Quarterly Portfolio Update

Pioneer Funds – Euro Corporate Bond
31 December 2009

Bond

Review

During the fourth quarter, corporate bonds continued to perform strongly, keeping ahead of government bonds. This positive performance can be attributed to a combination of ample liquidity, low interest rates, as well as signs of economic stabilisation, which created a beneficial environment for riskier assets.

The most recent surveys on bank lending show that credit conditions remain tight. While the banks have increased lending to large businesses, the supply of secured credit to households and small/medium companies is still decreasing. This data is positive for investment grade corporate bond spreads in the short term, as it demonstrates that credit is still available to much of our investible universe.

Furthermore, the improvement in credit conditions will allow investors and rating agencies to improve their forecasts for default rates. Default rates are now expected to come back to their long-term average as early as next year.

In broader terms however, this is less positive for the expected economic recovery as consumers have no access to credit and are therefore forced to de-lever, keeping private spending under pressure for the foreseeable future. This will also have a negative impact on the expected recovery of employment rates as small/medium companies are a significant driver of employment.

Portfolio Strategy and Outlook

Pioneer Funds – Euro Corporate Bond (Class A, non-distributing, EUR units) performed in line with its benchmark* during the quarter. A key contribution to performance came from our positioning in subordinated financial debt.

In terms of Portfolio strategy, although we retain our overweight exposure to subordinated financial debt, particularly to lower tier 2, we have scaled back the extent of this overweight as risk-adjusted returns now appear less attractive. We expect that credit quality will continue to improve for Financials; however, we think that there is still the possibility of negative surprises as some banks will face ongoing challenges this year.

In 2010 we believe that the focus will move towards name selection as the key driver of performance, in all sectors, and we are taking advantage of the primary market in order to gain exposure to good-quality names at a relatively cheap level. With the latest supply of new issues we moved from underweight to neutral in terms of spread duration (as rates are starting to rise along the curve) and we increased our exposure in Industrials and Utilities. We also continue to monitor the secondary market to find opportunities for switches that will improve the Portfolio's risk/return profile.

Within the Portfolio there are some bonds, which are still trading at lower valuations; we expect that as economic conditions improve and these values will have the opportunity to return to more normal levels, thus generating extraperformance.

Going into 2010 the market has already priced-in an increase in interest rates in the second quarter. In our opinion, this risk is quite modest for the first half of the year as the European Central Bank and the Federal Reserve are unlikely to change their monetary policy until there are signs of a sustained improvement in the labour market.

Finally, the strong returns seen on investment grade corporate bonds last year are unlikely to be repeated over the course of 2010 as yields are almost back to pre-recession levels and spreads are now near "fair value". A further significant compression of spreads is difficult to see from current levels and we believe that investment grade corporate bonds are going to be more of a 'carry' than a 'capital appreciation' story going forward.

* Benchmark is Merrill Lynch EMU Corporate Bonds Large Cap Index 95%, JPM Cash 1 Month Euro 5%.

Important Information