

**BRAZIL
RUSSIA
INDIA
CHINA**

BRIC INVESTMENT REPORT

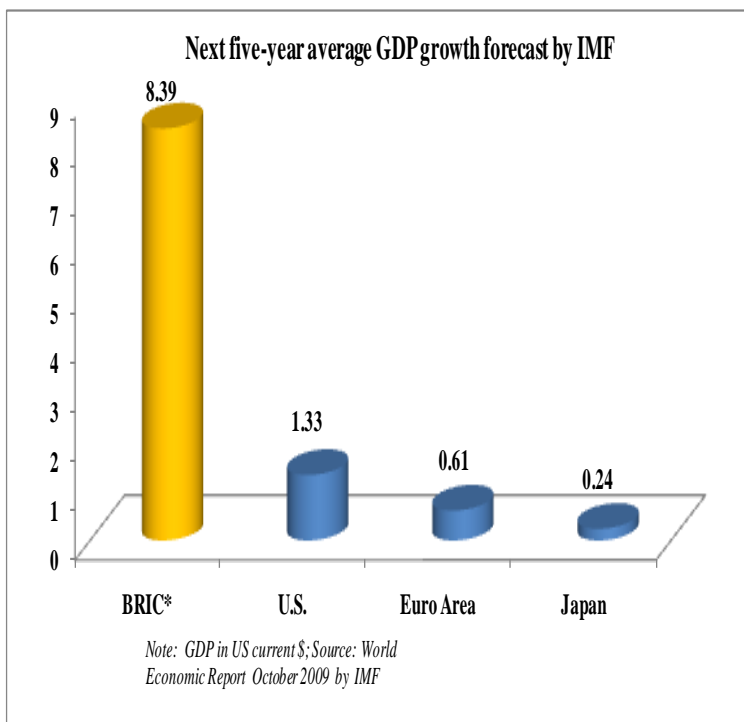
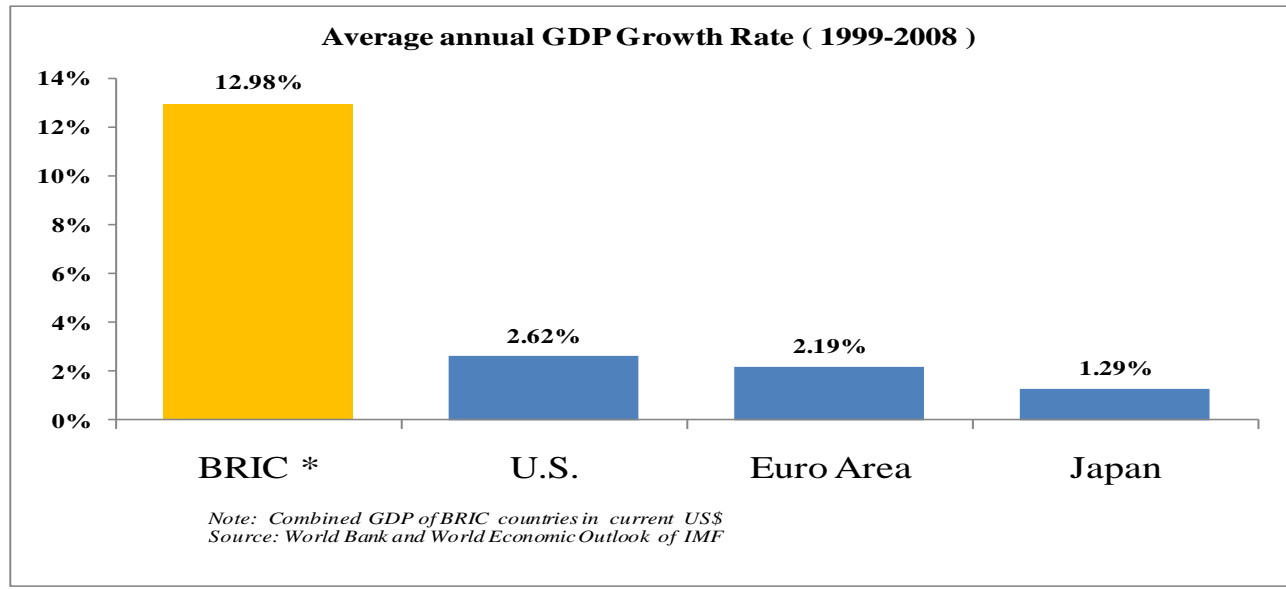


BOE RESEARCH PRIVATE LTD.

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BRIC REPORT OVERVIEW

Why BRIC: The world economic landscape has changed significantly with the growing influence of emerging economies. Among the emerging economies, BRIC countries - Brazil, Russia, India and China – play a major role in the current global economic order. BRIC economies are the fastest growing economies in the world. There are opportunities for high growth over the long-term in BRIC countries. The long-term growth outlook, unique resources and positive economic trends (*discussed later in the report*) have made these markets attractive for global investors. BRIC as an asset class has gained popularity in global wealth management.

Collectively, it is estimated that, these countries account for 41.8% of the world population (*as of December 31, 2008*). Contribution of Gross Domestic Product (GDP) of these countries to the world GDP is increasing at a faster rate.

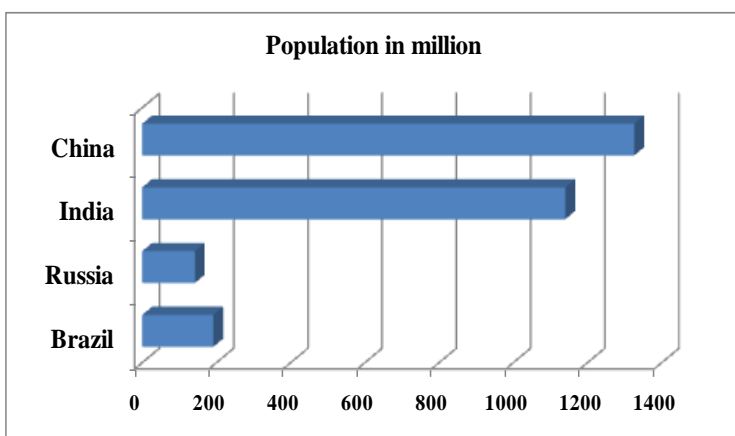
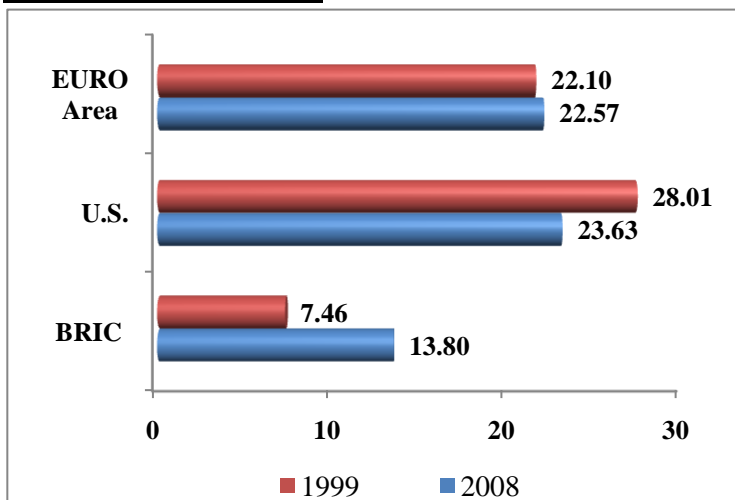
In 1999, the share of combined BRIC GDP to the world GDP was 7.5%, which rose to 13.8% in 2008. Over the past 10 years, the combined average GDP growth rate of BRIC countries has outpaced the advanced countries including the U.S. and the Euro nations.

Quick Fundamentals (Combined BRIC Economies)

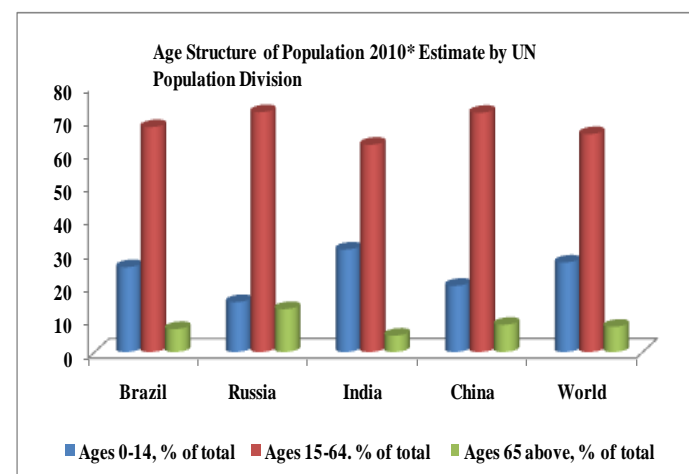
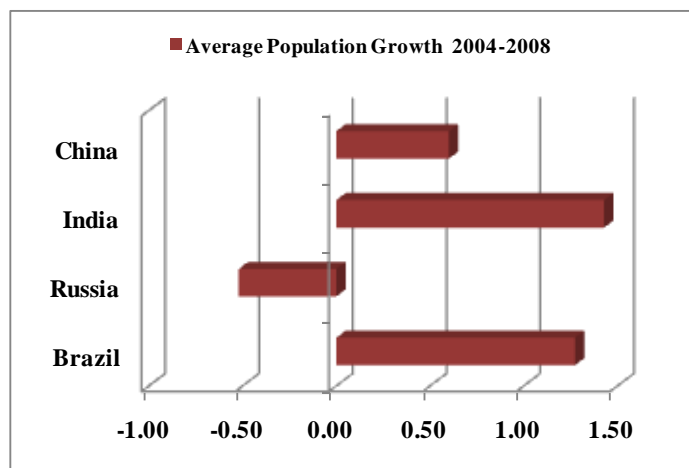
Total GDP Size (US \$ Trillion)	8.29
% of World GDP	13.8%
Total Population (Billion)	2.79
% of World Population	41.8%
Total Surface Area (Mill Sq. Km)	38.49
% of World Surface Area	28.1%
% of World Trade	14.1%
Total FDI Inflows (US \$ Billion)	265.24
% of World FDI Flows	15.6%

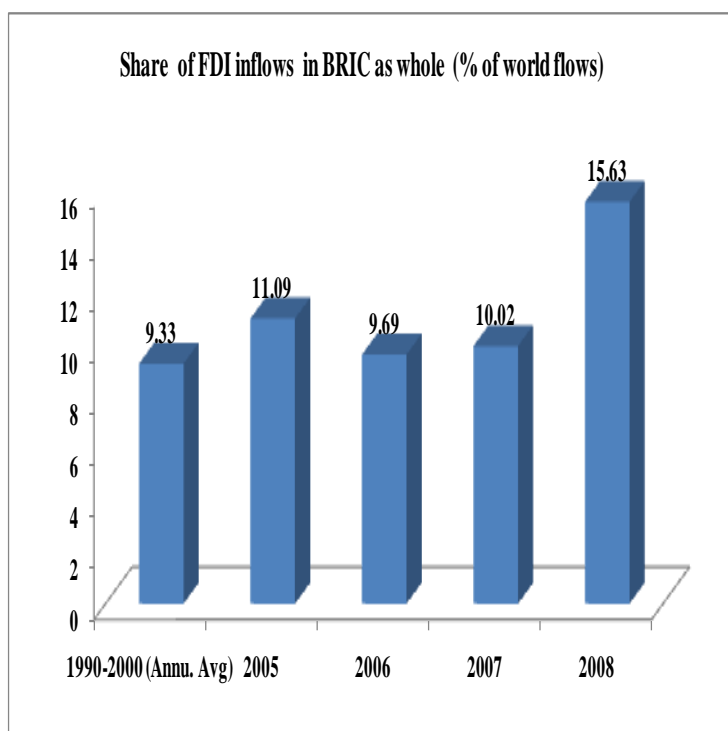
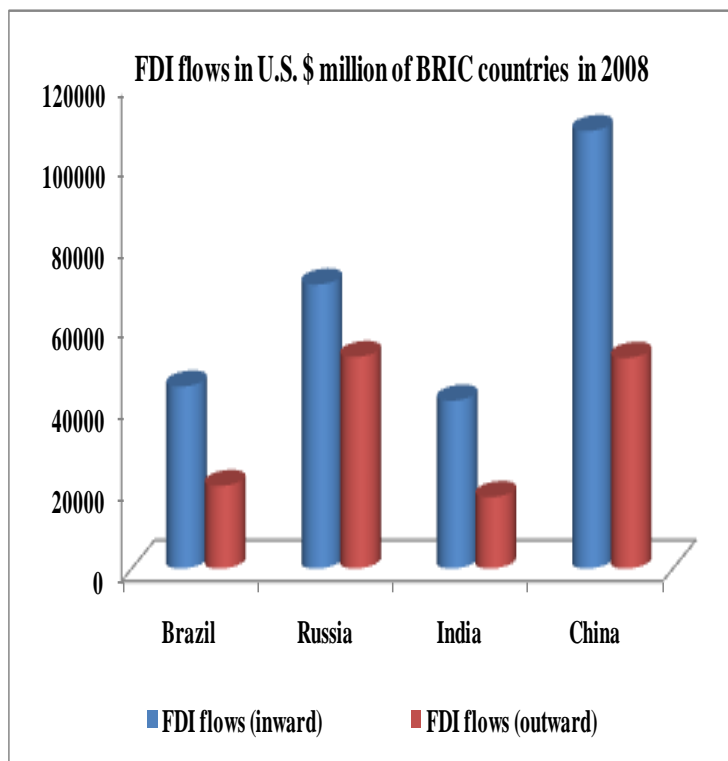
All Figures are of 2008: Sources: World Bank and World Investment Report

Share of World GDP (%):



Population: BRIC countries represent more than 41% of the world's population and 28.1% of the world's surface area. Except Russia, all countries in BRIC experience an absolute population rise. Russia's population is declining and the fall will increase as its population ages. According to the UN Population Division's *World Population Prospects 2008* report, by 2010, Russia's older population will account for a significant 12.1% of its total population compared to the world average of 7.6%. Among BRIC countries, India will have the lowest share of older population with 4.6% compared to the world average of 7.6% by 2010.





Economic Strength: BRIC countries gained significant economic momentum over the last decade. In 2008, despite the global economic recession led by the meltdown in the financial sector, which started in December '07, all BRIC countries expanded in terms of GDP. Economies of advanced countries either contracted or their growth slowed in 2008. This trend shows the strong resiliency of these countries. However, in H1 2009, Brazilian and Russian economies contracted. Over the next five years (2010-2014), the combined GDP of BRIC countries is expected to grow 8.4% on average, according to the International Monetary Fund's (IMF) World Economic Outlook October 2009 report.

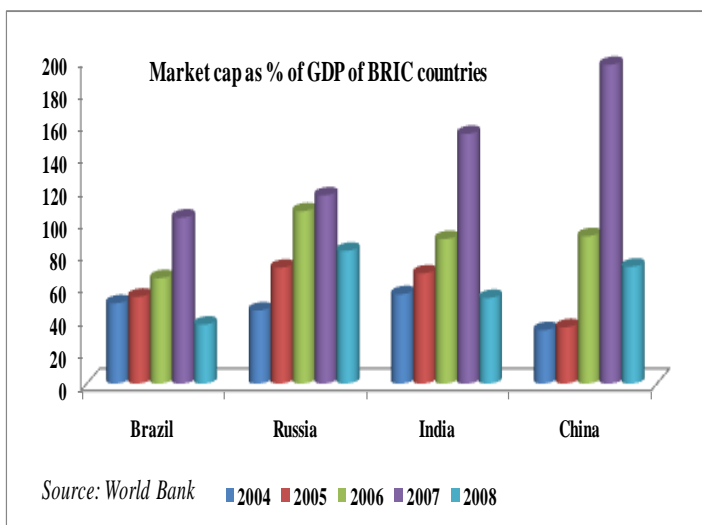
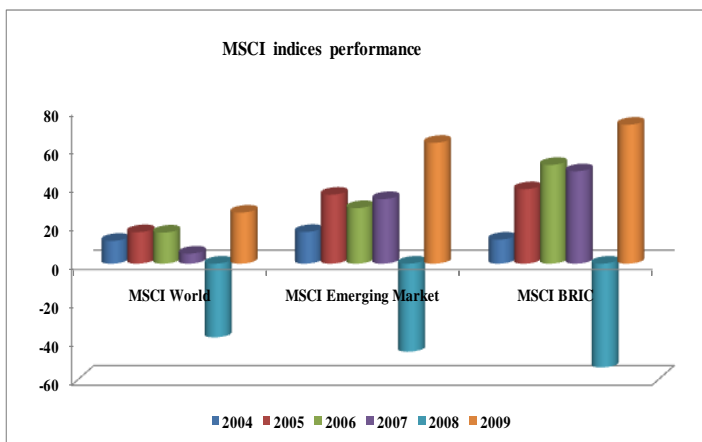
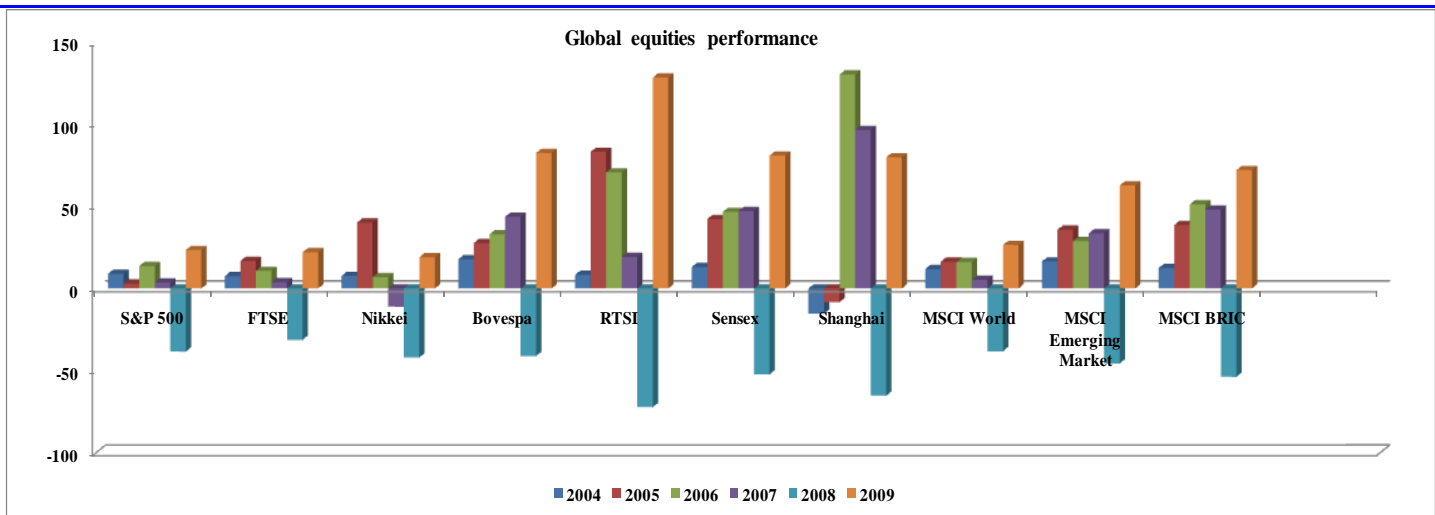
Brazil: Latin America's largest economy has an expanding global presence. Brazil is a major agricultural exporter and is widely perceived as a commodity-based economy. Favorable government policies helped reduce debt, increase foreign currency and stabilize inflation.

Russia: Russia has huge oil and gas reserves and is one of the largest energy exporters in the world. This economy registered growth for ten straight years as of 2008. The government has taken a slew of measures to bring reforms in tax, banking, labor and land codes.

India: Over the past five years, Indian economy grew on average 8.7%. The growing middle class population of India is the driving force behind the current economic growth. Economic reforms have helped reduce poverty, improve basic infrastructure and strengthened the economic performance.

China: Over the past 30 years, China has expanded at a rate of over 7% per annum. China is growing the fastest and is rapidly increasing its world influence. It is a great market for major consumer products. Further, it has become the 2nd largest exporter in the world, pushing the U.S. to the third spot.

BRIC's Growth Prospects Attract Higher FDI's: Foreign Direct Investments (FDI) into BRIC countries are rising. In 2008, FDIs into these countries grew 33.7% to US\$265.24 billion from US \$198.30 billion in 2007. BRIC countries' share of FDI inflows in total world FDI inflows rose to 15.6% in 2008 from 10.0% in 2007. Strong economic fundamentals are prime drivers of FDI inflows into BRIC countries.



Equity Market Performance: Following strong economic growth during 2004-'07, equity assets of BRIC countries outperformed those of other countries. During the period, BRIC countries' benchmark indices such as Brazil's Bovespa Stock Index, Russia's RTS Index, India's Sensitive Index (*of the Bombay Stock Exchange*) and China's Shanghai Composite Index had annual gains of 30.5%, 45.4%, 37.3%, and 50.8%, respectively. On the other hand, S&P 500, FTSE 100 and Nikkei 225 gained a modest 7.3%, 9.7% and 10.9%, respectively. Following the global economic recession, all major stock markets delivered negative returns in 2008. Markets of BRIC countries were the worst performers as global investors slashed investments in these markets. Recently, BRIC economies are leading the current economic recovery. In 2009, all major indices of BRIC markets posted impressive gains. Brazil's Bovespa, Russia's RTSI, India's Sensex and China's SCI advanced 82.7%, 128.6%, 81% and 80%, respectively in 2009.

Equities in these countries look buoyant. In each 'Country Report' (*discussed later*), we give a detailed historical equity return profile and growth outlook. During the recent economic recession, emerging markets have shown a lot of resiliency. These economies were the first to recover from the recession. Global investors have increased risk appetite towards emerging markets. BRIC markets have a prominent place among emerging markets. As BRIC countries appear to have successfully crossed the recent critical economic cycle, its equities are set to gain pace going forward.

