

# Timely insights from portfolio managers and industry experts on key financial, economic and political issues.

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## 2022 Outlook: Global Environment Favors Quality Stocks in Non-U.S. Markets

**London** - The increase in market volatility, driven by the Omicron variant, is yet another reminder that navigating global equity markets is likely to remain challenging in 2022. We believe, however, that higher-quality companies,<sup>1</sup> particularly those in international markets, may offer active managers attractive stock selection opportunities.

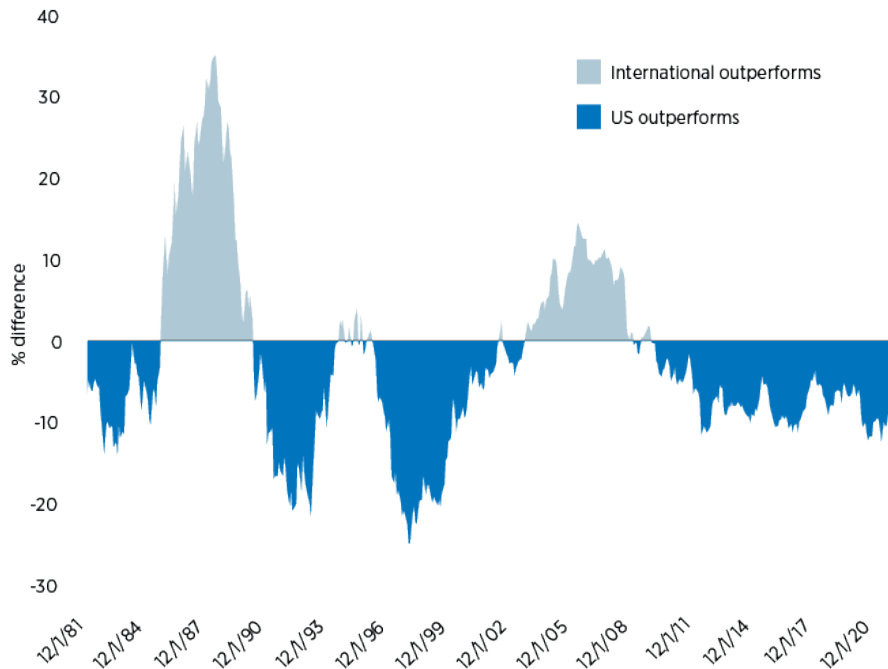
Along with COVID variants, countries and companies must contend with slower economic growth, ongoing supply chain issues and stubborn cost inflation. While uncertainties and risks persist, we think quality companies with consistent earnings growth and well-established market positions may be better equipped to withstand enduring pricing and supply pressures.

Moreover, in view of stretched U.S. stock market valuations, and the fact that international stocks have lagged U.S. stocks since 2009, we think the reins of market leadership may pass to international stocks in 2022 (Exhibit A).

Exhibit A

### Time for a Rotation in Leadership?

U.S. stocks have outpaced International stocks since 2009



Source: Zephyr Style Advisor, monthly data as of 11/30/2021.



**Christopher M. Dyer, CFA**  
 Director of Global Equity  
 Portfolio Manager  
 Eaton Vance Equity



**Ian Kirwan**  
 Global Equity Analyst  
 Eaton Vance Advisers  
 International Ltd.

"On a regional basis, we expect potentially solid economic growth across developed economies in 2022, albeit at a slower pace than the recovery-driven levels seen in 2021."



than the European Central Bank and the Bank of Japan. With inflation easing but still higher in the U.S. than in Europe or Japan, we expect U.S. real yields to rise at a faster pace than European and Japanese real yields. This could pressure U.S. equity valuations, which trade at a seemingly ever-expanding premium to their international peers.

### **Areas of opportunity for 2022**

Consistent with our outlook, we think there is significant potential in European markets and less opportunity in the U.S. Positioning in our global and international equity strategies reflects these views. In terms of sectors, we see potential value in select industrial and health care companies, particularly those with sustainable business models and leading market positions. We also see opportunity in high-quality companies that may be likely to benefit from the post-pandemic economic recovery or that trade at what we believe are artificially or temporarily depressed valuations. As always, reliable compounders form the backbone of our strategies.

**Bottom line:** Although global stock markets will likely face a range of socioeconomic challenges in 2022, we think international equities may be poised to outperform U.S. stocks, and that an active, high-quality investment approach may prove advantageous.

1. Higher-quality companies typically have consistent earnings, strong balance sheets, significant free-cash-flow generation, growing revenues and meaningful competitive advantages, whereas the opposite is true for their lower-quality counterparts. Historically, high-quality equities have outperformed over full market cycles.

2. Real yield is the nominal yield of a bond minus the rate of inflation.

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