

Equity Reloaded

Pioneer Funds – Global Trends
28 April 2009



Global Equity

Background

The severe risk aversion and panic in global equity markets since the collapse of Lehman Brothers last September has led to price dislocations in many stocks that have been sold down below their intrinsic value. The biggest dislocations have been in companies where there has been a real or perceived risk of needing additional capital. Markets have been capital constrained and this lack of availability has meant that investors have generally avoided businesses that need to raise new funding or refinance/renege existing credit lines. This has also been indiscriminate between good and bad companies as investors were not prepared to take any kind of risk associated with financing.

Global Trends – New Investment Ideas

Our strategy is to seek out themes that we believe will be influential in the economy of today and tomorrow. We have an unconstrained approach to stock selection, only backing companies where we have a high conviction in the business case. The number and type of themes within the Portfolio changes and often our holdings could be categorised under more than one area.

A key recent development in the first quarter, which we decisively acted on in March, was our backing of a new theme we call 'Recovery'. This is a focus on companies with decent business models where financing for the next three years or so is already secure.

We were still relatively defensively positioned in January and February, with around 10% in cash and 15% in gold. In March, we reduced cash to zero and gold to 5%, adding circa 20 new Recovery names to the Portfolio.

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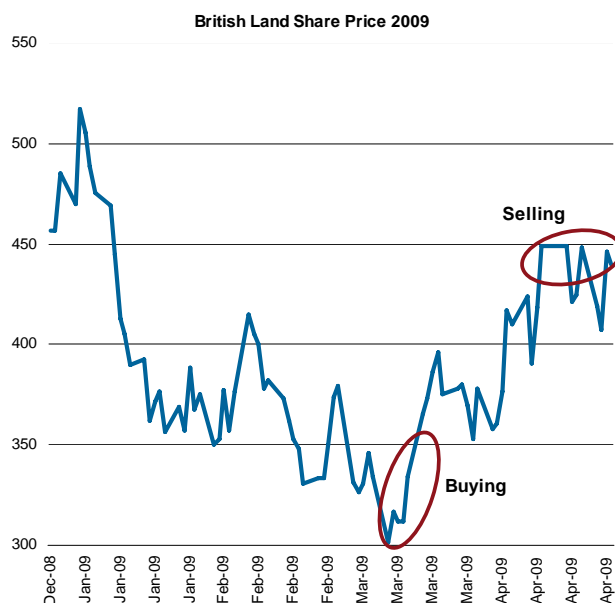
Following on from the Recovery theme, we have spotted an opportunity in companies that are out of favour due to financial concerns, but where a recapitalisation or new financing agreement, should alleviate any worries. With this complication out of the way, investors will be able to focus attention on the quality of the business and the attractive valuation. Therefore, these are companies that, once the focus turns from the financing issue, could also be classified under our 'Recovery' theme.

The key factor behind this new theme is that the financial concerns of investing in a company dissipate. Stocks can rally even before any improvement in fundamentals at the operating level, simply because of a reduction in risk premia.

Taking the UK as an example, it looks likely that the total raised in new rights issues this year, excluding any government bailouts, could be as much as 10% of market capitalisation. Similar figures are likely to be required in Europe and the US. It could be higher than this depending on what happens to the life insurers. We are currently tracking several opportunities in this area and have already purchased positions in British Land, Lafarge and Wolseley during the rights-issue process.

Indeed, our investment in British Land was so successful that we have already significantly reduced our holding after a 50% rally in just over one month since our initial investment.

In December, British Land's NAV included circa £9.5bn of property and £4.5bn net debt, giving an unencumbered property value of around £5bn. At the end of February, its market capitalisation was down to just £1.5bn. British Land had a rights issue raising about 40% new capital, which brought down its cost of capital, the risk premium dropped and its market cap increased to around £4bn.



Source: Bloomberg, 31 December 2008 – 23 April 2009

It is interesting to note that the impetus for the recent Portfolio changes in Recovery and Equity Reloaded themes came about following an extensive research trip, where Neil Robson, Head of Global and European Equities met with the management of many companies. This also coincided with the trough in markets and a time of maximum fear for investors. It proved to be a rewarding time to back our conviction that markets had simply gone too far in indiscriminately punishing quality businesses.

Outlook

After such a big change in the Portfolio and the fact that markets have had such a strong run since early March, we will be monitoring positions and opportunities carefully. Markets can change very quickly, but we expect that opportunities in the Equity Reloaded and Recovery themes will be around for quite a while. One of the hard things to judge in this volatile environment is how far markets will go.

At the start of March, the only direction that investors could see was down. Markets were pricing in an extreme equity risk premiums. We have now possibly moved to the next phase of the cycle. Valuations are less extreme, especially in some areas, and many investors are rebalancing their portfolios and taking on extra risk for fear of being left behind. The danger is that certain areas will shoot beyond their fundamentals due to short covering and herd mentality – witness some of the huge rallies in financial stocks that have doubled or even trebled in six weeks.

Hopefully, the economic slowdown is easing, but this change could be protracted and last throughout this year, maybe into

2010. Riskier assets have outperformed since March and especially in April, when lower quality and higher-beta stocks have rallied significantly. We may have turned the corner at least from a psychological point of view, but it is likely to be a rough ride in the year ahead. However, we firmly believe that quality, market-leading businesses could outperform from here for a prolonged period.

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