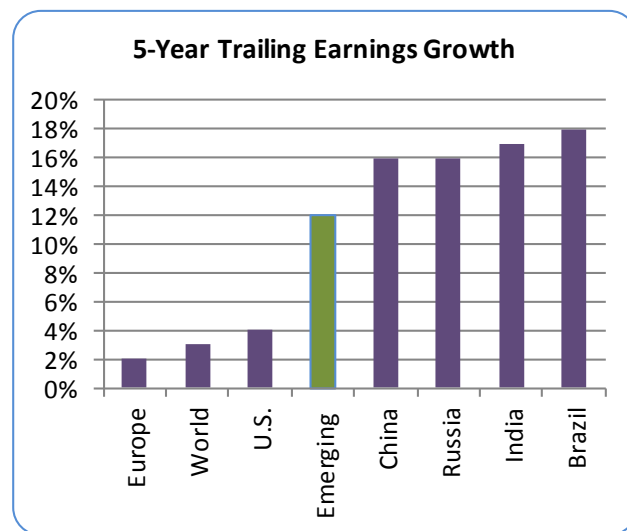
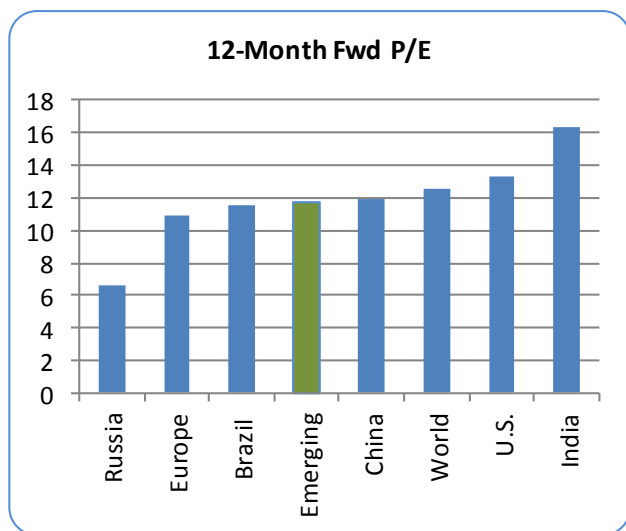




Emerging Markets

As part of our diversification strategy, Johnson Investment Counsel often utilizes international equities in portfolios as a means to obtain exposure to global markets and non-U.S. dollar denominated assets. Recently, international investing has been out of favor due to the debt crisis in Europe and a waning global growth environment. Within the context of international investing, there are two primary segments: developed markets and emerging markets. By definition, the growth profile of emerging markets has always been appealing to us as investors. Countries like the U.S., not to mention Europe, are in the mature stage of the growth cycle and simply will not keep pace with emerging markets from a growth standpoint. While we have obtained exposure to emerging markets through some of the international mutual funds that we own and also indirectly through larger, multi-national companies, valuation has been a deterrent to direct capital investment in recent years. Weakness in the markets over the past several months has provided a window of opportunity, where emerging markets are now trading at a discount to their developed markets counterpart.



Source: UBS Research, Goldman Sachs Global Asset Management

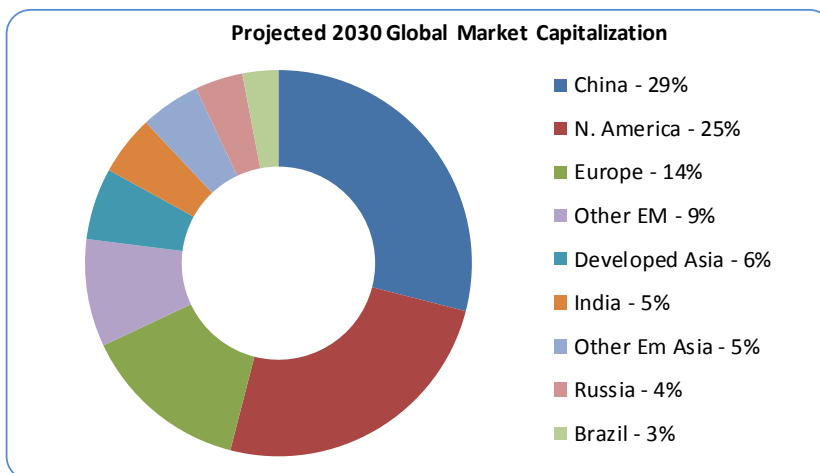


The fundamentals for the emerging markets include not only a strong population base, but also an expanding consumer base. While those two factors would logically go hand-in-hand, a growing middle class in these countries is a new development and key investment theme. The World Bank expects the middle class in emerging markets to expand by 800 million people through 2030 with Brazil, Russia, India and China (BRIC) expected to have 74% more middle and upper-middle class members by 2015. Discretionary income, once the luxury of a few, will now be enjoyed by many, which will drive economic growth.

