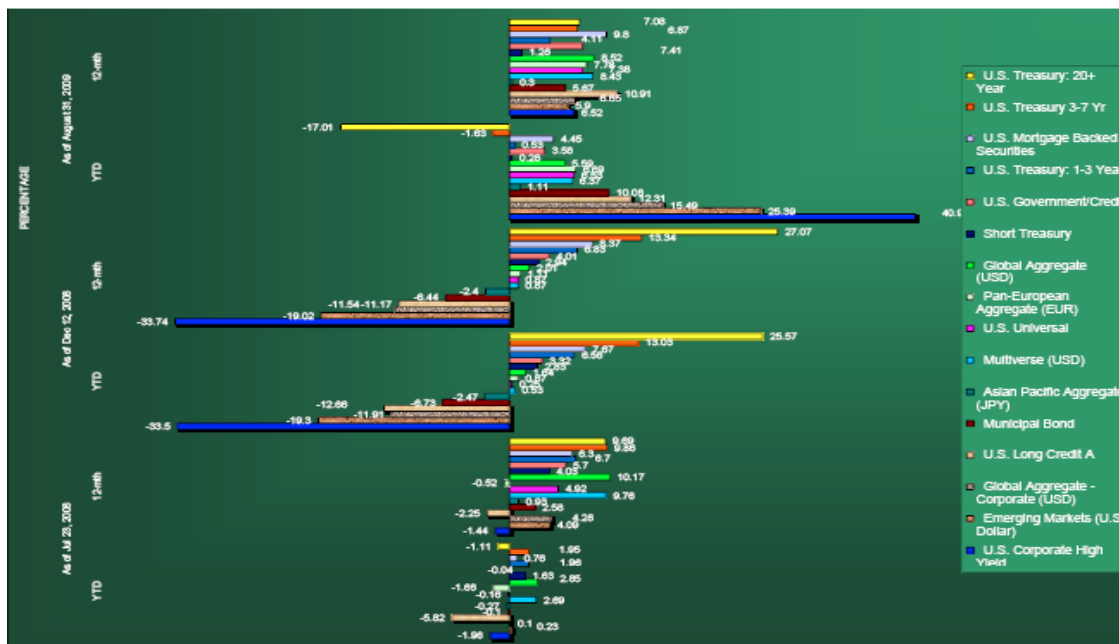




The going has been good for the global as well as GCC stock markets in August and September 2009, with glimpses of a global recovery or at best, a slowdown in the global recessionary trend round the corner. Positive manufacturing data in the US for the first time in August, since the last 19 months, shows that finally the US economy is on the path to recovery. This is in line with the IMF's recent forecast that global economies, including advanced economies will witness positive growth during the next few quarters. However, our opinion is that this growth may be largely on a backdrop of fiscal stimulus and inventory rebuilding by firms, rather than on strong private consumption and fixed investment spending. Unemployment is still on the rise. Low production, negligible fresh investment and falling employment data threaten to choke the green shoots of the economic turnaround sprouting in some of the major developed countries. In addition to that, there is considerable risk in the global financial system. A recent report of the Bank for International Settlements mentioned that the global financial system is still loaded with financial derivatives which touched \$426 trillion in September '09, due to a sharp rise of 16% in short-term futures and options which could pose a serious challenge to the global financial system. Moreover, for a sustainable recovery, a radical shift from public to private spending and rebalancing of aggregate demand across countries are a must. The latter would require a shift from domestic to foreign demand in the United States and a reverse shift from foreign to domestic demand in the rest of the world, particularly in Asia. We believe that henceforth, recovery in asset prices across various asset classes will be slow with occasional bouts of corrections keeping returns aligned to the underlying macros and movement of capital across different regions and sectors based on their strengths and weaknesses.

