Fasten your seat belt

Asian Equity Derivatives Strategy – 3Q12

July 2012

BNP PARIBAS
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For the past few months, Asian equities have been sold down and many short positions have been accumulated. Valuations have contracted to levels similar to last year's lows. The negative sentiment should be fairly priced-in at this stage.

We cannot rule out a potential de-risking triggered by further shocks in Europe. However, we believe that renewed intervention from central banks could trigger massive short-covering and bargain-hunting activities. This should lead to a rebound in risky assets.

With the extremely low interest rate environment, including low deposit rates and unattractive bond yields, investors should be willing to take risk to buy equities. Equity yields are at attractive levels versus bond yields. We believe that any asset allocation shift from bonds to equities could generate strong upward pressure in favor of equities. We suggest investors accumulate quality companies that can deliver decent yields. We prefer upside exposure with buffers or relative value strategies.

Risk parameters, implied volatilities, skews and convexities have eased from recent peaks. Despite the recent sell-off, implied volatilities and skews have not reached the levels seen at the time of the Lehman or 2011 debt crises. This is one of the key reasons we believe the bottom may be further down the road. As we believe the tail risk should be diminishing given a potential "global put" from Central Banks, we suggest investors buy put-spreads and sell the tail risk taking advantage of the rich convexity.

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I. Asian Equities Outlook

Winner Lee and Guillaume Derville

Second Quarter Legacy: The second quarter started in a risk-off mood. In our report *Watch your back* (16 February), we were cautious on Asia ex-Japan but remained upbeat on Japanese equities since the Bank of Japan (BoJ) started quantitative easing. In *All eyes are on the BoJ* (26 April), we highlighted the extraordinary flat skew situation in Japan, reflecting the fact that investors were positioned for a potential rally on NKY via upside Calls. The rally didn't materialize as risk aversion increased on the back of renewed European debt concerns. During the recent risk off process, the convexity of Japan indices exceeded the peak of the Lehman Crisis and came close to last year's peak. Investors were willing to sell convexity on Japan as the BoJ cushioned the downside by continuing to buy ETFs (on NKY and TPX).

In our 2Q Strategy report published on 19 April, we reiterated our cautious stance as we developed our argument around the *Complacency* theme (which we initiated in *Asian Sniper* on 22 March). In order to take advantage of the flat skew situation in the Asia-Pacific key indices, we advised investors to sell calls and buy puts. In May, the China AH arbitrage trade delivered good performance as the global risk-off intensified. We advised investors to unwind some of the AH pairs (ZTE, CM Bank, Ping An and Anhui Conch) on 17 May when the pairs reverted to mean.

Third Quarter Outlook: For the past few months, Asian equities have been sold down. Many short positions have been accumulated. Valuations contracted to similar levels as last year's lows. Both NKY and TPX are trading around 1x book value (better references as corporate earnings decline), which should be a strong support level as the book values of Asian companies remain intact. The negative sentiment should be fairly priced-in at this stage. During 2Q, the strength of the USD induced a lack of liquidity in equity markets (DXY strengthened from 78 to 83). This led to foreign outflows from Asia (ADXY broke below the low of last year) and we observed a shrinkage in Asian equity volumes.

We cannot rule out a potential de-risking that could be triggered by further shocks in Europe. However, we believe we will see more joint efforts from European leaders aimed at preventing a disaster (a proposed EUR750b bailout was being discussed at the G20 Summit and may be confirmed during the EU Summit on 28-29 June). Maintaining a cohesive eurozone is crucial for global stability and recovery. US Fed Chairman, Ben Bernanke, decided to extend Operation Twist by another six months to the end of December. The action will continue to depress long-term bond yields. He also sent out a message that Quantitative Easing (QE3) remains an option: *"If we are not seeing sustained improvement in the labor market then it would require additional actions."* We believe the Fed wants to save some bullets in case of further deterioration of the sovereign debt problem or growth issues. In a nutshell, it is a matter of liquidity flow: renewed intervention from central banks could trigger massive short-covering and bargain hunting activities. This should lead to a risky assets rebound as investors are sitting on the sidelines waiting for buying opportunities.

Q3 Strategy – Looking for buying opportunities: In the current extremely low interest rate environment (including low deposit rates and the unattractive bond yields), investors should be willing to take risk in buying equities as compared to bond yields, equity yields are at attractive levels. The S&P dividend yield is now 52bp higher than the US 10-year treasury yield and the yield spread is 4bp below last year's peak (56bp) and 70bp below its historical peak (1.23%). We believe that any asset allocation shift from bonds to equities could generate strong upward forces in favour of equities. We suggest investors accumulate quality companies that can deliver decent yields. We prefer upside exposure with buffers or a relative value strategy.

Turning bullish when derivative parameters are becoming stressed: Risk parameters, implied volatilities, skews and convexities have eased from recent peaks. **We have yet to see volatility and skew levels in the recent risk-off reach the levels seen during the Lehman Crisis or during the sovereign debt crisis last year. This is one of the key reasons, we believe, that the bottom may be further down the road.** Investors should monitor skew movement which reflects market sentiment and provides a good entry point. The surge in skew (implied volatility of Put minus implied volatility of Call) reflects a strong demand on protection versus upside exposure. Investors should be contrarian and turn bullish as the sentiment turns bearish.

Long delta in volatile markets: During the 2008 Lehman Crisis and 2011 European Debt Crisis, markets reached bottoms when volatilities and skews surged to distressed levels. At that time, long delta was a better way to get upside exposure as buying upside call was expensive as volatilities spiked up to roof. Under extremely bearish sentiment, investors are reluctant to sell put to finance upside calls. The current 3M skew levels are on average 3.2 vol-pt below last year's peaks and 2 vol-pt below the Lehman Crisis peaks. When markets are stressed, we suggest setting up a cushion collar to get upside exposure by selling a Down-and-In Put and buying a Call Spread at zero cost. Upon a high skew situation the knock-in barrier of the Put will be at a much lower level, making it harder to knock-in.

Comparison of 2008 Lehman Crisis and 2011 European Debt Crisis Peaks Using 3M and 1Y 90-110% Skews

Index	Current 3M 90-110% Skew	Current 3M 90-110% Skew (Percentile)	Last Year's peak 3M 90-110% Skew	Lehman Crisis' peak 3M 90-110% Skew	Current 1Y 90-110% Skew	Current 1Y 90-110% Skew (Percentile)	Last Year's peak 1Y 90-110% Skew	Lehman Crisis' peak 1Y 90-110% Skew
HSI	7.1	73.6	11.9	10.1	4.3	77.2	6.4	5.0
HSCEI	6.8	78.6	11.5	9.0	4.2	80.3	6.1	4.8
KOSPI2	7.4	74.2	12.8	10.0	3.7	59.1	5.8	5.2
TWSE	6.8	88.0	9.9	7.3	4.1	92.7	5.0	4.0
MSCI Sing	7.1	91.2	9.2	8.0	4.0	84.6	4.9	4.7
AS51	8.7	80.1	10.6	9.9	5.2	84.5	5.7	5.4
NKY	7.2	48.5	11.6	11.4	4.4	35.9	6.1	5.4
TPX	7.1	45.7	11.6	11.3	4.4	35.1	6.1	5.4

Note: Data as of 18 June 2012, percentile rank using data since 2008
Source: BNP Paribas

The valuation correction of Asian equities is close to last year's trough: According to our comparisons (based on the lowest P/E and P/BV of last year and the Lehman Crisis troughs), we are at levels that are close to the lows of last year.

3Q Strategies: We prefer upside exposure with buffers or relative value strategies. As we believe the tail risk should be diminishing given a potential "global put" from Central Banks, we suggest investors buy put-spreads and sell the tail risk taking advantage of the rich convexity.

Strategy 1: Buy Asia High Yield Basket and Sell MSCI Asia ex-Japan

Strategy 2: Zero-Cost Upside Exposure – Cushioned Collar

Strategy 3: Buy Gold (delta & volatility) in Euro

Strategy 4: Buy China Infrastructure Basket and Sell HSCEI

Strategy 5: Risk-adjusted Upside Exposure on China Banks [Worst-of-Call]

Strategy 6: China to Outperform India [Outperformance Call, Call vs Call]

Strategy 7: Hedging for Further Shocks in Europe [Put Spread, Put Condor]

Strategy 8: Sell Convexity to Finance Buying Put Spread

II. Key Themes and 3Q Strategies

Theme 1 – "From Easing to Risk-on Mode"

Winner Lee

Step One: Asian Easing is required to withstand any external shock

Asian easing has started: In our 2Q12 Quarterly Strategy we said: *we cannot ignore the potential de-risking in Europe and the US, the China slowdown, or the Japanese fiscal situation, and we do also understand, and often share, the adage "Don't Fight the Central Banks".* Over the past quarter, we have observed that central banks in Asia-Pacific have taken more proactive easing measures to tackle the external shock, given that inflation has pulled back.

- **Japan – BoJ easing:** On 27 April, the BoJ stepped up its fight against deflation by boosting the volume of JGB purchases and buying domestic assets. The net increase of JPY5t in its asset-purchase program was in line with market expectations, but the decision to buy an additional JPY10t of JGBs as part of that came as a surprise. On 7 May, the BoJ took action by buying JPY39.7b worth of ETFs and JPY2.3b of REITs. As we have discussed in the past, the Nikkei and Topix ETF purchases continue to put pressure on NKY and TPX volatilities.
- **China – monetary easing and fiscal stimulus:** China's economic figures were mixed with poor domestic demand, PMI remaining sluggish and investment growth stabilizing. There is strength in exports and imports but our China Economics Team does not think this is sustainable. With core inflation pulling back to 3% in May, the People's Bank of China (PBoC) started its first round of rate cuts (both benchmark deposit and lending rates by 25bp) on 8 June. Our China Chief Economist, Xingdong Chen, is expecting one more cut in interest rates in 3Q (most likely in August), unless the deterioration in the economy is worse than expected. He is expecting three more RRR cuts (totalling 150bp) to shore up money growth. In terms of domestic liquidity, May's new loans climbed to RMB793.2b, up RMB111b from April, representing 43.8% y-y growth. We believe this is supportive for countering China's sluggish economic growth. For the fiscal measures, we think they would be related to stimulating domestic consumption (such as household subsidies and infrastructure projects) to support employment.
- **China's stimulus for Hong Kong equities:** According to Hong Kong newspaper Ming Pao (15 May 2012), China's policymakers are planning to allow about USD50b (HKD400b) of QDII for mainland investors to buy Hong Kong-listed shares, signaling support for the new Hong Kong government. The market expects the good news to be announced after the new Chief Executive, Leung Chun-Ying, takes office on 1 July.
- **India – RBI easing, but is being hindered by high inflation:** The RBI cut the Cash Reserve Ratio (CRR) by 75bp on 9 March, followed by a cut in the repo rate of 50bp (to 8%) in April. However, India's re-accelerating inflation is frustrating. Its WPI inflation revised up to 7.69% (from 6.89%) in March, and May's figure was worrying at 7.55%. In response to this, in their June meeting the RBI put interest rate and CRR cuts on hold which surprised the market on the negative side. BNPP's Economics Team expect only a 50bp rate cut for the rest of 2012, and they have correctly pointed out that high food inflation will give limited room for further monetary easing in India.

- **Australia – RBA easing:** The RBA cut the cash rate by 50bp to 3.75% at its May board meeting and revised down its growth and inflation forecasts. On 5 June, they cut rates a further 25bp and left room for further cuts. BNPP's Regional Economist Dominic Bryant is expecting another 25bp cash rate reduction in July, and then staying flat for the rest of the year. He sees the labour market as firming, and with continued strength in the mining sector he believes the RBA is likely to be far more resistant to additional easing than the market has been pricing in (75bp cut for the rest of 2012).

BNP Paribas Global And Asia Pacific Interest Rates Forecasts

(%)	2010	2011	1Q12	2Q12	3Q12	4Q12	2013
China (1Y lending rate)	5.81	6.56	6.56	6.31	**6.06**	6.06	6.06
Hong Kong (HKMA base rate)	0.50	0.50	0.50	0.50	0.50	0.50	0.50
India (Repo rate)	6.25	8.50	8.50	8.00	8.00	**7.75**	7.50
Korea (7-day repo)	2.50	3.25	3.25	3.25	3.25	3.25	3.25
Taiwan (Discount rate)	1.625	1.875	1.875	1.875	1.875	1.875	2.250
Australia (Cash rate)	4.75	4.25	4.25	3.50	**3.25**	3.25	4.25
US (Fed funds rate)	5.81	6.56	6.56	6.31	6.06	6.06	6.06
Eurozone (Refinancing rate)	1	1	1	1	1	1	1.5

Source: BNP Paribas

Step Two: Europe and US Easing

- **Europe – Rate cut likely on further weakness:** According to *Market Mover* on 14 June, our European Economist reckons that *the rise in Spanish 10-year yields towards 7% and the speed at which the risk environment has soured, showed that the markets have not embraced the Spanish bank bailout plan in June. The longer the uncertainty prevails, the higher the probability the markets will become firmly shut to Spain and a full-blown bailout will become a necessity. What worsens the situation is that the economic outlook continues to deteriorate, with implications for inflation prospects. Hence, further weakness should open the door to a rate cut as soon as July's meeting."* The most likely scenario is a refinancing rate cut of 25bp.

- **EUR750b bailout was proposed:** According to the UK's *The Telegraph* (20 June), *"EU leaders are poised to announce a EUR750b deal to bailout beleaguered Spain and Italy by buying the countries' debts. Angela Merkel and other EU leaders have come under intense pressure at the G20 Summit on 20 June to take radical action to stem the growing euro crisis. Under the proposed deal, two European rescue funds – EUR500b European Stability Mechanism (ESM) and EUR250b European Financial Stability Facility (EFSF) – will be able to buy bonds issued by beleaguered European countries."* We think more concrete measures are likely to be confirmed during the EU Summit on 28-29 June.

- **US – QE3 and OT2:** The US Fed decided to extend its Operation Twist (OT) program until the end of this year, after the FOMC meeting on 20 June. The size of OT will be expanded by USD267b from the current USD400b, which will end in June. The Fed's official forecasts for 2012 GDP have been revised down to 1.9-2.4% from 2.4-2.9%. Chairman Bernanke reiterated that further action is necessary to support the economy if they do not see continued improvement in the labour market. He also revealed that QE3 remains an option: *"additional asset purchases would be among the things that we would certainly consider."* BNPP's North America Chief Economist, Julia Coronado, commented that the Fed's announcement *"has the feel of buying time as FOMC evaluates other options for supporting the economy"* and is expecting to see some more easing before year end. Some market participants are expecting QE3 to be announced as soon as the next FOMC meeting on 1 August, but we think overlapping of OT and QE is less likely, unless the US economy deteriorates dramatically.

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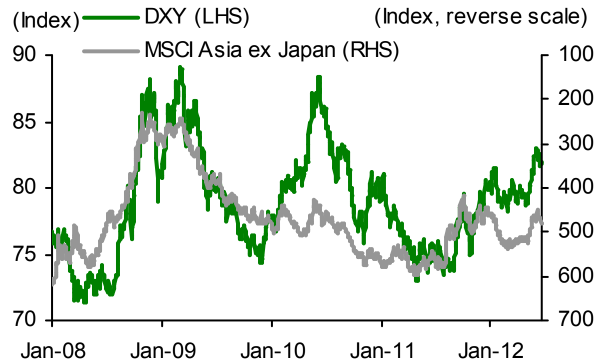
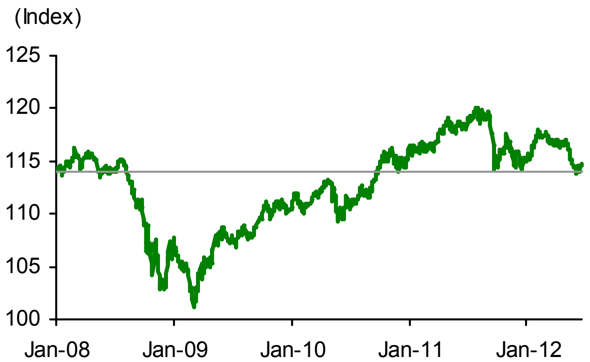
Step Three: Risk-On Mode, liquidity to return to risky assets

Asia outflows in 2Q: The USD de-risking process has dragged down Asia ex-Japan equities by a maximum of 16.1% since late February, whilst DXY strengthened by 6.1% to 83.0 on 31 May. However, the ADXY only weakened 2.7%. The key movers are the INR that depreciated by 13% against the USD from its YTD peak, to USD/INR55.9775 currently; followed by the IDR (-5.9%); KRW (-3.6%); and SGD (-2.5%). The current ADXY, which is highly correlated with Asian equities, is very close to the trough of last year, an important technical support level. The question is whether liquidity will come back. Indeed, the ADXY is still struggling to break up or down at the support level.

DXY strengthened 6.1% since late February



ADXY weakened 2.7% from its YTD peak



ADXY comprises of CNY (37.9%), KRW (13.69%), SGD (10.27%), HKD (9.22%), INR (7.52%), TWD (7.04%), THB (4.93%), MYR (4.53%), IDR (3.0%) and PHP (1.9%). Source: Bloomberg

Significant outflow from Asia-4 during 2Q12: Japan recorded massive outflow of USD9.1b since mid-April, reducing the maximum YTD foreign inflows of USD19b to only USD10b. In 2Q alone, the net outflows were the highest at USD6.2b. Taiwan and Korea recorded total foreign outflows of USD5.5b and USD3.3b since the beginning of 2Q with the majority leaving in May. Surprisingly, India's outflow situation was negligible at USD223m despite its deteriorating macro outlook.

Regional Equity Fund Flows (Asia-4)

(USD b)	2009	2010	2011	1Q12	2Q12
Taiwan	14.8	9.2	(9.5)	5.0	(5.5)
Korea	24.8	19.0	(7.2)	9.6	(3.3)
India	17.6	29.3	(0.5)	8.9	(0.2)
Japan	17.1	38.0	22.3	16.2	(6.2)
Total	**74.3**	**95.5**	**5.1**	**39.7**	**(15.2)**

Note: Taiwan, Korea, India – daily data; Japan – weekly data with one week time lag. Fund flow data up to 18 June 2012.

Sources: Bloomberg; BNP Paribas

Appreciating Asian currencies are beneficial for equities in the region. BNPP's FX Team is expecting most Asia-Pacific currencies to appreciate. They forecast the KRW to appreciate 5.22% against the USD by end-2012, followed by INR (3.66%) and TWD (2.98%). The AUD could appreciate 10.6% to 1.12. Our FX Team is expecting the JPY to weaken to 85 by 2Q and then appreciate to 78 by end-2012.

We are concerned about the INR, as Standard & Poor's warned it could downgrade the country's investment grade to junk. Our Regional FX Strategist Chin Loo Thio, has already adjusted USD/INR forecasts due to India's twin deficits and potential capital outflows.

BNP Paribas Asia Pacific Currency Forecasts

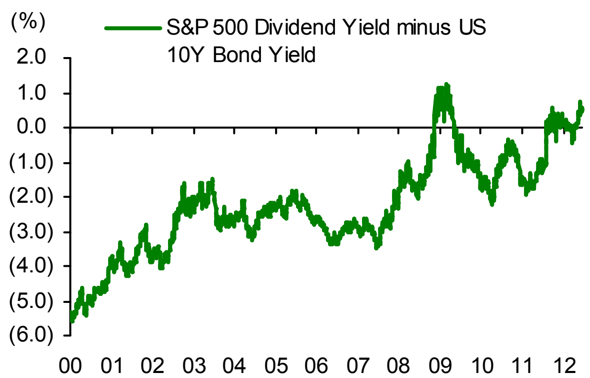
Currency	June Spot	4Q11	1Q12	2Q12	3Q12	4Q12	2013	% appreciation Current to end-2012
USD/SGD	1.27	1.3	1.24	1.28	1.26	1.24	1.15	2.22
USD/HKD	7.76	7.8	7.8	7.8	7.8	7.8	7.8	(0.52)
USD/RMB	6.36	6.29	6.32	6.33	6.31	6.29	6.2	1.06
USD/TWD	29.87	30.3	29.5	30	29.5	29	27.5	2.98
USD/KRW	1157	1152	1120	1200	1150	1100	1050	5.22
USD/INR	55.98	53.07	50	56	54	54	50	3.66
USD/JPY	78.99	77	76	85	80	78	80	(1.25)
AUD/USD	1.01	1.02	1.06	1.02	1.06	1.12	1.05	10.55

Note: Spot levels as of 19 June 2012
Source: BNP Paribas – Asia FX and Rates Compass – 11 June 2012

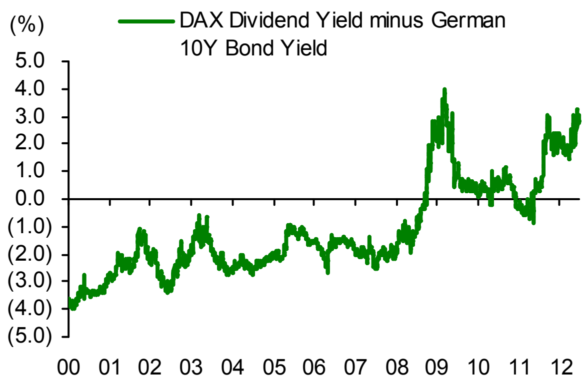
Get ready for a risk-on mode, liquidity needs to park somewhere: We believe market movement is a matter of liquidity flow: short-covering, bargain hunting and shifting from bonds to equities could generate a strong upward force on equities. The S&P dividend yield is now 52bp higher than the US 10-year treasury yield (having eased from the YTD peak of 74.8bp on 1 June), and the yield spread is 4bp below last year's peak (56bp) and 70bp below its historical peak (1.23%). Gold is our preferred asset class due to further global quantitative easing, especially if the Fed is going to implement QE3.

