

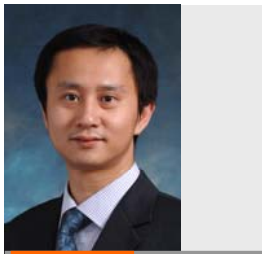
Spotlight

The growth story of China continues to evolve and the themes that are driving it today are different and more complex than those in its earlier years. Here, we present evidence to demonstrate how exposure to the themes driving the country's growth may be accessed through the Greater China region.

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Greater China Equity

Capturing China's growth through the Greater China region



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Michael has 11 years of experience, and since joining ING Investment Management Asia Pacific in 2004, he has been responsible for managing the ING Greater China Fund as well as researching equity markets in Taiwan, Hong Kong and China.

We expect that economic growth in China of 7-8% a year will be sustainable for the next ten years, presenting a powerful argument for long term portfolio positioning. The growth story of China, one of the world's fastest growing economies, continues to evolve. The themes that are driving it today are different and more complex than those in its earlier years, requiring in-depth analysis and an understanding of the various interlinking dynamics. In this article, we present evidence to demonstrate that, instead of investing in China alone, exposure to the themes driving the country's growth is better accessed through the Greater China region. Investing across this region offers diversification, as well as lower volatility when compared with Hong Kong, Taiwan and China markets in isolation. In our view, the argument holds that an active management approach is crucial for long term successful investment in the region.

What are the factors driving China's growth?

China has grown over the past 30 years to become one of the world's leading economies. As a result of this growth, it has become more attractive and accessible to international investors. Already the "world's factory", China is evolving from an emerging export-dominated economy into an advanced consumer-driven economy with a large and prosperous middle class, and is expected to be the third largest consumer market by 2025 (source: Wikinvest). Now the 2nd largest economy in the world, with growing income, spending on discretionary items such as automobiles, life insurance, health care and luxury goods is expected to fuel further growth and investment opportunities.

Whilst there are many themes driving China's growth, we believe there are three which have yet

to be fully appreciated by investors, and we expect these to be played out in the Greater China region in the medium term. These are:

- The internationalization of the Renminbi
- The integration of financial services
- The strength of gold mining in China

Investment theme – The internationalization of the Renminbi

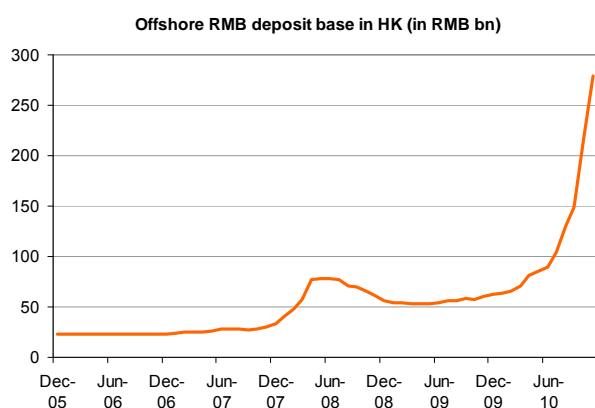
The expansion of the Renminbi (RMB) trade settlement pilot scheme allows banks in Hong Kong to establish RMB accounts for, and provide related services to, financial institutions. Furthermore, individuals and corporations are now allowed to make RMB payments and transfers through banks in Hong Kong without size limits. As a result, more RMB is now being traded outside of China and investors are gaining greater access to invest in offshore RMB assets and products.

In August 2010, China introduced another pilot scheme for RMB clearing banks in Hong Kong and Macau and other eligible institutions outside of China, to invest their RMB funds in China's interbank bond market. Previously, access to China's domestic bond market had been extremely limited due to China's capital account control. This scheme increases investment opportunities for eligible foreign institutions that receive offshore RMB, (otherwise known as CNH*), in their businesses and investments and promotes greater use of CNH, leading to the further internationalization of the RMB.

The policies introduced to date have led to a surge in the offshore RMB deposit base in Hong Kong, especially since August 2010, as shown in Figure 1. The offshore RMB deposit base totalled RMB 280 billion (USD 42.6 billion) as at 30 November, 2010, with the growth still accelerating. This compares with the onshore RMB deposit base of RMB 70 trillion or USD 10.7 trillion. Should the offshore base grow to 10% of the onshore size, we would see a growth of a further 25 times, to RMB 7 trillion (USD 1.1 trillion).

