

ING ORANGE VIEW



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YOUR  TO INVESTMENTS

Global Economic Outlook

World

- Industrial production, business confidence and real estate markets continue to show improvements.
- However, unemployment trends continue to worsen in many G7 countries and any turnaround would be protracted.
- Abundant liquidity and refusal of central banks to tighten monetary policy have led to a substantial rise in asset prices.
- With greater risk appetite and abundant liquidity, the US dollar continues to weaken against major currencies and commodities.

United States

- September's ISM non-manufacturing index rose to 50.9, marking the expansion of the service sector for the first time since the bankruptcy of Lehman Brothers.
- The unemployment rate continued to inch up, registering 9.8% in the month of September. The US lost 175,000 jobs in the month of September and while the pace of decline is abating, it will nevertheless be a long time before the unemployment rate reverses.
- The deep freeze of the US housing market continues to thaw with pending home sales increasing 12.1% compared to year ago in August.

Europe

- The ECB kept interest rates unchanged at 1% and there is little expectation of a rate hike in the near future.
- While Euro-zone industrial production improved 0.9% MoM in August, it remains 15.4% lower than previous year's level.
- The Euro-zone unemployment rate stood at 9.6%

Japan

- The Tankan index while still at -33, indicating that manufacturers are less pessimistic relative to June when the index was -48.
- The housing situation in Japan remains difficult as witnessed by the 38.3% fall in housing starts for August. Construction orders also fell 25.2% compared to the previous year.
- The unemployment rate unexpectedly improved to 5.5% in August as the number of employed increased by 290,000 compared to July. The job to applicant ratio also stopped worsening for the first time since January 2008 at 0.42.

Global Market Insights

Equities

- Global equity markets remain buoyant with abundant liquidity helping to push asset values higher.
- Optimism towards third quarter earnings remain high though third quarter earnings have so far provided more positive surprises.
- Unemployment trends remain difficult and we would expect the eventual turnaround in the labour market to be slow and incremental.
- Despite the substantial market rally, Asian and global emerging markets continued to receive substantial fund inflows helped by large size IPOs.
- The substantial outperformance of developing markets vs. developed markets can potentially reverse as economic recoveries in G7 countries continue to gain traction.

Bonds

- Global macro data continues to remain strong. The combination of inventory, fiscal policy and credit/financial conditions has temporarily boosted growth momentum significantly from Q2'09 onwards. However, the more than expected rise in the US unemployment rate in September serves as a reminder of the distinct possibility of another jobless recovery in the US.
- Underlying disinflation trends are still present and expected to persist. However, this may only come to the forefront again in 2010. We expect the Fed to keep interest rates in the 0-0.25% range until Q3'10 and to modestly increase them thereafter.
- Asset markets are being driven by the "liquidity-trade", as ample central bank liquidity and cash positions available in money market funds has started to flow into all asset classes that provide a yield that is in excess of cash.
- A sharp sell off in bond markets is unlikely. Beyond the sharp stimulus and inventory driven rebound, we expect bonds to perform relatively well as financial markets transition into a slower, broader recovery, where demand-pull inflation is not a near-term problem.

Returns

- Equity markets continued to climb in September, as abundant liquidity and optimism towards third quarter earnings kept equity prices well bid.
- Global government bonds had another good month on the back of a sharply weaker USD, and also somewhat lower yields, in spite of an improved macro backdrop.

Equities Benchmark	September	Year-to-Date	12 Months
MSCI World (USD terms)	3.99%	24.90%	-2.29%
Bond Benchmark	September	Year-to-Date	12 Months
World Govt Bond Index (USD terms, unhedged)	2.29%	4.57%	13.78%

Source - Bloomberg

Asia Pacific Economic Outlook

Overview

- Second quarter GDP growth rates were generally better than expectation across the region.
- The absolute level and rate of increase in unemployment is also much lower than beginning of the year forecasts.
- Second quarter earnings surprised positively with aggressive cost cutting helping to sustain profitability.
- Potential policy tightening by the Chinese government appears to be the key concern among investors with the local A share market particularly vulnerable to rumours regarding policy.

China

- China's Private Mortgage Insurance (PMI) stood at 54 in August, retaining the path of expansion.
- Industrial production was up 10.8% in July bringing the year-to-date total to up 7.5%.
- As evidence of domestic consumption strength, retail sales grew 15.2% in July.

