

ING ORANGE VIEW



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Global Economic Outlook

World

- There is increasing evidence and much hope that the Americas and Europe are set to join an already established Asian economic upturn this quarter. However, high unemployment and tight credit conditions are expected to temper the upturn.
- While investment sentiment has improved, investors by and large have been cautious thereby missing the strong market rally. Cash levels are still high and are being increasingly deployed providing support to asset markets.
- While bond yields have backed up over the last three months, concerns of imminent inflationary pressures are overdone. A high unemployment rate, low capacity utilisation and low velocity of money will keep inflation in check until economic recovery reasserts itself.
- Oil and other commodity prices remain on an uptrend supported by indications of global recovery. But, inventory levels are rising.

United States

- Equity markets are buoyant as expectations grow that the US economy will post sequential growth in the current quarter. Industrial production is also expected to be particularly strong as it recovers from sharp declines in the previous quarters. Accompanying this bounce, the labour market and housing indicators should also show some improvement.
- The 2Q09 corporate earnings will be an important factor in maintaining equity market momentum. American companies have addressed the adverse macro environment by dramatically cutting costs. This means that bottom line will perhaps surprise on the upside despite disappointing top line trend.
- Consumer spending has remained sluggish through June as in the past few months after a strong bounce early in the year, however, both housing starts and building permits have shown a modest improvement.

Europe

- The OECD has cut its outlook for the Euro area, predicting a 4.8% contraction in 2009 to be followed by a gradual recovery in 2010.
- The Euro area Private Mortgage Insurance (PMI) has continued to improve. With the latest reading at 42.6 however industrial orders declined for the ninth month in a row.
- The Bank of England has surprised the market by not extending its quantitative easing programme further this month and has stated that it will review the program in the context of the August Inflation Report.

Japan

- Following LDP's loss of the Tokyo local election, Prime Minister Aso has called a Lower House election for 30 August. There remains a high probability that the LDP could be on the brink of losing control over both houses of the Diet. Such a development will at least break the legislative gridlock but beyond that not much can be foreseen as the opposition DPJ has not published its manifesto.
- Despite unfavourable labour market conditions, consumer sentiment continues to rise reinforcing the message from other indicators such as PMI and new auto sales that consumption is being boosted by several government measures.
- The BoJ has extended its credit easing operations from end-September until year end.

Global Market Insights

Equities

- Fiscal stimulus programmes in play over the last six to nine months are probably at their peak level of efficacy. Accommodative monetary policy over the same time period has also reached its optimal level of effectiveness. Coupled together, this has propped up global demand in the face of global deleveraging and rising household savings. As the impact from these stimulatory policies fade away over the coming months some moderation in the rapid rise in investor sentiment is bound to follow.
- Emerging economies in Asia led by China and India are slowly but surely progressing on their path of incremental decoupling from the G7 economies. Low debt levels in the household, corporate and public sector is the key distinguishing factor between Asia ex Japan and the developed economies. This is also reflected in superior equity market performance.
- The previous six months have confirmed that a major systemic collapse have been averted and by extension that a recovery should emerge in time. Equity prices across regions fully reflect this improvement in economic outlook as valuations are rich. With buoyant investor sentiment and a slowly recovering economy on the one hand and rich valuations on the other, we recommend a neutral weighing in equities.

Bonds

- The outlook for the global economy has brightened in recent months on the back of a massive inventory correction, policy stimulus and easier financial conditions. For now this exerts upward pressure on bond yields, even if the lack of sustainable sources of private sector demand growth make a return to potential growth unlikely over the next year or two.
- With US monetary policy makers already having taken a lot of action, the majority of policy stimulus is likely to come from the fiscal side. We however do not expect any near-term tightening either and expect the Fed to keep interest rates in the 0-0.25% range until Q3'10, and only to modestly increase the policy rate thereafter. We project the ECB to keep the refinance rate at 1% until late 2010, and Japan to keep overnight rates at 0.1% throughout 2009 and 2010.
- After a strong performance of government bonds in recent weeks, the rally is likely to slow, as risk appetite recovers on the back of better than expected Q2 results. We favor European over US bonds.

