

Committee meeting of September 4, 2009

A lovely summer

The outlook for recovery in the second half of this year has become a bit brighter over the past few weeks, contributing to the rise in share prices, which were also boosted by surprisingly strong corporate earnings. **Although the worst now seems behind us some clouds remain on the horizon**, since growth will remain subdued for some time and sales are also likely to disappoint.

However, the current dynamic is positive. Private-sector economists, central banks and international institutions worldwide have raised their GDP forecasts. Securities analysts have also taken note of second-quarter earnings figures and have raised their earnings forecasts sharply.

Central bankers still cautious

Central banks are using very cautious language and are careful to point out the uncertainties that remain. Their attitude could have two positive effects: it could prevent investors from being overly disappointed by economic data when the pace of economic recovery slackens after the sharp rebound in manufacturing; and it could above all **provide reassurance that accommodative monetary policies will be maintained.** This is no doubt the objective of Ben Bernanke and his counterparts. This message also applies to fiscal policy. The OECD has thus pointed out that: "Preparing credible exit strategies and fiscal consolidation plans now, even if actual implementation will only commence later, is desirable". The statement of the G20 finance ministers, after their meeting in early September, expresses this same idea: "we will continue to implement [...] expansionary fiscal and monetary policies [...] until a global recovery is firmly secured".

The long-term environment for equity markets is buoyant

Given the positive trend in economic conditions and the attention that government authorities continue to focus on their economies, **we do not foresee another marked slump in economic activity**, but rather the stabilisation of growth below its potential. The exuberance in equity markets over the past few months (the MSCI AC World is up 60 % from its year-to-date low of early March) has brought investor sentiment indicators to very optimistic levels. Although they do not yet send a sell signal, the risk of a near-term correction has grown. **However, since institutional investors are still substantially underexposed to equities this should limit the magnitude of any technical correction**, particularly since valuations do not seem too high and the prospect of mergers and acquisitions is becoming an increasingly strong theme. **We have therefore increased our overweight in equities a bit.**

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Writing ended on September 10th



ASSET ALLOCATION

Allocation decisions

- We have raised our positive exposure to equity markets slightly, but with a tactical reduction in emerging markets considering their very strong performance since March.
- We are still neutral in government bonds, which are under pressure from the opposing forces of extremely low benchmark interest rates and the lack of inflationary pressure on one hand, and economic recovery and concerns about "exit strategies" on the other. Our preference goes to European bonds.
- We are overweight in IG credit, which continues to benefit from the economic recovery, even though spreads, at their current levels, are likely to narrow more slowly. We are underweight in HY credit, which we believe still carries substantial risks.
- Our position in commodities is still "wait-and-see", with an overweight in the less cyclical sectors of gold and agriculture.

Developed equity markets

- We have shifted some of our positions in this asset class to take advantage of the cyclical rebound in the global economy, with overweights in continental Europe and Japan, which are also attractively valued relative to their peers. We expect the Japanese market to receive a boost from the sharp upward revisions in earnings forecasts, while the prospect that

the new government will implement ambitious reforms could be a positive factor over the longer term.

- Neutral to slight overweight in the US, where the continued vigour of fiscal and monetary measures compensate for the diminished appeal of a safe-haven market.
- Exposures to Australia, the United Kingdom and Canada were reduced to neutral, slightly underweight and negative respectively, on our concern about the near-term outlook for cyclical commodities. Australia's solid growth and exposure to Asian economies have made its market relatively expensive. The country is also likely to tighten its monetary policy soon.

Emerging equity markets

- We have further reduced our position in Chinese equities, to slightly overweight.
- Our preference goes to Korea (stronger earnings forecasts and a buoyant technical configuration) and to Turkey, which offers relatively attractive valuations and solid economic fundamentals.
- Underweight in South Africa, where the outlooks for the economy and corporate earnings are unfavourable

Typical diversified model portfolio – Institutional clients

The model portfolio holdings below are measured against cash and may be transposed into any other portfolio whether benchmarked or not. **Due to changes in the portfolio optimisation process, valid comparisons with the previous month cannot be made this month.**

| | Alpha | sept-09 weights |
|--------------------------------------|-------|-----------------|
| MULTI-ASSET CLASS¹ | | |
| EQUITIES | | |
| Developed Equities | 0.2 | 0.6% |
| Emerging Equities | 0.2 | 0.3% |
| FIXED INCOME | | |
| Government Bonds | 0.0 | 0.0% |
| Investment Grade | 0.1 | 0.8% |
| High Yield | -0.1 | -0.4% |
| COMMODITIES | | |
| Brent Oil | 0.1 | 0.1% |
| Base Metals | -0.2 | -0.5% |
| Gold | 0.2 | 0.4% |
| Agricultural | 0.2 | 1.0% |
| Cash Euro | 0.0 | -2.4% |
| Module Total | | |

| | Alpha | sept-09 weights |
|--------------------------------------------------|-------|-----------------|
| EQUITIES: DEVELOPED COUNTRIES¹ | | |
| US | 0.0 | 0.2% |
| Canada | -0.3 | -1.6% |
| Euroland | 0.2 | 1.3% |
| Japan | 0.2 | 0.7% |
| UK | -0.1 | -0.9% |
| Switzerland | 0.1 | 0.5% |
| Australia | 0.0 | -0.1% |
| Module Total | | |

| | Alpha | sept-09 weights |
|-------------------------------------------------|-------|-----------------|
| EQUITIES: EMERGING COUNTRIES³ | | |
| Brazil | 0.0 | 0.0% |
| China | 0.0 | 0.3% |
| India | 0.0 | 0.0% |
| South-Korea | 0.1 | 0.7% |
| Taiwan | -0.1 | -0.4% |
| Russia | -0.1 | -0.2% |
| South Africa | -0.2 | -1.5% |
| Turkey | 0.2 | 1.0% |
| Module Total | | 0.0% |

BONDS: COUNTRIES SOVEREIGN⁴

| | Alpha | sept-09 weights |
|--------------|-------|-----------------|
| US | -0.1 | -3.1% |
| Euroland | 0.4 | 11.2% |
| Japan | -0.1 | -2.9% |
| UK | 0.0 | -1.7% |
| Switzerland | -0.1 | -3.4% |
| Module Total | | 0.0% |

PORTFOLIO STATISTICS

| | |
|----------------------------|-------|
| Average Ex-ante Volatility | 1.00% |
| Target Ex-ante Volatility | 0.78% |
| Real Ex-ante Volatility | 0.90% |

1- Hedged in Euro, 2- MSCI hedged in Euro
3- MSCI local unhedged, 4- JPM GBI hedged in Euro,
5- Forwards to Euro investor



ECONOMIC OUTLOOK

Viewpoint

The economy is recovering, right?

Although it is relatively easy to understand that two consecutive quarters of negative GDP growth mean the economy has "entered a recession", we can be less certain that one or more quarters of positive growth mean it is "coming out of a recession". And yet the prospect of economic recovery has been in the spotlight since 2nd quarter GDP growth estimates were released for Germany (+0.3 %), France (+0.3 %) and Japan (+0.9 %). Although economic activity **probably hit bottom in mid-2009**, should we be thrilled about the outlook for sluggish growth after such a brutal plunge? In other words, doesn't the very prospect of "coming out of a recession" carry with it the risk of disappointment, even if the economy does not fall back into negative growth?

Central banks are still very prudent about the economic outlook, no doubt because they want to calm expectations that the crisis is over and the economy is recovering. The US Federal Reserve, for example, feels that the economic situation is "stabilizing", yet points to various factors that could limit consumer spending, such as ongoing job losses, very slow income growth, decreasing property wealth and tighter credit conditions. In the United Kingdom, the BoE is faced with a recession it qualifies as "very deep". As for the euro zone, Jean-Claude Trichet emphasizes the persistent uncertainty, and does not exclude "bumpy roads" nor "contradictory signs". The message is fairly clear: **central banks are in no hurry to raise their key interest rates or to do away with "unconventional" monetary policy measures**. Just like the tortoise in Aesop's fable, they believe that "slow and steady wins the race". Although their approach is well accepted for the time being – since inflation is generally negative in most developed countries due to energy-related base effects – it could be challenged if these same effects start putting upward pressure on price indices. Moreover, if the oil barrel price remains at 70 USD until the end of the year it will be 75 % higher than it was a year earlier. In short, proclaiming that the economy is now on a strong path to recovery, as some governments are now doing, could cause some central banks to shift their

monetary policy too sharply. We believe however that they will resist such pressures.

Investors are a bit less positive about economic news. After dropping below zero last April and rising sharply until mid-June, the number of net positive surprises about the economic outlook relative to the market consensus seems to have hit a ceiling over the summer. However, most investors continue to be "positively surprised", even though economic news seems a bit less upbeat than over the spring, when the "green shoots" first appeared. Our analysis at that time has been validated, since the situation has not gotten worse. Moreover, the economy is clearly in a stronger position, since **most statistics continue to improve, particularly those concerning the US manufacturing and property sectors**. Still, investor response to good news has been less enthusiastic.

