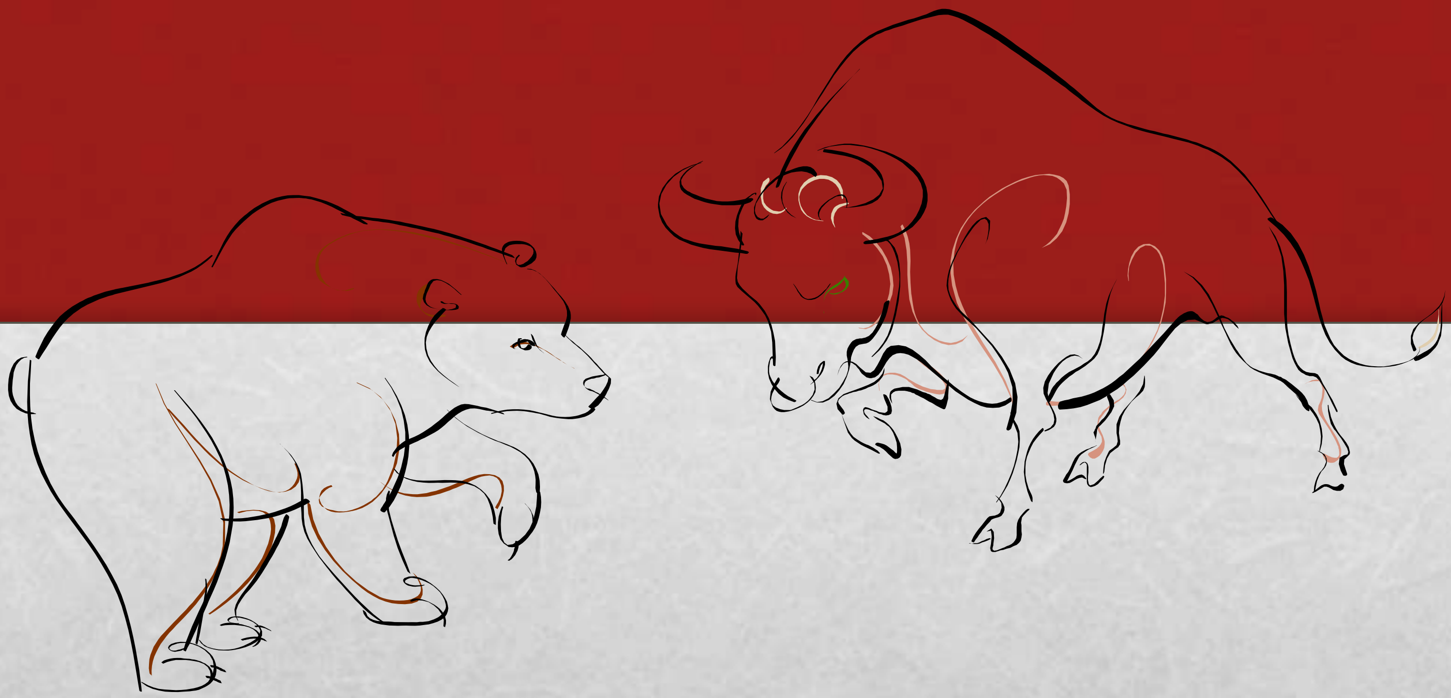
January 2009

2009 Equity Outlook



"Opportunities Amid Uncertainties"

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SBI E2-Capital

Contents

Executive summary

- 2008 was a tale of two halves in China. Solid economic growth with moderating but still high inflation in 1H was reversed by demand collapse in 2H, driven by global economic slowdown, credit tightening and financial tsunami

- China and other Asian economies realised that decoupling theory was a myth and the key to a turnaround will be greatly affected by the duration and depth of US recession

- Though US is adopting a “whatever it takes” attitude to stimulate its economy, the easing policies will not solve US’ structural problems overnight and these systematic issues will take time to unwind

- In Asia, only China has launched bold radical measures to shift their export-led models to more domestically reliant. Meanwhile, Japan slipped back into recession with emerging concerns of rising unemployment and corporate losses

Executive summary

- Going into 2009, we expect further initiatives from Chinese government to: 1) boost domestic consumption; 2) resuscitate the property sector and 3) stabilise equity markets

- In China, we expect a drawn out L-shaped scenario as recovery will take longer than many expected

- 2008 year-end rally will be short lived as we expect credit spreads to widen out from 2Q on larger than expected drop off in corporate profits, inventory/ accounts receivables impairments and rising corporate loan defaults

- Furthermore, continued asset de-leveraging will continue to weight down economic growth, prolonging recovery. We also expect the pace of investment and filter through effects of the Chinese government’s fiscal stimulus package to disappoint the market