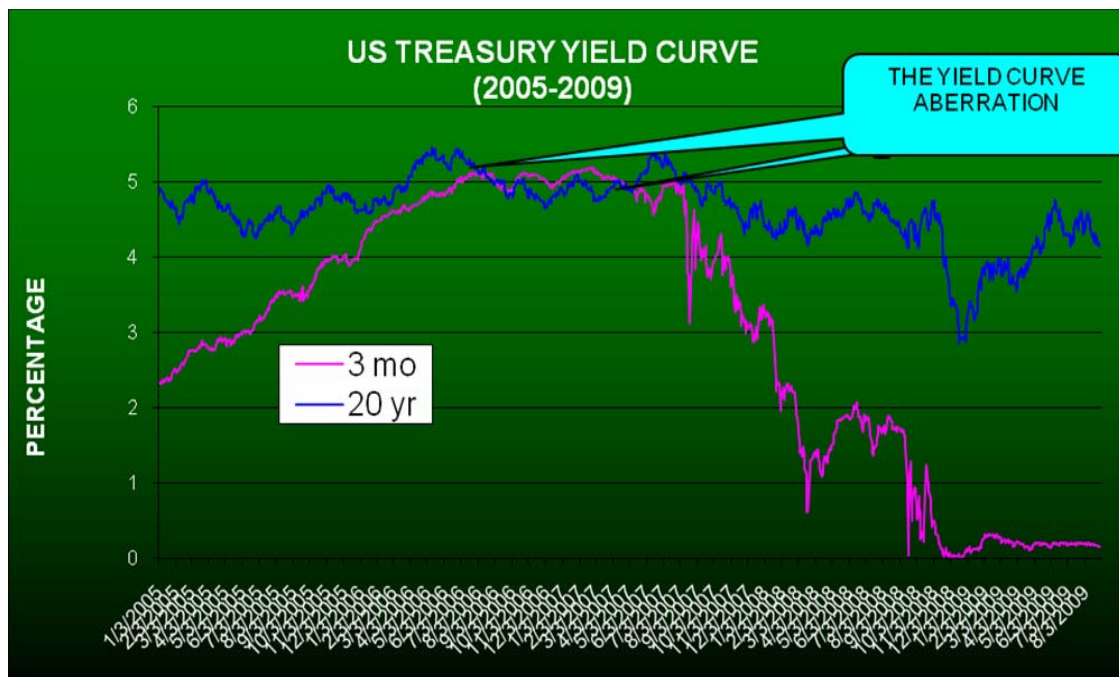
Fixed Income

The global fixed income market has become more attractive in the corporate high yield segment as investors' risk appetite comes back into play. The US Corporate High Yield Index has gained 40.95% as against a negative return of 17.01% in the US long dated (+20 years) Treasury Index this year until the end of August 2009. This is in sharp contrast to a gain of 25.57% in the US long-dated (+20 years) Treasury Index and a decline of 33.5% in US Corporate High Yield Index as on December 12, 2008.



Source: Lehman Brothers Global Bond Indices

We were early to detect the US yield curve aberration in July 2006 and the chances of a financial crisis, when the short-term 3-month treasury yield curve crossed above the long-dated (20+ year) treasury yield curve and remained above it until the onset of a major global financial crisis in April 2007.



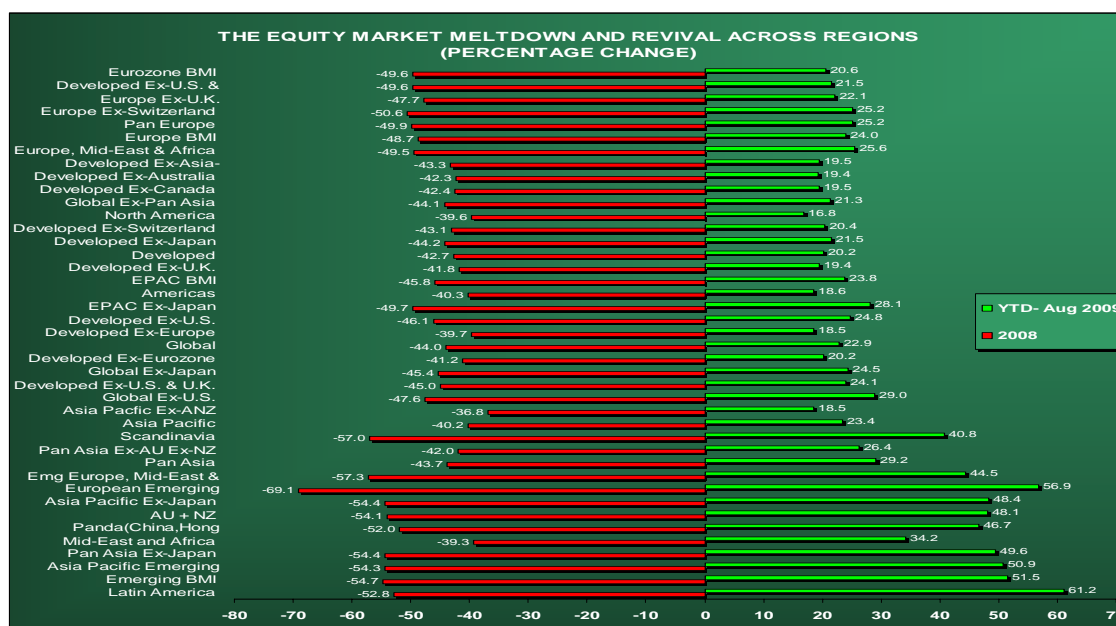
Source: US Treasury



Since then, the short-term yield has moved in the opposite direction and reached to zero level in December 2008 and has remained near zero level so far. This signifies that the real credit off-take has not yet started. However, investors' appetite for risk has grown over the last few months and we believe the trend will reverse again sooner or later. We expect, both corporate high yields and investment grades will continue to provide better returns but the downside risk level is increasing as spreads continue to shrink and duration bets across risk categories may not justify higher yields for long.