If things do not improve over the near term, we could see a new wave of investor uncertainty and pessimism that could easily be exacerbated by such exogenous factors as swine flu, for example. The global economy is still fragile and we are convinced that growth will remain below its potential for a few more quarters. **This does not mean however that we think the recovery will fizzle out.** Nonetheless, recent economic forecasts could be called into question if financial markets once again become "depressed" and share prices fall, spreads widen and currency volatility rises. In such a delicate environment, **reappointing Ben Bernanke to head the Federal Reserve was no doubt a wise decision.**

Consensus Forecasts: Growth & Inflation

| 28/08/2009 M= Mean; H=High; L=Low | GDP y.o.y% | | | | | | | | Inflation y.o.y% | | | | | | | | | | | |
|--------------------------------------|------------|------|------|------|--------|-----|------|------|------------------|-----|------|------|------|--------|------|-----|------|--------|--|--|
| | 2008 | | 2009 | | | | 2010 | | | | 2008 | | 2009 | | | | 2010 | | | |
| | M | H | L | -1M | M | H | L | -1M | M | H | L | -1M | M | H | L | -1M | | | | |
| Developed Economies | | | | | | | | | | | | | | | | | | | | |
| USA | 0.4 | -2.6 | -2.3 | -3.1 | [-2.6] | 2.3 | 3.9 | 0.3 | [2.1] | 3.8 | -0.5 | -0.3 | -0.9 | [-0.6] | 1.8 | 3.5 | 0.9 | [1.8] | | |
| Canada | 0.5 | -2.3 | -1.8 | -3.0 | [-2.3] | 2.2 | 2.9 | 1.4 | [2.1] | 2.4 | 0.5 | 0.8 | 0.2 | [0.4] | 1.8 | 2.6 | 1.3 | [1.8] | | |
| Euro zone | 0.6 | -4.3 | -3.6 | -4.7 | [-4.4] | 0.6 | 2.3 | -0.7 | [0.4] | 3.3 | 0.3 | 0.5 | 0.0 | [0.4] | 1.2 | 1.7 | 0.7 | [1.2] | | |
| UK | 0.7 | -4.3 | -3.2 | -4.8 | [-4.0] | 0.9 | 2.0 | -0.8 | [0.8] | 3.6 | 1.8 | 2.5 | 0.9 | [1.8] | 1.7 | 3.3 | 0.5 | [1.8] | | |
| Switzerland | 1.6 | -2.5 | -1.4 | -3.5 | [-2.5] | 0.3 | 1.9 | -0.8 | [0.3] | 2.4 | -0.4 | 0.2 | -0.6 | [-0.5] | 0.7 | 1.6 | -0.1 | [0.6] | | |
| Japan | -0.7 | -6.1 | -5.4 | -7.0 | [-6.2] | 1.3 | 3.5 | 0.3 | [1.4] | 1.4 | -1.2 | -0.8 | -1.6 | [-1.2] | -0.6 | 0.0 | -1.2 | [-0.6] | | |
| Australia | 2.1 | 0.3 | 0.8 | -0.4 | [-0.1] | 1.8 | 3.0 | 0.8 | [1.5] | 4.4 | 1.7 | 2.0 | 1.4 | [1.7] | 2.2 | 2.9 | 1.5 | [2.2] | | |

Source: Consensus Forecasts as of 10/08/2009



ECONOMIC OUTLOOK

Developed economies

Global economy has improved but is still convalescing

In its Interim Assessment of the economic outlook for Europe, the United States and Japan, the OECD says that its short-term forecasting models "point to an earlier recovery than envisaged a few months ago". The OECD did point out however that "the pace of the recovery is likely to be modest for some time to come". This is now the position of all major national and international institutions, which acknowledge the improvement but are still cautious about the future.

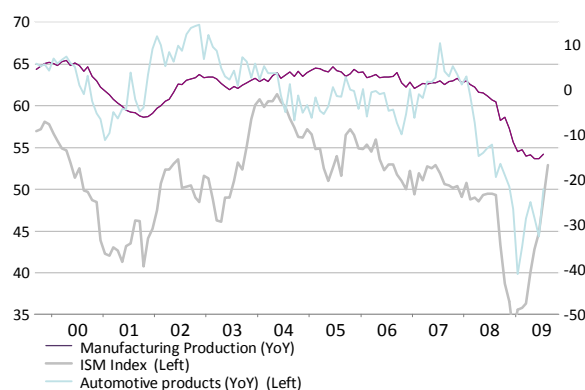
US manufacturing is growing again. ISM survey data for the manufacturing sector released on September 1 marks the return of positive growth, with the index rising above 50 for the first time since January 2008. Index components are favourable, with both orders and employment continuing to improve. The level of 52.9 reached in August is historically consistent with an annualised GDP growth rate of 3.7 %. GDP shrank 1 % in the second quarter.

Private consumption is still vulnerable. The US government's cash-for-clunkers programme had little impact on retail sales or consumer spending in July, since most of the 690,000 vehicles purchased under the programme (which cost taxpayers \$3 billion) were sold in August. Automakers have already said that this programme's success has enabled them to reopen some plants and thus limit layoffs. As a result, automotive production has increased significantly, from an annual rate of less than 4 million vehicles in June (the lowest this year) to 5.7 million in July. As with similar efforts in Europe, this stimulus programme will have only a temporary effect on growth. It may however have a more lasting impact on confidence. After contracting at an annualised real rate of 1 % in the second quarter, private consumption rose a modest 0.2 % in July and could continue to grow.

Fed is determined to be cautious. The Federal Reserve kept its fed funds target within the 0 % to 0.25 % range in August, where it has been since December, and Fed officials reiterated that "economic conditions are likely to warrant exceptionally low levels of the federal funds rate for an extended period". In a joint statement with the US Treasury, the Fed also announced that it would extend, until mid-2010, its TALF programme, which is mainly intended to ease credit to consumers and the commercial property sector. Purchases of Treasury securities are expected to be completed by the end of October. Since the initial target of \$300 billion has not been increased and the current pace of purchases (\$270 billion since March) is likely to slow somewhat, the transition should be smooth. The minutes of the last FOMC meeting show that its members were convinced that the Fed must continue to communicate that it has the tools and the willpower to begin a "withdrawal of policy accommodation at the appropriate time". Among other things, the committee members discussed the various tools that could be used to achieve a smooth transition,

such as: reverse repurchase agreements (which could be extended to counterparties other than primary dealers); a term deposit facility to reduce the supply of excess reserves; and measures to tighten the link between the interest rate paid on reserve balances and the federal funds rate.

United States – manufacturing recovers



Source: Factset, BNPP AM

Some good surprises in the euro area this summer. The results of purchasing manager surveys released on August 21 have confirmed various national survey findings that economic activity has stopped contracting. The PMI composite index has indeed jumped sharply in August, from 47 to the threshold level of 50. This trend suggests that we should see positive growth in the third quarter, particularly since the German Ifo index has been rising for five months, and the trend for the French manufacturing index is also positive. According to INSEE, the French national statistics bureau, the outlook for both foreign and domestic demand for French manufactured goods has improved. Furthermore, national accounts figures for the second quarter were better than expected and rather encouraging for the rest of the year. In France, and especially in Germany where GDP rose 0.3 %, inventory destocking continued (reducing GDP by 0.6 % in France and 1.9 % in Germany), and consumer spending rose (by 0.3 % and 0.7 % respectively) as rebates on new car purchases made in spring began to impact statistics. Business investment continued to decline in France but at a slower pace of -1 % (after -2.6 %) and rose 0.8 % in Germany, after falling 7.7 %. This may mainly be attributed to a pickup in the construction sector enabled by more favourable weather.



ECONOMIC OUTLOOK

Developed economies

Europe gets back on its feet

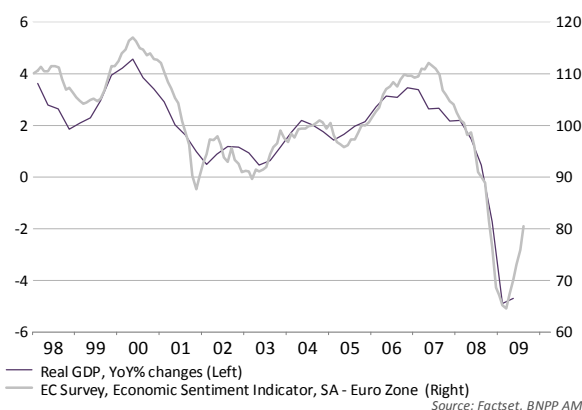
In the euro area, the components of GDP growth in Q2 (-0.1 % after -2.5 % in Q1) reveal a similar trend: a slight increase in private consumption, ongoing destocking (making a negative contribution of -0.7 %, after -0.8 % in Q1), and a positive contribution to growth from net exports, since imports have fallen more sharply than exports. Business investment continues to decline and public spending is supporting economic activity.

Beyond the near-term support that restocking is likely to provide, there are two main questions concerning the sustainability of the recovery now underway in the euro area's two largest economies: will foreign demand strengthen and will consumer spending be maintained once the direct impact of stimulus measures has faded?

The stronger global economy should boost exports, particularly in countries that export capital goods. Although the euro is higher now than last spring, it is unlikely to handicap exporters at its current level. Consumer spending however may be constrained by high unemployment and fears of job losses. The "windfall effect" of measures to support automobile sales have probably shifted consumer spending rather than actually increasing it, and some governments are already concerned about what may happen when these measures are withdrawn. By boosting manufacturing and reducing the number of layoffs (particularly at automotive part suppliers), these measures have also had a positive psychological impact. Restoring confidence is essential to economic recovery. Unemployment benefits and a high savings rate (15.6 % in Q1 vs. 13.8 % a year earlier, according to Eurostat) have traditionally provided a cushion for the euro area's economy. Yet despite this, annual GDP growth year-on-year fell to -4.9 % in the first quarter, which should be its lowest point over the current cycle.

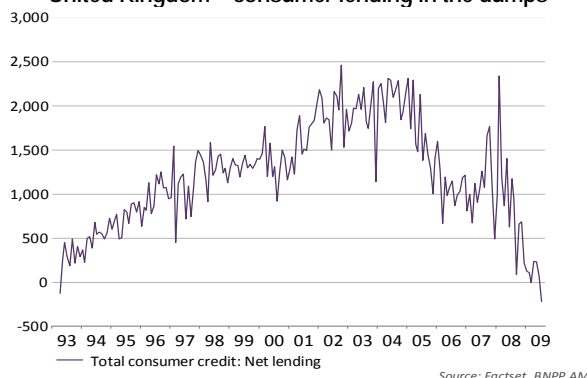
The ECB has raised its growth forecasts, but expect no change in monetary policy. After its last meeting of September 3, the ECB made no change to its benchmark interest rate, which it feels is "appropriate", and announced that its next 12-month refinancing operation on September 30 would be at 1 %. ECB officials decided not to increase the spread with the refi rate as previously discussed, and the overall tone concerning the economic situation was rather optimistic. Jean-Claude Trichet did indeed say that the recession was over, while repeating however that "uncertainties remain high". The GDP growth forecast was raised, with the central forecast for average annual growth now -4.1 %, vs. -4.6 % in June. ECB economists now expect slightly positive growth of 0.2 % in 2010, instead of 0.3 % contraction as forecast in June. This does not mean however that monetary tightening is around the corner, since inflation expectations are modest (0.4 % in 2009 and 1.2 % in 2010) and medium-term expectations are well anchored.

