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EUROPEAN EQUITY FUND, INC / MD
Form N-CSRS
September 08, 2006
UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D. C. 20549

FORM N-CSRS

Investment Company Act file number 811-4632

European Equity Fund, Inc.

(Exact Name of Registrant as Specified in Charter)

Two International Place

Boston, MA 02110

(Address of principal executive offices) (Zip code)

Registrant's Telephone Number, including Area Code (212) 454-7190

Paul Schubert

345 Park Avenue

New York, NY 10154

(Name and Address of Agent for Service)

Date of fiscal year end: 12/31

Date of reporting period: 06/30/06

ITEM 1. REPORT TO STOCKHOLDERS

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[GRAPHIC]

THE EUROPEAN
EQUITY FUND, INC.

LETTER TO THE SHAREHOLDERS

European equity markets, in line with global trends, experienced a difficult second quarter as investors started to question the sustainability of economic growth on the back of further central bank tightening, particularly in the US. In the subsequent wave of profit-taking and withdrawal from risk positions, the performance patterns of the earlier months of the year reversed and market segments associated with cyclicalities suffered the most: the industrials, technology, financials and consumer discretionary sectors, small and mid-cap stocks and stocks with sizeable emerging markets exposure. Among European countries, the Fund's focus markets of the European Monetary Union (EMU) were comparatively weak with the MSCI EMU declining by 4.2%.⁽¹⁾ Germany and the Netherlands delivered the worst performance of the larger markets while Spain fared better. Outside EMU, the UK market proved to be defensive while Sweden corrected more strongly. The Fund's preferred non-EMU markets, Switzerland and Norway, showed performance similar to the overall European market.

For the six months ended June 30, 2006, the European Equity Fund's total return was 15.31% (not annualized) based on net asset value and 16.81% (not annualized) based on share price. During the same period, the Fund's benchmark* gained 14.35% (not annualized).

In the first half of 2006, the Fund's good relative performance mainly resulted from the application of several key strategic themes, including a preference for industrial and energy stocks. In addition, the Fund's holdings in the financials sector boosted performance. The Fund's performance was hindered by the sharp correction in the mid-cap segment, to which the Fund is more exposed than its benchmark. In the industrials sector, the Fund sold the remainder of its position in Solarworld after the stock's strong performance. The proceeds were used to rebuild a position in Metso, which had suffered unduly in the market correction, providing an attractive re-entry opportunity. One of the key contributors to performance among the Fund's industrials holdings was Vallourec, a pipe producer in the oil services sector. Within the energy sector, the preference is still with the oil services stocks. However, the Fund has reduced its positions in Saipem and Acergy after their strong performance, reinvesting the proceeds in Cie Fen de Geophysiq, a French oil exploration company, and Total, one of our preferred oil majors. The Fund's holdings in the financial sector continue to be a key source of strong relative performance, despite the underperformance of Hypo Real Estate and Efg Eurobank during the second quarter. In particular, the Fund's cautious stance on ABN Amro and Allianz contributed strongly to the Fund's relative performance during the second quarter. Healthcare company Essilor International, which is the global

leader in corrective eyeglass lenses, also contributed positively to the relative performance. Among technology stocks, Ericsson reduced the Fund's relative performance during the second quarter, but remains a key holding for its exposure to emerging markets and new application growth in mobile infrastructure. Performance during the second quarter was also hindered by the Fund's position in DaimlerChrysler, which underperformed the benchmark; the company is in the midst of a restructuring that should enhance shareholder value.

On a country level, the Fund continued to reduce its exposure to German equities during the second quarter, as the valuation gap with the rest of Europe has closed. However, Germany remains the largest overweight country in the Fund, while the Netherlands and Spain remain the largest underweight countries. Switzerland, Norway, and Sweden continue to be key ex-benchmark countries.

The European Equity Fund resumed its open-market purchases of its shares only to a small extent by buying 2,750 shares during the first six months of 2006.** The

FOR ADDITIONAL INFORMATION ABOUT THE FUND INCLUDING PERFORMANCE, DIVIDENDS, PRESENTATIONS, PRESS RELEASES, DAILY NAV AND SHAREHOLDER REPORTS,

PLEASE VISIT www.germanyfund.com

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Fund's discount to net asset value for the six months ending June 30, 2006 was 9.91%, compared with 12.87% for the same period last year.

