Private Asset Management

Global Investment Committee

Outlook 2009

Investment strategy geared towards global recession

A Passion to Perform.

Deutsche Bank

Contents

Opportunities in the crisis

Dr. Helmut Kaiser,
Global Chief Investment Strategist

Dear Investors,

2008 will undoubtedly go down in financial history as an "annus horribilis". Most global equity markets are recording massive losses, the positive diversification qualities of established asset classes have crumbled entirely, and investors' confidence in the financial markets has been shattered.

The central banks' exemplary crisis management and the governments' economic programmes have prevented a collapse of the financial system. However, this does not mean that the repercussions of the financial crisis are behind us, as the real economic effects on consumers and companies are only just fully emerging. The first half of 2009 is also likely to be difficult. Accordingly, we anticipate a pronounced recession in the G7 countries next year. Likelihood is that only the emerging markets offer the prospect of positive growth rates.

However, there are still opportunities for investors, even in these difficult investment conditions. The marked drop in inflation should create leeway for further rate cuts, for example, which would be particularly beneficial for the bond markets. On the equity markets, the bleak outlook for H1 2009 is already largely factored into share prices. At the same time, the record lows reached in standard valuation ratios imply that good opportunities to enter this asset class could arise if earnings stabilise in the second half-year. The same applies to commodities, which have suffered a sharp fall in prices, and selected hedge funds, which should see a return to their former strength following a disappointing 2008.

I wish you a stimulating read and a successful investment year in 2009.

Helmut Kaiser

Dr. Helmut Kaiser

From financial crisis to global recession

2009 presents major challenges for investment strategy. There are high risks, on the one hand, but also attractive opportunities in some asset classes, on the other. Equity and corporate bond valuations look very favourable across all quality categories and irrespective of balance sheet strength. On the other hand, the financial crisis is not yet over, and there is considerable uncertainty as to the length and depth of a global recession. So there is much to suggest that the timing of any switches from fixed-income into equities or other riskier securities should be put off for some weeks at least and that close attention should be paid to the fundamental quality of the companies and issuers.

Recession is the consensus and the downside risks predominate

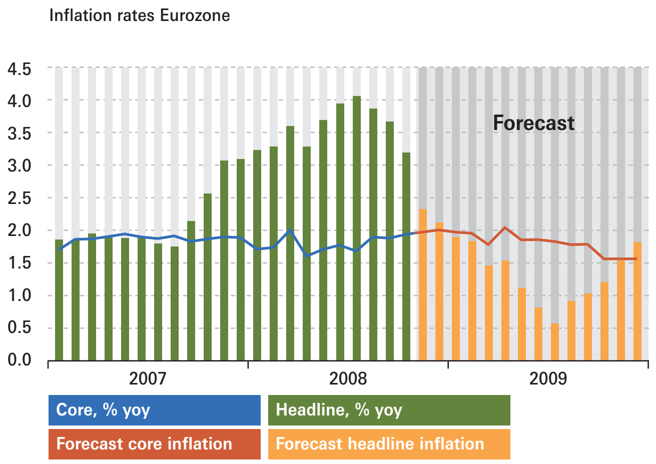
The growth outlook has deteriorated rapidly throughout the world. Drastic deleveraging and poorer credit conditions are likely to be a major drag on economic growth and corporate earnings, also in the mid term. Consequently, we are not just facing a cyclical downturn in growth; we are also likely to see a reduction in long-term growth potential in the US and Europe. The forecasts for world economic growth have been revised downwards over the past weeks. We expect growth in the G3 regions (the US, Europe and Japan) to slump to minus 1 to 1.5% in 2009. An important precondition for economic stabilisation is that the housing markets bottom out, but that is not in sight as yet. As a result of globalisation, the rapid fall-off in export demand is being felt worldwide. The massive monetary and fiscal policy support measures will take time to feed through. All in all, we expect a stabilisation or moderate recovery at the earliest in the second half of 2009. This should be supported by further fiscal measures in the coming months.

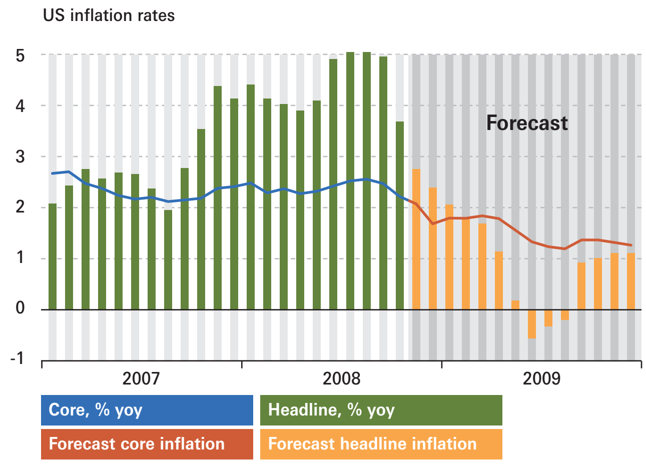
Emerging markets is expected to be the driving force in 2009

For the first time, world economic growth is expected to come entirely from the emerging markets in 2009. However, their growth rates are likely to decline, too, especially in Eastern Europe and Latin America. Asia, too, is likely to see a strong slowdown in growth but should still be a major contributor to world economic growth in 2009 with a rate of 5.5%. The

Inflation rates expected to ease appreciably

Inflation rates are expected to ease appreciably both in the US and in the Eurozone, whereby the reduction year over year should be more pronounced in the US than in the Eurozone. The main reasons for declining inflation rates are global recession, weaker consumer demand, and the steep fall in food and energy prices. Oil prices peaked in July 2008. Owing to the, in part, massive falls in energy and agricultural commodity prices since July 2008 core inflation should be higher than headline inflation especially in summer 2009.



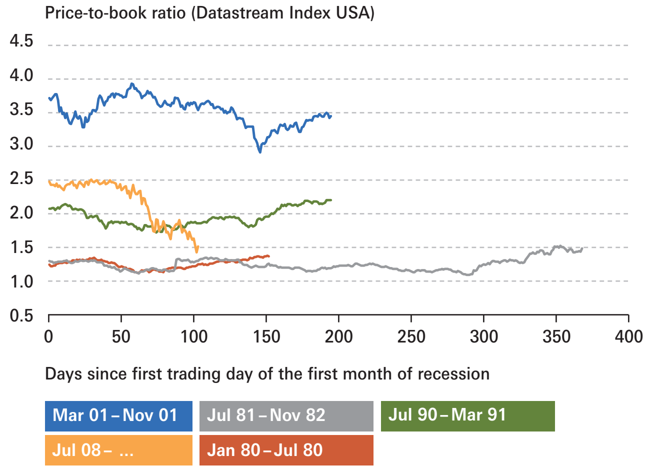


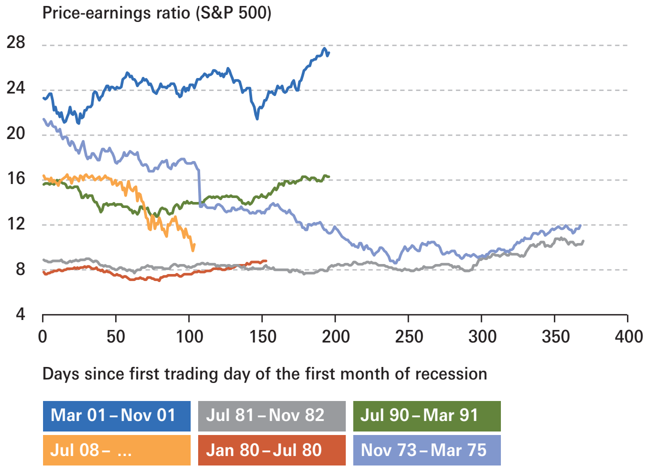
Sources: Deutsche Bank AG, Private Asset Management; Deutsche Bank AG, Global Markets; Thomson Reuters Datastream

As of: November 27, 2008

1980s lows not yet reached

Equity valuations during the US recessions since 1970: valuation levels on the US equity market have come down strongly in the past weeks. However, both the price-earnings ratio and the price-to-book ratio are still slightly above the lows for US equities witnessed during the US recessions in the 1980s.





Sources: Deutsche Bank AG, Private Asset Management; Thomson Reuters Datastream

As of: November 21, 2008

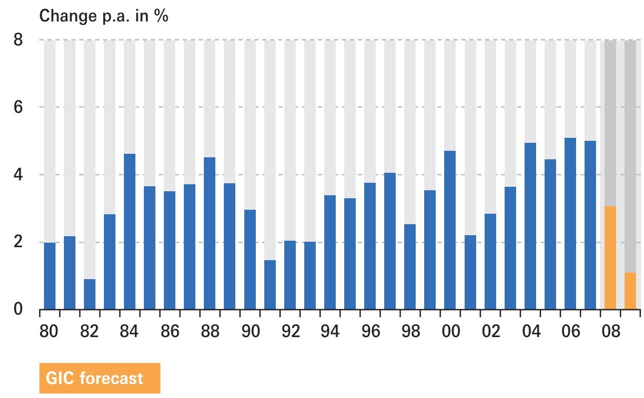
outlook differs considerably from region to region. While just a few months ago the global credit crunch still had an only limited impact on the emerging markets, they have been fully embroiled in the turbulence in recent weeks. Three different spillover channels have eventually caused all regions and countries to be affected more or less strongly. Countries with high government or corporate debt, as in Eastern Europe, are suffering from the worsened credit conditions. Commodity exporters in Latin America are witnessing sharply falling foreign exchange revenues and capital outflows, while export-sensitive countries in Asia are being hurt by sharply declining export demand from the G3 regions.

