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Strategy
Asia

Pan-Asia Road Ahead: 2H14 Outlook

From Rates to Growth; The Passing of the Baton

- Among EM, Asia is the most sensitive to a pick-up in the top-line as it is has the highest asset turn. In DM, Japan also enjoys high asset turns. Asia offers plenty of value with EPS revisions comparable to those in DM. Japan, too, is seeing improving EPS revisions, combined with cheap valuations. Within a Pan-Asian portfolio, we see the most attractive markets as Taiwan and Japan, the least attractive as the Philippines, Indonesia and Thailand. Our 12m MXASJ target is 680 (+17-18%).

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See Appendix A-1 for Analyst Certification, Important Disclosures and non-US research analyst disclosures.

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Pan-Asia Equity Strategy

From Rates to Growth; The Passing of the Baton

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- **Stronger global growth in 2H14 will support Asia** — Among EM, Asia is the most sensitive to a pick-up in the top-line as it is has the highest asset turn. In DM, Japan also enjoys high asset turns. Asia offers plenty of value with EPS revisions comparable to those in DM. Japan, too, is seeing improving EPS revisions, combined with cheap valuations. Within a Pan-Asian portfolio, we see the most attractive markets as Taiwan and Japan, the least attractive as Philippines, Indonesia and Thailand. Our 12m MXASJ target is 680 (+17-18%).

- **Banks, tech and industrials are most attractive, consumer defensives least** — Our house view is that UST yields will rise to 3.2% by year-end, the driver being stronger US and hence global growth. Banks would gain from a steeper yield curve and reduced credit risk as growth accelerates. Banks are one of only two sectors enjoying more positive than negative revisions to consensus earnings. Technology is the other; within tech, hardware looks a little more attractive than semicon. Industrials will benefit from stronger growth.

- **Asia has positive valuations, good relative revisions and money growth** — P/E for Asia is close to 1SD below the mean and P/BV 0.6SD below. China and Korea are the cheapest markets, the Philippines and India the most expensive. EPS revisions are better in the cyclical markets than in ASEAN. Asian revisions hold their own compared to other EMs, but are a small underperformer vs. DM. Assets on central-bank balance sheets are growing at 6% in Asia: growth is strongest in India and Taiwan, most anemic in the Philippines and Thailand.

- **OW China for 1st time in years, Thailand cut to UW and Korea to neutral** — Hong Kong loses out to China. China scores better than HK in terms of value and momentum (EPS revisions and price). Thailand is now an underweight, having been slowly trimmed from overweight. As for Korea, we are not more bearish, just more excited about the opportunities in China.

Pan-Asia Equity Strategy: Top Buys and Top Sells (Top Asia-Pacific Buys are a sub-set of our Focus List)

Top Buys					Top Sells				
Name	RIC	Rating	Price	Tgt Price	Name	RIC	Rating	Price	Tgt Price
Advanced Info	ADVANC.BK	1	Bt226	Bt270	Bank Danamon	BDMN.JK	3	Rp4,325	Rp3,225
Hon Hai Precision	2317.TW	1	NT$93.40	NT$112.00	Bharat Heavy	BHEL.BO	3	Rs255	Rs220
Hyundai Motor	005380.KS	1	W224,000	W320,000	China Coal Energy	1898.HK	3	HK$4.26	HK$3.10
Keppel	KPLM.SI	1	S$10.74	S$13.35	CITIC Pacific	0267.HK	3	HK$13.36	HK$6.00
MPEL	MPEL	1	US$32.35	US$55.00	China COSCO	1919.HK	3	HK$3.16	HK$3.04
MUFG	8306.T	1	¥617	¥800	Genting	GENT.KL	3	RM10.20	RM9.00
Largan Precision	3008.TW	1	NT$2,060	NT$2,200	Hyundai Heavy	009540.KS	3	W184,000	W155,000
Ping An Insurance	2318.HK	1	HK$61.40	HK$86.00	NCsoft	036570.KS	3	W180,500	W150,000
Rio Tinto	RIO.AX	1	A$58.72	A$71.00	PetroChina	0857.HK	3	HK$9.45	HK$7.50
Tata Motors	TAMO.BO	1	Rs451	Rs486	Toyota Boshoku	3116.T	3	¥1,087	¥860

Source: Citi Research

From Rates to Growth; Passing of the Baton

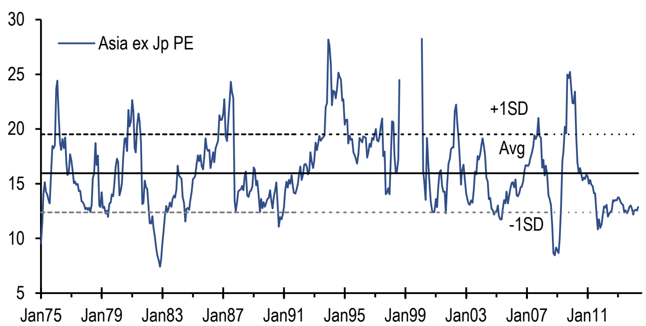
Asia-ex is up 5.1% ytd. A tad behind our original expectations for the mid-year but given where sentiment was in January the current return is probably better than most had expected. Chinese growth hasn't fallen off a cliff, so that is clearly better than expected. Taiwan, for a long time a favourite underweight, has also performed better than expected.

Valuations still at bottom end of range

Valuations remain well below historic averages for Asia. Slightly cheaper on P/E than P/BV.

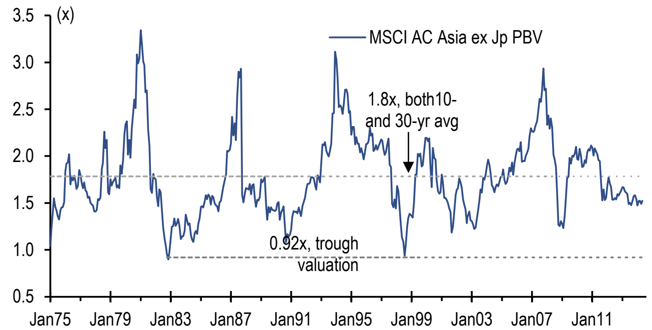
It does not matter whether investors prefer to focus on P/E or P/BV, valuations are very much at the bottom of their historic ranges. Figure 1 highlights the trailing P/E, and Asia is very much stuck at close to minus 1 SD below the mean. Since the late 1980s, this is now the longest period in which valuations in Asia have been stuck at this level.

Figure 1. Asia ex-JP Trailing PE



Source: MSCI, Citi Research

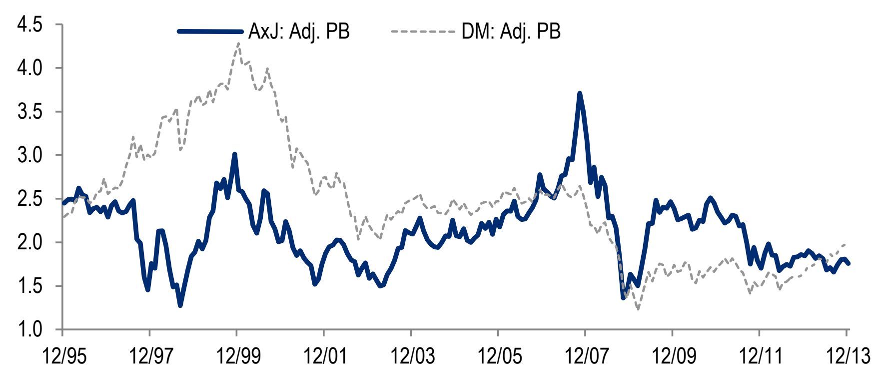
Figure 2. Asia ex-JP Trailing PB



Source: MSCI, Citi Research

In terms of P/BV, at 1.5x valuations are not quite as depressed as they are on an earnings basis but in the same way this has been the longest period for the region in which P/BV has effectively been stuck at these levels. An always interesting discussion is whether one sector or country (usually thought of as Chinese banks and China) are the root cause of valuations being cheap, but there are other countries too which contribute to this. So, for the sake of argument, we sector-adjust the valuations of Asia vs. developed markets to make them equally comparable. Even adjusting for differences in sector composition, Asia is cheap vs DM (see Figure 3).

Figure 3. Asia ex-JP's P/BV Compared to DM After Adjusting for Sector Compositions



Source: FactSet, Worldscope, Citi Research

Relative to developed markets, Asia is now trading at discounts of 28% on P/BV and 29% on P/E. So, the region has seen quite substantially de-rated over the last few years.

China and Korea are the cheapest markets, the Philippines and India the most expensive.

Within Asia there is a wide divergence. The cheapest markets on 2014E P/E are China at 9-10x and Korea at 10-11x. At the other end of the range are the Philippines on 22-23x and India on 19-20x. Markets trading above their historic P/E averages are India, Indonesia and the Philippines, with all the others at valuation discounts. Looking at P/BV, the distribution changes slightly as Malaysia joins the group trading at above-mean valuations.

Figure 4. P/E and P/BV of Asia Markets Compared to Historical Averages

	P/E			P/BV		
6/6/2014	Current	Avg	s.d.	Current	Avg	s.d.
AxJ	**13.0**	**15.9**	**3.7**	**1.54**	**1.80**	**0.34**
CN	9.6	14.7	4.5	1.42	1.89	0.77
HK	15.6	16.8	4.7	1.33	1.56	0.34
IN	19.4	16.9	4.1	3.16	3.05	0.91
ID	16.6	14.9	6.0	3.54	2.95	1.10
KR	10.7	12.7	3.9	1.09	1.29	0.33
MY	17.0	18.1	4.1	2.18	1.98	0.44
PH	22.5	18.0	4.0	3.08	2.14	0.77
SG	13.8	16.0	3.9	1.43	1.68	0.33
TW	18.1	22.6	10.2	1.94	2.10	0.53
TH	14.4	13.0	5.2	2.12	1.97	0.47

Source: MSCI, Citi Research

Sector-wise, valuations in 0.9-4.7x range for P/BV, 10-28x for P/E

Based on P/E, banks and real estate are cheapest, with healthcare and consumer staples the most expensive.

Within sectors, the spread of valuations is relatively large. In terms of P/BV, real estate trades at a discount (0.9x) whilst healthcare is commanding a lofty 4.7x. Healthcare is also the only sector trading above the post-1995 P/BV mean. Consumer staples continues to de-rate and is now at its post-1995 mean, having for many years traded well above it. Consumer cyclicals are also at mean P/BV but arrived there via a very different route to consumer staples, by re-rating.

Relative to the respective historical P/BV means, the cheapest sector is still telecoms at a 38% discount, followed by energy (1.4x, a 37% discount) and then tech (30% discount) and insurance (28%).

Translating this analysis to P/E, banks are cheapest at 10.6x (33% discount to post-1995 average), followed by real estate (11.8x, -32%), consumer discretionary (12.5x, -31%). The only other sector currently at sub-13x is technology (12.6x, and -50%). Technology is also the sector with the biggest discount vs its own history.

Figure 5. P/BV of APxJ Sectors Compared to Historical Averages

APxJ by Sector	P/BV (x) 6/6/2014	Since 1995 Avg	Low	Hi
Cons. Disc.	1.93	1.9	1.1	2.6
Cons. Staples	2.84	2.8	2.1	4.4
Energy	1.40	2.2	1.0	4.7
Health Care	4.67	3.5	1.7	5.9
Industrials	1.42	1.6	0.8	3.0
Info Tech	2.14	3.0	1.3	8.7
Materials	1.56	2.0	1.1	3.7
Telecom	2.16	3.4	1.8	7.1
Utilities	1.62	1.6	0.9	3.1
Financials	1.37	1.6	0.8	2.6
Banks	*1.50*	*1.9*	*1.1*	*2.8*
Diversified Financials	*1.75*	*1.8*	*0.7*	*4.3*
Insurance	*1.79*	*2.5*	*1.2*	*4.6*
Real Estate	*0.90*	*1.1*	*0.5*	*1.9*

Source: MSCI, Citi Research

Figure 6. P/E of APxJ Sectors Compared to Historical Average

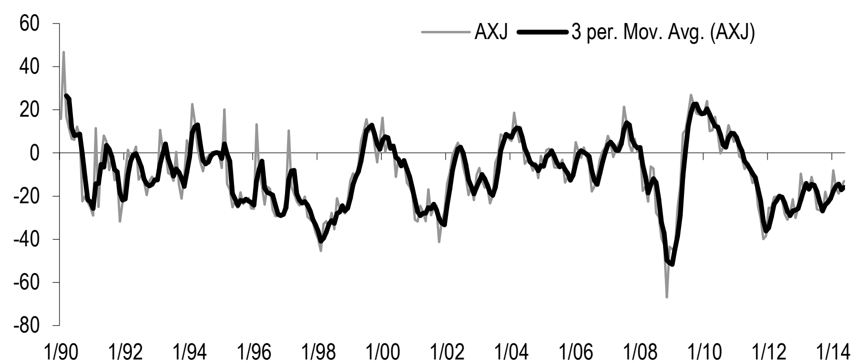
APxJ by Sector	P/E (x) 6/6/2014	Since 1995 Avg	Low	Hi
Cons. Disc.	12.5	18.2	8.9	69.0
Cons. Staples	23.6	21.0	14.4	29.8
Energy	12.7	14.1	5.7	26.9
Health Care	27.6	32.4	18.6	145.2
Industrials	21.4	20.2	-81.8	146.5
Info Tech	12.6	25.0	7.6	141.1
Materials	15.4	23.2	6.2	1292.7
Telecom	15.4	17.8	10.6	47.0
Utilities	18.5	17.2	9.7	35.8
Financials	11.9	18.8	-223.2	540.9
Banks	*10.6*	*15.9*	*-31.0*	*76.2*
Diversified Financials	*20.6*	*19.5*	*3.9*	*74.3*
Insurance	*18.1*	*12.1*	*-1427.4*	*148.2*
Real Estate	*11.8*	*17.2*	*5.5*	*38.9*

Source: MSCI, Citi Research

The most expensive sector is healthcare on 27.6x, though this is still at a discount to its own average of 32x. Consumer staples are on 23.6x, a 12% premium to the historic average. Next we have industrials on 21x, a 6% premium. Finally, the utilities are on 18.5x, an 8% premium. No great mystery about industrials being at a premium, as they are a cyclical and their ROE is currently below mean. The other 3 sectors, though, are all defensive/staples so the ROE is far from cyclical.

Earnings revisions grinding higher but still more down than up

Figure 7. Earnings Revision Index (ERI) of Asia ex JP

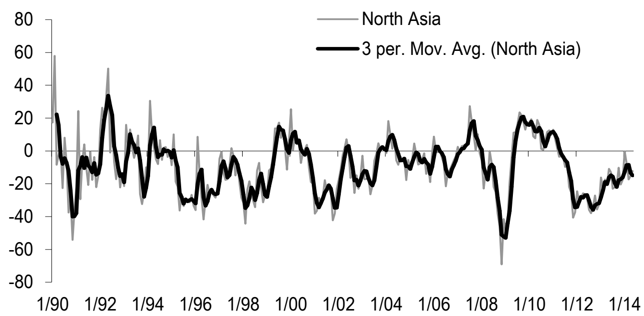


Source: IBES Aggregate, Citi Research

EPS revisions less bad than before but still more down than up – nothing new there.

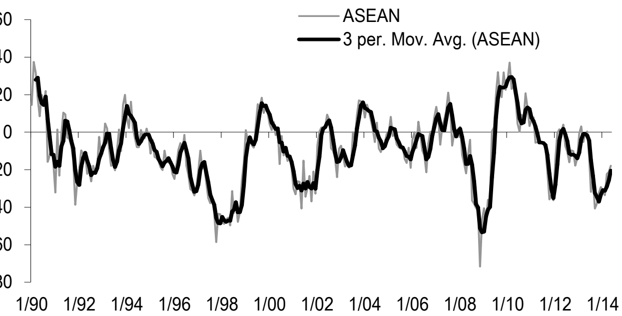
Downward revisions to earnings are still more plentiful than upward revisions in Asia-ex, see Figure 7. Over time that tends to be the case anyway, as also shown in Figure 7. Analysts, in effect, start off the year in optimistic mood and then cut earnings as the year progresses, most notably post H1 results. This also explains why historically in Asia-ex the weakest months for equity returns are always August and September. Given the history of starting high and working down, average EPS revisions (up-down/total) over time stand at -9.7, not at zero. With a current reading of -13.1, Asian revisions are not that far off where they usually are.

Figure 8. ERI of North Asia



Source: IBES Aggregate, Citi Research

Figure 9. ERI of ASEAN

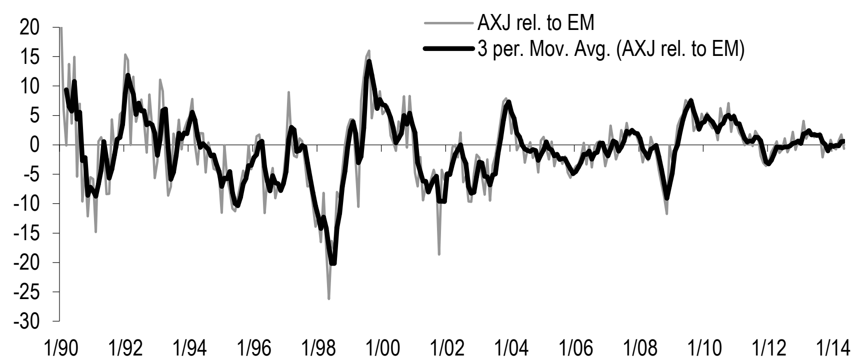


Source: IBES Aggregate, Citi Research

North Asian revisions, which are more cyclical, are doing better than those of South Asia.

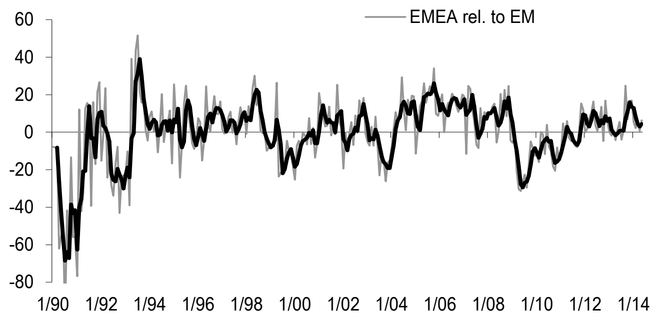
In terms of North Asia vs South Asia the latter is actually lagging driven predominately by the poor revisions in ASEAN whilst in North Asia the laggard is Korea. Even now at +25% earnings growth for 2014 the Korean earnings forecasts are the highest in Asia and second highest in GEMS after Chile. That earnings growth rate is still under downward pressure. So Korea has the worst EPS revisions in North Asia and it will stay that way until the analysts see sense. Historically better EPS revisions lead to better stock price performance but that hasn't materialized yet in terms of North Asia vs South Asia. Asia vs the GEMS universe and the region is at present holding its own, see Figure 10. Among the 3 regions Lat AM is faring the worst and EMEA the best (see Figures 11 & 12).

Figure 10. ERI of Asia ex-JP Relative to EM



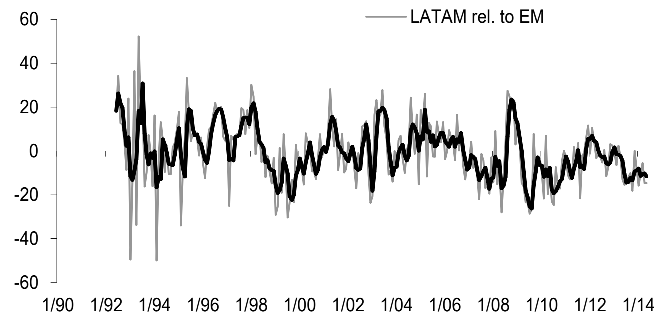
Source: IBES Aggregate, Citi Research

Figure 11. ERI of EMEA Relative to EM



Source: IBES Aggregate, Citi Research

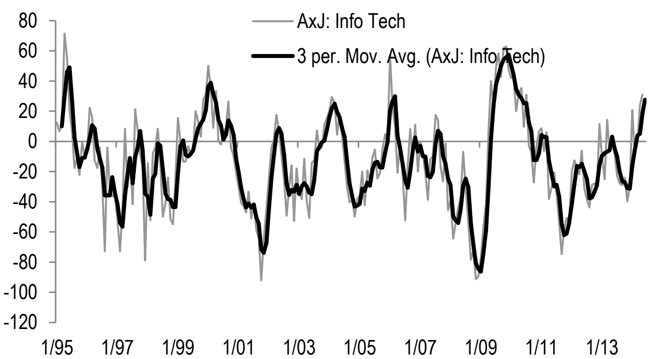
Figure 12. ERI of Latin America Relative to EM



Source: IBES Aggregate, Citi Research

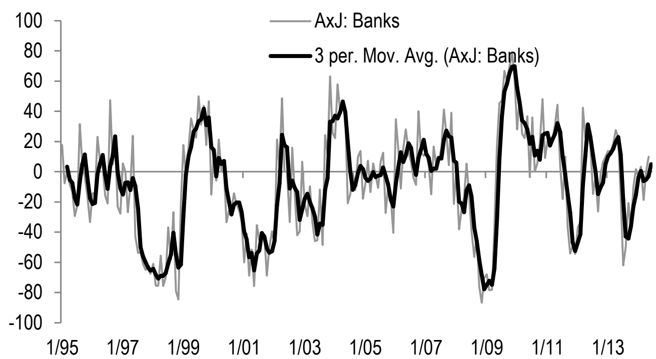
EPS revisions by sector, tech and banks the stand out

Figure 13. ERI of Tech in Asia



Source: IBES Aggregate, Citi Research

Figure 14. ERI of Banks in Asia

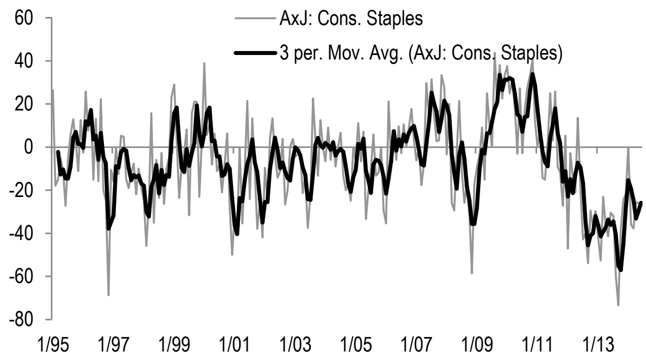


Source: IBES Aggregate, Citi Research

Banks and technology are the only two sectors with +ve EPS revisions. Materials and industrials are still weak, as are telecoms.

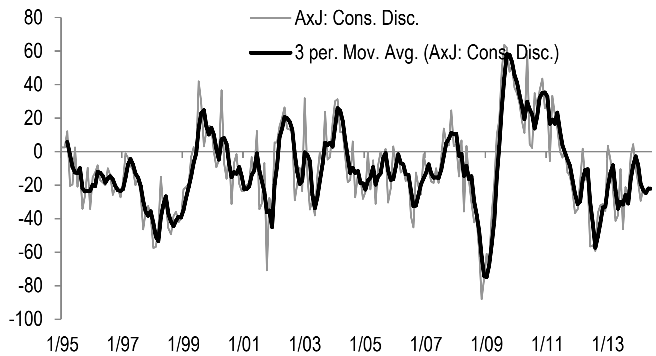
Across Asia-ex the best EPS revisions come from two sectors, technology is well in the lead (Figure 13) and then we have banks (Figure 14). Both currently have more upside revisions than downside revisions. These are the only two sectors which are in that fortunate position. The worst EPS revisions are to be found amongst real estate, telecoms, energy and insurance. Interestingly, consumer staples are still a favourite among investors yet the earnings revisions have been poor for a while and have recently rolled over again, see Figure 15. Interestingly compared to the consumer staples, consumer discretionary revisions have actually outperformed. Not only that but compared to the pre GFC peak, consumer discretionary earnings have outperformed consumer staples earnings by a factor of 3.

Figure 15. ERI of Consumer Staples in Asia



Source: IBES Aggregate, Citi Research

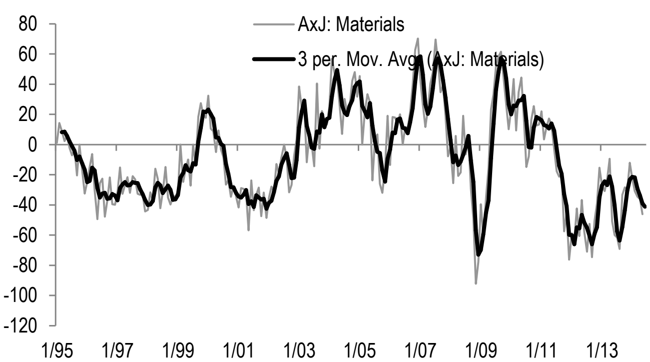
Figure 16. ERI of Consumer Discretionary in Asia



Source: IBES Aggregate, Citi Research

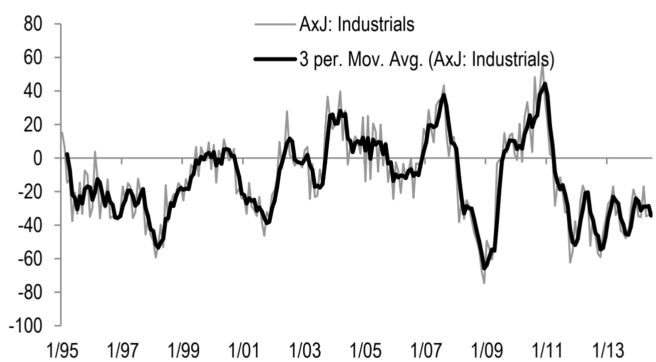
Amongst the weak EPS revisions sectors we still have the materials, see Figure 17 and industrials, see Figure 18. That effectively leaves us with two sectors which are enjoying upward revisions to earnings and the rest of the sectors are seeing downward EPS revisions. If the house view as far as a pick-up in global growth proves correct, the cyclical sectors will see the biggest benefit. At present that is, however, not what the earnings revisions are indicating.

Figure 17. ERI of Materials in Asia



Source: IBES Aggregate, Citi Research

Figure 18. ERI of Industrials in Asia



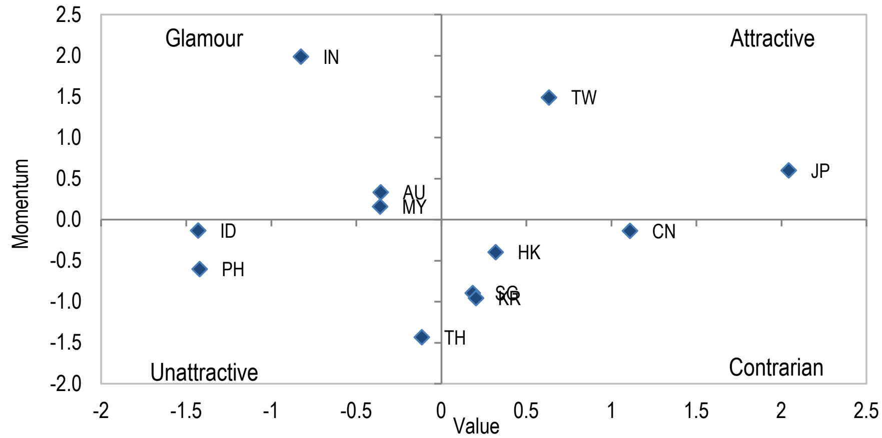
Source: IBES Aggregate, Citi Research

Country selection: Valuations & momentum by country

Value vs Momentum and the most attractive markets in Asia are Taiwan and Japan. Least attractive are the Philippines and Indonesia.

On the basis of our model which is a combination of looking for cheap markets (we use the simple average of P/E, P/CE, P/BV, P/S and DY) and improving EPS revisions as well as good price momentum all relative to the MSCI Asia Pac , see Figure 19. When we do this two markets within Asia Pac look attractively valued. The cheaper of the two is Japan –actually the cheapest market is Asia Pac and then we have Taiwan. The later isn't quite as cheap but it has better momentum –both price and EPS revisions than Japan. China is on the cusp of entering the attractive box. Valuations are already supportive and it is the cheapest market within Asia ex but it is still lacking just that little bit of EPS and price revision support. After China we have HK (note we are using MSCI data not the official stock markets). At the opposite end we have Indonesia, Thailand and the Philippines as unattractive markets with the latter being more expensive than the former two. Thailand is no longer more expensive, it just has rather poor EPS revisions.

Figure 19. Momentum and Value Rankings of Asia-Pacific Markets



Source: Citi Research

Amongst the contrarian markets we have HK, Singapore and Korea. China is there too and could go either way, move in to the attractive quadrant or fall off further in to the contrarian quadrant. It all depends on revisions and price performance. The market is already cheap. In the case of Korea as we have already mentioned the issue is just that we are going to have to live with further downgrades to earnings which will cap the stock market at least for the time being. In the case of Singapore, it is hard to convince investors of the virtues given the real estate exposure and timid export recovery.

The glamour market in Asia is India. China, HK, Singapore are contrarian bets.

In the glamour quadrant we have India. Great momentum-mostly price- as the EPS revisions continue to lag and valuations are a little on the rich side. Not by a lot but a little on the expensive side. Australia and Malaysia are a little bit more expensive than the average markets in Asia Pac but not by much and have slightly better momentum but again not a great deal more.

Sector selection: Valuations & momentum by country

Autos, banks, tech hardware, utils and industrials are all in the attractive quadrant.

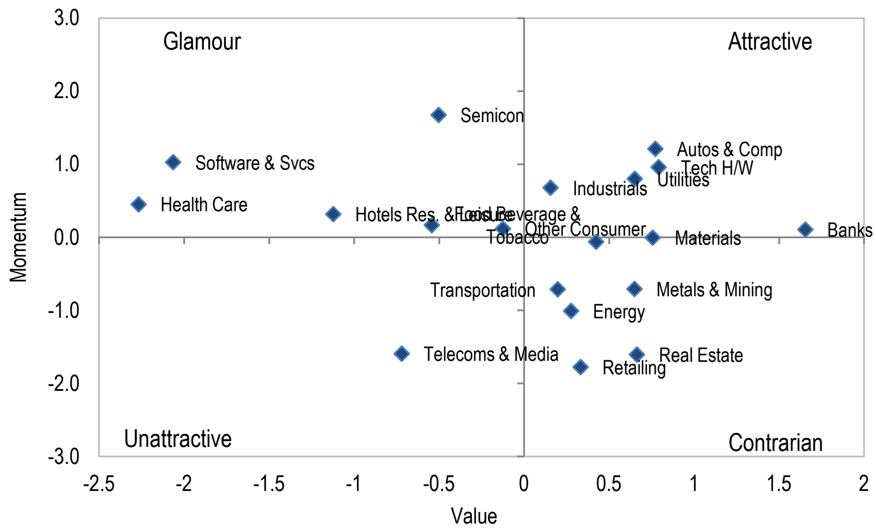
Combining valuations and momentum for sectors in the same way as we have for countries gives us the following picture, see Figure 20. Among the most attractive sectors we have auto and components, tech hardware, utilities and industrials. Interestingly, the banks have just moved in to the attractive quadrant. Materials at present is on the cusp. Yes, the sector is cheap but at present there isn't much sign of better momentum than is available in the rest of the market.

At the opposite end in the unattractive quadrant there is only 1 sector, telecoms. Relative to all others, the valuations are a little unattractive and, as we highlighted above, the earnings revisions remain quite poor.

Semicon and software are now in the glamour section. Getting a little expensive but with great momo.

Amongst the glamour sectors we have semicon, slightly expensive but with very good momentum, software and services, more expensive still than the semiconductor space but with lower momentum. The same too applies for healthcare. The other defensives which are screening as being glamorous are hotel and leisure, food and beverage and tobacco.

Figure 20. Momentum and Value Rankings of Asia ex-JP Sectors



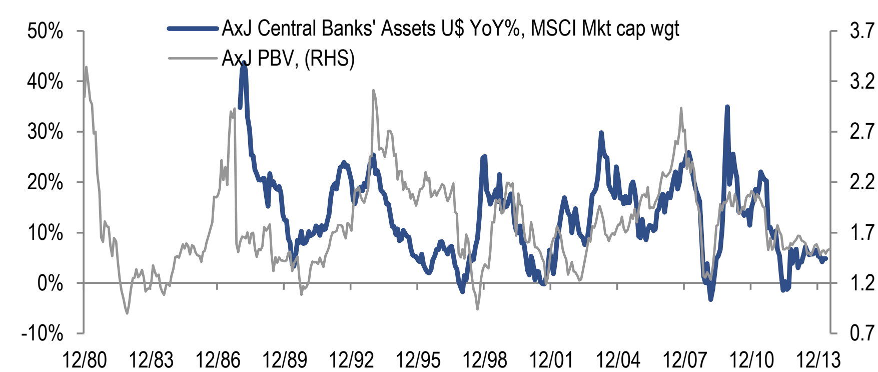
Source: Citi Research

In the contrarian corner we have retailing, real estate, energy, transport and mining. Among those, transport is the least expensive with real estate being the most expensive.

The overall picture is that defensives generally don't look particularly attractive, telecoms the least. This compares to cyclicals which generally screen better than most. Among the cyclicals, the auto sector and tech hardware are the most attractively valued, as are the industrials. Utilities have again benefitted from the rally in bond yields and so that makes them vulnerable to any change in yield expectations. The cheapest sector in the attractive quadrant is banks, and that by quite a long way.

Liquidity: Asia has more of it than the rest of GEMS

Figure 21. Central Bank Balance Sheet YoY Growth in Asia ex-JP

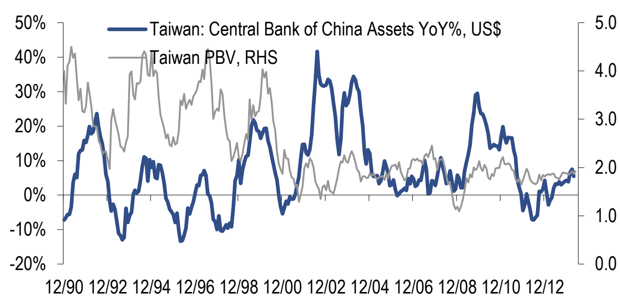


Source: Haver, MSCI, Citi Research

Asset side of Asian central banks is growing which is generally supportive of equities.

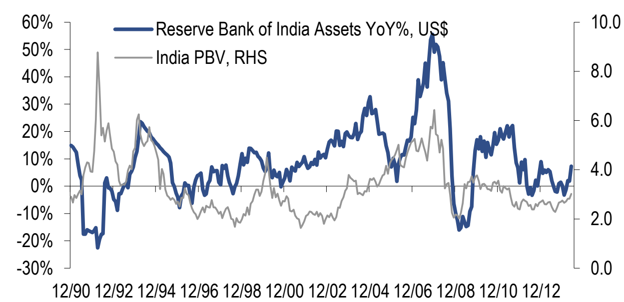
The way we look at liquidity is to see what is happening to the asset side of the balance sheet. The asset side encompasses what is occurring to the export side of the economy, what is happening to capital flows and then fx operations by the central bank. The way it works in Asia is better exports lead to rising exports, rising exports leads to better earnings and investors like to buy stocks with improving earnings and so Asia begets flows and flows lead to higher markets. Flows also mean upward pressure on the FX rate which in Asia central banks try to smooth and more often than not, this means rates are lower than they should be. Again helping equities. Figure 21 shows that in the case of Asia, where the asset side of the central bank balance sheet goes there goes the market (we've used P/BV as a proxy. Unlike the US, Japan or Europe where central banks create their own liquidity, QE, Asia does not. In Asia, economies get reliquified via the trade surplus in the absence of doing their own QE which is not something which we are forecasting.

Figure 22. Central Bank Balance Sheet YoY Growth in Taiwan



Source: Haver, MSCI, Citi Research

Figure 23. Central Bank Balance Sheet YoY Growth in India

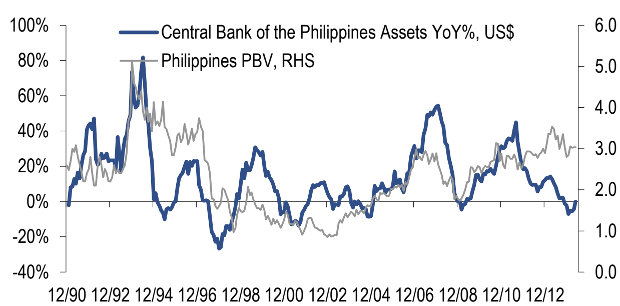


Source: Haver, MSCI, Citi Research

Taiwan and India are showing the strongest growth. The Philippines and Thailand the least.

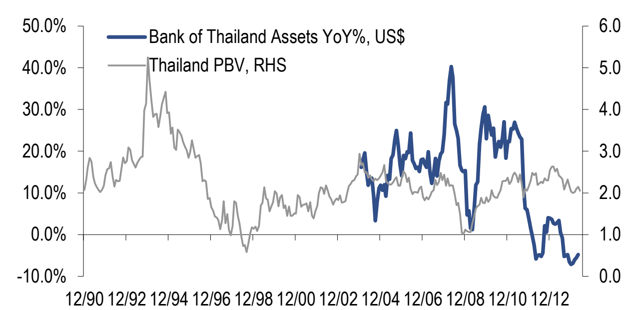
In Asia the strongest growth rate in the asset side is to be found in Taiwan, see Figure 22. In India too we have seen a pick up as of late helped by the strong capital flows. In the case of both Thailand and the Philippines the growth rate in the asset side of the CB's balance sheet has been quite anemic, see Figure 24 & 25. This makes the markets sensitive to swings in investor sentiment as there isn't a great deal of liquidity to support the current P/BV multiples.

Figure 24. Central Bank Balance Sheet YoY Growth in Philippines



Source: Haver, MSCI, Citi Research

Figure 25. Central Bank Balance Sheet YoY Growth in Thailand



Source: Haver, MSCI, Citi Research

The risk to the Asian liquidity environment is thus that there isn't much of a recovery in the 2nd half of 2014 in either the USA or Europe. As such trade surpluses either stay flat or shrink. The other risk is simply that we get a stronger US$ as the long end of the yield curve normalizes which then leads to capital outflows rather than

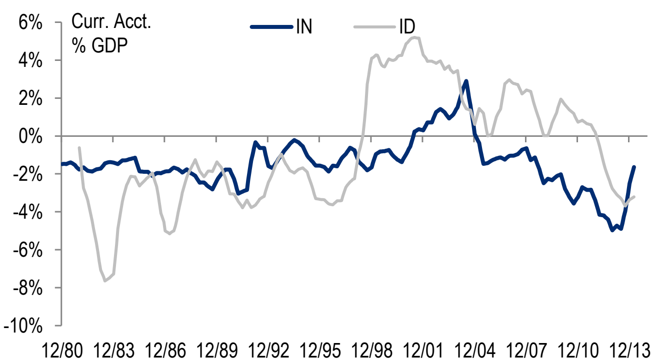
inflows. The focus then would be back on which countries in Asia run CA deficits and which of them run surpluses.

Higher bond yields are forecast for H2 2014

House view is for the long end in the US to hit 3.2%. This will put pressure on the CA deficit candidates again.

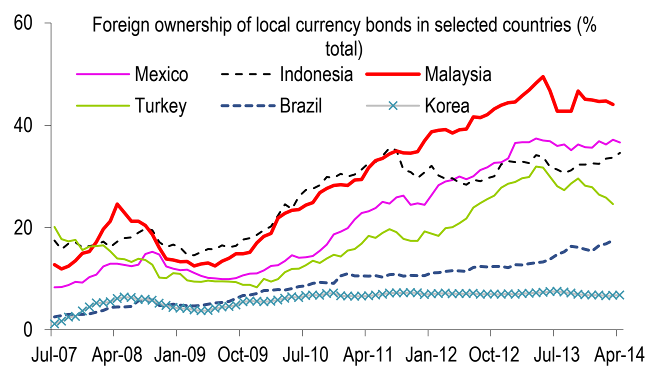
The first was the rally in the long end of the UST market. This effectively turned the underperformers of H2 2013 in to outperformers of H1 2014. Pressure on currencies and rates eased all of which allowed equities to rally. In the case of India we also had the election to focus on, something Indonesia is still subject to in H2 of this year. Our house view is that come year end, the UST will find itself at 3.2% rather than the current 2.55%. This is likely to become a headwind for those within Asia which still run CA deficits. Yes, India has shown substantial improvements and these improvements will help mitigate some of the pain from higher long rates which we expect in the 2md half. Indonesia too has shown improvements but to a lesser degree than India, see Figure 26, and so among the two remains the most vulnerable. In that regard the election outcome in July will be significant in deciding the direction for both the currency and the stock market. One area where Indonesia is also more vulnerable is the bond market. Though, foreign holdings of bonds are down from their 2011 peaks, these have started to rise again. After Malaysia, Indonesia has the 2nd highest weighting of foreigners in their own bond market.

Figure 26. Current Account to GDP in India and Indonesia



Source: CEIC, Citi Research

Figure 27. Foreign Ownership of Local Bonds



Source: CEIC, Datastream, Haver, Citi Research

Equity flow wise, India is the most vulnerable. Bond wise Malaysia and Indonesia.

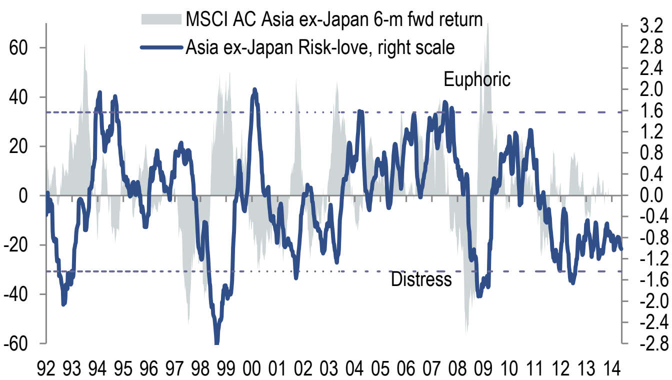
If, as we expect, the UST bill will sell off and rates will rise in H2 of 2014 it is therefore unrealistic to expect both the same returns and same markets to perform again in the 2nd half. The shift which would take place is one of interest rate sensitivity to growth sensitivity. With the prospects of stronger growth comes higher rates as well as the risk of a stronger US$. This is when those markets with a CA deficits start to look vulnerable and where those which have been reliant on the so called “reflation trade” also start to lose momentum. Where the reflation trade loses out, so the manufacturing trade begins to gain on US$ strength. Weakness of inputs (commodity products) is always a byproduct of a stronger US$ hence the industrials benefit from a more benign margin environment and also a pick-up in the topline. When it comes to topline, among the three regions of EM, Asia is best placed to capture the rising topline by virtue of having the highest asset turn. Within Asia, the top asset turn markets are Taiwan and Thailand at 103% followed by Korea at 88%. Those with the lowest asset turn are Hong Kong at 38%, Malaysia at 47% then Singapore and the Philippines at 51%.

Positioning and sentiment remain cautious

India is the big consensus overweight, Korea and Taiwan the big underweights.

Our sentiment indicator for Asia continues to point to sentiment being below average, see Figure 28 as such it is fair to say that investors are less than averagely enamored with the whole idea of equities in Asia. Retail participation remains low and by and large balances in the banking system continue to build see Figure 29.

Figure 28. Sentiment Indicator in Asia



Source: CEIC, Datastream, Citi Research

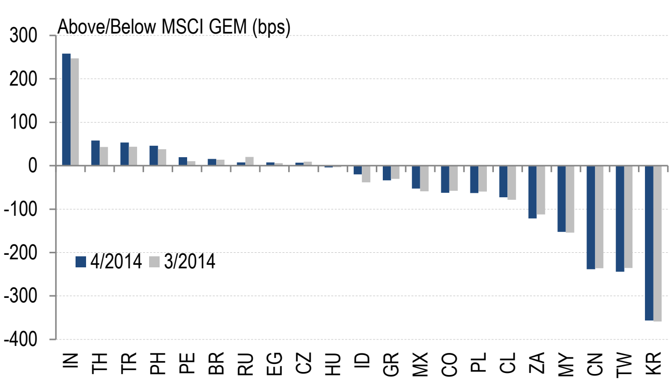
Figure 29. Deposits in Banks Are Abundant

		Deposits (US$bn)	% of Mkt cap	% of GDP	Deposits YoY%
CN	Mar-14	17,546	461%	189%	11%
HK	Mar-14	1,185	40%	433%	10%
IN	Mar-14	1,366	110%	73%	18%
ID	Mar-14	310	75%	36%	10%
KR	Mar-14	965	78%	74%	3%
MY	Mar-14	464	89%	149%	7%
PH	Mar-14	155	55%	57%	37%
SG	Mar-14	447	59%	151%	2%
TW	Mar-14	1,174	142%	240%	6%
TH	Mar-14	349	93%	91%	9%
Asia ex Jp		**23,961**	**193%**	**156%**	**10%**
AxJ ex CN		**6,414**	**74%**	**106%**	**5%**
AxJ ex CN,IN		**5,048**	**68%**	**120%**	**5%**

Source: CEIC, Haver, Citi Research

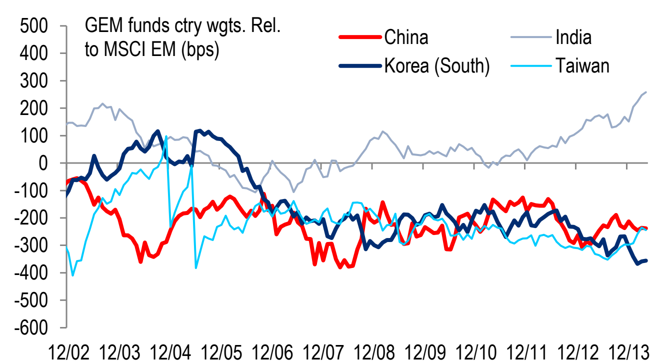
From the data we get, within a GEMS universe Asia is the least preferred region due to the sizable underweights investors have in Korea, Taiwan and also China so by virtue of these being underweight, it is no surprise that Asia is a consensus underweight (Figure 30). Within an Asian dedicated portfolio, investors have a slightly more optimistic outlook on China, see Figure 32. Malaysia is their biggest underweight followed by Taiwan and Korea (similar to the GEMS investors) then we have Singapore. The favourite market, by a long way – same as in GEMS – is India. From a GEMS perspective, the India overweight is the highest it has been since early 2002 see Figure 31. Then we have both the Philippines and Thailand as number 2 and 3 among the overweights.

Figure 30. Country Allocation in GEM Funds Relative to MSCI EM



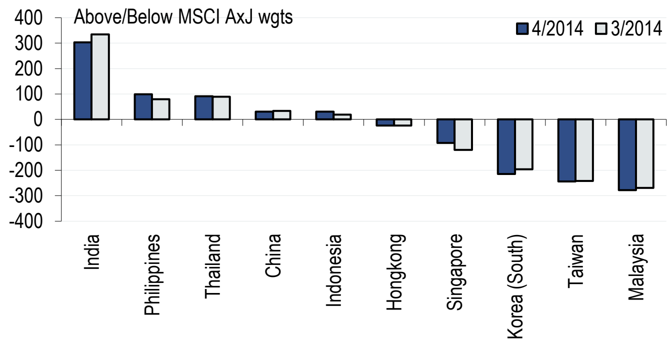
Source: EPFR, MSCI, Citi Research

Figure 31. India Has Become a Huge Overweight in EM Funds



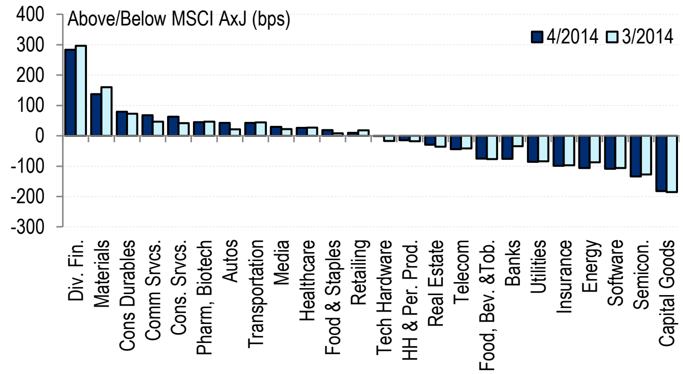
Source: EPFR, MSCI, Citi Research

Figure 32. Country Allocation in Asia Funds Relative to MSCI AxJ



Source: EPFR, MSCI, Citi Research

Figure 33. Industry Allocation in Asia Funds Relative to MSCI AxJ



Source: EPFR, MSCI, Citi Research

Few takers of cap goods, semicons, software and energy.

By sector, diversified financials are well liked followed by materials then a whole raft of defensives before we get to the autos. The least liked sectors are capital goods, semiconductors, software and energy. Insurance is the least liked of the financials followed by banks and then real estate.