At their June 20, 2006 Annual Meeting, the Fund's stockholders elected the four Directors who had been proposed by the Fund's Board and management. The stockholders also ratified the Board's selection of PricewaterhouseCoopers LLP as the Fund's independent auditors for the 2006 fiscal year.

The sources, opinions and forecasts expressed are as of July, 2006. There is no guarantee that the views, opinions and forecasts expressed herein will come to pass. This information is subject to change at any time based on market and other conditions and should not be construed as a recommendation for any specific security. Past performance does not guarantee future results.

(1) The MSCI-EMU Index is an unmanaged capitalization-weighted index that is comprised of more than 300 stocks of companies domiciled in the 12 countries utilizing the Euro currency. MSCI indices are calculated using closing local market prices and converted to US dollars using the London close foreign exchange rates. Index returns assume reinvested dividends and, unlike Fund returns, do not reflect any fees or expenses. It is not possible to invest directly into an index.

* As of November 1, 2005, the benchmark is the MSCI EMU Index. Prior to November 1, 2005, the benchmark was the DAX Index.

** The share buy back program was suspended for a portion of the semi-annual period.

Sincerely,

/s/ Christian Strenger

Christian Strenger

Chairman

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PRESENTATIONS, PRESS RELEASES, DAILY NAV AND SHAREHOLDER REPORTS,
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FUND HISTORY AS OF JUNE 30, 2006

ALL PERFORMANCE SHOWN IS HISTORICAL, ASSUMES REINVESTMENT OF ALL DIVIDEND AND

CAPITAL GAIN DISTRIBUTIONS, AND DOES NOT GUARANTEE FUTURE RESULTS. INVESTMENT RETURN AND PRINCIPAL VALUE FLUCTUATE WITH CHANGING MARKET CONDITIONS SO THAT, WHEN SOLD, SHARES MAY BE WORTH MORE OR LESS THAN THEIR ORIGINAL COST. CURRENT PERFORMANCE MAY BE LOWER OR HIGHER THAN THE PERFORMANCE DATA QUOTED. PLEASE VISIT www.germanyfund.com FOR THE FUND'S MOST RECENT PERFORMANCE.

TOTAL RETURNS:

<Table>

<Caption>

FOR THE
SIX MONTHS

ENDED FOR THE YEARS ENDED DECEMBER 31,
JUNE 30, -----

2006(b) 2005 2004 2003 2002 2001

<S>	<C>	<C>	<C>	<C>	<C>	<C>
Net Asset Value(a)	15.31%	7.17%	12.58%	59.62%	(34.43)%	(25.57)%
Market Value(a)	16.81%	9.66%	7.25%	68.81%	(35.76)%	(24.95)%
Benchmark	14.35%(3)	8.41%(1)	15.91%(2)	65.16%(2)	(34.14)%(2)	(23.20)%(2)

</Table>

(a) Total return based on net asset value reflects changes in the Fund's net asset value during each period. Total return based on market value reflects changes in market value. Each figure includes reinvestments of dividend and capital gain distributions, if any. These figures will differ depending

upon the level of any discount from or premium to net asset value at which the Fund's shares trade during the period.

(b) Total returns shown for the six month period are not annualized.

(1) Represents DAX Index* for 1/1/05-10/31/05 and MSCI-EMU** for 11/1/05-12/31/05.

(2) Represents DAX Index*.

(3) Represents MSCI-EMU Index**.

* DAX Index is a total rate of return index of 30 selected German blue chip stocks traded on the Frankfurt Stock Exchange.

** MSCI-EMU Index is an unmanaged capitalization-weighted index that is comprised of more than 300 stocks of companies domiciled in the 12 countries utilizing the Euro currency.

Index returns assume reinvested dividends and, unlike Fund returns, do not reflect any fees or expenses. It is not possible to invest directly into an index.

ON OCTOBER 27, 2005, THE FUND ADOPTED ITS CURRENT NAME AND INVESTMENT POLICIES. PRIOR TO THAT DATE THE FUND WAS KNOWN AS THE GERMANY FUND AND ITS OBJECTIVE WAS

TO SEEK LONG-TERM CAPITAL APPRECIATION PRIMARILY THROUGH INVESTMENTS IN GERMAN EQUITIES.