Euro area – business confidence improves



Bank of England still very cautious. after its August meeting, which unsurprisingly ended with the base rate maintained at 0.5 %, the BoE announced a £50 billion increase in its Gilt purchase programme, bringing the total to £175 million. Mervyn King insisted on the recession's severity, and the quarterly report on inflation released a few days earlier confirmed the perception of a "deeper recession than we first feared". The central bank foresees a slow recovery and moderate inflation of less than 1 % by the end of the year and less than 2 % in 2010 and 2011. This caution is justified by economic indicators released over the past few weeks. After rising above 50 in July, the CIPS index for the manufacturing sector fell back to 49.7 in August.

United Kingdom – consumer lending in the dumps



ECONOMIC OUTLOOK

Developed economies

Japan's quest for structural reform

The UK has however benefited from the improvement in the global economy, as seen by order backlogs, which continued to grow and should encourage UK firms to boost production. After declining 0.7 % in the second quarter, GDP could therefore begin to grow positively in the third, although this growth could be hindered by the still anaemic state of consumer and business lending.

The property sector shows signs of stabilizing as measured by prices and the number of mortgage loans granted. The latter has been rising since June and reached its highest level since April 2008 in July. This stabilisation will be a key factor in supporting domestic demand, which moreover will continue to be burdened by the highest jobless rate since 1996 and sluggish wage growth.

Stronger global demand boosts the Swiss economy.

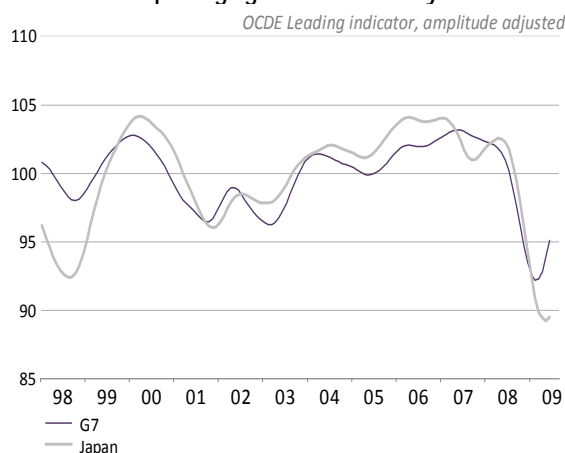
Switzerland's high exposure to the global economy is now a positive rather than a negative factor, as manufacturing activity picks up worldwide. The KOF "barometer" of the Swiss economy has been improving for the past four months and is now just barely negative (-0.04 in August), which according to KOF means that GDP could stop contracting in early 2010. GDP data for the second quarter is already encouraging with contraction of only 0.3 % (much less than expected) and private consumption and investment up 0.6 % and 1.1 % respectively.

Given the relative stability of the EUR/CHF exchange rate in August, at around 1.52, the Swiss franc should not be a key factor at the SNB's monetary policy committee meeting on September 17. We expect the central bank to maintain its Libor fluctuation margin at 0 % to 0.75 %, since Libor has been at 0.30 % since early September and therefore not far from the SNB's objective of bringing it gradually toward the low end of the fluctuation margin, i.e. around 0.25 %.

Japan's manufacturing rebound is well underway.

National accounts figures for the 2nd quarter now show a 0.9 % rebound in GDP after four quarters of contraction. However, this still leaves GDP growth year-on-year at -6.4 %, after a trough of -8.7 % in the 1st quarter. This improvement may mainly be attributed to foreign trade (rising exports and falling imports have added 1.3 % to growth) and a 0.8 % pickup in consumer spending (vs. contraction of 1.2 %) resulting from short-term fiscal stimulus measures that normally cannot be continued. So even though the outgoing prime minister has welcomed this quarterly growth, made possible by "the government's measures", the OECD feels that Japan's position in the economic cycle (a "possible trough") is a bit less favourable than that of other major economies, which it believes have hit a "trough" or are even "recovering".

Japan lags global economic cycle



Japanese economy is burdened by overcapacity, which is weighing on business investment (as shown by the Tankan and other business surveys), and by considerable overstaffing, unemployment hit a high of 5.7 % in July. Nonetheless, orders for capital goods rose in May and June, which could give business investment a small boost. According to the Economy Watchers survey Japan's economy seems to be hitting a plateau, whereas the PMI indices of the other major industrialised countries are approaching levels that reflect economic expansion, with the PMI composite index for the euro area now at 50 and the US ISM index for manufacturing up to 52.9 in August.

The results of the general election were as expected, with the Liberal Democratic Party (LDP) led by Taro Aso losing its majority in the Lower House to the Democratic Party of Japan. The DPJ's leader, Yukio Hatoyama is expected to become prime minister and to work to correct social disparities by implementing measures to support domestic demand over the near and long terms, and undertaking ambitious reforms to reduce corruption in government.

Bank of Japan stands pat. The BoJ has maintained its benchmark interest rate at 0.10 % since last December, even though it now feels that "the economic situation has stopped getting worse". It will however have to deal with the return of deflation (the headline and core-price indices were down 2.2 % and 0.9 % respectively in July year-on-year) and is unlikely to tighten monetary policy for quite some time.



ECONOMIC OUTLOOK

Developed economies

Special article – update on the US property market

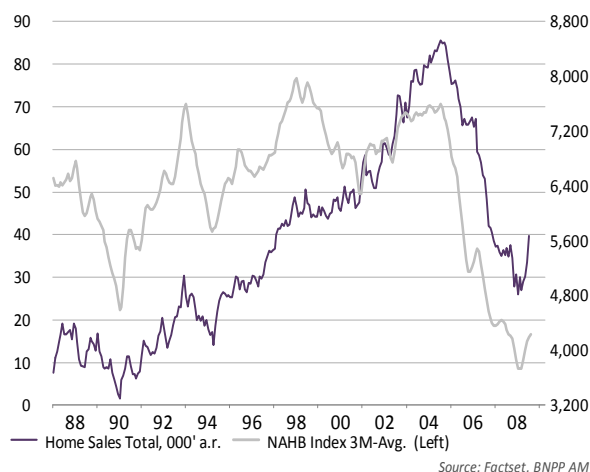
Housing market picks up. The most recent indicators have confirmed the impression that has been building over the past few months, that the US housing market has hit bottom and is slowly starting to recovery. The charts speak for themselves. Yet despite the increase in home sales over the past four months (9.6 % and 7.2 % for new and existing homes respectively in July) and in housing starts, these levels are of course much lower than those seen during the housing bubble. According to the National Association of Realtors, home sales in July thus reached an annualised rate of 5.6 million units, vs. an average rate of 7.5 million from 2002 to 2005, with foreclosed properties accounting for 31 % of existing home sales. Although the homebuilder confidence index reached its highest level in a year on August 18, this is still well below its long-term average of 52.

Government stimulus measures. The \$8,000 tax credit available to first-time homebuyers until the end of November accounts for much of the increase in home sales over the past few months. The outlook for the next six months is good and is consistent with the recovering US economy. Financial conditions have improved, with the Housing Affordability Index (which takes into account mortgage loan rates and home prices relative to median income) at its highest level since the NAHB has been compiling this index, or 18 years. Since the Federal Reserve's monetary policy will help keep interest rates low (the "conventional rate" on 30-year mortgage loans has been around 5 % since the beginning of the year) and home prices will be slow to increase, this should encourage consumers to purchase a home, especially if the tax credit programme is extended for another year and expanded to include all prospective homebuyers, as home-builders are trying to convince Congress to do.

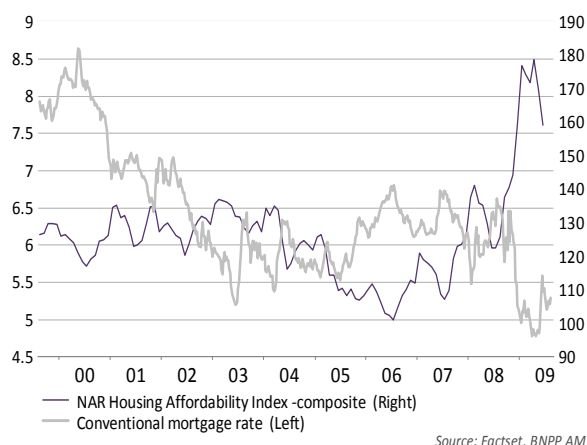
But there are still problems. For one thing, there is a large stock of unsold homes, with over 4 million at the end of July, representing 9.4 months of sales at the current rate, vs. a normal stock of 5 to 6 months. At the start of the year there was a year's worth of unsold homes. Prices continue to fall year-on-year, even though there are signs of stabilisation here also, with the home price index for the 20 largest cities down 15.4 % in June, vs. a low point of -19 % in January. Lastly, a weak labour market may delay the housing market's recovery as unemployment pushes some households into over-indebtedness and others postpone a home purchase for fear of losing their job.

Lastly, the weak economy is weighing on the **commercial property market** and although its effects will be less devastating than on residential property, a rising number of defaults could weaken the balance sheets of smaller US banks, which hold a high proportion of commercial real estate loans.