Executive summary

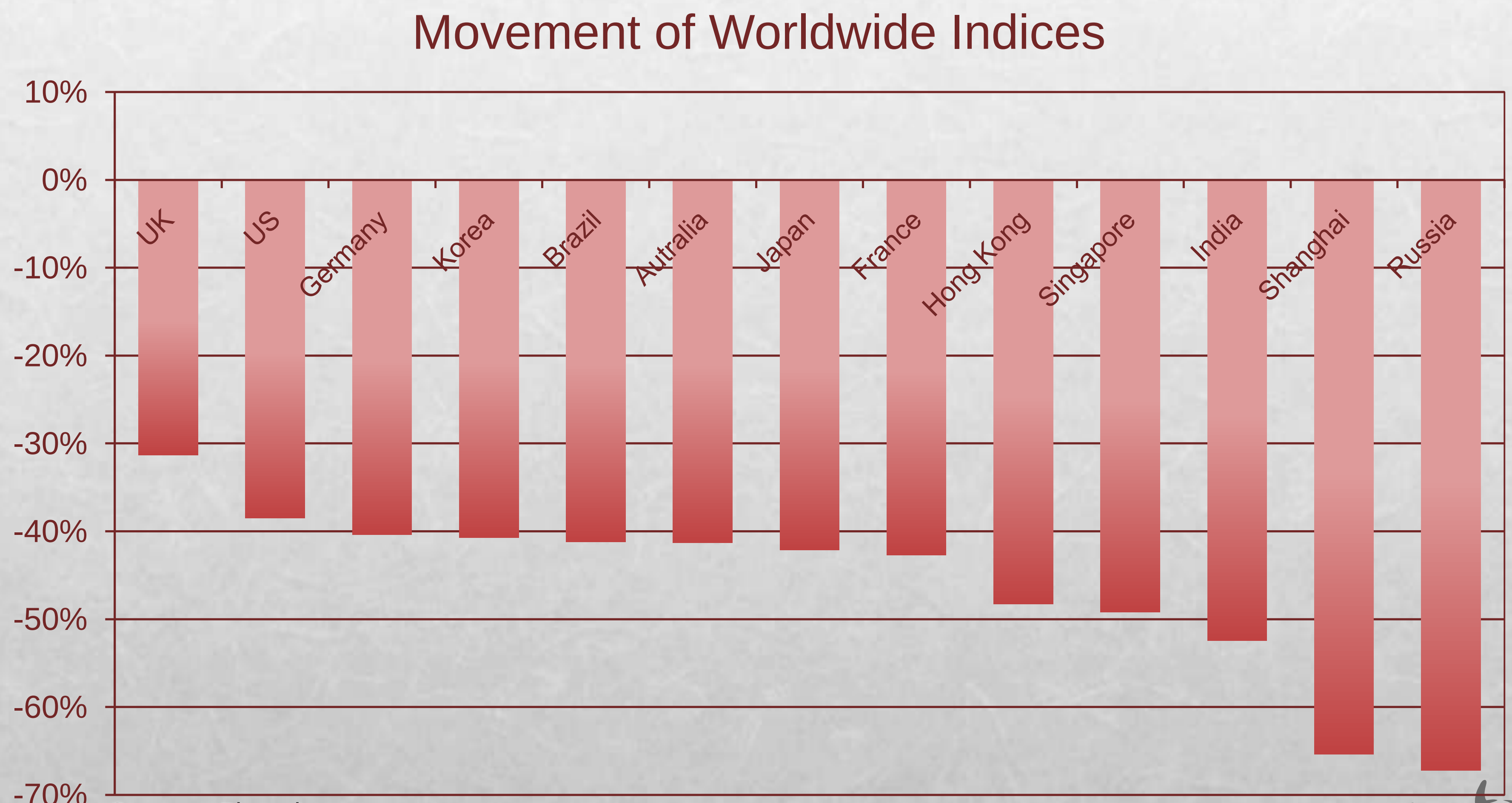
- We shift to a bottom-up approach for 2009 due to uncertainties in macro economy. We think market will reward companies which successfully navigate current economic conditions; 2) show strong working cap /balance sheet management and 3) display compelling valuations
- Equities portfolio constructed based on three core themes -
  - Companies with ability to vertically/horizontally integrate in downcycles
  - Sectors/business models with defensive qualities
  - Beneficiaries of government stimulus policies
- Our equities portfolio are –
  - Theme 1: Yurun (1068 HK), Noble Group (NOBL SP)
  - Theme 2: Shandong Weigao (8199 HK), Raffles Education (RLS SP) China Fishery (CFG SP), Times (1832 HK)
  - Theme 3: Zhuzhou CSR (3898 HK), Shanshui Cement (691 HK), CSCL (3311 HK), Solargiga (757 HK)

2008 at a glance

- Glad to see the back of 2008
  - Unprecedented volatility in global equity markets
  - Sub-prime crisis and credit tightening
  - Flight of liquidity and asset deleveraging
  - Hype in commodities super cycle….matched by bubble burst (oil started 08' at US$93/bbl, peaked at US$145/bbl and ended year at US$44/bbl)
  - Deterioration of global economic forecasts

- Decoupling theory is a myth
  - China and other Asian economics woke up to reality that their export-led models were very coupled with the US economy via 1) trade; 2) business/ investment confidence and 3) working capital

2008 at a glance



Source: Bloomberg

2008 at a glance

- Massive retreat in Hong Kong equity markets
  - HSI fell 48.3% to 14,387
  - HSCEI dropped 51.1% to 7,892
  - Daily average turnover shrank from HK$119.5b in Jan to HK$47.5b in Nov
  - Daily average turnover for Jan-Nov 08 of HK$74.8b decreased 14% YoY
  - Amount of IPO funds raised contracted 74% YoY to HK$65.9b (Jan-Nov)

