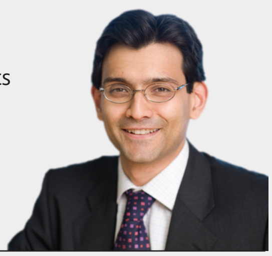
Aberdeen Emerging Markets Smaller Company Opportunities Fund, Inc.

Portfolio Manager Interview

August 2017

Devan Kaloo
Head of Global Emerging Markets Equities



Key points

- Most markets up during 2Q
- Active inflows outpace passive
- Brazil implements reforms despite Temer uncertainty
- China tightens liquidity for stability
- "Old" tech beats "new" tech on earnings

What has happened during the latest quarter?

Corporate earnings are improving, and investors seem less bothered about weaker commodity prices and the U.S. Federal Reserve (Fed). The U.S. dollar has weakened in part on a readjustment of expectations over the pace of further interest-rate increases. Most markets did well, although some were simply regaining lost ground. The exceptions were few and the reasons idiosyncratic. For example, Brazil performed poorly after President Michel Temer became embroiled in a corruption scandal which could pose a risk to reforms, and the Russian market struggled because of softer oil prices and deteriorating relations with the U.S. Additionally, Qatar was a laggard because regional rival Saudi Arabia is behind efforts to isolate the gas-rich country.

We are seeing active money returning to emerging markets. Why is this important?

Capital has been trickling back into the emerging markets since early last year, but we have always cautioned against excessive optimism because a lot of this money had gone into index-tracking passive investments such as exchange-traded funds (ETFs). To us, this suggests short-term money trading on differences in market valuations that could quickly reverse direction. However, year-to-date data show that active money going into dedicated emerging market funds is catching up with passive inflows. If this continues, 2017 could be the first year since 2010 when active inflows beat passive for this asset class. Why is this important? Active money suggests more conviction on the part of the investor. Investors are starting to believe that the worst is over and are positioning themselves for a sustainable recovery. Active money is also less likely to flee at the first sign of trouble. We're hopeful that this is a sign of things to come.

Aberdeen
Simply asset management.

"The Brazilian stock market saw its worst one-day decline since 2008 and the real fell by nearly 8%, after President Temer was implicated in a corruption scandal."

How concerned are you about political developments in Brazil?

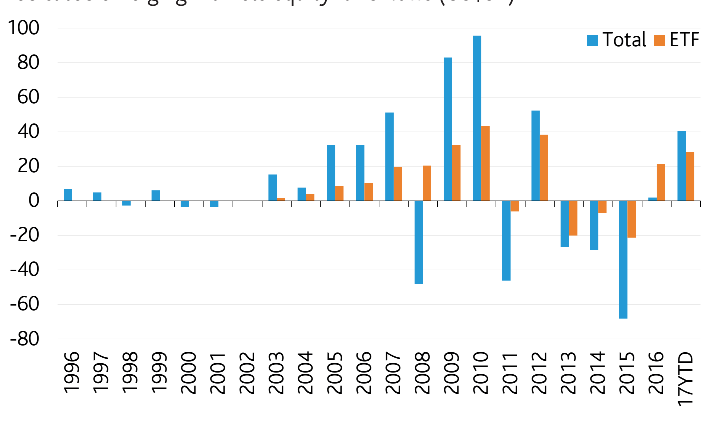
The Brazilian stock market saw its worst one-day decline since 2008 and the real fell by nearly 8%, after President Temer was implicated in a corruption scandal. He denied any wrongdoing and rejected calls to step down. Lawmakers recently voted not to send the case to the nation's supreme court. Popular support for the president has weakened, but there does not seem to be much desire for a leadership change so close to the next elections, which is slated for October 2018. In addition, this has not stopped Temer's administration from forging ahead with reforms.

What about liquidity tightening in China?

Tighter monetary conditions will need to be closely monitored in the coming months. China has been tightening liquidity in a bid to clamp down on the sale of so-called "wealth management products." Higher bank borrowing costs make it less profitable to sell them. So on the back of consecutive quarters of rising gross domestic product (GDP) growth, policymakers have tightened interbank lending without resorting to raising rates in the real economy. That said, China will likely support stable credit growth in preferred sectors to manage a controlled slowdown that will help deflate the country's debt bubble – a longstanding concern. Meanwhile, currency stability is a reflection of receding concerns over capital flight. Government intervention is also behind the recovery in the property market, as well as a pickup in construction activity.

