

Quarterly Portfolio Update

Pioneer Funds – European Potential

31 December 2009

Equity

Pioneer Funds – European Potential improved performance over the fourth quarter of the year and posted benchmark-comparable returns. The Portfolio returned 2.5% (Class A, non-distributing, EUR units), while its benchmark, the MSCI Europe Small Cap Index, returned 2% over the same period. Over 2009 as a whole the Portfolio lagged its benchmark but still posted positive returns in absolute terms of 28.7%.

At macroeconomic level, after falling back in October, European equity markets had a strong start to November until mid-month when the market retracted and finished slightly up. This volatile side-way pattern has continued from the start of October. The decline in share prices mid-month was partly driven by renewed fear on the back of sovereign debt risk in Greece and Dubai World. Economic data was mixed, manufacturing indicators show signs of topping out and unemployment is still rising. Markets have been driven by the good results season and a reduction in risk aversion.

Over the month of December concerns about Greece's economy continued as rating agencies put the country on negative credit watch. Fitch credit rating agency cut Greece's rating to a 10-year low, which saw Greek shares slump as a result. Additionally, the ratings agency Standard & Poor's cut Spain's credit outlook from stable to negative. Although this news shook European markets, they recovered later in the month and ended the year with the biggest annual gain since 1999, as confidence grew that the economy is recovering from recession.

Our relative outperformance over the fourth quarter of the year is primarily attributable to successful stock selection decisions, which accounted for over 150 basis points of positive contribution.

At sector level, stock selection within the Financials sector was the greatest contributor to relative performance over the period. Avoiding laggard names held in the benchmark, in addition to underweighting our exposure to the sector as a whole, accounted for almost 100 basis points of outperformance over the quarter. Within the Insurance industry in particular, our position in Sweden-based Storebrand rewarded after reporting very strong third-quarter results.

Elsewhere, our investments within Materials were also a significant contributor to relative performance. Vedanta Resources, a company which mines and processes metals, rewarded over the quarter after reporting results that were in line with expectations. We believe that the company is well positioned with an impressive pipeline of organic growth projects and that share prices should remain strong as they continue production of their new projects and as commodity prices recover.

Finally, in terms of key positive contributors, our investments within Industrials, particularly Capital Goods, proved beneficial over the quarter, with names such as Cardo (Sweden-based international engineering group) and Centrotherm Photovoltaics (a company which manufactures equipment used to produce solar cells) generating outperformance.

On the negative side, unsuccessful stock selection within Consumer Discretionary and Energy detracted and held back some relative performance over the period.

With regards to outlook, we acknowledge a recovery in economic data and believe that continued government stimulus packages and monetary policy should sustain economic recovery in the short term. However, we remain cautious and acknowledge growth will remain nominal due to the many external drivers of the recovery, such as stimulus packages. Valuation levels are at broadly fair value so we continue to favour stocks with strong balance sheets and cash generation. Additionally, the low interest rate environment should be beneficial for equities.

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