OECD NEAR-TERM OUTLOOK:

Brazil	2007	2008	2009(E)	2010 (E)
Real GDP Growth (%)	5.6	5.1	-0.8	4.0
Inflation	4.5	5.9	4.2	4.2
Fiscal Balance (% of GDP)	-2.2	-1.5	-2.4	-1.2
Cur. Account Balance (% of GDP)	0.1	-1.8	-1.3	-1.4

Figures for 2009-10 are OECD Projections

Russia	2007	2008	2009(E)	2010 (E)
Real GDP Growth rate	8.1	5.6	-6.8	3.7
Inflation	11.9	13.3	8.0	6.5
Fiscal Balance (% of GDP)	6.0	4.8	-6	-4
Current Account Balance (% of GDP)	5.9	6.1	3.3	2.9

Fiscal Balance for Consolidated Budget; 2009-10 for OECD Projections

India	2007	2008	2009(E)	2010 (E)
Real GDP Growth rate	9.0	6.5	5.9	7.2
Inflation	4.7	8.4	4.5	3.5
Fiscal Balance (% of GDP)	-6.1	-10	-11	-10
Current Account Balance (% of GDP)	-1.0	-1.3	-1.3	-1.4

Note: Data refer to fiscal year starting in April

Gross fiscal balance includes central, state govt. deficits and subsidies.

China	2007	2008	2009(E)	2010 (E)
Real GDP Growth rate	13.0	9.0	7.7	9.3
Inflation	7.4	7.2	2	0.5
Fiscal Balance (% of GDP)	3.5	4.2	-3	-2.7
Current Account Balance (% of GDP)	11.1	9.9	9.6	7.8

GDP and Inflation Changes are on y-o-y basis.

REPORT HIGHLIGHTS AND BRIC OUTLOOK:

Basic economic structures of BRIC countries indicate these countries are poised for higher economic growth going forward. Each of these countries has enough human and monetary capital to support the high growth potential. The above factors and those we have discussed in detail in the country reports demonstrate the potential of these countries to become leading players in the global economy.

In this research report, we present economic rationale, investment rationale and risk factor for investing in BRIC markets. In the economic rationale, we map out the demand, investment and trade patterns of each of these countries. In the investment rationale, we highlight the past market performance, current valuations and outlook. Under the risk factors, we include the weakness of each economy that could obstruct the growth pace. Further, in each of the country reports, we explore the key themes that will reshape the economy. Key themes are different for individual BRIC countries. These key themes will outline sectors that could outperform normal economic pace.

Performance of any economy depends on three key factors: demand, investment and trade. Although these countries show different patterns of demand, investment and trade, these patterns are suitable for their basic nature of economic resources. Currently, agriculture, infrastructure, energy, financial services and domestic demand have emerged as common themes reshaping the BRIC economies. BRIC countries are experiencing the highest growth rate among emerging markets. The pace of growth in these countries will likely continue to follow their high foreign exchange reserves and a number of structural reforms. Equity assets in these countries have already proved attractive. Brazil, Russia, India and China are the most important emerging markets in the current economic environment. We recommend investors to gain direct exposure to these countries in their portfolios.

BRIC COUNTRY REPORTS AT A GLANCE

China	India	Brazil	Russia
ECONOMIC RATIONALE			
Since 1978, China's economy has expanded over 8% annually. Over 40% of its GDP is invested in the economy. China has emerged as a major force in commodity markets. It has strong resiliency. Despite the economic slump, it expanded over 7% in the first nine months of 2009. China drives the Asian economies. Higher economic growth is supported by strong investment.	The Indian economy is diversified, reasonably balanced and structurally strong. India managed to weather the current global financial storm due to its strong banking system, robust domestic demand and low dependency on foreign trade. India's economy demonstrates strong resiliency supported by high investment and saving rate.	The Brazilian economy has already recovered from the recession. It has vast natural resources. Revival in commodity prices could drive economic growth. Upcoming international sports events such as FIFA World Cup in 2014 and Olympics in 2016 will boost infrastructure spending.	The Russian economy grew more than 7.3% annually on average over the past five years. It is the world's second-largest oil exporter and the largest natural gas exporter. FDI inflows into Russia are increasing. In 2008, FDI inflows were US\$ 70.32 billion, an increase of 27.68% from 2007. Russia has significant foreign currency reserves.
KEY THEMES			
Demand for Agricultural products will remain strong. Infrastructure builds the Chinese economy. Metal consumption is a key factor for the economy. Robust demand for energy will continue. China is a leading consumer of energy in the world. It has already emerged as a manufacturing hub for industrial goods in the world.	As both the population and per capita income are increasing, demand for agricultural products will surge. Rural economy is another feature. Growing middle class customers are emerging as a force in the consumer market. Strong banking system is a positive. Infrastructure boom is a key driver of the economy.	Agricultural products represent 36% of Brazil's exports. Brazil is the ninth largest producer of steel. Since 2000, the telecommunication industry has been playing a significant role in economic growth. Brazil is the largest electricity market.	The oil and gas sector is a key sector. Russia is the world's largest energy exporter. Infrastructure is a growing sector in Russia. Infrastructure spending is strong and will continue to be robust. Consumption boom is another key factor.
INVESTMENT RATIONALE			
Long-term outlook for Chinese equities appears strong as robust economic fundamentals will continue. Further, balance sheet of corporates are strong to support healthy earnings growth. Valuations of Chinese stocks will expand over the medium-to-long term. As global investors are upbeat on China, foreign investors will pump more funds into China.	Macroeconomic fundamentals of India appear impressive. Indian companies are showing strong earnings growth. Earnings growth outlook will be the key market driver going forward. Medium-term valuations will expand. We believe Indian equities will continue to gain momentum over the long term. Foreign funds are expected to rise.	Economy fundamentals are strong. Company earnings have already improved. Brazilian equities are trading at attractive valuation levels. Foreign funds flow will continue to rise. The pace of economic growth will set the market direction going forward.	After prolonged economic slump due to the global economic recession, the Russian economy is near stabilization. Considering the expected economic rebound in the near term, valuations of Russia's equities will rise. Russian markets will receive more foreign fund flows in the near term.
RISK FACTORS			
The current economic pace may lose some steam when the government slows lending and withdraw the stimulus program. Fear of asset bubble hangs over the Chinese economy. Volatility in international trade may impact the domestic economy. Population of the country is aging. Rapid industrialization will put downward pressure on natural resources.	Rising fiscal deficit is a major concern for the economic health of India. The government forecast fiscal deficit of 6.5% of GDP for 2009-10. Economic inequality is another concern. Poverty is still high. Poverty causes many social problems in India. Terrorism and naxalism are threats for national security.	Brazil imposed a 2% tax on foreign investment in equities and fixed income instruments from October 2009. This is a negative sign for attracting foreign funds. Brazil has tradition of low investment rate. To meet high growth, Brazil has to raise the investment rate.	The Russian economy's excessive dependence on the oil and gas sector reflects lack of diversification in the economy. The share of older population (65 years above) in total population is quite significant. Corruption is rampant in Russia.

CHINA COUNTRY REPORT AT A GLANCE

Economic Rationale	Key Theme	Investment Rationale	Risk Factor
Since 1978, China's economy has grown more than 8% per year.	Agricultural product demand will remain strong.	Historical performance reflects stock markets have given attractive returns. The government's continuous efforts for market-oriented economy is a positive sign.	Recent economic recovery of China was driven by bank lending and infrastructure. Once the government reduces these measures, the growth may lose pace over the near term.
More than 40% of China's GDP is spent on investment per year.	Infrastructure builds the Chinese economy. China is expected to spend US\$200 billion per year on infrastructure.	Long-term outlook for Chinese equities appear strong as robust economic fundamentals will continue. Further, balance sheets of corporates are strong to support healthy earnings growth.	The 73% rise in property sales in the nine months of 2009 highlight the risk of asset bubbles.
A major player in global trade.	China's metal consumption as a share of world consumption has increased from 10% to 25% in the past decade. While its economy has been growing by 9% a year since 1990, its consumption of metals has increased 17% per year.	Valuations of Chinese stocks will expand over the medium-to-long term	Total merchandise trend, including exports and imports, represent 2/3rd of GDP. Volatility in trade may impact the economy.
China has emerged as a major force in global commodity markets.	Strong demand for energy will remain. China has emerged from being a net oil exporter in the early 1990s to become the world's third-largest net importer of oil in 2006. China is also the world's largest producer and consumer of coal.	Fundamentals in domestic markets and global investor sentiments are strong.	Rapid industrialization and urbanization could create environment pollution problems.
The Industry sector (manufacturing and construction) is growing nearly 12% per year, outpacing normal economic pace, over the previous five years.			Population of the country among the most rapidly aging in the world.
Strong resilient capacity. Despite the global economic slump and weak exports, it expanded more than 7% in the first nine months of 2009			
A leading indicator of the Asian economy.			



CHINA COUNTRY REPORT:**Quick Fundamentals- Chinese Economy**

GDP Size (US \$ Trillion)	3.86
GDP Growth	9.0%
GDP Growth (Last 5-Year Avg)	10.8%
Population (Billion)	1.32
Population Growth(5-Year Avg)	0.56%
Revenue/GDP	20.4
External Debt/GDP	8.5
External Debt/GDP	0.19
Exports/GDP	35.0
Net FDI in 2008 (US \$ Billion)	108.3
Fiscal Balance (% of GDP)	-0.4

All Figures are of 2008: Source: World Bank, World Economic Outlook, Asian Development Bank

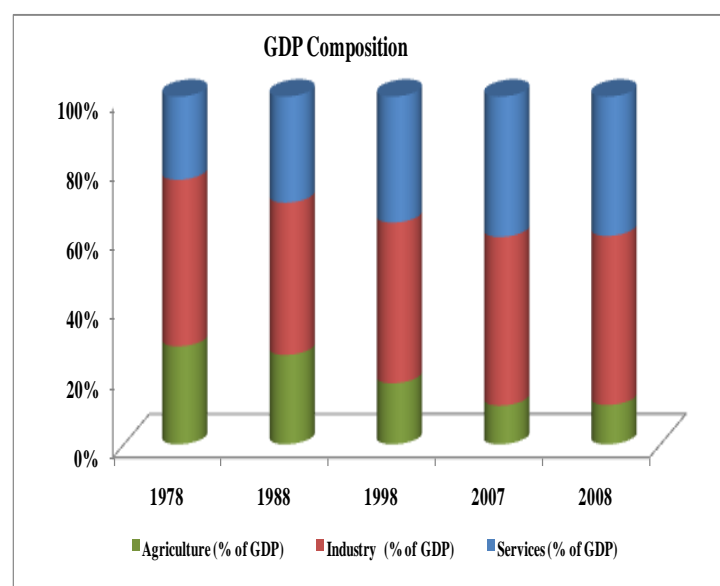
Population: China is the world's most populous nation. At the end of 2008, China's total population stood at 1.32 billion, representing 19.8% of the world population. During the previous five years (2004-2008), China's population grew 0.6% annually on an average. The government through extensive measures managed to control the pace of population growth. According to *World Population Prospects: The 2008 Revision* report by United Nations Population Division, people in the age group of 15-64 in China will represent 71.9% of the total population by 2010. People above the age of 65 will represent 8.2% of total population by 2010. This ratio is forecast to increase to 23.3% of total population by 2050. Although China's current population structure is supportive of the current pace of economic growth to some extent, the faster rate of growth in old age population could pose a threat to China's growth in the long run.

Political Structure: The People's Republic of China was founded in 1949 by the Chinese Communist Party (CCP). Since 1949, CCP has been ruling China. Mao Zedong was the first CCP Chairman, who ruled the country for nearly three decades. After gaining power in 1978, Deng Xiaoping initiated economic reforms. From 1989 to 2002, Jiang Zemin led the country. The CCP is now headed by Hu Jintao, who is also the State President.

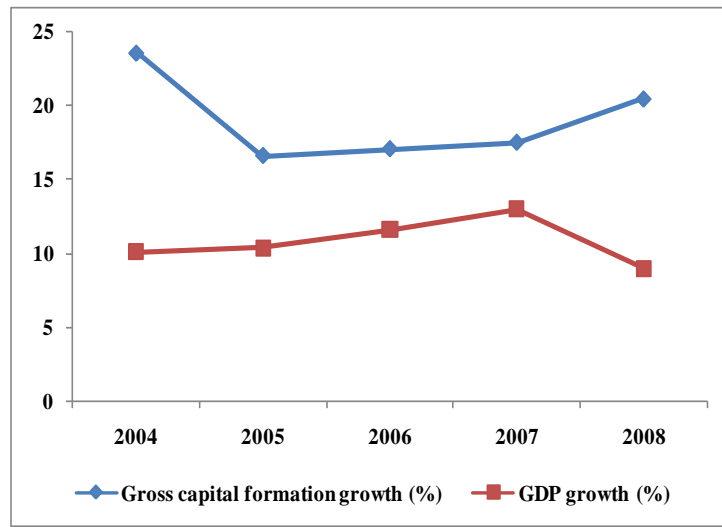
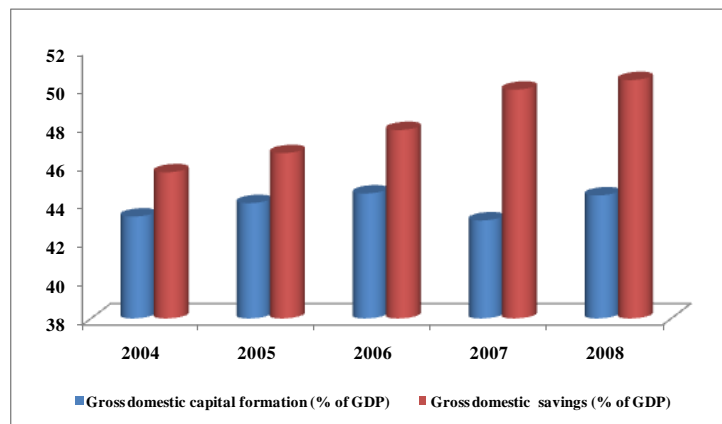
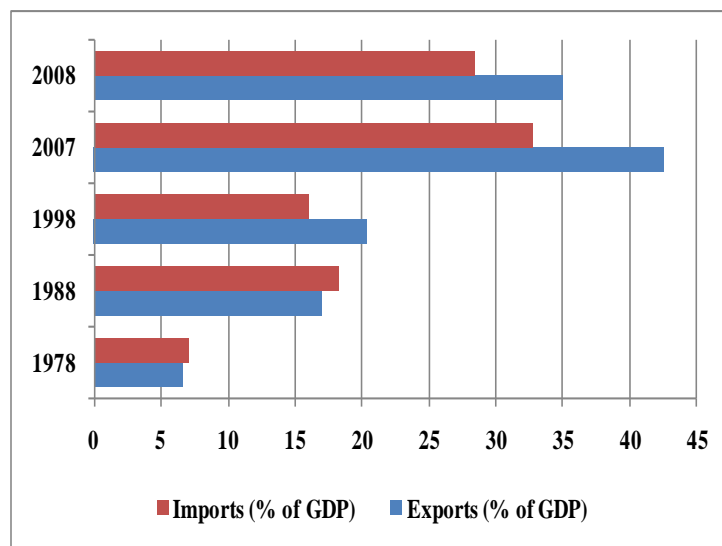
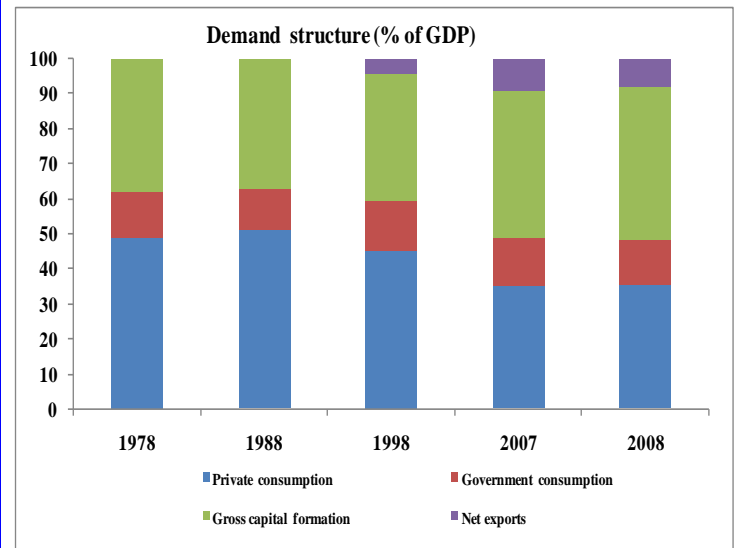
The CCP dominates the government. The politburo standing committee is the main decision making body. There is no formal political opposition to the CCP.

Policy Issues: China's leaders have been supportive of economic liberalization and sustainable growth alongside political control. The government continues to pursue economic liberalization ever since China gained accession to the World Trade Organization in 2001.

Overall Economy: Over the past 30 years, China has developed as a market-oriented economy. Since the end of the 1970s, the government has taken a slew of measures to improve the economic structure. China's growth rate has surprised the world. It is increasing its presence in the global economy. China is emerging as a manufacturing hub for industrial goods in the world. Asia's largest country will soon become an important production center in the world.

ECONOMIC RATIONALE:

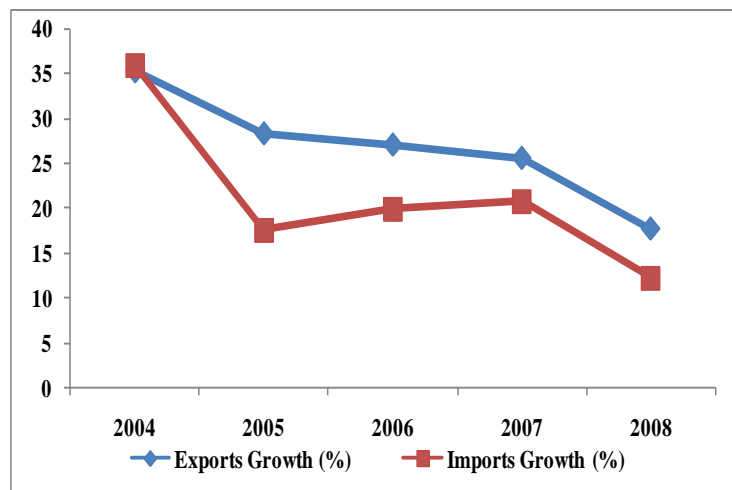
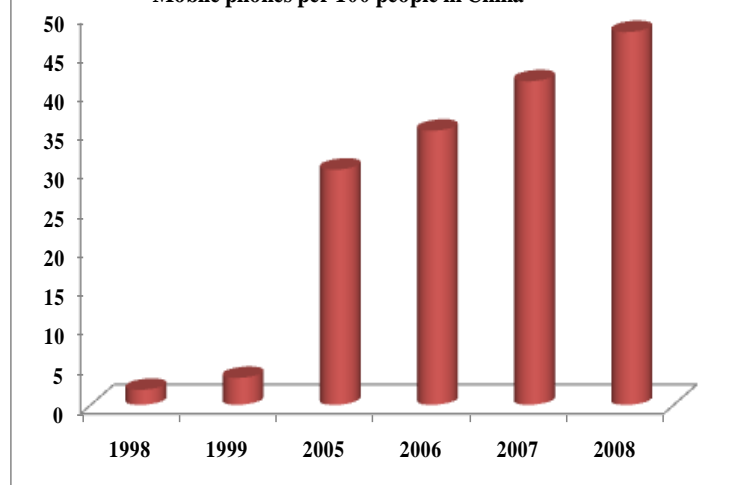
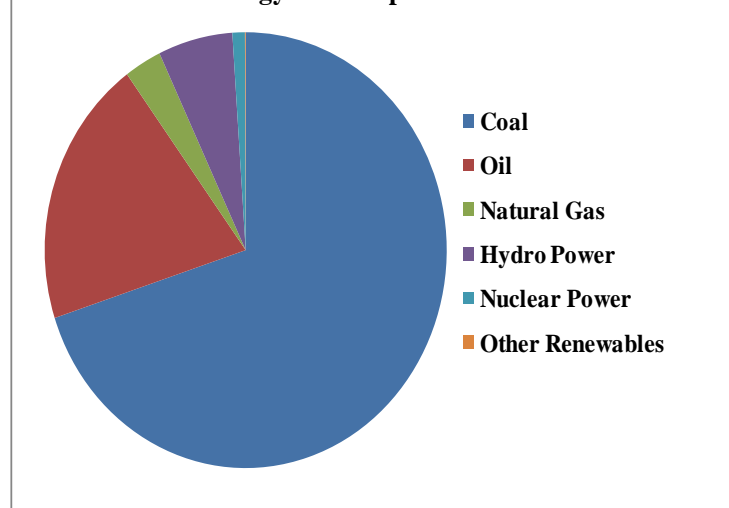
Higher GDP Growth Trend: Over the past 30 years, China has grown more than 8% annually on average. China's high growth rate has surprised the world. In China, the industrial sector represents nearly half of its total GDP. While the contribution of the industry and services sectors to the total GDP is on the rise, the share of agriculture has been constantly decreasing.

China: GCF & GDP Growth Trends**China: Savings & Investment Trends****China: Imports & Exports (% of GDP)****China: Demand Structure (% of GDP)**

In the GDP expenditure approach, final consumption (including private and government) constitutes half of GDP. The share of household consumption expenditure or consumer spending is declining, but the share of gross capital formation is increasing. In 1978, the share of household consumption expenditure in the GDP was 48.8% which fell to 35.4% in 2008.

Investment in Economy: Higher economic growth is supported by strong investment. Gross domestic capital formation (GCF) as a percentage of GDP in 2008 was 44.4%. During the previous five years, GCF as a percentage of GDP remained above 40%. The higher investment rate is a positive factor for a growing economy like China. Further, this strong investment in the economy was backed by robust gross domestic savings. Gross domestic savings as a percentage of GDP was 50.4% in 2008. During the previous five years, gross domestic savings as a percentage of GDP remained above 45%.

A Major Player in International Trade: The Chinese economy is getting more integrated with the global economy. Chinese exports are increasing at a faster rate. In 2008, exports increased 35%. However, export growth dampened in 2009 due to recession in key overseas markets. Exports of goods and services as a percentage of GDP are increasing. In 1978, total exports as a percentage of GDP was 6.6%, which rose to 20.3% in 1998. In 2008, this ratio was 35%. Manufactured goods account around half of total exports; industrial sector represents around half of total output.

