

## Rocks on Shocks

5 March 2007

### Country recommendations

Country	Recommended weight	Benchmark weight	Relative Position
Taiwan	24	21	3
Korea	29.9	27.9	2
Indonesia	3.7	2.7	1
Philippines	1.8	0.8	1
Malaysia	4.4	4.4	0
China	16.2	16.2	0
Singapore	6.4	8.4	-2
Hong Kong	13.4	15.9	-2.5
Thailand	0.3	2.8	-2.5

Source: Macquarie Research, March 2007

### Sector recommendations

Sector	Recommended weight	Benchmark weight	Relative Position
Information Technology	24.6	21.6	3
Financials	23.8	21.8	2
Consumer	14	12	2
Telecommunications	9.7	8.7	1
Real Estate	7.5	7.5	0
Utilities	4.4	4.4	0
Industrials	9.9	11.9	-2
Materials	4.1	6.1	-2
Energy	3.9	5.9	-2

Source: Macquarie Research, March 2007

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## Don't panic

### Event

- Fears of overvaluation in China and some weaker US data have seen Asian equity markets pullback in recent days.

### Impact

- Economic fundamentals in China remain solid and we see policy risk as exaggerated. Plain and simple fear of overvaluation has no doubt played an important role, given the A-share markets were up around 140% YoY and valuations are now stretched on any measure.
- US economic fundamentals have been mixed recently (most notably a huge drop in durable goods orders), although we see these risks as overstated. The risk from US housing is (slowly) fading, the China liquidity story remains in play, and previous "no growth" regions such as Japan and the Euro area are warming up after several years next to the strong global growth fire.
- A rise in market volatility was overdue. After all, in recent times volatility has been as low as it's been for a decade. For those investors concerned about further volatility, our quant analysis suggests that stocks with high dividend yields perform well in periods of heightened volatility, while those with strong price momentum tend to perform poorly. By sector, utilities is the clear standout outperformer in highly volatile markets, while healthcare underperforms. By country, Indonesia and China are the markets to avoid.
- Korea and Taiwan will be major beneficiaries of the turmoil, since a by-product of recent events is that the downtrend in the Yen appears to have been broken. The 6% rise in the Yen-Won cross rate over the past week will be very positive for exporters particularly in Korea, so there is the potential for short-term upside in the Korean auto and tech sectors for stocks like Hyundai Motors (005380 KS, Won68,000 Neutral, TP: Won70,000,) and LG Electronics (066570 KS, Won58,100, Outperform, TP Won64,000, ). Korea and Taiwan are also the cheapest and most under-owned markets in the region, so have the most to gain as money flows reverse out of overvalued markets like China and India.
- Finally, for those investors more concerned about the cyclical outlook than us, analysis by our microstrategy team suggests investors should focus on those stocks that have a high free cashflow yield, and those that rate highly on our measure of sustainable growth. The table below contains a list of 10 of our top stock picks and how they rate on our macro, micro and quant criteria.

### Fig 1 Our superstar stocks

BBG Ticker	Name	Current Price (Icy)	Target price (Icy)	Macro	Micro	Quant
035760 KQ	CJ Home Shopping	64,700	81,000	✓	✓	✓
2441 TT	Greatek Electronics	47.9	65	✓	✓	
032640 KQ	LG Telecom	11,700	12,500	✓	✓	
JTL SP	Jurong Technologies	1.02	1.45		✓	✓
URC PM	Universal Robina	17.75	26	✓	✓	✓
2330 TT	Taiwan Semiconductor	66.1	82.4	✓	✓	✓
6244 TT	Motech	440	688	✓		✓
PTT TB	PTT	210	256		✓	✓
000720 KS	Hyundai E&C	50,300	61,400	✓	✓	
035420 KQ	NHN Corporation	129,900	150,000	✓	✓	

Source: Macquarie Research, March 2007

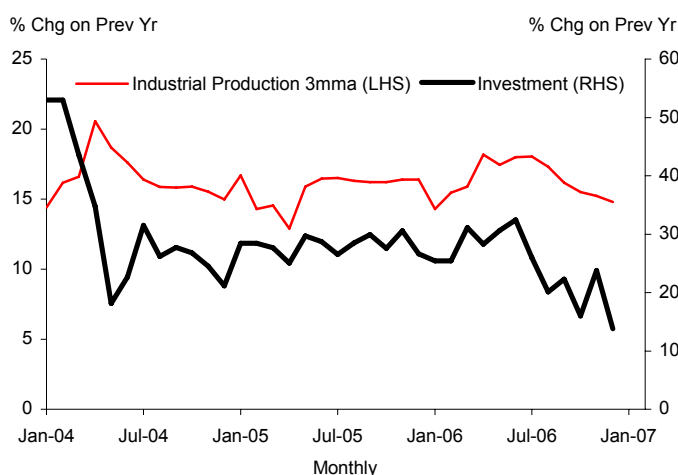
## Analysis

- Concerns about excessive valuations in China, and some weak US data have caused gyrations in Asian equity markets in recent days. However, we would argue that, from a fundamental perspective, not much has changed. The global outlook is still positive, and as a result we remain overweight the cyclical markets of Korea and Taiwan.

