CUMBERLAND

Global Equity and International Fund Strategies
Year End 2015 Review

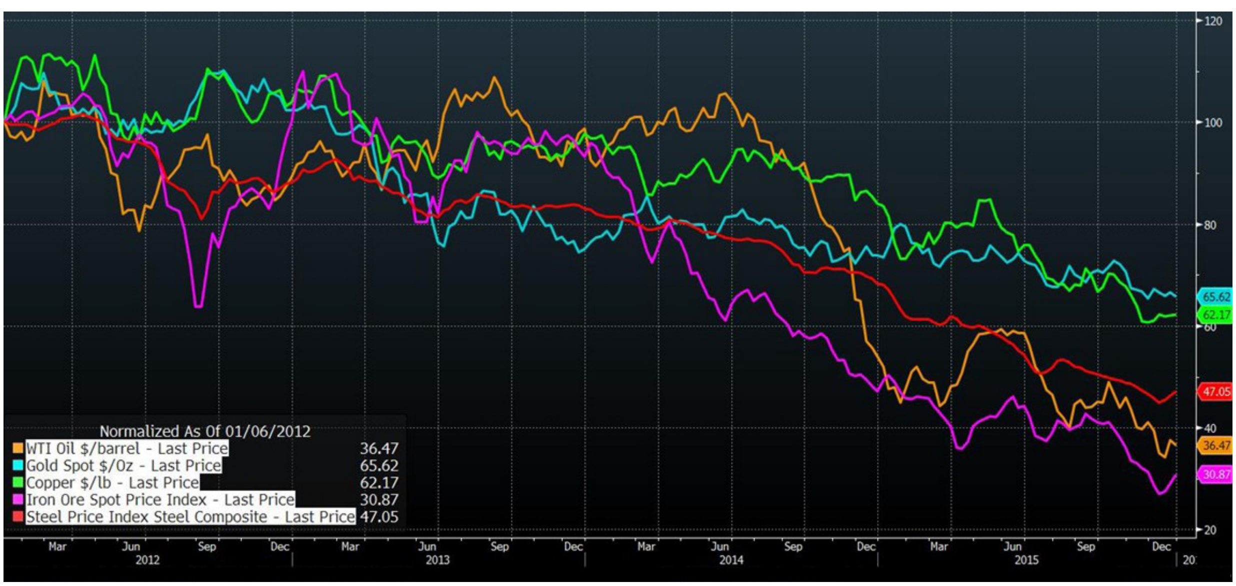
Global Macro Review

The latest installment of Star Wars – The Force Awakens entertained millions with the good fighting off the evil Empire. It is unfortunate that the Force could not exist in the real world and fight off all that is evil. There were 6,692 migrant deaths in the Mediterranean Sea in 2015 with more than one million irregular migrants arriving from Syria, Africa, and South Asia. Both are appalling statistics. Along with these gruesome numbers, we may also associate last year with the disturbing and dramatic increase in the number of large scale attacks. We connect this with the unfortunate events of the two terrorist attacks that took place in Paris in January and November given the media attention alongside these particular events. But the reality is that there were 385 terrorist attacks globally last year, many of which received little attention from Western media. This made the year a gloomy one indeed and this sentiment was also reflected in the turbulent and challenging markets. Sadly, as the frequency of terror attacks increases, the market reaction continues to be relatively more muted.

Despite the market not being shaken radically from shots of terror, there is anxiety for various reasons, one of which is that we have yet to witness a robust recovery or a global expansion since the last recession. Another reason is the growth realignment in China resulting from weaker demand, which led to a downturn in commodity prices and prolonged manufacturing overcapacity. Hence, there have been global repercussions and global deflation potentially. The producer price index is at its lowest average point for six years in the ten largest economies in Asia excluding Japan. For example, China's producer prices are down a cumulative 10.8% from their recent peak in 2011 and we can see the dramatic decline of various commodity prices in the chart below.