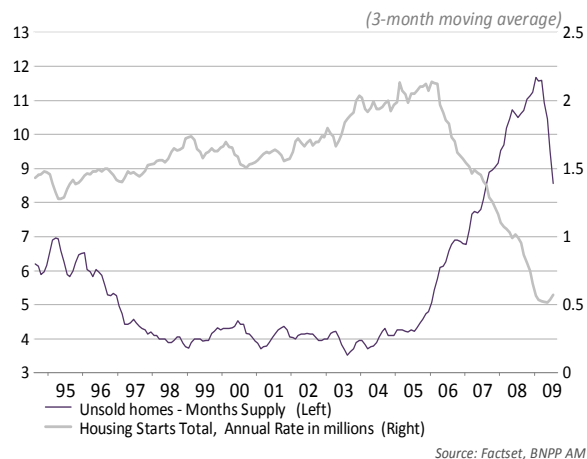
United States – home sales recover



United States – homes are more affordable



United States – still a large stock of unsold homes



ECONOMIC OUTLOOK

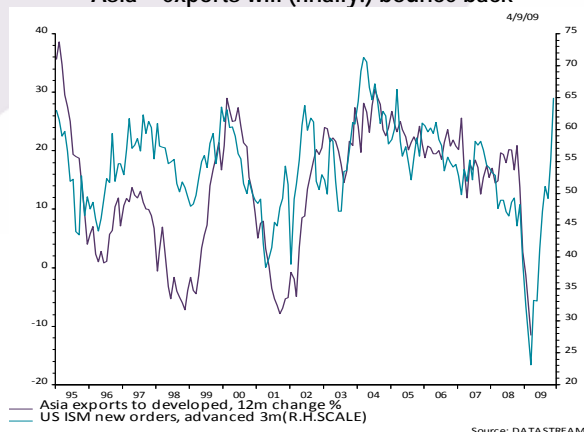
Emerging economies

Economic activity still robust

Emerging economies are still going strong. Industrial output has bounced back sharply and is even back to its pre-financial crisis level in Korea. This recovery has mainly been driven by domestic demand, which has been fuelled by expansive fiscal and monetary policies. Business confidence indicators show that economic activity continues to improve, with exports to the developed countries making an increasingly large contribution to growth. This is particularly true of China, where the government's aggressive efforts have rapidly restored growth.

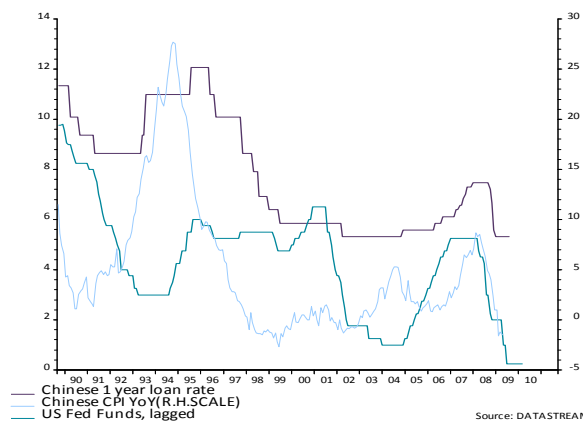
However, the likely slowdown in the flood of liquidity over the coming months will dampen growth. **With only a few exceptions, no further interest-rate cuts may be expected** and the spectre of normalisation is becoming inevitable. This is already the case in Israel and Korea is probably next in line.

Asia – exports will (finally!) bounce back



The appearance of pockets of speculation and the sudden plunge in new lending have sparked fears that **China** will soon tighten its monetary policy. **We believe however that the stricter attitude that Chinese authorities are taking towards new lending conditions is motivated more by a desire to preserve loan quality rather than to cool down economic growth.** Furthermore, now that the recovery appears to be more firmly entrenched, exceptional measures can no longer be justified. It should be noted that lending has surged over 30 % over the past year, and that a 1.2 % growth in loans is historically correlated with 1 % GDP growth. Lastly, it is too early to start raising interest rates, with inflation and the fed funds rate as low as they are.

China – interest rates will stay low for now



There is of course uncertainty as to how smooth the transition from rapid growth fuelled by public spending to more balanced growth supported by the private sector will be. This uncertainty explains the high volatility of Chinese equities, as seen by the plunge in A shares in August.

The strength of China's economy will not be affected over the medium term. Even if credit becomes tighter, the 8 trillion yuan of loans granted since the beginning of the year are financing many long-term projects that will continue to have a positive impact on statistics over the next few quarters. Furthermore, abundant liquidity remains available for strategic projects in such sectors as transportation and energy.

The foundations of personal consumption are solid, with brighter prospects for higher wages, employment and consumer confidence. This is reflected in the rebounding of property prices and the rapid growth of retail and automobile sales. With over 12 million automobiles forecast to be sold in 2009, China is expected to replace the United States as the world's largest market for cars. More favourable lending conditions will also support business activity. Lastly, **the stronger global economy will boost exports**, as confirmed by higher freight rates for ships leaving Shanghai and rising export orders.



ECONOMIC OUTLOOK

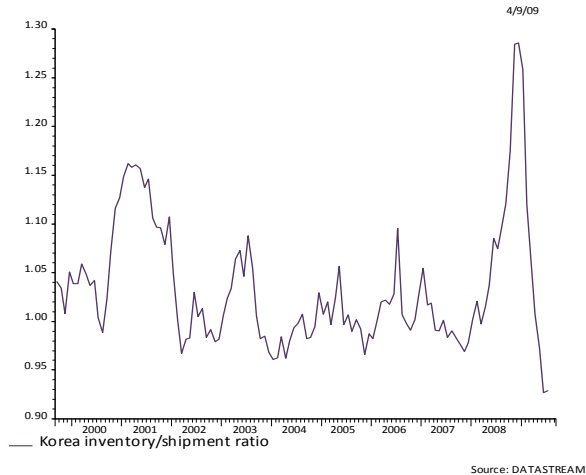
Emerging economies

Korea's recovery is one of the strongest among the emerging countries, much to the surprise of many observers. Industrial output is up for the seventh straight month, while business and consumer confidence are at their highest levels in 22 months and 7 years respectively. **We expect GDP growth to accelerate over the coming months** as firms restock and trade picks up, particularly with China, which purchases a quarter of Korean exports.

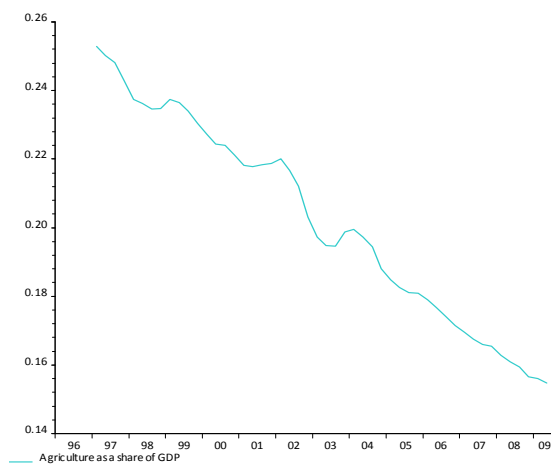
Taiwan's economy hit bottom in June and leading indicators point to a recovery over the coming months. This is the case of the semiconductor industry, where the ratio of new orders to shipments augurs well for a period of growth. A sharp rebound in GDP, driven by business investment and industrial output, is expected in 2010.

India's cyclical trough is already behind it, judging from the most recent economic data. Annualised GDP growth in the second quarter was 6.1 % and it seems to be on track to meet the government's target of 7 % to 8 %. India's economy, which is mainly driven by domestic demand, suffered relatively little from the 19 % drop in exports, as shown by the 7.8 % rebound in industrial output in June. The extensive monetary and fiscal measures implemented have been successful in sustaining business investment and private consumption. **In response to this significant improvement in the economy and the expected return of inflation, we expect the RBI to start tightening monetary policy in the first quarter of 2010.** The relatively dry monsoon season this year does pose a threat to farm output and therefore the economy, but the potential impact of this on domestic economic activity seems overestimated, since the primary sector's contribution to GDP is steadily shrinking.

Korea – restocking should boost production



India – Since 1950, agriculture's share of GDP has shrunk from 48 % to 15 %



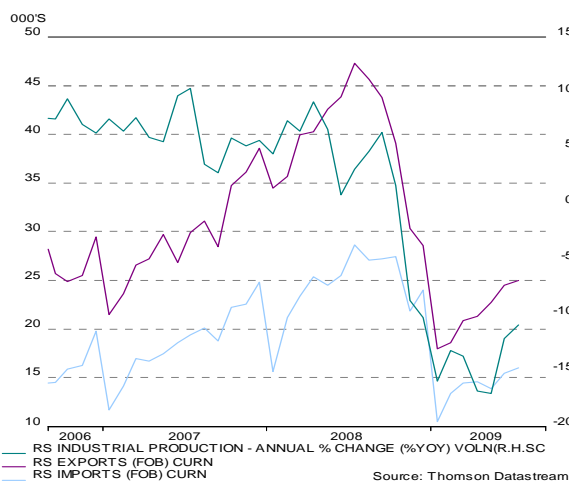
ECONOMIC OUTLOOK

Emerging economies

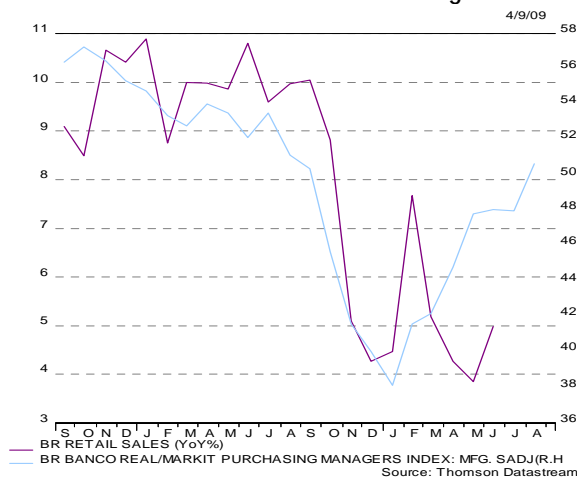
Russia's economy continues to perform poorly, with GDP expected to shrink 10 % over the first half of the year and inflation in the double digits. However, the outlook is expected to improve thanks to rising oil prices and the strengthening of the global economy. Indeed, the decline of industrial output has slowed from 16.8 % contraction in April to 10.85 % in July, a trend that is confirmed by the most recent survey data. The PMI index for manufacturing was 49.6 in August while the services index has already risen substantially to 52.2. Since the year-on-year inflation rate was stable in August at 11.6 %, the country's central bank is free to pursue its expansionary monetary policy.