Investments in funds involve risk including the loss of principal.

This Fund is not diversified and primarily focuses its investments in equity securities of issuers domiciled in European countries that utilize the Euro currency, thereby increasing its vulnerability to developments in that region.

Investing in foreign securities presents certain unique risks not associated with domestic investments, such as currency fluctuation and political and economic changes and market risks. This may result in greater share price volatility.

Closed-end funds, unlike open-end funds, are not continuously offered. There is a one-time public offering, and once issued, shares of closed-end funds are sold in the open market through a stock exchange. Shares of closed-end funds frequently trade at a discount to net asset value. The price of the Fund's shares is determined by a number of factors, several of which are beyond the control of the Fund. Therefore, the Fund cannot predict whether its shares will trade at, below or above net asset value.

The Fund has elected to not be subject to the statutory calculation, notification and publication requirements of the German Investment Tax Act (Investmentsteuergesetz). As a result German investors in the Fund may be subject to less favorable lump-sum taxation under German law.

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STATISTICS:

Net Assets	\$134,829,343
Shares Outstanding	11,829,244
NAV Per Share	\$ 11.40

DIVIDEND AND CAPITAL GAIN DISTRIBUTIONS:

RECORD DATE	PAYABLE DATE	ORDINARY INCOME	LT CAPITAL GAINS	TOTAL
05/05/06	05/15/06	\$0.090	\$ --	\$0.090
12/22/05	12/30/05	\$0.060	\$ --	\$0.060
12/22/04	12/31/04	\$0.025	\$ --	\$0.025
05/06/04	05/14/04	\$0.039	\$ --	\$0.039
11/19/02	11/29/02	\$0.010	\$ --	\$0.010
11/19/01	11/29/01	\$0.060	\$ --	\$0.060
09/03/01	09/17/01	--	\$0.020	\$0.020
11/20/00	11/29/00	--	\$2.180	\$2.180
09/01/00	09/15/00	\$0.190	\$0.120	\$0.310

OTHER INFORMATION:

NYSE Ticker Symbol	EEA
NASDAQ Symbol	XEEAX
Dividend Reinvestment Plan	Yes
Voluntary Cash Purchase Program	Yes
Annualized Expense Ratio (6/30/06)*	1.70%

* Represents expense ratio before custody credits. Please see "Financial Highlights" section of this report.

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PORTFOLIO BY MARKET SECTOR AS OF JUNE 30, 2006 (AS A % OF PORTFOLIO'S MARKET VALUE*)

[CHART]

<Table>

<S>	<C>
Financials	(34%)
Health Care	(4%)

Industrials	(15%)
Information Technology	(8%)
Telecommunication Services	(6%)
Utilities	(4%)
Materials	(7%)
Consumer Discretionary	(8%)
Consumer Staples	(4%)
Energy	(10%)

</Table>

10 LARGEST EQUITY HOLDINGS AS OF JUNE 30, 2006 (AS A % OF PORTFOLIO'S MARKET VALUE*)

1. Total SA	5.5
2. Societe Generale	3.9
3. E.ON	3.6
4. Banca Intesa Spa	3.5
5. Siemens	3.2
6. DaimlerChrysler	3.1
7. Axa	2.9
8. Capitalia Spa	2.9
9. Hypo Real Estate Holding	2.9
10. Compagnie De Saint-Gobain	2.7

* Percentage (%) of market value refers to all securities in the portfolio, except cash and equivalents.

Portfolio by Market Sector and 10 Largest Equity Holdings are subject to change.

Following the Fund's fiscal first and third quarter-end, a complete portfolio holdings listing is filed with the SEC on Form N-Q. The form will be available on the SEC's Web site at www.sec.gov, and it also may be reviewed and copied at the SEC's Public Reference Room in Washington, D.C. Information on the operation of the SEC's Public Reference Room may be obtained by calling (800) SEC-0330.

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INTERVIEW WITH THE LEAD PORTFOLIO MANAGER -- RALF OBERBANNSCHEIDT

QUESTION: WHAT IS THE IMPACT OF A STRONGER EURO ON THE EUROPEAN UNION'S (EU) EXPORT-DRIVEN ECONOMY?