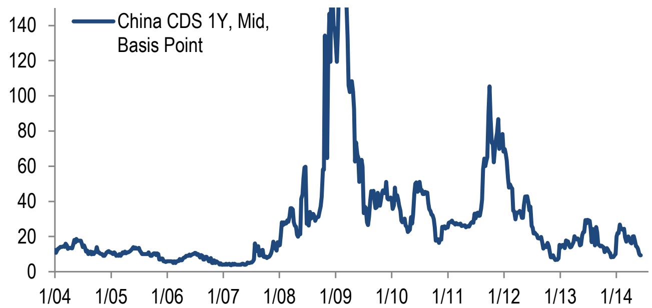
Key themes for H2 2014

1) We will see the usual EPS revisions post the release of the H1 numbers. The history in Asia is one of maximizing your EPS revisions in the post H1 period so be ready for revisions in July and August. Most vulnerable, Korea (25% EPS growth just won't happen). Least vulnerable is the Phils at 6%, China, HK and Sing at around 7%.

2) The house view is that on the back of robust US growth, the long end of the yield curve rises to 3.2% come year end. Expect some jitters amongst markets with CA deficits. Indonesia is the most vulnerable, Taiwan the least. Sector wise, real estate is the most vulnerable to higher rates whilst banks will benefit from higher lending spreads as will the cyclicals on the back of stronger growth.

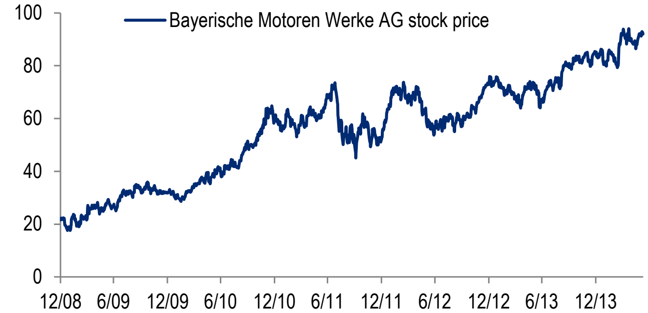
3) No China growth won't fall off a cliff, as such concerns regarding a China hard landing will subside as we go through the 2nd half. Interesting that equity investors in Asia/GEMS continue to be so bearish on the outlook for China when neither credit investors as per the China CDS, see Figure 34 or global investors, see Figure 35 with regards to BMW are hardly bearish on the outlook for China. Usually the bond investor is ahead of the equity investor and hard to see that global investors as proxied by BMW can get it so wrong vs the Asian or GEMS investor.

Figure 34. China CDS Yld Is Way Below GFC Levels



Source: FactSet, Citi Research

Figure 35. BMW's Stock Price Has Been Strong



Source: FactSet, Citi Research

4) Companies which are beginning to do "self-help", ie begin to reduce capex, working capital and begin to raise free cash flow or return cash to shareholders will do better than those waiting for the cycle to help them out.

Key risks:

1) Both a risk and opportunity. The house view comes true and the long end of the yield curve moves out to 3.2%. Bad for real estate-good for banks. Helpful for growth sentiment.

2) US$ rallies as the US economy accelerates. Commodity prices fall, CA deficit countries come under pressure. Good for manufacturing as input costs decline.

3) Unlike ours or the consensus forecast, US growth in H2 turns out disappointing. The US resorts to the next instalment of QE which then leaves the ECB, BOJ and US Fed all in pumping mode. Their own asset markets react more favorably than Asia.

4) In the same way that it applies to EM in aggregate, investors may just be too bearish on the outlook for Asian equities.

Figure 36. Asia: Country Views

Country	Recommended weighting	Why?	BULL	BEAR
China	Overweight	Lowest implied EPS growth to perpetuity, consensus underweight, low FX vulnerability, economy bottoming out.	Very low valuations, poor sentiment mean it does not take much to change expectations, subdued earnings expectations.	Credit sector seizes up as the real estate market collapses. NPL issues understated and will cause a hard landing.
Hong Kong	Underweight	House view of higher US long rates to 3.2% come year end put a ceiling on the real estate side of the market.	If China sentiment improves so will sentiment in HK. Higher long rates will help the HK banks. Market trading below average valuations.	Very interest rate sensitive market, real estate prices set to correct in 2014-2015.
India	Underweight	Much good news priced in to the market, only the Philippines is on a higher multiple. EPS still show more downward than upward revisions. Consensus most overweight since 2002.	Room for interest rate cuts in late 2014, CA deficit has shown big improvements. New government will revitalize the economy. Locals only just buying.	One of the biggest overweights in EM equities. Risk of policy exuberance. Higher UST in H2 could de-rail the market rally in both FX and the equity market.
Indonesia	Underweight	Local bond market still well held by foreigners. Political expectation high ahead of the July election. Valuations quite rich and liquidity not abundant.	Large populations, good demographics, domestic growth driven, not exports. CA will adjust and growth will resume.	Still among the fragile 5and more fragile than India. Valuations embed a lot of good news. Politics not a foregone conclusion.
Korea	Neutral	Pick-up in global growth set to benefit Korea, valuations vs self remain attractive. But EPS growth forecasts remain too high which will be a drag on performance	Few own it, many dislike it. No one can see a catalyst. Better global growth will help Korea.	Cyclical, always inexpensive, don't pay dividends, over-spend on capex with falling ROIC. Long term de-rating story.
Malaysia	Underweight	Defensive market, not particularly expensive but devoid of catalysts.	Defensive market, consensus underweight, large domestic pool of money.	Defensive market without clear winners from stronger global growth. high foreign ownership of local bonds.
Singapore	Overweight	Stronger global trade will filter in to better earnings and the banks are most sensitive to tighter money. Cheap.	Cheap market with an economy open to global trade. Cheapest market in ASEAN.	Pricing itself out of the market, consumer leveraged, sensitive to interest rates due to the property exposure.
Taiwan	Overweight	Good earnings revisions, esp in the technology space, increase in cross-Strait ties a +ve. Loan growth improving, valuations still supportive.	Large underweight by investors, very little fx vulnerability. Few foreign bond tourists. Exports improving. Strong EPS revisions.	Cyclical market, not expensive but neither inexpensive; who needs another tech gizmo?
Thailand	Underweight	Reasonable valuations but poor EPS revisions. Domestic side expensive but cyclical part of the market low priced.	Populist government, large foreign reserves, consumer spending stable, valuations still okay.	Consensus overweight, fiscal position stretched, as is the consumer.

Source: Citi Research

Country

Australia

Equity Market Is Consolidating After Its Recovery

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- **2014 is proving to be a year of more gradual advance** – After the ~30% rise over the 18 months from mid-2012, the height of the Euro and sovereign debt crisis, the Australian market, like other developed markets, is seeing more modest gains this year. A number of risks continue to affect the outlook, but on-going steady gains continue to seem the most likely course in coming months.

- **Valuations are back closer to "normal" and sentiment has improved** – Part of the challenge is that the recovery has lifted valuations substantially, and the market PE multiple is again around its medium-term average (Figure 1). Further re-rating that might underpin the market also seems less likely, for while investor sentiment has improved, it still looks to reflect a degree of caution (Figure 2).

- **Earnings have picked up but momentum may be slowing** – Stronger earnings growth could encourage more re-rating but, while earnings growth has picked up in FY14 (year to June), it is expected to moderate in FY15 (Figure 3). Steadier commodity prices until recently, a lower exchange rate, stronger household spending and improved financial markets have all helped in FY14, but the momentum doesn't seem as strong going into FY15 (Figure 4).

- **The economy is rebalancing but still faces some headwinds** – So far the economy has fared quite well as resource investment has begun to wind down, with housing activity rising strongly, consumer spending better, and investment in other industries showing signs of improvement (Figure 5). However, resource investment is set to fall further in the next few years and, in the near term, the tough Federal Budget looks likely to subdue spending for a while (Figure 6).

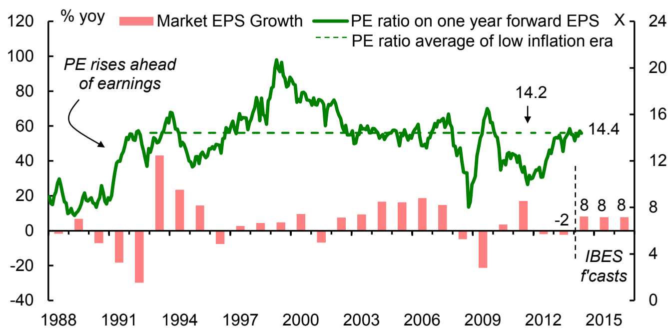
- **The equity market should still be able to generate decent returns** – Although the rebalancing of the economy will be on-going for a few years, and the pace may vary, there is the scope for more robust growth again for the broader economy as the resource investment boom passes. This should support earnings for a significant part of the equity market and, for the resource sector itself, rising output after the investment should help mitigate for moderating commodity prices

Australia: Top Buys

			Price	Target	Yield	ETR	2014E		
	Ticker	Rating	(Jun. 6)	Price	(%)	(%)	P/E (x)	P/BV (x)	ROE (%)
Top Buys									
Amcor	AMC.AX	Buy	A$10.64	A$11.43	3.9	12.8	17.8	4.1	21.3
Highly regarded management, defensive earnings profile, leading global market positions, potential for step change acquisitions and attractive yield									
Macquarie Group	MQG.AX	Buy	A$60.10	A$64.00	4.6	10.1	16.3	1.7	10.3
Good operating leverages to an upswing in capital markets, while growth options are not adequately captured in market expectations									
Rio Tinto	RIO.AX	Buy	A$59.40	A$71.00	3.7	24.2	10.0	1.9	22.4
Strong volume growth, relatively low capex intensity, strong cash flow yield, a defendable dividend and discount to NPV make RIO a compelling investment									
ResMed	RMD.AX	Buy	A$5.54	A$7.07	2.2	27.4	21.1	4.4	21.5
Growth is expected to be underpinned by new product launches, market share gains and greater adoption of home-sleep testing in the US									

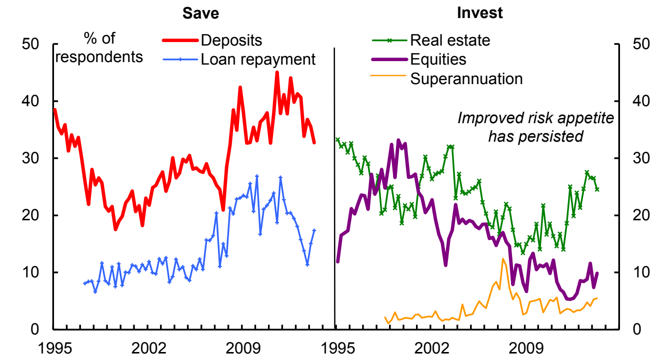
Source: Citi Research estimates

Figure 1. Market PE and Earnings Growth



Source: IBES, Datastream, Citi Research

Figure 2. Consumers' Preferred Use of Savings



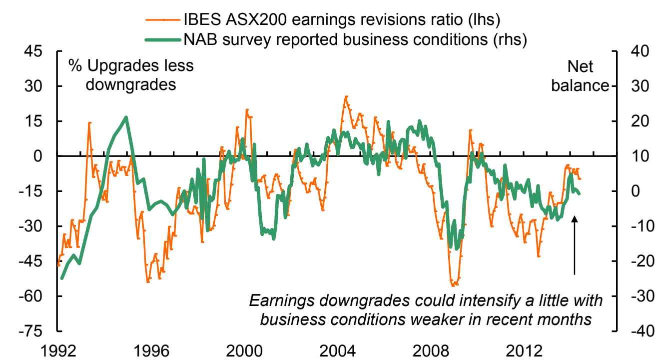
Source: Westpac/Melbourne Institute, Datastream, Citi Research

Figure 3. Underlying NPAT Growth (%)†

		Dec-12 Half	Jun-13 Half	Dec-13 Half	Jun-13 Year end	Jun-14F Year end	Jun-15F Year end
Market		-4.6	2.1	13.4	-1.4	12.4	5.9
Resources		-31.8	-11.4	35.0	-23.2	31.4	-0.2
Banks		8.9	11.8	9.8	10.3	8.2	4.6
Other Financials		18.9	1.1	5.2	9.1	7.7	11.4
Other: (Industrials ex Fins)		0.6	2.9	5.3	1.7	5.4	10.6
Of which:	Onshore*	4.9	4.4	1.5	4.7	2.2	10.4
	Offshore*	-8.4	-6.1	15.3	-7.1	15.1	10.8

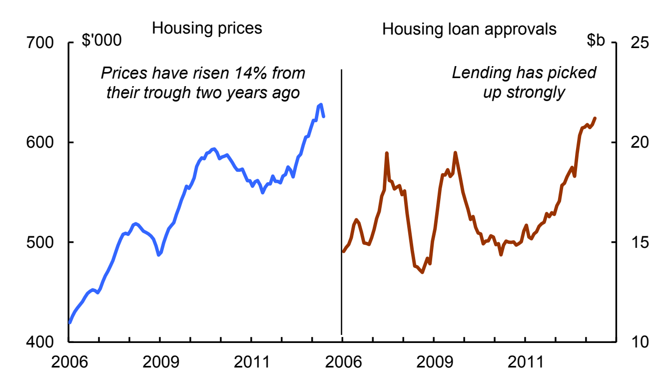
†Growth is over the pcp. *Offshore industrials are those with more than 50% earnings from overseas. Onshore are those with 50% or more of earnings from Australia.
Source: Company data, Citi Research

Figure 4. Business Conditions and Consensus Earnings revisions



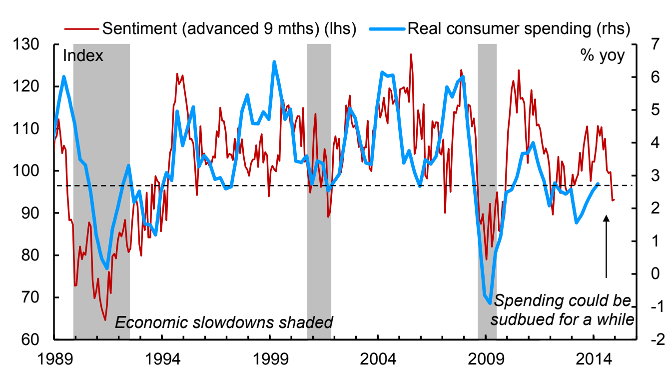
Source: NAB, IBES, Datastream, Citi Research

Figure 5. Housing Activity



Source: RP Data, ABS, Citi Research

Figure 6. Consumer Sentiment and Spending



Source: ABS, Westpac/Melbourne Institute, Datastream, Citi Research

China

Risk/Reward Looks Positive

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- **Slow growth recovery, fast-paced reform** – The restart of China's reform process at the same time as a turning property cycle may challenge the government's strategy of an orderly transition. The authorities have so far avoided stimulating the economy in an old-fashioned way, and this may open room for proactive reforms of SOEs, *hukou* and fiscal policy in 2H. We expect a positive risk/reward in the near term but cut our annual index target for MSCI China to 70, or 13% upside before year-end due to a slow start to reform.

- **The growth premium** – Due to an under-reported GDP deflator, China's economy could have grown at around 6%yoy in 1Q, much weaker than the officially reported 7.4%yoy. Further slowdown may trigger a surge in the unemployment rate and thus invite more policy easing. Export growth may stage a stable rebound in 2H when the base distortion is over, providing a buffer for further property slowdown. The equity market should gain support either way, though a sustainable rally would require a consistent and actionable reform plan.

- **The reform dividend** – Instead of defending a 7.5% growth target, top leaders are more likely to accept the reality of a new normal. The Leading Group of Reform had reviewed schemes for fiscal and *hukou* reforms and may launch them in coming quarters. SOEs will likely be divided into three groups: public, functional, and competitive purpose, with differentiated state controls. Visible reforms shall change market expectation and trigger market re-rating gradually.

- **Property and policy are risks** – Property price correction has pulled down the investment-centric growth rate and is the top risk of the economy in the near-term. Aggressive policy easing (including RRR cuts) is likely inevitable if property-led slowdown tests the bottom-line of growth, and is thus an upside risk of the market. Speeding up *hukou* reform is a better alternative that could avoid a nationwide property market crash without creating further policy distortions.

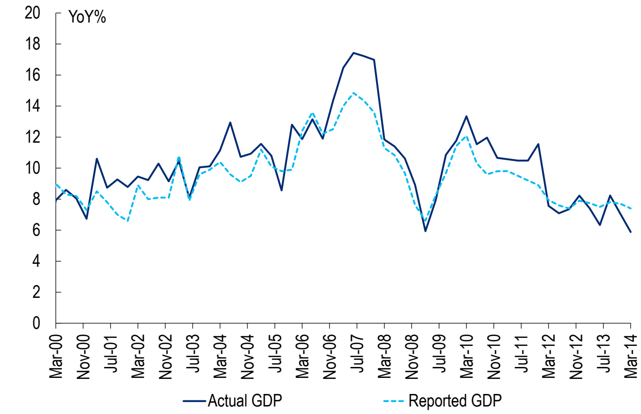
- **Position for reform bias** – China's economy may enter into a few years of difficult adjustment. Policy easing would be carefully designed to write off the impact of property sector correction. Export growth and reforms are two possible positive catalysts this year and beyond. We recommend to long banks, diversified financials, energy, healthcare and consumer as tactical and reform beneficiaries, and avoid capital goods and materials given a property-led investment slowdown.

China: Top Buys and Top Sells

	Ticker	Rating	Price (Jun.6)	Target Price	Yield (%)	ETR (%)	2014E P/E (x)	2014E P/BV (x)	2014E ROE (%)
Top Buys									
China Merchants Bank	3968.HK	Buy	HK$14.68	HK$19.00	5.7	35.3	5.3	1.0	19.9
Beneficiary of China's fiscal reforms, local government debt restructuring reforms and potential policy easing, despite negative impact from deposit rate liberalization									
Fosun Pharma	2196.HK	Buy	HK$28.90	HK$38.00	0.9	32.1	23.0	3.1	14.2
Poised to gain from China's structural aging trends, sector deregulation, and hukou reform									
HaiTong Securities	6837.HK	Buy	HK$11.62	HK$13.50	1.7	17.8	17.2	1.4	8.2
Leading broker that should gain from China's capital market reforms, China's securitization process and potential policy easing									
Mengniu Dairy	2319.HK	Buy	HK$37.45	HK$41.00	0.8	10.3	28.8	3.1	12.8
Downstream business has long-term growth potential, with liquid milk driven by product mix upgrade and baby formula by industry consolidation									
Top Sell									
Rongsheng Heavy	1101.HK	Sell/3H	HK$1.62	HK$0.78	0.0	-51.9	nm	0.9	-17.6
Ongoing losses with weakening balance sheet and cash flow amid structural industry headwinds									

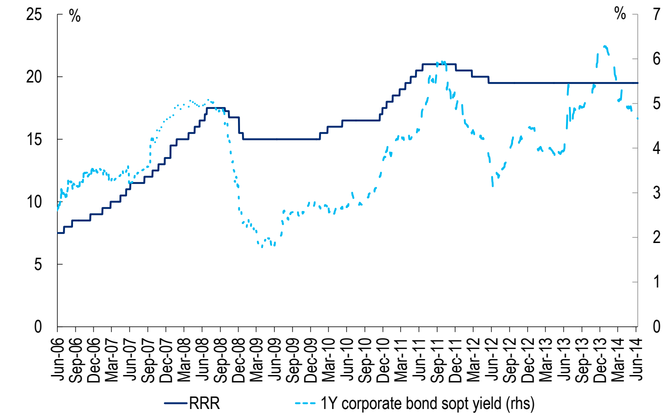
Source: Citi Research estimates

Figure 1. Actual GDP Growth vs. Reported GDP Growth



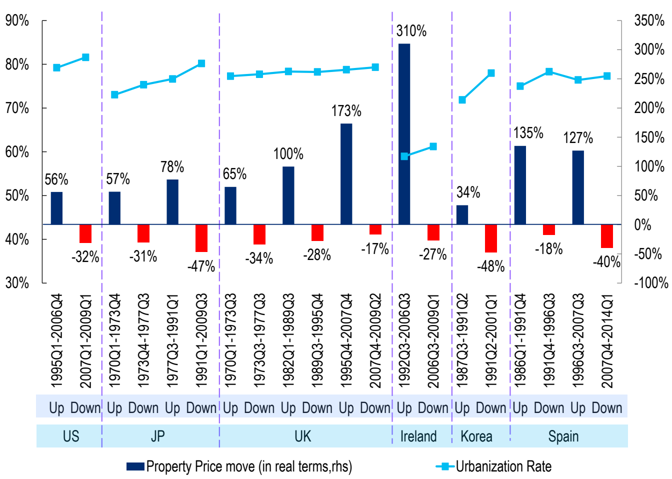
Note: Actual real GDP growth = Nominal GDP growth – Estimated GDP deflator (59%*CPI+41%*PPI+1.5). Source: CEIC and Citi Research

Figure 2. RRR vs. 1-year Corporate Bond Yield



Source: CEIC and Citi Research

Figure 3. Urbanization Rate vs. Property Price Correction



Source: OECD, BIS, Haver and Citi Research

Figure 4. MSCI China: SOE Ownership By Sector in 2013

	Government Holdings % Total
Banks	61.6
Consumer Discretionary	18.3
Consumer Staples	12.2
Diversified Financials	24.5
Energy	76.9
Health Care	25.2
Industrials	53.5
Information Technology	4.4
Insurance	45.9
Materials	33.6
Real Estate	26.8
Telecommunication Services	74.7
Utilities	48.9
Average	**53.0**

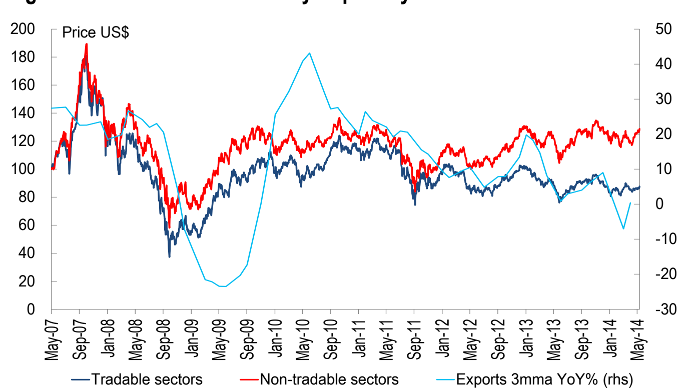
Source: Factset, Bloomberg and Citi Research

Figure 5. Sector Performance By Property Price Cycle

	08'Jan-09'Apr	09'May-10'Apr	10'May-12'Aug	12'Se -13'Dec	14'Jan-Present
Sectors/ Property cycle	**Down**	**UP**	**Down**	**Up**	**Down**
MSCI China	**-46.0%**	**38.3%**	**-17.1%**	**20.1%**	**-2.1%**
Consumer Discretionary	-51.2%	78.5%	-35.6%	24.6%	-7.6%
Consumer Staples	-35.3%	94.8%	-10.0%	14.5%	-9.0%
Energy	-48.7%	49.6%	-2.0%	-2.9%	1.1%
Industrials	-56.4%	27.0%	-38.7%	31.2%	-6.4%
Materials	-57.4%	22.5%	-40.5%	12.1%	-6.7%
Capital Goods	-51.2%	17.4%	-38.8%	30.2%	-6.4%
Transportation	-62.7%	44.6%	-38.3%	24.6%	-8.9%
Health Care	-	-	-33.2%	22.0%	-3.4%
Information Technology	-40.1%	139.3%	11.8%	95.6%	13.1%
Telecommunication Services	-49.5%	11.6%	9.9%	-3.4%	-4.3%
Utilities	-37.5%	-5.3%	5.4%	61.1%	2.8%
Banks	-30.5%	40.5%	-24.5%	21.8%	0.0%
Insurance	-36.2%	36.9%	-32.9%	20.8%	-10.0%
Real Estate	-46.3%	11.9%	-10.9%	21.9%	-12.0%
Diversified financials	-38.2%	28.7%	-54.4%	44.6%	-17.9%

Source: CEIC, Factset and Citi Research

Figure 6. Sector Performance By Export Cycle



Note: Tradable sectors: Consumer Discretionary, Consumer Staples, Energy, Industrials, Materials; Non-tradable sectors: Health Care, IT, Telecommunication Services, Financials. Source: CEIC, Factset and Citi Research

Hong Kong

Positive on Gaming and Property Developers

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- **FY14 HSI Target at 25,000** – The Hang Seng Index is currently trading at ~10x 2014E P/E, lower than the historical average of 12.7x (or 10.8x post GFC). While valuations remain undemanding, few catalysts for a re-rating are visible. We maintain our 2014 Hang Seng Index target at 25,000 (+13% ETR including ~4% dividend yield). Our bottom-up methodology (based on Citi analysts' TPs) suggests a more bullish target of 26,500.

- **Macau Gaming** — With an all-time record 40% of revenues being generated in the mass business (+37.4% YTD, vs. our forecast of +35% in 2014), up to 75% of Macau EBITDA will be generated in the fast growing/high margin mass business. In our view, investors' fixation on weekly headline GGR is now less relevant, as 60% of the headline GGR is generated from the low-margin VIP business (+7% YTD, vs. our forecast of +2.5% in 2014). Net-net, our Macau GGR FY14 forecast is at +13% YoY. With two new property openings in 2015, Macau is setting itself up for a strong 2015 given the easy 2014 comps.

- **Property** — We stick to our non-consensus view that the HK residential market is in consolidation mode, and now expect prices will stay flat rather than drop 10% in 2014. The Street believes HK home prices have already entered a bear market. YTD, home prices have declined less than 1% and the mass-residential segment is already showing signs of bottoming. We see significant upside risk to the Street's estimate of a 20-30% drop by end-2015. Resilient home prices would lead to both earnings and NAV upgrades for HK developers.

- **Conglomerates** — Our Hong Kong and China conglomerate universe is trading at a 28% discount to estimated NAV, nearly half a standard deviation below the 20% historical average discount.

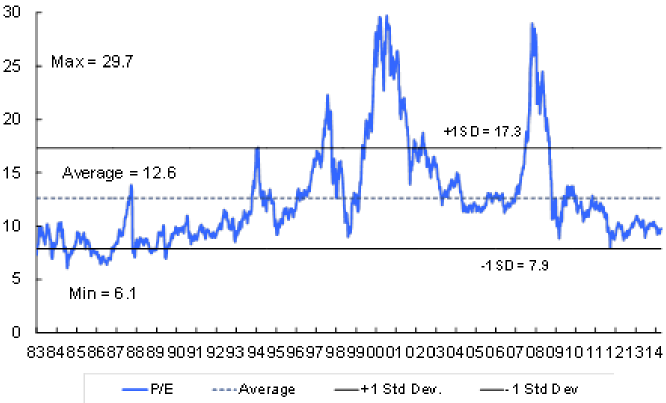
- **Banks** — With sector liquidity possibly affected by QExit and possibly higher regulatory liquidity and capital costs, HK banks will increasingly adopt a strategy of quality over quantity. We estimate a 70% probability of a rising effective lending rate in 2H14.

Hong Kong: Top Buys and Top Sells

	Ticker	Rating	Price (Jun.6)	Target Price	Yield (%)	ETR (%)	2014E P/E (x)	2014E P/BV (x)	2014E ROE (%)
Top Buys									
Cheung Kong	0001.HK	Buy	HK$135.40	HK$164.04	2.1	23.3	9.8	0.8	8.8
As a developer focused on mass residential, CKH should be a direct beneficiary of our expected recovery in the HK mass residential segment									
MPEL	MPEL.O	Buy	US$32.55	US$55.00	2.2	71.2	15.7	3.6	24.6
Cheapest name in the Macau gaming space; Further potential upside from Studio City and Philippines project									
Sands China	1928.HK	Buy	HK$54.35	HK$82.00	4.3	55.2	17.1	7.6	47.2
Dominant player in the mass market. Expected openings of the St Regis Hotel Tower in 4Q15 and Parisian in mid-2016 could be positive price catalysts in near term									
SHK Props	0016.HK	Buy	HK$107.60	HK$137.68	3.1	31.1	13.1	0.7	5.6
Attractive valuations with strong rental growth supported by improving property sales									
Top Sells									
CITIC Pacific	0267.HK	Sell	HK$13.42	HK$6.00	2.6	-52.7	23.9	0.6	3.0
Valuation unattractive: Trading at a ~14% premium to pro forma NAV									
Hong Kong Gas	0003.HK	Sell	HK$16.86	HK$14.55	2.0	-11.7	25.0	3.3	13.7
De-rating from more exposure to new upstream energy business, and expensive valuation									

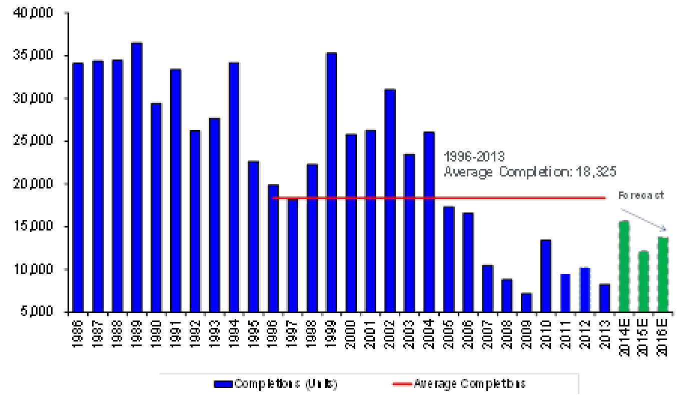
Source: Citi Research estimates

Figure 1. Hang Seng Index – Forward P/E Chart



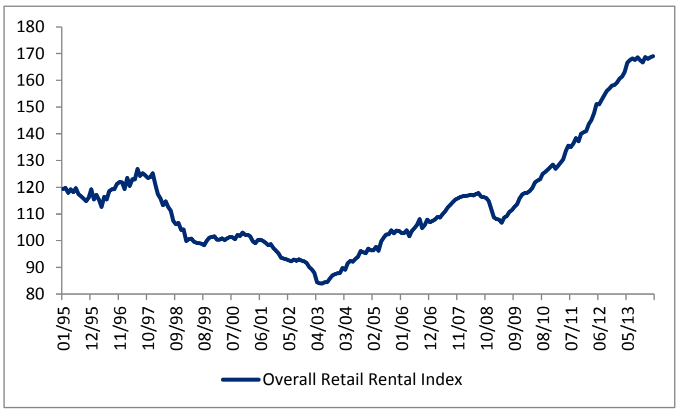
Source: Citi Research Estimates

Figure 2. HK Property – Residential Completions



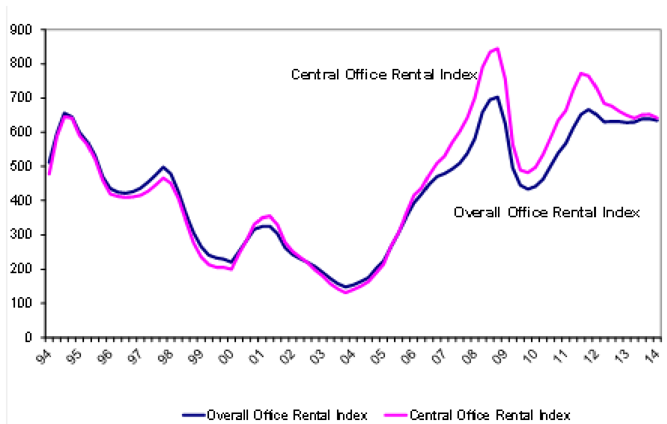
Source: RVD; Citi Research

Figure 3. HK Retail Rental Index



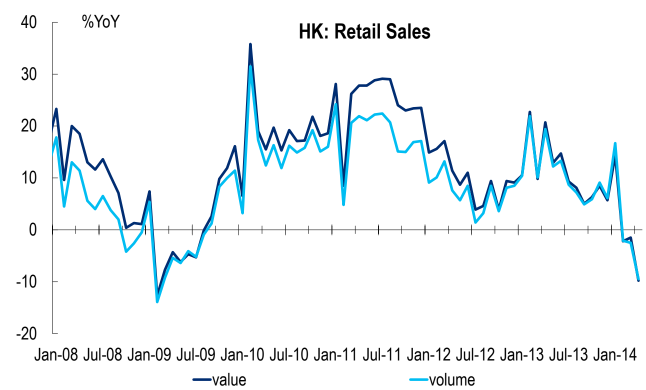
Source: RVD; Citi Research

Figure 4. HK Office Rental Index



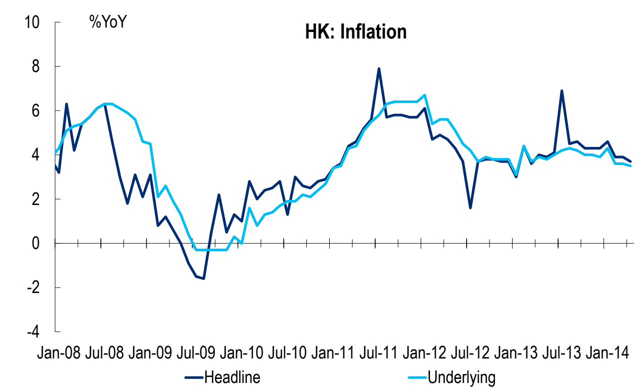
Source: Jones Lang LaSalle, Citi Research

Figure 5. Hong Kong Retail Sales (2008 - Current)



Source: HK Census and Stats Dept; Citi Research

Figure 6. Hong Kong CPI (2008 - Current)



Source: HK Census and Stats Dept; Citi Research

India

Now Waiting for the Real Thing/Swing

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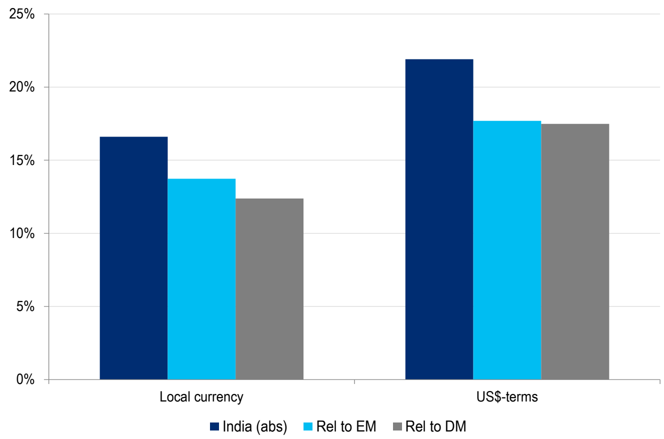
- **An election mandate and an electric start** — India is up 20% YTD (mid/ small-caps: 36% / 49%) because Modi's sweep is bigger than the market asked for, the Govt's quick and decisive start is more than it possibly hoped for, and there is an EM tailwind. The political swing has been big, but is now probably complete. We see +4% to Dec 14 (26,300 Sensex) as we now wait for the real thing/swing.
- **And a risk response: from market, and possibly ground up too** — Markets have expectedly turned it on: equities, then debt and FX. It's a pre-requisite: for meeting India's capital deficit, reviving risk-appetite to start investments, and inducing the consumer to spend. The capital raise dash has begun in earnest, investment talk is up (though no real action yet) and, surprisingly, the consumer too seems upbeat (so suggest some auto data, and auto/retail mgmt. speak). It's possibly the honeymoon, but the early risk response will boost the real one.
- **Economic response should still be back-ended** — Could the markets' risk response swing the economy's growth needle too? We would wait: it's still a bottoming business cycle, and there's balance-sheet and risk-aversion fixing to do. FY16 – at 6.5% GDP growth – should be the uptick year. We see macro cushion and stability: liquidity, rates and currency – and along with the needed fiscal fix (reiterated by new FM) – the economic response back-ended.
- **Balance-sheets over P&L** — We see the rest of the year as a play more on BS revaluation than an earnings or sharp capex revival, a thrust in reform measures and some sort of a re-balancing in the sharp pro-domestic sectoral swing that's happened in the market, leading into and out of the elections. We would OW Banks, Energy, Cement & IT, stay Neutral on Capital Goods and Consumer discretionary, and UW Staples, Metals, Utilities & Pharma.
- **Could it swing the other way?** — India been here before: market darling, momentum – and the 'structural' story'. And it has faltered before too; we see risks in the market getting ahead of itself – fullish valuations not having the patience for slow earnings upgrades, political expectations running too high and global developments. We would see upside risks in domestic investors – long missing, and well set up to extend the party (Owning India Inc: Success Has Many Fathers …..).

India: Top Buys and Top Sells

	Ticker	Rating	Price (Jun. 6)	Target Price	Yield (%)	ETR (%)	FY2015E P/E (x)	FY2015E P/BV (x)	FY2015E ROE (%)
Top Buys									
ICICI	ICBK.BO	Buy	Rs1,480	Rs1,700	1.5	16.4	14.9	2.1	14.8
Expected improvements in BS trends (falling levels of asset deterioration); continued improvements in profitability (rising ROEs)									
Jindal Steel & Power	JNSP.BO	Buy	Rs337	Rs385	0.4	14.6	12.5	1.3	10.5
Expansion projects are complete; as cash flows from projects improve and capex declines, deleveraging should improve equity value									
ONGC	ONGC.BO	Buy	Rs462	Rs455	2.5	1.0	13.5	2.1	16.4
Most levered to higher gas prices. Significant deregulated businesses offset regulatory uncertainties. Subsidy burdens peaked in FY14 and valuations are still reasonable									
Tata Motors	TAMO.BO	Buy	Rs437	Rs486	0.1	11.4	7.9	1.9	28.0
Strong product lineup at Jaguar Land Rover augers well for volume as well as profitability. Demand at China should remain healthy with Chery JV further buoying volumes									
Wipro	WIPR.BO	Buy	Rs509	Rs630	2.4	26.2	14.6	3.1	23.1
Demand commentary and deal wins remain good. Wipro is among the best placed in terms of margin levers to manage the impact of an INR appreciation									
Top Sell									
BHEL	BHEL.BO	Sell	Rs262	Rs220	1.1	-15.1	20.0	1.8	9.3
Capacity under-utilization, declining margins and stretched working capital cycle to continue till revival in power capex cycle, which will take at least another 2-3 years									

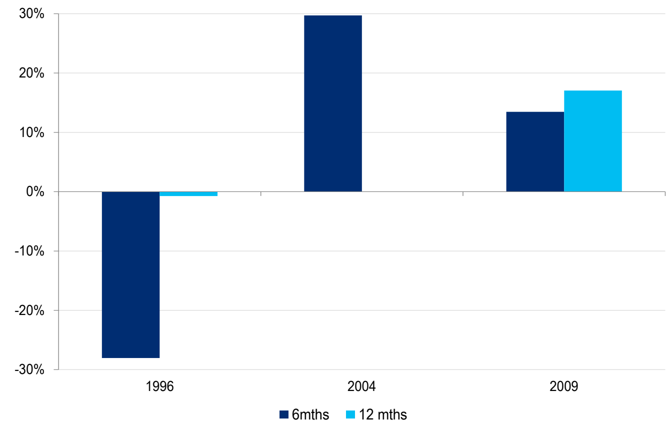
Source: Citi Research estimates

Figure 1. Election Swing: Indian Equities' 2014 YTD performance



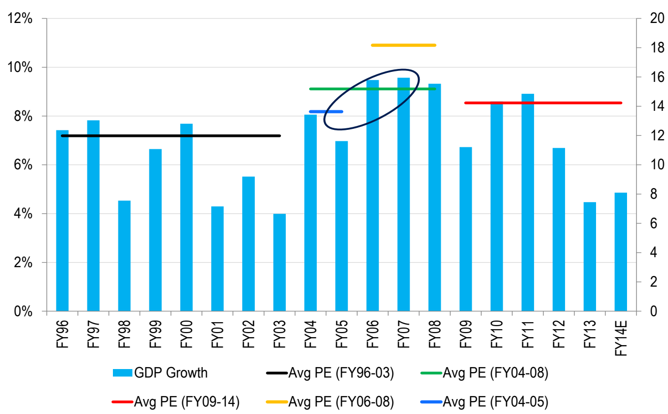
Source: Datastream, MSCI and Citi Research

Figure 2. Sensex Returns in 6/12 Mths, Starting 1mth After General Election Results



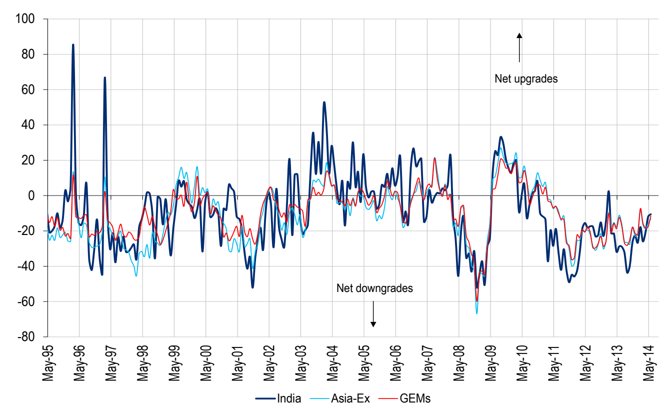
Source: Citi Research

Figure 3. India: GDP Growth and Valuations (1-yr fwd P/E)



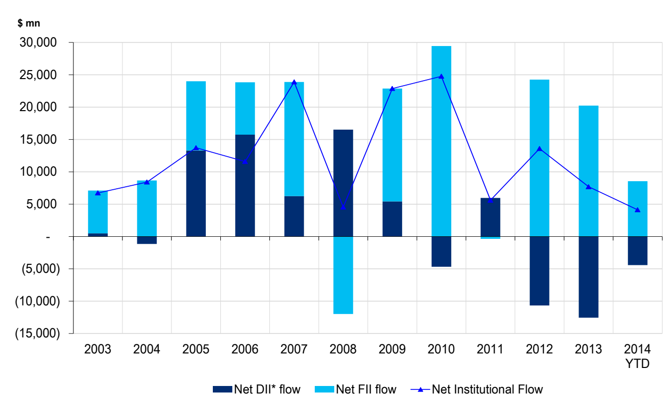
Source: CSO, MSCI, Datastream and Citi Research

Figure 4. Trends in Earnings Revisions: India vs. Peers



Source: Factset, IBES and Citi Research

Figure 7. Institutional (FII and Domestic) into Indian Equities



Source: Bloomberg and Citi Research

Figure 8. India: Comparison Of Asset Class Returns

Asset class	2007 peak – Mar'13	Apr'13 – To Date	2014 YTD
Sensex	-8%	35%	20%
BSE Mid-Caps	-38%	48%	36%
BSE small-Caps	-38%	68%	49%
Fixed income (term deposit)	54%	9%	4%
Gold	179%	-9%	-8%
Real Estate	25-150+%	9%	2%

Source: Bloomberg and Citi Research

Indonesia

All Eyes On Elections; Will the Euphoria Continue?

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- **Presidential election will go to only 1 round** – As only two presidential candidates are in the running, the election will be completed by July 9. Jokowi–Kalla will compete head to head with Prabowo–Hatta. The latest survey by Populi Indonesia indicated a clear lead for Jokowi–Kalla by 47.5% to 36.9%, with 15.6% undecided voters. We retain our end-2014 index target of 5,300, which was set in 4Q13. Our top picks are BBNI, SMGR, SCMA, ASII and LPPF.

- **Prabowo-Hatta gaining momentum** – Despite still trailing by more than 10ppt of the votes based on Populi Center survey, Prabowo-Hatta are gaining momentum (the previous LSI survey indicated Jokowi was leading by 35.4% vs 22.8%, with 41.8% undecided voters), bolstered by a stronger political coalition coupled with media support, in particular from Harry Tanoesudibyo and Aburizal Bakrie. Nonetheless, the latest survey indicated that it would be difficult for Prabowo-Hatta to win the election.

- **Policies to tackle CAD and weakening of the rupiah are needed** – Regardless of which presidential candidate wins the election, policies to tackle Indonesia's economic problems – such as the widening current-account deficit and a depreciating rupiah – will be executed only at end-2014. Fuel price adjustments are needed to reduce the budget pressure and import of oils.

- **Do the 2 candidates have significantly different policy agendas? No** – The economic platforms of the two presidential candidates are pretty similar. However, the Jokowi–Kalla team is regarded as having the stronger track record, given Jokowi's time as Jakarta governor and Jusuf Kalla's time as SBY's Vice President in 2004-09.

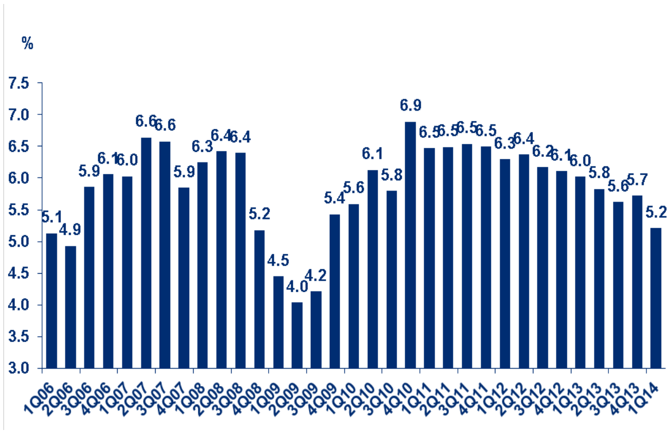
- **What are the catalysts and risks?** – Positive catalysts for the market would be 1) a smooth election process with no untoward events (Jokowi is seemingly the favoured investor choice); 2) formation of a strong cabinet (heavy with technocrats and professionals). Risks to the market are 1) volatility in the exchange rate; 2) unexpected political developments; 3) high oil prices.

Indonesia: Top Buys and Top Sells

	Ticker	Rating	Price (Jun. 6)	Target Price	Yield (%)	ETR (%)	2014E P/E (x)	2014E P/BV (x)	2014E ROE (%)
Top Buys									
Astra International	ASII.JK	Buy	Rp7,200	Rp8,250	3.4	18.0	13.2	3.1	24.6
Attractive valuation on 2015E PER of 12x and strong governance and track record									
Bank Negara Indonesia	BBNI.JK	Buy	Rp4,830	Rp5,450	2.1	15.9	9.6	1.7	19.0
Beneficiary of the new government infrastructure-related spending, attractive valuation, and improving franchise									
Matahari Department Store	LPPF.JK	Buy	Rp14,075	Rp15,500	1.1	11.2	27.0	nm	nm
Consignment model, strong supply chain (90% local sourcing), working capital metrics, coupled with lower interest cost through deleveraging to result in robust EPS growth									
Semen Indonesia	SMGR.JK	Buy	Rp15,325	Rp17,600	2.7	17.5	16.5	3.8	24.6
Increasing capacity by 37% up to 2017, economies of scale, and expected benefits from previous timely capacity expansion and infrastructure spending									
Surya Citra Media	SCMA.JK	Buy	Rp3,495	Rp4,000	1.9	17.0	29.1	14.4	56.1
Current market leader in FTA TV audience shares (c.30% split) fueled by Indosiar's transformation; sector-high ROE of ~55% and strong corporate governance									
Top Sell									
Bank Danamon	BDMN.JK	Sell	Rp4,310	Rp3,225	2.9	-22.2	10.2	1.2	12.4
Weak deposit franchise, slowing auto demand and competition									

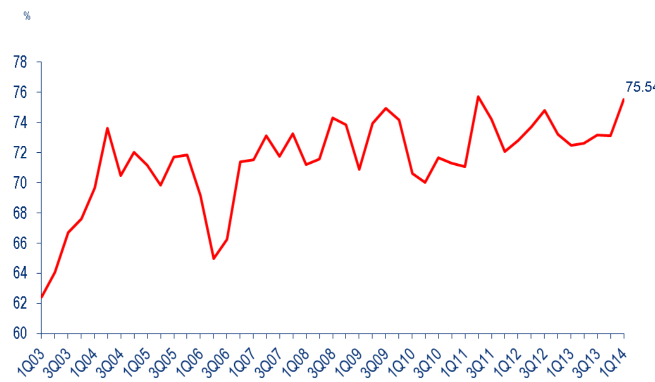
Source: Citi Research estimates

Figure 1. Quarterly GDP Growth (%)



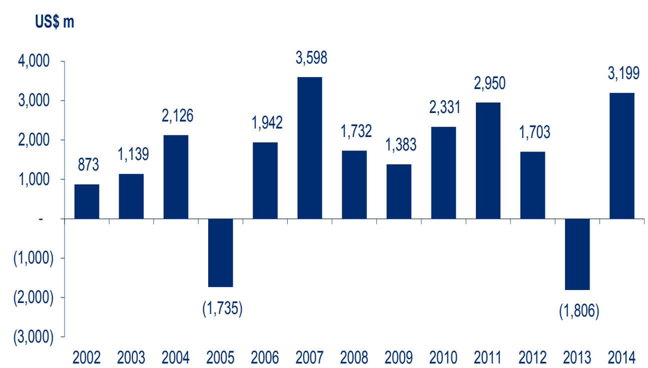
Source: Bloomberg, BPS

Figure 2. Manufacturing Utilization Rates



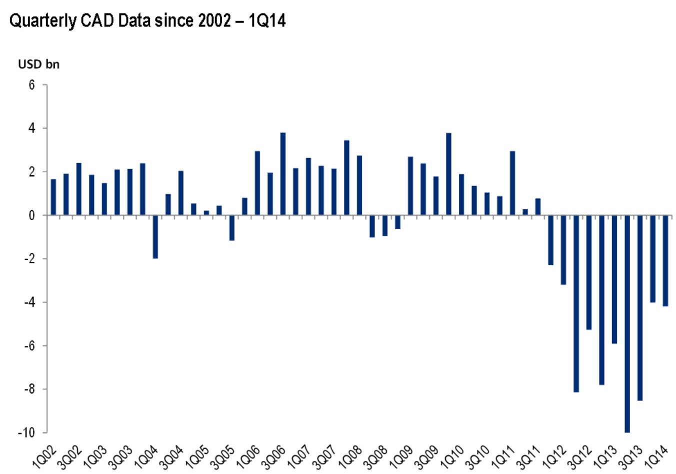
Source: Bank Indonesia, CEIC

Figure 3. Equity Net Foreign Inflow/Outflow, as at 6 June 2014



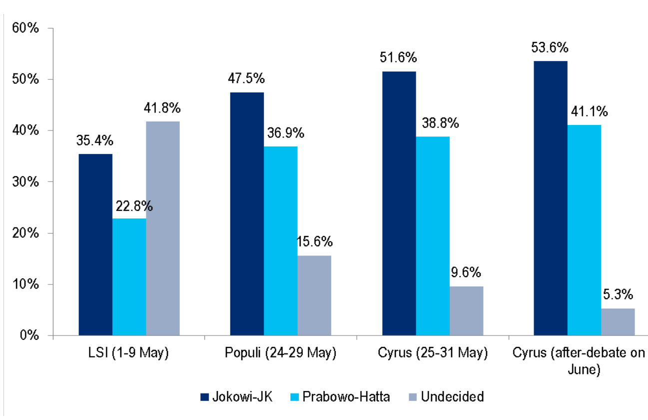
Source: IDX, Bloomberg

Figure 4. Quarterly CAD



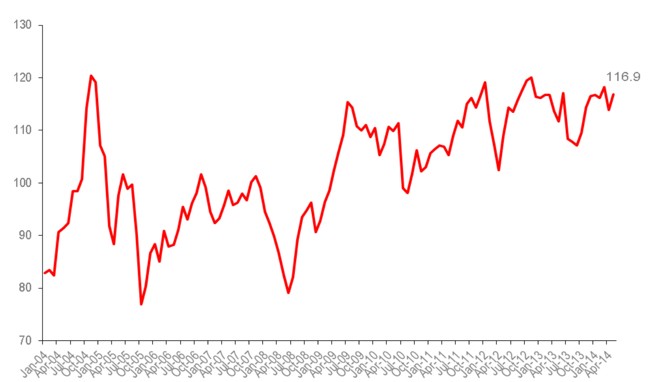
Source: Bloomberg

Figure 5. Latest Polling on Presidential Election (Various surveys)



Source: LSI, Populi, Cyrus Network, Various news articles

Figure 6. Consumer Confidence Index



Source: BI Survey, CEIC

Japan

Abenomics Market to Come Back Toward End of 2014

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- **Three reasons to be bullish** – Japan has performed poorly from the beginning of 2014, which we do not expect to continue in H2 2014 for three reasons. 1) The yen will likely depreciate by the end of 2014. 2) The economy will start to recover after the tax rate hike. 3) The market is attractively valued compared with both its history and peers.