### The China story remains the same

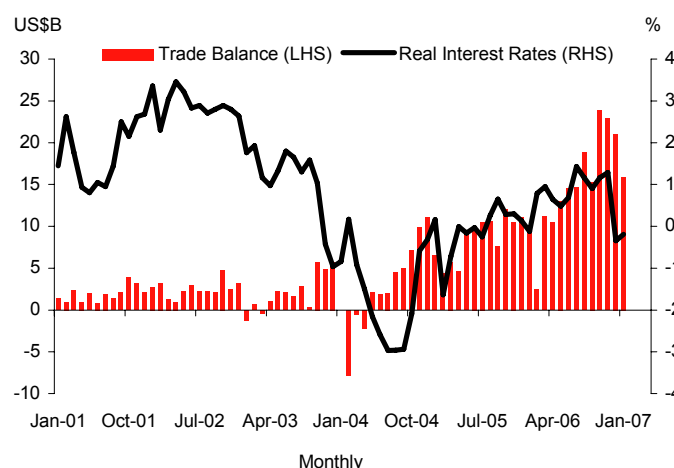
- Despite the huge amount of volatility in the Chinese equity market in recent days the macroeconomic story has not changed. Our China economist, Paul Cavey, believes the real economy is more or less right where officials want it to be. This is very different to mid-2006 when fixed asset investment was growing at around 30% YoY, and industrial production at just shy of 20%. Now, both have growth rates in the mid-teens (see Figure 1).
- Premier Wen Jiabao and other officials will talk about the real economy at the annual meeting of China's legislature, the National People's Congress (NPC), next week but we think the commentary will be more about maintaining the measures they put in place last year (such as the controls on bank lending), as opposed to announcing any new measures. Our base case is still for demand to accelerate during this year.
- Moreover, the liquidity story and currency appreciation story that has been such a powerful driver of markets in recent times has not changed: the trade surplus is still huge and interbank interest rates very low (see Figure 2).

**Fig 2 China's economy is not overheating...**



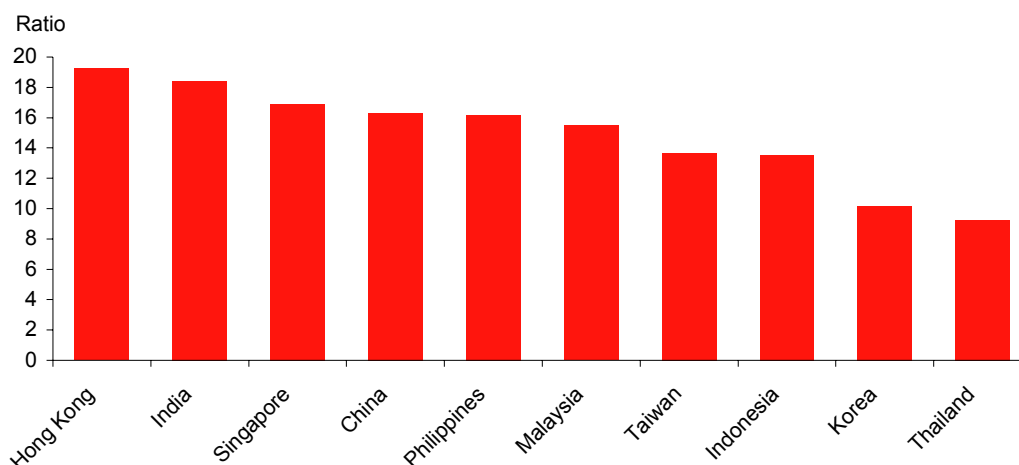
Source: Macquarie Research, February 2007

**Fig 3 ...and the liquidity story remains in place**



Source: Macquarie Research, February 2007

- These things said, the NPC – which will meet from March 5-16 – could prove challenging for equity markets. There could be lots of commentary about the elevated levels of asset prices and the need to keep price appreciation in check. So we cannot rule out further falls (and more volatility) in the market from here.
- If investors are concerned about overvaluation, they may find markets where valuations are far less stretched attractive. This would clearly be good news for Korea and Taiwan – our two key country overweights – given their undemanding valuations (see Figure 4).

