

Global Emerging Markets Update



Economic and market overview

Emerging market stocks rebounded in July. Upbeat corporate results, optimism over Europe's banking sector stress tests and anticipation that China is nearing the end of its current tightening cycle lifted sentiment.

Economic data remained largely positive, although growth momentum appeared to moderate, which temporarily unsettled markets with fears of a double-dip recession. South Korea's economy performed better than expected in the second quarter, while Russia was supported by rising consumer demand in the same period. However, China's second-quarter GDP growth decelerated, along with the expansion in India and China's monthly industrial output. Nevertheless, the IMF raised its 2010 GDP forecast for developing nations, with the global economy to be buttressed by Brazil, India and China.

Inflation quickened in India and Hong Kong, stabilised in Latin America and was benign elsewhere. Most central banks held interest rates steady, but India and Israel hiked rates. Beijing, meanwhile, will maintain curbs on property speculation, although Shanghai banks resumed lending to third-time homebuyers.

Following a period of exponential credit growth last year, China's banking regulator will inspect loans to local government investment vehicles as about 20% of these appear at risk of default. We share these concerns, but the ultimate parent, the state, has very deep pockets. India will conduct banking sector stress tests every six months, but we do not foresee any great issues. In other developments, Russia plans to sell stakes in state-owned companies and raise taxes in efforts to cut its budget deficit, while Hungary approved a controversial bank tax three times higher than levies proposed in other parts of Europe.

In politics, the new Czech government took office and will seek a vote of confidence in August. Mexico's leading opposition party, the PRI, was the biggest winner in state elections, though not on the scale some had expected. India's opposition protested against the liberalisation of fuel prices. And in further signs that it is strengthening its global influence, China agreed to invest US\$10 billion in Argentina's railways.

Markets have enjoyed a rally on hopes that any relapse in the global recovery can be avoided by further easing in both developed and emerging economies. Certainly, recent data suggest that some emerging economies, particularly those in Asia, could be headed for a slowdown, having experienced impressive growth so far this year. Yet others continue to show robust expansion, with the follow-through effects of rising inflation and interest rate hikes. This policy flexibility and increasingly autonomous nature of the recovery within emerging countries contrast with the prevailing weakness across much of the West, where deep structural problems are still unresolved, deleveraging has been far from meaningful and the preoccupation with imposing austerity may yet prove to be ill timed.

Although we maintain a cautious outlook, we are confident that our holdings, which are characterised by solid balance sheets, experienced management and sound business practices, will be able to meet whatever challenges lie ahead.

Portfolio activity

There were no major portfolio changes during the month.

Corporate news

Brazil: Mall owner **Multiplan** will invest 1.3 billion reais in two existing units and six new projects by 2012; it also has 980 million reais in its warchest for further acquisitions. **Vale** plans to invest US\$7.8 billion to expand the Carajás railway and build a new pier in Port of Ponta da Madeira. Separately, the mining giant managed to end a strike at its Sudbury, Ontario operations by offering workers a new agreement. It also posted healthy second-quarter profits, helped by higher iron ore prices. Earnings news was positive elsewhere too. **Bradesco** reported better-than-expected quarterly results on the back of improving loan and margin growth, as well as asset quality. **Lojas Renner's** net income jumped 90% from the previous year, driven by better sales and a substantial improvement in margins.

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China/Hong Kong: **Swire Pacific** delivered very respectable first-half results. Separately, rejigging within the group ended with Swire owning 75% of HAECO. **Hang Lung Group's** full-year performance was boosted by positive rental reversion and contribution from residential sales in Hong Kong.

India: The results of our holdings generally benefited from stronger domestic demand in the quarter ended June. They included lenders **HDFC**, drugmaker **GlaxoSmithKline India** and **Infosys**. Profits for consumer sector holdings **Hindustan Lever** and **Hero Honda** were pared by rising costs.