The outlook for **Brazil's** economy continues to improve. Industrial output keeps climbing upward to recovery, rising 2 % in July m/m, but is still negative on a year-on-year basis. Essentially driven by output and new orders, the manufacturing PMI entered growth territory in August for the first time since September 2008. The jobless rate has been falling steadily for the past four months, down to 8 % in July, which provides a solid foundation for consumer confidence. Furthermore, the country's central bank has confirmed market expectations with a unanimous decision to **stop expansionary monetary policy**, after having cut its key interest rate by 500 bp since January.

Russia – economic indicators are positive



Brazil – economic outlook is bright



BOND MARKETS

Government bonds

Highs and lows

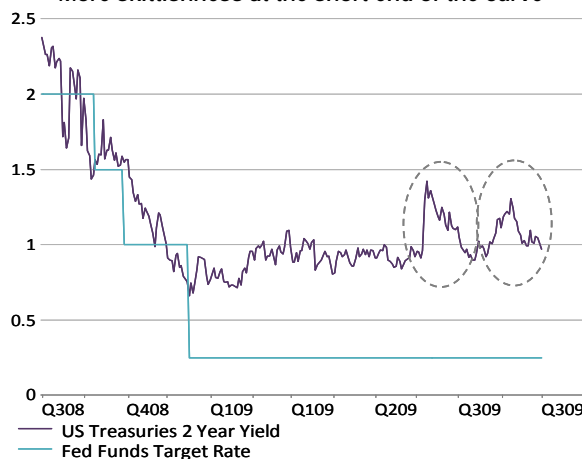
The stabilisation and subsequent improvement in economic indicators we have seen over the past few months has sparked debate about the particular shape the economic recovery might take. This brighter outlook has been good for the riskier asset classes and unfavourable to "safe-haven" investments, such as government bonds, now that investors have dismissed the possibility of a doomsday scenario. Bond yields have been bouncing up and down ever since. This is no doubt because investors are still a bit confused – although economic activity was quick to improve from such a low point recovery will not continue at this pace.

The economic outlook is still not that good. Low unemployment and substantial capacity under-utilisation are two reasons why growth and inflation are likely to be sluggish for a few more quarters. This will obviously put significant downward pressure on yields for a while. Furthermore, the near-term trend is still unfavourable to bond investors: with economic data surprisingly strong and leading indicators approaching or even exceeding an "expansionary" level. **These factors have left yields moving trendlessly, but jumping back and forth between new highs and lows. Although this situation complicates tactical allocation it does offer short-term investment opportunities.**

Monetary policies will also play a key role in government bond markets, and in particular the transition from accommodative measures to an orderly withdrawal of liquidity. For the time being, central bankers are generally trying to reassure investors that current monetary conditions will be maintained as long as necessary. They indeed seem more concerned about the risk of not doing enough rather than doing too much, particularly in the United States and the United Kingdom. Although this should normally be enough to calm investor nerves at the short end of the curve, we are in fact seeing, at least in the US, more and more skittishness here and this is likely to continue.

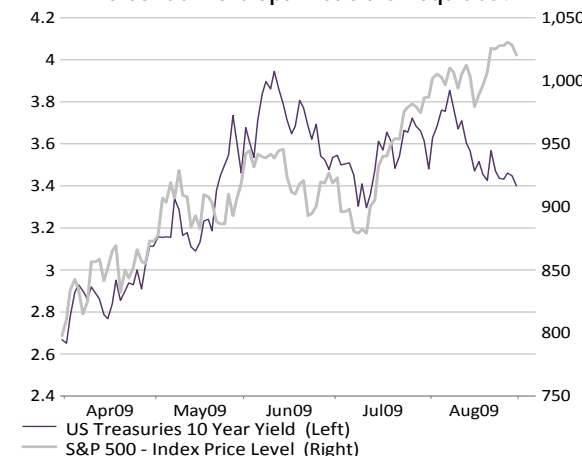
We are now therefore maintaining a **neutral** position in government bonds.

More skittishness at the short end of the curve



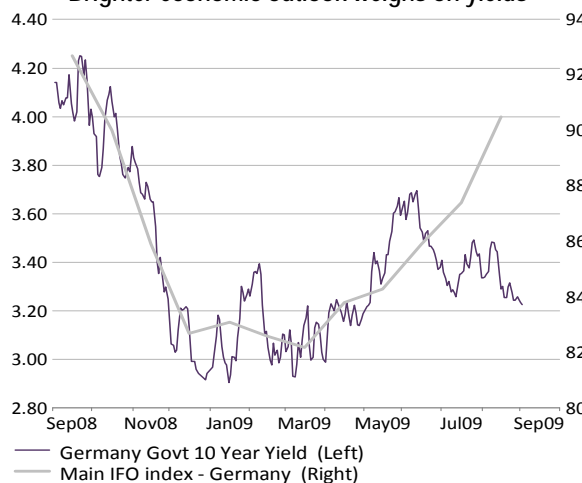
Source: Factset, BNPPAM

Are bonds more optimistic than equities?



Source: Factset, BNPPAM

Brighter economic outlook weighs on yields



Source: Factset, BNPPAM

BOND MARKETS

IG and HY credit

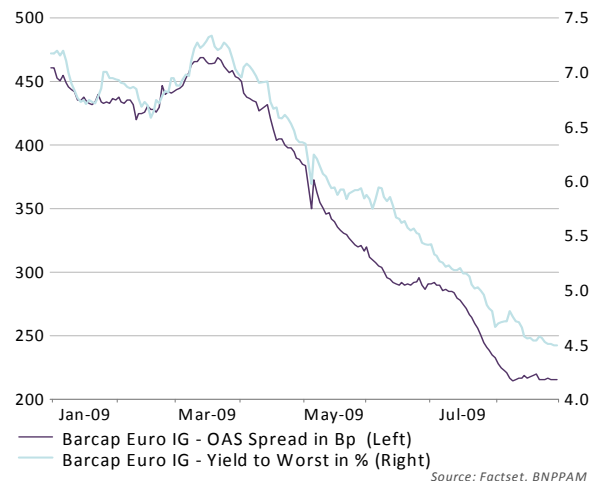
Let's catch our breath

It has been six months since equity markets hit bottom. Credit markets have done quite well over this period, with spreads narrowing very rapidly from historically high levels. With a Depression scenario no longer a threat, fewer fears about the financial system, economic conditions stronger and corporate earnings better than expected, investors have been more willing to take on risk and have been attracted back to credit. This has encouraged more and more firms to issue debt at increasingly advantageous terms.

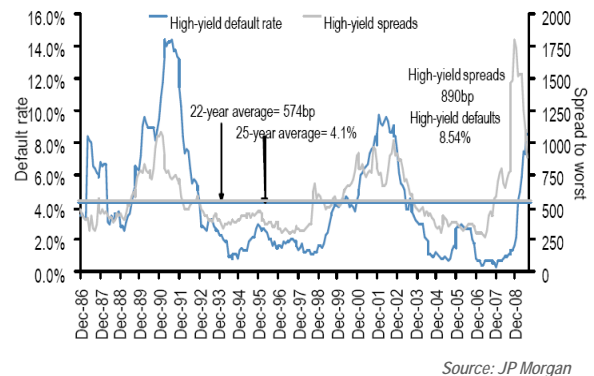
Although the overall trend for **Investment Grade** continues to be favourable, achieving gains in this market will not be as "easy" and will depend on the speed and the shape of economic recovery. Since the latter will be very slow, and not without risk, the road ahead for IG credit may be a bit bumpier. We believe however that **valuations are still attractive** and fund flows continue to support this market, although it should be noted that investor allocations in this asset class already seem quite substantial, with long-term exposure at an historically high level. We therefore remain **overweight** in IG credit.

This positive economic trend and these technical factors are also good for **High Yield** bonds, although the month of August was relatively weak, with a sharp drop in primary market issuance, less enthusiasm for issues on the secondary market, and fund flows more or less mixed. And yet, what makes us rather sceptical about the HY market has more to do with fundamentals and valuations. Economic recovery from a very deep bottom is not the same thing as fast growth, **since the problems that firms, and particularly the weakest, must face do not just disappear overnight** in an environment of sluggish GDP and earnings growth and large financing requirements. We continue to be cautious in this market, with a **slight underweight**.

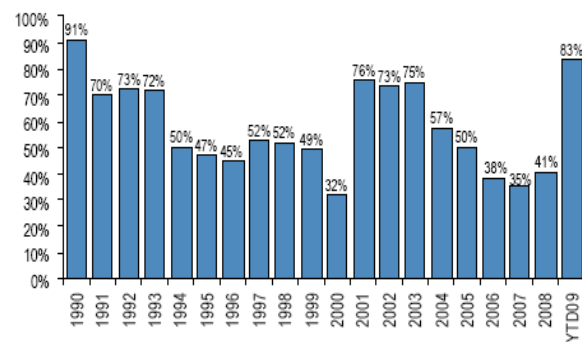
IG – spread compression is slowing



HY – default rate up, spreads down



HY – new issues mainly serve to refinance maturing debt



CURRENCY MARKET

A difficult autumn for the dollar

Normalisation is underway in the currency market. The US dollar, after first rising against our universe of currencies early in the year, is now tending to weaken. In terms of investment strategy, we believe it is wise to continue to take advantage of the correlation between "financial normalisation" and investor appetite for risk and dollars in the second half of 2009. **Thereafter, economic factors and fundamentals will once again play a key role in the currency market.**

The dollar could continue to suffer. The implied volatility of the 1-month forward EUR/USD rate fell slightly again last month. Except for the dollar's rise above 1.44 in early August, this rate has been relatively stable, with the euro hovering around 1.42 USD. Risk aversion, non-farm job losses in the United States and the outlook for inflation must be very closely monitored to understand where the dollar might be headed. As shown in the table below, **we will continue to play the strong correlation between risk appetite and EUR/USD for the rest of the year.** The normalisation of financial conditions could indeed revive investor risk appetite, which would push the euro up against the greenback. Another factor in favour of the euro is the surprising strength of recently published economic indicators (particularly in Germany) that has helped push EUR/USD above 1.45 in early September.

