



# FINANCIAL MARKET ANALYSIS

Volume 12, Issue 18

May 14, 2012

## Eurozone fears continue to weigh on equity markets

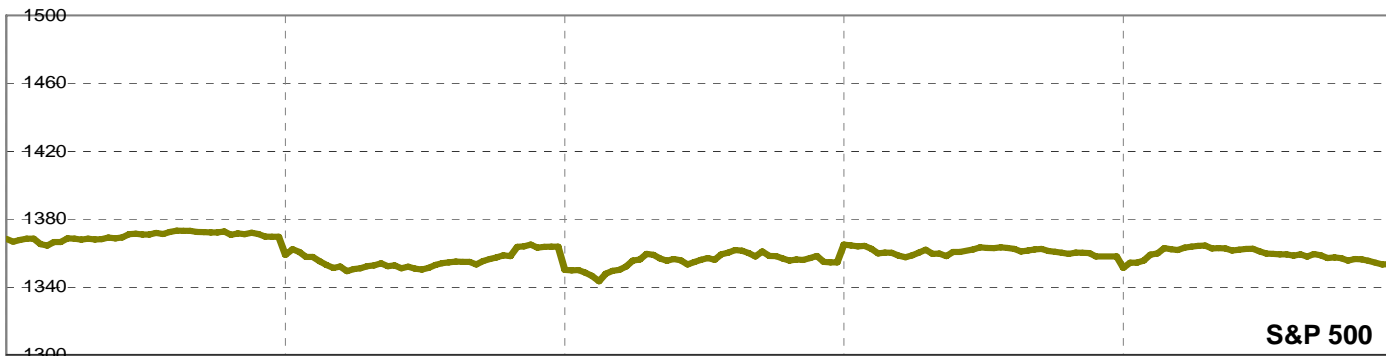
Equity markets headed south again last week as Eurozone concerns continued to dominate. The S&P 500 index fell -1.15% to end the week at 1,353.39, a two-month low. The People's Bank of China's reserve requirement ratio (RRR) cut over the weekend provided little respite as German Chancellor Angela Merkel's party lost a state election in Germany's most populous state. Focus is likely to stay on the Eurozone this week given a full meetings schedule – European Finance Ministers meet in Brussels (May 14-15), Merkel and Hollande (May 16) and the G8 (May 18-19). European data includes Eurozone IP (Monday), GDP & German ZEW (Tuesday), Eurozone CPI and Trade Balance (Wednesday). Auctions to note are Spanish bills and Italian bonds (Monday), Greek bills (Tuesday) and Spanish bonds (Thursday). In the UK, Trade Balance data is out on Tuesday, followed by ILO Unemployment and Jobless Claims on Wednesday. The Bank of England also releases its key Inflation report on Wednesday. In the US, data releases are concentrated mid-week: CPI, Empire State Manufacturing and Retail Sales on Tuesday, IP and FOMC minutes on Wednesday and Philly Fed on Thursday. In Asia, we have India WPI (Monday); Singapore Retail Sales and Korea Unemployment (Wednesday); Singapore NODX and final 1Q12 GDP, and Hong Kong Unemployment (Thursday).

	May 11 Close	Last week's return	YTD Return	YTD return (USD)
<b>S&amp;P 500:</b>	1353.39	-1.15%	+7.62%	+7.62%
<b>Stoxx Europe:</b>	227.49	+0.07%	+0.76%	+0.62%
<b>Nikkei 225:</b>	8953.31	-4.55%	+5.89%	+2.07%
<b>MSCI Asia ex Japan:</b>	418.68	-4.54%	+6.59%	+6.59%

### In this issue:

- *Europe economy: Greek exit back in the spotlight*
- *Japan equities: Implications of a Eurozone double-dip for Japanese equities*
- *Asia Pacific ex Japan equities: China: No game change yet, oversold rebound expected*

