5. Emerging Market Economic & Fixed Income Outlook

Asia: Bonds to Outperform Currencies

Dollar-based returns on holding short-term Asian currency instruments, as measured by the JP Morgan Emerging Local Markets Index (ELMI) picked up slightly in the past month. Regional currencies continued to enjoy another period of stability as the Japanese yen stayed within a fairly tight trading range of 117-121/$ in March. Moreover, still-healthy trade surpluses continued to be a key support; these in turn engendered liquid conditions in inter-bank markets across the region, allowing central banks to relax their monetary stance even further.

But an unfortunate side effect of these economic developments is that Asian interest rates have now fallen so far that carry trades on local-currency instruments are unattractive to dollar-based investors. And with Korean and Thai central bank officials now openly stating their reluctance to allow their currencies to strengthen further in lieu of export competitiveness concerns, it appears as if Asia's rising currency cycle is coming to an end. Indeed, such an outcome is implicit in our near-term forecasts for depreciating Asian foreign-exchange rates: Together with unattractive carry as a result of falling domestic rates, they make a compelling argument as to why we are cautious on holding Asian local currency instruments at this point.

Yield Curve Flattening Trades

But the fact that interest rates will likely continue falling across Asia has not been adequately captured by the shape of yield curves. This provides some opportunity for yield curve flattening trades across the region. Recent moves by Asian central banks suggest that the downtrend in interest rates will likely continue at least for the next 3-6 months (see individual country write-ups). Because low inflation (or in some cases outright deflation) and liquid inter-bank conditions (mostly as a result of continued external surpluses) are expected to dominate near term, the likely path of interest rates in most of the region appears to be downwards.

Yet yield curves in Singapore, Korea and Hong Kong remain upward sloping at the short end of the curve, between 1-3 months, implicitly pricing in interest rate rises in the near term. We believe that investors ought to put on yield curve flattening trades in these markets as the downtrend in interest rates still have some distance to go.

The Great Asian Bond Rally

We continue to favor over-weighting Asian external debt in favor of local-currency instruments. Riding on a wave of optimism that resulted in spectacular spread compression in early 1999, Asian bonds have continued to register broad-based gains in the month of March. Bond markets in Asia appeared to have benefited from buying by regional banks as well as European investors during the month.

Indeed, the Asian rally occurred *pari passu* with visible signs of improvement on the macro-economic front. Across the region, monthly profiles of industrial production in key economies continue to point to either outright recovery or output stabilization. To be sure, the genesis of such a recovery is not by nature enduring, as it reflects the "low-base" effect of a severe depletion in output at the depth of the Asian crisis in 1998. The quality of recovery, or lack thereof, remains a longer-term concern that may ultimately set a limit to future growth, perhaps in the year 2000 but not immediately. In the interim, clearer signs of Asia's budding revival are likely to keep bond markets fairly well supported, even at current tight spreads, in the coming months.

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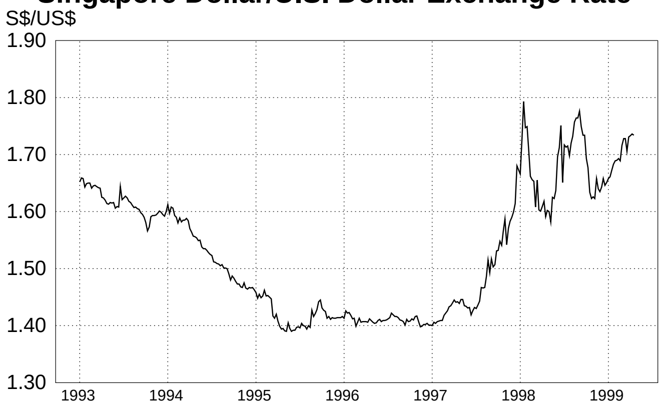
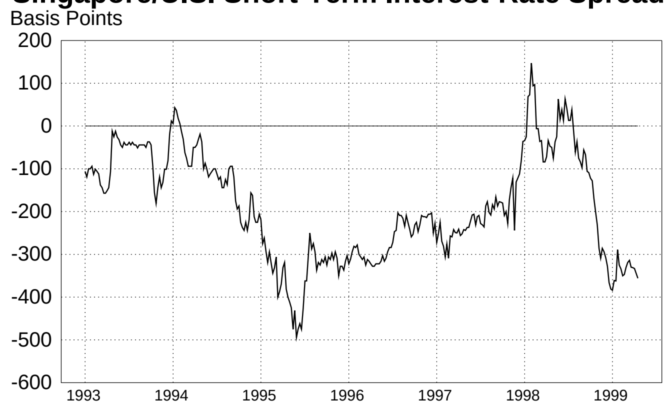
Asia

