Equity Market Surprise In 2016?

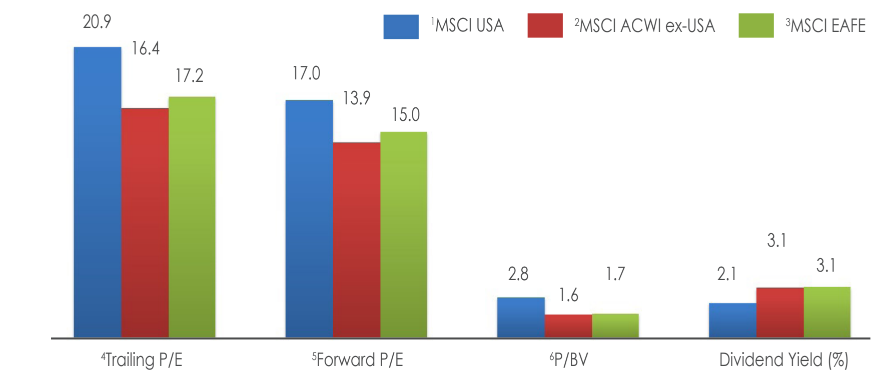
After underperforming in recent years, and being buffeted by last year's heightened volatility, we believe international equity markets could deliver a positive surprise in 2016. Though the global economy remains in a slow growth phase, we see tailwinds that could benefit international equity investors over the next year, and possibly longer. Continuing quantitative easing by major central banks, moderate improvement in global economic growth, as well as low energy and commodity prices are the major factors that could lift international equity prices.

We believe these trends have gained enough momentum to counter investor anxieties about interest rate hikes by the U.S. Federal Reserve and slower growth in emerging economies. In addition, valuations of international equities have become more favorable and the risk-reward tradeoff is more attractive now for long-term investors.

KEY TAKEAWAYS

Though the global economy remains in a slow growth phase, we see tailwinds that could benefit international equity investors over the next year, and possibly longer. Continuing quantitative easing by major central banks, moderate improvement in global economic growth, as well as low energy and commodity prices are the major factors that could lift international equity prices.

Foreign equities appear more attractively priced vis-a-vis U.S. stocks



[1] The MSCI USA Index is a free float-adjusted market capitalization-weighted index that is designed to measure large and mid cap US equity market performance.
[2] The MSCI All Country World ex US Index is a free float-adjusted market capitalization-weighted index of 47 countries, including developed and emerging markets.
[3] The MSCI EAFE Index is a free float-adjusted market capitalization-weighted index of 21 developed markets excluding the U.S. and Canada.

[4] Trailing price-to-earnings ratio. A stock's trailing price earnings multiple is its current price divided by the per-share earnings for the last 12 months.
[5] Forward price-to-earnings ratio. A stock's forward price earnings multiple is its current price divided by the expected per-share earnings for the next 12 months.
[6] Price to Book Value ratio. A stock's price to book value is its current price divided by the latest quarter's per-share book value.

Data source: MSCI. As of November 30, 2015

WORLD ECONOMY ADJUSTING TO A LOW-GROWTH ENVIRONMENT

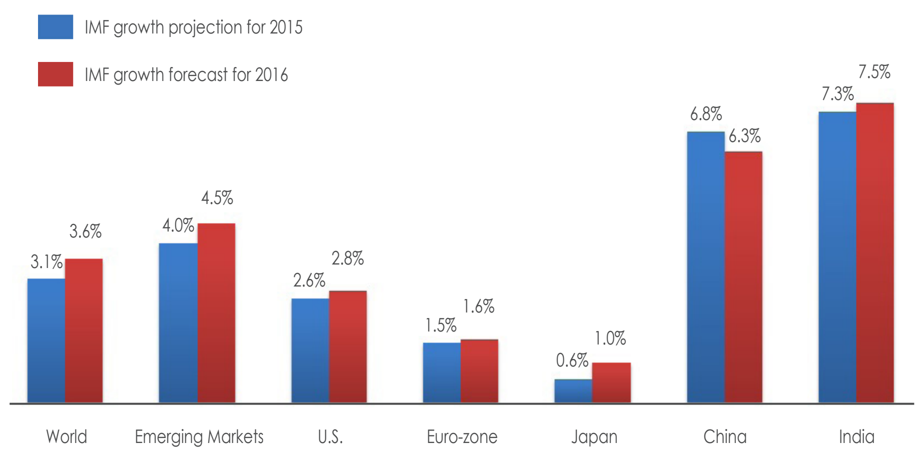
It has become evident in recent years that the global economy has entered a slower growth phase and is unlikely to regain annual expansion rates in excess of 5% anytime soon. China and other large emerging economies that powered global growth during the last decade have slowed. This has in turn deflated the 'Commodity Super Cycle' and weakened the economies of resource exporters, including developed countries such as Canada, Australia and Norway. Delayed policy support and structural challenges have restricted growth in the Euro-zone and Japan. Even in the U.S., the current global growth engine, the pace of expansion is slower when compared to previous recoveries.