Chart 1: Active inflows returning

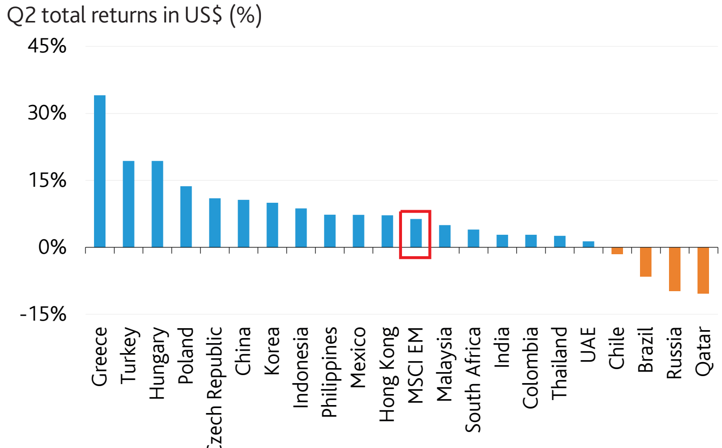
Dedicated emerging markets equity fund flows (US$bn)



Source: EPFR Global, Morgan Stanley Research, June 28, 2017
Estimates collated from weekly AuMs for reference. Numbers do not add up to YTD total, which are tallied using monthly AuMs.

Chart 2: Most markets up in 2Q

Q2 total returns in US$ (%)



Sources: Bloomberg, MSCI, June 30, 2017. Each country is represented by its respective MSCI country index. EM = Emerging Markets Index. Indexes are unmanaged and have been provided for comparison purposes only. No fees or expenses are reflected. You cannot invest directly in an index. **PAST PERFORMANCE IS NOT A GUIDE TO FUTURE RESULTS.**

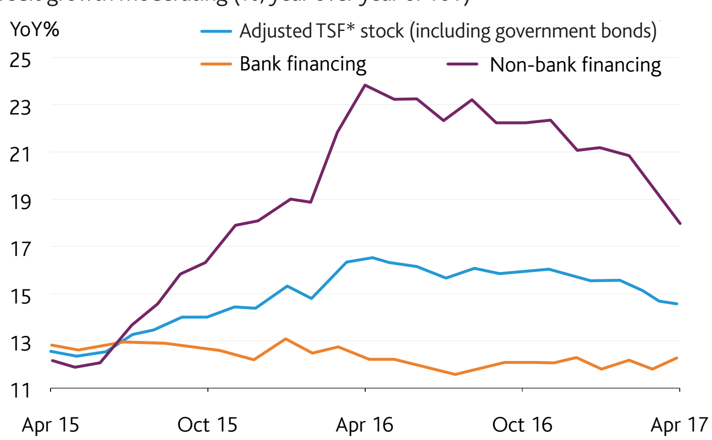
What is your view of the technology sector?

Information technology was the biggest driver of the index's gains during the first half of the year, and this sector now accounts for a larger weighting in the benchmark than financial stocks. To be more specific, it was the big Chinese internet stocks that were behind the index's gains. Historically we have had significant problems with the unconventional corporate structures used to circumvent laws prohibiting direct foreign ownership of internet companies in China, and the fact that Chinese law remains ambiguous on the legality of these structures. While this risk remains, internet firms have become an important part of the domestic stock markets and the economy, which potentially reduces the risk of the government ruling on these structures in a way that is detrimental to foreign investors.

"Information technology was the biggest driver of the index's gains during the first half of the year, and this sector now accounts for a larger weighting in the benchmark than financial stocks."

Chart 3: China – tightening cycle has begun

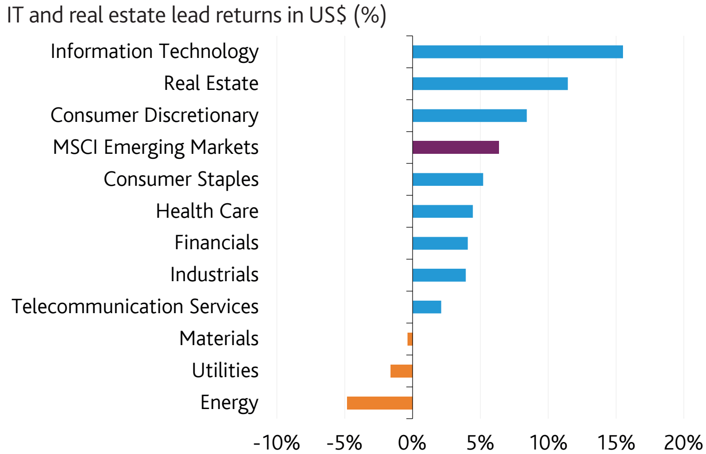
Credit growth moderating (%, year over year or YoY)



Sources: HSBC, CEIC, March 2017. For illustrative purposes only.

Chart 4: IT drives performance in 2Q

IT and real estate lead returns in US$ (%)



Source: Bloomberg, MSCI, June 30, 2017. For Illustrative purposes only. No assumptions regarding future performance should be made.
PAST PERFORMANCE IS NOT A GUIDE TO FUTURE RESULTS.

Contact us

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Open Monday to Friday 9am-5pm (ET)

About Aberdeen Emerging Markets Smaller Companies Opportunities Fund, Inc.

The Fund seeks long-term capital appreciation. The Fund's investment policy is to invest at least 80% of the Fund's net assets in equity securities of emerging market smaller company issuers. The principal investment objective of the Fund is long-term capital appreciation through investing primarily in equity securities of emerging market smaller company issuers.

Let us help you uncover the potential opportunities with the expertise we have built in emerging markets.

Ref: US-110917-45244-2
027364-0817-PHL
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