Singapore Dollar Outlook

Singapore Dollar/U.S. Dollar Exchange Rate

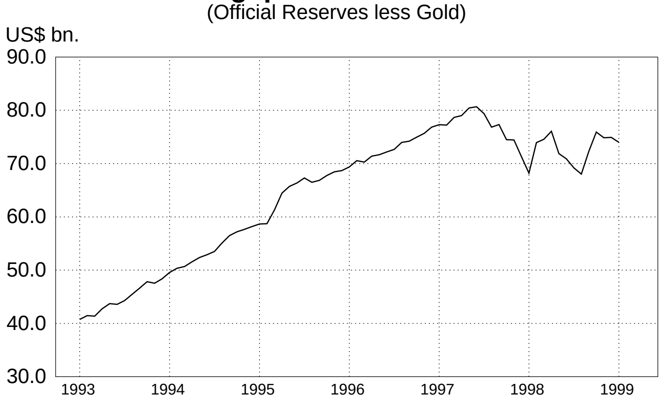


Singapore/U.S. Short-Term Interest-Rate Spread



Singapore's Reserves

(Official Reserves less Gold)



Singapore's Stock Market

Singapore
Key Economic Indicators and Forecasts

	1991	1992	1993	1994	1995	1996	1997f	1998f	1999f	2000f
Real GDP (yoy % chg.)	7.3	6.3	12.6	11.2	8.4	7.5	8.0	1.5	0.9	3.5
Inflation rate (%)	3.5	2.3	2.3	3.1	1.7	1.4	2.0	-0.3	-1.0	0.0
Current Acc't Bal. (% of GDP)	11.4	12.1	7.3	16.4	17.3	15.9	15.8	20.9	18.0	20.0
Trade Balance (US$ bn.)	-7.1	-8.7	-11.2	-5.9	-6.2	-6.3	-7.4	8.3	12.5	14.4
Int'l Reserves (US$ bn.)	38.9	45.5	53.2	64.6	78.0	107.8	119.6	84.5	86.0	-
Budget Balance (% GDP)	9.5	11.0	11.2	12.8	11.7	12.2	10.9	9.9	-3.0	0.5

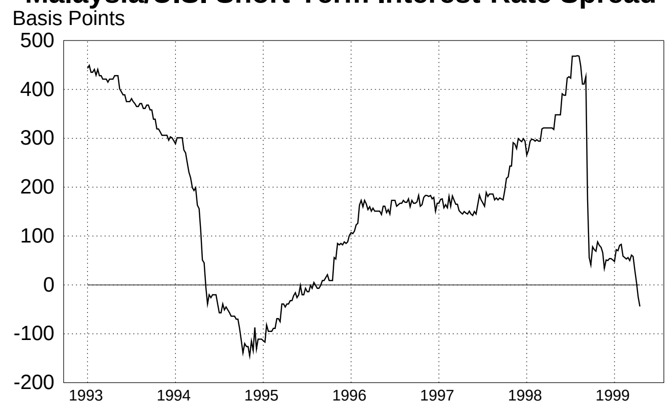
Malaysian Ringgit Outlook

Moderating inflationary pressures have allowed Bank Negara to cut its benchmark three-month KLIBOR intervention rate by 50 basis points to 6.5% last week. However, liquid conditions in the inter-bank market have engendered an even-sharper fall in the rate at which banks deal with each other—three month inter-bank rates have fallen 120 basis points in the last week to just 5.2%.

The government presented its White Paper on the economy to the parliament last week, which includes a growth target of 1% for 1999. The government also projects a fiscal deficit of only MYR5.9 billion in 2000 compared to MYR16.1 billion this year due to an expected increase in revenue from MYR50.3 billion this year to MYR62.91 billion next year. Expenditures are expected to rise from MYR47.2 billion this year to MYR48.9 billion next year.

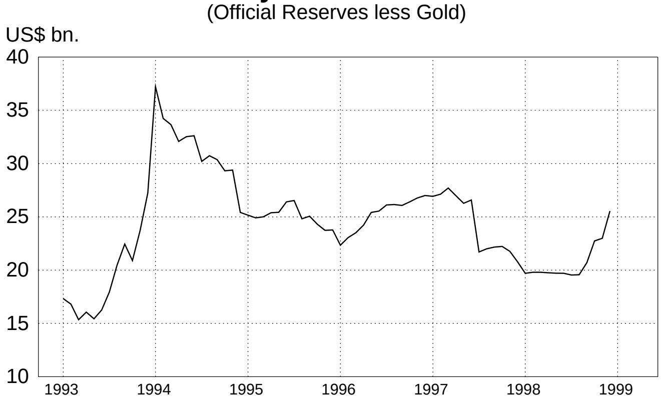
Malaysian Ringitt/U.S. Dollar Exchange Rate

