



Standpoint

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Whatever it takes

This magic formula used by Mario Draghi characterizes probably best the actions taken by both the ECB and the US Fed during the summer. Whether “unlimited”, in the case of the ECB, or “open-ended”, in the case of the US Fed, these words carefully chosen by the two central banks reflect their absolute commitment to address the concerns of their economies. Obviously, the message has been well received by investors as these words prompted a stock market rally despite a context of deteriorating macro economic data, fiscal balances and corporate earnings. After this initial burst of optimism, Citi analysts question the true meaning and scope of “whatever it takes” monetary policies.

A good thing with the “open-ended” approach of the US Fed is that the potential debate concerning the length and size of the program is immediately removed from the table. Citi analysts estimate that the addition of \$40 billion of MBS purchases by the Fed will account for greater than one-half

of all new US agency mortgage-backed supply. So yes, this is big money, and obviously, the objective of the Fed is that the monetary effect will be leveraged by the “expectations” factor which is less effective when amount and timing are fixed.

If the problem is not that people and companies can't borrow but that they don't want to because they've already got too much debt, then making borrowing cheaper doesn't help much. (Richard Cookson, Chief Investment Officer CPB)

Unfortunately, what recent history has taught us is that Quantitative Easing hasn't really been successful so far . . . At the time of launching QE1 and 2, the objectives of the US Fed were threefold: support housing market, revive credit

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Citi Outlook

A snapshot of Citi's global market views across a select group of asset classes, regions and currencies over the next three to six months.

Our Market Outlook reflects our assessment of each asset class independently of other asset classes. Global Investment Committee (GIC) still remain underweight in global equities but turned positive about European equities with only Japan and European equities having overweights. Within the fixed income universe, the GIC remains positive about Investment grade bonds and emerging debts. Meantime they cut out weights in US Treasuries now stepped down to underweight and stay underweight in all developed sovereign fixed income. In terms of currency, Citi forecasts that USD is likely to be negative in the frame of 0-3 months with risk on after Fed QE and policy actions. In the long term, however, they think that this may reserves as GREXIT and other significant concerns return to hurt risk appetite.

Global equities

Market	Market outlook	Portfolio allocation
	Negative	Underweight
US	Negative	Underweight
Europe	Positive	Overweight
Japan	Positive	Overweight
Latin America	Negative	Underweight
Asia Pacific	Negative	Underweight
Eastern Europe	Negative	Underweight

Global fixed income

Market	Market outlook	Portfolio allocation
	Positive	Overweight
US Treasuries	Negative	Underweight
US High Grade Corporate	Positive	Overweight
Core Euro Government Bonds	Negative	Underweight
Euro High Grade Corporate	Positive	Overweight
Japan Investment Grade	Negative	Underweight
High Yield	Neutral	Neutral
Emerging Market Debt	Positive	Overweight

and boost labour market. For Citi analysts, none of these objectives have been achieved. Surely, since 2008 there has been an economic rebound and there have been tentative signs of revival. However the context of the QE1 launch was different as companies' profits rebounded (though due to costs reductions effect rather than because of a true base effect) and government spending increased to stimulate the economy. Today, not only are private sectors deleveraging and banks facing tougher capital requirements that makes it difficult for money to find its way into the economy, but also the government must address an historical debt and fiscal cliff. In 2013, Citi analysts estimate that a combination of automatic tax hikes and spending cuts will remove about \$800 billion or 5% from the economy unless Congress and the Administration stop it. Although Citi analysts think there is little chance that these changes will be fully implemented, there is some probability that lawmakers will fail to undo the threat before significant financial market disruptions. In the coming months, the challenge will be to find the right political bargain that will put the fiscal deficit and the public debt back on the right track without arming the economy and this challenge does not rely in the hands of the central bank.

In the Euro Area, the recent history of monetary action also showed its limits. In the beginning of the year, the ECB raised hopes and opened a time window for political leaders by launching a 3-Year Long Term Repo Operation program.

The bad news is the continuing disagreement between Germany on the one hand and France, the European Commission on the scope of the ECB's supervisory role in euro area banking supervision, and on the speed with which progress towards banking union can be expected (Willem Buiter, Citi Chief Economist).

Crisis countries were supposed to boost their credibility by cutting spending, liberalizing markets and

privatizing assets. Instead, Athens was soon paralyzed by in-fighting, bailout promises were broken and early elections reignited doubts about the country's future in the euro. In Italy, Prime Minister Mario Monti alleviated a key labor market reform to avoid a confrontation with the unions. In Spain, Prime Minister Mariano Rajoy put his credibility at stake with three attempts at bank reform and three attempts at a budget. More recently, the German willingness to keep control on the criticized regional and local banks threatens the implementation of single bank supervisor in the Euro Area. Looking at the ECB's unlimited bond purchase program in such a dire political context, one might wonder if Draghi's "Whatever it takes" referred to the commitment of the central bank, or to the conditions under which the support will be granted. Indeed, by conditioning the support to a formal request made by the country to the ESM, the ECB is pushing the governments of the crisis countries further in the corner. The reluctance of the governments of Spain and Italy since the announcement of the ECB program to make this official request illustrates the price of the political cost related to the support of the ECB. Without a request, there will be no euro; it is in the hands of the political leaders that lay the keys of the crisis.

