

Why Invest in International Equities



...And Overcome Home-Country Bias?

As a global investment manager, with a long history of managing both U.S. and non-U.S. strategies, we see three reasons for investors to consider broadening a strictly U.S. portfolio. In addition, recent academic research presents further evidence why, in the long run, overcoming home-country bias may make good investment sense.

Three Good Reasons for International Investing

First of all, there is a world of investment opportunities overseas. Second, many U.S. brands are known worldwide (e.g., IBM or Coca-Cola), while some common U.S. brands are actually owned by non-U.S. companies (e.g., A&W Root Beer or Aquafresh toothpaste).¹ Third, some foreign stocks can be cheaper than U.S. stocks, relative to earnings; so investing internationally may earn U.S. investors more for their dollar.

1 Too Large to Ignore: With over two-thirds of the world's market capitalization outside of the United States, the magnitude of the international investment opportunity set is too big to ignore.

2 Access to Familiar Brands and World-Class Companies: Limiting a portfolio to U.S. companies minimizes its exposure to the breadth of the developed world's well-known brands and high-returning companies.

3 Getting More for Your Investment Dollar: When comparing certain international companies with their U.S. counterparts, the result may be lower valuations and higher return on equity, evidence that some international equities represent better value.

1 Why Ignore a World of Opportunities Overseas?

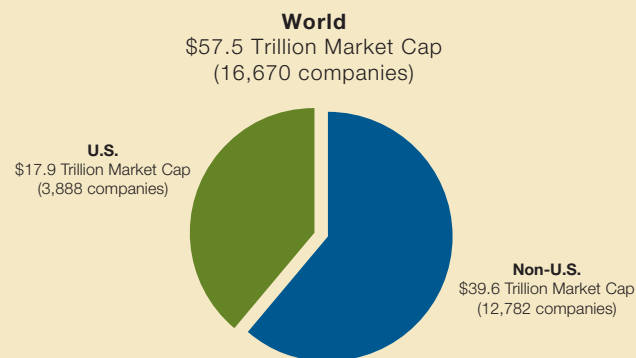
Many U.S. investors historically have restricted their investing activities to domestic markets. With the United States' solid regulatory environment, highly efficient and liquid securities markets, and powerful economy, that comes as no surprise. However, the interest of U.S. investors in international markets has grown, as businesses have become increasingly global. In fact, the U.S. component of global stock market capitalization has contracted, as the portion representing the rest of the world has expanded. Today, there are approximately three times as many foreign companies (12,782) as U.S. companies (3,888),² which indicates that by looking outside the United States, investors greatly expand their pool of potential opportunities.

2 Why Limit Access to the World's Top-Ranking Brands?

Rapid globalization of world trade has aided in the rise of multinational giants—companies that derive much of their revenue from global economies other than that of their home country. Also because of globalization, where a corporation is headquartered has become less relevant. As U.S. investors seek out the dominant players in a particular industry or market sector, they are finding that many of these market leaders are headquartered overseas. This is supported by the fact that where a company is headquartered has little effect on its overall business, as foreign sales have grown to become a significant part of many companies' total sales (as seen in the chart on the next page).

THE WORLD IN NUMBERS²

Expanding International Opportunity Set



Source: Compustat, Worldscope, December 31, 2006.

LEADERSHIP IN MANY INDUSTRIES HAS BECOME GLOBAL³

A portfolio consisting solely of U.S. stocks would miss out on the potential of some of the world's industry leaders.

Autos	Food	Oil
Toyota	Coca-Cola	ExxonMobil
Honda	PepsiCo	BP
Volkswagen	Unilever	Total
Pharmaceuticals	Telecommunications	Utilities
Johnson & Johnson	AT&T	E.On
Pfizer	Verizon	Iberdrola
GlaxoSmithKline	Telefonica	Enel

Source: FactSet. Industry leaders as measured by market capitalization (\$USD), as of June 30, 2007. Those highlighted in orange represent non-U.S.-based companies.

3 Why Not Get More for Your Investment Dollar?












As consumers, we generally evaluate products based on price, quality, and effectiveness, rather than by their country of origin. If investors evaluated businesses in the same way, they would find that there are opportunities to invest in high-returning and comparatively inexpensive companies overseas. In general, the importance of focusing on the creation of shareholder value is spreading to boardrooms around the globe, particularly in Europe, where corporations have undergone more than a decade of cost cutting. Although these positive changes have led to steadily improving returns on invested capital, shareholders have yet to be fully rewarded by higher stock market multiples, meaning that world-class companies can be found that are financially productive yet trade at a discount to their U.S. peers. The chart at top right supports this notion.

Why Overcome Home-Country Bias?

We have outlined three good reasons why, over the long term, it would be prudent for U.S. investors to add international stocks to their U.S. equity portfolios. There is another reason to overcome home-country bias and invest internationally.

“Home bias is the most persistent puzzle in international finance,” notes a 2005 academic study. The study also points out that while investors in the United States and from around the world tend to have a bias for their home-country markets,

HOME COUNTRY HAS LITTLE EFFECT ON A COMPANY'S BUSINESS⁴

International Stock	Country	Foreign Sales (%)
Nokia	 Finland	99
AstraZeneca	 U.K.	94
Vodafone	 U.K.	83
BP	 U.K.	79
Nestlé	 Switzerland	73
Total	 France	72
GlaxoSmithKline	 U.K.	70
Novartis	 Switzerland	65
Royal Dutch	 Netherlands	57
HSBC	 U.K.	42
Royal Bank of Scotland	 U.K.	16