Israel: **Teva Pharmaceutical's** second-quarter net profits jumped, thanks to solid sales and the launch of three new generic drugs in the US. The drugmaker strategically split its corporate structure into four geographic units and started up its 20-billion forint packaging plant in Hungary. Growth from **Check Point Software's** new and existing products drove first-half profits higher from a year ago.

Korea: Second-quarter corporate earnings reflected the improved economic backdrop. Recovering domestic consumption aided retail holding **Shinsegae**, which posted double-digit growth for both sales and operating profits. **Samsung Electronics** registered exceptional operating profit growth, driven by buoyant demand for semiconductors. Although it warned of a possible oversupply in DRAM chips in the latter half of 2010, it remains committed to its capital investment programme so that it can preserve its technology leadership. Lender **Busan Bank's** profits exceeded our expectations as its loan book began to grow again.

Malaysia: **Public Bank** posted good interim results, with profits driven by robust growth in net interest and financing income, while asset quality was better than its peers.

Mexico: Moody's cut **Femsa's** local bond rating after the Mexican brewer completed the sale of its beer business to Heineken. The Coca-Cola bottler, however, announced solid second-quarter results. **Asur's** total passenger numbers grew 25.5% in June from a year ago as international traffic improved in Cancun.

Philippines: **Ayala Land** increased the supply of residential units, given the strong demand for high-end homes. Separately, its REIT plan may be postponed because of rumours that the new government may change the existing rules for such instruments. The **Bank of the Philippine Islands'** bottom line was lifted by growth from both net interest and non-interest income.

Russia: **Lukoil** agreed to buy back a 7.6% stake in itself held by ConocoPhillips, with an option to purchase the remaining 11.6%.

South Africa: **Truworths'** trading statement showed a rise in full-year earnings, while **Massmart's** sales improved 10% year-on-year in the year to June, but **City Lodge** indicated a fall in earnings. In other news, Massmart received conditional approval from Namibia's antitrust authority to buy hardware chain M Pupkewitz and Sons.

Taiwan: **TSMC** delivered solid results that exceeded expectations, thanks to higher capacity utilisation, cost cuts and a better product mix that resulted in improved margins. The company also extended its lead with the migration to a significantly more complex 20-nanometre technology that should also drive costs down. **Taiwan Mobile's** performance was less impressive, with second-quarter profitability weighed down by asset write-offs that were brought forward.

Thailand: Our holdings generally reported robust second-quarter results: **Siam Cement** was aided by its paper business and volume growth from its new chemicals complex, while **PTTEP** benefited from increased sales volume and prices.

Turkey: **Akbank** will receive a €75 million loan from the European Investment Bank to support small and medium-sized businesses.

We hold the companies highlighted above.

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Performance of Global Emerging Stock Markets (%)