In the International Monetary Fund's (IMF) latest World Economic Outlook, they have brought down their expected near-term global growth rates marginally. They have forecasted growth in 2015 to be 3.1% which is a decline from 3.4% in 2014. Global activity is projected to gather some pace in 2016, to 3.6%. Similarily, the World Bank also expects 2016 global growth at 2.9%, an increase over 2015's low level of 2.4%. The medium-term prospects remain subdued due to lower

Decline of Commodity Prices 2011-2015

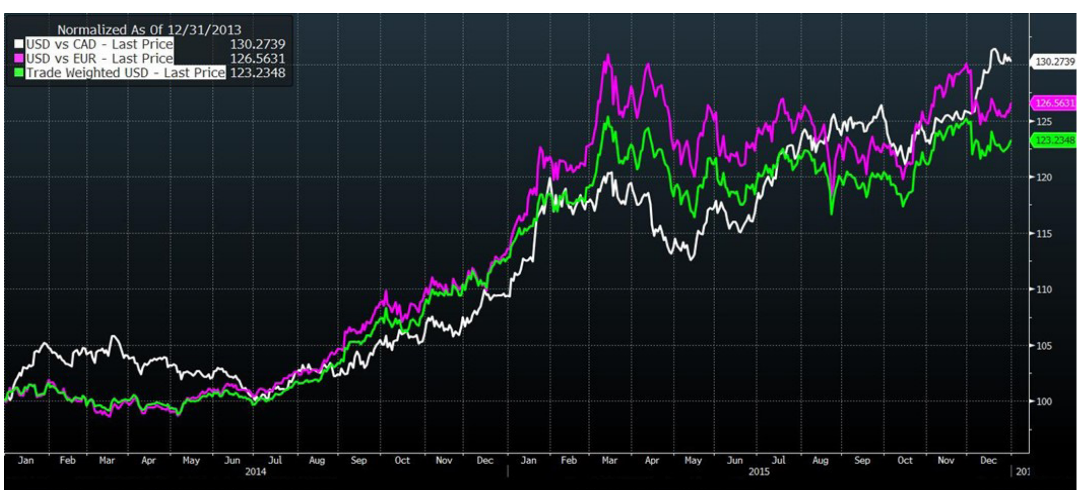


investment, unfavorable demographics and weak productivity growth. These forecasts however, hide important economic divergences and downside risks. Generally, the advanced economies look stronger as they benefit from lower commodity prices while emerging and developing economies will experience a slowdown from weaker exports. This does not bode well for near-term global economic growth as the larger portion of recent growth came from the emerging and developing markets.

We are seeing recovery in some advanced countries such as the United States and United Kingdom where output is accelerating and unemployment is declining. The divergence in the different growth rates is reflected in the different policies of their respective central banks. The U.S. is the most advanced in their monetary policy where they have already tightened and their economy is expected to grow 2.5%. The IMF expects the U.K. to have the next best growth rate at 2.3%. Trailing these countries are the eurozone at 1.7% and Japan at 1.2% where their respective monetary policies should continue to be accommodative. The European Central Bank's (ECB) President Draghi stated that the ECB is failing to achieve its mandate of price stability, which is defined as a year-on-year increase in the Harmonised Index of Consumer Prices (HICP) for the euro area of below 2%. For emerging market and developing economies as a whole, the IMF is expecting this past year will mark the fifth consecutive year of declining growth. The emerging markets are facing a multitude of headwinds including declining commodity prices, reduced capital flows, pressure on their currencies and increasing financial market volatility.

There were three major foreign exchange shocks that took place in 2015. The first one took place in January when the Swiss National Bank (SNB) abandoned the floor set for the Swiss franc's exchange rate against the Euro and as a consequence, the Swiss franc appreciated as much as 23%. Switzerland has 60% of their trade with the eurozone and that is where they need currency weakness. The Swiss economy is now in deflation. The second shock took place in August when China devalued the renminbi. There was a global impact as fear of weak demand and oversupply in commodities resulted in a further drop in commodity prices. This action by China appears to have spurred exporters of basic resources to devalue their currencies in order to remain competitive and retain revenue. Canada is an example of this with a 16% depreciation in the Canadian dollar against the U.S. dollar in 2015. The final shock came in December when the ECB did not deliver to the extent of market expectations and this drove the Euro up 4.5%. During the last recession, we experienced currency wars and a variety of countries racing to devalue their currency; a replay of which may take place.