**RMB ("Renminbi") is the official currency of the People's Republic of China. Two separate markets, onshore and offshore, exist for RMB due to China's restrictions on capital flows. CNY refers to onshore RMB within Mainland China, for which outside access is limited. CNH refers to offshore RMB traded predominantly on the Hong Kong interbank market*

Figure 1: The offshore RMB base in Hong Kong has exploded



Source: Bloomberg, as of 30 November 2010

The significant offshore deposit base in RMB clearly accelerates the need for China to develop CNH investment opportunities, including the development of the CNH bond market. The CNH bond market nearly doubled during the second half of 2010, with more than RMB 40 billion (USD 6.1 billion) issued by both corporate and financial issuers (the total is RMB 55 billion or USD 8.4 billion as of November 2010). Since the internationalization of the RMB is being developed first in Hong Kong, we believe that certain major Hong Kong-listed companies will be the main beneficiaries of this liberalization, as CNH investment opportunities continue to grow rapidly in China's offshore markets.

Investment theme – The integration of financial services

Due to the proximity of Hong Kong and Taiwan, their cultural ties and historical factors, these economies are closely interlinked with that of China. The various stages of development of these economies also mean that they complement each other in terms of financial services, such that investors have access to an integrated opportunity set in the Greater China region. Hong Kong and Taiwan's roles as financial services providers for China are expected to continue to expand as China's needs become increasingly sophisticated. The improving relations with China since the change of

government in Taiwan in 2008 have resulted in greater investment opportunities across the Greater China region, as companies in China, Hong Kong and Taiwan take advantage of the unique benefits available to them.

Hong Kong's role is evident in the transformation that the territory has undergone in the past two decades through the rapid expansion in its services sector, including financial services, which currently accounts for around 25% of its GDP. In 2010, Hong Kong was the biggest Initial Public Offering (IPO) market by fund raising in the world, with IPOs estimated at USD 57 billion, an increase of 79% over 2009. This position has mainly developed as the result of China's rapid growth, which is in turn attracting an increasing number of overseas companies choosing to have listings in Hong Kong, a recent example of which is Russian aluminium company, Rusal. We believe that this trend should continue as the Greater China markets broaden and deepen.

To take an example of a sub-theme within financial services, the loan-to-deposit ratio of the banking sector in China is still very low, as evident in Figure 2, despite the strong economic growth in 2009. With the top 20 global banks averaging a loan-to-deposit ratio of 88%, the ratios of China's major banks are much lower, ranging from 55% to 72%, suggesting significant scope for loan growth in the future. Indeed, in the next few years, we expect loan growth of 15-20% a year, as the economy continues on its path towards industrialization.

In addition, unlike their western counterparts, consumer financing, as well as financing for small and medium enterprises (SME), are both still in their infancy development stage in China, implying significant growth in the longer term, as the economy continues to evolve and its main industries move up the value-added ladder. Chinese banks are also relatively unscathed by the global financial crisis, since they have minimal off-balance sheet activities and securitization, thanks to the country's capital controls and the early stage of development within the banking sector.

Figure 2: Chinese banks' loan-to-deposit ratios are significantly below the global average

Name	% Weight	Loan to Deposit Ratio
China Construction Bank Corp	4.06%	60.24%
HSBC Holdings PLC	3.62%	79.53%
JPMorgan Chase & Co	3.41%	74.48%
Ind & Commercial Bank of China	3.24%	58.62%
Wells Fargo & Co	3.18%	89.30%
Bank of America Corp	2.69%	93.07%
Citigroup Inc	2.54%	77.18%
Agricultural Bank of China Ltd	2.24%	55.19%
Banco Santander SA	1.96%	136.70%
Bank of China Ltd	1.84%	72.13%
Global Top 20 Average		87.88%

Source: Bloomberg, as of 2 March 2011

Investment theme – The strength of gold mining in China

India and China are the world's top two gold consumers, with demand growing significantly as these two countries continue to develop. Assuming the top 10% of the populations by income in China and India buy 1/3 ounce of gold each a year, this demand already exceeds the estimated total global gold mining output in 2009. With increasing industrialization and prosperity, we can expect demand to continue to grow in the coming years. China is expected to consume around 527 metric tonnes of gold this year, second only to India, the largest gold consumer in the world.