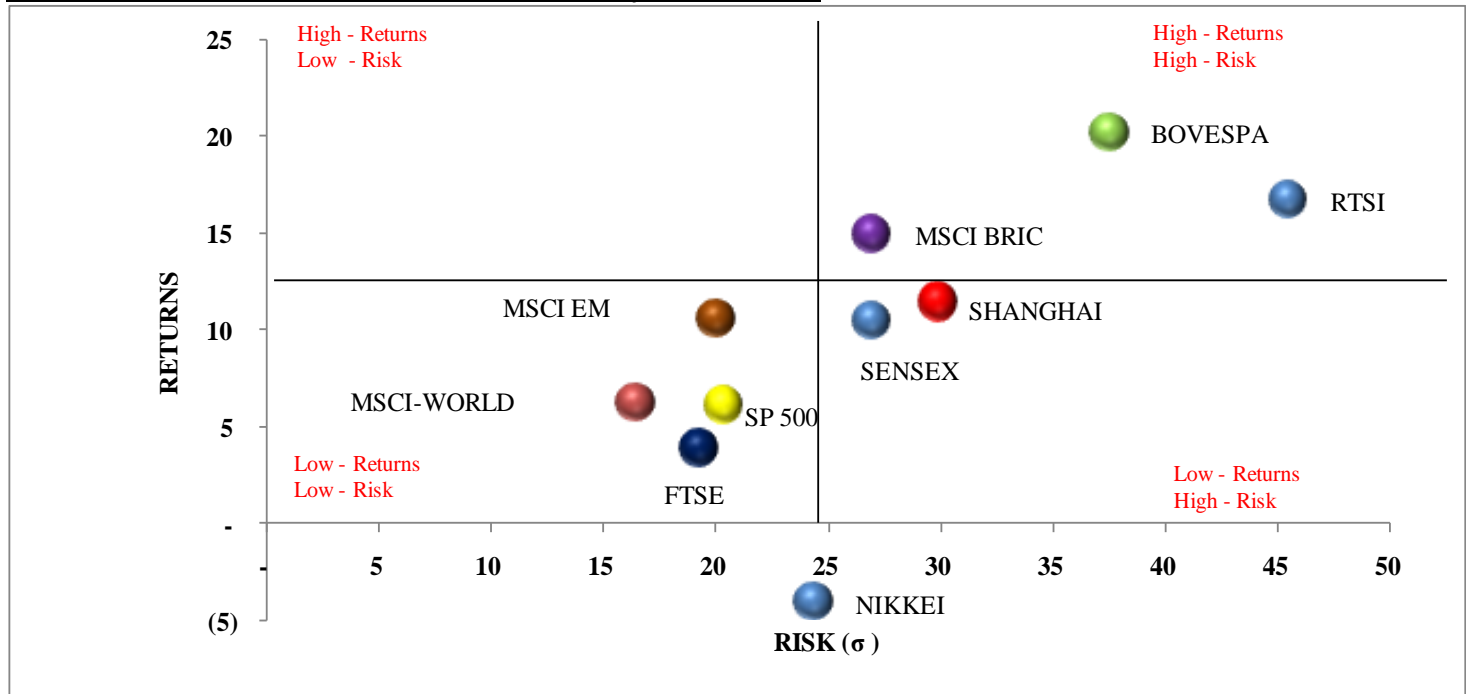
China: Imports & Exports (Growth)**Mobile phones per 100 people in China****China's Energy Consumption Pattern 2006****KEY THEMES:**

Agriculture, infrastructure, energy, manufactured goods and commodities, especially metals, are the key segments that will continue to reshape the Chinese economy.

Agriculture: Global demand for agricultural products is expected to increase due to supply concerns. With its growing population and increasing per capita income, China is expected to see a rapid rise in demand for agricultural products. As a result, prices of agri products will rise substantially. China is the world's largest consumer of wheat, rice, palm oil, cotton and rubber. It is the second largest consumer of soybeans, soy oil, and tea. Agriculture will be one of the key sectors that will impact the economy.

Infrastructure: Government spending on infrastructure is quite impressive. Roads, rail, aviation, ports and other physical infrastructure will be the key drivers for the economy. China currently spends about 9% of its GDP on infrastructure compared to 5% and 2.4% by Europe and the U.S., respectively. It is estimated that, over the next 10 years, China will spend \$200 billion a year on infrastructure development alone. Telecom, electricity and urban infrastructure will gain momentum going forward. Mobile subscriber base is rapidly expanding. Electricity consumption is growing and demand for urban infrastructure remains impressive.

Energy: China is a leading consumer of energy in the world. Demand for energy will rise in line with China's economic growth. China has emerged as the world's 3rd largest net importer of oil in 2006 from being a net oil exporter in the early 1990s. Natural gas use in China has also increased significantly in the recent years. Considering the growing demand for natural gas, China plans to raise imports through pipeline and liquefied natural gas (LNG). It is also the world's largest producer and consumer of coal, an important factor in world energy markets. China is a major consumer of oil globally. According to the Energy Information Administration (EIA), China consumed an estimated 7.8 million barrels per day of oil in 2008, the 2nd largest oil consumer in the world next to the U.S. During the same year, China produced an estimated 4.0 million bbl/d of total oil liquids, of which 96% was crude oil.

Past 15-Year Annualized Risk-Return Global Market Profile (1995-2009):

China's net oil import was 3.9 million bbl/d in 2008, making it the 3rd largest net oil importer in the world, next to the U.S. and Japan.

The EIA forecasts China's oil demand will remain strong over the short term. China's oil production is forecast to remain relatively flat at 4million bbl/d in 2009. According to Oil and Gas Journal (OGL), China had 16 billion barrels of proven oil reserves as of January 2009.

Manufactured Goods: Manufactured goods is a major contributor to overall GDP. Manufactured goods, such as office and telecommunication equipment and other electrical and electronic articles and textiles, represent a major share of exports. China has already emerged as a manufacturing hub for industrial goods in the world. Its low-cost environment, cheap labor and advanced infrastructure are positive factors promoting manufacturing activities in China.

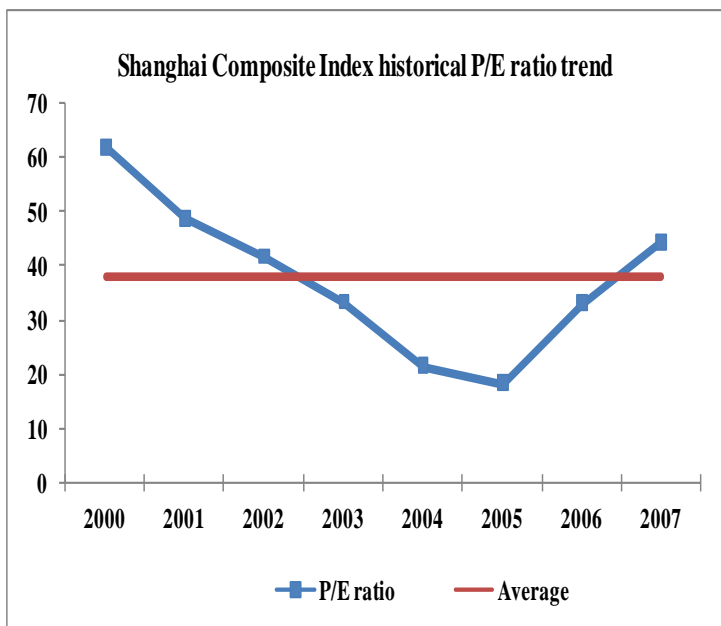
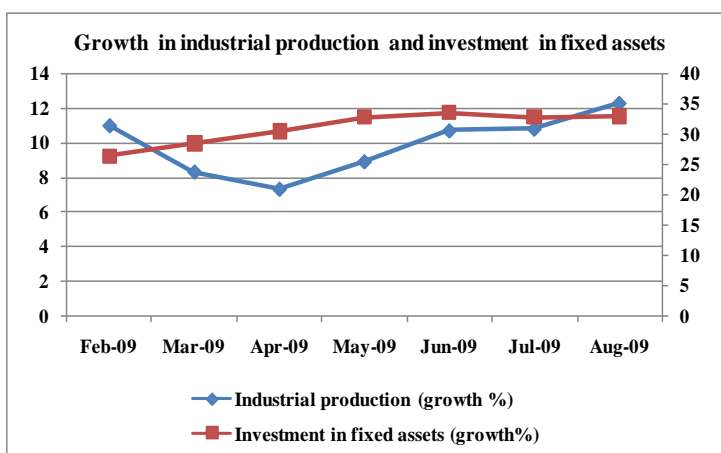
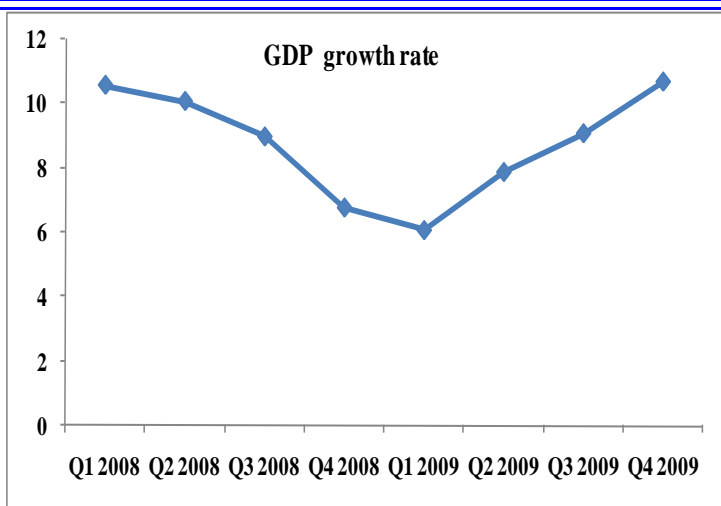
Metal Commodity: China's need for metal is intense to keep with the growth of its economy. Its metal consumption as a share of world consumption has jumped in the past decade from around 10% to 25%. China is now the world's top consumer of aluminum, copper, lead, nickel, tin, zinc, iron ore, and coal. It is also the world's top consumer and producer of steel.

While its economy has been growing at 9% a year since 1990, its consumption of metals has increased 17% per year. Industrialization, urbanization and infrastructure building will drive demand for metals in China. Hence, China will continue to play a key role in the global metal markets in the coming years.

INVESTMENT RATIONALE:

Historical Performance: In line with its economic growth, Chinese stocks have produced attractive returns. During past 15 years period calendar year 1995-2009, the Shanghai Composite Index (SCI) rose at 11.41% CAGR, outperforming the S&P 500 and the FTSE 100 indices by a wide margin. The strong performance of Chinese stocks has attracted global investors. Global investors have shown great interest in Chinese equities. Among the emerging markets, China is one of the best performers.

China's Growth Still Intact: Overall economic outlook for China appears buoyant as investment in the economy is strongly supported by high domestic savings, emerging wealth from consumers due to rising per capita income, huge foreign reserves and the government's pro-active measures.



Despite the global economic recession in 2008, China grew 9%. In 2009, China was the first among the major economies to recover from the slowdown. Further, in 2009, the Chinese economy expanded 8.48%. Basic economic indicators point that China is set to gain economic pace going forward.

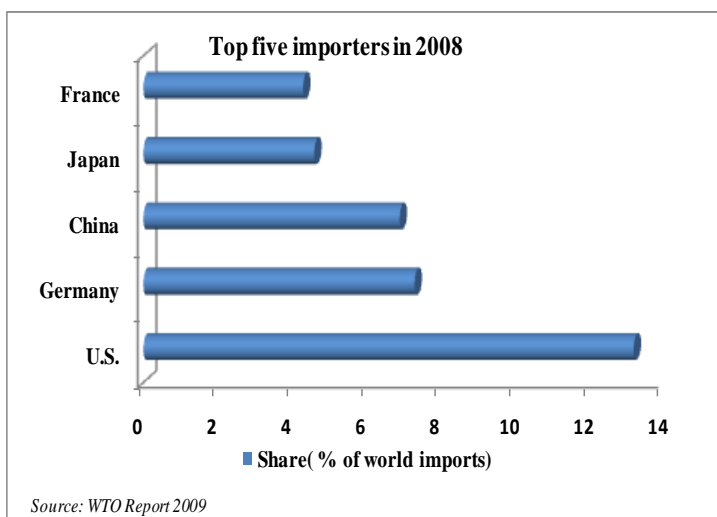
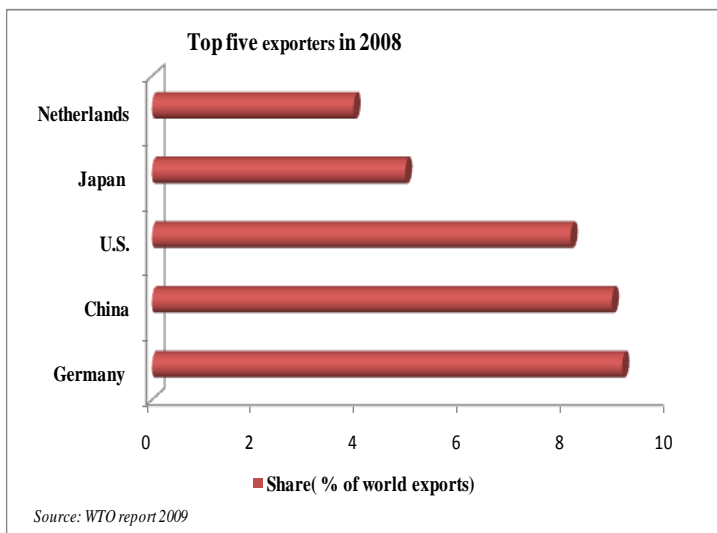
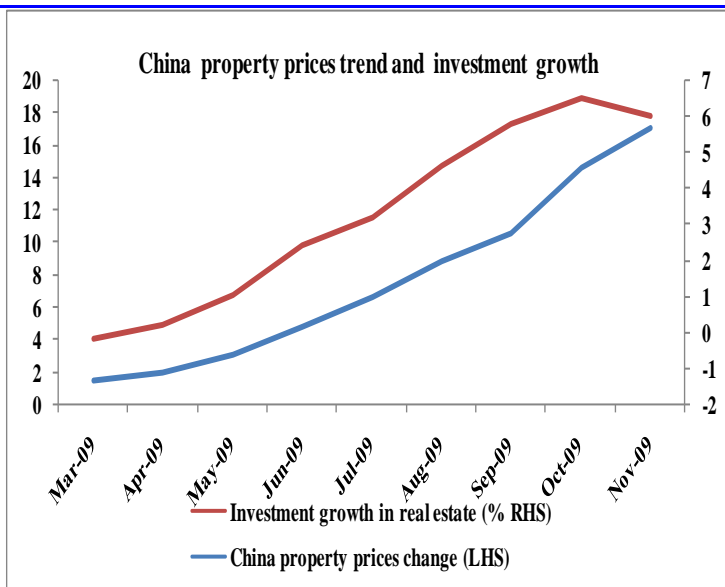
Although China has a considerable share of world exports, it posted a 6% growth in Q1 2009 despite the adverse impact of recession in overseas markets. China's exports fell for consecutive thirteenth months until November 2009. Hence, we believe the current economic recovery is not driven by exports. As there is only limited downside risk to China's growth story, in the long-term its equities could prove to be good investments.

Strong Earnings Prospects: China has already passed a critical point of economic uncertainty. Considering the favorable economic environment, higher bank lending trend and strong balance sheets of companies, we expect corporate earnings to expand going forward. We believe the earnings growth outlook is visible.

Medium-Term and Long-Term Valuations to Expand: Earnings outlook, a key driver for market direction, remains strong backed by robust macro-economic fundamentals. Although Chinese equities are currently trading at high P/E levels, strong growth outlook supports its valuation. We believe Chinese stocks warrant high valuations and its valuation multiple could expand in the medium-to-long term.

Upbeat Outlook by Global Investors: Global investors have shown great interest in the emerging markets in the past 10 years. Earnings growth was the most important structural element driving emerging markets over this period. China's strong economic fundamentals continue to support its earnings growth outlook. Hence, China has enjoyed a premium share of the fund flows to emerging markets and we expect the trend to continue.

Comfortable Liquidity Position: Savings rate in China is one among the best in the world. This robust savings environment has created some sound domestic financial institutions in China. Both domestic institutional players and retail investors play a vital role in Chinese capital markets.



RISK FACTORS:

Quality of Economic Recovery: In the first nine months of 2009, the Chinese economy expanded more than 7.5% on the government's stimulus program and record lending growth. China's growth could slow in mid-2010 when its stimulus package fades and weaker U.S. consumer demand fails to support an export-driven recovery. Chinese stocks run up as economic recovery strengthens and earnings improve. In 2009, the Shanghai Composite index rose 80%. We believe the improvements in the economy and corporate earnings have already been priced in and are unlikely to act as catalysts for a major rally.

Higher Property Prices: Home sales in 2009 jumped 75.5% y-o-y to CNY 4.4 trillion. That was up from a 73.4% gain in the first nine months. Property prices in 70 cities rose 1.5% y-o-y in 2009. Real estate asset price bubble hangs over the Chinese economy. Chinese investment in real estate rose 16.1% in 2009. Real estate accounts for more than 20% of total fixed-asset investment in China.

Excessive Dependence on Foreign Trade: China's share in global trade is increasing at a fast rate. In 2008, China was the second top exporter and the third top importer in merchandise trade. Volatility in foreign trade could have a great impact on the Chinese economy. China posted a straight eleventh month decline in exports in September 2009 due to the global recession.

Environmental Pollution: Rapid industrialization, urbanization and infrastructure creation will put downward pressure on natural resources. Pollution problems could be a threat to the overall development of China. Pollution issues are already visible.

Aging Population: Growing share of older population in total population is a concern. People above the age of 65 will represent 8.2% of total population by 2010. According to the *World Population Prospects: The 2008 Revision* report, this ratio will increase to 23.3% of the total population by 2050.

China: Social Indicators 2008		China: Business Environment	
Population (billion)	1.32	Doing Business 2010 Rank (Out of 180 countries)	
Population growth(%)	0.54	Doing business	89
Urban population (% of total)	44.90	Starting a business	151
Rural population (% of total)	55.10	Getting credit	61
Poverty (% of total population below national poverty line)	2.80	Protecting investors	93
Old age dependency ratio	8.20	Paying taxes	130
Life expectancy at birth (years)	72.99	Enforcing contracts	18
Literacy rate	93.30	Closing a business	65
<i>Source: World Bank, Human Development Report 2009: Some figures are of 2007</i>		Global Competitiveness Report 2009-10 (Out of 134 countries)	
		Rank	
		Global competitiveness index	29
		Financial market sophistication	78
		Overall infrastructure quality	66
		<i>Source: Doing Business 2010: Global Competitiveness Report 2009-10</i>	

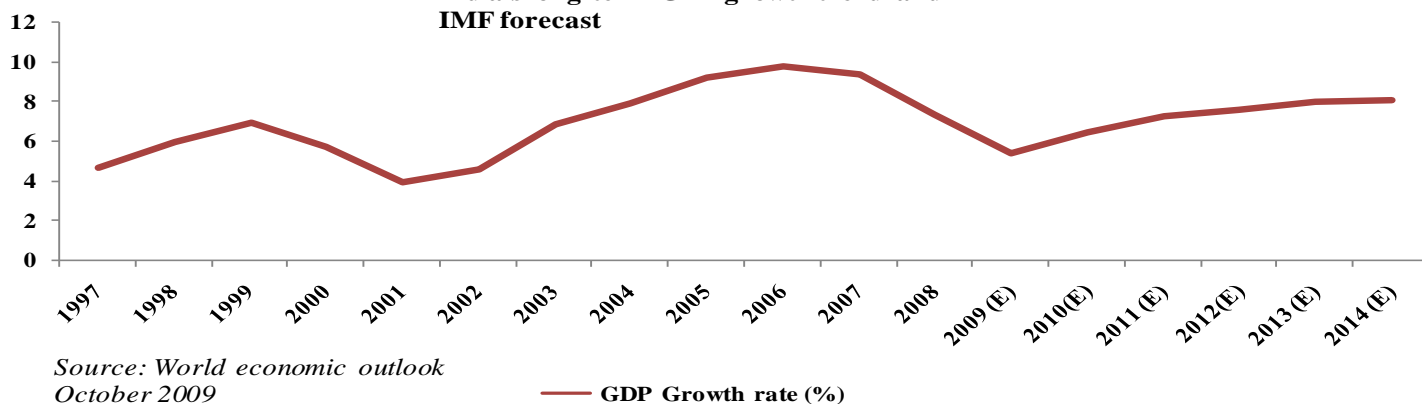
China: Key Economic Ratios	1978	1988	1998	2007	2008
GDP growth rate	11.7	11.3	7.8	13.0	9.0
Gross capital formation	37.8	37.8	37.1	43.3	42.6
Exports of goods and services/ GDP	6.6	16.9	20.3	42.5	35.0
Gross domestic savings/GDP	NA	NA	38.9	49.9	50.4
External debt/ GDP	NA	NA	17.5	10.8	8.5
Total debt service(% of exports of goods, services and income)	NA	9.6	8.7	2.1	2.3
Current account balance/GDP	NA	-0.9	3.0	10.7	9.6
Fiscal balance/GDP	NA	NA	-1.9	0.6	-0.4

China: Structure of Economy					
(% of GDP)					
Agriculture	28.2	25.7	17.6	11.1	11.3
Industry	47.9	43.8	46.2	48.5	48.6
Services	23.9	30.5	36.2	40.4	40.1
Household final consumption expenditure	48.8	51.1	45.4	35.6	35.4
Govt final consumption expenditure	13.2	12.0	14.2	13.4	13.2
Gross capital formation	38.2	37.0	36.2	42.1	43.5
Net exports	0.0	-0.1	4.2	8.9	7.8