What will the yen do after the elections? USD/JPY has been fluctuating around 96 over a fairly broad range since mid-June. It almost reached 98 on August 7, after the release of the US jobs report caused the dollar to surge. Thereafter the yen has tended to strengthen as Japan's tax

break holiday has encouraged the repatriation of foreign dividends. The economic programme presented by the Democratic Party of Japan, the winner of the August 30 elections, focuses heavily on boosting domestic demand and supporting small and medium-sized firms. This has led some market observers to conclude that the next Japanese administration would offer less resistance to a stronger yen. In any case, Japan's economy is still very weak with record unemployment and the outlook for growth and inflation still quite poor. Furthermore, in the first half of 2010 we expect the yen to become a more attractive benchmark currency for carry trades than the US dollar, which could weaken the yen a bit. **We expect the yen to fall slightly from its current level.**

Rest of G7 currencies. The **Australian** and the **Canadian** dollars have continued to benefit from increasing risk appetite and strong economic fundamentals. However, a sharp appreciation of the currencies of these commodity-exporting countries could become a problem in the current environment. In this sense, the CAD's appreciation is beginning to be seen as a potential risk factor by Canada's central bank. In fact, a too strong Canadian Dollar may reduce the competitiveness of Canadian manufacturers, who mainly export to the United States.

According to our fair-value model, the **pound sterling** is still undervalued as quantitative easing continues to put pressure on GBP to depreciate. However, it could therefore **begin to strengthen over the coming months** in response to financial normalisation and the currency's pro-cyclical nature, which will begin to come into play once the QE programme is completed.

FX Rate Forecast Summary (Major Currencies)

| End of Period | | 2008 | 04-Sep-09 | 3Q 2009 | | 4Q 2009 | | 1Q 2010 | | 2Q 2010 | |
|---------------|-----------|------|-----------|---------|------|---------|------|---------|------|---------|------|
| | | | | Min | Max | Min | Max | Min | Max | Min | Max |
| USD Block | EUR / USD | 1,39 | 1,42 | 1,40 | 1,45 | 1,43 | 1,48 | 1,40 | 1,45 | 1,40 | 1,45 |
| | USD / JPY | 91 | 93 | 93 | 98 | 95 | 100 | 100 | 105 | 100 | 105 |
| | USD / CAD | 1,23 | 1,09 | 1,08 | 1,13 | 1,08 | 1,13 | 1,10 | 1,15 | 1,10 | 1,15 |
| | AUD / USD | 0,70 | 0,85 | 0,83 | 0,88 | 0,85 | 0,90 | 0,85 | 0,90 | 0,85 | 0,90 |
| | GBP / USD | 1,44 | 1,63 | 1,64 | 1,74 | 1,71 | 1,82 | 1,68 | 1,78 | 1,68 | 1,78 |
| | USD / CHF | 1,06 | 1,07 | 1,05 | 1,09 | 1,05 | 1,09 | 1,09 | 1,12 | 1,09 | 1,12 |
| EUR Block | EUR / JPY | 126 | 132 | 133 | 140 | 138 | 146 | 143 | 150 | 143 | 150 |
| | EUR / GBP | 0,97 | 0,87 | 0,82 | 0,87 | 0,80 | 0,85 | 0,80 | 0,85 | 0,80 | 0,85 |
| | EUR / CHF | 1,48 | 1,52 | 1,50 | 1,55 | 1,53 | 1,58 | 1,55 | 1,60 | 1,55 | 1,60 |

Source: BNPP AM as of 4/9/2009



EQUITY MARKETS

Developed markets

Overweight strengthened over the coming months

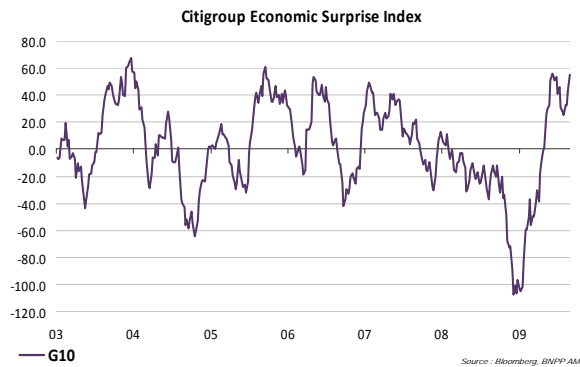
Although recent market euphoria could weigh on share prices over the near term, the improvement in economic conditions is likely to continue for a few more months and we believe fundamentals continue to favour equities, despite the many risks that still threaten the economy and financial markets. Over the longer term, fears of economic weakness and/or concerns about the timing of the withdrawal of highly accommodative monetary and fiscal policy measures and the strategies employed for this are likely to weigh on equity markets.

A favourable macroeconomic environment. Improving economic statistics and survey data and upward revisions of earnings forecasts, which are much higher than expected, are likely to continue to support the market for a few more months. Purchasing manager indices (the ISM in the US) have been recovering steadily after hitting bottom early in the year. They are now rising above the threshold level of 50 that separates economic expansion from contraction. **The current trend in new orders and inventories suggests that this cyclical upturn should last for a few more months.** History has shown that two-thirds of the stock market gains correlated with rising leading indicators occur as the ISM index recovers and rises to 50. Therefore, although the market has rallied quite strongly since its low of last March, the cyclical improvement in the economy should still enable further upside potential for equities.

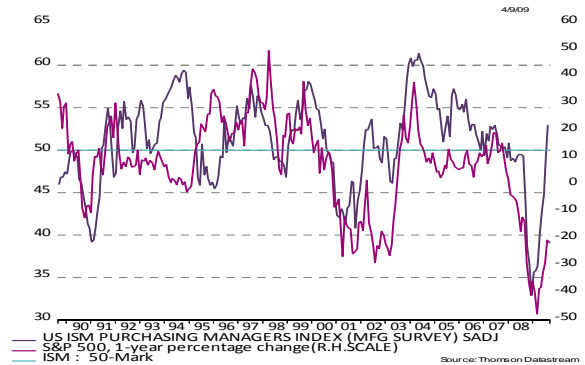
Corporate earnings. The second-quarter earnings reporting season has been rich in positive surprises; although some of these are partly attributable to previous sharp drops in earnings projections and to massive cost-cutting. The combination of this with clearly stronger economic news has resulted in **many upward revisions in earnings growth forecasts.** Although many of these revisions have already been made, given the upturn in the global economic cycle, we expect this trend to continue and to support equity markets.

Moreover, corporate earnings seem to be bottoming out. But although the base effect will be very favourable in 2010, earnings growth will still be severely constrained as weak pricing power continues to squeeze margins tightly, firms and consumers try to reduce debt, unemployment remains high and the effects of fiscal stimulus measures slowly fade – all of which will weigh on sales.

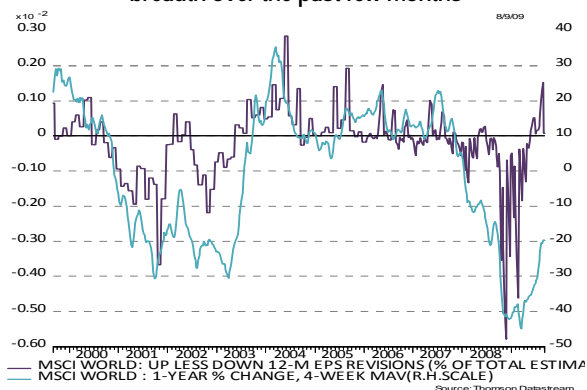
G10 countries – macroeconomic data much better than expected



Rising PMI indices imply further upside potential for equities



Earnings forecast revisions have shown much more breadth over the past few months



EQUITY MARKETS

Developed markets

Valuations now near neutral. After the very strong rally that began in March, valuations are no longer providing massive support to equity prices. Although both trailing and 12-month forward P/E ratios are still a bit below their averages, cyclically-adjusted ratios, such as those of Robert Shiller or Graham & Dodd, show that valuations are in line with their long-term trend.

Although valuations at this level are neutral or modestly favourable to equity markets, we see little chance of a substantial expansion of multiples in the current environment where risk aversion is still high and concerns about near-term deflation and high long-term inflation persist.

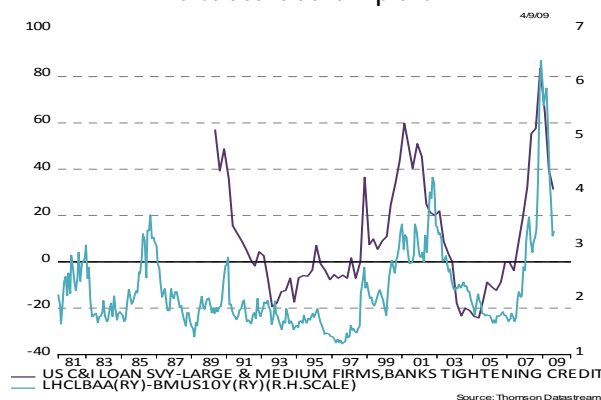
The credit crisis continues to subside, thanks to government support measures and the decisive actions of central bankers. Near-term interest rates, credit spreads and interbank market rates have thus all returned to their pre-Lehman bankruptcy levels. These low rates and sharply-sloped yield curves will be highly supportive to bank profit margins and earnings. This has helped to ease lending conditions (although the demand for credit is still weak) and support the economy.