Inflation: In free fall

2008 brought a swing in inflation expectations with a speed not witnessed before. While inflation rates picked up strongly around the world in the early summer and there had been considerable concerns that the rise in headline inflation, driven by commodity prices, would spill over to the core rates, over the past weeks inflation forecasts have been scaled back even more strongly than growth rates. The strong downward pressure on inflation rates has two causes. Firstly, commodity prices have come down very steeply, leading already to much lower headline inflation. In Euroland the inflation rate fell in November to 2.1 % year over year and by 3.2 % versus the previous month. As we expect sustained lower prices for energy and industrial metals in 2009, there are likely to be extremely favourable base effects in the early summer months. These base effects should lead to inflation rates in negative territory at times in the US and down to well below 1 % in the Eurozone. The second reason for the fall in inflation is the cyclical trend. The strong decline in capacity utilisation and rising unemployment are also exerting downward pressure on prices.

Global growth on the decline

At an estimated 1.2 %, global economic growth in 2009 will be the lowest since the global recession in 1932.



Average growth rates on a cumulative purchasing power parity weighted basis; gradual shift in favour of faster-growing economies produces an upward trend line.

Sources: Deutsche Bank AG, Global Investment Committee (GIC); IMF World Economic Outlook, November 2008

Deflation could well be an issue again, depending on the length and depth of the recession. However, in our scenario so far we see core inflation rates staying more or less constant; after all, they did not follow headline inflation up. Any inflationary risks from the strongly expansive monetary and fiscal policy measures are set to remain in the background for the present given the currently extremely weak economic outlook. The inflation issue will probably only become acute again if demand picks up appreciably again and interest rate policy and the economic stimulus programmes are not phased out in time. However, in our view, the risk of a prolonged recession is greater than a return of inflation.

Bond markets: Government bonds remain a safe haven

In the near term, the markets for government bonds should continue to be well supported by the recession risks, rapidly easing inflation rates and strong global risk aversion. The continued stream of bad economic news and the strong fall in inflation rates have in fact taken yields on 10-year US Treasuries to a level below 3 % at the end of November. The central banks therefore have leeway for further strong rate cuts. We meanwhile expect the ECB to cut its key rate to 1.5 % on a 12-month horizon and see the Fed funds rate then at 0.5 %.

While the inflation outlook is likely to present little risk of higher rates for some time, there is growing long-term setback potential for the bond markets from sharply rising global government issuance. The rescue plans for the banking sector and fiscal measures launched in the US and Europe and in other regions, too, are being financed to a large extent through government borrowing. At the same time, there will be less demand for US Treasuries from Asian central banks and oil-exporting countries as their foreign exchange revenues decline.

The bond markets are likely to remain underpinned as long as the flight to safety persists. Risks of setbacks on the bond markets are presented once funds are switched back on a larger scale from the bond markets into equities. However, this is unlikely to be an issue in the next few months.

Corporate bonds: Attractive return potential but timing difficult

The valuation levels for corporate bonds have meanwhile reached historic lows. The default probabilities implied in the risk premiums are well above the empirical values for past recessions. However, set against the attractive return potential, there is considerable risk. The comparison with past recessions could well be misleading. The nature and scale of the present deleveraging process is without precedent, and the current recession is likely to be more painful than the two previous ones. Nonetheless, some market segments also look attractive on a risk-adjusted basis.

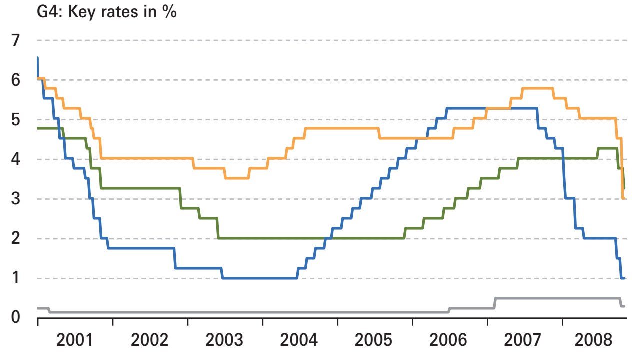
Equity markets: Hung between favourable valuations and high risk aversion

The environment for the equity markets is likely to remain very volatile at least in the coming weeks. In the short term, setback potential is presented by the further reduction of

Central bank rates at record lows – bond yields in free fall

Central bank rates are – or are expected to be – at their lowest levels for decades.

G4: Key rates in %

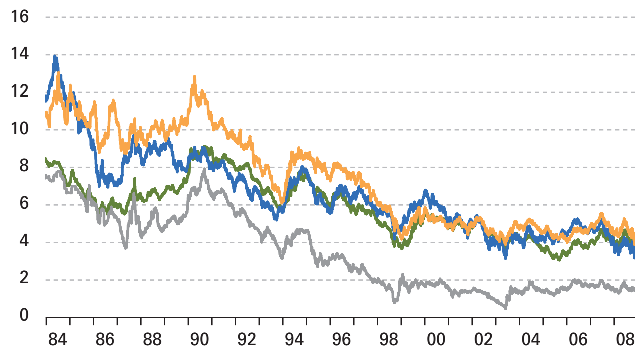


USA	1.00	Eurozone	3.25
UK	3.00	Japan	0.30

Sources: Deutsche Bank AG, Private Asset Management; Thomson Reuters Datastream As of: November 17, 2008

Yields on government bonds are gradually approaching Japanese levels.

G4: Yields on 10-year government bonds in %



USA	3.18	Eurozone (BUND)	3.35
UK	3.86	Japan	1.40

Sources: Deutsche Bank AG, Private Asset Management; Thomson Reuters Datastream As of: November 21, 2008

Price retracements on the US equity market in US recessions

Phase of recession			Retracement of the S&P 500*
Start	End	Months	%
Nov 48	Oct 49	11	-20.6
Jul 53	May 54	10	-14.2
Aug 57	Apr 58	8	-20.7
Apr 60	Feb 61	10	-13.9
Dec 69	Nov 70	11	-36.1
Nov 73	Mar 75	16	-48.2
Jan 80	Jul 80	6	-17.1
Jul 81	Nov 82	16	-27.1
Jul 90	Mar 91	8	-19.3
Mar 01	Nov 01	8	-36.8
Average		10	-25.4

* Owing to base effects the total retracement in % cannot be calculated as the sum of the retracements before and after the start of recession

Source: Deutsche Bank AG, Global Markets As of: November 21, 2008

earnings expectations that has to be feared. Valuations have meanwhile reached historically low levels on all criteria and do indeed offer attractive opportunities. However, given the uncertainty over the length and depth of the recession and the continued credit squeeze, caution and a focus on companies with strong balance sheets is still advised.

Alternative investments: Deleveraging to remain in focus
The outlook for the commodity markets continues to be clouded in some segments by the effects of the financial crisis and the reduction of riskier commodity positions as well as the abrupt slump in demand as a result of the sharp fall-off in world economic activity. Some commodities are currently in a vicious circle of declining demand and production cutbacks. Fundamental supports, such as the fact that the prices of a number of commodities are already close to production cost, are having no effect at present. Geopolitical events, too, are barely triggering any rises, for instance in the oil price, at the moment. Gold is an exception and is displaying relative strength thanks to its role as a "safe haven". A sustained turnaround in commodity prices only appears possible when the leading indicators signal an end of the global recession.

On the **currency markets**, the momentum has slackened appreciably of late. All the same, we see no reversal as yet of the trends prevailing since the summer. While the appreciation of the dollar should slow, it is likely to remain unchallenged as the preferred reserve currency, as the strong fall in US Treasury yields bears out. The yen should also continue to benefit in a world of falling interest rates and further deleveraging. For the emerging markets, we expect the currency depreciation across the board to give way soon to a more differentiated picture, with fundamental data acquiring more importance again. We remain sceptical especially for countries with high debt and strong external dependencies.

Hedge funds are currently struggling not only with a difficult market environment and the general deleveraging process but also with outflows of funds by their investors. This has led in part to forced sales and has hurt returns. As long as actual and expected outflows weigh on the hedge fund industry, its performance potential is limited.

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Dr. Konrad Aigner

In the grip of the financial market crisis

The effects of the financial market crisis are having a significant impact on the commodity markets. Both the reduction in risky commodity investments and the abrupt tail-off in demand due to the slump in the global economy have led to a sharp fall in commodity prices. We are currently witnessing a race between falling demand and cutbacks in production. A sustained trend reversal in commodity prices appears unlikely until economic leading indicators start to suggest an end to the global recession. As with other risky securities, investors should until then adopt a defensive approach to commodities.

