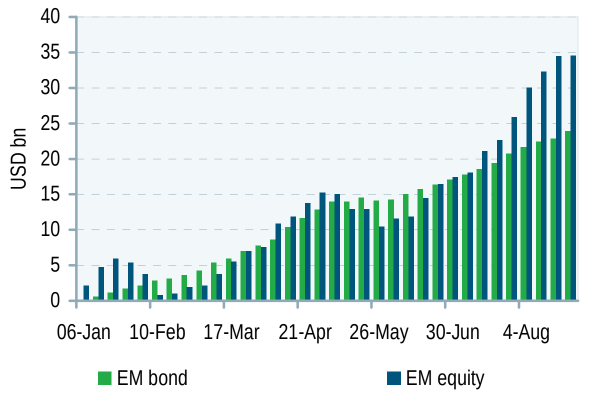


Sources: EPFR Global, Standard Chartered Research

Chart 27: Gold gains on risk aversion and continued strong investor interest

Sources: Bloomberg, Standard Chartered Research

Chart 30: YTD flows into EM bonds and equities are strong



Sources: EPFR Global, Standard Chartered Research

FX strategy summary

Currency	Fundamentals	S/T weighting (3-6 months)	M/T weighting (6 months+)
CNY	• Irregular, very gradual trend lower in USD-CNY fixes likely to year-end • Economic slowdown, benign ex-food inflation favour FX stability • Growth pick-up, policy mix, trade news favour faster 2011 CNY gains • Short USD-CNH offers better carry than short USD-CNY NDF • We are *Neutral* CNY and may move to *Overweight* early in 2011	Neutral	Neutral
HKD	• We see no reason for a change to the USD 7.75-7.85 link • USD-HKD edged up in August amid broader market jitters • Aggregate Balance is stable, as USD-HKD is comfortably within band • Weaker China growth should impact Hong Kong later in 2010 • We are *Underweight* HKD short-term, *Neutral* medium-term	Underweight	Neutral
KRW	• Bank of Korea well placed to foster stability in USD-KRW spot • Equity inflows have stalled since late April amid global slowdown • C/A surplus has improved due to weak KRW, strong exports • KRW may extend gains in 2011 on valuations, global growth pick-up • We raised our short-term FX rating to *Overweight* on 23-Mar-10	Overweight	Overweight
TWD	• Slowing export demand reinforces official preference for stable TWD • Very gradual near-term CNY appreciation may be reflected in TWD • Substantial external surplus remains important background positive • Major TWD advance (vs. USD) likely to be postponed until 2011 • We are *Neutral* S/term but *Overweight* further out	Neutral	Overweight
IDR	• Global recovery, low global interest rates should support IDR • Trade balance is deteriorating on strong domestic demand • Higher CPI inflation, positioning are short-term risks • We expect BI to raise rates in Q4, which should support the IDR • We reviewed and maintained both of our ratings on 13-Aug-10	Overweight	Overweight
MYR	• MYR has gained on FX liberalisation, strong fundamentals • Narrower trade balance surplus, BoP should be watched • BNM manages MYR against a basket with significant CNY weighting • Seasonal analysis shows MYR tends to outperform in Q4, Q1 • Economic slowdown, BoP are medium-term concerns	Neutral	Overweight
PHP	• Economic recovery and BoP dynamics provide support for PHP • Political developments are another positive • Inward remittances to drive PHP strength in Q4 • PHP should catch up with AXJ currencies into 2011 • We raised our short-term FX rating to *Overweight* on 07-Apr-10	Overweight	Overweight
SGD	• The economy should slow in 2011 on external exposure • The MAS will maintain gradual SGD NEER appreciation in October • BoP, fundamentals underline trend SGD strength • The SGD NEER trades at the strong end of the policy band • We raised our short-term FX rating to *Overweight* on 14-Apr-10	Overweight	Overweight

FX strategy summary (cont)

Currency	Fundamentals	S/T weighting (3-6 months)	M/T weighting (6 months+)
THB	• GDP rebound, robust trade and monetary tightening are THB positives • Seasonality and positioning are other near-term THB positives • Risk is a sharper-than-expected slowdown in the US and China • We raised our short-term FX rating to *Overweight* on 10-Aug-10 • Medium-term *Neutral* FX rating on political risk, China competition	Overweight	Neutral
VND	• Upward pressure on USD-VND has continued after devaluation • Further devaluations are likely given authorities' growth bias • Narrower trade deficit, inward FDI are positives • Further depreciation is priced in by onshore forwards/NDFs • We have had a short-term FX rating of *Neutral* since 24-Aug-09	Neutral	Neutral
INR	• Global fragility continues to weigh on the INR • India's growth outlook remains robust, but trade deficit is worrying • USD-INR is likely to trade in 45.80-47.50 range in the near term • INR gains to resume in Q4 as risk revives, FII inflows pick up • Faster CNY appreciation to help INR gains in 2011	Overweight	Overweight
PKR	• USD-PKR has resumed its uptrend on importer demand • Slowdown in private inflows, security concerns to weigh on the PKR • Export recovery, official aid are key to limiting PKR losses • Slow implementation of fiscal reforms poses risk to official inflows • Delay in release of aid would increase downside risks to PKR	Neutral	Neutral
SAR	• Inflationary pressures are likely to weigh on economy in 2010 • Fiscal stimulus is likely to support the economy in 2010 • USD-SAR forwards are in negative territory • We forecast a gradual growth recovery in 2010 and 2011 • We are *Overweight* SAR short-term, *Neutral* medium-term	Overweight	Neutral
AED	• Markets remain focused on Dubai's debt restructuring • USD-AED forwards are back to historical averages • Higher oil prices should support government revenues • Abu Dhabi will be a growth outperformer relative to Dubai • We are *Overweight* AED short-term, *Neutral* medium-term	Overweight	Neutral
KES	• KES has weakened abruptly amid broader market jitters • CBK surprised with a 75bps cut in July, no change expected in Sep. • Current account deficit has edged lower, but only marginally • We raised KES to *Neutral* from *Underweight* on 21-Jul-09 • Medium-term risks are evenly balanced; we are *Neutral* M/term	Neutral	Neutral
NGN	• Recent bi-weekly FX auctions have had a mild strengthening tone • Political, banking-sector event risk has faded to some degree • Oil price and production gains should lift external surplus • We raised our S/term FX rating to *Overweight* on 04-Nov-09 • We maintain a Medium-term recommendation of *Overweight*	Overweight	Overweight

FX strategy summary (cont)

