

February 18, 2008

Downunder Daily

The Secret of Successful Investing...

I get strong pushback on my cautious view from asset allocators: where else, they ask, can they go, aside from equities? They think Treasury yields are unsustainably low, credit has no appeal, the Fed's rapidly lowering the returns on cash, so equities – despite the jitters – remain the best house on a bad street.

Relative value indicators support that view. The much-watched bond yield-prospective earning yield model says that equities have never ever looked this cheap relative to Treasury bonds. Even allowing for the fact that the centre of gravity seems to move, the equity yield/bond yield ratio is now below the level that has signaled strong equity outperformance over the past few years (Exhibit 1).

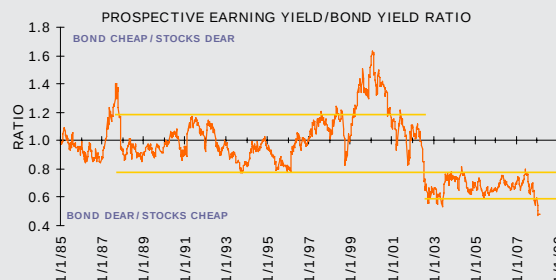
I have two problems with this argument. The first is cyclical: it would be very unusual for equities to bottom this soon in a recession (in the United States, after the print of only a negative payroll number). The bigger problem is that, on most absolute measures, equities look expensive or, at best, not cheap.

Exhibit 2 shows two long-term series of S&P500 price-earnings. One is the conventional trailing 12-month series, the other is the Graham-Dodd PE, which is based on a trailing 10-year average of real earnings. The Graham-Dodd PE is designed to capture price relative to through-the-cycle earnings. Given I think that we're in an earnings bubble – that is, earnings now are well above what's sustainable – this measure better reflects the expensiveness of equities.

Absolute value matters. As I tell my very best clients, the secret of successful investing is this: buy low and sell high. This subtle point is confirmed by Exhibit 3, which shows the historical relationship between the price you pay and the returns you get.

Exhibit 1

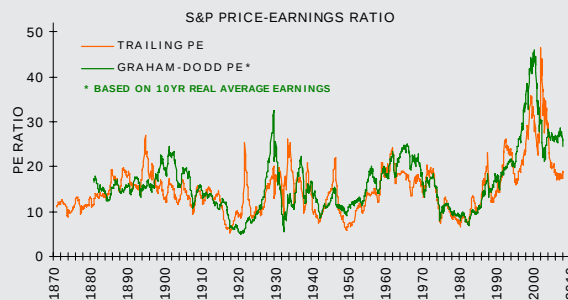
Where Else Would You Be...



Source: DataStream, IBES; Morgan Stanley Research

Exhibit 2

...Although Not Exactly Cheap



Source: Standard & Poor's, BEA; Morgan Stanley Research

Morgan Stanley does and seeks to do business with companies covered in Morgan Stanley Research. As a result, investors should be aware that the firm may have a conflict of interest that could affect the objectivity of Morgan Stanley Research. Investors should consider Morgan Stanley Research as only a single factor in making their investment decision.

For analyst certification and other important disclosures, refer to the Disclosure Section, located at the end of this report.

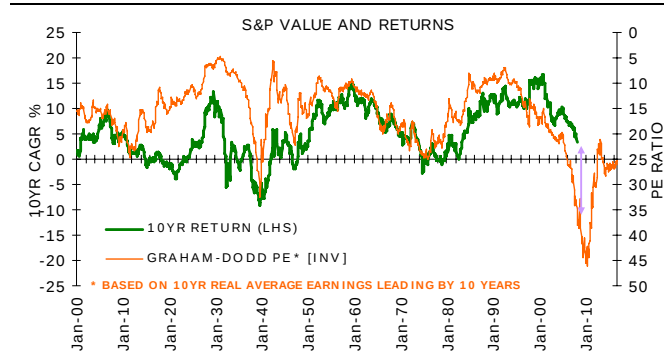
+ = Analysts employed by non-US affiliates are not registered pursuant to NASD/NYSE rules

February 18, 2008
Strategy and Economics

The heavy line is the 10-year return, the thin line is the Graham-Dodd PE, inverted (so the line is low when the PE is high) and pushed forward by 10 years (so the purchase price and the subsequent 10-year return are aligned). There have been three occasions when the Graham-Dodd PE exceeded 25: the early 1930s, the mid-1960s and 2000. Buying at that price in 1930 or 1966 produced negative returns over the following 10 years. We won't know the 10-year return on shares bought in 2000 until 2010, but my hunch is that it will also be negative.