Malaysia/U.S. Short-Term Interest-Rate Spread

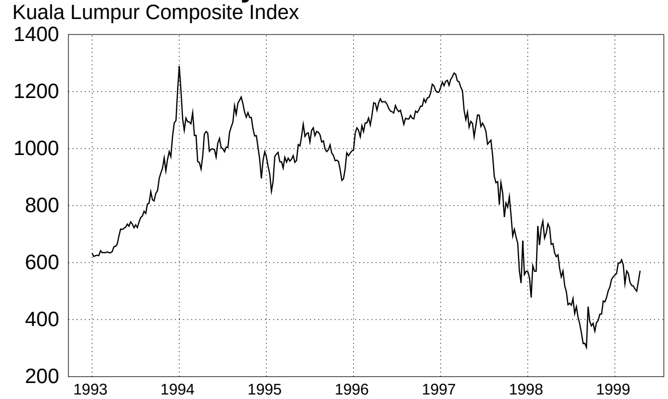


Malaysia's Reserves

(Official Reserves less Gold)



Malaysia's Stock Market



Malaysia
Key Economic Indicators and Forecasts

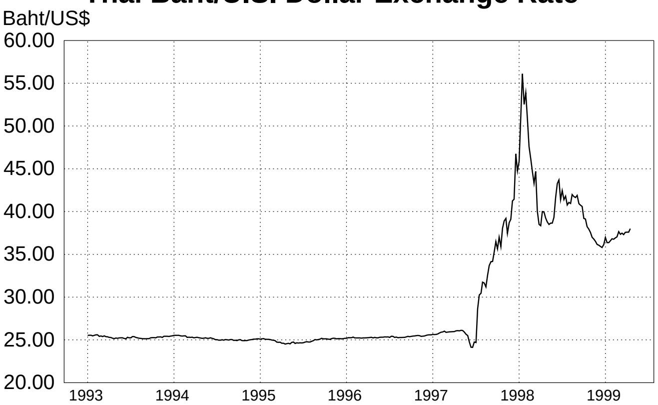
	1991	1992	1993	1994	1995	1996	1997f	1998f	1999f	2000f
Real GDP (yoy % chg.)	8.7	7.6	8.3	9.2	9.5	8.6	7.7	-6.2	-0.9	2.0
Inflation rate (%)	4.4	4.8	3.6	3.7	3.5	3.5	2.7	5.3	4.0	3.0
Current Acc't Bal. (% of GDP)	-8.8	-3.8	-4.8	-7.8	-9.9	-4.9	-5.1	14.8	4.9	1.8
Trade Balance (THB bn.)	-2.3	0.9	1.5	-0.8	-3.7	-0.1	0.2	14.9	8.6	5.9
Int'l Reserves (MYR bn.)	32.9	45.0	66.6	99.0	76.0	70.0	59.1	-	-	-
Budget Balance (% GDP)	-2.0	-0.8	0.2	2.3	0.9	0.7	2.4	-0.1	-5.7	-5.0

Thai Baht Outlook

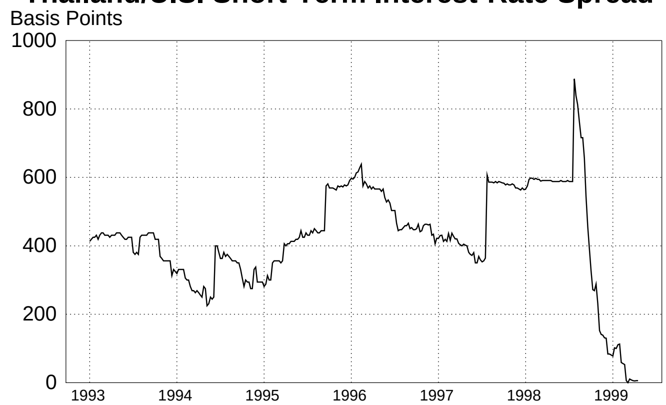
We believe that the rapid descent of Thai interest rates have probably come to an end. There are two countervailing forces, the net effect of which will be a major driver of interest rates in coming months. First, on the balance-of-payments side of the equation, continued capital outflow at a time when current-account surpluses are expected to diminish will likely have a negative effect on domestic liquidity over the medium term. Second, on the government budget side, part of the 6% of GDP budget deficit allowed for in the current fiscal year will likely be financed by domestic bond issuance.

Still, the problem of "crowding-out" (where the public sector competes with the private sector for limited funds and pushes interest rates up) will likely not be an issue for now, especially if domestic liquidity conditions remain flush. In other words, the net effects of the above two forces will likely be close to zero, and interest rates are likely to stabilize at current levels for the time being. But the balance of forces could well shift towards tightening liquidity and rising interest rates. Economic recovery would likely lead to rising imports and smaller trade surpluses in the coming months.

