



Aberdeen

Pan Europe Update

Market Overview

Better-than-expected corporate earnings and supportive economic data lifted European stockmarkets in July. Relief over the European banking sector stress test results, coupled with an easing of the proposed Basel III banking requirements further bolstered sentiment.

Solid growth in Germany offset weakness in Greece and other more indebted peripheral European economies, while the composite Eurozone purchasing managers' index accelerated in July, signalling a better growth outlook. A sharp rise in mortgage lending across the 16-nation bloc in June heralded a rebound in consumer confidence and banks' increased willingness to lend to the private sector. Recent improvements in Germany's labour market also helped keep the region's overall unemployment rate unchanged. German exports jumped by nearly 29% in May, as a weak euro whetted Asian demand, while industrial production rose in France and Italy.

In the UK, preliminary data showed second-quarter GDP growing at its fastest pace in four years, thanks to rebounding services, manufacturing and construction. Warm weather and a boost to spending from the World Cup drove July retail sales sharply higher, while mortgage approvals fell in June, amid tighter lending conditions and weaker confidence. The unemployment rate improved for a fifth straight month in June, but impending public sector job cuts may cloud the prospects for the labour market.

The fragile economic outlook prompted both the European Central Bank and the Bank of England to maintain their accommodative monetary policy stance. In other news, Spain, Ireland and Greece sold almost €10 billion worth of debt, but Hungary raised less than planned. Moody's lowered Portugal's debt rating to A1, citing the country's deteriorating finances and bleak economic prospects.

The worst of the debt crisis appears to be over for the Eurozone: confidence has returned to the region's financial markets; interbank lending has resumed after the results for stress tests on European banks were published, while the costs of insuring against countries defaulting continued to decline. Despite the more upbeat conditions, downside risks, such as economic imbalances and marked differences in competitiveness between northern Eurozone states and their Mediterranean counterparts remain unresolved. Germany's export-led economy is powering ahead, but Greece is languishing in an austerity-induced recession, whereas Spain and Portugal are struggling with subtrend growth. Other headwinds include the possibility of an eventual default (Greece has yet to restructure its debt) and the global unwinding of stimulus measures.

The uncertain economic backdrop notwithstanding, corporate results have surpassed expectations on the back of rigorous cost cuts and improving efficiency. The encouraging performance included many of our holdings and underlines the resilience of the corporate recovery across the continent. Against this backdrop, we are cautious about macroeconomic prospects, but are more optimistic about the quality of the holdings in the portfolio. We believe these companies are likely to fare better in uncertain times than their weaker rivals.

Model Portfolio News (Pan Europe)

Besides taking partial profits in French supermarket operator Casino and Spanish insurer Mapfre, there were no other major changes to the portfolio in July.

Note:

The changes mentioned in this part refer to our model portfolio, which is the basis for actual portfolios we manage that have similar investment objectives. However, there might be minor variations among these, so the above descriptions might not apply to the actual portfolios.

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Corporate News

Basic Resources: **Air Liquide** acquired South Korean gas supplier H-Plus SGS to meet the growing demand in the region, while **Rio Tinto** sold a stake in an iron ore mine in Guinea to Chinese company Chinalco. Dutch company **Fugro** won a US\$100 million contract to provide diving support for Petrobras. Earnings news was generally upbeat. **Fuchs Petrolub's** quarterly results exceeded expectations. **OMV** expects increased output and improved margins. **BHP Billiton** reported continued production growth in key areas but maintained a cautious short-term outlook. **Royal Dutch Shell's** and **Total's** growth were aided by improved margins. **BP's** underlying performance was decent, although the oil spill in the Gulf of Mexico resulted in a significant loss; the energy group will sell US\$7 billion-worth of assets to raise cash. **BG Group's** and **Eni's** output were muted.

Consumer goods: **BMW** raised its sales and earnings forecasts for the year on the back of solid sales in China and demand for the new 5-Series sedan. **AB Foods** said third-quarter revenue was backed up by strong performances across all divisions and was optimistic about its full-year earnings outlook. **Persimmon's** first-half sales rose, accompanied by improved debt and margins.

Consumer services: **Mothercare** revealed that robust international sales growth was outweighed by tougher conditions in the UK. **Pearson** upgraded its full-year forecast after reporting upbeat interim results; it also acquired Wall Street Institute and completed the sale of IDC. A dip in **Halfords'** like-for-like sales highlighted the tough retail environment, although it mitigated the sales shortfall through cost controls.