2008 at a glance

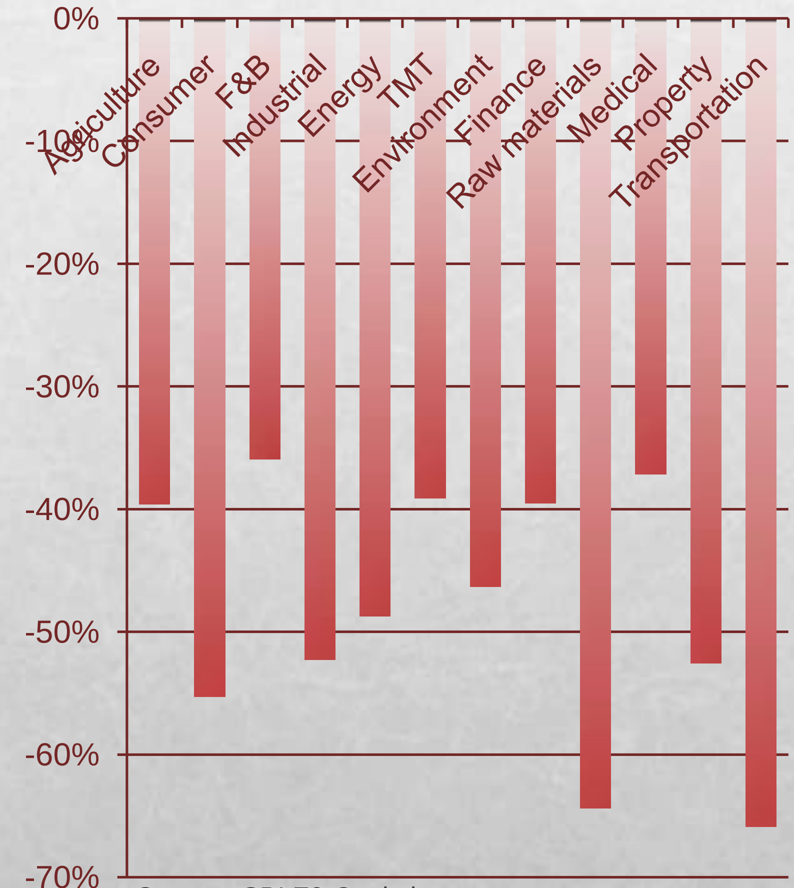
- 2008 was a tale of two halves…..

- 1H was still an extension of 2007, underlined by:
  - Strong China economic growth with moderating but still high inflation
  - Renminbi appreciation
  - Government initiatives to prevent over-heating and squeeze trade surplus
  - Solid commodities prices worldwide, led by surging oil prices

- 2H market collapse (peaking in Sep / Oct) due to financial tsunami. During this turmoil period:
  - Investors shifted from equities to high quality assets (even cash)
  - Investor mindset turned defensive as global economies stalled
  - Intra-sector wise, money converged to relative safer industry leaders

2008 at a glance

Sector Absolute Return



Source: SBI E2-Capital

Sector Relative Return

Source: SBI E2-Capital

2008 at a glance

- We underestimated impact of the following on local equities de-rating:
  - Inflation fighting polices of Chinese government in putting a brake on domestic property market
  - Asset class devaluation meltdown and fund redemption
- Our stock picks in 2008, which consisted mainly small caps, underperformed the market, though our sector strategies played well
- Relative performance of suggested sectors:
  - Retail consumption: F&B up 21.2%, other consumers down 15.3%.
  - Utilities: electricity up 47.8%, gas & water down 1.1%.
  - Healthcare/pharmaceuticals: medicals up 19.1%.
  - Upstream raw materials: raw materials down 32.5%.
  - Agriculture: agriculture up 14.6%.

Factors & influences into 2009

- "Whatever it takes for a recovery" attitude in the US…
  - Massive fiscal/monetary easing and intervention
  - Near zero interest rates (target range 0.00-0.25%)
  - Over aggressive rollout of unconventional policies (TARP, purchases of MBS)
  - Monetising of debt
- But are the easing policies enough (or quick enough) to arrest…
  - Plunging US consumption demand
  - Rising funding costs
  - Dysfunctional mortgage markets
  - Distressed banks and insurers

Factors & influences into 2009

- In our view, aggressive easing policies are unlikely to solve US' structural problems of:
  - Excesses in financial services markets
  - Highly indebted US consumers
  - Low consumer/household savings ratio
- These structural problems are systemic and need time to unwind
- Turnaround in markets unlikely to occur until US household sector start spending on discretionary and big ticket goods and services
- Furthermore, Japan economy is not helping the cause….. Asia's largest economy has recently slipped back into recession

Factors & influences into 2009

- Corporate Japan expected to reveal a series of bad results
  - Bellwether Toyota forecasts first operating loss in 71 years
  - Roll-on impact in demand for steel, chemicals and supply chain
- Rising unemployment on the horizon
  - Sony announced unprecedented 8,000 job cuts
  - Others expected to follow suit
- Weak domestic demand/economy and rising unemployment, come in the face of:
  - Conservative LDP seems reluctant to spend aggressively to stimulate economy
  - Shrinking social safety net
  - Little liquidity in Japanese job market