Devaluation of Currencies vs. USD



Global Equity and International Fund Strategies
Year End 2015 Review

Europe

A key issue for the UK will be the referendum that will take place before the end of 2017 at the latest on the question of whether they will remain a member of the European Union (EU). A recent opinion poll indicates that about 40% of the British public wants the UK to leave the EU, otherwise known as Brexit. Prime Minister Cameron's planned reforms require changes to the treaties governing the EU and will require the unanimous support of all EU members.

The general sentiment of those who want the UK to leave the EU believe Britain is being held back by the EU. They say the EU imposes too many rules on business and charges billions of pounds in membership fees for little return. However, those who want the UK to stay in the EU believe the UK gets a boost as selling to other EU countries is easier and the flow of young immigrants fuels economic growth.

Cameron has provided a letter to Donald Tusk, President of the European Council presenting his objectives:

1. *Economic governance:* Securing an explicit recognition that the Euro is not the only currency of the EU. The UK wants to safeguard steps that further financial union cannot be imposed on non-eurozone members and the UK will not have to contribute to eurozone bailouts;

2. *Competitiveness:* Setting a target for the reduction of the burden of excessive regulation and extending the single market;

3. *Immigration:* Restricting access to in-work and out-of-work benefits to EU migrants. Ministers want to stop those coming to the UK from claiming certain benefits until they have been resident for four years;

4. *Sovereignty:* Allowing Britain to opt out from the EU's founding ambition to forge an "ever closer union" of the peoples of Europe so it will not be drawn into further political integration. Giving greater powers to national parliaments to block EU legislation.

The EU leaders do not want to see the freedom of movement to be eroded as the freedom for people to move around Europe is enshrined in the EU treaties. It goes along with the three basic freedoms in the single market: freedom of goods, capital and services.

Cameron had a number of measures to reduce the number of EU nationals moving to the UK, including a four year delay for EU migrants wishing to claim in-work benefits such as tax credits or seeking access to social housing. These restrictions are an issue with the EU as it is seen as a fundamental freedom of the EU market and amounts to direct discrimination between EU citizens.

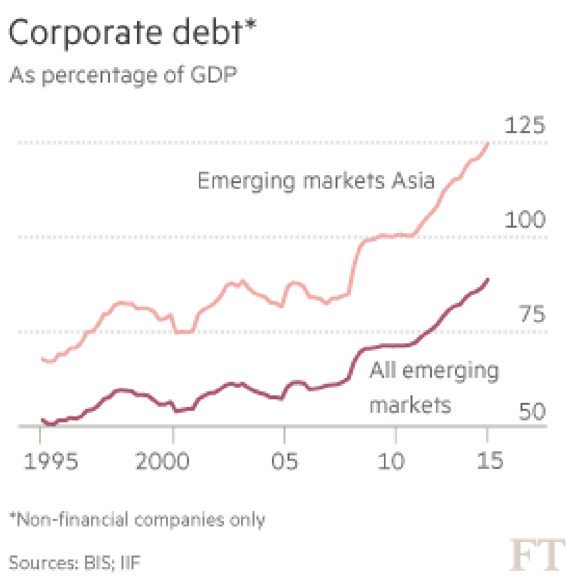
The debate, of course, is whether UK is better off staying or leaving. Those who favor the UK staying in the EU would be big business because it makes it easier for them to move money, people and products around the world. Meanwhile, those who want the UK to leave argue that an exit would allow the UK to negotiate trade deals as one country rather than being one of 28 nations. In addition, many small and medium-sized firms would welcome a cut in red tape and regulations.

There are various implications for a Brexit. First, the Scottish National Party have said they will push for a referendum on independence if the voters decide to leave the EU. Second on the economic front, a think-tank has estimated that leaving the EU could cost the British economy 2.2% of its GDP, mainly because of lower foreign direct investment. Extreme pessimistic scenarios reflect a decline in income between 6.3% to 9.5% of GDP. This would be a scenario where the UK is not able to negotiate favorable trade terms. It would cost the UK 78 billion euros annually if London quits the bloc and fails to agree to a free trade deal, and some firms have said they would look into leaving Britain if a Brexit takes place (such as Deutsche Bank which employs 9,000 people in the UK). The impact on the EU is also large. UK's national contribution to the EU budget was 14.5 billion euros in 2013 and this also opens the question of another country wanting special status. Overall, a consensus holds that a Brexit would diminish the status of the UK and EU alike, by varying degrees.