North Asia

- Hong Kong's second quarter GDP improved on a sequential basis up 3.3% QoQ and down 3.8% YoY.
- Korea's unemployment rate improved to 3.8% in July from the 4% reached in June.
- While second quarter GDP growth fell 7.5% YoY in Taiwan, it was nonetheless an improvement over the 10.2% fall witnessed in the first quarter.

South Asia

- Second quarter GDP grew a respectable 2.3% QoQ in Indonesia, registering a 4% growth YoY.
- Malaysia's economy remained sluggish with industrial production dropping 9.6% in June. However, Singapore saw a substantial rebound in industrial production, jumping 12.4% YoY.
- Philippines' OFW remittance remained robust, growing 3.3% in the month of June.
- India's total rainfall this monsoon season was 22.7% below normal, pointing towards a drop in farming incomes for the year.

Pacific

- Australia's private sector credit grew a mere 3% in the month of July, indicating the cautious stance of both private borrowers and bank lenders.

Asia Pacific Market Insights

Equities

- While it is now market consensus that the global economy is on the mend, the key concern for investors is potential policy tightening by China.
- Nevertheless, second quarter earnings showed higher than expected profitability due to aggressive cost cutting and the generally more positive business outlook.
- Earnings revisions maintained an upward bias with analysts factoring in a better economic environment for the remainder of 2009 and 2010.
- Second quarter GDP growth data showed sequential improvements in Asian economies, with the rate of unemployment increase slowing.
- Asia Pacific's 2009 estimated PE stands at 17.9X with an estimated earnings growth of +9.4% and three months earnings revision of +10.8%.
- While markets continue to move higher, any renewed fears over China policy tightening could have a negative effect on markets. Liquidity continues to triumph over fundamentals currently.

Bonds

- In contrast to the benign outlook for G3 bonds, the significantly higher resilience shown by Asian economies is likely to result in an earlier withdrawal of the accommodative monetary stance in the region.
- Headline inflation will continue to drift higher in Asia, fuelled initially by supply side factors and low base effects, and is likely to force liquidity sterilization measures in some of the Asian economies, although diminished supply concerns and ample liquidity are likely to provide some comfort to local bonds.
- We expect the amount of rate hikes to be modest, and believe the degree of tightening priced into most yield curves is exaggerated as the longer term growth outlook, and final demand from the developed world remains uncertain.
- While we are cautious in our outlook on bond markets, we remain fundamentally bullish on Asian currencies medium term and expect a majority of returns to be driven by currency strength.

Returns

- Asian markets resumed their uptrend with another very strong month in September. Asian assets continue to garner interest in light of faster economic growth and weak USD.
- Asian local currency bonds had a strong month, with bulk of the gains coming from Asian FX appreciation

Equities Benchmark	September	Year-to-Date	12 Months
MSCI Asia Pacific Ex Japan (USD terms)	8.84%	61.44%	26.74%

Bond Benchmark	September	Year-to-Date	12 Months
HSBC Asia Local Bond Index (USD terms)	3.04%	4.41%	9.62%

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

Indian Economic Outlook

- Monsoon season ends with a 23% deficit. North India (-35.8% of Normal rains) and East India (-23.6% of Normal) were impacted the most by poor monsoon.
- India's balance of payments (BoP) recorded a thin surplus (USD 0.1 bn) in Q1FY10 for the second consecutive quarter after the shock of deficits in Q2 and Q3 of FY09. India's trade deficit for August settled at USD 8.4 bn, higher than the average USD 6 bn for June and July.
- The Index of Industrial Production (IIP), for July 2009, rose 6.8% yoy, up from 6.4% a year back. For June, IIP growth was revised up to 8.2% from 7.8%.
- For the week ending 19 Sep, headline inflation stood at 0.83%. Inflation for the week ending 25 Jul was revised to -0.71% (from -1.58%). All major constituents of the WPI index – primary, fuel and manufacturing products – registered a w-o-w rise.

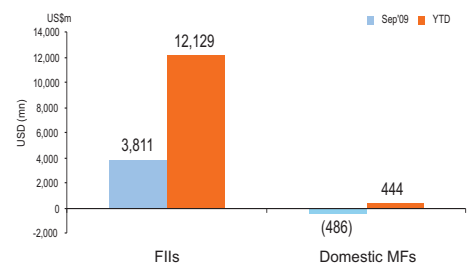
Source: www.rbi.gov.in

Indian Equity Market Insights

- The uptrend in equity markets continued and most developed and emerging market indices ended the month in positive.
- Indian market was one of the best performing market during last month outperforming most developed country Indices with both large cap and mid cap indices registering a gain of 9.3% and 9.7%, respectively.
- September saw significant inflows from FIIs into Indian markets. FIIs invested US\$3.8bn during the month taking the total inflow for the year to ~12bn. Domestic MFs turned cautious, selling US\$486m worth of equities.
- Bankex and Metals were the top performing sectors with gains of 18.1% and 14.5% respectively. FMCG and realty sectors fared poorly registering gains of 0.9% and 2.2%, respectively.