Current situation in China

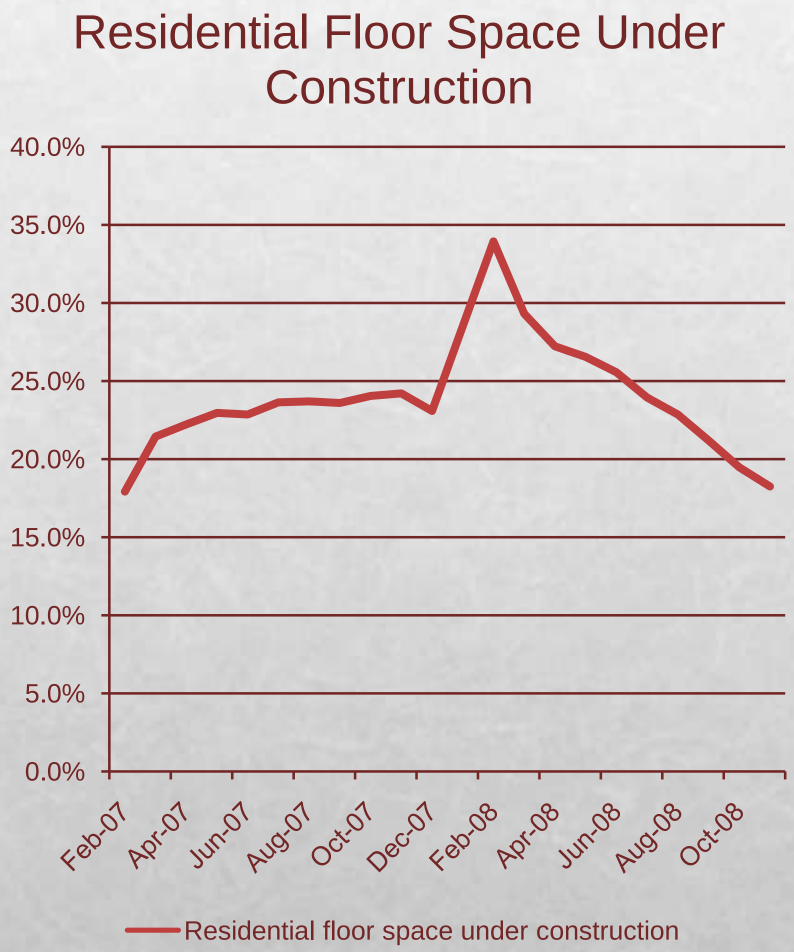
- Key reasons for abrupt economic slowdown since Oct:
  - Collapse of property market leading to lower demand for commodities such as steel
  - Plunging export demand (mainly from US) forcing industrial sector to a halt

- Broad based deteriorating economic figures
  - GDP grew 9.9% in 1-3Q, but expected to moderate to 8.7% for whole 2008
  - Exports rose 19.3% YoY from Jan to Nov, but fell 2.2% YoY in Nov
  - PPI fell to an increase of 2.0% in Nov, from 6.6% in Oct and 8.2% for Jan-Oct
  - PMI fell to a record low of 38.8 in Nov before improving slightly to 41.2 in Dec, but still well below the expansionary mark of 50
  - Oct power generation growth of -4.0% is worse since government started reporting monthly power figures in 95’
  - Guangdong, China’s largest power generating province/provincial city, fell 9.6%. Beijing plunged 24.3%

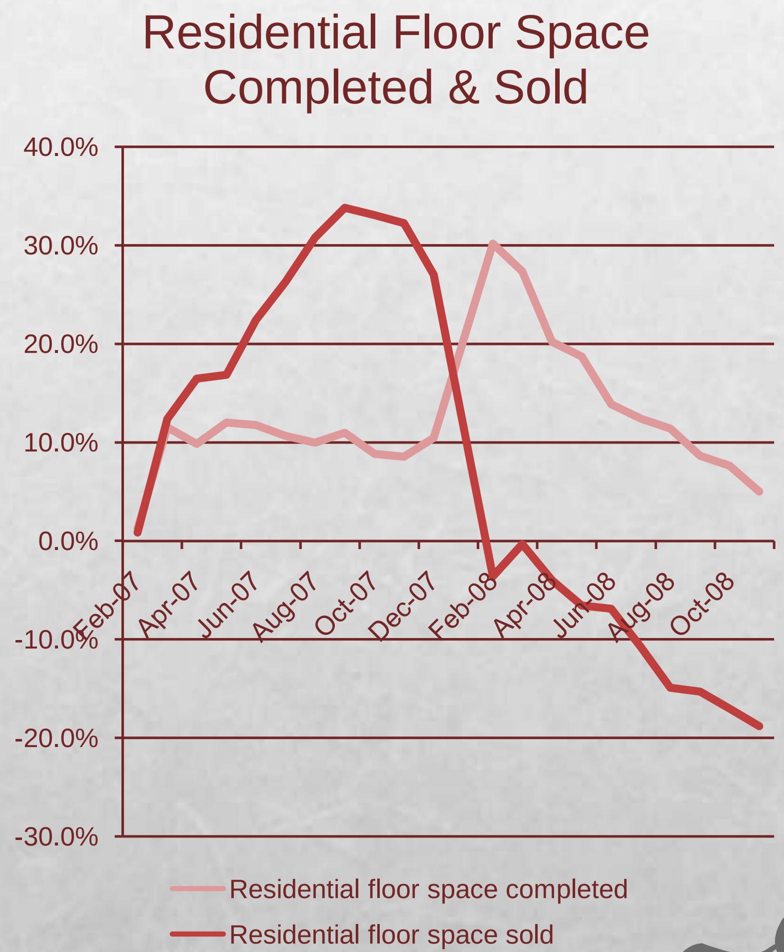
Current situation in China

- Domestic property sector anemic with residential floor space completed outstripping residential floor space sold
- With external demand contracting and surplus production capacity rising, risk to deflation is emerging

