Eagle International Equity Fund

Management

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Portfolio Co-manager

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Artio Global Investors
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Characteristics

Total Net Assets (millions)	$41.9
Number of holdings	195

Top Holdings

Vodafone
Suncor Energy
Nestlé
Fraport
Novo Nordisk
Toyota Motor
BHP Billiton
HSBC
LVMH Moët Hennessy • Louis Vuitton
Sberbank

Market Overview

Despite a retreat in the month of March, international markets saw strong first-quarter returns with most developed and emerging markets posting double-digit gains. The sole country to see negative returns was Spain, Europe's newest source of economic concern. Whereas Greece dominated financial headlines for all the wrong reasons throughout 2011, the country experienced some good news this quarter. First, the European Union signed off on an arrangement to help the country avert default and second, a sizable majority of private-sector bondholders said they would participate in a restructuring through a bond swap. These actions were good enough to have Fitch Ratings upgrade Greek debt from the"Selective Default"category (a ranking it still retains with Standard & Poor's).

While admitting that the European sovereign-debt crisis is not yet over and it may be some time before normalcy returns, many have expressed optimism that the Continent is gradually recovering, albeit in varying degrees. Euro-zone governments are now in the process of ratifying a treaty establishing the European Stability Mechanism (ESM), a permanent rescue fund of approximately €80 billion cash and the right to call another €620 billion in an emergency. The ESM would have the ability to lend money and allow countries to maintain a buffer to garner a top credit rating. Additionally, the permanent fund will run parallel to the emergency funds in the near term, providing ample liquidity to European countries.

At each of their meetings during the quarter, the European Central Bank (ECB) and the Bank of England maintained their low interest rates. As they did back in December 2011, in March the ECB allowed banks to borrow as much as they wanted at the benchmark interest rate for three years (the Long Term Refinancing Operation or LTRO) provided they could supply collateral. This effort is intended to ease fears of a banking liquidity crisis in countries such as Italy and Spain as well as encourage banks to lend, thereby stimulating growth. The Bank of England maintained its rate amid concerns that economic turmoil and high oil prices could negatively impact the British economy.

During the quarter, Japan marked the one year anniversary of the tragic natural and nuclear disasters that hit the country. Since then, the economy has gradually improved and for the first three months of this year, the country performed in line with other developed nations. However, national debt remains a concern and expectations by most, including ratings agencies, are for weak economic growth in 2012.

Emerging market returns lagged their developed counterparts in March but stronger returns in the two prior months were enough to result in outperformance for the overall quarter. In absolute terms, emerging Europe was the quarter's best performer followed by Latin America and emerging Asia. The Russian market was bolstered by higher oil prices and companies' potential to benefit from Europe's planned embargo of Iranian oil this summer.

Meanwhile, China reported that in February, the monthly trade deficit saw its weakest performance in over a decade. This was just another indication that the nation's economic growth rate is slowing. Few analysts are predicting a hard landing in China as more moderate growth is still likely and inflation is easing but concerns of a slowdown have been making headlines more frequently. It is important to bear in mind that the Chinese government has significant latitude to use monetary and fiscal policy measures to stimulate growth.

Portfolio Review

Stock selection in developed-market sectors was the leading contributor to returns while cash/currency positioning during this upmarket period was the primary detractor. In developed markets outside Japan, stock selection was particularly noteworthy in the energy, healthcare and industrials sectors. In Japan, stock selection in the consumer discretionary sector was a standout. Within emerging markets, the underweight did have a drag on results, some of which was offset by strong stock selection, notably in Russia.

In developed markets outside Japan, the consumer discretionary sector saw returns outpace the benchmark and our overweight positioning had a meaningful positive impact. While the strong returns were posted by several companies, many were clustered in the luxury goods category. For some time, this has been an area that we have found particularly attractive as an opportunity to capitalize on emerging-market consumption growth. The number of new millionaires coming out of emerging markets is increasing at a rapid rate and their subsequent demand for luxury goods, the status symbol of their new wealth, is also rising. As a reference point, we can look back to Japan in the 1990s when a similar boom took place and that nation consumed nearly 40 percent of the world's high-end goods.

While the developed markets' energy sector was one of the benchmark's weaker performers, several portfolio holdings went against this trend and saw returns well above average. One standout was an Ireland-domiciled upstream oil and gas-exploration entity with operations in and around the Caspian Sea, part of whose strong returns can be attributed to a belief that the company offered growth at a reasonable price, a strong balance sheet and the ability to generate sizable amounts of free cash annually through the remainder of the decade. This position as well as others in countries such as Canada easily offset the negative impact that was a result of an overweight to the sector. As stated in previous commentaries, we have a preference for upstream energy companies (those that search for and recover oil and gas) and seek to avoid integrated oil companies and refiners. We prefer companies with long reserves and low cost structures as well as oil service entities that often benefit from larger budgets to find and develop new projects as this effort is becoming increasingly more challenging and costly.