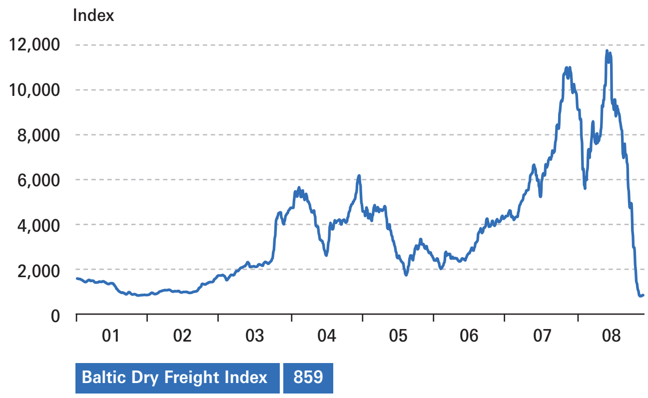
The insolvency of Lehman Brothers on 15 September 2008 heralded a new phase in the financial market crisis. There has been a sharp acceleration in price falls across all asset classes apart from government bonds, which are seen as a safe haven. Risk positions have been reduced and leveraged investments cut back as deleveraging takes hold. There have recently been extremely sharp declines in the price of commodities, which, like crude oil, are traded via relatively liquid futures markets. This suggests that financial market players are also deleveraging on the commodity markets. There is no end to this process in sight at present. Risk reduction and the unwillingness to take investment risks will weigh on the financial markets as a whole in the coming weeks and will also determine the commodity price trend. In the foreseeable future, we can therefore expect a general downtrend in prices amidst pronounced price volatility. A sustained trend reversal in commodity prices does not seem possible until there are signs of an end to the financial market crisis and the global recession. This is unlikely to be the case until some time next year. Until then, it appears sensible to adopt a defensive investment strategy towards commodities as well as other risky paper.

Global recession weighing on commodity prices

Contagion from the financial market crisis is compounded by the prospect of an economic slump of unprecedented speed. Since mid-September, the sharp downtrend has not been confined to stock market indices or commodity prices; business climate indices and economic indicators have also been heading due south. The Baltic Dry Freight Index is one example of this trend. This index tracks cargo rates for bulk goods on key shipping routes across the world and is an indicator of global trade activity. It therefore reflects the global spread of recession momentum. The index had already fallen at the beginning of 2008 before recovering in the spring and setting new record highs in the region of 12,000 points in early June. However, mounting fears over the economy caused the index to plummet in the summer, and it recorded lows only slightly above 800 at the start of November. Cargo rates have now reached levels which make it impossible for many shipping companies to operate profitably, prompting them to anchor vessels for the time being.

Baltic Dry Freight Index: Slump in cargo rates

The Baltic Dry Freight Index is an indicator of global trade activity. The extremely sharp drop in cargo rates signals a major decline in the global economy.



Sources: Deutsche Bank AG, Private Asset Management; Bloomberg
As of: November 20, 2008

This trend is similar to that on the commodity markets, where demand is plunging at unprecedented speed. This is having a negative impact on commodity prices, though producers are trying to slow down the decline in prices by shutting down capacity. We are currently witnessing a race between falling demand and cutbacks in production. At present, it is difficult to gauge the level at which prices will find their new equilibrium, and this depends on the market conditions specific to each individual commodity.

Weak demand dominates the short-term outlook for oil prices

Expectations for the trend in oil prices vary greatly depending on the investment horizon. Oil futures contracts of various maturities provide an indication of the differences in expectations. Prices for longer-dated futures contracts have dropped far less significantly than those for shorter-dated futures. The difference between 1-month and 12-month contract prices is therefore highly negative at present. Strong divergences in expectations across the various maturity segments often indicate that there is growing potential for a short-term trend reversal. The fact that the structure of futures prices is close to reaching extreme levels signals that resistance to further price declines is increasing. However, uncertainty surrounding the scope and extent of the fall in demand for oil will prevail in the short term. Supply issues, such as the disappointing supply trend in non-OPEC countries and OPEC's decision to cut production in October, are barely being acknowledged on the market at present. A number of oil exploration projects have already been cancelled or postponed due to the sharp drop in oil prices and the limited availability of loans. As a result, production increases in non-OPEC countries are likely to be disappointing – as was the case last year – and the oil price should rise again in the longer term.

Persistent pressure on industrial metals

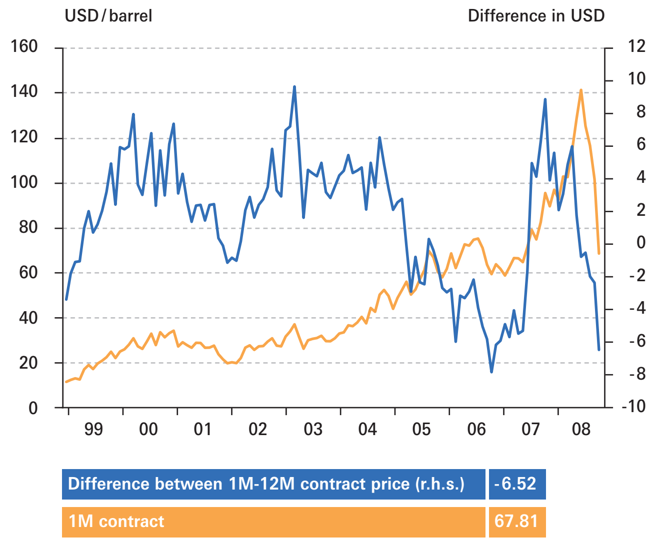
The race between falling demand and production cuts is well under way in the industrial metals market. Fears of a sharp drop in demand will also dominate this market in the short term. Based on the experience of past economic cycles, prices for industrial metals usually do not start to rise until the economy has picked up considerably and there are signs of a more restrictive monetary policy. As we are still far from reaching this stage of recovery, prices for industrial metals look set to remain under notable pressure. The economic cycle is less important for precious metals – particularly gold. The gold price should continue to be well supported thanks to its safe haven role in times of crisis.

Agricultural prices also not immune to the credit crisis

Diversified commodity investments often include agricultural products, whose prices are therefore similarly affected by the deleveraging process. Moreover, as the declining oil price is also eroding the competitiveness of biofuels, demand for the relevant raw materials such as sugar and maize is expected to weaken. However, the cycles of agricultural products tend to be substantially shorter, less sensitive to cyclical fluctuations in demand and more dependent on weather conditions and crop yields. As access to loans has also become more difficult for farmers due to the financial market crisis, the use of fertilisers, for example, is likely to be reduced. This will increase the risk of lower crop yields next year. Given that inventories remain low, crop losses due to such factors or to the weather would directly lead to higher prices.

Oil prices: Differing expectations

The oil price has dropped appreciably since July. The longer-dated futures contracts have fared better, leading to a highly negative difference between 1M and 12M contracts.



Sources: Deutsche Bank AG, Private Asset Management; Bloomberg

As of: October 31, 2008

Dr. Konrad Aigner is Strategist for commodities, international bond markets and asset allocation in the Investment Strategy Group of Private Asset Management at Deutsche Bank in Frankfurt.

Dr. Eric Jahn

Systematic macro funds weather the storm

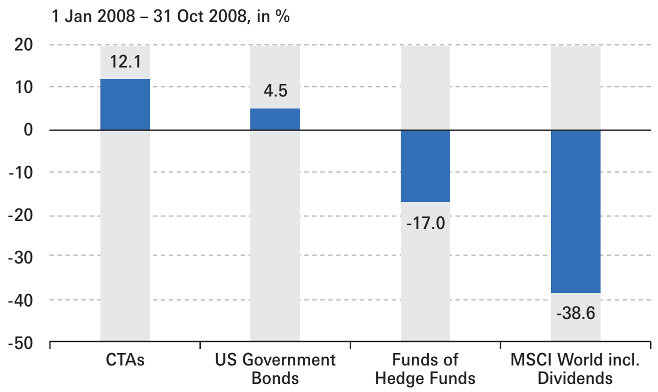
The hedge fund industry is currently in the throes of a consolidation process marked by outflows and an expected decline in the number of funds. So when selecting managers, it is important that they have sufficient liquidity and flexibility. In terms of individual strategies, we continue to recommend overweighting macro funds.

Besides a difficult market environment and the general deleveraging process in the financial system, redemptions by investors have been an added factor weighing on the hedge fund industry for some months. According to estimates published by Hedge Fund Research, investors withdrew a global net USD 31 billion from hedge funds in the third quarter of 2008, and further outflows are expected in the fourth quarter (and possibly beyond that).

Although hedge funds have already maintained a comparatively high level of cash throughout the year to date, they have been forced to liquidate positions to meet actual or expected outflows. This has led to selling pressure on many (especially equity) markets. It is also expected that there will be a marked decline in the number of hedge funds in the coming months, with smaller funds probably being affected in particular.

CTAs with high diversification potential

Systematic macro funds (CTAs) have managed to achieve a double-digit return on average year to date. CTAs have profited from pronounced trends above all in equities, commodities and currencies, thus making a strong contribution to portfolio diversification in times of turbulent financial markets.



Note: All returns in USD, Edhec indices for CTAs and funds of hedge funds, JPMorgan Bond Index for US Treasuries

Sources: Bloomberg; Edhec

Consequently, besides other aspects to be considered in manager selection, it is particularly important at present that the managers chosen have sufficiently high liquidity and flexibility so that, on the one hand, any outflows do not result in forced selling and, on the other, they can profit from attractive investment opportunities in the course of a potential market stabilisation.

Focus on individual strategies

Within a balanced hedge fund portfolio we recommend overweighting macro strategies and avoiding comparatively highly leveraged strategies (and funds). While systematic macro funds (CTAs) possess high diversification potential in a portfolio context (in October, for instance, CTAs were able to profit from falling equity markets), discretionary macro managers pursue a strategic approach across a range of asset classes.