Financials: Italian bank **Intesa Sanpaolo** sold Cassa di Risparmio della Spezia to French rival Credit Agricole, while **Vienna Insurance** now fully owns Dutch TBIH. In corporate results, Spanish insurer **Mapfre** reported lower net debt and rising premiums in the first half, but its bottom line was hurt by the higher year-on-year comparison. A recovery in business activity, record gross income and an improved risk outlook underpinned Spanish bank **BBVA's** profits over the same period. **Nordea's** second-quarter net profits slipped. **Close Brothers'** trading update showed positive loan growth, stable margins and an improved bad debt ratio. **Intermediate Capital Group's** second-quarter operational performance improved on realised gains.

Industrials: Corporate news flow was heavy amid the earnings season. A UK consortium comprising Onex Corporation and the Canada Pension Plan Investment Board offered to buy **Tomkins**. **Rolls-Royce** won multi-million contracts from several airlines and the Canadian Air Force. Meanwhile, **Meggitt** extended its contract with Bombardier to produce braking systems for its CSeries jetliners, while **Ultra Electronics** will provide radio communications systems to the US military. **Fenner** acquired Arizona-based MRI Medical in a strategic expansion into the medical arena. **Imtech** bought Sapphir to strengthen its position in Austria. The technical services provider also reported signs of a recovery in the maritime sector in the Far East.

June-quarter results were mostly positive. **MAN** benefited from a pick-up in its commercial vehicles unit and solid growth in Latin America. **Schneider's** profits were lifted by better demand and operational efficiency. **XP Power's** revenue was solid and it gained market share. **Robert Walters** reported growth in net fee income. **Rolls Royce's** interim revenues rose despite subdued market conditions. **SIG** said first-half profits will beat forecasts thanks to a rebound in insulation sales. On the flip side, **Kingspan's** revenue and profits were hurt by adverse weather in the first four months.

Pharmaceuticals: **Roche** posted good half-year profits. **GlaxoSmithKline's** underlying results were also strong but profits were dampened by legal costs. **Novartis's** impressive second-quarter earnings were driven by the success of recently launched drugs. **AstraZeneca's** robust second-quarter figures were driven by strong performance in emerging markets and key brands, such as Crestor, Seroquel and Symbicort.

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Real Estate: Strong interim numbers from **Unibail-Rodamco** demonstrated its portfolio's resilience. Separately the property developer received approval to buy Simon-Ivanhoe, which would bolster its position in Poland. Updates from **Great Portland Estates**, **Helical Bar** and **Land Securities** suggested a slowdown in the property market's rebound. **Derwent London** re-entered the commercial property market for the first time in three years with the acquisition of an office and retail building in the West End.

Telecoms: **Vodafone's** first-quarter sales were boosted by the recovery in Germany and the UK, while growth in emerging markets and data revenue remained robust. Conversely, **Ericsson's** second-quarter sales were affected by telecoms operators' spending cuts and supply chain bottlenecks. **Wincor Nixdorf's** sales grew in the third quarter, but lower margin products hurt its profits.

Utilities: Germany's government agreed to extend the operating life of nuclear power plants by more than 10 years. **Centrica's** better-than-expected first-half results were buoyed by a sharp increase in operating profits. The management, though, maintained its profit guidance for the full year in spite of the solid numbers.

We hold the companies highlighted above.

Performance of European Stock Markets[^]