ANSWER: Given the EU's sluggish domestic demand and its position as the world's leading export economy, appreciation of the euro currency is a critical factor to watch. The euro appreciated more than 8% vs. the US dollar in the first half of 2006. However, the latest trade data suggests that the recent appreciation in the euro has not yet dampened exports. Although demand from the US appears to have slowed, overall export demand for European goods continued to increase through May, driven by demand from emerging markets and oil-producing

countries, and survey data suggests that demand will remain robust. However, part of the reason for this may be that exporting companies often absorb the cost of short-term currency fluctuations, rather than pass the costs on to their customers. This means that companies may see lower profit margins, especially if the current strength of the euro persists.

QUESTION: AS GERMAN CHANCELLOR ANGELA MERKEL APPROACHES HER ONE-YEAR ANNIVERSARY AT THE HELM, HAS HER COALITION GOVERNMENT BEEN ABLE TO MAKE ANY PROGRESS ON REFORMS?

ANSWER: Criticism that Ms. Merkel's reform program seems to be stalling comes on the heels of recent announcements by the government regarding details on two reform programs -- one addressing health care and the other addressing corporate taxes. After months of negotiations, the coalition government reached an agreement on a watered down health care reform that economists believe results in increased labor costs for companies and lower disposable income for households without fully meeting the financial needs of the healthcare system. As far as the corporate tax reform, the overall impact of the recently announced plan will be a reduction in the corporate tax rate from 39% to 29%, resulting in 5 billion euros of tax relief. However, this reduction will be financed through a broadening of the tax base to include interest payments, which could discourage investment and is expected to increase the tax burden of smaller German companies, which tend to rely more heavily on financing. Thus, Ms. Merkel's government has produced some reforms, but they required significant compromise for the coalition to reach agreement.

QUESTION: VIVIANE REDING, THE EU COMMISSIONER FOR INFORMATION SOCIETY AND MEDIA, RECENTLY UNVEILED PLANS TO REGULATE ROAMING CHARGES ON MOBILE PHONES. WHAT IS THE RATIONALE BEHIND THIS MOVE TOWARD INCREASED REGULATION?

ANSWER: Pricing in the mobile phone market in the EU differs significantly from pricing in the US, where roaming is often included as part of a package of minutes. Mobile phone users in the EU pay international roaming charges averaging \$1.50 per minute -- and depending on the location, the rates can be significantly higher. Someone from the UK, for example, could pay \$4.00 per minute to call home from as close as France. This is primarily due to the fact that different companies operate the mobile networks in the various countries of the EU. Companies such as Vodafone in the UK, T-Mobile in Germany, and Telefonica in Spain charge each other wholesale prices for their customers to use each other's networks. Currently, the mobile operators are not obligated to pass on any reduction in wholesale prices to their customers. The plan proposed by Ms. Reding is meant to reduce prices paid by the consumer by linking the retail price to the wholesale price and capping the retail price at 49 euro cents per minute. European mobile operators, who generate revenues of approximately \$11 billion from roaming fees, have objected to the proposed regulation, saying that they have recently taken measures to offer reduced roaming rates to customers. The proposal's impact on mobile operators' bottom line is somewhat uncertain, as reduced per minute roaming rates could result in a higher volume of calls, but is expected to be negative overall. More importantly, mobile operators contend that the regulation will stifle innovation and discourage investment in faster networks. This comes at a time when EU regulation also puts the brakes on incentives for fixed line network upgrades.

The plan, which is subject to approval by the European Parliament, could go into effect within a year.

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ECONOMIC OUTLOOK

The recent equity market correction has put the macroeconomic debate over growth and inflation back into focus. The concerns are the same as before in similar market phases: economic growth is feared to slow down more than expected as the major central banks may fight accelerating inflation more aggressively. Yet, evidence for such a scenario from actual data is scarce. As expectations are adjusted to reflect those concerns and investors scale down their risks, particularly in the hitherto popular spread trades, the market is clearing some liquidity and momentum-driven exaggerations, providing a sound base for advances on the back of benign fundamentals: while global economic growth is likely to

moderate it should remain robust enough to support further earnings growth in the corporate sector.

