

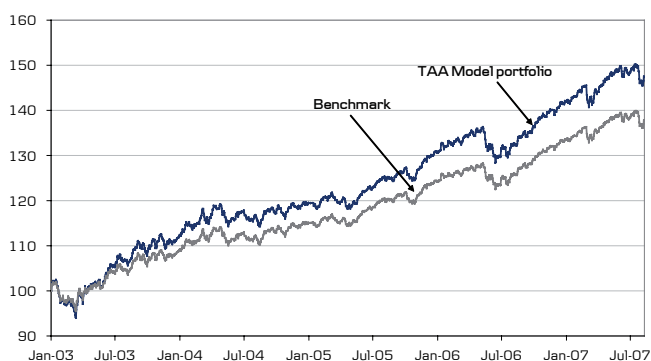
Tactical Asset Allocation

Danske Capital • 10 August 2007



Historical Performance

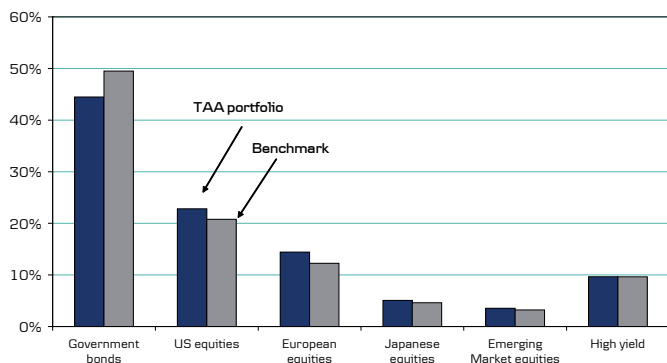
TAA Performance



Information Ratio: 1.4

Current recommendation

Model portfolio august 2007



Note: Benchmark is rebalanced at the beginning of each year

Performance results:

Portfolio return 2007 (ytd): 3.3 percentage points
 Performance 2007 (ytd): 0.6 percentage points

» a real and abrupt turn in the credit cycle poses a major tactical risk to global equities and hence to our allocation. However, we do not expect this to occur just yet.«

That was how we ended the last edition of this publication – and we were wrong. On the timing at least! The question now is 1) is this a real turn in the credit cycle? “no” is the answer in our opinion 2) how much damage has been caused and 3) where do we go from here? We think that what has happened so far in the credit space is manageable and constitutes a healthy correction in an asset class that has long been mispriced. On the other hand, we do not yet think this poses a major buying opportunity for either credit or equities (though sentiment in the credit space is close to panic, which normally constitutes a tactical buying opportunity). As such we continue to recommend a modest equity overweight of 5 percentage points and a neutral weight to high yield.

We are still of the opinion that US subprime and its underlying cause, i.e. the US housing recession, will not derail either the US economy or the global economy. Right now we think that what is causing the turbulence is basically that very few people, if any, understand what is going on and everybody is throwing numbers around. As we wrote in the last edition of this publication, we do not pretend to understand the risks stemming from credit either. However, we do think we have a proper understanding of the magnitude of the losses we are facing in US subprime – and these are manageable. Hence, even with the gearing on top, we think the total losses that our industry is facing from the debacle in US housing are manageable.

In that respect, consider the following. The Fed has said that losses stemming from US subprime will be in the range of USD 100bn. With a very pessimistic scenario, we arrive at USD 200bn. Indeed, that is a lot of money and this is by no means insignificant. Some people have already lost - and more will lose – significant sums of money. However, we need to put things into perspective. From the peak of the dot.com bubble to the bottom, the S&P500 lost around USD 6000bn in market capitalisation and the value of US household holdings of equity-related financial assets declined by almost USD 6500bn. In comparison we think the value destruction that the US economy is facing right now is rather insignificant and we are, quite frankly, tired of hearing about US subprime.

That does not change the fact that the situation is very unfortunate. The situation could get out of hand, were the sell off in equities to last and spreads continue to balloon upwards. For now, we think developments in corporate credit constitute a healthy correction and when things settle down, a true credit crunch will be far off. But the situation requires monitoring.

More importantly, the subprime story will be with us for some time yet, partly due to the fact that its underlying cause, the

housing market, is a slow moving market. We can only hope that when the next set of bad news emerges, people, especially equity investors, will prove more rational than they have been over the past 14 days. Developments in financial markets always demand respect, but this time around, we think that markets are wrong and global equities are once again trading below fair value.

Unfortunately, the credit story also means that the US economy will continue to be the centre of attention at a time when developments in the rest of the world are so much more interesting. For the record, we still think the Fed will be on hold well into 2008 (quite possibly for the full year) and still consider the strength of the global economy to be the biggest threat to our allocation.

