

Quarterly Asset Allocation Strategy

June 2011

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Highlights:

- While equity market performance may remain subdued in the near term, we expect selling pressure to gradually subside. From a valuation perspective, equities are getting cheaper and further corrections would present investors with bargain hunting opportunities.
- This year, economic growth in the US may not be as strong as last year but a weaker economy does not necessarily imply a double-dip recession. That explains why Federal Reserve chairman Ben Bernanke hinted that a third quantitative easing programme is not on top of the policy agenda.
- As major manufacturers in Japan started to restore their production, the global supply chain is expected to resume to normal in the third quarter. Such a development should gradually improve global industrial production and allay investor concerns on a worldwide economic slowdown.
- The Greek contagion is a concern. Although a full-blown European financial crisis is politically unpalatable, progress in discussion about Greek aid among the European Central Bank, the IMF and European leaders would be slow due to their diverse political interests.
- In Asia, investor confidence could return if local central banks could keep inflation under control over the next few months. Also, the valuation of Asia (ex Japan) equities is getting more attractive. These, coupled with resumption of global supply chain, should provide support to equity prices.

Asset Classes	Outlook
Equities Funds	+
US	+
Europe	=
Japan	=
Asia (ex Japan)	+
Emerging Markets (ex Asia)	+
Bond Funds	-
Government (Developed economies)	-
Corporate (Developed economies)	+
Emerging Markets	+
Money Markets Funds & Cash	=

Traditional Asset Classes

We believe equities are likely to outperform bonds in the longer term despite the recent sell-off. Major stock indices tumbled in May and early June due to disappointing US economic data and renewed concern about the European debt crisis. The MSCI World Equity Index was down by 1.7% in May. The JPM International Government Bond Index, on the other hand, gained 1.1% during the same period as investors sought shelter from rising economic uncertainties in the US and Europe.

While equity market performance may remain subdued in the near term, we expect selling pressure to gradually subside. From a valuation perspective, equities are getting cheaper and further corrections would present investors with bargain hunting opportunities. On the economics front, the sub-par economic readings over the past few months may partly be due to a temporary supply chain disruption after the earthquake in Japan. As major manufacturers in Japan started to restore their production, the global supply chain is expected to resume to normal in the third quarter. Toyota and Honda, two of Japan's biggest auto makers, earlier said that their domestic production would recover by the middle of this year. Such a development should gradually improve global industrial production and allay investor concerns on a worldwide economic slowdown.

US Equity Funds

This year, economic growth in the US may not be as strong as last year but a weaker economy does not necessarily imply a double-dip recession. At the first glance, the labour market seems to be deteriorating with May's unemployment rate rising to 9.1%, the highest so far this year. However, this may indicate that those workers who previously gave up on job-hunting are starting to return to the labour force. Another weak number was non-farm sector's employment which only increased by 54,000, the weakest reading since September last year. Nonetheless, some employers may put their hiring plans on hold because of the supply chain disruption caused by Japan's quake. Once production activity returns to normal, companies may resume their hiring activities.

Hence, the so-call economic "soft-patch" concern is likely to fade gradually over the next few months. That explains why Federal Reserve chairman Ben Bernanke hinted that a third quantitative easing programme is not on top of the policy agenda.

European Equity Funds

In Europe, the Greek contagion is a concern which hurt the performance of equity markets in the continent. In May, the German DAX index went down by 2.9%, underperforming S&P 500 (-1.4%), FTSE 100 (-1.3%) and Nikkei 225 (-1.6%).

Although a full-blown European financial crisis is politically unpalatable, progress in discussion about Greek aid among the European Central Bank, the IMF and European leaders would be slow due to their diverse political interests.