With official liquidity the main driver of generous asset valuations, the risk of asset market collapse is always with us. (Willem Buiter, Citi Chief Economist).

The actions taken by the central banks in the US and Europe may look like the long awaited "big bazooka" and are necessary to reduce tail risks and prevent a break down of the financial system in a period extreme stress. However, Citi analysts think that if fiscal authorities don't play their part, monetary efforts could turn out to be a mere short term asset inflationary tool which would substantially increase markets risks and deteriorate the credibility of monetary policy.

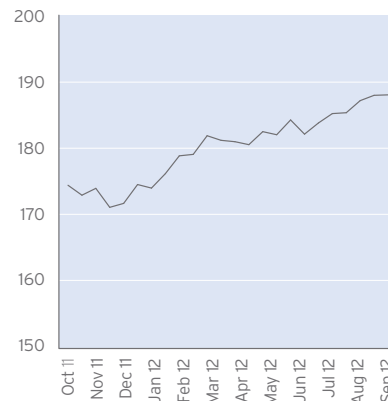
Europe

Fixed income

Monetary Policy Supportive to Corporate Bonds

While open-ended commitments by the ECB and the Federal Reserve substantially reduced tensions in European Sovereign Bonds markets, Citi analysts doubt that monetary tools will reflate economic activity any time soon. Once the dust settles, they expect slowing global growth, falling earnings expectations, and heightened geopolitical uncertainties to keep interest rates low in Core European bonds. In the near term, they also think that Sovereign bond spreads in the region will be driven by uncertainties regarding the timing and levels of OMT activation for Spain as well as Grexit talks. In particular, Citi analysts estimate that Spain will make an official support request in Q1 2013, but not without a period of heightened yields stress and markets

pressure. In the Corporate Bonds sector, Citi analysts observe that the rally which erased more than a third of the spread in the iBoxx, Main and Crossover indices during the summer has been largely driven by monetary factors rather than by improvements in corporate fundamentals. After a strong month of September, which was the biggest month ever in terms of non-financials issuances, they think that the pace of the rally will slow substantially. However, they still see supportive factors as previous peaks in the sector corresponded with peaks in liquidity injections over a three-month period (ECB's OMT has yet to be started) and as the open-ended nature of the Central Banks programs ensures commitment until signs of transmission into economic activity are observed.



Citi Euro BIG (EUR)

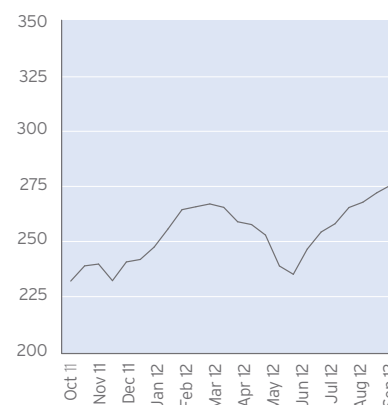
Data source: Bloomberg as of 30 September 2012.

Equities

European Earnings in Recession

Citi analysts observe that Europe successfully took the monetary and political hurdles that paved its way in September. The announcement of the ECB's uncapped Outright Monetary Transaction (OMT) program, the approval of the ESM by the German Constitutional Court and the Dutch general elections amongst others brought a long expected relief among investors. Citi analysts think that both ECB and US Fed monetary support can provide some further upside potential for European equities as risk appetite returns among investors. On the other hand, they don't believe that the new waves of monetary programs will suffice to revive the economic activity given the poor success of monetary transmission observed during the last few years. They also

remind that ECB's monetary support is conditioned by official requests from governments in needs, which is likely to generate tensions in the coming months. In particular, they expect a Spanish request to the ESM during the first quarter of next year. From an economic activity perspective, they expect a GDP contraction of -0.6% this year, and -0.9% for 2013. Citi analysts also observe that the Euro crisis has significantly affected corporate profitability. They estimate that earnings per share of Continental European companies have declined by approximately 15% since the peak in May last year, which puts European companies into a technical earnings recession. With the ongoing recessionary environment, Citi analysts think corporate earnings will rise by 0-10% next year following on from no



DJ Stoxx 600

Data source: Bloomberg as of 30 September 2012.

growth in 2012. Citi analysts continue to prefer Core Europe countries and German equities in particular and favor Defensive Growth strategies.

North America

Fixed income

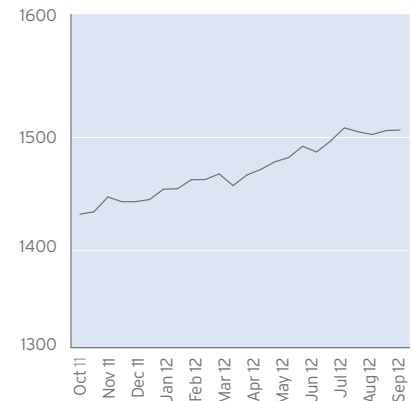
Moving down in quality and getting longer in duration in search for yield

Citi forecasts the global economy to grow only +2.9% in real PPP terms this year and +3.1% next year, a downward revision of -0.1% and -0.2% respectively from the previous quarter. As US fiscal cliff is approaching and the path to European stabilization still appears to be bumpy, Citi analysts forecast Treasury yields could move lower. Further, they think QE3 is likely to contribute to lower Treasury yields through increased demand through improved financial and economic conditions. Given the technical side of policy actions, Citi analysts think long duration likely benefits than short-term ends.