Returns

- A strong performance from equity markets over the past three months stalled in June as Japan gained, US remained flat and Europe declined.
- Global government bonds started the month poorly with a sharp sell off mid-June before rallying in the 2nd half of the month on the back of weaker risk appetite and green shoot concerns

Equities Benchmark	June	Year-to-Date	12 Months
MSCI World (USD terms)	-0.45%	6.35%	-29.50%
Bond Benchmark	June	Year-to-Date	12 Months
World Govt Bond Index (USD terms, unhedged)	0.11%	-1.50%	4.00%

Source - Bloomberg

Asia Pacific Economic Outlook

Overview

- Despite improvements in activity, exports remain negative on a year on year basis.
- Unemployment rates continue to climb though selective regions witnessing moderation as government stimulus plans take effect.
- In many countries, the resurgence in property transactions and rise in property prices continues unabated.
- The strength in Asian currencies have moderated in the past one month as the US dollar gained strength.

China

- China's PMI stood at 53.2 in June and points to continued expansion.
- Exports decline accelerated to 26.4% in the month of May.
- Domestic consumption remained firm with retail sales growing 15.2% in May.

North Asia

- Hong Kong's unemployment remained steady at 5.3% in May with no month on month worsening.
- Industrial production showed sequential improvement for Korea and gained 1.6% in May over the previous month.
- Taiwan's leading Index is also showing sequential improvement by gaining 3.3% in May.

South Asia

- Furthering its monetary easing efforts, Indonesia's central bank lowered its benchmark rate by 25bps to 6.75%.
- Despite the collapse in both imports and exports, Malaysia nevertheless posted a healthy RM10 billion trade surplus.
- Philippines' Overseas Filipino Workers (OFW) remittance remained robust growing 2.2% in the month of April.
- India's recent budget proved to be disappointing as no substantial new reforms were announced and fiscal deficit is expected to soar to 6.8% in FY10.

Pacific

- Australia's unemployment rose to 5.7% in the month of May inline with expectations.

Asia Pacific Market Insights

Equities

- Economic indicators in Asia ex-Japan has improved as global economic environment is showing signs of stabilisation.
- Fiscal policies have been successful in shoring up domestic demand and has helped cushion the blow from falling exports.
- Very low interest rate environment and better appetite for lending helped to revive property markets around the region with transaction volumes returning to pre-Lehman levels.
- Positive earnings upgrades continues for the region as analysts reassess their bearish estimates amid signs of stabilisation for the global economy.
- Asia Pacific's 2009 estimated PE stands at 15.5X with an estimated earnings growth of -2.6% and 3 months earnings revision of +5.6%.
- The next milestone for the market will be second quarter earnings where it will be likely that investors will focus more on future guidance than current earnings and will set the tone for equity market performance in the third quarter.

Bonds

- Inflation has bottomed in Asia, and is bound to rise to more normal levels on the back of base effects and the YTD rise in commodity prices. A sharp rebound in asset prices is a source of concern in several countries, particularly Korea.
- The monetary easing cycle is over, with only likely occasional rate cut in Indonesia and the Philippines rate hikes within 2009 for the rest of Asia are unlikely. For 2010 we expect Korea and India to be among the first to start tightening policy.
- Macro-indicators across Asia point to a budding economic recovery, but after the impact of fiscal stimulus has worn off and the restocking process is completed, the outlook for domestic and external demand for Asia remains uncertain. This sets the stage for short term upward pressure on bond yields, but a relatively bond friendly environment in the longer term.
- Asian bond yields are well off their mid-June peaks, when fiscal Sustainability concerns, inflation fears, and noise about exit strategies from quant easing had an exaggerated impact on bond markets globally. At current levels we retain a more neutral outlook on Asian bond markets.
- We remain fundamentally bullish on Asian currencies medium term, but see near term risks as risk appetite consolidates.

