

### Content

- i. Investment Seminars
- ii. Fund Promotion
- iii. Fund Focus of the month

### Investment Seminar

#### Will gold head for a traditional seasonal rally?

Gold and equities has historically moved in opposite directions. With the recent correction in the equities market, will gold be an attractive investment choice for investors?

Gold prices appear to follow a seasonal pattern and prices tend to soar in September. What are the contributing factors that affect the prices of gold?

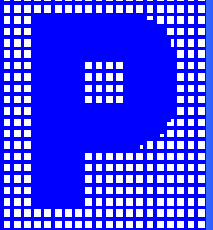
Join us in our seminar to find out more.

No	Date	Time	Venue	Theme	Speaker
1	14th Sept	12.30pm - 1.30pm	Raffles City Tower 6th Floor	Is there upside in the Gold market investment?	Dexter Tan
				Why should investors consider investing in high yield fixed income?	Investment Analyst
2	30th Sept	12.30pm - 1.30pm	Raffles City Tower 6th Floor	Is there upside in the Gold market investment?	Dexter Tan
				Why should investors consider investing in high yield fixed income?	Investment Analyst

### UOB United Gold & General Fund Promotion

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September 2009

## High Yield Bonds

Credit Spreads have widened as a reflection of the recent weakness in equities, but we feel that the dips in high yield bonds are still opportunities for longer term gains.

### Fed signaled loose monetary policy

The Federal Reserve on 19<sup>th</sup> August said that they will trim margin requirements for most banks seeking to obtain loans from the discount window. This means that banks will get easier financing in terms of an emergency even though credit conditions have improved. The Fed said that this was in response to its multi year review of collateral valuation and should not be viewed as a response to the financial crisis. This move by the Fed is a positive gesture for banks and therefore translates to better credit market conditions. Earlier in the year, the Fed has set a goal of buying up to \$1.25 trillion of agency mortgage backed securities, \$300 billion of Treasuries, and \$200 billion of agency debt in 2009 to help lower borrowing costs for home owners.

### Credit Markets can still improve some more

Figure 1 show that spread between the 3 month overnight index swap rate and the London Inter bank offered rate. The spread stood at about 236 basis points as of 14 August 09. Historically, the spread was about 100 basis points back in 2007. This shows that the spread can continue to narrow as the banking sector credit continues to heal.

Figure 2 shows the itraxx CMAN 5 Year Senior Financial Index, which has started to slope higher. The Swap Index hovered about 96.2 basis points and its recent inversion means that the credit spreads could widen in the short term but nevertheless, any distress sign in the credit market is a buying opportunity. In our view, the Swap Index could reach the average swap rate of about 50 basis points, which was the level in 2007.

Figure 3 shows the JP Morgan Subordinated Bank Tier 2 Asset Swap Rate, which has been heading lower and lower. This shows an improvement in bank asset quality, this shows that credit has improved and

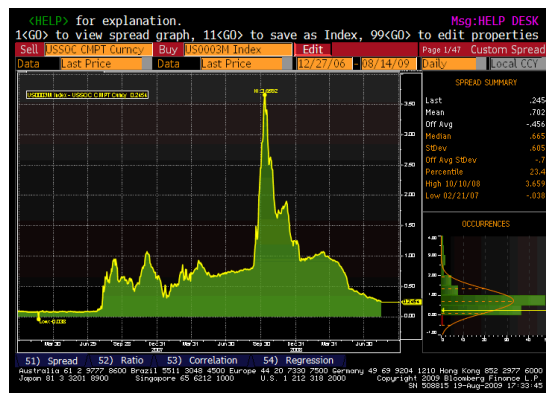


Figure 1: US 3 month LIBOR –OIS spread improving  
Source: Bloomberg



Figure 2: CMAN itraxx 5 Year European Financial Senior Tranche  
Source: Bloomberg



Figure 3: JP Morgan Banks Subordinated Tier 2 Swap Rate  
Source: Bloomberg

### Historical Relationship between High Yield and Equities

Empirically, the Schroder ISF Global High Yield has a positive correlation with the S&P 500 Index. This means that both assets tend to move in tandem primarily because of improving fundamentals in the credit markets. This is shown in Figure 4, where we see that for the past 6 months, high yield bonds have moved together with equities. In fact, just looking at the charts, we see that at some points, high yield bonds tend to lead equities. We see that high yield bonds bottom first before the equity market bottoms in March.