Currency	Fundamentals	S/T weighting (3-6 months)	M/T weighting (6 months+)
BWP	• BWP has ground lower against ZAR in recent quarters • Diamond demand in US is recovering from depressed levels • BWP REER had been boosted by higher local inflation • Faster BWP downward crawl vs. basket is warranted M/term • We raised our S/term FX rating on BWP to *Neutral* on 29-Apr-09	Neutral	Underweight
ZAR	• USD-ZAR remains bearish; losses to 7.0604 expected • C/A deficit widened more than expected in Q1 • Net offshore bond purchases continue to provide support • Further out, C/A deficit, structural shortfalls are mild negatives • We cut our short-term FX rating to *Neutral* on 14-Jan-10	Neutral	Underweight
ARS	• USD-ARS trend points to breach of 4.00 by Q4 • June GDP growth surpassed 11% y/y, FX reserves hit USD 51bn high • Official GDP forecasts upgraded to 8% for 2010, 4-5% for 2011 • We believe there is a non-trivial risk the Kirchners win 2011 election • We are *Neutral* ARS short-term and medium-term	Neutral	Neutral
BRL	• USD-BRL breached 1.75 in September; 1.7240 is near-term support • Selic rate was not hiked in September; no hike expected in October • Growth expectations are peaking, hawkish rates bias is waning • The BRL is supported by high real interest rates • We raised our short-term rating to *Neutral* on 22-Apr-10	Neutral	Overweight
CLP	• USD-CLP broke through 500 in September; bearish bias remains • Strong resistance at 512 caps correction; good entry point to buy CLP • Domestic fundamentals are shifting interest rate outlook to hawkish • CLP is a play on global reflation and bullish commodity theme for H2 • We raised our short-term rating to *Overweight* on 09-Aug-10	Overweight	Overweight
COP	• Optimism about fiscal reforms and domestic recovery support COP • But COP is now expensive on a NEER and REER basis • CDS spreads imply Colombia sovereign is nearing investment-grade • Though we are more sceptical, an upgrade should happen this year • We raised our short-term rating to *Neutral* on 18-Aug-10	Neutral	Neutral
MXN	• MXN remains most vulnerable to deterioration in US confidence • Recent series of softer US data will keep MXN on a bearish bias • Local headlines on political assassinations darken mood further • Central bank comments remain dovish; no hikes likely for some time • After review in May, we remain *Neutral* MXN short-term	Neutral	Neutral
PEN	• PEN remains stable, helped by official intervention • After 6% y/y growth in Q1, markets look for 10% y/y for Q2 • S&P raised Peru's foreign-currency rating to positive from stable • Central bank hiked 50bps in August; we expect another 50bps in Sep. • We are *Neutral* PEN, both short-term and medium-term	Neutral	Neutral

FX strategy summary (con'd)

Currency	Fundamentals	S/T weighting (3-6 months)	M/T weighting (6 months+)
EUR	• EUR seeing renewed weakness in H2 on downside growth surprises • Euro-area debt and fiscal concerns continue to weigh near-term • EUR-USD to stabilise from 2011, when fiscal woes shift to the US • Medium-term, EUR-USD is supported by growth recovery • We lowered our short-term rating to *Underweight* on 21-May-10	Underweight	Neutral
JPY	• JPY has strengthened on risk aversion, narrowing rate spreads • Fiscal austerity dampens growth outlook amid persistent deflation • BoJ has responded to JPY strength with new QE measures • JPY rates should decline further, undercutting JPY • We cut our short-term FX rating to *Underweight* on 07-Jan-10	Underweight	Underweight
AUD	• AUD remains supported for now by growth, rates and trade surplus • But the cycle is peaking; we expect this to weigh on AUD into Q4 • The AUD remains overvalued on a trade-weighted basis • AUD to fall sharply into 2011 as China slows • We lowered our short-term rating to *Neutral* on 21-May-10	Neutral	Underweight
NZD	• New Zealand's economic recovery appears to be faltering • RBNZ has begun tightening, but rate hike expectations have been cut • Rising soft commodity prices support the external balance • Medium-term, NZD to outperform AUD as RBNZ plays catch-up • We raised our short-term FX rating to *Neutral* on 03-Apr-09	Neutral	Overweight
CHF	• Swiss growth is rebounding, despite deleveraging, unemployment • Switzerland's external surplus is recovering • Capital outflows are not enough to recycle this • Overvaluation remains a major medium-term concern • We raised our short-term FX rating to *Overweight* on 01-Apr-10	Overweight	Neutral
GBP	• GBP is starting to see renewed weakness as recovery falters • Post-election rally is over and fiscal tightening starts in September • BoE remains firmly on hold, despite high inflation prints • GBP to rebound from Q4 on undervaluation, focus shift to the US • We lowered our short-term FX rating to *Underweight* on 21-May-10	Underweight	Neutral
CAD	• CAD continues to outperform on better Canadian dynamics • BoC has begun its gradual tightening cycle; more to come • Canada's external balance appears to have stabilised • The CAD is 11.79% overvalued vs. USD on OECD PPP basis • We have had a short-term FX rating of *Overweight* since 14-Jul-09	Overweight	Overweight

Commodities short-term views

Commodity	Short-term (1M) view	Comments
Energy		
Crude oil (near future, USD/b)		
NYMEX WTI	Neutral	• Level of US oil demand remains weak, and crude stock levels have been climbing • China demand growth has decelerated, but demand level remains firm • Macro indicators are mixed; WTI is likely to continue to track equities • We expect prices to remain range-bound in the near term, as US demand is unlikely to recover before Q4
Refined oil products (USD/b)		
Singapore gasoil	Neutral	• Auto sales in India and China continue to grow, albeit at slower rates • China's net exports remain high, as do Singapore stock levels • Demand from Indonesia, India and Vietnam remains intact but more subdued • Our expected trading high of c.USD 15/barrel for the spread to Dubai has been reached; we turn neutral
Agricultural products		
Softs (near future)		
NYBOT cocoa, USD/tonne	Neutral	• The market has plummeted on prospects of large main-season crops in Côte d'Ivoire and Ghana • Cocoa hoarding in Indonesia is unlikely to drive prices higher • Risk premium will decline if Côte d'Ivoire presidential elections are successful
NYBOT coffee, USc/lb	Neutral	• Strong demand for milds is sustaining Arabica coffee demand • Premium between Arabica and Robusta coffee has widened • Widening Robusta supply, particularly in Vietnam and Brazil, may cap upside
NYBOT sugar, USc/lb	Bullish	• Prices have marched higher on supply concerns in Brazil • Poor weather in Russia and Pakistan will further constrain global output • Investor demand has improved and will limit downside short-term
Fibres		
NYBOT cotton, USc/lb	Bullish	• Strong demand from China continues to support prices • Flood damage has also lifted import demand from Pakistan • We expect global stocks to remain tight this season
Grains & oilseeds (near future, Usc/bu)		
CBOT corn (maize)	Bullish	• Fears of a sharp drop in projected US yields have gripped the market • Larger planted acreage in the US will limit upside • Weaker-than-expected European output is also supporting prices
CBOT soybeans	Neutral	• Global stocks are ample and are likely to rise at the end of the season • Consumption is supported by a weaker global rapeseed harvest • Sub-optimal weather conditions likely to impact output in key producers Brazil and Argentina
CBOT wheat	Neutral	• Wheat supply is being rationed through much higher prices • Russia has decided to extend its wheat ban until late 2011 • Market is now likely to consolidate at current elevated levels

Commodities short-term views (con'd)