REGION/COUNTRY	INDEX/FUND	USD DOLLARS			LOCAL CURRENCY		
		MOM	3M	YTD	MOM	3M	YTD
DEVELOPED MARKETS							
US	Dow Jones	7.23	-4.28	1.87	7.23	-4.28	1.87
UK	FTSE Allshare	12.14	-1.60	-2.16	6.91	-4.19	0.66
Europe	FT Europe ex UK	11.71	-2.67	-7.91	5.46	-1.61	-0.60
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
ASIA PACIFIC							
EM Asia	MSCI Emerging Markets Asia	5.71	-2.02	1.69	4.60	0.54	1.52
	MSCI Emerging Markets Asia Small Cap	6.11	-3.25	3.03	5.16	-0.55	2.84
China	MSCI China	4.37	0.03	-1.87	4.08	0.05	-1.73
Hong Kong	MSCI Hong Kong	5.81	2.12	2.07	5.51	2.14	2.22
	MSCI Zhong Hua	4.78	0.62	-0.74	4.49	0.64	-0.60
India	MSCI India	0.73	-3.34	3.25	0.64	1.11	2.96
Indonesia	MSCI Indonesia	6.32	4.66	22.18	4.96	3.90	16.37
Korea	MSCI Korea	7.56	-5.90	3.43	4.14	0.45	5.08
Malaysia	MSCI Malaysia	5.57	1.43	15.40	3.73	1.32	7.21
Pakistan	MSCI Pakistan	9.10	0.16	11.86	9.32	2.18	13.69
Philippines	MSCI Philippines	2.85	0.82	11.50	1.06	3.29	9.86
Sri Lanka	MSCI Sri Lanka	14.64	28.74	36.48	13.86	27.44	34.57
Taiwan	MSCI Taiwan	9.58	-3.07	-4.41	9.28	-0.88	-4.23
Thailand	MSCI Thailand	6.12	7.04	18.17	5.74	6.77	14.40
GLOBAL EMERGING MARKETS							
Global Emerging Markets	MSCI Emerging Markets	8.40	-1.80	1.85	6.24	0.24	1.80
	MSCI Emerging Markets Small Cap	7.27	-2.52	5.03	5.41	-0.30	5.00
EMERGING MARKETS EUROPE MIDDLE EAST AFRICA							
EMEA	MSCI EMEA	12.79	-2.16	3.94	7.91	-1.06	4.31
	MSCI EMEA Small Cap	11.49	-3.48	10.21	5.99	-3.09	10.56
Czech Republic	MSCI Czech Republic	13.72	-2.35	-1.29	3.20	-3.47	2.05
Egypt	MSCI Egypt	5.33	-16.30	2.06	5.42	-14.32	5.79
Hungary	MSCI Hungary	13.42	-21.15	-10.89	6.30	-14.59	3.19
Morocco	MSCI Morocco	5.81	-3.08	8.32	0.52	-1.35	17.20
Poland	MSCI Poland	19.71	-5.53	-2.14	8.89	-1.50	5.05
Russia	MSCI Russia	11.41	-5.05	0.68	8.64	-2.04	0.82
South Africa	MSCI South Africa	12.59	0.66	6.52	7.27	-0.09	5.65
Turkey	MSCI Turkey	15.98	3.53	15.75	10.36	5.04	16.33
MIDDLE EAST							
Bahrain	Bahrain All Share Index ^A	-0.17	-12.44	-4.41	-0.17	-12.44	-4.41
Kuwait	Kuwait Stock Exchange Index ^A	3.12	-8.32	-5.07	1.71	-8.83	-5.00
	MSCI Kuwait	9.42	-1.00	15.92	7.96	-1.36	16.16
Oman	Muscat Securities Market Index ^A	3.90	-7.84	-1.17	3.90	-7.84	-1.17
Qatar	Doha Securities Market Index ^A	1.93	-6.84	1.06	1.88	-6.86	1.01
	MSCI Qatar	1.86	-6.46	7.55	1.80	-6.52	7.49
Saudi	Tadawul All Share Index ^A	3.12	-8.51	2.66	3.12	-8.51	2.65
UAE - Abu Dhabi	Abu Dhabi Securities Market ^A	1.26	-8.33	-7.21	1.26	-8.33	-7.21
UAE - Dubai	Dubai Financial Market General Index ^A	3.46	-13.08	-16.15	3.46	-13.07	-16.14
	MSCI UAE	5.78	-14.33	-10.84	5.78	-14.33	-10.85
Israel	MSCI Israel	-1.02	-12.98	-11.10	-3.60	-11.70	-11.38
Jordan	MSCI Jordan	-2.29	-9.16	-11.14	-2.36	-9.26	-11.14
LATIN AMERICA							
Latin America	MSCI Latin America	11.92	-1.11	0.20	9.18	0.49	0.18