In the equity segment, we favour defensive long / short equity and market neutral funds owing to the uncertain outlook for risky investments. While a stronger exposure to distressed debt funds proved premature in the past months, we recommend gradually extending the portfolio allocation towards this strategy, as the economic downswing should increase the supply of distressed debt and offer attractive investment opportunities in debt restructuring.

Despite the massive sell-off in convertible bonds, we recommend not underweighting convertible arbitrage funds in a hedge fund portfolio as convertible bonds present attractive investment opportunities in some cases at the current valuation levels. On the other hand, we remain underweight on fixed-income arbitrage funds as they offer unattractive return potential at currently increased risk.

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Hugo Capel Cure

Uncharted territory

European equity markets are caught between a series of conflicting forces. Our economic analysis points to short-term deflation but subsequent inflation as a by-product of aggressive monetary stimulus. Likewise, fundamental analysis cautions us to beware of earnings disappointments, but it is also apparent that there are unusual value situations in a historic context. All of these ingredients combine to give a volatile market environment as we head into 2009, but with plenty of opportunities for investors.

Macroeconomic uncertainties weigh stronger than company results

Investors are struggling to value companies with any degree of conviction in the current environment. Third quarter earnings have been largely ignored as both managers and investors are much more interested in estimating how 2009 might look. It is now apparent that the slowdown is no longer confined to the financial sector alone and expectations are being revised accordingly. In particular, analysts are rapidly downgrading their earnings estimates for both consumer and cyclical companies.

Recession or depression?

In much the same way that analysis of companies has seen a shift of focus from profit and loss statements to balance sheets, the economic focus is much more on the macro than the micro. Investors in cyclical industries in Europe, ranging from the discretionary consumer purchases, such as autos, through to traditional capital goods companies like Siemens or ABB, are trying to gauge the 'shape' of the eventual recovery in demand. If there is judged to be no prospect of economic stabilisation in 2009, then the focus will remain on companies with the most resilient balance sheets.

Unprecedented valuations

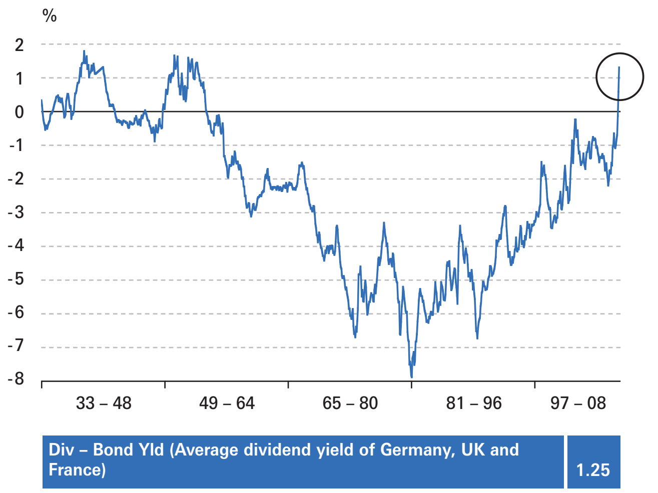
Current valuations arguably already discount the recessionary environment. Price-earnings ratios (PERs) in Europe are well below the average of the last 50 years, with substantial declines in earnings required to return the PERs to trend valuation levels. The popular comparison of the earnings yield with the risk-free bond yield gives a risk premium of more than 8 %, which has never stayed at such a high level over more than a few weeks in the past. In Europe, the dividend yield has reached levels above investment-grade bond yields and this has not happened since 1954. Even though dividend payouts will undoubtedly fall in some areas of the market, notably financials and cyclicals, most companies have sufficient cash-flows to maintain adequate cover.

Investment opportunities

Over the short-term, it is clear that bank deleveraging and redemptions across the mutual and hedge fund industries have depressed markets. However, those investors whose horizon extends beyond a few weeks currently have opportunities to invest at extremely attractive valuation levels. The volatility of stock price movements should begin to subside as investors have a clearer picture of economic conditions in 2009.

Dividend yield > bond yield for first time since 1954

The dividend yield has tended to be lower than government bond yields in recent years as investors anticipated a growth in capital as well as income from their stock market investments.



Sources: Global Financial Data Inc; Thomson Reuters Datastream; Deutsche Bank calculations As of: November 18, 2008

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Benjamin A. Pace III and Lawrence V. Adam

US Equities: Leading Indicator?

Declines in US equities in past months mirror declines seen during some of the worst recessions in US history. These declines reflects increased uncertainty as to the extent of the global recession. However, as valuations fall to historically attractive levels, we encourage investors to be patient and begin to anticipate the economic recovery. Assuming a modest recovery materializes in 2009, equity performance should improve.

The short-lived optimism that accompanied the election of Barack Obama as the forty-fourth president has diminished as economic indicators have worsened and credit conditions remain challenged. In the near term, equity market performance will likely be driven by the concern over the depth and duration of a global recession, the lack of visibility in 2009 corporate earnings and the extent to which the US government will engineer future bailouts. Further depreciation in equity prices may also lead to additional mutual fund and hedge fund redemptions which could push equities lower from current levels. As a result, we remain defensive in our equity exposure by favouring non-cyclicals (i.e. healthcare and consumer staples) and large caps over small caps.

For 2009, there are two questions that frame our view: How much of the negative macroeconomic factors have been priced into the equity market? And when might the US economy begin to emerge from recession?

The US equity market is widely accepted as a leading indicator and has likely priced in a recession similar to the 1973/75 and 2001 recessions. The S&P 500 is on pace to record its worst annual performance since the 47% decline during the Great Depression. In addition, the S&P 500's decline from its October 2007 peak has pierced 50% and exceeded the average decline experienced during the previous 19 bear markets dating back to 1929. This massive decline in equity prices has taken valuations to historically attractive levels:

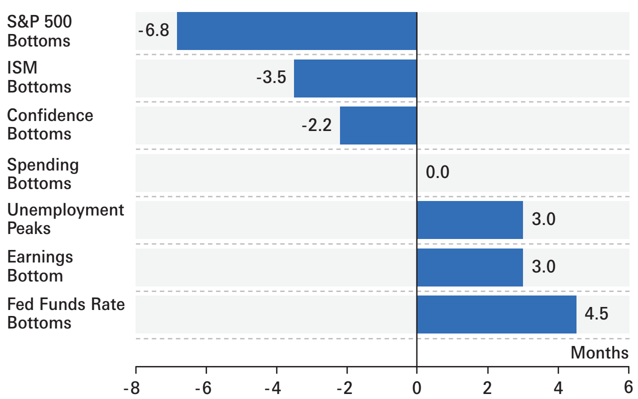
- The trailing PE of the S&P 500 is at its lowest level since 1982, when interest rates and inflation were much higher than current levels.
- The dividend yield of the S&P 500 is at its highest level since February 1991 and has surpassed the yield on the two and ten year Treasury notes.
- The market cap of the Wilshire 5000 ($8 trillion) is at its lowest ratio to GDP ($14 trillion) since 1990.

We caution investors against relying solely on valuations in times of economic turmoil as valuations are not necessarily a catalyst for a sustainable rally. However, taking a long-term view on the economy, there is an increasing probability that the economy begins to recover slowly during 2H09 as a result of fiscal and monetary stimulus, declining commodity prices and the fading impacts of declines in housing. We expect the S&P 500 to anticipate this rebound and move higher before the recession ends. Analysis since 1960 suggests that the S&P 500 typically bottoms, on average, three to seven months prior to the end of the recession.

In addition, while we expect only modest growth in earnings at best in 2009, expectations of an economic recovery, combined with historically low interest rates and inflation, should lead to P/E expansion and support our view that equities can move higher over the next 12 months. However, we reiterate that this is contingent upon the economy beginning to recover in 2H09.

Leading and lagging indicators

S&P 500, on average, bottoms before manufacturing, confidence, consumer spending, unemployment and earnings recover.



Data reflects recessions from 1960 – 2001

Sources: EcoWin; FactSet; S&P As of: November 24, 2008

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Peter Bickley

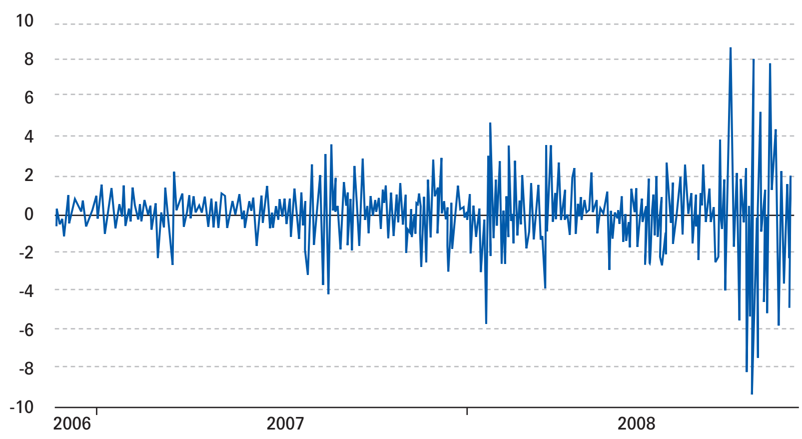
Coping with volatility

The UK economy is in recession, and we have got here earlier than most. Policy responses are cranking up, but at this point it is still difficult to assess the depth and duration of this downturn. Unsurprisingly, there is extreme volatility in share prices. Coming after a nasty bear market, this is a severe test for investors' nerves. The shrewd, though, know that volatility often equals opportunity.