# TAKING STOCK



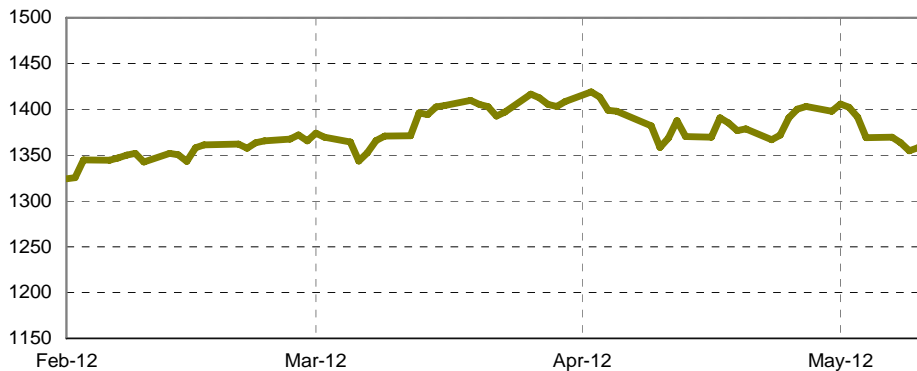
Monday May 7	Tuesday May 8	Wednesday May 9	Thursday May 10	Friday May 11
<p>S&amp;P: +0.04%</p> <p>STOXX: +1.26%</p> <p>Nikkei: -2.78%</p> <p>MSCI Asia ex Japan: -2.02%</p> <p><b>US:</b> Mar consumer credit rose US\$21.4bn (+10.2% annualized) to US\$2.54tn, largest increase since Nov '01 (Consensus +US\$9.8bn).</p> <p><b>EU:</b> The Eurozone Sentix index fell to -24.5 in May vs. market expectations of -15.7.</p> <p><b>JP:</b> BoJ meeting minutes: Many members agreed BoJ should steadily implement previous easing decisions. Few believe it is important to clearly explain purpose of JGB purchases. One member suggested BoJ explain the state of its JGB holdings in a transparent manner, said fiscal sustainability a prerequisite for functioning of monetary policy.</p> <p><b>AP:</b> Australia Mar building approvals rebounded to 7.4% after falling -8.8% in Feb. Mar retail sales rose 0.9%, more than 4 times the market estimate of 0.2%. Real retail sales rose 1.8% in 1Q12, the fastest gain in almost 3 years.</p> <p><b>AP:</b> Taiwan CPI inflation rose to 1.44% YoY in Apr, from 1.25% YoY in Mar, in line with market expectations. Core CPI rose to 1.18% YoY from 0.53% YoY in Mar, and averaged 0.69% YoY in Jan-Apr, lower than 2011's 1.10% YoY rise. WPI fell to -0.55% YoY (Mar -0.24% YoY, Consensus 0.0% YoY).</p> <p><b>AP:</b> Taiwan exports declined to -6.4% YoY in Apr vs. -3.2% YoY in Mar, below market expectations of -3.1% YoY. Imports rose to 2.1% YoY from -5.8% YoY in Mar, vs. market expectations of -2.1% YoY. The trade surplus narrowed to US\$0.69bn in Apr from US\$2.36bn in Mar.</p> <p><b>AP:</b> Indonesia 1Q12 GDP growth slowed to 6.31% YoY from 6.49% YoY in 4Q11.</p>	<p>S&amp;P: -0.43%</p> <p>STOXX: -1.93%</p> <p>Nikkei: +0.69%</p> <p>MSCI Asia ex Japan: -0.25%</p> <p><b>US:</b> The NFIB Small Business Optimism index increased to 94.5 in Apr from 92.5 in Mar.</p> <p><b>EU:</b> Mar German industrial production rose 2.8% MoM, recovering sharply from an upwardly revised -0.3% MoM fall in Feb (Prev. -1.3% MoM). This compares with market expectations of 0.8% MoM.</p> <p><b>EU:</b> UK BRC reported a slight easing of annual shop price inflation in Apr, to 1.3% YoY from 1.5% YoY in Mar, helped by a slowdown in food price inflation, to 4.3% YoY from 5.4% YoY in Mar.</p> <p><b>AP:</b> Australia's trade deficit widened to -A\$1.6bn in Mar (Feb -A\$0.7bn), the largest in almost two and a half years, and more than market expectations of -A\$1.3bn. Exports grew by 1.6%, the first increase for 2012. Imports jumped by 4.9%, more than erasing the two previous monthly declines.</p>	<p>S&amp;P: -0.67%</p> <p>STOXX: -0.35%</p> <p>Nikkei: -1.49%</p> <p>MSCI Asia ex Japan: -1.39%</p> <p><b>US:</b> Wholesale inventories rose 0.9% MoM in Mar, vs. 0.9% in Feb and market expectations of 0.6% MoM. Wholesale sales rose 0.5% MoM, vs. 1.1% MoM in Feb, leading to no change in the inventory/sales ratio of 1.17 months.</p> <p><b>EU:</b> The EFSF announced an agreement to authorize a payment of €5.2bn from the bailout fund, despite some noted opposition in the wake of Greek election results.</p> <p><b>EU:</b> IMF believes German growth can reach potential in 2H12; risk facing Germany is PIIGS; and German banking system still vulnerable to external shocks given high leverage ratios.</p> <p><b>EU:</b> The -3.3% YoY plunge in the Apr UK BRC like-for-like growth in annual retail sales values was far worse than market expectations of 0.5% YoY and more than reverses the 1.3% YoY climb in Mar.</p> <p><b>AP:</b> Malaysia export growth unexpectedly declined -0.1% YoY in Mar (Consensus +3.0% YoY). Import growth slowed to +1.6% YoY vs. expectations of +7% YoY. The trade surplus narrowed to RM10.45bn (Feb RM10.6bn).</p>	<p>S&amp;P: +0.25%</p> <p>STOXX: +0.82%</p> <p>Nikkei: -0.39%</p> <p>MSCI Asia ex Japan: +0.13%</p> <p><b>US:</b> Initial jobless claims for the week ending 5 May fell -1K to 367K, in line with market expectations for 368K. The 4-week average fell to 379.0K from 384.3K in the week prior.</p> <p><b>US:</b> The Mar trade deficit was -US\$51.8bn, vs. market expectations of -US\$50bn and -US\$45.4bn in Feb. Total exports rose 2.9% MoM; total imports rose 5.2% MoM.</p> <p><b>US:</b> Import prices fell -0.5% MoM in Apr, the largest drop since Jun '11.</p> <p><b>US:</b> The Apr Treasury budget statement showed an overall surplus of +US\$59.1bn (-26.4% YoY), vs. the -US\$40.4bn deficit in Apr '11, above market expectations for a +US\$35.0bn surplus.</p> <p><b>EU:</b> The UK MPC decided to hold the programme of asset purchases steady at £325bn.</p> <p><b>JP:</b> The current account posted a seasonally-adjusted surplus of ¥785.5bn in Mar, narrowing slightly from a ¥856.2bn surplus in Feb due to a wider trade gap. As a result, the current account generated an annualized ¥7.1trn surplus for 1Q12.</p> <p><b>AP:</b> Australia employment grew 15.5K (Consensus -5K) in Apr. The unemployment rate fell to 4.9% (Mar 5.2%).</p> <p><b>AP:</b> China Apr exports and imports grew by 4.9% YoY and 0.3% YoY, respectively. The trade surplus widened to US\$18.4bn (Mar US\$5.4bn).</p> <p><b>AP:</b> Bank Indonesia kept the policy rate at 5.75% and FasBI rate at 3.75%.</p> <p><b>AP:</b> Bank of Korea held the policy rate at 3.25%.</p>	<p>S&amp;P: -0.34%</p> <p>STOXX: +0.29%</p> <p>Nikkei: -0.63%</p> <p>MSCI Asia ex Japan: -1.08%</p> <p><b>US:</b> Apr PPI fell -0.2% MoM (+1.9% YoY), core PPI rose +0.2% MoM (+2.7% YoY).</p> <p><b>US:</b> May prelim Reuters/Michigan sentiment rose to 77.8 from 76.4 in Apr. The economic conditions index rose to 87.3 (Apr 82.9), but the economic outlook index fell to 71.7 (Apr 72.3).</p> <p><b>EU:</b> The EU Commission maintained its forecast for Eurozone GDP growth at -0.3% in 2012 and +1% in 2013. Overall EMU deficit to be 3.2% in 2012 and 2.9% in 2013. Sees Germany's growth at 0.7% and 1.7%, respectively, while its deficits are seen to be 0.9% and 0.7%. For France, the EU predicts growth of +0.5% and 1.3% and its deficits at 4.5% in 2012 and 4.2% in 2013.</p> <p><b>EU:</b> German final Apr CPI rose 0.2% MoM (2.1% YoY), vs. the preliminary reading of 0.1% MoM (2% YoY).</p> <p><b>EU:</b> UK Apr producer prices rose 0.7% MoM (3.3% YoY).</p> <p><b>EU:</b> UK Nationwide consumer confidence fell to 44 in Apr from 53 in Mar.</p> <p><b>AP:</b> China Apr data: CPI eased to 3.4% YoY, PPI fell to -0.7% YoY. IP grew 9.3% YoY; FAI grew 20.2% YoY; retail sales grew 14.1% YoY. M2 growth fell to 12.8% in Apr, and monthly RMB lending fell from 1,010bn to 682bn. M1 grew 3.1% YoY.</p> <p><b>AP:</b> Hong Kong 1Q12 GDP grew 0.4% in both YoY and QoQ SA terms (Consensus 1.1% YoY, 1.0% QoQ SA).</p> <p><b>AP:</b> India Mar IIP fell -3.5% YoY (Consensus +1.7% YoY).</p> <p><b>AP:</b> Malaysia's central bank kept the OPR on hold at 3%.</p>

