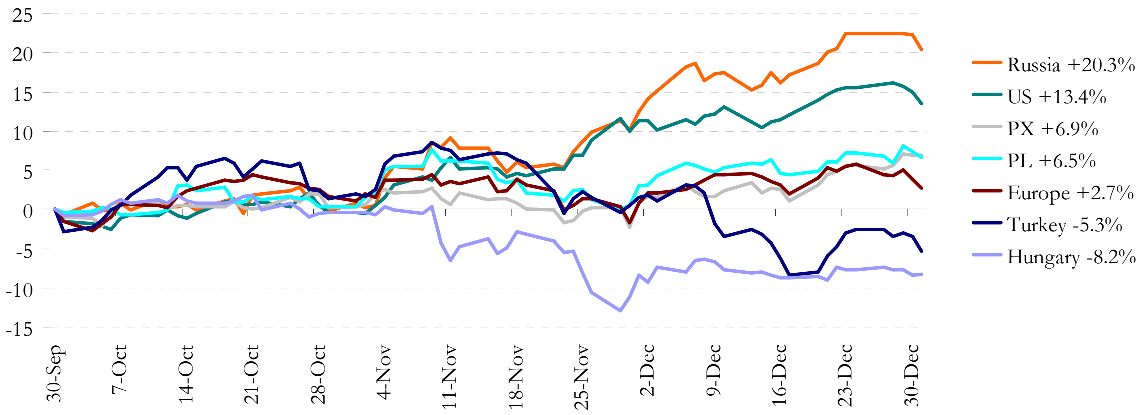
Outlook – January 2011

Equity and bond market outlook

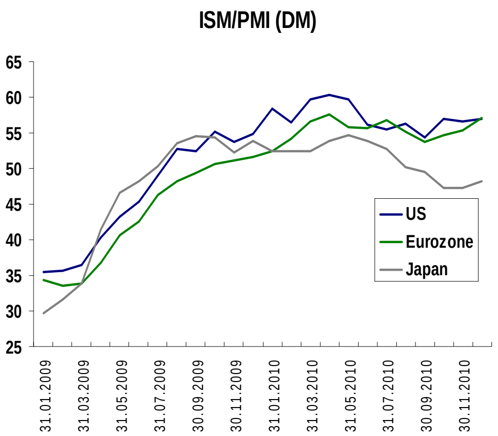
In the fourth quarter, the majority of the share markets continued on their upward trend. The MSCI World Index strengthened by 9% in dollar terms (11.7% in forint terms), with this good result primarily down to the low valuation levels, the high degree of liquidity, and a resurgence of M&A activity. Although fears of a slowing in Chinese growth triggered a negative market correction in November, this decline proved to be short-lived.

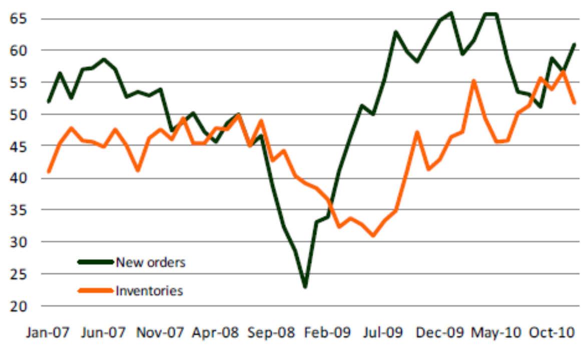
Regional equity markets Q4 (in local currency)



Source: AEGON Fund Management, Bloomberg

The purchasing managers' indexes (PMI/ISM) present a favourable picture, which is reflected not only in their value, but in their structure itself. In the US economy the decline in inventory stocks, accompanied as it is by a growth in orders, can be seen as a very positive sign. The upswing is the result of a pick-up in domestic demand.

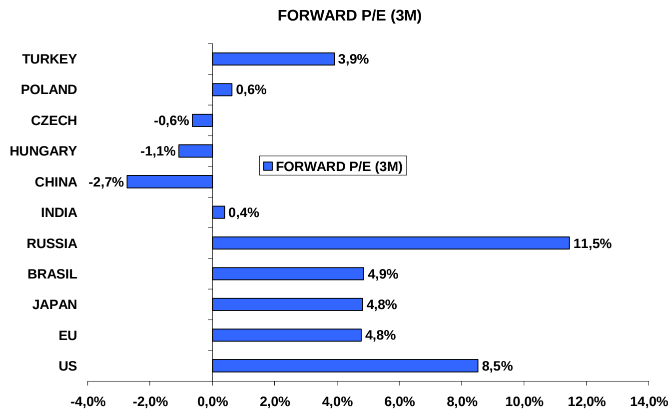




Source: AEGON Fund Management

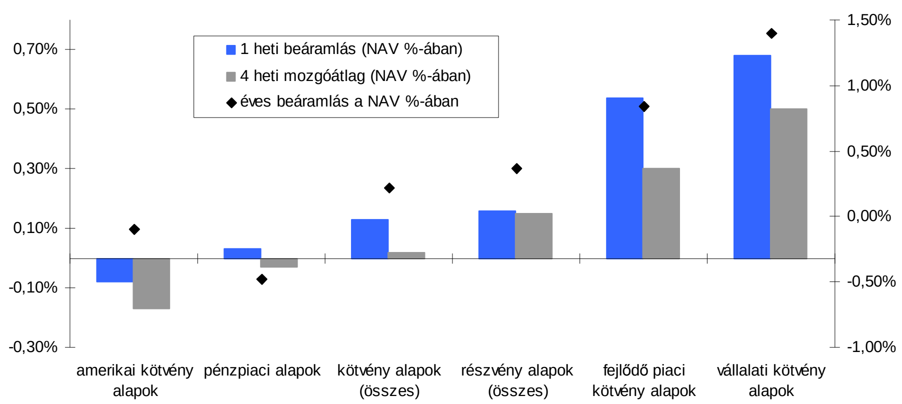
Source: Wood & Company

Despite the fact that 2011 year-end EPS expectations have grown, the pricing of the market (based on P/E ratios) has become somewhat less favourable, due to the significant growth that has occurred in traded prices. The market as a whole has become more expensive, but nevertheless, valuation levels still remain attractive. The corporate earnings forecast for Russia and the USA rose at an above-average rate, with the stock exchanges of China and Central and Eastern Europe lagging behind in this respect. Overall we are optimistic with regard to the equity markets in the forthcoming period, because the valuation levels are favourable both in historical and absolute terms (that is, in comparison to bond yields).