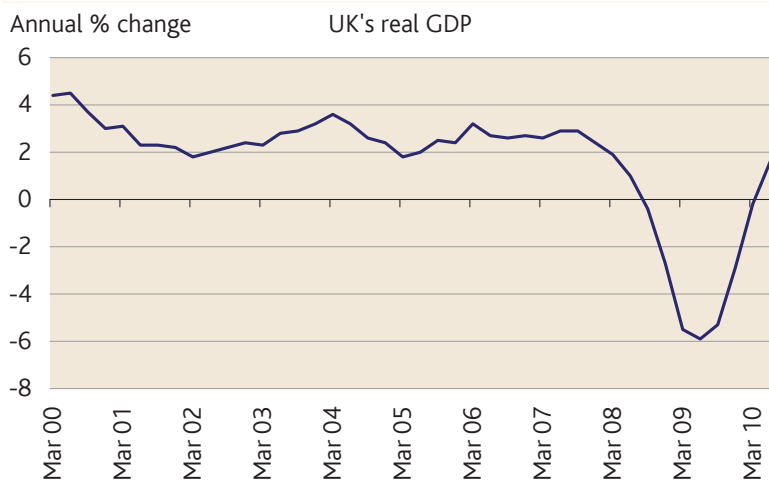
Region/Country	Index/Fund	USD Dollars			Local Currency		
		MOM	3M	YTD	MOM	3M	YTD
UK	FTSE Allshare	12.14%	-1.60%	-2.16%	6.91%	-4.19%	0.66%
UK	FTSE 100	12.33%	-1.83%	-3.41%	7.09%	-4.41%	-0.62%
UK	FTSE 250	11.58%	-0.79%	5.70%	6.37%	-3.41%	8.75%
UK	FTSE Small Cap	8.63%	-2.78%	-0.88%	3.57%	-5.34%	1.98%
UK	FTSE 350 Real Estate	13.42%	-1.64%	-9.31%	8.13%	-4.23%	-6.69%
Europe	FT Europe	11.82%	-2.62%	-6.71%	5.96%	-2.61%	-0.74%
Europe	FT Europe ex UK	11.71%	-2.67%	-7.91%	5.46%	-1.61%	-0.60%
Denmark	Denmark - OMX Copenhagen 20 Index	11.23%	-1.77%	11.97%	4.53%	-0.16%	23.23%
Finland	Finland - OMX Helsinki 25 Index	13.43%	-1.91%	3.81%	6.56%	-0.22%	14.08%
France	France - CAC 40	12.77%	-3.37%	-13.16%	5.93%	-1.71%	-4.62%
Germany	Germany - DAX	9.71%	-1.49%	-6.09%	3.06%	0.20%	3.20%
Ireland	Ireland - ISEQ Overall Index	7.81%	-15.46%	-9.77%	1.27%	-14.01%	-0.90%
Italy	Italy - MIB30	15.52%	-1.65%	-15.16%	8.85%	0.22%	-6.93%
Netherlands	Netherlands - AEX	11.28%	-5.19%	-8.10%	4.53%	-3.56%	0.94%
Norway	Norway - OBX	17.27%	-8.10%	-7.57%	9.45%	-5.87%	-3.42%
Portugal	Portugal - PSI 20	11.07%	0.61%	-17.50%	4.33%	2.34%	-9.39%
Spain	Spain - IBEX	21.46%	0.97%	-17.36%	14.10%	2.70%	-9.18%
Sweden	Sweden- OMX Stockholm 30 Index	12.20%	0.45%	12.39%	4.11%	-0.32%	13.09%
Swiss	Swiss - SMI	4.79%	-2.42%	-3.04%	1.19%	-5.95%	-2.65%
World	MSCI AC World Free	8.17%	-4.98%	-1.68%	5.83%	-5.37%	-0.98%
World	Citigroup World Government Bond	3.64%	4.32%	2.56%	3.64%	4.32%	2.56%

[^] Total indices performance table for the month ended 31 Jul 10

Source: Bloomberg

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Focus: Genuine recovery or dead cat bounce?



Source: Bloomberg, 31 Jul 10

A surprisingly strong burst of momentum in the UK's second-quarter GDP numbers has allayed fears of a double dip recession, but the broad-based pick-up in activity has not altered the fragile economic outlook. With the UK about to enter an almost unprecedented period of fiscal austerity, the pace of recovery could slow in the second half, as extensive cuts in public spending and jobs, both domestically and in continental Europe, begin to bite.

During the month, we met the following companies:

France: Dassault Systemes, Danone, SES Global, Unibail-Rodamco.

Germany: Allianz, BMW, Krones, Linde, MTU Aero Engines, Tognum, Wincor Nixdorf.

Netherlands: Philips Electronics.

Spain: BBVA.

Switzerland: Barry Callebaut, Roche.

UK: Advanced Computer Software, Anite, Aveva Group, Berkeley Group, BP, CareTech, Carnival, Close Brothers, Croda, Development Securities, Fairfield Energy, GlaxoSmithKline, Helical Bar, Inmarsat, Pearson, Provident Financial, PZ Cussons, Rathbone Brothers, National Grid, Nationwide Accident Repair.

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