## Over the Weekend May 12 and May 13

**AP:** The People's Bank of China cut the reserve requirement ratio for the 2<sup>nd</sup> time this year. The 50 bps cut effective May 18 will bring RRR for large banks to 20%.

# US/NORTH AMERICA

S&P 500 (1/2/2012 to 11/5/2012)



Source: Bloomberg

## Economic Outlook

### Softer employment unlikely to signal a fundamental shift in recovery's path

The negative tone in recent economic reports, including previous soft payroll gains, is unlikely to signal a fundamental shift in recovery's momentum. Indeed, softer employment gains in April were unsurprising and in line with the "payback scenario" from exaggerated winter gains. Citi analysts still expect average increases this year in a 175K range. Although 2Q12 growth is expected to dip to near 1.5%, that is largely a correction to overshooting inventory accumulation, while some volatile components of final demand could impart some upside.

Business investment leads appear stronger than recent GDP data indicate and consumers remain on a sustainable recovery path, led by reviving auto sales and other discretionary spending rising at a 5% rate. Earlier concerns about rising gasoline prices and further drag from declines in home prices are not playing out. Gasoline prices fell noticeably in April and remain weak, while home prices have been surprisingly steady through the traditionally weak winter season.

## The Week Ahead

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- Citi analysts expect that the **consumer price index** was unchanged in April at 0.0%, with a sharp decline in energy costs, especially gasoline, offsetting a trend rise in core prices.
- Retail sales** growth probably subsided in April (0.0%), after some solid gains in the first quarter.
- Business inventories** likely rose by a modest 0.4% in March.

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- Industrial production** probably posted a solid increase in April (0.7%), led by a strong showing in manufacturing and a bounce back in utilities output.

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- Initial jobless claims** for the week ending May 12 were probably little changed at 370K, pushing the four-week moving average down and partially reversing some of the recent swell.
- The **Conference Board's leading economic index (LEI)** was probably flat in April (0.0%) after six consecutive monthly increases.

## Equities

### Uncertainty amongst investors

	Last week's close	Last week's return	YTD return
S&P 500	1353.39	-1.15%	+7.62%
DJIA	12820.60	-1.67%	+4.94%
Nasdaq	2933.82	-0.76%	+12.62%

Credit conditions have improved modestly underscoring the view that economic conditions are likely to stay positive through year-end and thus support corporate profits as they relate strongly with industrial activity.

Yet, the Citi Economic Surprise Index argue that some inflection point off of its dropping trend is needed to feel confident to wade back into a new equity market rally effort given the lack of sentiment or correlation signals. Citi analysts believe that earnings upside surprises and beating expectations alone may not be enough to generate greater investor appetite for stocks.

Indeed, Citi analysts believe that some clarity with respect to substantial political/fiscal challenges is most likely needed to pull down equity risk premiums and allow for multiple price-to-earnings (P/E) expansion. This may then renew business and investor confidence.