On Investment grade bonds, Citi analysts believe that spreads will return to their QE2 tights in the near term, but limited catalysts to go further. Hence Citi

analysts believe moving down in quality and buying relatively stable 10-year (and under) BBB paper will benefit from continued spread compression in the near term (1-2 months) as fundamentals for Investment Grade bonds are expected to be supportive: companies are sitting on large cash balances while defaults rates are expected to stay low with ample liquidity.

High yield spreads, however, have compressed nearly 200bp since the early June creating the most pleasant environment for corporate issuers. With all the macro news flow subsided, high yield bonds seem to have few reasons for dramatic changes in valuations at the current record low yields. At such, while Citi analysts continue to favor a move down in quality over the medium term, they trimmed out some weights to neutral.



Citi US BIG

Data source: Bloomberg as of 30 September 2012.

Equities

Need upside catalysts in the short term but a 10% gain plausible by next year

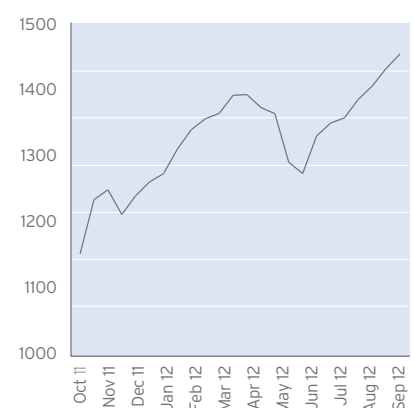
The markets positively responded to Bernanke puts that helped equities reach new highs. But with Fed's accommodation and all the good news now priced in the markets, there are still lingering uncertainties; the upcoming 3Q12 reporting period (with downward guidance potential), the November elections, the fiscal cliff and plausible corporate restraint around policy direction.

There is no argument that liquidity driven asset reflation leveled up trading ranges of risk assets but Citi analysts expect some near-term volatility after the ~15% rise in the S&P500 since June and the markets likely need to be fueled by upside catalysts to grind higher during the reporting season. Indeed, the Panic/Euphoria Model and intra-stock

correlation argue for some pullback in index levels, although valuation and credit conditions suggest that further gains are plausible next year.

Nonetheless, Citi analysts believe that a repeat of 2011's near-bear market correction is unlikely and remain optimistic about US market making further gains next year and forecast for S&P500 of 1,615 by end-2013, a 10% gain from the current level on the ground that easing credit conditions still support continued US economic expansion, with the prospect of sustained margins and modest EPS growth next year.

In terms of sectors, they prefer Diversified Financials, Semis & Semi Equipment, Tech Hardware & Equipment, Insurance, Telecom Services, and Utilities than Autos & Components, Consumer Durables & Apparel, Retailing, Media, Capital Goods, and Materials.



S&P 500 Index

Data source: Bloomberg as of 30 September 2012.

Japan and Asia Pacific

Japan equities

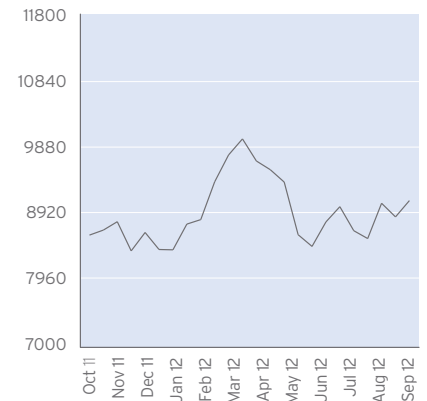
Limited Downside Risks

Citi analysts think downside risk is limited for TOPIX. The Bank of Japan said it would maintain accommodative measures until the employment outlook improves significantly, and the BoJ decided on additional easing measures in light of downside risk to the Japanese economy. What is more, Prime Minister Noda made it clear he plans to compile another supplementary budget for FY12. As such, we think policy expectations will continue to bolster share prices. At the same time, significant upside looks unlikely as concerns about corporate earnings due to weakness for the Japanese and global economies will likely put a lid on growth.

Citi analysts believe the strong yen against the dollar, in which the yen has been strengthening since mid-

2007, has entered its final phase, and they think the dollar has entered a longer-term uptrend. They conclude that Japanese equities remain undervalued on CAPE (Cyclical Adjusted PE) and other metrics. We set our TOPIX target at 920 for End -2013.

Upside risk factors include further economic stimulus measures in China, the US economy recovering more rapidly than expected, and progress with nuclear restarts. Downside risk factors include the emergence of a financial crisis in Europe, a surge in the price of crude on a destabilization of the situation in the Middle East, and yen strengthening versus the euro.



