Investment Outlook

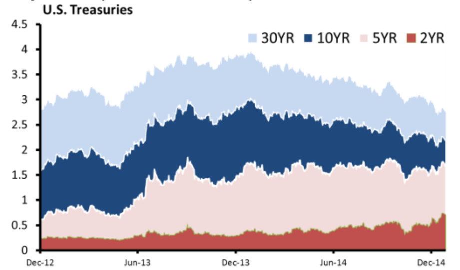
Global economy and markets

Global themes for the first quarter of 2015 should continue to focus on oil prices, monetary policy divergence, and the threat of disinflation. Oil prices have plunged more than 50% from highs reached during the middle of 2014 and is changing the economic landscape. Driven by weak demand and a big increase in supply in the United States and elsewhere, this has boosted consumer purchasing power in oil-consuming countries, suppressed inflation in developed economies, pushed up the value of the US dollar, and weakened several oil-producing countries. Weaker global growth and the outright threat of deflation in the Eurozone are offsetting the positive global impact of a rebound in the US economy. While the Fed is expected to start raising policy rates within the year the European Central Bank (ECB) has just recently announced a 1 trillion Euro expanded asset purchase program, in addition to the on-going mammoth liquidity injection from the Bank of Japan's monetary stimulus. Emerging markets look to have a tough road ahead with the USD expected to continue to outperform and with contagion fears coming to the fore as oil-exporting countries continue their decline and see continued strain on their finances (Latam, Russia).

On the local front, another credit upgrade provided some validation of the country's solid fundamentals and long term growth story. Equity investors remain positive on the stock market given favorable economic data, low inflation and the anticipation of upbeat corporate earnings this year. Local fixed income will also benefit as the global liquidity and low inflation put downward pressure on rates.

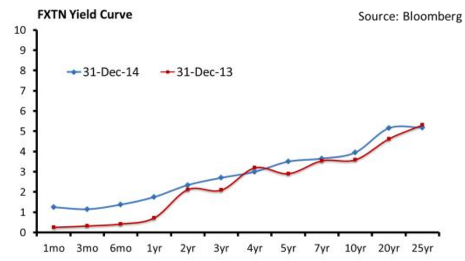
Developed market bonds

Yields on safe-haven assets dropped to their year-lows in the 4th Quarter last year. US Treasuries continue to remain well-bid on relative value as global growth concerns and emerging market contagion fears remain. While the Fed was noticeably less hawkish in its tone regarding its rate guidance rhetoric at the December FOMC meeting, rate hikes are still expected to commence by the second half of the year. We expect rates on safe-haven assets to remain low in the short term, however, as long as there is uncertainty in the timing of the rate hike and volatility is elevated. We expect the 10 year U.S Treasury bond yield to move back above the 2% level as we approach the 2nd quarter of 2015.



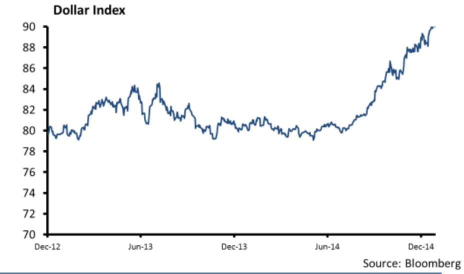
Emerging market bonds

EM economic growth surprised to the downside in 2014 and we expect this trend to continue into 2015 due to the challenging fundamental backdrop: a strong US dollar, depressed commodity prices, geopolitical unrest and sluggish Eurozone growth. However, it is important to note that emerging markets are not a homogeneous group of countries and many EM economies may stand to benefit from the oil price decline through several channels. Those that are net importers of oil and should benefit from lower trade and fiscal imbalances which should in turn boost GDP. That said, in times of uncertainty and volatility, short-term panic and contagion have the potential to trigger broad-based selloffs across emerging markets and risky assets, including currencies.



Philippine bonds

Positive sentiment reigned on the market on back of the country's sound financial health. The sentiment was anchored on the success of its recent USD-denominated issuance, better-than-expected December inflation and the most recent T-bill auction rejection. The country's credit rating was also recently upgraded by Moody's Investors Service more than a year after it achieved minimum investment status, still riding on better state finances, continued prospects for strong economic growth, and resilience to global risks. The Philippines was upgraded from Baa3 grade with a "positive" outlook issued in October last year to Baa2 with a "stable" outlook. With the lowered inflation projections for 2015, we see value on the belly and long-end of the curve and expect local GS to trend lower and continue to track the recent rallies in global bond yields.