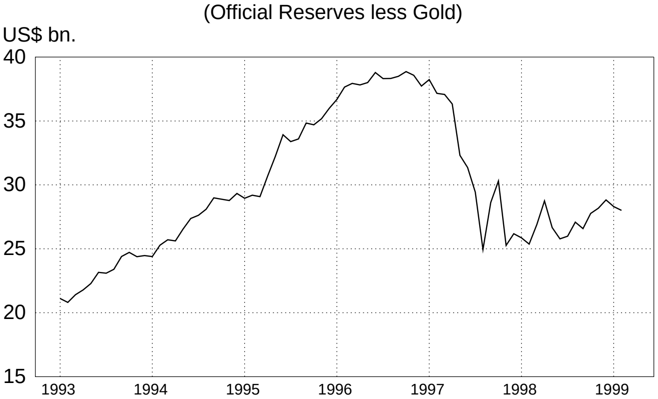
Thai Baht/U.S. Dollar Exchange Rate



Thailand/U.S. Short-Term Interest-Rate Spread



Thailand's Reserves
(Official Reserves less Gold)



Thailand's Stock Market

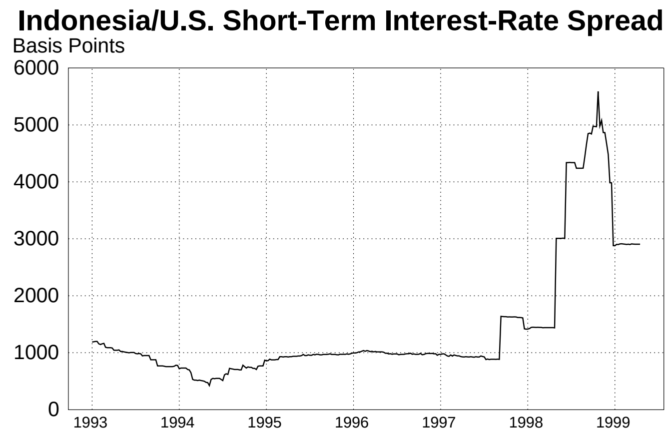
Thailand
Key Economic Indicators and Forecasts

	1991	1992	1993	1994	1995	1996	1997f	1998f	1999f	2000f
Real GDP (yoy % chg.)	8.6	8.1	8.4	8.9	8.8	5.5	-0.4	-9.6	-2.4	2.4
Inflation rate (%)	5.7	4	3.4	5.1	5.8	5.8	5.6	8.1	3.9	4.4
Current Acc't Bal. (% of GDP)	-7.6	-6.3	-6.4	-8.1	-13.6	-14.7	-3.1	10.9	8.7	7.7
Trade Balance (THB bn.)	-9.7	-8.1	-8.8	-9	-15	-16.4	-4.6	10.6	9.6	8.7
Int'l Reserves (US$ bn.)	17.3	20.4	24.5	29.3	36	38.7	27	26	28	-
Budget Balance (% GDP)	4	2.4	1.7	2.8	3.2	0.7	-0.6	-2.4	-5	-3

Indonesian Rupiah Outlook

One-month SBI rates continued to fall, by 100 basis points to 36.4% at Wednesday's weekly auction. This came on the back of a 0.2% month-on-month fall in March CPI inflation, or at a year-on-year rate of 45% (compared to a peak of 82% last year). A senior BI official this week said that the central bank's SBI target was now 30%, given that base money now has room to expand, the exchange rate has stabilized and inflation has eased.

Meanwhile, output figures show little signs of recovery. Investment Minister Hamzah has reported that the government approved foreign direct investment projects of only US$56 million from January 1 through March 15 this year, down from US$5.1 billion for the same period in 1998.



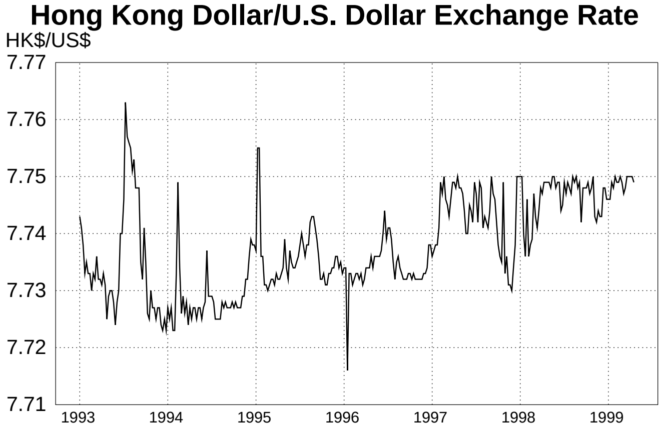
Indonesia
Key Economic Indicators and Forecasts