Exhibit 3

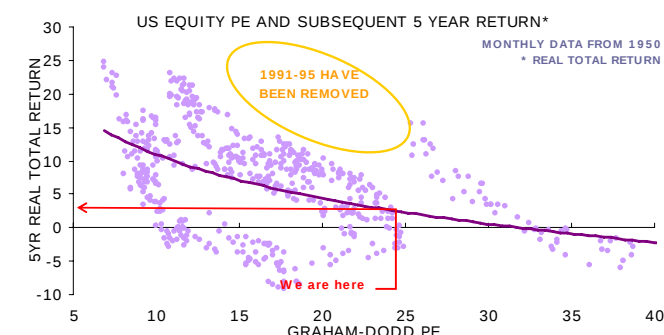
The Secret: Buy Low, Sell High



Wall Street is not offering the same once-in-a-generation opportunity to sell that it did in 1930, 1966 or 2000. But it remains expensive, in my view. Exhibit 4 shows a scatter plot of 10-year returns and purchase price. The average real return (including reinvested dividends) from buying a market as expensive as today's has been around 3%. (Note, I've excluded the TMT bubble from this analysis. If that is included, then the average return is around 4½%.)

Exhibit 4

Not a Promising History



Many investors' equity risk premium – the additional reward required to hold a risky asset (equities) – is assumed to be around 3%. So that implies that a conventional investor would, even at today's levels, be better off on a 10-year horizon in a risk-free asset that returns anything over 0%. For example, a 10-year inflation-protected Treasury bond now offers a risk-free real return of 1.5%. In other words, I think it's attractive – even on a 10-year view – to buy index-linked bonds today, rather than the S&P500. Equities simply aren't yet cheap enough to compensate for the risk, in my view.

Exhibit 5

The Short View: Prospective 2-Year Excess Returns

S&P RETURN VERSUS 2YR TREASURY BOND

		END-PERIOD FORECAST PE					
		11	12	13	14	15	16
2 YEAR EPS GROWTH	-8 %	-17.0	-13.4	-9.8	-6.4	-3.1	0.1
	-6 %	-15.2	-11.5	-7.8	-4.4	-1.0	2.3
	-4 %	-13.4	-9.6	-5.9	-2.3	1.1	4.4
	-2 %	-11.6	-7.7	-3.9	-0.3	3.2	6.6
	0 %	-9.8	-5.8	-1.9	1.8	5.3	8.8
	2 %	-8.0	-3.9	0.0	3.8	7.5	11.0
	4 %	-6.2	-2.0	2.0	5.8	9.6	13.2
	6 %	-4.4	-0.1	3.9	7.9	11.7	15.3
	8 %	-2.6	1.8	5.9	9.9	13.8	17.5
	10 %	-0.8	3.6	7.9	12.0	15.9	19.7
	12 %	1.0	5.5	9.8	14.0	18.0	21.9

Assumes constant pay-out ratio. Dividends/bond coupons not reinvested.
Current prospective PE is 13.4. EPS refers to prospective earnings.
Grey: equities return less than 3% more than a 2yr note (2yr=2.09) S&P500=1355

Source: IBES, Bloomberg; Morgan Stanley Research

Not many investors do 10-year asset allocation any more. How do equities stack up on a shorter time horizon?

The numbers in Exhibit 5 show the potential returns on holding equities over the next two years compared to the apparently skinny 1.9% return on offer from a 2-year Treasury note. Buying a 2-year note and holding it to maturity locks in that return, so the excess equity return depends on only two things: the change in earnings over the period, and the PE at the end of the period. The table provides a range of outcomes based on those two variables.

The grey shading in the table indicates combinations of earnings growth and end-period PEs where the equity return doesn't exceed the return on the 2-year note by more than 3%. That is, where the equity return won't beat the equity risk premium. So, for example, if earning forecasts fall by 2% per year and the end-period PE is 14, equities will return 0.3% per year less than the 2-year note. Not worth it, in my view. Do I think that earnings/PE combination could occur? Absolutely.

Disclosure Section

The information and opinions in Morgan Stanley Research were prepared or are disseminated by Morgan Stanley Asia Limited (which accepts the responsibility for its contents) and/or Morgan Stanley Asia (Singapore) Pte. (Registration number 199206298Z, regulated by the Monetary Authority of Singapore, which accepts the responsibility for its contents), and/or Morgan Stanley Asia (Singapore) Securities Pte Ltd (Registration number 200008434H, regulated by the Monetary Authority of Singapore, which accepts the responsibility for its contents), and/or Morgan Stanley Taiwan Limited and/or Morgan Stanley & Co International plc, Seoul Branch, and/or Morgan Stanley Australia Limited (A.B.N. 67 003 734 576, holder of Australian financial services license No. 233742, which accepts responsibility for its contents), and/or Morgan Stanley India Company Private Limited and their affiliates (collectively, "Morgan Stanley"). For important disclosures, stock price charts and rating histories regarding companies that are the subject of this report, please see the Morgan Stanley Research Disclosure Website at www.morganstanley.com/researchdisclosures, or contact your investment representative or Morgan Stanley Research at 1585 Broadway, (Attention: Equity Research Management), New York, NY, 10036 USA.