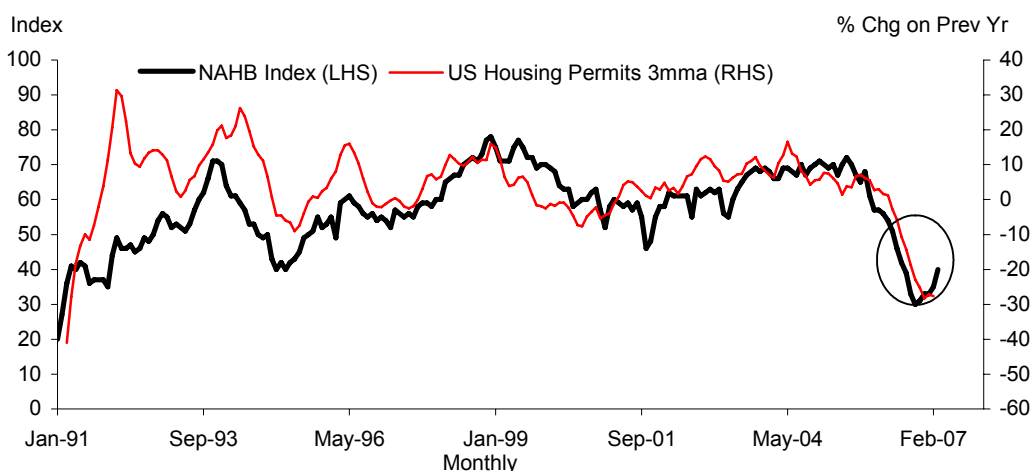
**Fig 4 Korea's PER ratio is the second-lowest in the region**

Source: Macquarie Research, February 2007

### US concerns are overdone...were investors beaten by a head fake?

- Some weaker data (most notably January's durable goods orders) and concerns about the sub-prime mortgage backed market in the US have clearly increased nervousness about US growth.
- The durables goods orders data were unambiguously weak. However, we think that investors have overreacted to this data. At the current economic juncture, the key question is whether the housing market weakness is flowing through to the consumer. So far it hasn't. But it's the next logical step in the cycle, so this is where investors' focus should be. If consumer spending holds up, the investment cycle will too.
- In a housing market downturn there are two ways that consumer spending can slow. First, a sharp downturn in residential construction activity causes employment in that sector to weaken, pushing the economy into a downward spiral of slowing employment growth and slowing consumption growth (The "construction sector channel").
- The second channel is when house prices stop growing (start falling), the reduced tailwind (headwind) from the wealth effect can slow consumer spending directly, again pushing the economy into a downward spiral of slowing consumption growth and slowing employment growth (the "wealth effect channel"). Where are we now in this process?
- In our view, most of the risk from the first channel has passed. With several of the leading indicators of the residential construction sector – such as mortgage applications, the NAHB survey, and housing permits – either stabilising or improving (see Figure 5) we believe the worst for this sector is behind us. The risk of a broad-based slowing in the US economy is now largely confined to the wealth-effect channel.

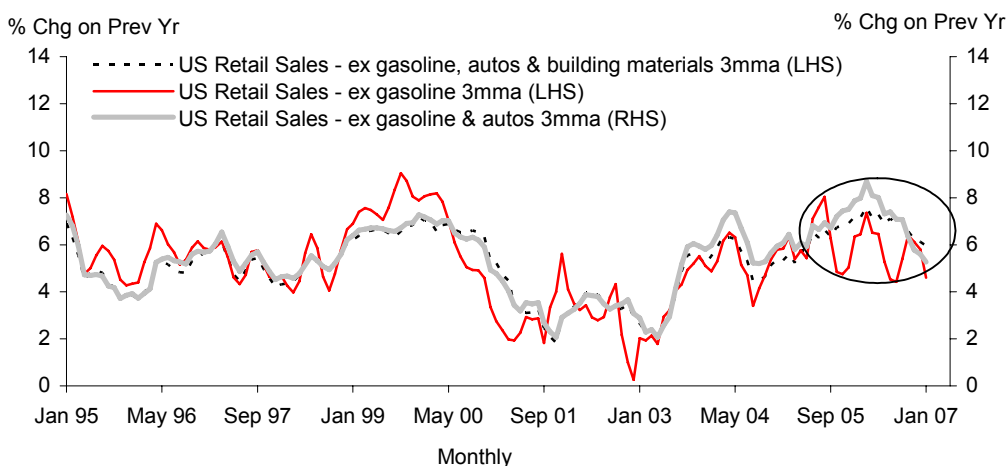
**Fig 5 The housing market is stabilising**



Source: NAHB, US Census Bureau, Macquarie Research, March 2007

- It is important to note that wealth effects can take some time to manifest themselves. So it is not sound judgement to conclude that ‘it hasn’t happened yet so it won’t happen’. That said, so far the news has been positive. As Figure 6 makes clear, underlying retail sales remain healthy – YoY growth rates in the three commonly quoted measures of underlying retail sales are currently around their average over the past 12 years. True, growth rates have slowed somewhat since mid last year. But in our view, this more reflects a return to trend after a period of above-trend growth, rather than anything more concerning.