Returns

- Since bottoming in October 2008, Asia Pacific ex-Japan equities have been outperforming global markets for eight months in a row.
- Asian local currency debt had a relatively poor month, with currencies generally weakening, and yields rising on the back of expected tightening and inflation fears.

Equities Benchmark	June	Year-to-Date	12 Months
MSCI Asia Pacific Ex Japan (USD terms)	0.92%	33.01%	-22.21%
Bond Benchmark	June	Year-to-Date	12 Months
HSBC Asia Local Bond Index (USD terms)	-0.49%	0.26%	2.92%

Source - Bloomberg

Recommended Asset Exposures	
International Equities	Neutral
Asian Equities	Underweight
International Bonds	Overweight
Asian Bonds	Neutral
Cash	Neutral

Indian Economic Outlook

India

- The Index of Industrial Production (IIP), during April 2009, rose 1.4% yoy, above expectations. This compares with March IIP numbers of -0.8% yoy (revised). This increase has come after two consecutive months of negative growth.
- The recent revision by The Indian Meteorological Department (IMD) on their monsoon forecast for June-September season suggests a worrisome situation for the agriculture sector.
- Wholesale Price Index based inflation for the week-ended June 13, 2009 came in at -1.14% yoy, somewhat away from expectations and moving up from -1.61% in the previous week.

Source: www.rbi.gov.in

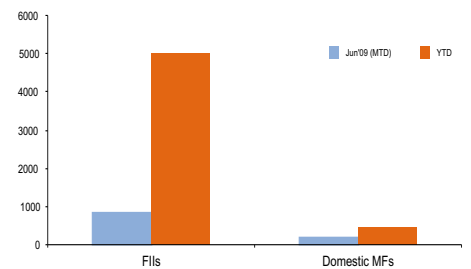
Indian Equity Market Insights

India

- Market took a breather in month of June after a couple of consecutive months of massive gains. Most developed markets ended the month on a flattish note.
- Indian markets also performed in line with global markets and did not register any significant gains. Both the large cap and mid cap indices ended the month at similar levels as May.
- Both FIIs and MFs continued to invest in Indian market. While FIIs invested US\$824m in the equity markets, MFs were net buyer to the tune of US\$186m in June.
- IT and FMCG were the top performing sectors during June registering gains of 9.7% and 7.9% respectively. After a great last month, Realty sector paired some of the gains falling 16%.

Source: ING IM Internal Research Team & www.sebi.gov.in

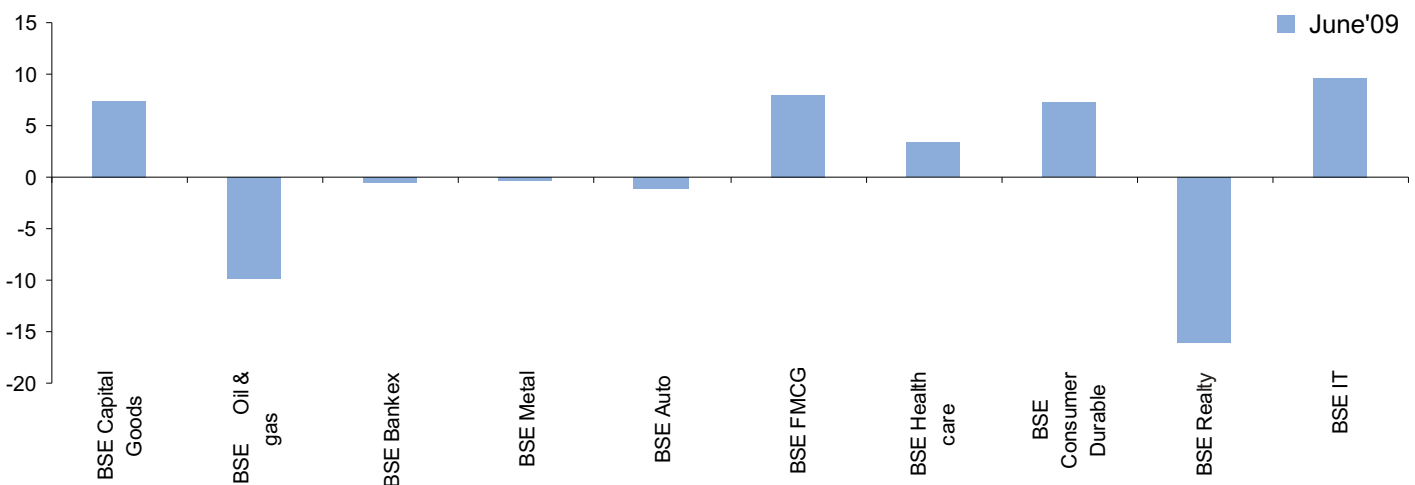
FII and MF Trend (Inflows)