Equities

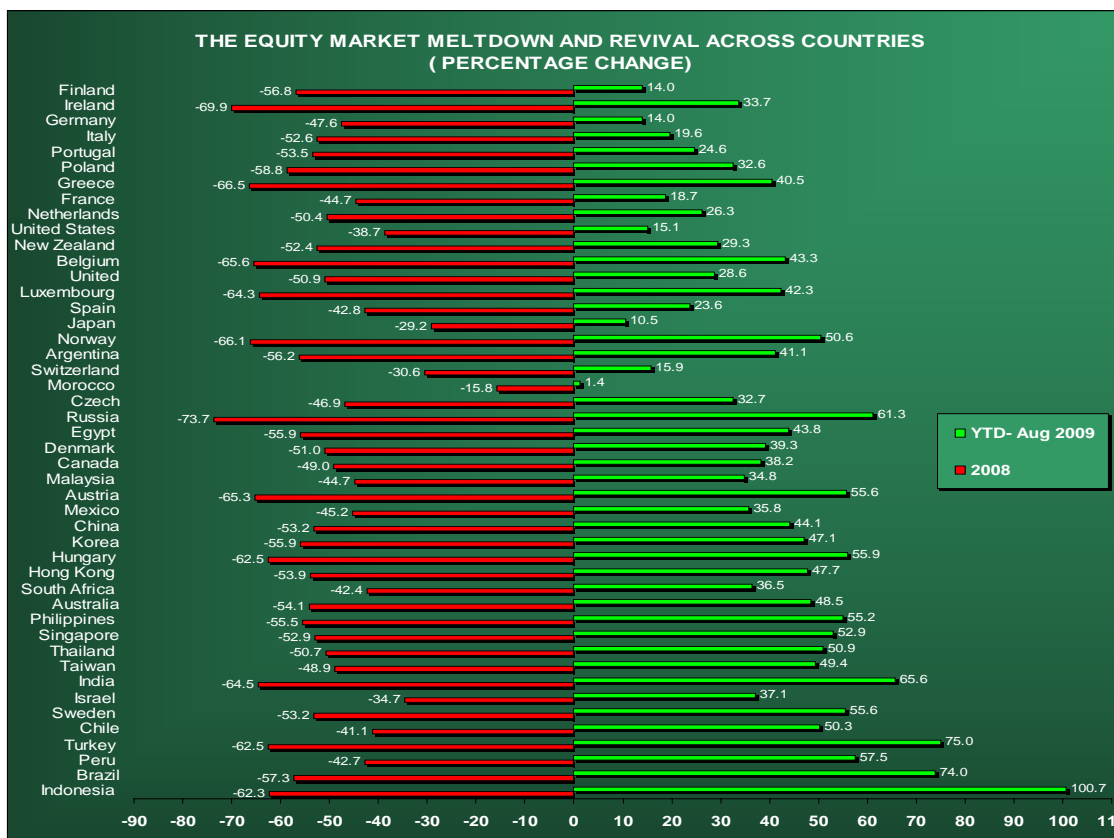
Across global equity markets, the impact of the financial crisis and the recession was far too severe and extremely volatile. As we know, global equity markets declined sharply by 44% during 2008 and another 13% during the first quarter of 2009 but started reviving thereafter until August 2009. Across regions, revival was the strongest in Latin America which entered into positive territory of 8.4%, recovering from last year's decline of 52.81%, while Emerging Markets as a whole, Asia Pacific Emerging Markets and Mid-East and Africa remained in negative territory of around 5%. The European Emerging markets lagged behind in their run with more than 12% in losses to cover up. Among developed regions, Australia and New Zealand recorded the strongest revival with almost 89% of last year's losses mainly on account of a sharp recovery in mining and resources companies in Australia, while developed markets ex. US and Japan still remained deep in negative territory with a recovery of only around 43% of last year's losses.