Current situation in China



Source: National Bureau of Statistics



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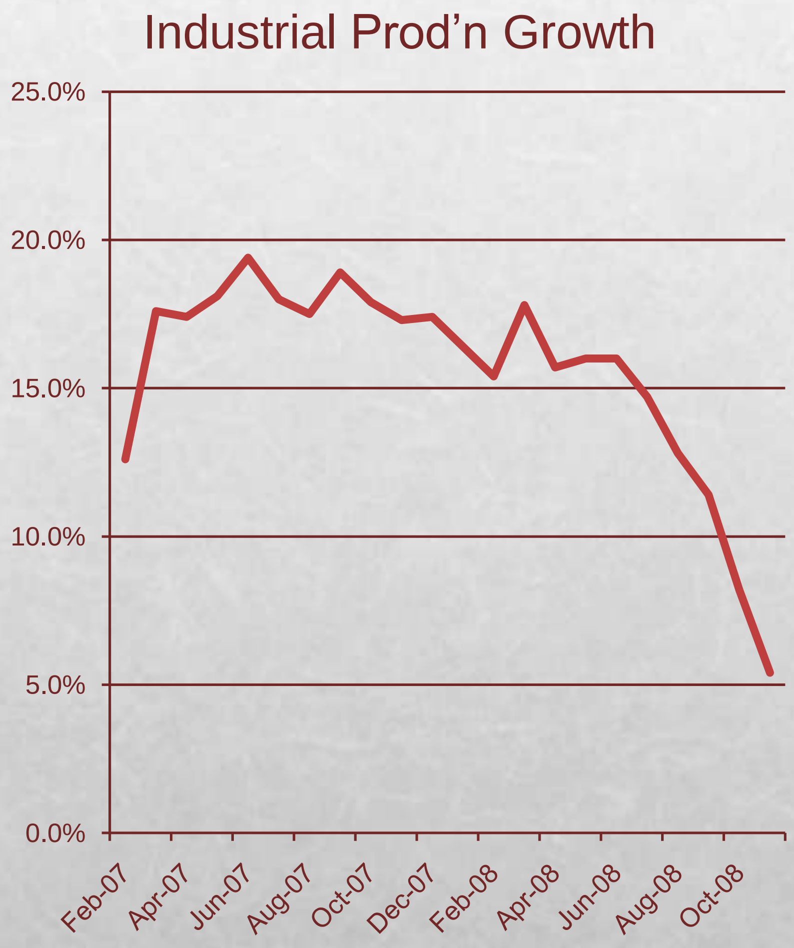
Current situation in China



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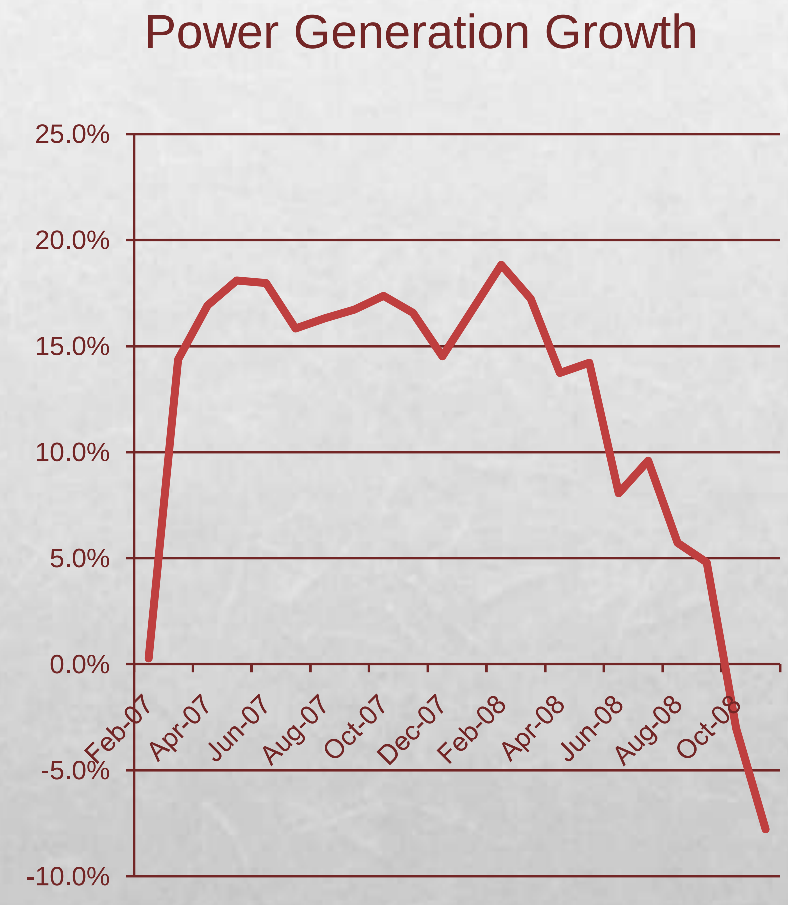

Source: National Bureau of Statistics

Current situation in China

- Sharp U-turn in Central Government policies from inflation fighting to supportive economic growth

- Announces RMB4,000b fiscal stimulus package with aim at reducing savings and boosting consumption
  - Focus on infrastructure investment
  - Bolster relatively poorer hinterland regions
  - Narrow income gap between urban and rural areas
  - Improve social safety net (healthcare, education etc...)