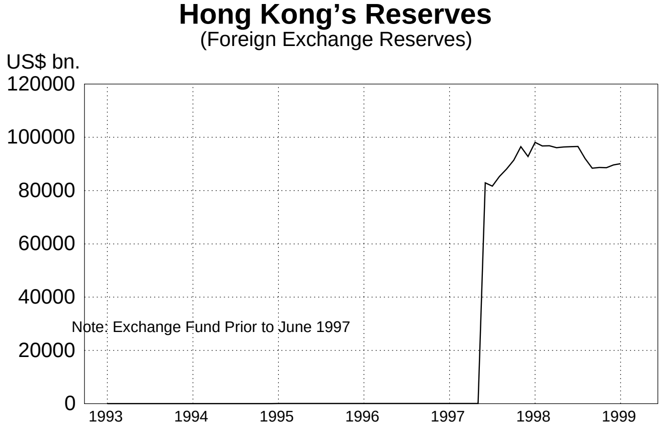
	1991	1992	1993	1994	1995	1996	1997f	1998f	1999f	2000f
Real GDP (yoy % chg.)	8.9	6.4	7.3	7.5	8.2	7.8	4.9	-13.7	-3.4	1.5
Inflation rate (%)	9.9	5.0	10.2	9.6	9.0	6.6	10.3	77.6	20.0	10.0
Current Acc't Bal. (% of GDP)	-3.5	-2.3	-1.5	-1.7	-3.4	-3.5	-3.5	3.6	7.5	7.5
Trade Balance (US$ bn.)	3.3	6.7	8.5	8.1	4.8	7.0	11.8	22.7	23.6	25.3
Int'l Reserves (US$ bn.)	-	-0.4	-0.4	1.0	0.4	0.5	-0.2	-	-	-
Budget Balance (% GDP)	0.2	-0.2	-0.6	0.0	0.0	0.2	0.0	-4.8	-5.0	-3.0

Hong Kong Dollar Outlook

On the back of interest rate cuts in Europe, the Hong Kong Association of Banks today announced a 25 basis-point reduction in prime lending rates to 8.5%. The Association last cut the prime rate by 25 basis points three months ago. The latest rate cut is not surprising, given that market anticipation has already put downward pressure on domestic interest rates. Still, the spread between prime and inter-bank borrowing rates remains relatively wide at around 300 basis points after the cut. Indeed, given intense competition among banks in the mortgage lending business, mortgage rates at some banks were actually below the prime over the past week.

The reduced likelihood of a near-term devaluation of the renminbi—given Premier Zhu Rongji's expressed commitment in the current visit to the U.S. as well as the announcement of stronger-than-expected growth of 8.3% in China during the first quarter—has also effectively alleviated upward pressures on Hong Kong interest rates. This, in turn, is likely to give a boost to domestic consumption demand, essentially via an increase in stock prices. The Hang Seng index has risen by 19% so far this year.





Hong Kong
Key Economic Indicators and Forecasts

	1991	1992	1993	1994	1995	1996	1997f	1998f	1999f	2000f
Real GDP (yoy % chg.)	5.1	6.3	6.1	6.4	3.9	4.6	5.3	-5.3	-3.0	1.0
Inflation rate (%)	11.6	9.3	8.5	8.2	8.6	6.0	5.7	2.6	-1.0	0.0
Current Acc't Bal. (% of GDP)	6.6	5.3	7.0	1.2	-4.3	-1.7	-3.8	2.8	4.2	2.8
Trade Balance (US$ bn.)	-2.1	-4.3	-3.8	-10.9	-20.0	-18.4	-21.1	-11.0	-8.0	-11.0
Int'l Reserves (US$ bn.)	28.9	35.2	43.0	49.3	55.4	63.8	90.1	95.0	95.0	-
Budget Balance (% GDP)	3.9	3.3	2.5	1.2	-0.3	1.4	2.7	1.7	1.3	-

New Taiwan Dollar Outlook

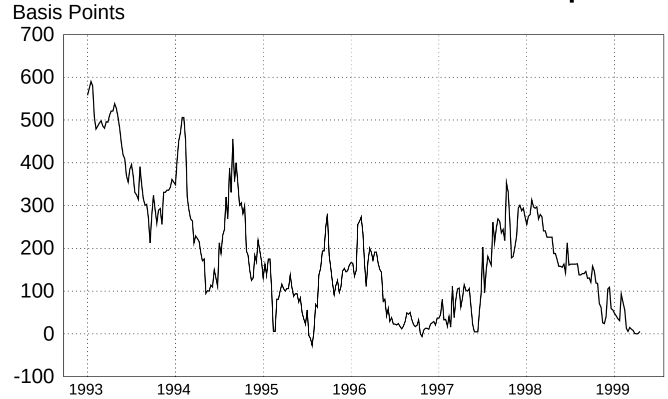
The Council for Economic Planning and Development (CEPD), the government's economic policy planning unit, expects the economy to bottom out by May, on the back of an imminent export recovery. New reports suggest that the government may raise its 1999 economic growth forecast from 4.74% currently to about 5%. Exports rose by 3.5% in 1Q99, in contrast to a contraction of 13% in 4Q98.