- **Yen to depreciate by the end of 2014** –There are two drivers for yen depreciation: the BOJ and US Treasury yields. We expect the BOJ to add monetary easing in October 2014 for two reasons. 1) The yen depreciation impact on CPI inflation weakens: 2) The rate of increase in wages is still low to achieve the inflation goal of 2%. In our view, US Treasury yields are likely to rise reflecting the improvement in the US economy and the closer exit of the US monetary easing.

- **The economy restarts to recover** – There were concerns over the negative impact of the consumption tax rate hike in April. So far, available economic indicators suggest that the economy will not deteriorate as it did in 1997, the last time the government hiked its policy rate.

- **Attractive valuation** – The CAPE of TOPIX is about 11x. The is well below previous peaks of c20x, suggesting plenty of upside in Japanese equities. Looking at international comparisons, the Japanese PER of 14.1x is lower than 16.7x for the US and 15.8x for Europe ex-UK. There seems to be room for Japanese equities to catch up with other markets.

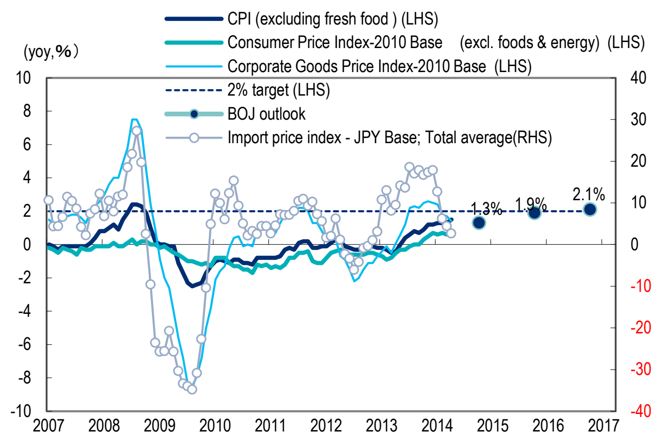
- **Overweight Auto, Machinery and Financials** – Given likely depreciation of the yen and the improvement in the US economy, we see auto and machinery as likely to outperform. Capex is showing signs of recovery, which will likely benefit the machinery sector. Financials are a big laggard. Gradual climbs in interest rates and rises in equity markets should help them to outperform the market.

Japan: Top Buys and Top Sells

			Price	Target	Yield	ETR	2014E		
	Ticker	Rating	(Jun. 6)	Price	(%)	(%)	P/E (x)	P/BV (x)	ROE (%)
Top Buys									
Bridgestone	5108.T	Buy	¥3,695	¥4,700	1.5	29.6	9.4	1.6	15.4
1) Evidence of impressive price control ability thanks to strong brand value; 2) High exposure to the North American market, where latent demand has accumulated									
Honda	7267.T	Buy	¥3,580	¥4,000	2.3	14.3	10.0	1.3	10.8
Earnings are likely to improve from FY3/14 stemming from new model launches in North America and Southeast Asia and the recent trend toward yen weakness									
Seven & i Holdings	3382.T	Buy	¥4,188	¥4,700	1.6	14.0	19.8	2.0	8.8
As the largest player, we think Seven & i Holdings will benefit from continued growth for the domestic convenience store market and its oligopolization									
Sumitomo Mitsui Financial	8316.T	Buy	¥4,266	¥6,500	2.8	55.4	8.4	0.9	7.1
Valuations have fallen to historically low levels. We believe interest rate normalization and other positives have not been priced in									
Top Sells									
Toyota Boshoku	3116.T	Sell	¥1,082	¥860	1.7	-18.9	14.9	1.1	7.2
Larger-than-expected impact from prolonged production problems in North America and mix deterioration in Asia and Oceania overhang outlook for earnings									
Toyo Suisan	2875.T	Sell	¥3,110	¥2,800	1.6	-8.4	16.7	1.6	7.8
Profit growth is likely to slow due to intensified competition in the instant noodle business in both Japan and overseas markets									

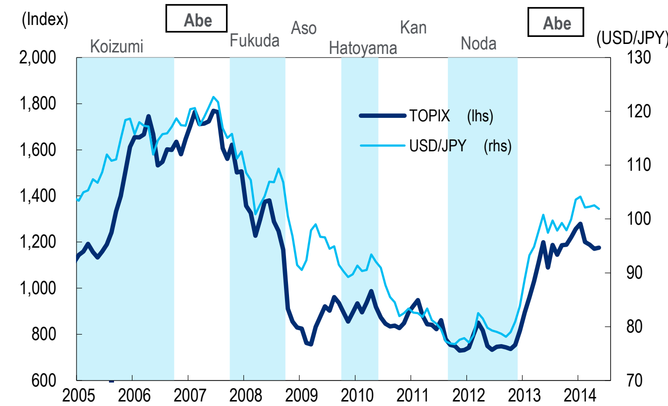
Source: Citi Research estimates

Figure 1. CPI, CGPI and Import Price Index



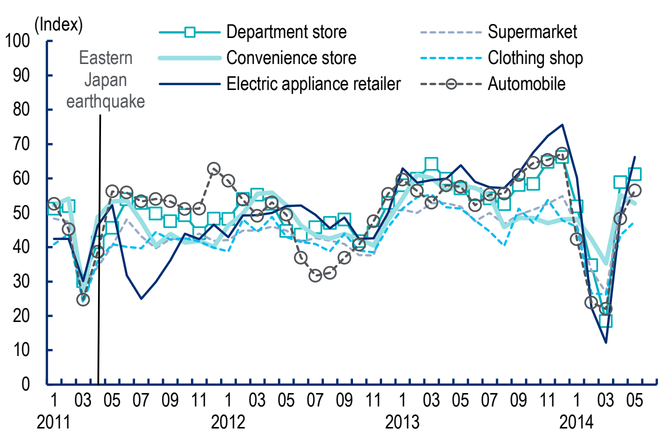
Source: Astra Manager, and Citi Research

Figure 2. TOPIX, the USD/JPY and Prime Ministers



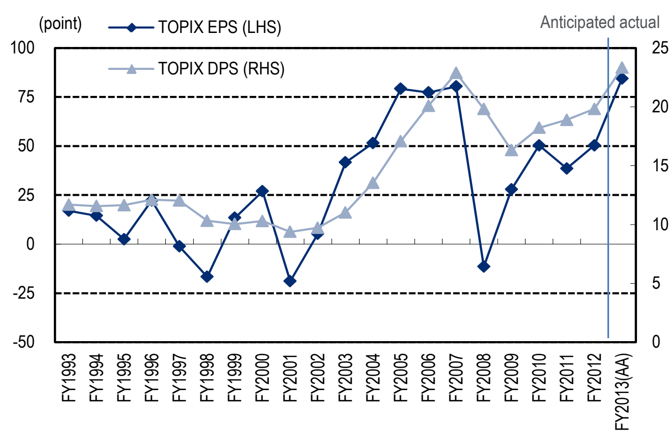
Source: Datastream, and Citi Research

Figure 3. Economy Watchers Survey of Retail Sectors



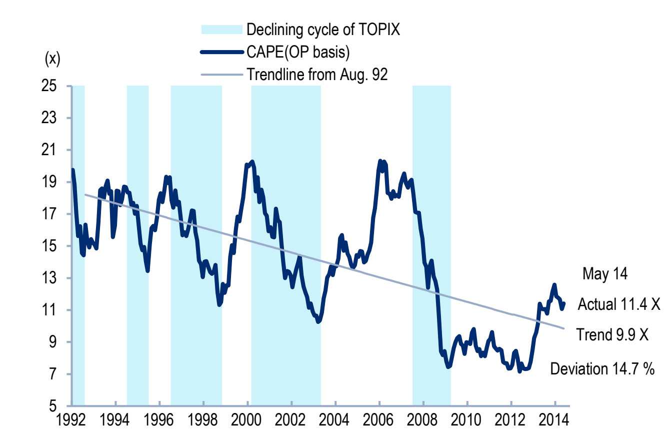
Source: Cabinet Office and Citi Research

Figure 4. TOPIX EPS and DPS



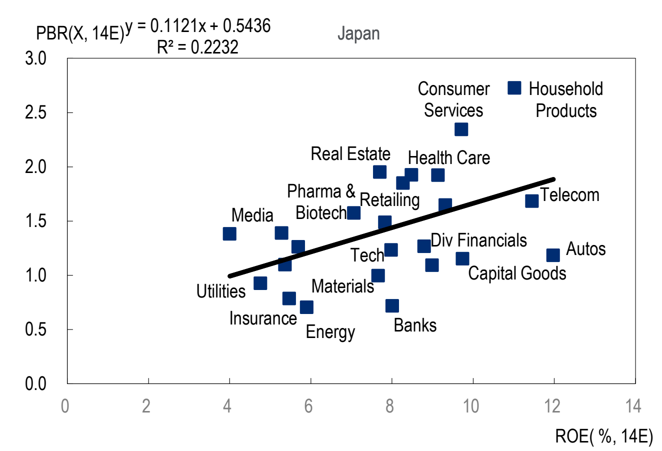
Source: Bloomberg, and Citi Research

Figure 5. CAPE for TOPIX



Note: Shaded sections denote periods of decline for TOPIX (10%+ decline over a 12-month or longer period). Deviation calculated using the natural log difference between CAPE and the trendline at end-May.
Source: Citi Research.

Figure 6. ROE vs PBR By Sector



Source: Citi Research, Worldscope, MSCI, Factset

Korea

Valuation Merit to Emerge Amid Economic Rebound

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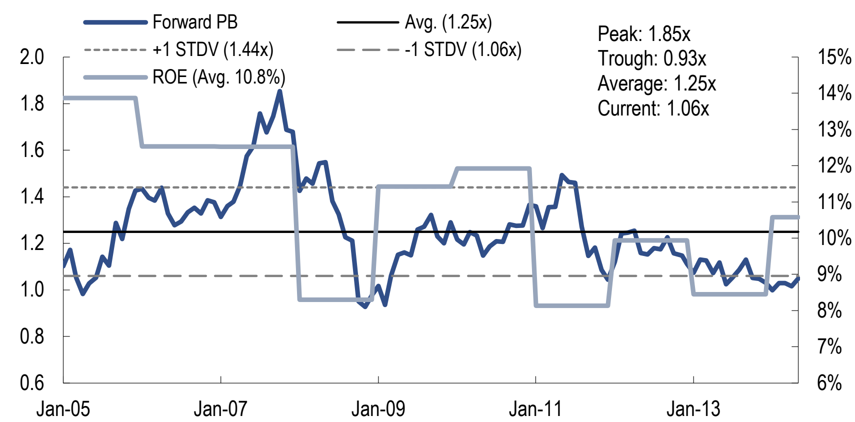
- **KOSPI target 2300** – Based on our economists' 3.0% global GDP growth for 2014E, we expect Korea's GDP to recover to 3.8% in 2H14 (vs. 3.5% in 2H13). We set our 2014E KOSPI target at 2300, based on 2014E P/B of 1.23x (ROE of 10.6%), a slight discount to the historical average of 1.25x (ROE of 10.8%).
- **Top-down overweight on Korea** – Our GEMS strategist is positive on EM given 1) higher GDP than the pre-crisis level, 2) low expectations, 3) improving liquidity, and 4) cheap valuations. He remains overweight on Korea, as his country/sector allocation model has a cyclical, pro-global growth tilt.
- **Positive macro outlook for 2H14** – Domestic demand and exports in Korea are likely to add to growth momentum, along with improvements in employment and the global economy. The end of Fed tapering likely in 2H14 and quantitative easing of the ECB and BoJ seem to have induced a risk-on mode in global financial markets and provide upside to equities.
- **Downside risks remain** – We think the risks come from the aftermath of the ferry sinking incident in Apr and appreciation of KRW. Furthermore, possible delays in forming a new cabinet after the regional elections in early Jun could weigh on economic sentiment.
- **Low valuations** – Korea currently trades at 1.06x 14E P/B vs the historical average of 1.25x, with 14E P/B at 1SD below mean. We forecast 10.6% ROE for 2014E vs the historical average of 10.8%.
- **Sector picks** – We would overweight the tech and auto sectors for higher earnings visibility and cheap valuations.

Korea: Top Buys and Top Sells

	Ticker	Rating	Price (Jun. 6)	Target Price	Yield (%)	ETR (%)	2014E P/E (x)	2014E P/BV (x)	2014E ROE (%)
Top Buys									
Hyundai E&C	000720.KS	Buy	W52,800	W80,000	0.8	52.7	9.2	1.1	12.4
Biggest laggard in the E&C sector. Strongest overseas E&C player with accumulating overseas order backlog (book to bill ratio of 4x)									
Hyundai Motor	005380.KS	Buy	W225,000	W320,000	0.9	43.1	5.4	0.8	16.4
Improving global autos demand, refreshing model cycle and likely capacity roadmap announcement									
Hyundai Wia	011210.KS	Buy	W180,500	W225,000	0.3	24.9	9.8	1.7	19.1
Solid EPS growth on China engine capacity addition and cyclical machinery turnaround; potential beneficiary from HMC/Kia capacity expansion									
SEC	005930.KS	Buy	W1,457,000	W1,800,000	1.0	24.5	7.2	1.2	18.8
High rerating opportunities still ahead on 1) resilient smartphone, 2) multi-year memory growth and 3) improving mid-term shareholder return policy									
SK Hynix	000660.KS	Buy	W46,450	W62,000	0.0	33.5	8.2	2.0	27.3
Most leveraged pure memory play on persistent strong memory fundamentals on the back of structural changes in competitive landscape									
SKT	017670.KS	Buy	W218,500	W270,000	4.3	27.9	8.4	1.2	15.0
Strong earnings growth expected with 1) rising ARPU, 2) improved marketing discipline and 3) less depreciation as peak capex cycle is over									
Top Sells									
Hyundai Dev	012630.KS	Sell/3H	W28,900	W26,000	0.2	-8.3	22.8	1.0	4.4
Structural deterioration in the margin profile for housing projects and unattractive landbank profile should disappoint market's heightened expectation									
Hyundai Heavy	009540.KS	Sell	W182,500	W155,000	1.1	-14.0	nm	0.8	-2.0
Global order momentum slow (-15% in 2014E) and significant downside risk to consensus (2014E OP: Citi –W140bn vs. the Street: W500bn)									
NCSoft	036570.KS	Sell	W165,000	W150,000	0.4	-8.5	15.4	2.6	18.7
Market expectations for new games seem too high									

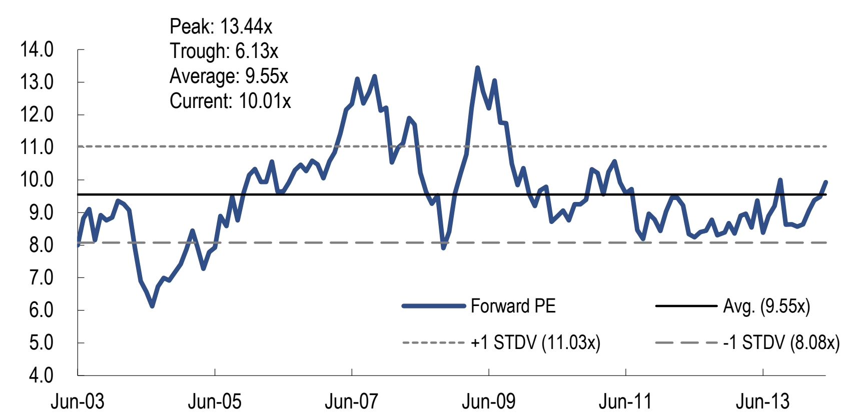
Source: Citi Research estimates

Figure 1. Forward PB Trends



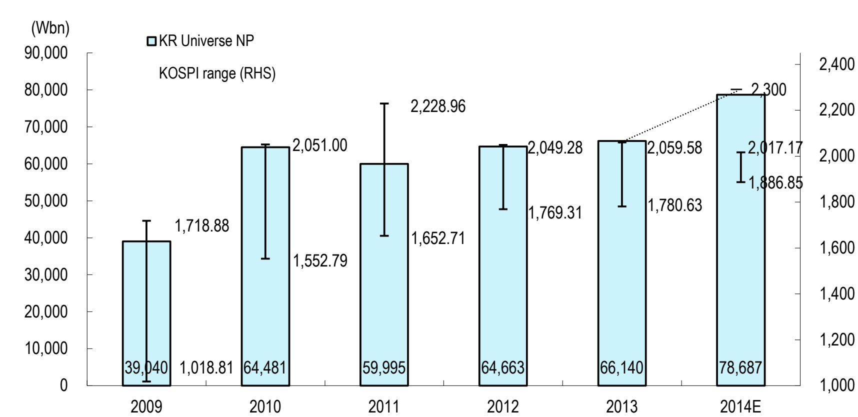
Source: Citi Research

Figure 2. Forward PE Trends



Source: Citi Research

Figure 3. KR Universe NP Trends vs. KOSPI Range



Source: Citi Research

Malaysia

Earnings Cuts Still a Feature

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- **Valuations +1 S.D.** — The KLCI now trades at ~16.0x P/E, above the historical mean of 14.4x, and at 2.07x fwd P/B (above mean of 1.95x). Our KLCI target is 1,894 (based on a bottom-up approach), which translates to a P/E of 16.2x, slightly above +1 S.D. of 15.6x. YTD, KLCI, with flat performance, has underperformed ASEAN peers in both LCY and USD terms. Foreign portfolio inflows into Malaysia picked up in May after 3-4 months of declines and we see Malaysia positioned for a stronger pick-up in 1H15 as cost normalization, benefits from a lower ringgit, secondary effects from ETP projects and accelerated consumption kick-in before the GST implementation in April 2015.

- **Sector rotation in play** — Sector rotation featured as an alpha generator, with developers as the best performing sector YTD, after being badly hit in 2H13 by concerns over property cooling measures (e.g. hiking of the real property gains tax, higher purchase band for foreigners). Telecoms and industrials (construction conglos) also continued to perform YTD. Consumer discretionary, transport and healthcare names underperformed.

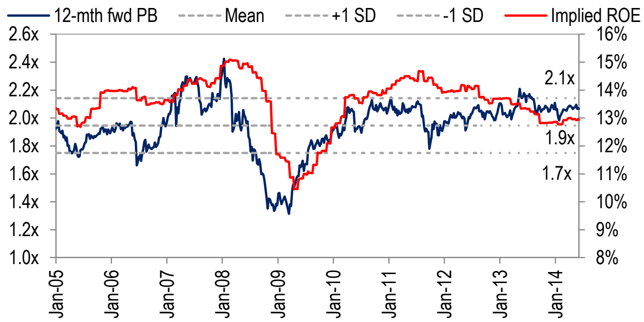
- **Top picks** — We expect the KLCI to remain range-bound as it is trading above mean and is still exhibiting negative earnings revisions as it digests domestic challenges. We expect stock picks to feature as return drivers for 2H14 and would reiterate our preference for several longer-term structural stories, especially where 1H14 stock price performance has been muted: *Maybank* (diversified business to play rising investment cycle), *SapuraKencana* (growth potential from oil/gas projects), *Sime Darby* (plantation earnings recovering, property spinoffs) and *IHH* (best leveraged to SG's greying population theme). We also like *AirAsia* (beneficiary of the new KLIA2 Terminal, cost-side initiatives, and likely disposal gains) and *MAHB* (leveraged to MY's investment in tourism infrastructure).

Malaysia: Top Buys and Top Sells

	Ticker	Rating	Price (Jun. 6)	Target Price	Yield (%)	ETR (%)	2014E P/E (x)	2014E P/BV (x)	2014E ROE (%)
Top Buys									
AirAsia	AIRA.KL	Buy	RM2.51	RM2.80	2.2	13.4	11.6	1.3	11.5
Beneficiary of new KLIA2 Terminal in addition to cost-side initiatives and likely disposal gains									
IHH	IHHH.KL	Buy	RM4.18	RM4.80	0.5	15.3	40.8	1.8	4.5
Offers the best leverage to Singapore's greying population theme									
MAHB	MAHB.KL	Buy	RM7.65	RM10.00	2.1	32.8	23.6	1.6	7.7
Best leverage towards Malaysia's heavy investment in tourism-related infrastructure									
Maybank	MBBM.KL	Buy	RM9.84	RM11.11	5.1	18.0	12.6	1.8	14.3
Diversified business model to play the rising investment cycle, Malaysia's economic transformation									
SapuraKencana	SKPE.KL	Buy	RM4.04	RM5.40	0.0	33.7	17.4	1.9	13.1
Continued growth potential from oil/gas projects									
Sime Darby	SIME.KL	Buy	RM9.52	RM10.60	3.6	14.8	15.5	1.9	11.6
Diversified business with earnings potential from a recovery in plantations and possible property spin-offs									
Top Sells									
Genting Berhad	GENT.KL	Sell	RM10.00	RM9.00	0.8	-9.2	20.8	1.4	8.6
Trading at 14% discount to NAV, half S.D. premium to its historical average									
Maxis	MXSC.KL	Sell	RM6.72	RM6.00	6.0	-4.8	23.3	9.8	38.8
Expensive valuation with below-par operating performance									

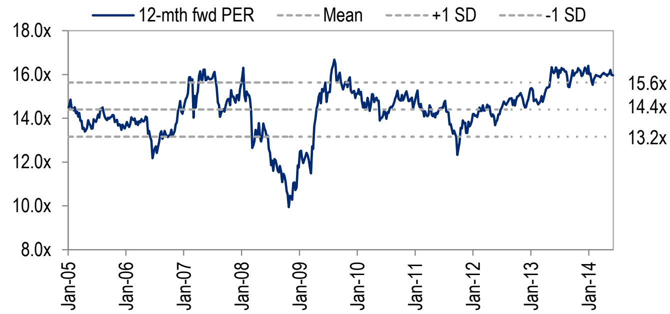
Source: Citi Research estimates

Figure 1. KLCI 12M Forward PB vs ROE



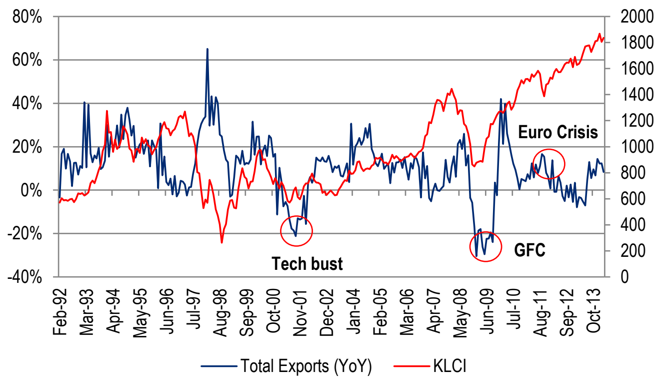
Source: CEIC, Citi Research

Figure 2. KLCI 12M Forward PE



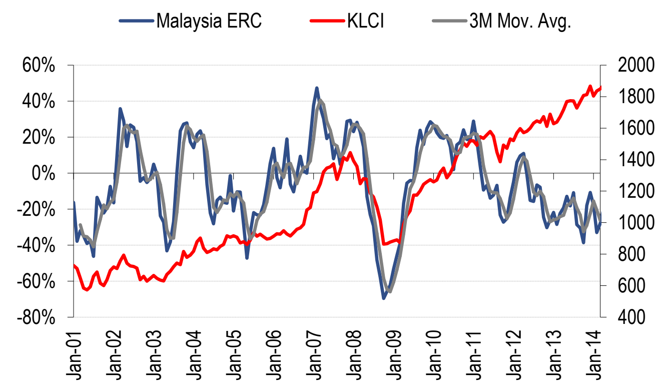
Source: CEIC, Citi Research

Figure 3. Malaysia Total Exports Growth (YoY) vs KLCI



Source: CEIC, Citi Research

Figure 4. Malaysia Earnings Revision Count



Source: Citi Research, Factset

Figure 5. Malaysia — EPS Growth by Sector

EPS Growth	CY07	CY08	CY09	CY10	CY11	CY12	CY13	CY14E	CY15E
Commercial Banks & Other Financial Services	64%	1%	13%	20%	18%	8%	4%	6%	10%
Industrials (Conglomerates)	28%	-9%	-44%	38%	69%	2%	-7%	8%	14%
Industrials (Offshore)	31%	34%	25%	28%	-13%	9%	13%	36%	12%
Industrials (Transport)			161%	42%	-13%	-143%	-28%	88%	98%
Consumer Staples	47%	2%	-14%	33%	0%	-19%	-15%	35%	10%
Consumer Discretionary	-16%	8%	11%	51%	5%	-5%	-11%	7%	10%
Real Estate	0%	-69%	4%	74%	10%	18%	-30%	-7%	-5%
Telecommunications	21%	-28%	-2%	26%	4%	2%	6%	3%	9%
Healthcare	19%	20%	63%	10%	-32%	-15%	15%	19%	23%
Utilities/Materials	31%	-26%	-6%	-9%	-9%	27%	2%	0%	16%
TOTAL	**30%**	**-11%**	**-2%**	**27%**	**11%**	**8%**	**-1%**	**8%**	**12%**

Source: Citi Research estimates, dataCentral, MSCI

Philippines

Macro Growth Drivers Intact But Facing ST Reversal Risk

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- **Investment and consumption drivers intact despite slower GDP** – Rising investments and domestic demand are expected to re-accelerate GDP growth to 6.2% in 2H14. Food inflation trajectory has been stronger than expected but CPI is still seen as staying within a 4-5% band. Impact of the reserve hike on liquidity conditions provides BSP some flexibility to delay expected 25bp hike to 4Q.

- **Modest growth expectations limit downside earnings risk** – Earnings revision indicator (ERI) has been in neutral territory. Inflation uptrend and heightened competition pose risks to margins. Risk of sharp downgrades to core earnings is limited, in our view, given modest expectations of 8.6% consensus earnings growth in 2014. In some sectors, quality of earnings is improving (i.e. stronger recurring income for banks). Domestic top-line growth remains robust for consumer companies. Real estate reservation sales are showing signs of slowing but this would impact future revenue flows.

- **Still some upside for PSEi on 12M view but NT market vulnerabilities exist** – Buoyed by strong foreign buying (US$1bn YTD), the market's 12M PE has rerated 6.5% YTD and is at 18.2x, 1.1 SD above mean. Aside from vulnerability to profit-taking, the strong negative correlation of market valuations to rising LT bond yields could trigger a de-rating in the near term. Nonetheless, our bottom-up price targets for PSEi stock constituents still point to a 12M target of 7,400 (equivalent to 19.2x 12M forward PE).

- **Catalysts/risks** − Positive catalysts include possible Moody's rating upgrade in 3Q, accelerated bidding of PPP projects and strong GDP growth in 4Q. Meanwhile, political noise is likely to continue to heighten as we near 2016 elections, but should still not be a big market factor in 2014. Aside from risks of reversal of flows and de-rating as LT yields rise, a sustained rise in inflation could trigger an earlier-than-expected rate hike, which is a potential risk.

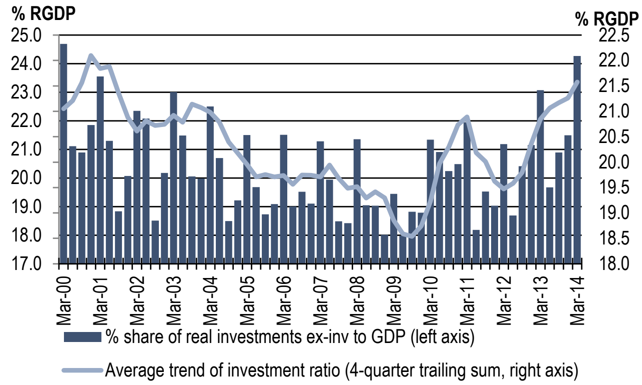
- **Preferred plays –** Given near-term vulnerabilities, we prefer laggards with improved prospects for core earnings recovery: PLDT, SM Inv. and Metrobank. We continue to like BDO given strong core earnings growth, while casino opening is a catalyst for Melco Crown. JFC is our least preferred on valuations.

Philippines: Top Buys and Top Sells

	Ticker	Rating	Price (June 6)	Target Price	Yield (%)	ETR (%)	2014E P/E (x)	2014E P/BV (x)	2014E ROE (%)
Top Buys									
Banco de Oro	BDO.PS	Buy	P90.2	P96.0	1.8	7.4	16.9	1.8	11.1
Best positioned to benefit from credit growth recovery with strong liquidity and capital position; Improving core earnings growth									
Melco Crown	MCP.PS	Buy	P13.4	P19.0	0.0	41.8	NM	4.1	-14.5
Top pick in Philippine gaming space; catalyst is opening of City of Dreams Manila in 4Q14									
Metrobank	MBT.PS	Buy	P85.2	P97.7	0.9	15.6	13.8	1.6	12.0
Laggard banking stock benefiting from momentum in credit growth									
PLDT	TEL.PS	Buy	P2,888.0	3,215.0	6.5	17.9	15.3	4.6	28.9
Poised to benefit from better pricing from industry rationalization with rising data take-up driving recovery in revenue growth									
SM Investments	SM.PS	Buy	P780.0	P 920.0	1.3	19.1	19.8	2.5	13.6
Laggard conglo that is a play on the Philippines' macro theme with improved signs of recovery in the retail segment									
Top Sell									
Jolibee	JFC.PS	Sell	P180.0	P135.0	0.9	-24.3	37.8	7.5	21.4
Brand premium factored in expensive valuation									

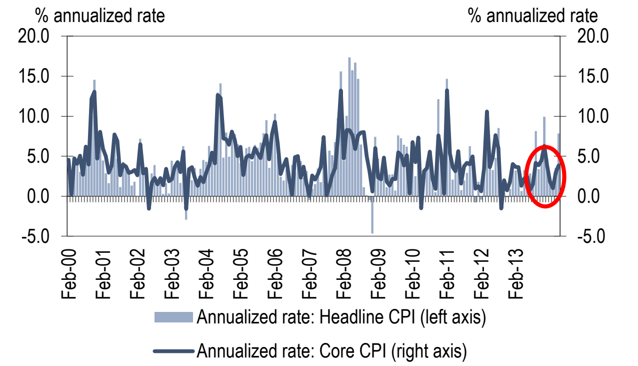
Source: Citi Research estimates

Figure 1. Investments to GDP Ratio Continues to Rise



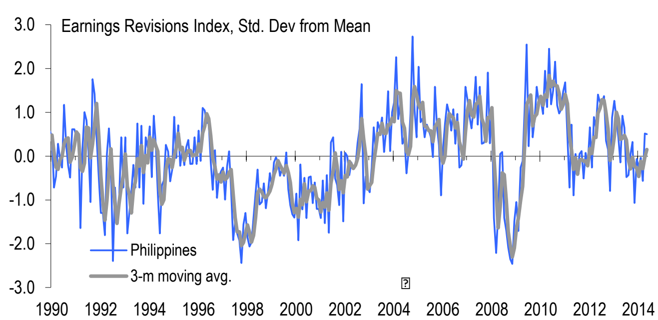
Source: CEIC, Citi Research

Figure 2. Excess Liquidity, Food Prices Causing Inflationary Pressure



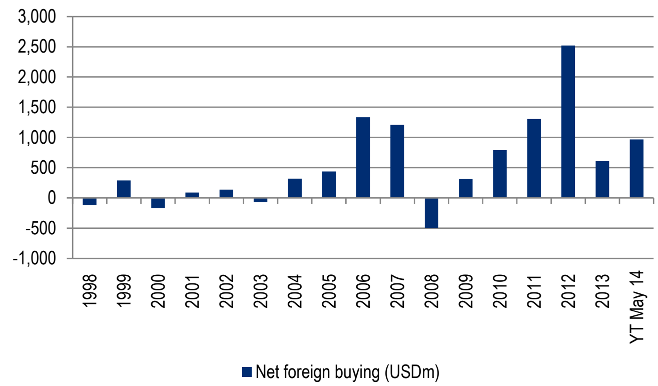
Source: CEIC, Citi Research

Figure 3. Earnings Revisions in Neutral Territory



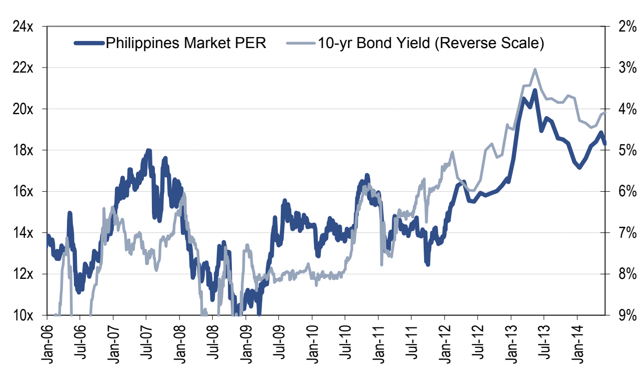
Source: ERI, CEIC, Citi Research

Figure 4. Close to US$1bn Net Foreign Buying YTD



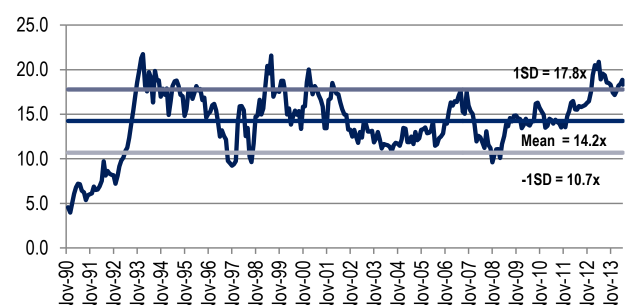
Source: PSE, Citi Research

Figure 5. PE vs 10-yr Bond Yield



Source: Citi Research, as of 6 June 2013

Figure 6. Market PE at 18.3x, 1.1 SD Above Mean



Source: Citi Research, as of 6 June 2014

Singapore

Beats Start to Feature

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- **The need for exports to grow** — Singapore's market has historically performed as exports recovered. While there are early signs that exports are improving after two years of weakness, upside potential may be more muted this cycle given domestic challenges in labor and costs. A strong externally led recovery will be critical for helping Singapore's leveraged households with debt digestion. While earnings revisions continue to be negative, the rate of decline has been improving (post 1Q14 results to -9% vs. -19% post FY13 results and -20% post 3Q13).

- **Valuations just above mean** — STI is currently trading at 15.5x forward PE (slightly above mean of 15.2x) and 1.26x forward PB (slightly above -1S.D.). Our STI target of 3,278 implies a PE of 15.4x. Year to date, the 4% rise in the STI has underperformed ASEAN peers (in USD terms) other than Malaysia. YTD, performance has come from consumer discretionary, conglomerates (Jardine's Indonesian exposure) as well as select REITS. Yield-heavy names have performed more strongly, especially in April, in tandem with lower 10Y SGS yield ~228bps (vs. 259bps at early 2014) though this had begun to moderate in June.

- **Top picks** — We prefer stocks exposed to external drivers**.** *Keppel Corp* (rig cycle intact despite oil-price volatility); *Wilmar* (conduit for Asia's food needs); *DBS* (highest NIM/earnings leverage to eventual SGD rate rise); *NOL* (under-appreciated logistics unit); and *Keppel Land* (potential divestment of MBFC Tower 3).

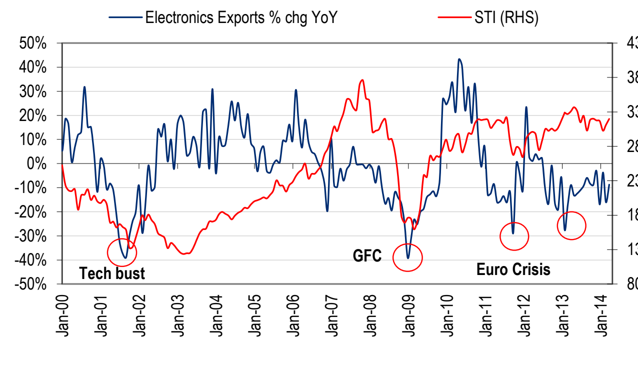
- **Investors starting to think about next election cycle** — Post the 2011 election, Singapore's growth rates were lowered as policies (labor & immigration issues) were adjusted for greater social inclusiveness. Singapore's ageing population has also boosted funding needs to spur health and social spending. Demographic-linked issues will be a key issue for the next election cycle in 2015-16.

Singapore: Top Buys and Top Sells

	Ticker	Rating	Price (Jun. 6)	Target Price	Yield (%)	ETR (%)	2014E P/E (x)	2014E P/BV (x)	2014E ROE (%)
Top Buys									
DBS	DBSM.SI	Buy	S$17.08	S$19.00	4.1	15.3	10.9	1.2	11.0
Highest NIM/earnings leverage to eventual SGD rates rise									
Keppel Corp	KPLM.SI	Buy	S$10.75	S$13.35	4.2	28.4	12.2	1.9	16.0
Rig cycle intact despite oil-price volatility									
Keppel Land	KLAN.SI	Buy	S$3.46	S$4.05	3.8	20.8	12.6	0.7	6.0
Sustainable pre-sales from China; potential divestment of MBFC Tower 3									
NOL	NEPS.SI	Buy	S$0.98	S$1.17	0.0	20.0	nm	1.0	-1.0
Under-appreciated APL logistics									
Wilmar	WLIL.SI	Buy	S$3.24	S$3.87	2.0	21.5	12.3	1.0	8.7
Conduit for Asia's food needs, and now part of Indonesia's energy needs									
Top Sells									
Cosco	COSC.SI	Sell	S$0.72	S$0.60	1.4	-15.3	39.6	1.2	3.0
Subdued margin outlook									
Starhub	STAR.SI	Sell	S$4.22	S$3.55	4.7	-11.1	18.6	55.7	nm
Premium valuations, weak EPS growth outlook and unattractive yield spread									

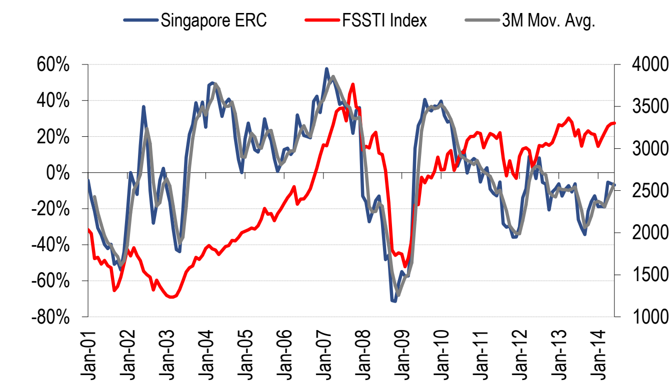
Source: Citi Research estimates

Figure 1. Singapore Electronics Exports % Chg YoY vs STI



Source: Bloomberg, CEIC, Citi Research

Figure 2. Singapore Earnings Revision Count



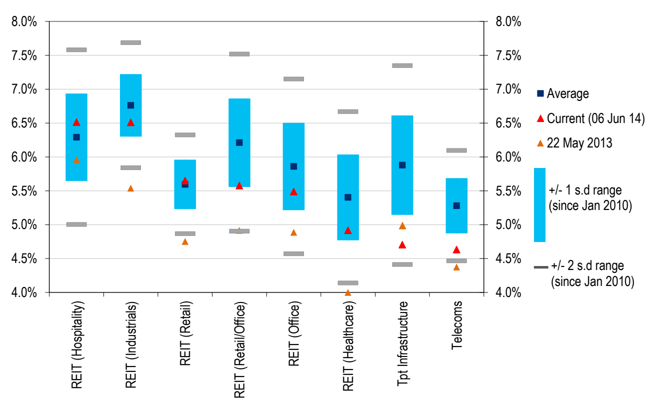
Source: Factset, Citi Research

Figure 3. Singapore General Elections – Key Statistics

	1988	1991	1997	2001	2006	2011
Total no. of parliamentary seats	**81**	**81**	**83**	**84**	**84**	**87**
Walkover	11	41	47	55	37	5
Contested	70	40	36	29	47	82
% contested	**86%**	**49%**	**43%**	**35%**	**56%**	**94%**
Seats won by						
PAP	80	77	81	82	82	81
Opposition	1	4	2	2	2	6
Total no. of valid votes (mn)	**1.34**	**0.78**	**0.72**	**0.63**	**1.12**	**2.01**
PAP	0.85	0.48	0.47	0.47	0.75	1.21
Opposition	0.49	0.31	0.25	0.15	0.38	0.80
PAP's share of valid votes (%)	**63.2**	**61.0**	**65.0**	**75.3**	**66.6**	**60.1**
ppt chg from previous election	-1.6	-2.2	4.0	10.3	-8.7	-6.5
PAP led by	Lee Kuan Yew	Goh Chok Tong	Goh Chok Tong	Goh Chok Tong	Lee Hsien Loong	Lee Hsien Loong
STI % chg 1-mth post polling date	**-4.4%**	**-3.3%**	**+3.2%**	**+11.9%**	**-9.0%**	**0.5%**

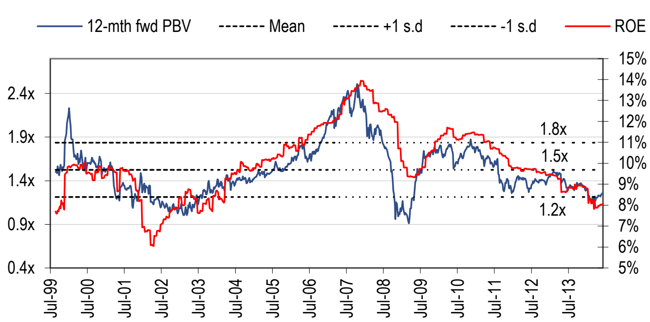
Source: Citi Research, Datastream, Elections Department

Figure 4. SG Dividend Plays – Current Dividend Yield vs Mean and SD



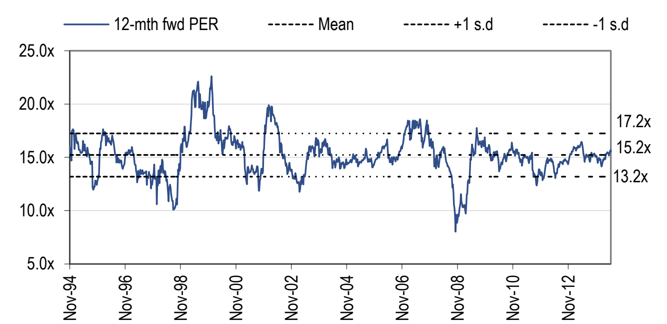
Source: Datastream, Citi Research

Figure 5. STI 12M Forward PB vs ROE



Source: Datastream, Citi Research

Figure 6. STI 12M Forward PER



Source: Datastream, Citi Research

Taiwan

Cross-straits at Cross-roads

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- **Window for passing key economic policy legislation is closing** — The December 2014 mayoral elections mark the end of the nearly 3-year period with no distractions from elections during which the Ma Administration could have ratified the key cross-strait trade treaties with China. There will be another opportunity in the first 5 months of next year, but the LY will need to pass a new cross-strait negotiation oversight bill and then ratify the Services and the Goods Agreements within that time. Moreover, it is uncertain as to whether the Services Agreement will need to be renegotiated and the Goods Agreement has yet to be completed.

- **New KMT leadership emerging** — Low poll ratings for President Ma are opening an opportunity for a new generation of KMT leaders to emerge. The results of the New Taipei and Taipei City elections will impact the success of these new leaders' ability to gain national office and KMT party influence. New Taipei City mayor Eric Chu is a likely presidential candidate; in a TVBS poll earlier this year, Chu polled the highest among four potential KMT candidates, drawing to a tie with likely DPP presidential candidate Tsai Ing-wen. However, if he chooses not to run for re-election in favor of a presidential bid, he risks losing this key election to the DPP.

- **Market implication is for ST slowing of economic drivers** — The correlation of progress on cross-strait negotiations and Taiwan economic performance (via capex spending, wage growth and then consumption) is significant, suggesting that the current delay could impact market earnings potential. However, liquidity and demand for equities remain buoyant and the prospects for longer term political consensus developing within Taiwan should help support share prices in this interim period. Thus, be prepared for PE multiple expansion.

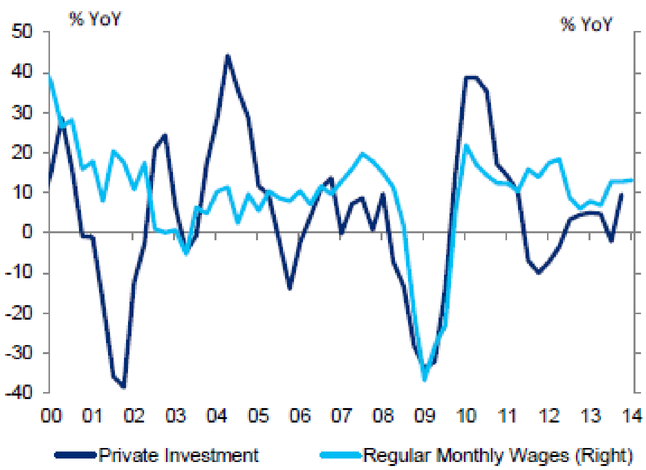
- **Smartphone and tablets beginning to offset decline in PC demand** — The launch of the iPhone 6 as well as the growing market for Chinese branded and unbranded smartphones have sparked the tech sector after nearly three years of underperformance. Moreover, based on historical correlations, any USD yield increases will allow for further TWD weakness, further supporting tech names.

