

Accessing Global Growth By John P. Calamos, Sr.

■ he aspiration of many executives of middle market companies is to "go global" - taking their company's products and services to an international customer base. Expanding globally can mean not only an increased revenue stream but also a more diverse client base. As an investment firm we agree, and feel there is an excellent opportunity to continue to grow our business not only in the United States but globally. We recently opened an office in London and are contemplating an office in Hong Kong. The same can be said about the portfolios of investors. We feel portfolios should also reflect a more global theme. We believe a successful asset allocation strategy going forward should be both global and long-term in its perspective, but highly individualized in its implementation. Long-term trends in the global economy are an important factor in asset allocation because they provide a foundation and context for investment opportunities and asset allocation decisions. For example, although the U.S. economy has not fully recovered, we see many signs that point to a slow-but-positive economic growth. Corporate America continues to demonstrate innovation and resiliency. We're encouraged by many positive earnings announcements – the result of exciting global business plans.

While we believe the U.S. will continue to be a leader in the global economy, the most compelling growth story of the future centers on the emerging markets. Clearly, emerging economies are no longer emerging – they have arrived – and the growth of the middle class around the world is a compelling long-term investment theme. With a rapidly expanding middle class and extensive infrastructure build-out projects, emerging economies are stoking demand for a wide range of goods and services. These are trends that we believe will set the stage for the growth of companies not only in those emerging economies but in developed nations, as well.

According to the Economist, emerging markets already rep-

resent more than half of global GDP at purchasing power parity (which assumes that a sum of money has the same purchasing power across countries). But from an investment point of view, the emerging markets currently comprise less than 15% of investors' exposure in international equity market cap. This may present an additional opportunity as investors will shift globally and adjust their asset allocations to better reflect global GDP. Additionally attractive demographics, a growing middle class, improved governance and generally strong fiscal policies all support a secular growth story that is likely to persist for several decades. On the other hand, emerging markets' volatility causes many investors to be concerned about investment risks within emerging markets equities. But as is always the case, where there is volatility there is opportunity.

The Emerging Middle Class Consumption

It is clear that the emerging economies no longer muster the same connotation that they once did. Since the Asian crisis of 1997, there have been steady improvements in the fiscal policies of many emerging economies. Dramatic increases in foreign currency reserves, less debt, lower inflation, smaller budget deficits and higher GDP growth are among the factors providing a solid foundation for sustainable economic growth, providing a long-term opportunity that we feel should be considered in your asset allocation. This shift may be not merely a tactical market timing play but rather a substantial long-term opportunity. Many factors contribute to this favorable long-term global theme. A key contributor to the strength of emerging markets is favorable demographics. Future population growth is expected to occur mainly in emerging economies, as populations in the developed economies continue to age. The size of the middle class in emerging economies is projected to far outnumber the middle classes in developed economies within the coming decade. These are the future consumers all over the world,



and consumer goods. They want to emulate the success of the growth of the U.S. middle class over the last 100 years. This is surely a positive for the world and for world peace, as well. Globally, the middle class is roughly 1.8 billion people. A recent estimate by the Organisation for Economic Co-operation and Development (OECD), a Paris-based economic think tank, suggests the middle class could rise to 3.2 billion by 2020 and 4.9 billion by 2030. Of this growth, roughly 85% will come from Asia ex-Japan. This growth is matched by increases in the purchasing power of the middle class. Another OECD estimate shows global middle class spending increasing from \$21 trillion to \$56 trillion by 2030, in constant 2005 dollars. The shift in middle class purchasing power across regions is illustrated in Figure 1. As this growing wave of the emerging middle class moves East and South, it brings with it the ideas and innovation that will drive investment, consumption and growth opportuni-

OECD predicts a significant shift in the composition of the worldwide middle class in the next 30-40 years. According to Figure 1, the United States currently comprises about 20% of the total middle class population, but is expected to be only 3-5% of the total by the year 2048. This is not bad news for the United States, but rather good news for global economies as consumer spending and standards of living increase around the world.