## Bonds

### Preference for high-grade corporates and emerging market debt

	May 11 2011	May 4 2011	Apr 27 2011
2-yr Try:	0.258%	0.254%	0.258%
5-yr Try:	0.746%	0.784%	0.826%
10-yr Try:	1.838%	1.879%	1.935%

**Treasuries:** Treasuries underperformed most sectors during the first quarter but Citi analysts do not believe the recent sell-off signals the start of a structural bear market. Once risk assets finish drowning in a sea of liquidity, fundamentals are expected to reassert themselves and yields are likely to trend lower.

**High-grade corporates:** While further spread tightening is likely to be more gradual, Citi analysts believe that valuations are still attractive and the high grade credit market continues to offer potential for positive performance this year.

**High-yield corporates:** Any pull-back in high yield could disproportionately impact the lowest quality issuers. Citi analysts as such favour high single B to double B issuers, particularly credits with improving fundamentals.

**EMD:** Increased corporate bond issuance in emerging markets may present opportunities to pick up yield while benefiting from stronger domestic growth.

## Currencies

### USD: Anticipating overall USD strength medium-term

	June 2012 forecasts		
	EURUSD	USDJPY	USDCAD
	1.3	81	0.99

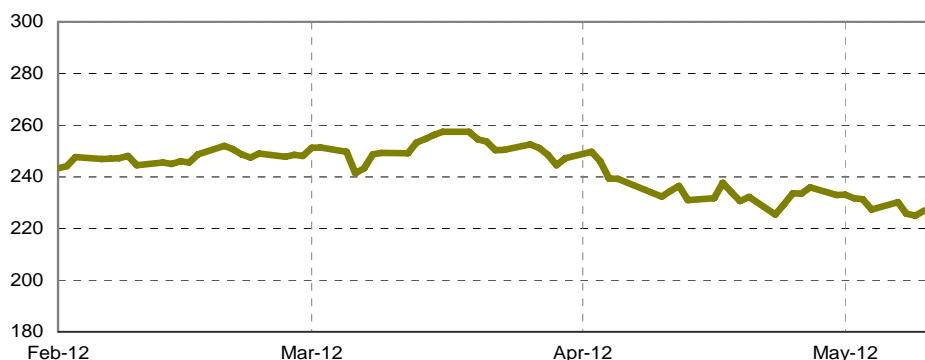
USD performance has been mixed – generally stronger against EM currencies (not surprising given fears around China growth), but slightly weaker against most G10 currencies (unusual given the rise in global risk aversion). The fact that USD has not performed better might be attributed to a softer patch of US economic data.

Citi analysts' central scenario remains one of a modest recovery in global risk appetite, and their leading indicators suggest that consensus global growth expectations could be revised up slightly. In particular, US growth is expected to hold up well even if downside risks in the Euro Area periphery and China persist. As such, USD is likely to perform well throughout the remainder of 2012, especially against European currencies, including those in CEEMEA. Meanwhile, USD/CNY appears more likely to move sideways than trend downwards near-term, which should constrain the upside potential in China-sensitive Asian and Latam currencies and AUD.

Source: CIRA

# EUROPE

STOXX (1/2/2012 to 11/5/2012)



Source: Bloomberg

## Economic Outlook

### Greek exit back in the spotlight

After the results of the Greek legislative elections, Citi analysts have raised the probability of a Greek exit from the Euro Area to a range of 50-75% from 50% previously. Although there is some hope that there will be a pro-European center-left government coalition, it is unlikely that such a coalition will be able to implement the required austerity measures and structural reforms.

Euro Area member states would then face three options, out of which Citi analysts regard as most likely the adoption of measures to 'ring-fence' other Euro Area countries potentially under attack by markets.

The vulnerability of the Greek sovereign budget is shown by the latest EU Commission forecast for Greece's primary budget figure for 2013 — revised to a deficit of 2.0% of GDP from a surplus of 1.8% of GDP expected in March when the second Greek Program was set up.

## The Week Ahead

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- **Euro Area:** With mixed data from large member countries, Citi analysts expect a small increase in area-wide **industrial production** in March (+0.2% MoM, -1.5% YoY).

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- **France:** Headline inflation is expected to moderate slightly in April, with the **consumer price index** rising only by 0.2% MoM.
- **Netherlands:** Citi analysts expect the recession in the Netherlands to continue in **1Q12**, with **GDP** likely to contract further (-0.4% QoQ).

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- **Euro Area:** Citi analysts expect March **trade balance** of €5.2 billion, up from €3.7 billion in February.

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- **Spain:** Citi analysts expect that **1Q12 GDP** contracted by 0.3% QoQ as indicated by INE's flash estimate.

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- **Germany:** Seasonal factors probably led to an increase in **producer prices** on a monthly basis in April (0.5% MoM, 2.8% YoY).

## Equities

### Two key supports for equities – Valuation and Policy

	Last week's close	Last week's return	YTD Return
STOXX	227.49	+0.07%	+0.76%
FTSE 100	5575.52	-1.41%	+0.06%
DAX	6579.93	+0.28%	+11.56%

Risk aversion has risen in recent weeks following elections in Greece and France, as investors are faced with heightened uncertainty. Despite these events, Citi analysts note that European equities, European banks and the euro (vs. USD) are all broadly flat on the year which hardly suggests a crisis in markets. In addition, broad pan-European bond yields, weighted by bond market size, are meaningfully lower in 2012.

