

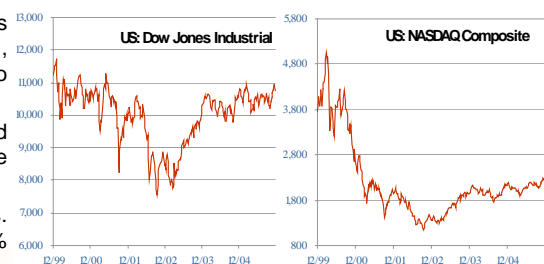
# PRU MONTHLY INVESTMENT BRIEFING

December 2005

October's global inflation scare has run its course such that the US Federal Reserve Board may slow the pace of its interest rate rises. With the prominent exception of the UK, optimism about 2006 economic growth has strengthened. Oil prices of up to \$70pb seem well discounted. All factors bode well for Asian equities. The mining and commodities sectors remain in the ascendancy as China's economy booms. Neglected sectors, such as retailing, media and telecoms, remain in the doldrums; among the laggards, only the technology sector shows any real signs of life. Most key drivers pushing share prices higher, remain in place - abundant liquidity, a healthy corporate sector and undemanding valuation. Europe, Asia, emerging markets and Japan are the most favoured.

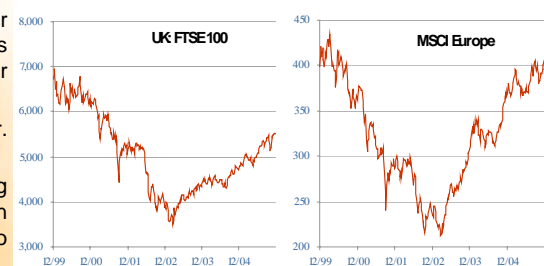
## United States

- The economic impact of Hurricane Katrina and surging fuel prices was remarkably short-lived. With fuel prices easing, inflation has started to fall, such that the Fed is nudging its way to slower rate rises encouraged, no doubt, by the again rising household debt servicing burden.
- Third quarter company profits were generally healthy. Share buybacks and dividend growth lent support. Valuations have fallen to levels where selective value is apparent.
- Investor sentiment recovered well from October's inflation-based concerns. The 2006 IBES consensus P/E ratio of 13.9 (based on projected 11% earnings growth) is no longer so far out of line with international comparisons.
- Our view remains broadly unchanged; the market contains plenty of dynamic and interesting companies, but great selectivity and careful research is required.



## Europe

- The sharp recovery from the brief October setback boosted investor confidence and confirmed the market's strong upward momentum. Exports continue to prosper helped by the 13% decline in the euro against the dollar so far this year.
- The real driver for European shares is the buoyancy of the corporate sector. The recent surge in takeover activity has been especially influential.
- With valuation still low and the momentum of corporate change remaining powerful, we see further upside potential. Restructuring plays, western European companies with high emerging European exposure are likely to generate the best returns.
- Stock-picking remains a key skill, especially for small and medium-sized companies. Although less obviously undervalued than in the recent past, lack of research coverage is still likely to reveal exciting opportunities.



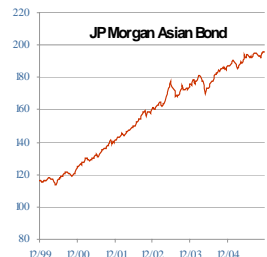
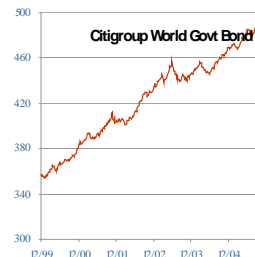
## Japan

- Optimism about Japan's economic prospects and outlook is becoming widespread. The fundamentals look promising. Economic data continue to point to a sustainable economic recovery, sufficient to bring an end to deflation.
- Growth is becoming more broadly based, with stronger domestic demand making a contribution, alongside exports. Corporate profits are forecast to rise by 8% in 2006.
- There are potential risks, not least the possibility of interest rate rises. The overwhelming impact of the overseas investors since the market lowest point in April 2003 might be a source of weakness if high expectations are not met.
- Such is the strength of economic and corporate changes that a major market reverse appears unlikely, confirming the case for staying fully invested. Indeed, those who have missed out on the rising Japanese equity market might welcome any setback.



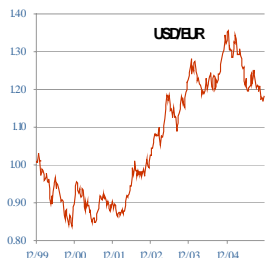
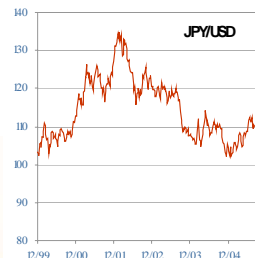
**Bonds**

- Optimism about the outlook for the world economy in 2006 is providing leading central banks with the opportunity to move away from their easy monetary policies.
- Headline inflation remains above target, boosted by declining oil prices. There has been considerable divergence in government bond markets, but little recent change in corporate bond yield spreads, nor any significant increase in issuance.
- The outlook depends on continued benign inflation/interest rates which has driven down yields to historically low levels. Inflation should moderate further, provided that there is no fresh spike in oil prices, nor any secondary inflation pressures.
- In the bond space, we continue to favour government bonds in the UK and in Europe, especially 10-15 year maturities. Among corporate bonds, we like top quality issues (A-AAA credits), although we now believe some high yield issues offer good value.