Japanese Equity Funds

In the near term, we are still cautious on Japan. March's earthquake and the subsequent nuclear contamination left their scars on both economic statistics and corporate results. Retail sales in April fell by 4.8%, more than expected. The trade account slumped into JPY 496 billion deficit in April from March's JPY 1.4 billion surplus. Exports dropped by 5.45% due to power outages and supply disruptions. Both Toyota Motor and Honda slashed their annual profit forecasts due to the impact of the massive earthquake.

Asian (ex Japan) Equity Funds

In 2011, Asia (ex Japan) equity funds are still expected to do well. In the short term, however, the economic picture is complicated by disappointing US data and disruption in manufacturing supplies caused by the earthquake and nuclear disasters in Japan. In April, South Korea's industrial production, a bellwether for global manufacturing and trade activities, unexpectedly contracted by a seasonally adjusted 1.5% month-on-month. The effect of monetary tightening in China and India were also felt in their economic statistics. China's official Purchasing Managers Index fell to 52.0 in May from 52.9 a month earlier. India's GDP growth decelerated to 7.8% in Q1 this year from Q4's 8.3%.

Investor confidence could return if central banks in Asia could keep local inflation under control over the next few months. Also, the valuation of Asia (ex Japan) equities is getting more attractive after the recent corrections. These, coupled with resumption of global supply chain, should provide support to equity prices in the later half of this year.

Emerging Markets (ex Asia) Equity Funds

We are positive on the long-term outlook of emerging markets (ex Asia) but the recent economic uncertainties stirred fear that demand for natural resources produced by Russia and Brazil, two of the world's largest emerging economies, may moderate. Brazil's GDP expanded 4.2% year-on-year in the first quarter, down from 5% a quarter ago. In May, Russia's RTS equity index plummeted by 6.8%, underperforming other emerging markets. The WSJ reported that so far this year, five Russian IPOs have been called off while many of those that have managed to be listed did not perform.