Commodity	Short-term (1M) view	Comments
Metals		
Base metals (LME 3M, USD/tonne)		
Aluminium	Neutral	• A rally across the base metals complex should provide some support • China continues to export metal, adding to world oversupply • Demand is rising and warehousing deals are propping up prices
Copper	Very bullish	• Recent PMI data from China suggests upside surprises on demand • LME stocks continue to fall, and speculative interest is strong • Chilean mine output has turned higher but still lags demand growth
Lead	Bullish	• Demand is heading into a strong period before the year-end • LME stocks remain low • Problems continue at major smelter in Peru
Nickel	Neutral	• Stainless steel demand is showing early signs of improvement • Nickel pig iron production could be impacted by power problems • Mine supply should be boosted by settlement of major strike action
Tin	Neutral	• The long-term outlook is bullish, but a period of market consolidation is overdue • Recovery in demand is starting to lose momentum • Stocks are high in China and market is oversupplied
Zinc	Bullish	• Margins at smelters are being squeezed by low treatment charges • Physical premiums are trending higher in Europe
Precious metals (spot, USD/oz)		
Gold	Bullish	• Demand growth was stronger than expected in Q2 • Indian imports are surprising on the upside • Speculative interest remains strong, despite macroeconomic recovery
Palladium	Very bullish	• Prices have broken higher in recent weeks and technical picture looks strong • Improvement in China's auto sector bodes well for demand • Demand for physical ETFs is lacklustre for now
Platinum	Bullish	• Strong rebound in truck sales is boosting demand from diesel sector • China's imports were still strong in July • Speculative interest is muted
Silver	Bullish	• Has outpaced other precious metals in recent weeks, suggesting underlying strength • Rally in gold should help to support prices

Forecasts – Economies

Forecasts in BLUE (RED) indicate upward (downward) revisions over the past month

Country	Real GDP growth (%)				Inflation (yearly average %)				Current account (% of GDP)			
	2009	2010	2011	2012	2009	2010	2011	2012	2009	2010	2011	2012
Majors												
US^	**-2.6**	**2.5**	**1.0**	**1.9**	1.5	0.6	**0.4**	**1.2**	-2.9	-3.5	-3.6	-3.7
Euro area	-4.1	**1.7**	**2.0**	2.4	0.3	**1.5**	**1.8**	1.9	-0.3	**-0.3**	**-0.2**	0.3
Japan	-5.2	**2.5**	1.0	1.5	-1.4	-1.0	-0.7	0.5	2.8	3.6	3.6	3.0
UK	-4.9	**1.4**	1.8	2.4	2.2	**3.1**	**2.4**	1.5	-1.3	-1.7	-1.6	-1.4
Canada	**-2.3**	**3.0**	**2.2**	**2.5**	0.3	1.9	2.0	2.0	-2.7	-2.6	-2.5	-2.4
Switzerland	-1.5	1.9	2.5	2.6	-0.5	1.3	1.7	1.8	8.4	10.2	11.0	10.5
Australia	1.3	3.2	3.8	3.0	1.9	2.6	3.4	2.5	-4.1	-3.5	-3.7	-4.0
New Zealand	-1.6	1.6	2.0	2.5	2.1	**2.5**	3.0	2.5	-6.0	-5.5	-5.0	-5.5
Asia*	5.2	7.9	6.8	6.9	1.4	3.5	4.0	3.4	4.0	3.0	3.1	3.3
Bangladesh*	5.9	5.5	6.0	6.5	6.7	6.0	6.3	6.3	2.1	1.0	0.8	0.5
China	**9.1**	10.0	**8.5**	8.0	0.1	**2.5**	**4.0**	**3.0**	**5.9**	**4.8**	**5.3**	**6.0**
Hong Kong	-2.7	**6.0**	5.0	5.0	0.5	**2.5**	**4.0**	**4.0**	9.0	9.5	10.0	11.0
India*	7.4	8.1	8.5	8.8	3.9	8.2	5.0	4.5	-3.0	-2.7	-1.5	-1.5
Indonesia	4.5	6.2	6.5	7.0	4.9	**5.4**	**6.1**	6.2	2.0	1.0	0.5	0.5