**Fig 6 The consumer really has not missed a beat**



Source: US Census Bureau, Macquarie Research, February 2007

- Other indicators of the consumer sector also remain in good shape – consumer sentiment is healthy, while the labour market is tight and wages are picking up.
- If, like us, you believe that the cyclical outlook remains healthy, an overweight position in the cyclical markets of Taiwan and Korea is the best way to capitalise on this view. Figure 7 shows our top country stock picks for both countries.

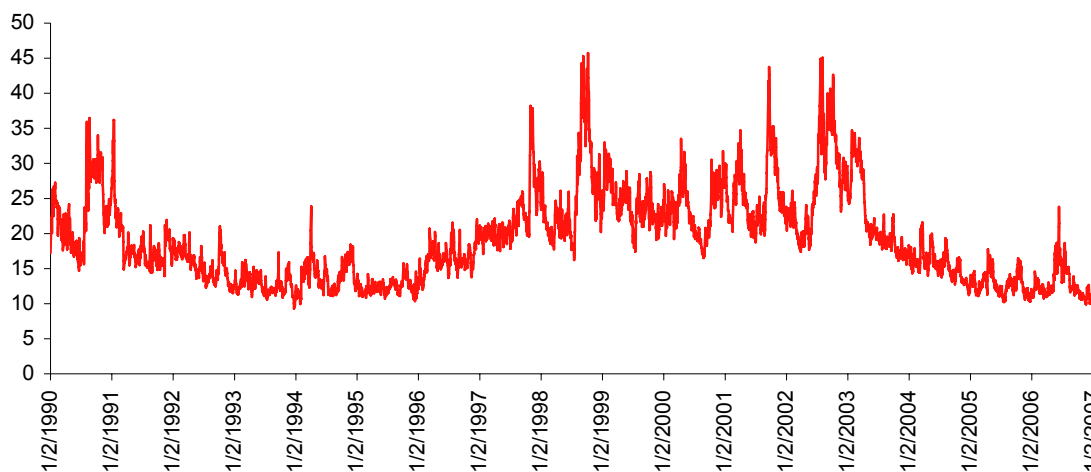
**Fig 7 Our top picks in our top markets**

Name	BBG Ticker	Price (Icy)	Target Price (Icy)
<b>Taiwan</b>			
TSMC	2330 TT	66.8	82.4
Greatek	2441 TT	48.7	65
Powertech	6239 TT	140.5	200
Motech	6244 TT	480	688
<b>Korea</b>			
Kookmin Bank	060000 KS	84,100	112,500
Shinhan Financial Group	055550 KS	53,300	71,200
Hyundai Steel	004020 KS	34,000	46,000
GS E&C	006360 KS	84,900	98,000

Source: Macquarie Research, March 2007

### Volatility – What should you do when markets misbehave?

- Equity market volatility has clearly spiked in recent days (see Figure 8). But it is important to bear in mind that this spike has come from an exceptionally low level. In our view, a large part of the reason for the very low level of volatility in recent years is due to the extraordinary growth in liquidity during this period.
- When a lot of people have a lot of money to invest, and financial markets are very sophisticated (enabling participants to capitalise on all kinds of market mispricing), a reduction in market volatility is not a surprising outcome.

**Fig 8 Market volatility has spiked from a very low level**

Source: Macquarie Research, March 2007

- Naturally enough, economic downturns – such as in the early 1990s and in 2000/01 – are periods when equity market volatility is high. If you are not as constructive as us on the global cyclical outlook, a rise in equity market volatility has to be part of your base case. Which stocks should you hold in this type of environment? We break this question down into two categories:
  - ⇒ What attributes should your stocks have?
  - ⇒ What sectors and countries should you be overweight/underweight?

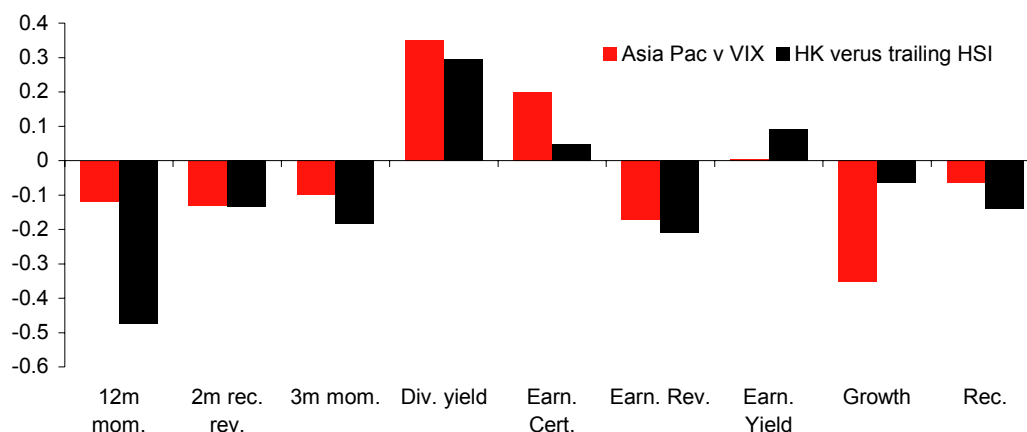
#### Individual Stock Attributes

- According to our quant team, you should avoid stocks with good momentum, and hold stocks with high dividend yields.
- To find which factors perform well when the market is more volatile, we have regressed information coefficients for various strategies against volatility. Regressions have been estimated with factor returns and volatility estimates concurrent.