The improvement in export performance is not surprising in the context of a global and Asian monetary easing. The shipment/inventory ratio for consumer durable goods also adds to the recovery story. Durable inventories are falling at an unsustainable rate relative to shipments, and this is likely to result in restocking at least by mid-1999.

The economy should also benefit from a domestic monetary easing. Real short-term rates have fallen by 400 basis points from February 1998, while the real effective exchange rate is down 6% year/year. Easing monetary conditions have also led to a recovery in asset prices: the domestic stock market index has gained by about 13% so far this year.

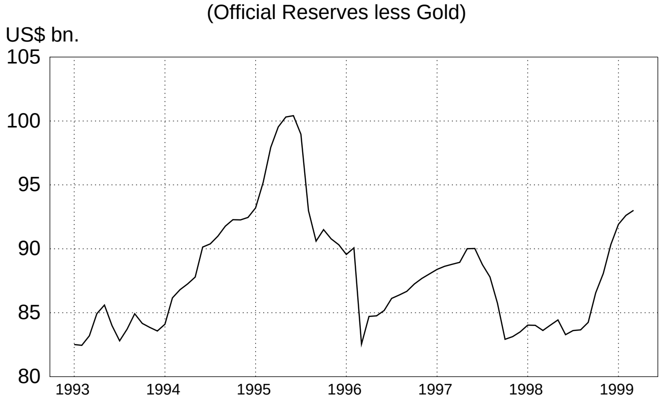
New Taiwan Dollar/U.S. Dollar Exchange Rate

Taiwan/U.S. Short-Term Interest-Rate Spread

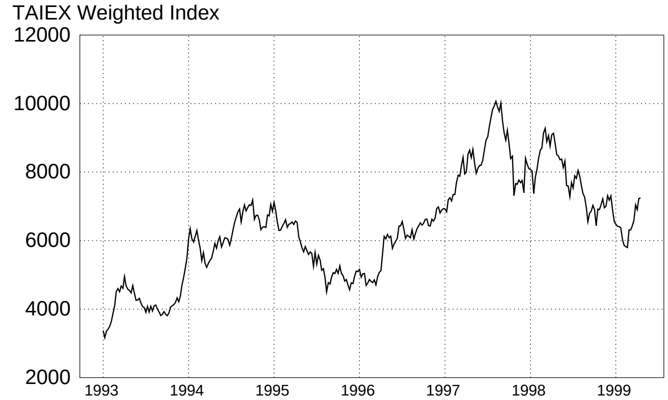


Taiwan's Reserves

(Official Reserves less Gold)



Taiwan's Stock Market



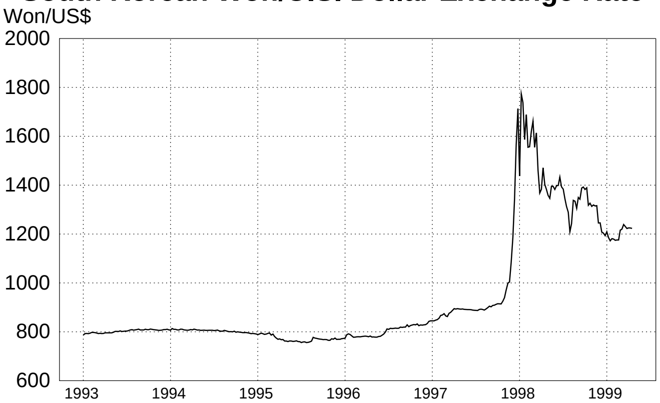
Taiwan
Key Economic Indicators and Forecasts

	1991	1992	1993	1994	1995	1996	1997f	1998f	1999f	2000f
Real GDP (yoy % chg.)	7.6	6.8	6.3	6.5	6.0	5.7	6.8	4.8	3.5	5.1
Inflation rate (%)	3.6	4.5	2.9	4.1	3.7	3.1	0.9	1.7	0.5	1.0
Current Acc't Bal. (% of GDP)	6.9	4.0	3.2	2.7	2.1	4.0	2.8	1.8	2.9	2.0
Trade Balance (US$ bn.)	13.3	9.5	8.0	7.7	8.1	13.6	7.7	5.9	8.9	6.4
Int'l Reserves (US$ bn.)	82.4	82.3	83.6	92.4	90.3	88.0	81.5	84.5	86.0	-
Budget Balance (% GDP)	-7.9	-5.4	-5.2	-5.7	-7.4	-7.4	-6.2	-7.2	-6.7	-6.4