Indeed, while risk assets have sold off, they are generally around 10-15% above 2H11 lows. Bank funding markets, to date, have been more resilient than previous periods of stress. Citi analysts continue to see valuation and policy as the two key support mechanisms for share prices.

All in, valuations look attractive unless corporate earnings collapse and Citi analysts continue to back a broad central bank liquidity put.

## Bonds

### Favour German Bunds

	May 11 2011	May 4 2011	Apr 27 2011
2-yr Try:	0.091%	0.082%	0.102%
5-yr Try:	0.547%	0.550%	0.640%
10-yr Try:	1.516%	1.584%	1.699%

German Bunds remain Citi's favoured government market given the substantial growth undertow from periphery countries and the likelihood of additional European Central Bank (ECB) easing later this year.

In the UK, the greater risk to Gilts are a weakening of the government's position and a reversal of fiscal tightening; something that Citi analysts think could likely trigger a rapid response from ratings agencies and the markets. Assuming that does not happen, they see the combination of fiscal restraint, weak growth and quantitative easing as supportive for Gilts.

## Currencies

### EUR: Downward pressures remain GBP: Stable vs. USD and EUR basket

June 2012 forecasts		
GBPUSD	USDCHF	EURGBP
1.57	0.92	0.83

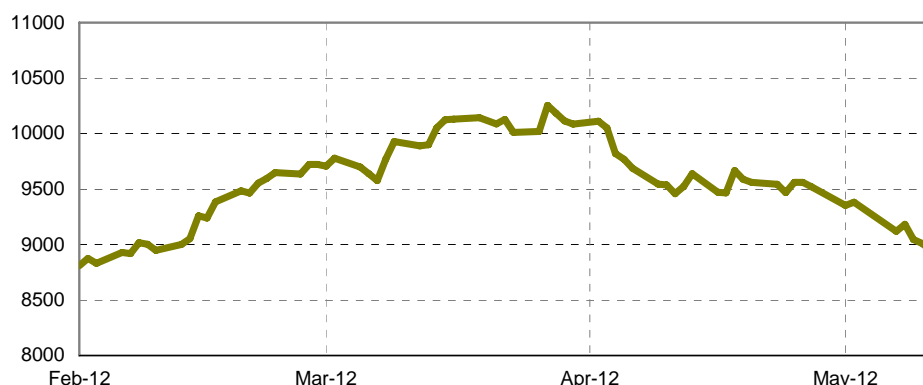
EUR/USD may stay flat near-term due to two key opposing drivers. On one side, a move towards relatively easier monetary policy by the European Central Bank versus the Federal Reserve has exerted downward pressure. By contrast, the general improvement in risk appetite helped to ease risk premiums around the EMU periphery. But downside pressures remain longer-term given the potential for a rise in EUR risk premium and the likelihood of further ECB accommodation this year. A weaker EUR may also help to mitigate the adverse growth effects of fiscal tightening in the periphery countries.

GBP is being pulled in different directions by valuation (cheap) and economic and monetary conditions (not helpful). GBP remains the cheapest G10 currency. Citi analysts still expect a further increase to the UK QE2 programme. Tight fiscal policy and easy money is normally currency unfriendly and policymakers probably see stable GBP at competitive levels as part of the policy package.

Source: CIRA

# JAPAN

## Nikkei 225 (1/2/2012 to 11/5/2012)



Source: Bloomberg

## Economic Outlook

### Summer power shortage blues

Japan will face power shortages this summer as all 54 nuclear power stations based in the country ceased operations earlier this month amid safety concerns. Unlike last summer, the Kansai area (i.e. Kansai Electric Power Company district), which had been depending most heavily on nuclear power, is set to suffer the most. According to government estimates, the power supply capacity in the Kansai area this summer will be 15.7% lower than the estimated peak demand under the assumption that nuclear power stations will not restart. To reduce peak demand while limiting the negative impact on production may be more difficult this summer than last. Last summer, companies had to make significant efforts, such as rotating production schedules to include middle-of-the-night and weekend shifts, in order to cut peak power demand while limiting the negative impact on economic activity. These efforts were possible last year given the strong sense of urgency following the March 11 earthquake but may be much more difficult this year in a more normal situation. While Citi analysts expect the negative impact of power shortages on the economy to be relatively limited, the uncertainties are meaningful.

## The Week Ahead

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- The **domestic corporate goods price index** probably increased 0.2% MoM in April (-0.1% YoY) after a 0.6% MoM rise in March.

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- Private machinery orders** ex ships and power plants (private core orders) likely decreased -4.0% MoM in March (+3.8% YoY) after rising 4.8% MoM in February and 3.4% MoM in January.
- The **tertiary industry activity index** probably rose 0.1% MoM (+5.0% YoY) in March after no change in February.

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- Real GDP** probably increased 0.9% QoQ and 3.8% QoQ annualized in the first quarter, registering a substantial rebound from negative growth in the previous quarter, mainly driven by consumer spending and rebuilding demand after the March 2011 disaster.

## Equities

### Implications of a Eurozone double-dip for Japanese equities

	Last week's Close	Last week's return	YTD return
Nikkei	8953.31	-4.55%	+5.89%
Topix	758.38	-4.35%	+4.09%

The Eurozone is the third largest export destination for Japan, after China and the US. In the 2008-2009 recession (first of the double-dips), the ratio of the amount of the decline in exports from Japan to Europe to global exports was high in sectors such as general machinery and transport equipment. Over the same period, the ratio of the amount of decline in local sales by the European subsidiaries of Japanese firms to global sales was high in sectors such as precision equipment and glass & ceramics.