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

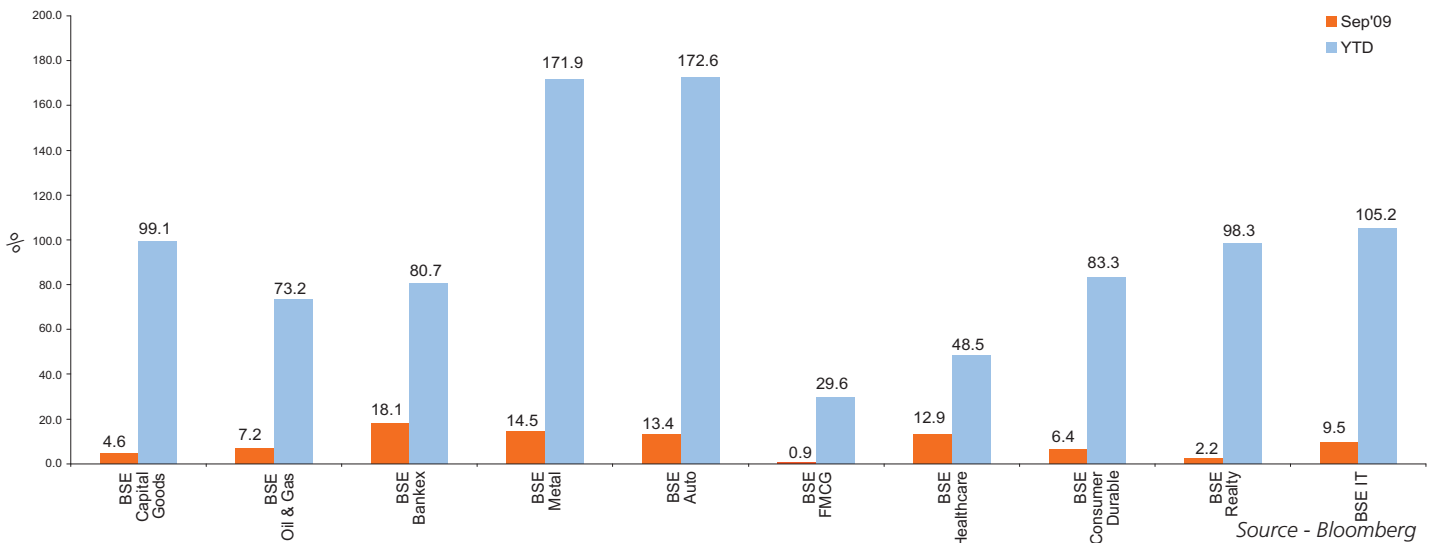
FII and MF Trend



Source: www.sebi.gov.in

Snapshot of Sectoral Trend

% change compared to previous month.



Source - Bloomberg

ING Overview of Sectoral Trend

Industrial Manufacturing and Construction

- Like other sectors, signs of recovery are visible in industrial manufacturing as well. However, pricing environment remains tough and continues to be a challenge for all players. Significantly lower private spending compared to last couple of years is also hurting the sector. We continue to remain cautious on the sector.

Information Technology

- We are seeing some signs of recovery in IT spending with announcement of new deals by various players. However, growth rates are unlikely to return to pre 2007 levels anytime soon. Valuations in the large cap space has moved up sharply and discounts a very sharp growth in earnings in the next couple of years. Mid cap space has also moved up but still provide some opportunities. We are cautious on the sector.

Steel

- Global steel production continues with improvement in production numbers as it de-grew by -5% yoy for the month of Aug'09 as against a de-growth of -18% yoy for the aggregate of first eight months of 2009. Globally, re-stocking phenomenon over next few months should support the prevailing steel price levels. Concerns over the sustainability of demand and prices post re-stocking remains unsettled. Data points coming out of China regarding production, consumption, and exports are the key indicators to watch for and would be instrumental in the sustainability of the production momentum.

Media

- With visible signs of improvement in Indian economy, ad growth outlook has improved significantly. However, after another good month in the market, valuations are stretched both in print and broadcasting space. We have turned cautious on the sector.