| Emerging Markets Growing Consumer Base (Millions) | | | |
|---|------|------|----------|
| Country | 2010 | 2015 | % Change |
| China | 52 | 98 | 88.5% |
| India | 35 | 69 | 97.1% |
| Russia | 35 | 49 | 40.0% |
| Indonesia | 13 | 27 | 107.7% |
| Brazil | 14 | 20 | 42.9% |
| Turkey | 10 | 14 | 40.0% |
| Mexico | 8 | 11 | 37.5% |
| South Africa | 5 | 6 | 20.0% |
| Total | 172 | 294 | 70.9% |

Source: Boston Consulting Group, Research Magazine

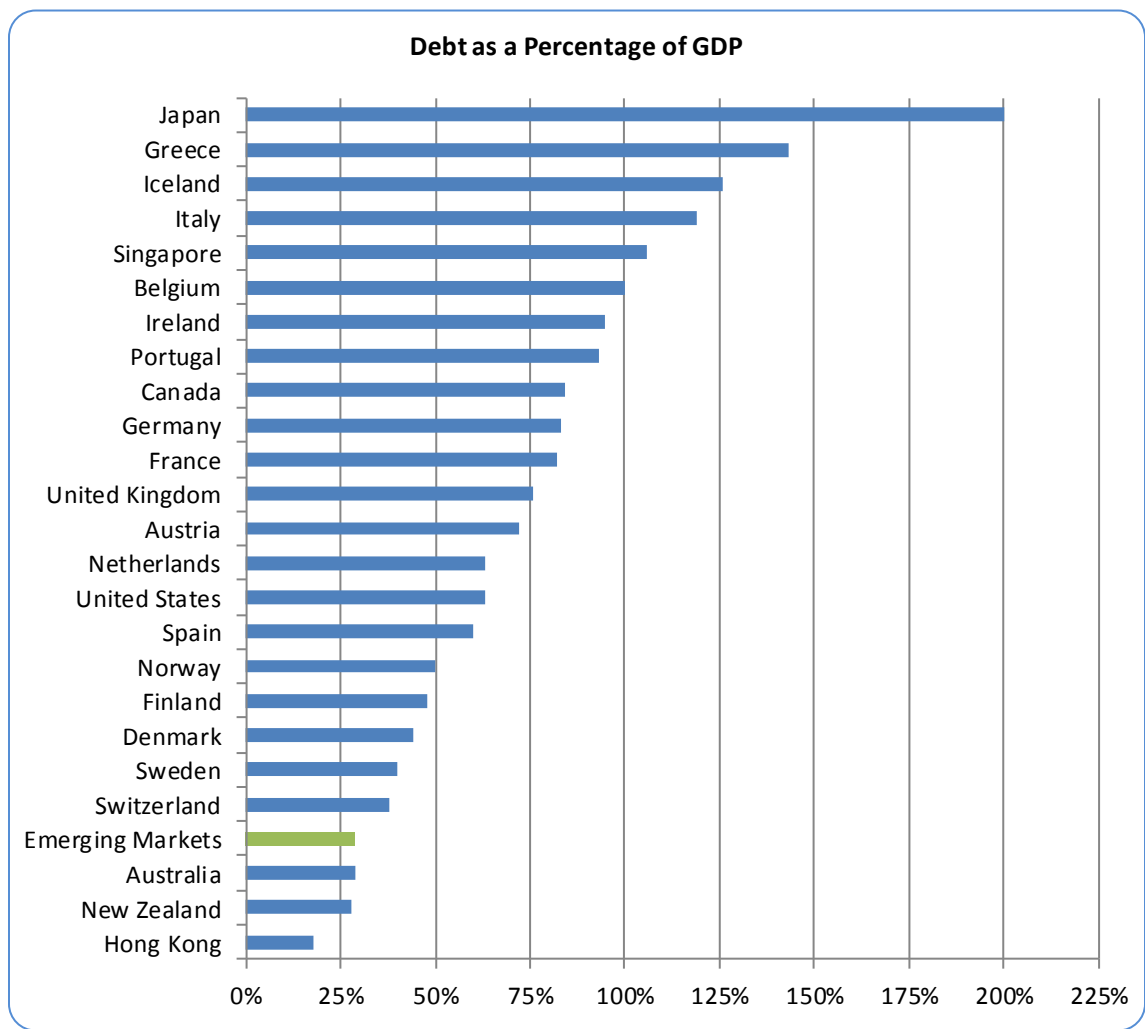
It is projected that by the end of the decade, the BRIC nations will grow to be as large as the U.S. from a gross domestic product standpoint. An example of this tremendous growth has been the change in the automobile market where China is now the largest market in the world. This growth in the emerging market consumer base will benefit not only their local economies, but global economies as well, including U.S. companies. Today, emerging markets represent two-thirds of the world’s population and foreign exchange reserves, one-third of the population, but only 13% of the equity market capitalization (source: Aberdeen Asset Management). It is projected that by 2030, emerging markets will represent 55% of global market capitalization.