The UK is now in recession and our media are loving it. Competing with each other for the most depressing headlines, they are doing a good job of ensuring that consumer confidence is as damaged as possible. Our prime minister boasted that he had abolished "boom and bust", which shows that those who walk on water sometimes drown. We should recall that a period of very low or negative growth was exactly what the Bank of England wanted to achieve, but we have got here by a very unexpected and frightening route, including the very real possibility of a complete banking collapse. It is not surprising, then, that policymakers' feet are hard on the accelerators.

Shock waves

Daily volatility in the UK equity market has become extraordinary.



UK FTSE 100 Index Daily change in % / Start 17.11.2006 / End 19.11.2008

Source: Thomson Reuters Datastream — As of: November 20, 2008

This recession is harder to read than most; given that it stems primarily from an over-extended household sector, it was at first likely to be lengthy, albeit shallow. With a hobbled banking sector, it is now set to be deeper, but with the Monetary and Fiscal taps turned full on, it may prove shorter than most currently assume. The one thing that we can all agree is that right now we just do not know.

This is difficult for the stock market, where nerves are already frayed by a bear market which seemed to come from nowhere and by the spectre of financial collapse, which is only now slowly receding. As a result, we are seeing quite extraordinary daily volatility; at one level, of course, we all know that as we read and watch the daily news, but the chart puts it into much starker relief. This really is unprecedented market behaviour.

Elevated volatility is not per se unusual, especially at inflection points. Whether as illustrated by the chart or by reference to the Chicago VIX, we can match volatility to uncertainty with a very good fit – and uncertainty is at its highest when trends are turning. We can hope – but not assume – that the bear market is at a terminal stage. More usefully, how can we deal with today's market conditions?

Previous articles have discussed the UK market's lumpy sector make-up. Resources, currently friendless as commodities wilt, are expected to recover strongly when the world comes to its senses and this should drive the index higher even if banks continue to languish. Many high quality, financially robust and cash-flow rich companies are sitting on derisory valuations, even after draconian assumptions for profit falls.

Shrewd investors look to the long term and like to lock in value when it is available rather than chase it when it is not. That is the opportunity in today's volatility; on the big down days, raise your head from your hands and tuck away stocks for the future.

Peter Bickley is Chief Economist and Head of Asset Allocation Strategy at Tilney Private Wealth Management.

Soon-Gek Chew

Facing the downturn

Asian markets are impacted by recessionary conditions in the developed markets due to trade and capital market links. On the positive side, inflation is falling with energy prices contracting sharply. More interest rate cuts and fiscal measures to boost growth are forthcoming. Asia's financial and corporate sector has entered the credit crisis on stronger balance sheets than during the Asian currency crisis in 1998. In the context of global deleveraging and capital repatriation, our preference is to be in invested in countries with high reserves, current account surpluses and little dependency on external bank financing.

Asia ex-Japan is expected to grow by 5.5 % in 2009 and 5.9 % in 2010, on the back of growth of 7.6 % in 2008. In contrast, the global economy is experiencing the lowest growth since the 1980s, with forecast growth of 1.2 % in 2009 and 2.5 % in 2010. Asia cannot escape the global slowdown, as it has many export dependent economies. There are only a few large economies with sizeable autonomous domestic demand, namely China, India and Indonesia. Even in China, fixed asset investment growth has a high correlation with exports, and the slowdown is expected to intensify next year.

Inflation has started to fall over the last few months, providing flexibility for monetary easing. Chinese inflation is now running at 4 % in October and Indian wholesale prices at 9.9 %. China, India, Korea, Taiwan, Hong Kong and Vietnam have cut rates.

China has announced a fiscal boost amounting to USD 586 billion, or about 16 % of GDP, to be spent largely on infrastructure, the export and agricultural sector over 2009 and 2010. With USD 2 trillion in foreign reserves, China has the financial resources and will to reflate its economy. However, the pace of deceleration in exports and investment is rapid, and we expect China to grow by a lower 7.6 % in 2009.

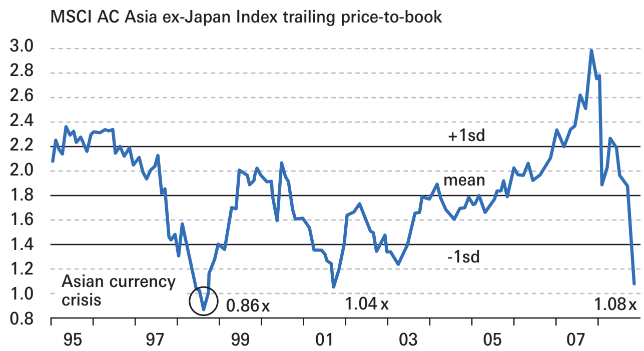
The Asia ex-Japan equity index has fallen by more than 50 % this year on global recession concerns and widespread deleveraging. Longer term growth fundamentals have taken a backseat to technical unwinding and capital repatriation. In a deleveraging world, our preferred markets within Asia are those whose economies have strong foreign exchange reserves, balance of payment and fiscal surpluses. These include China, Taiwan, Hong Kong and Singapore. We are cautious on Korea and India, where parts of the corporate and banking sector have external financing dependencies.

Overall, Asia's financial and corporate sector has entered the global credit crisis on a stronger footing than during the Asian currency crisis. Asian banks have adequate capital and corporate gearing is around 20 %, half the levels of the previous Asian crisis. Asset quality is not impaired. On a price to book basis, Asia is trading at 1.08 times, close to the bottom reached during the Asian crisis. The price to book has averaged 1.8 times over the last 13 years, with a high of 3 times and a low of 0.86 times. The forward price earnings ratio of the markets is less helpful a measure at this point of earnings deceleration. Expected earnings volatility is high in the wake of macroeconomic uncertainty and currency volatility.

In the face of indiscriminate selling, it makes more sense to sit through the investments which are trading close to book values. One could consider adding exposure in 2009 on signs of stabilisation of the economies and earnings.

Asia ex-Japan price-to-book valuation

Asia is trading at close to one time book value. Valuation are close to bottom reached during the Asian Crisis.



Source: Bloomberg As of: October 27, 2008

Soon-Gek Chew is Chief Investment Officer for Private Wealth Management at Deutsche Bank in Asia.

Marshall Gittler

Continue to underperform

With its domestic economy still fragile and the yen strengthening, Japan has been hard hit by the downturn in the global economy. Its continuing political crisis only makes matters worse.

We first downgraded Japanese stocks from "outperform" in June of 2006. Since then, the market is down 47 %, vs. a 32 % decline in the US and a 35 % decline in Europe. Moreover, from the time we downgraded it to the peak, Japan rose only 13 %, vs. 21 % for the US and 24 % for Europe over the same period. The Japanese market's time in the spotlight was brief – barely three years from the rescue of Resona bank in April 2003 until February 2007. Now the Nikkei index is back to the level of 1982. Investors would do well to remember this fact when next they read that "stocks always go up in the long term" – whomever they are reading should be careful to define which stocks and how long the long term is.

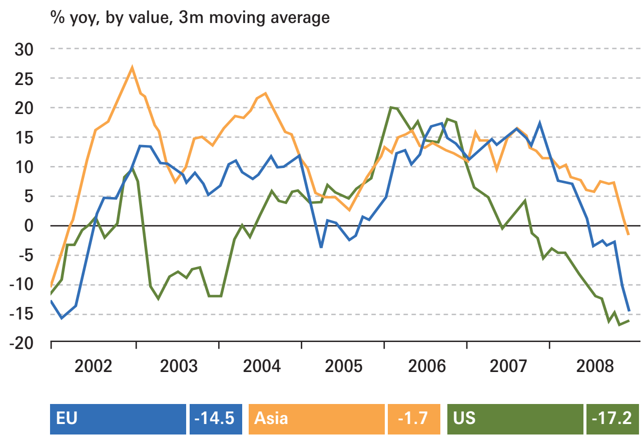
Japan's problems remain as we have said before. The domestic economy is still fragile, and the economy depends on foreign demand, which is now collapsing as the world falls into recession. Faced with years of deflation, Japanese companies have focused on cutting costs and reducing debt. Wages were an obvious place to start. The result is a labour force that is now about one-third part-time workers, whose low wages and low confidence in their futures translate into sluggish domestic demand. Instead, growth has come from buoyant external demand, particularly from the nation's fast-growing hinterland, Asia. Exports to the US began to decline on a year-on-year basis in September of last year; exports to Europe turned negative in May of this year; but with the Asian economies holding up, exports to the region continued to grow until October, when they fell 4 % yoy. The result was a sharp 7.7 % decline in the value and 6.1 % fall in the volume of exports during the month and a trade deficit for the third month in a row (SA). The decline in exports was widespread, with almost all sectors affected. As the recession abroad intensifies, we expect Japanese exports to decline further and for the economy – now officially in recession as GDP has contracted for two consecutive quarters – to worsen further. The global risk aversion that is causing investors to take off yen carry trades, thereby strengthening the yen, only makes things worse.