Taiwan: Top Buys and Top Sells

	Ticker	Rating	Price (Jun. 6)	Target Price	Yield (%)	ETR (%)	2014E P/E (x)	2014E P/BV (x)	2014E ROE (%)
Top Buys									
Catcher	2474.TW	Buy/1H	NT$284.00	NT$355.00	1.8	26.8	14.3	2.5	18.7
New capacity expansion based on significant multi-year client commitment									
Hon Hai	2317.TW	Buy	NT$93.20	NT$112.00	1.9	22.1	10.0	1.3	14.6
Improving margin visibility and substantial Apple product cycle for iPhone 6 and iTV									
Largan	3008.TW	Buy	NT$2,045.00	NT$2,200.00	1.4	9.0	19.7	6.4	38.1
The lens market is in a long-term spec upgrade trend and Largan as the leader can cherry-pick orders									
President Chain Store	2912.TW	Buy	NT$235.50	NT$260.00	2.5	12.9	26.4	8.4	35.1
Accelerating store expansion for the domestic 7-11 business and overseas subs (Philippine Seven, Starbucks China) along with improving margin outlook									
Top Sells									
Hermes Microvision	3658.TWO	Sell	NT$1,220.00	NT$865.00	1.3	-27.8	28.3	7.4	28.7
Revenue to decelerate despite growing semiconductor industry capex									
Quanta Computer	2382.TW	Sell	NT$80.10	NT$64.00	4.7	-15.4	16.3	2.4	15.1
Street is overly-optimistic on the cloud-server contribution and iWatch shipments in 2014									

Source: Citi Research estimates

Figure 1. Capital Spending vs Monthly Wage Growth

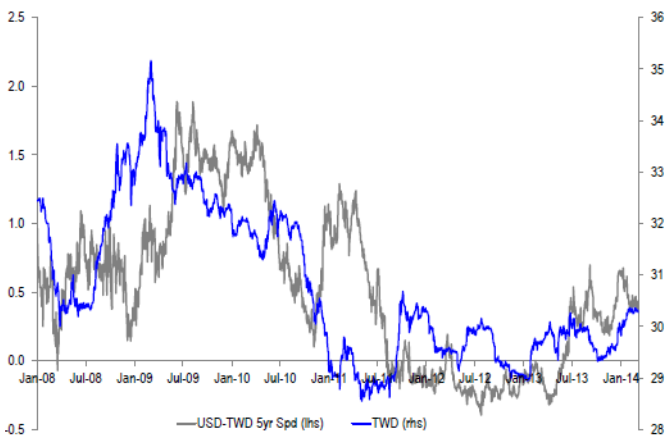


Source: CEIC, Citi Research

Figure 2. Monthly Wage vs Retail Sales Growth

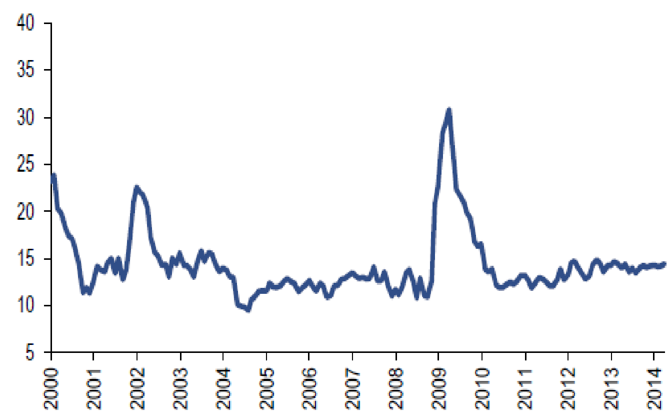
Source: CEIC, Citi Research

Figure 3. USD/TWD 5yr Bond Yield Spread vs TWD



Source: Bloomberg, Citi Research

Figure 4. Forward PE Ratio



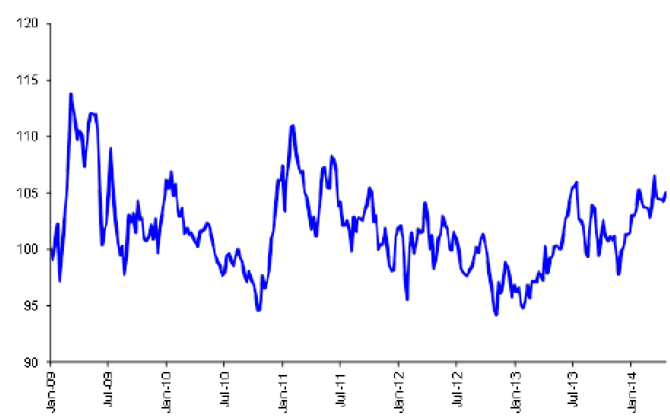
Source: MSCI, Citi Research

Figure 5. Election Calendar

Date	Election	Key Issues		
December 2014	City Mayors	Taichung and New Taipei are important swing elections		
November 2014	Legislative Yuan	Current Mix	Blue:	61%
			Green	38%
March 2016	Presidential	Likely Candidates	KMT:	Vice President Wu Den-yih
				New Taipei Mayor Chu Li-lun
			DPP:	DPP Chairman Tsai Ing-wen

Source: Citi Research

Figure 6. Taiwan Stock Market Relative to Asia ex-Japan



Source: Bloomberg, Citi Research

Thailand

Will This Time Be Different?

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- **Street protest led to coup; junta exit strategy is key** – After protests against the amnesty bill led to government stagnation and election impasse, the army decided to take over by staging a coup in May. NCPO (National Council for Peace and Order) is in charge of making key decisions. Next steps will be the establishment of a reform assembly, pushing through reform agendas, and return to normal electoral politics. NCPO expects this to take at least 15 months. (See also Thailand Strategy - At a Crossroads: Will this Time Be Different?)

- **Injection of rice money provides near-term boost; income still issue** – NCPO has been quick to accelerate Bt92bn rice pledge payments to farmers, hoping to revive the rural economy. However, given that new crop will be sold at a substantial discount to prior year under pledging price, we are concerned on the income effect down the road and consumption recovery may be short-lived.

- **Excitement around review of infra projects** – NCPO brought Bt2trn infra plan and Bt350bn water projects back for consideration. This caused excitement on GDP upside and certain stocks to run (contractors, consumers). Fiscal deficit may approach limit; hence, actual progress could be slower than expectation.

- **Economic and earnings expectations; bottoming out** – Military intervention seems to at least forestall further stalemate from FY15 budget gridlock. This should limit further GDP and earnings downgrades. However, pace of recovery (11% 15E EPS growth) may not provide room for big upgrades considering high consumer debt and limited spending vs 2010 and 2012 recoveries.

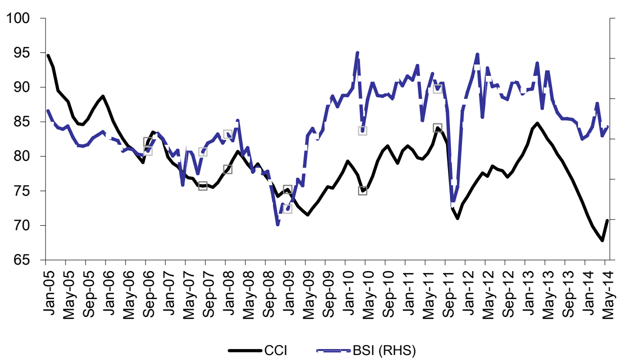
- **Buy selectively; downside remains** – Given the strong run on hopes of a domestic demand recovery despite unclear execution plan and challenges / priorities required, we maintain our cautious view and hold to only a few quality names. While market may see 'event driven' moves, esp. on reform policy, we believe it is too early for structural improvements that might trigger a re-rating.

Thailand: Top Buys and Top Sells

	Ticker	Rating	Price (Jun. 6)	Target Price	Yield (%)	ETR (%)	2014E P/E (x)	2014E P/BV (x)	2014E ROE (%)
Top Buys									
ADVANC	ADVANC.BK	Buy	Bt240.0	Bt270.0	5.3	17.8	19.0	15.4	81.8
Still on 3-year earnings uptrend from 3G conversion; market share gain after network rollout									
BBL	BBLf.BK	Buy	Bt191.5	Bt210.0	4.0	13.6	10.0	1.2	11.9
Laggard bank; recovery in corporate loans									
KBANK	KBANKf.BK	Buy	Bt199.5	Bt215.0	2.5	10.3	10.7	1.9	18.9
Consistent earnings from non-interest income									
PTTGC	PTTGC.BK	Buy	Bt67.0	Bt87.7	4.8	35.7	8.8	1.2	13.9
Laggard with attractive yield									
SCC	SCC.BK	Buy	Bt436.0	Bt532.0	3.4	25.5	13.4	2.9	22.8
Cement demand should bottom									
Top Sells									
IVL	IVL.BK	Sell/3H	Bt27.0	Bt17.4	0.7	-34.8	42.1	2.1	5.0
Stock has run ahead of ROE improvement									
SIRI	SIRI.BK	Sell/3H	Bt2.0	Bt1.7	7.3	-6.0	9.1	0.9	17.4
Launches to be subdued for next 1-2 years									
TISCO	TISCO.BK	Sell	Bt42.0	Bt35.0	5.1	-11.6	7.9	1.3	17.8
Strong rebound post-coup without real improvement in auto business									

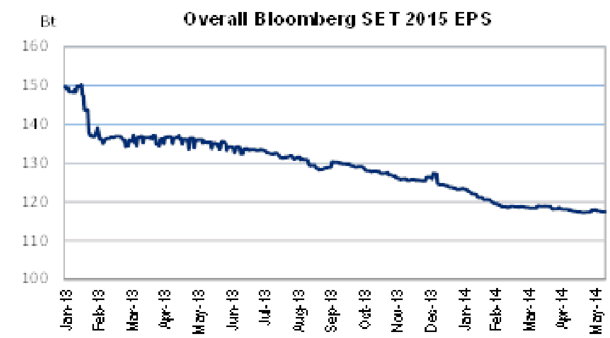
Source: Citi Research estimates

Figure 1. Consumer and Business Confidence: Recent Uptick After Year-Long Slump



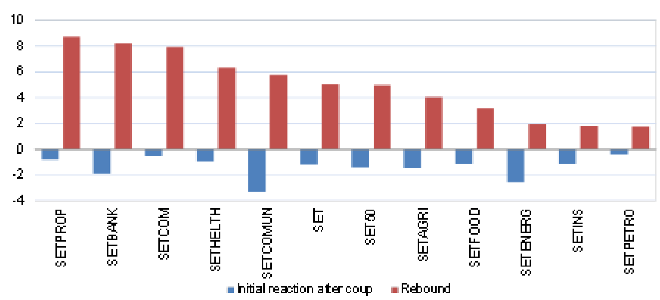
Source: UTCC, BOT and Citi Research

Figure 2. Earnings Revisions Look to Be Bottoming But Scope For Upward Revisions Unclear



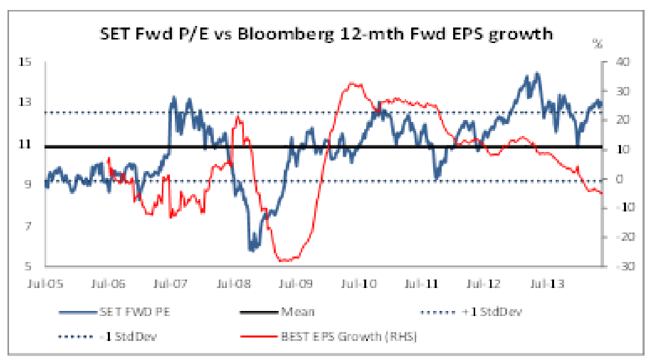
Source: Bloomberg and Citi Research

Figure 3. High Beta Rally in Anticipation of Domestic Demand Recovery



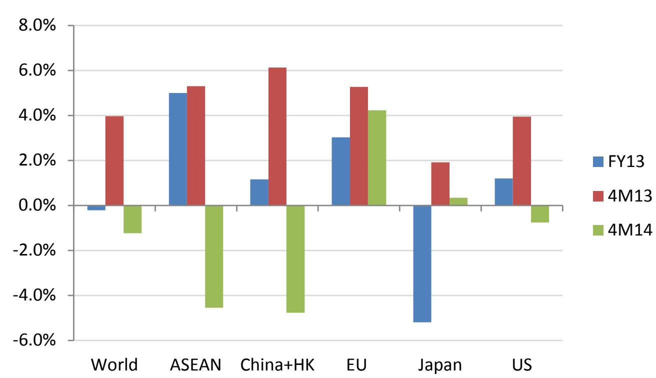
Source: SETSmart and Citi Research

Figure 4. Valuation: Pricing in Recovery



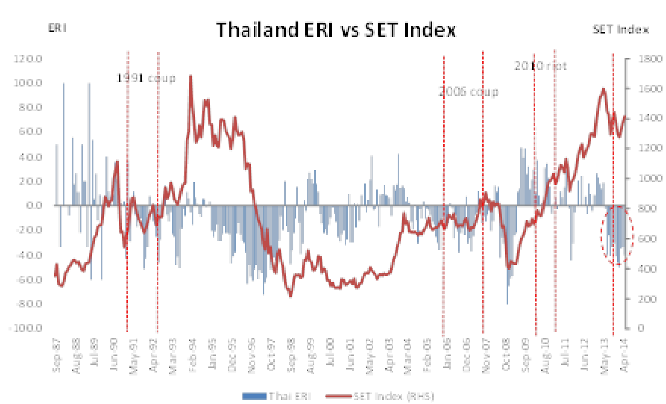
Source: Bloomberg and Citi Research

Figure 5. Export Recovery Remains Patchy; Drag From China



Source: Ministry of Commerce

Figure 6. SET and Past Coups: Earnings Remain Key Driver



Source: SET, FactSet

Sector

Autos & Auto Parts

Overly Punished DM Asia, Healthily Growing EM Asia

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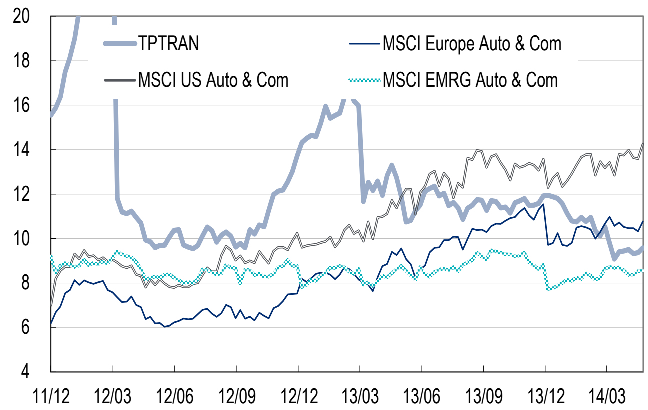
- **Japan: oversold shares offer buying opportunity** — PERs of Japanese automakers have been rapidly falling since last December, which we ascribe to fears of yen strength, of intensifying competition in North America, and of the consequences of the consumption tax hike in Japan. However, we think shares have been oversold and that there are good buying opportunities, given that automakers are still competitive at ¥95/$ and can deliver ample cash flow.
- **Korea: a mixed-bag** – Stronger KRW (vs. USD & JPY) has been the backdrop of lackluster share prices YTD. While a few headwinds remain (currency direction, labor negotiation), fundamentals and earnings momentum should improve into 2H14E, typically for HMC, on new products materializing. Capacity expansion announcement is still a wildcard, which could lead to multiple-driven price performance. HMC and Wia (011210.KS; W185,500; 1) are our top picks.
- **China: normalized growth on rising base** – We expect some growth deceleration in 2H14 on a high base but believe fundamentals remain healthy from a SAAR perspective (2014: 11% y-y vs. 5M14; 15%). Market concerns on auto sales correlation with property look overdone. We like Dongfeng Motor for margin recovery plus new product contribution from the likes of X-trail, and we have a Sell on BYD for its rich valuation and declining traditional motor business.
- **India: positive on 4-wheelers** – We expect a recovery after 9-12 months in both passenger cars and heavy trucks. Anecdotally, some green shoots are sprouting (dealers report more enquiries, conversion ratios have improved). Freight rates have picked up as well – which augurs well for CVs. Our top pick remains Tata Motors (JLR's product cycle, domestic turnaround and valuations), followed by Maruti Suzuki (MRTI.BO; Rs2,470.85; 1) and M&M (MAHM.BO; Rs1,234.90; 1).
- **Indonesia: still positive growth in 2014** – We expect 2W and 4W markets to grow by 4% and 13% respectively in 2014. Competition is limited in 2W volume (61% market share for Astra), but more intense in the 4W market with Astra (Toyota and Daihatsu) facing up in the low MPV segment against Honda's Mobilio and Suzuki's Ertiga. However, Astra's LCGC has come to the rescue with strong market share and is performing better than expected.

Autos & Auto Parts: Top Buys and Top Sells

	Ticker	Rating	Price (Jun. 6)	Target Price	Yield (%)	ETR (%)	2014E P/E (x)	2014E P/BV (x)	2014E ROE (%)
Top Buys									
Astra International	ASII.JK	Buy	Rp7,200	Rp8,250	3.4	18.0	13.2	3.1	24.7
Cheap valuation on 2015E PER of 12x; a proxy for the Indonesian market with a strong track record and good execution									
Dongfeng Motor	0489.HK	Buy	HK$12.22	HK$15.00	2.2	25.0	7.0	1.2	17.8
Margin recovery with decline in dealers' rebate ratio and utilization rate improvement; Nissan's strong commitment to China; cheap valuation									
Fuji Heavy	7270.T	Buy	¥2,791	¥3,900	1.9	41.6	10.5	2.8	30.4
Margins to improve through FY3/16 E on the new Legacy, sales incentives being kept low, inventory scant, capacity upgrades this summer									
Hyundai Motor	005380.KS	Buy	W225,000	W320,000	0.9	43.1	5.4	0.8	16.4
Positive model cycle mainly backed by New Sonata and further expected capacity expansion announcement (likely US) should be key positives for the share price									
Tata Motor	TAMO.BO	Buy	Rs437	Rs486	0.1	11.3	8.0	2.0	28.0
Strong product lineup at Jaguar Land Rover augers well for volume as well as profitability. Demand in China should remain healthy with Chery JV further buoying volumes									
Top Sell									
BYD	1211.HK	Sell	HK$40.2	HK$39	0.2	-2.9	80.3	3.4	4.2
Rich valuation embedding high expectation for its EV business while its traditional motor business has been continuously declining in sales volume									

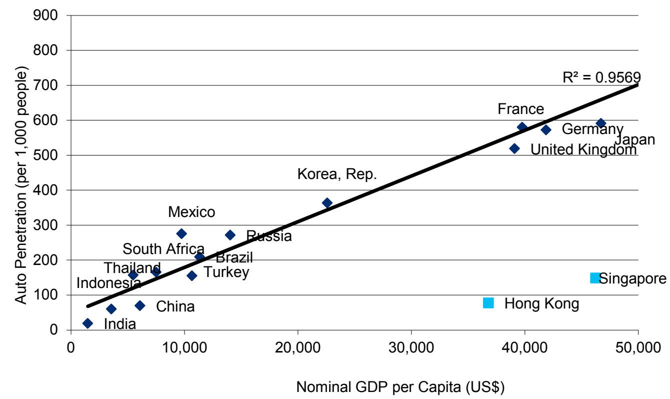
Source: Citi Research estimates

Figure 1. Global Automaker and Auto Parts Maker Valuations



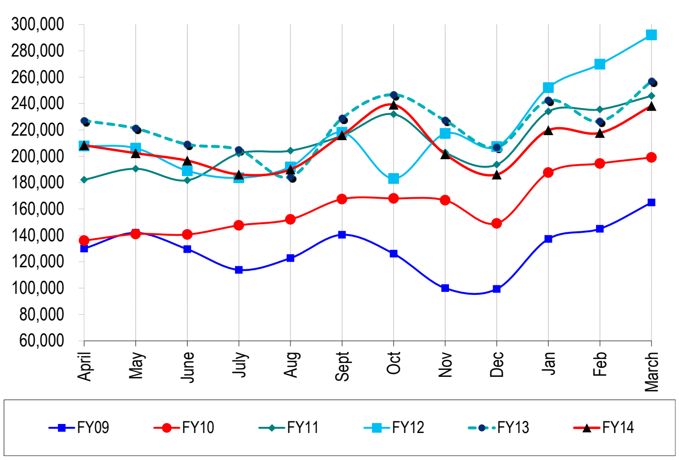
Source: Bloomberg, Citi Research

Figure 2. Global Auto Penetration vs. Nominal GDP per Capita (2012)



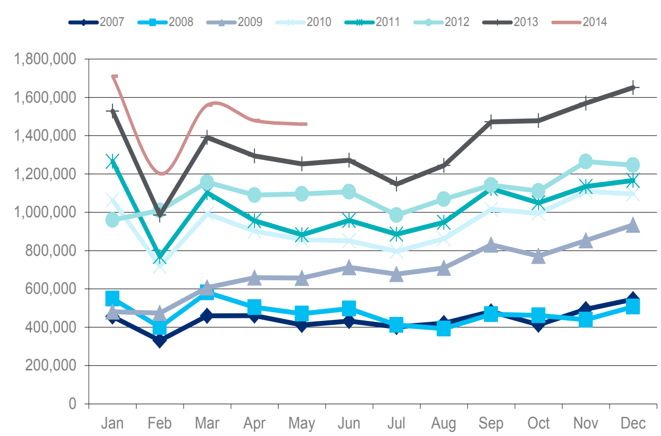
Source: World Bank, Citi Research

Figure 3. Indian PV: Monthly / Annual Domestic Volumes (units)



Source: SIAM

Figure 4. China PV: Monthly / Annual Domestic Volumes (units)



Source: CAM

Banks

Mostly Cloudy, Partly Sunny

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Salman Ali / Indonesia

Joanne Lee / Korea

Robert Kong / Malaysia & Singapore

Minda Olonan / Philippines

Kritapas Siripassorn / Thailand

- **Selectivity the prudent course given array of uncertainties** – We still see continued pressure in emerging markets from a very moderate but gradual tapering by the US Fed in 2014/15. In the midst of uncertainties regarding credit growth, the interest rate environment, regulation etc, we recommend a selective approach in the pan-Asian banking sector.

- **Divergence of share price performance** – Since the beginning of the year, share prices of Asian banks have shown large divergences in performance, depending on region. Past performance may provide the investment opportunities; weak performers like the banks in Japan and Hong Kong look attractive.

- **Japanese banks poised for snapback** – Year-to-date, Japanese bank shares have been the weakest performers, reflecting pessimism about core earnings growth and the absence of notable returns to shareholders. As we expect NII to rise in the current year, thanks to loan growth, and bank managements to focus more on shareholder returns, after confirming they are well capitalized, we should see a substantial bounce-back in Japanese bank shares.

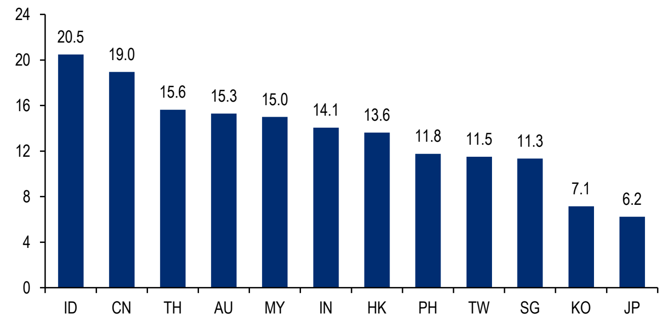
- **Asian bank preferences** – Overweight: Japan, Thailand, HK. Neutral: China, Australia, Singapore, Indonesia, Taiwan. Underweight: Korea, India, Malaysia, Philippines.

Banks: Top Buys and Top Sells

	Ticker	Rating	Price (Jun. 6)	Target Price	Yield (%)	ETR (%)	2014E P/E (x)	2014E P/BV (x)	2014E ROE (%)
Top Buys									
Bank Negara ID	BBNI.JK	Buy	Rp4,830.0	Rp5,450.0	2.2	15.0	9.1	1.5	17.8
Only Buy among Indonesia banks on relative valuation: low cost of funds (stable NIMs), good fee momentum, controlled opex growth									
DBS	DBSM.SI	Buy	S$17.1	S$19.0	4.7	15.9	9.4	1.1	11.9
Multiple business engines have driven record quarterly profits; beneficiary of eventual global rates normalization with its China exposure									
Hang Seng Bank	0011.HK	Buy	HK$128.1	HK$140.0	4.4	13.7	14.4	2.2	16.0
Non-consensus ROE re-rating story via future rate hike and possible disposal of Industrial Bank stakes									
Kasikornbank	KBANKf.BK	Buy	Bt199.5	Bt215.0	2.9	10.7	9.4	1.7	18.9
Resilient business model with non-interest income; also prudent lending in upcycle should help in slowdown									
MUFG	8306.T	Buy	¥600.0	¥800.0	2.7	36.0	8.5	0.6	7.1
Strong momentum in overseas profits will lead to progress in core earnings. In better position to implement shareholder return policies									
Top Sells									
Bank Central Asia	BBCA.JK	Sell	Rp11,050.0	Rp8,150.0	1.3	-24.9	14.8	3.0	21.7
Expensive valuations with declining CASA market share and narrow fee income base									
CIMB	CIMB.KL	Sell	RM7.2	RM6.8	4.0	-2.4	11.0	1.5	13.8
Downside to our target price looks limited, but we still see near-term ROE weakness due to challenges in Indonesia and integration of recent acquisitions									
IndusInd Bank	INBK.BO	Sell	Rs544.0	Rs420.0	0.7	-22.1	17.7	2.8	17.1
Concerns around concentrations in business model									

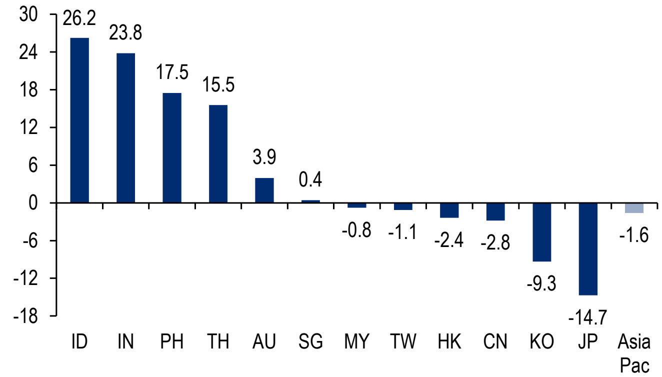
Source: Citi Research estimates

Figure 1. Asia Banks: 2014E Return on Equity



Source: Company Reports and Citi Research Estimates

Figure 2. Share Price Performance 2014Ytd (%)



Source: DataStream, Citi Research

Figure 3. Share Price of Top Buy Stock: MUFG

Source: Citi Research

Figure 4. Share Price of Top Buy Stock: Kasikornbank

Source: Citi Research

Figure 5. Share Price of Top Buy Stock: Hang Seng Bank

Source: Citi Research

Figure 6. Share Price of Top Buy Stock: DBS

Source: Citi Research

Conglomerates

Valuation Remains Cheap; Fosun Is Our Top Pick

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- **Valuation remains undemanding** – Our Hong Kong and China conglomerate universe is up 2% YTD (vs Hang Seng Index's -1%) and is trading at a 28% discount to estimated NAV, nearly half a standard deviation below the 20% historical average discount.

- **Fosun** – We continue to rate Fosun as one of our top picks in the conglomerate space as it will not only enjoy the appreciation of Fosun Pharma but also has multiple catalysts for further re-rating in 2H14. Catalysts include 1) being a potential candidate of private bank, 2) owning a €12bn war chest after CSS acquisition and 3) further update on Cainiao. Fosun is now trading at 23% discount to NAV (vs historical average of 22%) or 1.1x FY14E P/B.

- **Wharf** – Wharf is a quality conglomerate with solid recurring cash flow of ~HK$9bn from its core investment portfolio in HK. We believe the group remains attractive as it ramps what will be a 2.4m sq.m. commercial portfolio in Mainland China. Wharf's balance sheet is strong (net gearing ratio improved to 20% vs 22% a year ago). After the recent sell-off, Wharf is now trading at a ~50% discount to NAV (vs 37% historically) or 0.5x FY14E P/B.

- **CITIC Pacific** – In April 2014, CITIC Pacific announced additional details on the acquisition of CITIC Limited. The consideration would be RMB226.9bn (roughly 1.0x 2013 P/B). Based on our estimates, CITIC Pacific's pro forma NAV could rise to HK$11.79, still implying that the stock is trading at a rich ~14% NAV premium. CITIC Pacific is our Top Sell in the space.

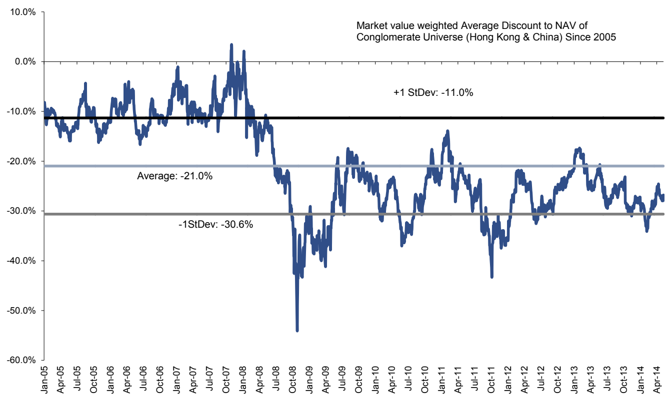
- **Singapore** – Keppel is a play on a global E&P cycle in which NOCs play an increasing role in capex due to their increasing emphasis on energy self reliance. Keppel is the only global shipyard that is able to fulfill demands by NOCs for local content requirements given its "Near Customer Near Market" strategy. Citi has an above-consensus order win estimate of S$6.5bn (vs S$2bn currently secured). The fundamental outlook is underpinned by [1] its record order backlog (1Q14: S$14.4bn), which has been largely driven by demand for the group's proprietary jackups; and [2] superior operating margin outlook in excess of 14%. In addition, we believe O&M operating margins could surprise on the back of rising revenue contributions from higher priced rigs.

Conglomerates: Top Buys and Top Sells

	Ticker	Rating	Price (Jun. 6)	Target Price	Yield (%)	ETR (%)	2014E P/E (x)	2014E P/BV (x)	2014E ROE (%)
Top Buys									
Fosun International	0656.HK	Buy	HK$9.41	HK$11.29	1.6	21.4	11.7	1.1	10.3
Multiple catalysts for further re-rating in 2H14									
Keppel	KPLM.SI	Buy	S$10.75	S$13.35	4.2	28.4	12.2	1.9	16.0
Only global shipyard able to fulfill demands by NOCs for local content requirements									
Wharf Holdings	0004.HK	Buy	HK$55.25	HK$67.50	3.6	25.8	12.6	0.5	4.5
Trading at ~50% discount to NAV; sizeable investment property pipeline and strong pre-sales of development properties in China; solid rental income in Hong Kong									
Top Sell									
CITIC Pacific	0267.HK	Sell	HK$13.42	HK$6.00	2.6	-52.7	23.9	0.6	3.0
Valuation unattractive: trading at ~14% premium to pro forma NAV									

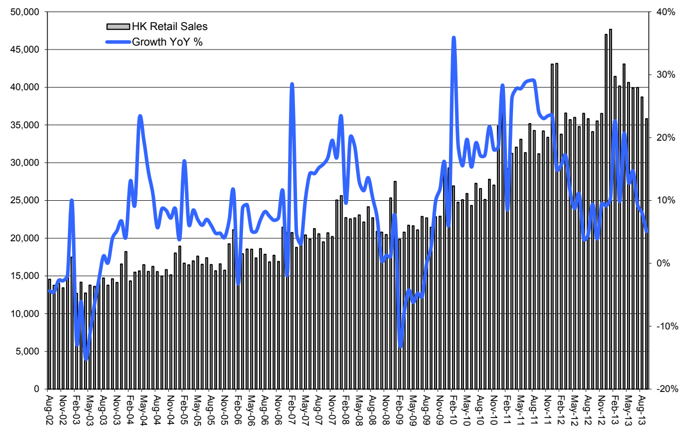
Source: Citi Research estimates

Figure 1. Regional Conglomerates – Price to Mean NAV Discount



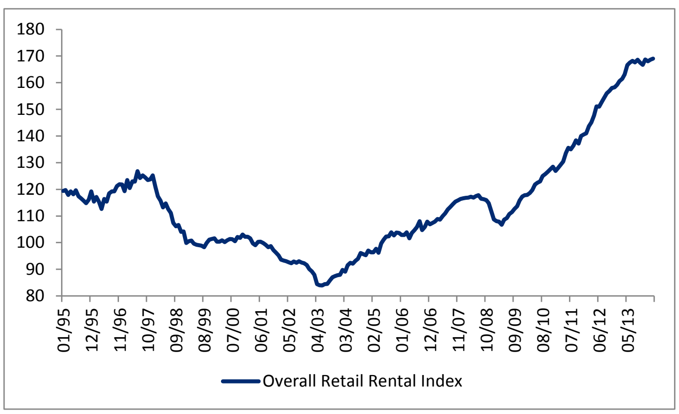
Source: Citi Research Estimates

Figure 2. HK Retail Sales by Value (HK$M) (2002 – Current)



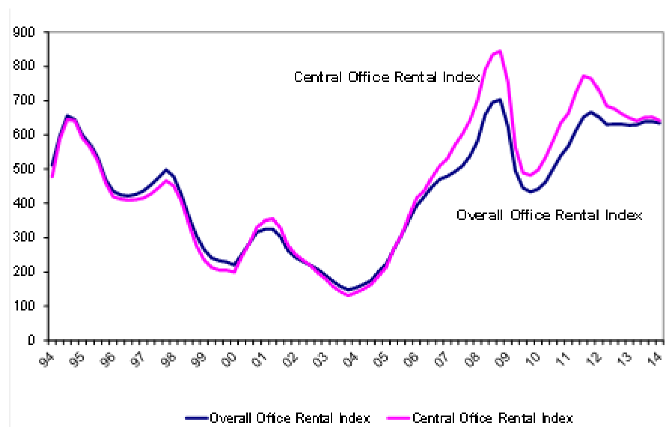
Source: CEIC, Citi Research

Figure 3. HK Retail Rental Index



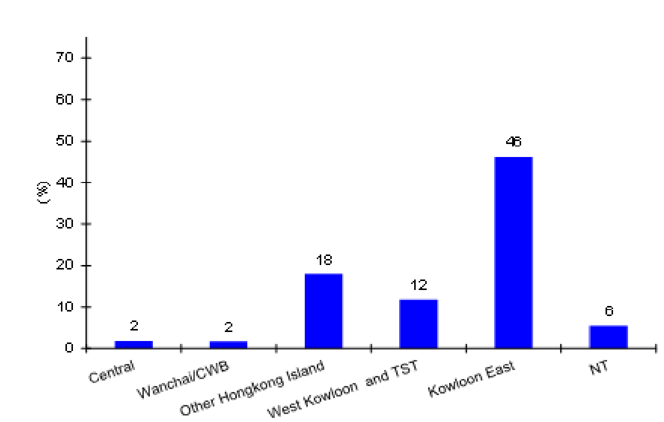
Source: RVD; Citi Research

Figure 4. HK Office Rental Index



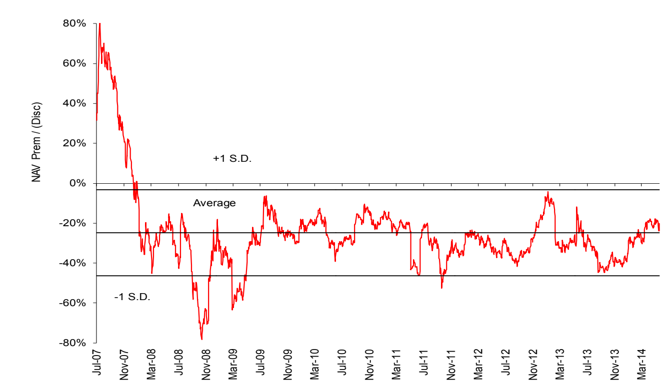
Source: Jones Lang LaSalle, Citi Research

Figure 5. HK Property – 2014-2017 New Supply as a % of Existing Grade-A Office Space



Source: Rating and Valuation Dept, Citi Research

Figure 6. Fosun – NAV Discount



Source: Citi Research Estimates

Consumer

Slowing Consumer Spending Trends Make Us Cautious

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Peter Kurz / Taiwan

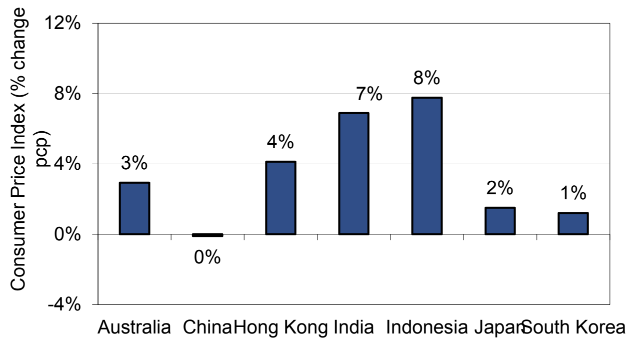
- **Look for market share gains, not market growth** – Emerging market consumer spending growth is slowing, while developed markets in Australia and Japan have been above trend. With slowing consumer demand, our top picks are those companies that have a good track record of winning market share.
- **Australian spending looks better...but some pressure building** – Australian retail spending was strong in the first four months of 2014, which contrasts the past three years. However, the Government budget will drag on incomes. We prefer retailers that can take market share, such as Super Retail Group.
- **China and Hong Kong see slower sales** – Retail sales trends have been weak and weighed on profit margins. As retailers cycle weaker trends, we expect some improvement, which could provide a better outlook in 2015E. Given lingering sales weakness and lack of earnings visibility, the risk/ reward should be more favorable for companies with earnings momentum. Our top pick within retailing is Anta Sports.
- **Indian demand also subdued** – Overall consumption in India's grocery sector was ~9.5% in CY13 vs. 18.1% in CY12. Per press reports, positive signs have been emerging, with growth above 20% in segments like packaged water and ice creams (for key players). Generally, management commentary is subdued (in line with Mar-14 Q results). We remain negative on the sector as a whole, given weak fundamentals and high valuations. Our top Buys are ITC and Emami (EMAM.BO; Rs482.00; 1), which trade at healthy discounts to the broader peer group.
- **However, positive consumption trends in Japan** – On 1 April 2014, Japan hiked its consumption tax to 8% from 5%, the first increase since 1997. In March revenue rose 10% YoY for food products and soft drinks, with revenue up 20% for alcoholic beverages and 60% for cosmetics. Trends, post the tax hike, have been encouraging. The rise in wages and the wealth effect owing to higher equity prices have started to positively impact consumer discretionary stocks, particularly premium products. We are seeing market share gains for premium brands like Asahi, within its beer range.

Consumer: Top Buys and Top Sells

			Price	Target	Yield	ETR	2014E		
	Ticker	Rating	(Jun. 6)	Price	(%)	(%)	P/E (x)	P/BV (x)	ROE (%)
Top Buys									
Anta Sports Products	2020.HK	Buy	HK$11.44	HK$14.00	4.3	26.7	16.5	3.0	18.9
Continues to win market share and improve productivity for its exclusive distributors. Recent order book growth has been in the double-digits									
Asahi Group	2502.T	Buy	¥3,080	¥4,000	1.6	31.4	19.4	1.7	8.7
Capital-management initiatives underway. Asahi's Japanese beer sales have been reported as good since the tax hike and it is winning market share with premium products									
ITC	ITC.BO	Buy	Rs336.70	Rs410.00	2.0	23.8	27.6	9.1	35.8
Steady cigarette business combined with improved margins in other segments. Leads to mid-to high-teens profit growth and increasing FCF yield support									
Super Retail	SUL.AX	Buy	A$8.53	A$10.80	4.7	31.3	14.1	2.1	15.7
Recent weakness looks a buying opportunity for a company with the opportunity to grow market share and increase its direct sourcing capabilities									
Top Sells									
Hindustan Unilever	HLL.BO	Sell	Rs634	Rs545	1.9	-12.2	35.8	32.0	101.1
Weak volume growth and increasing reliance on cost cuts to support earnings. Given high PE ratio, we see downside risk									
Wesfarmers	WES.AX	Sell	A$42.42	A$35.80	5.3	-10.3	20.0	1.9	11.1
We expect weaker earnings growth, held back by lower coal prices and weak earnings at Target. High PE looks unjustified given risks and growth prospects									

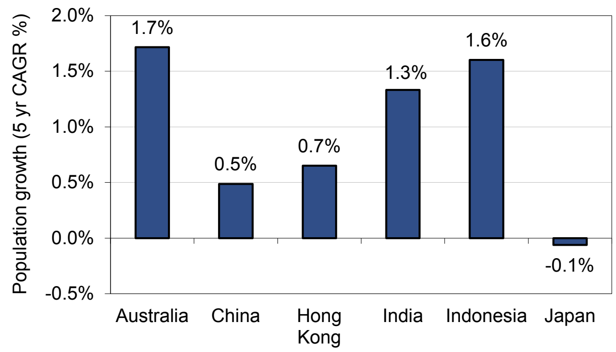
Source: Citi Research estimates

Figure 1. CPI By Country



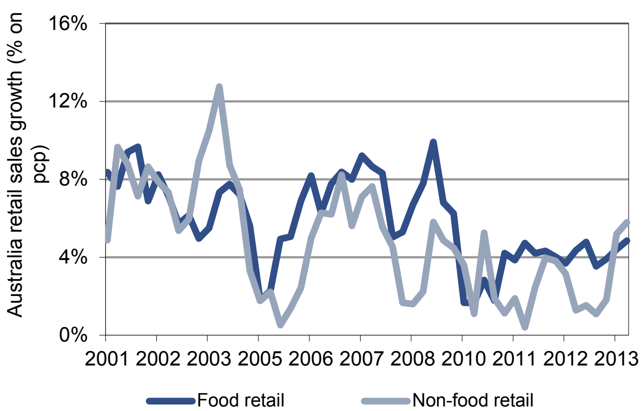
Source: Datastream, March 2014 vs March 2013

Figure 2. Population Growth By Country (avg annual five years)



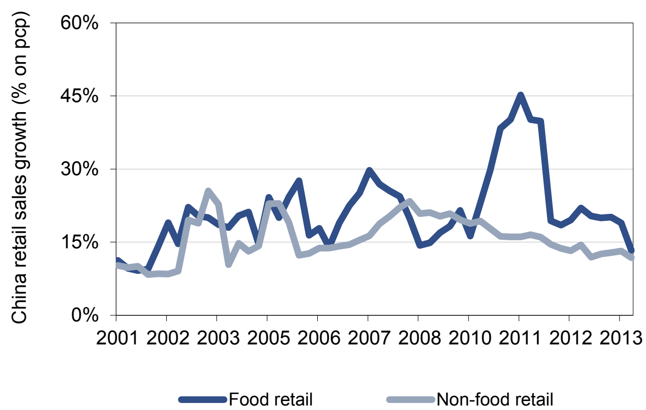
Source: Datastream, Population 5-yr CAGR to December 2013

Figure 3. Australian Retail Sales Trends



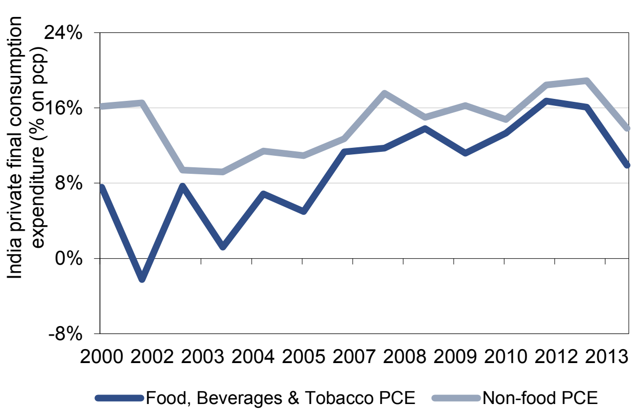
Source: Datastream, Quarterly data to March 2014

Figure 4. China Retail Sales Growth



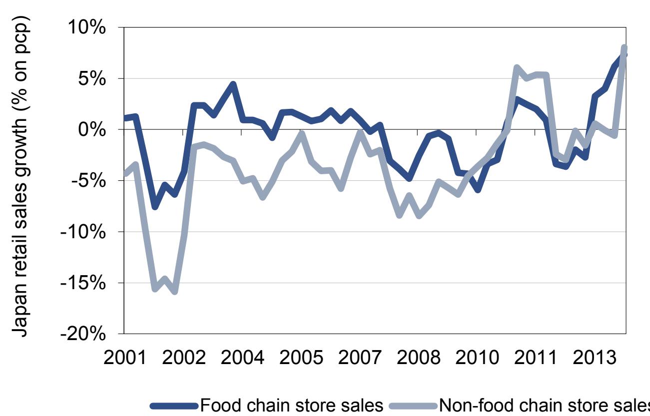
Source: Datastream, Quarterly Data to March 2014

Figure 5. Indian Consumption Expenditure Growth



Source: Datastream, Annual data to June 2013

Figure 6. Japan Retail Sales Growth



Source: Datastream, Quarterly data to March 2014

Gaming

Bullish: EBITDA Resilient, Headline GGR Irrelevant

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- **Macau** – With an all-time record 40% of revenues being generated in the mass market (+37.4% YTD, vs. our forecast of +35% in 2014), up to 75% of Macau EBITDA will come from this high-margin business. In our view, investors' fixation on weekly headline GGR is now less relevant, as 60% of headline GGR is from the low-margin VIP business (+7% YTD, vs. our forecast of +2.5% in 2014). Net-net, our Macau GGR FY14 forecast is at +13% YoY. With two new property openings in 2015, Macau is setting itself up for a strong 2015 given the easy 2014 comps. The recent noise has hit valuations and with GGR projections falling across the street, expectations are low. Although there are few short-term catalysts, it should not be difficult to beat these new lowered expectations.

- **Prefer mass-focused Cotai plays** – In FY14, we expect Cotai will generate 7% and 37% YoY growth in VIP and mass, respectively (vs. -1% and 31% YoY in Peninsula). During 4M14, Cotai mass continued to outperform Peninsula and grew 45% YoY (vs. +31% YoY in Peninsula). In our view, the migration of GGR and EBITDA towards Cotai will continue (with Cotai expected to capture 46% and 60% of 2014 Macau's GGR and Macau's EBITDA, respectively).

- **Philippines** – In 2014, we expect Philippines GGR to reach US$2.3bn, +20% YoY. By 2015, we expect GGR to grow to US$3.0bn (+34% YoY), as the opening of City of Dreams Manila (as well as improving volume at Solaire) should lead to the creation of critical mass at Entertainment City and help expand the market. We continue to rank MCP as our top pick in Philippines gaming.

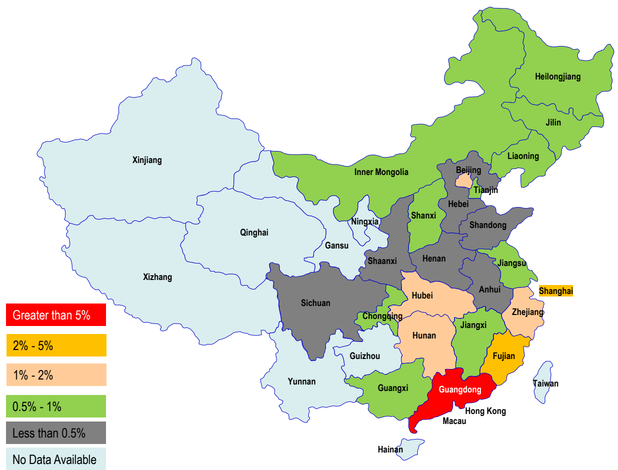
- **Australia** – Australian GGR is showing a mild recovery in FY14E as disposable income on the East Coast improves. Regulatory changes in QLD are also supporting improved trends. Our top Buy is Aristocrat as its broadened product portfolio is underpinning market share growth.