Source: www.sebi.gov.in

Snapshot of Sectoral Trend

% change compared to previous month.



Source - Bloomberg

ING Overview of Sectoral Trend

<p>Industrial Manufacturing and Construction</p> <ul style="list-style-type: none"> After a few consecutive months of negative growth IP numbers turned positive in April registering growth of 1.4%yoy. We expect spending by government to continue, however private sector spending is still under pressure. Valuations have run up significantly and are at a substantial premium to overall market. We maintain a cautious outlook on the sector. 	<p>Information Technology</p> <ul style="list-style-type: none"> In spite of talks of multiple green shoots in the US economy, situation on ground remains tough. While the order cancellations have stopped, demand scenario has not improved significantly. Due to the poor demand, pricing remains under pressure impacting margins. Adverse movement of currency is also impacting the profitability of IT services companies. We continue to maintain a cautious view on IT sector. 	<p>Steel</p> <ul style="list-style-type: none"> Reported world crude steel production for the month of May 2009 was down ~20% YoY (up ~7% MoM) as real demand from capital formation remained weak with no clear visibility of near term revival. Recent steel price increase globally has resulted in some idle capacities to re-start the production. The downside risk to domestic steel prices at this point seems quite limited as (i) Domestic consumption is going strong (ii) Global inventory levels are lower from their peaks (except Europe) (iii) Increasing global prices resulting into lesser "low priced import" threat and (iv) Increasing protectionism worldwide. 	
<p>Media</p> <ul style="list-style-type: none"> In broadcasting space, the fight for top position in the GEC (General Entertainment Channel) space continues with top three channels changing places almost every week. However, ad growth remains poor leading to low overall revenue growth for most companies. While a modest recovery is expected in the current year, things are likely to normalise only by next year. We maintain our cautious view on the sector. 	<p>Telecom</p> <ul style="list-style-type: none"> Month of June saw the launch of Tata Teleservices' GSM services in India, beginning with Chennai and rest of Tamil Nadu, under the brand Tata Docomo. We expect entry of another two players in the next 6 months. We also expect 3G auction to finally see the light of the day in another 2-3 months. We expect the competition in wireless space to intensify with entry of new players and MNP. We maintain our cautious stance on the sector. 	<p>Bank</p> <ul style="list-style-type: none"> Banking sector is expected to report strong earnings growth during the Q1FY10, primarily driven by higher treasury gains (due to higher volatility in G-Secs and strong equity markets). Also, in 1QFY09, several banks had large MTM losses due to hardening of yields and earnings were subdued for several state-owned banks. 	
<p>Pharmaceuticals</p> <ul style="list-style-type: none"> US FDA troubles and concerns have further ballooned for the sector. Most of the top brass including Sun Pharma, Ranbaxy, Lupin and now Cipla too have major to small issues to be sorted with US FDA. Resolving these is the top priority for most as was clearly visible in Ranbaxy Board changes. In the domestic and emerging markets growth continues though somewhat subdued due to restructuring sales forces or cautious approach to avoid riskier sales. Large MTM losses on hedges have been the trouble point for most of the companies in view of rupee depreciation. The earnings estimates for most of the companies in the sector are not prone to recessionary concerns. Overall the outlook and the valuations for the sector seem to be good, with some company specific risks. 	<p>FMCG</p> <ul style="list-style-type: none"> AC Nielsen FMCG retail-sales audit figures for April-May '09 indicate 16.2% YoY growth, lower than 19% YoY growth in FY09. The coming quarters would be quite challenging for the FMCG companies as replicating previous years strong topline performance on a high base and post the price rollbacks would not be easy. We expect incremental growth to be volume driven largely as companies focus on volumes off take and market share in their priority list. Monsoons hold considerable significance for both input costs and rural consumption for the year ahead. 	<p>Cement</p> <ul style="list-style-type: none"> Most cement companies should report strong Q1FY10 earnings reflecting the benefits of recent price hikes and stable costs. However, cement prices should come under pressure from the second half of FY10 due to significant capacity addition over the last 6 months and further forecasted capacity additions in FY10. This should lead to a fall in operating profit margins for cement companies. Moreover, any potential hike in excise duty without a corresponding increase in prices and an increase in costs could lead to a further fall in margins. 	
<p>Auto</p> <ul style="list-style-type: none"> While the first and second quarters of the financial year have historically been the weakest quarters for auto demand, Q1FY10 has seen a sharp improvement in volumes. While volumes for cars and two wheelers initially picked up due to high discounts, new launches and easier availability of finance have sustained the momentum in Q1FY10. Demand for commercial vehicles has improved sequentially (though still down a year-on-year basis) due to the government stimulus packages. Going ahead, as economic activity improves and banks ease lending, auto volumes could continue to show strong growth. 			