NIKKEI 225 Index

Data source: Bloomberg as of 30 September 2012.

Asia-Pacific equities

Asian Conundrums

"Will Asia equities join the developed market's parade soon?" asked a cautious Asian investor.

It seems unfair to him that Asia equities have been lagging behind DM equities even though Asia economies are growing much faster and their governments have less levered balance sheets than DM counterparties. Furthermore, Asia equities trade at a discount.

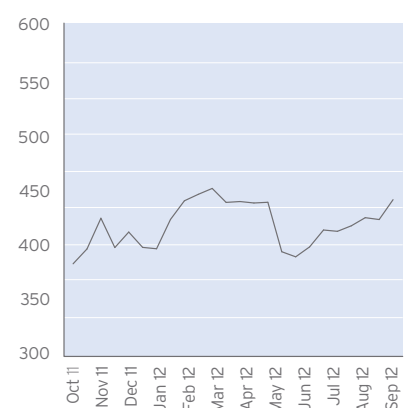
With leading indicators of global growth stabilizing, regional liquidity growing again as Asian central bank balance sheets begin to expand, and the US dollar weakening Citi Asia strategist believes some catch-up in equity market performance in Asia ex Japan and a shift towards more cyclical names is likely in the near term.

Another frequently asked question would be if the time has now come

to switch the weights between Hong Kong and China equities as the relative return gap between two markets widens further. However Citi analysts still remain biased in favour of Hong Kong and wait for a green light to China.

Valuations in general do not explain the underperformance of the Chinese market. Indeed, capital outflows and decelerating PBOC balance sheet appear to the root of weak Chinese equity market and lead to multiples contraction. The fundamental side is also not helping as Chinese earnings continue to revised down and earnings growth is now trailing the regional average.

Citi analysts think the expansion of assets side of PBOC balance sheet likely works as a signal to buy Value on the ground that Value as a strategy has delivered better returns



MSCI Asia Pacific Ex-Japan

Data source: Bloomberg as of 30 September 2012.

in both the A share market and for MSCI China. Empirically A-shares respond well to forward P/E and P/BV while MSCI China to trailing P/E, P/cash flow and/or dividend yield.

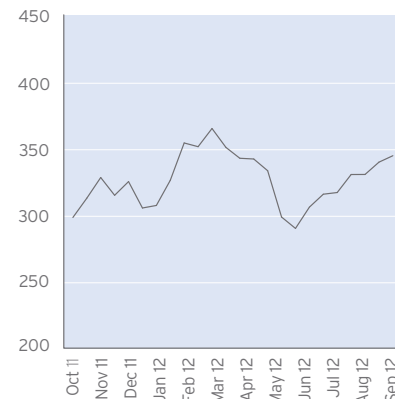
CEEMEA and Latin America

CEEMEA equities

Limited impact from US QE3

Citi analysts have significantly reviewed to the downside their GDP growth forecast for Central and Eastern Europe. They expect a GDP contraction of -1% in Czech Republic and in Hungary while they think the Polish economy will slow down to 2.4% this year. Citi analysts point out weaker external demand and worse domestic spending indicators. Citi analysts also think that weak industrial production, falling construction output and subdued retail sales growth will drive the Polish GDP to slow down further to towards 2.2% in 2013 while other Central European countries could benefit of a modest rebound. In such a difficult growth context, Citi analysts expect monetary policy to be skewed to the downside, which is a major shift in the case of Poland. Russia and South Africa are likely to be further impacted by the slowdown of the Chinese and

European demand for commodities. Also, strong wages increases in Russia have contributed to support retail sales this year, but Citi analysts think expect the growth rate of wages to decrease into next year. Unlike in other Eastern European countries, higher inflation pressures are likely to drive the National Bank of Russia to hike rates further in the coming months. They forecast 3.5% GDP growth in Russia this year and a modest rebound to 4% in 2013. In Turkey, Citi analysts observe that Q2 GDP reading provided encouraging signals about the much needed re-balancing of the economy in favor of net exports despite the strong deceleration of the overall economic activity. They forecast 2.5% GDP growth in 2012 and 4.3% in 2013. From a market perspective, Citi analysts don't think that recent QE3 announcement in the US will provide a similar boost to stock markets in



MSCI EM EMEA

Data source: Bloomberg as of 30 September 2012.

CEEMEA as the ones observed after QE1 and QE2 launches. Back then Emerging Markets were on the path of economic rebound lead by Chinese demand, inflation was kicking and yield much more attractive than today.

