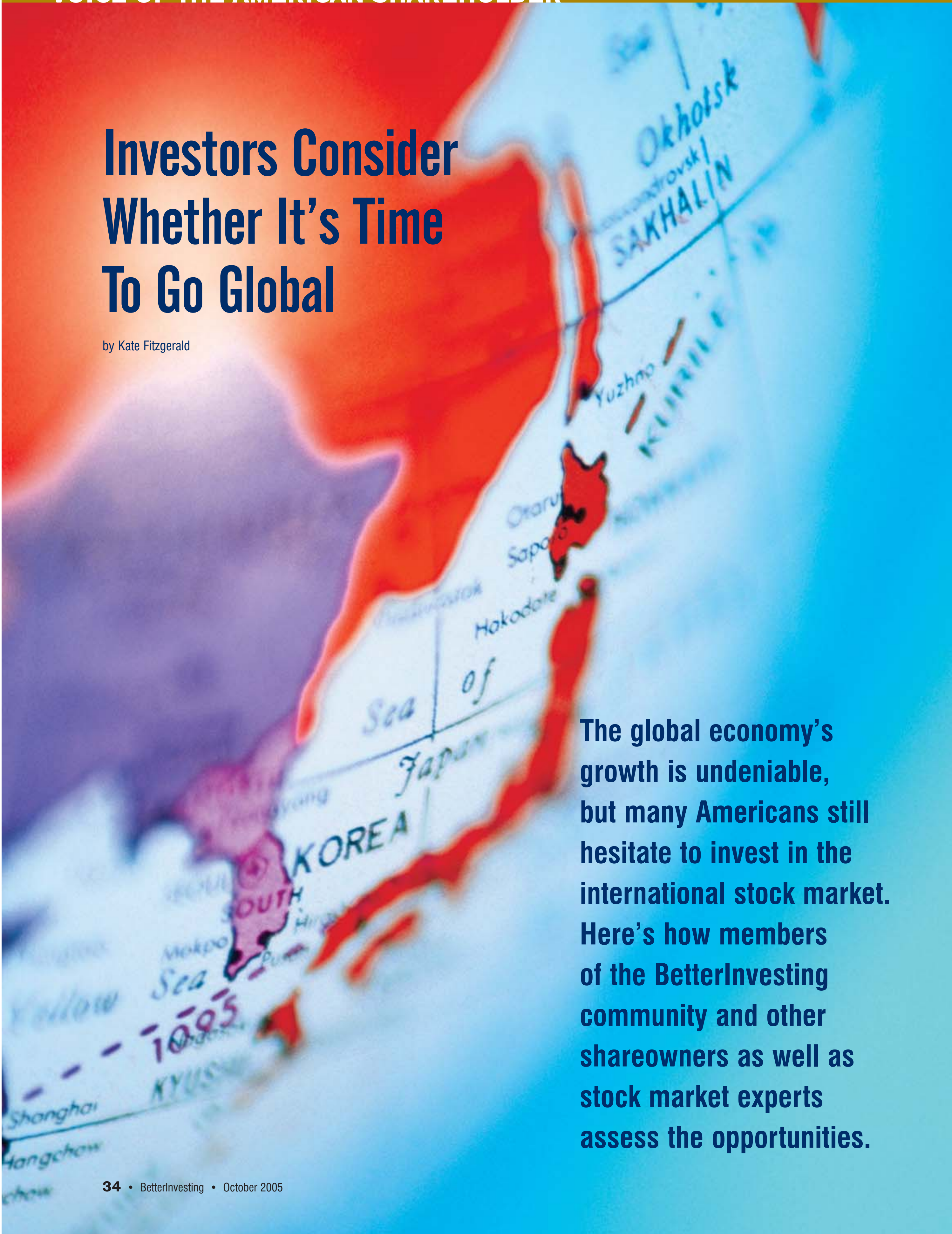


Investors Consider Whether It's Time To Go Global

by Kate Fitzgerald

The global economy's growth is undeniable, but many Americans still hesitate to invest in the international stock market. Here's how members of the BetterInvesting community and other shareowners as well as stock market experts assess the opportunities.

Headlines about China's explosive economy, the revaluation of China's yuan and America's role in an increasingly global economy have raised some questions for members of Denver's Rollin' Wagon Investment Club. They wonder if they're making the right moves, because the buzz surrounding international stocks suggests they should look overseas.