Gaming: Top Buys and Top Sells

	Ticker	Rating	Price (Jun.06)	Target Price	Yield (%)	ETR (%)	2014E P/E (x)	2014E P/BV (x)	2014E ROE (%)
Top Buys									
Aristocrat	All.AX	Buy	A$5.22	A$6.00	3.3	18.2	23.5	7.0	31.2
Strong growth profile with an EPS CAGR of 23% over the next three years and strong cash generation									
Las Vegas Sands	LVS.N	Buy	US$74.74	US$97.00	2.7	33.0	18.6	8.4	43.4
Riding on robust mass growth in Macau and improving RevPAR trend in Vegas with Japan optionality									
Melco Crown (Philippines)	MCP.PS	Buy	P13.40	P19.00	N/A	41.8	N/A	4.1	N/A
Top Philippines gaming pick; cheapest name in the Philippines gaming space (23% discount to its Philippines peers); expecting COD Manila to open in 4Q14									
MPEL	MPEL.O	Buy	US$32.55	US$55.00	2.2	71.2	15.7	3.6	24.6
Cheapest name in the Macau gaming space; further potential upside from Studio City and Philippines project									
Summit Ascent	0102.HK	Buy	HK$11.80	HK$23.00	N/A	94.9	N/A	6.8	9.8
Only pure gaming play in the IEZ and will operate as a monopoly for four years									
Top Sells									
Macau Legend	1680.HK	Sell	HK$5.88	HK$5.40	N/A	-8.2	41.2	4.8	13.6
Despite a 31% decline YTD, the stock is still trading at 11.9x FY15E EV/EBITDA on our discounted 2018 estimates, a 3% premium to Macau large-caps									
Travellers	RWM.PS	Sell	P9.71	P9.50	0.6	-1.5	45.0	4.7	16.8
Most expensive name in the Philippines gaming space; trading at ~12x 2015E EV/EBITA, a 35% premium to domestic peers									

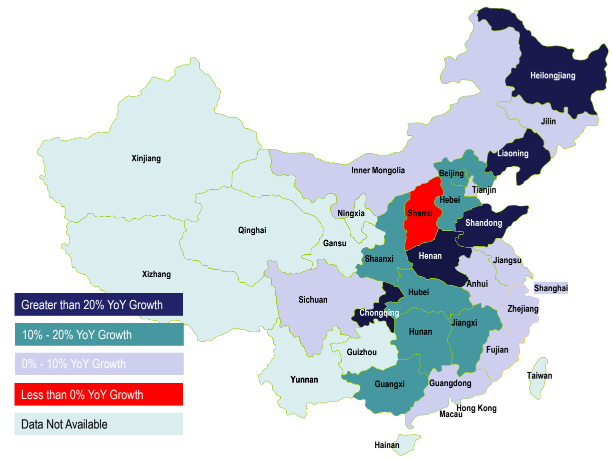
Source: Citi Research estimates

Figure 1. Mainland China Visitation to Macau (Penetration Rate)



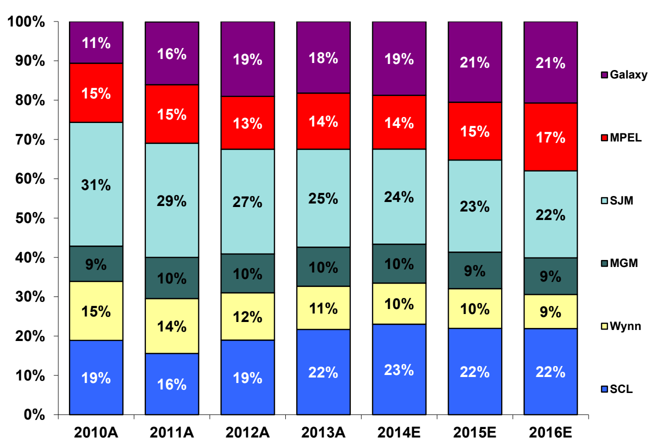
Source: DICJ; Citi Research

Figure 2. Mainland China Visitation to Macau (YoY Growth Rate)



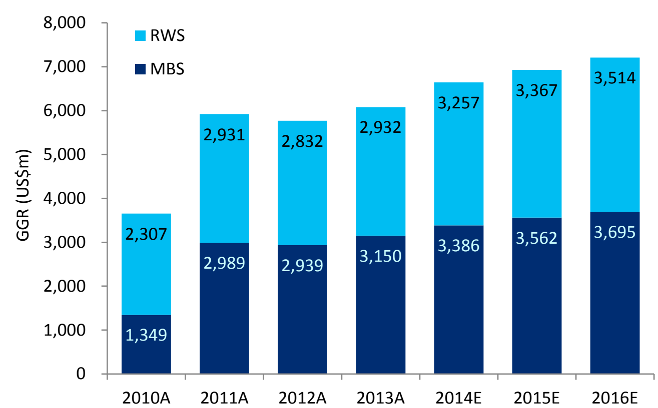
Source: Industry Sources; Citi Research estimates

Figure 3. Macau GGR and Mainland Visitation Growth (2009-Apr 2014)



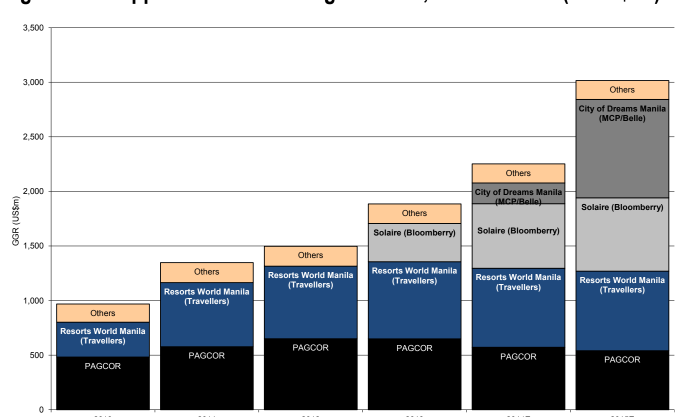
Source: DICJ; Citi Research

Figure 4. Singapore – Market Share By Property (2010A – 2016E)



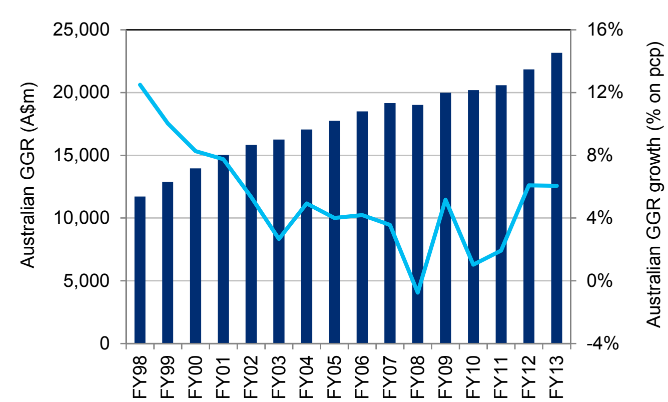
Source: Company Report; Citi Research estimates

Figure 5. Philippines Gross Gaming Revenue, 2010 – 2015E (in US$bn)



Source: Company Report; Citi Research estimates

Figure 6. Australian Gambling Expenditure



Source: ABS, Citi Research

Healthcare

Focus on Earnings in China, Value Addition in India

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- **China: Focusing on earnings** – Our in-depth industry and government checks suggest '14 growth of 14-15%, which is below 16-18% in '12/'13 but still likely to be one of the better sector performances in China. With valuations at the higher end of the historical range, we expect stock performances to diverge and our top picks are those that could potentially deliver strong earnings or beat market expectations, namely Fosun Pharma (2196.HK; HK$29.25; 1), Lijun and CSPC.

- **India: Beyond defensive** – Macro recovery hopes (post elections) diminish the sector's defensive appeal but scope is ample for value addition & non-linear growth over the long term. Fundamentals are unchanged & INR strength is the only tangible risk. However, given a more upbeat market, we stress near-term earnings momentum & valuation comfort in our top picks of LUPN & ARBN.

- **Japan: Domestic environment getting tougher** – Due to the government's push to promote the use of generics, we expect Japan's drug market will be unconducive to growth over the next few years. Instead, growth will need to come from the globalization of blockbuster drugs like Astellas' Xtandi and Ono's Nivolumab, both of which are in the oncology field. The government will allow patients to use drugs or medical technologies even before insurance coverage is available, which will help global players make profits quicker.

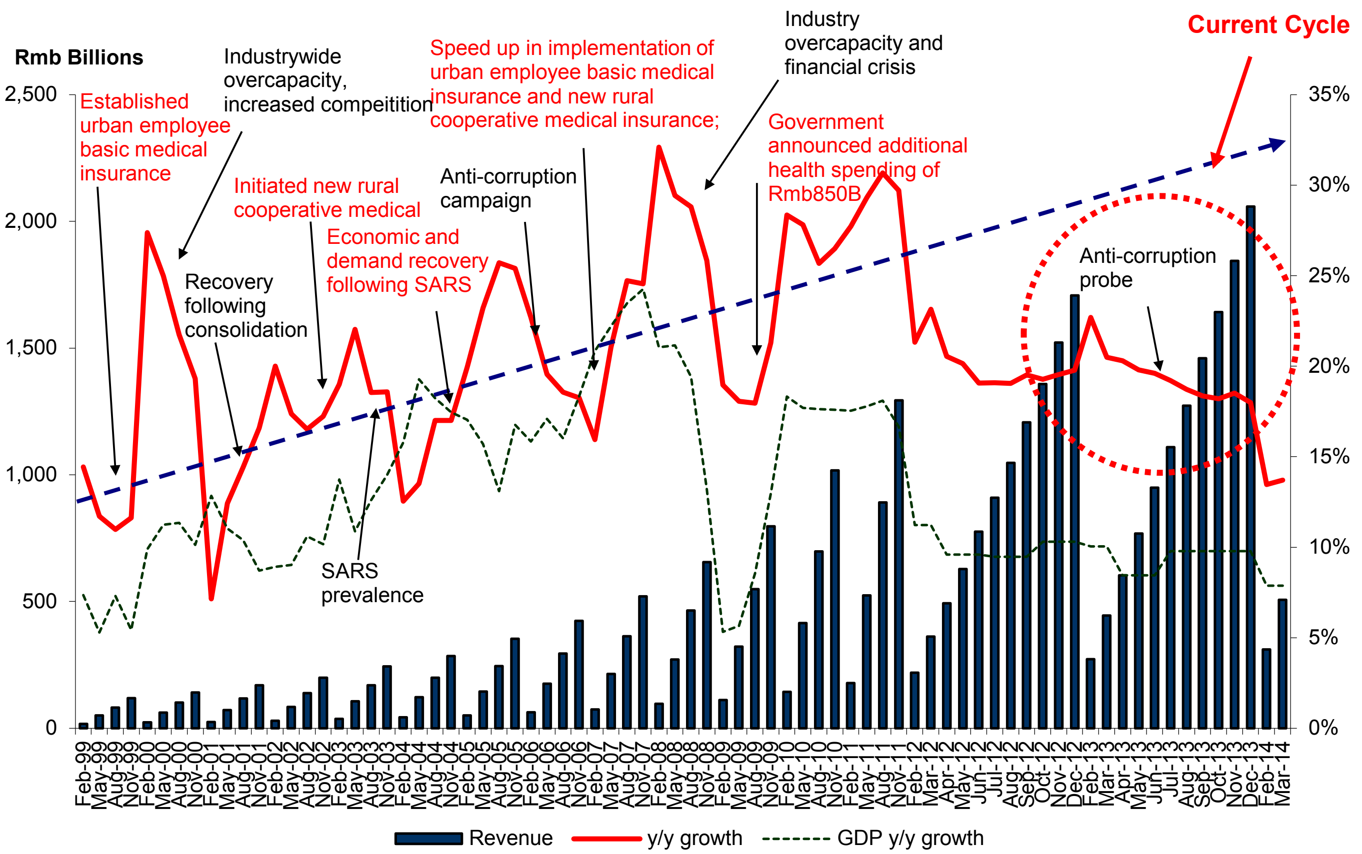
- **Taiwan: Major drug approval and licensing news expected soon** – Managements of some of the largest drug developers by market value – TaiGen, TWi Pharma, PharmaEngine, and Taiwan Liposome – have stated that they expect drug approvals or licensing agreements for key products in the upcoming year. If the announcements are encouraging, they could fuel enthusiasm for the sector, while disappointing results could lead to a pullback.

Healthcare: Top Buys and Top Sells

	Ticker	Rating	Price (Jun. 6)	Target Price	Yield (%)	ETR (%)	2014E P/E (x)	2014E P/BV (x)	2014E ROE (%)
Top Buys									
Astellas	4503.T	Buy	¥1,336	¥1,700	2.0	29.4	32.3	2.4	7.9
Blockbuster prostrate cancer drug Xtandi will grow to US$5bn sales by 2021E. Company is proactive in buying back and retiring shares									
Aurobindo Pharma	ARBN.BO	Buy	Rs647	Rs835	0.4	29.4	12.9	3.7	33.1
Improving US portfolio, smart acquisition in EU & traditional strengths (strong R&D, vertical integration) give us comfort on growth prospects. Valuations are attractive									
CSPC Pharma	1093.HK	Buy	HK$6.30	HK$8.60	1.0	37.5	29.3	3.7	14.5
Well positioned to capture growth opportunities in the upcoming value chain shift in China given an established R&D platform and a solid pipeline (160+ candidates)									
IHH Healthcare	IHHH.KL	Buy	RM4.18	RM4.80	3.5	15.3	40.8	1.8	4.5
Strong track record and robust business model underpinned by good execution and aggressive expansion plans across its three key markets									
Lijun Int'l	2005.HK	Buy	HK$3.07	HK$4.00	1.8	31.9	17.0	3.0	18.1
Growth to be driven by: 1) accelerating industry consolidation, 2) cost advantages in soft bag market, 3) capacity expansión, 4) sales ramp-up of vertical soft bags									
Lupin	LUPN.BO	Buy	Rs945	Rs1,290	0.6	36.5	18.7	4.9	29.3
Resilient business model with a proven execution track record; strong earnings momentum expected to continue									
TWi Pharma	4180.TWO	Buy	NT$300	NT$375	0.0	25.0	NM	9.5	-18.8
Successful Paragraph IV challenges to drive growth. Most significant opportunities are for generic versions of Lidoderm, Dexilant, and Megace ES (first-to-file)									
Top Sell									
Eisai	4523.T	Sell	¥4,185	¥3,500	3.6	-12.6	39.02	2.60	6.6
Even though high dividend may support stock price level, Eisai does not have earnings driver after Aricept patent expiration									

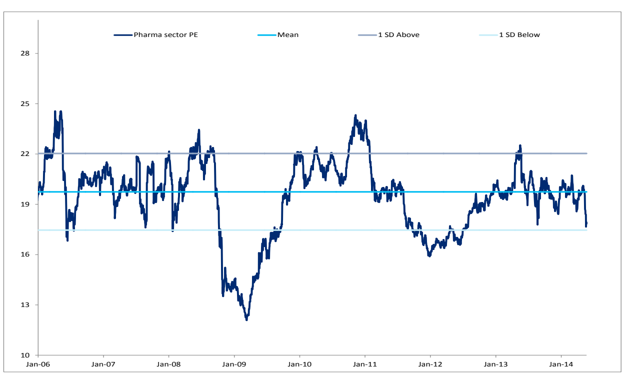
Source: Citi Research estimates *(Please note: FY15E for India stocks)*

Figure 1. Revenue Cycle of Chinese Healthcare Sector (1999-1Q14)



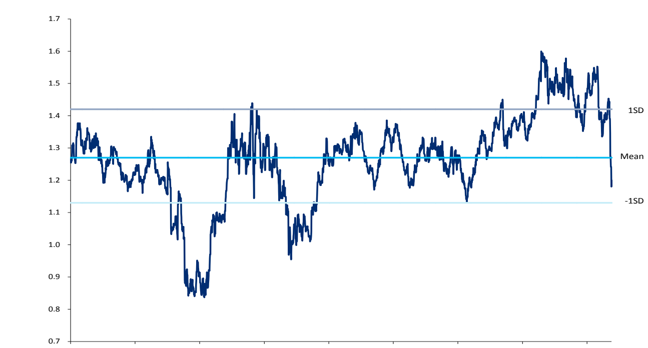
Source: Citi Research, Wind

Figure 2. Indian Pharma PE: At 1SD Below Mean



Source: Bloomberg

Figure 3. Indian Pharma vs. BSE Sensex: Relative PE Below Mean



Source: Bloomberg

Insurance

Big Caps Preferred; China a Stand-out

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- **China** – Life insurance fundamentals have been improving steadily ytd, and the trend should continue in 2H14. NBV growth has accelerated due to good progression in the agency channel and protection products, despite volatile topline trends for bancassurance. Maturity payments and surrender rates, while still high, are gradually decreasing. Competitive pressure from WMPs and online MMFs is also easing, as their returns fall. On the P&C side, combined ratio is still under modest pressure due to rising loss ratios for auto and intensifying competition for agriculture. We expect nil underwriting profit growth this year.

- **Korea** – We are overall bearish on Korea's insurance sector in 2H14, given (a) slowing new business growth (except for SLI and SF&M), (b) only a mild earnings recovery, (c) doldrums in interest rates, and (d) capital pressure. However, we believe SLI and SF&M (000810.KS; W268,000; 1) will continue to outperform the sector, given (i) ongoing market share gain from second tier non-lifers, (ii) better underwriting margin trend with cost-cut effort, (iii) strong capital base and (iv) positive news flows on Samsung group ownership restructuring.

- **Taiwan** – Sector outlook clouded by (i) flattening yield curve in recent months, (ii) regulatory-influenced product mix shift to reduce deposit-like insurance policies, and (iii) a possibly lower rate environment on a sustainable basis that affects long-term returns. We prefer Cathay (2882.TW; NT$46.75; 2) over Fubon (2881.TW; NT$43.35; 2) at the current juncture as Fubon's higher proportion of bancassurance FYP can be affected more by a product mix shift.

- **Thailand** – Insurance demand has remained weak since 2H13 but we continue to see strong FYP trend for a few bancassurance players (MTL-KBANK, BBL-BLA, KT-Axa). Past periods of a weak economy and low rates witnessed strong push for endowment products so the FYP trend may not be as weak as economy. We remain positive on a long-term view.

- **Singapore/Malaysia** – Great Eastern (GELA.SI; S$21.58; 2) continues to enjoy broad based weighted new premium growth in Singapore/Malaysia, with a business bias towards regular premium to drive strong NBEV growth (1Q14: +11% yoy) and a selective ILP strategy. GEH is trading at 1.07x our 2014E embedded value forecast of S$20.30.

Insurance: Top Buys and Top Sells

	Ticker	Rating	Price (Jun. 6)	Target Price	Yield (%)	ETR (%)	2014E P/E (x)	2014E P/BV (x)	2014E ROE (%)
Top Buys									
China Life	2628.HK	Buy	HK$21.30	HK$27.00	2.8	29.5	14.3	1.9	13.9
Pure life play that benefits from gradual improvement in sector fundamentals									
Ping An	2318.HK	Buy	HK$60.15	HK$86.00	1.7	44.7	10.9	1.7	16.8
Strongest operating trends among peers; forerunner and leader in integrating Internet finance with insurance business									
Samsung Life	032830.KS	Buy	W101,500	W130,000	2.0	30.0	18.0	1.0	5.8
Benefits from market share gain in healthcare new biz, cost savings from lay-offs and expected interest spread inflection point by YE2014									
Top Sell									
Hyundai M&F	001450.KS	Sell	W29,200	W27,000	3.4	-4.1	7.4	1.1	15.1
Market share loss in healthcare new biz, rising capital concern and deeper-than-peers' contraction in mortality margin									

Source: Citi Research estimates

Figure 1. Growth Trends For Asian Insurers

	2009	2010	2011	2012	2013	2014E	2015E
APE							
China Life	-0.3%	25.0%	-9.6%	-7.4%	-9.8%	12.6%	12.2%
China Pacific	48.7%	34.9%	-6.3%	-10.0%	-0.6%	16.2%	14.2%
China Taiping	42.0%	30.1%	-10.8%	-0.7%	50.6%	25.0%	20.9%
NCI	54.0%	23.6%	-23.0%	-16.2%	-23.1%	7.1%	12.4%
Ping An	40.5%	39.8%	-2.9%	-3.2%	10.9%	15.5%	16.3%
AIA	-22.0%	7.4%	13.1%	13.8%	30.4%	13.1%	12.7%
Great Eastern	-19.7%	20.4%	10.3%	4.8%	20.1%	4.9%	9.7%
Hanwha Life	4.3%	7.7%	12.1%	25.1%	-21.3%	7.1%	5.8%
Samsung Life	6.3%	-3.6%	8.0%	36.4%	-11.1%	10.4%	8.7%
Tongyang Life	2.5%	10.6%	-6.2%	4.3%	10.1%	7.6%	8.8%
Dongbu	-7.2%	0.5%	27.3%	2.9%	-15.0%	3.0%	4.0%
HM&F	na	6.6%	38.5%	8.1%	-10.0%	4.0%	4.0%
Samsung F&M	46.9%	9.1%	10.2%	24.5%	-3.8%	6.3%	5.0%
Cathay Life	0.8%	53.5%	-0.6%	19.1%	-25.0%	24.5%	8.4%
Fubon Life	63.9%	85.8%	-12.8%	12.1%	-12.3%	-3.3%	10.8%
Bangkok Life	56.4%	17.2%	7.4%	-24.7%	35.3%	20.7%	14.5%
AMP	9.2%	3.8%	104.7%	6.6%	7.3%	7.3%	7.3%
New business value							
China Life	27.2%	12.0%	1.8%	3.1%	2.2%	5.3%	9.3%
China Pacific	36.9%	22.0%	10.1%	5.2%	6.2%	9.0%	12.1%
China Taiping	56.4%	35.0%	22.8%	2.7%	36.6%	13.4%	15.6%
NCI	na	na	-8.0%	-4.3%	1.5%	4.3%	10.1%
Ping An	38.2%	31.4%	8.5%	-5.4%	14.1%	13.8%	15.0%
AIA	-43.7%	22.4%	39.7%	27.5%	25.4%	19.4%	16.4%
Great Eastern	-11.3%	30.0%	19.7%	-3.3%	19.1%	4.8%	9.4%
Hanwha Life	-2.0%	3.0%	7.0%	21.8%	-5.8%	6.4%	4.6%
Samsung Life	10.2%	-4.9%	5.8%	6.3%	-1.2%	11.6%	7.9%
Tongyang Life	0.2%	12.2%	-6.8%	-27.6%	11.3%	7.4%	8.3%
Dongbu	50.3%	-11.3%	0.5%	2.5%	-1.3%	3.0%	4.0%
HM&F	-29.0%	-2.7%	11.6%	18.5%	-0.1%	2.7%	4.0%
Samsung F&M	31.2%	0.1%	4.2%	34.4%	13.8%	7.1%	5.0%
Cathay Life	8.1%	7.5%	7.0%	8.7%	-14.7%	8.2%	8.4%
Fubon Life	50.4%	38.5%	12.9%	13.2%	-21.6%	14.6%	10.8%
Bangkok Life	na	37.3%	-24.4%	19.1%	1.4%	19.8%	16.4%
AMP	-10.4%	-14.4%	57.8%	-3.9%	5.8%	6.6%	6.6%
Embedded value							
China Life	18.8%	4.5%	-1.8%	15.3%	1.4%	8.3%	8.8%
China Pacific	40.6%	11.9%	3.2%	19.1%	6.7%	8.9%	8.6%
China Taiping	59.4%	28.5%	23.2%	35.7%	55.0%	13.2%	12.6%
NCI	na	na	74.4%	16.1%	13.3%	14.8%	14.0%
Ping An	26.4%	29.5%	17.2%	21.3%	15.3%	13.3%	12.8%
AIA	na	18.0%	10.1%	15.3%	7.7%	11.3%	11.5%
Great Eastern	7.7%	13.5%	5.5%	7.8%	6.6%	4.8%	5.3%
Hanwha Life	30.6%	3.5%	6.4%	-9.1%	19.1%	11.9%	16.4%
Samsung Life	5.5%	23.2%	9.5%	4.7%	2.2%	12.8%	13.3%
Tongyang Life	30.9%	12.1%	3.9%	12.5%	4.4%	13.6%	14.8%
Dongbu	25.5%	23.2%	26.5%	19.4%	8.1%	13.6%	14.2%
HM&F	25.3%	19.8%	17.6%	16.4%	12.8%	17.6%	14.0%
Samsung F&M	24.7%	21.6%	15.6%	14.8%	1.9%	12.6%	13.6%
Cathay Life	40.3%	10.3%	5.8%	18.9%	2.2%	4.1%	4.5%
Fubon Life	65.7%	20.6%	13.2%	23.8%	7.3%	7.7%	7.6%
Bangkok Life	na	51.1%	16.4%	20.5%	22.6%	23.0%	22.5%
AMP	5.9%	-2.0%	41.3%	7.5%	3.3%	3.1%	2.7%

Source: Company data, Citi Research estimates

Internet & Games

All About Mobile Monetization

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- **Mobile coming of age** – Smartphone-based mobile internet users should exceed desktop internet users in China within the next 12 months, and mobile monetization is a key focus by operations and investors. Across developing Asia, ex China (SE Asia and India) mobile internet is also becoming a key focus with the ramp of the microchat heavyweights: WeChat, Line and Kakau Talk as key catalysts. We highlight: 1) mobile game platform players, such as Tencent and Qihoo, and 2) mobile ad players, such as Baidu. We reiterate our Buy on SFUN for "vertical value" with a unique combination of offline resources/relationships across China's property sector creating a proprietary database and competitive moat that complement the company's dominant online presence in its space.

- **Mobile games deepen market penetration** – The mobile games market in China is expected to double this year from c. US$1.5bn in 2013. In this market, we expect platform players such as Tencent, Qihoo's mobile assistant, and 91 Wireless to benefit from this exceptional growth in mobile games demand, competitive and fragmented developer markets, and penetration into new demographic segments. We also expect continued polarization of users toward fewer leading apps store/platform players, with Tencent (0700.HK; HK$118.50; 1), Baidu, and Qihoo being the ultimate market leaders. We recommend investors to invest in platform vs. developer at this stage.

- **Ad spending eventually to follow user attention** – We estimate that mobile ads accounted for ~3% of total ad budgets, vs. 22% of total media consumption time and ultimately expect this "monetization gap" to narrow. Despite lagging adoption of mobile ads by advertisers, lower unit price, and form factor challenges, we are seeing the migration to mobile ad formats gradually picking up. Expect bigger advertisers to allocate more budgets to mobile in FY14.

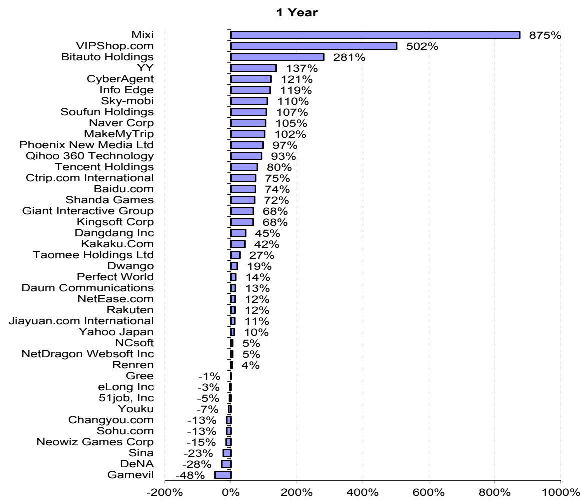
- **Regional focus** – Microchat will continue to dominate the focus in Korea with potential spin-out to unlock SOTP value by the key players. In India and SE Asia we expect an intense private equity and VC focus in the last 2 years to move toward listed markets through 2014 and 2015 with mobile business models dominating investor focus. Investors should expect listed pure plays to hence emerge for these markets.

Internet & Games: Top Buys and Sells

	Ticker	Rating	Price (Jun. 6)	Target Price	Yield (%)	ETR (%)	2014E P/E (x)	2014E P/BV (x)	2014E ROE (%)
Top Buys									
Baidu	BIDU.O	Buy	US$172.34	US$215.0	0.0	24.2	32.9	7.6	24.2
Beginning to monetize mobile traffic in both search and app platforms, and would start to exhibit operating leverage after the years of investment in FY12/13									
Qihoo	QIHU	Buy	US$85.54	US$165.0	0.0	92.9	34.7	11.3	27.1
Poised to become mobile market leader in China, with its mobile apps store emerging as a leading games platform									
SouFun	SFUN.N	Buy	US$11.19	US$19.4	0.0	73.7	12.2	5.4	52.6
Dominant position in the online property ad/eComm market. SF Card and fast-growing listing services drive secular growth in both primary and secondary markets									
Top Sell									
NCsoft	036570.KS	Sell	W165,000	W150,000	0.5	-8.5	15.4	2.6	18.7
Market expectations for new games seem too high									

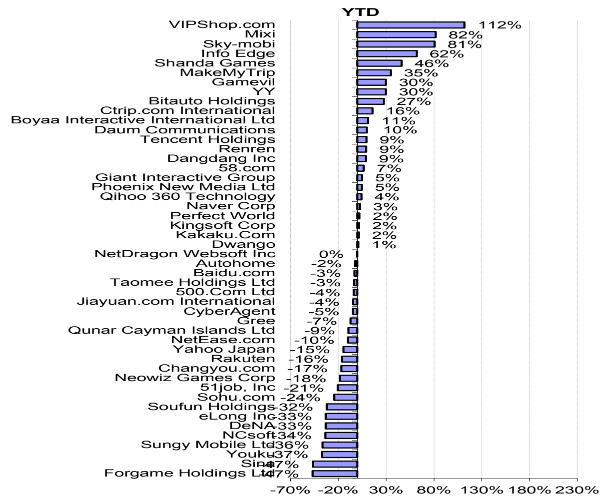
Source: Citi Research estimates

Figure 1. 1 Year Share Price Performance



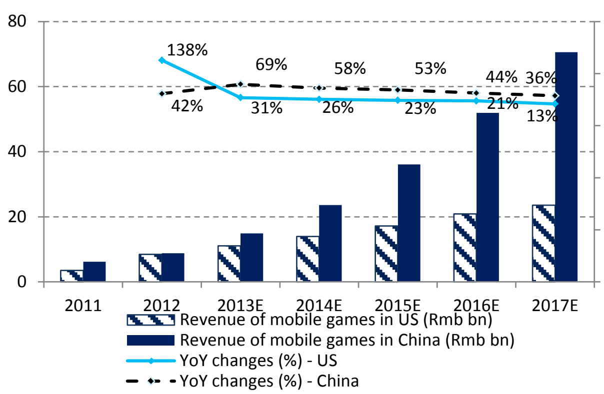
Source: Reuters, and Citi Research (06 Jun 2014)

Figure 2. YTD Share Price Performance



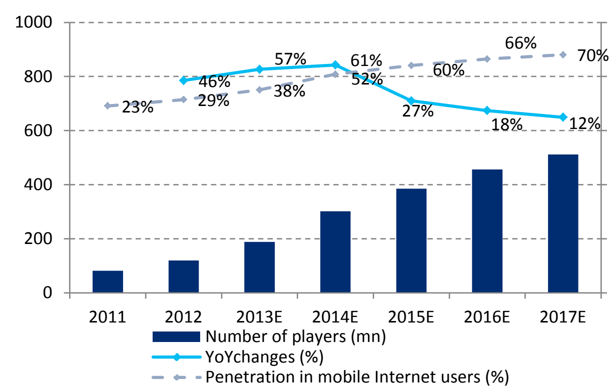
Source: Reuters, and Citi Research (06 Jun 2014)

Figure 3. Comparison: Revenue Of Mobile Games in US and China



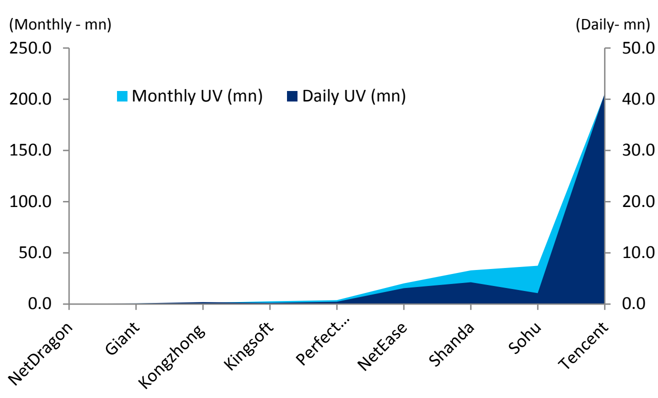
Source: iResearch, and Citi research

Figure 4. Number of Smart Device Game Players in China



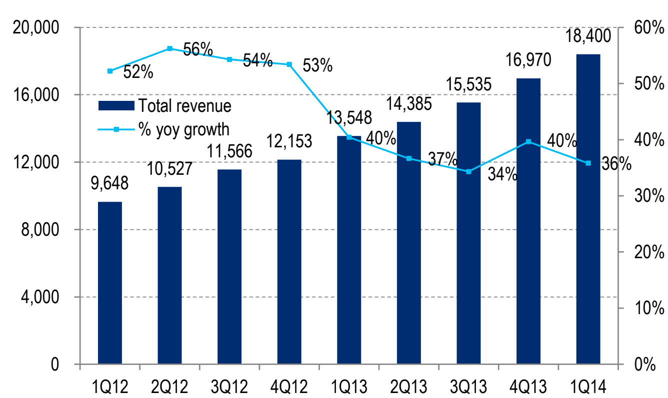
Source: iResearch, and Citi research

Figure 5. Tencent: Dominant Position in Monthly/Daily UV on PC for Online Games in Dec. 2013



Source: iResearch, and Citi research

Figure 6. Tencent: Solid Revenue Growth (Rmb mn;%)



Source: Company data, and Citi research

IT Services

Elections Done; Back to Fundamentals

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- **Still constructive** — Post the ~25% underperformance vs the market YTD on the back of (a) Weaker than expected March quarter and (b) INR appreciation/relative positioning issues, we believe the sector is well placed on growth/valuations. Demand trends remain strong and valuations at ~14x 1-year forward are attractive – maintain positive view with Wipro/HCLT as top picks.

- **Demand outlook** — IT Services demand remains decent as highlighted by recent deal win announcements. However, trends in 4QFY14 were a little weaker than anticipated at the start of the year with some weakness in the Retail vertical and some pressure in relatively commoditized services. Overall, we expect revenue growth for the industry to be largely similar to FY14.

- **Discretionary spends need to be monitored** — Views on discretionary spends remain mixed, partly due to how different companies define "discretionary spends". We think there is a lot of activity around newer technologies, but ERP system integration/packaged implementation remains to see a significant upturn. Trends need to be keenly watched particularly given the impact of SaaS/Cloud on the ERP ecosystem; any pick-up could lend further upside to overall growth.

- **Currency concerns** — Post the elections in India, a lot of investors are concerned about the potential impact of a sharp INR appreciation. Our analysis suggests that there is almost no correlation for absolute stock performance but on a relative basis, the first leg of INR appreciation always invites some knee-jerk sector rotation away from IT and results in some relative underperformance. In the medium term, demand remains the single most important driver for stock performance. Citi views remains for a range bound INR (59 – 62/$).

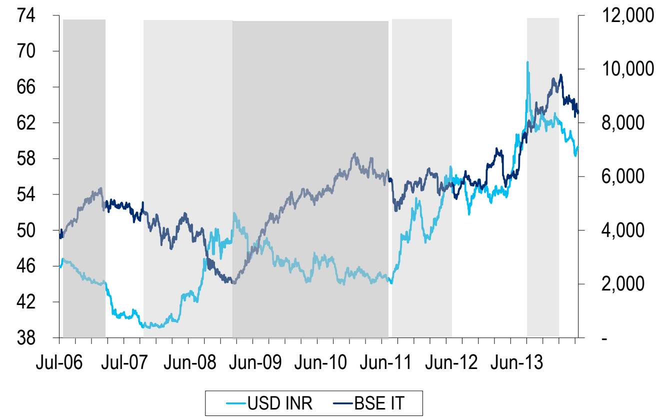
- **Top picks are Wipro and HCL Tech** — (a) Wipro – while 1QFY15 guidance is weak, it is partly seasonal. Demand commentary and deal wins remain good; we expect an uptick in 2Q. Wipro is also among the best placed in terms of margin levers to manage the impact of an INR appreciation. (b) HCL Tech – steady performance continues and valuations at ~14x forward P/E offer upside.

IT Services: Top Buys

			Price	Target	Yield	ETR	FY15E		
	Ticker	Rating	(Jun. 6)	Price	(%)	(%)	P/E (x)	P/BV (x)	ROE (%)
Top Buys									
HCL Tech	HCLT.BO	Buy	Rs1,324.00	Rs1,570.00	2.1	20.7	14.1	3.7	29.9
Steady performance continues and valuations are attractive									
Mindtree	MINT.BO	Buy	Rs780.15	Rs785.00	1.5	2.2	12.4	3.2	28.6
Strong business momentum and company continues to invest well, which should help sustain growth									
Wipro	WIPR.BO	Buy	Rs508.90	Rs630.00	2.4	26.2	14.6	3.1	23.1
Demand commentary and deal wins remain good. Wipro is amongst the best placed in terms of margin levers to manage the impact of an INR appreciation									

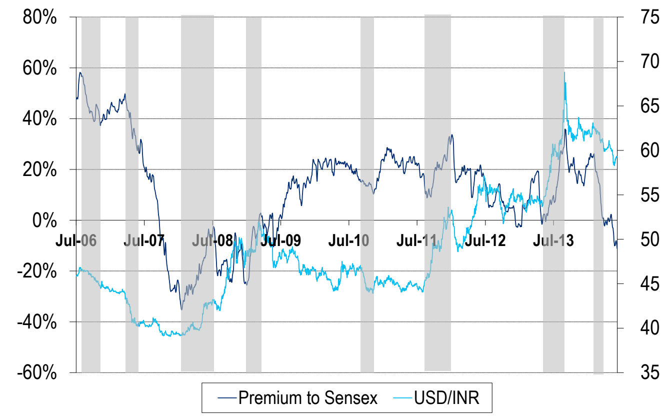
Source: Citi Research estimates

Figure 1. Absolute Performance – Almost No Impact From INR Move



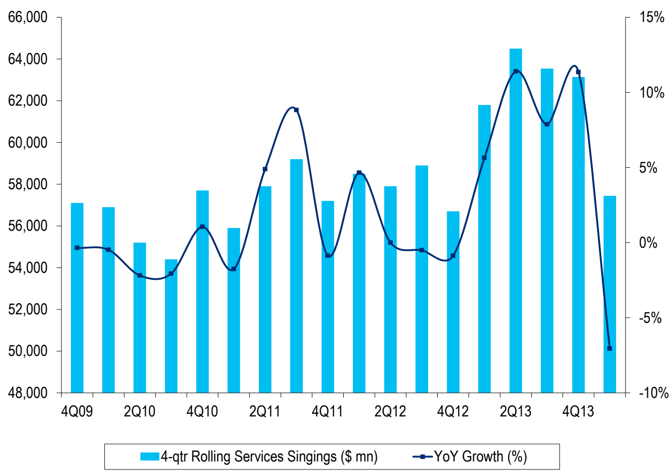
Source: Bloomberg, IBES, Citi Research

Figure 2. Relative Performance – Some Initial Impact From INR Move



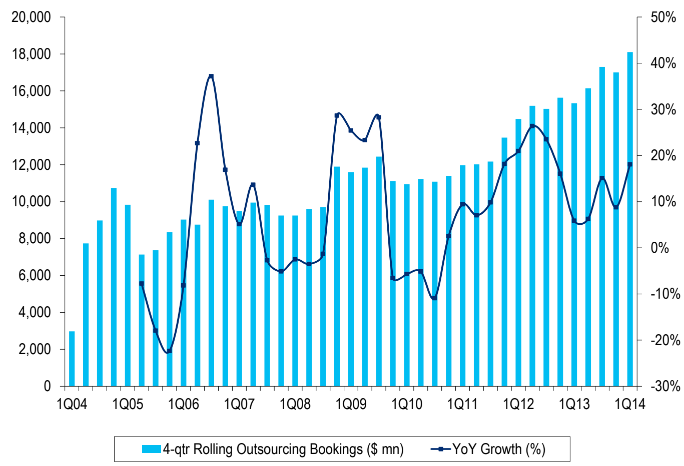
Source: Bloomberg, IBES, Citi Research

Figure 3. IBM Services Signings



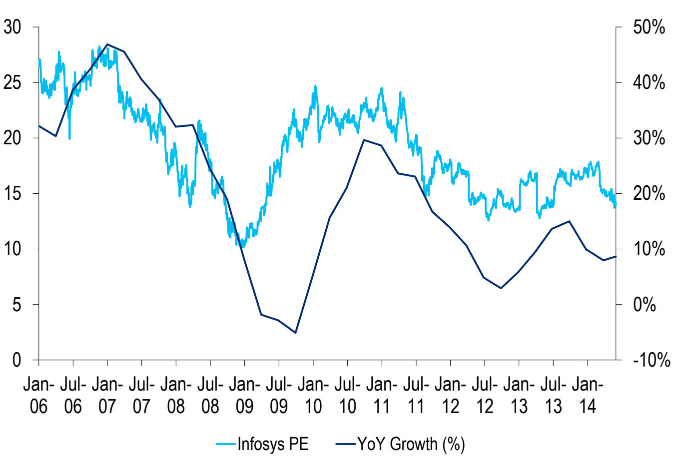
Source: Company Reports, Citi Research

Figure 4. Accenture – Outsourcing Bookings



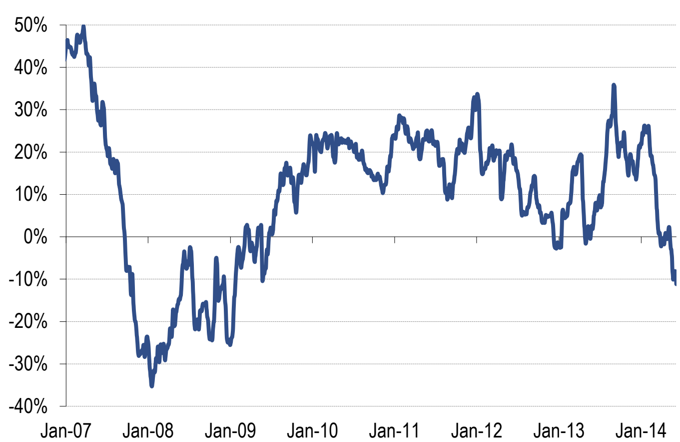
Source: Company Reports, Citi Research

Figure 5. Valuations Closely Correlated With $-revenue Growth



Source: I/B/E/S, Company Reports, Citi Research; Quarterly reported yoy growth rates in $-revenues have been interpolated for the time series

Figure 6. BSEIT Now Trades At ~10% Discount to Sensex



Source: Datacentral, Citi Research; Stock movement post every fall due to disappointing guidance or commentary over past couple of years.

Metals & Mining

Weak Demand and Plenty of Supply; Focus on Self-Help

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Tatsuro Ochi / Japan

Sungmee Park / Korea

Timothy Chen / Taiwan

Claire Yuan / China

- **Weak demand outlook in China** – Although China manufacturing PMI edged up by 0.4ppt to 50.8 in May, suggesting that improving liquidity and credit conditions since the beginning of the year have stabilized manufacturing activity, demand for materials remained weak given the decelerating FAI Ytd and drop in FS new starts (-22% YTD).

- **Focusing on self-help as demand remains muted** – In light of muted demand for commodities, metals & mining companies are turning to self-help initiatives. These include asset spin-offs, cost-reduction drives, capex cuts, and SOE reforms in China.

- **Selectively positive on commodities that have supply disruptions** – Citi is neutral to bearish on most commodities. However, we are positive on those that are subject to supply disruptions. We are nickel bulls and see further upside despite the 50+% rally in prices year-to-date on the back of the Indonesian ore export ban. Citi's commodity team expects price will peak at US$26,500/t in 2016.

- **Pan-Asia stock picks** –We have four top Buys and three top Sells in the pan Asia region. Top Buys are: Baosteel, NSSM, POSCO and Rio Tinto. Top Sells are: China Coal, NMDC and Alumina.

Metals & Mining: Top Buys and Sells

	Ticker	Rating	Price (Jun 6)	Target Price	Yield (%)	ETR (%)	2014E P/E (x)	2014E P/BV (x)	2014E ROE (%)
Top Buys									
Baosteel	600019.SS	Buy	Rmb3.93	Rmb5.70	5.9	50.9	8.5	0.6	6.7
High earnings visibility due to high-end product mix; 0.56x PB at more than 1SD below historical average. Strong BS, attractive dividend yield at ~6%									
Nippon Steel & Sumitomo Metal	5401.T	Buy	¥309	¥410	2.2	34.6	9.9	1.0	10.7
India steel volumes have been resilient in a muted-demand environment. Improved FAMD performance and steel price hikes; attractively valued option on the steel cycle									
POSCO	005490.KS	Buy	W288,000	W350,000	2.8	24.3	11.2	0.5	4.8
Asset restructuring by new CEO; earnings bottoming in 2014E with undemanding valuation at ~0.5x PB									
Rio Tinto	RIO.AX	Buy	A$59.40	A$71.00	3.7	23.2	10.1	1.9	22.4
Strong volume growth, relatively low capex intensity, strong cash flow yield, solid balance sheet, a discount to NPV make RIO a compelling investment									
Top Sells									
Alumina	AWC.AX	Sell	A$1.43	A$0.90	0	-37.1	nm	1.3	-3.0
We are cautious on AWC's ability to deliver on market earnings estimates based on cost pressures combined with application of A$ and Brazilian Real									
China Coal	1898.HK	Sell	HK$4.26	HK$3.10	1.9	-25.4	15.2	0.5	3.4
Highly sensitive to coal price with deteriorating balance sheet									
NMDC	NMDC.BO	Sell	Rs191.1	Rs155.0	4.3	-14.7	11.2	2.3	21.9
Orissa ban to have a limited impact – some mines could resume soon; weak global prices should cap domestic hikes. Valuation unattractive									

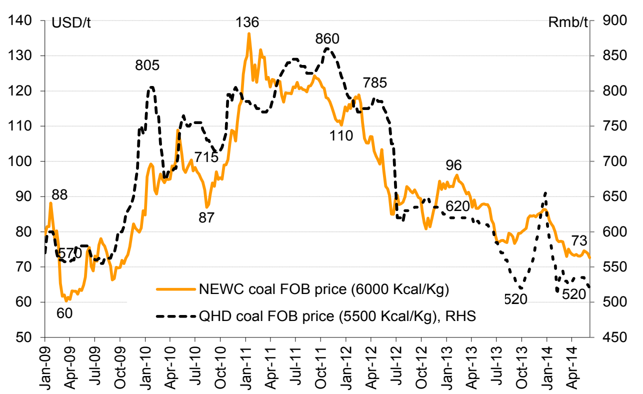
Source: Citi Research estimates

Figure 1. Citi Commodity Price Forecasts

		Q1 2014	Q2 2014E	Q3 2014E	Q4 2014E	Q1 2015E	Q2 2015E	Q3 2015E	Q4 2015E	2012	2013	2014E	2015E	2016E	2017E	2018E
Energy																
NYMEX WTI	USD/bbl	98.0	98.0	102.0	90.0	93.0	86.0	92.0	84.0	94.1	98.0	97.0	88.8	83.0	78.0	80.0
ICE Brent	USD/bbl	108.0	103.0	106.0	99.0	97.0	93.0	97.0	93.0	111.7	108.7	104.0	95.0	90.0	85.0	85.0
Henry Hub Natural Gas	USD/MMBtu	5.20	4.90	4.90	4.80	4.50	4.40	4.50	4.60	2.75	3.73	5.00	4.50	4.90	4.90	5.50
Base Metals																
LME Aluminum	USD/MT	1,752	1,740	1,780	1,800	1,830	1,860	1,890	1,900	2,049	1,888	1,770	1,870	1,950	2,100	2,200
LME Copper	USD/MT	7,005	6,650	6,700	6,800	6,800	7,000	7,200	7,500	7,945	7,352	6,785	7,125	7,700	8,000	8,200
LME Lead	USD/MT	2,127	2,050	2,150	2,250	2,350	2,100	2,200	2,370	2,072	2,158	2,145	2,255	2,350	2,400	2,360
LME Nickel	USD/MT	14,693	16,500	17,450	17,800	20,000	20,500	22,000	23,500	17,592	15,105	16,610	21,500	24,500	26,000	25,000
LME Tin	USD/MT	22,622	22,900	23,000	24,000	25,000	24,000	23,000	25,000	21,108	22,340	23,130	24,250	25,000	24,000	23,000
LME Zinc	USD/MT	2,027	2,010	2,050	2,100	2,150	2,200	2,250	2,300	1,963	1,940	2,045	2,225	2,300	2,350	2,320
Precious Metals																
COMEX Gold	USD/T. oz	1,297	1,310	1,330	1,340	1,340	1,350	1,360	1,400	1,669	1,416	1,320	1,365	1,380	1,400	1,420
Silver	USD/T. oz	20.5	20.4	20.8	21.0	21.5	21.9	22.4	23.2	31.2	24.0	20.7	22.3	22.5	23.0	23.1
Platinum	USD/T. oz	1,428	1,445	1,500	1,525	1,525	1,565	1,640	1,675	1,552	1,490	1,475	1,600	1,710	1,800	1,960
Palladium	USD/T. oz	745	800	830	850	875	900	900	925	645	728	805	900	935	980	980
Bulk Commodities																
Hard Coking Coal (Spot)	USD/MT	122	117	130	135	145	150	155	160	191	148	130	153	180	190	200
Thermal Coal Asia (NEWC)	USD/MT	79	72	72	80	88	84	82	85	94	84	76	85	85	90	100
Iron Ore Spot (TSI)	USD/MT	120	110	102	100	98	92	85	85	128	135	108	90	80	83	85
Agriculture																
CBOT Corn	USd/bu	450	470	440	380	420	450	505	505	695	578	435	470	515	N/A	N/A
CBOT Wheat	USd/bu	616	650	655	655	650	640	635	635	750	684	645	640	615	N/A	N/A
CBOT Soybeans	USd/bu	1,355	1,425	1,300	1,075	1,050	1,050	1,000	1,100	1,465	1,406	1,290	1,050	1,075	N/A	N/A
CBOT Rice	USD/cwt	15.5	15.3	15.4	15.0	14.4	14.2	14.1	14.1	14.9	15.5	15.3	14.2	N/A	N/A	N/A
NYB-ICE Cotton	USd/lb	88.0	90.0	85.0	75.0	75.0	75.0	75.0	75.0	80.0	83.3	85.0	75.0	N/A	N/A	N/A
Sugar#11	USd/lb	16.5	18.0	18.0	18.0	18.5	18.5	18.5	18.5	21.6	17.5	17.6	18.5	N/A	N/A	N/A
ICE Coffee	USd/lb	152	185	200	200	200	200	200	200	175	126	180	200	N/A	N/A	N/A
ICE Cocoa	USD/MT	2,880	3,100	3,300	3,300	3,400	3,400	3,500	3,300	2,348	2,405	3,145	3,400	N/A	N/A	N/A

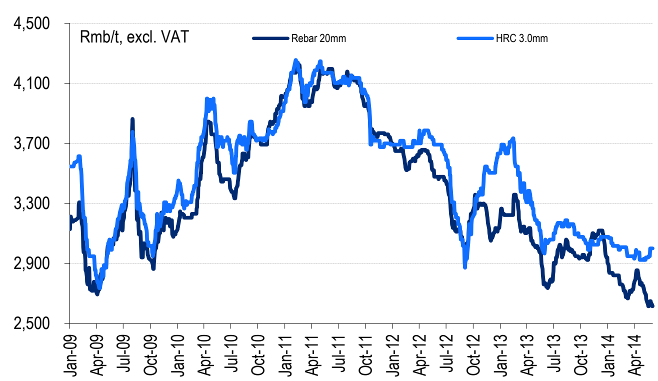
Source: Citi Research

Figure 2. QHD vs. NEWC coal price



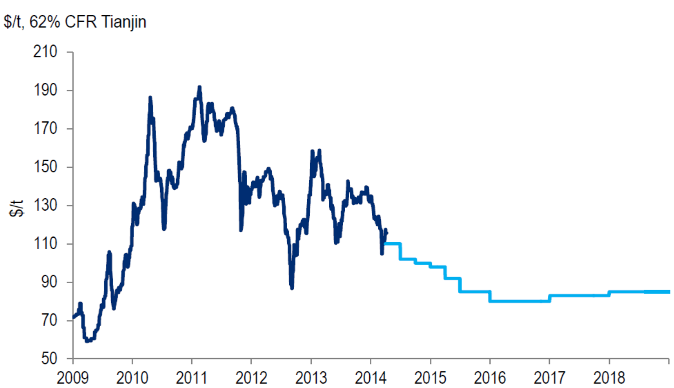
Source: SXCOAL, Bloomberg, Citi Research

Figure 3. Shanghai Rebar and HRC Prices



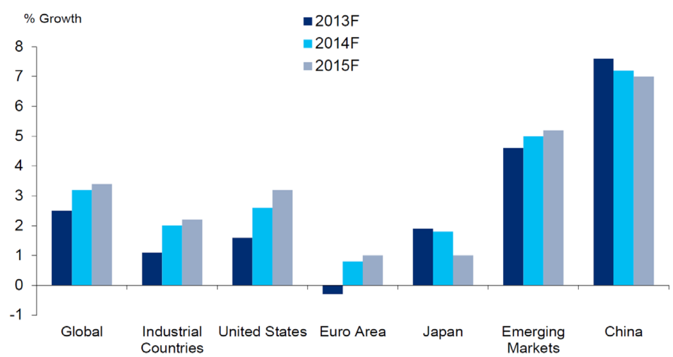
Source: Mysteel, WIND, Citi Research

Figure 4. Iron Ore Prices and Forecasts



Source: Bloomberg, Citi Research

Figure 5. Citi Economic Forecasts For Selected Countries And Regions



Source: Citi Research

Oil, Gas & Chemicals

Focus on SOE Reform and Natural Gas Price Hike

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- **Oil price outlook** – Our global commodity team expects geopolitics to be an upside risk factor for oil price in the near-term though fundamental demand/ supply analysis points to a more bearish price in the medium to longer term. The team forecasts Brent to average US$109/bbl in 2014 and US$105/bbl in 2015.