Source: FactSet, IMF, Worldbank, World Federation Exchange, Goldman Sachs Global ECS Research estimates



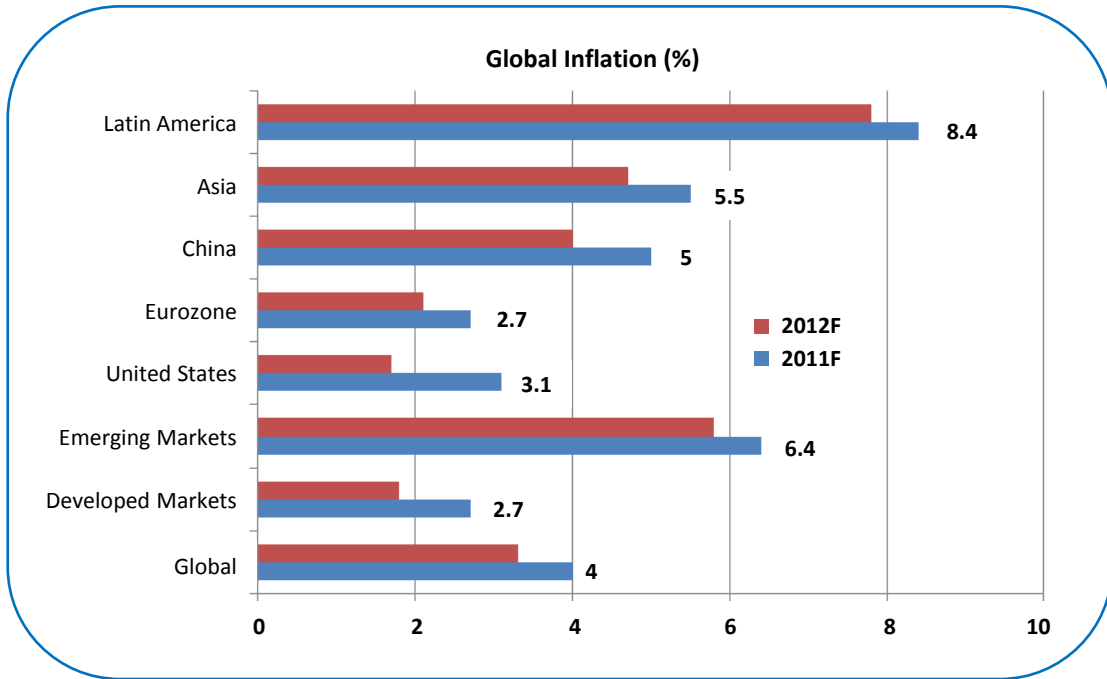
The credit fundamentals of the emerging market space have also made impressive strides over the last 20 years. A comparison of external debt to gross domestic product (GDP) reveals that the emerging markets are positioned in better fashion relative to developed markets, with average debt/GDP ratios of 29% vs. 90%, respectively. This is due in part to the export nature of emerging markets as well as more prudent management of currency reserves and entitlement spending.



Source: Bloomberg



With all of these positives, the emerging markets do carry risks. Their volatility has been higher than developed markets and local inflation has at times resulted in a pause in the growth story.



Source: Citigroup; Anticipated global inflation

The emerging market space is also reliant on global consumption and as such, will swing with the cyclicality of the global economy. This also reinforces why valuation and entry points are so crucial in our timing of the implementation of emerging markets exposure into portfolios. It is our belief that the reward currently outweighs the risks and that with time, we believe that an allocation to emerging markets will enhance the long-term growth prospects of portfolios while increasing diversification.

Should you have any questions on emerging markets and its role in portfolios, please do not hesitate to contact your Portfolio Manager at 513.661.3100.