

## Taking a look at smaller companies and markets

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**06.10.2009**

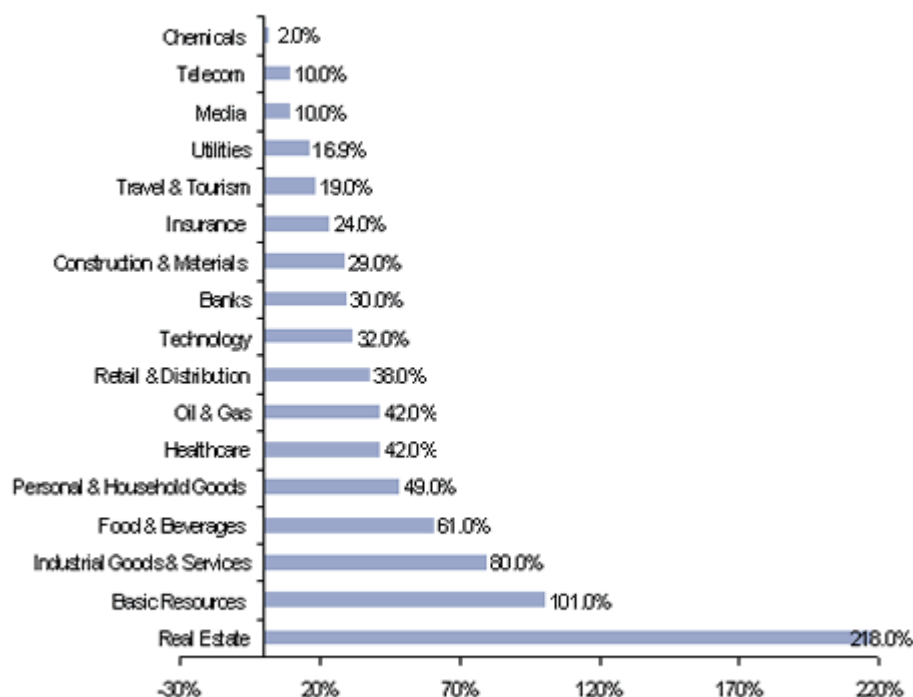
- 'Risk was King' – leveraged or cyclical sectors, and emerging or risky markets are winners so far in 1-3Q09; outperformers of 2008 (utilities, telecoms) are clear underperformers
- Two steps ahead, one step back– rather cautiously optimistic markets in the coming quarter, facing short-term weaknesses from time to time
- Investors to keep an eye on markets and sectors that have been lagging behind the recent performance (SEE and Austria - insurance and financials)

Hard data coming in from the real economy has already provided the first indications that, although the situation is not bright, it is not as bad as previously expected. Erste Group analysts see a movement in the real economy similar to that seen in the financial markets, where panic has created a highly oversold situation. For equity markets, they would also expect a period of stabilization, after markets finish being driven by the correction of the overdone risk aversion and a first wave of improving views on fundamentals.

Throughout 2Q09 and 3Q09, 'Risk was King'. The more leveraged and cyclical, and the more emerging and risky the regional market, the better. Real estate was far and away the best performing sector in Erste Group's CEE universe, gaining 218.0%. Basic resources and industrial goods and services, delivering 101.0% and 80.0%, respectively, followed suit. The outperformers of 2008, such as utilities and telecoms, are clear underperformers so far.

On a regional basis, Emerging Latin America (+75.9%) and Emerging Europe (+67.4%) have been the hottest equity markets so far this year. Admittedly, Russia and Turkey have clearly played a vital part in this strong comeback of Emerging Europe, however, the CEE region (represented in NTX), having gained 34.1% YTD, also managed to outperform established Western equity markets.

## CEE sector performances 1-3Q09



Source: *Factset, Erste Group Calculations*

### Outlook

For the coming quarter, we expect rather cautiously optimistic markets, facing short-term weaknesses from time to time – two steps ahead, one step back. Generally, it might be worth taking a look at smaller companies and markets, which could “fall victim” to still growing flows into equity markets, says Henning Esskuchen, Co-Head of CEE Equity Research and author of the report.

Erste Group analysts say a continued decline in risk aversion - as expressed in further declining discount rates - should help sectors and companies that are still far below their previous price levels. A second factor would be evidence of further improvements in corporate fundamentals. In this regard, and in terms of earning revisions, EPS consensus and EPS growth, cyclicals and financials seem to be the favorites with strong recovery trends setting in strongly rather in 2011.

### Country allocation

#### Potential upside based on a simplified valuation by country

Index	# of ratings*	# of reasonable results**	Percentage
BET (Romania)	30	8	58%
ATX (Austria)	234	20	40%
CROBEX (Croatia)	17	8	25%
ISE 30 (Turkey)	303	23	24%
RTS (Russia)	479	43	24%
WIG 20 (Poland)	201	20	16%
PK (Czech Republic)	142	13	12%
SBI (Slovenia)	20	4	9%
BUX (Hungary)	74	7	3%