Analyst Certification

The following analysts hereby certify that their views about the companies and their securities discussed in this report are accurately expressed and that they have not received and will not receive direct or indirect compensation in exchange for expressing specific recommendations or views in this report: Gerard Minack. Unless otherwise stated, the individuals listed on the cover page of this report are research analysts.

Global Research Conflict Management Policy

Morgan Stanley Research has been published in accordance with our conflict management policy, which is available at www.morganstanley.com/institutional/research/conflict/policies.

Important US Regulatory Disclosures on Subject Companies

The research analysts, strategists, or research associates principally responsible for the preparation of Morgan Stanley Research have received compensation based upon various factors, including quality of research, investor client feedback, stock picking, competitive factors, firm revenues and overall investment banking revenues. Certain disclosures listed above are also for compliance with applicable regulations in non-US jurisdictions.

STOCK RATINGS

Morgan Stanley uses a relative rating system using terms such as Overweight, Equal-weight or Underweight (see definitions below). Morgan Stanley does not assign ratings of Buy, Hold or Sell to the stocks we cover. Overweight, Equal-weight and Underweight are not the equivalent of Buy, Hold and Sell. Investors should carefully read the definitions of all ratings used in Morgan Stanley Research. In addition, since Morgan Stanley Research contains more complete information concerning the analyst's views, investors should carefully read Morgan Stanley Research, in its entirety, and not infer the contents from the rating alone. In any case, ratings (or research) should not be used or relied upon as investment advice. An investor's decision to buy or sell a stock should depend on individual circumstances (such as the investor's existing holdings) and other considerations.

Global Stock Ratings Distribution

(as of January 31, 2008)

For disclosure purposes only (in accordance with NASD and NYSE requirements), we include the category headings of Buy, Hold, and Sell alongside our ratings of Overweight, Equal-weight and Underweight. Morgan Stanley does not assign ratings of Buy, Hold or Sell to the stocks we cover. Overweight, Equal-weight, and Underweight are not the equivalent of buy, hold, and sell but represent recommended relative weightings (see definitions below). To satisfy regulatory requirements, we correspond Overweight, our most positive stock rating, with a buy recommendation; we correspond Equal-weight to hold and Underweight to sell recommendations, respectively.

Stock Rating Category	Coverage Universe		Investment Banking Clients (IBC)		
	Count	% of Total	Count	% of Total IBC	% of Rating Category
Overweight/Buy	1048	44%	333	45%	32%
Equal-weight/Hold	986	41%	308	42%	31%
Underweight/Sell	346	15%	98	13%	28%
Total	2,380		739		

Data include common stock and ADRs currently assigned ratings. An investor's decision to buy or sell a stock should depend on individual circumstances (such as the investor's existing holdings) and other considerations. Investment Banking Clients are companies from whom Morgan Stanley or an affiliate received investment banking compensation in the last 12 months.

Analyst Stock Ratings

Overweight (O or Over) - The stock's total return is expected to exceed the total return of the relevant country MSCI Index, on a risk-adjusted basis over the next 12-18 months.

Equal-weight (E or Equal) - The stock's total return is expected to be in line with the total return of the relevant country MSCI Index, on a risk-adjusted basis over the next 12-18 months.

Underweight (U or Under) - The stock's total return is expected to be below the total return of the relevant country MSCI Index, on a risk-adjusted basis, over the next 12-18 months.

More volatile (V) - We estimate that this stock has more than a 25% chance of a price move (up or down) of more than 25% in a month, based on a quantitative assessment of historical data, or in the analyst's view, it is likely to become materially more volatile over the next 1-12 months compared

with the past three years. Stocks with less than one year of trading history are automatically rated as more volatile (unless otherwise noted). We note that securities that we do not currently consider "more volatile" can still perform in that manner. Unless otherwise specified, the time frame for price targets included in Morgan Stanley Research is 12 to 18 months.