INDIA COUNTRY REPORT AT A GLANCE

Economic Rationale	Key Themes	Investment Rationale	Risk Factors
<p>The Indian economy has continued its growth momentum. Since 1997, it has expanded more than 7% annually. Since 1991, the Indian government has continued its economic reform programs. Investment in the economy is high. In 2008, gross capital formation was 39% of GDP. The Indian economy has successfully transferred from an agri-based economy to a moreover diversified economy. The services sector contributes more than 50% to GDP. The resiliency of the economy is still intact. During the recent global economic recession, Indian economy was the least impacted. After structural reforms, private sector is playing a significant role in the economic growth momentum. The impressive performance of private players has created significant number of jobs. FDI flows to India are modest. It has strong foreign currency reserves.</p>	<p>Agricultural products demand will rise with growing population and an increase in per capita income. Rural economy is a significant part of the Indian economy. The expenditure of rural people is increasing. The growing rural economy is a positive factor. More than 70% of the total population live in rural areas. India plans to increase spending on infrastructure to 9% of GDP from the current level of 5%. In the 11th Five Year Plan, India plans to spend about U.S.\$500 billion. Roads, ports, airports, electricity and telecom are the main infrastructure sectors. Indian telecom network is the third largest in the world. Banking sector is a key sector for India. Balance sheets of Indian banks are strong. The sound and efficient banking system protected the Indian economy from the recent global economic recession. Asset quality has been improving.</p>	<p>Earnings outlook of Indian companies appear strong. As the balance sheets of major private companies are very healthy, growth prospects look promising supported by robust economic fundamentals. Earnings momentum will boost investor confidence. The medium-term valuation of Indian equities will expand as earnings could grow significantly in the next one to two years. Fund flows into Indian equities will gain pace with better fundamentals. Earnings outlook appear strong. The long-term outlook of Indian equities also appear buoyant. Improving risk appetite of investors towards emerging markets is a major boost as India's economic fundamentals are strong.</p>	<p>Rising fiscal deficit is a major concern. Government, in its budget, forecasts fiscal deficit of 6.5% of GDP for 2009-10. Off-budget liabilities could increase the deficit further. If state budget deficits are included, total fiscal deficit could cross 12% of GDP. Inequality in the economy is a threat to India. Poverty ratio is quite high. This dismal trend is a threat to socio-economic development of India. Inclusive growth and economic prosperity are not equally divided. India is in the grip of some serious issues affecting its national security. Naxalism, a movement by armed tribals, has spread to major parts of the country. Terrorism is another threat to India's national security.</p>

India's long-term GDP growth trend and IMF forecast



INDIA COUNTRY REPORT:**Quick Fundamentals
(Indian Economy)**

GDP Size (US \$ Trillion)	1.2
GDP Growth (Last Year)	7.1%
GDP Growth (Last 5-Year Avg)	8.7%
Population (Billion)	1.15
Population Growth(5-Year Avg)	1.4%
Revenue/GDP	13.6%
External Debt/GDP	18.8%
Exports/GDP	24.0%
FDI Last Year (US \$ Billion)	41.5
Fiscal Balance	-6.2%

All figures of 2008: Source: World Bank and CSO India

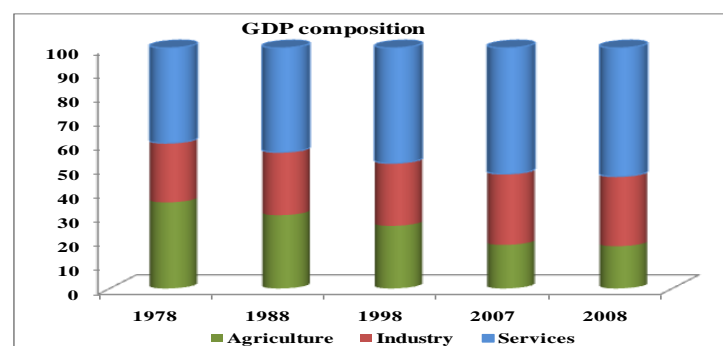
Population: India is the 2nd largest populous nation in the world. At the end of 2008, total population stood at 1.13 billion, accounting for 17% of the world population. Over the previous five years, India's population grew 1.4% on average. India's current demographic figure is favorable for economic growth. According to *World Population Prospects: The 2008 Revision* report by United Nations Population Division, people in the age group of 15-64 will represent 62.3% of total population by 2010. Share of old age population (*more than 65 years old*) will be 4.9% by 2010. Young people make up a large share of the current population.

Political Structure: India is the largest democratic country in the world. It has a multi-party political culture, where regional political parties play a key role in national politics. Prime minister is the leader of the government, requiring the support of a majority in the parliament. President is the head of state, who has limited executive power. However, the President can influence the formation of governments when no party secures a clear mandate from the people. The judiciary is totally independent.

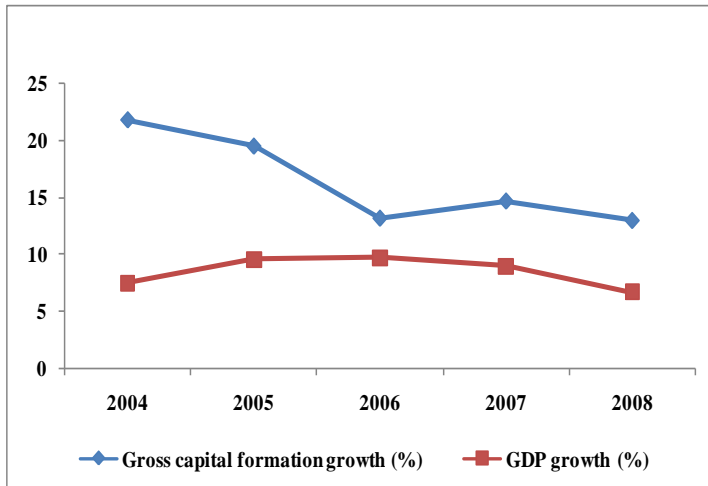
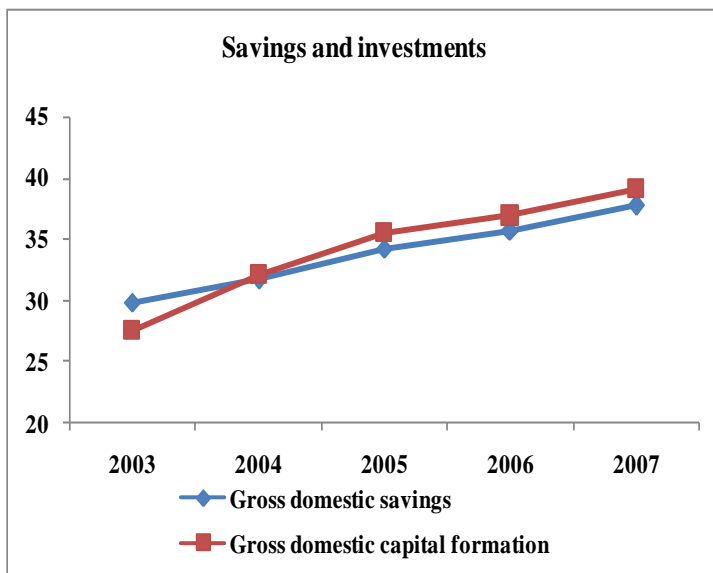
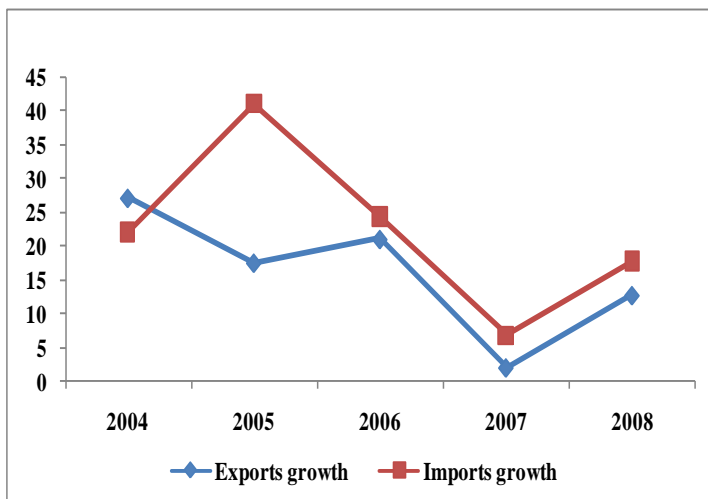
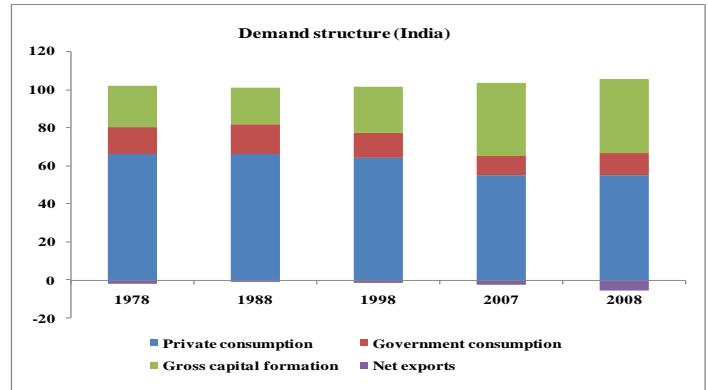
Policy Issues: In 1991, the government brought drastic economic reforms programs. Privatization, liberalization and trade integration have become key features of the economy. These structural reform programs have supported economic growth. Since then, successive

governments have supported economic reform programs.

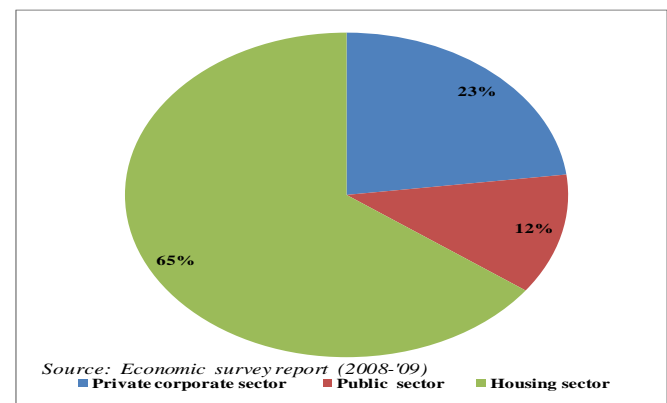
Overall Economy: The Indian economy is diversified, reasonably balanced, and structurally strong. The \$1.2 trillion Indian economy represents 3.1% of the world's gross domestic product. India accounts for one-sixth of the world population. After 1990-91, Indian economy saw dramatic improvements following structural reforms such as privatization, liberalization and trade reforms. Since then, India's GDP has quadrupled. India registered an average annual growth rate of 8.7% over the previous five years. Despite the global recession in 2008-2009, Indian economy expanded 7.1% in Q4 FY09 (*financial year ends on March 31*), 2nd highest growth rate after China. India managed to weather the current global financial storm due to its strong banking system, robust domestic demand and its low dependency on foreign trade. This reflects India's resiliency.

ECONOMIC RATIONALE:

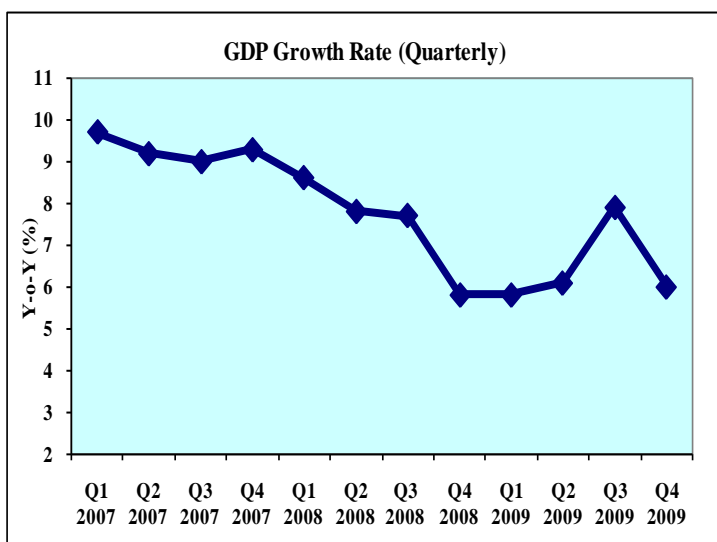
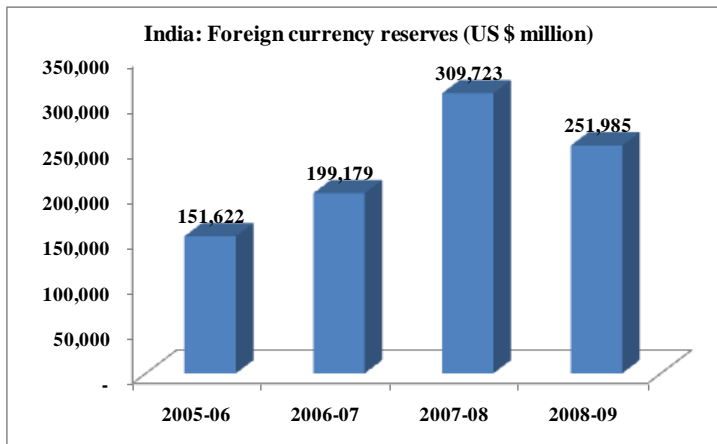
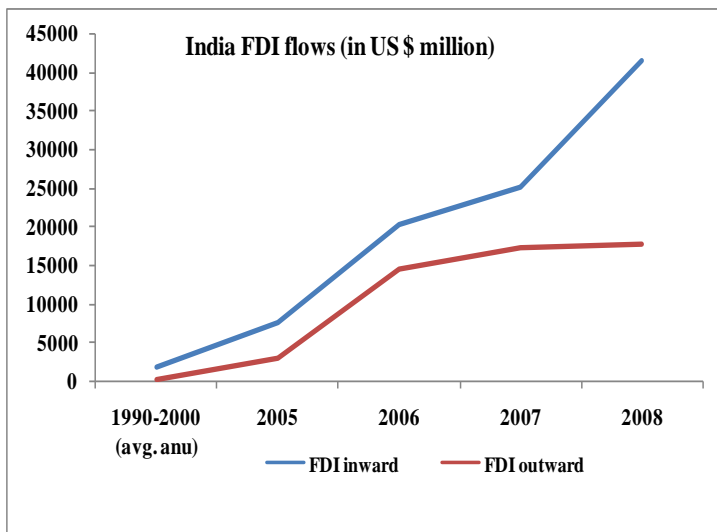
Economic Growth: India managed to generate more than 8.7% annual growth in GDP over the past five years. The growth momentum was supported by strong domestic economic factors. Moreover, India is a diversified economy. In 2008, agriculture, industry and services sectors contributed 17.6%, 29% and 53.4%, respectively to GDP. Agriculture's share of GDP had declined to 17.6% in 2008 from 35.8% in 1978. On the other hand, share of the services sector had increased to 53.4% in 2008 from 39.5% in 1978. The services sector is a key driver of the economy.

India: GCF & GDP Growth Trends**India: Savings & Investment Trends****India: Exports & Imports (Growth)****India: Demand Structure**

Higher Investments and Savings: Private consumption accounted for more than half of total GDP in 2008. Government consumption represented 11.6%. Gross capital formation accounted for 39% of GDP in 2008. The share of household spending dropped to 54.7% in 2008 from 71.8% in 1978. During the previous five years, India's GDP expanded 8.7% annually. Higher investment rate in the economy supported strong growth. Gross capital formation has grown 16.4% over the past five years. Savings rate is also impressive considering the current growth rate. Gross domestic savings rate as a percentage of GDP was 37.7% in 2008. The household sector has a large share in gross domestic savings, with 24.3% of GDP.

Domestic savings (2007-08): By Sector

Exports and Imports: India is relatively less integrated with global trade. Exports of goods and services as a percentage of GDP were 24% and imports 30% in 2008. India had a share of 1.1% of global exports in 2008 and 1.8% of global imports. India managed to post 6.7% growth in 2008-09 despite the recent global economic crisis. Although exports faced trouble due to weak global markets, India weathered the crisis following robust domestic demand.



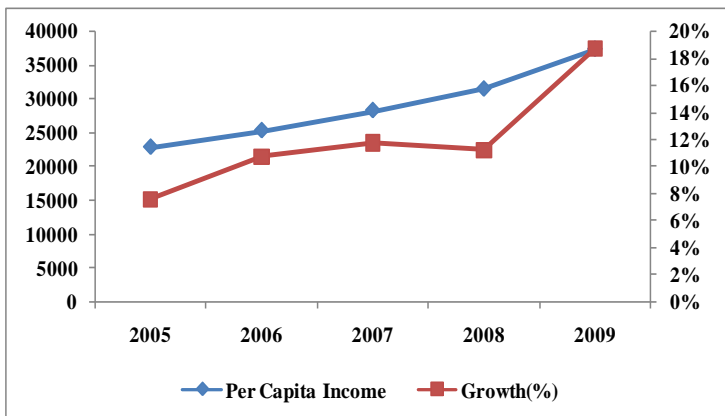
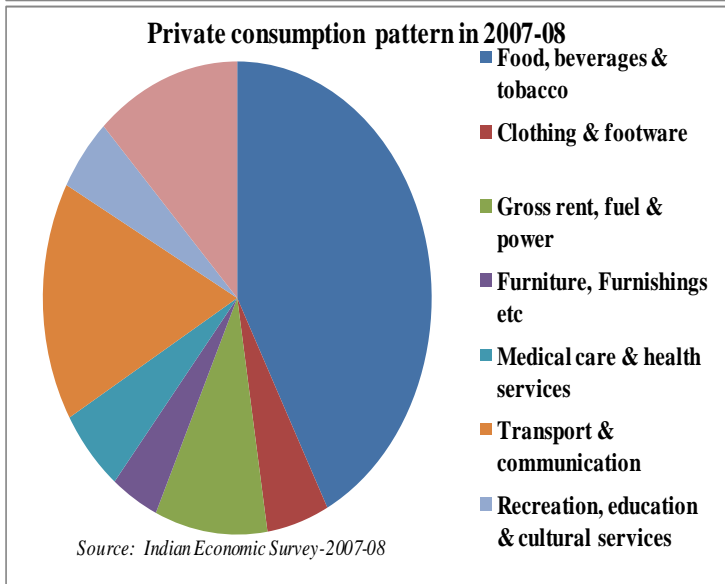
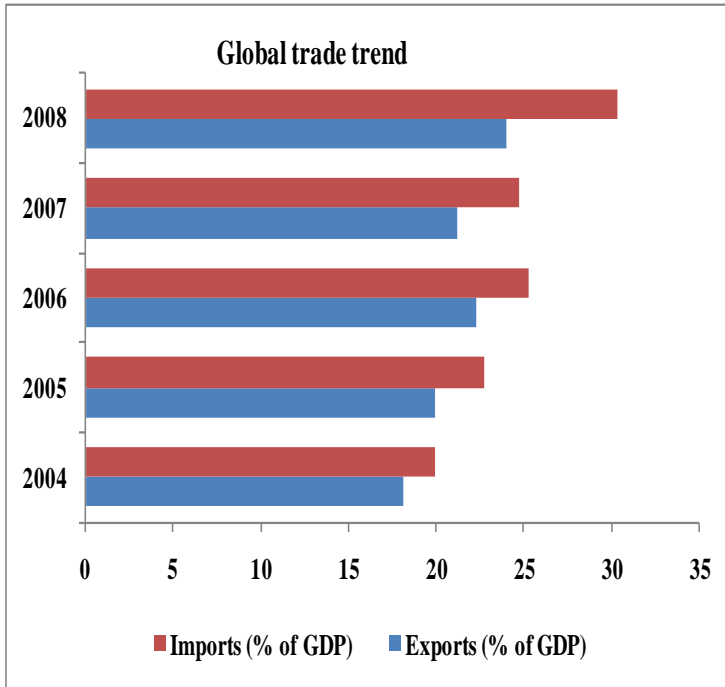
Increasing FDI Flows: India has emerged as a leading destination for foreign direct investments. Globally it stood 13th in receiving FDIs in 2008. India attracted US\$41.55 billion of FDIs in 2008. The flow was modest considering other top countries in the FDI chart. The FDI flow more than doubled over the past three years. Total cumulative amount of FDI till July 2009 was US\$1.17 trillion. If India continues to deliver sound growth over the long term, overseas investors will pump money into the corporate sector. Further, a proactive government at the centre, which supports liberalization of the economy, should help accelerate FDI flows. The FDI investment outlook in India appears positive going forward.

India's FDI outflows are also modest. In 2008, total outward FDI flows were US\$17.86 billion. Given the growing influence of the private sector in the economy, Indian companies have increased their presence in global markets. As a result, overseas investments by Indian companies will increase over the near term.

Modest Foreign Currency Reserve: India's foreign exchange reserves improved to US\$251.98 billion at the end of March 2009 from US\$ 151.62 billion in 2005-06. With the Indian economy rebounding and foreign capital inflows increasing, we expect the foreign exchange reserve base to expand in the near-term.

India Passes Critical Point: The Indian economy registered 7.9% growth in Q3 2009 compared to 6.1% Q2 2009. Economic indicators such as higher industrial production, rebound in domestic demand, pick up in stock market and currency appreciation reflect that the Indian economy is poised for a strong recovery. These positive macro-economic indicators reflect the Indian economy has already fully recovered from the recession.





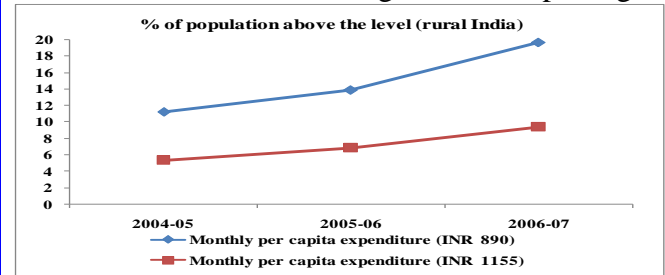
KEY THEMES:

Agriculture, rural economy, growing middle class, banking and financial services, infrastructure, and skilled labor and education are the key themes that will drive the Indian economy.