Despite this improvement riskier bank assets are still threatened by high default rates on consumer and mortgage loans (as unemployment rises) and the ongoing deterioration of the commercial property sector. Banks are therefore very likely to make additional provisions on these riskier loans, particularly since their loan loss reserve ratios are still low, despite the provisions they have already made, and there will be very strong political and regulatory pressure to get banks to increase their capital adequacy ratios. This sword of Damocles over the heads of bankers also threatens the supply of credit to the private sector. Although central banks continue to be extremely accommodative, when and how they implement their strategies to exit from their "crisis" monetary policies will be a critical factor that could frighten investors. Over the coming months we will therefore be closely monitoring two-year interest rates, which are highly dependent on benchmark rate expectations.

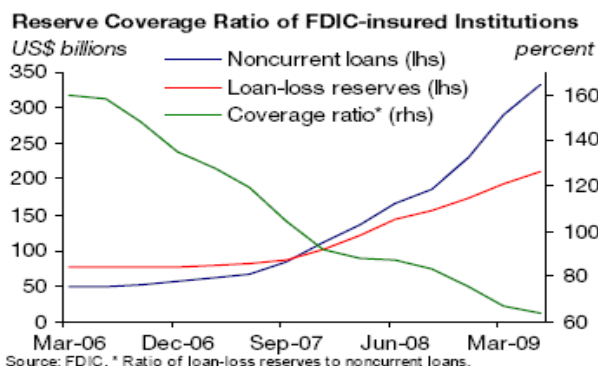
12-month forward P/E ratio is slightly below neutral



Credit conditions improve



United States – growth of loans at risk continue to outpace provisions



EQUITY MARKETS

Developed markets

Technical factors. The recent plunge in risk aversion, which resulted in an almost euphoric situation, and the fact that September has traditionally been a challenging month for stock markets, could put a damper on share prices over the coming weeks.

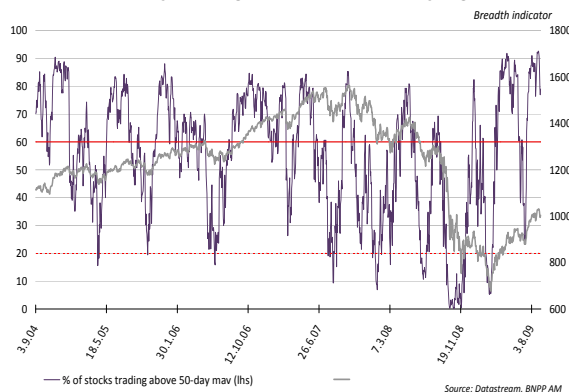
The very limited exposure of life-insurance companies, pension funds and other institutional investors to equity markets will continue to be a very strong supporting factor if share prices start to stumble. A massive structural increase in equity holdings by these institutions cannot be expected for the time being however, with risk aversion still as high as it is in historical terms. The ratio of cash holdings to aggregate equity market capitalisation is also at a very high historical level, despite its recent decline. Since many investors missed the last rally they still have abundant cash "reserves" to purchase equities, particularly if prices dip, and yields on cash and government bonds are still low.

Long-term trend indicators are sending a clearly bullish signal. The Coppock indicator for example, which is proven to be very effective in signalling the start of a long bull market, has been heading upward since the end of spring. As for the 200-day moving average, it has been climbing steadily since late July.

Conclusion

Economic and survey data and upward revisions of earnings forecasts, which are much stronger than expected, are likely to continue to be supportive of equity markets for a few more months. Beyond this period, the main threats to this asset class will be another sharp slump in the global economy (perhaps as fiscal stimulus fades) and expectations of tighter monetary policies.

The very high percentage of S&P 500 stocks above their 50-day average indicates overbuying



Cash holdings still very high relative to equity market capitalisation



Long-term trend indicators continue to improve



EQUITY MARKETS

Developed markets

Cyclical rebound should favour European and Japanese markets

We prefer Continental Europe and Japan

With the economy recovering, especially global trade, we prefer markets that offer high exposure to the exports cycle. We are therefore now overweight in Continental Europe, and particularly in the euro area, and have increased our overweight in Japan. These two regions, which traditionally compete in export markets, should not be significantly handicapped by the strength of their currencies, since the euro/yen exchange rate has been relatively stable for six months.

The **euro area** also offers **particularly attractive relative valuations** and a still positive relative performance trend. We expect these favourable factors to more than compensate for the region's earnings forecast revisions, which continue to lag those of the other developed economies. The **Japanese market** offers **very favourable earnings revisions momentum** and valuations that are still relatively attractive.

Now neutral in Australia and still neutral in the United States

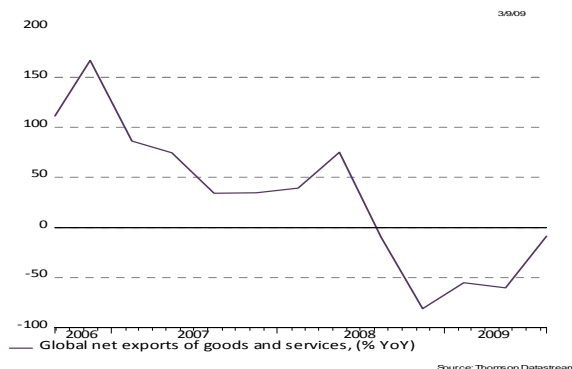
The general decline in risk aversion gives the **US market** a relative disadvantage. However, valuations relative to other developed markets are now back to neutral, after being quite high, and the earnings revisions momentum seems to have stopped deteriorating in comparison. The **Australian market** is feeling the pinch of the consolidation of commodity prices and is handicapped with much less attractive valuations and earnings forecasts than its developed market peers. Furthermore, the RBA could raise its interest rates well before the other major central banks. Nonetheless, this market's exposure to Asian recovery and strong relative price trend still justifies a neutral position for the time being.

Caution in Canada, and in the UK to a lesser extent

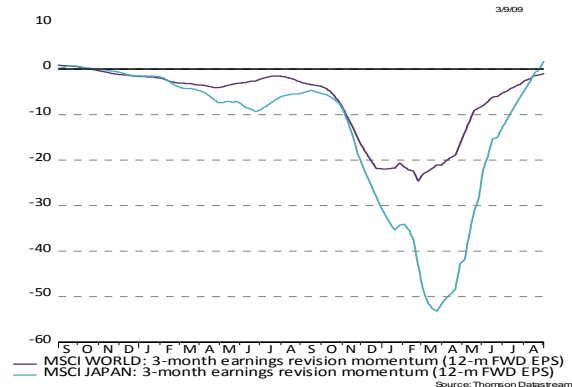
The **Canadian market**, which is currently a bit expensive, also faces the problem of cooler commodity prices, in addition to the strength of the CAD relative to the US dollar. Earnings growth forecasts are therefore clearly not as favourable as those of the other developed equity markets.

The relative price trend is also unfavourable for the time being. Lastly, the **UK market**, which offers neutral relative valuations, must also face the **consolidation of prices in commodity markets, to which it is highly exposed**. This has naturally weighed on this market's forecast earnings growth. The UK's lack of cyclical exposure is also a disadvantage now that the global economy is recovering.

Global trade recovers



Japan's strong earnings revisions momentum



Canada's relatively high valuations



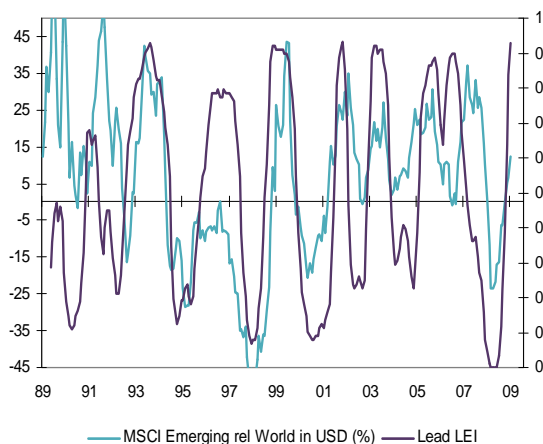
EQUITY MARKETS

Emerging markets

Expect a pause in emerging-market outperformance

The trend is still bullish for emerging markets, for which the economic outlook is positive in both structural and cyclical terms. Valuations are back up to their historical trend but have yet to weigh on the market. **After rising 85 % since the trough of March 2009, we expect gains to slow over the near term.** Now that the economic situation in the industrialised countries is less uncertain and their risk premium has dropped, investors will be more inclined to invest in developed equity markets, which will temporarily reduce the relative appeal of emerging equities.

Our model of OECD leading indicators (see chart below) has returned to an extreme level that also points to a pause in the outperformance of emerging markets.

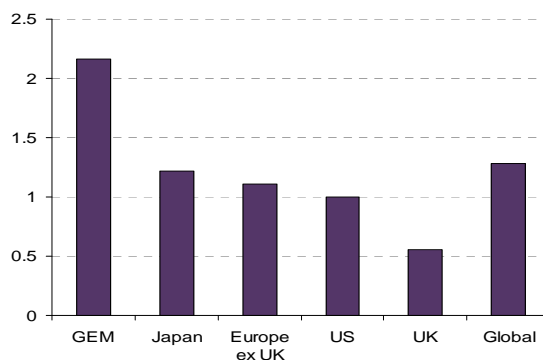


The trend in emerging short-term interest rates relative to the benchmark rates of the developed economies has also become unfavourable.

Indicators of risk appetite and investor sentiment have reached excessive levels far beyond those seen in developed markets.