COMPARING DEVELOPED-MARKET VALUATIONS⁵

Index	P/E	P/BV	P/CF	ROE (%)
MSCI US Index	17.8	3.0	12.3	16.7
MSCI EAFE Index	16.0	2.5	10.4	15.3
MSCI Europe Index	14.8	2.5	10.2	17.2
MSCI Japan Index	20.6	2.7	10.5	16.1

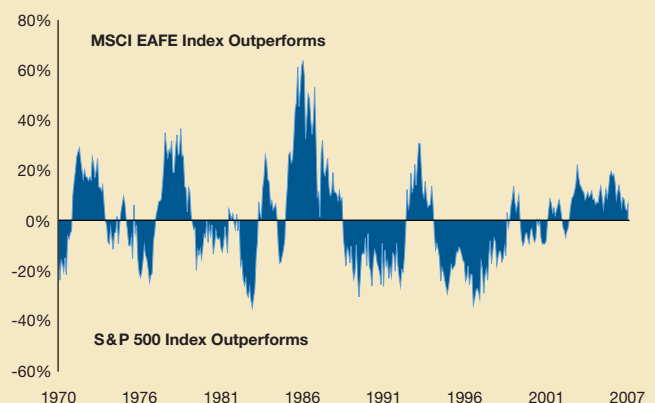
As of June 30, 2007. Source: FactSet. Valuation characteristics are trailing. Please note that investors cannot invest in an index.

there is no risk or return advantage: “By investing largely in their home country, typical investors accept a far from optimal combination of portfolio returns and portfolio volatility.”⁵ Why?

The principle of diversification holds that allocations to uncorrelated markets (across many sectors and asset classes) should smooth out a portfolio's volatility over time. Thus, a portfolio holding both U.S. and international stocks should perform as well as or better than a portfolio invested solely in U.S. stocks with less volatility. This principle, however, has been challenged by the increasing correlation between U.S. and international equity markets, minimizing the risk-reducing potential of international investments. Countering this concern, a study entitled *International Diversification: Have We Missed the Forest Through the Trees?*⁶ concluded that although international stocks do not greatly reduce volatility during short time periods, over the long term, global diversification does a good job of lowering a portfolio's overall volatility of returns.⁷

Supporting this is the fact that, historically, returns of U.S. and international equities (represented, respectively, by the S&P 500 Index and the MSCI EAFE Index) have moved in opposing directions, as seen in the following chart.

RETURNS ARE CYCLICAL⁸



Lazard Is Your Passport to International Markets

At Lazard Asset Management, highly experienced portfolio management teams, along with our global research platform of analysts, focus on both U.S. and international companies, seeking to identify financially productive companies at good valuations. With offices around the world, Lazard has a long history of investing prudently wherever value can be found.

Note that how and how much one should invest internationally ought to be part of an important conversation between investors and their financial advisors.

Did you know that international companies owned these familiar brands?⁹

NESTLÉ

Domiciled in Switzerland, Nestlé's many brands include:

Alpo | Butterfinger | Carnation
Instant Breakfast | Coffee-Mate |
Deer Park | Dreyer's Ice Cream |
Fancy Feast | Friskies | Juicy Juice
| Lean Cuisine | Mighty Dog |
Nescafé | Nestea | Nestlé Crunch
| Nestlé Toll House | Poland Spring
| PowerBar | Purina ONE | Rolo |
Smarties | Stouffer's | Taster's
Choice | Tidy Cats

CADBURY SCHWEPPE'S

Domiciled in the United Kingdom, the company's familiar brands (other than its chocolate candy) include:

7 UP | A&W Root Beer | Bazooka
Bubble Gum | Bubblicious |
Canada Dry | Celestial Seasonings |
Certs | Chiclets | Dentyne | Diet
Rite | Dr. Pepper | Halls |
Hawaiian Punch | Hires Root Beer |
Mott's | Nantucket Nectars | Spring
Valley | Squirt | Sunkist Orange |
Trident | Welch's | Yoo-Hoo

UNILEVER

Also domiciled in the United Kingdom, Unilever's familiar brands include:

Ben & Jerry's | Birds Eye | Breyers
| Dove | Good Humor | Hellmann's
| Klondike Bars | Knorr | Lawry's
| Lever 2000 | Lifebuoy | Lipton |
Pond's | Popsicle | Q-tips | Ragú
| Suave | Skippy | Slim-Fast |
ThermaSilk | Vaseline | Wish-Bone
| Wisk

NOTES:

- 1 A & W Root Beer (Cadbury Schweppes), Aquafresh (GlaxoSmithKline).
- 2 As of December 31, 2006. Source: FactSet. Includes companies with a market capitalization of US \$100 million or greater.
- 3 As of June 30, 2007. Source: FactSet. Industry leaders as measured by market capitalization (\$US new explanation).
- 4 As of June 30, 2007. Source: FactSet.
- 5 As of June 30, 2007. Source: FactSet. Please note that an investor cannot invest in an index. Indices are unmanaged and have no fees. The performance quoted represents past performance. Past performance does not guarantee future results.
- 6 Warren Bailey, Cornell University, Johnson Graduate School of Management, Alok Kumar, University of Notre Dame, Mendoza College of Business, David Ng, Cornell University, Department of Applied Economics and Management, and *Home Bias: Evidence from U.S. Individual Investors*, November 8, 2005.
- 7 "International Diversification: Have We Missed the Forest for the Trees?" *New York Times*, Study conducted by AQR Capital Management, February 27, 2005.
- 8 As of June 30, 2007. Source: FactSet. Please note that an investor cannot invest in an index. Indices are unmanaged and have no fees. The performance quoted represents past performance. Past performance does not guarantee future results.
- 9 Sources: www.nestle.com/Brands/Brands.htm, www.cadburyschweppes.com/EN/Brands, and <http://www.unileverusa.com/ourbrands>.

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