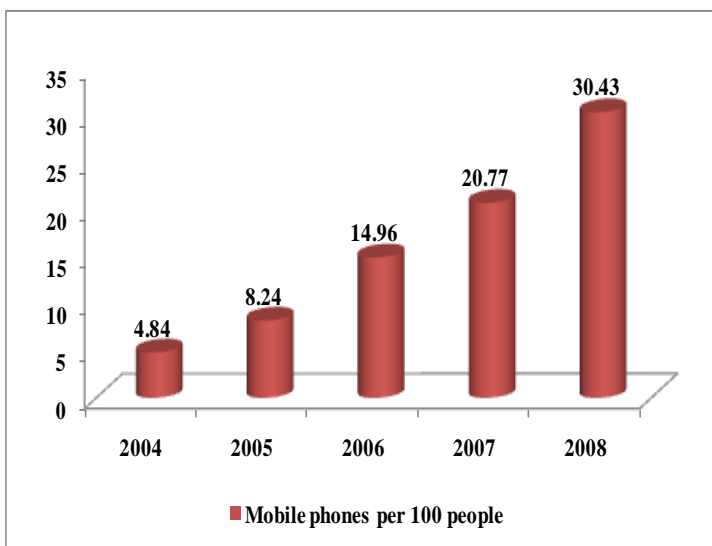
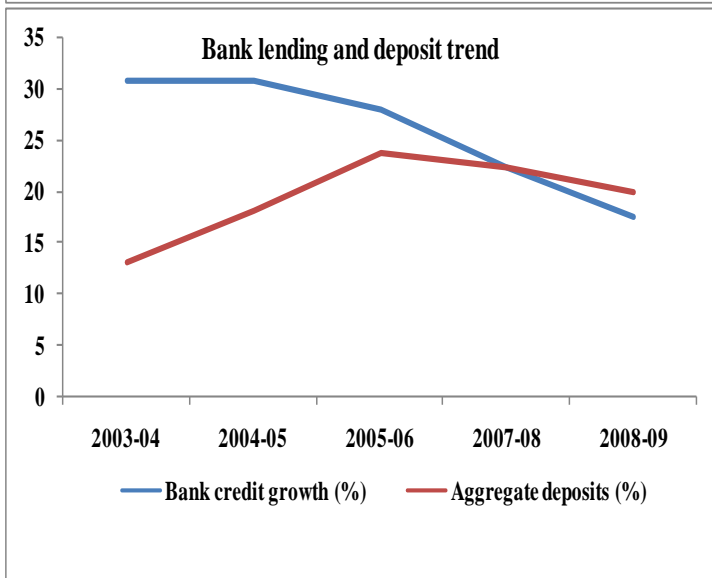
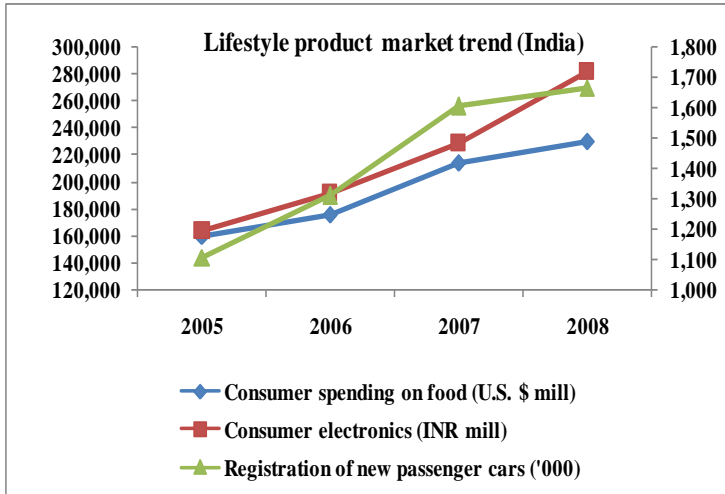
Agriculture: The agriculture sector represents one-fifth of the total GDP and employs about 60% of the total labor force. The rising population will lead to an increase in demand for agri products. Increasing per capital income will also drive the demand for agri products. Rising incomes will allow Indian consumers to spend more money on better food such as meat and processed dairy products. Poultry has been one of the fastest-growing sectors over the past few years, with production growing 53.9% y-o-y in 2004. Prices of agri-products will likely rise going forward. In the total private consumption, expenditure on food, beverages and tobacco represented 42.3% of total household spending in 2007-08.

Rural Economy: More than 70% of the total population lives in rural areas. Per capita income of the rural population is rising. Given the improving infrastructure in rural areas with the help of government-sponsored schemes, the rural economy is no more dependent only on agriculture. The spending power of rural consumers has increased recently. Hence, the rural economy, which is somewhat isolated from the global economy, provides cushion from many external shocks like the recent global financial crisis.

Rural areas currently account for more than half of Indian consumption. Rural markets will continue to remain vital for the Indian economy. Going forward 'Rural India' will also see higher consumption growth.



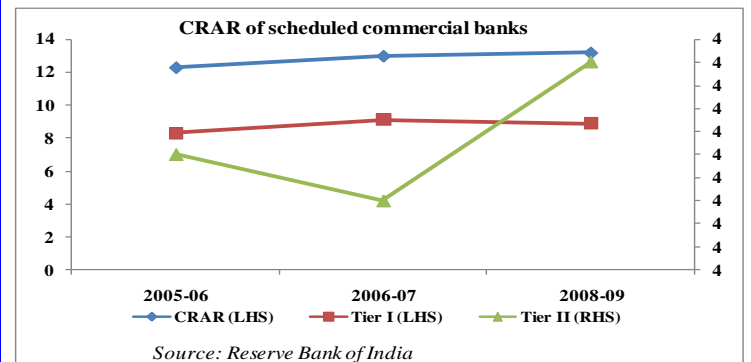
Growing Middle Class: Growing middle class consumers are playing a key role in India's consumer market. There is a large and growing middle class of more than 50 million Indians with disposable income ranging from INR 200,000 - INR 1,000,000 per year (\$4,200-\$21,000).



Increasing middle-class consumers will make India a leading consumer market in the world. Now, India ranks 12th in the global consumer market. Considering its strong economic growth potential, we expect per capita income to rise further going forward.

In India, there are around 31.5 million people paying income tax. Income growth will be the biggest driver of consumption. Food, tobacco and beverages represent 42% of consumer spending now, but this will decline over the long-term with transport and healthcare taking a higher share in total consumption. India has recently seen higher growth of sales in cars, mobile phones and consumer electronics.

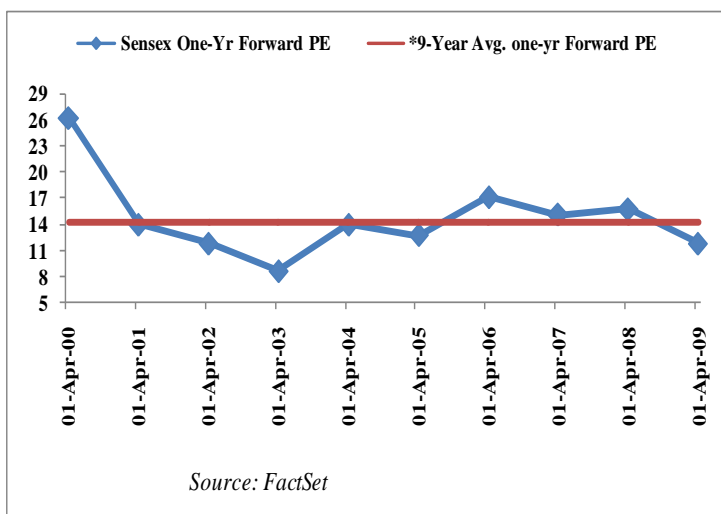
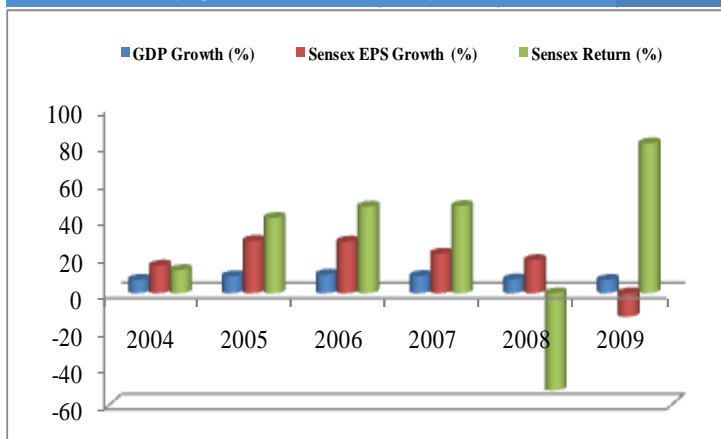
Banking and Financial Services: Banking is a key sector for India. Balance sheets of Indian banks are strong. Banking and financial services have played a crucial role in the recent economic momentum. Further, Indian banks were the least impacted by the recent global financial meltdown as its fundamentals were strong. The sound and efficient banking system protected the Indian economy from the recent global economic meltdown. Scheduled Commercial Banks' capital to risk-weighted assets ratio (CRAR), a measure of the capacity of the banking system to absorb unexpected losses, improved to 13.2% at the end of March 2009 from 13.0% at the end of March 2008, significantly above the stipulated minimum of 9.0%. Asset quality has been improving over the past few years as reflected in the declining *NPA-to-Advances* ratio. Despite the global economic recession, *net NPA to net advances* ratio rose a marginal 1.1% in 2008-09 from 1.0% in 2007-08. Significantly, gross NPA to gross advances ratio remained constant at 2.3%. Over the past five years, bank credit grew 25.9% on average and aggregate deposits expanded 19.4% on average.



Indicators of infrastructure capacity creation

Item	2006-07	2007-08	2008-09
Power capacity addition	6,853	9,263	3,454
Addition to refinery capacity petroleum (MT)	7	12	29
Road length upgraded (NHAI km)	636	1,683	2,203
Road works completed under PMGSY (km)	30,710	41,231	52,405
RKMs electrified (railways)	361	502	797
Addition to port capacity (MTPA)		27	24
Addition to switch capacity -telecom (000 lines)	9,603	7,159	14,393

Source: Economic survey report 2007-08 (India). Financial year ends on 31 March



Source: FactSet

Infrastructure: India achieved more than 8.7% annual GDP growth over the past five years. Infrastructure was the key driver behind this growth. To maintain the same growth momentum, India should spend more on infrastructure. The Eleventh Five Year Plan envisaged total investment in physical infrastructure (*electricity, railways, roads, ports, airports, irrigation, urban and rural water supply and sanitation*) to increase to 9% of GDP by the end of the plan period (2007-12) from around 5% of GDP in 2006-07. Taking this into consideration, investment in physical infrastructure alone has been estimated to be about U.S. \$500 billion (@ INR 40/US\$). While the central government is projected to fund 37.2% of the estimated amount, the state governments and private sector are expected to fund 32.8% and 30.1%, respectively. Roads, ports, airports, electricity and telecom are the main infrastructure investment areas. The Indian telecom industry continued to register significant growth in 2008-09. Indian telecom network, with about 414 million connections in February 2009, is the 3rd largest in the world. At the current pace, the target of 500 million connections by 2010 appears well within reach.

Skilled Labor and Education: Considering its current growth momentum and its growth potential, India needs a large pool of skilled manpower. It has a large educated population. Over the past five years, the Indian economy grew over 8.7% per annum. During this phase, skilled labor shortage was visible. As the Indian economy has already recovered from the recent slowdown, demand for skilled manpower will gain pace. The education sector will provide adequate support to produce quality human capital. Hence, the education sector will grow at a faster rate going forward.

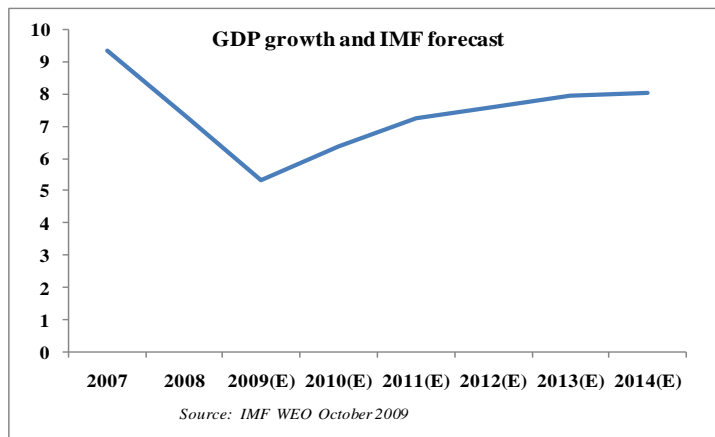
INVESTMENT RATIONALE:

The economic growth momentum during 2003-2007 was impressive with an average growth of 8.6%. In line with the economic growth momentum, Indian equities performed well. Aided by earnings growth and valuation multiple expansion, this bull phase gave robust returns to investors. However, due to the collapse of credit markets worldwide, the Sensex started to fall from January 2008. From its all-time peak of 20,873 points on January 8, 2008, the index declined to 8,160 points on March 09, 2009. In 2008, the Sensex was down 52%.

On January 8, 2008, the Sensex was valued at 25x its one-year forward earnings, a steep premium to its 9-year average one-year forward P/E of 14 (*Source, FactSet*). Valuations were high at that time. Hence, selling pressure and subsequent weak economic conditions pulled markets down.

After falling sharply, the Sensex started to bounce back from early March 2009. On March 09, 2009, the Sensex was valued at 10x its one-year forward earnings, a steep discount to 9-year average one-year forward P/E of 14. We believe the valuation at that stage was too cheap. As a result, investors showed interest in buying on dips. As economic conditions have shown improvement driven by government-sponsored stimulus packages, Indian equities have started gaining momentum.

Further, the clear electoral victory of the Congress-led United Progressive Alliance (UPA) gave a strong boost to investor sentiments. On May 18, 2009, the Sensex hit its upper circuit twice and jumped 2,110 points or 17% to 14,284. On October 30, 2009, the Sensex closed at 15, 896.28.



Key Fundamentals Remain Strong: India's macroeconomic fundamentals appear impressive. Inflation, foreign currency reserve, liquidity position, credit off-take growth and industrial production are all in a comfortable position. The Indian economy is largely driven by domestic demand. Considering its favorable demographic structure and growing middle class consumers, India is poised for higher growth in the long term.

Indian Corporate Performs Well; Earnings to Expand: Major emerging markets have seen a rapid run up in equities on strong support of impressive performance by companies.

In India, earnings momentum boosted valuations during 2003-07. In 2008, earnings growth slowed due to the global economic recession.

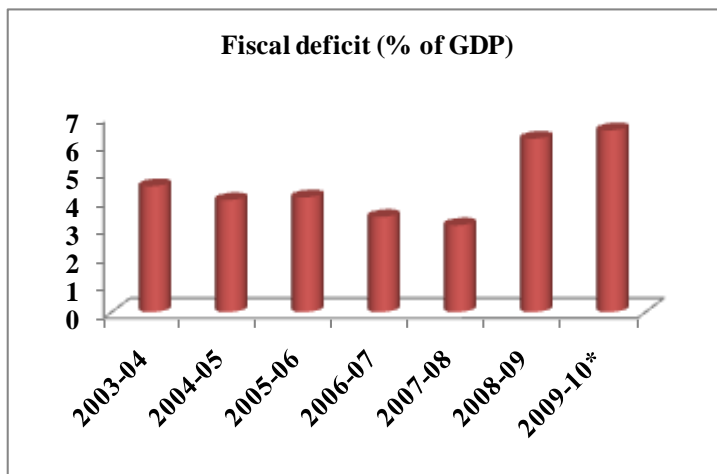
However, from Q3 2009 corporate earnings rebounded. Indian companies managed to make profits despite lower sales in Q3 2009. The rebound in corporate profits is a healthy sign for the market going forward. Profits expanded primarily because of input cost savings, which lifted margins. An analysis of standalone financials of close to 1,350 companies (*excluding banks and other financial institutions*), which announced September quarter numbers, showed that their total profits grew by a little over 50%, making a strong recovery from the decline seen in September 2008. However, sales declined 8.5% y-o-y in Q3 2009. Given the improving economic fundamentals, Indian companies could deliver impressive results in the coming years.

Medium-Term Valuations to Expand: The key drivers for the market for the next 3-12 months are as follows: the pace of global economic recovery, earnings performance of Indian companies, impact of weak monsoon on overall GDP growth, revival of the Indian economy and flow of funds to emerging markets. Major world economies are showing signs of improvement, slowly emerging from the worst global economic recession since the Great Depression in the 1930s. The recovery process is strong and its impact will be stronger on emerging economies such as India. As a result, global investors should have an increasing risk appetite, which could boost fund flows to emerging markets.

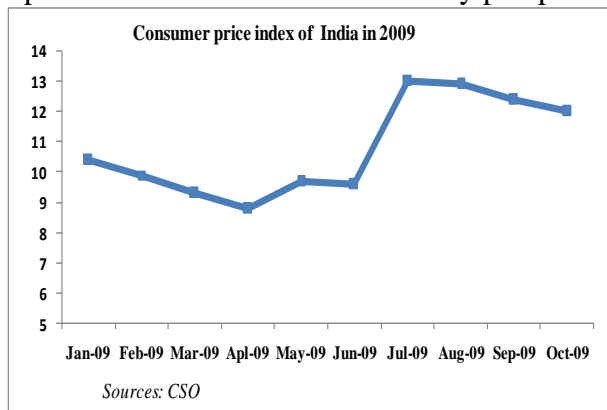
Indian Equities Outlook Buoyant: India's long-term economic growth appears robust. Asia's third-largest economy is set to continue its growth momentum on the following factors: strong domestic demand supported by large middle class consumers, favorable demographic structure with a growing share of youth population, lower dependence on global trade, strong resilient capacity and impressive contribution from private sectors. Considering these favorable trends, we believe Indian equities will continue to gain momentum over the long term.

RISK FACTOR:**Rising Fiscal Deficit May Affect Sovereign Rating:**

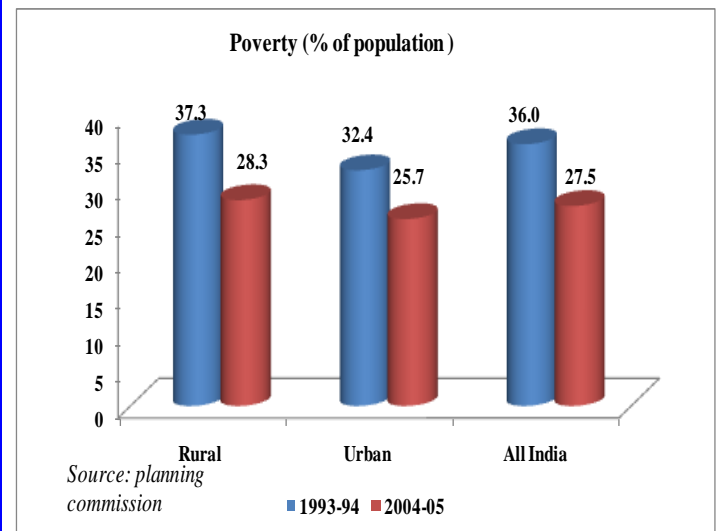
Rising fiscal deficit is a major concern for the economic health of India. The government forecast fiscal deficit of 5.5% of GDP for 2010-11 in its budget. Further, off-budget liabilities could increase the figure. If state budget deficits are included, the total fiscal deficit could cross 12% of GDP. Higher budget deficit could force the government to borrow more, which will adversely impact macro-economic fundamentals.



Rise in Inflation a Near-term Concern: Inflation will be a concern in the near-term. Inflation is set to rise, driven by an increase in cost of food items and primary articles. The weak monsoon, which provides about 70% of the rainfall in the country, could lead to a shortage of agricultural products. Inflationary pressure will push interest rates higher, which could restrict the credit growth in the economy. The slower credit growth will impact the current economic recovery prospects.



Higher Poverty: Although India managed higher economic growth during the past five years, the absolute number of people living below the poverty line is increasing. This dismal trend reflects inequality in the economy and is a threat to socio-economic development of India. Inclusive growth and economic prosperity is not equally divided. About 28.6% of people live below the national poverty line.



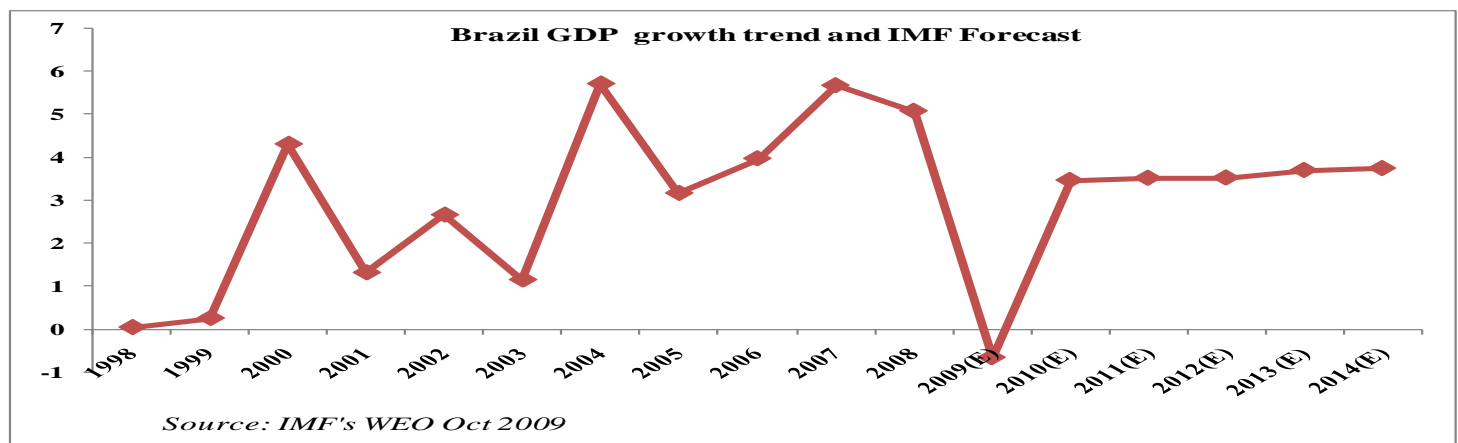
National Security Threat: India is facing some serious issues affecting its national security. Naxalism has spread to major parts of the country. Terrorism is another grave threat to India's national security. These problems have a wider impact on socio-economic lives of Indians.

