

MEDIA RELEASE

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The quality of emerging markets debt will continue to improve as the developed world faces further downgrades, says First State's Williamson

Whilst the advanced economies' credit ratings remain under pressure from high levels of debt and rising pension liabilities, the investment case for emerging markets' sovereign debt will continue to strengthen, according to **Helene Williamson**, Head of Emerging Markets Debt at First State Investments. The fund manager says that the level of debt of the advanced economies has risen sharply from around 77% of GDP in 2007 and is expected to exceed 100% of GDP in 2011. In contrast, emerging markets' average debt-to-GDP ratio currently stands at about 34%.

Williamson manages the **First State Emerging Markets Bond Fund**, which was launched last month. The fund aims to achieve a combination of income and capital appreciation through investing predominantly in hard currency debt securities issued or guaranteed by governments, financial institutions or companies in emerging markets. It maintains a broadly diversified portfolio comprising primarily US dollar-denominated sovereign and quasi-sovereign debt instruments.

Helene Williamson comments:

'Emerging nations are now in a much stronger position to service their debt obligations than the world's advanced economies. We expect this to become even more pronounced over the next few years as emerging economies remain supported by their good fiscal positions, relatively low financing needs and favourable demographics.

Helene Williamson continues:

'Advanced economies with their ageing populations have to cope with rising pension liabilities, which are not included in debt-to-GDP ratios but are increasingly taken into account by credit rating agencies. Most emerging market countries have younger populations and enjoy a "demographic dividend" and higher growth rates. Their financing requirements are also considerably lower than those of advanced economies. Next year gross financing needs of emerging countries are expected to account for only about 8% of their GDP, whilst the developed

world would have to raise over 27% of GDP. The strong ability of emerging markets to repay their debts is reflected in their improving credit ratings and, in our view, this trend is set to continue.'

The average rating of emerging markets countries has been on a long-term upward trend. In 1994, the average rating was BB-; by 2010, the average rating has moved to investment grade BBB-. In contrast, developed markets have seen a number of downgrades over the past seven years, which most recently included the US and several European countries. The relative credit strength of emerging market countries has also been reflected in the risk premium over US Treasuries, which has declined sharply since 2009 and can potentially reduce further, in Williamson's view. She says that despite a positive long-term outlook for emerging markets debt, her fund will focus on the higher quality of its investment universe:

'The major risk facing emerging markets today is the state of the developed world. Despite their own fundamentals remaining strong, emerging markets are not immune to occasional 'contagion', which was why emerging market bonds sold off in September on heightened market nervousness about Greece, Italy and the European banking sector. Accordingly, despite a strong long-term outlook for the asset class, we are relatively cautiously positioned in our funds at the moment.

'We are concerned about the current market environment in Western Europe and do not believe that the European Financial Stability Facility, as it stands at the moment, is going to solve the 'European problem'. With correlations between different asset classes remaining high, we are positioned in the higher quality end of the emerging market debt investment universe, which comprises Latin America, Asia and Middle Eastern credits.'

Helene Williamson concludes:

'The euro periphery crisis has underlined the attractiveness of emerging markets debt for many pension funds and other investors because it has focused the debate on countries' debt levels. It has highlighted the superior credit quality of emerging markets in terms of debt-to-GDP, fiscal deficits, international reserve cushions and lower pension obligations.'

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Notes for Editors

About First State Investments

First State Investments provides specialist asset management services to wholesale and institutional investors across a diverse range of asset classes, including Asia Pacific and global emerging market equities, global equities, property securities, infrastructure, global natural resources and emerging markets debt.

First State Investments forms part of the asset management division of the Commonwealth Bank of Australia. In Australia we operate as Colonial First State Global Asset Management ('CFSGAM'). First State and CFSGAM collectively manage £87.7 billion on behalf of investors worldwide (as at 30th September 2011) and have offices in Sydney, New York, London, Edinburgh, Hong Kong, Singapore, Jakarta and Tokyo. In London and Edinburgh it has more than 200 staff.

CFSGAM (including First State) is a signatory to the United Nations' Principles for Responsible Investment, a voluntary program which encourages best practice in environmental, social and corporate governance issues.

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