Malaysia	-1.7	**6.2**	**4.5**	**6.0**	0.6	2.0	2.5	2.5	16.7	17.0	15.0	15.5
Pakistan*	1.2	4.1	**2.5**	4.5	20.8	**11.7**	**15.0**	**12.0**	**-5.6**	**-2.0**	**-3.0**	**-3.2**
Philippines	0.9	**6.8**	5.0	5.0	3.2	**3.8**	3.3	4.0	5.3	5.5	5.2	4.8
Singapore	-1.3	**11.0**	**4.0**	**8.0**	0.6	2.9	2.5	**2.5**	19.1	17.0	15.0	15.8
South Korea	0.2	6.0	4.1	5.2	2.8	2.7	2.8	3.0	5.1	**2.0**	**1.0**	**0.5**
Sri Lanka	**3.5**	**6.8**	6.5	7.0	3.5	**5.2**	5.1	5.5	-2.0	**-6.0**	-2.0	-2.5
Taiwan	-1.9	**8.8**	4.1	**6.0**	-0.9	1.3	**2.2**	2.2	11.2	**9.6**	**8.4**	**7.5**
Thailand	-2.3	**6.3**	**4.0**	5.8	-0.8	3.2	3.7	3.8	7.1	**3.0**	**1.3**	**0.4**
Vietnam	5.3	6.7	7.2	7.0	7.0	9.5	8.5	8.0	-7.0	-8.5	-6.5	-6.0
Africa*	1.2	4.8	6.0	5.8	10.5	7.7	7.9	6.6	-2.5	-0.2	1.0	1.7
Angola	-0.2	**6.0**	8.0	7.0	14.0	15.0	10.0	9.0	-3.5	3.0	3.0	5.0
Botswana	-4.0	7.6	3.9	4.3	8.3	6.8	**6.6**	**7.2**	0.5	3.0	5.2	6.0
Cameroon	2.0	3.0	4.0	3.5	3.0	2.5	2.5	2.0	-6.0	-4.2	-4.0	-3.5
Côte d'Ivoire	3.7	3.0	5.0	5.5	5.0	3.5	2.5	2.5	1.5	-1.5	-1.5	-1.0
The Gambia	4.0	4.5	6.0	6.0	6.5	6.8	6.0	6.0	-17.0	-18.0	-18.0	-17.0
Ghana	4.7	7.7	9.8	11.1	19.5	**11.0**	**10.8**	**9.7**	-10.2	-8.0	2.0	3.8
Kenya	2.6	3.8	4.9	4.0	21.1	**4.3**	7.4	7.3	-4.5	-4.0	-4.2	-4.7
Nigeria	4.2	6.6	8.5	7.8	12.0	**10.4**	**11.9**	**7.6**	2.0	8.0	12.0	14.0
Sierra Leone	4.0	5.0	6.0	6.0	10.0	7.5	7.5	7.5	-9.1	-8.5	-6.5	-5.5
South Africa	-1.8	3.0	3.6	3.8	7.4	**4.6**	**5.0**	5.3	-4.3	-4.9	-5.3	-5.8
Tanzania	5.5	5.9	6.4	6.7	12.7	**6.0**	8.0	7.2	-9.0	-7.0	-10.1	-9.9
Uganda	6.3	6.4	6.8	7.5	13.5	**5.2**	7.7	6.5	-6.4	-7.2	-7.8	-6.8
Zambia	6.4	5.5	5.8	6.4	13.6	**8.9**	10.5	9.8	-3.2	-4.2	-3.2	-2.8
MENA*	2.5	4.4	4.3	4.3	5.5	5.4	6.9	6.5	4.6	7.9	7.1	6.5
Algeria	2.1	4.0	5.0	5.0	5.6	5.0	3.5	3.0	-1.0	1.0	2.0	2.0
Bahrain	3.0	3.0	4.0	4.0	1.2	**2.5**	3.5	3.5	2.0	14.0	17.0	17.0
Egypt*	4.7	**5.3**	**6.0**	5.0	**9.9**	**11.7**	**10.0**	8.5	-2.3	-1.8	-1.0	-1.0
Iran*	**1.0**	**3.0**	3.0	4.0	**13.5**	**12.0**	16.0	15.0	11.0	10.0	11.0	10.0
Jordan	3.0	**3.4**	**3.5**	5.0	0.2	**5.2**	**5.3**	5.0	-10.0	-8.8	-7.0	-6.0
Kuwait	-5.5	3.0	3.5	3.0	3.0	**3.5**	4.5	4.0	20.0	26.0	22.0	20.0
Lebanon	**7.0**	**6.7**	**6.0**	4.5	3.4	3.5	4.5	4.5	-11.5	-9.5	-12.0	-12.0
Libya	2.0	5.0	5.0	4.0	**2.4**	**3.0**	**4.0**	6.0	22.0	31.0	22.0	20.0
Morocco	**4.9**	**4.0**	4.5	4.5	**1.0**	**1.1**	2.5	2.5	-0.5	-0.1	0.5	0.5
Oman	3.7	4.0	4.0	4.0	3.6	**4.0**	6.0	6.0	1.0	6.5	7.0	7.0
Qatar	9.0	**8.0**	4.0	4.0	-5.0	**-2.0**	**3.0**	5.5	4.2	17.0	25.0	20.0
Saudi Arabia	0.2	3.0	3.5	3.0	4.4	**5.7**	4.5	4.0	6.0	10.0	6.5	5.5
Tunisia	**3.0**	3.5	4.0	4.5	**3.5**	**4.8**	**4.0**	3.5	-4.0	-3.4	-2.5	-2.5
Turkey	-4.7	**6.2**	**5.8**	5.5	6.3	8.2	6.5	5.5	-2.2	**-2.8**	**-3.7**	-5.7
UAE	1.3	3.0	4.5	5.0	1.5	1.0	3.5	4.0	0.0	3.2	3.5	5.0
Latin America*	-2.0	5.4	4.0	4.2	4.7	5.2	4.7	4.7	-0.2	-1.6	-2.0	-2.3
Argentina	0.9	**7.1**	**4.0**	3.5	6.2	**8.9**	8.5	8.3	3.7	1.5	0.5	0.5
Brazil	-0.2	6.3	3.9	4.5	4.9	**5.8**	4.8	4.5	-1.5	-2.7	-2.9	-3.0
Chile	-1.5	**5.2**	4.0	4.5	1.5	3.3	3.6	4.0	2.2	2.8	1.5	1.1
Colombia	0.8	3.7	4.5	4.8	2.5	3.0	3.8	4.5	-1.9	-3.0	-3.3	-2.8
Mexico	-6.5	3.7	4.0	3.8	5.3	4.3	3.9	4.1	0.5	-1.3	-1.5	-2.5
Peru	0.9	**7.5**	5.0	4.0	**2.9**	2.5	3.0	3.25	-0.5	-1.5	-2.4	-2.6
Global*	-1.7	3.4	2.7	3.2	1.8	2.1	2.2	2.3	--	--	--	--