After overtaking South Africa as the world's top gold producer in 2007, China's gold production hit a record in 2009, at an estimated 300 metric tonnes, rising more than 5% over 2008. Between 2001 and 2009, China's gold production increased by 62%, compared with the global total output, which decreased 9% during this period. China's rapid growth has mainly been the result of the liberalization of the private gold mining industry in 2002, which allowed privately-owned companies to become involved in gold mining.

With technological advances being made in the China gold industry in the past 20 to 30 years and the increased capital expenditure by the private sector since 2002, recovery rates and output have improved significantly and processing technologies have almost reached international standards. We expect this to positively impact the industry as higher profitability will allow further technological breakthroughs. China's share of global gold mining production, at 13% for 2009, is therefore expected to continue to rise. To put this into perspective, based on gold prices of USD 1,200 per ounce, China's 2009 production of 300 tonnes of gold is worth approximately USD 13 billion, which represents 4.4% of the country's current account surplus in 2009 of USD 297 billion.

Figure 3: Gold mining in China

	Gold Mining Output (in metric Tonne)			Volume Growth	
	2009	2008	2001	Since 2008	Since 2001
China	300	285	185	5%	62%
Australia	220	215	285	2%	-23%
US	210	233	335	-10%	-37%
SA	210	213	402	-1%	-48%
Russia	185	176	152	5%	22%
Peru	180	180	138	0%	30%
Canada	100	95	160	5%	-38%
Indonesia	100	60	130	67%	-23%
World Total	2,350	2,260	2,570		

Source: USGS, as of 27 May 2010

Whilst listed gold mining companies are currently concentrated in the developed markets of the US, Canada, Australia, Germany and the UK, the liberalization of China's private gold mining industry, the existence of integrated financial services in the Greater China region, the availability

of more capital in Asia and the mere fact that China is the largest gold producer in the world, is likely to result in more gold mining companies being listed in Greater China. This is already evident in the growing number of gold companies listing in Hong Kong. In addition, the existence of a value-added dimension, that is the manufacture and sale of gold jewellery and gifts, traditions that are firmly entrenched within Chinese (as well as Indian) culture and custom, result in further potential investment opportunities as China's borders continue to open, benefiting the tourism and retail segments in the region.

Greater China for diversification, risk reduction and performance

Turning to global performance comparisons, Figure 4 shows that the Greater China markets significantly outperformed global markets in six of the past ten years. More importantly, the winning year and losing year averages show comparatively small underperformance in "losing years" (average -2.5%) versus the level of outperformance in "winning years" (average 16.1%). We believe that the solid performance is the result of the region's strong fundamentals and a desire on the part of investors to participate in a fast-growing region. Since Greater China is still growing at a rapid pace as China continues its industrialization and liberalization, we expect the outperformance to be maintained in the long term.

Figure 4: Significant outperformance on a global basis

	MSCI World AC (%)	MSCI Golden Dragon Index (%)	Outperf/Underperf of GD Index (%)	Winning Year (%)	Losing Year (%)
2001	-16.2	-10.8	5.4	5.4	
2002	-19.3	-19.8	-0.5		-0.5
2003	34.0	48.4	14.4	14.4	
2004	15.2	14.0	-1.2		-1.2
2005	10.8	9.9	-0.9		-0.9
2006	21.0	39.1	18.1	18.1	
2007	11.7	37.6	25.9	25.9	
2008	-42.2	-49.5	-7.3		-7.3
2009	34.6	66.7	32.1	32.1	
2010	12.7	13.2	0.5	0.5	
Average				16.1	-2.5

Source: MSCI net dividend re-invested Total Return Index in USD

In the past ten years, market performances have generally been strong and the three markets of China, Hong Kong and Taiwan did not tend to move in unison, except when external factors have had an upper hand, such as the extreme financial market stress seen during the global financial crisis in 2008, the impact of the terrorist attacks in the US in 2001 and the accounting scandals and resulting corporate collapses in 2002. It is noteworthy that a change in the Taiwanese government in 2008 resulted in significant

improvement in cross-strait relations, and hence economic prospects for Taiwan. Indeed, since the change in government, Taiwan, which we consider a “hidden jewel”, has outperformed China, as shown in Figure 5, contributing to the solid performance for Greater China strategies.