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REGION/COUNTRY	INDEX/FUND	USD DOLLARS			LOCAL CURRENCY		
		MOM	3M	YTD	MOM	3M	YTD
	MSCI Latin America Small Cap	9.07	3.40	8.55	6.25	5.18	8.61
Argentina	MSCI Argentina	15.90	8.66	15.05	15.90	8.66	15.05
Brazil	MSCI Brazil	13.73	-2.70	-3.65	11.01	-1.10	-2.76
Chile	MSCI Chile	12.07	11.21	15.64	6.74	12.36	18.96
Colombia	MSCI Colombia	13.24	16.59	29.45	8.84	10.10	16.76
Mexico	MSCI Mexico	5.84	-3.85	3.84	3.82	-0.78	0.52
Peru	MSCI Peru	8.00	11.30	13.22	8.00	11.30	13.22
FRONTIER MARKETS							
	MSCI Frontier Markets	5.89	-4.42	6.58	4.85	-4.23	7.87
Botswana	MSCI Botswana	6.84	-1.28	3.13	3.16	-0.87	5.67
Bulgaria	MSCI Bulgaria	8.67	-11.63	-17.89	2.22	-9.80	-9.55
Croatia	MSCI Croatia	4.81	-8.69	-4.65	-0.82	-7.06	4.16
Estonia	MSCI Estonia	10.76	-14.80	27.14	4.13	-13.04	40.02
Ghana	MSCI Ghana	-3.85	-3.38	32.63	-4.04	-1.78	33.37
Jamaica	MSCI Jamaica	3.37	-0.97	20.62	3.95	-4.13	16.18
Kazakhstan	MSCI Kazakhstan	4.44	-18.12	-20.00	4.44	-18.12	-20.00
Kenya	MSCI Kenya	3.21	3.02	24.49	1.33	7.03	31.54
Lebanon	MSCI Lebanon	-2.32	-5.72	-4.40	-2.32	-5.72	-4.40
Lithuania	MSCI Lithuania	5.84	-3.41	7.05	-0.49	-1.42	17.90
Mauritius	MSCI Mauritius	8.07	1.14	-3.44	2.48	-0.59	-3.76
Nigeria	MSCI Nigeria	3.04	-2.89	25.19	3.30	-3.39	25.76
Romania	MSCI Romania	15.04	-15.71	-5.00	5.28	-11.46	5.01
Serbia	MSCI Serbia	9.48	-21.55	-7.69	4.72	-14.22	12.67
Slovenia	MSCI Slovenia	2.75	-10.50	-15.18	-3.39	-8.65	-6.59
Tunisia	MSCI Tunisia	11.54	8.40	10.30	7.30	10.88	21.91
Ukraine	MSCI Ukraine	6.47	-17.36	34.21	6.30	-17.67	32.25

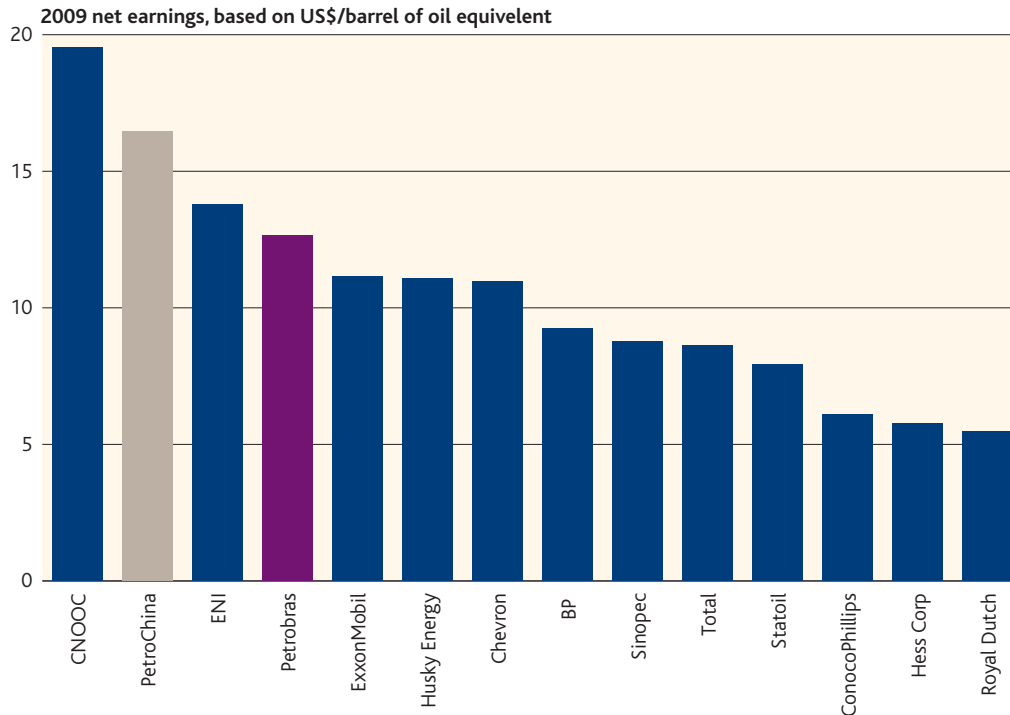
As at 31 July 2010.