- Aggressively running down existing inventory
  - Imports fell 17.9% in Nov as many companies running down inventory (up 15.6% in Oct)

Current situation in China

Areas	Details of Government Initiatives
Fiscal	▪ Central government RMB4,000b fiscal stimulus package ▪ 24 provincial and local governments have separately announced stimulus packages totaling RMB18,000b
Monetary	▪ PBoC cuts interest rates 5 times in 3 months. 1-yr lending rate of 5.31% is lowest since Feb 02 ▪ Deposit reserve ratio lowered to 14.5%
Property sector	▪ Reduction of minimum down payments to 20%. Lowering of floor for interests rates to 70% of benchmark rate ▪ Reducing tax-free resale hurdle from 5 years to 2 years ▪ Sales of home with ownership <2 years will now be taxed on the profit, not on the sales price ▪ State Council encourages lenders to increase loans to developers of low-priced housing
Stock market	▪ Scrapping of stamp duties
Tax	▪ VAT reforms ▪ Increase export tax rebates ▪ Retail fuel tax reform and abolition of road maintenance fees

Current situation in China

- Shifting from export-led model to domestic consumption-led model
- But we have our concerns….
  - Fiscal stimulus package needs financial support from provincial and city governments
  - Thus much of the infrastructure (roads, ports and railway) will occur in wealthier cities and provinces, which already have more infrastructure capacity
  - Good "bang for buck", but positive effects take time to filter through system
  - But export and FAI still account for 34.6% and 55.6% of GDP, so transition will take time
  - Domestic consumption robust (up 21.9% Jan to Nov, up 20.8% in Nov), but may not accelerate fast enough to offset drop off in exports

What to expect in 2009

- Uncertainties abound within an extremely challenging environment
- Key is duration of depth of global economic recession
- In Asia, only China has shown penchant for bold radical measures. Other Asian countries are dragging their feet
- Pull back in market liquidity during 1Q redemption window (Madoff scandal)
- Further initiatives from Chinese government expected:
  - Direct measures to boost domestic consumption (lowering of tax-free threshold)
  - Measures to further resuscitate the property sector (local tax incentives etc)
  - Equity market stability measures (SOE share repurchases, short selling)

What to expect in 2009

- We expect a **drawn out L-shaped scenario** as recovery will take longer than many expect
- Year-end rally in equity market will be short lived
- Credit spreads may narrow in 1Q, but will likely widen from 2Q onwards as:
  - Higher than expected drop off in corporate profits
  - Inventory, accounts receivables impairments
  - Emergence of household / corporate defaults leading to increasing NPLs
  - Potential under performance by banks
- Continued asset de-leveraging will continue to weigh down economic growth, prolonging recovery

What to expect in 2009

- Pace of investment of RMB4,000b fiscal stimulus package will likely disappoint
  - Shortage of skills, labour and management
  - Resources in key beneficiary sectors (eg. railway construction) will be stretched
- Effects of pump priming not at their most effective until de-leveraging is complete
- Market disappointed with pace of economic recovery may show through from end of 2Q
- ….and for Hong Kong?
  - As corporate sector in Hong Kong is generally less leveraged than their China counterparts, the de-leveraging process will be completed faster than the Mainland
  - However, as the Hong Kong bourse is heavily tied to the fortunes of China and the US, a sustained economic rally is difficult

Upside & downside risks

- Upside risk
  - Larger than expected fiscal pumping by local governments
  - Increased investments into market by state bodies (eg. Lottery Funds, MoF)
  - Obstacles in 2008 becoming springboards in 2009 (commodity prices, inflation, interest rates, RMB appreciation)
- Downside risk
  - Social stability issues emerging
  - Migrant worker unemployment spilling over to urban unemployment
  - Larger than expected industry wide inventory and accounts receivables impairments

Equities strategy

- In our view, current macro economic uncertainties not conducive to top-down research approach
- Shifting to bottom-up research approach in 2009
  - Individual stock selections over sector-based strategy
  - Building a "Best of Breed, High Conviction" equities portfolio
- Market will reward companies which:
  - Successfully navigate current economic conditions
  - Show strong working capital and balance sheet management
  - Display compelling valuations

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Equities strategy

- Equities portfolio constructed based on:
  - One of three core themes -
    - Companies with ability to vertically/horizontally integrate in downcycles
    - Sectors/business models with defensive qualities
    - Beneficiaries of government stimulus policies
  - With most (or all) of the following five criteria -
    - Under-appreciated companies
    - Strong positioning
    - Financial fundamentals
    - Compelling valuation
    - Relative Size and liquidity

Equities strategy

Themes	Details
Companies with ability to vertically/horizontally integrate in downcycles	• Global markets (including developed markets of US and Europe) will become more price sensitive going forward • Increasing pressure for companies to lower cost of production • Companies which lie in the middle of the supply chain with no access to upstream material inputs or downstream end-user customers will find their business models increasingly obsolete • Companies with strong balance sheets can leverage this current global economic weakness to vertically integrate at a lower marginal cost to lower cost of production to gain market share over competitors
Sectors/business models with defensive qualities	• Companies entrenched in non-cyclical industries (eg. healthcare, consumer staples) or counter-cyclical industries (eg. education) which will offer buffer to the expected sharp downturn in the Chinese economy • Business models with sufficient flexibility to shift within the supply chain to increase earnings visibility
Beneficiaries of government stimulus policies	• Fiscal stimulus policies are geared towards fixed asset investments. Key beneficiaries are railway, construction materials, environmental sectors • New bank loans likely to favour large scale enterprises and projects which are government backed, with lower credit risk • Sectors and companies which benefit from policies to widen the social safety net and narrowing of urban/rural income gap (eg. agriculture, healthcare)