Figure 5: Not all three markets move in unison

	MSCI Taiwan	MSCI Hong Kong	MSCI China
2001	10.0	-18.6	-24.7
2002	-24.7	-17.8	-14.0
2003	41.9	38.1	87.6
2004	9.0	25.0	1.9
2005	6.4	8.4	19.8
2006	20.0	30.4	82.9
2007	8.4	41.2	66.2
2008	-46.5	-51.2	-50.8
2009	79.2	60.2	62.3
2010	21.8	23.2	4.6

Source: Bloomberg, as of 31 December 2010

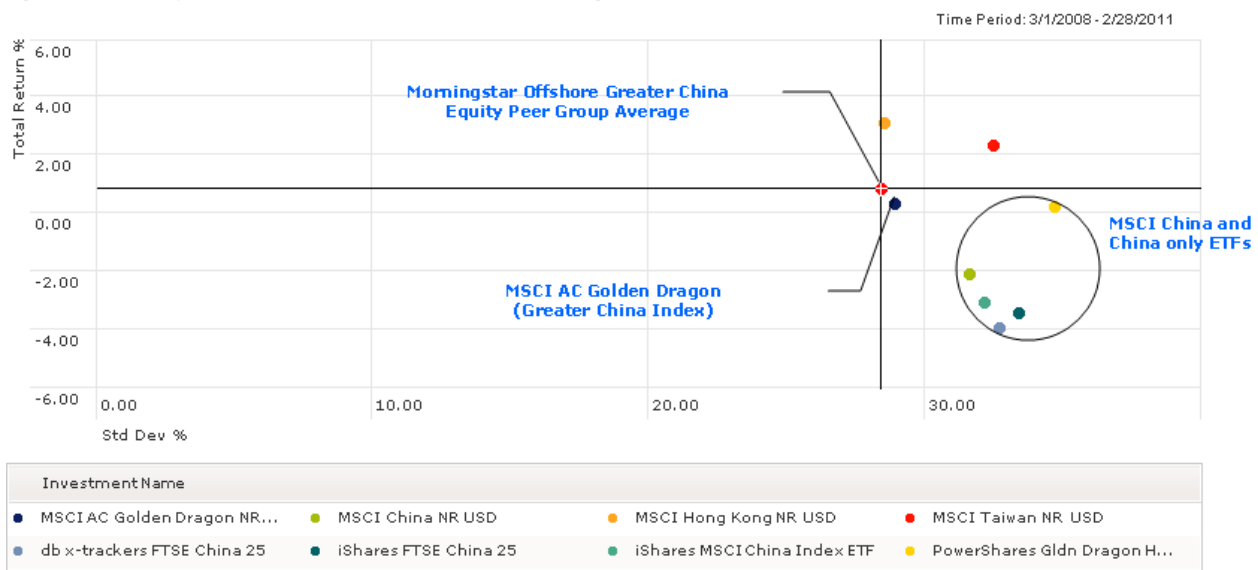
When compared to China-only strategies, strategies investing in Greater China provide greater diversification. This intuitively makes sense as China, Hong Kong and Taiwan are at different stages of market and economic development. The types of companies that each country has to offer can therefore also be very different and are indeed complementary, with Taiwan generally dominant within the integrated and upstream IT and manufacturing sectors, Hong Kong more exposed to regional conglomerates and financials and China providing fast-growing consumer and industrial investments.

As Figure 6 shows, companies with a business location in China are not just listed in China, since red chips and ‘H’ shares are also available. Red chips are shares of mainland Chinese companies incorporated and listed in Hong Kong and subject to Hong Kong law due to their domicile, whilst ‘H’ shares are companies incorporated in China, regulated by Chinese law and listed on the Hong Kong Stock Exchange. With strategies where ‘A’ share exposure is available, either through China’s Qualified Foreign Institutional Investor (QFII) scheme or through participatory notes (P notes), the investment managers of Greater China strategies are often able to benefit from the arbitrage opportunities available between the Hong Kong-listed shares of Chinese companies and their ‘A’ share counterparts.