Even though high yields and stocks tend to move together, we like high yields because investors in the latter have preferred claims to the companies' cash flows.



Figure 4: Schroder Global High Yield Bond Fund vs S&P 500 Index

Source: Bloomberg

### The Fund we have in mind

There are 5 funds on the platform that invest in high yield bonds, the Schroder Global High Yield Bond Fund, the PIMCO High Yield Bond Fund, the Fidelity US High Yield Bond Fund, the Fidelity European High Yield Bond Fund and the Franklin Templeton High Yield Bond Fund.

However we like the Schroder Global High Yield Bond Fund because it is well diversified but majority of its exposure is in the US. In fact, as of 30 June 2009, 81.5% of the portfolio is in the US while 2.7% is invested in Canada. The following table highlights the performance of the fund thus far

Schroder Global High Yield Bond Fund Performance (as of 18 Aug 2009)						
	1 mth	3 mth	YTD	1 Year	3 Year	5 Year
Absolute Return	4.84	9.30	28.22	1.27	1.49	3.84
Maximum Drawdown				-26.82		
Volatility				16.39		
Semi variance				19.59		
Sortino Ratio				0.14		

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18th August 2009

## Buy Gold and Equities on Dips

**Equities** – Equities would be volatile, but the medium term is still higher.

**Commodities** – A sell off in gold is a great time to buy more

**Fixed income** – High Yields still preferred

### Equities – Slow, volatile recovery

Equities had been running higher for the past month, with most of the top gainers coming from the emerging markets. Some of the past performing stock indexes in the past 1 month (from 17 July 09 to 18 Aug 09) include Turkey and Vietnam. The Turkish ISE National 100 Index gained 20.52% while the Ho Chi Minh Stock Index gained about 16.54% in the past month alone. If we look at the correlation matrix of the major indexes for the past 1 year (Table 1), we noticed that there has been some disconnect between the Japanese and the US stock markets. In this aspect, portfolios with US stock market exposure could consider adding some Japanese equity funds.

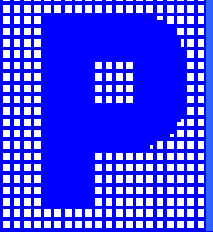
**Table 1: Correlation Matrix of Various Equity Indexes**

	S&P 500 Index	STI Index	Bombay Sensex Index	Hang Seng Index	FTSE 100 Index	Shanghai Composite Index	Nikkei 225 Index	Bovespa Index	Russian RTS Index	Germany DAX Index
S&P 500 Index	1	0.296	0.38	0.324	0.474	0.051	-0.03	0.709	0.216	0.56
STI Index	0.296	1	0.664	0.861	0.512	0.348	0.495	0.527	0.632	0.482
Bombay Sensex Index	0.38	0.664	1	0.634	0.43	0.331	0.283	0.459	0.517	0.452
Hang Seng Index	0.324	0.861	0.634	1	0.428	0.504	0.574	0.541	0.577	0.408
FTSE 100 Index	0.474	0.512	0.43	0.428	1	0.109	0.291	0.719	0.563	0.848
Shanghai Composite Index	0.051	0.348	0.331	0.504	0.109	1	0.307	0.227	0.158	0.082
Nikkei 225 Index	-0.03	0.495	0.283	0.574	0.291	0.307	1	0.196	0.408	0.22
Bovespa Index	0.709	0.527	0.459	0.541	0.719	0.227	0.196	1	0.56	0.713
Russian RTS Index	0.216	0.632	0.517	0.577	0.563	0.158	0.408	0.56	1	0.505
Germany DAX Index	0.56	0.482	0.452	0.408	0.848	0.082	0.22	0.713	0.505	1

Source: Bloomberg, from 18 Aug 08 to 18 Aug 09

### Report Highlights

*Japan and the US had negative correlations in the past 1 year.*



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## UTalk Sept 2009

The VIX, which tracks the implied volatility of stocks on the S&P 500, is starting to form a base support level, which shows that the option traders are betting for some volatile movement in equities. The Index has traded sharply higher on a sell off in equities on 17<sup>th</sup> August 2009, and has continued to stay above 25. This shows that the equity market could start to see some volatility in the month ahead. (See Chart 1)

In this chart, the VIX closed at 27.89 on 17<sup>th</sup> August 09. This shows that the market is pricing in an approximate 8% move to the downside on the S&P 500 in the subsequent 30 days.