Note: Data based on S&P Broad Market Price Indices



Though Emerging Markets witnessed strong recovery as compared to developed markets, the momentum across countries widely varied with Indonesia gaining a hefty 38.4% by the end of August '09 after recovering 62.3% of 2008's losses. The other Emerging Markets which recorded remarkable recovery were Brazil (net +16.6%), Peru (net +14.9%), Turkey (net +12.5%) and Chile (net+92%). Among other major emerging markets, India kept its footstep in positive territory with a 1.1% gain, while China still remained in negative territory of 9.1% and Poland remained deep in negative territory with a 26.2% net loss until August 2009. Over the same period, developed Europe continued to lag behind with Finland deep in negative territory with a net 42.8% loss, followed by Ireland (net -36.3%), Germany (net -33.6%), Italy (net -33%), Portugal (net -28.9%), Greece (net - 25.98%), France (net -25.93%) and Netherlands (net - 24.1%). The US markets continued to remain in the red with a net decline of 23.6%, while the only two developed markets that entered into the positive territory with a net gain of around 2% were Sweden and Israel.



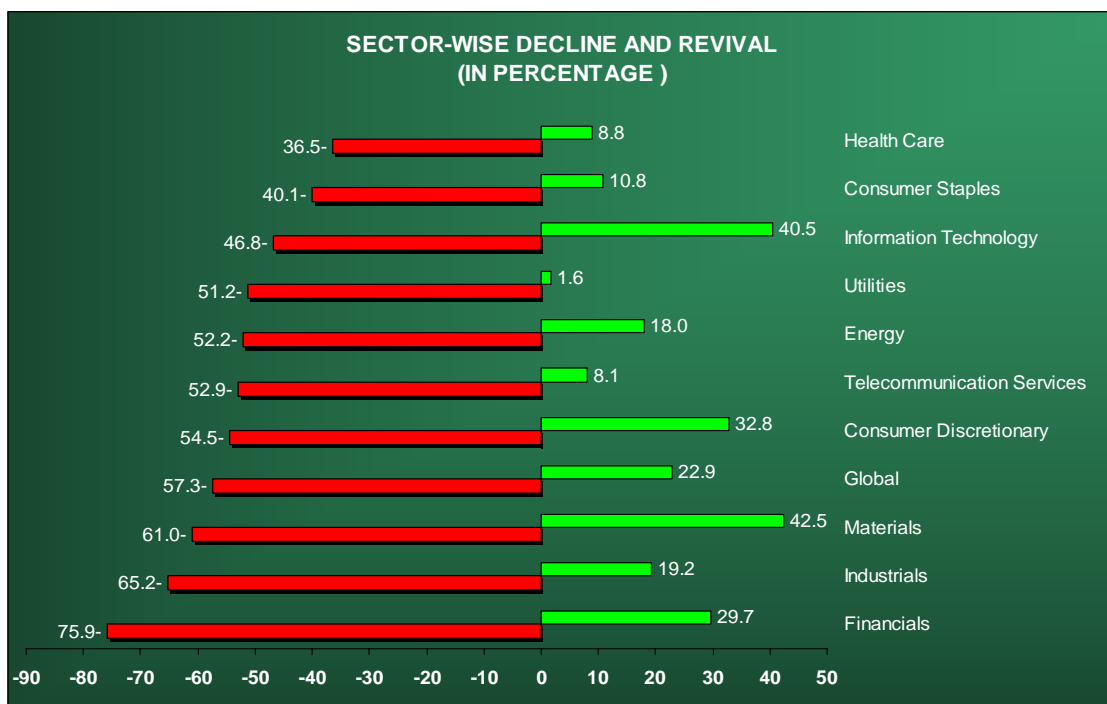
Note: Data based on S&P Broad Market Price Indices

We believe the real impact of the recession has still not been felt in the developing equity markets and its impact is going to remain for longer. The initial optimism that the recession



has slowed down and signs of growth are sprouting out in major developed economies may be because of the after effects of the policy measures and an impulsive comeback from the overreaction due to investors' loss of confidence. Many of the major developing and developed economies are still structurally very weak in terms of excessive credit and leveraging, huge current account deficit and higher share of real estate investments in GDP, the balancing of which, will take longer time than expected.

This is also evident from the contrarian movement of equity prices across various sectors as cyclical sectors such as Materials, Information Technology, Consumer Discretionary and Financials have recorded the highest percentage recovery as against non-cyclical sectors such as Utilities, Consumer Staples, Health Care and Telecommunication Services.