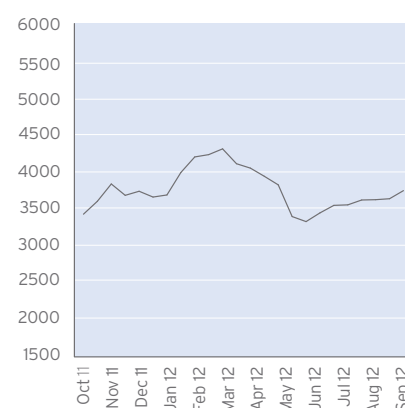
Latin America equities

Earnings Probably Bottomed in Q2

Citi analysts left their GDP growth expectations unchanged for Latin America at 2.4% for this year with Brazil slowing down at 1.4% and Mexico stable at 3.9%. However, they raised their 2012 inflation estimates for both countries on the back of pressure on food prices. This has not substantially altered their monetary policy calls in the region as they still expect an additional 25bp cut in Brazil, although they have delayed the start of monetary tightening to

October 2013. In Mexico, Citi analysts still see the central bank on hold for the foreseeable future. Citi analysts observe that the slowdown of the Chinese imports has a major effect on commodity exporters' trade balance and Brazil in particular as the country saw a trade deficit for the first time in over 10 years in June which impedes

the potential positive spill-over of the US Fed's QE3. In a challenging and slowing economic context, earnings across the region have continued to disappoint. Citi analysts observe that Q2 was the fourth successive quarter of y/y earnings contraction. More than half the companies under coverage missed our analysts' Q2 net profit estimate. In aggregate, net earnings were down 46% y/y in USD, worse than the 39% contraction that the aggregated bottom up forecast implied. Citi analysts also observe large divergences as Mexican companies reported much better results, with 78% beating or coming in line versus Brazil at 46%. Andean companies disappointed heavily as 88% missed our analysts' net profit estimates. Going forward, Citi analysts believe earnings should improve from here as annual reporting is getting easier, EPS growth expectations have been revised much



MSCI EM Latin America

Data source: Bloomberg as of 30 September 2012.

lower and as economic acceleration is expected in both Brazil and China for the second half of the year. For 2012 Citi analysts maintain their top down estimate 0% to -5% EPS growth and forecast +10% to +15% for 2013.

Global REITs and commodities

Real Estate Investment Trusts (REITs)

A new source of upside; development business

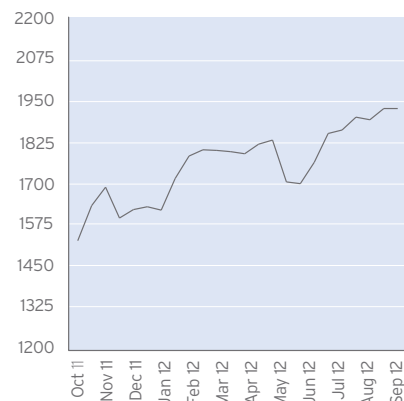
REITs are up 16.5% Year-to-date. Since bottoming in 2009, REITs have benefited from the low interest rate environment, helping the sector reach the post-recession highs. REITs have taken advantage of low rates by refinancing debt at attractive levels, buying assets given a cost of capital advantage and funding new developments accretively.

The transaction cap rates have returned back towards all time lows making purchase prices not cheap anymore versus building costs. Considering attractive spread between building and buying, high aggregate occupancy and recovering employment, more REITs have chosen to add development as one of their core businesses. Citi analysts believe the development business will

be likely another source of upside for REITs given low yields on acquisitions, less competition from private developers, increasing occupancies and an extremely favorable capital environment.

The current construction levels across the US do remain at extremely low levels at only 0.7% given the average starts was 1.9% when industry occupancy levels have been above 91% which is the current rate.

Simply put, rents have more room to rise due to the lack of new supply. REITs therefore would benefit in 2 ways: increased net operating income (NOI) as occupancies and rents move up, and for those active in development - the ability to develop at attractive yields.



EPRA/NAREIT Global Index

Data source: Bloomberg as of 30 September 2012.

Commodities

Further policy stimulus could spur commodity markets higher

With a number of bumps in the multiple roads to continued global supply growth, some commodities look likely to see further upward price pressures while others appear to be tested given global demand recession.

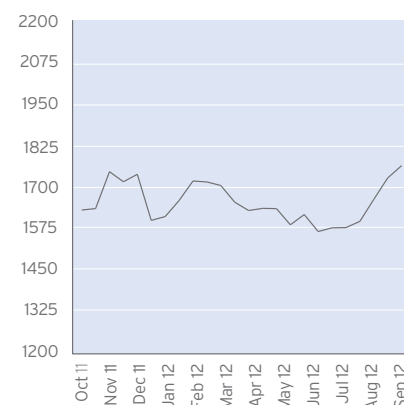
Gold has remained a favored asset class for investors, and after muted returns in 2011 and the first half of 2012, it has returned to strength. The precious metals have responded strongly to policy actions, with silver up +25% and gold up +10% during the 3rd quarter. Empirically the gold price has a strong negative relationship to the US dollar. As major central banks including ECB, the US Fed, the Bank of Japan joined a global chorus of monetary easing providing upside support to the commodity complex, Citi analyst think gold is likely to shine again

in the backdrop of a strengthening of the negative correlation.

With a more constructive outlook for precious metal, they increased 2013 gold price forecast by 3.2 from \$1695 to \$1749 oz%. And also they upgraded platinum and palladium price targets by more than 5% from 2013 onwards.

