EQUITIES | GLOBAL INVESTING

Navigating Shifting Currents in International Equity Markets

By: Christopher M. Dyer, CFA | September 27, 2021

London - We see some challenging crosscurrents driving the international equity markets, although we are optimistic about their long-term prospects overall. Here, we offer some perspectives on what we see as areas of lingering concern, and how we believe investors can best navigate this complex, shifting backdrop.

We have come through an extended period in which style factors have been the main drivers of performance across global equity markets. For several years, it was largely growth and momentum factors that drove stock markets higher, with a significant assist from central bank policies.

In late 2020 and early 2021, we saw a rotation into cyclicals and value stocks, as part of the *re-opening trade* after vaccine approvals and rollout. More recently, the energy and information technology sectors —strange bedfellows indeed — have led market performance.

Weighing Uncertainty

In aggregate, the global equity market has performed exceptionally well over the past of couple years, but today we see some particularly challenging areas. As investors, we must wrestle with and weigh the following questions:

- Have we already seen peak growth and will the impact of the Delta variant be greater than expected? We have recently seen a number of downgrades to countries' GDP forecasts.
- Will inflation eat into corporate profit margins and consumer spending at deleterious levels?
- Do the recent weak U.S. nonfarm payroll figures suggest companies are more cautious on their outlooks?
- Will the impending tapering by the U.S. Federal Reserve eliminate much of the liquidity that has driven financial markets throughout the pandemic?
- What risk do the extensive supply chain disruptions and semiconductor shortages pose to the global economy and the ability of supply to meet demand?
- How concerned should we be about the prospect of contagion from the Chinese property sector or a stalemate on the U.S. debt ceiling?

Given these significant areas of uncertainty, international equity investors may be wondering about the right positioning for their portfolios going forward. Would it be more opportune to lean into growth, pile into value or bet on cyclicals? Or even, possibly, add to emerging market positions following the weakness in China's equity market?

As we see it, for suitable investors the answer may be to pursue a core, blended portfolio approach that features both long-term compounders together with sustainable cyclical and value opportunities. Unlike many other international equity managers, our views on China and emerging markets have been cautious. Likewise, we have not favored growth stocks whose valuations, in our view, have been driven skyward by low interest rates.

Favoring Disciplined Active Managers

We believe that we are now in an environment that favors disciplined bottom-up active managers. We continue to expect that international equities will outperform their U.S. counterparts in the coming years, given their more attractive valuations that can help drive an overdue geographical rotation. We favor companies with strong, sustainable business models and solid balance sheets that will, in our view, be better positioned to navigate the shifting scenarios currently challenging the global markets.

Bottom line: In this type of complex, shifting macro environment, we believe active management — featuring a bottom-up approach to stock selection — is the best way to navigate the challenges, uncertainties and opportunities presented by the global marketplace.

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Active management involves risk as it attempts to outperform a benchmark index by predicting market activity, and assumes considerable risk should managers incorrectly anticipate changing conditions.

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