- **China Oils** – In 2H14, the key things to look at include Sinopec's selldown of its marketing division, PetroChina's disposal of the Eastern Pipeline Co and China's potential natural gas price hike. Sinopec is our top pick as we believe the selldown will release value of its marketing business by getting a higher valuation as a standalone company. In addition, by introducing strategic investors, Sinopec hopes to expand its non-fuel business at gas refilling stations which could be an earnings driver. For PetroChina, we have factored in ~Rmb20bn EBIT growth from natural gas price hike around mid-2014. Although the disposal of the Eastern Pipeline Co will boost reported earnings, we think Petrochina is expensive at 12.4x 2014E recurring earnings.

- **Chemicals** – We stay positive on the global ethylene cycle in the next 2-3 years after cutting 2016-17 capacity growth to 3.3% and 3.1%. We expect the cycle to extend into 2017 with various delays in US greenfield crackers, and expect no new naphtha crackers in China over 2H14-1H17. Our preferred products are ethylene, PE and PP. MEG and SM supply additions are limited but softer demand may cap margin upside. Phenol, AN, PTA, oxo-alcohols, CPL and synthetic rubber will remain tough on rising self-sufficiency in China.

- **India** – Post the strong mandate in the General Elections, the new govt could initiate new reforms on transparency in subsidy sharing, incentivising E&P investments, improving regulatory and investment climate for gas development, in addition to pushing further the reforms in O&G sector which were kick-started by the previous govt but ran into implementation issues (e.g. gas pricing reform, diesel price deregulation, direct transfer of subsidies). We prefer SOEs over private companies to play the reform theme, with our top upstream and downstream picks being ONGC & BPCL (BPCL.BO; Rs620.50; 1) respectively.

Oil, Gas & Chemicals: Top Buys and Top Sells

	Ticker	Rating	Price (Jun. 6)	Target Price	Yield (%)	ETR (%)	2014E P/E (x)	2014E P/BV (x)	2014E ROE (%)
Top Buys									
LG Chem	051910.KS	Buy	W264,000	W320,000	1.5	22.7	11.7	1.4	12.5
Differentiated product mix, volume growth, solid I&E margin									
Lotte Chem	011170.KS	Buy	W168,500	W235,000	0.7	40.2	15.0	0.9	6.1
Tight MEG supply in 2H14, healthy PE/PP margins									
ONGC	ONGC.BO	Buy	Rs418.50	Rs455.00	2.3	11.0	14.8	2.3	16.7
1) Most leveraged to higher gas prices, 2) likely peaking of the subsidy burden, 3) reasonable valuations, 4) material earnings contribution from deregulated businesses									
PTTGC	PTTGC.BK	Buy	Bt67.00	Bt87.70	4.8	35.7	8.8	1.2	13.9
Competitive feedstock advantage over naphtha crackers									
Sinopec	0386.HK	Buy	HK$7.14	HK$8.23	4.4	19.7	9.5	1.1	12.6
Selldown of the marketing division will likely release value by getting a higher valuation as a standalone company. Current valuations are undemanding									
Top Sell									
PetroChina	0857.HK	Sell	HK$9.37	HK$7.50	4.3	-15.7	10.4	1.2	11.5
Growth in gas earnings will likely be wiped out by declining oil earnings, and valuation is unattractive on a recurring earnings basis									

Source: Citi Research estimates

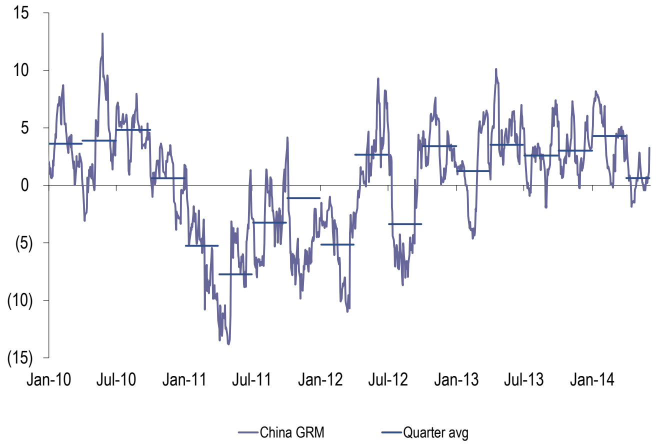
Figure 1. China Oils – 2014E EPS Sensitivity to Oil Price and Refining Margin (Rmb)

Sinopec	Refining margin (US$/bbl)						
Brent (US$/bbl)	$2.9/bbl	$2.4/bbl	$1.9/bbl	$1.4/bbl	$0.9/bbl	$0.4/bbl	-$0.1/bbl
129	0.76	0.74	0.73	0.71	0.69	0.67	0.66
124	0.72	0.71	0.69	0.67	0.66	0.64	0.62
119	0.69	0.67	0.66	0.64	0.62	0.61	0.59
114	0.66	0.64	0.62	0.61	0.59	0.57	0.56
109	0.62	0.60	0.59	0.57	0.55	0.54	0.52
104	0.59	0.57	0.55	0.54	0.52	0.50	0.49
99	0.55	0.54	0.52	0.50	0.49	0.47	0.45
94	0.52	0.50	0.48	0.47	0.45	0.43	0.42
89	0.48	0.47	0.45	0.43	0.42	0.40	0.38
84	0.45	0.43	0.42	0.40	0.38	0.37	0.35

PetroChina	Refining margin (US$/bbl)						
Brent (US$/bbl)	$3.0/bbl	$2.0/bbl	$1.0/bbl	$0.0/bbl	$-1.0/bbl	$-2.0/bbl	$-3.0/bbl
129	1.07	1.04	1.01	0.99	0.96	0.93	0.90
124	1.01	0.98	0.95	0.92	0.90	0.87	0.84
119	0.94	0.92	0.89	0.86	0.83	0.81	0.78
114	0.88	0.85	0.83	0.80	0.77	0.75	0.72
109	0.82	0.79	0.77	0.74	0.71	0.68	0.66
104	0.76	0.73	0.70	0.68	0.65	0.62	0.59
99	0.71	0.68	0.65	0.63	0.60	0.57	0.54
94	0.63	0.61	0.58	0.55	0.53	0.50	0.47
89	0.57	0.55	0.52	0.49	0.46	0.44	0.41

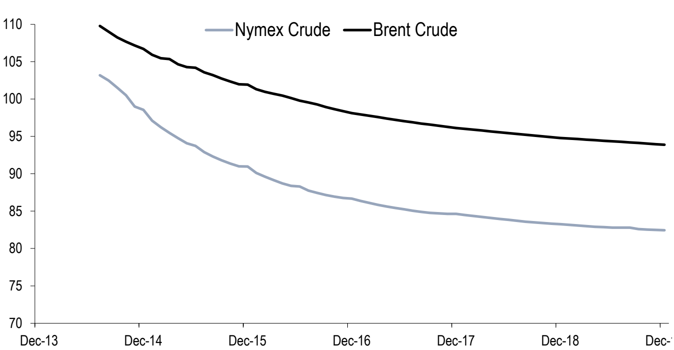
Source: Citi Research

Figure 2. China Domestic GRM (US$/bbl)



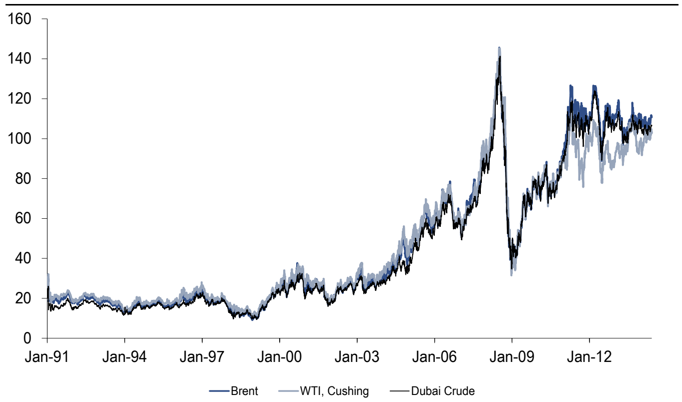
Source: Bloomberg, NDRC, Citi Research

Figure 3. Brent/WTI Forward Price Curve (Contango/ Backwardation – US$/bbl)



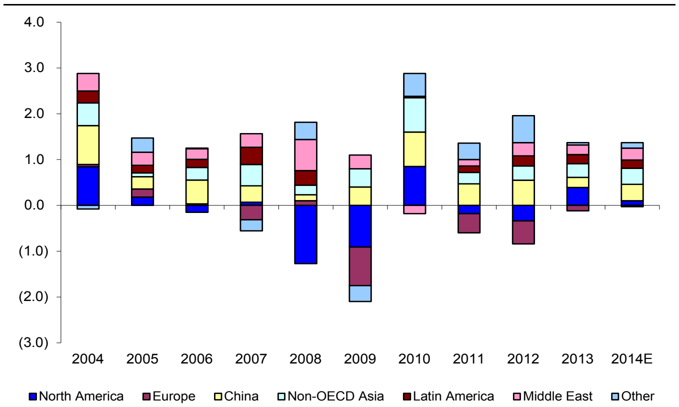
Source: Bloomberg, Citi Research

Figure 4. Long-term Brent, WTI and Dubai (US$/bbl)



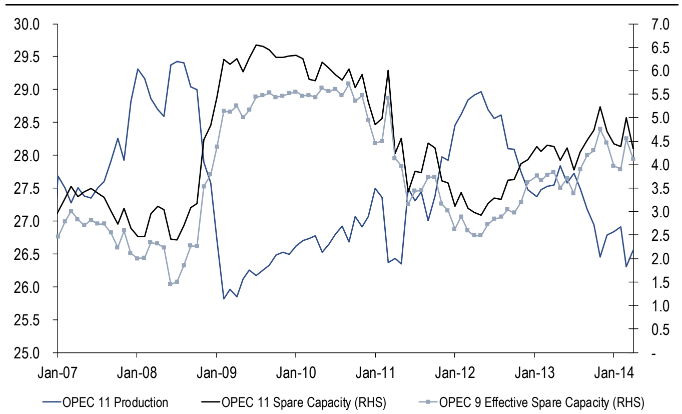
Source: Bloomberg, Citi Research

Figure 5. IEA Forecasts – Global Oil Demand Growth (mbpd)



Source: IEA, Citi Research

Figure 6. OPEC Production and Spare Capacity (mbpd)



Source: Bloomberg, Citi Research

Property

Critical Point Arriving in China

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- **China: More loosening must be powerful and timely to catalyze a rebound:** Pressure in the physical market could be even greater than in the FY08/11 downcycle. To avert a potentially serious correction, measures will need to be powerful and timely (in Jun/Jul), including 1) HPR relaxation – we expect more key cities (except Tier 1) to relax from now until Jun/July; 2) Credit easing – more favorable terms for mortgage costs/ down-payments; 3) Less negative media reporting to improve buyer sentiment. We expect the sector to be volatile in the short term driven by mixed news flow about price cuts and lackluster volume.

- **HK: Mass-home prices bottoming out; Buy Developers:** Believing that mass-home prices have already bottomed out after 15 months of consolidation, we see significant upside risk to the Street's estimate of a 20-30% drop by end-2015. Prices in the luxury segment, though, are still likely to fall 5-10%. We prefer developers and are less bullish on landlords/REITs.

- **Singapore: Differing strategies:** Going into 2H, we stick with broadly different strategies for REITs vs developers. For S-REITs, our "buy and hold" strategy is premised on the sector being impacted more by macro themes like bond yields and currency. We see a rotation into the small/mid-caps given that valuations for big-cap names look fair. We advocate a selective "trade and be nimble" strategy for developers as we see the lack of a structural re-rating story this year.

- **Australia: Growth headwinds for retail and office, fund managers and residential developers still the bright spot:** We see the A-REIT sector as fairly priced with the most earnings upside for residential developers and fund managers. Growth headwinds could persist for retail and office into FY15 with potential growth in market rents thereafter. In the interim, fund managers benefit from sustained inflows given a relatively attractive yield for Australian real estate.

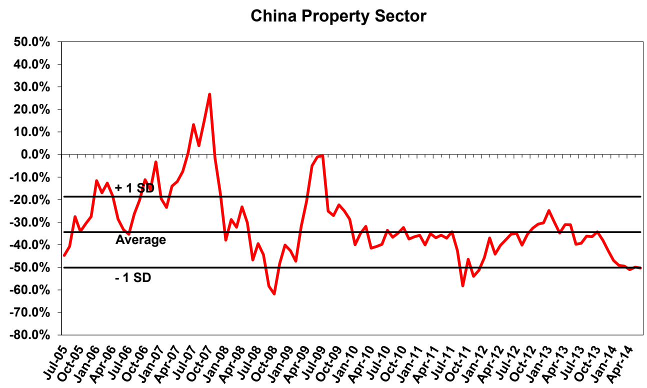
- **India –** *Sharp demand slowdown continues.* Post the elections, BSE Realty is up ~60% in the last month, with hopes of a macroeconomic recovery. However, absorption continues to decline sharply, and has now started impacting prices. **Thailand***: Presales bottomed out in 1Q14* and look set to improve in 2Q-3Q14 on improved buyer sentiment. Prefer landed property over condo.

Property: Top Buys and Top Sells

	Ticker	Rating	Price (Jun. 6)	Target Price	Yield (%)	ETR (%)	2014E P/E (x)	2014E P/BV (x)	2014E ROE (%)
Top Buys									
Charter Hall Group	CHC.AX	Buy	A$4.40	A$4.31	5.1	3.0	17.4	1.7	8.6
Continues to benefit from strong fund inflows into its funds management platform									
COLI	0688.HK	Buy	HK$19.42	HK$27.60	2.9	45.5	6.8	1.2	19.2
Steady and defensive growth with potential asset injection a catalyst									
Shimao Property	0813.HK	Buy	HK$14.56	HK$25.30	5.7	71.6	4.4	0.9	21.7
Conviction Buy among Tier 2 China players with balanced defensive growth and sales/earnings growth visibility in FY14									
SHKP	0016.HK	Buy	HK$107.70	HK$137.68	3.1	31.1	13.1	0.7	5.6
Attractive valuations with steady performance in all segments									
Sunac	1918.HK	Buy	HK$4.10	HK$8.28	8.3	107.7	2.4	0.6	29.5
After consistently posting high-growth in FY11-13E, we see Sunac's sustainable re-rating to Tier 2 as highly probable									
Top Sell									
DLF	DLF.BO	Sell	Rs233.90	Rs155.00	0.9	-32.9	34.1	1.5	4.4
Cash flows need to pick up (cash interest cost of Rs9.6bn vs operating cash flow of Rs910mn in 4QFY14). Weak demand environment continues to impact sales									

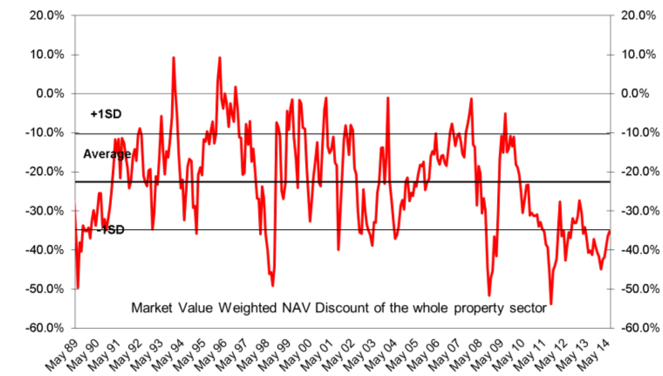
Source: Citi Research estimates

Figure 1. China Property — Discount to NAV (10 Jun 2014)



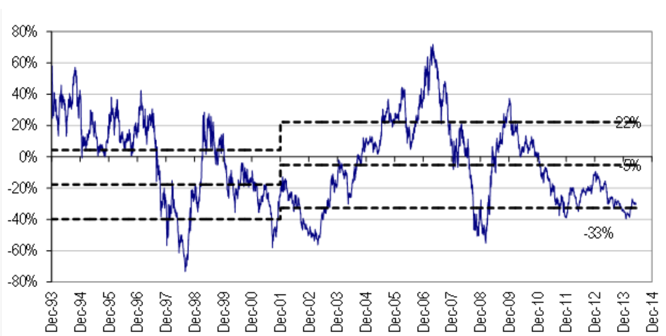
Source: Datastream; Citi Research

Figure 2. Hong Kong Property — Discount to NAV (10 Jun 2014)



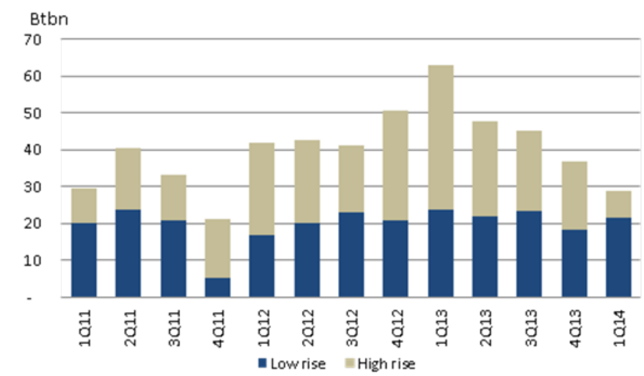
Source: Source: NBS; Citi Research

Figure 3. Singapore Developers — Historical Price to RNAV



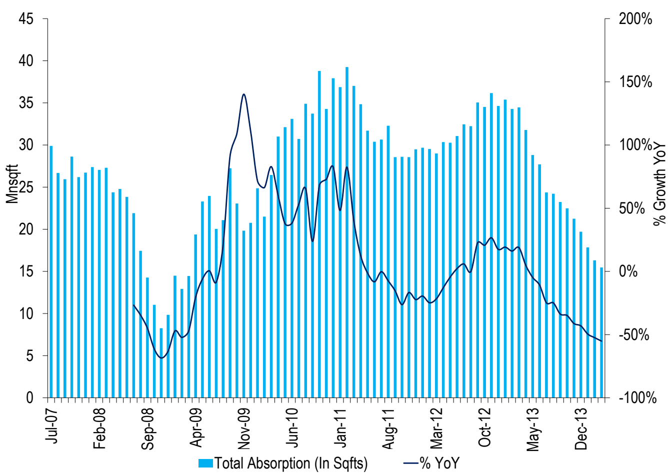
Source: Datastream; Citi Research

Figure 4. Thailand — Aggregate Presales of 7 Developers



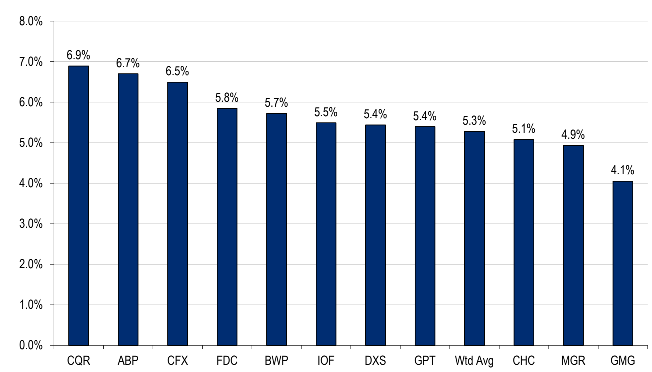
Source: Company; Citi Research

Figure 5. India — Residential Demand in Key Cities* Has Fallen Sharply



Source: Prop Equity, Citi Research, * 11 key cities excluding Mumbai

Figure 6. Australia — A-REIT Sector Dividend Yields



Source: Citi Research

Semiconductors & TFT-LCDs

Strong Logic/Memory, Weak LCD/Touch

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- **Foundry: strong growth in 2H14** – 4G LTE roll-out, smartphone demand in emerging markets and tablet demand continue to drive foundry sector demand across the board in 2014. Market share concentration in TSMC is expected to expedite in 2H14, as TSMC is only shipping small volume to Apple in 2Q, and 20nm would account for >20% of its rev in 4Q14 from less than 1% in 1Q14.

- **OSAT: sector margin expansion continues** – Our thesis of an upward margin trend in the OSAT sector from 2013 onward (thanks to increasing operating leverage, improving efficiency and maximized operation) is playing out. With the strong demand in 2H14 on-going and the possible exit of one big player from the market, we expect the margin expansion to continue.

- **Memory: Multi-year strength on DRAM consolidation and NAND discipline** − Disciplined capex by the 3 DRAM consolidators (Samsung, Hynix and Micron) should sustain current favorable DRAM dynamics (price decline within cost reduction curve) even in the mid-term. We also expect NAND dynamics will continue to improve on restocking demand kick-in along with some supply adjustment (new capacity ramp-up schedule) in 2H14E.

- **Display: Weak China TV end demand a concern; switch to value adders** – We remain cautious on commodity LCD panel makers due to weaker than expected China TV demand. Also, we do not expect the recent panel price rebound to sustain in the mid-term given inventory concerns. On the other hand, we suggest investors switch to LED names Everlight (2393.TW; NT$73.00; 1) and Epistar (2448.TW; NT$69.60; 1) on the long-term driver of surging LED lighting adoption. We also like Radiant as it should benefit from being the major supplier of multiple new products (Xiaomi TV2, potential 5.5” iPhone 6 and iTV).

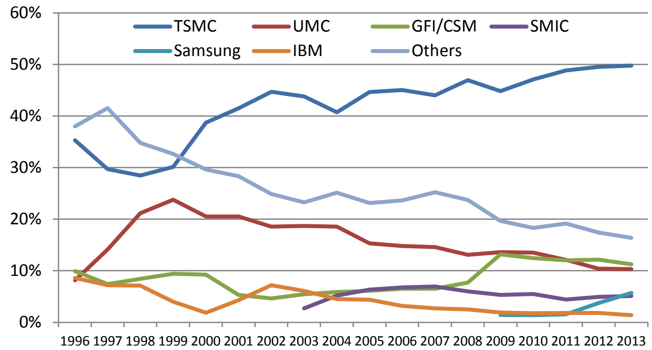
- **Touch: profit pool to shrink** − We are bearish on the industry outlook due to 1) rising competition with tier-2 makers entering the market (e.g., O-film / Henghao/ panel makers) and 2) emerging technology to cause uncertainty in the long-run.

Semiconductors & TFT-LCDs: Top Buys and Top Sells

	Ticker	Rating	Price (Jun. 6)	Target Price	Yield (%)	ETR (%)	2014E P/E (x)	2014E P/BV (x)	2014E ROE (%)
Top Buys									
LG Display	034220.KS	Buy	W26,800	W36,000	0.0	34.3	11.4	0.8	7.5
A cyclical investment case on 1) undemanding valuation, 2) passing through earnings and 3) differentiation with ongoing capacity/product shift to premium panels									
Radiant	6176.TW	Buy	NT$122.5	NT$165.0	5.7	40.4	11.4	2.4	21.6
Strong 2H recovery driven by new product cycles (larger tablets/smartphones/TV); competitive edge to sustain with LGP competence and solid client relationships									
SK Hynix	000660.KS	Buy	W46,450	W62,000	0.0	33.5	8.2	2.0	27.4
Most leveraged pure memory play on persistent strong memory fundamentals on the back of structural changes in competitive landscape									
SPIL	2325.TW	Buy	NT$50.8	NT$58.0	6.3	20.4	14.3	2.3	16.8
Strong demand in 2H14, possible exit of a big player, continuous margin expansion and market share gain									
TSMC	2330.TW	Buy	NT$122.5	NT$142.0	2.4	18.4	13.6	3.2	25.2
Strong 20nm shipment warrants ~20% HoH rev growth to TSMC in 2H14. Sustainable technology leadership in 28nm, 20nm and 16nm									
Top Sells									
Mediatek	2454.TW	Sell	NT$500.0	NT$405.0	3.9	-15.1	18.5	3.2	19.2
Lagging position in 4G LTE solutions means it will be hit by 3G to 4G migration and 3G subsidy cut									
Sharp	6753.T	Sell	Y310.0	Y210.0	0.0	-32.3	19.1	2.5	14.3
Financial condition remains crucial and LCD panel business has oversupply risk despite the demand increases in Sep-q high season									

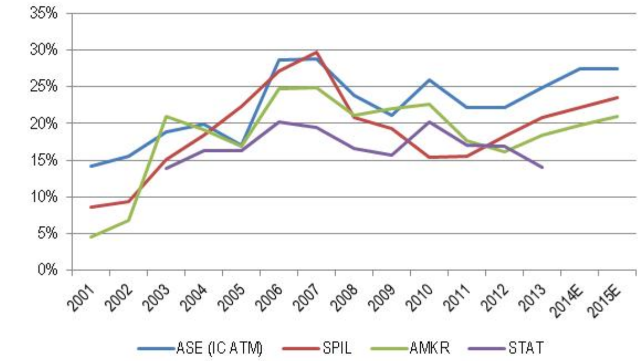
Source: Citi Research estimates

Figure 1. Foundry Market Share Trends



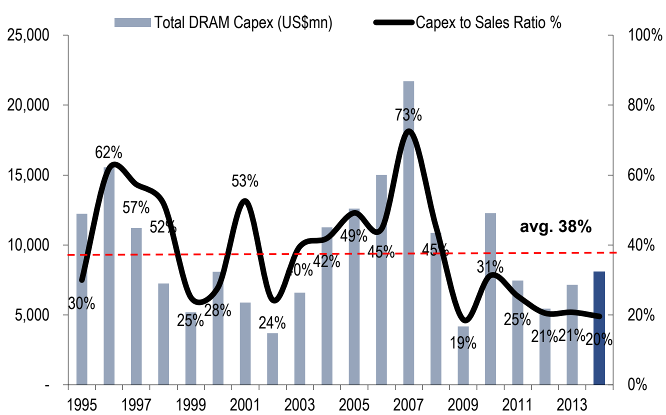
Source: Gartner

Figure 2. Gross Margin Trends of Top 4 OSAT Makers



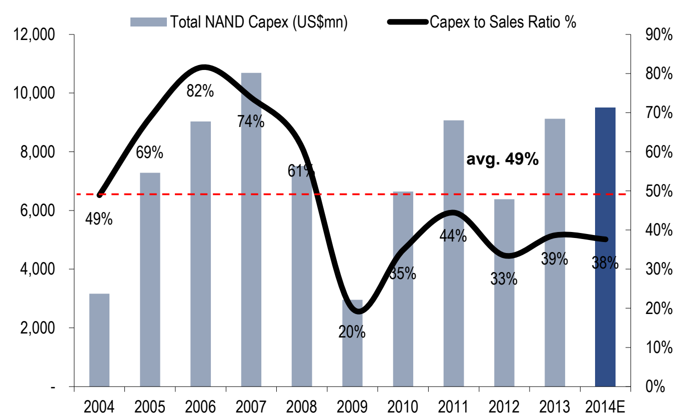
Source: Company data, Citi Research

Figure 3. DRAM – Capex and Capex/Sales Trends



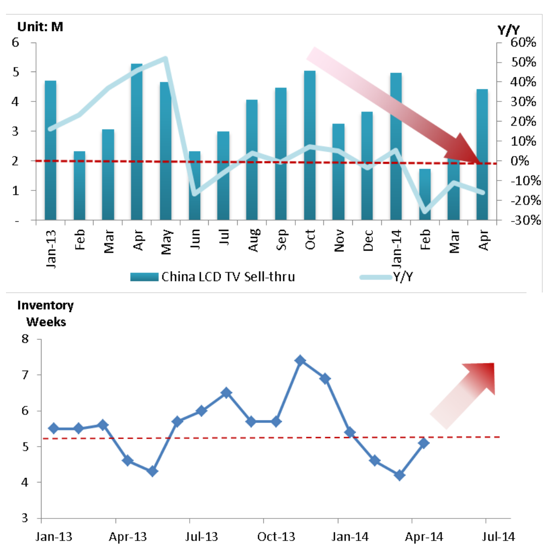
Source: WSTS, Company data, Citi Research estimates

Figure 4. NAND – Capex and Capex/Sales Trends



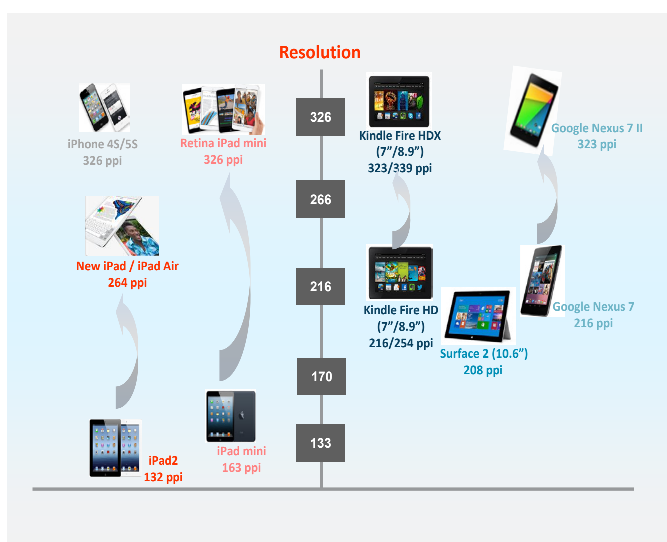
Source: WSTS, Company data, Citi Research estimates

Figure 5. China LCD TV Market Growth & Inventory Level



Source: SigmaIntell, Citi Research Estimates

Figure 6. Resolution Upgrade Trend



Source: Citi Research

Small/Mid-Caps

Prefer China Exporters and Taiwan

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Alex Chang / China

Catherine Chan / China

Ferry Wong / Indonesia

Timothy Chen / Taiwan

- **Stellar performance in India/ASEAN YTD** – Small-cap indexes YTD outperformed large-caps by 17.8% in India, 6.7% in Thailand, 6.3% in Malaysia and 4.3% in Singapore. This was partly thanks to easing concerns over US tapering and slippage of US treasury yield. ASEAN/India remain favoured shelters for global money inflows. In contrast, Indonesia/China/HK small-caps underperformed large-caps by 0.7/1.4/6.3%. We prefer China Exporters for an improving global economy and lower material costs, and are bearish on China's Materials sector given a slowdown in the domestic macro and oversupply. We like Taiwan for lower valuations than ASEAN markets.

- **Valuation screen of Regional SMID –** In view of their YTD strong performance, ASEAN markets generally are trading at premiums to their means during 1996-2013, at a 32% premium for Thailand, 20% for Malaysia and 3% for Singapore. Korea is not cheap, either, at a 25% premium on strong domestic consumption. India and China are the cheapest markets at 27% discounts to past averages.

- **China exporters performed well YTD** – We recently raised Yue Yuen to our top pick in China's export sector on the back of stock correction by >10% from YTD high and margin expansion from relocating plant away from China into Indonesia / Vietnam. Stock slippage was triggered by strike in Dongguan and anti-Chinese protests in Vietnam, but YY expects no financial impact in Vietnam. Stock will realize gross margin expansion to 21-22% in 2016E from 19-20% in 2013 on plant relocation. Compelling valuation of 9x PE and 5-6% yield for 2015E.

- **Posiflex is top pick in Taiwan, and Surya Citra Media in ASEAN** – Posiflex is a leading POS maker with own brand in Taiwan and is capturing growth momentum from global/national chains like Starbucks India, McDonald's India and Outback Steakhouse. SCM should benefit from more ad revenue from the soccer World Cup and Indonesian presidential elections. SCM's two TV stations – SCTV and Indosiar – have consistently been highest rated in Indonesia.

Small/Mid-Caps: Top Buys and Top Sells

	Ticker	Rating	Price (Jun. 6)	Target Price	Yield (%)	ETR (%)	2014E P/E (x)	2014E P/BV (x)	2014E ROE (%)
Top Buys									
China State Cons	3311.HK	Buy	HK$13.50	HK$15.40	2.0	16.0	14.9	2.8	20.5
Core proxy for China urbanization and social housing momentum. Expectation of asset injection this year									
Haier Elec Grp	1169.HK	Buy	HK$19.64	HK$25.60	0.6	30.8	17.6	4.2	28.2
Stock down >25% YTD after wider de-rating, but fundamentals remain intact for rising penetration of home appliances in rural areas									
Haitian	1882.HK	Buy	HK$17.30	HK$18.60	1.9	9.4	16.9	3.2	19.8
Remains on track to achieve double-digit earnings growth on market share gain despite weak China macro									
Posiflex	8114.TW	Buy	NT$196.50	NT$242.00	3.8	27.0	22.2	7.8	36.9
Global/national chains incl Starbucks India, McDonald's India and Outback Steakhouse are key customers with growth momentum									
Surya Citra	SCMA.JK	Buy	Rp3,510.00	Rp4,000.00	1.9	16.5	29.2	14.5	56.1
Our top media pick in Indonesia. World Cup and presidential elections this year should stimulate ad revenue growth									
Yue Yuen Ind	0551.HK	Buy	HK$24.25	HK$31.00	4.6	32.5	10.9	1.2	9.3
Top pick among China exporters for continued margin expansion and recent unwarranted stock correction									
Top Sell									
Skyworth	0751.HK	Sell	HK$3.83	HK$3.40	4.5	-6.7	6.8	1.0	15.1
Beginning phase of China smart TV price war									

Source: Citi Research estimates

Figure 1. Ranking of Small-cap P/B in Asia – Thailand the Most Expensive and India the Cheapest

		Historical range since 1996			Premium / discount:
	May-14	Historical avg	Lowest	Highest	current vs mean
Asia ex JP & AUS	1.3	1.4	0.6	2.5	-5%
Thailand	2.0	1.5	0.4	3.0	32%
S. Korea	1.3	1.0	0.3	2.3	25%
Malaysia	1.5	1.2	0.6	2.8	20%
Singapore	1.2	1.2	0.4	2.1	3%
Taiwan	1.6	1.5	0.6	3.2	3%
HK	1.0	1.1	0.4	2.2	-11%
Indonesia	1.7	2.0	0.3	6.9	-16%
China	1.0	1.4	0.4	4.6	-27%
India	1.6	2.2	0.8	5.3	-27%

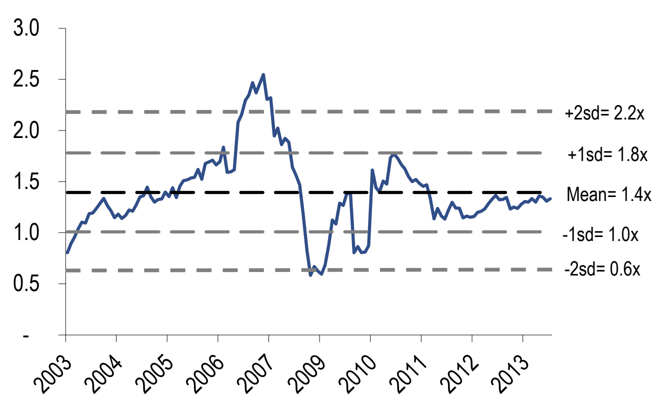
Source: Citi Research, S&P

Figure 2. Citi S&P Small-Caps Relative Performance (Small-Caps vs. Large-Caps) By Markets, 2000-14 YTD

Relative Performance	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013	1Q14	2014YTD
Pan Asia x Japan	-4.1%	11.7%	9.2%	14.0%	0.0%	4.1%	2.4%	4.0%	-7.3%	28.8%	1.0%	-7.6%	-1.0%	-0.5%	2.6%	0.6%
India	2.6%	10.1%	15.2%	70.5%	10.8%	-7.3%	-2.0%	28.6%	-9.4%	39.9%	-2.5%	-10.8%	17.8%	-16.2%	-0.2%	17.8%
Thailand	9.5%	18.5%	-9.5%	-79.3%	-7.3%	-21.3%	4.7%	-25.3%	-3.5%	32.5%	8.5%	-5.1%	10.7%	-1.0%	2.5%	6.7%
Malaysia	-15.8%	1.9%	-1.5%	-4.0%	-14.7%	-15.9%	21.5%	2.9%	-12.3%	17.5%	5.2%	-3.5%	0.8%	8.8%	4.0%	6.3%
Singapore	-0.3%	16.2%	18.3%	22.2%	9.7%	17.3%	6.0%	1.5%	-13.1%	26.3%	1.3%	-4.8%	15.3%	-5.6%	4.3%	4.3%
Taiwan	-6.5%	13.1%	17.0%	-8.5%	-5.0%	0.6%	7.0%	-5.4%	-3.0%	50.6%	-6.8%	-10.1%	6.2%	13.6%	5.1%	3.1%
South Korea	-5.9%	22.7%	-9.2%	16.4%	0.5%	34.1%	4.5%	25.5%	-4.3%	-10.7%	-11.9%	5.0%	-12.1%	-0.7%	6.4%	0.4%
Indonesia	-2.0%	-10.4%	10.5%	1.5%	-8.6%	22.1%	-9.4%	2.3%	-10.3%	-36.7%	26.0%	-1.1%	5.6%	-6.6%	6.0%	-0.7%
China	19.7%	18.4%	-19.1%	-69.1%	-4.9%	-4.9%	-8.8%	10.7%	-4.3%	58.5%	6.7%	-16.1%	5.3%	11.8%	4.5%	-1.4%
Hong Kong	-8.0%	18.0%	15.4%	43.8%	-4.4%	-8.4%	2.1%	-10.0%	-10.2%	39.0%	-9.1%	-15.7%	-10.9%	5.6%	-0.1%	-6.3%
Australia	-4.9%	4.1%	9.8%	-43.1%	17.0%	-1.9%	3.7%	-3.7%	-11.6%	19.3%	11.9%	-4.3%	-9.5%	-10.8%	-0.5%	-2.3%
Japan	13.7%	8.2%	8.2%	13.8%	6.2%	12.5%	-17.6%	-4.7%	8.8%	-0.4%	5.1%	10.3%	-2.5%	-3.3%	3.4%	3.0%

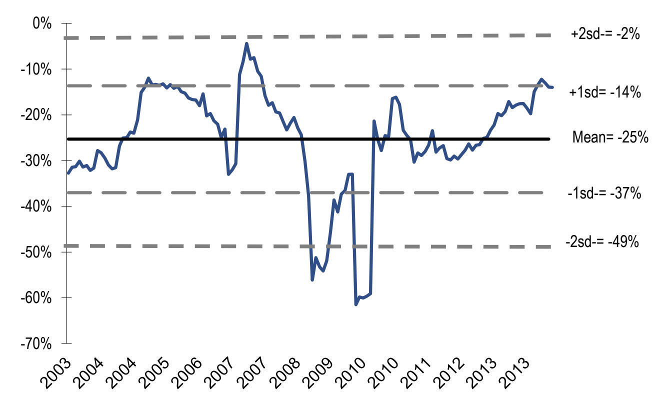
Source: Citi Research, S&P

Figure 3. Citi S&P Asia Pacific ex-Japan Small Caps Historical P/B



Source: Citi Research, S&P

Figure 4. P/B Discount of Small-caps to Large-caps in Asia ex-Japan



Source: Citi Research, S&P

Telecoms

Return and Loss of Pricing Power

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- **Competitive dynamics could start to change** – Changes in network supply/demand are creating opportunities and risk on the pricing front for Asian telecoms. While voice/data prices have dropped significantly in the past owing to excess network supply from aggressive build-outs, we see these as moderating for most markets. Given that pricing competition is driven by excess network supply, a reduction (or increase) in this will change the competitive dynamics.

- **Positive re-pricing candidates** – Indonesia and Philippines are most likely to see improvements in voice/data pricing, in our view. We see significant data demand in these markets in light of current low smartphone penetration levels (15-20%), which will rise significantly on greater handset affordability. Supply growth, on the other hand, will be fairly moderate as consolidation is more likely than expansion. PLDT, Globe (GLO.PS; P1,692.00; 1) and XL could benefit from accelerating revenue momentum.

- **Negative re-pricing candidates** – Risk is likely to materialize over the longer-term in Taiwan, Malaysia, China and India. Network supply may rise in these markets via either new entrants (licenses or MVNOs) or aggressive network build-outs/upgrades. Excessive network supply growth raises risk of softer price points. At risk, in our view, are RCOM (RLCM.BO; Rs150.70; 3H), Maxis (MXSC.KL; RM6.71; 3), FET, CHT (2412.TW; NT$96.50; 3) and TWM.

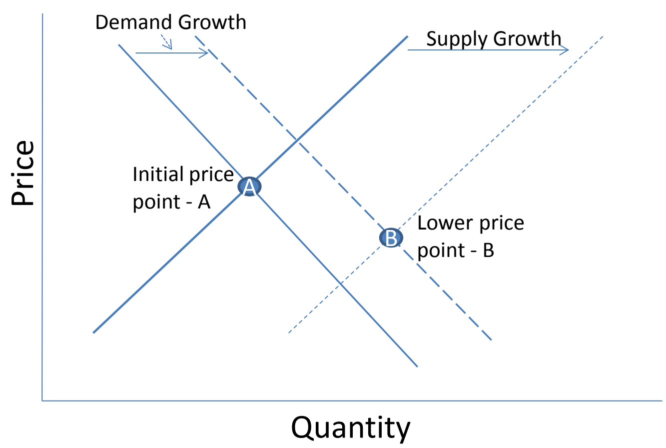
- **Yield spreads should be monitored in the near-term** – Sector valuation multiples have expanded during an extended period of low interest rates. Given Citi's outlook of rising bond yields over the next 1-2 years, we find yield spreads to be risky, with Singapore, Malaysia and Taiwan telcos trading at >1 SD below historical yield spreads. Rising bond yields may further compress yields. Indonesia and Philippine telcos, however, are far less exposed to the risk of rising rates (negative yield spread for Indonesia, above mean for Philippines).