But so far, the 14-member club has taken little action on international developments, beyond discussing what's in the news, says Don Van Wyke. He's treasurer of the club, which has survived for 31 years primarily by avoiding rash actions, he says.

"We've evaluated our portfolio to assess our international exposure, and we're not making any significant changes in our portfolio," Van Wyke says. "But we know we need to watch China, and we realize that from now on we're dealing with an increasingly global economy."

The club's attitude parallels those of hundreds of investors polled by Harris Interactive in the most recent BetterInvesting Voice of the American Shareholder survey. Fifty-six percent of shareholders polled said they believe international investments will be important in the future, but just 33 percent said they feel comfortable making this type of investment.

Jacqueline Marazzi, one of 18 members of the Learn & Earn Investment Club in Escondido, Calif., says she's frankly uncomfortable with making international investments because of many warnings she has received from experts about its high risk. "Our club has discussed foreign investments, but it's not a direction we want to go," she says.

An Eye on the World

As intriguing as international investing sounds, it's unfamiliar territory to the average U.S. shareholder, and it's an area into which investors should proceed with caution. But at the same time, it's no longer possible to ignore the global economy, or the fact that if present trends continue, China's rapid economic growth may eventually leapfrog economies of the United States and Europe.

"Most people in the U.S. haven't considered investing internationally, but that's changing with the dollar's steady fall," says Axel Merk, manager of the Palo Alto, Calif.-based Merk Hard Currency Fund.

But Merk isn't saying that individual investors should jump into international stocks. Instead, he thinks shareholders should look closely at their portfolios to see how they're being affected by global developments, since the U.S. stock market is increasingly intertwined with international economies.

"Any discussion about world economic growth right now is actually about selling products to the U.S., the largest consumer market in the world," Merk says. If a domestic downturn causes Americans to cut spending, it will hurt not just U.S. companies but also those in China and elsewhere where growth depends on our buying power.

China is not the only wild card. As democracy continues to spread throughout the world, new free-market economies are springing up and creating new growth and investment opportunities on every continent.

But respected Wall Street advisers aren't advising American shareholders to rush out and invest in the upstart telecommunications companies of foreign republics. Instead, stock market analysts say investors should begin to view existing investments through a global lens so that they can make informed decisions about how individual companies and sectors are being affected by world political events and economic trends.

The Lure of International Stocks

Most U.S. shareholders participating in the most recent Voice of the American Shareholder survey agree that it's time to factor international stocks into their portfolios. The majority agree that international investments help diversify portfolios; they also help guard against a weak U.S. economy and could produce larger returns.

Given the fact that the U.S. stock market has been relatively flat since mid-2004, it's no surprise that many U.S. investors have already noticed that some international funds have begun to outperform domestic U.S. funds. In the poll, 86 percent of shareowners said the declining value of the U.S. dollar is one reason international funds are thriving; 84 percent mentioned the move of U.S.-company operations overseas. Other reasons cited by a majority of shareholders included strong growth abroad, high oil prices, and slow economic growth and rising interest rates in the United States.

The majority of respondents have most of their portfolios invested in domestic markets, but a growing number are adding international investments to the mix. U.S. shareholders currently have 84.2 percent of their portfolios invested domestically. The remaining 15.8 percent of the average shareholder's portfolio is invested internationally, which is up from 12.9 percent five years ago. These same shareholders expect to have 18.6 percent of their total portfolios invested internationally five years from now.

Shareholders must start thinking about diversifying their portfolios to reflect some international risk, says Dean Junkans, San Francisco-based chief investment officer for Wells Fargo Private Client Services.

"International stocks have performed well lately versus U.S. stocks, and there is a growing realization that investors need to look globally for growth," he says. "Sixty percent of the world's total equity market value is outside the U.S., and that percentage continues to grow as wealth expands in many countries across Asia." Even if they're not investing directly in foreign-based companies, a growing number of Americans are consciously investing in multinational U.S.-based companies whose profits are driven by growth in emerging nations, he says.

The Information Gap

Regarding their desire to add global diversification to their portfolios, 38 percent of shareholders polled in the recent survey said they are most likely to do this by investing in individual stocks in U.S.-based companies with a global presence. Two-thirds indicated they're not likely to invest in individual stocks in foreign companies or international bond funds.

