

Prudential International Investments Advisers, LLC.

Global Investment Strategy – August 2009

By John Praveen, Chief Investment Strategist

For Market Commentary Interviews Contact: Lisa Villareal, 973-367-2503/lisa.villareal@prudential.com

Financial Market Outlook & Strategy: Further Stock Gains Likely, Year-end Target Raised. Bond Under Pressure

John Praveen's Global Investment Strategy – August 2009 remains positive on the outlook for stocks in H2 2009 and expects further gains despite the solid equity gains thus far. The drivers for further equity gains are: 1) the global GDP recovery proceeding faster than expected, growth expectations being revised higher, and uncertainty about the timing of the GDP recovery has been removed; 2) earnings recovering and earnings expectations being revised higher and likely to surprise on the upside; 3) inflation 'sweet spot' approaching with deflation pressures easing, but inflation still remaining under control; 4) continued stabilization in financial market conditions and risk appetite improving further. ***Given the further improvement in the growth, inflation and earnings outlook, we have raised our 2009 year-end forecast for the U.S. stock market (S&P 500) from 1100 to 1150-1200. We continue to expect international markets to outperform the U.S. market.***

In the near-term, stocks are experiencing a technical correction given the strong gains and the overbought conditions. In addition, questions about the strength and sustainability of the economic and earnings recovery and fears about premature rate hikes are likely to contribute to equity volatility. ***However, we expect stocks to rebound from this correction and post further gains into year-end.***

Bond yields are likely to remain under modest upward pressure as the economic recovery is proceeding faster than expected. Japan's GDP has already turned positive and GDP growth in Europe and U.S. is also expected to turn positive in Q3 and strengthen further in Q4, pushing yields higher. Further, inflation is close to a trough and expected to turn positive as base effects begin to reverse, removing a tail wind for bonds. However, central banks remaining on extended hold is likely to limit the rise in bond yields. A technical equity market correction and macro data disappointment in the near-term are also likely to support bonds.

Among global stock markets, we remain overweight Emerging Markets, and modest overweight in the U.K. and Japan. We remain underweight on the U.S. and Eurozone. ***Among Government bond markets***, we have a modest overweight in Japan and U.K., and modest underweight in U.S. Treasuries and Eurozone bonds. We remain overweight Emerging Market bonds.

Among global sectors, we remain Overweight in Financials, Information Technology, Modest Overweight in Energy, Materials and Industrials. We remain Underweight in Consumer Staples, Healthcare, Consumer Discretionary, Telecomms, and Utilities.

The global asset allocation and strategy models presented are hypothetical models shown for illustrative purposes only, and does not necessarily reflect the management of any actual account. Following the models presented may not result in profitable investments.

Financial Market Outlook: Further Stock Gain on Faster GDP Rebound and Earnings Recovery. Year-end Target Raised

Stocks: Further Stock Gains on Faster GDP Rebound, Deflation Set to Ease & Earnings Recovery. Year-end Target Raised

- Stocks rebounded sharply in late July /early August after the correction in late June/early July fuelled by better-than-expected Q2 earnings and broad evidence that the recovery from the recession is proceeding faster than earlier expected.
- The Great Global Recession appears to be winding down faster than expected with GDP growth turning positive in Japan, Germany, and France in Q2. Eurozone Q2 GDP came in close to flat, the U.S. posted a much smaller Q2 GDP decline, and both Europe and U.S. are on track to positive GDP growth in Q3. China, Korea and several emerging economies posted stronger-than-expected GDP growth.
- Headline inflation fell deeper into negative territory in July, but inflation appears to be close to a trough and is expected to turn positive in late Q3 and Q4. Over the next few months, equity markets are likely to enjoy the inflation 'sweet spot' with deflation pressures easing, but inflation remaining under control. Central banks are currently on hold with policy rates at record lows and unlikely to raise rates well into H1 2010.
- There was a positive earnings surprise in Q2 with U.S. earnings coming in much better than expected, driven by sharply improved earnings in Financials. U.S. Q2 earnings declined -28%. Global earnings expectations are being revised up with the GDP recovery proceeding ahead of schedule, solid Financials earnings with diminished loss write-downs, and increased profitability due to the steep yield curve. The rebound in industrial production augurs well for Industrials earnings while the rise in oil and commodity prices should support Materials and Energy earnings.
- Equity market valuation multiples rose further in July with the sharp rally in global equity markets. Trailing P/E multiples in Developed Markets are now at the highest level since 2004. However, despite the sharp equity rally, stocks retained their valuation advantage relative to bonds.
- ***Despite the solid equity gains thus far, we remain positive on the outlook for stocks in H2 2009 and expect further stocks gains with: 1) the Global GDP recovery proceeding faster than expected and growth expectations being revised higher, uncertainty about the timing of the recovery has been removed; 2) Earnings recovering and earnings expectations being revised higher and likely to surprise on the upside; 3) Inflation 'sweet spot' approaching with deflation pressures easing, but inflation remaining under control; 4) Continued stabilization in financial market conditions and risk appetite improving further.***