Telecoms: Top Buys and Top Sells

	Ticker	Rating	Price (Jun. 6)	Target Price	Yield (%)	ETR (%)	2014E P/E (x)	2014E P/BV (x)	2014E ROE (%)
Top Buys									
AIS	ADVANC.BK	Buy	Bt240.0	Bt270.0	5.3	17.8	10.8	19.0	15.4
With successful 3G licensing, we forecast 22% EPS CAGR (FY14-16E) and 14% EBITDA CAGR driven by significant regulatory cost savings vs. concession agreements									
PLDT	TEL.PS	Buy	P2888.0	P3215.0	6.5	17.9	7.9	15.3	4.6
Re-pricing candidate supported by strong data demand and steady supply. Yield at ~7% is one of the highest in the region									
SK Telecom	017670.KS	Buy	W218500	W270000	4.3	27.9	3.5	8.4	1.2
Leadership with LTE build-out will likely allow SKT to take back higher ARPU, higher quality subs from LGU									
XL Axiata	EXCL.JK	Buy	Rp5250.0	Rp6500.0	0.2	24.0	7.1	nm	3.0
Re-pricing candidate supported by strong data demand growth and steady industry supply addition but XL to benefit from incremental supply from Axis acquisition									
Top Sells									
Far Eastone	4904.TW	Sell	NT$66.4	NT$53.0	5.7	-14.5	9.0	18.4	3.0
Competition to intensify, driven by increased marketing and larger handset subsidies after incumbents launch LTE service in 2H14 coupled with entry of new players									
Taiwan Mobile	3045.TW	Sell	NT$97.9	NT$82.0	5.3	-11.0	12.8	17.0	6.6
Competition to increase in both mobile services and cable TV, which together account for ~95% of EBITDA. Risk of payout cut due to high leverage									

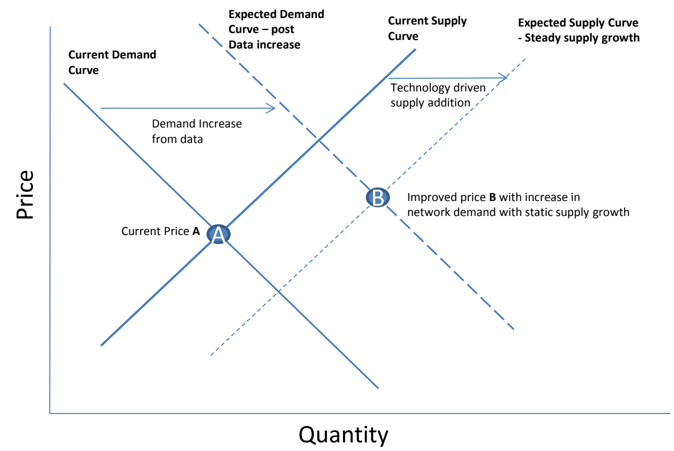
Source: Citi Research estimates

Figure 1. Negative Price Impact of Faster Supply Growth With More Limited Demand Growth



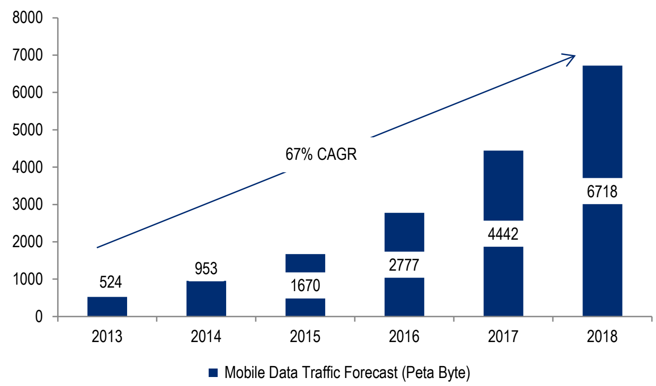
Source: Citi Research

Figure 2. Pricing Improvements When Demand Growth Outstrips Supply Growth



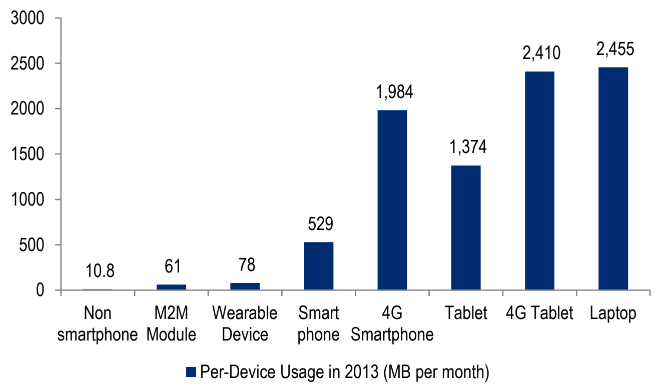
Source: Citi Research

Figure 3. Cisco VNI Asia Pacific Mobile Data Traffic Forecast



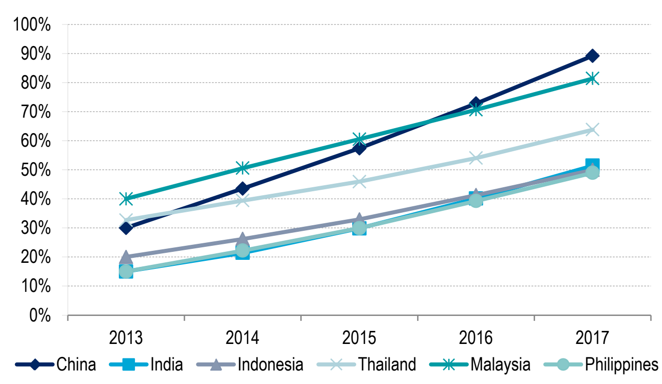
Source: Cisco, Citi Research

Figure 4. Average Monthly Data Use Per Device Type



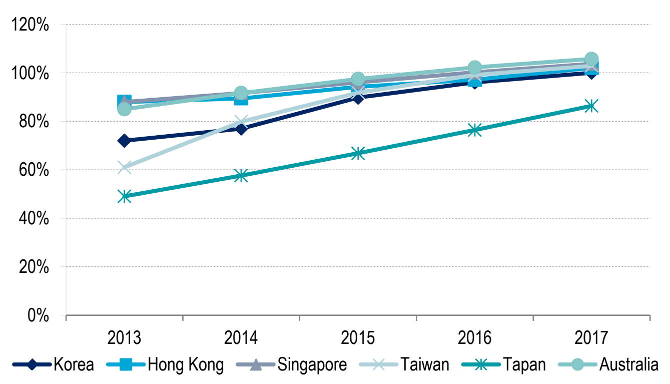
Source: Cisco

Figure 5. EM Asia – Smartphone Penetration By Market



Source: Citi Research

Figure 6. DM Asia – Smartphone Penetration By Market



Source: Citi Research

Transportation

More Constructive on China/HK Names

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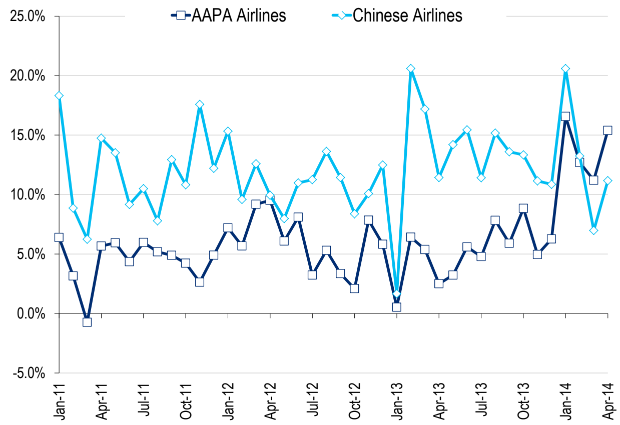
- **China/HK names to relatively outperform** – With monetary policy easing, moderate fiscal stimulus, and improving export demand (from recovery in US/EU), we expect China's economy to stabilize in 2H14. As such, we see the transportation space in China/HK outperforming ASEAN peers.
- **Airlines: Buy Air China and AirAsia** – Chinese airline yield finally stabilized in May-14. Although upside is capped with limited business traffic recovery, we believe the worst is now behind. We like Air China as it is best positioned to capture robust international outbound traffic and the future return of business traffic. While we still expect yields to drag on earnings in ASEAN, AirAsia has been aggressive in scaling back capacity and in cost-side initiatives.
- **Shipping: dry bulk to gradually improve, container remains depressed** – We continue to expect dry bulk to improve with supply/demand in balance. China's domestic coal shipments will be further supported with the scrapping of old vessels. We expect CSD to benefit from improving coal shipment volume and price, and thus to turn profitable in 2014. On the container side, large vessel deliveries and orders have continued in 2014, meaning pressure on freight rates.
- **Container ports: benefit from global trade recovery** – With the improving export trends from China/HK, we continue to like Cosco Pacific (1199.HK; HK$10.82; 1) and we recently turned positive on HPH Trust (HPHT.SI; US$0.75; 1) on easy volume comps and a relatively resilient 7% yield. We also like ICT (ICT.PS; P111.00; 1), which is uniquely positioned for a global trade recovery (as well as new projects in LatAm).
- **Airports: still well positioned long term** – We have Buys on AOT (AOT.BK; Bt195.50; 1) and MAHB (MAHB.KL; RM7.68; 1), but near-term upside maybe limited following the coup in Thailand and the MH370 incident.
- **Logistics: well-managed operators continue to grow** – While domestic consumption trends have been more muted, we continue to like KLN as a best-of-breed logistics operator with a global customer base/acquisition ambitions.

Transportation: Top Buys and Top Sells

	Ticker	Rating	Price (Jun. 6)	Target Price	Yield (%)	ETR (%)	2014E P/E (x)	2014E P/BV (x)	2014E ROE (%)
Top Buys									
Air China	0753.HK	Buy/1H	HK$4.38	HK$7.89	1.5	81.4	10.3	0.8	7.6
With its industry leadership & better capacity management, Air China is well positioned when Chinese airlines' yield stabilizes; undemanding valuations									
AirAsia	AIRA.KL	Buy	RM2.51	RM2.80	1.9	13.4	11.6	1.3	11.5
Only Buy-rated airline in ASEAN; solid cost control and capacity management									
China Shipping Development	1138.HK	Buy	HK$4.53	HK$7.37	0.0	62.4	25.4	0.6	2.3
Earnings set to turn around in 2014E on expected improvements in China's coal freight market thanks to supportive government policies									
Kerry Logistics Network	0636.HK	Buy	HK$12.10	HK$15.00	1.0	25.0	21.2	1.4	6.9
Best-of-breed logistics operator with a global customer base and acquisition ambitions									
Top Sell									
China Shipping Container Lines	2866.HK	Sell	HK$1.89	HK$1.69	0.0	-10.7	45.1	0.7	1.6
Challenging operations due to industry S/D imbalance; large exposure to Asia-Europe routes facing competition from P3									

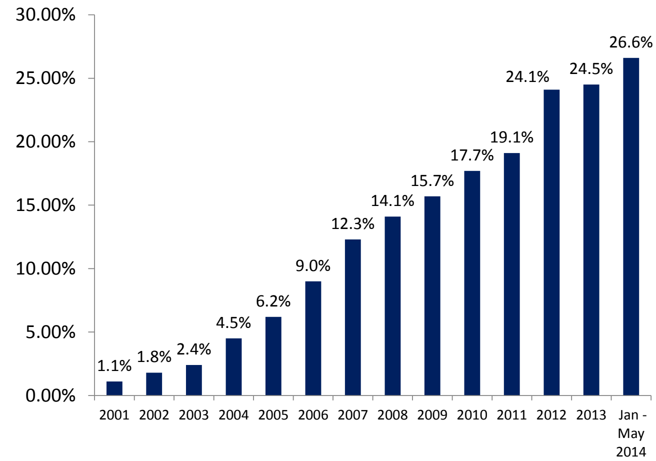
Source: Citi Research estimates

Figure 1. China and Asian Airlines: RPK Growth



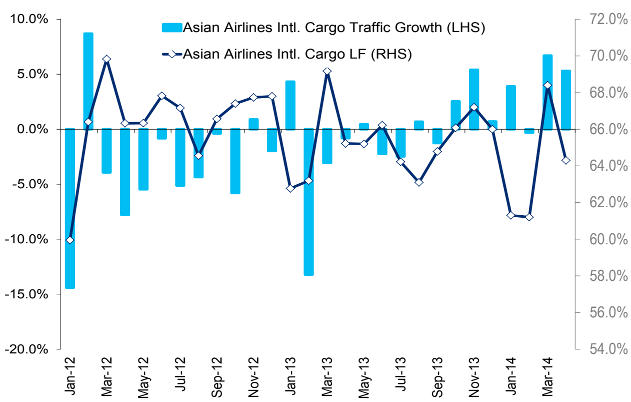
Source: AAPA, CEIC, Citi Research (AAPA member airlines include ANA, Asiana, Bangkok Airways, Cathay Pacific, China Airlines, DragonAir, EVA Air, Garuda Indonesia, Japan Airlines, Korean Air, Malaysia Airlines, Philippine Airlines, Royal Brunei Airlines, Singapore Airlines and Thai Airways)

Figure 2. Asia LCC Capacity Share (%) of Total Seats



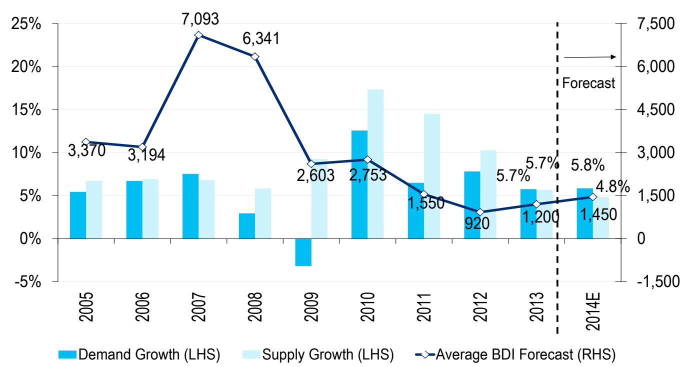
Source: CAPA, Citi Research

Figure 3. Asia Pacific Airlines International Cargo Traffic & LF



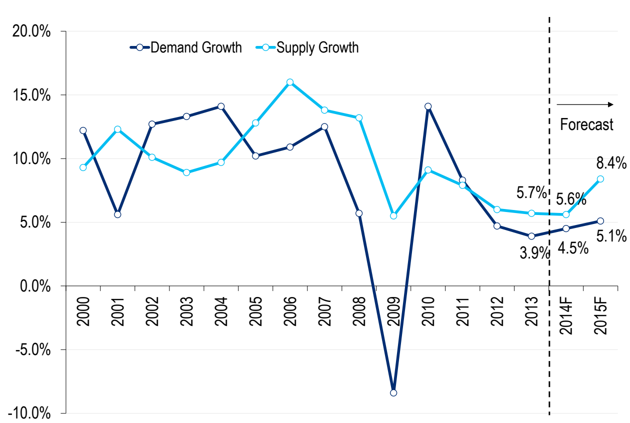
Source: AAPA, Citi Research

Figure 4. Dry Bulk Shipping Demand and Supply Forecast



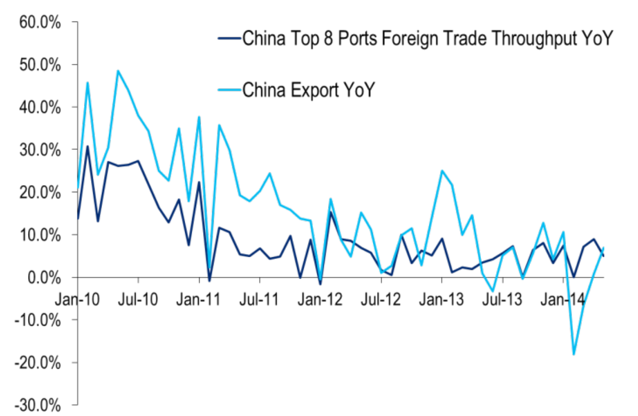
Source: Clarkson, Citi Research Estimates

Figure 5. Container Shipping Demand and Supply Forecast



Source: Alphaliner, Citi Research Estimates

Figure 6. China Port Foreign Trade Throughput vs. Export Growth



Source: Chineseport.cn, CEIC, Citi Research

Utilities

Gains from High Structural Growth and Easing Fuel Costs

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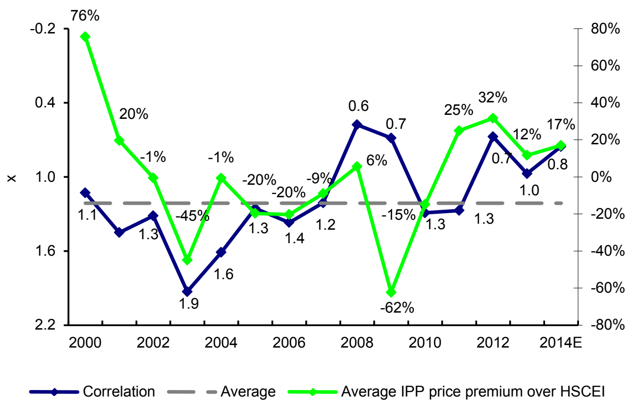
- **Summary** – Asia's utility and clean-energy sector should enjoy high structural growth in 2H14E on emission cuts, lower fuel costs and favorable govt policies, particularly in India and Korea. While new policies in China have slowed, execution of existing policies should sustain growth. Our top sector picks are CRP, Longyuan, Huaneng Renewables, ENN, Power Assets, and KEPCO.
- **PRC IPPs: Low coal costs; new capacity adds value** – Contracted coal price could -5% qoq in 3Q14E under current spot prices, positive to IPPs. CRP has high capacity growth of +16% pa in FY14-15E.
- **PRC wind: Sound fundamentals** – Longyuan's EPS would +15% yoy in 1H14E, despite wind speed cut. Huaneng Renewables' capacity +27% pa in 14-15E.
- **PRC gas: Double-digit volume growth** – PRC NG sales volumes were up 13-25% yoy in 4M14, outperforming national NG usage at +7% yoy. Share price pull-back post citygate price hike, if any, would be an enhanced buying opportunity.
- **PRC power equipment: Product mix change on emission cut** – PRC wind farm would +12% yoy to 18GW in FY14E while new coal-fired plants would -16% yoy to 30GW. We like Goldwind (2208.HK; HK$9.20; 1) for both volume and margin growth.
- **Hong Kong utilities: Proxy for bond investment** – Share-price rebound amid US$ 10-year bond yield down from 3.0% to 2.4% YTD looks unsustainable. Citi expects the yield to reach 3% in 2015E. We prefer PAH for M&A benefits.
- **Other regional utilities** – KEPCO would benefit from structural change to raise its generation from low-cost nuclear from 31% in FY13 to 37% in FY15E. We raised India's power sector to Neutral from Underweight for better gov't policy.

Utilities: Top Buys and Top Sells

	Ticker	Rating	Price (Jun. 6)	Target Price	Yield (%)	ETR (%)	2014E P/E (x)	2014E P/BV (x)	2014E ROE (%)
Top Buys									
CR Power	0836.HK	Buy	HK$20.90	HK$26.50	3.6	30.4	8.9	1.4	16.2
High capacity growth of +16% pa in 14-15E; Unit fuel cost to drop 5-6% yoy in 2014E									
ENN Energy	2688.HK	Buy	HK$53.75	HK$63.00	1.3	18.5	20.0	4.2	22.5
High NG sales volume growth of 25% pa in 2014-15E									
Huaneng Renew.	0958.HK	Buy	HK$2.79	HK$3.35	1.1	21.2	17.8	1.3	8.1
High capacity growth of 27% pa in 14-15E									
KEPCO	015760.KS	Buy	W39,750	W47,500	3.2	22.7	9.7	0.5	5.1
Structural improvement with generation mix from low-cost nuclear plants to rise from 31% in 2013 to 37% in 2015E									
Longyuan	0916.HK	Buy	HK$8.72	HK$9.50	1.1	10.0	18.7	1.7	9.4
Recurrent profit growth of 21% yoy in FY14E and 18% yoy in FY15E									
Power Assets	0006.HK	Buy	HK$66.40	HK$75.00	3.8	16.8	2.4	1.0	56.7
HK$40bn or 30% of market cap is net cash available for EPS-accretive M&As, after spinning off HK power business in Jan 2014									
Top Sells									
HKCG	0003.HK	Sell	HK$16.86	HK$14.55	2.0	-11.7	25.0	3.3	13.7
20% share price rally in 5M14 solely due to US$ 10-year bond yield down from 3.0% to 2.4%, which Citi expects to reverse; De-rating from more risky new energy business									
HK Electric Investment	2638.HK	Sell	HK$5.22	HK$4.30	7.2	-10.4	9.4	0.7	9.5
Distribution cuts on higher interest costs from 2017E; De-rating on rising yield curve									

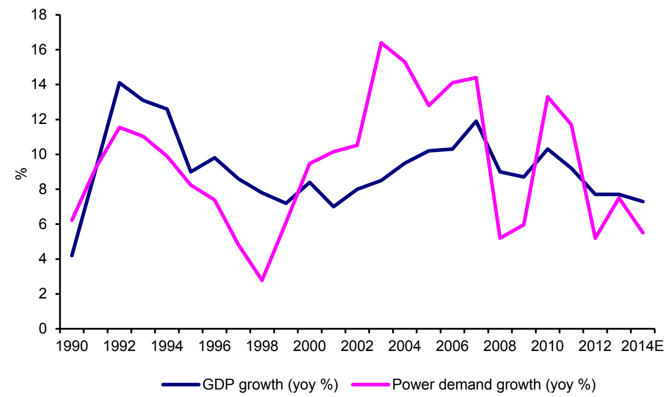
Source: Citi Research estimates

Figure 1. Correlation between (i) multiple of PRC annual power demand growth vs. PRC annual GDP growth; and (ii) relative performance of PRC IPP share prices and HSCEI



Source: National Bureau of Statistic and Citi Research Estimates

Figure 2. PRC Annual Power Demand and GDP Growth



Source: NDRC, China Electricity Council and Citi estimates

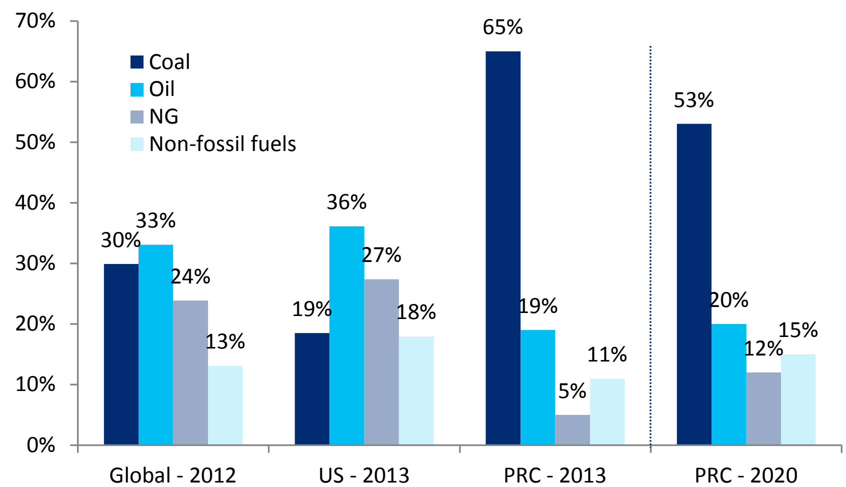
Figure 3. PRC IPPs: FY14E Net Profit Sensitivity

(Rmbm, except HK$m for CRP)	Huaneng	Datang	Huadian	CRP	CPI	Average
Base case net profit	**11,819**	**4,004**	**4,375**	**11,164**	**2,573**	**n/a**
Case 1. Net profit change with extra 1% cut in average coal price	370	129	177	265	62	n/a
% change	3.1%	3.2%	4.0%	2.4%	2.4%	3.0%
Case 2. Net profit change with extra 1% cut in power tariff	-684	-258	-356	-524	-111	n/a
% change	-5.8%	-6.4%	-8.1%	-4.7%	-4.3%	-5.9%
Case 3. Net profit change with extra 1% increase in utilization hours	286	127	150	242	42	n/a
% change	2.4%	3.2%	3.4%	2.2%	1.6%	2.6%
Case 4. Net profit change with extra 25bp interest rate cut	223	240	163	149	50	n/a
% change	1.9%	6.0%	3.7%	1.3%	1.9%	3.0%

Huaneng Power International (0902.HK; HK$7.83; 1); China Resources Power (0836.HK; HK$21.35; 1); Datang International Power Generation (0991.HK; HK$3.15; 1); China Power International (2380.HK; HK$2.87; 1); Huadian Power International (1071.HK; HK$4.56; 1)

Source: Company Reports and Citi Research estimates

Figure 4. Primary Energy Consumption Composition Comparison in 2013 and PRC in 2020



Source: CPNN

Economics

Asia Economics

'Goldilocks' Returns, But the Bears Still Linger

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- **Exports moderately strengthening, divergent domestic demand dynamics.** Financial conditions look tight in CN, IN & ID but still growth supportive in others, and optimism for structural reforms post-election has risen in both IN & ID.

- **Inflation looks benign for most…**Core inflation/inflation expectations muted for most which supports our view that CN has space to ease. We believe the three countries worth watching are ID, PH and MY. Indo inflation is above target and we see greater odds of a subsidized fuel price hike before year-end (which would be credit positive). PH has the most positive output gap in Asia plus weather-related price risks and overly accommodative monetary setting may warrant the start of rate hikes in 3Q14. MY is already signaling the start of rate hiking cycle in Jul driven more by financial stability concerns as persistently negative real rates and resilient growth could spur excessive risk taking.

- **Financial Stability concerns could weigh more heavily on policy decisions.** Our expectation of a very gradual pace of Fed Funds adjustment (only 2% rate by end of 2016) alongside ECB now expected to launch QE in 2H14 should still be risk-supportive, but also raises risks that EM Asia's financial cycle gets extended further, which could exacerbate financial imbalances and output volatility later on. This likely factors into CN's reluctance for broad-based easing and raises lingering questions on how to time the reversal of macroprudential tightening when the financial cycle turns.

- **"Goldilocks scenario" remains conducive to extended carry trades.** We see three viable triggers for a sharp disruption: 1) bigger positive US data surprises with inflation building that could prompt a sharp re-pricing of expectations on Fed Funds rates – we don't see material inflation building just yet – thus, a low inflation recovery in US would still be carry-friendly; 2) policy miscalculation by CN that could spark a big enough shock to financial stability and risk appetite – but we think there are still policy levers that can be used to contain these risks (though this is a worry); 3) big political shocks, e.g. risk for serious post-election disappointments from IN or ID. Our base case is a market positive outcome on both elections and policies – in the event we are wrong on the latter, we think there's still some time before the markets face a serious enough risk of disappointment.

Figure 1. Key Macro Forecasts

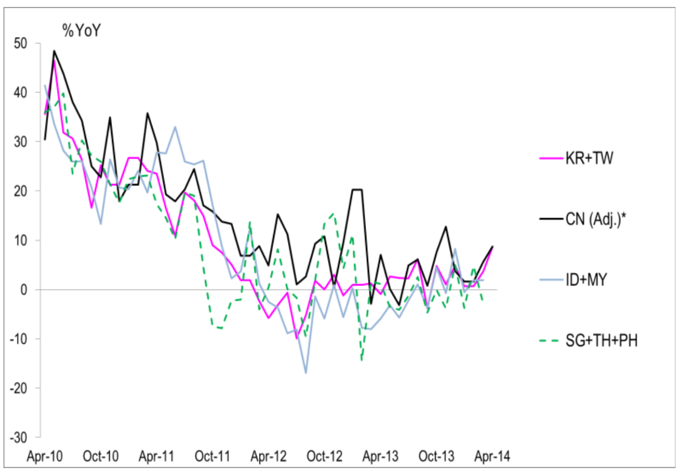
	GDP Forecasts (%YoY)			CPI Forecasts (%YoY)			CAB Forecasts (% of GDP)		
	2013	2014F	2015F	2013	2014F	2015F	2013	2014F	2015F
Asia-Pacific	6.3	6.2	6.3	3.7	3.5	3.8	2.2	2.1	1.5
Asian NIEs	2.9	3.6	3.9	1.7	2.1	2.7	8.3	7.0	6.3
SEAN	5.2	4.5	5.3	4.3	4.8	4.9	-0.5	0.6	0.0
China	7.7	7.3	7.0	2.6	2.6	3.2	2.0	2.0	1.5
Hong Kong	2.9	3.2	3.6	4.3	3.9	3.7	2.1	2.8	3.2
India**	4.9	5.6	6.5	9.5	8.0	6.5	-2.0	-2.3	-2.5
Indonesia	5.8	5.3	5.5	6.4	6.5	6.7	-3.3	-2.4	-2.1
Malaysia	4.7	5.4	5.6	2.1	3.5	4.5	4.0	4.4	4.0
Mongolia	11.7	10.0	9.0	10.5	13.1	12.0	-30.9	-17.9	-19.7
Philippines	7.2	6.9	7.3	2.9	4.1	4.0	3.5	3.4	2.9
Singapore	3.9	3.5	4.0	2.4	1.8	1.3	18.3	18.0	18.0
South Korea	3.0	3.9	4.0	1.3	2.1	3.1	6.1	3.9	2.9
Sri Lanka	7.3	7.2	7.4	6.9	5.7	6.5	-3.9	-3.3	-3.0
Taiwan	2.1	3.2	3.8	0.8	1.2	2.0	11.7	11.0	10.2
Thailand	2.9	0.5	2.8	2.2	2.4	2.1	-0.7	2.2	-1.1
Vietnam	5.4	5.7	5.9	6.6	5.4	6.8	5.3	4.1	2.9

Note: * Asian NIEs are Hong Kong, Korea, Singapore, and Taiwan. ** SEAN-4 includes Indonesia, Malaysia, the Philippines and Thailand. Asia-Pacific is Asian NIEs + SEAN-4 + China + India + Mongolia + Sri Lanka + Vietnam, GDP-weighted. *** India Fiscal year runs from April-March.
Source: CEIC Data Company Limited, and Citi Research estimates.

While exports are looking better, domestic demand dynamics varies

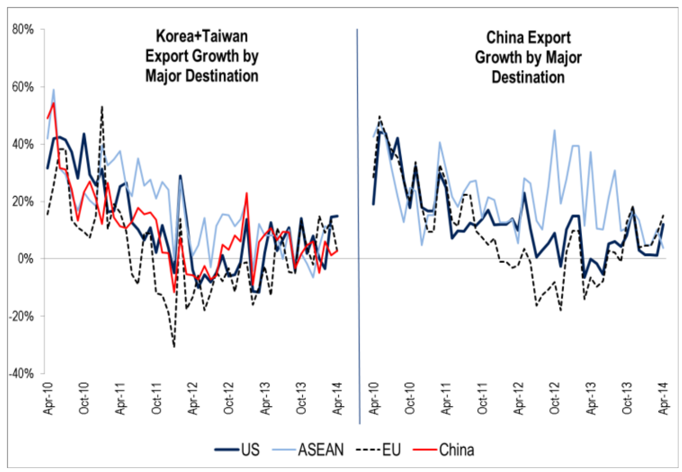
More signs of life in EM Asia's exports, but nothing to write home about. If March was a mixed bag for exports, April has so far been decisively more positive, though the growth momentum among the North Asian exports still looks relatively subdued by historical standards (Figure 2) and while US data continues to gradually improve, China and other parts of EM continue to face growth headwinds. The multi-speed global growth backdrop can be seen in the divergence in performance of export markets – both China, Korea and Taiwan all show a more pronounced pick-up in growth of exports to the US, but they diverge on growth momentum for both exports to EU and ASEAN, plus NIEs are showing more subdued export growth to China even after Chinese New Year (Figure 3). On a sectoral level, tech exports in North Asia seem to be doing particularly well (especially in Korea) – the expected launch of iPhone 6 in July/Aug could provide a bit of boost for Taiwan tech exports by mid-year, but ASEAN tech exports lost momentum (again) highlighting the still volatile nature of this industry and, perhaps, the lack of follow thru business investment pick up in the US so far.

Figure 2. Asia's Export Growth (%YoY) – Moderate improvements underway….



Source: CEIC, Citi Research; Note: *We adjust the China export series for the export over-invoicing via HK; We also smooth out for the lunar new year effect.

Figure 3. … but one can clearly see the impact of the multi-speed world as % YoY export growth diverges by geography

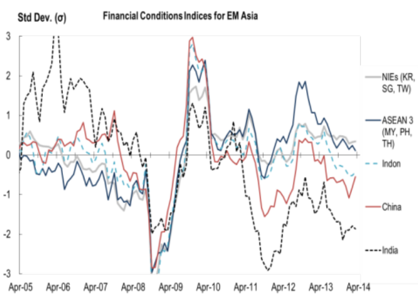


Source: CEIC, Citi Research

Ability of financial conditions to support domestic demand growth varies substantially across the region. Our Citi Financial Conditions Indices (FCI) for China, India and Indonesia are all acting as constraints to economic activity, with the latter two exacerbated by the impact of need to curb the CA deficit (Figure 4). However, financial conditions in most others have been marginally supportive so far. GDP data in 1Q14 point to a mixed picture – we think China's GDP growth is much weaker than what was officially reported and still points to further slowdown,[1] while Indonesia's 1Q14 data also surprised to the downside, alongside Thailand, Singapore and Hong Kong. However, Malaysia's and, to a lesser extent, Korea's economic activity both surprised to the upside. Cyclical and structural factors point to varied growth vulnerabilities in domestic demand – Korea and Taiwan seem to be seeing some domestic demand rebound alongside net exports after years of subdued performance, while China and Indonesia's domestic demand slowdown look more concentrated on investments than consumption. We argued in the previous monthly that we think private consumption growth in Thailand, Malaysia

[1] See *China Macro View - A Reality Check on GDP Deflator and Job Creation* (9-May-2014).

Figure 4. Financial Conditions are tight in China, India & Indonesia vs. history, but still slightly growth supportive in others

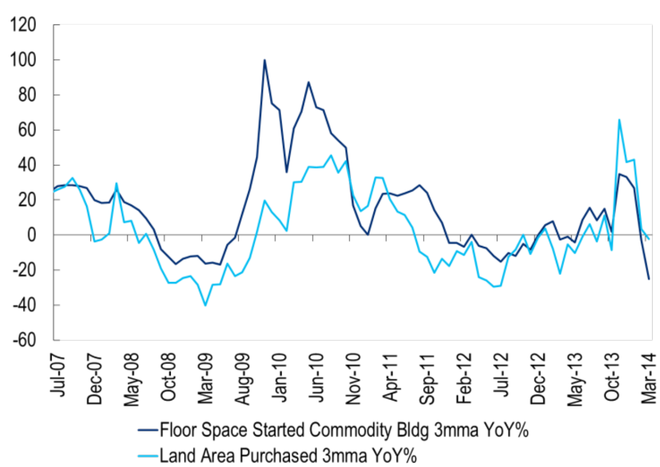


Source: Citi Research estimates
Note: For details on methodology, see *Asia Macro View - Financial Conditions Present a Mixed Picture for EM Asia*.

and Singapore are more vulnerable to high levels of household debt.[2] However, a more pronounced secular weakness in private consumption seem more visible in Singapore, given that consumption has been crimped further by macro-prudential curbs like TDSR caps, slowing labor productivity growth, and real wage growth. Thai consumption weakness is a combination of debt overhang and idiosyncratic political shocks while Malaysia's private consumption has defied expectations and proved resilient so far in 1Q14, but should inevitably slow.

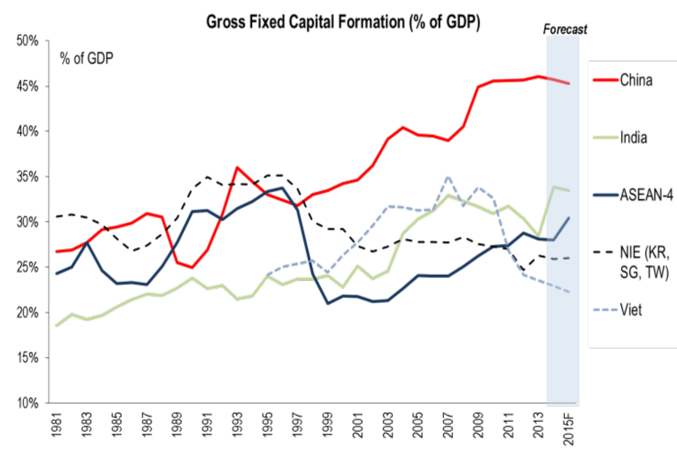
The outlook for investments will vary depending on both demand factors influenced by varying financial conditions, but also more structural/supply-side issues related to debt overhang and diminishing potential returns among the more industrialized Asian countries. Our biggest worry continues to be China, especially given the unprecedented credit-fueled investment growth in the post-GFC years and now the deteriorating conditions in the property sector that could feed into broader based investment slowdown (Figure 5)[3]. Vietnam's investment has already been going through more than three years of massive bank deleveraging that may further be weighed down by the FDI vulnerabilities following recently damaging serious anti-China riots. However, even though financial conditions still look supportive among other countries – Korea & Taiwan seem to be on a modest upswing, growth in domestic investment may still be constrained by constraints to potential growth in the higher income countries of Korea, Singapore and Taiwan. With decent dose of structural reforms and stable macro environment, we think investment prospects are most promising in South and Southeast Asia (Figure 6). Recent landslide win by India's BJP led coalition bodes well for a rebound in India's investment given the high priority by the new leadership, as highlighted in the BJP manifesto, and we already anticipate a reversal of declining investment to GDP ratio as soon as this FY 2015.

Figure 5. China – Indicators for property investment signal a sharp downturn — Floor Space Starts and Land Purchase, 3mma YoY%



Source: CEIC, Citi Research

Figure 6. Historical and Forecast path for Gross Fixed Capital Formation, as a % of GDP

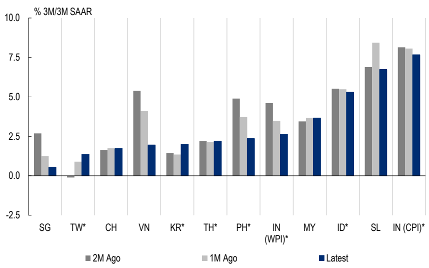


Source: CEIC, Haver, Citi Research

[2] See *Asia Macro and Strategy Outlook - Dissecting 3Ds: Debt, Demographics & (Income) Disparity* (2-May-2014).

[3] For more details on deterioration in property sector, please see *China Macro View - Risk of a Property Market Slump: The Tail Is Getting Fatter* (19-May-2014).

Figure 7. EM Asia - Core Inflation remains manageable in most places, measured in %3M/3M SAAR



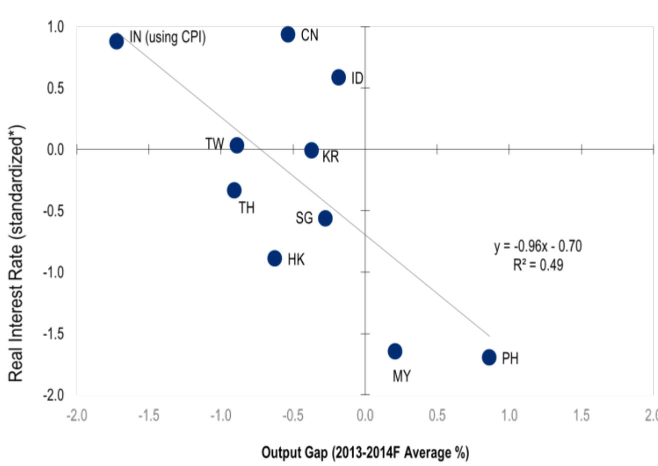
Source: CEIC, Haver, Citi Research
*Note: official core inflation for IN, ID, KR, PH, TH, and TW

Inflation looks manageable for most, but there are exceptions

Inflation pressures remain fairly benign for most… Unlike the gradual build-up of inflation in the early post GFC years in early 2010 from very depressed levels, sparking much talk about normalizing policy rates in the region, overall inflation momentum has been largely muted, and has been particularly benign in the case of China, thus warranting our view that PBoC has policy space to ease. We expect they could relax M2 growth targets, ease macro-prudential policies on property and, eventually, cut RRR rates (though the hurdle for a broad-based easing as opposed to targeted easing seems high). A big drive of recent modest positive inflation surprises in a few places, namely India, Taiwan and Thailand – have largely been driven by food inflation, but we see limited second round effects so far. Core inflation across the board has been generally benign (Figure 7) and we estimate most economies are operating on narrowing but still negative output gap (Figure 8).

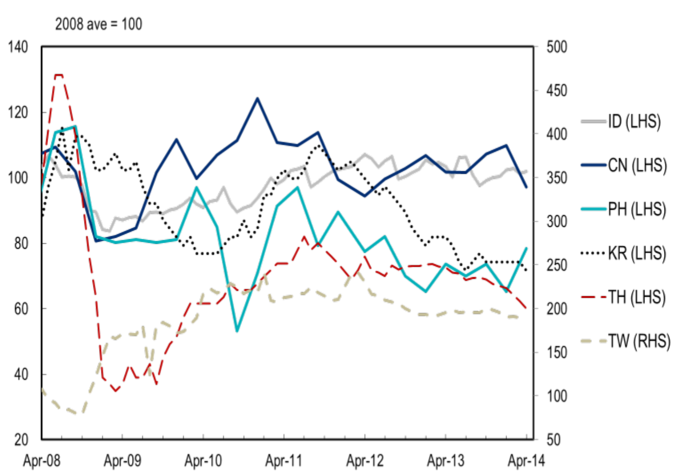
We think there are three worth watching – Indonesia, Philippines and Malaysia. Indonesia's inflation is expected to persist well above the official target (4.5%-5.5% in 2014F, 4-% in 2015F), and the odds of pending subsidized fuel price hike forecast by year-end has risen significantly as we expect presidential elections will conclude by July, leading us to raise our end-2014 inflation forecast to 7.3% (vs. 5.3%). As the economy has been slowing, we don't expect much second round inflationary impact but we wouldn't rule out further rate hikes starting 4Q14. Philippines is facing the "quadruple risks" of strong growth driving positive output gap, very low real rates, abundant liquidity and scorching hot weather driving up food prices, all of which make a recipe for potentially unhinging inflation expectations (Figure 9). BSP is likely to tighten further beyond the benign 200bps RRR hikes since March, we think by hiking by ~100bps in the next 12 months starting in 3Q14. However, if USD strength remains muted for longer, the risk that BSP adjusts more slowly will rise. Similarly, though we think Malaysia is a less severe case of demand-driven inflation risk given dissipating effect of administered price adjustments, we think BNM will start hiking rates in July (another 25bps in Sep and possible more thereafter) for financial stability reasons, as persistently negative real rates and resilient growth could spur excessive risk taking.

Figure 8. Expected Real Interest Rate vs. Output Gap



Source: Bloomberg, Consensus Economics, Citi Research
Note: Real interest rate is the short-term (policy) rate discounted by the forward looking 12M consensus inflation forecasts normalized over 10yr history

Figure 9. Inflation expectations seem very well anchored (except Philippines needs monitoring)

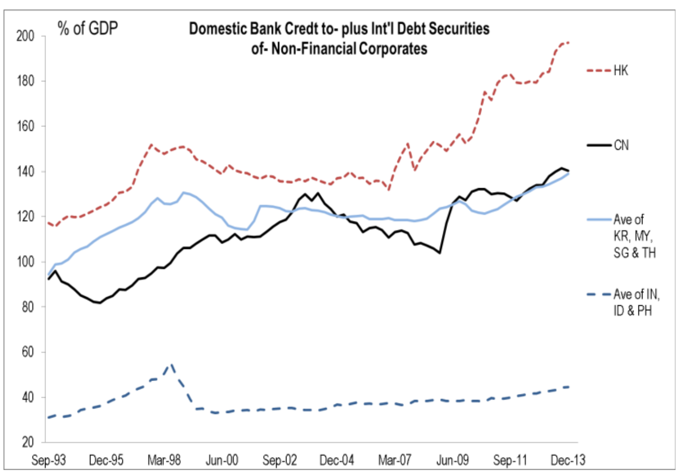


Source: CEIC, Citi Research; Note: Korea, Philippines and Thailand survey inflation expectations in the next 12months while China, Indonesia and Taiwan survey future price expectations (in 6M for ID & TW);

Should financial stability weigh more heavily on monetary policy decisions?

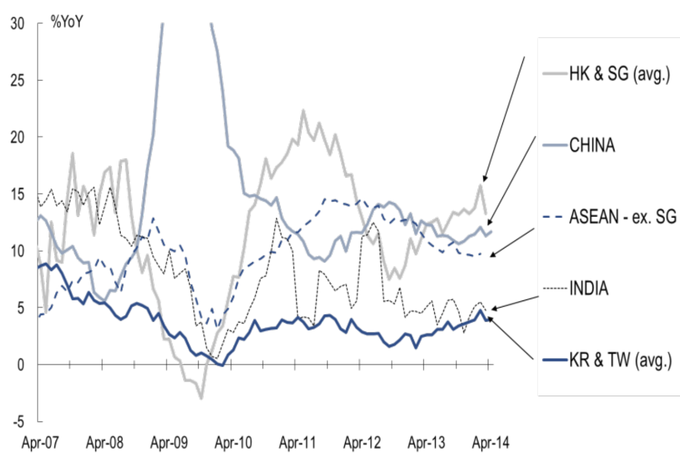
The likely action facing BNM in July of needing to curb financial vulnerability from excessive risk-taking raises an **important question on the extent to which Asian CBs should lean more heavily against the wind of the region's financial cycle.** While we expect the Fed's ongoing withdrawal of QE and pending rate hike is partly due to the need to unwind risks to credit overheating/asset bubbles (alongside improving growth), it is likely that Fed hiking cycle will continue to be a gradual adjustment and that the longer term equilibrium for the Fed Funds rate will still be lower than where it was historically (projected to be only ~2% by end-2016, or 175bps in 2.5years, as opposed to the 425bps Fed Funds hikes in 2 years (from mid-2004 to mid-2006). Expectation of such extended and gradual approach to withdrawing of Fed's accommodative monetary policies alongside ECB now expected to move in the opposite direction this year has helped keep barometers of risk appetite such as US 10yr term premium and the VIX supportive, but also raises concerns about the disconnect that arises between asset prices and fundamentals as well as worries that the financial cycle in Emerging Asia will be lengthened further, going into 6th or 7th year (Figure 10). This could exacerbate financial imbalances and create greater risk of output volatility later on once the Fed starts hiking.[4]

Figure 10. History of domestic bank credit + international debt securities by Nationals (% of Country GDP)



Source: Haver, BIS, IMF, CEIC, Citi Research
Note: The international debt securities data are based on the nationality and not residency of the issuer. We didn't add cross border bank claims as there will be double-counting with the IMF IFS data on domestic bank claims.

Figure 11. Credit Growth in Real Terms (%YoY)



Source: Haver, CEIC, Citi Research

It is always complex to diagnose an unsustainable credit boom versus a healthy dose of financial deepening needed for economic development. While empirical studies show that a banking crisis is always preceded by a credit boom, the other way around is more often than not untrue – i.e. in majority of the cases, credit booms don't lead to a banking crisis. However, findings from Dell'Ariccia et al (2012) show that, among 170 countries they analyze from 1960s to 2010 citing 175 episodes of "credit booms", 60% of those cases are followed by subpar economic

[4] This is a recurring issue we've discussed in the past. For example, see *Asia Macro and Strategy Outlook - Time to Lean (a Little More) Against the Wind* (21-Apr-2011) and *Asia Macro and Strategy Outlook - On the Lookout for Excessive Leverage* (1-Mar-2013).

recoveries.[5] In the absence of clear systemic fragilities in the banking system in Asia (to be discussed in the next section), it is the subpar nature of recovery amid an already subdued but improving global growth backdrop that lingering worries are centered on.

Credit booms can be defined in varying ways – one can look at the rate of growth of credit in real terms, as in Figure 11, which suggest that real credit growth via the banking system was particularly strong among offshore financial centers (HK and Singapore) and China (and the latter will likely be even higher if we include shadow banking sources of financing). Another approach is to de-trend credit data using HP filter and establish a threshold beyond which a deviation from trend is identified as a credit boom. A simpler benchmark, but one that must be interpreted with caution, is to look at the rate in which credit has expanded vis-a-vis GDP – we shade a rather arbitrary threshold of 5ppts, based on a benchmark used for a broader definition of credit boom in an IMF (2011) event study.[6] Based on this metric, and discounting episodes where the increase in credit to GDP was driven by a negative shock to the denominator (post GFC quarters or the floods that hit Thai GDP on a rolling 4qtr basis from 4Q2011 to 1H 2012), it is clear that where the bank credit boom seems particularly long and pronounced is in Singapore, China (especially if we include HK) and Malaysia, though if we add credit via off balance sheets of the banks and non-bank financial corporations, the situation in China is the bigger issue, alongside Thailand and Malaysia (relating to households). Thus, the threat of subpar recovery on the domestic demand side could loom larger here, but with global liquidity conditions still somewhat supportive, and Fed Governor Janet Yellen signaling only a gradual rise in policy rates, plus no obvious signs of fragility in the banking system, this raises the odds that this financial cycle could be lengthened further in some countries.

This is where macro-prudential policies (MPPs) are supposed to come in to lean against the wind, to mollify the amplitude of the financial cycle in order to reduce the vulnerabilities later on. IMF finds that Asia is already the most proactive region globally in using MPPs in recent years, especially when it relates to housing market, with loan to value caps being the most popular.[7] So far, along with a host of other housing related measures (including stamp duties), residential mortgage-related lending seems to have slowed much more dramatically in the heavy MPP-users with the most negative real interest rates – HK and Singapore (Figure 12), but seems elevated everywhere else except KR & TW (rising from the lows), highlighting the need to be vigilant. Financial disintermediation of savings and regulatory arbitrage (e.g. the rise of China's shadow banking) is still a risk when real rates stay too low for too long, and we welcome BNM's signal to act. The lingering question will be how to time the reversal of MPP tightening when the financial cycle turns in order to prevent excessive and destabilizing de-leveraging. We think this is an issue China may need to confront earlier on, but others like Singapore and HK would need to also address once the Fed starts hiking interest rates next year. The jury is still out on how orderly this process will be.

Banks of more levered countries seem to have decent capital buffers, but the system is not really being tested yet. We have seen bank liquidity (via LTDs) tighten across most countries varying degrees in recent years except the Philippines, where deposit growth far outstripped loan growth (Figure 13). Financial

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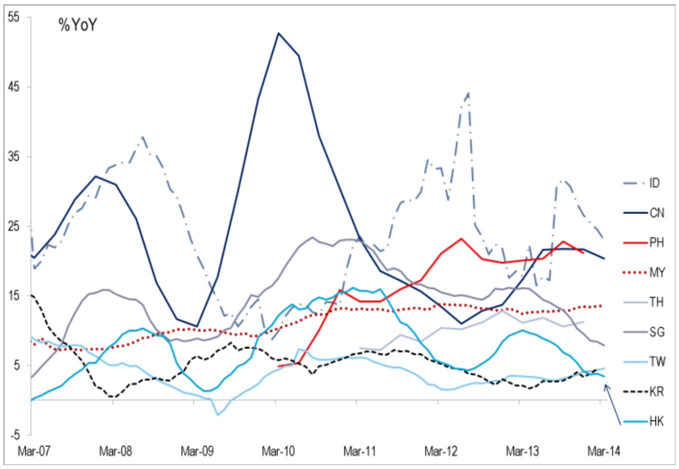
[5] G. Dell'Ariccia, D. Igan, L. Laeven, H. Tong, B. Bakker & J. Vandebussche. "Policies for Macrofinancial Stability: How to Deal with Credit Booms." *IMF Staff Discussion Note* (June 2012).

[6] International Monetary Fund. "Toward Operationalizing Macroprudential Policies: When to Act?". Chapter 3, *Global Financial Stability Report* (Sep 2011)

[7] See Chapter 4. Of IMF's Regional Economic Outlook – Asia Pacific (April 2014).

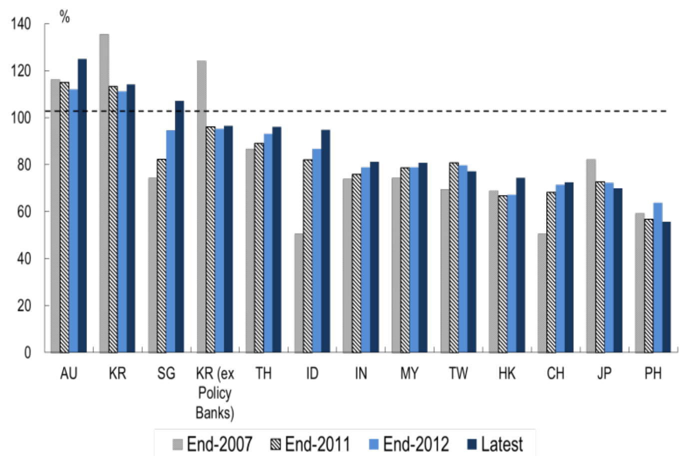
cycle has already been correcting in Indonesia, but we believe leverage is not a systemic issue. Moreover, most banks in EM Asia have decent capital buffers, and at least for the more levered countries people tend to worry about the most – China, Singapore, Thailand and Malaysia – capital ratios seem to have broadly improved since 2007. Nonetheless, it's far from clear what the eventual losses will be when the credit cycle turns, especially if we also get a sharp correction in property-related collateral values, and thus, the need for supervisory authorities to remain vigilant.