However, the base metals forecasts have been lowered slightly with 2013 copper prices down 2.9% from \$8200 to \$7,965/t. They believe that eventually a commodity demand pick-up should emerge, but it is likely to lag well into 2013, after leaving the US fiscal cliff behind and seeing a clear sign of China rebound.

They also estimate that the subsequent economic slowdown may lead to decline in the US petroleum demand by -800kb/d but only in a slow fashion spanning two years or longer of



Golds US\$/troy oz.

Data source: Bloomberg as of 30 September 2012.

which impact would be roughly a 3-4% decline in global oil prices. They forecast Brent at \$105 in the 3 month framework and \$100 in the 6-12 months.

Currencies

Euro

Citi analysts observe that the Euro rebounded strongly in September against the USD after the European Central Banks announced the implementation of an unlimited government purchase program while the US Fed's commitment to support the US labor market provided an additional boost to the European currency as risk appetite returned among investors. However, Citi analysts see limited scope for further Euro strengthening as they doubt that too many more potential EUR positives will emerge in the near future. They indeed expect Eurozone growth will remain weak and force the ECB to accommodate further in coming months while Grexit risks clouds the outlook for EUR and emergence of details from the Troika's Athens visit in September could present increased headwinds for the single currency. Furthermore, internal and external political tensions around a Spanish official support request to the ESM and further fiscal savings plans are likely to weigh on the Euro. Citi analysts forecasts EUR/USD at 1.15\$ in the 6-12 months.

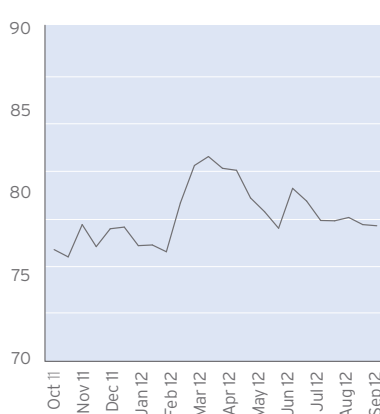


Euro-Dollar (USD/EUR)

Data source: Bloomberg as of 30 September 2012.

Yen

USDJPY trades close to the lowest levels of the year at the end of Q3, but Citi analysts suspect the downside is limited. Citi analysts believe that upcoming general elections will play a major role in determining the course of the JPY. They indeed observe that the Liberal Democratic Party is currently leading in the polls and in a strong position to oust the current leading party of Prime Minister Noda. Citi analysts also observe that among the different candidates, Shinzo Abe appears to be most proponent to monetary easing. Notably, the LDP called for a revision in BoJ law, including drastic monetary easing measures such as raising the BoJ's inflation goal to 2% and having the central bank begin purchases of foreign bonds. Clearly, the LDP plans to promote aggressive FX diplomacy and is targeting a "Heisei-era Louvre Accord." Citi analysts believe that the BoJ is likely to be put under pressure to step up monetary easing and adopt a FX policy more conducive to JPY depreciation. Citi analysts forecast USD/JPY at 76¥ over a 6-12 months period.



Dollar-Yen (JPY/USD)

Data source: Bloomberg as of 30 September 2012.

Pound sterling

GBP has been a source of safe haven flows from Europe all year but has compared unfavorably against the commonwealth currencies and USD along most fundamentals. The September rally runs counter to domestic fundamentals, which remain very weak on growth, competitiveness and monetary policy axes. Recent data suggest that Q3 GDP growth is likely to be positive, but Citi analysts regard this chiefly as a technical rebound from the erratic weakness in Q2 caused by the Queen's Jubilee and the sharp drop in construction activity. Inflation is likely to fall further in coming months and, even with recent rises in energy and food prices, probably will drop below the 2% target around year-end. However, Citi analysts point out that GBP has been moving against the USD in tandem with EUR and they expect it to continue to trade fairly closely. Citi analysts forecast EUR/GBP at 0.76£ over a 6-12 months period and GBP/USD at 1.51\$ over the same period.



Pound-Dollar (USD/GBP)

Data source: Bloomberg as of 30 September 2012.

Investing in Petrostates

Kingsmill Bond, Citi Research's Russia Strategist

Dictionaries define petrostates as those whose wealth stems from the sale of oil and where oil is the key fiscal foundation. There is no universally accepted benchmark number to determine this, although the World Bank uses guiding thresholds of 10% of GDP in oil production and 40% of exports derived from oil. We believe that net exports of hydrocarbons (both oil and gas) as a percent of GDP is the best way to filter for petrostates because gross numbers fail to take account of domestic consumption.

By adding market liquidity criteria, we have a group of 8 countries dominated by Middle East (UAE, Qatar, Kuwait, Saudi Arabia), also including Nigeria, Kazakhstan, Russia and Norway. Interestingly the list of petrostate candidates very clearly excludes Canada, Mexico and Malaysia, three countries often thought of as possible petrostates. The reason in the case of Canada is that GDP from sources other than oil is relatively large, while for the other two that their net exports are relatively low because of large domestic consumption. Similarly, Brazil and Argentina were still net hydrocarbon importers in 2011.

These markets have, of course, a number of identities and drivers apart from oil, and oil is only one of a number of commodities that drive different markets. So the question to ask is why we believe the petrostate identity is paramount and why oil is different to other commodities.