* Fiscal year starts in April in India, March in Iran, July in Bangladesh, Pakistan, and Egypt

** 2008 USD GDP weighted total of the regional economies covered in this publication

^ Inflation: Core PCE deflator used for US

Source: Standard Chartered Research

Forecasts – Markets

Forecasts in BLUE (RED) indicate upward (downward) revisions over the past month

Country	Exchange rate vs. USD						Short-term interest rates					
	07-Sep-10	Q4-10	Q1-11	Q2-11	Q3-11	Q4-11	07-Sep-10	Q4-10	Q1-11	Q2-11	Q3-11	Q4-11
Majors												
US	N.A.	N.A.	N.A.	N.A.	N.A.	N.A.	0.25 (FFTR)	0.25	0.25	0.25	0.25	0.25
Euro area	1.28	1.17	1.20	1.23	1.26	1.30	1.00 (Refi Rate)	1.00	1.00	1.25	1.50	1.75
Japan	84.2	92	90	88	86	85	0.10 (O/N Call Rate)	0.10	0.10	0.10	0.10	0.10
UK	1.54	1.43	1.47	1.51	1.55	1.58	0.50 (Bank Rate)	0.50	0.50	0.50	0.50	0.50
Canada	1.04	1.10	1.13	1.15	1.12	1.09	0.75 (O/N Lending Rate)	1.25	1.50	1.75	2.00	2.25
Switzerland	1.01	1.13	1.11	1.10	1.08	1.05	0.25 (LIBOR Target)	0.25	0.50	0.75	1.00	1.25
Australia	0.92	0.85	0.85	0.82	0.78	0.79	4.50 (OCR)	4.50	4.50	4.75	5.00	5.50
New Zealand	0.72	0.68	0.72	0.71	0.69	0.70	3.00 (OCR)	3.25	3.50	3.75	4.25	4.75
Asia												
Bangladesh	69.40	69.00	69.00	69.00	69.00	69.00	6.50 (RRP)	6.50	6.50	6.50	6.50	6.50
China	6.79	6.75	6.71	6.64	6.57	6.50	5.31 (1Y Base Lending)	5.31	5.31	5.58	5.85	5.85
Hong Kong	7.77	7.78	7.79	7.78	7.77	7.76	0.28 (3M HIBOR)	0.30	0.30	0.30	0.30	0.30
India	46.60	45.50	44.00	44.60	44.20	43.50	5.75(Repo rate)	6.25	6.50	6.50	6.50	6.50
Indonesia	9,003	8,800	8,800	8,900	8,800	8,500	6.50 (BI Rate)	7.00	7.75	8.00	8.00	8.00
Malaysia	3.12	3.08	3.05	3.18	3.12	3.00	2.75 (OPR)	2.75	3.00	3.50	3.50	3.50
Pakistan	85.80	87.8	88.6	89.0	90.0	90.8	12.86 (6M KIBOR)	13.40	13.80	13.80	13.80	13.80
Philippines	44.37	44.00	43.50	44.50	43.00	41.50	4.00 (RRP)	4.25	4.50	4.75	5.00	5.25
Singapore	1.35	1.33	1.32	1.34	1.31	1.28	0.50 (3M SIBOR)	0.50	0.50	0.50	0.50	0.50
South Korea	1,176	1,140	1,100	1,120	1,100	1,050	2.25 (Base Rate)	2.50	2.75	3.00	3.25	3.50
Sri Lanka	112.45	112.00	111.50	111.80	111.20	111.20	7.25 (RP)	7.25	7.50	7.50	8.00	8.00
Taiwan	31.94	31.60	31.20	31.10	30.75	30.25	1.38 (Discount Rate)	1.63	1.75	1.88	2.00	2.13
Thailand	31.21	30.50	30.25	31.50	30.80	30.20	1.75 (1-day Repo)	2.00	2.00	2.00	2.00	2.50
Vietnam	19,470	19,900	20,000	20,400	20,500	20,800	8.00 (Base Rate)	9.00	10.00	10.00	10.00	10.00
Africa												
Angola	90.85	93.00	93.50	93.75	94.00	94.25	20.3 (91-day T-bill)	18.50	18.50	18.00	18.00	18.00
Botswana	6.91	6.87	6.98	7.00	7.00	7.00	10.0% (Bank Rate)	10.00	10.00	10.00	10.00	10.50
Cameroon	512	561	556	547	533	504	4.25 (TIAO)	4.00	4.00	4.00	4.00	4.25
Côte d'Ivoire	512	561	556	547	533	504	4.25 (Discount Rate)	4.25	4.25	4.25	4.25	4.25
The Gambia	29.5	30.50	29.75	30.40	31.00	31.30	9.58 (91-day T-bill)	10.50	11.00	11.25	11.50	11.50
Ghana	0.93	1.45	1.44	1.42	1.38	1.37	12.64(91-day T-bill)	11.50	10.70	10.30	9.90	9.60
Kenya	80.85	80.5	79.8	79.5	79.4	79.0	2.2 (91-day T-bill)	2.40	3.00	3.60	4.20	4.85
Nigeria	151	148	148	146	144	144	6.0% (MPR)	6.00	6.00	6.00	6.50	6.50
Sierra Leone	3,825	4,000	4,125	4,150	4,175	4,175	15.94 (91-day T-bill)	14.00	13.50	13.00	13.20	13.25
South Africa	7.23	7.30	7.40	7.50	7.60	7.60	6.50 (Repo Rate)	6.00	6.00	6.00	6.50	7.00
Tanzania	1517	1500	1520	1480	1530	1550	3.21 (91-day T-bill)	4.90	5.20	6.60	6.80	7.20
Uganda	2265	2260	2280	2220	2260	2300	4.68 (91-day T-bill)	4.60	4.95	5.50	5.40	5.80
Zambia	4,850	5,100	5,050	4,950	4,900	4,940	5.56 (91-day T-bill)	5.90	6.40	6.70	7.00	7.30
Middle East and North Africa												
Algeria	73.66	73.00	73.50	72.00	71.75	71.75	3.28 (Interbank Rate)	3.28	3.28	3.25	3.25	3.25
Bahrain	0.38	0.38	0.38	0.38	0.38	0.38	0.50 (1-wk Deposit Rate)	0.50	0.50	0.50	0.50	0.50
Egypt	5.70	5.57	5.59	5.62	5.60	5.60	8.25 (O/N Depo Rate)	8.25	8.25	8.25	8.25	8.25
Iran	9,950	9740	9740	9740	9740	9740	…	…	…	…	…	…
Jordan	0.71	0.71	0.71	0.71	0.71	0.71	5.00 (Repo Rate)	5.00	5.00	5.00	5.00	5.00
Kuwait	0.29	0.27	0.27	0.27	0.27	0.27	2.50 (Discount Rate)	3.00	3.00	3.00	3.00	3.00
Lebanon	1,501	1,508	1,508	1,508	1,508	1,508	…	…	…	…	…	…
Libya	1.28	1.31	1.31	1.30	1.29	1.29	…	…	…	…	…	…
Morocco	8.66	9.35	9.25	9.00	8.90	8.90	5.00 (1M Depo Rate)	5.00	5.00	5.00	5.00	5.00
Oman	0.39	0.39	0.39	0.39	0.39	0.39	2.00 (Repo Rate)	2.00	2.00	2.00	2.00	2.00
Qatar	3.64	3.64	3.64	3.64	3.64	3.64	2.00 (O/N Deposit Rate)	2.00	2.00	2.00	2.00	2.00
Saudi Arabia	3.75	3.75	3.75	3.75	3.75	3.75	0.25 (Reverse Repo Rate)	0.25	0.25	0.25	0.25	0.25
Tunisia	1.48	1.49	1.49	1.46	1.45	1.45	4.50 (Money Market Rate)	4.50	4.50	0.00	0.00	0.00
Turkey	1.50	1.58	1.60	1.57	1.55	1.55	7.00 (1-week repo)	7.00	7.50	8.00	8.00	8.00
UAE	3.67	3.67	3.67	3.67	3.67	3.67	1.00 (Repo Rate)	1.00	1.00	1.00	1.00	1.00
Latin America												
Argentina	3.95	4.02	4.05	4.08	4.10	4.12	9.00 (7d Rev Repo)	10.00	10.50	10.50	10.50	10.50
Brazil	1.73	1.63	1.70	1.72	1.78	1.70	10.75 (Selic)	10.75	11.25	11.50	11.50	11.50
Chile	498	485	490	485	475	425	2.00 (Overnight Rate)	4.00	4.75	5.50	5.75	6.00
Colombia	1,803	1,835	1,800	1,820	1,840	1,790	3.00 (Min Rev Repo)	3.50	4.50	5.00	5.50	5.50
Mexico	12.96	12.00	12.25	12.60	12.50	12.10	4.50 (TdF)	4.50	4.50	4.50	5.00	5.25
Peru	2.80	2.76	2.70	2.78	2.70	2.60	2.50 (Reference Rate)	3.75	4.50	5.25	6.00	6.00