Equities strategy

Criteria	Details
Under-appreciated companies	• Unrecognised growth and/or under-appreciated business models offers greatest scope for upward revaluation • Companies with solid fundamentals which have been unfairly oversold during the recent de-leveraging process
Strong positioning	• Defensive nature • Structural strategic and competitive advantage • Sustainable competitive positions to benefit from the expected intensifying of attrition during economic downturn
Financial fundamentals	• Appealing earnings prospect • Healthy balance sheet with extensive cash position • Above average operating performance / profit margins
Compelling valuation	• Justifiable pricing with sound upside potential • Limited downside risk
Size and liquidity	• In a market where trading liquidity is shrinking, size and liquidity matters • The stocks in our equity portfolio has an average market capitalisation of US$878m and average 3-month daily trading volume of US$4.5m

Equities portfolio

Themes	Stock Picks
Companies with ability to horizontally/vertically integrate	• Yurun (1068 HK, HK$9.12) • Noble Group (NOBL SP, S$1.11)
Sectors/business models with defensive qualities	• Shandong Weigao (8199 HK, HK$11.40) • Raffles Education (RLS SP, S$0.59) • China Fishery (CFG SP, S$0.66) • Times (1832 HK, HK$2.00)
Beneficiaries of government stimulus policies	• Zhuzhou CSR Times (3898 HK, HK$5.88) • Shanshui Cement (691 HK, HK$1.81) • China State Construction (3311 HK, HK$1.25) • Solargiga (757 HK, HK$1.94)

Yurun (1068 HK) – Horizontal consolidation

Ticker: 1068 HK Price: HK$9.12	Mkt cap: US$1,790.2m Daily t/o, 3 mth: US$7.0m Free float: 55.9%	12 mth range: HK$6.30-13.96 3 mth abt. return: -8.8% 3 mth rel. return: -2.0%

- Yurun has been positioning itself since establishment as a quality, hygienic and safe meat producer, which allows it to charge premium prices and gain market share on small & individual players
- Although ASP and dollar gross margin will drop following the correction in pork price, this negative impact will likely be offset by sales volume increase backed by recovery in hog supply and capacity expansion
- China's rising food standards have been pushing small players, who lack sufficient capital to upgrade facilities, out of the market
- Amid this backdrop, the company has been able to continuously expand its upstream capacity by acquiring those poor-managed firms at attractive valuation and then, turn them around normally within 6-12 months

Noble Group (NOBL SP) – Moving up & down stream

Ticker: NOBL SP Price: S$1.11	Mkt cap: US$2,391.2m Daily t/o, 3 mth: US$22.8m Free float: 52.2%	12 mth range: S$0.46-2.70 3 mth abt. return: +26.1% 3 mth rel. return: +40.8%

- The metals-to-agriculture asset medium supply chain conglomerate is prime candidate to vertically integrate am across its various commodities pipelines
- Strong balance sheet and cash flow. Its cash-on-hand of US$1.1b (end-3Q08) is highest ever. Net gearing of 40.1% lower than many of its competitors
- As commodity price falls, working cap is released back to the company and becomes a “funding source”. Working cap inflow was US$1.3b in 3Q08
- Global footprint allows them to take advantage of arbitrage opportunities. Current planned investments include sugar refineries, ethanol processing facilities, coal mines and grain silos
- Vertical integration during commodities downcycle allows NOBL to consolidate supply chain and lower overall cost of production when upcycle returns
- Offers good long-term value at 4.8x 08F and 5.7x 09F P/E

Shandong Weigao (8199 HK) – Leader in Defensive Sector

Ticker: 8199 HK Price: HK$11.40	Mkt cap: US$1,573.0m Daily t/o, 3 mth: US$1.1m Free float: 36.2%	12 mth range: HK$5.76-17.08 3 mth abt. return: +11.8% 3 mth rel. return: +20.1%

- Medical devices is defensive sector with resilient demand. Growth of sales in China's medical devices industry in first eight months was 32.0% to RMB44.3b
- Hard-to-replicate strategy of leveraging a comprehensive product portfolio and extensive distribution, which brings defensibility to the company's business model
- Direct distribution network covering 80.3% Class 1 hospitals, 23.9% Class 2 hospitals and 6.2% Class 3 hospitals (5,000+ direct and indirect distribution channels)
- Ability to win market share in foreign supplier-dominated markets is the company's key growth strategy. Projected 3-yr net profit CAGR of 54.3%

Raffles Education (RLS SP) – In a class of its own

Ticker: RLS SP Price: S$0.59	Mkt cap: US$913.6m Daily t/o, 3 mth: US$4.2m Free float: 62.4%	12 mth range: S$0.41-1.49 3 mth abt. return: +12.4% 3 mth rel. return: +25.5%

- Education sector is a counter-cyclical industry and China's education and training is a sunrise industry. College graduates was 4.8m in 2007 (2004: 2.5m)
- China accounts for 74% of revenues. Company has 15 colleges in China. It also owns Oriental University City (OUC) in Langfang, Hebei – a 3.31m sqm self contained campus with 19 colleges and 57,000 students
- Strong government support. Directive issued in 2006 to accelerate reform and development of vocational education market, through the construction of 100 "model institutes"
- Cash prepayment model generates solid cash flows and good earnings visibility. Students prepays each 12 week term, or in the case of OUC, prepays for the entire year. Drop out rate is low as credits not easily transferable to other institutes

China Fishery (CFG SP) - Demand spurred by the slowdown

Ticker: CFG SP Price: S$0.66	Mkt cap: US$344.1m Daily t/o, 3 mth: US$0.3m Free float: 21.8%	12 mth range: S$0.40-1.99 3 mth abt. return: -9.6% 3 mth rel. return: +0.9%