Despite the volatility in the equity markets, European leading indicators continue to climb (the German Ifo, for example, reached a 15-year high in June), fueling optimism for potential upwards revisions to GDP growth.(1) We continue to see variations across Euroland, with industrial production in Germany, for example, picking up while it contracted in France. In addition, the French INSEE was the one European indicator that declined in June. However, the services sector is doing better in France than Germany.

We expect Euroland growth of about 2% for the remainder of the year; however, for 2007 the combination of the ECB hiking cycle, a less positive export contribution to growth and fiscal consolidation from local governments could put pressure on the recent improvements. Although inflation remains above the ECB's 2% target due to the impact of higher energy prices, the core rate remains contained.

The European Central Bank (ECB) raised interest rates by 0.50% in the first half of 2006. Although we expect another 0.50% hike in the second half of the year, we believe that the ECB does not want to jeopardize the economic recovery and that any sign of a deterioration in the economic outlook could mean the end of the rate hike cycle. This will have to be balanced as energy prices remain high and optimism rises for above-trend GDP growth.

(1) The Ifo Business Climate Index is a closely watched indicator of German business conditions, based on a monthly survey of about 7,000 companies. It is widely seen as a barometer for economic conditions in the whole of the Eurozone, which is a term used to describe the 11 EU countries that joined the third stage of EMU and adopted the euro. The Eurozone, or Euroland countries are Austria, Belgium, Finland, France, Germany, Ireland, Italy, Luxembourg, The Netherlands, Portugal and Spain.

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THE EUROPEAN EQUITY FUND, INC.

SCHEDULE OF INVESTMENTS -- JUNE 30, 2006 (UNAUDITED)

SHARES	DESCRIPTION	VALUE
-----	-----	-----
	INVESTMENTS IN GERMAN SECURITIES - 23.9%	

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COMMON STOCKS - 22.2%

AUTOMOBILES - 3.1%

84,000	DaimlerChrysler	\$ 4,147,332
--------	-----------------	--------------

CHEMICALS - 1.0%

17,200	K + S	1,386,488
--------	-------	-----------

ELECTRIC UTILITIES - 3.5%

41,000	E.ON	4,717,237
--------	------	-----------

ELECTRONIC EQUIPMENT & INSTRUMENTS - 1.6%

17,000	Wincor Nixdorf	2,171,684
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INDUSTRIAL CONGLOMERATES - 3.1%

48,100	Siemens	4,182,254
--------	---------	-----------

INDUSTRIAL GASES - 1.1%

19,000	Linde	1,463,105
--------	-------	-----------

MACHINERY - 0.9%

17,000	Rheinmetall	1,184,377
--------	-------------	-----------

REAL ESTATE - 2.8%

62,500	Hypo Real Estate Holding	3,793,561
--------	--------------------------	-----------

SOFTWARE - 2.5%

16,000 SAP 3,374,184

TEXTILES, APPAREL & LUXURY GOODS - 2.6%

74,400 Adidas Salomon 3,554,488

Total Common Stocks

(cost \$16,155,293) 29,974,710

PREFERRED STOCKS - 1.6%

HEALTHCARE PROVIDERS & SERVICES - 1.6%

13,000 Fresenius

(Cost \$1,426,469) 2,164,143

RIGHTS - 0.1%

CHEMICALS

19,000 Linde AG - Rights

(Cost \$0) 73,337

Total Investments in German Securities

(cost \$17,581,762) 32,212,190

INVESTMENTS IN AUSTRIAN

COMMON STOCKS - 3.2%

COMMERCIAL BANKS -- 1.0%

21,750 Wiener Staedt Vers.+ \$ 1,278,739

CONSTRUCTION MATERIALS - 1.0%

28,300	Wienerberger Ag+	1,349,150
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INSURANCE - 1.2%

50,000	Uniqa Versicherungen	1,623,187
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Total Investments in Austrian Common Stocks

(cost \$3,789,263)	4,251,076
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INVESTMENTS IN DUTCH

COMMON STOCKS - 1.3%

FOOD & STAPLES RETAILING - 1.3%

40,169	Koninklijke Numico Nv*	
(Cost \$1,686,405)	1,801,521	

INVESTMENTS IN FRENCH

COMMON STOCKS - 29.3%

AIRLINES - 1.7%

40,000	Zodiac SA*	2,247,922
--------	------------	-----------

BEVERAGES - 2.3%

15,800	Pernod-Ricard	3,130,067
--------	---------------	-----------

CONSTRUCTION MATERIALS - 2.7%

50,000	Compagnie De Saint-Gobain+	3,572,290
--------	----------------------------	-----------