$$Factor\_return_t = \alpha + \beta \bullet TrailingVolatility_t + \varepsilon_t$$

- Information coefficients are the rank correlations between each factor and subsequent month's return across an entire market. This effectively measures the return to a strategy.
- The regression therefore identifies which strategies the market rewards when volatility is high. Figure 9 shows the results of their regression analysis. They find that a high dividend yield is clearly beneficial, while momentum is a large negative. The great attraction of these results is that they accord with theoretical priors and so make perfect intuitive sense.

**Fig 9 Coefficients of ICs v volatility**



Source: Macquarie Research, March 2007

- Figure 10 gives a list of stocks that are likely to outperform based on this model, while Figure 11 shows a list of stocks that have high price momentum and so should be handled with care if market volatility rises sharply.

**Fig 10 High yielding stocks with a positive Macquarie Alpha are likely to outperform**

Code	Name	F'cast Div Yield	Macquarie Alpha
2343	PACIFIC BASIN SHIPPING LIMITED	6.8%	11.4%
303	VTECH HOLDINGS LTD	6.4%	13.6%
522	ASM PACIFIC TECHNOLOGY	5.2%	2.5%
6	HONGKONG ELECTRIC HOLDINGS	5.0%	1.4%
11	HANG SENG BANK LTD	5.0%	3.4%
903	TPV TECHNOLOGY LTD	4.9%	0.8%
737	HOPEWELL HIGHWAY INFRASTRUCTURE	4.5%	3.6%
2388	BANK OF CHINA (HONG KONG) HOLDIN	4.4%	3.2%
2356	DAH SING BANKING GROUP	4.3%	2.8%
2	CLP HOLDINGS LIMITED	4.3%	3.1%

Source: Macquarie Research, February 2007

**Fig 11 Beware of momentum stocks in a volatile market**

Code	Name	12m momentum	Macquarie Alpha
966	CHINA INSURANCE INTERNATIONAL	200.8%	-3.2%
297	SINOFERT HOLDINGS LTD	174.3%	-1.2%
322	TINGYI (CAYMAN ISLN) HLDG CO	98.3%	-1.4%
308	CHINA TRAVEL INTL INV HK	88.6%	-2.7%
83	SINO LAND CO	80.9%	-1.5%
27	GALAXY ENTERTAINMENT GROUP LTD	77.8%	-14.4%
659	NWS HOLDINGS LTD	72.5%	-0.6%
144	CHINA MERCHANTS HLDGS INT.	69.1%	-0.5%
45	HONGKONG & SHANGHAI HOTEL	68.7%	-1.4%
1068	CHINA YURUN FOOD GROUP LTD	66.6%	-0.6%

Source: Macquarie Research, February 2007

### Sectors and Countries

- It is also interesting to approach this question from a sector and country viewpoint. Since 1995 (which is the earliest period for which we have sectoral data) we identify six periods where volatility was greater than one standard deviation above average.
- Figure 12 shows the three sectors that underperformed and outperformed the most during the periods in question. For example, in period 1 healthcare performed the worst, industrials second worst, and consumer discretionary third worst; while utilities, telecommunications and consumer staples were the three top performing sectors.

**Fig 12 Sector performance in periods of high volatility**

		Underperform	Outperform
Period 1	27/10/97-12/01/98	Health Care Industrials Cons. Disc.	Utilities Telecommunications Cons. Staples
Period 2	03/8/98 - 25/3/99	Cons. Staples Telecommunications Health Care	Financials Utilities IT
Period 3	10/04/00 - 15/05/00	Telecommunications Health Care Cons. Staples	Utilities IT Industrials
Period 4	12/10/00 - 01/05/01	Health Care Telecommunications IT	Utilities Cons. Staples Industrials
Period 5	04/09/01 - 16/11/01	IT Telecommunications Cons. Disc.	Utilities Health Care Energy
Period 6	19/6/02 - 11/04/03	IT Telecommunications Financials	Energy Materials Utilities

Source: Macquarie Research, March 2007

- To aggregate these periods we use a 5-4-3 scoring system, where the best/worst performing sector in each period receives five points, the second best/worst four points etc (we think that a 3-2-1 scoring system biases the weight too heavily to the best/worst performing sector). The results are presented in Figure 13.