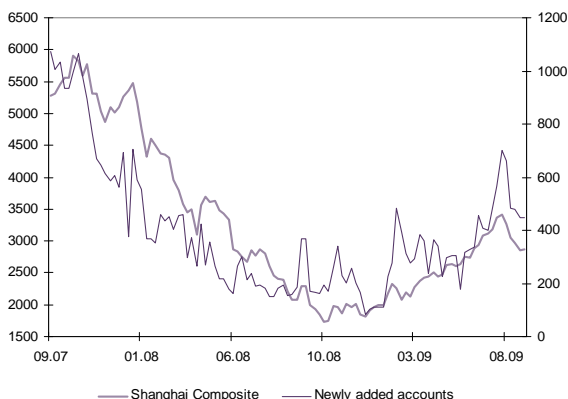
Furthermore, with earnings revisions ratios now at record levels, emerging markets are vulnerable to the slightest disappointment. Lastly, the Chinese have probably stopped rebuilding their stocks of raw materials and this will dampen commodity prices and weigh on equity markets exposed to commodities, such as those of Brazil and Russia.

Risk appetite – emerging markets still too popular and overbought (Crédit Suisse index)



The speculative bubble in domestic Chinese A-shares has finally deflated. The violence of this correction was amplified by the large number of small speculators in the Shanghai and Shenzhen exchanges (accounting for over 70 % of trading volume), whereas Hong Kong-listed shares have held up well. This implies that **the volatility of domestic shares is mainly due to the liquidation of speculative positions** rather than to any real deterioration of underlying business fundamentals.

Euphoria in China – the bubble has deflated (a bit)



But this does not necessarily mean a return to the basic trend and the impressive gains seen in the first half of the year. Monetary policy is now in a transitional phase and efforts will be made to remove the excess liquidity that enabled the rally in the first half. In the absence of a large infusion of liquidity by monetary authorities Chinese equity investors will have to pay more attention to business fundamentals and earnings growth.

EQUITY MARKETS

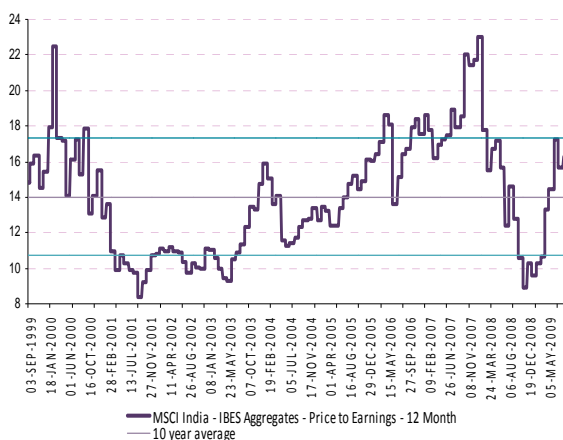
Emerging markets

Under these conditions, security analysts are expecting EPS growth of "only" 20 % in 2010, underpinned by stronger profit margins, the leverage enabled by low interest rates and the yuan's depreciation. **We are therefore reducing our overweight in China.**

We are increasing our exposure to Korea in light of its strong growth prospects and the confidence shown by the country's firms and consumers. The trend in upward earnings revisions is still quite strong, although they have largely been priced in. The won's potential for appreciation offers additional appeal.

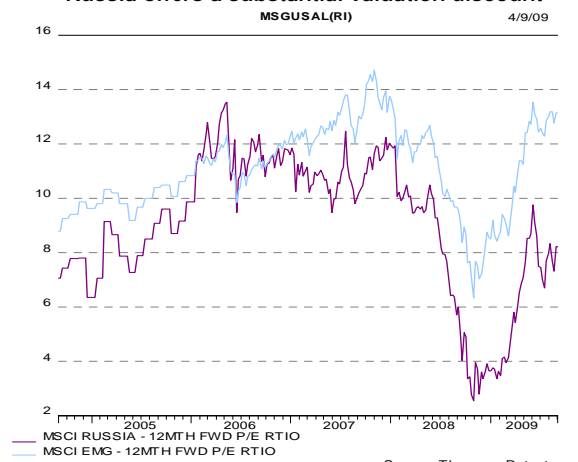
After trading between 15,000 and 16,000 points since mid-July, India's **Sensex** index finally broke through major resistance in early September and reached its highest level in 15 months. It is now heading towards 18,000. This optimism is justified by a stream of good economic news and even brighter prospects for domestic demand and corporate earnings. Foreign fund flows also continue to support the market and we expect this trend to continue given the potential of India's economy and the fact that most fund managers are still underweight in Indian equities. However, there are downside risks. Along with share prices, valuation multiples have also doubled since March and greatly increased the likelihood of a near-term correction. The monsoon season has also had a significant impact on Indian equity markets. Lastly, India's central bank will probably be one of the first to reverse its accommodative monetary policy, which will not be good for equities. **In conclusion, we recommend a neutral position in the Indian market.**

India – valuations are under pressure



Russia's RTS index is up 80 % this year, making it one of the strongest performers in the emerging universe. The surge in Russian equities may mainly be attributed to the ruble's consolidation against the dollar and rising commodity prices. This market also offers additional upside potential in the form of low valuations, with Russian shares trading at a discount of 40 % relative to their emerging peers, based on projected 2010 earnings. It should be noted that this discount is at least three times higher than any observed over the past eight years. Nonetheless, considering how far Russia's economy lags behind those of the other developing countries, **we prefer to adopt a cautious stance and a neutral position in this market.**

Russia offers a substantial valuation discount



Source: Thomson Datastream

Brazil's economy has stood up relatively well to the global economic slump. Historically low interest rates and the recovery of commodity prices have played a large part in the 54 % gain Brazilian equities have posted since the beginning of the year. However, it is now clear that Brazil's central bank will not pursue its monetary easing and the country's firms could also be adversely affected over the near term by the government's reforms in the oil industry. **We therefore are maintaining our neutral position in the Bovespa.**

ALTERNATIVE STRATEGIES

Commodities

We will wait-and-see about commodities

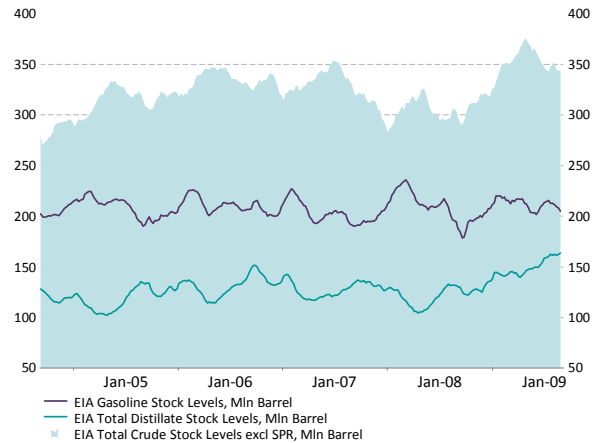
While better than expected economic news fuelled a spectacular rebound in equity markets this summer, **crude oil prices** were relatively constrained and could not overcome the \$75 resistance levels. This may be attributed to the slow pace of recovery in fundamentals. Indeed, crude oil and petroleum product stocks remain high and continue to reflect weak demand. The supply of oil has also been relatively responsive to price, with the OPEC members gradually increasing production from a low of 28.1 mb/day in February to 28.7mb/day this summer. Although we may assume that oil producers will do everything possible to prevent the barrel price from plunging, there seems to be little upside potential for now. With the hurricane season off to a calm start and natural gas prices very low, we prefer to maintain a **neutral position** until we see a more favourable opportunity to enter this market, where prices could reach overshoot the \$75 level by the end of the year.

After moving more or less trendlessly for several months, **gold** rebounded sharply in early September, back up to \$1000 an ounce. Although this bullishness may not last for long, **the fundamentals for physical demand are likely to improve** during this period of the year and could provide a solid foundation for stronger gains over the coming months. **We remain overweight.**

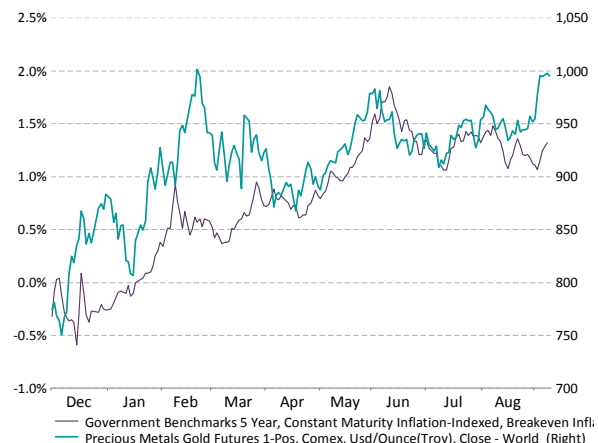
We are still wary about base metals. Although the demand for industrial metals should now be sustained by restocking in the manufacturing sector and infrastructure projects launched under economic stimulus programmes, **the decrease in Chinese metal imports could limit the near-term potential of base metals**, particularly when stock levels are already high. A prolonged correction in prices might provide an interesting buying opportunity, especially for metals like copper.

We are still **overweight** in **agricultural commodities**. Domestic factors in the US market severely depressed grain prices over the summer. Although planting dates were initially delayed, good weather conditions diminished investor confidence. Yet, this delay has increased the risk of frost damage since weather conditions are likely to deteriorate in October. With a weak dollar supporting exports and ethanol production boosting demand even more than expected, there seems to be good upside potential at current prices.

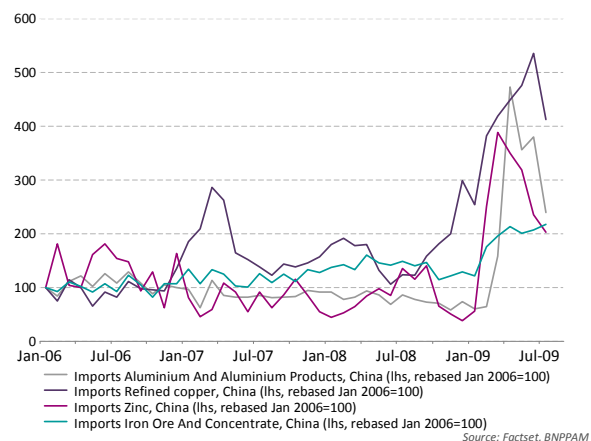
Oil – stock levels still high



Gold – price returns to test \$1000



Base metals – Chinese imports decline



Source: Factset, BNPPAM



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