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

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Equities

Seizing Opportunity with Value Equity in 2022

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Boston - Our research shows that value equity indexes —with their heavy weighting of cyclically sensitive sectors such as finance, energy and basic materials — tend to outperform during expansionary, reflationary economic periods. Today, the implied yield curve may well be signaling the start of another U.S. economic expansion — a positive portent for value equities. We believe that adding some value equity as a diversification[1] hedge against other more correlated assets will ultimately prove to be a path to building better outcomes.

"Adding some value equity to portfolios as a diversification hedge against other more correlated assets may ultimately be the path to building better outcomes for investors."

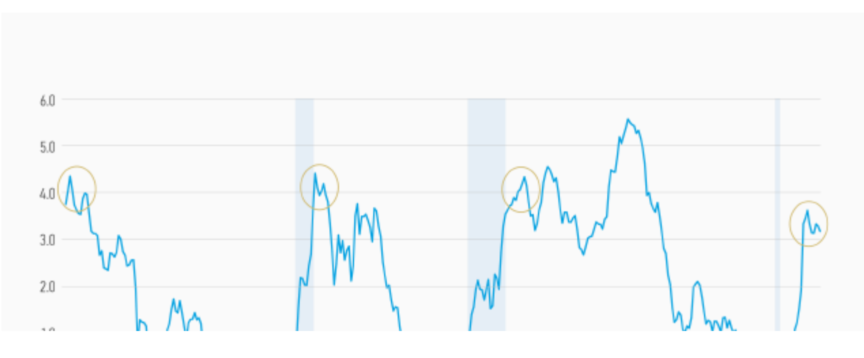
Stars potentially aligning for value equity...

While our *Opportunistic Value* investing approach focuses on individual stock picking, the U.S. macroeconomic backdrop is setting up to favor value equities, broadly. Our research shows that value equity indexes —with their heavy weighting of cyclically sensitive sectors such as finance, energy and basic materials — tend to outperform during expansionary, reflationary economic periods. These periods of outperformance, exemplified by accelerating profit growth, can often last many years and are often preceded by severe economic contractions such as the one we just experienced (see outperformance of Russell 1000 Value from 1981 to 1986, 1992 to 1993, 2000 to 2006).[2]

One common feature marking the onset of past U.S. economic expansions has been a steepening of the U.S. yield curve (Display 1). Typically, as the U.S. begins to recover, monetary authorities remain accommodative on the short end, while longer-term nominal rates (including their embedded inflation premium) tend to remain more elevated —steepening the curve. As shown below, the implied yield curve today may be signaling the start of another U.S. economic expansion — a positive portent for value equities.

Display 1: U.S. Economic Expansions Generally Begin with a Steep Yield Curve

Ten-Year Treasury Bonds Versus Shadow Fed Funds Rates 1992 Through Mid-November 2021



The key point is that the status quo bias inherently ignores the potential generational shift of future inflation, the drivers behind it and the wide-reaching impacts of higher interest rates across the yield curve. We believe this creates ample opportunity for alpha generation.

Bottom line: Our philosophy targets strategically advantaged companies with high investment returns and strong cash flow generation. We look to invest in the stocks of these companies when they are out of favor or misunderstood by the broader market and, therefore, trading at a discount to intrinsic value — an approach we refer to as *Opportunistic Value* investing. We leverage our dedicated team of equity analysts, with an average of over two decades of experience, to find these opportunistic values. When we do find them, we invest with conviction, and we use a series of team disciplines to fight complacency and remain on an opportunistic footing for our investors.

1. Diversification does not eliminate the risk of future loss.
2. The index performance is provided for illustrative purposes only and is not meant to depict the performance of a specific investment. Past performance is no guarantee of future results.

Russell 1000® Value Index is an index that measures the performance of those Russell 1000 companies with lower price-to-book ratios and lower forecasted growth values.

RISK CONSIDERATIONS

Investing entails risks and there can be no assurance that any strategy will achieve profits or avoid incurring losses.

There is no assurance that a portfolio will achieve its investment objective. Portfolios are subject to market risk, which is the possibility that the market values of securities owned by the portfolio will decline and may therefore be less than what you paid for them. Market values can change daily due to economic and other events (e.g. natural disasters, health crises, terrorism, conflicts and social unrest) that affect markets, countries, companies or governments. It is difficult to predict the timing, duration, and potential adverse effects (e.g. portfolio liquidity) of events. Accordingly, you can lose money investing in this portfolio. Please be aware that this portfolio may be subject to certain additional risks. In general, equities securities' values also fluctuate in response to activities specific to a company. Stocks of small-and medium-capitalization companies entail special risks, such as limited product lines, markets and financial resources, and greater market volatility than securities of larger, more established companies. Investments in foreign markets entail special risks such as currency, political, economic, market and liquidity risks. Illiquid securities may be more difficult to sell and value than publicly traded securities (liquidity risk). Non-diversified portfolios often invest in a more limited number of issuers. As such, changes in the financial condition or market value of a single issuer may cause greater volatility. The impact of the coronavirus on global markets could last for an extended period and could adversely affect the Fund's performance.