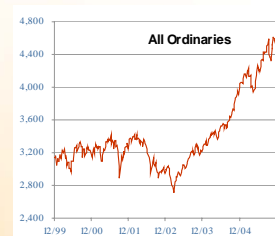
**Currency**

- The US dollar strengthened against the yen despite growing indications the Japanese economy is experiencing a sustainable recovery, and despite persistent trade and current account deficits in the US.
- The yen has suffered from a dispute between the Bank of Japan and the ruling Liberal Democratic Party over the future of monetary policy. Prudential believes the dollar has benefited from the interest rate premium offered by the US over Japan.
- The dollar has strengthened most of this year as the US's economic recovery gained traction. We look at the inflation-adjusted trade-weighted yen index to gauge value. This index has declined steadily since 2001, indicating the yen remains competitive.



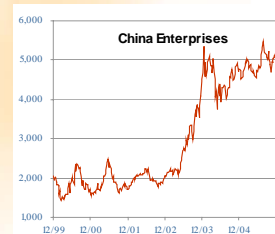
**Australia**

- The All Ordinaries Index rose 5% in November. The best performing sectors were healthcare and utilities; the worst was telecoms. Unemployment was 5.2% in October 2005 compared to 5.1% in September. The trade deficit was AUD1.6bn in September 2005, compared to AUD1.5bn in August. Retail sales fell 0.3% yoy in September.
- It appears that the obvious and correlated imbalances in the economy have now subsided; high consumer spending, rising house prices, high mortgage growth. To the extent that commodity strength remains resilient, the economy could see a soft landing, albeit with sustained low housing price inflation and a subdued consumer.
- We continue to see several sectors as stretched on valuation with the market over-paying for perceived growth. This is creating opportunities as investors overlook lower growth opportunities with strong valuation support.



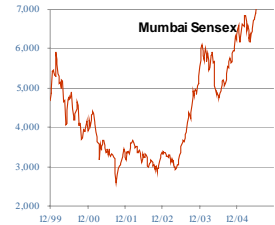
**China / Hong Kong**

- Hong Kong gained - the Hang Seng Index was up 7% - as a recent US Federal Reserve meeting suggested a possible peaking of interest rate hikes in the near future. Interest rate sensitive sectors such as property and banks outperformed. The long-awaited Link REIT made its debut with the stock up 15% on the first day of trading.
- China also rebounded after the recent sharp correction with the Hang Seng China Enterprise Index up 8%. Insurance and telecom stocks outperformed while basic material like steel and coal underperformed. Macro data points towards a robust economy. Industrial production reached a record high in October, led by autos and steel.
- Hong Kong continues to look expensive relative to the region; we see value in banks and property investors, however. In China, value is emerging; we prefer infrastructure plays such as ports and power companies.



**India**

- November was a robust month - the Mumbai SENSEX Index jumped nearly 17%, rebounding strongly from October's fall. Post the recent rally, careful stock picking is crucial to generating profits over the medium term.
- Foreign institutional investors (FIIs) turned net buyers of US\$915m (until November 29, compared with net sales of US\$841m in October), while domestic mutual funds continued buying stocks worth US\$120m (versus \$614m in October). Year-to-date, FIIs have a net investment of \$8.8bn, while domestic institutions have invested \$3.3bn.
- GDP growth for the quarter ended September 2005 was stronger than expected, at 8% yoy, just slightly lower than the June quarter's 8.1%. The principal reason was the continued acceleration in the services sector's growth to 10.1% compared with 9.8% in the previous quarter.



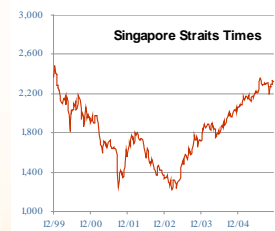
**Korea**

- The KOSPI gained 15% - which more than offset last month's decline. A key driving force behind the rally continued to be strong local fund inflows which topped U\$1bn during the month.
- Macro-economic data was a little mixed, however. October's industrial production data came in better-than-expected rising 8% yoy although the gain was not broad-based but skewed heavily to semiconductor and handset sectors. Excluding them would result in flat year-on-year growth.
- 3Q05 results were mixed. Exporters continued to experience sharp yoy decline in earnings due to the strong won and high raw material costs. On the other hand, financials such as banking and brokerage surprised on the upside on the back of lower provisioning charges and strong brokerage commission.



**South East Asia**

- Singapore's Straits Times Index rose 6%, as 3Q05 GDP growth was revised up to 7% yoy from an earlier estimate of 6.0%. The government has thus revised its 2005 economic growth forecast to 5% from 3.5%-4.5% previously. Forward looking indicators support the government's expectations that growth should moderate to 3%-5% in 2006.
- Malaysia's KLCI fell 2%, lagging the region on the back of inflation concerns. Stronger economic growth, rising inflation and accelerating capital outflow prompted Bank Negara to raise the benchmark overnight policy rate by 30bp to 3%, the first time in seven years. Inflation is likely to remain above 3% until the first quarter of 2006.
- Thailand also underperformed, with the SET Index down 3%. Nevertheless, it is one of Prudential's favoured markets given strong valuation and dividend yield support. Concerns like the unwinding of petrol subsidies, oil price delta, risk of increased interest rates, bird flu etc have become more subdued recently.



**Taiwan**

- Taiwan was another strong performer, with the Taiwan Weighted Index up over 10%, underpinned by tech stocks given the improved outlook for tech exports ahead of the year-end holiday season sales.
- September's exports and industrial production growth, at 22% and 6.3% yoy, respectively beat expectations. This suggests demand in tech and China remain robust and the export growth recovery should continue near term.
- The market was also buoyed by the opposition Kuomintang (KMT) party's expected victory in December's local elections, which could provide a stronger foundation for improved cross-strait relationships with China. The elections have been largely viewed as a mid-term assessment of the pro-independence government.



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