Global Equity and International Fund Strategies
Year End 2015 Review

Emerging Markets

Compounded by the decline in commodity prices is the build-up of debt in the emerging markets. We have seen this story play out before. In the U.S., it was the housing bubble bursting and in the Europe, it was Greece's insolvency crisis. Capital flowed into emerging markets given interest rates were so low elsewhere, leading to firms financing imprudent projects. This has resulted in emerging market debt growing from 150% of GDP in 2009 to 195% of GDP today. Corporate debt has also increased dramatically, from about 50% of GDP in 2000 well over 75% as shown below. As we discussed above, China's growth has slowed and this has significant cross-border implications. Capital inflows into emerging markets have either slowed or stopped as a result and it is exacerbated by the increase in rates in the US. The question that remains is whether this debt issue will create a crisis as the ones we experienced in the U.S. and Europe or whether it will merely result in slower growth.



The term "BRIC", an acronym for an association of four major emerging economies was coined in 2001 by then-chairman of Goldman Sachs Asset Management, Jim O'Neill. The countries were Brazil, Russia, India, and China that are all developing or newly industrialised countries. The commonality was their large, fast-growing economies and significant influence on regional and global affairs. Today, the BRIC nations are faced with problems that are in contrast to their origin of the acronym.

With China's growth rate expected to slide below 7% for the first time since 1981, the risk to its economic stability is questionable. China has a current account surplus and foreign exchange reserves and thus, we would expect China to protect itself and as a result, the world economy from economic disaster. However, the case of Brazil is a different story where they are in a recession and the risk is much higher. Brazil's current account deficit means it relies on foreign capital reflected by its twelve-fold increase in its corporate bond market since 2007. In mid-December, Fitch became the second of the three big credit rating agencies to downgrade Brazil's debt to junk status. To add to the pile, President Rousseff faces impeachment proceedings. India is in healthier shape than other emerging economies, although the shine on India post Modi's election win has already dimmed. Russia, which is already in a recession, made adjustments post the sanctions placed on them and a continuous decline in the oil prices will be a further negative.

Although the IMF is forecasting higher growth in emerging markets in 2016, past debt cycles suggest a challenging year ahead for these markets.

Portfolio Review

Consistent with our investing style, we maintained a lower risk profile and minimal exposure to commodities, which resulted in a lower portfolio volatility. As you are aware, we believe in investing in companies with strong growth potential and high quality earnings over the long-term. This has been our strategy since inception of our investment mandate over ten years ago now. The end of the commodity boom creates risks. The decline in commodity prices frequently leads to credit issues for some commodity-producing companies. Countries such as Canada, Australia, Russia, Brazil and South Africa are negatively impacted by the decline in commodity prices as their revenues decline.

Global Equity and International Fund Strategies
Year End 2015 Review

We are currently not invested in any emerging countries directly. However, the developing world accounts for over half of the global economy in purchasing power parity terms and therefore, these countries matter much more than before. We are invested in multinationals which have exposure to various BRIC countries along with other developing countries and as a result, they warrant our attention to actions taking place in this region.

2015 turned out to be the biggest year ever for mergers and acquisitions (M&A). Global M&A volume of $4.304 trillion pushed 2015 ahead of 2007's total when the previous record of $4.296 trillion was obtained. Healthcare and Technology were the key sectors with the largest number of M&A deals, with Healthcare accounting for 14% of the activity. The largest healthcare transaction of Pfizer's $160 billion proposed acquisition of Allergan PLC was announced in November. Like a number of other healthcare deals, Pfizer's acquisition is driven largely to obtain Allergan's lower Irish tax rate where the estimated tax savings are expected to be $21 billion. However, not long ago Comcast walked away from their offer to purchase Time Warner Cable as the government did not agree with their union. Despite the disappointment however, Comcast continued to do well.

Cumberland Global Equity Portfolio

Our Global Equity portfolio had a total return for the fourth quarter of +7.3% (C$) compared to its benchmark return of +8.9% (C$), for an underperformance of 1.6%. In U.S. dollar terms, the portfolio had a quarterly return of +3.9% (US$) vs. the MSCI World at +5.6% (US$). For the year, the Global Equity Portfolio's return of +13.6% (C$) trailed its benchmark's return of +18.0% (C$) by 4.4%. In U.S. dollar terms, the portfolio's return of -4.8% trailed the Index's return of -0.9% for the year.