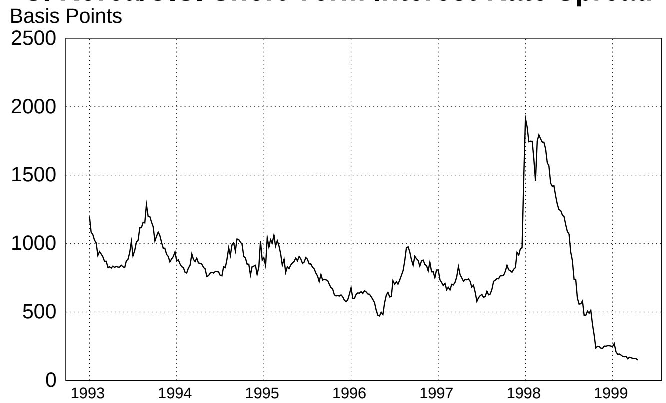
Korean Won Outlook

The economy expanded by 3.1% during the first quarter—its first positive outturn since 4Q97—according to recent Bank of Korea (BoK) estimates. Industrial indicators point to rising demand in the absence of excess supply, while news flow suggests fixed investment sentiment is beginning to improve. Continued monetary easing and fiscal expansion should strengthen these bullish trends. The BoK has raised its 1999 growth forecast to 3.8% from 3.2%. The BoK also expressed concern over a rising won on account of capital inflows, indicating that the government may "indirectly" intervene to curb the appreciation trend, possibly through early retirement of foreign debt. True, currency strength may not be desirable for Korean exporters, but officials may find the scope for official guidance of the won exchange rate to a particular level increasingly limited, as the won is now far more subject to market forces than it was before. However, this by no means suggests greater volatility. Indeed, one may argue that, given increased depth and liquidity in the non-deliverable forward market as a result of the participation of Korean banks, the likelihood of sharp gyrations in the exchange rate has been reduced. That said, currency strength as a result of sustained inflows will likely be curbed by an easy monetary stance.

South Korean Won/U.S. Dollar Exchange Rate

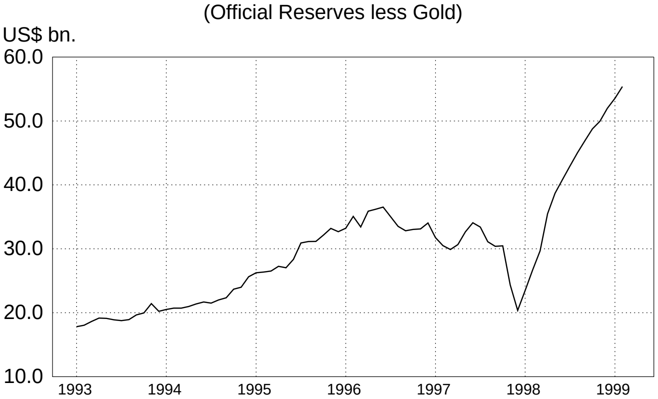


S. Korea/U.S. Short-Term Interest-Rate Spread

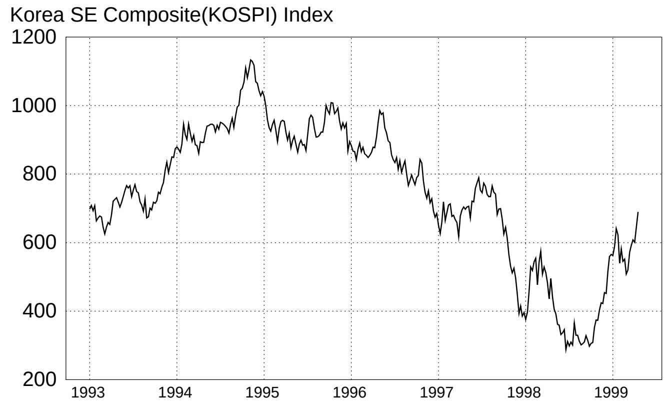


South Korea's Reserves

(Official Reserves less Gold)



South Korea's Stock Market



Korea
Key Economic Indicators and Forecasts

	1991	1992	1993	1994	1995	1996	1997f	1998f	1999f	2000f
Real GDP (yoy % chg.)	9.1	5.1	5.8	8.6	8.9	7.1	5.5	-5.5	2.2	4.0
Inflation rate (%)	9.3	6.2	4.8	6.2	4.5	4.9	4.4	7.5	2.0	3.0
Current Acc't Bal. (% of GDP)	-2.8	-1.3	0.3	-1.0	-1.9	-4.7	-1.8	13.0	5.3	2.6
Trade Balance (US$ bn.)	-9.7	-5.1	-1.6	-6.3	-10.1	-20.6	-8.5	39.9	20.0	10.0
Int'l Reserves (US$ bn.)	13.7	17.2	20.2	25.6	32.7	33.2	25.0	56.6	82.7	-
Budget Balance (% GDP)	-0.8	-0.3	0.1	0.6	0.5	0.0	0.0	-6.0	-5.0	-5.0

Philippines Peso Outlook

The BSP announced a 1% cut in reserve requirements to 14% last week, effective April 16. In a bid to boost bank lending, the central bank also announced that new loans extended after March 31 would be exempt from the present loan-loss provision of 1.5%. These measures, coupled with a moderation in March inflation to 8.8% from 9.9% in February, are expected to bring the key 91-day T-bill rate to below 11%, according to BSP Governor Gabriel Singson. The rates on 91-day T-bills cleared at 11.4% at this week's auction, continuing a downtrend amounting to a fall of 200 basis points over the last three months.