As if this was not enough, the new prime minister, Taro Aso, has proved no more capable of turning around the country than his two predecessors in the preceding two years. He was expected to call a snap election upon taking office that would revive confidence in the government, but two months after coming into office that plan is on the back burner and public support for his administration has fallen to 37 %, according to a recent poll. His 5 billion yen fiscal stimulus plan to boost growth was labeled "incoherent" and "chaotic" by two newspapers, and there is now talk that he too could resign before elections have to be held next September.

With the economy in decline, the currency strengthening, and the political class unable to come up with appropriate strategies to deal with the problems, we see no reason to get excited about Japanese shares now even if valuations are at historically low levels.

Japanese export growth

Exports to the US started to decline last year, exports to Europe turned negative earlier this year, but it was only in October that exports to Asia fell below the previous year's level. This removes the last underpinning of growth from the Japanese economy.



Source: Bloomberg — As of: October 2008

Marshall Gittler is Chief Strategist for Private Wealth Management at Deutsche Bank in Geneva.

Dr. Uwe Hoffmann

US Treasuries – headed for a Japanese-style yield curve?

The Fed's policy rate has rapidly approached the low of the previous rate cutting cycle. Yet this time around, it seems close to certain that 1 % is not going to be the bottom. As the Fed funds target rate approaches the "zero bound", many observers turn their eyes to the Japanese experience to figure out what may come next. Yet the Japanese "zero interest rate policy" may not provide the best guidance.

No less than Ben Bernanke himself has long been keen to emphasise that a central bank has not run out of ammunition once its policy interest rate is cut to zero. The Bank of Japan (BoJ) eventually engaged in "quantitative easing", flushing the banking system with excess liquidity and purchasing huge amounts of long-dated Japanese government bonds in order to stabilise the financial system, to reduce long-term interest rates and to reduce the discount on risky assets such as stocks and corporate bonds.

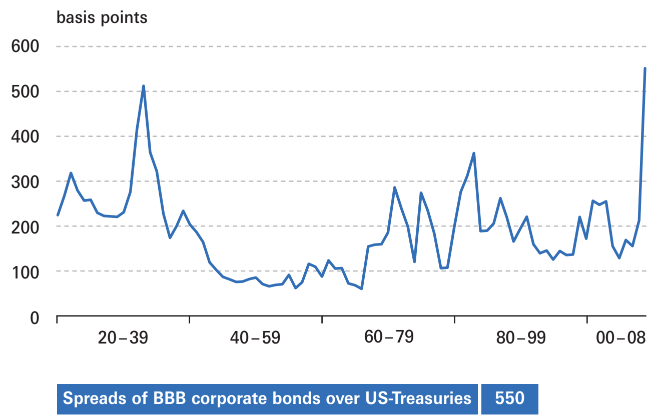
Bernanke's key criticism of the BoJ's measures was that they were not bold enough to tackle the deflation problem. So it is little surprising to see that the Fed and US Treasury have taken much more aggressive measures in the course of months than the Japanese authorities had taken over the course of a decade, including a swift (although bumpy) recapitalisation of the banking system, sovereign guarantees for new bank borrowing, direct central bank lending to the corporate sector and, most recently, the planned purchase of risky assets, especially agency mortgages, on a grand scale by the Federal Reserve.

This latest asset purchase programme may well be the most significant measure taken so far and goes indeed to the heart of the problem: a housing market depressed by excessive mortgage debt and a capital market derailed by homeowners defaulting on their mortgages. The implications for the bond markets seem relatively clear: short-term rates will be at or close to zero for longer than markets currently anticipate, and long-term Treasury yields may well fall significantly below 3 %. That would indeed bring the Treasury market closer to the yield curve prevailing in Japan.

Yet unlike JGB's, which in 2003 were 95 % owned by Japanese investors, around half of the federal debt is currently owned by non-domestic investors. As the Fed finances its debt purchases by printing money, it will need to keep a close eye on the confidence of these foreign investors. Losing their confidence would be highly detrimental to the Treasury market and US bond markets in general, as well as the US dollar. Therefore, while our base case is for a flatter Treasury yield curve with 10-year rates going well below 3 %, a loss of confidence could trigger a sharp sell-off and steepening of the yield curve.

Corporate bond spreads are firmly in depression territory

The difference between the yields of BBB-rated corporate bonds and Treasury yields now exceeds to the all-time high reached during the Great Depression. This is a disturbing comparison, considering that the US experienced a massive economic contraction during that period. Given that both monetary and fiscal stimulus has been implemented much faster and much more vigorously in recent months than in the early 1930's, it seems unthinkable that we should face such dire conditions again. This, in turn, suggests that corporate bonds offer better value than Treasuries over the medium to long-term.



Source: Moody´s

As of: November 30, 2008

Dr. Uwe Hoffmann is Head of Fixed Income, Private Asset Management International at Deutsche Bank in London.

Matthias Pannhorst

Foreign exchange markets in the grip of the financial crisis and recession

The financial market crisis has now clearly spilled over to the real economy. In our view, the looming global recession will impact foreign exchange markets, too, until well into next year.

The trends prevailing on currency markets since the summer are likely to persist for some time yet as they nearly all have the same root cause: the continued risk aversion on the markets and the deleveraging process in the global financial system have globalised a crisis which has its roots in subprime mortgages and now virtually affects all asset classes. Although, on the whole, the foreign exchange market is still influenced to a large extent by equity markets, the transmission channels differ with respect to the individual currencies.

- **USD** The US currency has benefited in recent months from massive capital inflows into the dollar area. In past years financial institutions in particular made considerable use of cheap US dollar funding, but emerging markets mostly used dollar financing as well. The debt reduction process in both these areas is not over yet. While the momentum for the dollar has slackened, deleveraging, risk aversion, low commodity prices and a well advanced interest rate cycle should continue to provide support in the coming months, although the pace of the rise should slow appreciably.

- **EUR** The euro remains strongly dominated by dollar movement. Scope for rate cuts, recession, structural differences within the euro zone, and plummeting export demand suggest continued weakness.

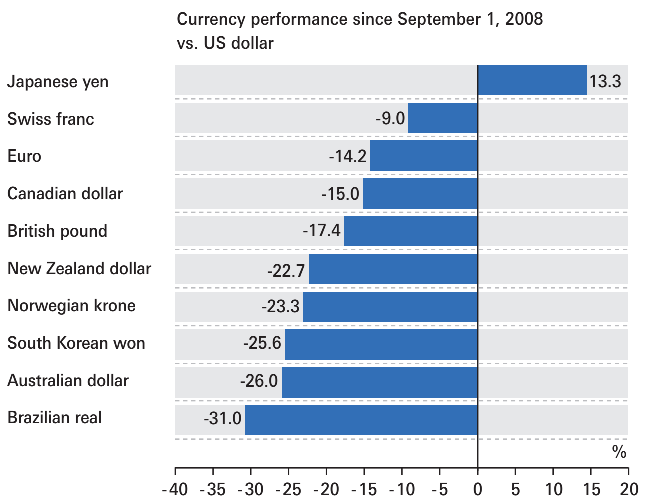
- **JPY** Japan's interest rate disadvantage is shrinking and, with that, so too is the incentive for Japanese investors to hold investments abroad, which was very much the case in the past. With carry trades continuing to underperform, the yen is likely to benefit further. A risk would be drastic intervention by the Bank of Japan.

- **GBP** Public finances have deteriorated sharply as a result of government investments in a number of troubled banks. On top of that, there are potential liabilities under guarantees given for the banking system. At the same time, the pound sterling has lost almost a fourth of its value (vs. the US dollar) since August. While at first sight a weak currency would appear helpful for Britain, which will probably be hit harder by the global downswing than most of its Western European neighbours, the pace and scale of the currency's depreciation gives cause for concern. Given falling interest rates, a high external deficit and a strongly contracting economy, the pound should remain weak.

- **Emerging Markets** EM currencies have fallen across the board. However, it will probably be more the fundamental criteria again that decide when recoveries set in and how lasting they will be. Countries with high deficits and strongly managed exchange rates will have a harder time. Flexible exchange rates allow more leeway in monetary policy, especially in response to capital outflows, without provoking a rise in inflation. Above all, Eastern European currencies and the rouble should continue to suffer from high external government and corporate debt respectively.

US dollar dominates

Since the financial crisis last escalated at the beginning of September, the foreign exchange markets have been influenced above all by the strength of the dollar. Only the yen has benefited even more from the global deleveraging process, while emerging markets and high-interest currencies lost most.



Source: Bloomberg As of: November 20, 2008

Matthias Pannhorst is Fixed Income and FX Strategist in the Investment Strategy Group, Private Asset Management at Deutsche Bank in Frankfurt.

Dr. Stefan Mitropoulos

Real estate markets in the downturn

The global financial crisis and recession in leading economies are causing many commercial property markets to weaken. The upshot: much lower total returns on direct real estate investment. In the more difficult environment, investors should concentrate on quality properties leased long-term in relatively stable markets.

The ongoing financial crisis and the ever worsening economic outlook are causing conditions on the real estate markets to deteriorate in many countries. This is also reflected in the total returns on direct real estate investment. The British property market, where the fall in commercial property prices has even accelerated of late, continues to be the hardest hit in Europe. According to Investment Property Databank (IPD), 2008 is set to be the worst year since the property index was first launched in 1987. The data for October show a negative total return of 20 % year over year. By contrast, the NCREIF Property Index still showed a plus of 5.3 % for the US in the third quarter of 2008. However, there, too, the slowdown is expected to continue. This is indicated by a first small drop versus the preceding quarter.