Note: Data based on S&P Broad Market Price Indices

Real Assets

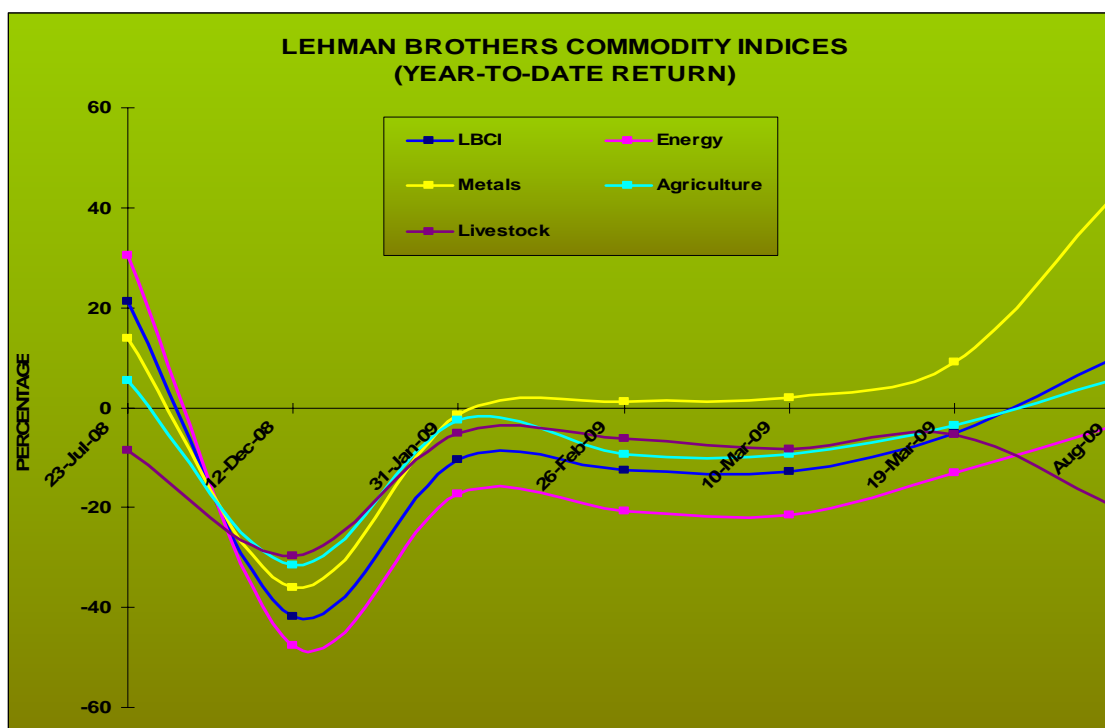
Real Assets such as commodities and real estate have low correlation to equities and provide substantial diversification and risk reduction benefits to an investment portfolio.

Commodities

During the 2008 financial crisis and the recession that followed, commodities excepting precious metals were also the hardest hit alongside equities. The Lehman Brothers



Commodity Index (LBCI) had declined by 41.9% as of December 12, 2008 and continued to decline further by another 12.9% until March 10, 2009, but revived thereafter as the fiscal stimulus packages announced by various governments created an atmosphere of optimism and major developing economy China started spending on infrastructure and building up reserves. Commodities prices continued their upward trend through the second quarter and the LBCI had gained 10.34% by the end of August mainly on the strength of a 43.53% gain in the Industrial Metals Index. The long-term (1991-2009Q1) correlation of commodities with equities and Govt. bonds are 0.15 and -0.3, respectively and thus can provide immense diversification benefits.



Source: Lehman Brothers Commodity Indices

However, with the exception of metals; energy, livestock and agriculture indices were down by 50.72%, 50.13% and 25.5% respectively, on a cumulative basis until August 2009 over 2007. With metals as an exception mainly on account of stockpiling by China and continued investments in infrastructure by China and India, energy remained in negative territory of 3.2%. The decline in livestock and agriculture indices showed continued decline of public consumption demand for foodstuff on account of escalating poverty in many poor countries and increasing unemployment in developed and developing economies. We don't foresee industrial and base metal prices maintaining a sustainable uptrend until the second quarter of 2010, though minor up-cycles are possible due to speculators, CTAs and intermediary investors such as ETFs and ETNs.



Precious metals, on the other hand, continued their uptrend, mainly on account of the 'where-to-hide' factor during the recent financial crisis and as an asset of the last resort following the near collapse of the global financial system and recession. Gold has gained around 17.7% since the beginning of this year and currently consolidating for another 17% to 18% jump (\$1200-1250/oz.) in the coming months supported by a weakening dollar and the gold season ahead until February 2010. Silver has recorded huge year-to-date appreciation of 55.4% and so also Platinum by 45.7% and Palladium by 73.6% until the beginning of the third week of September, though prices of these precious metals started correcting recently as increasing optimism surrounds global growth prospects. We expect precious metal prices to remain strong until the end of the current year and may gradually start easing during the first quarter of 2010 as funds move into other productive assets. The Dow Jones UBS Precious Metal Sub-Index which proxies for the precious metal segment recorded a 9.5% year-to-date return so far by the third week-end of September and after a short correction may continue further by another 20% before correcting when global growth prospects become more visible.