Source: Bloomberg

ATR KimEng Asset Management: 17th Floor, Tower One and Exchange Plaza, Ayala Triangle, Ayala Avenue, 1226 Makati City, Philippines
Direct: +632-8481381 | Fax: +632-8410315 | E-mail: ird@atram.com.ph | Website: www.atram.com.ph

Global economy and markets

Currencies

We still see bias for U.S. Dollar strength, particularly given expectations that China, Japan and the Eurozone will continue with its easing measures in 2015. Against the peso, local positives seem to point to strength for the local currency and we expect it to fare better compared to other currencies in the region. It remains below the Php45 level although we expect it to weaken past this support, but not past Php46 to the dollar, the closer we get to the Fed's policy rate lift-off.

Commodities

Oil prices are likely to remain weak in 1Q2015 given the shale oil supply and the prospect of a stronger US dollar and sluggish global growth/expectations. Demand for gold may push prices higher given a flight to safety in a risk-off environment.

Developed market equities

We expect the US economic recovery to continue to gain a more solid footing this year through modest economic growth with tempered inflation. Also, consumer spending is expected to pick-up given lower commodity prices as well as employment and wage growth improvements. Low oil prices are likewise positive for corporate profit margins and earnings growth. Expect US equity markets to benefit from flows from QE measures carried out by the other developed economies. European equities may outperform on the near term given current valuations and as money supply continues to expand in the region, being the direct beneficiary of the ECB's QE program.

Asia (ex-Japan) equities

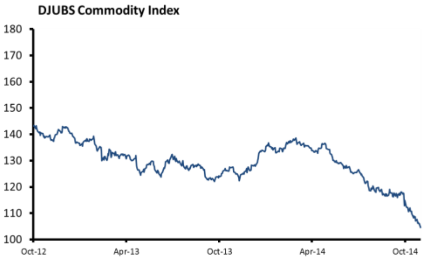
We are positive on Asian equities for 1Q2015 given still attractive regional valuations at 12x 2015 price-to-earnings ratio, with China and India likely to drive growth. India is still in a long-term bull market due to its weight on the information technology sector. On the other hand, we have China's central bank relaxing the amount of reserves commercial banks are required to hold, confirming its easing bias in 2015, and the government's commitment to provide fiscal support and undergo reforms.

Emerging market (non-Asian) equities

On EM equities, a stronger USD remain a risk factor for EM fund flows. Weaker EM currencies however can help the growth of EM exports, while the lower oil price could also be positive for crude importers' economies. Valuations have come down and EM equities looks quite appealing from a long term investment perspective given overall growth in Emerging Market economies is expected to exceed Developed Markets.

Philippine equities

We are neutral on Philippine equities for 1Q of 2015. While the country's macro story remains rock solid, market valuations look a bit stretched. It is currently the most expensive market in the region trading at 18x 2015PE. It may be vulnerable to profit-taking after the 20% return in 2014 given that global growth concerns are increasing. We recognize, however, there are positive upside risks. The Philippines, being a net importer of oil, is expected to be a significant beneficiary especially from the point of view of inflation. Lastly, election spending should start this year for the 2016 presidential elections, which should be felt in the mid half of the year.



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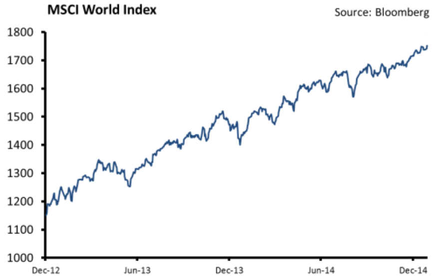

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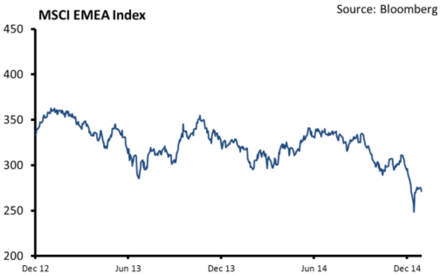

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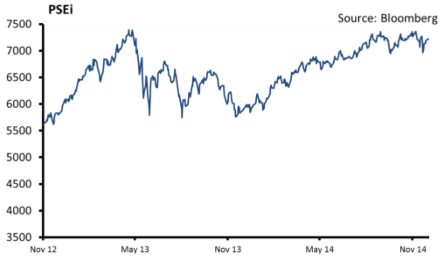

