

9 January 2008

## Growth differential supporting CEE stock markets

### Highlights:

- **Sub-prime crisis and liquidity shortage has had a limited impact on CEE economies**
- **No more big-bang news expected, although risk aversion might put a burden on growth**
- **Emerging Europe to become the strongest gainer (after Asia) within total emerging markets**

An Erste Group research report, "CEE Equity Strategy", confirms that the sub-prime crisis will take time to fade out and will remain an issue in 2008 although its impact on CEE economies is limited. *"The outlook of slowly growing economies is likely to result in weaker global stock market performance in 2008. Nevertheless, the brake on growth should not be as significant in CEE, as companies have been producing strong cash flows during the recent boom years and should be able to finance capital expenditures to a greater extent"*, says Henning Esskuchen, Equity Co-Head at Erste Group.

### Stable environment expected for CEE

Although 2008 will witness maturing business cycles and a reduction in growth globally, the CEE region continues to have positive levels of growth, supported by ongoing convergence.

*"The financial markets have seen a bit of an overreaction to the sub-prime crisis in 2007. Even though markets have recovered slightly, the sell-off could provide for some further recovery potential. This would soften the impact of the economic outlook and even offer opportunities among cyclical stocks, which would not be the obvious choice in maturing economies"*, so Esskuchen further.

*"Another factor that speaks in favour of equity investments in general is the abundance of cash that should be looking for reasonable returns after the recent sell-off calms down. Importantly, a domestic source of cash becomes an increasingly visible factor. Poland is THE example for the region, and even though we do not expect this to happen at the same magnitude in other markets (anytime soon), one should keep in mind the rising fund industry in markets such as Croatia and even the soon to start pension system in Romania"*, states Esskuchen.

### CEE economies have continued to show impressive growth figures

CEE economies have continued to show impressive growth figures, despite the worsened global economic outlook. However, in most CEE economies, growth is going to slow down somewhat. While the US sub-prime mortgage market crisis and liquidity shortage on major markets have had a limited impact on CEE economies, high commodity prices (particularly of crude oil, wheat and milk powder) have elevated inflation in CEE. In Romania, even though the current account deficit is something to behold, we remain comforted by the fact that the structure of imports (investments) is rather natural for a country at this stage and consumption is not a massive concern. The performance of the Romanian market will strongly depend on the sentiment towards the country and its economic conditions.

### Outlook

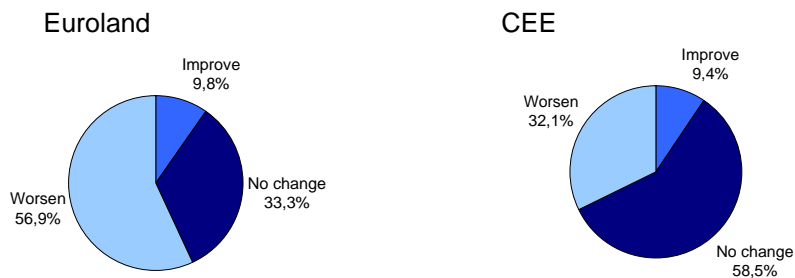
#### Emerging Europe becoming the strongest gainer within total emerging markets - after Asia

Emerging markets gained in terms of weight in Global Equity funds, at the expense of developed markets. Moreover, global emerging market funds improved their view on Emerging Europe and its weight increased, contrary to Emerging Asia and Latin America. However, we should also mention that the weight of cash increased by some 80 basis points.

### Optimistic expectations for Central and Eastern Europe

The ZEW/Erste Bank sentiment indicator<sup>1)</sup> shows, that the economic expectations in CEE are by far more optimistic than in the Euroland: while in Euroland 2/3 of respondents have worsening economic expectations and only 1/3 expect a stable environment, in CEE is it vice versa: 2/3 expect a stable environment and 1/3 have worsening economic expectations.

#### Economic expectations



Source: ZEW<sup>1)</sup>

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1) Data from the ZEW/Erste Bank sentiment indicator. ZEW, the Centre for European Economic Research, Mannheim, and Erste Bank der oesterreichischen Sparkassen, Vienna, carry out a monthly survey for Central and Eastern Europe, Austria, and the Eurozone asking financial market experts about their assessment and expectations with regard to economic and financial market data. The results of the most recent survey conducted between 30 October and 19 November 2007 were published in the December issue of the "Financial Market Report CEE". 73 financial market experts participated in the survey.