Impact on Asset Allocation

The Opportunity of Equities. Today, investors in the U.S. need to think more globally than in the past with their asset allocation and, in particular, within their equity allocation. Investors typically choose equities for their long-term capital appreciation potential. But in times of uncertain economic growth, investors have shied away from equities, particularly those issued

by growth-oriented companies, because of concerns that the issuing companies may struggle. Many investors have also sold equities due to fears about economic recovery and volatility. As a result, the prices of many growth-oriented equities have fallen to levels that are extremely attractive to us. We believe investors are overlooking the more encouraging news in the economy, particularly the strength in emerging markets, as well as the fundamentals of many leading businesses. For us, these factors make a strong case for equities.

The global economy offers a breadth of growth opportunities. Innovative companies can be found in all markets. It is important to focus on what a company does, not where its headquarters are located. Investors should seek to access companies that are participating in the growth of emerging market consumer consumption. These companies are often based in developed markets, including the United States.

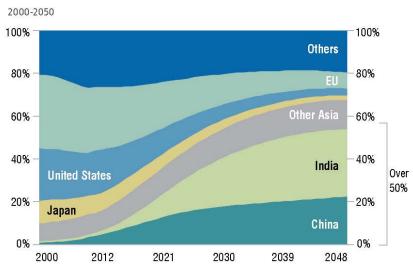
Rethink the role of emerging markets. In past decades, emerging markets were considered a secondary or even tactical element within an asset allocation. As they become an increasingly important driver of the global economy, they may warrant a more core role within an equity portfolio. However, particularly within core allocations, risk management remains paramount, particularly as the risks of investing in emerging markets may be greater than those of investing in developed markets. Look for funds with strategies in place for managing volatility. Investors need to distinguish between companies in emerging markets, often a more volatile investment, and global companies that can access the emerging market middle class consumption.

Where We See Growth

Based on our view of the global economy, we believe a number of themes will create growth opportunities for companies all over the world.

Wealth Management

FIGURE 1. GLOBAL MIDDLE CLASS CONSUMPTION



Source: OECD Development Centre, Working Paper No. 285, "The Emerging Middle Class in Developing Countries," Homi Kharas.

These are the future consumers all over the world, striving for upward mobility, better education, individual liberty and consumer goods. They want to emulate the success of the growth of the U.S. middle class over the last 100 years.

Theme: Demand for technological innovations

We expect technology to be a leading sector for the next decade, as corporations all over the world continue to invest in ways to enhance productivity in a highly competitive global environment. We also believe consumers will continue to seek out devices such as cellular phones and tablet computers that help them stay connected to one another and to information. We believe the rapidly growing base of emerging market consumers will be a particularly important market for technology innovators.

Theme: Global infrastructure build-out and re-building

As they prosper, emerging markets are embarking on aggressive infrastructure projects, while government stimulus in countries like the U.S. has been directed to infrastructure improvements. Companies in the industrials, energy and materials sectors can capitalize on these themes.

Theme: Prosperity of emerging markets consumers

As emerging markets consumers look to improve their quality of life, we believe companies in the consumer discretionary and consumer staples sectors are positioned to benefit.

Theme: Asset reflation

We believe governments in developed markets will continue to print money and buy assets that have fallen in value as a way to keep their economies moving. This strategy leads to currency devaluation, which in turn inflates the cost of other assets, such as gold and energy.

In conclusion, we believe the current landscape, even with its challenges, offers exciting choices for investors who want to look longer term and – like the business they manage – re looking to broaden their horizons to discover opportunities around

the globe.

Note: There is no assurance that the views and investment opportunities, discussed above will come to pass or provide positive investment results. The opinions referenced are as of the date of publication and are subject to change due to changes in the market or economic conditions and may not necessarily come to pass. Information contained herein is for informational purposes only and should not be considered investment advice. Equity securities are subject to "stock market risk" meaning that stock prices in general (or in particular, the prices of the types of securities in which a fund invests) may decline over short or extended periods of time.

As a result of political or economic instability in foreign countries, there can be special risks associated with investing in foreign securities, including fluctuations in currency exchange rates, increased price volatility and difficulty obtaining information. In addition, emerging markets may present additional risk due to potential for greater economic and political instability in less developed countries.

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