Global Investment Strategy – August 2009

- *Given the further improvement in the growth, inflation and earnings outlook, we have raised our 2009 year-end forecast for the S&P 500 from 1100 to 1150-1200. We continue to expect international markets to outperform the U.S. market.*

In the near-term, stocks experiencing a technical correction given the strong gains and the overbought conditions. In addition, questions about the strength and sustainability of the economic and earnings recovery and fears about premature rate hikes are likely to contribute to equity volatility. *However, we expect stocks to rebound from this correction and post further gains into year-end.*

Bonds: Bond Yields Under Pressure With Faster Exit From Recession, Inflation Trough

- Global government bonds posted modest gains in July due to concerns about the global GDP recovery earlier in the month. U.S., Eurozone, and Japanese bonds all posted modest increases in US\$, but U.K. Gilts declined modestly. Emerging Markets bonds continued to rise strongly
- *Looking ahead, bond yields are likely to be under modest upward pressure as the economic recovery is proceeding faster than expected. Japan's GDP has already turned positive and GDP growth in Europe and U.S. is also expected to turn positive in Q3 and further strengthen in Q4, pushing yields higher. Further, inflation is close to a trough and expected to turn positive as base effects begin to reverse, removing a tail wind for bonds. Stronger growth and inflation data are likely to continue to put upward pressure on bond yields. However, central banks remaining on extended hold is likely to limit the rise in bond yields. A technical equity market correction and macro data disappointment in the near-term are also likely to support bonds.*
- *U.S. Treasury yields are likely trend up modestly with the economy on track to post positive GDP growth in Q3. The German and French GDP rebound and faster recovery in Eurozone as a whole is likely to put upward pressure on Eurozone yields. U.K. Gilts yields are likely to trend modestly lower with relatively weaker GDP growth, and the expansion of the BoE's QE programs. JGB yields are expected to trend modestly lower, still benefiting from the easy monetary policy and deflationary pressures.*

Investment Strategy: Overweight Stocks on Faster GDP Rebound and Earnings Recovery

ASSET ALLOCATION: Stocks vs. Bonds

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Remain Overweight Stocks: We expect further stocks gains with GDP recovery proceeding faster than expected, earnings recovery, better pricing power with an inflation 'sweet spot' approaching, continued stabilization in financial market conditions and improving risk appetite. However, stocks in a technical correction in the near-term given the strong gains and the overbought conditions, as well as questions about the strength of the economic and earnings recovery and fears about premature rate hikes.

Remain Underweight Bonds: Government bond yields likely to be under modest upward pressure as the economic recovery is proceeding faster than expected. Further, inflation is close to a trough and expected to turn positive, removing a tail wind for bonds. Stronger growth and inflation data are likely to continue to put upward pressure on bond yields. However, central banks remaining on extended hold is likely to limit the rise in bond yields.

GLOBAL EQUITIES

Overweight: Emerging Markets Continued improvement in macro outlook with strong Q2 GDP rebound due to massive stimulus packages and faster recovery in developed markets. Increased risk appetite is a positive and likely to lead to further gains for EM stocks. The rally in oil and commodity prices is a positive for earnings. However, EM now trades at a premium to DM on some valuation measures.

Modest Overweight: U.K. & Japan 1) UK: Macro outlook is relatively less positive but valuations and sector composition are positives for U.K. stocks. Earnings likely to surprise on the upside; 2) Japan: GDP rebound in Q2. Earnings remain on recovery track. Yen depreciation (trade weighted) is a positive.

Modest Underweight: Eurozone Faster than expected GDP recovery with Q2 GDP almost flat, and likely to turn positive in Q3. Relative valuations are attractive. However, Eurozone earnings outlook relatively less attractive. Euro appreciation is a further negative for stocks.