Citi analysts compared the period since March 2012 (when the spread of Spanish sovereign yield over German sovereign yield widened), with phases in 2010 and 2011 when share prices corrected on Euro fears. They found no major changes and believe this may be because investors shared concerns about weakening economies before real economies actually deteriorated. In a scenario where the Eurozone recession gets worse, they prefer domestic demand sectors, companies with high percentage of sales in the US and low percentage in the Eurozone, and income stocks.

Source: CIRA

## Bonds

### Some JGB underperformance around the fiscal year-end expected

	May 11 2011	May 4 2011	Apr 27 2011
2-yr Try:	0.105%	0.113%	0.111%
5-yr Try:	0.246%	0.270%	0.263%
10-yr Try:	0.853%	0.892%	0.897%

Ongoing downgrades to Japan's growth outlook and continued expectations of Bank of Japan (BoJ) bond purchases are supporting JGBs. The divergence between Japanese yields and the other major markets looks overstretched, however, and Citi analysts think that there may be potential for some JGB underperformance around the fiscal year-end. But with policy rates likely to remain near zero for a long time and the BoJ maintaining its duration commitment, Citi analysts believe that calls for a fiscally driven bear-market are premature.

## Currencies

### JPY: USD/JPY stable for now

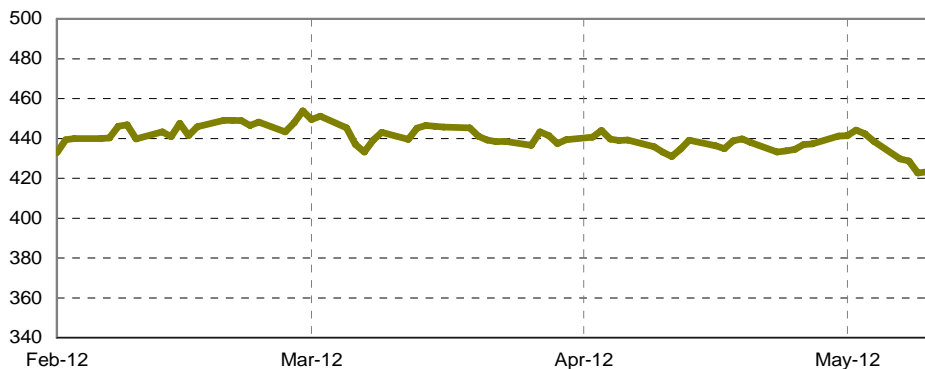
	June 2012 forecast
USDJPY	81
EURJPY	105
AUDJPY	83.5

USD/JPY has retraced nearly 40% of its sharp move higher between February and mid-March this year, correcting what was an overshoot in Citi analysts' opinion. Their forecast is for USD/JPY to basically flat-line over the next 12 months.

One important factor to their outlook is that they do not expect the Bank of Japan to provide enough stimulus for a weaker yen. Having said that, Citi analysts acknowledge that the BoJ may still opt to ease monetary policy again if the recent slide in USD/JPY continues. Additionally, should exports stay weak, the continued deterioration in trade flows could act to push the yen weaker, although Japan still has a cushioning income account surplus. Meanwhile, money flows also appear supportive of a broadly steady yen.

# ASIA PACIFIC EX JAPAN

MSCI Asia ex Japan (1/2/2012 to 11/5/2012)



Source: Bloomberg

## Economic Outlook

### China: Still hopeful of above 8% growth

Citi analysts believe the government still aims for above 8% growth, and a rebound of growth before the National Party Congress. The recent data should convince the government that growth will not rebound automatically in the absence of policy support. As such, further policy easing may include: 1) Two RRR cuts this year to bring M2 growth to 14% and the next one is likely to take place by end-July; 2) Fiscal deficit close to the budgeted level (effectively 2.4% of GDP); 3) Extension of property policy easing from first home purchase to second home purchase, accompanied by adequate funding of social housing programs; and 4) Launch of new infrastructure projects under the 12th Five-Year Plan.

But given that we are already halfway through 2Q12, further policy easing is likely to have more impact on 2H12 and 2013. Citi analysts now forecast 2Q12 growth at 7.5% YoY (8.0% saar), but continue to think seasonally adjusted growth may have already bottomed in 1Q12. All in all, Citi analysts believe above 8% growth is still achievable with sustained policy easing. However, due to larger-than-expected drag from property investment as well as its spillover effect on consumption, they have downgraded their 2012 annual growth forecast from 8.4% to 8.1%. The risk of below 8% growth becomes clear and present if policy easing continues to lag behind.

## Equities

### China: No game change yet, oversold rebound expected

	Last week's close	Last week's return	YTD Return
MSCI Asia ex Japan	418.68	-4.54%	+6.59%

The April data continued to show the downward trend of the economy and a sub-8% growth in 2Q12 appears inevitable. But Citi analysts believe it is not a game change yet. The RRR cut last weekend suggests that policymakers were fighting back to defend the growth. To win the battle, policy fine-tuning may have to be upgraded to aggressive easing, and Citi analysts expect an oversold rebound in the market.

In their view, the market opportunity may lie in the fact that the Chinese authorities still have the firepower to stabilize growth, while there are risks on how soon the policy action would turn into growth recovery and how much the quality of growth will be sacrificed to defend 8% growth.

The H-share market appears oversold on external uncertainties and domestic policy delay, in Citi analysts' view. The recent sell-off has erased most of the gains in the HSCEI while the A-share market outperformed firmly. Citi analysts expect the H-share market to outperform if the oversold rebound materializes in the near term.