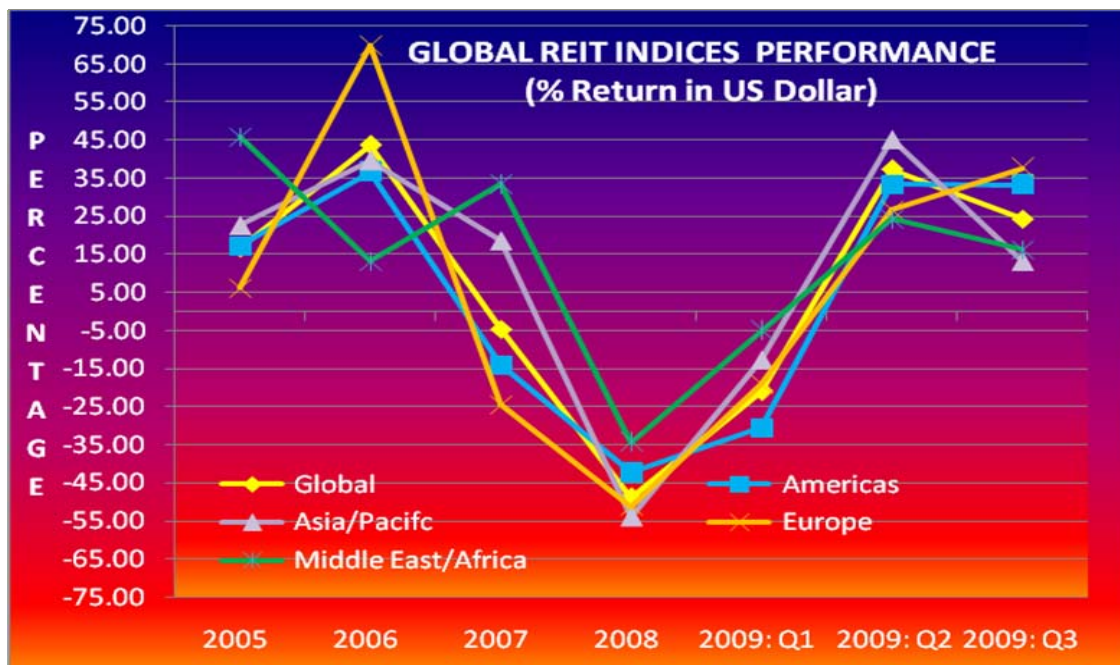
Source: QuoteMedia.com

Real Estate

The prospects of global real estate investing though varying widely across different regions are still quite uncertain in the medium term on the backdrop of bleak US industrial and employment outlook. In the US the total value of "specially serviced" loans grew from \$8.2 billion in January to \$46.9 billion in September according to a study by CoStar Group. The study also identified nearly \$80 billion in "seriously delinquent" loans to go along with \$6.3 billion in properties seized by banks through foreclosure. We could envisage rental income



falling if the global downturn continues which will again have an adverse impact on real estate prices. In the real estate sector, REITs are best placed to take advantage of value opportunities and their ability to raise equity and leverage positions. During the second and third quarters of 2009, global REITs have been able to recover almost 88.1% in lost value over 2008 and the first quarter of 2009. In the Americas, the recovery has been around 91.4%, while in Asia Pacific around 87.5%, in Europe 91.4% and in Middle East & Africa region around 102.6%, over the same period.