Nevertheless, slower global growth is not necessarily negative for equity investors. It is true that the downshift from vigorous growth led to increased investor fears and market volatility, as governments and central banks rolled out support measures and corporations refined their business strategies to survive in the new environment. This phase of adjustment is probably near its end as aggressive quantitative easing has revived the major economies and global economic growth is expected to see moderate gains starting this year.

The International Monetary Fund (IMF) now expects global growth to accelerate in 2016, relative to last year, helped by the large developed countries. The U.S., Euro-zone, and Japan are expected to expand at a faster pace, as improved consumer sentiment lifts domestic spending. Important economic indicators, including the unemployment rate, wage growth, and credit demand, are all currently moving in the right direction in these countries. Downside risks, such as budget cuts, sovereign defaults, and lack of political and policy consensus, have also eased considerably when compared to recent years.

The IMF now expects global growth to accelerate in 2016, relative to last year, helped by the large developed countries. The U.S., Euro-zone, and Japan are expected to expand at a faster pace, as improved consumer sentiment lifts domestic spending. Downside risks, such as budget cuts, sovereign defaults, and lack of political and policy consensus, have also eased considerably when compared to recent years.

Global economic growth is projected to accelerate in 2016



Data source: International Monetary Fund

QUANTITATIVE EASING LIKELY TO LIFT EUROPE AND JAPAN

Despite the revival, aggregate growth rates in the Euro-zone and Japan remain below the targets set by the respective central banks. In addition, low input costs and surplus capacities have restrained current inflation trends well below the desired levels. It is also important for the Euro-zone and Japan to keep their currencies weak to help exports, and quantitative easing is typically an effective tool to achieve that. Accordingly, the European Central Bank (ECB) and the Bank of Japan are expected to sustain their bond purchases, or even expand these programs this year.

The ECB recently announced that it will continue its bond purchases through March 2017, against the earlier schedule of September 2016. If inflation expectations do not move closer to the ECB's target, it is possible that the central bank will increase its monthly bond purchases from the current €60 billion. The Bank of Japan could also follow a similar path if the country's growth rate and inflation trends continue to fall short of targets. Quantitative easing programs have so far been beneficial for equity markets, most notably in the U.S., and could continue to support European and Japanese markets this year.

Quantitative easing programs have so far been beneficial for equity markets, most notably in the U.S., and could continue to support European and Japanese markets this year.

Among Emerging Markets, China is successfully making the transition to a consumer-driven economy and India has a reform-oriented government that is gradually introducing policy measures aimed at boosting long-term growth.

CHINA AND INDIA LIKELY TO SHINE AMONG THE EMERGING MARKETS

Despite the persistent pessimism about China's future growth, we believe the country is successfully making the transition to a consumer-driven economy. The share of services in China's aggregate economic output now exceed 50%, a significant shift from the last decade when manufacturing and exports dominated. In addition, the services sector in China is growing faster than other sectors and should support aggregate growth in the coming years. Domestic demand in China continues to increase at a healthy pace, helped by the monetary easing and moderate fiscal stimulus measures.

India is expected to see the fastest growth rate among the large emerging economies in 2016 and beyond. The country now has a reform-oriented government that is gradually introducing policy measures aimed at boosting long-term growth, especially in the manufacturing sector. What's more, India is also one of the largest beneficiaries of low oil prices. Reduced energy import costs and lower subsidies have helped the country to improve its external trade and fiscal deficits substantially. Lower inflation risks should allow India's central banks to bring down interest rates further this year.

LOW FUEL COSTS AND INTEREST RATES TO BOOST CONSUMER SPENDING

After a short-lived rebound during the second quarter of 2015, crude oil prices have slipped again and are now at the lowest in a decade. Average retail gasoline prices have dropped below $2 per gallon in many states in the U.S., a significant decline when compared to recent years. Similarly, fuel prices in Europe are now at the lowest in more than six years. Though savings from reduced fuel costs for an average household in the developed countries are now substantial, the positive impact on consumer spending was lower than expected in 2015. However, strengthening labor markets should encourage more consumers to spend their savings from low fuel prices this year.