Last month the Euro area unemployment rate hit a 25 year low at 6.9 percent. We think this is yet another sign of the structural change within the European economy, especially as wage pressures are nowhere near the levels that the current level of unemployment would have generated in the past. However, this cannot continue forever, and signs are emerging that capacity in the Euro area is becoming ever tighter. The ECB continue to warn about inflationary pressures (Trichet even called an un-

scheduled press conference after the August tele-meeting of the governing council, just so he could say «strong vigilance» and thus signal that barring an atom bomb or major financial crisis they will hike in September – though he also underlined that the ECB never precommits!) and although we do think that they are well ahead of the curve, we think they are right to hike. 4.25 by September is a done deal. From there the short-term outlook is difficult, but we think risks are skewed firmly on the upside and expect the ECB to be in proper restrictive territory by end 2008.

Turning to equity markets, volatility has clearly increased. We think the coming quarters will prove to be quite interesting but also more difficult for people like us. We are certain that we will face a proper correction (and not just the wobbling that has characterised markets the past couple of weeks) over the coming quarters, but the more we see of these mini corrections with subsequent rallies, the more likely it is that equity markets will also fall victim to the kind of exuberance that has characterised rate and spread markets over the past couple of years. What does that mean? It means that equities will become expensive before this expansion ends and that one day a correction will emerge which will end up being the start of a new bear market. That day remains, in our opinion, some time away, which is why we continue to recommend overweighting equities.

Latest strategy changes:

08/06/07:	Equities downweighted 5%, bonds upweighted accordingly. Global equities downweighted from 8% to 4%, European equities downweighted from 2 to 1%. Overall equity overweight 5%	01/01/06:	Equities overweight increased to 8% at the expense of bonds
25/04/07:	Global equities downweighted 2% to 8% overweight, bonds upweighted accordingly, European equity overweight of 2% retained, overall equity overweight 10%	06/12/05:	Cash downweighted to neutral 0%, bonds upweighted accordingly Europe downweighted to neutral, US upweighted accordingly to -5%
01/01/07:	Equities upweighted 2%, bonds downweighted accordingly	20/10/05:	Japan overweighted to +3%, USA downweighted to -7%
22/08/06:	European equities upweighted 2%, bonds downweighted accordingly	05/09/05:	Europe, Japan, Emerging Markets overweighted to +2%, USA downweighted to -6%
07/06/06:	Japan, Emerging Markets downweighted to neutral, USA upweighted to neutral	20/05/05:	Equities downweighted 5%, bonds upweighted accordingly

Quantitative indicators for Tactical Asset Allocation

Asset classes	Equities/Bonds	High Yield/Equities	High Yield/Bonds
Valuation (+/- 2)	buy(+1) Yield gap	sell(-2) High Yield gap	sell (-1) Credit Spread
Trigger 1 (+/- 1)	neutral (0) Risk appetite	sell (-1) Slope of the yield curve	sell (-1) Slope of the yield curve
Trigger 2 (+/- 1)	neutral (0) Production	neutral(0) Capacity Utilisation	buy (+1) Real Interest Rate
Trigger 3 (+/- 1)	neutral (+1) Volatility	neutral (-1) Volatility	buy (+1) Investments
Total Score (+/- 5)	+2 neutral	-4 sell	0 neutral

USA: Merrill Lynch Master High Yield Index OAS

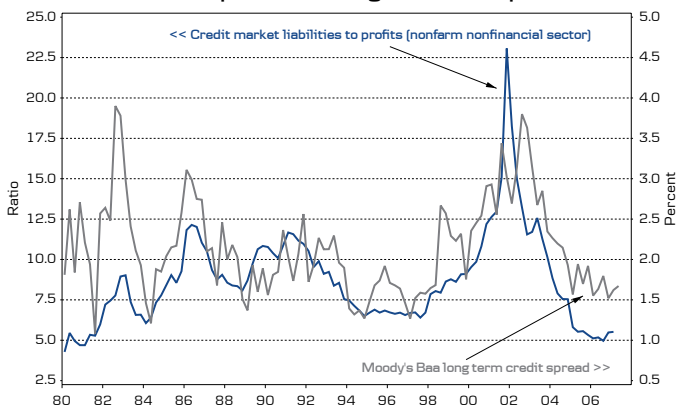


Yet another bubble is correcting!

Needless to say, the source of the action over the past month has been the US credit markets, where the uncertainty surrounding US subprime filtered through to high yield markets.

So far, in our view, what has happened in high yield constitutes a healthy correction and not a real credit crunch. Healthy, because just as the low level of government bond yields has created excesses, so has the low level of spreads. Private equity people are simply arbitraging companies' balance sheets and private equity managers are not supposed to be paid fortunes for that, while investors bear all the risk. When the dust settles, we think that the leveraged as well as the corporate bid for equities will remain intact, simply because equities are still the cheapest asset, both in absolute as well as in relative terms.