Forecasts are for end of period

Source: Standard Chartered Research

Forecasts – Commodities

Forecasts in BLUE (RED) indicate upward (downward) revisions over the past month

	Market close	m/m	Change YTD	y/y	Q2-10	Q3-10	Q4-10	Q1-11	Q2-11	Q3-11	Q4-11	2009	2010	2011
	03-Sep-10	%	%	%	A	F	F	F	F	F	F	A	F	F
Energy														
Crude oil (near future, USD/b)														
NYMEX WTI	74.6	-7.9	-6.3	+9.3	78	80	88	93	90	93	95	62	81	93
ICE Brent	76.7	-4.0	-1.2	+15.2	79	79	88	93	90	93	95	63	81	93
Dubai spot	74.6	-4.0	-4.7	+11.2	78	77	85	89	86	89	91	62	79	89
Refined oil products cracks and spreads														
Singapore naphtha (USD/b)	0.1	-	-	-	-0.5	-2.0	-3.0	2.0	-1.5	-0.9	1.5	-0.9	-0.6	0.3
Singapore jet kerosene (USD/b)	13.2	-8.5	+41.2	68.2	11.7	10.8	12.0	11.5	12.5	10.0	11.5	8.3	11.0	11.4
Singapore gasoil (USD/b)	12.1	-16.4	+78.3	50.9	11.3	11.2	12.3	11.0	11.5	9.5	12.0	7.3	11.0	11.0
Singapore regrade (USD/b)	1.1	+178.0	-56.0	-860.0	0.4	-0.5	-0.3	0.5	1.0	0.5	-0.5	0.9	0.0	0.4
Singapore fuel oil 180 (USD/t)	-5.8	+24.6	+169.9	228.7	-6.7	-6.0	-6.5	-5.0	-5.5	-6.5	-7.0	-4.6	-5.6	-6.0
Coal (USD/t)														
API4	88.9	-2.5	+10.3	+43.8	90	90	95	102	94	102	106	65	90	101
API2	91.6	-4.1	+9.5	+35.5	87	92	95	103	98	104	108	70	88	103
globalCOAL NEWC*	93.9	+2.2	+10.8	+41.6	100	98	105	115	108	115	125	72	99	116
Metals														
Base metals (LME 3m, USD/tonne)														
Aluminium	2,147	-0.1	-1.9	+18.3	2,129	2,200	2,100	2,000	1,900	1,875	1,825	1,706	2,157	1,900
Copper	7,646	+4.7	+4.6	+23.0	7,066	7,250	7,850	8,100	8,300	8,400	8,500	5,207	7,361	8,325
Lead	2,168	+1.8	-9.5	-4.5	1,976	2,000	2,300	2,400	2,450	2,550	2,600	1,740	2,129	2,500
Nickel	21,600	+0.4	+19.8	+26.1	22,544	21,000	21,000	21,500	21,500	22,500	22,500	14,762	21,172	22,000
Tin	21,200	+3.7	+26.8	+50.6	17,895	19,000	20,000	21,000	22,000	23,000	23,000	13,412	18,541	22,250
Zinc	2,151	+3.1	-14.3	+14.0	2,064	2,000	2,150	2,250	2,300	2,300	2,350	1,690	2,132	2,300
Steel (CRU assessment, USD/t)**														
HRC, US	619	-7.2	+1.1	+13.0	752	671	693	736	745	749	769	531	692	750
HRC, Europe	706	-4.5	+24.3	+18.1	739	730	740	740	751	755	772	569	697	755
HRC, Japan	832	-3.8	+19.7	+19.0	799	866	870	876	900	903	915	757	809	899
HRC, China	645	+4.9	+10.6	+3.5	659	645	640	652	661	672	698	528	631	671
Precious metals (spot, USD/oz)														
Gold (spot)	1247	+3.7	+13.9	+25.7	1,197	1,250	1,400	1,300	1,250	1,125	1,025	974	1,252	1,175
Palladium (spot)	530	+7.3	+29.5	+80.6	495	520	580	550	600	625	625	265	519	600
Platinum (spot)	1,555	-0.7	+6.6	+24.5	1,632	1,600	1,700	1,800	1,900	1,900	1,900	1,210	1,624	1,875
Silver (spot)	19.9	+7.5	+17.6	+22.3	18.3	20.0	22.0	20.0	19.0	17.5	16.5	14.7	20.0	18.0
Agricultural products														
Softs (near future)														
NYBOT cocoa, USD/tonne	2,727	-10.8	-17.1	-5.9	2,987	3,000	2,950	2,850	2,900	3,100	2,900	2,797	3,004	2,938
LIFFE coffee, USD/tonne ***	1,604	-10.8	+24.0	+14.2	1,383	1,600	1,400	1,250	1,200	1,150	1,150	1,462	1,416	1,188
NYBOT coffee, USc/lb	185	+11.0	+36.1	+54.5	140	150	145	130	128	127	127	125	142	128
NYBOT sugar, USc/lb	20.6	+10.8	-23.6	-11.0	15.5	16	13.5	13.0	12.0	12.0	12.0	18.0	17.0	12.0
Fibres														
NYBOT cotton No.2, Usc/lb	91.0	+7.6	+20.3	+59.1	81	82	85	80	78	78	77	57	81	78
Grains & oilseeds (nr future)														
CBOT corn (maize), USc/bushel	450	+15.5	+8.5	+44.6	355	365	360	400	430	440	450	374	363	430
CBOT Soybeans, USc/bushel	1,030	-2.3	-1.0	+4.9	957	975	1,000	1,000	1,050	1,000	1,000	1,031	972	1,013
CBOT wheat, USc/bushel	708	+4.2	+30.8	+57.0	466.8	575	525	600	605	605	605	529.8	516	604
CBOT rice, USc/cwt	11.5	+6.9	-21.0	-17.2	11.7	11.0	11.5	12.5	12.0	11.0	10.0	13.3	12.0	11.0
Thai B rice 100%, USD/tonne*	490	+7.7	-16.9	-9.3	466	460	470	490	490	480	475	562	487	484
Edible oils (3m future)														
Palm oil (MDV,MYR/tonne)	2,695	-0.7	+6.0	+19.4	2,473	2,600	2,700	2,750	2,750	2,750	2,750	2,228	2,585	2,750
Soyoil (CBOT, USc/lb)	40	-1.5	-0.1	+18.3	39	40	41	43	43	43	43	35	40	43

*weekly quote **monthly average ***10 tonne contract

Sources: Bloomberg, Platts, CRU, Standard Chartered Research

Forecasts – Interbank rates

Forecasts in BLUE (RED) indicate upward (downward) revisions over the past month

	Q3-10	Q4-10	Q1-11	Q2-11	Q3-11	Q4-11
US						
3M USD LIBOR	0.40	0.40	0.40	0.40	0.40	0.40
6M USD LIBOR	0.55	0.55	0.55	0.55	0.55	0.55
12M USD LIBOR	0.90	0.90	0.90	0.90	0.90	1.00
Euro area						
3M EUR LIBOR	0.90	1.10	1.35	1.60	1.85	2.20
6M EUR LIBOR	1.15	1.40	1.65	1.95	2.20	2.45
12M EUR LIBOR	1.40	1.80	2.10	2.40	2.65	2.85
Japan						
3M JPY LIBOR	0.30	0.30	0.35	0.36	0.38	0.40
6M JPY LIBOR	0.40	0.45	0.48	0.39	0.50	0.52
12M JPY LIBOR	0.65	0.67	0.70	0.70	0.70	0.75
UK						
3M GBP LIBOR	0.70	0.70	0.75	0.80	0.85	0.90
6M GBP LIBOR	1.00	1.00	1.10	1.15	1.20	1.25
12M GBP LIBOR	1.40	1.50	1.60	1.85	1.90	1.90
Canada						
3M CAD LIBOR	1.20	1.50	1.75	2.00	2.25	2.50
6M CAD LIBOR	1.50	1.75	2.00	2.25	2.50	2.75
12M CAD LIBOR	1.95	2.10	2.25	2.50	2.75	3.00
Switzerland						
3M CHF LIBOR target	0.25	0.25	0.50	0.75	1.00	1.25
6M CHF LIBOR	0.30	0.40	0.70	1.15	1.40	1.65
12M CHF LIBOR	0.70	0.90	1.20	1.45	1.70	1.95
Australia						
3M AUD LIBOR	5.50	5.55	5.65	5.80	6.05	6.65
6M AUD LIBOR	5.90	5.95	6.05	6.25	6.55	7.15
12M AUD LIBOR	5.60	5.70	5.80	6.00	6.20	6.40
New Zealand						
3M NZD LIBOR	3.50	3.70	4.25	4.50	4.75	5.05
6M NZD LIBOR	3.85	4.15	4.65	4.85	5.10	5.40
12M NZD LIBOR	4.40	4.60	4.90	5.10	5.50	5.70
Hong Kong						
3M HKD HIBOR	0.30	0.30	0.30	0.30	0.30	0.30
6M HKD HIBOR	0.40	0.40	0.40	0.40	0.40	0.40
12M HKD HIBOR	0.70	0.70	0.70	0.70	0.70	0.80
Korea						
3M CD rate	2.95	2.95	3.20	3.40	3.60	3.80
Indonesia						
3M JIBOR	7.00	7.30	8.30	8.50	8.50	8.40
6M JIBOR	7.20	7.80	8.60	8.80	8.80	8.70
12M JIBOR	7.50	8.10	9.00	9.20	9.10	9.00
Malaysia						
3M KLIBOR	2.85	2.85	3.10	3.60	3.60	3.60
6M KLIBOR	2.90	2.90	3.15	3.65	3.65	3.65
12M KLIBOR	3.05	3.05	3.30	3.80	3.80	3.80
Singapore						
3M SGD SIBOR	0.50	0.50	0.50	0.50	0.50	0.50
6M SGD SIBOR	0.60	0.60	0.60	0.60	0.60	0.60
12M SGD SIBOR	0.90	0.90	0.90	0.90	0.90	1.00
Thailand						
3M BIBOR	1.90	2.05	2.05	2.10	2.15	2.60
6M BIBOR	2.05	2.10	2.15	2.30	2.45	2.70
12M BIBOR	2.10	2.15	2.20	2.40	2.50	2.75
South Africa						
3M JIBAR	6.10	6.28	6.38	6.60	7.28	7.54
6M JIBAR	6.40	6.66	6.72	7.25	7.49	7.82
12M JIBAR	6.67	6.63	6.98	7.12	7.52	8.02
Turkey						
3M TRLIBOR	7.70	7.80	8.30	8.60	8.60	8.60
6M TRLIBOR	8.40	8.50	9.00	9.10	9.10	9.10
12M TRLIBOR	9.50	9.70	9.80	9.80	9.80	9.80