Source: AEGON Fund Management

The market's mood is turning to optimism; but the considerable influx of new money into the equity funds from the bond funds could give rise to even more demand. As the economic upturn continues, the danger of excessive inflation may occasionally cause concern, but for the time being the trends in price levels are generally favourable in terms of their impact on corporate business results.



Source: Deutsche Bank

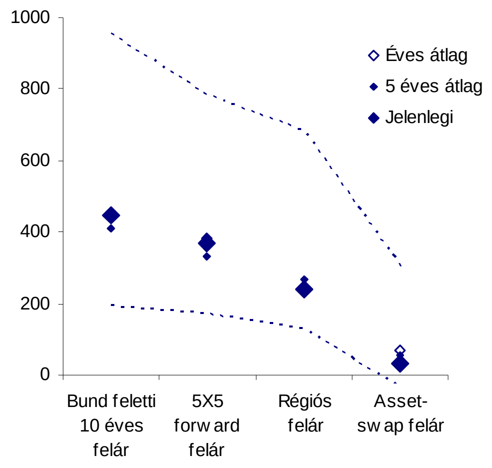
The bourses of Central and Eastern Europe could profit from the growing appetite for risk and the demand generated by German's very strong economy. To date the BUX index has underperformed considerably as a result of the pension fund changes, but in our opinion the news has already been priced in, so we don't expect any further significant underperformance by the Hungarian share index in the coming period.

Parallel to this, Polish shares are less attractive, precisely due to pension fund changes under way in Poland at the moment, which also have a negative market impact, although they are less drastic than the Hungarian measures. The most important event of the first quarter could be the stock-exchange flotation of the Romanian compensation fund, which we expect to perform very well.

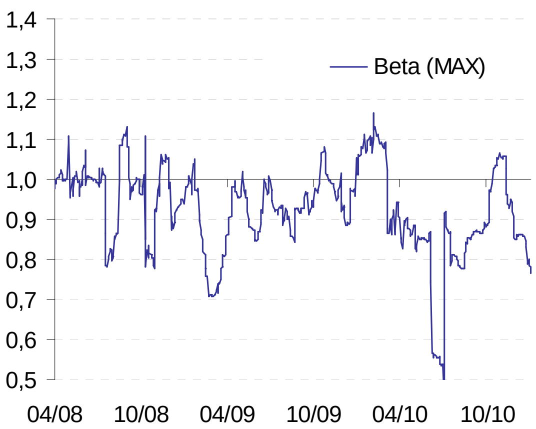
At the beginning of 2011 the economic environment for the Hungarian bond market was mainly negative, so a rise in yields is anticipated. Although the state's liquidity can be seen as good following the nationalisation of the pension funds, the Hungarian market remains highly sensitive to the extreme situation in the global market. Besides this, problems are also mounting up in the bank system, which could break to the surface when the current freeze on evictions comes to an end. On the other hand, there are increasing signs that the government will announce an economic policy package at the end of February that will dispel the present doubts regarding the sustainability of public finance, and the future of the gaping hole that will remain in the state budget once the extraordinary revenues are exhausted.

On the valuation side, despite the relatively high yields, of around 7-7.5%, the bond market cannot be regarded as cheap. Compared to long-term interbank interest rates and euro-denominated Hungarian government securities, Hungarian forint bonds clearly look depressed in a historical analysis. One factor that nevertheless favours the market is the high proportion of underweighted players: we can be confident that sooner or later they will have to buy Hungarian bonds, thus pushing down the yields. Another consequence of the state's favourable liquidity position is that it means no significant issuer pressure is likely on the supply side.

Domestic forint bonds are a little pricy



Positioning of domestic players



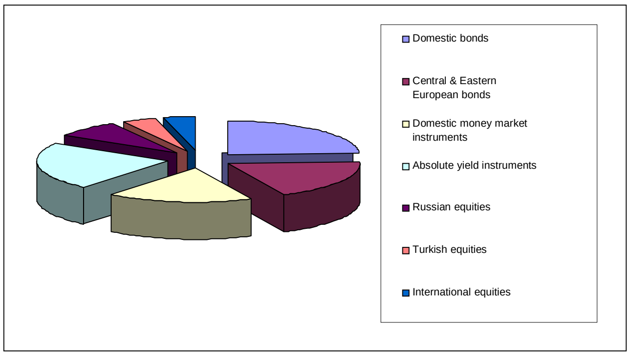
Source: AEGON Fund Management, Bloomberg

Recommended portfolio:

In the current market environment, AEGON Fund Management regards the following portfolio composition as offering the ideal combination of balanced performance and a medium risk profile:

Sample Portfolio (January 2011)

Assets	Weight
Domestic bonds	24%
Central & Eastern European bonds	19%
Domestic money market instruments	18%
Absolute yield instruments	22,5%
Russian equities	8,5%
Turkish equities	4%
International equities	4%



Source: AEGON Fund Management

Prepared by AEGON Global Asset Management / AAM CEE

Supervisory body: Hungarian Financial Supervisory Authority

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