India: Social Indicators 2008		India: Business Environment	
Population (billion)	1.13	Doing Business 2010 Rank (Out of 180 countries)	Rank
Population growth(%)	1.34	Doing business	133
Urban population (% of total)	29.10	Starting a business	169
Rural population (% of total)	71.90	Getting credit	30
Poverty (% of total population below national poverty line)	28.60	Protecting investors	41
Old age dependency ratio	4.90	Paying taxes	169
Life expectancy at birth (years)	69.89	Enforcing contracts	182
Literacy rate	66.00	Closing a business	138
<i>Source: World Bank, Human Development Report 2009: Some figures are of 2007</i>		Global Competitiveness Report 2009-10 (Out of 134 countries)	Rank
		Global competitiveness index	49
		Financial market sophistication	16
		Overall infrastructure quality	76
		<i>Source: Doing Business 2010: Global Competitiveness Report 2009-10</i>	

India: Key Economic Ratios	1978	1988	1998	2007	2008
GDP growth rate	5.7	9.6	6.2	9.1	7.1
Gross capital formation	20.5	23.6	22.6	38.7	39.2
Exports of goods and services/ GDP	6.3	6.1	11.2	21.2	24.0
Gross domestic savings/GDP	NA	NA	22.3	37.7	NA
External debt/ GDP	NA	NA	25.8	19.8	18.8
Total debt service(% of exports of goods, services and income)	13.8	29.6	8.7	NA	NA
Current account balance/GDP	NA	NA	0.1	-1.0	-3.0
Fiscal balance/GDP	NA	NA	-6.9	-2.8	-6.3
India: Structure of Economy					
(% of GDP)					
Agriculture	35.8	30.5	26.0	18.1	17.6
Industry	24.7	26.2	26.1	29.5	29.0
Services	39.6	43.4	47.9	52.4	53.4
Household final consumption expenditure	71.9	71.0	65.1	54.8	54.7
Govt final consumption expenditure	8.0	11.8	12.8	10.0	11.6
Gross capital formation	18.0	19.6	23.8	39.0	39.0
Net exports	1.1	-0.9	-1.7	-3.8	-5.3
<i>Source: World Bank</i>					

BRAZIL COUNTRY REPORT AT A GLANCE

Economic Rationale	Key Themes	Investment Rationale	Risk Factors
<p>The Brazilian economy recovered from recession in just two quarters. Low cost stimulus package and fiscal discipline means the economy is in better shape than other developing economies.</p> <p>Stable FDI flows - Brazil has the second largest net FDIs among all BRIC nations after China. Brazil's strong growth potential is the main driving factor for the FDI inflows.</p> <p>Brazil's vast natural reserves are economic assets. Brazil has large reserve of oil and natural gas. Brazil is the ninth largest producer of steel in the world. Brazil had 12.6 billion barrels of proven oil reserves in 2009, the second-largest in South America after Venezuela. Brazil had 12.9 trillion cubic feet (Tcf) of proven natural gas reserves in 2009.</p> <p>Brazil's exports as a percentage of GDP is the lowest among BRIC nations. Lower dependence on exports means its economy is better positioned to face external shocks.</p> <p>FIFA World Cup and 2016 Olympics to improve Brazil's infrastructure.</p>	<p>Agriculture is a key sector as it employs 1/4 th of the workforce. It also forms a substantial portion of Brazil's exports. Agricultural product prices will surge in the near term in global markets.</p> <p>Electricity is a major sector. Brazil is the largest Latin American electricity market. Hydroelectricity generation capacity meets 85% of its electricity demand. Conventional thermal generating sources provided only a small part of Brazil's electricity supply, contributing about 8% in 2007. Power consumption in Brazil is rising.</p> <p>Brazil's housing and commercial construction is set to receive a huge boost from the preparations for 2014 FIFA World Cup.</p> <p>Telecom industry contributes 6.5% of GDP and is expected to attract substantial foreign investment over the next few years.</p> <p>Infrastructure projects will get a boost due to the staging of FIFA World cup and Olympics.</p>	<p>Brazil's Bovespa Index was trading at 10.08x its reported earnings in October 2009, which represents a discount to the Bovespa's 10-year average of 11.62. Hence, Brazilian equities seem to be attractive at October 2009 levels. Further, economic growth prospects and earnings recovery will boost valuations. Equities will rise going forward taking cues from domestic economic news.</p> <p>Brazil's Bovespa has grown at a CAGR of 15.4% over the last 10 years. This growth rate is even higher than China's average growth rate of 13%. The Bovespa has continuously outperformed the Dow Jones, S&P and the FTSE 100 indices.</p> <p>The economy has already recovered from the recession. With the recovery prospects, foreign funds will continue to rise. Brazil's Bovespa rose above the 67,000 point mark, following good corporate results, and GDP growth outlook.</p>	<p>Brazil has a traditionally low savings and investment rate. Hence, over the long term, Brazil will have to raise its savings and investment ratios if growth is to meet the government's target of 5%.</p> <p>The Brazilian economy is excessively dependent on foreign investment. . However, the move could also undermine the credibility of the Brazilian government internationally as it had reiterated that no such tax will be imposed on FIIs.</p> <p>A 2% tax imposition on capital flows may turn away prospective investors. The tax imposed by the Brazilian government can be seen as a move to pacify local businesses whose exports were becoming less competitive due to the appreciation of the real.</p>



BRAZIL COUNTRY REPORT:**Quick Fundamentals (Brazilian Economy)**

GDP Size (US \$ Trillion)	1.61
GDP Growth	4.53%
GDP Growth (Last 5-Year Avg)	4.72%
Population (Million)	190
Population Growth (5-Year Avg)	1.12%
Revenue/GDP	20.40%
External Debt/GDP	17.80%
Exports/GDP	14.33%
Net FDI in 2007 (US \$ Billion)	34.50
Fiscal Balance (% of GDP)	-0.40

All Figures are of 2008: Source: World Bank, World Economic Outlook, Asian Development Bank

Population: Brazil is the most populous nation in Latin America. At the end of 2008, Brazil's total population stood at 189.9 million. During the previous three years, Brazil's population grew 2.1% annually. According to *World Population Prospects: The 2008 Revision* report by the United Nations Population Division, people in the 15-24 age group will represent 17.3% of Brazil's total population by 2010. People in the above-65 age group will represent 6.9% of total population by 2010. The older class population in Brazil is much lower than in China and Russia while it is more than in India. This ratio is forecast to increase to 22.5% of the total population by 2050. The higher percentage of young population in Brazil is expected to stimulate economic growth. The relatively low percentage of ageing population will place fewer burdens on the Brazilian economy compared to developed economies where people in the above-65 age group comprise over 20% of the population.

Political Structure: Brazil was under military rule from 1964 to 1985. Currently, Brazil's democratic political spectrum is dominated by four political parties – Workers Party, Brazilian Social Democratic Party, Brazilian Democratic Movement Party and Democrats. The president is deemed as Head of State as well as the government and can be elected for a maximum of two terms encompassing four years each.

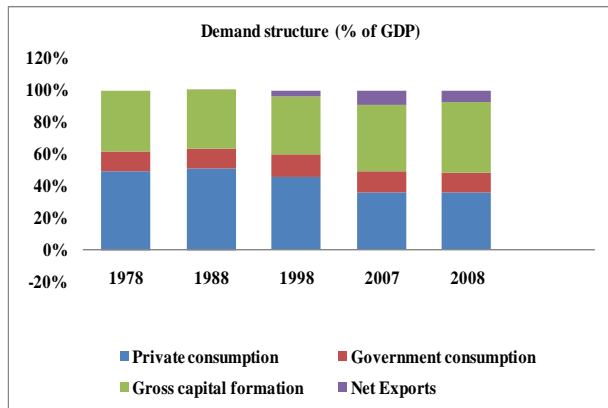
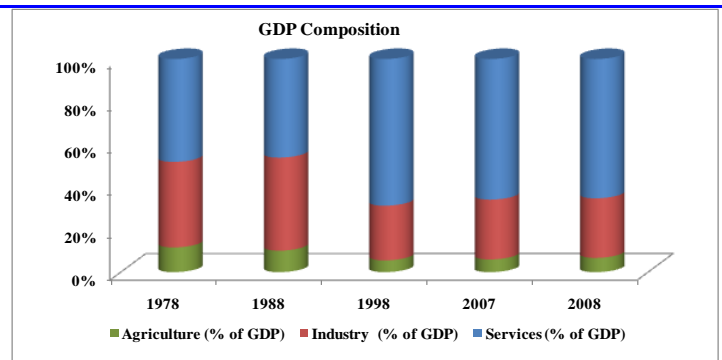
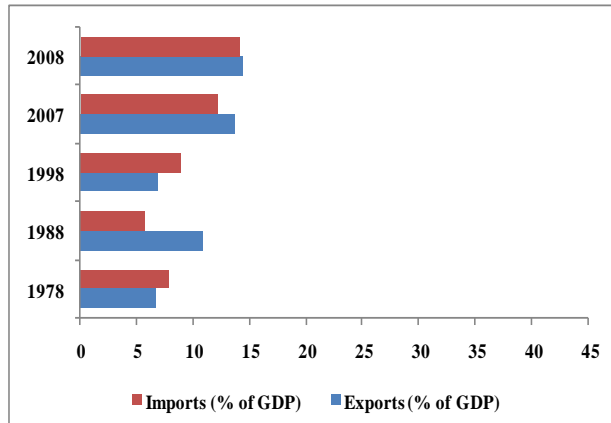
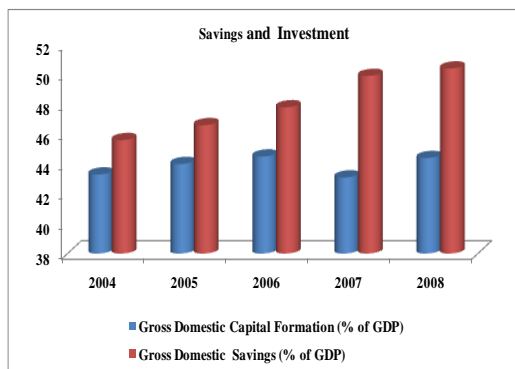
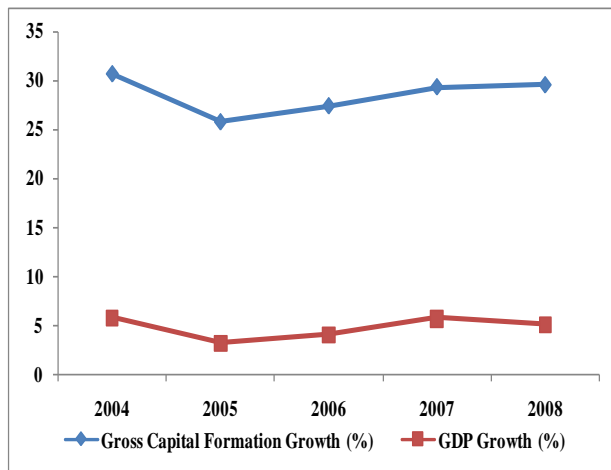
Currently, Luiz Inácio Lula da Silva, a founding member of the Worker's Party, is serving his second term as president after being re-elected in 2006.

The Worker's Party is a socialist political party formed in 1980 and has been ruling Brazil since 2002. The next general elections are scheduled to be held in October, 2010. Latest opinion polls indicate that Jose Serra of the Brazilian Social Democratic Party could be elected as the next President.

Policy Issues: Brazil has traditionally welcomed and is dependent upon foreign investment. As a developing economy, Brazil's domestic savings are insufficient to drive long-term growth and hence the country has opened doors to foreign investors. Brazil receives the highest foreign investment (\$45 billion of FY08 inflow) in Latin America and the third highest among BRIC nations (China – \$108 billion, Russia – \$70.3 billion and India – \$41.5 billion). The country also seeks to promote exports and has various free trade agreements with other Latin American countries.

Brazil's government undertook a sustained privatization drive through much of the 1980s as well as the 90s especially in the energy, telecom and transportation sectors. Foreign investment accounted for 48% of the revenue from privatization programs in the period 1990-2007.

Overall Economy: Brazil's economy has grown at an average annual rate of 4.5% in the period 1960-2008. However, Brazil has grown at a rate of only 3.2% since 1999 which is low compared to India (7.2%), China (9.8%) and Russia (6.9%). The low GDP growth rate since 1999 is mainly due to extremely tight monetary and fiscal policies adopted by successive governments. These tight policies were a result of various economic shocks suffered by Brazil since 1999 which led the governments to adopt a policy of stabilization. Since 1999, Brazil has adopted a discreet monetary policy targeted at keeping inflation in check. Over the years, Brazil has become less dependent on agriculture while contribution of the industrial and service sectors to GDP growth has increased.



ECONOMIC RATIONALE

Brazilian Economy – Least Dependent on Exports:

Brazil's exports as a percentage of GDP is the lowest among the BRIC nations– 13.5% in 2008 compared to 36.3% for China and 41.4% for Russia. The low dependence on exports as a means of value addition to GDP augurs well for Brazil as it indicates that the country is less dependent on other economies. This is also one of the major reasons why Brazil recovered from recession in just two quarters while Russia is still feeling the impact of the decline in overseas demand.

Brazil Posts Trade Surplus in FY 2009 Despite

Recession: In 2009, Brazil registered an accumulated trade surplus of \$24.62 billion, a slight y-o-y decline of 0.2%. Brazil's 2009 exports totaled \$152.25 billion while imports totaled \$127.63 billion. Brazil's trade surplus contrasted with Russia's 41.0% y-o-y trade surplus decline to \$88.0 billion in YTD October 2009. China registered a trade surplus of \$160.0 billion in YTD November 2009. The slight trade surplus decline in 2009 is due to the increase in imports as a result of currency changes. Brazil posted a trade surplus of \$394.0 million in Feb, 2010 after a deficit of \$166.0 million in January, 2010. However, we are impressed by Brazil's trade surplus despite the recessionary environment across the world.

Brazilian Economy Recovers from Recession: Brazil's economy expanded 2.0% in Q4 FY09 on a q-o-q basis. Brazil invested in large-scale public infrastructure projects and gave tax breaks to companies and individuals to recover from the global financial crisis. The positive GDP growth indicates Brazil's recession was short, spanning just two quarters of negative growth. Brazil was one of the last economies to fall into recession and one of the first to post a recovery. Brazil's economy and fiscal situation will be in a better shape compared to other BRIC nations in 2010 due to its relatively small stimulus package. China, India and Russia's economic stimulus packages were 13%, 8% and 8%, respectively of FY08 GDP, while Brazil's was a modest 0.2% of GDP. Brazil has also implemented fiscal discipline by postponing 6% of planned 2009 expenditure. Brazil's GDP declined only 0.2% in 2009 which was primarily a result of the excellent performance of the services sector, which grew 2.6%, offsetting the performance of the agriculture and industry sectors, which declined 5.2% and 5.5%, respectively. Brazil's Finance Ministry has forecasted FY10 GDP growth of 5.2%.

FIFA World Cup and 2016 Olympics to Improve Brazil's Infrastructure: Rio de Janeiro's selection as host of the 2016 Olympics is expected to attract a wide range of investors in Brazil. The Brazilian stock market has surged substantially in FY09 after the country posted a relatively fast recovery from recession. Steel, mobile-phone, airline and media companies are expected to benefit from Olympics-related investments. Investors are expected to pump approximately BRL30 billion (US\$17.01 billion) in new spending over the next seven years, according to Brazil's Ministry of Sports. The Ministry also stated that, according to a preliminary estimate, the event could bring in up to BRL 90 billion (US\$51.27 billion), including indirect investments and other long-term impacts.

Stable FDI Flows:

BRIC FDI Flows 1990-2008 (%)				
	Brazil	Russia	China	India
FDI Inflow	16.54%	22.39%	48.37%	12.69%
FDI Outflow	16.59%	37.91%	30.84%	14.66%
Net FDI	16.50%	8.57%	63.98%	10.94%

Brazil has relatively stable FDI flows compared to other BRIC nations. It received the 2nd largest net FDI among all BRIC nations in the 1990-2008 period, after China.

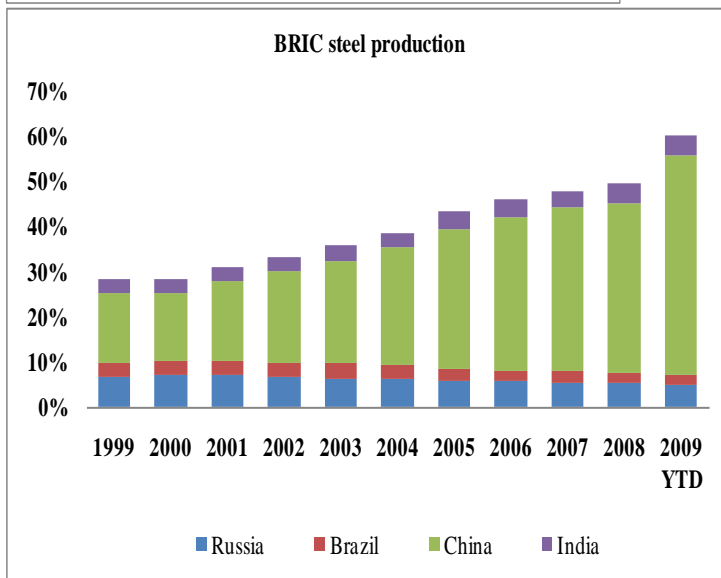
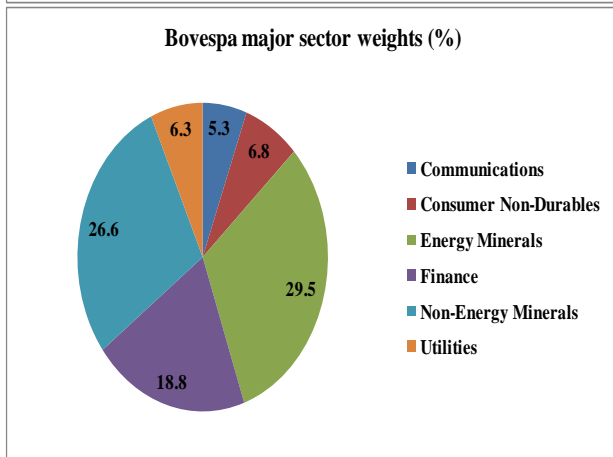
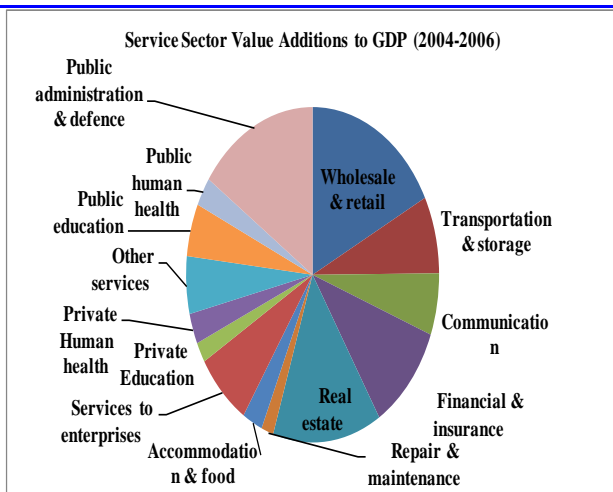
Brazil's Vast Natural Resource Reserve to Drive Substantial Revenue Growth: The discovery of vast new offshore oil deposits, estimated to contain 14-50 billion barrels of oil, could significantly help the Brazilian economic growth over the next few years. The Brazilian government has announced a series of new bills to make optimum use of the new oil bed discoveries. One of the bills proposes a reduction in the share of oil revenues that go to the states and municipalities closest to the fields. This is aimed at spreading the oil revenues more evenly across Brazil. State-owned oil and gas giant Petrobras will be the sole operator of the new oil reserves with a minimum 30% stake in all future projects in the pre-salt layer fields. Government has created a new state-owned company, Petrosal to manage the exploration and production in oil fields.

KEY THEMES:

Service sector, agriculture, steel, energy, infrastructure, and commodities, especially metal, are the key industries that will continue to drive the Brazilian economy.

Services: The Brazilian service sector accounts for 65.8% of the country's GDP. The Brazilian government has continued to liberalize its service sector, especially the telecommunications and financial services industries. The government supported privatization subsequent to 1996 lead to a large inflow of investments in the telecommunications, energy and transportation sectors in Brazil. The service sector was resilient in FY09 posting a growth of 2.6%.

Agriculture: Agriculture is one of the key sectors of the Brazilian economy. Agriculture contributes approximately 5.8% of GDP and forms 36% of Brazilian exports. In 2008, major contributors to Brazil's field agricultural production (60% of total agricultural production) were soybeans (26.1%), corn (14.0%), sugarcane (13.9%), coffee (7.1%) beans (4.8%) and rice (4.7%). Brazil is the world's largest producer of sugar, coffee and orange juice, the 2nd largest producer of soybeans and the 3rd largest producer of corn. Livestock accounts for 40% of Brazil's overall agricultural production. Brazilian agriculture industry employs a quarter of the country's total labor force.



Steel Industry: Brazil accounts for more than 70% of total steel production in Latin America and 3% of world production. It is the 9th largest producer of steel in the world producing 33.8 million tons in 2007 and 33.7 million tons in 2008 compared to 25.8 million tons in 1998. Brazil was also the 5th largest net exporter of steel in 2006 with 10.7 million tons. Domestic consumption of steel in 2008 was approximately 24 million tons. IBS (Brazilian Steel Institute) expects Brazil's steel consumption in 2009 to reach 18.7 million tons, 22.2% less than 2008.

However, IBS expects steel consumption to grow in 2010 through 2012, but does not expect production to reach 2008 levels.

Telecom Industry: Telecommunications companies have played an important role in Brazil's economic growth since the early 2000s. Penetration of fixed line and mobile telephony, as a percentage of homes, between 2001 and 2006 increased from 58.9% to 74.5%. Thirty-four thousand locations in Brazil currently have telephone services. In 2007, the telecommunications industry contributed approximately 6.5% of Brazil's GDP. Taxes collected from the industry represent nearly 40.3% of the net operating revenue of telecom companies — one of the largest tax burdens in the world. An investment of BRL\$11.9 billion was made in 2007, employing over 312,000 people.

Infrastructure: Brazil's construction industry has been hit by the global economic slowdown. However, the government's Growth Acceleration Program launched in 2007 is committed to supporting infrastructure projects. Brazil's housing and commercial construction is set to receive a huge boost from the preparations for 2014 FIFA World Cup, which is estimated to inject US\$43 billion into the infrastructure sector. The 2016 Olympics would also boost infrastructure spending.