German Bonds are acting as a safe haven within the eurozone: Investors were selling bonds ahead of the Greek Election on 17 June. This has two implications: 1) investors were ready for a risk-on mode; or 2) investors were afraid that Grexit would cause a euro collapse, thus making German bonds no longer safe. The risk of Greece leaving the euro and causing a further crisis across Europe has reduced since the country's left-wing party Syriza finished second in the recent elections (with 26.9% of votes) with the New Democracy Party (pro bailout) gaining 29.7% of votes. Similar to the situation in the US, Germany's equity yield is 2.8ppt above the 10Y bond yield (max of 4% in March 2009). Thus, a shift from bonds to equities could also happen in Europe soon.

US Equity minus Bond Yield Spread



Germany Equity minus Bond Yield Spread

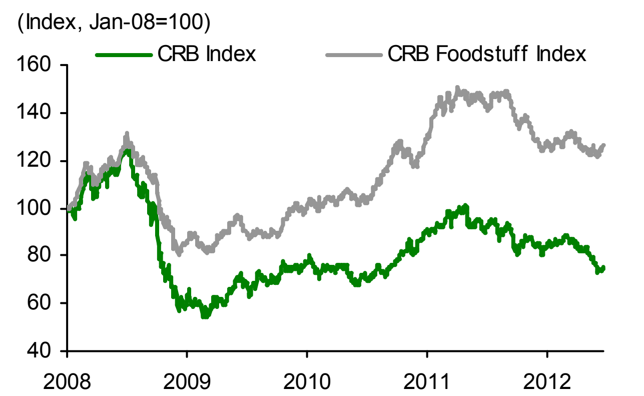


Note: Yield spread data up to 18 June 2012
Source: Bloomberg

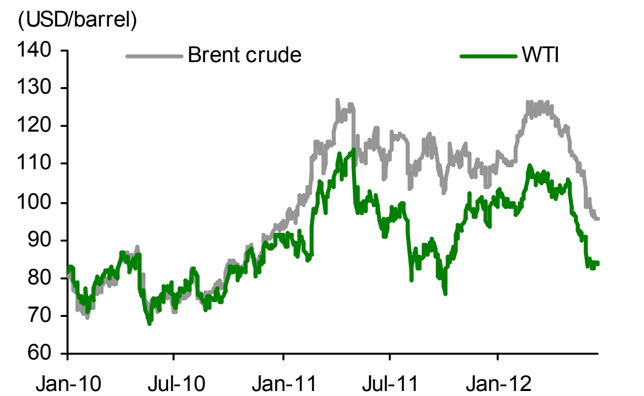
Commodity space: The de-risking process for commodities started earlier than the correction in US equities, but at a similar time to the emerging market (EM) equities correction in late February. CRB fell 14.9% from its YTD peak and foodstuffs eased 2.5%. The fall in commodities helps inflation to ease and therefore puts less pressure on Asian central banks to cut interest rates, which is crucial to cushion further external shocks.

Volatility on Oil and Gold: WTI collapsed by 24.7% from its YTD peak of USD109.77/bbl, and the 3M implied volatility surged from its YTD low of 23.4 vol-point to the recent peak of 37.7 vol-point, up 14.3 vol-point. For Gold (GLD US), the shift in the implied volatility is a lot less at 7 vol-point compared to the recent 23 vol-point. However, the 3M realized volatility on both WTI and Gold are hardly gains. **BNPP's Head of Commodity Derivatives Strategy Harry Tchilinguirian, is expecting WTI to recover to USD105/bbl by end-2012, 25.1% potential upside from the current level. Investors can consider Buy Call on WTI or accumulate Asia Oil companies from current levels. Our best pick is CNOOC (883 HK) in our Asia High Yield BUY basket of Strategy 1.**

CRB Fell 14.9% from YTD Peak

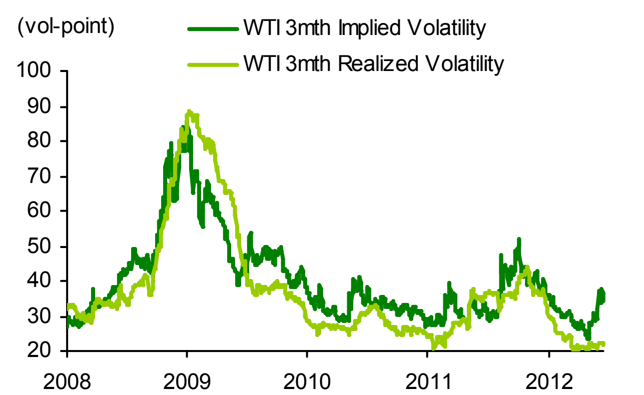


WTI Corrected 24.7% from YTD Peak

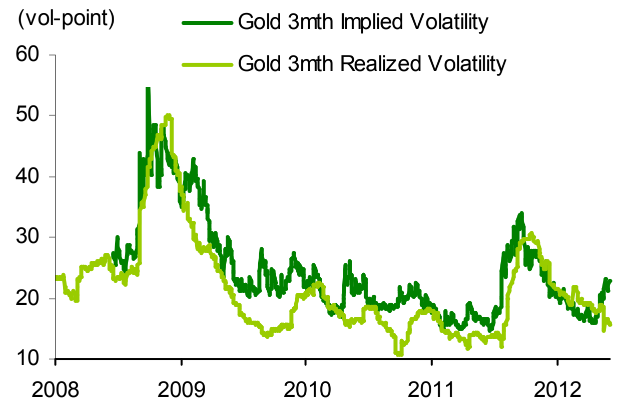


Source: BNP Paribas

3M Implied and Realized Volatility on WTI



3M Implied and Realized Volatility on Gold



Source: BNP Paribas

Strategy 1: Asia High Yield BUY Basket

Winner Lee

⇨ **Buy Asia High Yield Basket and Sell MSCI Asia ex-Japan Total Return Swap [NDUECAXJ; USD 3M Libor – 20 bps]**

Rationale: Accumulate quality companies that can deliver high yield

BNPP BUY stocks: Under the extremely low interest rate environment and with the recent global risk-off, equity yield is becoming more attractive. We advise long-term investors to accumulate quality companies that can deliver high yield. We have selected 10 high yield stocks that BNPP rates BUY recommendation and that have at least 20% upside potential.

Beta of 1.0659: Investors can consider buy-on-dip on this Asia High Yield Basket. The basket is trading at very tempting valuations of 8.2x P/E and 5.6% dividend yield in 2012. With the high yield spread over deposit rate, we are expecting the basket to be attractive. For relative strategy, the Asia High Yield BUY basket has a beta of 1.0659 over the MSCI Asia ex-Japan, and therefore should rebound better than the benchmark. The Asia High Yield Basket can trade up to USD30m per day, while MSCI Asia ex-Japan Total Return Swap can trade up to USD30m-200m per close (breakable with 30bp break fee).

Asia High Yield BUY

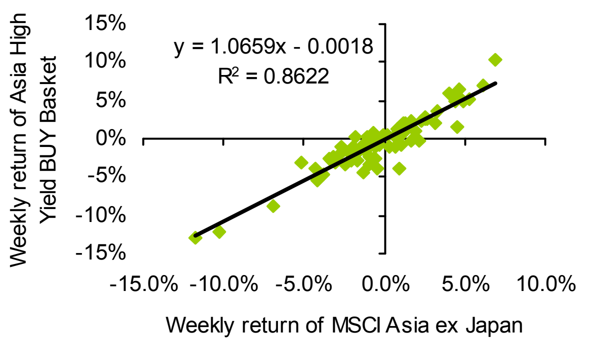
Code		Sector	Share price	Target price	Upside (%)	2012E P/E (x)	2012E P/BV (x)	2012 DY (%)	Weight (%)
017670 KS	SK Telecom	Telecoms	122,000	180,000	47.5	4.4	0.5	7.9	10.0
030200 KS	KT Corp	Telecoms	28,600	39,000	36.4	4.5	0.5	7.1	10.0
3988 HK	Bank of China 'H'	Banks	2.91	3.63	24.7	5.0	0.8	6.6	9.9
1398 HK	ICBC	Banks	4.43	6.09	37.5	5.1	1.2	5.7	10.0
010950 KS	S-Oil Corp	Energy	95,400	132,000	38.4	7.8	1.9	5.4	10.0
1301 TT	Formosa Plastics	Materials	79.4	97.00	22.2	11.5	1.9	5.1	10.6
1171 HK	Yanzhou Coal	Energy	12.58	24.90	97.9	6.0	1.2	5.4	9.7
11 HK	Hang Seng Bank	Banks	103.3	143.42	38.8	10.2	2.3	5.0	10.0
388 HK	HK Exchanges	Financials	109.9	155.88	41.8	19.3	12.5	3.8	9.9
883 HK	CNOOC	Energy	15.3	18.30	20.0	7.8	1.8	3.5	9.9
Average					**40.5**	**8.2**	**2.5**	**5.6**	**100.0**

Sources: Bloomberg; BNP Paribas

Asia High Yield Basket

Source: Bloomberg

Market Beta = 1.0659



Note: regression using weekly returns since 2011

Strategy 2: Zero-Cost Upside Exposure – Cushioned Collar on Asian Indices

Winner Lee

⇨ **Buy Dec-12 ATM-125% Call Spread and Sell Dec-12 ATM Down-and-In Put with different Knock-In barriers on NKY, TPX, HSI and HSCEI at zero cost [Continuous monitoring] (indicative)**

Rationale: Take advantage of the steep skew to get free upside exposure

We initiated this idea on 7 June, when we became aware of the steep downside skew situation and when the market corrected to the comparable valuations of last year's troughs. We suggest selling the Down-and-In Put (DIP) as we believe the tail risk is low given that European leaders want to maintain a cohesive Eurozone. After the Greek election results were confirmed and with less concern over a possible Grexit contagion, the tail-risk has actually been diminishing, reflected by falling skew and convexity.

Asian Sniper-070612.pdf: http://www.bnppresearch.com?E=cadjdkbgff

Cushioned Collar – zero cost upside exposure on Asia: The structure involves buying an ATM-125% Call Spread and financing it by selling an ATM DIP. This is an approach to sell the tail-risk on expectation that the index will not touch the DIP barrier. Investors will not lose money if NKY, Topix, HSI and HSCEI do not correct more than 10.5%, 11.5%, 12% and 13.5% respectively from current levels at maturity. We believe adding a 25% cap on the upside is reasonable given that the global economic recovery will be tough.

Steep downside skew: The downside skews of the regional indices were much steeper on 7 June, therefore the DIP barriers were a lot lower. The current DIP barriers shifted up a bit and become less attractive. However, investors can re-visit the idea whenever the downside skews return to the elevated levels, which could possibly happen should there be any shock in Europe during 3Q.

Better risk-reward profile: The Cushioned Collar provides a better downside risk profile than a simple long portfolio, as investors are basically avoiding losses on the downside unless the DIP's barrier is being touched. It will perform as good as a long exposure unless the index rallies over 25% at maturity. **Investors can consider cash extraction and switch to a cushion collar to keep their upside exposure.**

Dec-12 ATM-125% Cushioned Collar (7 June 2012)

Index	DIP Barrier	% to Knock-In	Lehman Crisis Index Low	Downside from 2008-09 Low (%)	6M 80-100% Downside Skew (vol-pt)	Percentile Rank
NKY	86.5	13.5	7,055	(15.3)	9.8	93.5%
TPX	**86.0**	**14.0**	**701**	**0.1**	**9.8**	**93.7%**
HSI	**80.0**	**20.0**	**11,016**	**(39.4)**	**8.7**	**92.3%**
HSCEI	**76.0**	**24.0**	**4,990**	**(46.8)**	**8.3**	**94.1%**

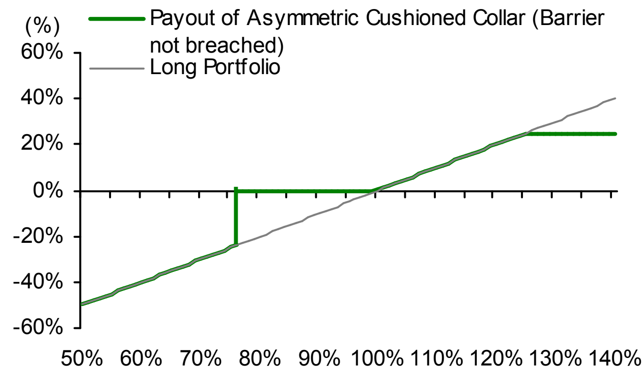
NKY & TPX maturities: 14-Dec-12; HSI & HSCEI maturities: 28-Dec-12; Please refer to table on Page 2 for PE and PB comparisons.
Type: Continuous monitoring; Note: Pricing as of 7 June 2012; Source: BNP Paribas

Dec-12 ATM-125% Cushioned Collar (19 June 2012)

Index	DIP Barrier	% to Knock-In	Lehman Crisis Index Low	Downside from 2008-09 Low (%)	6M 80-100% Downside Skew (vol-pt)	Percentile Rank
NKY	89.5	10.5	7,055	(18.5)	9.0	90.0%
TPX	**88.5**	**11.5**	**701**	**(4.6)**	**9.1**	**90.0%**
HSI	**88.0**	**12.0**	**11,016**	**(50.9)**	**8.1**	**87.0%**
HSCEI	**86.5**	**13.5**	**4,990**	**(43.3)**	**7.9**	**89.6%**

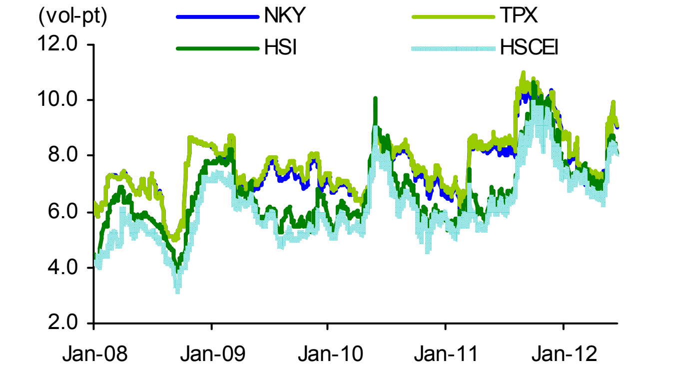
NKY & TPX maturities: 14-Dec-12; HSI & HSCEI maturities: 28-Dec-12; Please refer to table on Page 2 for PE and PB comparisons.
Type: Continuous monitoring; Note: Pricing as of 19 June 2012; Source: BNP Paribas

Cushioned Collar (on HSCEI) vs Long Portfolio



Sources: Bloomberg; BNP Paribas

6M 80-100% Downside Skew



Note: data up to 16 June 2012; Source: BNP Paribas

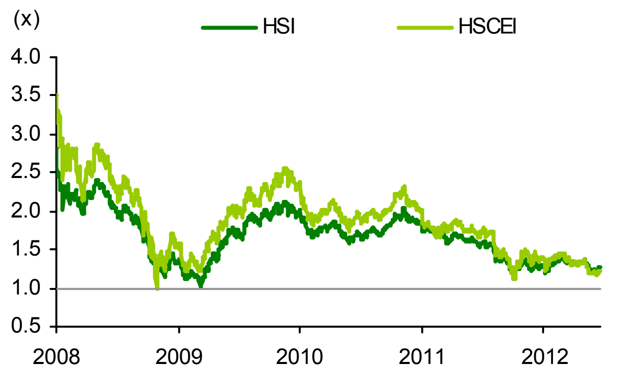
- **The valuation correction in Asian equities is close to last year's trough:** According to our comparisons (based on the lowest P/E and P/BV of last year and the Lehman Crisis troughs), we are at levels that are close to the lows of last year. As such, the correction should have discounted a large portion of negatives and any central bank action or government stimulus could cause a significant rebound triggered by bargain hunting and massive short-covering.
- **Topix seems to be the safest:** The current TPX index and valuation levels are all very close to their corresponding lows during the Lehman Crisis. In terms of P/BV ratio, HSI and HSCEI are still trading at about 20% premium to their troughs of the Lehman Crisis.

Comparison of Lehman Crisis and Last Year's Lows Using 12-month Forward P/E and P/BV

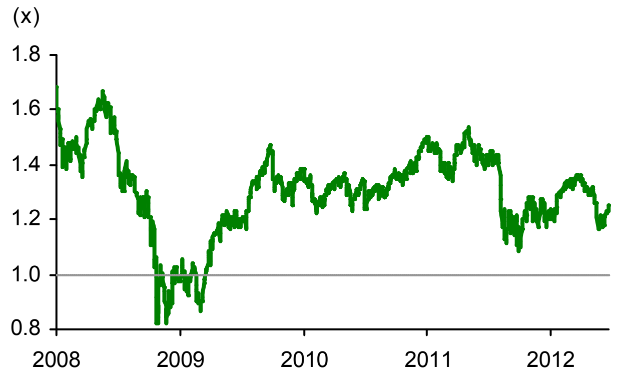
Index	Current P/E (x)	2008 Low P/E (x)	Difference (%)	2011 Low P/E (x)	Difference (%)	Current P/BV (x)	2008 Low P/BV (x)	Difference (%)	2011 Low P/BV (x)	Difference (%)
HSI	10.0	7.6	(24.5)	8.7	(13.1)	1.28	1.01	(20.9)	1.12	(11.9)
HSCEI	7.6	6.1	(20.6)	6.6	(13.1)	1.23	0.99	(19.8)	1.11	(9.3)
KOSPI2	10.1	7.7	(23.4)	8.2	(18.8)	1.26	0.82	(34.4)	1.09	(13.4)
TWSE	14.5	8.7	(40.0)	12.2	(16.0)	1.59	1.01	(36.5)	1.47	(7.8)
STI	13.1	7.8	(40.8)	11.6	(12.1)	1.27	0.93	(27.1)	1.20	(5.3)
NIFTY	12.7	8.3	(34.0)	12.9	2.1	2.09	1.62	(22.9)	2.10	0.2
AS51	12.2	8.0	(34.6)	10.1	(17.3)	1.58	1.25	(21.1)	1.46	(7.3)
NKY	13.0	10.0	(22.7)	13.5	4.2	1.04	0.80	(22.8)	1.02	(2.3)
TPX	12.2	11.4	(6.9)	12.7	3.8	0.85	0.79	(7.7)	0.84	(1.6)

Sources: Bloomberg; BNP Paribas

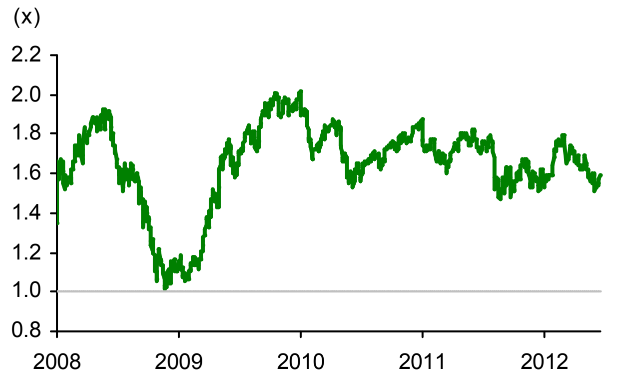
HSI and HSCEI – 12-month Forward P/BV



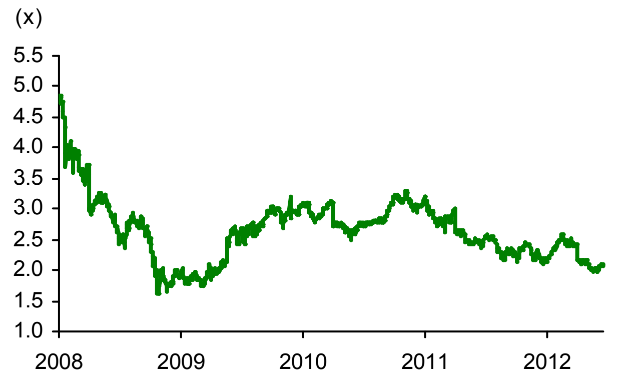
Kospi2 – 12-month Forward P/BV



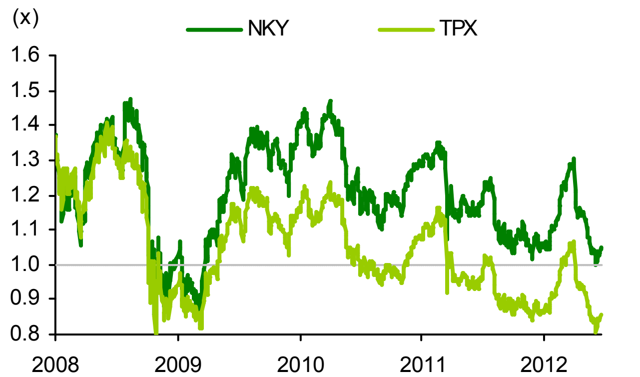
TWSE – 12-month Forward P/BV



Nifty – 12-month Forward P/BV



NKY – 12-month Forward P/BV



AS51 – 12-month Forward P/BV

Note: PB up to the close of 18 June 2012
Source: Bloomberg

Strategy 3: Buy Gold (delta & volatility) in Euro

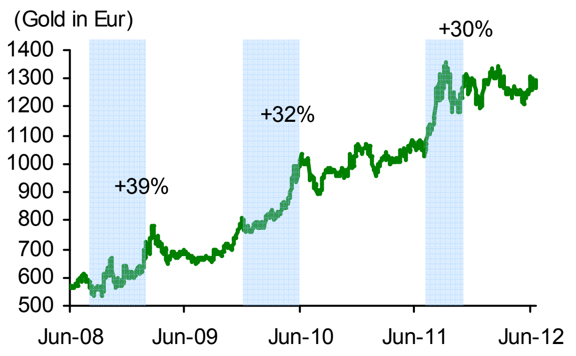
Anthony Wong and Guillaume Derville

- **Buy 3M 105% Call on Gold in EUR (XAUEUR) at 3.61% (indicative)**
- **Buy 3M ATM or 105% Worst-of-Call on [XAU, USD/EUR] at 1.05% or 0.5% respectively (indicative)**
- **Buy 3M ATM or 105% Worst-of-Call on [XAUEUR, USD/EUR] at 2.1% or 1.08% respectively (indicative)**
- **Buy 3M Variance Swap on XAU at 22.75 vol-pts (indicative)**