Healthcare stock selection in developed markets outside Japan was also robust. However, like energy, it was one of the benchmark's weaker performers and some of the benefit realized by positions held was partially offset by a decision to carry a relative overweight. Two individual standouts, both European, included one of the world's largest providers of products to treat diabetes and an ophthalmic optics company. The former has benefited from an increased occurrence of diabetes from emerging-market populations, largely due to dietary changes, and governments coming under increased pressure to treat the disease. In the case of the latter, during the quarter the company's board proposed a dividend for the 2011 fiscal year and issued revenue guidance for the 2012 fiscal year that was in line with analyst's estimates. This news sent the share price higher. Within the industrials sector, the fund also benefitted from positive stock selection.

Staying within developed markets outside Japan, the materials sector was the largest detractor primarily due to Canadian and U.K. positions that are directly related to gold mining. The price of gold dropped by over 7 percent in March and as a result, companies that extract the metal suffered. However, we continue to like the sector and view the supply/demand characteristics of several commodities and raw materials such as gold, copper and coal as favorable and believe the sector's oligopolistic firms have pricing power and strong profitability potential.

Turning to Japan, while we continue to maintain our historical underweight, we have recently increased exposure. For the first time in many quarters, the Japanese equity market performed in line with the broader index due in part to the government enacting their own version of quantitative easing, an expanded asset purchase program that predictably weakened the yen. While our allocation decision had a slight positive effect (pulled down by an underweight to financials), the bulk of the benefit to relative returns this quarter came from strong stock selection in the consumer discretionary and industrials sectors. Companies are starting to regain production capabilities one year after the supply chain was disrupted by the earthquake and tsunami. The focus of the fund's holdings are those firms that export, such as makers of automobiles, heavy equipment and robotics, many of which are enjoying renewed strength and seeing once depressed share prices rebounding. However, we still have concerns about the high levels of Japanese government debt and intend to avoid investments that are domestically-related.

Finally, the underweight to emerging markets, which as stated above performed better than their developed counterparts for the quarter, did detract from results. The underweight to Brazil in particular detracted. However, this was partially offset by stock selection, particularly in Russia. One of the best individual performers was one of the nation's largest banks (second largest by market value in

Europe) which in late March announced record annual profits although they were below market expectations. The Russian government is preparing to sell a significant portion of its stake in the bank; this is expected to help it become a more dominant player internationally.

Overall, we see a longer term decoupling of emerging markets from the developed world and the performance of individual countries to be driven more by domestic policies and domestic consumption. Our belief is that most emerging-market governments have the policy latitude to get through any soft patch in the global economy and do what we anticipate, which is increase domestic consumption. However, this theory could be undermined if there is a dramatic shift in the developed world that slashes emerging market exports.

We continue to believe that significant growth in the emerg- ing market middle class will play a large role in determining the performance of a multitude of industries and companies in the years ahead. As a result, we continue to hold direct investments within local emerging markets, and also global franchises within the developed world that are garnering a large share of the emerging-market consumer's wallet. In particular, global companies with strong balance sheets, superior management, solid brands and brand awareness, sustainable cash flows and dividends. We also feel that the current environment is a positive one for commodities and hard assets and that sovereign debt along with regulatory issues will continue to cast a shadow over the financial sector. Lastly, we are drawn to what we see as positive long-term fundamentals of several industries while a combination of unattractive valuations and a negative outlook leads us to largely avoid areas such as utilities.

International investing presents specific risks, such as currency fluctuations, differences in financial accounting standards, and potential political and economic instability. These risks are further accentuated in emerging market countries, where risks can also include possible economic dependency on revenues from particular commodities or on international aid or development assistance, currency transfer restrictions, and liquidity risks related to lower trading volumes. Investing in small- and mid-cap stocks may involve greater risks than investing in larger, more established companies. These companies often have narrow markets and more limited managerial and financial resources.

International Equity

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Growth companies are expected to increase their earnings at a certain rate. When these expectations are not met, investors may punish the stocks excessively, even if earnings showed an absolute increase. Growth company stocks also typically lack the dividend yield that can cushion stock prices in market downturns.

The companies engaged in the technology industry are subject to fierce competition and their products and services may be subject to rapid obsolescence. The values of these companies tend to fluctuate sharply.

Benchmark Index
Morgan Stanley Capital International All Country World-ex US Index (MSCI ACWI-ex US) is a free float-adjusted market capitalization index that is designed to measure equity market performance in the global developed and emerging markets.

Artio Global Investors is the subadviser to the Eagle International Equity Fund..x

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