Brazil Energy Overview	
Proven Oil Reserves (January 1, 2009E)	12.6 billion barrels
Oil Production (2008E)	2,396 thousand barrels per day
Oil Consumption (2008E)	2,520 thousand barrels per day
Crude Oil Distillation Capacity (2009E)	1,908 thousand barrels per day
Proven Natural Gas Reserves (January 1, 2009E)	12.9 trillion cubic feet
Natural Gas Production (2008E)	466 billion cubic feet
Natural Gas Consumption (2008E)	835 billion cubic feet
Recoverable Coal Reserves (2005E)	7,791 million short tons
Coal Production (2008E)	7.6 million short tons
Coal Consumption (2008E)	27.3 million short tons
Electricity Installed Capacity (2007E)	96.9 gigawatts
Electricity Production (2007E)	437 billion kilowatt hours
Electricity Consumption (2007E)	402 billion kilowatt hours
Total Energy Consumption (2006E)	9.6 quadrillion Btus
Total Per Capita Energy Consumption (2006E)	51.2 million Btus
<i>Source: Energy Information Administration</i>	

Oil: Brazil had 12.6 billion barrels of proven oil reserves in 2009, second-largest in South America after Venezuela, according to the Oil and Gas Journal. Between 1997 and 2006, the sector's contribution to Brazil's GDP jumped from 2.7% to 12%. Brazil ranks 15th in world's proven oil reserves and 14th in oil production (2006 statistics). In 2008, Brazil's daily production reached an average level of 2.4 million barrels of oil/day (compared to 2.1 million barrels/day in 2007). These volumes do not meet the Brazilian domestic market demand, as oil consumption has grown at a rate of 5% over the last 30 years. Brazil has one of the fastest-growing energy markets in the world and remains the largest industrial capacity in Latin America. State-owned Petrobras controls nearly all crude oil production in Brazil. Brazil's largest oil producing region is Rio de Janeiro, which contributes over 80% of total production. The Energy Information Administration (EIA) expects Brazil's FY10 oil production to reach 2.81 million barrels/day due to Petrobras bringing numerous projects on stream in early 2009. According to its strategic plan, Petrobras plans to increase its Brazilian refining capacity to 3.0 million barrels/day by 2020.

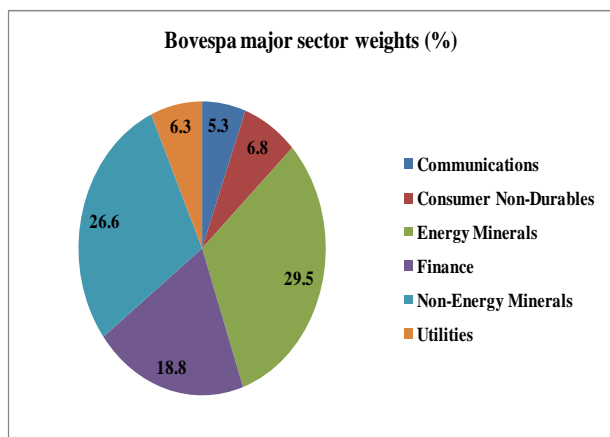
Ethanol: Brazil is the largest exporter of Ethanol in the world with 86,000 barrels/day in 2008. It produced 454,000 barrels/day of ethanol in 2008, up from 365,000 in 2007. According to Petrobras, ethanol accounts for more than 50% of current light vehicle fuel demand in Brazil, and the company expects this to increase to over 80% by 2020.

Electricity Sector: Brazil is the largest Latin American electricity market, with power consumption that is more than double the combined consumption of Argentina, Bolivia, Chile and Uruguay. The country has the largest water storage capacity in the world, being highly dependent on hydroelectricity generation capacity, which meets 85% of its electricity demand. However, dependence on hydroelectricity makes the country vulnerable to power shortages during droughts. Conventional thermal generating sources provided only a small part of Brazil's electricity supply, contributing about 8% in 2007. Natural gas contributed 45% of Brazil's conventional thermal power generation in 2007 followed by petroleum products (34%) and coal (17%). Brazil's residential sector consumes 40% of electricity output followed by the industrial sector with 25%. Brazil has two nuclear power plants, the 630-megawatt (MW) Angra-1 and the 1,350-MW Angra-2. State-owned Eletronuclear, a subsidiary of Eletrobras, operates both plants. Eletronuclear plans to build four new nuclear power plants by 2030 to meet growing Brazilian electricity demand.

Natural Gas: Brazil had 12.9 trillion cubic feet (Tcf) of proven natural gas reserves in 2009. Natural gas consumption is a small part of the country's overall energy mix, constituting a mere 7% of total energy consumption in 2006. However, natural gas demand is rising with Brazil consuming 835 Bcf in 2008, up from 701 Bcf in 2007.

INVESTMENT RATIONALE:**Brazilian Stocks Continue to Rise on Positive**

Economic Outlook: In early January 2010, Brazil's Bovespa rose above the 70,000 point mark (*the first time since June 2008*), on the back of good corporate results, record low interest rates, continued rise in commodity prices and government stimulus plan. Bovespa is now close to its all-time high of 73,000 which it reached in May 2008. Bovespa is currently the 4th largest in the world in terms of market capitalization. Earlier in the year, the Brazilian stock market saw the \$8 billion IPO of Spain's Banco Santander, the world's largest in 2009. The Brazilian Bovespa appreciated 82.7% in 2009. Brazil's GDP grew 1.9% in Q2 FY09 followed by a 9% growth in Q3 FY09. FIIs have invested approximately \$17 billion in Brazilian equities in YTD 2009. The positive GDP growth outlook by the Brazilian Finance Ministry and the country's Central bank should help attract more FIIs. Additionally, Brazil's recent success in leading the emerging market recovery from the recession should make the country a favorable destination for investors who wish to divert their investments from developed markets towards emerging markets.



Bovespa Posts Excellent Historical Returns: Brazil's Bovespa has grown at a CAGR of 15.4% over the last 10 years. This is even higher than China's average growth rate of 13%. Bovespa has been consistently outperforming the Dow Jones, S&P and the FTSE 100 indices recently. It rose from 13,874 in 1999 to 68,588 in 2009.

Leadership in Commodities and Metals Production:

The rally in commodity prices benefited Brazil substantially. Income and infrastructure growth in emerging as well as developing economies should sustain the demand for commodities including metals. Brazil is the number one producer of sugar, beef and coffee and the second biggest producer of soybean, corn and poultry. In metals, Brazil is the number one producer of quartz and niobium and the second largest producer of iron ore and bauxite. It is also the largest exporter of Ethanol.

Bovespa Trading at a Discount to its 10-Year Valuation History:

Brazil's Bovespa Index was trading at 11x its reported earnings in December 31, 2009, at a slight discount to its 10-year average of 11.62. Considering the country's growth prospects, Brazilian equities seem to be attractive at 2009 end levels.

RISK FACTORS:

Brazil Imposes 2% Tax on Capital Inflows: Brazil imposed a 2% tax on foreign investment in equities and fixed income instruments from October 2009. Foreign direct investment in the economy will not be subject to the tax. The 2% tax is expected to slow the appreciation of Brazil's real, which gained more than 35% against the U.S. dollar in 2009. The 2% tax was implemented despite the government reiterating throughout 2009 that no such tax would be imposed. The tax imposed by the Brazilian government can be seen as a move to pacify local businesses whose exports were becoming less competitive due to the appreciation of the real. However, the move could undermine the credibility of the Brazilian government internationally as it had reiterated that no such tax will be imposed on FIIs.

Brazil Has a Traditionally Low Investment Rate:

Since 1999, Brazilian domestic investment averaged a mere 17.5% of GDP compared to China's 40%. This is one of the major reasons why Brazil's GDP has grown at a modest 3.3% from 1999, much lower than other BRIC nations. Investment rate increased to 19%, the highest since 2000. However, it was still much low compared to the 41.8% investment rate of developing economies in Asia and the international average of 24%. Hence, over the long term, Brazil will have to raise its investment rates if GDP growth has to meet the government's growth target of 5%.

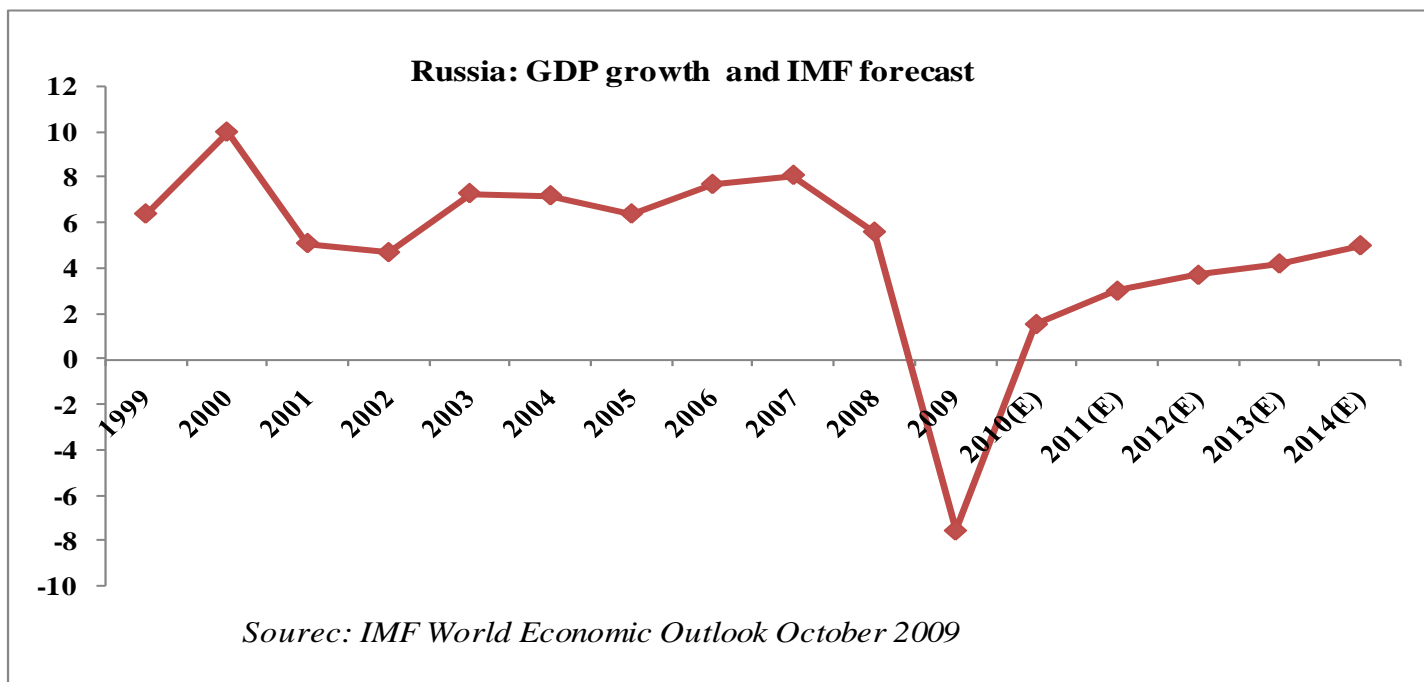
Brazil: Social Indicators 2008		Brazil: Business Environment	
Population (million)	190.1	Doing Business 2010 Rank (Out of 180 countries)	Rank
Population growth(%)	2.04	Doing business	129
Urban population (% of total)	74.80	Starting a business	126
Rural population (% of total)	25.20	Getting credit	87
Poverty (% of total population below national poverty line)	18.57	Protecting investors	73
Old age dependency ratio	10.20	Paying taxes	150
Life expectancy at birth (years)	72.5	Enforcing contracts	100
Literarcy rate	90.00	Closing a business	131
<i>Source: World Bank, Human Development Report 2009: Some figures are of 2007</i>		Global Competitiveness Report 2009-10 (Out of 134 countries)	Rank
		Global competitiveness index	29
		Financial market sophistication	78
		Overall infrastructure quality	66
		<i>Source: Doing Business 2010: Global Competitiveness Report 2009-10</i>	

Brazil: Key Economic Ratios	1978	1988	1998	2007	2008
GDP growth rate	3.2	-0.1	0.0	5.7	5.1
Gross capital formation	23.0	22.7	17.0	17.7	18.9
Exports of goods and services/ GDP	6.7	10.9	6.9	13.7	14.3
External debt/ GDP	27.1	35.5	28.6	17.8	NA
Total debt service(% of exports of goods, services and income)	58.1	45.7	79.5	27.8	NA
Current account balance/GDP	NA	1.2	-4.0	0.1	-1.8
Fiscal balance/GDP	NA	NA	-1.9	-1.5	-2.3

Brazil: Structure of Economy					
(% of GDP)					
Agriculture	11.6	10.1	5.5	6.0	6.7
Industry	40.1	43.6	25.7	28.1	28.0
Services	48.3	46.2	68.8	66.0	65.3
Household final consumption expenditure	26.7	26.8	27.6	28.3	29.8
Govt final consumption expenditure	27.1	26.6	26.7	27.0	28.5
Gross capital formation	24.1	23.9	25.8	28.1	32.0
Net exports	21.9	22.7	19.9	16.6	9.7

RUSSIA COUNTRY REPORT AT A GLANCE

Economic Rationale	Key Theme	Investment Rationale	Risk Factor
<p>The Russian economy has grown since 1999. Over the past five years, it expanded more than 7.5% on an average.</p> <p>Since 2003 consumer demand and investment outpaced the economic growth. Private consumption rose at 11.3% in 2008. Fixed investments expanded 22.4% in 2008. Retail trade growth was 13% in 2008. Russia is the world's largest energy exporter. Given the recovery in the global economy, Russia is all set to benefit from oil price rise. Russia is the world's second-largest oil exporter and largest exporter of natural gas.</p> <p>Russia is witnessing higher FDI inflows. In 2008, FDI inflows were US\$ 70.32 billion, an increase of 27.7% from 2007. Russia's strong foreign currency exchange reserves cushion the economy from any external shocks. This is a positive signal for an economy like Russia which heavily depends on oil and gas.</p> <p>The Russian economy continued to post fiscal balance till 2008.</p>	<p>Oil and gas is a key sector for the economy. Energy, including oil and gas, represents 67.7% of total exports.</p> <p>Infrastructure spending is strong and will continue to be robust in Russia. The Russian government is committed to spending US\$400 billion by 2015 on 302 projects.</p> <p>Robust performance of the energy sector, low-income tax and favorable government initiatives supported consumption boom in Russia.</p> <p>Household consumption expenditure also rose more than 10% annually over 2004-08.</p> <p>Russia is technologically advanced. Apart from oil and gas, critical technology is also used in aerospace, aviation, shipbuilding, automotive, and construction sectors.</p>	<p>After the prolonged economic slump due to the global economic recession, the Russian economy is near stabilization driven by higher commodity prices and the government's socially-oriented stimulus program</p> <p>Both economy and earnings will recover in the near term. Oil prices have almost doubled since February 2009, lifting earnings outlook for the world's biggest energy exporter. Major companies are set to report higher earnings results.</p> <p>Following an early economic recovery in emerging markets, foreign investors are increasing holdings in the fast-growing economies. Russian markets will receive more foreign fund flows in the near term.</p>	<p>Any volatility in oil and gas prices in the international level has direct impact on the economy. As energy represents more than 67% of total exports, any slowdown in overseas markets cause economic downturn in the domestic economy</p> <p>The share of old age population (65 years above) in the total population is quite significant. The share of old age population (more than 65 age) will be 12.9% by 2010. It will rise to 23.4% of the total population by 2050.</p> <p>Corruption is rampant in Russia. Transparency International's Corruption Perceptions Index (CPI) put Russia in 146th place. Last year it was in 147th place.</p>



RUSSIA COUNTRY REPORT:**Quick Fundamentals (Russian Economy)**

GDP Size (US \$ Trillion)	1.61
GDP Growth	7.3%
GDP Growth (Last 5-Year Avg)	7.3%
Population (Million)	141.80
Population Growth(5-Year Avg)	-0.2%
Revenue/GDP	31.6%
External Debt/GDP	28.9%
Exports/GDP	33.4%
FDI Inflows(U.S. \$ Billion)	70.32
Fiscal Balance (% of GDP)	3.8%

All Figures are of 2008: Source: World Bank,

Population: The population of Russia has been declining. Over the past five years, Russia's population contracted at 0.40% per annum. In 2008, total population stood at 141.80 million. The share of old age population (65 years above) in total population is quite significant. According to *World Population Prospects: The 2008 Revision* report by United Nations Population Division, by 2010, people in the age group of 15-64 will represent 72.1% of the total population and people above 65 years old 12.9%. The share of old age population is expected to rise to 21.5% of the total population by 2050.

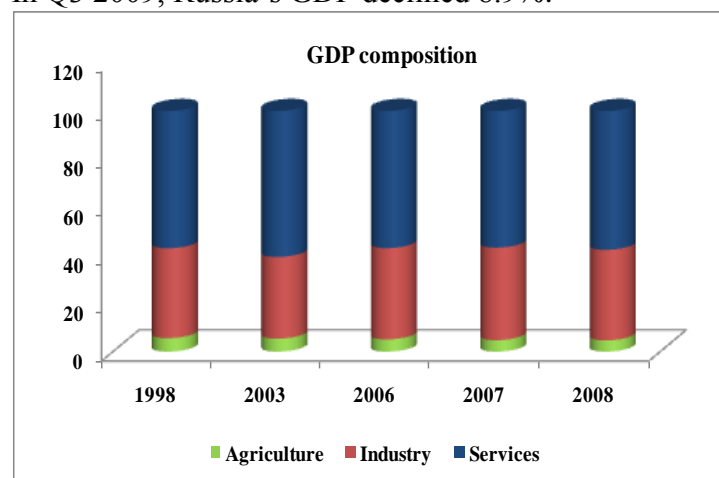
Political Structure: Like the Soviet Union before, Russia is a collection of diverse territories at different stages of development. Boris Yeltsin won the first democratic presidential election in June 1991 and was re-elected in July 1996. Powers of the executives were greatly increased by a new constitution adopted in 1993. The 1999 and 2003 parliamentary elections increased the influence of pro-Kremlin political forces, easing the passage of reform legislation. Vladimir Putin was elected in March 2000 and re-elected to a second term in March 2004. His loyal ally, Dmitry Medvedev won the presidential election in March 2008 and took over in May 2008.

Policy Issues: Following the government's continuous initiatives, reforms accelerated in tax, bank, labor, and land code. As a result, foreign direct investment in the country increased over 200% between 2005 and 2007. Diversifying the economy, which is heavily dependent on commodities, is the main near-term policy challenge.

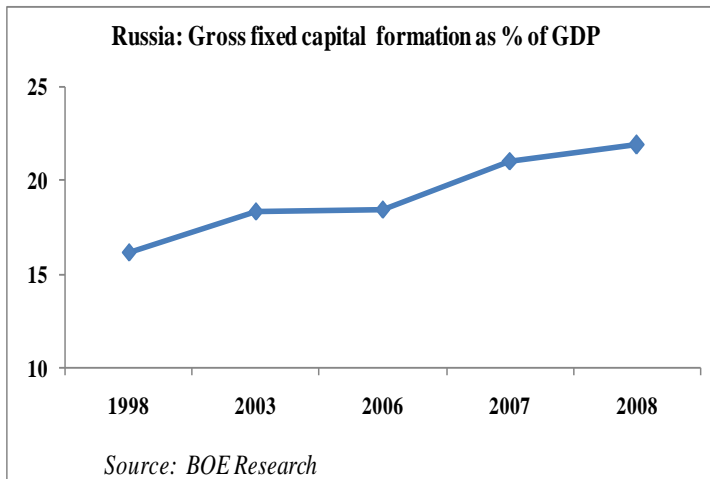
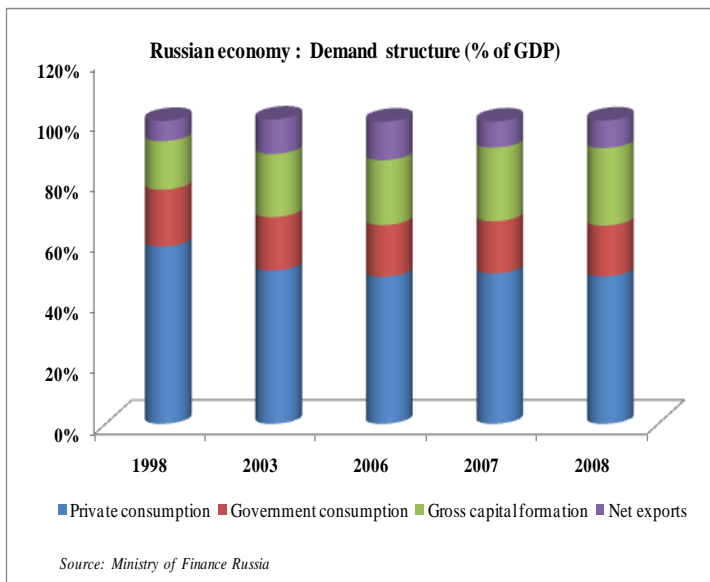
Overall Economy: The Russian economy is dominated by the energy sector. Crude oil exports represent the largest share of Russian exports. More than a quarter of the world's natural gas reserves are located in the Russian territory. In 2007, Russia was the 2nd largest producer of oil and the largest producer of gas. It is also the world's largest exporter of natural gas, the 2nd largest oil exporter and 3rd largest energy consumer. Although Russia heavily depends on oil and gas, it is well prepared for periods of declining oil prices. Its sizeable foreign exchange reserves form a cushion against possible external shocks. Since 2003, consumer demand and investments have accounted for much of the country's growth, delivering 12% and 10% average annual gains.

ECONOMIC RATIONALE:

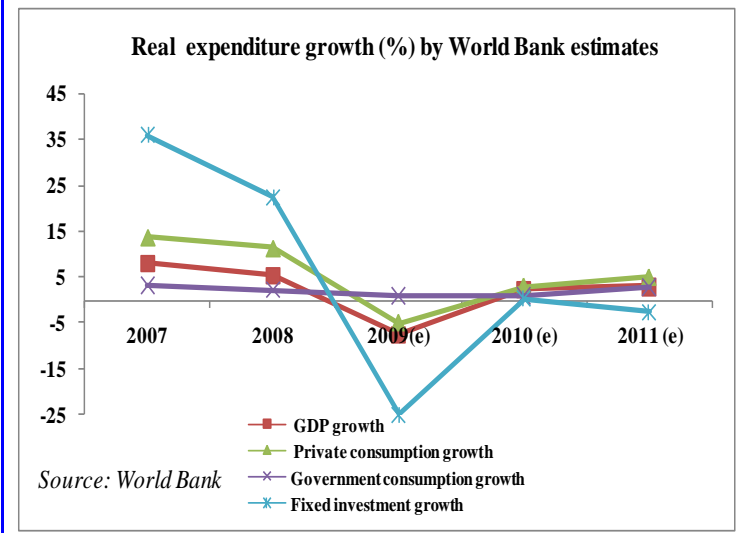
Strong Economic Growth: The Russian economy expanded more than 7.5% on average annually over the past five years. Hurt by the recent global recession, this economy contracted for the first three quarters in 2009. In Q3 2009, Russia's GDP declined 8.9%.