Source: Data obtained from NAREIT

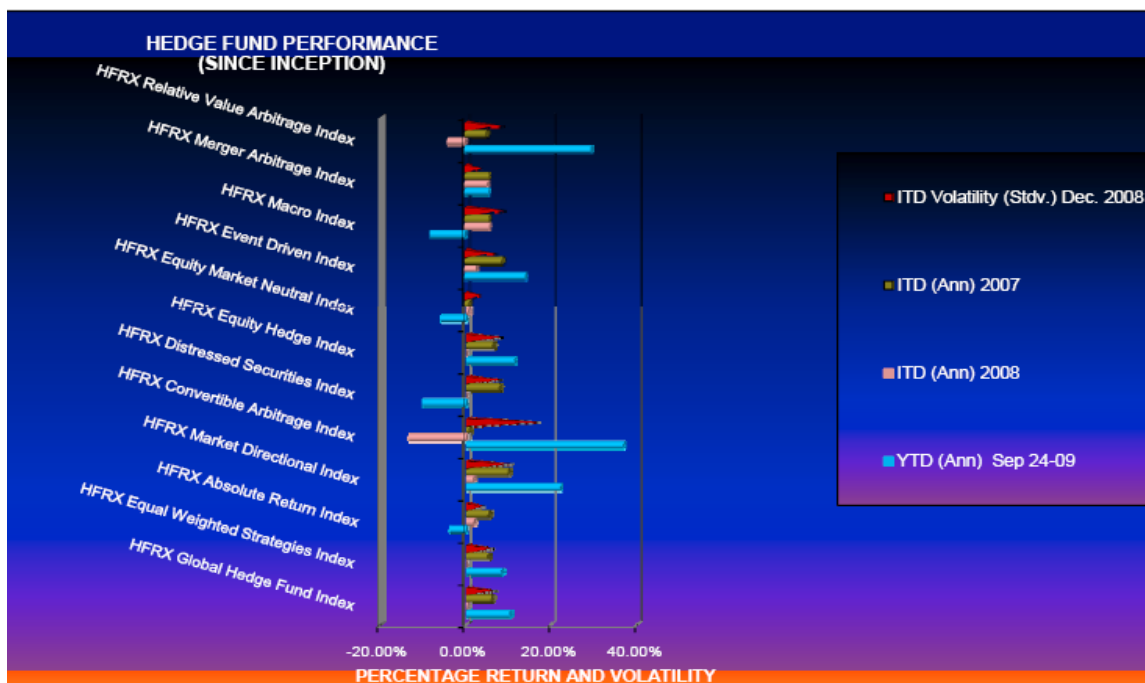
Direct Investments

Direct investment opportunities related to mergers and acquisitions, private placements, structured deals as well as through private equity and venture capital funds declined considerably during the first nine months of 2009 as the revival of global economies still remain uncertain at large. The global value of deals fell 37 per cent to \$1.62 trillion as compared to \$ 2.57 trillion during the same period last year. Third-quarter deal volume of \$412.4 billion was down 34 per cent from the second quarter and most of the deals so far are distressed situations except for a few strategic moves such as Pfizer's \$68 billion takeover of Wyeth. Secondary investors still shy away from such opportunities. In the private equity and venture capital space, fundraising has been abysmal on account of the uncertain environment. In the US, 25 venture capital funds raised \$1.7 billion in the second quarter of 2009 as against \$4.61 billion raised by 49 funds in the first quarter of 2009. In Europe, the private equity and venture capital industry is in limbo on account of the new EU law. The extremely hostile exit



market had made it virtually difficult for funds to recycle during the first half of the current year. So far, most of the IPOs came from large corporations in China and other Asian countries. Global equity capital market offerings were up 4 per cent at \$547.6 billion for the first nine months of 2009, compared to the same period last year. The third quarter has also seen the highest quarterly volume of IPOs globally – reaching \$26.1billion – since the second quarter of 2008. However, of the five \$1 billion-plus IPOs priced during the third quarter, four were Chinese, including China State Construction’s \$7.3 billion IPO and a \$5.1 billion deal from Metallurgical Corp of China. Equity capital market offerings in the US fell sharply to \$32.7billion during the third quarter after record-breaking second-quarter volumes of \$105.8billion on huge levels of equity issuance to fund TARP (troubled asset relief programme) repayment. In Europe, the IPO market was virtually negligible at around \$753 million, though equity private placements were as high as \$135.5 billion during the first nine months, just \$31billion less than the total for 2008. As equity markets improved during the third quarter and volatility subsided, it seems the markets may be moving from distressed to a growth scenario, however, it is too early to bet on account of macro uncertainties.

Hedge Funds



Source: Data obtained from Hedge Fund Research Institute

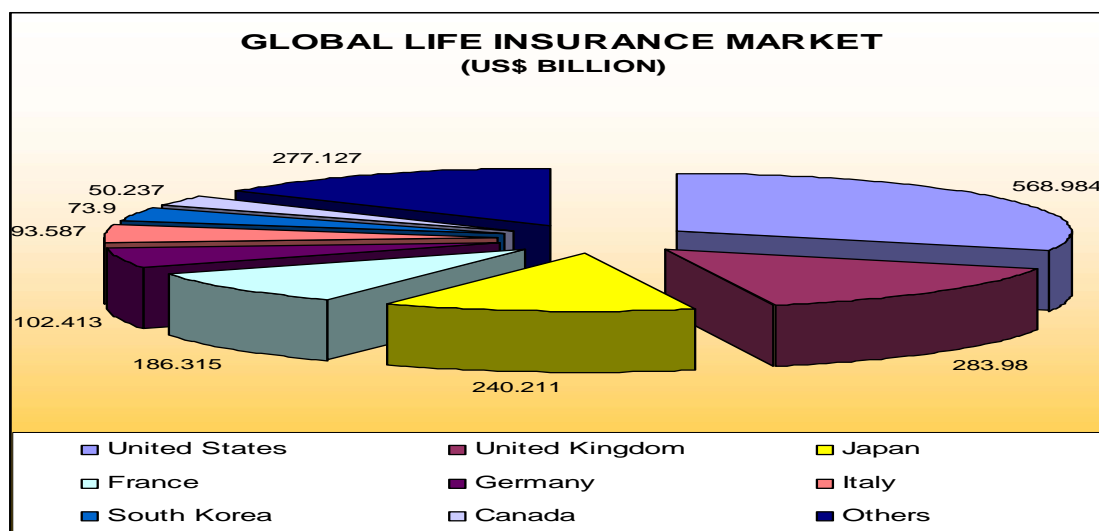
Assets invested in the hedge fund industry increased by \$100 billion in the second quarter of 2009, ending at \$1.43 trillion, according to figures released by Hedge Fund Research, Inc., a