The key contributor to this year's performance was the stock selection within and overweight allocation to the Healthcare sector. Other long-term investments such as Fresenius SE, Visa, Schweiter Technologies, and Essilor were key contributors.

Our Qualcomm investment was a key detractor from our performance and it hit our non-discretionary loss limit which caused us to sell it from the portfolio. Fortunately, the loss from this holding was mitigated by the strong upward move in Sandisk. This was a recent purchase, but shortly after its purchase, the Company received an offer from Western Digital for U$19 billion, pushing the stock up 53.2% from when acquisition rumors first arose. Our average cash level of 10% also detracted from performance overall. Finally, other areas that were detractors from performance included our underweight in both Japan and Information Technology along with holdings such as Hyundai Motor.

In terms of other portfolio activity, we sold EBay and McKesson and bought Allergan and Keyence. Keyence is a leading global provider of industrial automation products which offers a wide portfolio of automation solutions including sensors, measurement systems, tag readers, machine vision systems, marking technologies, and microscopes. Keyence products are primarily used by clients to enable improvements in manufacturing productivity, quality control, inventory management and safety. Allergan, following the sale of its generics business to Teva has become a pure play pharmaceutical company with an innovative R&D driven business.

Cumberland International Fund

During the quarter, Cumberland International Fund had a return of +5.8% (C$) vs. its MSCI EAFE benchmark's return of +8.1% (C$), underperforming the benchmark by 2.3%. In U.S. dollars, the Fund returned +2.1% (US$) during the quarter vs. the MSCI EAFE benchmark's return of +4.7% (US$). The Fund's cash level remained around 13% at quarter-end, which is a similar to the level as we entered the quarter. While this elevated cash level protected the portfolio during the downturn in the third quarter, it was a drag on performance during the fourth quarter and for most of this year. Following the large decline in the market in September, many of the lower quality stocks made a strong rebound in October causing our portfolio to lose some

Global Equity and International Fund Strategies
Year End 2015 Review

of its outperformance. **As a result, the Fund's return of +21.4% for the year exceeded the benchmark's return of +18.1%, for an outperformance of +3.3%.** In U.S. dollar terms, the Fund had a return of +1.3% vs. -0.8% for the Index.

The key contributor to this year's performance was the stock selection and the overweight allocation to the Healthcare, Information Technology, and Utilities sectors. In terms of individual names, the largest contributors were Cheung Kong Infrastructure, Dassault Systèmes, and Fresenius SE. Being underweight Energy and Materials also contributed to the Fund's performance.

As with our Global Equity mandate, our conservative asset allocation with an average cash level of 13% detracted from overall performance. Another key area that also detracted from performance was our underweight in Japan and our overweight allocation to Consumer Discretionary and certain investments, namely Hyundai Motor and Samsung Electronics, both of which have been profiled in prior quarterly reports.

In terms of transactions, we bought Schlumberger, Keyence, and Allergan. Schlumberger, the world's leading oil service company, is an investment we have had for many years in the past and have reintroduced to the portfolio. Keyence and Allergan were discussed above.

Index Performance

Fourth Quarter

The total returns of the global markets for the fourth quarter in US$ and local terms are:

	Q4 2015 USD Total Return (%)	Q4 2015 Local Total Return (%)
MSCI World	5.6	5.6
S&P 500	7.0	7.0
Canada S&P/TSX	-4.5	-1.4
Euro Stoxx	2.8	5.7
MSCI Emerging Markets	0.5	0.5
Germany DAX	8.5	11.2
UK FTSE 100	1.0	3.7
France CAC 40	1.5	4.5
Switzerland SMI	2.0	3.6
Japan Topix	8.9	9.8
Hong Kong Hang Seng	5.4	5.4
Korea KOSPI	0.6	-0.1

The key benchmark, the MSCI World Index, had a total (price and dividend) return of +5.6% in US$ and +8.9% in C$ for the fourth quarter. The other key benchmarks of MSCI EAFE had a total return of +4.7% in US$ and +8.1% in C$ while the S&P 500 had a total return of +7.0% in US$ and +10.5% in C$. Global markets outperformed the Canadian market once again this quarter which returned -4.5% in US$ and -1.4% in C$. The Canadian dollar depreciated by +3.8% against the U.S. dollar in the quarter. Thus, with the depreciation of the Canadian dollar, the returns increased when translated back to the Canadian dollar.