Telecom

- Month of September saw the competition in telecom space intensifying even further with Tata DOCOMO's per second billing plan. Tata DOCOMO added more than 3m subscribers on its network on the back of its new plan prompting other players to react with lower tariff plans. We remain negative on the sector due to intensifying competition in the wireless space.

Auto

- The months of August and September witnessed strong growth in two wheelers and passenger car sales on the back of a strong recovery in demand. Growth in the two wheeler segment was partly driven by inventory build up ahead of the festival seasons. Growth in the passenger car segment was led by strong growth in the compact car segment. Commercial vehicles have also begun registering Y-o-Y growth as demand for goods carriers increases. This trend is expected to get stronger during the second half of FY10 on the back of stronger industrial production and changes in emission norms.

FMCG

- The consumer goods space is lately witnessing some aggressive marketing and strategic action as a part of companies' efforts to boost sales. The main challenge for the industry in this price competitive scenario will be to maintain the overall value growth as all companies compete for a larger pie of the market share. Product introduction by way of new launches or innovations and inorganic growth are crucial for growth in the forthcoming quarters.

Cement

- Year on year growth in cement dispatch numbers was strong in the month of August due to strong demand from infrastructure sector and low base effect. The weak monsoons in the early part of August led to relatively little construction activity being disrupted whereas the sales of August 2008 were impacted by a normal monsoon leading to a lower base. The base for cement demand remained weak in September and October 2008 as well, which will lead to a strong demand on a Y-o-Y basis for the next couple of months. This will lead to stronger Y-o-Y Q2 results due to stronger volumes and relatively higher prices. However the longer term impact of a weak monsoon coupled with significant capacity additions should lead to lower prices and profitability from the second half of FY10.

Bank

- Rising inflationary expectations, RBI's intention to undo monetary accommodation and potential bond-selling to fund credit in the coming quarters, point towards a reversal of interest rate cycle. Any increase in the held-to-maturity limit can only provide temporary relief. Banks with poor franchise quality could witness margin pressure while asset quality concerns continues. 2QFY10 results for the banking sector are expected to be driven by higher treasury gains and low provisions.

Source: ING IM Internal Research Team

Indian Debt Market Overview

Market Impact

- Government securities market saw softening of rates as the H1 borrowing calendar came to an end and the second half borrowing calendar was expected to be lighter. At the same time, statements from Reserve Bank officials stating that they were examining the limit on HTM portfolio of the banks came as a positive surprise. Further, RBI along with many other central banks of the world stated that it was too early to exit from stimulus as rebound in growth was still in its initial stages, which added to the positive sentiment and as a result 10 yr benchmark index saw a low of 7.05% during the month. However, rates hardened a bit by the end of the month as the borrowing calendar for second half of FY10 was worse than expectation since the borrowing is front loaded with entire borrowing being completed by first week of February 2010. At the same time, there was no announcement on relaxing of the HTM limit till end of the month. As a result, the 10 yr G-sec rate ended at 7.20% at the end of September 2009 after seeing a low of 7.05% during the month.
- Going forward we expect markets to remain volatile within a 15-20 bps range with a possibility of rates moving higher in the next 4-6 weeks as inflation is expected to rise sharply by then with base effect kicking in. Also, the industrial production numbers are expected to post good performance during the next 2-3 months. However, if there is any substantial (higher than expected) relaxation in the limit for HTM portfolio of banks, we could see a positive impact on the rates.
- Yield on the 10 year benchmark G-sec softened up from 7.44% at the end of August 2009 to 7.20% at the end of September 2009. Yield on the 5 yr benchmark security fell, however to a lower extent than 10 year benchmark, from 7.17% at the end of August 2009 to 7.07% at the end of September 2009.
- Corporate yields softened marginally along with fall in rate of the G-Sec market. 10yr corporate bond yield fell from 8.86% to 8.80%, while 5 year bond yield reduced from 8.50% to 8.44%.
- Short end of the corporate bond curve i.e. 18-24 months papers softened the most, with 2 year bond yields falling from 7.05% to 6.70% and 18 months yield falling from 6.70% to 6.15% during the month of September. This was due to reduced fear of RBI taking any steps to unwind stimulus by either reducing liquidity in the system of increasing interest rates. However, going forward, as inflation is expected to increase rapidly, this segment is expected to underperform as the fears of RBI taking any unwinding steps would return, in short to medium term.
- INR Swap curve has hardened with 5 year swap moving up from 6.38% to 6.60%. 2 year swap rates moved up on inflation concerns from 5.26% at end of August 2009 to 5.49% at the end of September 2009. 5 year G Sec - Swap spread reduced from 79 bps to 50 bps during the month as Swap moved up and G-sec yields softened.