leading provider of hedge fund industry data. This marks the first quarterly increase in assets since 2Q 08, when total industry capital peaked at \$1.93 trillion. The recent asset growth was fueled by performance gains, as the HFRX Global Hedge Fund Index gained 10.34% spurred by a gain of 36.79% in Convertible Arbitrage, 29.28% in Relative Value Arbitrage, 22.02% in Market Directional and 14.03% in Event Driven strategies. Regionally, hedge funds focusing on the Emerging Markets such as China, India, BRIC and Russia were the star performers with year-to-date gain of 41.39%, 38.45%, 31.89% and 31.69%, respectively by the end of August 2009. Over the same period, on a sector specific basis, Alternative Energy, Energy Infrastructure and Metals stole the show with year-to-date gain of 31.7%, 22.19% and 19.55% respectively. However, investors looking at hedge funds should consider the long-term risk-return characteristics of different strategies and should not get carried away by short-term gains. In this regard, Event Driven, Distressed Securities, Merger Arbitrage, Market Directional, Equity Hedge, Absolute Return, Relative Value Arbitrage, Macro and Equal Weighted Strategies are far superior.

Life Settlements

Starting this quarter, we are adding a new asset class 'Life Settlements' to our coverage of alternative asset classes. The secondary market on Life Settlements was valued at \$16 billion in 2008 according to a study conducted by Life Insurance Settlement Association (LISA) and is expected to grow to between \$90 billion and \$140 billion by 2016 according to Conning Research and Consulting. Existing and potential secondary markets on life settlements are prevalent in most of the developed and developing economies with more than 50% in the US, UK and Japan alone, with the rest of the world catching up slowly.



Source: OECD Insurance Statistics, 2008



The life settlements alternative asset class provides significant risk mitigation through portfolio diversification, particularly during adverse economic conditions as risk minimization becomes extremely desirable. Return on life settlement assets vary between 9% and 13% with very high return to risk reward ratio of 7.57 times as they have low volatility and skewness as compared to traditional asset classes.

Index	QxX	SPX	AGG	IYR	GSG
Mean	0.00197	-0.04156	0.00048	-0.059	-0.05087
SD	0.00026	0.05939	0.02439	0.13063	0.12076
Skewness	0.32696	-0.55358	1.89962	-0.52456	-0.22117

Note: QxX Index is the Goldman Sachs's Longevity Mortality Index, S&P 500 Index (SPX), the US iShares Aggregate Bond Index (AGG), the US iShares Dow Jones Real Estate Fund Index (IYR) and the US iShares S&P GSCI Commodity Indexed Trust(GSG).

Life settlements are based on longevity and mortality and are thematically in line with Pension and Sovereign Funds' investment objectives with negative and very little correlation with traditional asset classes. As human mortality is uncorrelated with the movements of financial markets, life settlements can provide steady returns regardless of the state of the financial markets.

Index	QxX	SPX	AGG	IYR	GSG
QxX	1.00	0.09	-0.35	-0.16	0.21
SPX	0.09	1.00	-0.45	0.39	0.54
AGG	-0.35	-0.45	1.00	0.44	-0.09
IYR	-0.16	0.39	0.44	1.00	0.44
GSG	0.21	0.54	-0.09	0.44	1.00

The uncorrelated nature of this alternative asset makes it an integral part of portfolio diversification and risk management strategy with the growing trends to explore this asset class.

Asset Allocation Perspective

We still believe that considerable global risk is ahead of us in terms of the spill-over effect of the recession in the developed economies to emerging economies and further to the private sector. While major economies such as the US, Japan, Germany and France are showing some signs of improvement and major developing economies such as China and India are still growing at an attractive rate, the sustainability of global growth will much depend on improvement in structural deficiencies in these countries and a more equitable distribution of wealth within and among nations. Looking ahead, the asset markets are going to be on a



bumpy ride with sporadic uptrends and hiccups, as investors switch among different asset classes looking for better returns. Under such a scenario, we suggest that investors should calibrate different asset allocation options keeping their risk low. Investors can contact us at postmaster@smartinternationalholdings.com for their specific needs such as investment policy statement, investment objectives, global investment and asset allocation strategy.

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