Global Equity and International Fund Strategies
Year End 2015 Review

In the MSCI World benchmark, Information Technology with +8.6% (US$) and Healthcare with +6.7% (US$) were the top performing sectors in the quarter. The two worst performing sectors in this benchmark were Energy with a -1.4% return and Utilities with +0.7%.

The two best performing sectors during the fourth quarter in the MSCI EAFE benchmark were Information Technology with +10.2% (US$) and Industrials with +6.2% (US$). Similarly to the Global benchmark, the two worst performing sectors in the EAFE benchmark were Energy at -0.4% and Materials at +1.1%.

Annual Index Performance

The total returns of the global markets for 2015 in US$ and local terms are:

	2015 USD Total Return (%)	2015 Local Total Return (%)
MSCI World	-0.9	-0.9
S&P 500	1.4	1.4
Canada S&P/TSX	-23.0	-8.3
Euro Stoxx	-3.7	7.2
MSCI Emerging Markets	-14.9	-14.9
Germany DAX	-1.7	9.6
UK FTSE 100	-6.7	-1.4
France CAC 40	0.5	11.9
Switzerland SMI	1.1	1.1
Japan Topix	11.0	12.1
Hong Kong Hang Seng	-4.0	-4.0
Korea KOSPI	-4.6	2.5

The key benchmark, the MSCI World Index, had a total (price and dividend) return of -0.9% in US$ and +18% in C$ for the year. The other key benchmarks of MSCI EAFE had a total return of -0.8% in US$ and +18.1% in C$ while the S&P 500 had a total return of +1.4% in US$ and +20.7% in C$. Global markets outperformed the Canadian market once again this year which returned -23.0% in US$ and -8.3% in C$. The Canadian dollar depreciated by +16.0% against the U.S. dollar in 2015. Thus, with the depreciation of the Canadian dollar, the returns increased when translated back to the Canadian dollar.

The U.S. market had their worst annual performance since 2008. Had it not been for a small group of stocks (Facebook, Amazon, Netflix and Google), the broad market struggled. The dollar gained 11.4% against the Euro.

Europe's benchmarks did well this year in local currency terms, with Italy being the top performer with +13.9% return. The UK market was negatively impacted from their high exposure to commodity listings such as Anglo American (-74%) and Glencore (-69%).

In the MSCI World benchmark, Healthcare with +5.2% (US$) and Consumer Staples with +4.2% (US$) were the top performing sectors in 2015. The two worst performing sectors in this benchmark were Energy with a -25.0% return and Materials with -17.2%.

The two best performing sectors for 2015 in the MSCI EAFE benchmark were Consumer Staples with +6.3% (US$) and Healthcare with +5.7% (US$). Similarly to the Global benchmark, the two worst performing sectors in the EAFE benchmark were Energy at -22.1% and Materials at -19.2%.

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Global Equity and International Fund Strategies
Year End 2015 Review

Outlook

We do not expect a robust macro environment for the coming year. With this as a backdrop, we will ensure the companies in the portfolio are efficient and have the ability to allocate their capital effectively.

It would not be surprising for companies to be more muted on their earnings growth. We would expect our companies to have strong balance sheets to fund their future growth.

In summary, we will continue to focus on companies that have the following characteristics:

1. Operate in industries that have secular growth and as such, should survive in any type of economic environment
2. Have a global footprint
3. Strength and leadership in a product or service
4. Lower volatility given the company's overall stability
5. Limited exposure to commodities
6. Growth in free cash flow
7. An attractive valuation

The MSCI World benchmark is trading at a Price to Earnings (P/E) valuation of 16x next year's earnings, which is in line with last quarter's 15.7x but still higher when compared to the ten-year P/E average of 14.5x. At these valuation levels and with lower growth prospects, it is natural to err on the side of caution, but investing opportunities may arise if pessimism in the market continues.

We expect our portfolio companies to grow their earnings at a rate exceeding the market average for the coming year and overall, we still believe earnings growth from quality companies are the key to good investment performance.

S. Yang
Lead Manager, Global Equities
January 7, 2016