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

Going Forward

- Markets are expected to remain volatile as inflation numbers will start inching up towards positive numbers territory and market builds in expectation of a possible reduction in liquidity through an increase in CRR or supply of MSS bonds.
- The corporate bond curve is expected to flatten further, with the short end of the corporate curve expected to underperform the longer end as any form of reversal would impact the shorter term yields more.

Our Portfolio Strategy

Recap - August 2009

1. We increased the duration of the Long term Bond and Gilt funds as we expected a pull back in the rates due to completion of the borrowing calendar for the first half of the fiscal year and the lower supply of G-sec in the second half.
2. In short term fund we have maintained mark to market component at around 30% and increased accrual assets to around 30% of the fund, which would help in getting better carry with minimal impact of any increase in interest rates.
3. In Liquid fund, we have been maintaining a judicious mix of cash and very short term instruments. We expect rates of 1-3 months CDs and CPs to remain stable and hence would like to remain invested in upto 3 months CD's and good quality corporate CP's.

Strategy going forward

1. In the long bond funds and the Gilt fund, we would look to actively manage duration to take advantage of any mispricing or spread widening / contraction. As the market is expected to remain range bound, we would look to increase duration when rates are attractive and reduce duration at lower rates after booking some profits.
2. In the Short Term fund we would continue to have a mix of accrual assets and mark to market assets to get a decent accrual income with minimum impact of any increase in interest rates.
3. In Liquid fund, we have been maintaining a judicious mix of cash and very short term instruments. We expect rates of 1-3 months CDs and CPs to remain stable and hence would like to remain invested in upto 3 months CD's and good quality corporate CP's.

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 revision 	<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"> • Accommodative monetary stance • Deficit spending & bond supply • Muted core inflation and weak consumer demand • 	<ul style="list-style-type: none"> • Return of risk appetite/ demand for risky assets • Exit of accommodative monetary policies • Inflation worries escalating • Increasing fiscal deficits, rising public debt 	<p>Medium</p> <p>Low</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 fiscal stance • Excess liquidity • Extent of growth rebound 	<ul style="list-style-type: none"> • Higher G3 bond yields • Increased inflation and higher commodity prices • Premature and excessive monetary policy tightening 	<p>Low</p> <p>Medium</p> <p>Low</p>
Indian Equity	<ul style="list-style-type: none"> • Gradual decline in share of monsoon crop, 50% increase in key crop prices in last 4-5 years and the fact that 34% of agri GDP comes from non farm incomes would limit the impact on agri GDP growth. • There is expectation that loan demand will accelerate in second half of the year as industrial activity has picked-up in recent months. • Earnings are likely to be upgrades post the September quarter results which are expected to be strong (as reflected in the advance tax numbers released by leading companies) 	<ul style="list-style-type: none"> • India is facing drought with cumulative rainfall on an all-India area weighted basis being 25% below normal, making the current monsoon season potentially one of the worst since 1973. • Credit growth remains weak (YTD loan growth is 2%, compared to 5.7% at this point in FY09 and 2.8% in FY08). • Earnings upgrades for FY2010E and FY2011E have so far lagged the strong ascent of the market and stock prices. 	<p>Medium</p> <p>Medium</p> <p>Low</p>
	Key Drivers	Key Risk	Outlook
GILT OUTLOOK MATRIX			
Short Term	<ul style="list-style-type: none"> • Possibility of hike in HTM limit of Banks by RBI • Easy liquidity 	<ul style="list-style-type: none"> • Possible reversal in accommodative monetary stance • Increasing inflation due to higher food prices • Better economic numbers 	Neutral
Long Term	<ul style="list-style-type: none"> • Rise in central bank policy rates 	<ul style="list-style-type: none"> • A possible "U" shaped recovery scenario for the world economy 	Negative
CORPORATE BOND OUTLOOK MATRIX			
Short Term	<ul style="list-style-type: none"> • Stability in the underlying G-sec base curve • Easy liquidity 	<ul style="list-style-type: none"> • High supply in terms of refinancing and reissuances by banks and corporates. 	Neutral
Long Term	<ul style="list-style-type: none"> • Rise in central bank policy rates • Large investors in fixed income mutual funds can exit in one day notice 	<ul style="list-style-type: none"> • Lower pick up in credit growth • A possible "U" shaped recovery scenario for the world economy 	Negative

Source: ING IM Internal Research Team

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As on 27.10.2009

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