Why the petrostate identity is paramount

Writing in 1997, Terry Karl in 'The paradox of plenty' argued that the transfer of wealth to the petrostates during the 1970s was larger than at any time since the looting of Latin America

in the sixteenth century. Meanwhile the 1970s oil boom is widely described as the largest peacetime transfer of wealth in history. However, the wealth transfer of the last decade has been larger still in dollar terms, as both the real oil price and volumes have been higher. Russia's GDP has increased nearly tenfold in the last decade, in the same way as that of Saudi Arabia increased in the 1970s.

Moreover, the vast wealth tends, in most instances, to produce a similar and highly predictable response in terms of rentier behaviour, Dutch disease and so on, which come to be the key drivers of economies and markets.

Why oil is different

Oil differs from other commodities because it is worth so much more, because it is a critical factor in processing other commodities (especially base metals and bulk commodities), because the OPEC cartel is so powerful and because its history is different from that of other commodities. Moreover, unlike industrial commodities, demand growth for oil is not dominated by China alone.

The advantages of petrostates

Petrostates have built up remarkable amounts of wealth, which can be seen by looking at wealth funds, reserves or government debt levels. Over the course of the last decade our eight focus petrostates have built up wealth funds and stabilisation funds of over \$2,500bn, and this sum is increasing by around \$200bn a year. Also, petrostates have built up foreign reserves of over \$1,600 bn, with over \$1,200 bn in our eight focus markets alone, making up some 31% of their GDP. Finally, most petrostates have been able to use the oil money to reduce state debt levels as a

percentage of GDP very significantly. The average level of government debt to GDP for our eight focus petrostates in 2011 was 17% compared to nearly 100% in the West.

Strong macroeconomic framework

As a result of the oil money, the petrostates have a very robust macroeconomic framework. They run large current account surpluses, large fiscal surpluses, and have good growth levels. As would be expected for countries that for the most part hold down their currencies, inflation levels are relatively high. Our current forecast is that the oil price remains elevated for the next 2-3 years, gradually declining to the \$80-90 level (in real terms) in 2020. So in theory there should still be a river of cash flowing into the petrostates. There are also a number of disadvantages of being a petrostate, stemming from political corrosion, price volatility, currency appreciation and petrostates structural difficulties to diversify their economies away from oil which is a major problem when oil money dries up, as the petrostates found out to their cost in the 1980s. However, having lived through the misery of the 1980s, most petrostates have taken some lessons to heart and are likely, in our view, to cut expenditure more rapidly when oil prices fall, reducing their macroeconomic exposure. They have also been conscious about spending to assure economic diversification, especially in the GCC countries, including Saudi Arabia. Finally, as we have seen, many countries have accumulated fabulous amounts of wealth during the boom years, using this to pay down debts, and build up wealth funds and reserves.

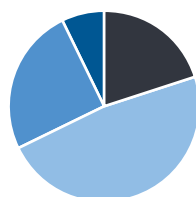
Final word

Asset allocations

Euro-tilted model portfolios

Defensive

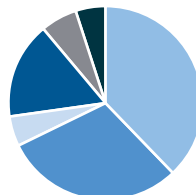
Seeking primarily capital preservation over time and only willing to accept very minor portfolio value fluctuations from month to month.



- EUR Cash **20%**
- EUR Government Bonds **48%**
- EUR Corporate Bonds **25%**
- European Equities **7%**

Income-oriented

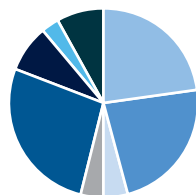
Seeking growth of wealth over time but unwilling to accept significant fluctuations in the value of portfolio from month to month.



- EUR Government Bonds **38%**
- EUR Corporate Bonds **30%**
- EUR High Yield Bonds **5%**
- European Equities **16%**
- Global Equities **6%**
- Global REITs **5%**

Growth and income

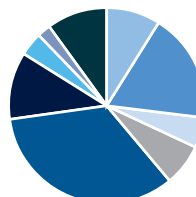
Seeking long-term capital growth foremost but unwilling to accept significant losses on value of portfolio over the medium term.



- EUR Government Bonds **23%**
- EUR Corporate Bonds **23%**
- EUR High Yield Bonds **4%**
- Emerging Market Debt **4%**
- European Equities **27%**
- US Equities **8%**
- Pacific Equities **3%**
- Global REITs **8%**

Growth oriented

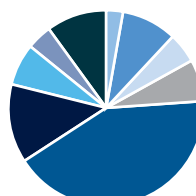
Seeking long-term capital appreciation and willing to tolerate measured medium-term volatility in order to enhance longer-term performance.



- EUR Government Bonds **9%**
- EUR Corporate Bonds **18%**
- EUR High Yield Bonds **5%**
- Emerging Market Debt **7%**
- European Equities **34%**
- US Equities **11%**
- Pacific Equities **4%**
- Emerging Markets Equities **2%**
- Global REITs **10%**

Aggressive Growth

Seeking long-term capital appreciation and can accept potentially large losses on portfolio over the near-to-medium term in order to maximise long-term performance.