These shareowners' reluctance might have a good foundation. It's usually difficult to get reliable firsthand information about many foreign companies because financial-reporting systems aren't as well developed as in the United States and Europe, says James Berman, president of JBGlobal LLC, New York, N.Y., a longtime investor in global markets. Also, many foreign countries' governments and economies are unstable or have short track records as destinations for investment dollars. Therefore, a great deal of research is needed to evaluate investments in foreign markets.

"By the time you make an investment in a company in a foreign country, it should not be foreign to you," Berman says. "You should know the political and economic situation there because you're making an investment in the currency of that country. Think of making an investment in the country as much as in a company there."

Caution About China

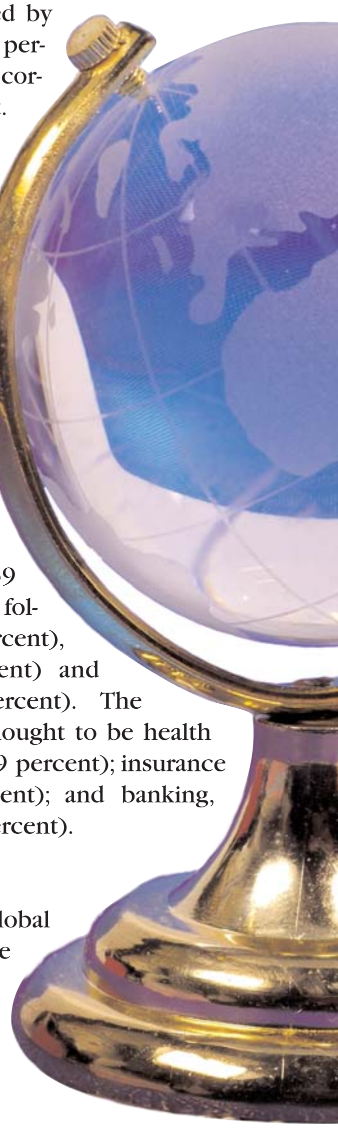
Nancy Hamlin, member of an investment club in Medford, Ore., was able to do some firsthand research in foreign investments when she traveled to China earlier this year with a few other club members. "Seeing China with my own eyes convinced me that it's going to have a huge effect on us," she says. "Their energy and desire for cars is incredible. What I saw made me think China will eventually outdo the U.S." One bright spot she noticed with her investor's eye: the popularity of U.S.-based fast food brands, such as McDonald's and Yum! Brands' KFC.

Individual investors are advised by most Wall Street analysts against investing directly in Chinese companies for a host of reasons, including the communist government's heavy-handed role in managing the economy.

Last July the Chinese government announced a revaluation of its currency, the yuan, and its intention to allow its value to float along with natural market dynamics. This is viewed as a positive by many stock market analysts, but they also express a note of caution because the government controls the Chinese economy. This is an unnatural situation.

"The question is whether China will truly allow the yuan to float and not interfere with it," says Susan Stewart, president and co-founder of Washington, D.C.-based Charter Financial Group, which manages a large portfolio for a group of high-balance private investors. "Investing directly in China is too risky because of the geopolitical risk there and the government's involvement in things."

American shareowners also have a cautious attitude about investing in China. Fifty-one percent said they don't plan to invest in China, while almost a third said they're taking a "wait and see" approach. The largest barrier to investing in China is the lack of confidence in the communist government, followed by human-rights violations and a perception of corruption at Chinese corporations and in the government.



The biggest advantage to investing in China, according to half the shareowners polled, is the supply of workers available in China. Nearly as many (48 percent) cited a fast-growing economy as a positive. The outsourcing of manufacturing to China was viewed as a plus by 45 percent of investors polled.

Manufacturing is considered the best investment in China by 59 percent of shareholders polled, followed by technology (39 percent), telecommunications (31 percent) and information technology (25 percent). The worst sectors generally were thought to be health care (36 percent); real estate (29 percent); insurance (28 percent); media (26 percent); and banking, finance and education (all 23 percent).