Source: Standard Chartered Research

Forecasts – Rates

Forecasts in BLUE (RED) indicate upward (downward) revisions over the past month

Country	Government bonds							Swaps						
	07-Sep-10	Q3-10	Q4-10	Q1-11	Q2-11	Q3-11	Q4-11	07-Sep-10	Q3-10	Q4-10	Q1-11	Q2-11	Q3-11	Q4-11
Asia														
China								*Interest Rate Swap (against 7-Day repo), Act/365, Quarterly*						
2Y	2.17	2.25	2.30	2.40	2.60	2.80	2.90	2.24	2.30	2.35	2.50	2.80	3.00	3.10
5Y	2.64	2.55	2.50	2.60	2.80	2.95	3.10	2.76	2.70	2.60	3.10	3.25	3.35	3.45
10Y	3.24	3.20	3.15	3.25	3.35	3.50	3.70	3.09	3.10	3.00	3.20	3.50	3.70	3.90
Hong Kong								*Interest Rate Swap, Act/365, Quarterly*						
2Y	0.46	0.50	0.55	0.60	0.70	0.90	1.20	0.64	0.70	0.70	0.80	1.00	1.20	1.50
5Y	1.13	1.10	1.00	1.00	1.10	1.20	1.35	1.58	1.55	1.45	1.45	1.60	1.70	1.80
10Y	1.99	1.95	1.85	1.80	1.90	2.15	2.30	2.41	2.35	2.25	2.20	2.30	2.40	2.50
India								*Overnight Index Swap, Act/365, Semi-Annual*						
2Y	6.82	7.20	7.50	7.50	7.25	7.25	7.00	6.35	6.75	7.00	7.00	6.75	6.75	6.50
5Y	7.73	7.80	7.95	8.00	8.00	8.00	7.80	7.02	7.25	7.50	7.25	7.25	7.25	7.00
10Y	7.99	8.00	8.25	8.25	8.25	8.25	8.15							
Indonesia								*Interest Rate Swap, Act/360, Semi-Annual*						
3Y	7.27	7.20	7.50	8.20	8.25	8.20	8.15	8.25	8.20	8.30	8.75	8.60	8.35	8.20
5Y	7.55	7.50	7.85	8.55	8.45	8.45	8.40	8.50	8.45	8.60	9.10	8.80	8.60	8.40
10Y	8.11	8.05	8.20	8.75	8.65	8.65	8.60							
Malaysia								*Interest Rate Swap, Act/365, Quarterly*						
3Y	3.16	3.15	3.10	3.35	3.70	3.70	3.75	3.30	3.30	3.25	3.50	3.85	3.90	3.95
5Y	3.33	3.30	3.25	3.50	3.85	3.85	3.90	3.57	3.55	3.50	3.75	4.10	4.10	4.15
10Y	3.69	3.75	3.65	3.85	4.15	4.15	4.20	3.99	4.05	3.95	4.20	4.55	4.55	4.65
Pakistan														
3Y	13.03	12.20	11.90	11.60	11.40	11.40	11.30							
5Y	13.09	12.30	12.10	11.80	11.60	11.60	11.50	*See Note 1.*						
10Y	13.17	12.50	12.30	12.10	12.00	12.00	11.90							
Philippines								*Interest Rate Swap, Act/360, Quarterly*						
2Y	5.00	4.90	5.05	5.25	5.45	5.65	5.80	4.50	4.40	4.55	4.75	4.90	5.05	5.15
5Y	5.30	5.20	5.30	5.45	5.65	5.85	6.00	5.01	4.90	4.95	5.00	5.00	5.05	5.05
10Y	6.30	6.20	6.30	6.40	6.50	6.70	6.80							
Singapore								*Interest Rate Swap, Act/365, Semi-Annual*						
2Y	0.42	0.50	0.50	0.50	0.50	0.60	0.70	0.89	0.95	1.05	1.10	1.20	1.40	1.55
5Y	0.68	0.65	0.65	0.65	0.65	0.75	0.90	1.65	1.60	1.60	1.55	1.50	1.60	1.75
10Y	2.14	2.10	2.05	2.05	2.10	2.20	2.30	2.38	2.35	2.35	2.40	2.50	2.60	2.75
South Korea								*Interest Rate Swap, Act/365, Quarterly*						
3Y	3.69	3.60	3.50	3.70	3.90	4.10	4.30	3.64	3.55	3.40	3.60	3.75	3.95	4.10
5Y	4.14	4.10	4.00	4.10	4.20	4.30	4.40	3.84	3.80	3.70	3.75	3.85	3.90	4.00
10Y	4.49	4.40	4.20	4.30	4.40	4.50	4.60	4.11	4.00	3.80	3.90	3.95	4.00	4.05
Taiwan								*Interest Rate Swap, Act/365, Quarterly*						
2Y	0.32	0.40	0.60	0.70	0.90	1.15	1.25	0.91	1.10	1.30	1.50	1.65	1.80	1.85
5Y	0.91	0.90	1.00	1.00	1.10	1.25	1.40	1.31	1.30	1.20	1.30	1.45	1.60	1.80
10Y	1.23	1.15	1.10	1.10	1.30	1.45	1.60	1.61	1.55	1.45	1.45	1.60	1.70	1.90
Thailand								*Interest Rate Swap, Act/365, Semi-Annual*						
2Y	2.36	2.30	2.45	2.60	2.80	3.00	3.20	2.08	2.00	2.30	2.60	2.95	3.25	3.50
5Y	2.67	2.60	2.70	2.80	2.95	3.10	3.25	2.78	2.70	2.85	3.00	3.20	3.40	3.60
10Y	2.87	2.80	2.90	3.00	3.10	3.25	3.40	3.28	3.20	3.25	3.30	3.40	3.50	3.65
Vietnam														
2Y	9.95	10.25	10.75	11.25	11.50	11.50	11.75							
5Y	10.45	10.50	11.00	11.50	11.75	11.75	12.00	*See Note 1.*						
10Y	10.45	10.50	11.00	11.50	11.75	11.75	12.00							

Note 1. Forecasts are not available, as these financial instruments are at a nascent stage of development.