Oil prices are at their lowest levels in a decade

Weekly Europe Brent spot price in $ per barrel

Data source: U.S. Energy Information Administration

In addition, despite the rate increase by the U.S. Fed, borrowing costs remain exceptionally low for consumers in the developed markets. Interest rates in Europe and Japan are expected to remain around the current levels while only modest increases are likely in the U.S. Improving economic conditions, corporate earnings, and wage growth should reduce the risk of loan losses and encourage banks to lend more.

CURRENCY DRAG ON RETURNS LIKELY TO EASE FOR INTERNATIONAL INVESTORS

International equity investors were hurt in recent years by the decline of most major currencies against the U.S. Dollar. With the U.S. Fed being the only major central bank in the developed world likely to raise interest rates, there are apprehensions that the dollar could strengthen further. However, we believe the negative impact of currency movements on international equity returns will not be as significant in

2016 when compared to recent years. First, the substantial losses of major currencies against the dollar could limit the extent of further weakness. Second, additional rate hikes by the U.S. Fed are likely to be measured and spread out over a longer period. This should restrict the widening of interest rate differential between the U.S. and other countries, and limit further currency declines. Finally, the positive economic effects of cheaper currencies, such as more competitive exports, could boost earnings further. This may lift potential U.S. Dollar returns from international equities, after adjusting for currency movements, to attractive levels.

To conclude, we believe the current favorable economic and monetary policy trends make international equities quite attractive for long-term investors. The valuations of international equities, emerging market equities in particular, are inexpensive relative to U.S. domestic equities. If the positive trends highlighted earlier are sustained, 2016 could turn out to be a year when international equities reverse their long period of underperformance and start rewarding patient investors.

Strengthening labor markets should encourage more consumers to spend their savings from low fuel prices, which are now at their lowest levels in a decade.

This publication is for informational purposes only. This publication is not intended to provide tax, legal, insurance or other investment advice. Unless otherwise specified, you are solely responsible for determining whether any investment, security or other product or service is appropriate for you based on your personal investment objectives and financial situation. You should consult an attorney or tax professional regarding your specific legal or tax situation.

The information contained in this publication does not, in any way, constitute investment advice and should not be considered a recommendation to buy or sell any security discussed herein or to invest in any particular market or country. Past performance is not indicative of future results. It should not be assumed that any investment will be profitable or will equal the performance of any security mentioned herein. Thomas White International, Ltd., may, from time to time, have a position or interest in, or may buy, sell or otherwise transact in, or with respect to, a particular security, issuer or market on our own behalf or on behalf of a client account. All holdings are subject to change at any time.

FORWARD LOOKING STATEMENTS

Certain statements made in this publication may be forward looking. Actual future results or occurrences may differ significantly from those anticipated in any forward looking statements due to numerous factors. Thomas White International undertakes no responsibility to update publicly or revise any forward looking statements.

Are You Positioned for a World of Opportunities?

"Our strategy is to seek smoother, more consistent returns by stressing excellent local stock selection as opposed to betting on major country and sector moves.

To succeed in this approach, we have built an exceptional global research team that uses our proprietary techniques to identify the most attractive stocks in each of the major regions of the world. This in effect is our trump card."

— Thomas S. White, Jr., Portfolio Manager

THE THOMAS WHITE DIFFERENCE

Thomas White International manages $2.1 billion in assets across multiple global, international and domestic equity mandates. The diverse client base spans public, corporate, endowment, Taft-Hartley, and separately managed account platforms.

We use Proprietary Research. At Thomas White, we value international stocks within distinct valuation groups based on region, industry, sector, or country, which provide us with an extensive range of investment opportunities.

Our investment process differs from the crowd. Our approach to valuing common stocks combines the execution of thorough historical studies, with the application of in-depth fundamental securities analysis. Valuing global stocks in nearly 50 countries, this industry-based stock selection process employs tailor-made valuation frameworks refined and tested over the 40-year history of the Thomas White organization and its predecessors.

Our veteran analysts on average have more than seventeen years of experience working together as a team. Our research and analysis is generated by our professionals, both in Chicago and in our Asia office in Bangalore, India, most of whom have spent their entire careers at Thomas White.

Our investment approach seeks to benefit from buying undervalued stocks and selling them when they return to fair value. Our analysts find that investors tend to overvalue a company against its industry peers when the intermediate business environment is favorable, producing strong earnings growth and then undervalue a company when the environment depresses its business outlook. This pattern is a reflection of human behavior — it occurs in every industry and country around the world. It is this phenomenon that explains a stock's wide price swings above and below its intrinsic value as a business.

For more information, please contact:

Gabriel J. McNerney, CFA
(312) 663-8318
gmcnerney@thomaswhite.com
thomaswhite.com