Source: ING IM Internal Research Team

Indian Debt Market Overview

- All markets enter in a consolidation phase
- Bond yields across the major markets close flattish after a steep rise earlier in the month
- After front loading of government borrowing, market expects lower size of borrowings going ahead
- Expectation of oil price deregulation will be good news for Bond markets as it signals fiscal discipline from the government
- Rise in US treasury yields at the longer end and better stock market performance, indicates market expectations of faster economic recovery, rising inflationary expectations and a neutral stance on rates by the central banks
- Expectation of oil price deregulation will be good news for Bond markets as it signals fiscal discipline from the government

Macro Economic Matrix

FACTOR	Impact on Debt Market				
	Very Negative	Negative	Neutral	Positive	Very Positive
Economic Growth				✓	
Credit Deposit Trends					✓
Fiscal Situation	✓				
Inflation					✓
Liquidity Situation					✓
External Sector			✓		
Monetary Policy Stance					✓

Source: ING IM Internal Research Team

Our portfolio strategy

- We have increased the duration of the Long term Bond and Gilt funds as we expect rates to come lower going forward on reduced sizes of government auctions and better government revenues on account of Disinvestment proceeds, 3G spectrum auction, better tax revenues as economic growth picks up and lesser amount of subsidies.
- In short term fund we have increased the mark to market component to 35% from 20% last month as we feel Bond yields could ease further due to lack of supply and in tandem with fall in government yields.
- In Liquid funds, we have been maintaining a judicious mix of cash and short term instruments. We expect shorter end of the curve to remain stable and hence would like to remain invested in 1-3 month CDs and good quality corporate CPs.

Going Forward

- Markets are expected to remain volatile with central banks also giving mixed signals as to the monetary policy stance but most of the major central banks have by and large done with their rate cutting spree and are expected to be on wait for few months before taking any decision as to stay put or raise rates.
- Inflation will continue to remain subdued for few months before base effect starts kicking in. CPI numbers however could remain higher.