The central bank also cut its key overnight rates by 37.5 basis points, bringing the overnight borrowing rate to 11.375% and the overnight lending rate to 13.375%. This represents the sixth consecutive week in which rates have been cut, and the ninth rate cut this year. Although ample domestic liquidity is likely to keep rates low in the short term, there is a longer-term risk that rates will head up at the end of the year. This could occur either if the government deficit is not contained or the government is unable to fully fund the deficit with foreign loans.

Asian currency comments by:
Chia Liang Lian (65) 330-7194
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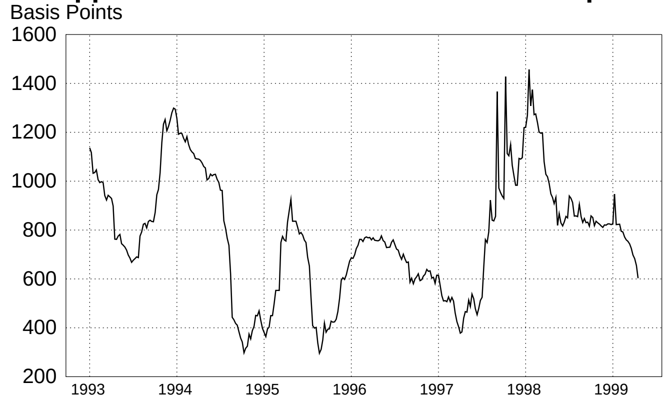
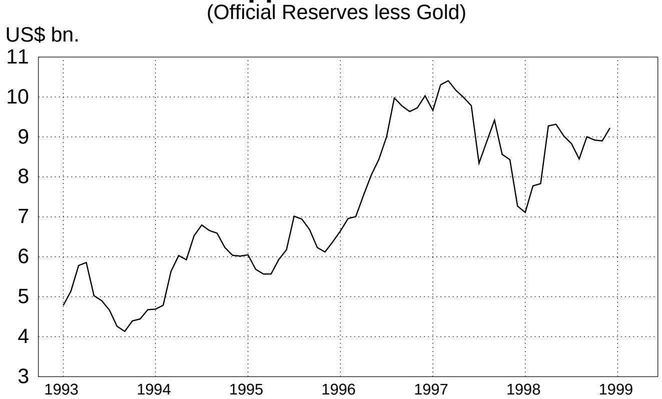
Philippine Peso/U.S. Dollar Exchange Rate

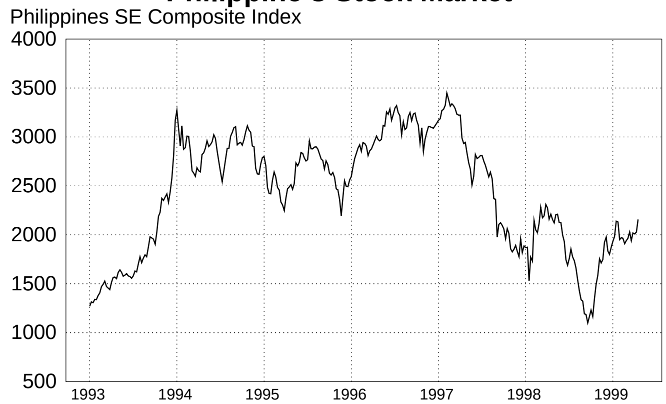
Philippine/U.S. Short-Term Interest-Rate Spread



Philippine's Reserves
(Official Reserves less Gold)



Philippine's Stock Market



Philippines
Key Economic Indicators and Forecasts

	1991	1992	1993	1994	1995	1996	1997f	1998f	1999f	2000f
Real GDP (yoy % chg.)	-0.6	0.3	2.1	4.4	4.8	5.8	5.2	-0.5	1.3	2.6
Inflation rate (%)	18.8	8.9	7.6	9.1	8.1	8.5	5.1	9.7	8.1	7.0
Current Acc't Bal. (% of GDP)	-1.9	-1.6	-5.7	-4.3	-4.5	-4.7	-7.1	0.6	-0.7	-1.6
Trade Balance (US$ bn.)	-3.2	-4.7	-6.2	-7.8	-8.9	-11.3	-10.7	-0.2	-1.0	-2.3
Int'l Reserves (US$ bn.)	3.2	4.4	4.7	6.0	6.4	11.6	9.2	9.5	10.6	-
Budget Balance (% GDP)	-2.0	-1.2	-1.5	1.0	0.6	0.6	0.1	-1.8	-2.4	-1.7