Figure 6: Greater China funds provide diversification

Securities Class	Business Location	Domicile	Listing	Currency	Greater China Fund
China					
H Shares	China	China	Hong Kong	HKD	✓
Red Chips	China	Hong Kong	Hong Kong	HKD	✓
A Shares	China	China	China	CNY	Potentially
B Shares	China	China	China	USD/HKD	Potentially
Hong Kong	Hong Kong	Hong Kong	Hong Kong	HKD	✓
Taiwan	Taiwan	Taiwan	Taiwan	TWD	✓

Figure 7: The 3-year risk-return profile of the Morningstar Greater China universe is superior to MSCI China and ETFs



Source: Morningstar, as of February 28, 2011

Investment Name	Std Dev %
MSCI AC Golden Dragon NR USD	28.94%
MSCI China NR USD	31.66%
MSCI Hong Kong NR USD	28.56%
MSCI Taiwan NR USD	32.49%
Db x-trackers FTSE China 25	32.71%
iShares FTSE China 25	33.41%
iShares MSCI China Index ETF	32.18%
PowerShares Gldn Dragon Halter USX China	34.71%
Morningstar Offshore Greater China Equity Peer Group Average	24.82%

Source: Morningstar, as of February 28, 2011

Active management for success

We believe active management is crucial in the Greater China region, where the macro and micro environment are constantly evolving. Our goal is to identify attractively priced stocks with above average sustainable earnings growth. We believe that the most effective investment process is characterized by a well-balanced combination of quantitative and qualitative analysis.

Quantitative screening

With a Greater China investment universe of around 3,200 stocks, a quantitative filter must be applied. The filtering process should aim to identify securities with sufficient market capitalization and with adequate daily liquidity where we use above US\$300 million and above US\$3 million a day respectively. These filters provide an investment portfolio with sufficient liquidity.

Fundamental research

The filtered stocks must undergo rigorous fundamental research to identify the stocks that have attractive valuations and growth prospects. Our process entails quantitative and qualitative elements, as well as bottom-up and top-down elements.

Bottom-up analysis – A range of qualitative and quantitative techniques are used to determine the attractiveness of a stock, including regular company visits and analyst meetings, and quantitative information from annual reports and research reports. Factors considered include the business outlook, valuations, financial performance and management quality.

Top-down analysis – Alongside the bottom-up analysis, top-down analysis is performed to capture information relating to macroeconomic factors affecting stock performances. The key variables that we examine are macroeconomic trends, interest rates and corporate spreads, currency outlook, political and regulatory environment, financial liquidity, market earnings revisions and valuations.

Strong on-the-ground presence and proven investment expertise

The investment approach we advocate requires strong on-the-ground presence in the Greater China region, as well as proven investment expertise in this area. We believe these are essential, since a thorough understanding of the dynamics of the economies and companies results in stronger and consistent alpha generation in the long term. These factors must be combined with a stringent and independent risk management framework to ensure that portfolio risk is effectively managed.

Figure 8: ING's Greater China Equity has generated alpha due to its active management style, strong regional presence and proven investment expertise



Source: Morningstar, as of February 28, 2011

What does ING offer in the Greater China equity space?

ING Investment Management has an extensive presence in 11 Asian countries, where we have 260 investment professionals covering the region. Our **ING (L) Invest Greater China Fund** is managed by a team of 5 investment managers with an average of 14 years investment experience. The team is located in Hong Kong and has in-depth knowledge of the Greater China markets due to our strong local presence in the Greater China region. We have a total of more than 40 investment professionals located in our offices in China, Hong Kong and Taiwan.

**ING has entered into an agreement to sell ING IM's Philippine business to the Bank of the Philippine Islands (BPI). We anticipate the sale shall complete in 1H 2011. Until then, ING IM Philippines continues to be part of ING.*

Disclaimer

ING (L) Invest Greater China is a sub-fund under ING (L) Invest, a variable capital investment company established in Luxembourg, and is recognized under Section 287 of the Securities and Futures Act, Chapter 289 of Singapore Act ("Act"). ING (L) Invest is the responsible person as defined under the Act and has appointed ING Investment Management Asia Pacific (Singapore) Ltd as its corporate representative in connection with the offer of Shares in the Fund.

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