- As one of the cheapest white-meat fish, Pollock's demand has been encouraged by current economy slowdown
- The company's ASP of Alaska pollock increased 18.4% in 3Q FY12/08A. Harvest volume will increase in FY12/09F as Russian government has raised its total allowable catch by around 10%
- The steep drop in the oil price will largely ease the company's cost pressure and improve its operating margin in FY12/09F. Fuel costs accounted for 27.2% of total sales in 3Q FY12/09A
- Orders in hand will protect fishmeal division in 4Q despite the declining fishmeal price. The segment should be able to maintain a thin profit in FY12/09F

Times (1832 HK) – Properly positioned to defend slowdown

Ticker: 1832 HK Price: HK$2.00	Mkt cap: US$224.1m Daily t/o, 3 mth: <US$0.1m Free float: 27.6%	12 mth range: HK$1.18–3.80 3 mth abt. return: -20.4% 3 mth rel. return: -25.9%

- The company is a hypermarket chain in eastern China, concentrating on secondary cities
- As consumption in secondary cities appears less affected by the economic slowdown as well as relatively steady demand for staples, we consider Times is defensive
- It had 62 stores, including 45 hypermarkets and 17 supermarkets, at end-Jun. Sites for 17 new stores have been confirmed. Six will open in 2H FY12/08F and 10 in 2009. Normally new stores take up to two years to breakeven
- Net margin in 1H FY12/08A widened 0.4pcp to 4.3%, which was at higher-end of the industry range, thanks to less-competitive environment in the secondary cities and the company's effective management in operating expenses

Zhuzhou CSR (3898 HK) – Cheapest railway play

Ticker: 3898 HK Price: HK$5.88	Mkt cap: US$817.4m Daily t/o, 3 mth: US$2.1m Free float: 42.1%	12 mth range: HK$3.02-12.16 3 mth abt. return: +22.5% 3 mth rel. return: +31.6%

- Railway is the key area of investment for government's RMB4,000b stimulus package. Investment in 2009 budgeted to be RMB600b, almost double 2008
- Equipment manufacturers have better long term prospects (relative to contractors) in our view given: 1) less cyclical business nature; 2) pure exposure to railway infrastructure investment; 3) higher entry barriers and profitability
- Zhuzhou CSR's current order books stand at RMB3.0b, with RMB2.0b to be booked in FY12/09 and RMB1.0b to be booked in FY12/10
- Growth areas for the company are: 1) urban rail, 2) high power load locomotive and 3) power semiconductors. Tender win for the Shenyang Metro was the first urban rail to adopt power equipment fully developed by domestic suppliers
- At 14.6x 08F and 11.8x 09F P/E, Zhuzhou is the cheapest railway sector play offering good risk-to-reward

Shanshui Cement (691 HK) – Favourite in the materials sector

Ticker: 691 HK Price: HK$1.81	Mkt cap: US$626.8m Daily t/o, 3 mth: US$0.9m Free float: 43.4%	12 mth range: HK$0.76-3.36 3 mth abt. return: +7.7% 3 mth rel. return: +15.7%

- Shanshui's market share is estimated at ~33% in Shandong and ~10-15% in Liaoning, its two main markets. Local market share (in presence cities) estimated to be upwards of 80%
- Favourable view on Shandong and Liaoning's cement sector, driven by: 1) aggressive elimination of old capacities and 2) infrastructure investment from fiscal stimulus packages of central and provincial governments
- Increased infrastructure investment favours scaled players such as Shanshui as they can offer better guarantees on production volumes, consistency and quality control
- Weak property market in 1H 09 will hurt small local players which typically align themselves with property developers. This will accelerate industry consolidation

CSCL (3311 HK) – Potential upside in China infrastructure exposure

Ticker: 3311 HK Price: HK$1.25	Mkt cap: US$391.4m Daily t/o, 3 mth: US$2.2m Free float: 36.5%	12 mth range: HK$0.60-3.78 3 mth abt. return: +16.8% 3 mth rel. return: +25.5%

- Prime beneficiary of HKSAR government's aggressive infrastructure investment schedule to boost local economy. CSCL has 10.0%+ market share in Hong Kong construction segment, back by a 30-yr track record
- Secured HK$10.0b new contracts in 2008, Contract backlog of HK$22.8b to be booked over next 2-2.5 years
- Exposure to solid emerging countries such as UAE, Dubai, Abu Dhabi, Macau and India
- To smooth out revenue streams and lift gross margins, company diversified into infrastructure investment in 2007. It currently operates one heat and electricity plant and two toll bridges in China. We expect more asset injection from parent group and/or acquisitions from third parties
- Potential upside in securing construction works from China's infrastructure investment. Company exploring options including: 1) partnerships/JVs/ sub-licensing agreements with parent co's construction arm and 2) partnering with other Chinese contractors

Solargiga (757 HK) – Competitive player in sunrise industry

Ticker: 757 HK Price: HK$1.94	Mkt cap: US$420.5m Daily t/o, 3 mth: US$1.2m Free float: 35.6%	12 mth range: HK$1.13-7.10 3 mth abt. return: -12.2% 3 mth rel. return: -5.7%

- Bottleneck of polysilicon supply is expected to be resolved by 2010, which will spur solar PV installation and encourage a consumption shift back to crystalline silicon products

- The company is China's second largest manufacturer of monocrystalline silicon ingots. Major products include ingots and wafers used in crystalline silicon solar systems

- The company plans to double its ingot capacity to 4,000 tonnes by 2009 and increase wafer capacity to 150m pieces from 48m

- With several long-term contracts signed 2008, company has largely secure its polysilicon supply in 2009. The long-term contracts will also bring down the blended procurement cost, which will favor gross margin in short term

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