**Fig 13 Sector performance in periods of high volatility**

	Underperform	Outperform	Net Score
Utilities	0	27	27
Energy	0	8	8
Materials		4	4
Financials	3	5	2
Industrials	4	6	2
Cons. Staples	8	7	-1
Cons. Disc.	6		-6
IT	13	7	-6
Health Care	17	4	-13
Telecommunications	21	4	-17

Source: Macquarie Research, March 2007

- Some key points of note from this analysis are:
  - ⇒ Utilities is the clear outperformer in volatile markets. In the six periods shown above, utilities is the best performing sector on four occasions, and is in the top three sectors in all six periods. If you are concerned about volatility, you should be heavily overweight utilities. Figure 14 contains our top picks from our head of utilities, Sylvia Chan.

**Fig 14 The utilities sector outperforms in volatile markets**

Name	BBG Ticker	Price (Icy)	Target Price (Icy)
CKI Holdings	1038 HK	26.9	28.5
MMC Corp	MMC MK	5.2	6.75
Tenaga Nasional Berhad	TNB MK	11.7	12.6
Perusahaan Gas Negara	PGAS IJ	8900	12000

Source: Macquarie Research, March 2007

- ⇒ Energy is the next best sector. This is not so much because it does spectacularly well in volatile markets, it just never does badly (as evidenced by the zero score in the underperform column).
  - ⇒ Telecommunications does poorly. Except for the Asian crisis period it has underperformed in every period. The underperformance in periods 2-5 does not surprise us. During these periods the sector was, generally speaking, priced as a growth sector. Things have clearly changed since then and we now see it as having solid defensive qualities. In this case, we think that history is not a good guide to future outcomes.
  - ⇒ IT tended to outperform in volatile markets prior to 2000, but has been a consistent underperformer since then. It seems that prior to 2000 this sector could do no wrong. Since then it has reacted to events as any cyclical sector should.
- Figures 15 & 16 show the results of the same analysis by country.

**Fig 15 Country performance in periods of high volatility**

		Underperform	Outperform
Period 1	27/10/97-12/01/98	HK ID CH	TW PH IN
Period 2	03/8/98 - 25/3/99	CH ID TW	KR HK TH
Period 3	10/04/00 - 15/05/00	IN HK ID	CH TW SG
Period 4	12/10/00 - 01/05/01	IN CH SG	TH PH KR
Period 5	04/09/01 - 16/11/01	CH PH TW	MY TH IN
Period 6	19/6/02 - 11/04/03	PH KR ID	TH IN CH

Source: Macquarie Research, March 2007

**Fig 16 Country performance in periods of high volatility**

	Underperform	Outperform	Net Score
TH	0	17	17
MY	0	5	5
KR	4	8	4
TW	6	9	3
IN	10	10	0
SG	3	3	0
PH	9	8	-1
HK	9	4	-5
CH	17	8	-9
ID	11	0	-11

Source: Macquarie Research, March 2007

- Again there are some very interesting points of note:



- ⇒ Thailand performs very well during volatile periods. In part, this is because it has never performed particularly poorly when markets are volatile (note that period 1 which is around the time of the Asian crisis doesn't start until October 1997, so it misses the huge fall in the Thai market in August 1997). But it is also due to the fact that in more recent times it has tended to outperform during periods of heightened volatility. It may be that investor caution towards the Thai market post-Asian crisis has turned it into a great defensive play. At present we are very underweight Thailand due to the political risk. However, if you are less concerned about the political risk, and more concerned about a sharp spike in volatility than us, Figure 17 contains our top stock picks for Thailand (see also our recent Thai strategy piece *Offering defensive qualities*, 28 February).

**Fig 17 Thailand has outperformed in recent periods of heightened volatility**

Name	BBG Ticker	Price (Icy)	Target price (Icy)	PER FY06	Yield FY06
PTT	PTT TB		256	6.4	5.5
KBANK	KBANK TB		75	11.2	2.3
BBL	BBL TB		125	11.9	2.3
TOP	TOP TB		60	6.9	5
AOT	AOT TB		70	13.9	4.5

Source: Macquarie Research, March 2007

- ⇒ Indonesia is to be avoided. It has never performed well in volatile markets and regularly does poorly. The (coincidental) timing of political events in Indonesia has probably had some effect on this analysis. But it may also be that during times of general market volatility, the political risk premium rises sharply, causing markets in those countries with perceived political risk to underperform.
- ⇒ Countries such as the Philippines and India are lotteries – sometimes they do really well, other times they perform really poorly. For those investors who think volatility is on the rise, and like a punt, Figure 18 shows our top five stock picks for both countries.