Analyst Industry Views

Attractive (A): The analyst expects the performance of his or her industry coverage universe over the next 12-18 months to be attractive vs. the relevant broad market benchmark, as indicated below.
In-Line (I): The analyst expects the performance of his or her industry coverage universe over the next 12-18 months to be in line with the relevant broad market benchmark, as indicated below.
Cautious (C): The analyst views the performance of his or her industry coverage universe over the next 12-18 months with caution vs. the relevant broad market benchmark, as indicated below.
Benchmarks for each region are as follows: North America - S&P 500; Latin America - relevant MSCI country index or MSCI Latin America Index; Europe - MSCI Europe; Japan - TOPIX; Asia - relevant MSCI country index.

Other Important Disclosures

Morgan Stanley produces a research product called a "Tactical Idea." Views contained in a "Tactical Idea" on a particular stock may be contrary to the recommendations or views expressed in this or other research on the same stock. This may be the result of differing time horizons, methodologies, market events, or other factors. For all research available on a particular stock, please contact your sales representative or go to Client Link at www.morganstanley.com.

For a discussion, if applicable, of the valuation methods used to determine the price targets included in this summary and the risks related to achieving these targets, please refer to the latest relevant published research on these stocks.

Morgan Stanley Research does not provide individually tailored investment advice. Morgan Stanley Research has been prepared without regard to the individual financial circumstances and objectives of persons who receive it. The securities/instruments discussed in Morgan Stanley Research may not be suitable for all investors. Morgan Stanley recommends that investors independently evaluate particular investments and strategies, and encourages investors to seek the advice of a financial adviser. The appropriateness of a particular investment or strategy will depend on an investor's individual circumstances and objectives. The securities, instruments, or strategies discussed in Morgan Stanley Research may not be suitable for all investors, and certain investors may not be eligible to purchase or participate in some or all of them.

Morgan Stanley Research is not an offer to buy or sell or the solicitation of an offer to buy or sell any security/instrument or to participate in any particular trading strategy. The "Important US Regulatory Disclosures on Subject Companies" section in Morgan Stanley Research lists all companies mentioned where Morgan Stanley owns 1% or more of a class of common securities of the companies. For all other companies mentioned in Morgan Stanley Research, Morgan Stanley may have an investment of less than 1% in securities or derivatives of securities of companies and may trade them in ways different from those discussed in Morgan Stanley Research. Employees of Morgan Stanley not involved in the preparation of Morgan Stanley Research may have investments in securities or derivatives of securities of companies mentioned and may trade them in ways different from those discussed in Morgan Stanley Research. Derivatives may be issued by Morgan Stanley or associated persons.

Morgan Stanley and its affiliate companies do business that relates to companies/instruments covered in Morgan Stanley Research, including market making and specialized trading, risk arbitrage and other proprietary trading, fund management, commercial banking, extension of credit, investment services and investment banking. Morgan Stanley sells to and buys from customers the securities/instruments of companies covered in Morgan Stanley Research on a principal basis.

With the exception of information regarding Morgan Stanley, research prepared by Morgan Stanley Research personnel are based on public information. Morgan Stanley makes every effort to use reliable, comprehensive information, but we make no representation that it is accurate or complete. We have no obligation to tell you when opinions or information in Morgan Stanley Research change apart from when we intend to discontinue research coverage of a subject company. Facts and views presented in Morgan Stanley Research have not been reviewed by, and may not reflect information known to, professionals in other Morgan Stanley business areas, including investment banking personnel.

Morgan Stanley Research personnel conduct site visits from time to time but are prohibited from accepting payment or reimbursement by the company of travel expenses for such visits.

The value of and income from your investments may vary because of changes in interest rates or foreign exchange rates, securities prices or market indexes, operational or financial conditions of companies or other factors. There may be time limitations on the exercise of options or other rights in your securities transactions. Past performance is not necessarily a guide to future performance. Estimates of future performance are based on assumptions that may not be realized. Unless otherwise stated, the cover page provides the closing price on the primary exchange for the subject company's securities/instruments.

To our readers in Taiwan: Information on securities/instruments that trade in Taiwan is distributed by Morgan Stanley Taiwan Limited ("MSTL"). Such information is for your reference only. The reader should independently evaluate the investment risks and is solely responsible for their investment decisions. Morgan Stanley Research may not be distributed to the public media or quoted or used by the public media without the express written consent of Morgan Stanley. Information on securities/instruments that do not trade in Taiwan is for informational purposes only and is not to be construed as a recommendation or a solicitation to trade in such securities/instruments. MSTL may not execute transactions for clients in these securities/instruments.