All performance are measured using total return except for those marked ^.

Source: Bloomberg

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Focus – Petrobras and PetroChina: satisfying long-term global energy demand



Source: BMO Capital Markets, Company reports, June 2010

Petrobras and PetroChina surpassed most of their global peers in net earnings in 2009. More recently, both reported upbeat second-quarter results. The competitive edge for resource companies lies in stable production that can meet growing demand. Petrobras has no problems with future reserves, having found opportunities within Brazil's under-developed territorial waters, unlike other oil companies with mature assets. A strong cash position has allowed PetroChina to buy various assets overseas; the company plans to spend another US\$60 billion in the next decade on further acquisitions.

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During the month, we met with the following companies:

Brazil: American Banknote, AMIL, BM&FBovespa, Bradesco, BRF Brasil Foods, CETIP, Cielo, Grupo Pao de Acucar, Iguatemi, Itau Unibanco, Localiza, Lojas Renner, Multiplan, Sabesp, Totvs, Ultrapar, Wilson Sons.

Chile: Embonor.

China/Hong Kong: Agricultural Bank of China, Café de Coral.

India: Bharti Airtel, Bosch, MakeMyTrip, Mphasis, Reliance Industries, SKS, Tata Power.

Indonesia: Petra Foods.

Israel: First International Bank of Israel.

Kazakhstan: KazMunaiGas.

Korea: LG Household & Health Care, Samsung Electronics.

Malaysia: Aeon Co, Carlsberg Malaysia, Guinness Anchor, Lafarge Malayan Cement, Nestle Malaysia, Panasonic Manufacturing, QSR Brands, SP Setia.

Mexico: Banorte.

Pakistan: BOC Pakistan.

Philippines: Asian Terminals, Ayala Land, Bank of the Philippine Islands, Philippine Long Distance Telephone.

Poland: Eurocash.

Romania: BRD.

Russia: TransContainer.

South Africa: MTN.

Sri Lanka: Aitken Spence, National Development Bank.

Taiwan: Acer, Cathay Financial Holdings, China Life Insurance, Chroma Ate, Chunghwa Telecom, Fubon Financial, Hon Hai Precision, President Chain Store, Taiwan FamilyMart, Taiwan Mobile, Uni-President Enterprises.

Tanzania: African Barrick Gold.

Thailand: Bangkok Bank.

Turkey: Anadolu Efes.

UAE: Aramex, Dubai Financial Markets, First Gulf Bank, Sorouh.

Vietnam: BaoViet, Kinh Do Corp, Saigon Securities, Tan Tao Investment Industry, Vinamilk.

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For more information

Client Services

Tel: +65 6395 2701

Fax: +65 6438 0743

Aberdeen Asset Management Asia Limited

21 Church Street

#01-01 Capital Square Two

Singapore 049480

Tel: +65 6395 2700

Fax: +65 6535 7159

www.aberdeen-asia.com

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