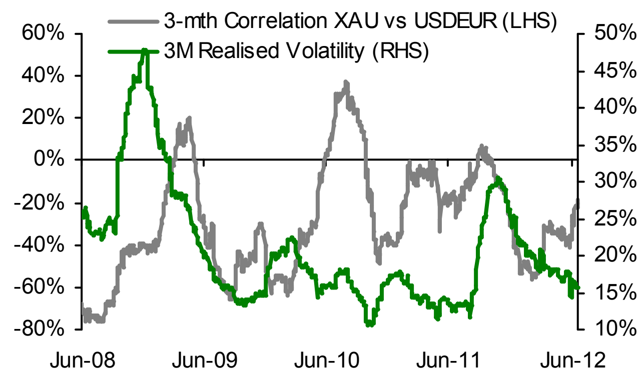
Rationale: Intensification of risk aversion has supported gold in EUR during previous crises

- **Gold in EUR is a safe haven:** Investors have long been debating whether gold is a risk-on or risk-off asset. Persistent negative real interest rates and global currency debasement are drivers that have lead gold to higher prices and have supported a strong bull trend for years. Gold prices have been consolidating since the summer of 2011's sovereign debt risk aversion spike. Nevertheless, history and recent price actions on different asset classes, indicates that an intensification of the sovereign debt crisis might lead to a resumption of the bullish underlying trend. Meanwhile, we suggest investors look at gold in EUR as it was able to deliver positive returns to investors during the previous large-scale market downturn. Going long gold in EUR is effectively buying gold and selling EUR.
- **Contagion in the eurozone:** Spain's debt issues, along with concerns about eurozone financial stability, sent the euro to a two-year low against the USD earlier this month. Spain's 10 year interest rate went above 7% as the Spanish economy appeared to be collapsing and as the country sought a bailout worth EUR100b. The concerns about bank runs in euro nations are intensifying and the contagion effect has spread to Cyprus. Cyprus Popular Bank was told by the European Banking Authority to raise EUR1.8b by end of June. There is speculation that Italy will follow Spain in seeking bailout.
- **Central banks purchases and investment demand will also be key drivers:** According to the World Gold Council, central banks have been a net buyer since 2Q09 when governments launched worldwide stimulus packages. The World Gold Council also said that in 1Q12 investment demand registered yearly growth which was led by solid demand for ETFs and similar products. The comments coincided with our comments earlier on the negative interest rate and global currency debasement or weak EUR – which is one of the reasons we argue gold is in demand.

Gold in EUR is a safe haven



Gold is volatile during market downturn



Source: Bloomberg, BNP Paribas

Asset Returns during Previous Market Downturns

Lehman brother crisis - Autumn 2008	**12-Sep-08**	**06-Mar-09**	**Return (%)**	**Move**
SX5E	3278.0	1817.2	-45	Down
EUR	1.4189	1.2676	-11	Down
GOLD	757.61	939.90	24	Up
XAUEUR	**533.97**	**741.45**	**39%**	**Up**
Greek Debt Crisis - Spring 2010	**15-Jan-10**	**08-Jun-10**	**Return (%)**	**Move**
SX5E	2,940.25	2,510.84	-15	Down
EUR	1.4380	1.1972	-17	Down
GOLD	1,130.05	1,243.93	10	Up
XAUEUR	**785.81**	**1038.92**	**32%**	**Up**
European Sovereign Debt Crisis - Summer 2011	**01-Jul-11**	**12-Sep-11**	**Return (%)**	**Move**
SX5E	2,875.7	1,995.0	-31	Down
EUR	1.4511	1.3607	-6	Down
GOLD	1,485.1	1,812.83	22	Up
XAUEUR	**1,023.5**	**1,332.5**	**30**	**Up**

Sources: Bloomberg; BNP Paribas

Theme 2 – "Chindia Engines are Slowing Down"

Winner Lee

China and India are slowing down, but India's high inflation situation will be a key obstacle to further easing measures.

China's growth slowed further: China's PMI plunged 2.9ppt to 50.4, surprising the market on the downside as consensus was looking for 52. The output index dropped to 52.9 from a strong 57.2 in April, with new orders plunging 4.7ppt to 49.8 while export new orders fell 1.8ppt to 50.4, indicating domestic demand was possibly even weaker than the overseas demand that was hampered by the deteriorating eurozone.

Strength in exports and imports: China's exports growth was 15% y-y in May and imports rose to 12.7%, surprising the market on the upside. However, our China Chief Economist Xingdong Chen, challenges the sustainability of this. Industrial production growth improved marginally to 9.6% y-y from 9.3% y-y and investment growth stabilized at 20.1% y-y with improving funding and launches of new projects. Based on current growth strength, Xingdong expects 2Q is likely to see growth dipping to around 7.5% which is the bottom-line level. He expects growth picking up in 3Q when government policy is gradually transmitted to the real economy.

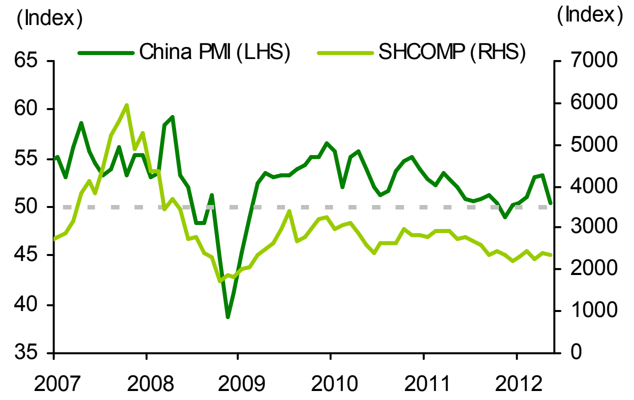
Asian Instant Insight-110612.pdf: http://www.bnppresearch.com?E=caehekbgff

Indian GDP for 4QFY12 was weaker than expected at 5.3%: India said its economy grew at 5.3% in 4QFY12, its slowest pace in nine years and far below consensus' expectation of 6.1% y-y. Richard Iley, BNPP Chief Regional Economist, believes India's growth-inflation trade off continues to deteriorate, and the latest GDP report showed that the economy came close to a hard landing scenario with annualized growth averaging just 4%. India's industrial production was up just 0.1% y-y in April after contracting 3.5% y-y in March due to weaker domestic demand and tumbling exports hurting the economy. Richard believes *"Reform, not stimulus, is required to reboot India's macro-economic performance".*

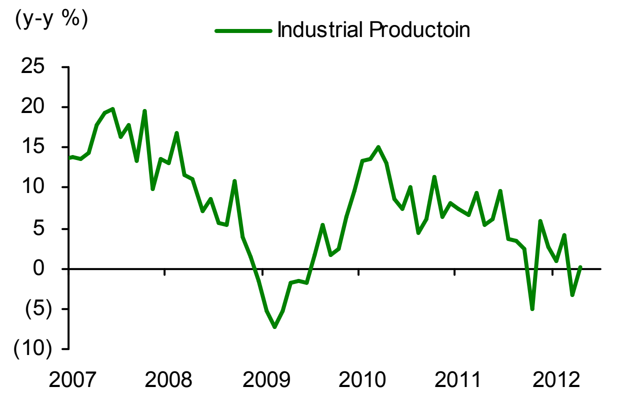
Macro Monday-110612.pdf: http://www.bnppresearch.com?E=caegekbgff

S&P to downgrade India: Standard & Poor's warned India may become the first of the BRIC bloc to lose its investment-grade status if economic reforms aren't implemented soon. S&P revised India's long-term rating from "Stable" to "Negative" on 25 April and its current rating at BBB- is one notch above junk status. India's investment prospects would take a hit if the rating were to be cut to junk, which is possible, resulting in a drop in capital inflows (even outflows) and higher costs for companies in India wanting to raise funds overseas. India's financial situation remains worrying, and with its fiscal deficit at 5.9% of GDP and its current account deficit at 3.3% of GDP, it is hard to reverse the fiscal deterioration in the current gloomy outlook.

China's PMI



India's Industrial Production



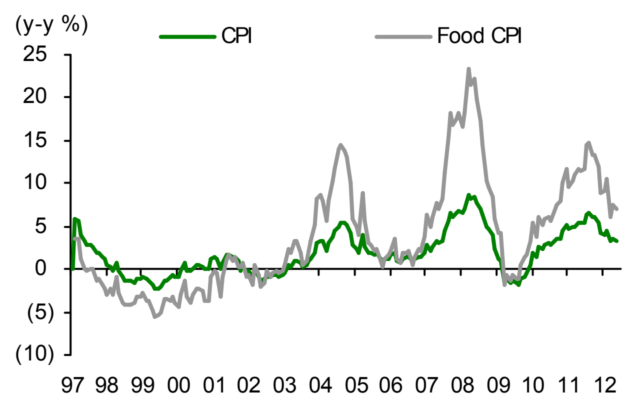
Source: Bloomberg

China's inflation is now under control, monetary easing is becoming more relaxed: With the fall in commodity prices and weakening in the demand side, China's core inflation eased further, to 3% in May, providing more flexibility on RRR and interest rate cuts so as to withstand further external shocks. China can also increase the money supply and stimulate loan growth to help prevent a hard landing scenario. May's new loans climbed to RMB793.2b, up RMB111b from April and 43.8% y-y, which is crucial to support growth. The interest rate cut that was announced by the PBoC on 7 June was really a vaccination to prevent further deterioration of China's economic growth, as well as a signal that China's policymakers are aware that the slowdown has materialized. Xingdong is expecting three more RRR cuts (total 150bp) this year and one more interest rates cut in 3Q (likely in August) unless the deceleration in the economy is worse than expected.

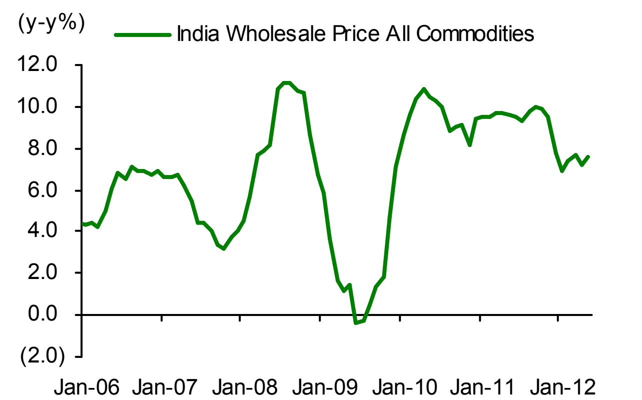
Asian Instant Insight-080612.pdf: http://www.bnppresearch.com?E=caechkbgff

India's inflation remains worrying: India's re-accelerating inflation is frustrating. Its WPI inflation revised up to 7.69% (from 6.89%) in March, and May's figure was worrying at 7.55%. Richard noted that the key source of the high WPI figure came from India's food inflation problem, as a result of the rapid and volatile price increases of fresh fruit and vegetables. The RBI cut the CRR by 75bp on 9 March and then cut the repo rate by 50bp to 8% in April. However, they put interest rate and CRR cuts on hold in their June meeting, which surprised the market on the negative side. Indeed, BNPP's Economics Team only expect 50bp of rate cuts for the rest of 2012 and they have correctly pointed out that high food inflation will give limited room for further monetary easing in India.

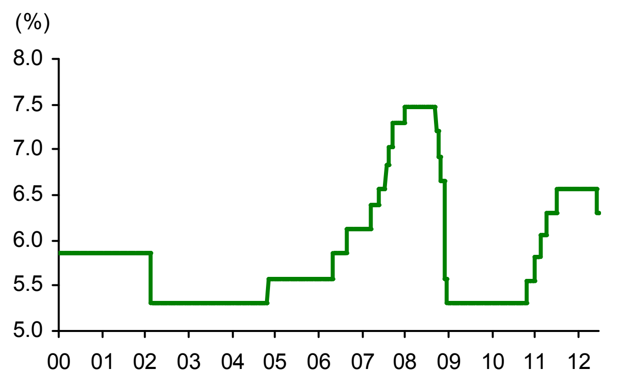
China's Inflation Cools Down to 3%



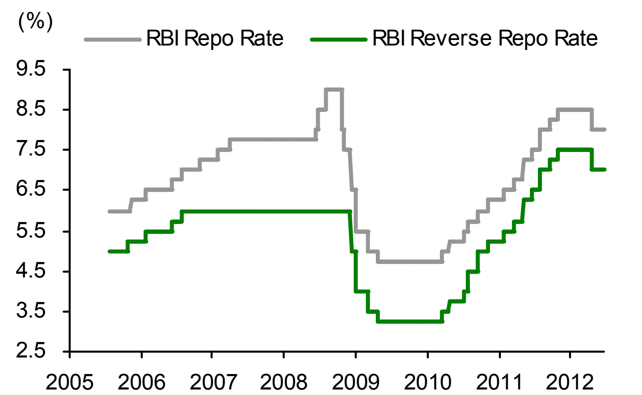
India's WPI



China's 1Y Lending Rate



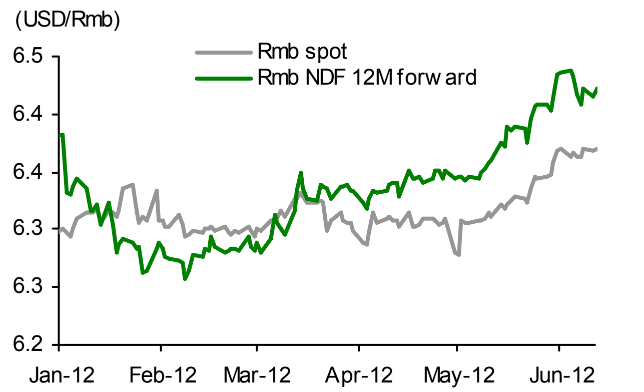
RBI Repo and Reverse Repo Rates



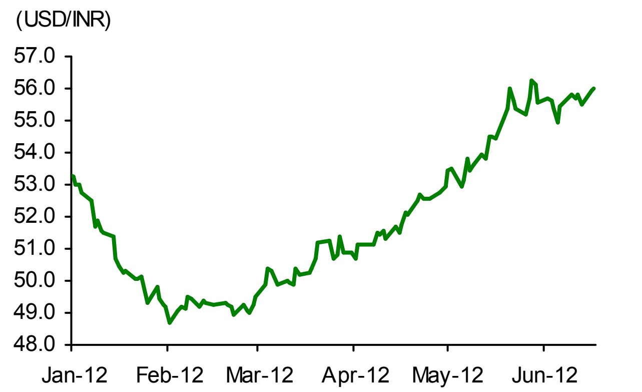
Source: Bloomberg

Weakening of the RMB and INR: RMB spot eased 0.9% YTD and the 12-month NDF forward is trading at 500bp premium to spot. This indicates an expectation of 0.8% depreciation against the USD over the next 12 months. As the trade surplus has eased, the RMB is under less pressure to appreciate. Whereas, the INR is under huge pressure as investors are worried about its elevated inflation and twin deficits. It depreciated 4.8% YTD against the USD and 13% from its YTD peak, implying significant fund outflows from India. However, equity outflow from India was not significant at USD223m between 1 April and 15 June, compared to the huge foreign equity outflow from Taiwan (USD5.5b) and Korea (USD3.26b).

RMB Spot and NDF 12-month Forward



INR Depreciated 4.8% YTD against the USD



Source: Bloomberg

Strategy 4: China Infrastructure Basket

Winner Lee and Samuel Cheng

⇨ **Buy China Infrastructure Basket and Sell HSCEI**

Rationale: Get ready for China to spur growth via fiscal stimulus

China is gradually increasing fiscal spending although the scale should be a lot less than the RMB4t stimulus package of 2008: On top of monetary easing, the market is expecting China to use fiscal policy to stem domestic growth in order to cushion for a soft landing scenario. The fiscal measures may include cutting taxes and speeding up spending on infrastructure projects to ensure growth of more than 8.5% in 2H12. In 2008, the National Development and Reform Commission (NDRC) released an RMB4t economic stimulus package to reignite the economy, and the focus was on transportation infrastructure and power grid construction projects.

It seems the NDRC has kicked started a new wave of fixed asset investment: According to Hexun news, since May the NDRC has started speeding up approvals on various local government infrastructure projects, including steel plants, airports and highways. For example, on 25 May the NDRC approved Zhangjiang's application to develop a huge iron steel production base (the designed annual output is 10m tonnes of steel). The budgeted investment amounts to RMB69.9b. The NDRC approved a further two large iron and steel projects on 25 May, with total budgeted investment exceeding RMB100b.

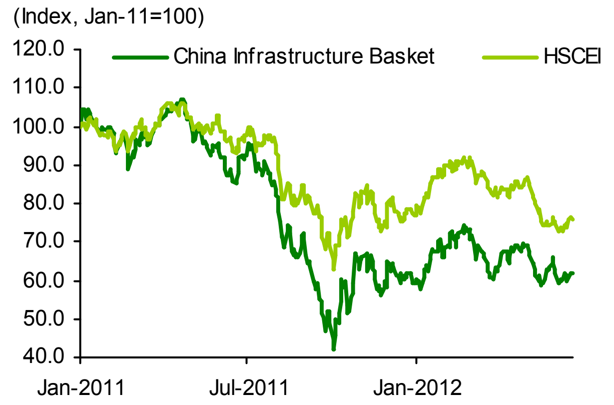
Railways, Infrastructure, Cement and Steel players are the potential beneficiaries: We identify China Communication Construction (1800 HK), China Railway Group (390 HK), China Railway Construction (1186 HK), CSR Corp (1766 HK), Sany Heavy (631 HK), Zoomlion Heavy (1157 HK), Anhui Conch Cement (914 HK), China National Building Material (3323 HK), West China Cement (2233 HK), Angang Steel (347 HK) and Maanshan Iron & Steel (323 HK) in the China Infrastructure Basket. The basket is trading at 1.2x P/BV, 14.1x P/E and 2.2% DY in 2012.

China Infrastructure Basket

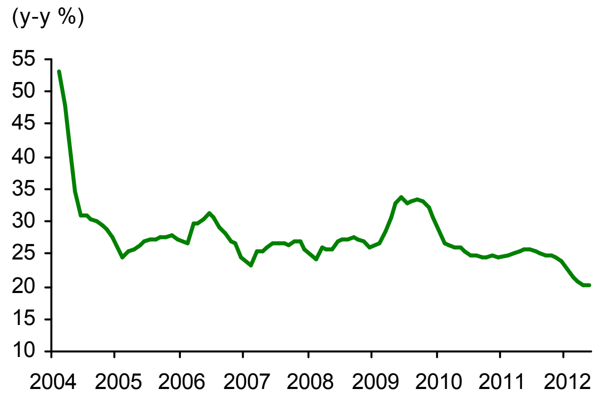
Code	Name	Price (HKD)	Mkt cap (USD m)	Est T/O (USD m)	2012 P/BV (x)	2012 P/E (x)	2012 DY (%)	Weight (%)
1800 HK	China Communications Construction	6.7	13,119	15.4	1.1	6.9	3.5	9.0
390 HK	China Railway Group	3.11	8,785	9.3	0.7	8.3	2.0	9.0
1186 HK	China Railway Construction	6.24	9,031	17.0	0.9	8.6	2.6	9.0
1766 HK	CSR Corp	5.91	10,547	11.0	2.0	14.9	1.8	9.1
631 HK	Sany Heavy Equipment Int'l	4.38	1,757	3.2	1.8	11.4	1.8	9.0
1157 HK	Zoomlion Heavy Industry Science	10.86	12,279	28.6	1.6	7.8	3.0	9.1
914 HK	Anhui Conch Cement	23.05	14,016	44.5	2.0	12.1	1.4	8.9
3323 HK	China National Building Material	9.16	6,374	59.9	1.3	5.9	2.3	9.4
2233 HK	West China Cement	1.68	923	3.7	1.2	6.6	2.5	9.1
347 HK	Angang Steel	4.54	4,553	5.2	0.5	na	1.8	9.3
323 HK	Maanshan Iron & Steel	1.85	2,572	3.9	0.4	58.3	1.6	9.0
Average					**1.2**	**14.1**	**2.2**	**100.0**

Sources: Bloomberg; BNP Paribas

China Infrastructure Basket



China FAI – New Construction Cumulative Y-Y



Source: Bloomberg

Investment shows early evidence of policy effect: BNPP's China economist, Ken Peng, sees that the headline FAI growth continues to trend downward, edging down from 20.2% to 20.1% y-y YTD. Funding conditions seem to have improved from the first four months. Overall FAI funding picked up slightly from 16.5% in the first four months to 16.8% in Jan-May. The budget for existing projects also lifted from 14.5% to 16%. New project funding rose from 21.6% to 22%. Ken also pointed out a bigger m-m improvement on railway investment growth (from -43.6% y-y in the first four months to -41.6% y-y in January-May).