**Fig 18 Macquarie's top picks should help ensure you end up on the right side of the coin toss**

Name	BBG Ticker	Price (Icy)	Target price (Icy)
<b>India</b>			
ICICI Bank	ICICIBC IN	855.35	1085
Bharti Airtel Ltd	BHARTI IN	727.1	750
Grasim Industries	GRASIM IN	2155.45	3215
Reliance Industries	RIL IN	1366.75	1590
Tata	TCS IN	1255.6	1672
<b>Philippines</b>			
BDO	BDO PM	55.5	78
PLDT	TEL PM	2440	2740
Globe	GLO PM	1375	1613
URC	URC PM	17.75	26
SM Prime	SMPH PM	11.25	14.25

Source: Macquarie Research, March 2007

### One for the bears

- Not surprisingly, volatile markets tend to be down markets – economic downturns are (thankfully) not the norm so there is naturally heightened uncertainty about the future path of events.
- When looking for companies that do well in falling markets, our microstrategy team finds that companies that have a high free cash flow yield, and score well on their measure of sustainable growth, tend to perform well.

**What is sustainable growth?**

- Sustainable growth focuses on the growth potential of a company, sector or market. Its axiom is that a stock's growth is a function of the level of financial resources retained and reinvested by the company, and the rate of return from those funds retained. The sustainable growth potential of a company therefore becomes a function of the rate of return on existing equity, and new equity retained (see Figure 19).

**Fig 19 Sustainable growth definition**


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Sustainable growth = Retention rate × Return on capital

OR

Sustainable growth = (1 – Dividend payout ratio) × Return on equity

Source: Macquarie Research, March 2007

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**Why focus on it?**

- We believe that sustainable growth is a reliable measure of the likely future growth rate of companies. Back-testing has shown it to be a better predictor of stock performance than EPS growth, which can be volatile and mean-reverting. One could argue that it has been mean-reverting to sustainable growth!
- The strength of the sustainable growth model is its ability to identify strong business models. The key strength of the measure is that it considers both the issue of returns (in the form of ROE), and the financial resources being retained to grow the business, via the payout ratio.

**Why focus on free cash flow yield?**

- Free cash flow yield is a good indicator of the health of the balance sheet. It suggests the company is unlikely to have a 'crisis of liquidity' when the economic environment changes unexpectedly. This is a clear defensive characteristic.
- Combined with sustainable growth it becomes an even more powerful indicator. High sustainable growth implies that the company can grow its business organically at a good rate without any major change in its capital structure – either dilution or debt. A high cash flow yield would mean that a large proportion of that growth could be turned into cash, further improving the health of the balance sheet.

**The stocks list**

- With the defensive qualities of these variables in mind we have screened for 30 stocks (out of the ~500 companies within our Asia ex Japan & financials coverage), that stand out in terms of the following criteria:
  - ⇒ Analyst recommendation is a BUY or a NEUTRAL
  - ⇒ Eliminate stocks with negative free cashflow yield based on FY06-07 average
  - ⇒ High sustainable growth based on FY05-08 average
  - ⇒ High and/or increasing free cashflow yields based on FY06-07 average