ELECTRICAL EQUIPMENT - 0.1%

6,000	Legrand Promesses	168,709
-------	-------------------	---------

ENERGY EQUIPMENT & SERVICES - 1.0%

8,000	Cie Fen de Geophysiq	1,379,326
-------	----------------------	-----------

INDUSTRIAL CONGLOMERATES - 1.7%

20,000	Neopost SA+	2,277,574
--------	-------------	-----------

INSURANCE - 3.9%

118,100	Axa	3,873,213
---------	-----	-----------

15,000	CNP Assurances	1,425,401
--------	----------------	-----------

5,298,614

The accompanying notes are an integral part of the financial statements.

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SHARES	DESCRIPTION	VALUE
--------	-------------	-------

METALS & MINING - 1.9%

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2,100 Vallourec+ \$ 2,522,969

NATIONAL COMMERCIAL BANKS - 3.8%

35,000 Societe Generale 5,144,353

OIL, GAS & CONSUMABLE FUELS - 5.5%

111,600 Total SA 7,338,620

SPECIALTY RETAIL - 1.5%

20,700 Essilor International 2,082,140

TELECOMMUNICATIONS SERVICES - 1.6%

100,000 France Telecom SA 2,148,486

TEXTILES, APPAREL & LUXURY GOODS - 1.6%

22,000 LVMH Moet Hennessy Loui V Sa 2,181,972

Total Investments in French Common Stocks

(cost \$35,357,321) 39,493,042

INVESTMENTS IN SWEDISH

COMMON STOCKS - 2.3%

COMMUNICATIONS EQUIPMENT - 2.3%

940,000 Ericsson

(Cost \$3,151,496) 3,105,066

INVESTMENTS IN ITALIAN

COMMON STOCKS - 13.1%

COMMERCIAL BANKS - 8.5%

800,000 Banca Intesa Spa 4,682,958

60,000 Banca Italease 3,005,324

468,000 Capitalia Spa 3,837,137

11,525,419

ENERGY EQUIPMENT & SERVICES - 1.0%

59,000 Saipem+ 1,342,261

HEALTHCARE PROVIDERS & SERVICES - 1.1%

170,000 Amplifon Spa 1,445,978

INSURANCE - 2.5%

70,000 Assicurazioni Generali+ \$ 2,548,020

150,000 Ergo Previdenza Spa+ 847,380

3,395,400

Total Investments in Italian Common Stocks

(cost \$12,886,510) 17,709,058

INVESTMENTS IN SWISS

COMMON STOCKS - 5.7%

DIVERSIFIED CONSUMER SERVICES - 1.3%

1,900 SGS SA 1,799,331

ELECTRICAL DISTRIBUTION --1.1%

117,000 ABB Ltd* 1,518,736

INSURANCE - 1.4%

24,000 Baloise Holding -R 1,840,803

NATIONAL COMMERCIAL BANKS - 0.9%

22,000 Credit Suisse Group 1,228,508

TEXTILES, APPAREL & LUXURY GOODS - 0.9%

7,500 The Swatch Group Ag-B 1,264,389

Total Investments in Swiss Common Stocks

(cost \$6,270,478) 7,651,767

INVESTMENTS IN FINNISH

COMMON STOCKS - 2.7%

MACHINERY - 1.5%

57,000 METSO OYJ 2,066,803

PAPER MILLS - 1.2%

75,000 UPM-Kymene Oyj 1,615,199

Total Investments in Finnish Common Stock

(Cost \$3,684,976) 3,682,002

The accompanying notes are an integral part of the financial statements.

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SHARES	DESCRIPTION	VALUE
-----	-----	-----
INVESTMENTS IN SPANISH COMMON STOCKS -- 5.7%		
COMMERCIAL BANKS - 1.9%		
126,100	Banco Bilbao Vizcaya Argentaria	\$ 2,591,588

COMMUNICATIONS EQUIPMENT - 1.3%		
90,000	Indra Sistemas SA	1,765,695
&nb		