Bond Funds

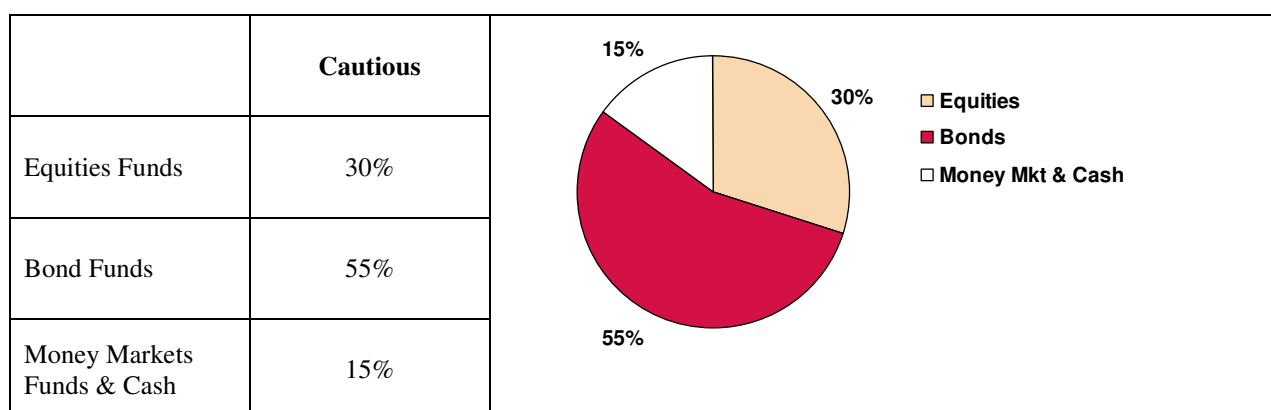
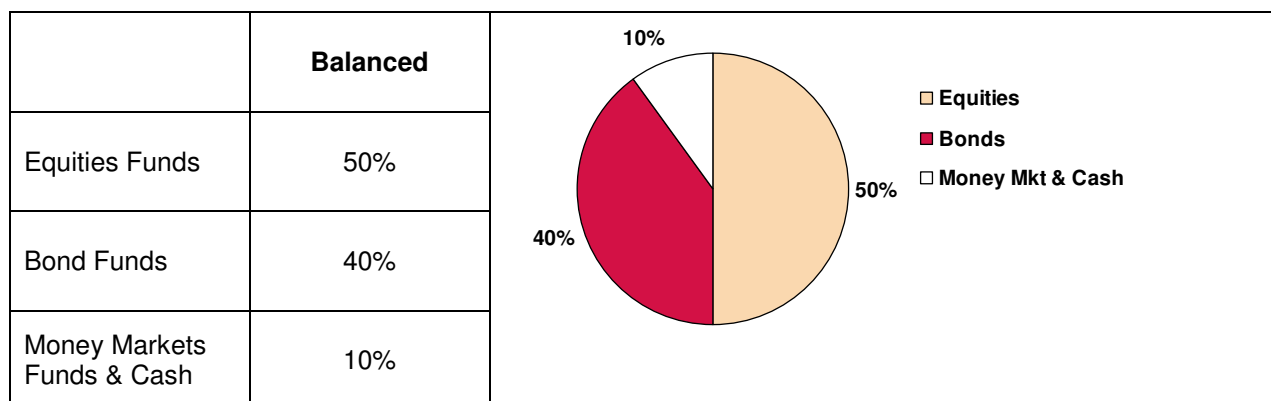
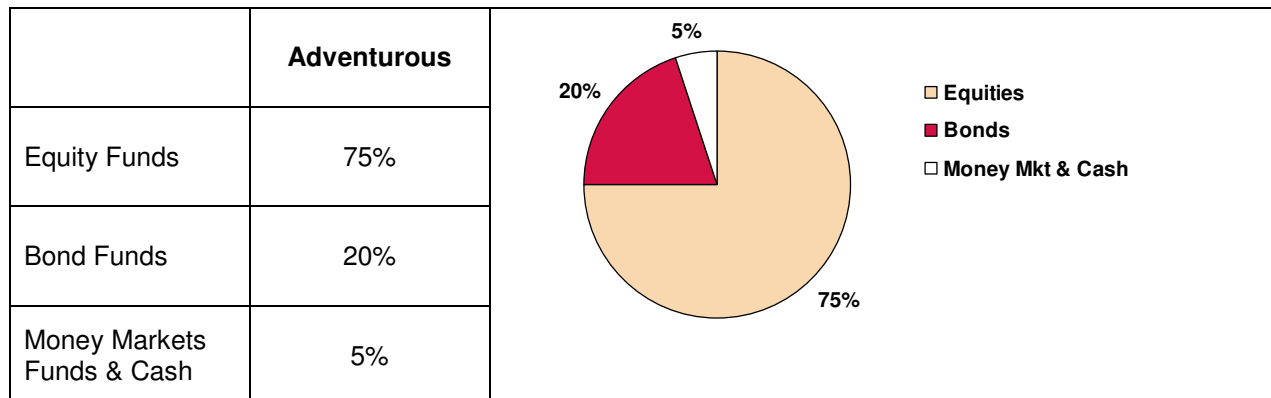
Despite the recent rally, bond funds are expected to underperform equity funds in 2011. US treasury yields are low due to flight-to-safety purchases triggered by concern over the European debt crisis and the uncertainty after the end of US quantitative easing. However, should the Fed stop their bond purchasing programme, Treasury yields may start to increase. In Europe, central banks are becoming increasingly vigilant on inflation due to rising fuel and food prices. In April, the European Central Bank raised policy rate (by 25 basis points to 1.25%) for the first time since May 2009.