Asian Instant Insight-110612.pdf: http://www.bnppresearch.com?E=caehekhgab

Green shoots are also found in the construction machinery and railway sectors: BNPP's Head of Regional Industrials, Tina Li, said that the May excavator y-y sales decline is narrowing and utilization hours have been improving, which hints at signs of a construction demand recovery. She also said that new locomotive orders tendered by CRIC and locomotive batch production resumed after an 11-month suspension, which shows a positive development in the railway industry. For construction machinery, Zoomlion Heavy Industry (1157 HK) is Tina's top BUY in the sector, which is trading at 7.3x 2012 P/E. She also has a BUY rating on Sany Heavy Equipment International (631 HK). For railway, she recommends both CSR (1766 HK) and Zhuzhou CSR (3898 HK).

China Construction Mach-120612.pdf: http://www.bnppresearch.com?E=caeghkbgff

CSR-130612.pdf: http://www.bnppresearch.com?E=caeiikhgab

China Infrastructure Basket is relatively defensive: The basket gained 3.8% YTD and outperformed the HSCEI by 5.5%. The China Infrastructure Basket can trade up to USD10m per day with the consideration of board lot (USD200k per unit). We are flexible in constituents and weightings.

Strategy 5: Risk-adjusted Upside Exposure on China Banks

Winner Lee and Samuel Cheng

- **Buy Sep-12 ATM or 105% Worst-of Call on China Banks [CCB, ICBC, BOC and CM Bank] at 3.85% and 2.2% (Implied correlation at 90 vol-pt; indicative)**

BNPP's Head of China Research, Dorris Chen, published her latest report on China Banks expressing her bullish views on China's banking sector since the rate liberalization has been in operation.

China Banks on 11 June 2012: http://www.bnppresearch.com?E=caefhkbgff

China Banks on 20 June 2012: http://www.bnppresearch.com?E=cagabkbgff

Interest rates liberalization in operation: Dorris sees the positive side in the PBoC's initial attempt to liberalize interest rates. The marginal funding cost for banks is set by wealth management products (WMP), whose rate is higher than deposit rates. By lifting deposit rates and lowering WMP rates, banks increase the attractiveness of deposits, lower incremental funding costs and stabilize sources of funding.

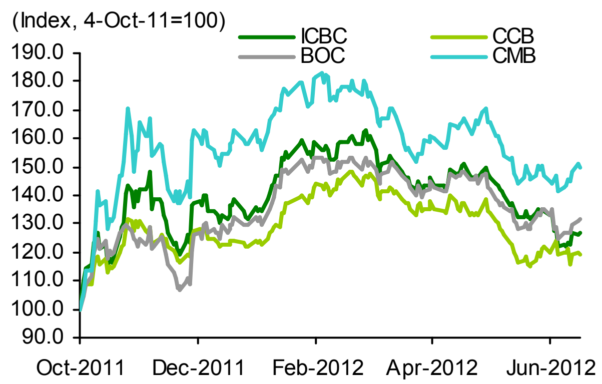
Lending activities to recover soon: Stabilized funding enables banks to lend to more FAI projects. She reiterates that her estimated RMB3.75t of retired loans in 2012 allows banks to lend more to FAI projects than new credit data suggests. The gap between new FAI loans and new corporate mid-to-long term loans stands at a high RMB1.3t at end 4M12, supporting her argument.

Further easing moves and strong new loan growth are the key catalysts: Dorris believes the concerns over NIM downside will urge banks to intensify their lending to SMEs, which would offset the negative impact. More importantly, potential funding source stabilization will allow banks to increase daily average interest bearing assets and move their credit assets from short-term bill financing to longer-term FAI projects, which not only provides upside potential for banks' NIM but is also important to the overall sentiment around the China stock market. Moreover, May new loans in China surged to RMB793.2b, increasing RMB111b from April (up 43.8% y-y) and beating market estimates of RMB700b. The strong loan growth momentum, together with potential easing moves, would be the catalysts for buoying the sector.

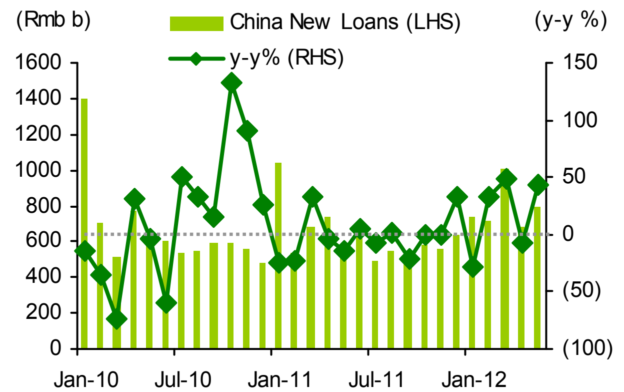
Very tempting valuations: Dorris believes the sentiment on China banks is unlikely to revert soon, but the valuations are getting attractive at 5-7x P/E in 2012, delivering over 3.5-6.5% DY. She thinks the average 1.0x P/BV in 2012E provides valuation support.

Low cost upside exposure on China Banks: We suggest using Worst-of-Call to get upside exposure on China Banks to limit the downside risk at the premium. Although the implied correlation is expensive at 90%, we believe their rebounds would be in tandem. The payoff is the same as a plain-vanilla call but only on the worst performer, breakeven requires the worst performer to gain 3.85% for ATM strike and 7.2% for 105% strike.

China Banks Performance



China New Loans at RMB793.2b in May



Source: Bloomberg

Strategy 6: China to Outperform India

Winner Lee

- **Buy Dec-12 105/120% Outperformance Call Spread on HSCEI over Nifty [conditional HSCEI > ATM at maturity] at 2.35% (indicative)**
- **Buy Dec-12 105% Call on HSCEI and Sell Dec-12 105% Call on Nifty at 82bps (indicative)**
- **Buy Dec-12 95/80% Put on Nifty at 2.5% (indicative)**

Rationale: Positioning HSCEI to outperform Nifty

HSCEI has underperformed: HSCEI lost 4.1% YTD and underperformed Nifty by 13.3% as the market was positive on Indian equities after the RBI became more proactive in cutting the CRR and interest rates. India's re-accelerating inflation has put pressure on the RBI to implement further monetary easing. We are expecting HSCEI to outperform Nifty given China's core inflation fell back to 3% in May, and it can be flexible in easing any further external shock.

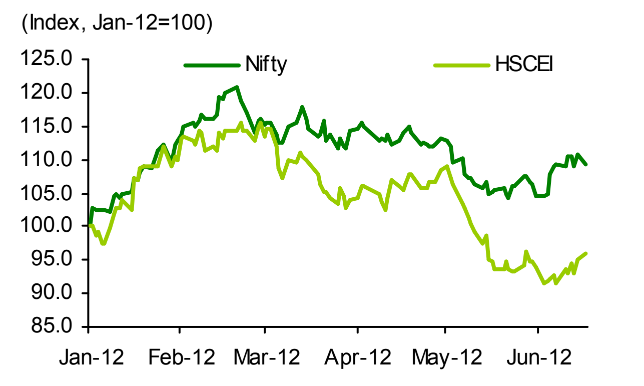
S&P to downgrade India: As discussed in the theme section, Standard & Poor's warned India that it may revise down its current credit rating of BBB- to junk status. India's investment prospects would take a hit if the rating were to be cut to junk, which is possible, resulting in capital outflows and higher costs for Indian companies.

INR to stay weak: The INR depreciated significantly by 13% from its YTD peak of USDINR48.695 in February. BNPP's Regional FX Team is expecting India to hover between the current level and around USDINR54 by year-end. If the S&P downgrade happens, the capital outflow could cause further weakening of the INR, and therefore equity investors would incur losses from both equity and currency. As such, going long India equities is becoming less favourable.

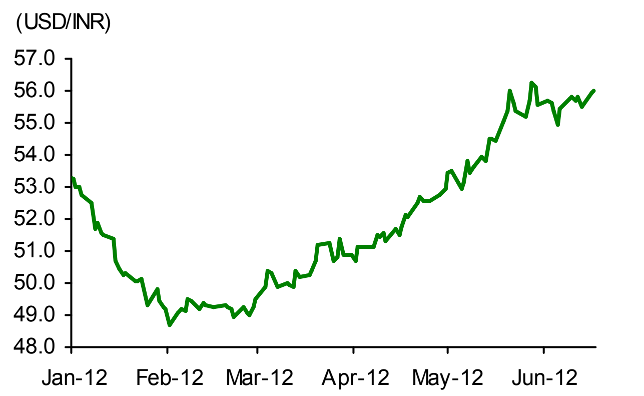
Outperformance Call Spread: We advise investors to consider an Outperformance Call Spread conditional on HSCEI to generate positive return at maturity, which helps cheapen the premium slightly.

Directional exposure via plain-vanilla options: Call vs Call is a cheaper way to get relative exposure by selling Call on Nifty to finance upside Call on HSCEI. Investors will have a positive return when the 105% Call on HSCEI becomes in-the-money and outperforms Nifty. It will generate losses when Nifty gains more than 5% and outperforms HSCEI. Bearish investors who want to hedge against the possible downgrade in India can consider taking advantage of the steep skew to buy Put Spread.

HSCEI vs Nifty



INR Depreciated 4.8% YTD Against the USD



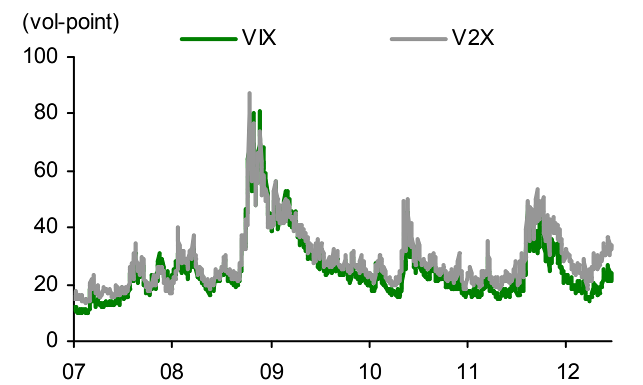
Source: Bloomberg

Theme 3 – "Reality Check on Global Risk Parameters"

Winner Lee

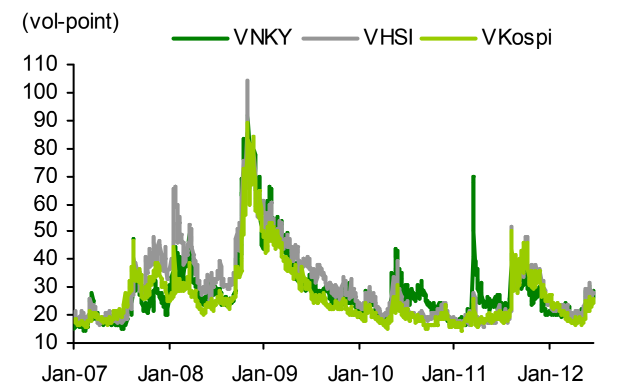
Global and Asian Risk Gauges eased: Global risk gauges eased after Spain received a EUR100b bailout and Grexit concerns eased as the political parties that support Greece's bailout won enough seats to form a coalition government. The euro saw short-term relief and stabilized at around the 1.26-level. However, the sovereign debt issue in Europe is not something that can be solved within a short period of time and the problem is being continuously postponed. We believe the eurozone turmoil remains a hidden bomb in the financial markets.

Global Risk Gauge – VIX and V2X



Note: data up to 15 June 2012
Source: Bloomberg

Asian Risk Gauge – VNKY, VHSI and VKospi

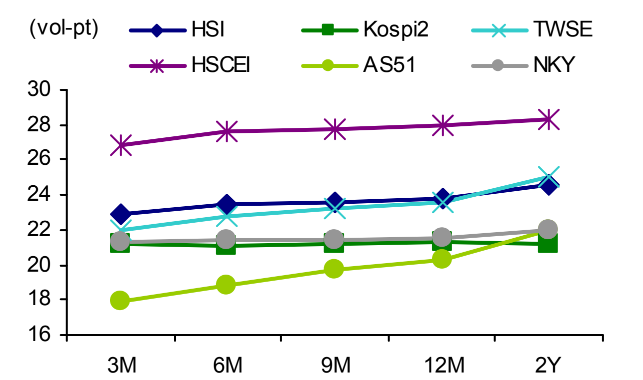


Note: data up to 18 June 2012
Source: Bloomberg

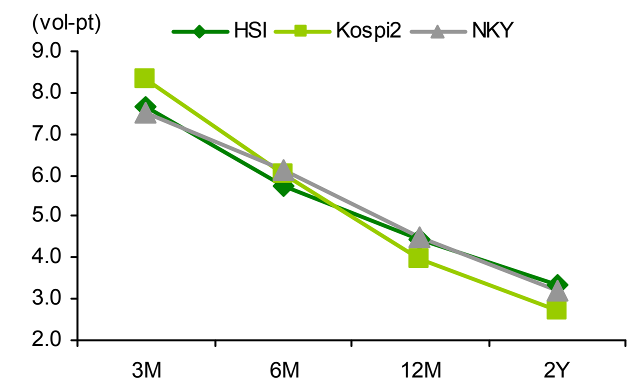
Flattening term structures: The implied volatility term structures of the regional indices climbed up since the global de-risking over the past two months but eased a bit over the past few days. The term structures have shifted from upward sloping to flattening as the short-dated volatilities spiked more dramatically. HSCEI is trading with the highest volatility term structure.

Steep skew term structures: The short-dated skews of the Asian indices spiked up significantly over the past two months. Kospi2 now has the steepest skew term structure.

Implied Volatility Term Structures



90-110% Skew Term Structures

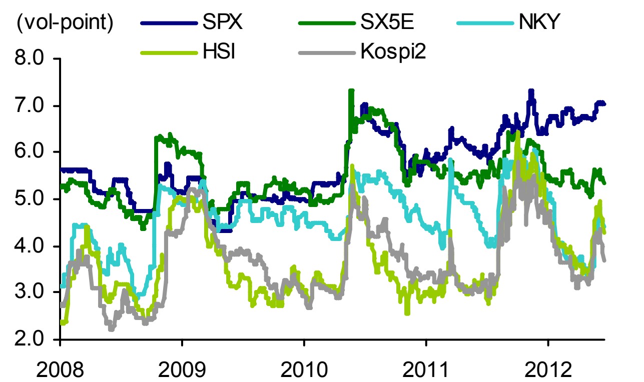


Note: data up to 18 June 2012
Source: BNP Paribas

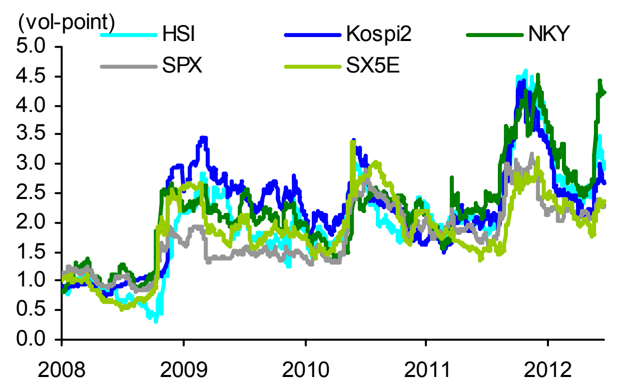
Asian skews have retreated from their recent peaks: During the global risk-off from April to May, Asian skews spiked up more significantly than the US and Europe due to more demand on protection. With the Grexit concerns over, the 1Y 90-110% skew of HSI, Kospi2 and NKY eased and they were trading at 79th, 69th and 44th percentile respectively since 2008.

Investors were actively selling the historical high convexity on NKY: Asian convexities are rebounding as well, due to more demand for Var Swap to hedge against the tail risk. The 1Y Convexity (Var Swap – Vol Swap) of NKY, HSCEI and Kospi2 have gained 161bp, 64bp and 47bp since the beginning of May. The convexity of NKY has spiked to comparable levels to last year, trading at 99th percentile (2008-current). Investors were actively selling the convexity on NKY at reasonably high levels and we believe the BoJ's purchase of ETFs provides a crucial support in any down turn.

1Y 90%-110% Skew



1Y Convexity (Var Swap – Vol Swap)



Note: data up to 15 June 2012; Source: BNP Paribas

Spain is in the eye of the storm: Moody's downgraded Spain's government bond rating from A3 to Baa3 (3 notches down, to the lowest investment grade) on 13 June. The key reason for this dramatic downgrade was the government's decision to seek up to EUR100b of external funding from the EFSF or ESM, which was twice the size of Moody's previous base case estimate. **Moody's put Spain on a review for a possible further downgrade, with the results of the review released within three months. Under this scenario, a big sell off on Spanish bonds would happen.** On 30 April, S&P cut its credit ratings for 11 Spanish banks, including the two largest Spanish banks – Banco Santander and Banco Bilbao, citing "potentially negative implications" after the country was downgraded two notches to BBB+ from A on 26 April. On 17 May, Moody's also downgraded 16 Spanish banks including Santander. The Spanish economy is running twin deficits, with a current account deficit at 3.9% of GDP and a fiscal deficit of 8.9% of GDP during 2011. The country's economic condition continues to deteriorate as domestic consumption contributes more than 50% of the GDP and unemployment is astonishing at 24.7%.

Foreign Currency LT Debt Credit Rating

Country	S&P	Moody's	Fitch
Germany	AAAu	Aaa	AAA
France	AA+u	Aaa	AAA
Spain	BBB+	Baa3	BBB
Portugal	BB	Ba3	WD
Ireland	BBB+	Ba1	BBB+
Italy	BBB+u	A3	A-
Greece	CCC	C	CCC

Source: Bloomberg – WCDM

Spanish Banks' EUR100b bailout: According to the *Hong Kong Financials* report by our analyst Dominic Chan on 14 June 2012, *"Spanish Banks' excessive exposure to the real estate sector, particularly property developers during the property boom in the last decade, was the main culprit responsible for their weakened balance sheet. House prices have fallen by 21% from their peak in March 2008, while the unemployment rate in Spain has risen to 24.3% in April 2012. Spanish banks have also been relying on wholesale funding to fund their increasing property exposure, taking advantage of the global liquidity and low interest environment."*

Major Spanish Banks Comparison

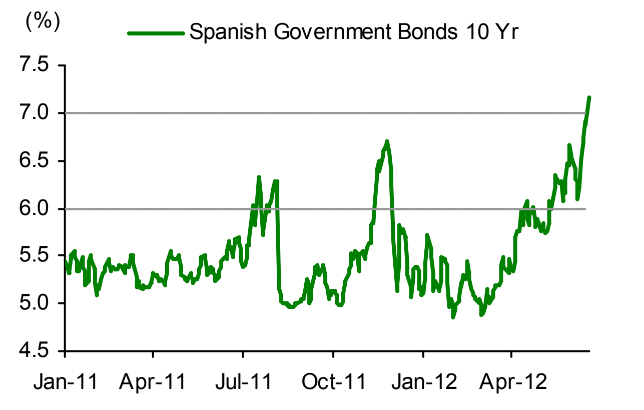
Name	Market Cap (USD m)	Total loans (USD m)	Total assets (USD m)	Core Tier 1 ratio	NPL (%)	LLR/NPL (%)	Net profit 1Q12 (y-y%)	Net profit FY11 (y-y%)	Share price Perf (YTD%)
Banco Santander	45,083	972,775	1,621,978	10.0	3.9	61.8	(24)	(35)	(17.1)
BBVA	26,588	466,372	774,604	10.7	4.0	60.0	(13)	(35)	(22.9)
Caixabank	9,206	243,101	350,470	10.4	5.3	61.0	(84)	(13)	(39.1)
Banco Sabadell	3,243	95,431	130,167	9.0	6.0	49.4	(5)	(39)	(46.0)
Banco Popular	2,960	133,285	169,680	9.8	8.1	49.5	(46)	(19)	(52.8)
Bankia SA	2,050	249,490	392,489	8.1	7.1	61.6	n/a	(934)	(72.4)
Banesto SA	1,794	92,306	141,067	9.0	4.9	56.4	(88)	(73)	(29.9)
Bankinter	1,278	56,243	77,101	8.6	4.4	42.9	2	20	(48.4)
Average				**9.7**	**5.5**	**55.3**	**(37)**	**(141)**	**(41.1)**

Extraction from Hong Kong Financials report by Dominic Chan on 14 June 2012;
Note: CaixaBank's Core T1 ratio would come off by 167bps to 10.7% upon integrating Banca Civica; Sources: Company reports; BNP Paribas

Spanish 10Y bond yield is at an alarming level: The 10Y Spanish bond yield exceeded 7% on 18 June. The high bond yield level implies an expensive borrow cost for the country's new debts, indicating a heavy burden for the Spanish government.

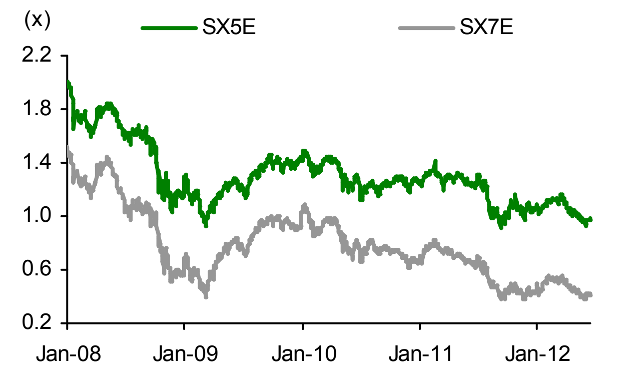
Deteriorating book value of European banks: The P/BV of the EuroStoxx Banks slumped to its YTD low of 0.3813x (2.6% above last year's trough of 0.3713x), and rebounded 10.5% to 0.4213x recently. A large portion of the negatives should have been discounted, but the deterioration in book values seems never-ending.