Sources: Bloomberg, Standard Chartered Research

Forecasts – Rates (con'd)

Forecasts in BLUE (RED) indicate upward (downward) revisions over the past month

Country	Government bonds							Swaps						
	07-Sep-10	Q3-10	Q4-10	Q1-11	Q2-11	Q3-11	Q4-11	07-Sep-10	Q3-10	Q4-10	Q1-11	Q2-11	Q3-11	Q4-11
Majors														
United States								*Interest Rate Swap, 30/360, Semi-Annual*						
2Y	0.52	**0.50**	**0.60**	**0.60**	**1.10**	**1.30**	1.60	0.69	**0.75**	**0.80**	**0.85**	**1.30**	**1.50**	1.70
5Y	1.49	**1.50**	**1.50**	**1.50**	**1.60**	**1.70**	2.10	1.66	**1.57**	**1.65**	**1.65**	**1.75**	**1.85**	2.25
10Y	2.71	**2.75**	**2.75**	**2.75**	**2.80**	**2.80**	2.90	2.67	**2.79**	**2.85**	**2.85**	**2.90**	**2.90**	3.00
Africa														
Ghana														
2Y	12.75	**13.80**	13.50	13.25	12.50	12.00	12.00							
3Y	13.00	**14.00**	**13.80**	13.50	12.75	12.25	12.25	*See Note 1.*						
Kenya														
2Y	3.65	**4.50**	**4.60**	**4.80**	**5.00**	**5.30**	5.60							
5Y	4.20	**8.00**	7.90	8.00	8.20	**8.50**	8.80	*See Note 1.*						
10Y	5.95	**11.00**	**11.20**	**11.30**	**11.50**	**11.70**	11.90							
Nigeria														
2Y	6.91	**8.00**	**7.50**	**7.20**	**7.40**	**7.60**	7.80							
5Y	9.20	**9.10**	**9.30**	**9.10**	**9.30**	**9.50**	9.70	*See Note 1.*						
10Y	8.29	**9.00**	**9.30**	**9.40**	**9.60**	**9.80**	9.90							
South Africa								*Interest Rate Swap, Act/365, Quarterly*						
2Y	6.17	**6.50**	**6.60**	**6.80**	**7.10**	**7.20**	7.50	6.33	**6.50**	**6.50**	**7.00**	**7.30**	**7.60**	7.80
5Y	7.09	**7.80**	**7.90**	**8.00**	**8.30**	**8.40**	8.50	7.07	**7.60**	**7.70**	**7.90**	**8.10**	**8.20**	8.40
10Y	7.96	**8.50**	**8.60**	**8.70**	**8.50**	**8.60**	8.70	7.42	**8.00**	**8.30**	**8.10**	**8.00**	**8.20**	8.40
Uganda														
2Y	6.45	**7.50**	8.00	7.75	7.50	7.70	7.70							
5Y	9.20	**9.00**	9.50	9.30	9.10	9.35	9.35							
10Y	10.77	**11.30**	11.70	11.50	11.30	11.50	11.50							
Middle East														
Saudi Arabia								*Interest Rate Swap, Act/360, Annual*						
2Y								1.11	1.70	2.20	2.60	2.70	2.90	3.20
5Y	*See Note 1.*							2.39	3.10	3.30	3.40	3.50	3.60	3.70
10Y								3.66	4.20	4.50	4.65	4.70	4.80	5.10
United Arab Emirates								*Interest Rate Swap, Act/360, Annual*						
2Y								2.48	2.60	2.80	3.20	3.30	3.50	3.60
5Y	*See Note 1.*							3.35	3.90	4.10	4.30	4.30	4.50	4.60
10Y								4.42	5.10	5.25	5.40	5.40	5.60	5.70

Note 1. Forecasts are not available, as these financial instruments are at a nascent stage of development.

Sources: Bloomberg, Standard Chartered Research

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Contacts

Chief Economist and Group Head of Global Research

Gerard Lyons
+44 20 7885 6988
Gerard.Lyons@sc.com

Global

Alex Barrett	Head of Client Research	**London** +44 20 7885 6137 Alex.Barrett@sc.com
Will Oswald	Head of Fixed Income Research	**Singapore** +65 6307 1527 Will.Oswald@sc.com
Callum Henderson	Head of FX Research	**Singapore** +65 6530 3282 Callum.Henderson@sc.com
Christine Shields	Head of Country Risk Research	**London** +44 20 7885 7068 Christine.Shields@sc.com
Christophe Duval-Kieffer	Head of Quantitative Research	**London** +44 20 7885 5149 Christophe.DuvalKieffer@sc.com
Michael Haigh	Head of Commodities Research	**Singapore** +65 6530 8113 Michael.Haigh@sc.com
Kaushik Rudra	Head of Credit Research	**Singapore** +65 6427 5259 Kaushik.Rudra@sc.com
Razia Khan	Head of Macroeconomic Research	**London** +44 20 7885 6914 Razia.Khan@sc.com

East

Nicholas Kwan	Head of Research, East	**Hong Kong** +852 2821 1013 Nicholas.Kwan@sc.com

China

Stephen Green	Regional Head of Research, Greater China	**Shanghai** +86 21 6168 5018 Stephen.Green@sc.com

Korea

SukTae Oh	Regional Head of Research, Korea	**Korea** + 822 3702 5011 SukTae.Oh@sc.com

South East Asia

Tai Hui	Regional Head of Research, South East Asia	**Singapore** +65 6530 3464 Tai.Hui@sc.com

West

Marios Maratheftis	Head of Research, West	**Dubai** +9714 508 3311 Marios.Maratheftis@sc.com

Africa

Razia Khan	Regional Head of Research, Africa	**London** +44 20 7885 6914 Razia.Khan@sc.com

Americas

David Mann	Regional Head of Research, the Americas	**New York** +1 646 845 1279 David.Mann@sc.com

Latin America

Douglas Smith	Regional Head of Research, Latin America	**New York** +1 212 667 0564 Douglas.Smith@sc.com

Europe

Christophe Duval-Kieffer	Regional Head of Research, Europe	**London** +44 20 7885 5149 Christophe.DuvalKieffer@sc.com

India

Samiran Chakraborty	Regional Head of Research, India	**Mumbai** + 91 22 6735 0049 Samiran.Chakraborty@sc.com