Underweight: U.S GDP posted a much smaller decline in Q2 and turning positive in H2. Positive Q2 earnings surprise, but valuations expensive relative to other markets. U.S. underperforms international markets during equity market rallies.

GLOBAL BONDS

Overweight: Emerging Markets EM bonds are likely to be supported by strengthening risk appetites as the global economy recovers further in H2. The macro outlook for EM continues to improve further, suggesting a further narrowing of spreads. Emerging economies recovered in Q2 with strong rebound and are on track to recover further in H2 2009. After a long period of cutting rates sharply, some EM central banks are beginning to remain on hold. However, the decline in inflation still gives them room to cut rates if growth disappoints.

Modest Overweight: U.K., Japan 1) UK: Relatively weaker GDP recovery and Quantitative Easing should support U.K. Gilts. Increasing supply and low level of yields could put some upward pressure on yields. 2) Japan: JGB yields are expected to trend modestly lower, still benefiting from the easy monetary policy and deflationary pressures and questions about the sustainability of growth after the Q2 rebound.

Modest Underweight: U.S., Eurozone 1) U.S. Treasury yields are likely trend up modestly with GDP growth and inflation on track to turn post positive in Q3. However, the Fed remaining on extended hold is likely to limit the rise in bond yields. Valuations are expensive. 2) Eurozone: Stronger than expected recovery in the Eurozone is a negative for bonds. Less support from QE. Valuations are expensive.

GLOBAL SECTORS

Overweight: Financials, Info. Technology. Modest Overweight: Energy, Materials, Industrials.

Modest Underweight: Consumer Staples, Healthcare. Underweight: Consumer Discretionary, Telecomms, Utilities.

CURRENCIES

Overweight: Euro; Neutral: Sterling; Underweight: U.S. Dollar, Yen.

The dollar likely to struggle with stronger economic recovery and the ballooning fiscal and current account deficit. However, there could be some near-term volatility due to questions about the strength of the economic recovery. Yen weakness with increase in carry trade.

Regional Equity Strategy

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Emerging Markets (EM): Emerging economies recovered in Q2 with strong rebound in Asia – led by China, India and Korea - on the recovery in exports and massive fiscal stimulus packages boosting domestic demand, while recovery in energy and commodity prices boosted economies in Latin America and EMEA. Emerging economies are on track to recover further in H2 2009 and 2010 with the recession ending in developed economies. The recovery in oil and commodity prices is a positive for earnings, especially for EMEA and Latin America. Increased risk appetite is likely to lead to further gains for EM stocks. However, EM now trades at a premium to DM on some valuation measures. Near-term, emerging economies - especially China - in a technical correction. **Remain Overweight.**

U.K.: U.K. Q2 GDP fell more than expected, down -3.2% QoQ annualized, after sinking -9.3% earlier in Q1. While Q2 GDP disappointed, the continued improvement in business confidence and stabilization in industrial activity suggest that GDP will recover in Q3. Valuations and sector composition remain positives for U.K. stocks. The BoE held the bank rate at 0.5% in August, and increased its Quantitative Easing program by £50bn to £175bn. However, earnings outlook has been relatively weak with U.K. earnings expectations revised down. **Remain Modest Overweight.**

Japan: Japan's GDP has posted a solid 3.7% annualized rebound in Q2 after plunging -11.7% annualized in Q1. The BoJ left its policy rate unchanged in August, after extending its QE program in July. Earnings are likely to recover in coming quarters after troughing in Q1 2009 driven by the recovery in domestic and global GDP growth. The depreciation of the yen on trade weighted basis is a positive for Japanese stocks. **Remain Modest Overweight.**

Eurozone: Faster-than-expected Eurozone recovery with Germany and France lifting Q2 GDP close to flat and on track to turn positive in Q3. Early expectations are for Eurozone Q3 GDP to rise around 0.8% QoQ annualized, accelerating to over 3% in Q4. However, weakness in Italy and Spain are likely to be a drag on Eurozone GDP. The ECB left rates unchanged at 1% at its August meeting and made no change to its €60bn covered bond program. Recent appreciation of the euro is a modest negative for Eurozone stocks. Eurozone Q2 earnings estimated to decline -39.7% in Q2 after a sharp -43% in Q1. However, earnings are expected to improve in H2 2009 with Eurozone emerging from recession faster than expected. **Reduced Underweight.**