Figure 12. Residential Mortgages to Households (%YoY, in local currency)



Source: CEIC, Citi Research; Note: We look at the data on real estate lending under households/consumer loans category, or explicitly when mentioned as residential mortgages, to distinguish this from lending to property developers.

Figure 13. Asian Banks – Loan to Deposit Ratios (%), 2007, 2011, 2012, latest



Source: CEIC, Citi Research

What could spark a serious end to this period of calm for risk assets? We see three potential viable triggers, <u>none seems imminent to us</u>: <u>First</u>, US data surprising to an even greater degree than expected, especially with signs of inflation building that could prompt a sharp recalibration of expectation in Fed rates. There could already be a few hiccups later on this year as we expect US data will continue to improve, and the exaggerated moves on US treasuries correct itself (we forecast 10yr Treasury yield at 3.2% by year-end); <u>Second</u>, policy errors/miscalculation by Chinese authorities on the extent of slowdown (with rising defaults) that could spark a big enough shock to financial stability and overall risk appetite; and <u>Third</u>, some unforeseen geopolitical shock that seriously threatens growth prospects globally/in the region and inflicts sufficient damage to risk appetite. In the last few years, we've seen the election of more right-biased nationalist leaders in the region -- Shinzo Abe in Japan, Geun-Hye Park in South Korea, and more recently, a landslide victory for Narendra Modi in India. We think single-party political systems such as those run by both the Communist parties in China and Vietnam intrinsically lean on nationalism. Adding territorial disputes to the mix doesn't help. Others worry that a correction to the frothier valuations in US equity markets could be the trigger, but with US data surprising to the upside now, we don't see a correction to be meaningfully large enough to prompt a sustained broad-based risk sell-off.

There is also the risk that election-related optimism in market-favored India and Indonesia lead to disappointments later on, but we don't see that as an imminent shock in the next 2 months (even much longer in Indonesia since new government doesn't take office until Oct) – "honeymoon period" where there is some benefit of the doubt will likely lingering around the first 100 days in office. A key event to watch in India is the new government budget out in early July.

Global Political Insights

Beware the *Vox Populi*

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- **This year, the political risk temperature has been high. But markets have barely batted an eyelash, localizing these risks.** Could this uncoupling be misplaced as QE recedes?

- **It seems like political risk is on the front page every day: crowds of protestors gathering, a rally calling for independence, a military coup, or scenes of civil conflict.** Is there more unrest globally, or is 24/7 media coverage creating this perception? Is social media to blame? We think the answer to this question lies in better understanding what we call ***Vox Populi risk***, a new variation of political risk which we have been tracking for the past two years. We define *Vox Populi* risk as shifting and more volatile public opinion that poses ongoing, fast-moving risks to the business and investment environment.

- **There has been a dramatic and measurable increase in the number of elections, mass protests and government collapses over the past three years — a 54% increase versus the previous decade — as well as a proliferation of new and fringe political parties, many of which are anti-establishment.** The new *Vox Populi* is being fueled by growing perceptions of incoming inequality and anxiety about globalization, particularly amongst middle classes. In developed markets, this has resulted in new and alternative political parties which are having an impact on policy debate and increasing the formation of fragile coalitions and referendum risk.

- In **emerging markets**, there is a greater chance of street demonstrations, rebellions and sustained tensions that elections may fail to resolve. In some cases, local protests can become geopolitical risks almost overnight, as in the Syrian civil war and Ukraine's Euromaidan. For petrostates, a fall in petroleum prices is leading to an outcry for improved governance and a more equitable distribution of income.

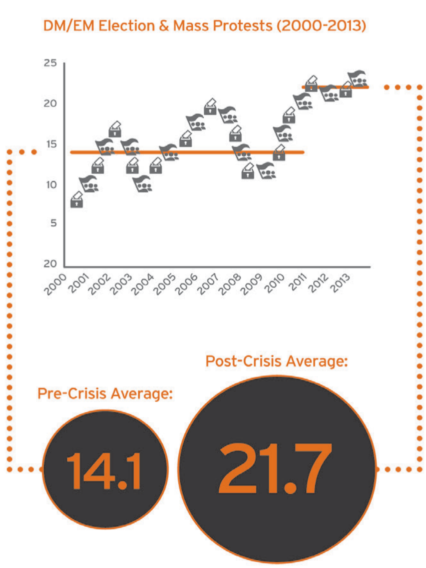
- In **Europe**, anti-establishment and euroskeptic parties had their strongest-ever showing in May's European Parliament elections. These groups, and not the left, are now the European political alternative, signaling challenges ahead in further political contests. These parties are a mixed group of Brussels critics, anti-system populists, and traditional nationalists, even extremists, with little in common that would unite them in Strasbourg. More notably, many are attempting to re-brand their appeal to attract a broader segment of discontented voters. Heading into the 2015 election cycle, this vote represents a significant "midterm" signpost for the embattled national governments.

Figure 2. Major Political Developments of the First Half of 2014

Russia-Ukraine crisis	South China Sea tensions
Thailand coup d'etat	Syrian civil war
Libya coup d'etat	Iran nuclear negotiations
South African election gives ANC a reduced majority	Turkey local elections and AKP hegemony
India election gives BJP landslide	European elections & the rise of non-mainstream parties

Source: Citi Research

Figure 4. The Yearly Average of Elections and Mass Protests in Major Markets Has Jumped 54% in the Post-Crisis Environment



Source: Citi Research

Figure 1. Political Signposts – 2014 2H

July 9	Indonesian presidential election
July 13	Slovenian parliamentary election
August 10	Turkish presidential election
September 14	Swedish general elections
September 18	Scottish independence referendum
September 20	New Zealand general elections
October 5	Brazilian general elections (runoff on October 26)
November	Lebanese parliamentary election (tentative)
November 4	United States midterm election
November 9	Catalonia independence referendum (Spain)
December	Last date for Romanian presidential election

Source: Citi Research

Figure 3. For More Information on *Vox Populi* Risk, See Our New Report:

Citi GPS: TAKING IT TO THE STREETS - What the New Vox Populi Risk Means for Politics, the Economy and Markets

Source: Citi Research

The second half of the year will feature several significant political signposts, both in DM and EM. We're tracking key EM elections in Indonesia, Turkey and Brazil, as well as United States midterm elections, and high-profile independence votes in Scotland and Catalonia. In the background, ***geopolitical risks in the Middle East and in the Asia-Pacific*** continue to simmer, with tensions spiking periodically. Nevertheless, we see little appetite either to resolve these tensions or conversely to exacerbate them, suggesting they will continue to disrupt local markets on occasion.

In **Indonesia**, as in India earlier this year, the opposition is expected to take power. The opposition PDI-P has nominated popular Jakarta governor Joko Widowo. The presidential election is July 9. In **Turkey and Brazil,** the storyline is shaping up to be incumbent re-election. Prime Minister Recep Tayyip Erdogan's AKP party maintained control in March's local elections, putting Erdogan on track to become Turkey's first executive president despite public discontent and corruption scandals. The Turkish election is August 10. The Brazilian election will heat up after the World Cup in Rio de Janeiro. President Dilma Rousseff's approval rating has improved, but she faces both challenges from Aecio Neves and Eduardo Campos, as well as the criticism of the business community for her economic policies. Rousseff leads her closest rival Neves, 41%-22% in the latest Datafolha poll, suggesting a runoff may be the base case. The election is October 5, with a runoff on October 26.

In the **United States**, Republicans' chances to regain the US Senate have risen, with a minimum of three pickups likely. Still, control of the Senate will come down to races in individual states like Louisiana, Arkansas, Alaska and North Carolina. The outcome may be uncertain right through election night. The election is November 4.

In the textbook cases of what we call ***referendum risk***, independences votes will take place in **Scotland and Catalonia** in the second half of the year. As these DM governments struggle with regionalism, secessionism and a drive for the return of sovereignty, even a failed vote may set the stage for a market-moving surprise. Based on today's polling, we expect the vote in Scotland to fail. The latest Survation poll shows the 'No' side up by 10%. In Catalonia, the two-part ballot question may keep the region inside Spain but force Madrid's hand on greater devolution of power. Scotland votes on September 18, and Catalonia on November 9.

Figure 5. Major-Market Elections for 2015-2016

2015	**Date**	**Citi GDP 2014F**		**Governing Party**	**Government Orientation**
Nigeria	February 14	6.4%	↔	People's Democratic Party	Center-right
Finland	April (TBD)	1.1%	↑	Coalition Party (coalition)	Center-right
United Kingdom	May 7 (TBD)	3.6%	↔	Conservative Party (coalition)	Center-right
Turkey (legislative)	June 13	3.5%	↑	AKP	Center-right
Mexico (legislative)	July 5	4.0%	↑	PRI	Center-left
Denmark	September (TBD)	1.5%	↑	Social Democrats (coalition)	Center-left
Argentina	October (TBD)	0.0%	↑	Front for Victory	Center-left
Canada	October (TBD)	2.7%	↔	Conservative Party	Center-right
Poland	October (TBD)	3.6%	↔	Civic Platform (coalition)	Center-right
Portugal	October (TBD)	2.0%	↑	Social Democratic Party	Center-right
Spain	December (TBD)	1.6%	↑	Partido Popular	Center-right
2016	**Date**	**Citi GDP 2015F**		**Governing Party**	**Government Orientation**
Croatia	February (TBD)	1.2%	↑	Social Democratic Party (coalition)	Center-left
Taiwan	March	3.8%	↑	Kuomintang	Center-right
South Korea	April	4.0%	↔	Saenuri Party	Center-right
Ireland	April (TBD)	3.3%	↑	Fine Gael (coalition)	Cross-party
Japan (Upper House)	July (TBD)	0.9%	↓	Liberal Democratic Party	Center-right
United States	November 8	3.1%	↑	Democratic Party	Center-left
Russia (legislative)	December	2.3%	↑	United Russia	Centrist
Australia	January 2017 (TBD)	2.9%	↔	Liberal Party (coalition)	Center-right

Source: Citi Research. GDP forecasts are given for the year prior to the election.

Will 2015 will be another political year? The focus may return to a slow-growth Europe, with elections in Portugal, Spain, the United Kingdom and Poland. In May's European Parliament elections, many parties in government fared notably poorly. The broader Union-wide move against austerity will likely be anchored further, as socio-economic conditions have not materially improved in most EU states, even if growth is nominally improved or positive. In the face of such voter discontent, ***the likely policy impact will come from national governments who feel compelled toward a more populist tone***. For that reason, political risk from government policy is likely to rise in these member states. For example, we expect the British Conservatives to continue to press immigration, European devolution, and even a Brexit referendum as issues as they attempt to fend off UKIP in next year's UK election.

Appendix A-1

Analyst Certification

The research analyst(s) primarily responsible for the preparation and content of this research report are named in bold text in the author block at the front of the product except for those sections where an analyst's name appears in bold alongside content which is attributable to that analyst. Each of these analyst(s) certify, with respect to the section(s) of the report for which they are responsible, that the views expressed therein accurately reflect their personal views about each issuer and security referenced and were prepared in an independent manner, including with respect to Citigroup Global Markets Inc and its affiliates. No part of the research analyst's compensation was, is, or will be, directly or indirectly, related to the specific recommendation(s) or view(s) expressed by that research analyst in this report.

IMPORTANT DISCLOSURES

Hyundai Marine & Fire (001450.KS)

Ratings and Target Price History
Fundamental Research

Analyst: Ss Kim

	Date	Rating	Target Price	Closing Price
1	30-Sep-11	1M	*38,000.00	29,350.00
2	7-Oct-11	Stock rating system changed		

	Date	Rating	Target Price	Closing Price
3	7-Oct-11	*1	38,000.00	29,350.00
4	23-Apr-12	*2	*34,000.00	32,250.00

	Date	Rating	Target Price	Closing Price
5	8-Jan-13	*3	*27,000.00	32,100.00

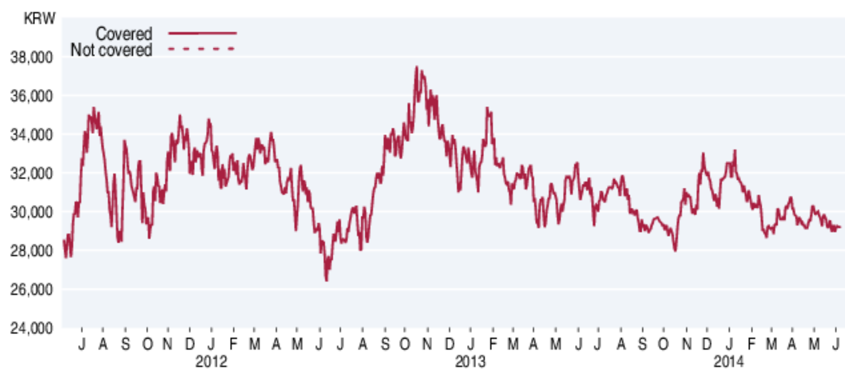
* Indicates change

Rating/target price changes above reflect Eastern Standard Time

Hyundai Marine & Fire (001450.KS)

Ratings and Target Price History
Best Ideas Research
Relative Call (3 Month)

Analyst: Ss Kim



* Indicates change

Rating/target price changes above reflect Eastern Standard Time

Hyundai Heavy Industries (009540.KS)

Ratings and Target Price History
Fundamental Research

Analyst: Ethan Kim

	Date	Rating	Target Price	Closing Price
1	2-Oct-11	1M	*436,000.00	281,000.00
2	7-Oct-11	Stock rating system changed		
3	7-Oct-11	*1H	436,000.00	302,000.00
4	9-Jul-12	1H	*340,000.00	262,000.00
5	13-Aug-12	1H	*300,000.00	243,500.00
6	18-Oct-12	*1	*290,000.00	247,000.00
7	17-Jun-13	*2	*220,000.00	193,500.00
8	4-Jul-13	2	*200,000.00	177,000.00
9	6-Feb-14	*3	*170,000.00	213,000.00
10	12-May-14	3	*155,000.00	185,000.00

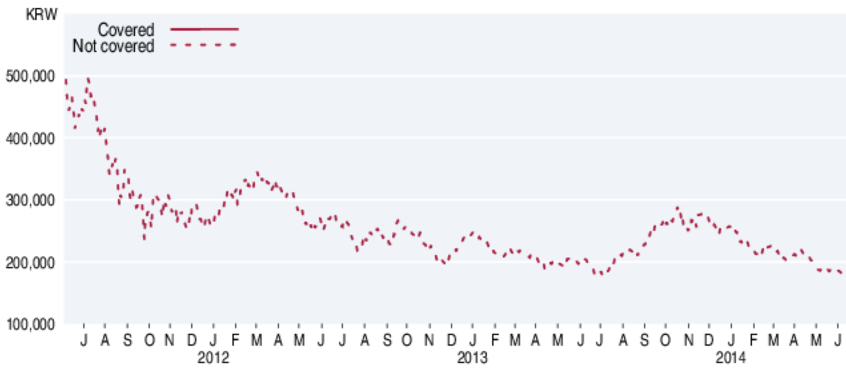
* Indicates change

Rating/target price changes above reflect Eastern Standard Time

Hyundai Heavy Industries (009540.KS)

Ratings and Target Price History
Best Ideas Research
Relative Call (3 Month)

Analyst: Ethan Kim



* Indicates change

Rating/target price changes above reflect Eastern Standard Time

KEPCO (015760.KS)

Ratings and Target Price History
Fundamental Research

Analyst: Pierre Lau, CFA

	Date	Rating	Target Price	Closing Price
1	17-Aug-11	1L	*30,000.00	21,650.00
2	7-Oct-11	Stock rating system changed		
3	7-Oct-11	*1	30,000.00	21,800.00
4	5-Dec-11	1	*32,000.00	25,200.00
5	16-Feb-12	1	*30,000.00	24,900.00
6	8-Oct-12	1	*35,000.00	27,700.00
7	15-Mar-13	1	*39,000.00	31,100.00
8	12-Aug-13	1	*38,000.00	29,550.00
9	11-Feb-14	1	*43,500.00	36,500.00
10	13-May-14	1	*47,500.00	40,800.00

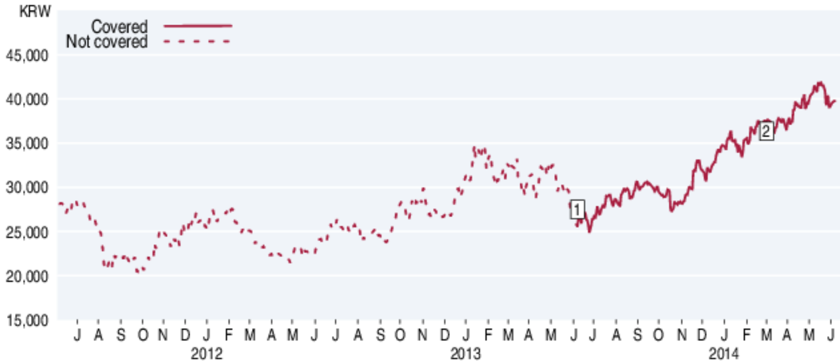
* Indicates change

Rating/target price changes above reflect Eastern Standard Time

KEPCO (015760.KS)

Ratings and Target Price History
Best Ideas Research
Relative Call (3 Month)

Analyst: Pierre Lau, CFA



	Date	Rating	Target Price	Closing Price
1	7-Jun-13	*ADD MP	-	25,600.00
2	3-Mar-14	*REM MP	-	37,550.00

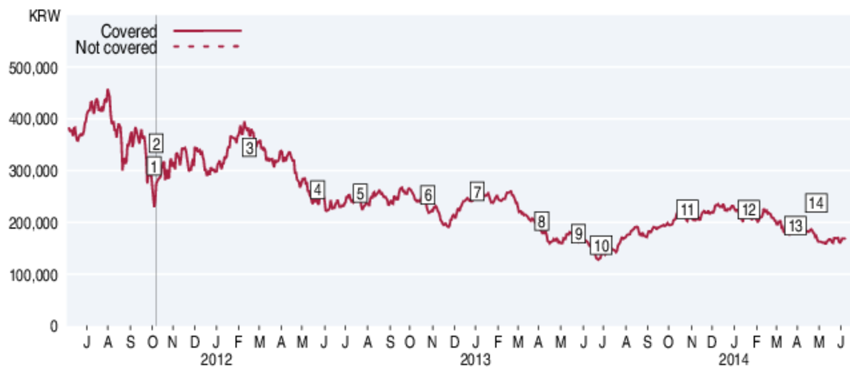
* Indicates change

Rating/target price changes above reflect Eastern Standard Time

Lotte Chemical (011170.KS)

Ratings and Target Price History
Fundamental Research

Analyst: Oscar Yee



	Date	Rating	Target Price	Closing Price
1	5-Oct-11	*2H	*285,000.00	229,500.00
2	7-Oct-11	Stock rating system changed		
3	16-Feb-12	2H	*390,000.00	369,000.00
4	23-May-12	2H	*295,000.00	237,000.00
5	23-Jul-12	2H	*285,000.00	245,000.00
6	25-Oct-12	2H	*280,000.00	222,500.00
7	3-Jan-13	*1	*320,000.00	260,000.00
8	4-Apr-13	1	*275,000.00	182,000.00
9	27-May-13	1	*255,000.00	162,000.00
10	27-Jun-13	1	*195,000.00	136,500.00
11	28-Oct-13	1	*240,000.00	202,500.00
12	22-Jan-14	1	*280,000.00	216,500.00
13	28-Mar-14	1	*260,000.00	188,000.00
14	28-Apr-14	1	*235,000.00	173,500.00

* Indicates change

Rating/target price changes above reflect Eastern Standard Time

Lotte Chemical (011170.KS)

Ratings and Target Price History
Best Ideas Research
Relative Call (3 Month)

Analyst: Oscar Yee

	Date	Rating	Target Price	Closing Price
1	30-Jan-13	*ADD MP	-	249,500.00
2	27-May-13	*REM MP	-	162,000.00

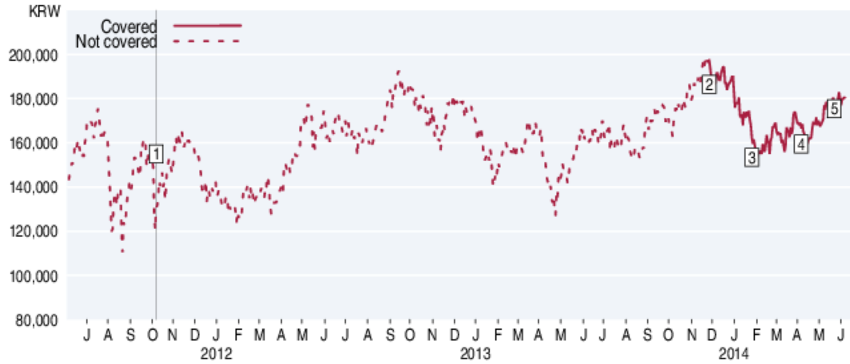
* Indicates change

Rating/target price changes above reflect Eastern Standard Time

Hyundai Wia (011210.KS)

Ratings and Target Price History
Fundamental Research

Analyst: Ethan Kim
Covered since November 27 2013



Date	Rating	Target Price	Closing Price
1 7-Oct-11	Stock rating system changed		
2 27-Nov-13	*1	*245,000.00	197,500.00
3 26-Jan-14	1	*220,000.00	168,000.00
4 7-Apr-14	1	*210,000.00	166,500.00
5 22-May-14	1	*225,000.00	178,500.00

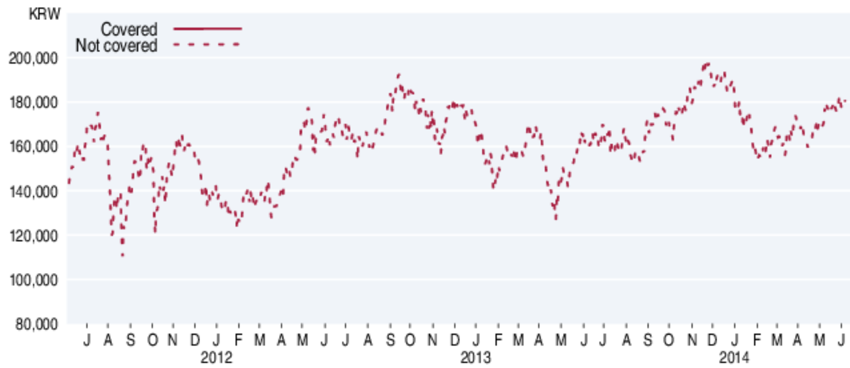
* Indicates change

Rating/target price changes above reflect Eastern Standard Time

Hyundai Wia (011210.KS)

Ratings and Target Price History
Best Ideas Research
Relative Call (3 Month)

Analyst: Ethan Kim
Covered since November 27 2013



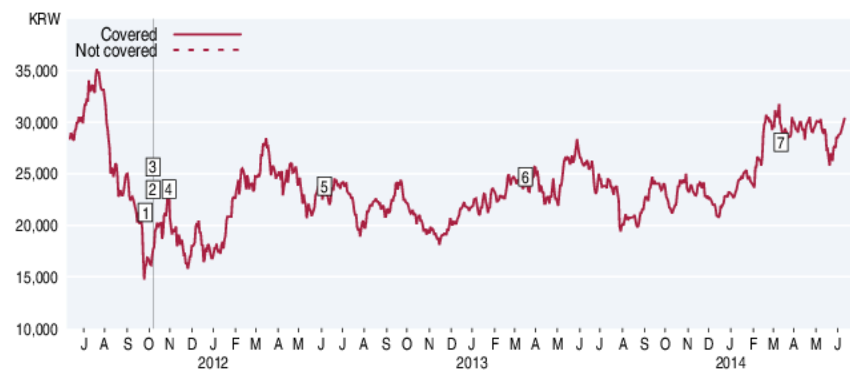
* Indicates change

Rating/target price changes above reflect Eastern Standard Time

Hyundai Development (012630.KS)

Ratings and Target Price History
Fundamental Research

Analyst: Sungmee Park, CFA



Date	Rating	Target Price	Closing Price
1 27-Sep-11	*1M	*23,700.00	16,000.00
2 7-Oct-11	Stock rating system changed		
3 7-Oct-11	*1H	23,700.00	17,700.00
4 31-Oct-11	*2H	*23,500.00	23,350.00
5 6-Jun-12	2H	*24,000.00	23,250.00
6 18-Mar-13	*3H	*21,000.00	24,000.00
7 13-Mar-14	3H	*26,000.00	29,650.00

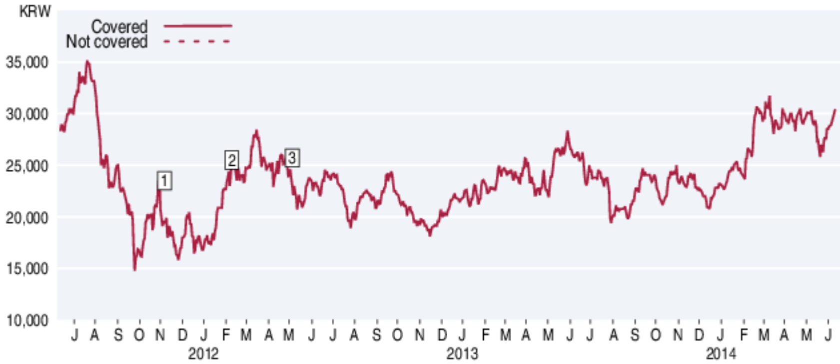
* Indicates change

Rating/target price changes above reflect Eastern Standard Time

Hyundai Development (012630.KS)

Ratings and Target Price History
Best Ideas Research
Relative Call (3 Month)

Analyst: Sungmee Park, CFA



	Date	Rating	Target Price	Closing Price
1	7-Nov-11	*REM LP	-	19,550.00
2	9-Feb-12	*ADD LP	-	25,400.00
3	4-May-12	*REM LP	-	23,000.00

* Indicates change

Rating/target price changes above reflect Eastern Standard Time

SK Hynix (000660.KS)

Ratings and Target Price History
Fundamental Research

Analyst: Henry H Kim, CFA

	Date	Rating	Target Price	Closing Price
1	21-Jul-11	1M	*39,000.00	23,650.00
2	31-Aug-11	1M	*36,000.00	19,100.00
3	7-Oct-11	Stock rating system changed		
4	7-Oct-11	*1	36,000.00	21,500.00
5	27-Oct-11	1	*35,000.00	23,800.00
6	7-Dec-11	1	*33,000.00	22,400.00
7	21-Feb-12	1	*34,000.00	28,300.00
8	28-Mar-12	1	*41,000.00	30,550.00
9	26-Jul-12	1	*39,000.00	20,400.00
10	26-Jun-13	1	*45,000.00	30,250.00
11	10-Jan-14	1	*52,000.00	38,500.00
12	9-Jun-14	1	*62,000.00	46,450.00

* Indicates change

Rating/target price changes above reflect Eastern Standard Time

SK Hynix (000660.KS)

Ratings and Target Price History
Best Ideas Research
Relative Call (3 Month)

Analyst: Henry H Kim, CFA

	Date	Rating	Target Price	Closing Price
1	16-Mar-12	*REM MP	-	28,800.00

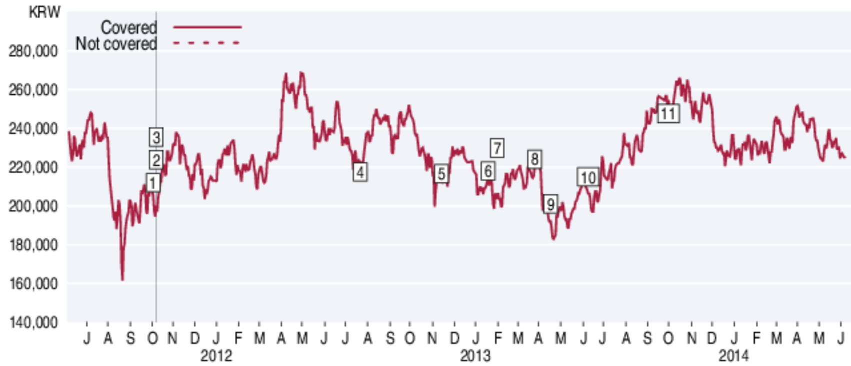
* Indicates change

Rating/target price changes above reflect Eastern Standard Time

Hyundai Motor (005380.KS)

Ratings and Target Price History
Fundamental Research

Analyst: Ethan Kim



	Date	Rating	Target Price	Closing Price
1	4-Oct-11	1M	*320,000.00	205,000.00
2	7-Oct-11	Stock rating system changed		
3	7-Oct-11	*1	320,000.00	200,000.00
4	23-Jul-12	1	*300,000.00	219,000.00
5	14-Nov-12	1	*280,000.00	216,500.00
6	18-Jan-13	1	*260,000.00	213,500.00
7	31-Jan-13	1	*254,000.00	205,000.00
8	26-Mar-13	1	*262,000.00	220,500.00
9	17-Apr-13	1	*256,000.00	192,500.00
10	9-Jun-13	1	*270,000.00	208,000.00
11	1-Oct-13	1	*320,000.00	254,500.00

* Indicates change

Rating/target price changes above reflect Eastern Standard Time

Hyundai Motor (005380.KS)

Ratings and Target Price History
Best Ideas Research
Relative Call (3 Month)

Analyst: Ethan Kim

	Date	Rating	Target Price	Closing Price
1	9-Aug-11	*REM MP	-	194,000.00
2	7-Nov-11	*ADD MP	-	237,000.00
3	25-Apr-14	*REM MP	-	236,000.00

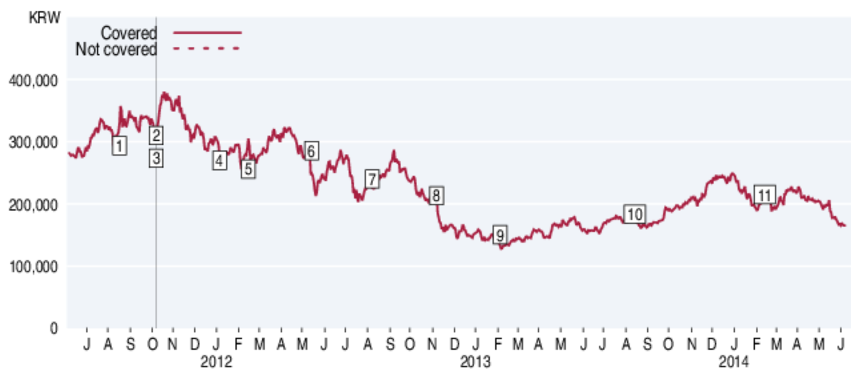
* Indicates change

Rating/target price changes above reflect Eastern Standard Time

NCsoft (036570.KS)

Ratings and Target Price History
Fundamental Research

Analyst: Irene Cho
Covered since February 13 2014



	Date	Rating	Target Price	Closing Price
1	17-Aug-11	1L	*380,000.00	329,500.00
2	7-Oct-11	Stock rating system changed		
3	7-Oct-11	*1	380,000.00	310,000.00
4	5-Jan-12	*2	*300,000.00	276,500.00
5	15-Feb-12	*3	*240,000.00	305,000.00
6	15-May-12	3	*210,000.00	248,500.00
7	8-Aug-12	3	*180,000.00	224,000.00
8	7-Nov-12	3	*150,000.00	213,000.00
9	5-Feb-13	3	*110,000.00	132,500.00
10	14-Aug-13	3	*135,000.00	181,500.00
11	13-Feb-14	3	*150,000.00	215,000.00

* Indicates change

Rating/target price changes above reflect Eastern Standard Time

NCsoft (036570.KS)

Ratings and Target Price History
Best Ideas Research
Relative Call (3 Month)

Analyst: Irene Cho
Covered since February 13 2014

	Date	Rating	Target Price	Closing Price
1	8-Sep-11	*REM MP	-	339,500.00

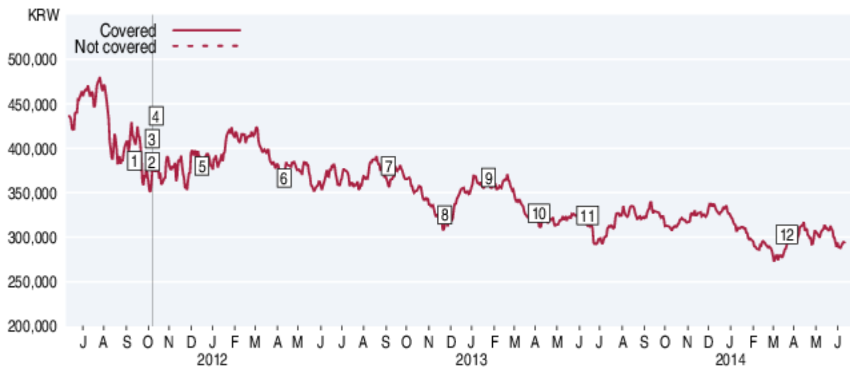
* Indicates change

Rating/target price changes above reflect Eastern Standard Time

POSCO (005490.KS)

Ratings and Target Price History
Fundamental Research

Analyst: Sungmee Park, CFA



	Date	Rating	Target Price	Closing Price
1	13-Sep-11	1M	*530,000.00	416,000.00
2	7-Oct-11	Stock rating system changed		
3	7-Oct-11	*1	530,000.00	376,000.00
4	13-Oct-11	1	*490,000.00	376,000.00
5	16-Dec-11	1	*470,000.00	386,500.00
6	11-Apr-12	1	*440,000.00	371,500.00
7	5-Sep-12	1	*420,000.00	358,000.00
8	23-Nov-12	1	*370,000.00	313,500.00
9	24-Jan-13	*2	*380,000.00	365,500.00
10	5-Apr-13	2	*360,000.00	312,500.00
11	13-Jun-13	2	*340,000.00	313,000.00
12	21-Mar-14	*1	*350,000.00	292,000.00

* Indicates change

Rating/target price changes above reflect Eastern Standard Time

POSCO (005490.KS)

Ratings and Target Price History
Best Ideas Research
Relative Call (3 Month)

Analyst: Sungmee Park, CFA

	Date	Rating	Target Price	Closing Price
1	8-Feb-12	*REM MP	-	407,000.00
2	9-Feb-12	*ADD MP	-	409,000.00
3	24-Sep-12	*REM MP	-	377,000.00

* Indicates change

Rating/target price changes above reflect Eastern Standard Time

Samsung Electronics (005930.KS)

Ratings and Target Price History
Fundamental Research

Analyst: Henry H Kim, CFA

Date	Rating	Target Price	Closing Price
1 31-Aug-11	1L	*1,200,000.00	744,000.00
2 7-Oct-11	Stock rating system changed		
3 7-Oct-11	*1	1,200,000.00	860,000.00
4 28-Oct-11	1	*1,300,000.00	945,000.00
5 7-Dec-11	1	*1,400,000.00	1,056,000.00
6 16-Mar-12	1	*1,800,000.00	1,238,000.00
7 9-Apr-12	1	*1,900,000.00	1,317,000.00
8 25-Jun-12	1	*1,970,000.00	1,132,000.00
9 1-Jul-13	1	*1,950,000.00	1,326,000.00
10 26-Jul-13	1	*1,900,000.00	1,303,000.00
11 7-Jan-14	1	*1,800,000.00	1,304,000.00

* Indicates change

Rating/target price changes above reflect Eastern Standard Time

Samsung Electronics (005930.KS)

Ratings and Target Price History
Best Ideas Research
Relative Call (3 Month)

Analyst: Henry H Kim, CFA

Date	Rating	Target Price	Closing Price
1 16-Mar-12	*ADD MP	-	1,238,000.00
2 31-Jan-14	*REM MP	-	1,280,000.00

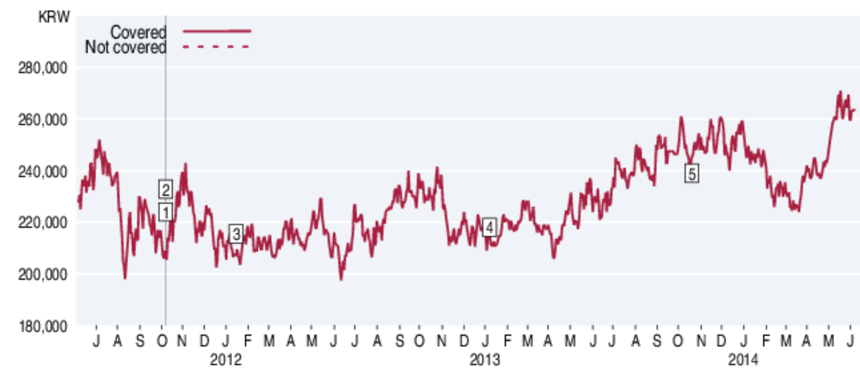
* Indicates change

Rating/target price changes above reflect Eastern Standard Time

Samsung Fire & Marine (000810.KS)

Ratings and Target Price History
Fundamental Research

Analyst: Ss Kim
Covered since January 16 2012



Date	Rating	Target Price	Closing Price
1 7-Oct-11	Stock rating system changed		
2 7-Oct-11	*1	270,000.00	206,999.98
3 16-Jan-12	1	*280,000.00	206,999.98
4 8-Jan-13	1	*260,000.00	215,000.00
5 21-Oct-13	1	*290,000.00	245,500.00

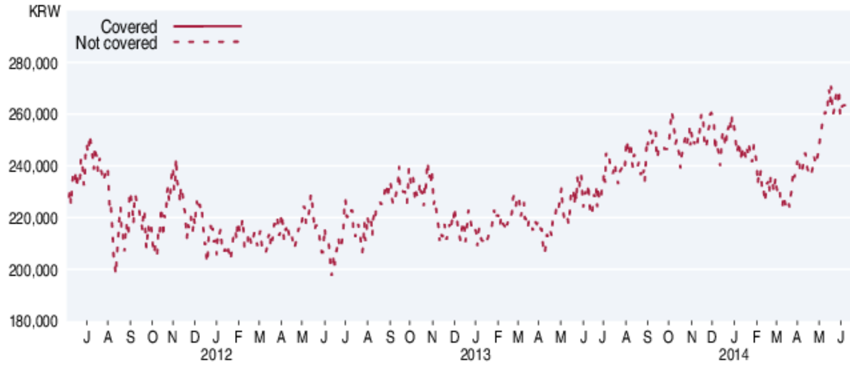
* Indicates change

Rating/target price changes above reflect Eastern Standard Time

Samsung Fire & Marine (000810.KS)

Ratings and Target Price History
Best Ideas Research
Relative Call (3 Month)

Analyst: Ss Kim
Covered since January 16 2012



* Indicates change

Rating/target price changes above reflect Eastern Standard Time

SK Telecom (017670.KS)

Ratings and Target Price History
Fundamental Research

Analyst: Sean Lee, CFA

	Date	Rating	Target Price	Closing Price
1	16-Jun-11	1M	*180,000.00	153,000.00
2	22-Jun-11	1M	*185,000.00	158,500.00
3	7-Oct-11	Stock rating system changed		
4	7-Oct-11	*1	185,000.00	157,500.00
5	23-Mar-12	1	*170,000.00	142,000.00
6	5-Jul-12	1	*155,000.00	128,500.00
7	27-Sep-12	1	*175,000.00	144,500.00
8	16-Jan-13	1	*190,000.00	166,000.00
9	24-Apr-13	1	*230,000.00	189,500.00
10	31-Jul-13	1	*254,000.00	220,500.00
11	10-Oct-13	1	*270,000.00	228,000.00

* Indicates change

Rating/target price changes above reflect Eastern Standard Time

SK Telecom (017670.KS)

Ratings and Target Price History
Best Ideas Research
Relative Call (3 Month)

Analyst: Sean Lee, CFA

	Date	Rating	Target Price	Closing Price
1	16-Jan-13	*ADD MP	-	166,000.00
2	5-Feb-14	*REM MP	-	204,500.00

* Indicates change

Rating/target price changes above reflect Eastern Standard Time

LG Chem (051910.KS)

Ratings and Target Price History
Fundamental Research

Analyst: Oscar Yee

	Date	Rating	Target Price	Closing Price
1	25-Sep-11	*1L	*440,000.00	316,500.00
2	7-Oct-11	Stock rating system changed		
3	7-Oct-11	*1	440,000.00	322,000.00
4	23-May-12	1	*390,000.00	275,000.00
5	29-Jan-13	1	*360,000.00	313,000.00
6	20-May-13	1	*350,000.00	278,000.00
7	27-Jan-14	1	*320,000.00	262,000.00

* Indicates change

Rating/target price changes above reflect Eastern Standard Time

LG Chem (051910.KS)

Ratings and Target Price History
Best Ideas Research
Relative Call (3 Month)

Analyst: Oscar Yee

	Date	Rating	Target Price	Closing Price
1	4-Nov-11	*ADD MP	-	372,500.00
2	30-Jan-13	*REM MP	-	302,000.00
3	27-May-13	*ADD MP	-	256,000.00
4	8-Apr-14	*REM MP	-	272,000.00

* Indicates change

Rating/target price changes above reflect Eastern Standard Time

LG Display (034220.KS)

Ratings and Target Price History
Fundamental Research

Analyst: Henry H Kim, CFA
Covered since August 16 2012

	Date	Rating	Target Price	Closing Price
1	20-Jul-11	1M	*37,000.00	30,550.00
2	21-Sep-11	1M	*27,000.00	21,300.00
3	7-Oct-11	Stock rating system changed		
4	7-Oct-11	*1	27,000.00	20,050.00
5	13-Jan-12	1	*33,000.00	26,850.00
6	13-Jun-12	1	*32,000.00	22,750.00
7	17-Aug-12	1	*31,000.00	27,000.00
8	12-Oct-12	1	*32,000.00	27,150.00
9	30-Oct-12	1	*36,000.00	32,500.00
10	10-Jan-13	*2	*32,000.00	29,850.00
11	4-Jul-13	2	*30,500.00	26,900.00
12	11-Oct-13	*1	30,500.00	24,300.00
13	24-Jan-14	1	*32,000.00	26,750.00
14	24-Apr-14	1	*36,000.00	28,750.00

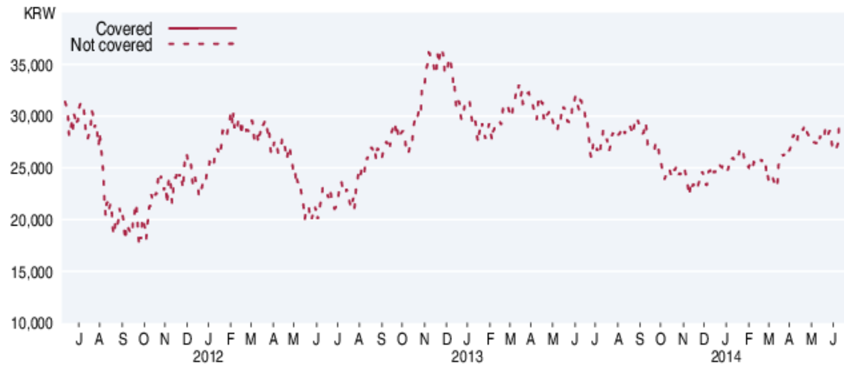
* Indicates change

Rating/target price changes above reflect Eastern Standard Time

LG Display (034220.KS)

Ratings and Target Price History
Best Ideas Research
Relative Call (3 Month)

Analyst: Henry H Kim, CFA
Covered since August 16 2012



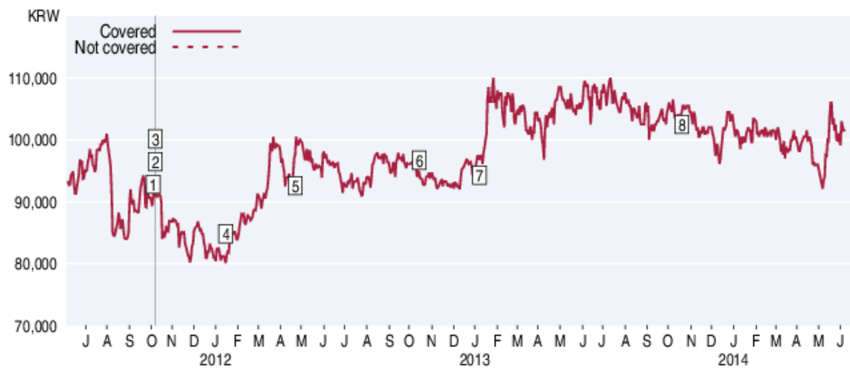
* Indicates change

Rating/target price changes above reflect Eastern Standard Time

Samsung Life (032830.KS)

Ratings and Target Price History
Fundamental Research

Analyst: Ss Kim
Covered since October 5 2011



	Date	Rating	Target Price	Closing Price
1	5-Oct-11	2M	*100,000.00	90,799.99
2	7-Oct-11	Stock rating system changed		
3	7-Oct-11	*2	100,000.00	91,800.00
4	16-Jan-12	2	*90,500.00	80,100.00
5	23-Apr-12	*1	*121,000.00	97,500.00
6	14-Oct-12	1	*115,000.00	94,900.00
7	8-Jan-13	1	*118,000.00	96,800.00
8	21-Oct-13	1	*130,000.00	104,500.00

* Indicates change

Rating/target price changes above reflect Eastern Standard Time

Samsung Life (032830.KS)

Ratings and Target Price History
Best Ideas Research
Relative Call (3 Month)

Analyst: Ss Kim
Covered since October 5 2011

	Date	Rating	Target Price	Closing Price
1	5-Oct-11	*REM LP	-	90,799.99

* Indicates change

Rating/target price changes above reflect Eastern Standard Time

Hyundai E&C (000720.KS)

Ratings and Target Price History
Fundamental Research

Analyst: Sungmee Park, CFA

	Date	Rating	Target Price	Closing Price
1	7-Oct-11	Stock rating system changed		
2	7-Oct-11	*1	110,000.00	57,000.00
3	20-Oct-11	1	*90,000.00	64,100.00
4	29-May-12	1	*83,000.00	69,900.00
5	4-Jan-13	1	*90,000.00	73,700.00
6	2-Jul-13	1	*85,000.00	56,800.00
7	3-Apr-14	1	*80,000.00	56,400.00

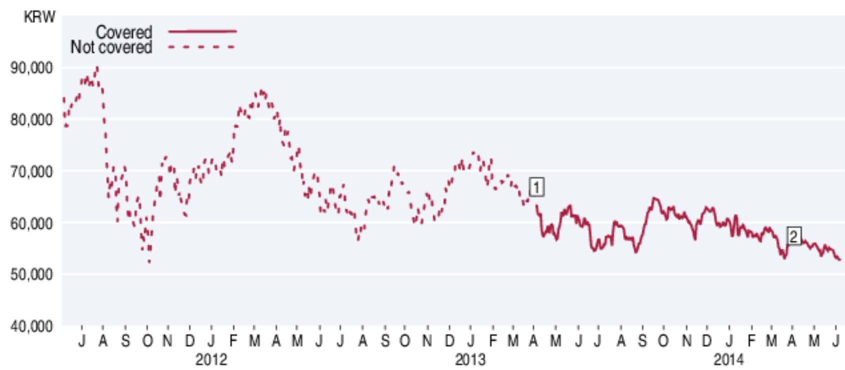
* Indicates change

Rating/target price changes above reflect Eastern Standard Time

Hyundai E&C (000720.KS)

Ratings and Target Price History
Best Ideas Research
Relative Call (3 Month)

Analyst: Sungmee Park, CFA



	Date	Rating	Target Price	Closing Price
1	4-Apr-13	*ADD MP	-	63,200.00
2	3-Apr-14	*REM MP	-	56,400.00

* Indicates change

Rating/target price changes above reflect Eastern Standard Time

Citi is acting as financial advisor to China Petroleum & Chemical Corp and ENN Energy Holdings in the proposed takeover of China Gas Holdings.

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Citi is currently mandated as sole bookrunner on the sale of Samsung Electronics' 6% stake in CSR Plc.

Citi is currently mandated as Financial Advisor to LG Chem, Ltd on the announced and pending acquisition of NanoH2O, Inc.

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Craig Williams, Analyst, holds a long position in the securities of Macquarie Group Limited.

Mark Tomlins, Analyst, holds a long position in the securities of Wesfarmers Ltd,Rio Tinto Ltd,Amcor Limited.

Manabu Hagiwara, Analyst, holds a long position in the securities of Mitsubishi UFJ Financial Group,Sumitomo Mitsui Financial Group.

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	12 Month Rating			*Relative Rating*		
Data current as of 31 Mar 2014	**Buy**	**Hold**	**Sell**	**Buy**	**Hold**	**Sell**
Citi Research Global Fundamental Coverage	49%	40%	12%	1%	98%	1%
% of companies in each rating category that are investment banking clients	55%	53%	45%	58%	53%	42%

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