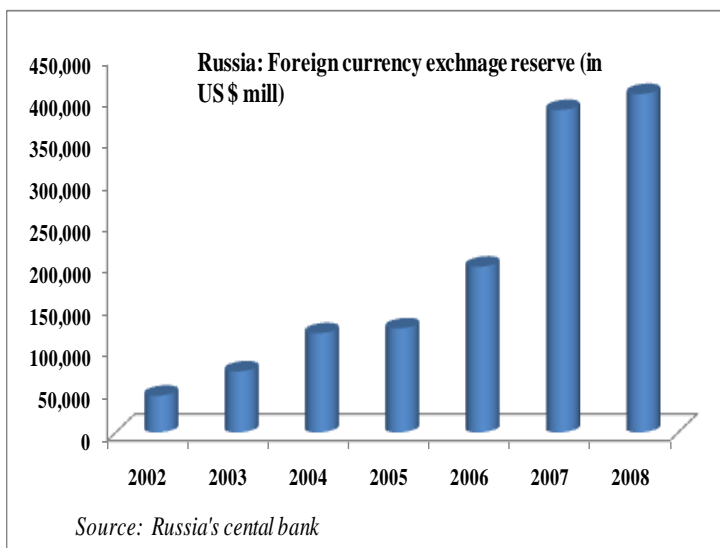
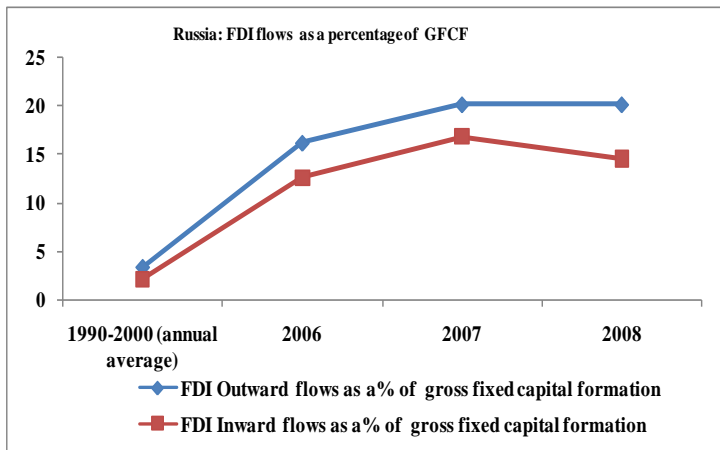
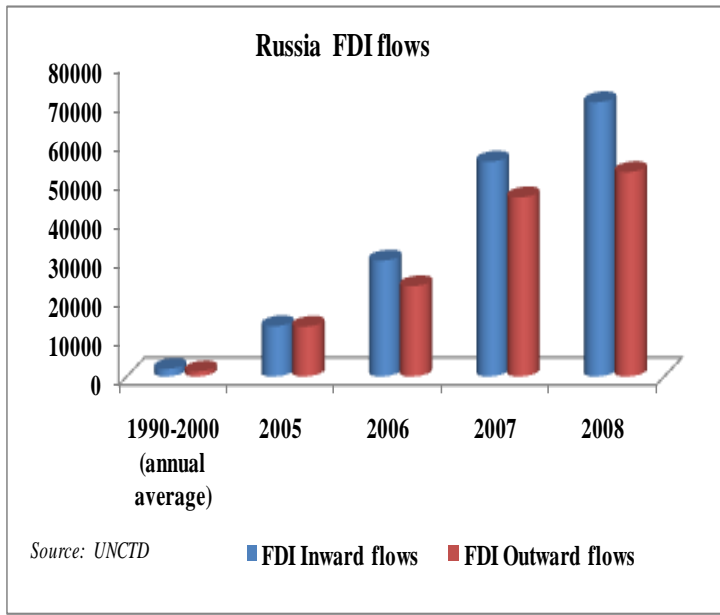
Share of the agriculture sector in GDP is decreasing. The agriculture sector's share, which was 5.6% in 1998, fell to 4.7% in 2008. The services sector represents more than half of GDP.



Demand Structure of GDP: The Russian economy is primarily driven by domestic demand. Household spending represented about half of the GDP in 2008; Government consumption accounted for 16.7%. Gross capital formation's share rose to 25.5% in 2008 from 16% in 1998. Thus, investment in the economy is constantly rising. Both private consumption and fixed investments are growing at high rates. Private consumption grew at 11.3% and fixed investments rose 22.4% in 2008. The Russian economy is highly dependent on oil and gas. About 30% of Russian gross domestic product comes from oil and gas.



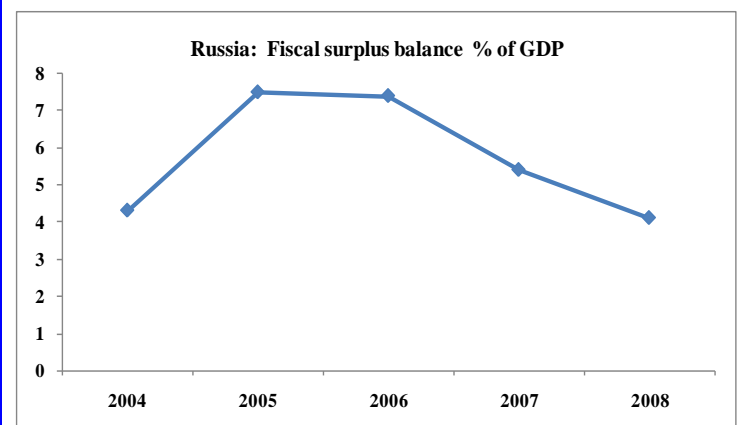
Exports and Imports: Russia's exports and imports, including goods and services, accounted for 33.4% and 22.5% of GDP, respectively. Oil, gas, timber and metals are the prime export items. Russia is the world's 2nd largest oil exporter and largest natural gas exporter. Oil accounts for 34.5% of Russian exports and gas 12%. Timber is another major export item; Russia exports about 30% of the 186 million cubic tons of timber it logs annually. In 2008, Russia's share in world merchandise export was 1.2% and import 1.8%. Energy, including oil and gas, accounted for 67.7% of exports to countries outside the region. Machinery and other equipment made up 54.3% of imports from those countries.

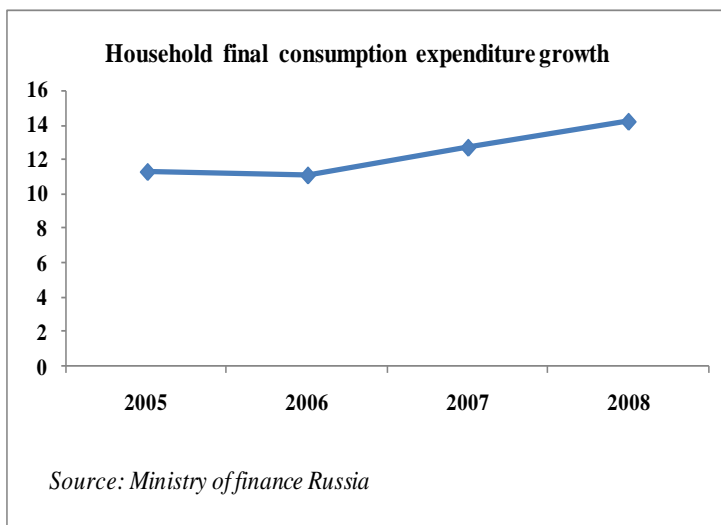
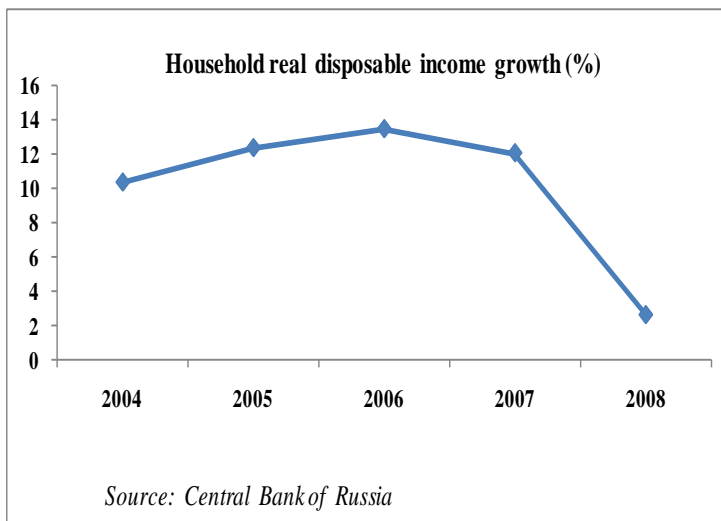
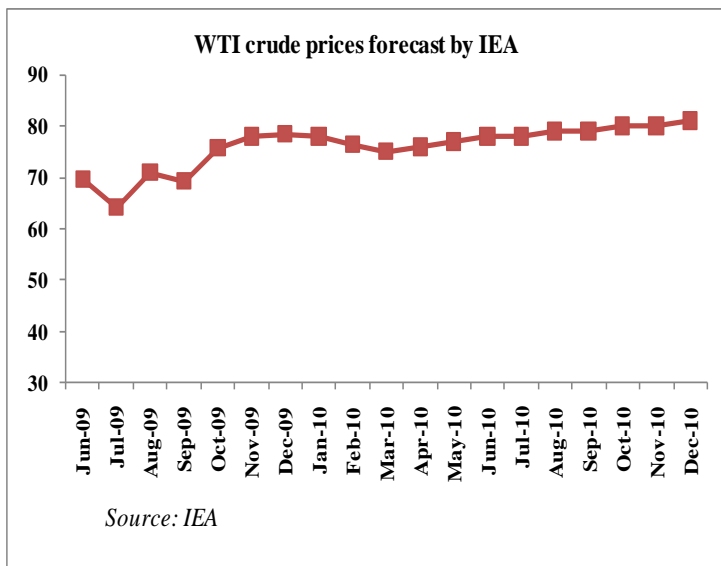


Sound FDI Flows: Foreign Direct Investments in Russia are increasing. In 2008, FDI inflows were US\$ 70.32 billion, an increase of 27.7% from 2007. Higher economic growth is the prime factor for FDI inflows. Russia's total outflows were US\$52.39 billion in 2008, a rise of 14% from 2007. Higher FDI outflows were due to strong overseas expansion of Russian companies driven by higher profit margins, increased growth potential, and access to technological and management know-how. Both FDI outflows and inflows will gain pace going forward.

Strong Foreign Exchange Reserves Cushion the Economy from External Shocks: Russia has a strong foreign exchange reserve base, a positive factor for the economy. Although the heavy dependency of Russia on oil and gas is a source of concern, the Russian economy is relatively well prepared for periods of declining oil prices. The country's strong foreign exchange reserves form a cushion against possible external shocks. According to the International Monetary Fund (IMF), Russia had foreign currency reserves of US\$368.22 billion as of September 30, 2009.

Fiscal Surplus Balance: The Russian economy continued to post fiscal balance in 2008. This is another sign of strength of the economy. Fiscal balance as a percentage of GDP stood at 5.4% in 2007 and 4.1% in 2008. As Russia derives a major share of revenue from oil and gas, high oil prices helped it achieve fiscal balance. Following the recent global economic recession, the government expects a budget deficit of 8.6% of GDP for 2009. The government plans to reduce this deficit to 3% by 2012, based on a conservative oil price forecast of US\$55-US\$57/bbl and tax revenue of 15.5% of GDP.



**KEY THEMES:**

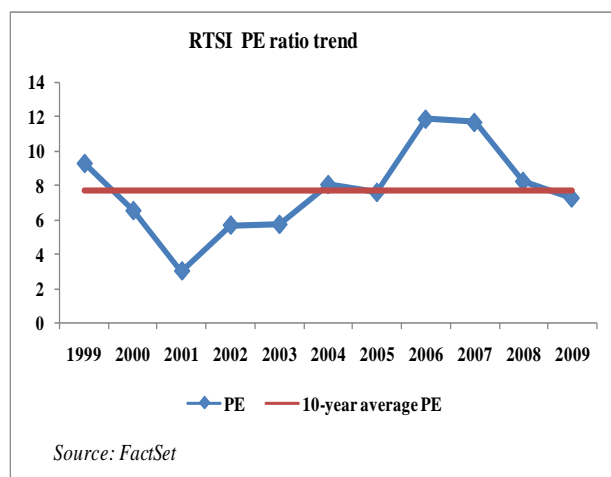
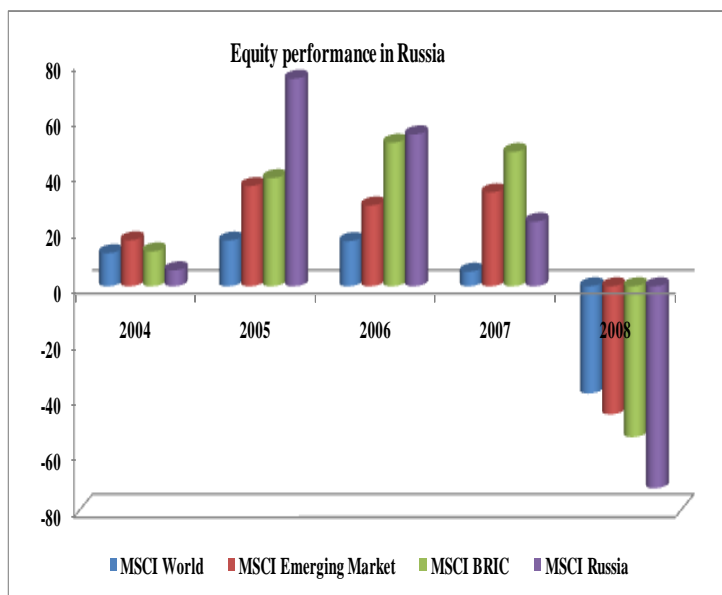
Key themes that will reshape the Russian economy are oil and gas, infrastructure, and consumption boom.

Oil and Gas: It is a key sector in the Russian economy. Russia is the world's largest energy exporter. It has the 2nd largest coal reserves in the world and is the 3rd largest energy consumer. As the global economic outlook is improving, oil and gas demand is set to rise which in turn will drive prices higher. This should benefit the Russian economy. According to the *International Energy Agency (IEA)*, monthly average prices of West Texas Intermediate (WTI) crude oil will rise to about US\$81 per barrel by December 2010.

Infrastructure: It is a growing sector in Russia. Infrastructure spending is strong and will continue to be robust. The focus will be on improving the energy distribution network as well as the electricity and road projects. Real estate is also booming. Russia, with its sizeable foreign exchange reserve and surplus budget, is well placed to fund infrastructure projects. The Russian government is committed to spending US\$400 billion by 2015 on 302 projects and US\$300 billion on the railways system by 2030.

Consumption Boom in Russia: The Russian economy has been posting high growth rates in the recent years. Growth was driven by domestic consumption. Household real disposable income registered strong growth over the past five years. Robust performance of the energy sector, low income tax and favorable government initiatives supported the consumption boom in Russia. From 2004 to 2007, household real disposable income grew more than 10% on an average. Its growth slowed down to 2.7% in 2008 due to the recent global economic recession.





Household consumption expenditure also rose more than 10% annually over 2004-08. As the Russian economy is near stabilization, consumption will gain pace going forward. Consumer activity has contributed to dynamic growth in trade, retail, telecommunications and services following rising incomes.

Technologically Advanced Economy: Strong Russian scientific knowledge provides excellent opportunities for R&D partnerships with its research institutes and universities. In the oil and gas sector, Russia uses modern and advanced technology. Critical technology is also used in aerospace, aviation, shipbuilding, automotive, and construction sectors.

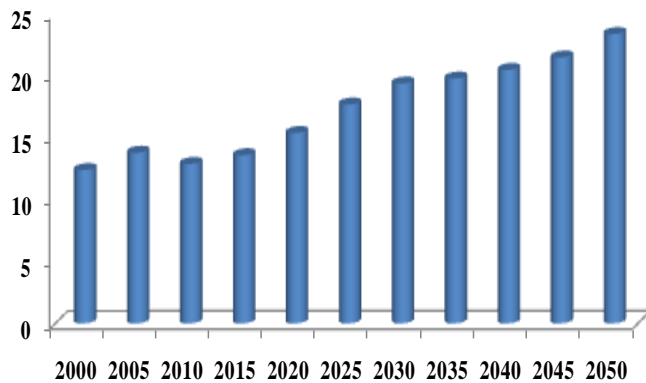
INVESTMENT RATIONALE:

Russian equities delivered impressive performance during 2003-2007. The MSCI Russia Index delivered an average annual return of 39.3% during 2003-07. Following the global financial market crisis in 2008, MSCI Russia index plummeted 72.2%. In 2009, MSCI Russia index jumped 85.2% as signs of economic recovery emerged.

Russian Economy at a Critical Point: After the prolonged economic slump due to the global economic recession, the Russian economy is near stabilization driven by higher commodity prices and the government's socially oriented stimulus program. Russia's output contracted a sharp 8.9% in Q3 2009. As global commodity prices have already started rebounding, the Russian economy should recover in the near term. According to the International Monetary Fund's (IMF) *World Economic Outlook, October 2009*, Russia is expected to grow 1.5% in 2010. In 2014, the Russian economy is expected to expand 5%.

Potential Valuation Multiple Expansion: Considering the expected economic rebound in the near-term, valuation of Russian equities are likely to rise. Both the economy and earnings should recover in the near-term. Oil prices have almost doubled since February 2009 lifting earnings outlook for the world's biggest energy exporter. Major companies are set to report higher earnings. At the end of 2009, the RTS Index traded at 7.3x its reported earnings, at a modest discount to its 10-year average P/E of 7.7 (Source: FactSet). Hence, Russian equities look attractive at the end of 2009 levels.

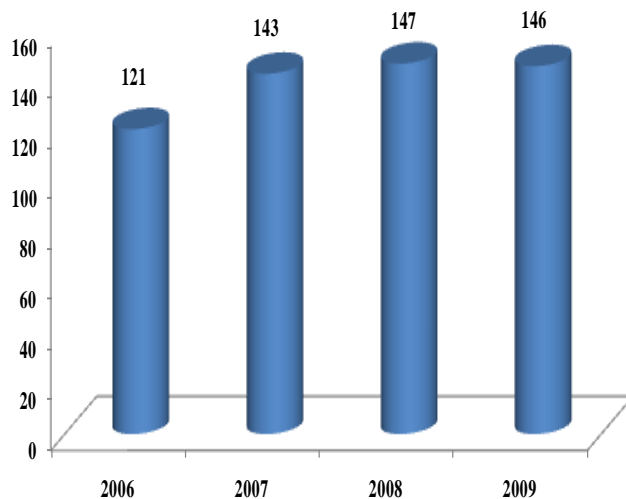
Russia's % of old age population



Source: UN Population

■ % of aged 65 or over

Corruption level in Russia (Rank on CPI)



Source: Transparency International

Foreign Fund Flows Expected to Rise: Following an early economic recovery in emerging markets, foreign investors are increasing holdings in the fast growing economies. Russian markets will receive more foreign fund flows in the near term.

RISK FACTOR:

Excessive Dependence on Oil and Gas: The Russian economy's excessive dependence on the oil and gas sector reflects the economy lacks diversification. Any volatility in oil and gas prices in the international level has direct impact on the economy. As energy represents more than 67% of total exports, any slowdown in overseas markets cause economic downturn in the domestic economy.

Ageing Population: The current population structure in Russia is unfavorable. The share of old age population (*above 65 years*) in the total population is quite significant. According to World Population Prospects: The 2008 revision report by United Nations Population Division, by 2010, people in the age group of 15-64 will represent 72.1% of the total population and people above 65 years 12.9%. The share of old age population will rise to 23.4% of the total population by 2050.

Higher Corruption Level in Russia: Corruption is rampant in Russia at both political and bureaucratic level. Corruption is a major hindrance in the economic growth of Russia. According to data from the Russian Interior Ministry, the average amount of bribe has increased 250% in the past year. According to Transparency International, a non-profitable organization, Corruption Perceptions Index (CPI), put Russia in 146th place in 2008. In 2007, it was placed in 147th place.

Russia: Social Indicators 2008		Russia: Business Environment	
Population (billion)	1.41	Doing Business 2010 Rank (Out of 180 countries)	Rank
Population growth(%)	-0.21	Doing business	120
Urban population (% of total)	73.00	Starting a business	106
Rural population (% of total)	27.00	Getting credit	87
Poverty (% of total population below national poverty line)	20.00	Protecting investors	93
Old age dependency ratio	23.40	Paying taxes	103
Life expectancy at birth (years)	67.85	Enforcing contracts	19
Literarcy rate	99.00	Closing a business	92
<i>Source: World Bank, Human Development Report 2009: Some figures are of 2007</i>		Global Competitiveness Report 2009-10 (Out of 134 countries)	
			Rank
		Global competitiveness index	63
		Financial market sophistication	92
		Overall infrastructure quality	86
		<i>Source: Doing Business 2010: Global Competitiveness Report 2009-10</i>	

Russia: Key Economic Ratios	1998	2003	2006	2007	2008
GDP growth rate	-5.3	7.3	7.4	8.1	7.3
Gross capital formation	20.5	23.6	22.6	38.7	39.2
Exports of goods and services/ GDP	31.2	35.1	33.7	30.5	33.4
Gross domestic savings/GDP	NA	NA	NA	NA	NA
External debt/ GDP	70.1	43.0	31.3	35.8	28.7
Total debt service(% of exports of goods, services and income)	12.0	11.7	13.8	9.1	13.0
Current account balance/GDP	0.1	8.2	9.4	5.9	6.1
Fiscal balance/GDP	-4.8	2.4	7.4	5.4	3.8
Russia: Structure of Economy					
(% of GDP)					
Agriculture	5.6	5.4	5.1	4.7	4.7
Industry	37.4	34.0	38.0	38.5	37.6
Services	57.0	60.7	57.0	56.8	57.7
Household final consumption expenditure	58.5	50.6	48.5	49.6	48.6
Govt final consumption expenditure	18.7	17.1	17.1	17.2	16.7
Gross capital formation	16.0	20.8	21.4	24.3	25.5
Net exports	6.7	11.3	12.7	8.6	9.1
<i>World Bank; Russian Federal State Statistics Services</i>					

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