U.S.: U.S. GDP growth is on track to turn positive, around 2.8% annualized, in Q3 as the fiscal stimulus boosts consumption and government spending after posting a much smaller -1% decline in Q2. Earnings surprise on the upside with stronger than expected Q2 earnings. Earnings recovery in H2. However, the U.S. remains expensive relative to other markets. In August, the Fed left rates unchanged and signaled that it would not expand its Treasury buying program, but would extend the program to the end of October. Given its defensive characteristics, the U.S. has underperformed international markets during equity market rallies. Given our expectations of further stock gains, international markets are likely to outperform the U.S. Hence we remain underweight in the U.S. **Increased Underweight.**

Regional Bond Strategy

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Emerging Markets: EM bonds are likely to be supported by strengthening risk appetite as the global economy recovers further in H2. The macro outlook for EM continues to improve, suggesting a further narrowing of spreads. Emerging economies recovered in Q2 with strong rebound in Emerging Asia on the recovery in exports and massive fiscal stimulus packages while recovery in energy and commodity prices boosted economies in Latin America and EMEA. Emerging economies are on track to recover further in H2 2009 with recession ending in developed economies. After a long period of cutting rates sharply, some EM central banks are beginning to remain on hold. However, the decline in inflation still gives them room to cut rates if growth disappoints. If the DM recovery is not as robust, EM yields are likely to rise faster as risk aversion returns. Further, the increase in fiscal spending is likely to increase EM bond supply leading to some upward pressure on yields. **Remain Overweight.**

Japan: Japan's economy rebounded in Q2 with GDP rising 3.7% annualized, the first positive GDP reading in five quarters. However, there are concerns about the sustainability of the recovery after the Q2 rebound, a positive for JGBs. JGB yields are likely to benefit from the BoJ's easy monetary policy with the bank leaving its target overnight call rate unchanged at 0.1% in August after extending its QE policy in July. Bonds are also likely to benefit from deflationary pressures with Japanese nationwide core inflation fell at its sharpest pace on record, falling -1.7% YoY in June due to base effects and lower fuel prices. High levels of real interest rates is a further positive. However, rich valuations relative to stocks, low nominal interest rates and recovering GDP growth are likely to put some upward pressure on JGB yields. **Modest Overweight.**

U.K.: U.K. Gilts are likely to benefit from the relatively weaker GDP growth outlook after Q2 GDP fell more than expected, down -3.2% QoQ annualized, after sinking -9.3% earlier in Q1. U.K. headline inflation held at 1.8% in June, with prices also unchanged MoM. Base effects from the rise in electricity prices will begin to fall out of the YoY rate in August and September, sending inflation lower. The BoE held the bank rate at 0.5% in August. The BoE also decided to increase its QE program by £50bn to £175bn after completing nearly 90% of the program by July. Gilts also have relatively stronger momentum compared with other bond markets in recent months. However, the already low levels of nominal and real yields are likely to keep the downtrend in U.K. yields modest. **Modest Overweight.**

Eurozone: Eurozone Q2 GDP surprised on the upside, coming in at just -0.4% QoQ annualized decline, well ahead of consensus expectations of a -1.5% decline, and a sharp improvement from the -9.7% plunge in Q1. Early expectations are for Eurozone GDP to turn positive in Q3, rising around 0.8%. Headline inflation sunk to a record low of -0.7% YoY in July, driven by the decline in energy prices. However, inflation is likely to have troughed in July and likely to rise over 1% in late 2009 due to base effects from the sharp drop in oil prices in late 2008. The ECB left rates unchanged at 1% in August and made no changes to its covered bond program. However, since the fiscal stimulus was relatively small in Eurozone, growing bond supply is not a negative for Eurozone bonds. This is likely to limit the rise in Eurozone yields. **Modest Underweight.**

U.S.: U.S. GDP posted a smaller decline in Q2, down -1% QoQ annualized, a significant improvement over the -6.4% decline in Q1 and is on track to turn positive in Q3 as the fiscal stimulus boosts consumption and government spending. Although base effects from oil prices pushed headline inflation to -2% YoY in July from -1.2% in June, headline CPI is expected to turn positive in late Q3 and Q4 2009. Rising fiscal deficit and increased Treasury supply continue to be negatives for Treasuries with the budget deficit for FY 2009 expected to grow to \$1.85trn or 11.9% of GDP. Further, nominal yields are still low relative to history, putting upward pressure on yields. Continued stabilization in financial market conditions and improving risk appetite are also negative for Treasuries. However, the Fed remaining on extended hold is likely to limit the rise in bond yields. Possibility of an equity market correction in the near-term is also likely to support Treasuries. **Modest Underweight.**

Global Sector Strategy

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Our global sector model ranks sectors on a comparative basis using macro factors, valuation, earnings and risk measures.