GDP Forecast for 2011

2011 GDP Forecast (%)	US	UK	Eurozone	Japan	China	Hong Kong	Philippines	Singapore
Market Consensus	2.7	1.6	1.7	0.0	9.3	5.3	5.1	5.7
AIA	2.9	1.4	1.5	1.0	9	5.2	5.5	5.5

Source: AIA & Consensus Economics

Benchmark Portfolios



Note: Range for equities and bonds is $\pm 10\%$
 Range for money markets instruments & cash is $\pm 5\%$

Key Market Data

Equities	Month-end Level	Monthly Change	YTD Change
S&P 500	1,345	-1.4%	7.0%
Dow Jones	12,570	-1.9%	8.6%
Nasdaq	2,835	-1.3%	6.9%
FTSE 100	5,990	-1.3%	1.5%
DAX	7,294	-2.9%	5.5%
Nikkei 225	9,694	-1.6%	-5.2%
Hang Seng Index	23,684	-0.2%	2.8%
Straits Times	3,160	-0.6%	-0.9%
Taiwan Weighted	8,989	-0.2%	0.2%
KOSPI	2,142	-2.3%	4.5%
Brazil Bovespa	64,620	-2.3%	-6.8%
Russia RTSI	1,889	-6.8%	6.5%
India SENSEX	18,503	-3.3%	-9.8%
China H Index	13,268	0.5%	4.5%
Thailand SET	1,074	-1.8%	4.0%
Malaysia KLCI	1,558	1.5%	2.6%
Philippine PSEI	4,245	-1.7%	1.0%
Jakarta JCI	3,837	0.5%	3.6%

Commodities	Month-end Level	Monthly Change	YTD Change
Gold (comex)	1,535.9	-1.3%	8.1%
WTI crude oil (nymex)	102.7	-9.9%	12.4%

Currencies	Month-end Level	Monthly Change	YTD Change
Euro (EUR-USD)	1.4396	-2.8%	7.6%
JPY (USD-JPY)	81.52	-0.4%	-0.5%

Bonds (10-year yield)	Month-end Yield (%)	Monthly Change (Basis Points)	YTD Change (Basis Points)
US	3.06	-23	-23
UK	3.29	-14	-10
Germany	3.02	-22	6
Japan	1.17	-4	4

As at the end of May 2011
Source: Bloomberg

Disclaimer

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Philam Asset Management, Inc. (PAMI) is an asset management company that manages and distributes nine (9) mutual funds. PAMI is a wholly owned company of Philam Life – the largest and most profitable insurance company in the Philippines and the undisputed market leader for over 60 years, and AIA – the largest pan-Asian life insurance company, with a unique heritage of serving the world's most dynamic region for 90 years. Established in 1992, PAMI is one of the largest fund managers in the Philippine mutual fund industry with more than PhP1Billion in assets under management. It has an experienced team of investment professionals that have specialized skills in portfolio management in major asset classes. PAMI provides unparalleled investment experience in managing client assets and track record in delivering strong returns. PAMI is a multi-awarded fund house that is able to deliver impressive fund performance across all asset classes year after year.

About Philam Life

The Philippine American Life and General Insurance Company (“Philam Life”) is the largest life insurance company in the Philippines and the market leader for 60 years.

Philam Life offers an extensive line of innovative products that provides solutions to various financial needs including income protection, retirement, education, investment, health, personal accident, group life and credit life. With approximately 6,000 agents and over 70 branch offices nationwide, Philam Life has one of the largest distribution networks in the industry. Philam Life is a member of the AIA Group, a leading life insurance organization in Asia Pacific.

About AIA Group

The AIA Group is a leading life insurance organisation in Asia Pacific that traces its roots in the region back more than 90 years. It provides individuals and businesses with products and services for life insurance, retirement planning, accident and health insurance as well as wealth management solutions. Through an extensive network of more than 320,000 agents and approximately 23,500 employees across 15 geographical markets, the AIA Group serves the customers of over 23 million in-force policies in the region.

The AIA Group has branch offices, subsidiaries and affiliates located in jurisdictions including Australia, Brunei, China, Hong Kong, India, Indonesia, Macau, Malaysia, New Zealand, Philippines, Singapore, South Korea, Taiwan, Thailand and Vietnam.

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