Further strong losses on real estate equities

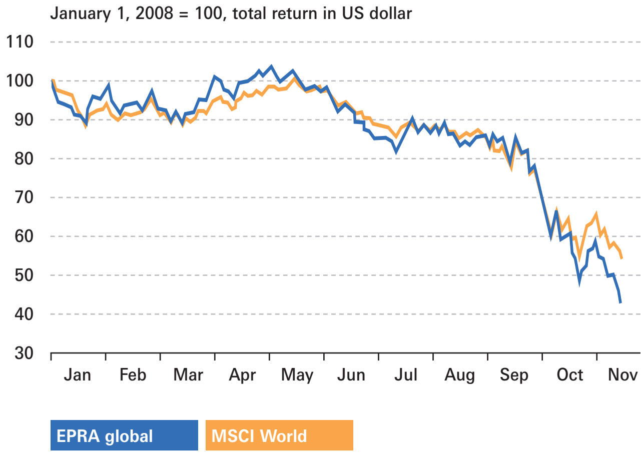
The real estate markets are therefore gradually witnessing the development that has been anticipated in the stock prices of listed real estate companies for some time. However, with the further escalation of the financial crisis, property stocks have been hit far more strongly than the fundamental outlook would appear to warrant. After heavy losses already last year, the FTSE EPRA NAREIT global property stock index is also well into negative territory so far in 2008. Since the beginning of the year to the end of November, the index lost about 45 % in euro terms and 52 % in US dollar terms. Property stocks performed more or less in line with the equity market generally until some way into October but have underperformed again more recently. Driving factors have probably been concerns over refinancing problems at individual companies and expected falls in property values in a number of markets.

Focus on quality and low leverage

Property stocks are likely to remain very volatile in the currently more difficult environment. As with unlisted investments, investors should concentrate on upmarket property portfolios of above-average quality – a strategy currently favoured by institutional real estate investors. This includes modern interior, prime locations, and especially long-term lease contracts with tenants of high credit quality. Another point on which to focus is that the companies should not be too highly leveraged, and above all that their refinancing is assured for the coming quarters. Finally, preference should be given to regional markets that, given low growth in supply, promise a relatively stable development in the coming years. Despite the general deterioration on the global real estate markets, such locations can be found in Europe as well as in North America and Asia.

Property stocks remain under pressure

Global property stocks moved largely in line with the market until October. They have underperformed again more recently.



Source: Thomson Reuters Datastream — As of: November 19, 2008

Dr. Stefan Mitropoulos is Real Estate Specialist and Equity Strategist in the Investment Strategy Group of Private Asset Management at Deutsche Bank in Frankfurt.

Dr. Elke Speidel-Walz

Under mounting pressure

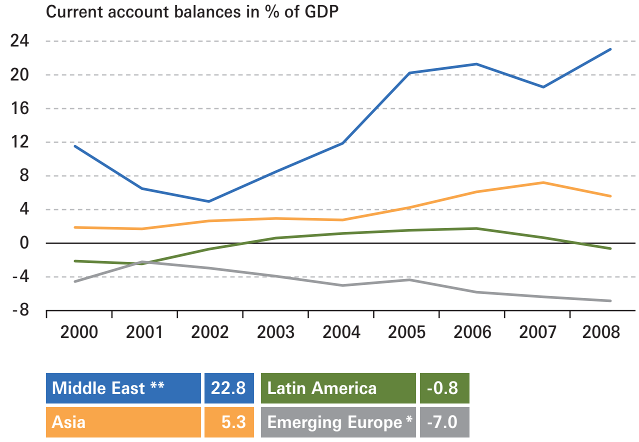
The growth outlook for the emerging markets has deteriorated further with the recession in the G3 countries. While they alone will contribute to global economic growth in 2009, performance will differ from region to region. Growth in Eastern Europe and Russia, which has been buoyed to a large extent by debt and foreign capital inflows, is likely to fall strongly. The situation for the Latin American countries with a strong commodities bias is similar as their commodity exports are likely to sink. In Asia, the outlook is mixed: China and India will also see slower growth but will be the dominant economies in the region, with growth close to their long-term potential. The region as a whole is expected to grow at 5.5% next year.

Bond markets: Rising default risks, volatile currencies
The emerging bond markets have come under massive pressure. In some countries, there are acute or sharply increased default risks: Pakistan, Ukraine and Hungary had to be rescued from national bankruptcy with extensive IMF programmes. In the currently difficult global environment, Argentina's economic policy errors in the past have driven the country to the verge of bankruptcy again. Ecuador is officially in default. Turkey and South Africa face no acute financing problems as yet, but their very high borrowing requirements in 2009 could weigh on these markets for some time.

Macroeconomic weakness is now visible
Generally, countries with high government and/or corporate debt are suffering most from the global credit crunch. This is true especially if the debt is short term and/or in foreign currency. In these cases, the strong depreciation of the emerging market currencies in the past weeks creates a vicious circle of rising debt service burdens, capital outflows and further currency depreciation. The central banks face the dilemma of either being forced to abandon their inflation targets, even if currency weakness drives up inflation, or accepting growth risks with higher interest rates. These macroeconomic weaknesses prevail in most countries in Eastern Europe such as Hungary or Russia on a more or less pronounced scale. The strong economic growth in the past years was financed by a credit boom. Overheating with strong wage escalation and declining competitiveness were the result. Despite the strong growth in export revenues also in Eastern Europe, the current account deficits have been driven up further from their, in part, already high levels by even stronger import demand. As a result, these countries were very vulnerable to a crisis on the international capital markets. Another problem is the strong presence of West European banks in Eastern Europe. Struggling with capital shortages at home, they are cutting back on lending by their foreign subsidiaries.

Strong mixed development in the current accounts

The current account positions show a very mixed development: the oil-exporting countries and Asia have high surpluses, in Latin America the deficits are low by historical standards, in Eastern Europe the deficits are continuously rising.



* Bulgaria, Croatia, Czech Republic, Estonia, Hungary, Latvia, Lithuania, Poland, Romania, Slovak Republic, Turkey
** Bahrain, Egypt, I.R. of Iran, Jordan, Kuwait, Lebanon, Libya, Oman, Qatar, Saudi Arabia, Syrian Arab Republic, United Arab Emirates, Republic of Yemen

Sources: Deutsche Bank AG, Private Asset Management; IMF World Economic Outlook, October 2008

Commodity-dominated markets have generally suffered heavy setbacks. In Mexico and Brazil, the bond markets are not suffering as a result of default risks, thanks to the positive fundamental situation and moderate debt service burden, but above all from the global pressure on almost all currencies, except for the USD. The recent troubles at several large companies are due to miscalculated currency speculation and the temporary extreme shortage of USD liquidity that made it difficult to service foreign currency loans.

Outlook-bond markets

All in all, the outlook for the emerging bond markets will remain difficult so long as the global tensions on the credit market have not unwound and global risk aversion leads to capital outflows from all risky markets. However, in the mid term, the prospects for Latin American countries with solid fundamentals such as Mexico and Brazil and for most Asian countries look positive again. Owing to the structurally much weaker position of East European countries the crisis on these markets is likely to be longer.

Mixed outlook for the BRIC countries

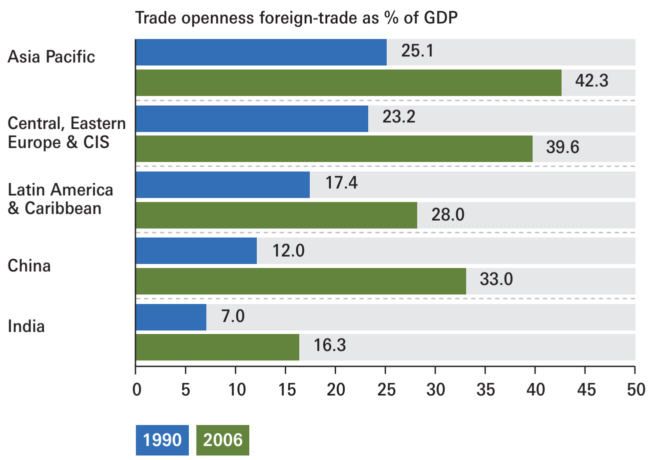
In **Russia**, the financial markets are suffering not only from the negative external influence but also from a number of internal macro and microeconomic problems. Not only the equity market but also the Russian bond market is under heavy pressure despite high foreign exchange reserves and the state's net creditor position. Banks and companies have high levels of debt in foreign currency. The central bank is having great difficulty stemming the currency's decline despite large-scale market intervention and has already had to widen the range for tolerated rouble depreciation. The foreign exchange reserves have melted away at an unprecedented rate of late, from USD 600 billion in June to USD 450 billion in mid-November. Economic growth is likely to halve next year. Oil accounts for two thirds of the country's export revenues and the budget for 2009 is based on an unrealistically high oil price of close to USD 100. The financing problems at many banks and companies will also crimp growth. Nonetheless, the expansive fiscal policy will keep inflation in the double digits. The previously high current account surplus is likely to swing into deficit in 2009. The government budget is still in surplus. The so-called break-even level for the oil price, the price at which the budget is just in balance, is probably around USD 75 and could quickly rise to USD 90. The risks for a reversal into budget deficits are high. The foreign exchange reserves are likely to go on shrinking.