\* number of analysts providing consensus data

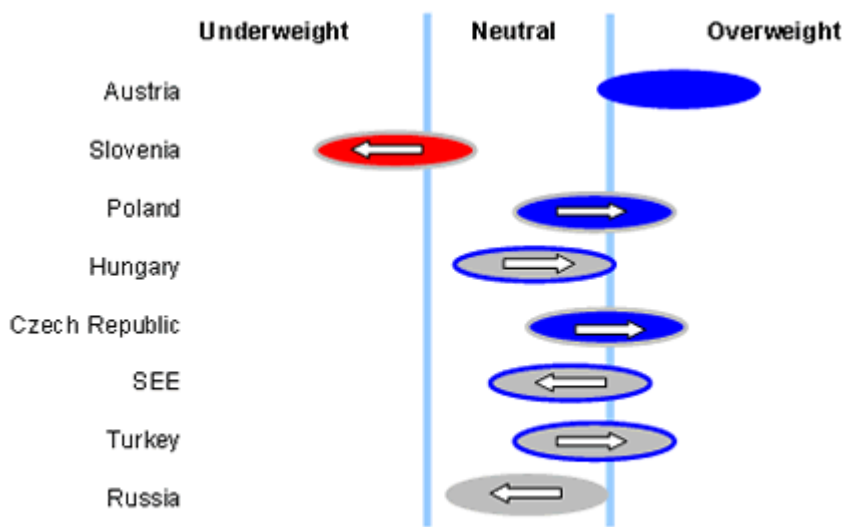
\*\* number of reasonable results based on available consensus estimates

Source: Factset, own calculations

- Romania is facing some economic difficulties and we do not expect it to be among the first to recover quickly. However, the country was hammered in the previous wave of risk aversion and was left at an extremely depressed level, with very thin volumes traded. With improving views on a stabilization/recovery of the global economy, Romanian companies should finally find their place in a better world again.

- Austria, in the middle of any development within CEE, also presents an appealing case. While cyclicals have already used up most of their upside potential, financials (including insurance and defensive stocks) contribute to the indicated theoretical performance.
- Croatia might offer a case similar to Romania's, but it seems that flows ventured back into that market a bit earlier compared to Romania. Also, the solution to the deadlock over its EU negotiations should have already driven some positive market development.
- Russia and Turkey have been quite prominent targets, once emerging markets in Europe started to lose their pariah status. However, there is still interesting potential left, paired with decent investable size.
- Poland and the Czech Republic have also been classic targets since the recovery in CEE. Hence, only moderate upside is left. Similarly to Austria, cyclicals took over defensives and financials too quickly, leaving more upside for the latter. Also, real estate contributes to the positive part of the outlook.
- Hungary - as one of the markets in the region that indeed was just saved by an international bailout - recovered rapidly; consequently, not much upside is left here until fundamentals improve significantly.

### Country allocation proposal



### Sector allocation

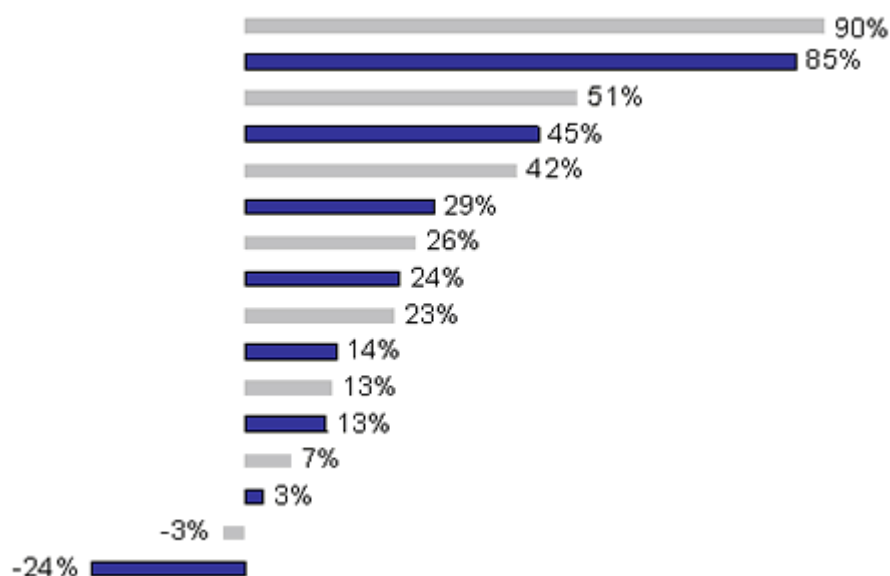
Potential upside based on a simplified valuation by sector

Index	# of ratings*	# of reasonable results**
Technology	29	8
Insurance	14	2
Real Estate	38	8
Retail	27	6
Banks	136	12
Oil & Gas	75	7
Personal & Household Goods	16	4
Construction & Materials	55	9
Healthcare	52	9
Food & Beverages	17	6
Industrial Goods & Services	63	12
Telecom	67	6
Utilities	48	5
Travel	20	4
Chemicals	21	5
Basic Resources	57	5

\* number of analysts providing consensus data

\*\* number of reasonable results based on available consensus estimates

Source: Factset, own calculations



Technology had the strongest outcome. However, Erste Group analysts point to a question mark regarding the upside potential of permanent restructuring candidates such as Sygnity. Their positive view on Asseco Poland, however, was nicely confirmed.

As previously mentioned, financials and real estate have a strong showing. Banks and insurance companies still have quite some recovery potential, having been the most prominent victims of the crisis in the region and elsewhere. Erste Group analysts have to stress the still imminent risks within the sector, but any indication that companies are managing to get closer to earnings again should be seen as a trigger. The rather weak performance outlook for industrials, chemicals and basic resources confirms our suspicion that these sectors were too much in favor once the euphoria of economic stabilization/recovery started.

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