Source: Bloomberg

Index/Currency	Price as of Dec. 31	Percent Change		
		QoQ	YTD	YoY
MSCI World Index	1709.7	0.7%	2.9%	2.9%
MSCI AC Asia ex Japan Index	563.73	-0.2%	2.2%	2.2%
MSCI EMEA Index	270.77	-10.6%	-17.5%	-17.5%
PSEi	7230.6	-0.7%	22.8%	22.8%
USD / PHP	44.72	-0.5%	0.7%	0.7%
USD / JPY	119.78	9.2%	13.7%	13.7%
EUR / USD	1.2098	-4.2%	-12.0%	-12.0%

Source: Bloomberg

Security	Yield as of Dec. 31	Change in Yield (bps)		
		QoQ	YTD	YoY
US Treasuries 2YR	0.66	10	28	28
US Treasuries 5YR	1.65	-10	-9	-9
US Treasuries 10YR	2.17	-32	-86	-86
US Treasuries 30YR	2.75	-44	-122	-122
PHIL. FXTN 2YR	2.75	62	63	63
PHIL. FXTN 5YR	3.33	-67	42	42
PHIL. FXTN 10YR	3.86	-33	26	26
PHIL. FXTN 20YR	4.98	-10	34	34

Source: Bloomberg

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Global Macro Outlook	The global markets will still be tracking signs of economic growth. With the drop in oil prices, easing inflationary pressures and accommodative central bank actions (liquidity injection of ECB and BoJ), global liquidity will help drive the market.

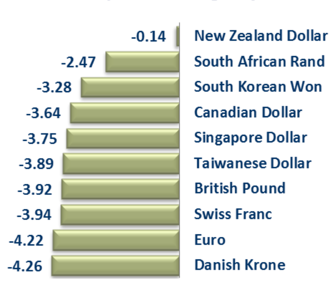
Asset Class	Factors and Drivers	Current View	Prev. View
Fixed Income			
• US Treasuries	Rates remain well-bid on global weakness but ongoing improvement in U.S economy to bring rate hike sometime in 2H15.	=	+
• Asia	A strong macro backdrop, supportive growth prospects and ongoing reform stories in Asia continue to provide opportunities for investors. Credit spreads are relatively tight but seen to hold.	=	-
• Emerging Markets	Most local currency bonds may get hit as USD outperforms. Certain areas at risk of selective defaults (i.e Latam, Russia, etc) so we remain cautious in this space.	-	-
• Philippines	Easing inflation risks seen, bringing yields lower.	=	+
Equity			
• Global	US economic recovery to continue this year. Global QE should be supportive of equity markets. European companies might surprise earnings to the upside as money supply continues to expand in the region	=	=
• Asia	Positive ASEAN countries on improving fiscal policies. Avoid commodities driven economies such as Australia and Malaysia. China to implement their loosening measures should economy show signs of weakness.	=	=
• Emerging Markets	EM likely to exceed DM in terms of economic growth. China and India are likely to be the main drivers of growth this year. Bullish on India's IT sector.	=	=
• Philippines	Fundamental macro story remains rock solid but valuations a bit stretched. Recent rally driven by QE liquidity.	+	=
Currencies			
• USD	Stronger economic figures from the U.S. to cause dollar outperformance against other currencies.	=	+
• PHP	Positive domestic factors could give strengthening bias to the peso but expect it to stay within 44 to 45 for now.	=	=
Commodities	Prices will remain generally lower as global growth concerns continue to affect demand negatively. Oil price decline seen to continue in the medium term on supply glut and OPEC strategy shift to protect market share.	=	-
REITS	Neutral in the medium term due to the delay in US interest rate hike already has fair valuations.	=	+

Legend :

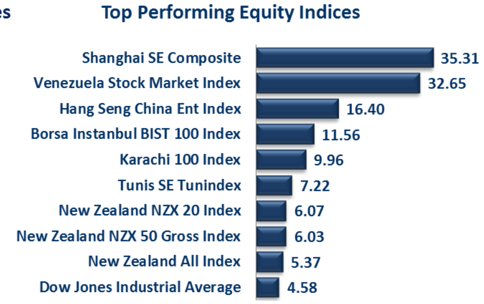
— —	Underweight	—	Slightly underweight	=	Neutral	+	Slightly overweight	++	Overweight

Percentage Gain/Loss in 4Q 2014 (Source: Bloomberg)

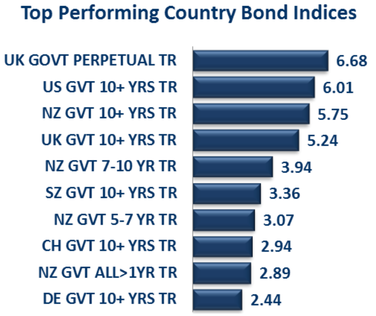
Top Performing Major Currencies



Top Performing Equity Indices



Top Performing Country Bond Indices



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