Key Global Forecasts

	Key Drivers	Key Risks	Risk Rating
World Economy	<ul style="list-style-type: none"> • Deleveraging of consumer, financial and corporate sectors • Continued co-ordinated approach to the financial and economic crises 	<ul style="list-style-type: none"> • Emerging markets decline into recession • Protectionism emerges 	<p>High</p> <p>Low</p>
Global Equities	<ul style="list-style-type: none"> • Prospects for economic growth • Earnings growth and the extent of revisions 	<ul style="list-style-type: none"> • Earnings downgrades surprise on the downside • Availability of credit diminishes 	<p>High</p> <p>Medium</p>
Global Bonds	<ul style="list-style-type: none"> • Accomodative monetary stance • Deficit spending & bond supply • Weak growth, despite recent green shoots • Increased G-20 & IMF support to EM economies 	<ul style="list-style-type: none"> • Return of risk appetite/ demand for risky assets • Inflation worries escalating • Increasing fiscal deficits, rising public debt 	<p>Medium</p> <p>Low</p> <p>Low</p>
Asian Equities	<ul style="list-style-type: none"> • Extent Asia is impacted by the global economic slowdown • International investors appetite for risk 	<ul style="list-style-type: none"> • Earnings revisions surprise to the downside • Valuations fail to halt market slide 	<p>High</p> <p>High</p>
Asian Bonds	<ul style="list-style-type: none"> • Bond supply and deteriorating fiscal dynamics • Accomodative monetary stance • Weak growth, despite recent green shoots • Increased G-20 and IMF support to EM economies 	<ul style="list-style-type: none"> • Increased bond supply • Higher G3 bond yields • Increased inflation (due to higher commodity prices) 	<p>Low</p> <p>Low</p> <p>Low</p>
Indian Equities	<ul style="list-style-type: none"> • Possible divestment, increase in permissible FDI in sectors like insurance, steps towards consolidation of state-owned banks, oil price deregulation, continued infrastructure thrust, etc would be viewed positively. • IMD expects the South-West Monsoon to cover the entire country by the middle of July and the Central Western region within this week. • Excluding metals and real estate, aggregate Sensex earnings are expected to grow by nearly 15% during the 1QFY10. Several sectors are expected to sustain their recovery mode – Autos, Cement, Pharma. Even Metals and Real Estate would show sharp improvement QoQ. 	<ul style="list-style-type: none"> • The government has a big task ahead of it in the form of striking the right balance between growth and fiscal prudence. Current valuations of the markets are factoring multiple expectations from the new government. • In its second-stage forecast, India Meteorological Department (IMD) has reduced its South-West Monsoon rainfall estimate for 2009 to 93% from 96%. • 1QFY10 quarterly earnings season is the key event risk. 	<p>Medium</p> <p>High</p> <p>Low</p>
	Key Drivers	Key Risks	Outlook
Indian Bonds (Gilt outlook)	<ul style="list-style-type: none"> • Soft monetary policy stance • Lower borrowing by the government • Inflation declining/weak economic numbers • Easy liquidity • SLR demand from banks 	<ul style="list-style-type: none"> • Higher supply on account of government bond auctions • Recent rise in commodity prices • Inflationary expectations on better economic numbers 	<p>Positive</p>
	<ul style="list-style-type: none"> • Neutral monetary Policy stance • Inflation declining/weak economic numbers • SLR demand from banks 	<ul style="list-style-type: none"> • Expansionary fiscal policy measures resulting in huge government borrowing • Rebound in economic growth 	<p>Positive</p>
Indian Bonds (Corporate bond outlook)	<ul style="list-style-type: none"> • Attractive spreads • Increase in FII limit • Huge inflows in fixed income funds • Neutral monetary Policy stance • Weak economic growth • Credit spreads at attractive levels 	<ul style="list-style-type: none"> • High supply in terms of refinancing and reissuances by banks and corporates • Credit markets to remain strained • High issuances at the longer end of the curve • Weak corporate earnings • Large investors in fixed income mutual funds can exit in one day notice 	<p>Positive</p> <p>Positive</p>

Source: ING IM Internal Research Team

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