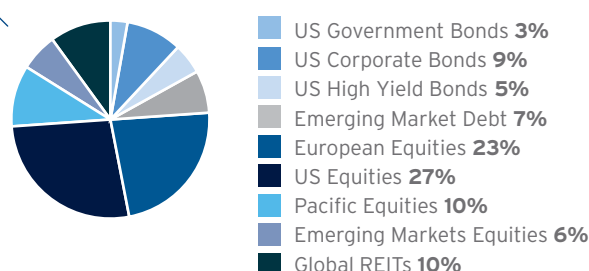
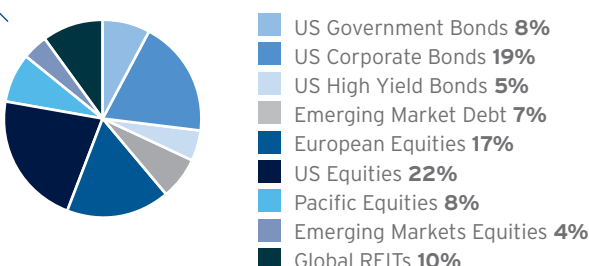
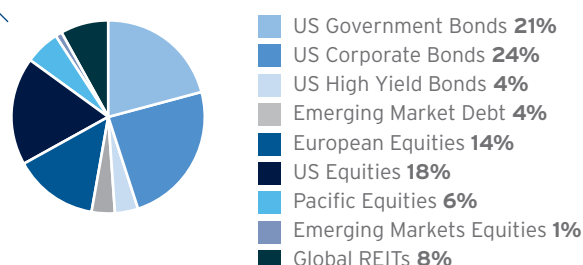
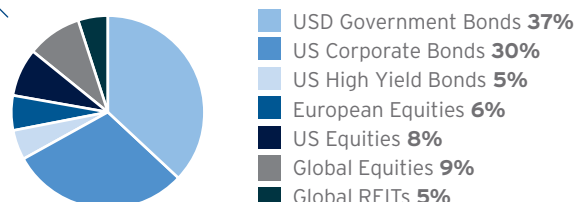
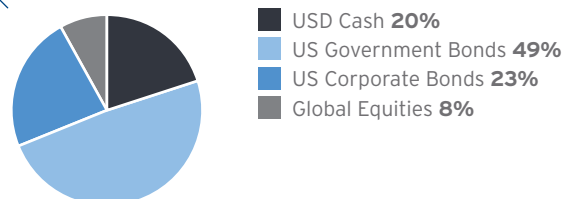
- EUR Government Bonds **3%**
- EUR Corporate Bonds **9%**
- EUR High Yield Bonds **5%**
- Emerging Market Debt **7%**
- European Equities **42%**
- US Equities **13%**
- Pacific Equities **7%**
- Emerging Markets Equities **4%**
- Global REITs **10%**

Spotlight on allocations

The suggested allocations are intended to be general in nature and are not to be construed as specific investment advice. Investors are encouraged to consult with their Financial Professional to determine their allocation needs based on their risk tolerance, suitability and goals.

Data Source: Citibank NA as of October 2012

USD-tilted model portfolios



About the Citi asset allocation process

The Citibank tactical portfolio allocations are based on the work of the Global Investment Committee (GIC) of Citi Private Bank. The membership of the committee is comprised of experienced investment specialists from across Citi. The GIC deliberates on the macroeconomic and financial market environment in order to formulate an outlook across multiple asset classes and is responsible for maintaining tactical model portfolios based on this outlook. The tactical weights that are applied to the Citibank portfolios are aligned to the decisions of the GIC.

Allocation to bond and equity markets

- The GIC remain underweight on global equities and overweight on global bonds.

Despite the risk on after Fed QE and other major central banks' policy actions, the GIC still remains cautious about its portfolio allocations given growing concerns over the real growth and the equity market is likely vulnerable to upcoming earning releases. Globally, corporate earnings are falling and forecasts continue to be revised down and may argue for earnings recessions.

Allocation to regional equity markets

- The GIC remain overweight on Japanese equities and European equities whereas underweight on US and Emerging Market equities.

Valuations for Japanese equities are still cheap historically and against its other developed market peers. US equity valuations are relatively expensive than other developed peers and there are still lingering uncertainties. Even though Citi analysts are positive about US equities in the long term and think there is likely a 10% or more upside to go further in 2013, they think the current new high may offer a good chance of taking profits with many uncertainties lingering.

Despite very early signs of global demand stabilizations from some emerging markets, they think they can see the real growth in 2013 and still remain very cautious about emerging markets.

Allocation to government and credit markets

- The GIC remains overweight on investment-grade corporate bonds and emerging market debt, and remain underweight on government bonds. They are neutral on high-yield bonds.

Considering the still uncertain macroeconomic environment, the GIC turned underweight in treasuries.

Important Disclosure

"Citi analysts" refers to investment professionals within Citi Investment Research and Analysis, Citigroup Global Markets and voting members of the Global Investment Committee and Global Portfolio Committee of Citi Private Bank.

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