Source: CIRA

## Bonds

### Prefer Philippines bonds

Asian rates have sold off sharply on improved global growth, back-up in US yields, and for a few markets (e.g. Thailand), additional supply. Within the bond space, Citi analysts still like PHP bonds relative to others – the belly of the curve has been relatively resilient, with the back end sold off sharply (partly on the big turnaround shift in expectations about BSP's policy action) – to the point that 10yr PHP bonds are now trading slightly higher in yields (pre-tax) to 10yr Indonesia bonds. Indeed, Citi analysts still prefer the Philippines given lower foreign positioning, solid fiscal position, benign inflation risks, ample domestic liquidity, and rating upgrade prospects.

## The Week Ahead

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- **India:** April WPI probably remained sticky (6.8% YoY) with the base effect likely to result in 'non-food manufactured product inflation' coming in at sub 5% levels.

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- **Korea:** The seasonally adjusted unemployment rate likely remained at 3.4% in April.
- **Singapore:** Retail sales growth probably moderated to 9.9% YoY in March after a 19.0% YoY surge in February which had been distorted upwards by the moving Chinese New Year holiday.

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- **Hong Kong:** The unemployment rate likely stayed at 3.4% s.a. during the February-April period.
- **Singapore:** Final 1Q12 GDP growth probably came in at 1.8% YoY, above the Advance Estimate of 1.6% YoY (4Q11 3.6% YoY).
- **Singapore:** April NODX likely returned to positive territory of +0.4% YoY (March -4.3%).

## Currencies

### AUD: Still vulnerable

### EM Asia: It's all about the CNY

June 2012 forecasts		
AUDUSD	NZDUSD	USDSGD
1.03	0.82	1.25

Citi analysts expect the pace of AUD depreciation to slow but continue to look for a move back to parity in the 6-12 month horizon. Concerns around China's slowing economy have continued to come to the forefront, while prices of key commodities produced in Australia have also remained depressed and AUD does not appear to have fully responded to this. Moreover, there is still risk of further rate cuts by the Reserve Bank of Australia.

CNY remains pivotal for EM Asia currencies. USD/CNY has basically flat-lined since end-December 2011 and recent weaker global trade volumes combined with domestic Chinese growth pressures suggest that USD/CNY is more likely to move sideways rather than trend further downwards in the near term. If so, this could constrain the upside potential in many EM Asia currencies.

# WORLD MARKETS AT A GLANCE

	Previous Week's Close	52-Week High	52-Week Low	Weekly Return	YTD Return	YTD Return (USD)
<b>UNITED STATES</b>						
Dow Jones Industrial Average	12820.60	13338.66	10404.49	-1.67%	+4.94%	+4.94%
S&P 500	1353.39	1422.38	1074.77	-1.15%	+7.62%	+7.62%
Nasdaq	2933.82	3134.17	2298.89	-0.76%	+12.62%	+12.62%
<b>EUROPE</b>						
DJ Euro STOXX	227.49	289.23	194.63	+0.07%	+0.76%	+0.62%
FTSE 100	5575.52	6084.08	4791.01	-1.41%	+0.06%	+3.77%
DAX	6579.93	7523.53	4965.80	+0.28%	+11.56%	+11.40%
<b>JAPAN</b>						
Nikkei 225	8953.31	10255.15	8135.79	-4.55%	+5.89%	+2.07%
TOPIX	758.38	879.48	703.88	-4.35%	+4.09%	+0.33%
<b>ASIA</b>						
MSCI Asia ex Japan	418.68	495.97	353.80	-4.54%	+6.59%	+6.59%
Hong Kong Hang Seng	19964.63	23707.95	16170.35	-5.32%	+8.30%	+8.32%
Shanghai Composite Index	2394.98	2884.14	2132.63	-2.33%	+8.89%	+8.69%
Taiwan Weighted Index	7401.37	9089.47	6609.11	-3.89%	+4.66%	+7.83%
Korea KOSPI	1917.13	2192.83	1644.11	-3.62%	+5.01%	+5.91%
Mumbai Sensex	16292.98	19131.70	15135.86	-3.20%	+5.42%	+4.69%
Singapore Straits Times Index	2883.40	3227.28	2521.95	-3.58%	+8.96%	+12.90%
Kuala Lumpur Composite	1584.32	1609.33	1310.53	-0.42%	+3.50%	+6.69%
Thai Stock Exchange	1191.01	1247.72	843.69	-2.97%	+16.16%	+17.61%
Jakarta Composite Index	4114.14	4234.73	3217.95	-2.43%	+7.64%	+6.46%
Philippines Stock Exchange Index	5158.14	5329.76	3715.01	-2.63%	+17.98%	+21.76%
Australia All Ordinaries	4342.69	4833.90	3829.40	-2.62%	+5.63%	+3.64%
<b>EMEA</b>						
Russia MICEX Index	1392.00	1748.30	1242.75	+0.06%	-0.73%	+5.81%
South Africa JSE All Shares Index	34038.46	34647.73	28305.41	-0.26%	+6.42%	+6.24%
Turkey ISE National 100 Index	58872.62	66541.00	48600.16	-0.24%	+14.84%	+21.30%
<b>LATIN AMERICA</b>						
Mexico Bolsa Index	38888.79	40050.21	31561.51	-1.32%	+4.89%	+8.28%
Brazil Bovespa Index	59445.21	68969.99	47793.49	-2.26%	+4.74%	+0.45%
<b>COMMODITIES</b>						
Gold	1579.40	1921.15	1471.90	-3.83%	+1.00%	+1.00%
Oil	96.13	110.55	74.95	-2.40%	-2.73%	-2.73%
<b>FIXED INCOME</b>						
Citigroup World Government Bond Index	619.50	619.50	579.86	+0.24%	+1.68%	+1.68%

