Invesco

Investment Perspective

International Growth

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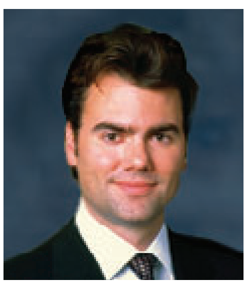

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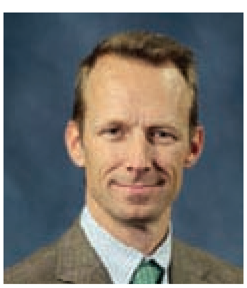

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International Markets: First Quarter Review and Outlook

Increased volatility amid subdued recovery opens new decade

Around the globe, most economic indicators continued to improve, boosted by significant government economic stimulus. But after the strong recovery in equity prices during 2009, international markets exhibited a more tempered recovery during the first quarter of 2010, largely because of fiscal concerns plaguing several European countries and reservations about sustainability.

Performance recap

Performance during the first quarter reflected a recovery, although it's still relatively fragile, especially in Europe. The MSCI EAFE Index – considered broadly representative of European and Asian stocks – returned 0.87% during the quarter, compared with 19.47% and 2.18% for the third and fourth quarters of 2009, respectively. Emerging markets were a bright spot, delivering solid returns versus the MSCI EAFE Index and solid revenue growth versus developed markets. While economic growth continued to recover, we remained cautious of earnings that were generally driven by reductions in operating costs and capital expenditures rather than by strong revenue growth. But company balance sheets remained strong, and valuations – supported by strong dividends and high free cash flow yield – began to approach fair value.

Performance as of March 31, 2010 (%)
International markets opened the decade with performance reflecting a subdued recovery.

	3 MO	1 YR	3 YR	5 YR	10 YR
MSCI EAFE Index	0.87	54.44	-7.02	3.75	1.27
MSCI Europe Index	-1.80	56.10	-7.81	3.45	1.78
MSCI Japan Index	8.18	37.87	-9.03	1.26	-2.99
MSCI AC Asia Pacific ex-Japan Index	2.05	76.85	3.88	12.69	8.09
MSCI Emerging Markets Index	2.40	81.08	5.16	15.65	9.78
MSCI World ex-U.S. Small Cap Index	5.41	74.55	-7.34	4.13	6.90
S&P 500 Index	5.39	49.73	-4.16	1.92	-0.65
Russell 2000 Index	8.85	62.76	-3.99	3.36	3.68

Source: Lipper Inc.
Returns are annualized for periods of one year or more and cumulative for periods less than one year.
-An investment cannot be made directly in an index. Past performance cannot guarantee comparable future results.

Data as of March 31, 2010, unless otherwise stated.

Asia ex-Japan

China continued to be an economic growth engine, leading the recovery from recession both in Asia and globally during the quarter. But concerns remained that strong growth could lead to a rise in inflation, and signs of inflation have accelerated in China and India. Both countries have begun monetary tightening in response to concerns about potential inflation and asset bubbles, and we expect this to continue. Stretched valuation levels in both China and India caused us to seek exposure to less expensive Southeast Asian markets, such as Indonesia, the Philippines and Malaysia.

Japan

Bouncing back from its stint as 2009's weakest developed market performer, Japan was the strongest performing developed market during the first quarter, with the MSCI Japan Index returning 8.18%. The Japanese economy showed signs of recovery, including a rebound in exports, improvement in the retail sector and improved earnings in response to a cyclical upturn.

But problems — including deflation, reduced capital expenditures and no wage growth — continued to plague Japan's economy. In addition, Japan's economy remained challenged by unfavorable demographics, a high level of borrowing and, most importantly, low returns on corporate capital. These factors made Japan a less attractive long-term investment relative to other Asian markets.

Europe

Hampered by the falling value of the euro against the U.S. dollar and negative market sentiment in the wake of Greece's debt crisis, European equities were down 1.80% during the first quarter. Europe lagged the rest of the world, likely due to weaker gross domestic product (GDP) growth. Europe's "PIIGS" — Portugal, Italy, Ireland, Greece and Spain — continued to concern investors because of the potential for their debt levels to exceed their GDPs. Consequently, we kept our exposure to these countries low.

However, economic growth has clearly stabilized in Europe, reflecting healthy consumer savings rates and an increased demand for exports. Earnings were relatively good, and revenue generation started to pick up. European stocks traded at a valuation discount versus other global markets, which offered attractive investment opportunities during the quarter. In addition, low expectations in Europe continued to enhance opportunities to find high-quality, undervalued investments that have been largely ignored by skittish investors.

International small caps

Strong outperformance by international small caps during 2009 eliminated their valuation discount versus international large caps. But we viewed — and continue to view — international small caps as attractive investments because:

- While small caps outnumber large caps, fewer investors consider them. As a result, small caps are largely under-researched.
- Stock pricing in the small-cap market segment is extremely inefficient. We try to exploit these pricing inefficiencies by investing in undervalued companies that have competitive growth potential and low debt levels.
- The valuation discount between non-U.S. small caps and U.S. small caps continued to create investment opportunities.

Emerging markets

Following a strong recovery in 2009, emerging markets continued their economic expansion during the first quarter. We have started seeing economic improvement from economies not so dependent on government stimulus packages. Emerging market economies got additional support from an increase in exports from Western countries.

Earnings in emerging markets continued to point to a path of broad-based recovery, and valuation is around long-run average. Emerging market positives included strong balance sheets in the public and private sectors; an abundance of structural growth drivers, including high savings rates and favorable demographics; and low credit penetration.

We remained cautious, however, that earnings growth may be more forecast than reality. In addition, bullish market sentiment regarding emerging markets made compelling opportunities more difficult to find because of huge inflows driving up valuations. Finally, monetary tightening in China could cause negative market sentiment to develop.

Implications for investors

In general, international markets looked more attractive from a valuation standpoint than U.S. markets during the first quarter. While economic recovery in international markets clearly continued after the dramatic turnaround during 2009, questions about sustainability and the fragile economies of PIIGS cloud the investment outlook.

Irrespective of the investment outlook, we focus on consistently implementing our earnings, quality and valuation (EQV) process — investing in high-quality growth stocks at attractive valuations — to help weather a variety of different economic environments and potentially improve long-term investor results.

About risk

Foreign securities have additional risks, including exchange rate changes, political and economic upheaval, relative lack of information, relatively low market liquidity, and the potential lack of strict financial and accounting controls and standards.

Investing in developing countries can add additional risk, such as high rates of inflation or sharply devalued currencies against the U.S. dollar. Transaction costs are often higher, and there may be delays in settlement procedures.

Investing in a single-country strategy involves greater risk than investing in a more diversified strategy due to lack of exposure to other countries.

Investing in a strategy that invests in smaller companies involves risks not associated with investing in more established companies, such as business risk, stock price fluctuations and illiquidity.

Political and economic conditions and changes in regulatory, tax or economic policy in Japan could significantly affect the market in that country and surrounding or related countries.