**Chart 1: The Chicago Board of Options Exchange Implied Volatility on the S&P 500 Index**



Source: Bloomberg

*The VIX has been trending higher recently*

One of the catalysts for the sell off in stocks is China. The Shanghai Composite has broken the 3000 support level which was seen as a key technical support level. A correction in the Chinese stock market would like affect the rest of the Asian markets. China had been perceived as the market to lead the Asian growth story and whatever impacts the Chinese economy would affect the rest of Asia.

**Chart 2: The Shanghai Composite**



Source: Bloomberg

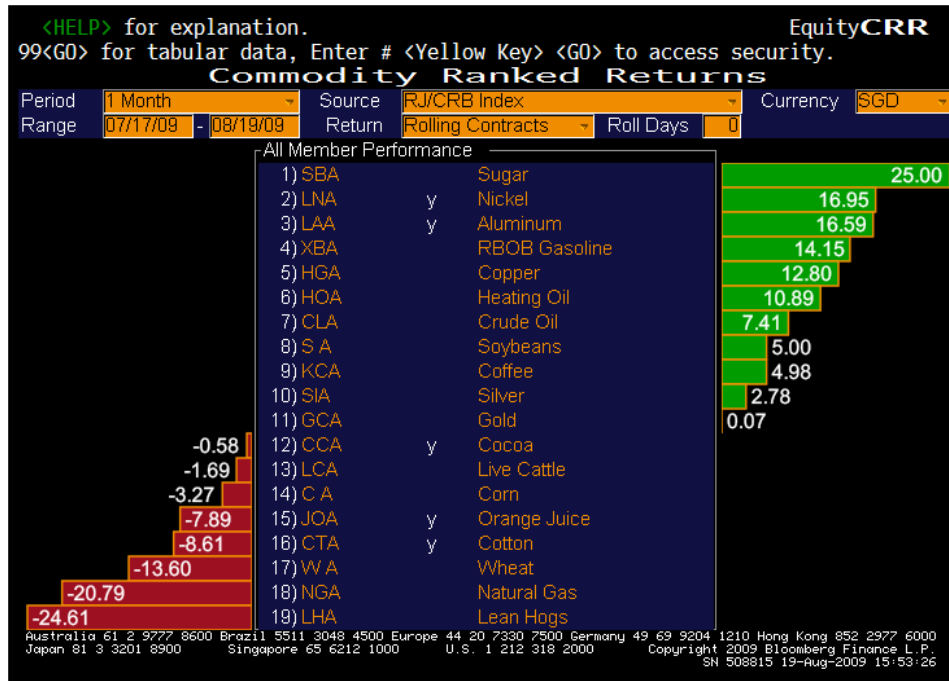
Moving forward, we are still positive on equities on the whole, and would advocate buying on dips as the market trends higher in a volatile fashion.

### Commodities – Accumulate Gold on Dips

Commodities has had a mixed picture in the past 1 month. Sugar has been trending higher on concerns that there will not be enough sugar cane crop this year. This year's unpredictable weather caused shortfalls in sugar cane crops and is pushing prices higher worldwide. The price of sugar traded about its thirty year high of 23 US cents per pound and is the best performing contract in the CRB Jefferies Index, gaining about 25% from 17<sup>th</sup> July 2009 to 18<sup>th</sup> August 2009. Aluminum, Gasoline and Copper also posted gains the past month on expectations of an economic recovery.

*A Correction in Chinese Stocks could impact the rest of the Asian stock markets.*