Source: Bloomberg (As at May 11, 2012)

# CURRENCY FORECASTS

Currency		14-May-12	Jun-12	Sep-12	Dec-12	Mar-13	Jun-13	Sep-13	Dec-13	Mar-14	Jun-14
<b>G10-US Dollar</b>											
Euro	EURUSD	1.29	1.3	1.29	1.27	1.25	1.26	1.27	1.29	1.3	1.3
Japanese yen	USDJPY	80	81	81	80	80	81	82	84	85	85
British Pound	GBPUSD	1.61	1.57	1.56	1.55	1.54	1.56	1.59	1.61	1.64	1.65
Swiss Franc	USDCHF	0.93	0.92	0.94	0.95	0.97	0.97	0.96	0.96	0.96	0.96
Australian Dollar	AUDUSD	1.00	1.03	1.02	1.01	1.00	0.98	0.95	0.93	0.90	0.90
New Zealand	NZDUSD	0.78	0.82	0.81	0.80	0.78	0.75	0.71	0.67	0.64	0.63
Canadian Dollar	USDCAD	1.00	0.99	0.99	0.98	0.98	0.97	0.97	0.97	0.97	0.97
Dollar Index	DXY	80.43	80.17	80.79	81.46	82.14	81.78	81.26	80.74	80.24	79.96
<b>G10 Crosses</b>											
Japanese yen	EURJPY	103	105	104	102	100	102	105	108	110	111
Swiss Franc	EURCHF	1.20	1.20	1.20	1.21	1.21	1.22	1.23	1.24	1.25	1.26
British Pound	EURGBP	0.80	0.83	0.83	0.82	0.82	0.81	0.80	0.80	0.79	0.79
Swedish Krona	EURSEK	9.00	8.85	8.82	8.79	8.75	8.73	8.70	8.68	8.65	8.65
Norwegian Krone	EURNOK	7.57	7.55	7.54	7.52	7.50	7.50	7.50	7.50	7.50	7.50
Norwegian Krone	NOKSEK	1.19	1.17	1.17	1.17	1.17	1.16	1.16	1.16	1.15	1.15
Australian Dollar	AUDNZD	1.28	1.26	1.26	1.27	1.28	1.31	1.35	1.39	1.42	1.43
Australian Dollar	AUDJPY	80.2	83.5	82.4	81.3	80.2	79.3	78.4	77.5	76.6	76.3
<b>EM Asia</b>											
Chinese Renminbi	USDCNY	6.32	6.31	6.28	6.25	6.22	6.20	6.17	6.14	6.11	6.10
Hong Kong Dollar	USDHKD	7.76	7.75	7.75	7.76	7.76	7.76	7.76	7.75	7.75	7.75
Indonesian Rupiah	USDIDR	9264	9368	9386	9369	9352	9339	9327	9314	9302	9289
Indian Rupee	USDINR	53.6	53.2	53.6	53.8	54.0	53.4	52.6	51.8	51.1	50.9
Korean Won	USDKRW	1149	1148	1138	1125	1112	1082	1049	1017	985	981
Malaysian Ringgit	USDMYR	3.07	3.08	3.05	3.02	2.98	2.96	2.94	2.92	2.90	2.91
Philippine Peso	USDPHP	42.6	43.0	42.7	42.4	42.0	41.9	41.8	41.6	41.5	41.5
Singapore Dollar	USDSGD	1.25	1.25	1.24	1.23	1.21	1.20	1.19	1.18	1.17	1.17
Thai Baht	USDTHB	31.2	31.0	30.8	30.5	30.2	30.1	30.1	30.0	30.0	30.0
Taiwan Dollar	USDTWD	29.5	29.7	29.4	29.1	28.8	28.7	28.5	28.4	28.2	28.3
<b>EM Europe</b>											
Czech Koruna	EURCZK	25.27	24.54	24.7	24.94	25.17	24.94	24.64	24.34	24.04	23.86
Hungarian Forint	EURHUF	290	298	294	290	286	286	287	289	290	289
Polish Zloty	EURPLN	4.26	4.15	4.14	4.13	4.12	4.07	4.02	3.96	3.91	3.90
Israeli Shekel	USDILS	3.82	3.79	3.84	3.89	3.94	3.94	3.93	3.91	3.90	3.86
Russian Ruble	USDRUB	30.1	29.8	30.5	31.2	32.0	32.1	32.1	32.2	32.2	32.0
Russian Ruble	Basket	34.2	33.8	34.4	35.0	35.7	35.9	36.1	36.3	36.5	36.5
Turkish Lira	USDTRY	1.79	1.76	1.78	1.81	1.85	1.84	1.84	1.83	1.82	1.81
South African Rand	USDZAR	8.14	8.08	8.19	8.29	8.39	8.53	8.68	8.83	8.98	9.07
<b>EM Latam</b>											
Brazilian Real	USDBRL	1.97	1.84	1.82	1.80	1.77	1.76	1.74	1.72	1.70	1.71
Chilean Peso	USDCLP	487	494	496	498	500	498	495	493	490	490
Mexican Peso	USDMXN	13.6	13.2	13.0	12.8	12.5	12.4	12.4	12.3	12.2	12.3
Colombian Peso	USDCOP	1763	1823	1821	1811	1801	1811	1823	1836	1848	1857

Source: CIRA, Bloomberg (As May 14, 2012; Forecasts as of April 13, 2012)

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