Spanish 10 Year Bond Yield is Worrying



Note: data up to 15 June 2012
Source: Bloomberg

EuroStoxx Banks' P/BV close to last year's low



Note: The top five largest banks of SX7E are Banco Santander (contributes 20.5%), followed by Deutsche Bank (13.4%), BNP Paribas (13.1%), Banco Bilbao (11.9%) and Intesa Sanpaolo (7.1%).

Strategy 7 – Hedging for Further Shocks in Europe

Winner Lee and Anthony Wong

- ⇨ **Buy Sep-12 95/85% Put Spread**
- ⇨ **Buy Sep-12 Put Condor [Buy 90%, Sell 80%, Sell 70% and Buy 60%]**

Rationale: Monetizing the steep downside skew to cheapen the cost of protection

Put Spread / Put Condor on Asia ex Japan Equities

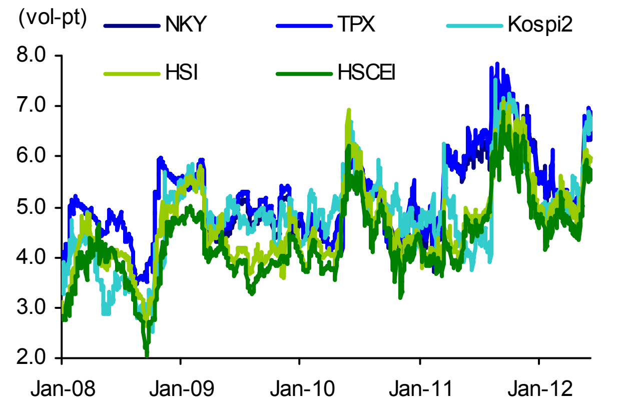
Index	Offer Sep-12 95/85% Put Spread	Offer Sep-12 90%/80%/70%/60% Put Condor
NKY	1.67	0.83
HSI	2.06	1.08
HSCEI	2.33	1.27
Kospi2	1.50	0.74
TWSE	2.55	1.34
MSCI Singapore	1.74	0.85
Nifty	1.49	0.75
AS51	1.59	0.78

Note: Option pricing as of 20 June 2012
Source: BNP Paribas

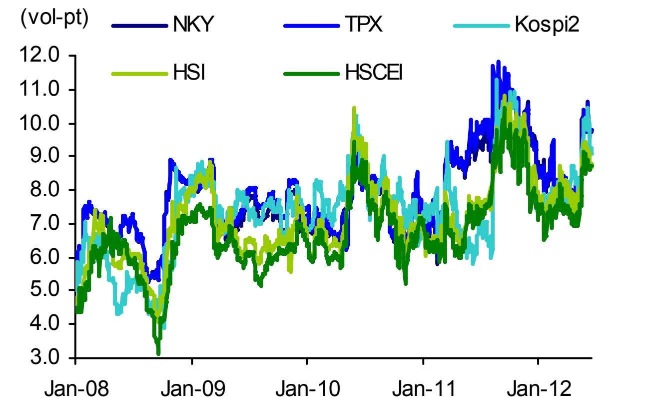
Equity bottom may be further down the road. Risk parameters, implied volatilities, skews and convexities have eased from recent peaks. The recent spike in volatilities and skews has yet to reach the levels seen during the Lehman Crisis or during the sovereign debt crisis last year. This is one of the key reasons, we believe, that the bottom may be further down the road.

Downside skew is steep: The 3M 85-95% and 80-95% downside skews of the regional indices remain elevated (although they have eased a bit from their recent peaks), trading at around 90th percentile since the beginning of 2008. Investors can take advantage of the rich downside skew to sell OTM (Out-of-The-Money) Put to cheapen the premium. As such, we are suggesting the Put Spread or Put Condor.

3M 85-95% Downside Skew



3M 80-95% Downside Skew



Source: BNP Paribas

Strategy 8: Sell Convexity to Finance Buying Put Spread

Winner Lee and Anthony Wong

Rationale: Global central banks would increase combined efforts to prevent another Lehman-type Crisis, but further de-risking seems unavoidable

⇨ **Sell Dec-12 Convexity and Buy Dec-12 95/80% Put Spread on NKY**

Convexity and Put Spread

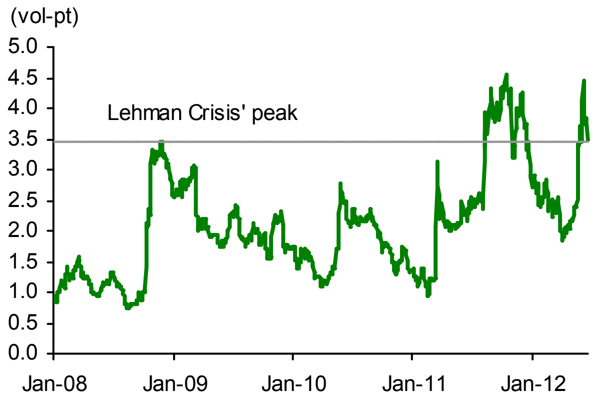
Indices	Bid Dec-12 Convexity (Var-Vol) vol-point	Offer Dec-12 95/80% Put Spread (%/vol-point)
NKY	3.40	2.95% (28.35/22.4)
Kospi2	3.40	2.41% (28.2/22.3)
HSI	3.60	3.34% (29.75/24.5)
HSCEI	3.85	3.7% (34.2/29)

Option pricing as of 20 June 2012
Source: BNP Paribas

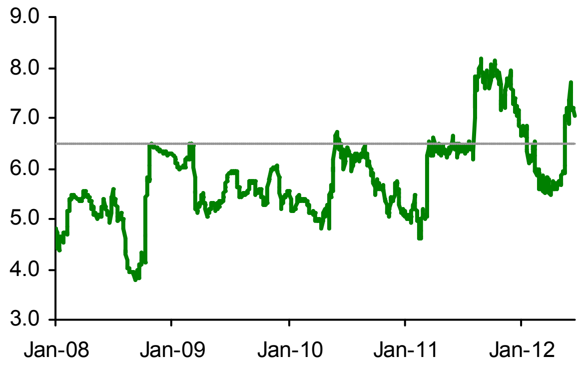
Sell the rich convexity: The 6M Asian convexities spiked dramatically over the past two months and exceeded their Lehman Crisis peaks. Investors were rushing to buy variance to hedge themselves against a tail risk event of Grexit contagion (collapse in the euro as well as spike in the CDS of PIIGS countries) which could lead to a Lehman-type crisis. The convexities have eased quickly over the past few days after Grexit concerns abated. The 6M convexity on NKY is remaining high at 3.4 vol-point, trading at 92%-tile since 2008. Investors are more willing to sell convexity on NKY, because central banks globally have increased efforts to prevent a disastrous scenario and the BoJ's purchases of NKY and TPX ETFs should provide a good cushion for any dramatic correction.

Take advantage of the steep downside skew to buy Put Spread: Although the downside skews have eased a bit from their recent peaks, they remain steep compared to their historical levels. Investors can take advantage of the steep downside skew to cheapen the protection premium. Some investors may still want to protect against a further USD de-risking scenario (weakening in the euro), before any QE3 is implemented.

6M Convexity (Var-Vol) on NKY

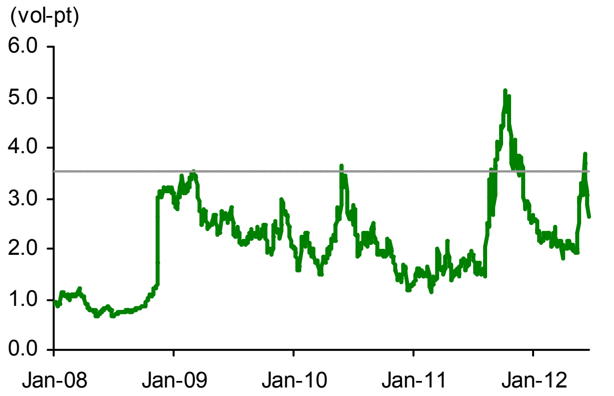


6M 95/80% Downside Skew on NKY

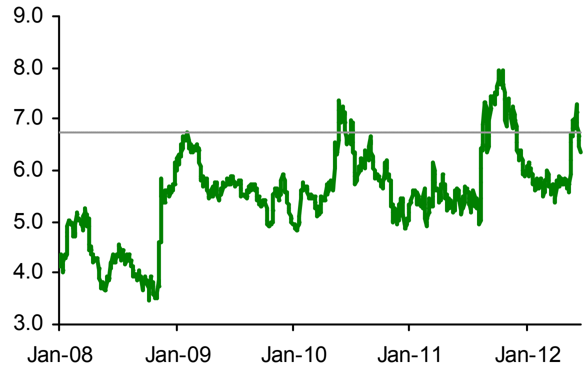


Note: Data up to 18 June 2012
Source: BNP Paribas

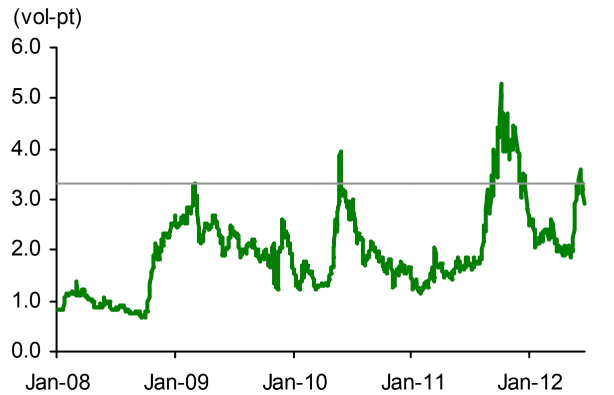
6M Convexity (Var-Vol) on Kospi2



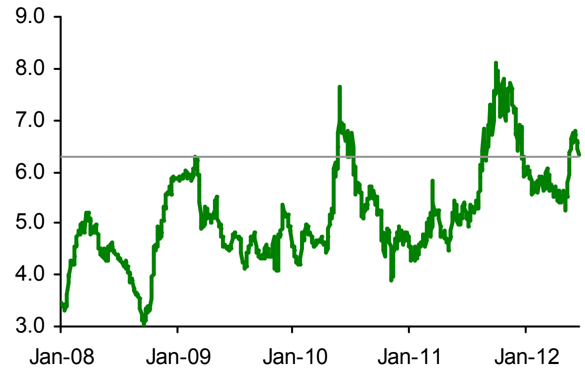
6M 95/80% Downside Skew on Kospi2



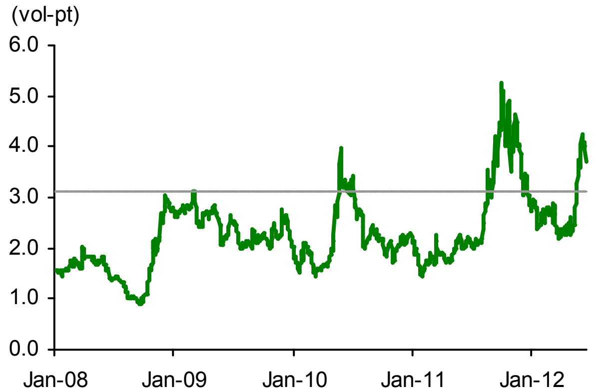
6M Convexity (Var-Vol) on HSI



6M 95/80% Downside Skew on HSI



6M Convexity (Var-Vol) on HSCEI



6M 95/80% Downside Skew on HSCEI

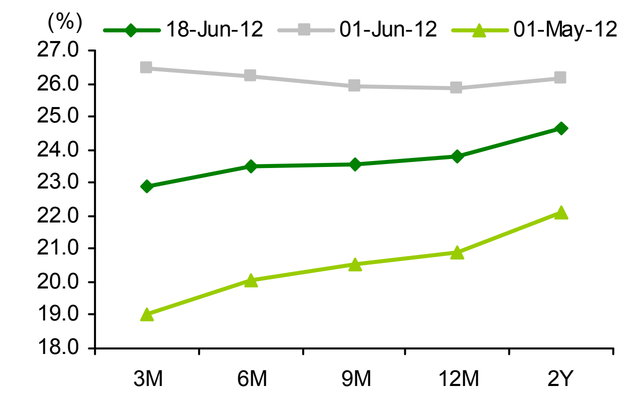
Note: Data up to 18 June 2012
Source: BNP Paribas

III. Hidden Assets

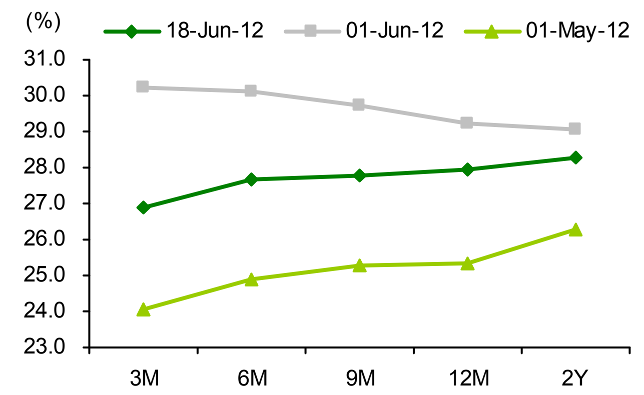
Volatility outlook

Asian implied volatility term structures shifted down and turned slightly upward sloping: The volatility market has seen less stress over the past few days and the term structures shifted down by few vol-points, especially for the short-dated volatilities. The term structure of Kospi2 is the only one that remains flattened. The term structures have a chance of returning to upward sloping over the short-run but the markets remain fragile towards any shock in Europe.

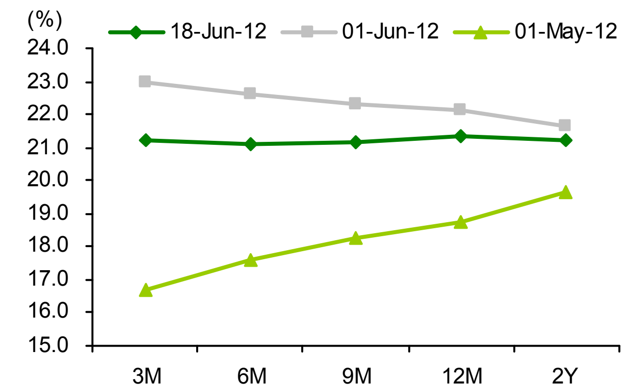
Implied Volatility Term Structure – HSI



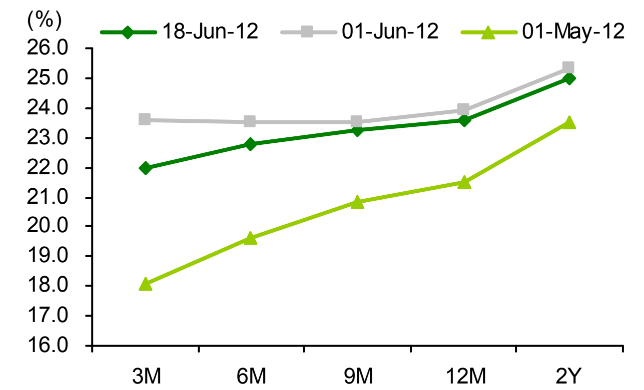
Implied Volatility Term Structure – HSCEI



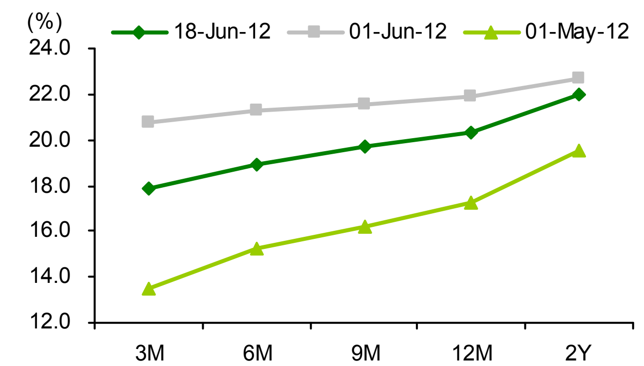
Implied Volatility Term Structure – KOSPI 200



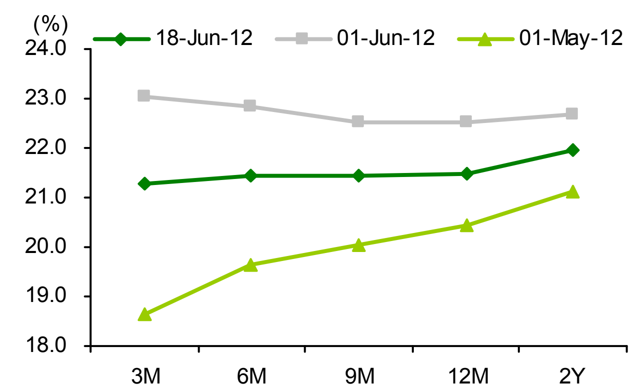
Implied Volatility Term Structure – TWSE



Implied Volatility Term Structure – AS51



Implied Volatility Term Structure – NKY

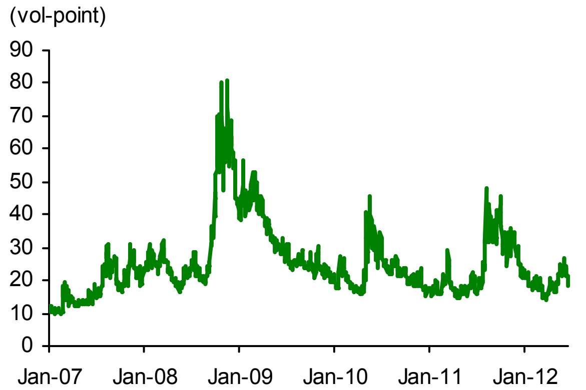


Note: Data as of 18 June 2012
Source: BNP Paribas

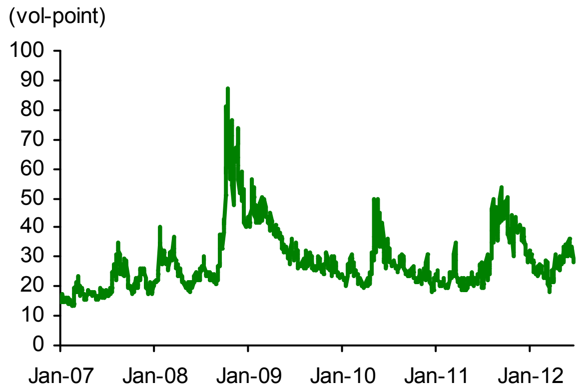
Risk Barometer – Fear Index

The Asian fear indices are seeing less stress: The Asian fear indices all eased from their recent peaks. However, their recent highs have not yet touched the peaks seen during the European sovereign debt crisis in 2010 and 2011.

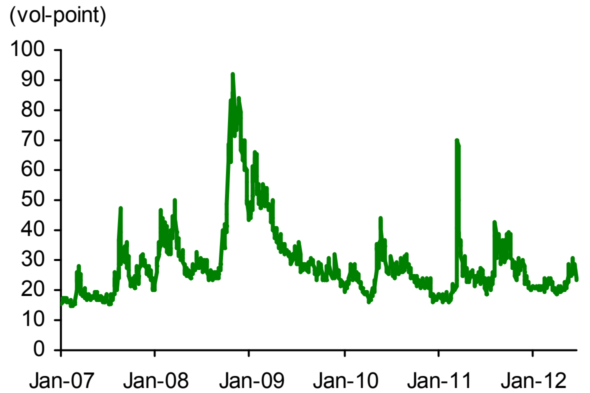
VIX (S&P 500 Volatility Index)



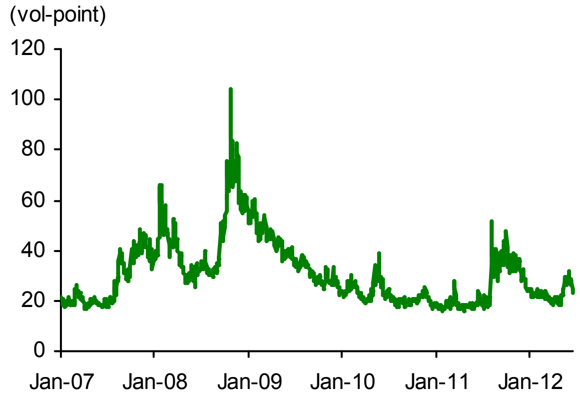
V2X (EuroStoxx Volatility Index)



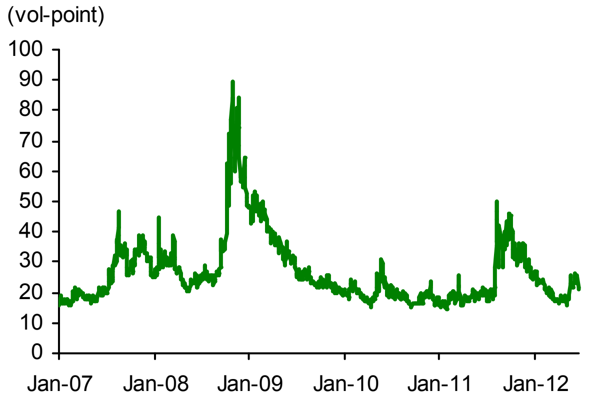
VNKY (Nikkei 225 Volatility Index)



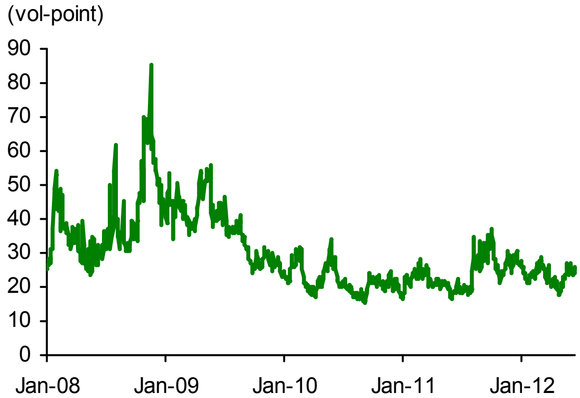
VHSI (HSI Volatility Index)



VKOSPI (Kospi2 Volatility Index)



INVIXN (India NSE Volatility Index)

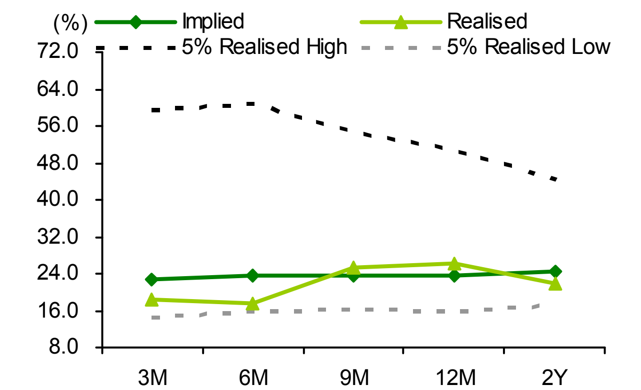


Note: Data as of 18 June 2012
Source: Bloomberg

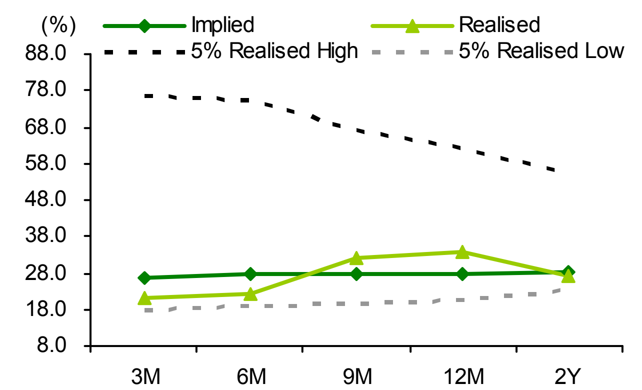
Volatility Cone

The implied volatility term structures have all moved up since the risk-off situation started, but the term structures of HSI, HSCEI, Kospi2 and NKY are trading at the lower end over the historical top 5th and bottom 5th percentile over the past five years.