Chart 3: 1 Month Return for the CRB Jefferies Index

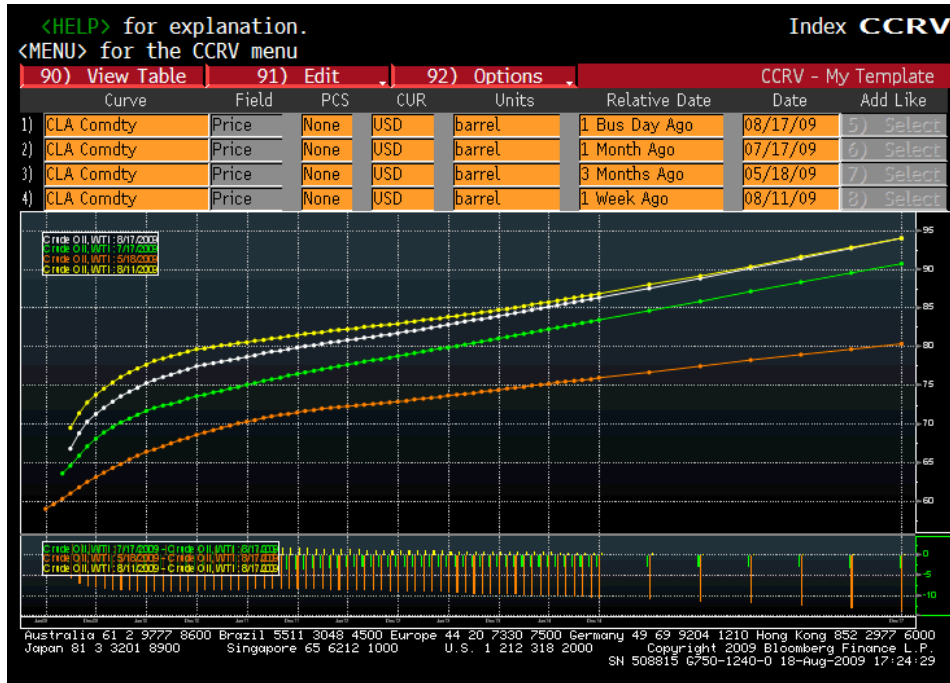


Source: Bloomberg

Crude oil, supposedly the leading contract for the commodity market, has been trading in a contango (see Chart 4), which implies that the futures price has been higher than the spot price. OPEC President flouted agreed output limits and increased oil supply to a year high and consensus is looking for the cartel to leave output unchanged at the upcoming OPEC meeting come September 9<sup>th</sup>. On 19<sup>th</sup> August, Kuwait's oil minister said that the oil price was satisfactory and sees no need to change oil supply.

*Sugar continued to trade higher, while cotton and wheat came under pressure.*

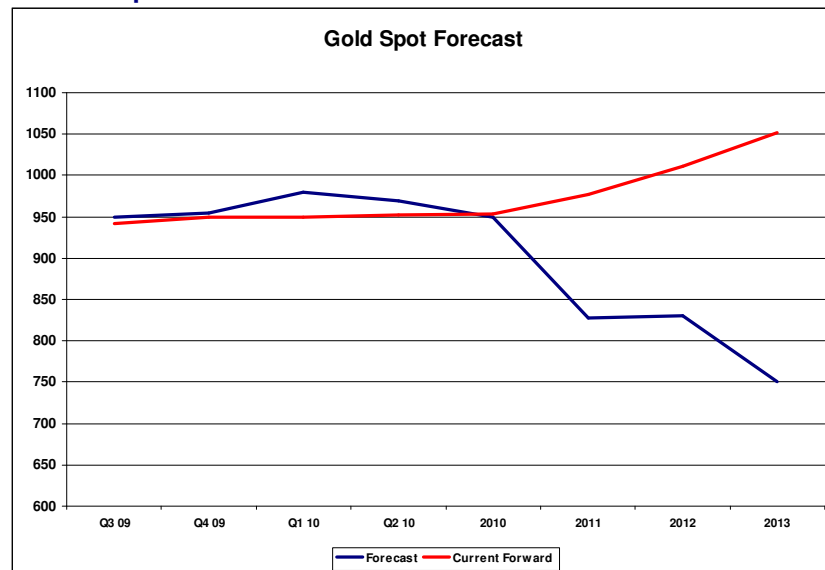
Chart 4: Crude oil Forward Curves



Source: Bloomberg

Within commodities, we prefer the precious metal as a hedge against our buy on dips equity strategy. The precious metal had done well in the recent banking crisis and the market's consensus against a depreciating US dollar would also bid well for the precious metal.

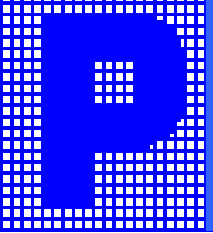
Chart 5: Spot Gold Forecast and Current Forward Curve



Source: Bloomberg

WTI Crude had been in a contango since 3 months ago

We like gold because of a market consensus of a depreciating US dollar



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## UTalk Sept 2009

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