Investment update on the
Baring Europe Select Trust

While investor sentiment towards European smaller companies has been inevitably affected by the ongoing debt crisis in the region, we believe that the fall in markets over the last 12 months has exposed some compelling value for bottom-up stock pickers.

A key factor underpinning this view is that, unlike their large-cap peers, European small-cap equities are predominantly driven by stock specific issues, rather than external macroeconomic forces. This means that stock selection is vital when investing in smaller companies and we place significant emphasis on company research as we try to identify firms with strong balance sheets, sustainable margins and quality management.

This strategy underpins a strong long-term performance record and our preference for firms displaying “quality” characteristics has also rewarded investors in the year-to-date, with the Baring Europe Select Trust returning 10.2% in Sterling terms. Over the same period, the HSBC Smaller Companies Europe ex UK Index has delivered just 0.8%*.

Despite the weak outlook for growth in Europe, we are encouraged that there are smaller companies in the region which continue to flourish. French payment services provider Ingenico is a case in point and the company continues to register strong results due to its exposure to the growing trend for mobile commerce solutions.

While stock selection leads us to maintain a clear preference for core markets such as Germany and France, the recent performance of Spanish Health Care firm Grifols and Italian bank Banca Generali highlight that it is possible for individual companies in the periphery to shine and prosper if they offer competitive products, valuable services or have exposure to resilient growth in the US and the emerging markets.

We remain alert to the valuation discrepancy between the North and South and we have recently taken advantage of this to initiate new holdings in two Spanish companies which we believe have resilient business models and whose operational performance is not dependent on the health of the Spanish consumer. More generally, European smaller companies remain attractively valued, in our view, with valuations still well below their long-term averages on a variety of measures.

Although recent comments by European Central Bank President Mario Draghi to do “whatever it takes” to safeguard the euro are encouraging, it remains difficult to be anything more than cautious on the near-term outlook for economic activity in Europe. However, recent months have shown that it is possible for some stocks to perform well irrespective of the macroeconomic backdrop and we believe that there is significant potential for selected smaller companies to continue to perform strongly in the coming months.

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***Past performance is not a guide to future performance.** Source: Barings, Morningstar, as at 31st July 2012. On a NAV per unit basis with net income reinvested, in Sterling terms.

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