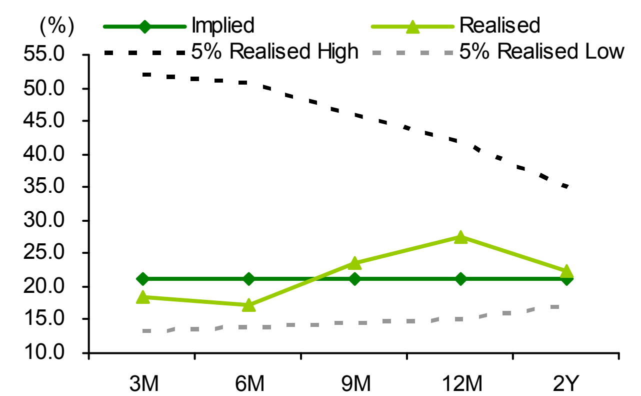
Volatility Cone – HSI



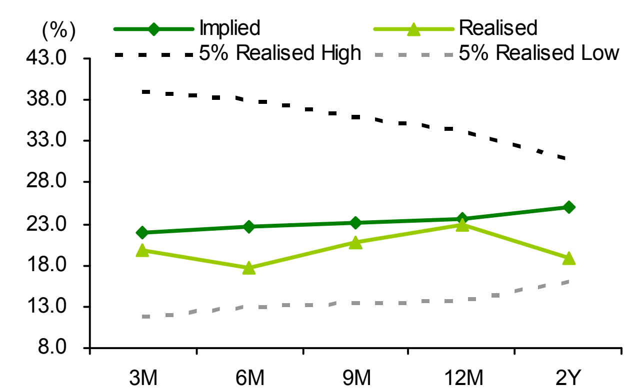
Volatility Cone – HSCEI



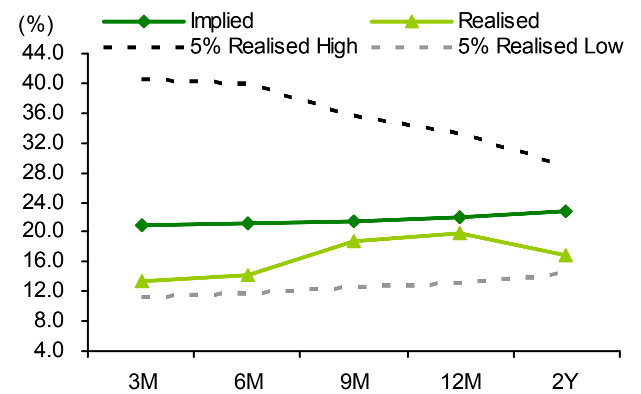
Volatility Cone – Kospi 200



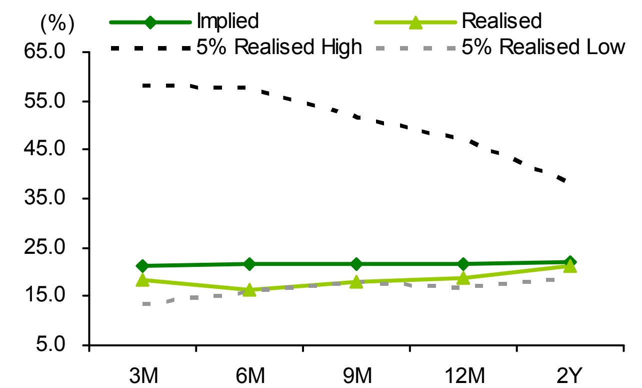
Volatility Cone – TWSE



Volatility Cone – AS51



Volatility Cone – NKY

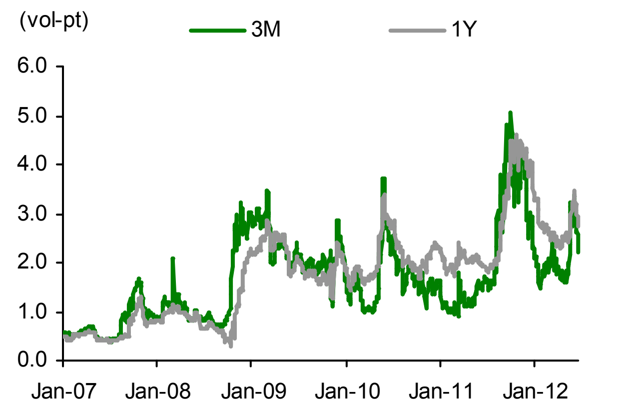


Note: dotted lines are the top- 5 percentile and bottom-5 percentile over the past five years.
Note: Data as of 18 June 2012
Source: BNP Paribas

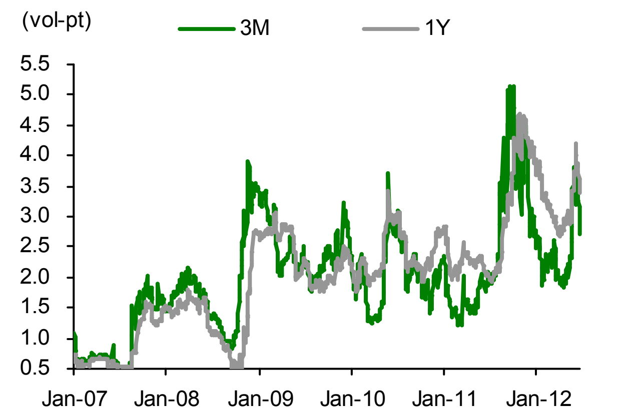
Convexity (Variance minus Volatility Spread)

Convexity is cooling off: Convexity of the regional indices is cooling off quickly, especially for the short-term maturity. The recent spikes were getting close to their Lehman Crisis peaks. The exceptional cases were in NKY and TPX, as their convexities spiked significantly to the levels very close to their peaks of last year. As such, selling convexity on NKY was active as an excellent volatility arbitrage opportunity.

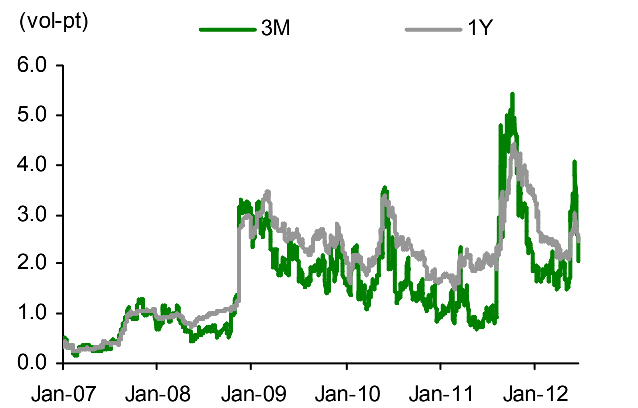
Convexity (Var-Vol) 3M and 1Y – HSI



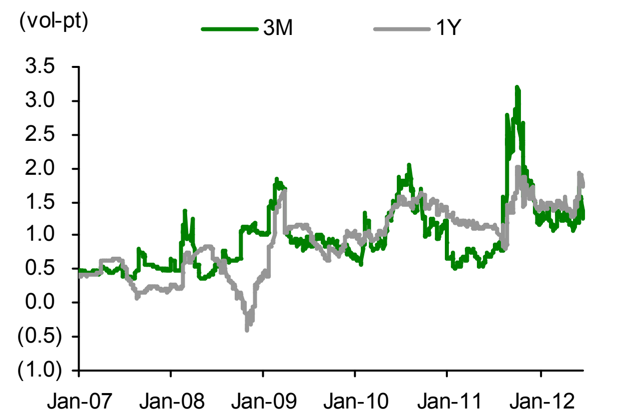
Convexity (Var-Vol) 3M and 1Y – HSCEI



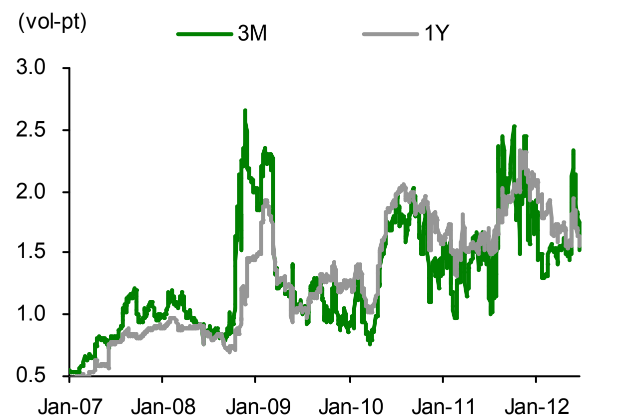
Convexity (Var-Vol) 3M and 1Y – Kospi 200



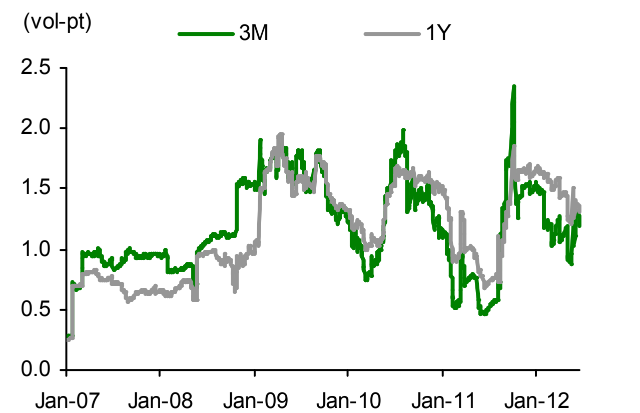
Convexity (Var-Vol) 3M and 1Y – TWSE



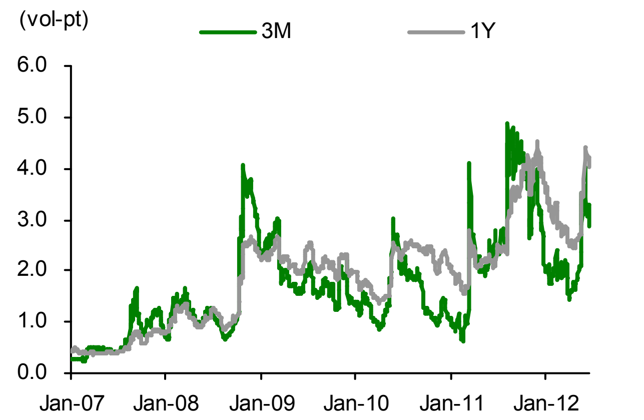
Convexity (Var-Vol) 3M and 1Y – AS51



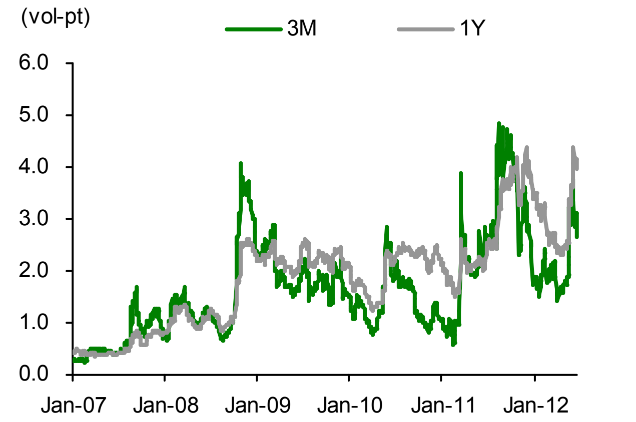
Convexity (Var-Vol) 3M and 1Y – MSCI Singapore



Convexity (Var-Vol) 3M and 1Y – NKY



Convexity (Var-Vol) 3M and 1Y – Topix



Note: Convexity (Variance Swap minus Volatility Swap Spread) is estimated by (Implied Variance Swap minus Implied Volatility of ATM Straddles) / 2; data up to 18 June 2012
Source: BNP Paribas

Correlation Outlook

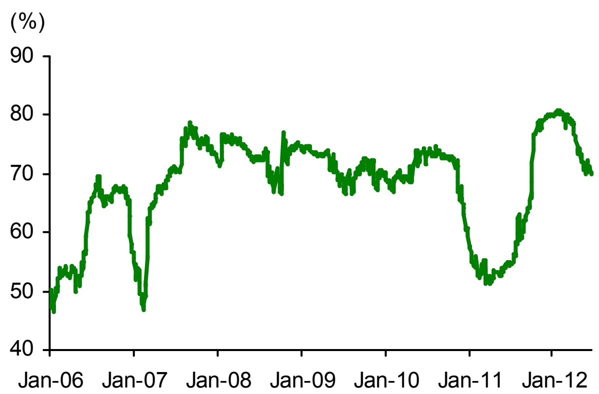
Asian correlation is trending downwards: The realized correlations of the regional indices including Japan all fell, but remain above 70 vol-point. While the correlation of HSI-Kospi2-TWSE is the highest in terms of percentile rank, with 75.3 vol-pt, at the 82nd percentile.

6-Month Realised Correlation Of Regional Indices

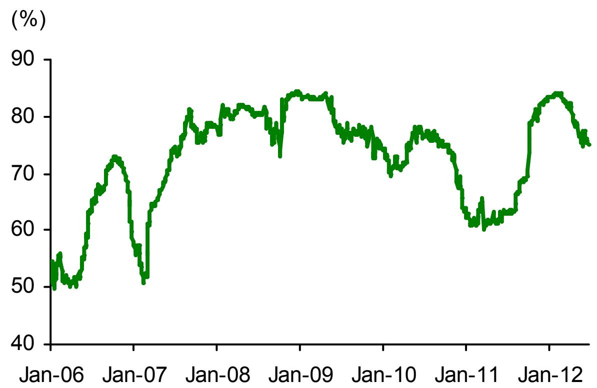
Regional Indices	Correlation (vol-point)	5Y Max (vol-point)	5Y Low (vol-point)	Deviation from Max (vol-point)	Percentile Rank (%)
HSI-AS51-NKY	70.2	80.7	46.3	(10.5)	48.7
HSI-HSCEI-NKY	75.0	84.5	49.9	(9.5)	46.7
HSI-Kospi2-NKY	74.2	79.2	42.6	(4.9)	62.8
HSI-Kospi2-TWSE	75.3	84.0	41.5	(8.8)	81.8

Note: Correlation data as of 18 June 2012
Source: BNP Paribas

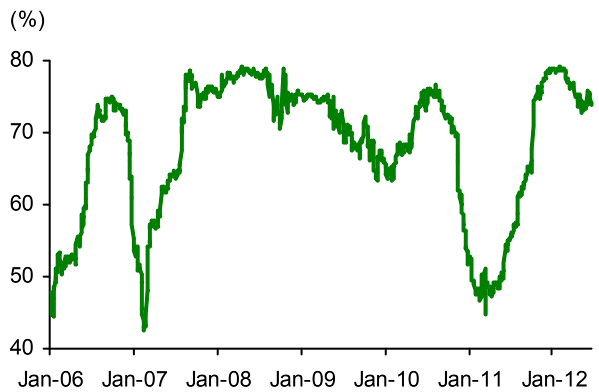
6-Month Realised Correlation – HSI-AS51-NKY



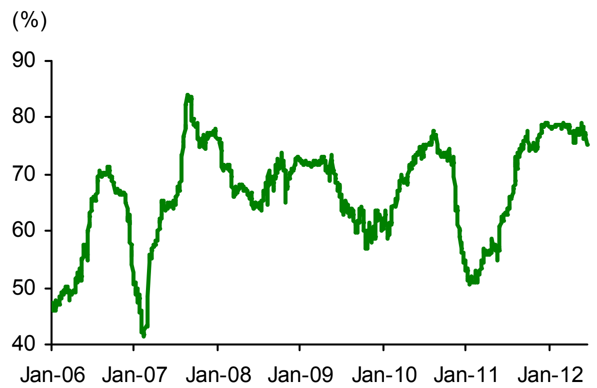
6-Month Realised Correlation – HSI-HSCEI-NKY



6-Month Realised Correlation – HSI-KOSPI2-NKY



6-Month Realised Correlation – HSI-KOSPI2-TWSE

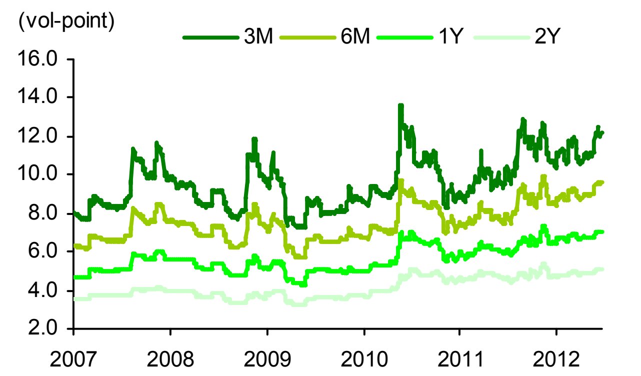


Note: Correlation data up to 18 June 2012
Source: BNP Paribas

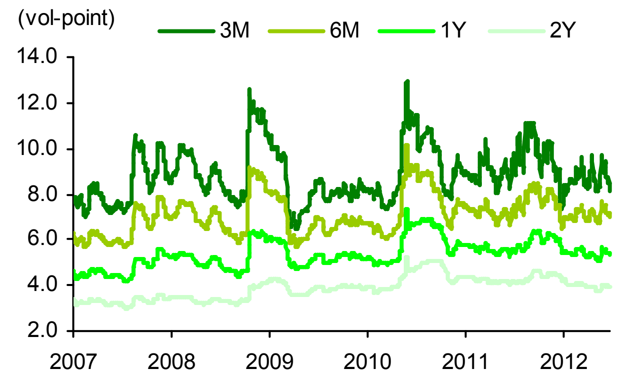
Volatility Skew

The SPX skew steepened: The SPX skew steepened further with the 3M 90-110% skew rising 1.6 vol-pt since the beginning of 2Q. The SPX skew for different maturities are all trading at over the 95%-tile over the past six years, indicating a cautious sentiment in US equities.

90-110% Skew – SPX



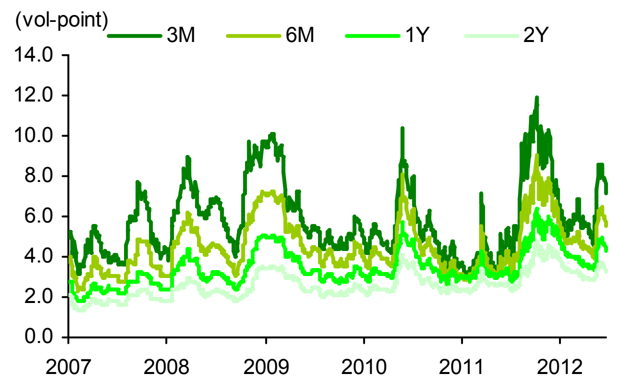
90-110% Skew – EuroStoxx



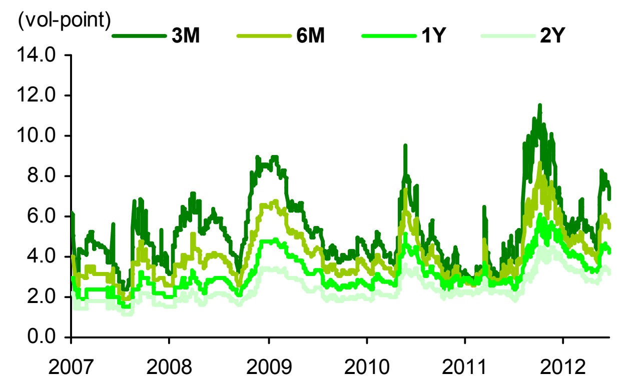
We defined 90-110 skew as the implied volatility of 90% strike minus the implied volatility of 110% strike.
Note: Skew data up to 18 June 2012
Source: BNP Paribas

Steepened Asian skews: Asian skews spiked since the massive sell off in May, but the short-dated skews eased more significantly over the past few days. Volatility and skew levels haven't reached the levels seen during the 2008 Lehman Crisis or the 2011 European debt crisis.