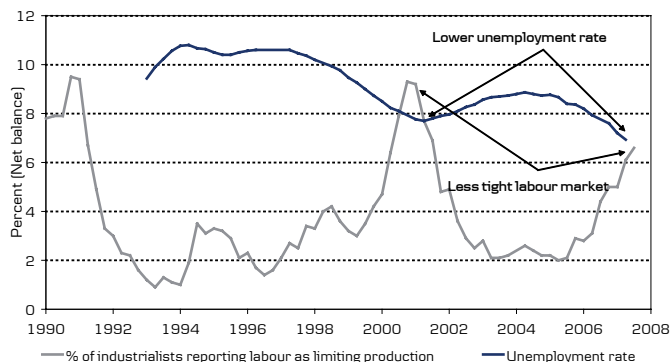
USA: Corporate leverage & credit spread



One of the reasons why we think that this is not yet the end of the credit cycle is the excellent health of most parts of the corporate community around the globe. As the chart on the left shows, US corporates are in excellent shape. However, some sectors have started to re-leverage, including corporates with lower grade ratings and they are the ones that are finally paying for it.

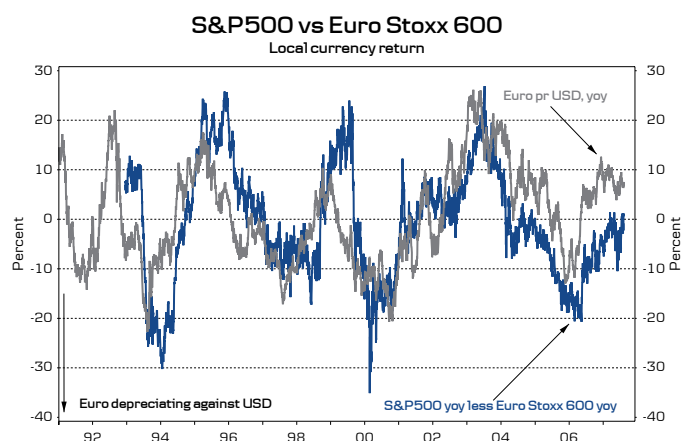
We do think the best is behind us. As major corporates start to re-leverage that will contribute to increased volatility in general and higher spreads in particular. And while we do think that, tactically, spreads are most likely to narrow somewhat, the fundamental case for generally higher spreads remains. Therefore we chose not to change our neutral recommendation on high yield.

Euroland: Labour market



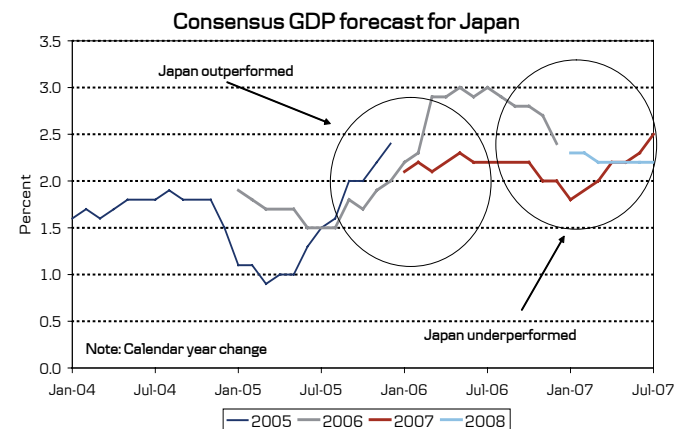
We have been recommending a slight European bias in the general equity overweight for the past year which has been a marginally good call. The main driver is the changing fundamental landscape in Europe. In that respect, note the chart on the left. Euro area unemployment has fallen to the lowest level ever. At the same time the labour market is not as tight as one would have feared just a few years ago.

Going forward we expect the improving labour market to support growth through job creation and higher wages. As such the composition of Euro area growth will change. That will keep growth above potential and thus force the ECB to continue tightening. How soon they will take rates to restrictive is difficult to say, but we expect the ECB to reach 4.75 to 5 at the end of next year.



Having outperformed quite substantially, European equities seem to have settled down recently. One reason is surely the strength of the Euro, as illustrated in the chart on the left. However, European equities have not underperformed as one would have expected from looking at the chart.

There are several reasons for this. First of all European companies have become more efficient thus enhancing their ability to handle an appreciating currency. Furthermore and much more importantly, European companies are now far more exposed to Eastern Europe and Asia than just a few years ago thus lowering the importance of the EUR/USD. Going forward we do not have a strong call on European vs. US equities, but we do think that risks are skewed towards European outperformance. We are thus sticking to our European bias.



We note with satisfaction that Japanese equities have stopped underperforming (in local currency terms). However true out-performance is way off.

We are still of the opinion that the underlying Japanese economy is in better shape than it has been for many years, but it is a very slow moving process. Furthermore, investors have been disappointed with Japanese companies several times, thus losing faith in their potential. Most recently, Abe's humiliating defeat at the upper house election does not help at all.

When Japanese equities rallied in 2005 it coincided with a massive shift in consensus growth expectations. Such circumstances are difficult to repeat given already fair projections for Japanese growth over the coming years. We continue to look for a time to re-enter the Japanese market, but we have not yet found it.

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First date of publication

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