- **Financials** - Earnings growth in Q2 surprised on the upside and likely to recover sharply during H2. Improved financial market conditions and steep yield curves are positives. Diversified Financials also benefit from increase in capital market activities. Insurance benefiting from equity market gains. Consumer Finance remains relatively weaker. **Overweight.**
- **Information Technology** - Macro outlook remains positive with ongoing recovery in tech orders. Earnings revisions continue to strong and better than most other sectors. Valuations are expensive relative to other global sectors. New product launches and high cash levels are positives. European Tech firms benefit from smaller exposure to consumers and Financials. **Overweight.**
- **Energy** - Oil prices remain volatile in recent months. However, oil prices are likely to recover and trade between \$70-\$75 in H2 with faster GDP recovery. Relative earnings outlook is negative, but likely to be revised higher with strong earnings revisions in recent months. However, sector valuations are at par with the market. Oil Services have attractive valuations and supported by continued demand for maintenance. **Modest Overweight.**
- **Materials** - Concerns about GDP recovery has kept commodity prices volatile. However, the CRB index remains solid, driven by still strong demand for commodities such as iron ore. Outlook for Construction Materials remains weak with housing markets still in a decline. M&A activity and improvement in demand due to increased fiscal spending are positives. **Modest Overweight.**
- **Industrials** - Industrial activity is rebounding sharply after the sharp decline in Q1. Global business confidence continues to rise with manufacturing confidence indices posting gains in all regions. Fiscal stimulus in the U.S. and China are positive for infrastructure spending. Valuations are attractive. Earnings outlook remains weak, but likely to be revised higher. **Modest Overweight.**
- **Consumer Staples** - Continued improvement in the global GDP outlook is a negative for the sector. Relative valuations are attractive. Earnings growth is better compared with other sectors. However, increase in oil and commodity prices are negative for the sector due to an increase in input costs. Prefer international Tobacco relative to U.S. on growing U.S. regulations. **Modest Underweight.**
- **Healthcare** - Easing of risk aversion is a negative for Healthcare. Further, Pharma faces headwinds such as regulatory risk, political pressures, pricing weakness and downgrades to long-term earnings outlook. Current valuations are modestly attractive relative to the market. Sector's earnings and dividend growth remain relatively solid. **Modest Underweight.**
- **Consumer Discretionary** - Sector fundamentals remain negative with unemployment continuing to rise and household earnings growth anemic in major developed markets. Sector earnings outlook remains negative relative to other global sectors. Relative valuations are also expensive. Consumer fundamentals in emerging markets are supported by government spending. **Underweight.**
- **Telecomm Services** - Consumer fundamentals remain negative. Valuations are at par with other global sectors. Earnings outlook is a modest negative with continued negative earnings revisions due to weak consumer as well as business spending. Big Telecomms favored due to their strong and stable cash flows and cost saving opportunities. **Underweight.**
- **Utilities** - Sector likely to underperform with the decline in risk aversion. European Utilities face headwinds of expensive valuations, regulatory headwind, and weak pricing power. Sector valuations are attractive. Earnings revisions have held up well due to the ability of Utility operators to pass on higher input costs to customers. **Underweight.**

Strategy Summary:

Asset Allocation – Overweight: Stocks. Underweight: Bonds.

Global Equities – Overweight: Emerging Markets; Modest Overweight: U.K. & Japan; Modest Underweight: Eurozone; Underweight: U.S

Global Bonds – Overweight: Emerging Markets; Modest Overweight: U.K., Japan; Modest Underweight: U.S., Eurozone

Global Sectors – Overweight: Financials, Info. Technology; Modest Overweight: Energy, Materials, Industrials; Modest Underweight: Consumer Staples, Healthcare; Underweight: Consumer Discretionary, Telecomms, Utilities.

Currencies – Overweight: Euro; Neutral: Sterling; Underweight: Yen, U.S. Dollar.

Disclosure:

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