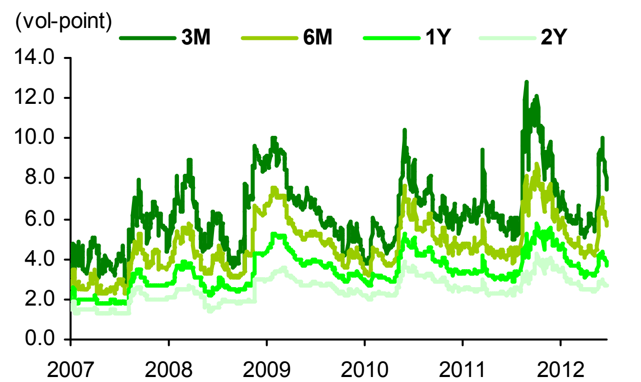
90-110% Skew – HSI



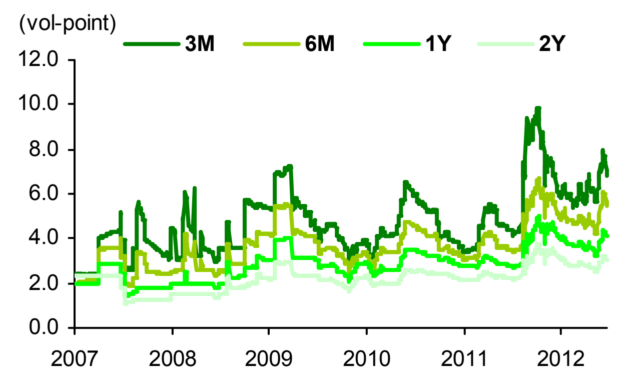
90-110% Skew – HSCEI



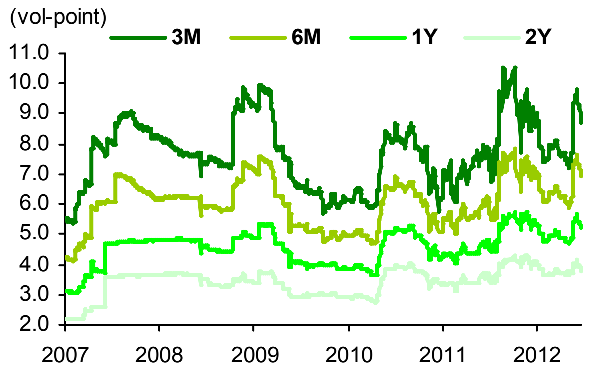
90-110% Skew – Kospi 200



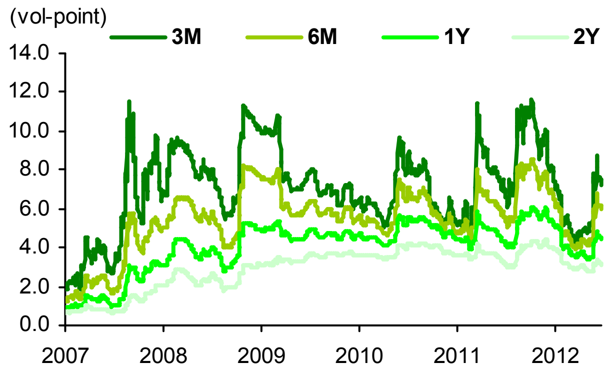
90-110% Skew – TWSE



90-110% Skew – AS51



90-110% Skew – NKY

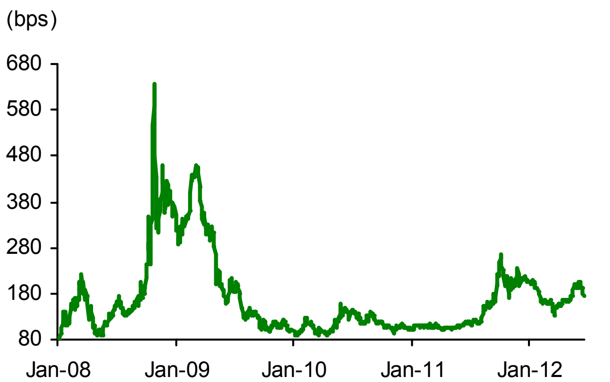


We defined 90-110 skew as the implied volatility of 90% strike minus the implied volatility of 110% strike.
Note: Skew data up to 18 June 2012
Source: BNP Paribas

Credit Spread

Asian credit spreads are easing from recent peaks: The Markit iTraxx Asia ex-Japan IG and Japan IG data that reflect credit risks, surged by a maximum of 29% and 41% respectively since the beginning of 2Q, to 205bp and 218bp. Thereafter, the credit spreads have become less stressed, easing 13.7% and 20.7%. Comparing this to data since 2010, they are now trading at the 82nd and 80th percentile.

Markit iTraxx Asia ex Japan IG



Markit iTraxx Japan IG

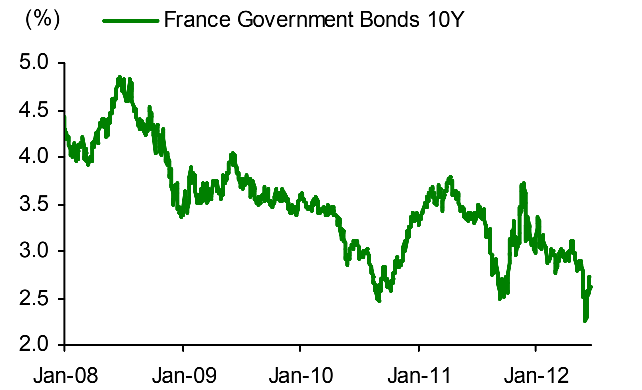
Markit iTraxx Asia ex Japan IG index comprises 40 equally-weighted investment grade CDS index of Asian entities.
Markit iTraxx Japan IG index comprises 50 equally-weighted investment grade CDS on Japanese entities.
Note: CDS data up to 18 June 2012
Source: Bloomberg

European Bond Yields

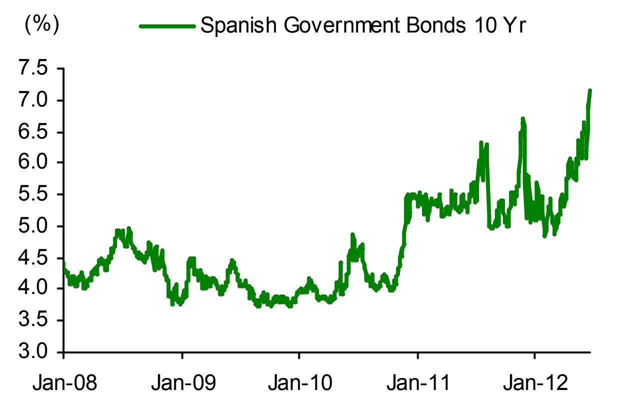
Funding costs in Spain and Italy are becoming a major worry: The macro condition in Europe continues to deteriorate; the Spanish 10Y bond yield exceeded 7% on 18 June and the Italian 10Y bond yields reached a recent high at 6.08%. Within the eurozone, Germany and France are in a better condition. However, we saw rebounds in their yields ahead of the Greek election, and we believe these imply: 1) some investors are ready for a risk-on mode; or 2) some are concerned that Germany and France could be dragged down by the PIIGS countries. Liquidity continues to be parked in US treasury bills and JGBs, indicating that risk-on has not yet started.

German 10Y Government Bond Yield

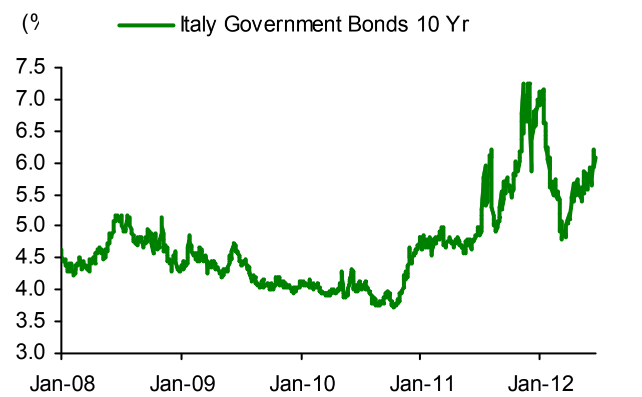
France 10Y Government Bond Yield



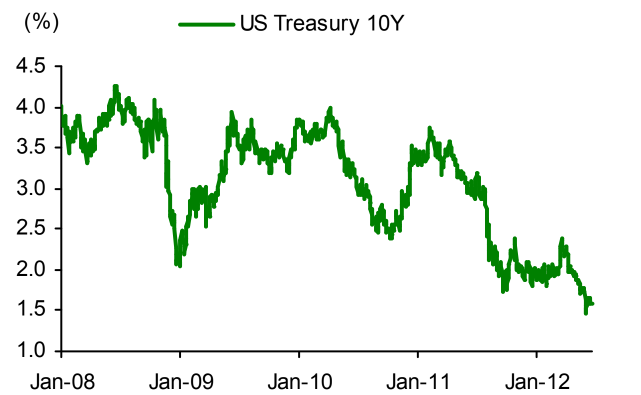
Spanish 10Y Government Bond Yield



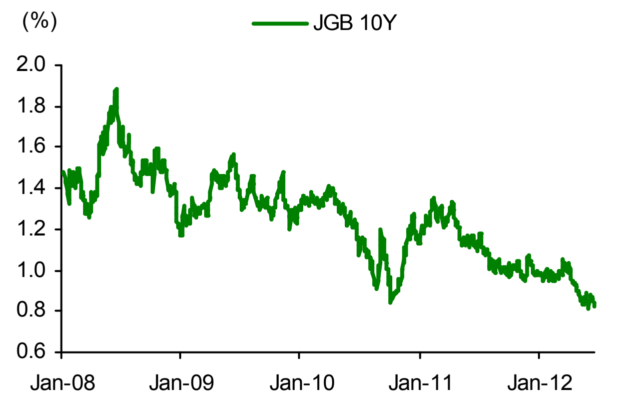
Italy 10Y Government Bond Yield



US 10Y Government Bond Yield



JGB 10Y Bond Yield



Note: Government bond yield data up to 18 June 2012
Source: Bloomberg

APPENDIX 1: TRACK RECORD

Date	Report – Major calls in 2012	Comment [Cut off on 13 Jun 2012]
7 June 2012	**Asian Sniper** – Winner Lee **Zero-Cost Upside Exposure** ⇒ Buy Dec-12 ATM-125% Call Spread and Sell Dec-12 ATM Down-and-In Put with different Knock-In barriers on NKY, TPX, HSI and HSCEI at zero cost [Continuous monitoring] (indicative)	None of the indices breached the DIP barriers since then.
6 June 2012	**Asian Sniper** – Anthony Wong **Yield Enhancement on Japanese Equities** ⇒ Sell July-12 105% Call on TPX at 0.81% (indicative) ⇒ Sell July-12 105% Call on TPX Bank Index (TPNBNK) at 1.65% (indicative)	TPX and TPNBNK advanced 1.1% and 0.6% respectively since then, both less than the call strike of 105%.
1 June 2012	**Long Short Idea** – Samuel Cheng ⇒ Long Tingyi (322 HK) & Short Want Want China (151 HK) [Borrow fee: 50 bps (indicative)]	Tingyi advanced 2.9% and outperformed Want Want China by 0.9% since then.
31 May 2012	**Asian Sniper** – Anthony Wong and Guillaume Derville **Golden Opportunities** ⇒ Buy 3M 105% Call on Gold in EUR (XAUEUR) at 3.55% (indicative) ⇒ Buy 3M ATM or 105% Worst-of-Call on [XAU, USD/EUR] at 1.0% or 0.5% respectively (indicative) ⇒ Buy 3M ATM or 105% Worst-of-Call on [XAUEUR, USD/EUR] at 2.4% or 1.25% respectively (indicative) ⇒ Buy 3M Variance Swap on XAU at 21.85 vol-pts (indicative)	XAUEUR edged up 1.2% since then.
30 May 2012	**Long Short Idea** – Samuel Cheng ⇒ Long Wipro (WPRO IN) & Short HCL Technologies (HCLT IN) [via synthetic futures]	Wipro dropped 3.8% since then, slightly underperformed HCL Tech by 0.2%.
30 May 2012	**Asian Sniper** – Winner Lee and Samuel Cheng **Worst-of Strangles on Key Asian Indices** ⇒ Buy Aug-12 95/105% Worst-of Strangles on HSCEI, Kospi2 and Nifty at 2.8% (indicative) [ATM Worst-of Straddles offered at 6.4%; ATM Worst-of Call plus ATM Best-of Put cost 5.7%; implied correlation at 84%]	NIFTY and Kospi2 rose 3.5% and 1.0% and HSCEI is almost unchanged since then.
28 May 2012	**Asian Sniper** – Anthony Wong, Nadejda Semonova and Guillaume Derville **Silver Bullet on NKY Dividends & Volatility** ⇒ Buy 2016 NKY Dividend at 158.5 div pt and Buy Dec14 90% Put on NKY at 10.7% (23.1 i.v., 0.5% vega) (indicative)	NKY 2016 dividend stayed flattish at 158.5 div pt and NKY edged down slightly 0.1%.
24 May 2012	**Asia Derivatives Focus** – Winner Lee and Anthony Wong **Worst-of Straddles** ⇒ Buy Dec-12 ATM Worst-of Straddles on HSCEI, Kospi2 and NKY at 8.6% (indicative) ⇒ Buy Dec-12 ATM Worst-of Straddles on HSCEI, Kospi2 and Nifty at 9.5% (indicative)	All the underlying indices advanced since then: NIFTY (+4.1%), Kospi2 (+2.7%), HSCEI (+1.2%) and NKY (+0.3%).

Date	Report – Major calls in 2012	Comment [Cut off on 13 Jun 2012]
21 May 2012	**Asian Sniper** – Winner Lee and Anthony Wong **Short-term pains and medium-term gains on HSI and HSCEI** ⇒ Buy Aug-12 105/120% Call Spread on HSI 95% KI offered at 1.0% [59% discount to plain-vanilla Call at 2.44%] (indicative) ⇒ Buy Aug-12 105/120% Call Spread on HSCEI 95% KI offered at 1.3% [53 % discount to plain-vanilla Call at 2.77%] (indicative) ⇒ Buy Aug-12 110% Lookback Call on HSI, 1M lookback at 3.6% [plain-vanilla Call at 1.34%] (indicative) ⇒ Buy Aug-12 110% Lookback Call on HSCEI, 1M lookback at 4.9% [plain-vanilla Call at 1.84%] (indicative)	HSI and HSCEI dropped by 3.9% and 2.4% to their one-month lows, and then rebounded 7.7% and 6.2%, respectively.
17 May 2012	**Asian Sniper** – Winner Lee **Hedging activities in favour** ⇒ Sell Aug-12 110% Call and Buy 90% Put on NKY, TPX and NIFTY at 0.59%, 0.59% and 0.21%, respectively (indicative) ⇒ Buy Aug-12 95/80% Put on Kospi2, HSI, HSCEI and TWSE at 2.0%, 2.9%, 3.7%, and 2.9%, respectively	TWSE, NKY, TPX, HSI and HSCEI dropped 3.3%, 2.8%, 0.9%, 0.4% and 3.6% respectively, while NIFTY and Kospi2 edged up 5.2% and 1.1%.
17 May 2012	**Asian Sniper** – Winner Lee **Short-term weakness on Samsung Electronics** **Relative Strategy – Outperformance Call** ⇒ Buy Jul-12 105/120% Outperformance Call Spread on Kospi2 over Samsung Electronics and Sell 90% Underperformance option at 1.5% (indicative) **Protection or Yield Enhancement** ⇒ Sell Jul-12 105% Call and Buy 95% Put on Samsung Electronics at 0.1% (indicative) ⇒ Sell Jul-12 105% Covered Call on Samsung Electronics receives 2.8% (indicative) **Arbitrage Opportunity – Common vs Preference** ⇒ Long Samsung Electronics Preference (005935 KS) and short Samsung Electronics (005930 KS) [Borrow fee at 40bps]	Samsung Electronics outperformed Kospi2 by 2.9% since then. Samsung Electronics rose 3.9%, less than the Call strike of 5%. The preference share outperformed the ordinary share by 0.8% since then.
10 May 2012	**Asia Derivatives Focus** – Anthony Wong and Winner Lee **The A-Train is Moving** ⇒ Buy Sep-12 105/120% Outperformance Call Spread on XIN50 over SPX or SX5E at 4.25% or 5.25% ⇒ Buy Sep-12 105/120% Outperformance Call Spread on XIN50 over SPX or SX5E minus 90% Put at 2.75% or 3.75% (indicative)	XIN50 outperformed SX5E by 1.3% since then.
7 May 2012	**Index Rebalancing: HSI & HSCEI 2Q12** – Samuel Cheng ⇒ HSI: No constituent change but a relatively big weight lifting on AIA (1299 HK) due to free-float change ⇒ HSCEI: New China Life (1336 HK) is added to replaced China Railway Construction (1186 HK)	HSCEI confirmed our constituent prediction and the weight change of AIA, but HSI surprisingly decided to add Sands China in this quarter.
7 May 2012	**Asian Sniper** – Winner Lee **Bearish Risk Reversal on NIFTY** ⇒ Sell Aug-12 105% Call and Buy 95% Put on Nifty at zero cost (indicative)	NIFTY dropped the most by 5.5% and then rebounded back to almost the original level.

Date	Report – Major calls in 2012	Comment [Cut off on 13 Jun 2012]
4 May 2012	**Asian Sniper** – Winner Lee **Downside Risk Reversal or Yield Enhancement on COLI** ⇒ Jul-12 90/110% Downside Risk Reversal [Sell 110% Call (29.1 i.v.) and Buy 90% Put (33.7 i.v.)] on COLI (688 HK) at 1.03% (indicative) ⇒ Sell Jul-12 110% Call on COLI (688 HK) receives 1.69%, 28 i.v. (indicative)	COLI dropped the most by 13% and then rebounded to 2.5% above the initial level.
3 May 2012	**Index Rebalancing: Kospi 200 2012 Rebalancing** – Samuel Cheng ⇒ Predicted 11 additions and 11 deletions	We forecast correctly 10 pairs of additions and deletions out of the 11, with an excellent hit ratio of 90.9%.
27 April 2012	**Asian Sniper** – Winner Lee **Hedging for potential earnings disappointment in Taiwan** ⇒ Buy June-12 95% Down-and-Out Put on TWSE with knockout 80% (discrete monitoring) at 1% (indicative) ⇒ Buy June-12 95%/80% Put Spread on TWSE at 1.20% (indicative)	TWSE dropped the most by 7.8% and about 5.2% currently.
26 April 2012	**Asia Derivatives Focus** – Anthony Wong and Winner Lee **All eyes are on the BoJ** ⇒ Buy Japan Top BUY Exporters Basket (BNJPTOPE Index) and Sell NKY	The Japan Top BUY Exporters Basket slightly underperformed NKY by 2.3% since then.
25 April 2012	**Asian Sniper** – Winner Lee **HSCEI to outperform HSI** ⇒ Buy Sep-12 or Dec-12 ATM/110% Outperformance Call on HSCEI over HSI at 2.3% or 2.75% (indicative) ⇒ Buy Sep-12 or Dec-12 ATM/110% Outperformance Call on HSCEI over HSI [conditional to HSI>ATM at maturity] at 1.5% or 1.7% (indicative) ⇒ Buy 28-Jun-12 ATM Call on HSCEI and Sell 28-Jun-12 ATM Call on HSI at 80bps (indicative)	HSI and HSCEI dropped 7.9% and 10.7% respectively. HSI outperformed by 2.8%.
19 April 2012	**Asian Equities Derivatives Strategy 2Q12 – "Asian Easing"** ⇒ **Bullish exposure on NKY contingent on JPY:** Buy Dec-12 Call Spread 105/120% contingent on USDJPY touching 88 at 1.4% (discrete monitoring; vanilla at 3.25%, this is a 56.9% discount) ⇒ **China AH Arbitrage:** Buy 28-Jun-12 105/125% Outperformance Call Spread on FTSE China A50 Index (XIN50) over HSCEI at 2.9% (quanto USD, indicative) ⇒ **China Equities to Outperform:** Buy 28-Jun-12 ATM/115% Outperformance Call Spread on HSCEI over HSI at 1.4% ⇒ **China Consumers to Outperform:** Buy China Consumer Top Picks Basket (BNCNTOPC Index) and Sell HSCEI ⇒ **Cross-region Relative Strategy:** Buy an equally-weighted basket of [AS51, Kospi2 and TWSE] and Sell SPX ⇒ **Insurance against Complacency:** Sell Jun-12 110% Call and Buy 90% Put on Asian indices	The contingent call is not activated as JPY strengthened since then. XIN50 outperformed HSCEI by 9.6%, as HSCEI slid 12.5% since then. HSCEI underperformed HSI by 3.2%. China Consumer Top Picks Basket underperformed HSCEI by 2.5%. The equally-weighed basket underperformed SPX by 2.5%.