In **Brazil**, heavy losses have been witnessed on the financial markets and especially in the currency, -26 % vs. the USD year to date, despite the still robust state of the economy. The sectors that rely on commodity prices are the weak point. Domestic consumer demand, on the other hand, is still very robust considering the external headwind and the monetary dampening over the last 12 months. The banking sector is solid, and the state's debt situation is still reasonable. It remains to be seen whether the central bank can switch to a rate easing phase next year. Set against the price-damping effects of the expected economic downturn, there are the inflationary effects of currency depreciation. However, all in all, there is much to suggest that in the mid term Brazil's bond and equity markets will offer attractive upside potential again from their currently very low level.

In **China**, too, the growth risks have increased considerably of late, although the solidity of the banking system and the low level of government and private-sector debt actually shield the country more or less from the present crisis. The growth risks here stem from plummeting export demand and the weakness on the domestic housing market, which

Trade openness: An advantage turns into a disadvantage

The opening of the emerging markets brought strong growth to these economies in the past years. In times of recession in the G3 countries, they are exposed to the sharp fall-off in exports.



Sources: Deutsche Bank AG, Private Asset Management; Fitch Ratings clouds the outlook for investment demand. The weakness on the property market is a result of past restrictive monetary policy, which was to cool down this overheated market. However, set against the downturn, primarily in the market for luxury housing, there is continued strong demand in the lower-priced segment driven by urbanisation and rising incomes. Last year, urban real incomes rose by 10% and rural real incomes by 14%. Household debt is low at 13% of GDP including home loans. Extensive fiscal and monetary policy measures to stimulate the economy should ensure that growth does not fall far from long-term potential growth of 7 – 8%. The priority at the moment is on stabilising the domestic housing market, investment in infrastructure – which is needed anyway – and social security for the rural population.

In **India** – as in China – the banking sector is relatively robust and affected little by the global credit crisis. As India's economy is far less open than China's, the effect of the fall-off in exports is not as pronounced as in China. On the other hand, owing to the lower saving ratio and higher budget deficits India has far less leeway for stimulating the economy. In 2009, growth is likely to fall below the long-term potential path, which is estimated at 7.5%.

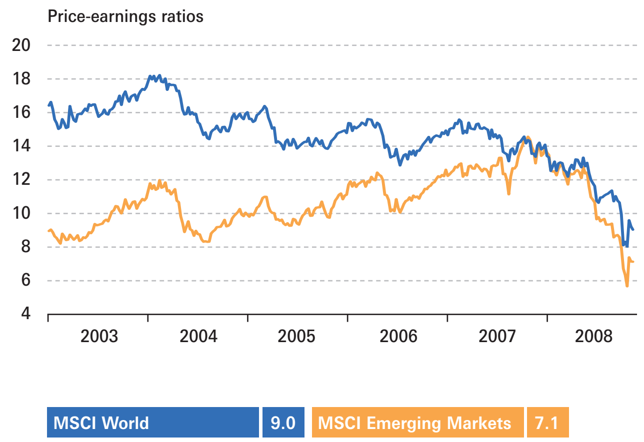
Equity markets: Valuation, fundamental position and long-term structural changes are positives in some countries

Emerging market equities are meanwhile very cheap both in absolute terms by historical comparison and relative to the established markets. Valuation levels have fallen well below those of the industrial countries, which does not appear warranted given the better longer-term earnings prospects. The historical comparison also suggests a recovery. The valuation of many Asian emerging markets is currently even below the low point during the Asia crisis. However, the fundamental situation, with the exception of Eastern Europe, is much improved: well capitalised banking sector, lower debt, liberalisation, reforms, more flexible exchange rates. On the other hand, the opening of the economies over the past years means that the growth outlook and earnings expectations in almost all the emerging markets are strongly exposed to the recession in the developed countries through exports of merchandise and / or through lower commodity prices.

The positive factors for future equity market performance are favourable valuation, fundamentally more robust economies, structural changes in terms of demographics and / or urbanisation, an economic policy focus on energy efficiency, and infrastructure development. This holds especially for China and India and to some extent as well for Brazil and Mexico although Brazil is hurt by the outlook for commodity prices and Mexico by the US recession, especially in the automotive sector. Despite the very favourable valuation and the positive mid-term growth outlook in some emerging markets, a turnaround on these financial markets is unlikely in the short term. A sustained recovery of the emerging markets is only probable once the uncertainty over the length and depth of the recession in the US and Europe and the threat of a prolonged deflationary development recedes into the background again.

Valuations at absolute and relative lows

Emerging market equity valuations are meanwhile not only below their historical lows but also below the level for the equity markets in the industial countries.



Sources: Thomson Reuters Datastream; I/B/E/S As of: November 14, 2008

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Key factors for equities / bonds / alternative investments*

Europe

Equity market

+ (Positive factors)

- Market conditions should improve in the medium term thanks to fiscal and monetary policy measures
- Sliding commodity prices, a weaker currency and cost-reduction programmes should limit the decline in earnings
- Historically low valuation

– (Negative factors)

- Falling demand for goods leads to diseconomies of scale
- Further deterioration in economic outlook in short term
- Profit growth rates will decline in the coming quarters
- Overly high analyst forecasts; low earnings visibility

➡ **Share prices should remain weak in the short term and are unlikely to rise until the medium term**

Bond market

+ (Positive factors)

- Safe haven role of government bonds in the confidence crisis in the money and financial markets
- Core inflation rate (excluding energy and food) remains moderate due to effects of globalisation
- Sharp drop in consumer price inflation due to falling commodity prices
- Slump in sentiment indices and leading indicators points to strong slowdown in growth
- Further ECB key rate cuts expected

– (Negative factors)

- Higher supply of government bonds to finance fiscal policy measures
- Differences in fiscal policy measures of euro participants will increase pressure on spreads to widen

➡ **Persistently low bond yields expected**

USA

Equity market

+ (Positive factors)

- Profit cycle more advanced than in the European market; earlier recovery is therefore likely
- Support for the economy from strong monetary and fiscal stimulus
- Highly attractive relative to bonds

– (Negative factors)

- Negative profit revisions and recessionary conditions are detrimental
- Further negative reports expected from problem sectors
- Banks' restrictive lending is making refinancing and M&A activity difficult

➡ **Risks to share prices will prevail in the short term; notable upside potential unlikely until medium term**

Bond market

+ (Positive factors)

- Safe haven role of government bonds in the confidence crisis in the money and financial markets
- Mortgage market problems hit consumer spending
- Sharp drop in consumer price inflation due to falling commodity prices
- Slump in sentiment indices and order intake points to strong slowdown in growth

– (Negative factors)

- Higher supply of government bonds to finance fiscal policy measures
- High inflation rate relative to the current yield level
- Risk of capital outflows in the event of excessive US dollar weakness

➡ **Persistently low bond yields expected**

* Source: Deutsche Bank AG + = Positive factors – = Negative factors ➡ = Assessment

Japan

Equity market

+

- Strong integration of companies in Asia, the fastest-growing region
- Historically favourable valuation
- Declining commodity prices provide relief

–

- Particularly affected by global growth fears due to highly cyclical structure
- Strong yen erodes competitiveness
- Further negative profit revisions expected
- Current fiscal stimulus programme is inadequate

➡ **Japanese equities are highly dependent on global factors; potential for rising share prices is lower than in other markets**

Bond market

+

- Weak domestic economy and persistently low inflation rates
- Repatriation of foreign investments and unwinding of carry trades
- Central bank biased towards boosting liquidity further to avoid threatening weak growth momentum

–

- High level of government debt
- Stabilising real estate prices limit the relative attractiveness of bonds
- Normalisation of monetary conditions

➡ **Persistently low bond yields expected**

Alternative Investments

Commodities

+ Structurally robust demand from Asia; a number of commodities are trading close to the levels of marginal production costs; persistently low inventories for many commodities

– Growth fears and the concomitant fall in demand for commodities are pushing down commodity prices; heightened risk aversion is generating additional pressure on prices due to sales of commodity investment products

Hedge funds

+ Widely diversified hedge fund investments have a stabilising influence on portfolios during difficult market phases. With suitable manager selection, there is a chance of achieving a higher return than in traditional asset classes

– Increased credit costs and difficult market conditions could continue to impair performance. Manager risk is greater compared to traditional market risks

Real estate

+ Weaker fundamental data are largely priced into real estate securities; falling prices in individual markets generate buying opportunities

– Continued restrictive lending and economic downswing are weighing on real estate markets; transaction volumes have slumped on many markets; sharp drop in total returns

Currencies

+ Dollar appreciation should slow, but no foreseeable turnaround in EUR and GBP as yet. JPY is still benefiting from current conditions despite the significant decline in fundamental data

– EM currencies remain under pressure. Caution is particularly advised vis-à-vis Russia and Eastern Europe

➡ **Return potential with diversification qualities in times of crisis are arguments for an addition of alternative investments to portfolios**

Sources/Fuentes: Bloomberg; Deutsche Bank AG; EcoWin; Edhec; FactSet; Fitch Ratings; Global Financial Data Inc; I/B/E/S; IMF World Economic Outlook; Moody's; S&P; Thomson Reuters Datastream

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