Fig 20 Thirty defensive stocks

**Sustainable growth screen - Non-financials**  
(Ranked by 2005-08 average sustainable growth and FCF yield)

Rank	Stock code	Stock name	Sector	Recom	Mkt cap (US\$ M)	EPSg	Payout	Sus Growth	FCF Yield	
						Avg (05-08)	Avg ROE Avg (05-08)	Avg (05-08)	Avg (05-08)	
1	PSL TB	Precious Shipping	Transportation	Outperform	778	10.0	26.7	44.3	32.5	19.7
2	TATA IN	Tata Steel	Materials	Outperform	6,182	28.7	18.5	41.9	34.2	18.0
3	SCC PM	Semirara Mining	Materials	Neutral	114	-26.4	17.5	32.6	26.9	18.3
4	IRPC TB	IRPC PCL	Energy	Outperform	3,405	1.9	23.6	17.7	13.5	22.0
5	HZ IN	Hindustan Zinc	Materials	Outperform	6,376	86.8	7.2	55.2	51.3	7.9
6	SAIL IN	Steel Authority of India	Materials	Outperform	10,694	40.4	20.1	49.6	39.6	10.3
7	048870 KQ	Core Logic	Semiconductors & Semiconductor Equipment	Outperform	177	-5.1	27.8	24.2	17.4	17.4
8	2498 TT	High Tech Computer	Technology Hardware & Equipment	Outperform	6,418	85.0	42.3	58.9	34.0	10.3
9	STLT IN	Sterlite Industries	Materials	Outperform	6,339	75.8	1.8	30.1	29.6	9.6
10	032640 KQ	LG Telecom	Telecommunication Services	Outperform	3,381	218.4	11.5	21.0	18.6	12.4
11	TTNP MK	Titan Chemicals Corp	Materials	Outperform	842	88.9	23.2	14.1	10.8	14.2
12	028150 KQ	GS Home Shopping	Retailing	Neutral	513	8.5	31.1	18.6	12.8	13.2
13	754 HK	Hopson	Real Estate	Outperform	3,125	60.4	31.6	27.1	18.5	11.2
14	ACC IN	Associated Cements Co	Materials	Neutral	4,085	90.1	21.3	35.3	27.8	7.2
15	TEL PM	PLDT	Telecommunication Services	Outperform	9,565	15.6	50.7	42.5	21.0	9.4
16	GAMB IN	Gujarat Ambuja Cements	Materials	Outperform	4,326	66.8	21.8	35.9	28.1	6.5
17	716 HK	Singamas	Transportation	Outperform	383	22.5	30.4	18.0	12.5	11.6
18	TLKM IJ	Telkom	Telecommunication Services	Outperform	20,177	37.0	43.5	47.3	26.7	6.7
19	049070 KQ	Intops	Technology Hardware & Equipment	Neutral	223	15.0	19.4	24.7	19.9	8.2
20	017670 KS	SK Telecom	Telecommunication Services	Neutral	16,993	13.1	38.3	20.8	12.8	10.6
21	THBEV SP	Thai Beverage	Food Beverage & Tobacco	Outperform	4,321	12.7	37.5	24.9	15.6	9.5
22	GRASIM IN	Grasim Industries Limited	Materials	Outperform	4,851	36.0	13.0	28.6	24.9	6.2
23	2889 HK	China Special Steel	Materials	Outperform	154	32.0	21.6	24.2	19.0	7.9
24	INTP IJ	Indocement	Materials	Outperform	2,328	164.4	11.1	18.2	16.2	8.7
25	TOP TB	Thai Oil	Energy	Outperform	3,383	5.4	39.3	23.8	14.4	9.2
26	8078 TT	Compal Communications	Technology Hardware & Equipment	Neutral	1,786	37.8	56.2	43.9	19.2	7.5
27	012330 KS	Hyundai Mobis	Automobiles & Components	Outperform	7,312	14.5	15.2	24.3	20.6	7.0
28	000880 KS	Hanwha Corp	Materials	Outperform	2,770	11.0	17.8	13.5	11.1	10.1
29	6153 TT	Career Technology	Technology Hardware & Equipment	Outperform	252	6.8	36.6	17.0	10.8	10.2
30	012450 KS	Samsung Techwin	Technology Hardware & Equipment	Outperform	2,887	108.5	18.6	19.3	15.7	8.3

Source: Macquarie Research, March 2007

## Important disclosures:

## Recommendation definitions

## Macquarie Australia/New Zealand

Outperform – return >5% in excess of benchmark return (>2.5% in excess for listed property trusts)  
 Neutral – return within 5% of benchmark return (within 2.5% for listed property trusts)  
 Underperform – return >5% below benchmark return (>2.5% below for listed property trusts)

## Macquarie Asia

Outperform – expected return >+10%  
 Neutral – expected return from -10% to +10%  
 Underperform – expected return <-10%

## Macquarie First South Securities (South Africa)

Outperform – expected return >+5%  
 Neutral – expected return from -5% to +5%  
 Underperform – expected return <-5%

Recommendations – 12 months

Note: Quant recommendations may differ from Fundamental Analyst recommendations

## Recommendation proportions

	AU/NZ	Asia	RSA
Outperform	43.12%	58.91%	42.20%
Neutral	48.98%	22.92%	46.80%
Underperform	11.90%	18.17%	11.00%

For quarter ending 31 December 2006

## Volatility index definition\*

This is calculated from the volatility of historic price movements.

**Very high–highest risk** – Stock should be expected to move up or down 60–100% in a year – investors should be aware this stock is highly speculative.

**High** – stock should be expected to move up or down at least 40–60% in a year – investors should be aware this stock could be speculative.

**Medium** – stock should be expected to move up or down at least 30–40% in a year.

**Low–medium** – stock should be expected to move up or down at least 25–30% in a year.

**Low** – stock should be expected to move up or down at least 15–25% in a year.

\* Applicable to Australian/NZ stocks only

## Financial definitions

All "Adjusted" data items have had the following adjustments made:  
 Added back: goodwill amortisation, provision for catastrophe reserves, IFRS derivatives & hedging, IFRS impairments & IFRS interest expense  
 Excluded: non recurring items, asset revals, property revals, appraisal value uplift, preference dividends & minority interests

EPS = adjusted net profit / efpowa\*

ROA = adjusted ebit / average total assets

ROA Banks/Insurance = adjusted net profit / average total assets

ROE = adjusted net profit / average shareholders funds

Gross cashflow = adjusted net profit + depreciation

\*equivalent fully paid ordinary weighted average number of shares

All Reported numbers for Australian/NZ listed stocks are modelled under IFRS (International Financial Reporting Standards).

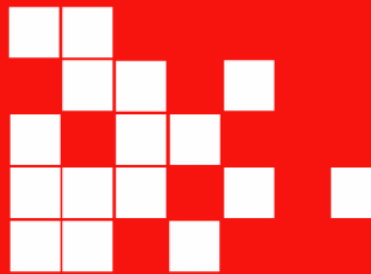
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