Date	Report – Major calls in 2012	Comment [Cut off on 13 Jun 2012]
22 March 2012	**Asia Derivatives Focus** – Anthony Wong and Winner Lee **Complacency** ⇒ Sell Jun-12 110% Call and Buy 90% Put on NKY (pays 55bps) and Nifty (receives 10bps) ⇒ Buy Jun-12 Lookback Put, 90% strike (strike equals 90% of the highest close before maturity) ⇒ Buy Jun-12 95/80% Best-of Put Spread on HSCEI / Kospi2 / NKY / AS51 at 85bps (indicative)	NKY and NIFTY corrected 15.2% and 2.1% respectively since then.
21 March 2012	**Long Short Idea** – Samuel Cheng ⇒ Long Sharp (6753 JP) and Short Sony (6758 JP) [Borrow fee: 40 bps (indicative)]	The price of Sharp surged 23% after Hon Hai's acquisition. We advised investors to unwind their positions on 29 March to lock-in 21% of profits generated in seven trading days.
7 March 2012	**Long Short Idea** – Samuel Cheng ⇒ Long FamilyMart (8028 JP) and Short Lawson (2651 JP) [Borrow fee: 40 bps (indicative)]	FamilyMart rose 3.2% while Lawson rose 6.3%; slightly underperformed by 3.1% since then.
6 March 2012	**Asian Sniper** – Winner Lee **Lower Growth Target on China, Downside Risk Reversal on HSCEI** ⇒ Sell May-12 110% Call on HSCEI and Buy 90% Put at 80bps	HSCEI plunged the most by 15.9% and lost 12.9% at maturity.
1 March 2012	**Asia Derivatives Focus** – Anthony Wong **Asian Twin-Win** ⇒ Buy a 1x Dec-12 100-115% Call Spread and 0.5x Dec-12 ATM Put financed by selling a 1.5x Dec-12 ATM Down-and-In Put with different knock-in barriers on NKY, HSI, HSCEI and TWSE at zero cost (indicative)	None of the indices dropped through their corresponding knock-in barrier. NKY: -10.2% HSI: -8.8% HSCEI: -14.8% TWSE: -10.5%
29 February 2012	**Asian Sniper** – Anthony Wong ⇒ Sell Put on HSCEI 2013 Dividends with a strike of 325 dips and buy Call on HSCEI 2013 Dividends with a strike of 350 dips at 13.0 dips ⇒ Sell Put on HSCEI 2013 Dividends with a strike of 325 dips and receive 13.0 dips	HSCEI 2013 Dividends rose from 350 dips to 351 dips since then.
28 February 2012	**Asian Sniper** – Winner Lee **India is the most vulnerable to rising inflation** ⇒ Sell Jun-12 105% Call (21.4 i.v.) and Buy Jun-12 95% Put (25.6 i.v.) on NIFTY receives 70 bps (indicative)	NIFTY made a maximum loss of 10.0% and the loss narrowed to around 4.4%.

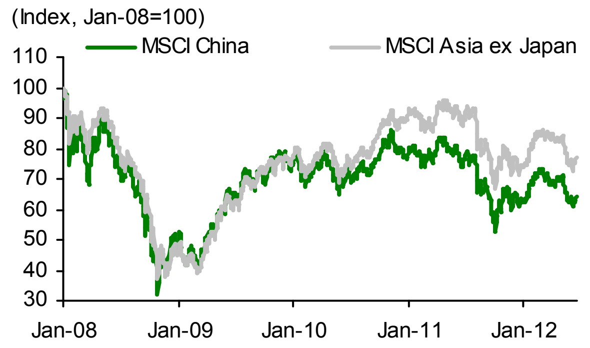
Date	Report – Major calls in 2012	Comment [Cut off on 13 Jun 2012]
27 February 2012	**Asian Sniper** – Winner Lee **Cautious on Japanese Banks – Deteriorating Outlook** **Single-stock Exposure:** ⇒ Sell 11-May-12 105% Call on Mitsubishi UFJ (8306 JP) receives 2.54%, 27.1 i.v. (indicative) Sumitomo Mitsui Financial (8316 JP) receives 2.21%, 25.8 i.v.) Mizuho Financial (8411 JP) receives 2.34%, 27 i.v. (indicative) **Sector Exposure:** ⇒ Sell 11-May12 105% Call and Buy 95% Put on TPNBNK at 1.52% [Call 21.4 i.v., Put 25.8 i.v.] (indicative) **Outperformance:** ⇒ Long Dec-12 105/120% Outperformance Call on NKY over TPNBNK at 3.6% (indicative)	Mitsubishi UFJ, Sumitomo Mitsui Financial, Mizuho Financial and TPNBNK dropped 16.9%, 15.6%, 12.9% and 17.1% respectively at maturity, whilst NKY dropped about 11% and outperformed TPNBNK by 6.1% in the same period.
23 February 2012	**Asia Derivatives Focus** – Winner Lee and Anthony Wong **Hanjeongsik - Korean set meal** ⇒ Buy Samsung Electronics Preference (005935 KS) and Sell Samsung Electronics (005930 KS) [Borrow fee: 75bps]	Samsung Electronics preference share outperformed the ordinary share by 2.3% since then.
16 February 2012	**Asia Derivatives Focus** – Winner Lee and Anthony Wong **Watch your back!** **Implementation 1: Bearish Risk Reversal on Asia ex Japan Indices** ⇒ Sell Jun-12 110% Call and Buy 90% Put on HSI / HSCEI / H-FIN / Kospi2 at 1.46%, 1.67%, 2.31% and 0.35% (indicative) **Implementation 2: Cheap hedge or Call-Overwriting on China Financials and China Properties** ⇒ Sell Jun-12 110% Call on H-FIN receives 2.51% **Implementation 3: Call-Overwriting on Earnings Disappointment** ⇒ Sell Jun-12 110% Call on China Life receives 4.1% ⇒ Sell Jun-12 110% Call on Ping An receives 5.0% **Alert: BOJ Easing!** ⇒ Buy Jun-12 105% Outperformance Call on NKY over HSI / SPX / Kospi2 / Nifty	HSI, HSCEI, H-FIN and Kospi2 dropped 11.3%, 17.8%, 16.4% and 5.9% respectively since then. China Banks and China Properties mostly down a bit, Sell call can receive premium. China Life and Ping An fell 18.3% and 8.9% respectively.
15 February 2012	**Index Rebalancing: India S&P/CNX NIFTY 1H12** – Samuel Cheng ⇒ Addition: Asian Paints (APNT IN) ⇒ Deletion: Reliance Power (RPWR IN)	100% hit ratio on our predictions. Bank of Baroda (BOB IN) was also added to replace Reliance Communication (RCOM IN).
14 February 2012	**Asian Sniper** – Winner Lee **Positioning the China AH Opportunities via FTSE China A50 Index** ⇒ Buy Jun-12 105% Call on XIN50 at 4.15% (indicative) ⇒ Sell Jun-12 105% Call on HSCEI (receives 3.7%) and Buy Jun-12 105% Call on XIN50 (cost 4.15%) at 45bps (indicative) ⇒ Sell Jun-12 105% Call on HSCEI (receives 3.7%) and Buy Jun-12 105% Call on China A50 Tracker (2823 HK) (cost 4.55%) at 85bps (indicative)	HSCEI slumped 16.6% since then, while XIN50 and A50 Tracker slid 2.0% and 9.2%. The latter two outperformed HSCEI.

Date	Report – Major calls in 2012	Comment [Cut off on 13 Jun 2012]
10 February 2012	**Index Rebalancing: HSI & HSCEI 1Q12** – Samuel Cheng ⇒ HSI: Addition: Sands China (1928 HK) & Wynn Macau (1128 HK) ⇒ HSCEI: No Addition and Deletion	No constituent change to both HSI & HSCEI.
8 February 2012	**Asia Derivatives Focus** – Winner Lee and Anthony Wong **Get on the A-Train: Go Local** ⇒ Long Ping An A-shares (601318 CH) and Short Ping An H-shares (2318 HK) [Borrow fee: 40bps (indicative)] ⇒ Long Anhui Conch A-shares (600585 CH) and Short Anhui Conch H-shares (914 HK) [Borrow fee: 3.5% (indicative)] ⇒ Long ZTE A-shares (0000763 CH) and Short ZTE H-shares (763 HK) [Borrow fee: 1.75% (indicative)] ⇒ Long China Merchants Bank A-shares (600036 CH) and Short China Merchant Banks H-shares (3968 HK) [Borrow fee: 40bps (indicative)]	ZTE H/A premium narrowed from 15.9% premium to 17.5% discount, made 33.4% returns and CM Bank H/A premium narrowed from 13.8% to 2.7%, made 11.1% returns. We advised investors to take profit on 17 May.
19 January 2012	**Asia Derivatives Focus** – Anthony Wong **Positioning on cheap NKY implied volatility** ⇒ Buy Dec-13 130%, 140% or 150% Call on NKY at 1.75%, 1.0% or 65bps, respectively (indicative) ⇒ Buy Dec-13 Quanto USD 110/130% Call Spread on NKY at 4.4% (indicative) ⇒ Buy Dec-13 Quanto USD 110% strike Call on NKY with a Knock-in barrier of 140% at 4.2% (indicative)	NKY dropped 1.2% and 3.9% on a Quanto basis since then.
17 January 2012	**Asian Sniper** – Anthony Wong **Position on cheap NKY-implied volatility via straddles spread with AS51 or SPX** ⇒ Buy Dec-13 NKY-AS51 volatility spread via ATM straddles and receive 0.3% premium (22.7% vs 23%) or 2.15 vol-pts (20.75 vol-pts vs 22.9 vol-pts) (indicative) ⇒ Buy Dec-13 NKY-SPX volatility spread via ATM straddles and receive 2.75% premium (22.7% vs 25.45%) or 2.5 vol-pts (20.75 vol-pts vs 23.25 vol-pts) (indicative)	NKY, AS51 and SPX 100-days volatility realized at around 17.3, 13.7 and 13.3 vol-pts respectively. The 60-day realized vol spread was higher than entry level suggested.
9 January 2012	**Asian Equities Derivatives Strategy 1Q12 – "Will the rope hold?"** ⇒ **Bullish exposures** in order to hedge the Upside Risk: **Long NKY 2013** (at 170.5 dips) and **HSCEI 2012 Dividends** (at 325 dips) ⇒ **Downside Risks Hedges:** Best of Puts, Put Spread, Down-and-Out Puts, and Tail-risk Hedges via Variance Spreads (HSCEI vs. HSI and KOSPI vs. SPX)	NKY 2013 dividend and HSCEI 2012 dividend rose to 191 dips (+20.5 dips) and 375 dips (+50 dips) respectively since then. We advised investors to take profit on HSCEI dividend on 10 April.
12 January 2012	**Long Short Idea** – Samuel Cheng ⇒ China Telecom (728 HK) and Short China Unicom (762 HK) [Borrow fee: 40 bps (indicative)]	We advised investors to unwind their positions to lock-in profits (18%) on 2 March.
2 January 2012	**Asian Sniper** – Anthony Wong ⇒ **Sell NKY Convexity before it lowers**: Sell Dec-13 Variance Swap on NKY at 29.6 vol-pts and Buy Dec-13 Volatility Swap on NKY at 25.9 vol-pts to receive 3.7 vol-pts (indicative)	NKY 60-days volatility realized at around 15 vol-pts.

APPENDIX 2: COUNTRY PERFORMANCE

Performance Charts

China



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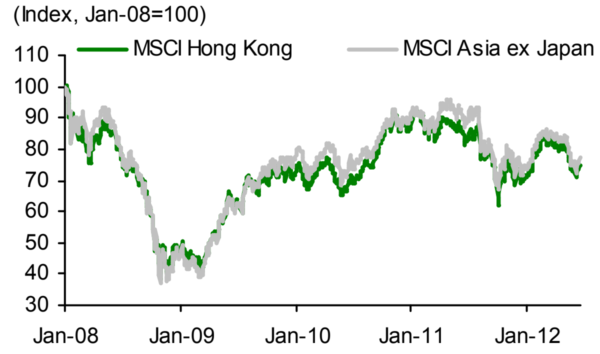

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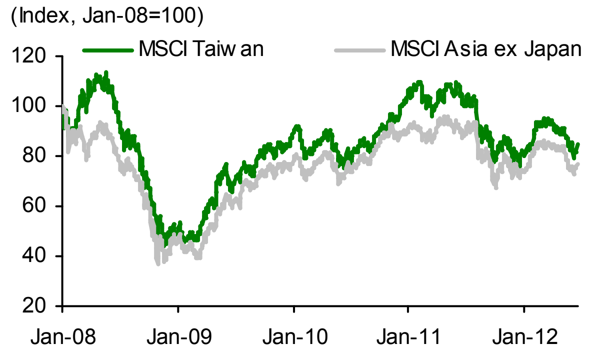

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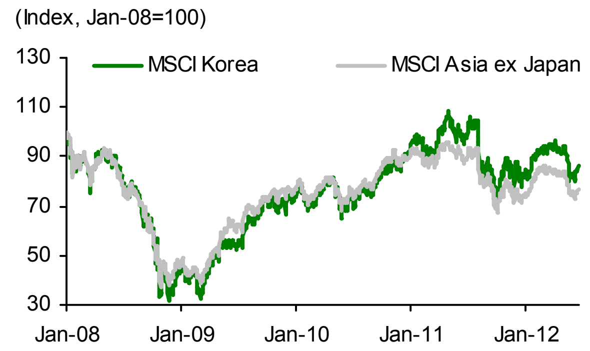

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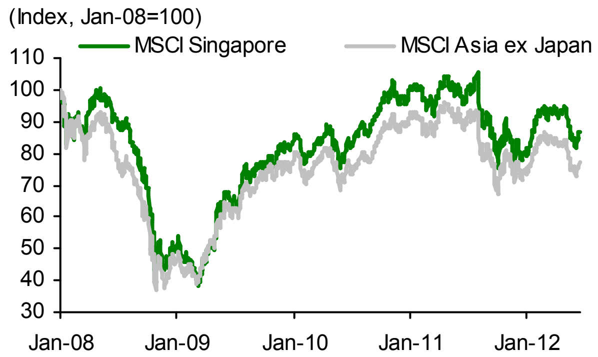

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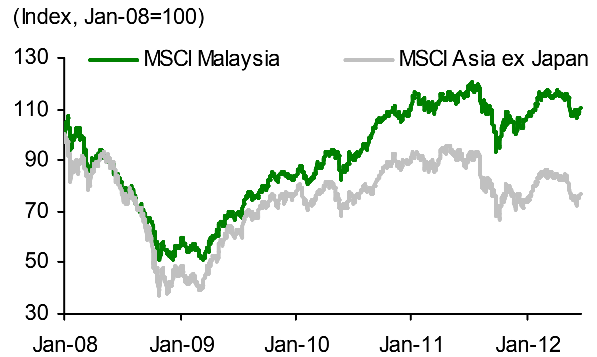

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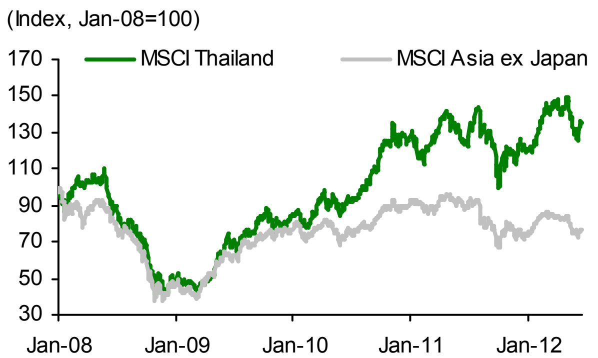

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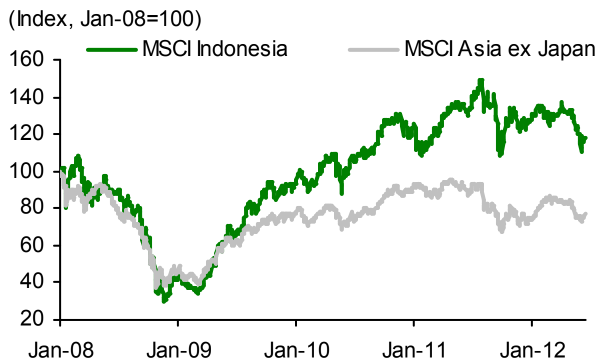
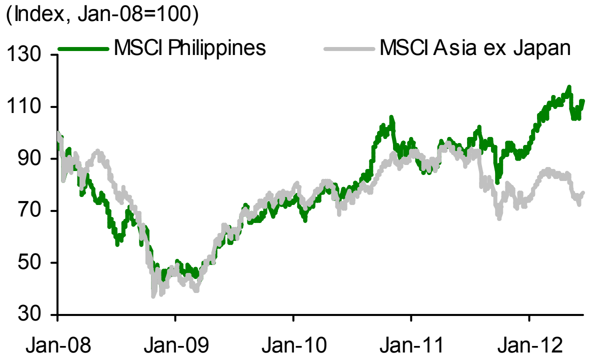


Note: data as of 18 June 2012
Sources: Bloomberg; BNP Paribas

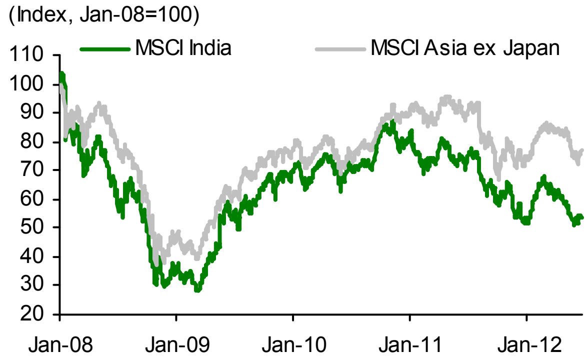
Appendix 2: Country Performance (cont'd)

Performance Charts

Philippines



India



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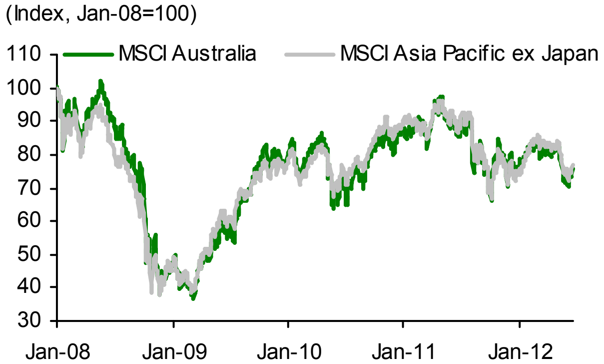

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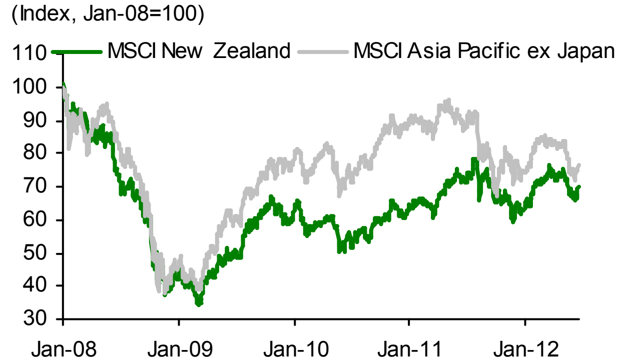
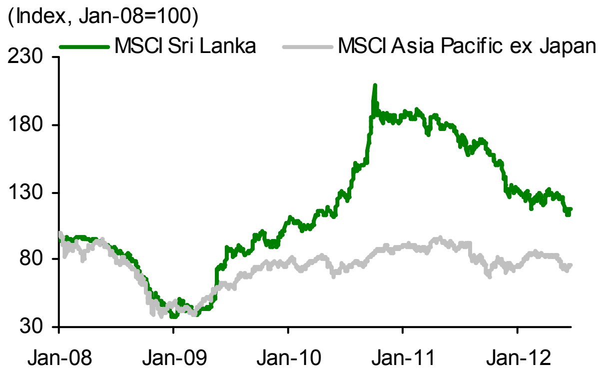
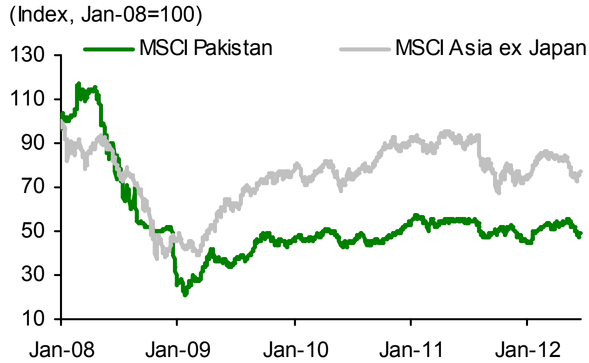


Sri Lanka



Pakistan



Note: data as of 18 June 2012
Sources: Bloomberg; BNP Paribas

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Anhui Conch Cement (914 HK)	5
Bank of China 'H' (3988 HK)	5
CCB (939 HK)	5
China Communications Construction (1800 HK)	5
China National Building Material (3323 HK)	5
China Railway Construction (1186 HK)	5
China Railway Group (390 HK)	5
CNOOC (883 HK)	5
CSR Corp (1766 HK)	5
Hang Seng Bank (11 HK)	5
HK Exchanges (388 HK)	5
ICBC (1398 HK)	5
Sany Heavy Equipment Int'l (631 HK)	5
West China Cement (2233 HK)	5
Yanzhou Coal (1171 HK)	5
Zoomlion Heavy Industry Science (1157 HK)	5

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