To our readers in Hong Kong: Information is distributed in Hong Kong by and on behalf of, and is attributable to, Morgan Stanley Asia Limited as part of its regulated activities in Hong Kong. If you have any queries concerning Morgan Stanley Research, please contact our Hong Kong sales representatives.

Certain information in Morgan Stanley Research was sourced by employees of the Shanghai Representative Office of Morgan Stanley Asia Limited for the use of Morgan Stanley Asia Limited.

Morgan Stanley Research is disseminated in Japan by Morgan Stanley Japan Securities Co., Ltd.; in Hong Kong by Morgan Stanley Asia Limited (which accepts responsibility for its contents); in Singapore by Morgan Stanley Asia (Singapore) Pte. (Registration number 199206298Z) and/or Morgan Stanley Asia (Singapore) Securities Pte Ltd (Registration number 200008434H), regulated by the Monetary Authority of Singapore, which accepts responsibility for its contents; in Australia by Morgan Stanley Australia Limited A.B.N. 67 003 734 576, holder of Australian financial services licence No. 233742, which accepts responsibility for its contents; in Korea by Morgan Stanley & Co International plc, Seoul Branch; in India by Morgan Stanley India Company Private Limited; in Canada by Morgan Stanley Canada Limited, which has approved of, and has agreed to take responsibility for, the contents of Morgan Stanley Research in Canada; in Germany by Morgan Stanley Bank AG, Frankfurt am Main, regulated by Bundesanstalt fuer Finanzdienstleistungsaufsicht (BaFin); in Spain by Morgan Stanley, S.V., S.A., a Morgan Stanley group company, which is supervised by the Spanish Securities Markets Commission (CNMV) and states that Morgan Stanley Research has been written and distributed in accordance with the rules of conduct applicable to financial research as established under Spanish regulations; in the United States by Morgan Stanley & Co. Incorporated, which accepts responsibility for its contents. Morgan Stanley & Co. International plc, authorized and regulated by Financial Services Authority, disseminates in the UK research that it has prepared, and approves solely for the purposes of section 21 of the Financial Services and Markets Act 2000, research which has been prepared by any of its affiliates. Private U.K. investors should obtain the advice of their Morgan Stanley & Co. International plc representative about the investments concerned. In Australia, Morgan Stanley Research, and any access to it, is intended only for "wholesale clients" within the meaning of the Australian Corporations Act. RMB Morgan Stanley (Proprietary) Limited is a member of the JSE Limited and regulated by the Financial Services Board in South Africa. RMB Morgan Stanley (Proprietary) Limited is a joint venture owned equally by Morgan Stanley International Holdings Inc. and FirstRand Investment Holdings Limited, which is wholly owned by FirstRand Limited.

The information in Morgan Stanley Research is being communicated by Morgan Stanley & Co. International plc (DIFC Branch), regulated by the Dubai Financial Services Authority (the DFSA), and is directed at wholesale customers only, as defined by the DFSA. This research will only be made available to a wholesale customer who we are satisfied meets the regulatory criteria to be a client.

The information in Morgan Stanley Research is being communicated by Morgan Stanley & Co. International plc (QFC Branch), regulated by the Qatar Financial Centre Regulatory Authority (the QFCRA), and is directed at business customers and market counterparties only and is not intended for Retail Customers as defined by the QFCRA.

The trademarks and service marks contained in Morgan Stanley Research are the property of their respective owners. Third-party data providers make no warranties or representations of any kind relating to the accuracy, completeness, or timeliness of the data they provide and shall not have liability for any damages of any kind relating to such data. The Global Industry Classification Standard ("GICS") was developed by and is the exclusive property of MSCI and S&P.

Morgan Stanley has based its projections, opinions, forecasts and trading strategies regarding the MSCI Country Index Series solely on publicly available information. MSCI has not reviewed, approved or endorsed the projections, opinions, forecasts and trading strategies contained herein. Morgan Stanley has no influence on or control over MSCI's index compilation decisions.

Morgan Stanley Research, or any portion hereof may not be reprinted, sold or redistributed without the written consent of Morgan Stanley.

Morgan Stanley Research is disseminated and available primarily electronically, and, in some cases, in printed form.

Additional information on recommended securities/instruments is available on request.

The Americas

1585 Broadway
New York, NY 10036-8293

United States

Tel: +1 (1) 212 761 4000

Europe

25 Cabot Square, Canary Wharf
London E14 4QA

United Kingdom

Tel: +44 (0) 20 7 425 8000

Japan

4-20-3 Ebisu, Shibuya-ku
Tokyo 150-6008

Japan

Tel: +81 (0) 3 5424 5000

Asia/Pacific

Three Exchange Square
Central

Hong Kong

Tel: +852 2848 5200