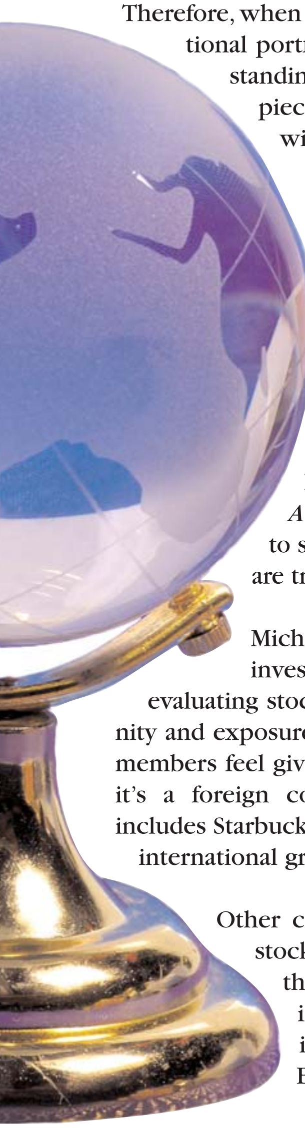
Globalize Your Portfolio

So how do you cautiously add global diversity to your portfolio? The first step is to observe what you see happening in global markets and try to link those events to your own portfolio.

Shareowners in the poll identified certain countries' growth as having a positive effect on the U.S. economy. Forty-four percent of investors who are comfortable investing internationally believe Japan will have a positive effect on the U.S. economy in the long run; an equal percentage feel this way about the European Union. Thirty-seven percent of these shareholders believe China will have a positive effect on the United States in the long run, compared with 32 percent for India. Only 16 percent thought Russia would have a positive impact on the U.S. economy.

Another basic tactic for diversifying your portfolio is to have investments in companies in both developed and less-developed countries, says John Schloegel, vice president of investment strategies for Austin, Tex.-based Capital Cities Asset Management.

"You will typically find that the more developed the market is, the less volatility it has," he says. "For example, the U.K., Germany and Canadian markets are generally much less volatile than Malaysia, Korea or Russia. Therefore, when investors are constructing an international portfolio, they should have a good understanding of the volatility level of the various pieces so that the final portfolio is aligned with their risk objectives."



Some investment advisers don't believe it's necessary to follow events in foreign countries to have a stake in global markets. "Having a global presence in your portfolio does not necessarily need to be exotic," says Gary Stroik, who runs a portfolio for private investors as president of Little Silver, N.J.-based Wealth Builders, Inc., and is the author of *All About Dividend Investing.* "One way is to simply invest in foreign companies that are traded on the domestic stock market."

Michael Oakley of Renton, Wash., says his investment club is taking that approach by evaluating stocks in terms of international opportunity and exposure. The club holds Nokia stock, which members feel gives them some global muscle because it's a foreign company. The club's portfolio also includes Starbucks, which members feel is powered by international growth.

Other clubs are applying the same logic to stock they hold in American companies that are supplying technology to emerging countries and economies. These include 3M, Honeywell and General Electric.

"Another stock held by a lot of individual investors is Emerson Electric," Junkans says. "This is a company that does about 7 percent of its business with China, so if the currency is favorable, it makes companies exporting products to China look favorable to American investors." *(No investment recommendation is intended for any of the companies mentioned in this article.)*

But other advisers say it's not enough to simply invest in U.S. companies doing business overseas. "The stock price of U.S. companies that do business overseas more closely correlates with the U.S. stock market than the market of the countries they work in," says Jason Papier, a principal with PW Johnson, a wealth management firm based in Sunnyvale, Calif. In his opinion, merely investing in U.S. multinationals doesn't provide adequate international exposure to add global diversity to your portfolio.

Expand Your Reach

For those shareholders who want to explore investing outside U.S. borders, a good way to start is to focus on companies in a particular foreign country and begin doing research on them for possible future investment. It may be harder to get the same type of information about foreign companies that's readily available regarding U.S. companies, but technology and electronic communications are rapidly melting geographic barriers that made foreign investment difficult in the past.

"The flow of information through electronic channels has greatly enhanced investing opportunities overseas," says Charter Financial's Stewart. "By closely reviewing information from world markets, it's possible to spot trends that can prove to be profitable." Examples include her company's recent investment in a British gypsum supplier to the construction industry.

"For me, successful international investing requires a great deal more research and paying close attention to an individual company's performance rather than looking at sector performance," she says.

The bottom line for individual investors is that today's portfolios should reflect the increasingly global economy, and shareholders must begin to look at their investments from a broader point of view.

"Many U.S. companies do business internationally, and that's one way of looking at your portfolio," Junkans says. "But in the long run investors are going to have to think about allocating their assets in a world economy." BI

Free-lance journalist Kate Fitzgerald writes about the Voice of the American Shareholder survey for BetterInvesting Magazine.