January 15, 2021
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Todd Asset Management

# A Synchronized Global Recovery

*Todd Asset Management Q4 2020 International Market Commentary*

| | 4Q 2020 | 1 Year | 3 Year* | 5 Year* | 7 Year* | 10 Year* |
|---|---|---|---|---|---|---|
| MSCI ACWI ex-US (Net) | 17.0% | 10.7% | 4.9% | 8.9% | 4.8% | 4.9% |
| MSCI ACWI (Net) | 14.7% | 16.3% | 10.1% | 12.3% | 8.9% | 9.1% |
| MSCI ACWI ex-US Value (Gross) | 20.5% | -0.2% | 0.2% | 6.3% | 2.4% | 3.4% |

* *Annualized Total Returns.*

International markets performed well through the fourth quarter of last year, and the MSCI ACWI ex-US Index, led by the Emerging Markets, outperformed the S&P for both the quarter and the trailing six month period. We believe this recent outperformance is probably the beginning of a new cycle where International Markets should outperform the US Market as a synchronized global recovery starts and cyclical forces shift to favor them. This good performance comes despite mixed news on the Pandemic negatively impacting consumption in most of Europe and Japan. Concerns that weighed on sentiment during the fall were resolved. The Brexit deal was negotiated. Concerns of a ramp up in trade tensions with China abated after the US election went for Mr. Biden. Commodity prices continue to firm and interest rates moved up as anticipation of an economic recovery continue to grow. China continued to see an economic recovery and is thought to have actually eked out modest year over year GDP growth in the fourth quarter, making them the best performing economy in the world last year.

Global economies are in the first inning of a recovery. Following a fierce pandemic recession, the combination of government spending, extraordinarily low interest rates and pent up demand should lead to a reflation and recovery to start a new economic cycle. All of these elements are in place now and investors are waking up to the fact that growth cycles usually last years. Some points we would make about the current environments include

- Current indicators suggest worldwide economies continue to improve. Commodity prices (copper, oil etc.) and early cycle stock markets (Korea) have been strong since November. The Citigroup European Economic Surprise index remains near all-time highs. Lockdown depressed International growth is expected to surpass US growth in the second half of the year.
- Coincident with the new economic cycle, a value cycle is beginning. It should benefit international investors. The Energy and Financial sectors improved to join Technology, Industrials and Materials as the leadership last quarter. This is a significant change from earlier in the year providing evidence that a value rotation is occurring.
- The dollar has been weaker, as investors anticipate larger fiscal and current account deficits. A weaker dollar usually leads to outperformance of International Markets versus the US, and we believe that will occur now as well. Those cycles normally last 7 to 10 years.
- More stimulative policies are expected in the US (which should aid international companies exporting to us) and in foreign markets. The EU Recovery fund is being launched.

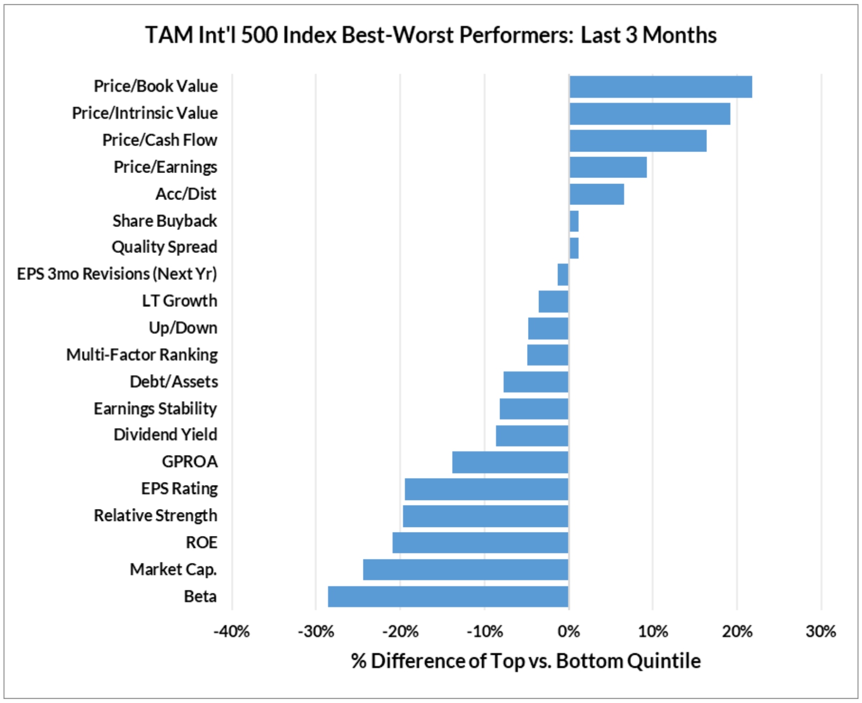
Meanwhile, Japan, the UK, China and many others are pursuing fiscal and monetary stimulus. These programs should boost growth for the next few years.
- The ACWI ex-US has outperformed the S&P 500 since May, when the dollar began to weaken. Coincidentally, the dollar began weakening when the idea of the EU recovery fund was introduced.

There are potential concerns to be aware of:

- Markets and international currencies have surged, and may consolidate after a strong run.
- Pandemics are unpredictable, and new variants could accelerate infection rates.
- Later this year there could be a "Taper Tantrum" as worldwide fiscal stimulus remains strong, but should taper off after vaccinations and a return to normal. Worldwide monetary stimulus is strong, but could taper after the pandemic as well.

The MSCI ACWI ex-US index has not broken its' old high yet, which was set in 2007 but it has risen above the 2018 highs. Considering the economic recovery is only beginning, we are optimistic that it should be able to continue improving. Many of the leading countries within the index have jumped to new highs. Germany is at new highs, while Japan, China and the Emerging Markets ETF are all at multi-year highs. Looking forward, if we are at the beginning of an economic expansion and experiencing dollar weakness, International economies should have the potential for better growth and their markets should benefit from those trends as well.

## ***Factor Analysis***

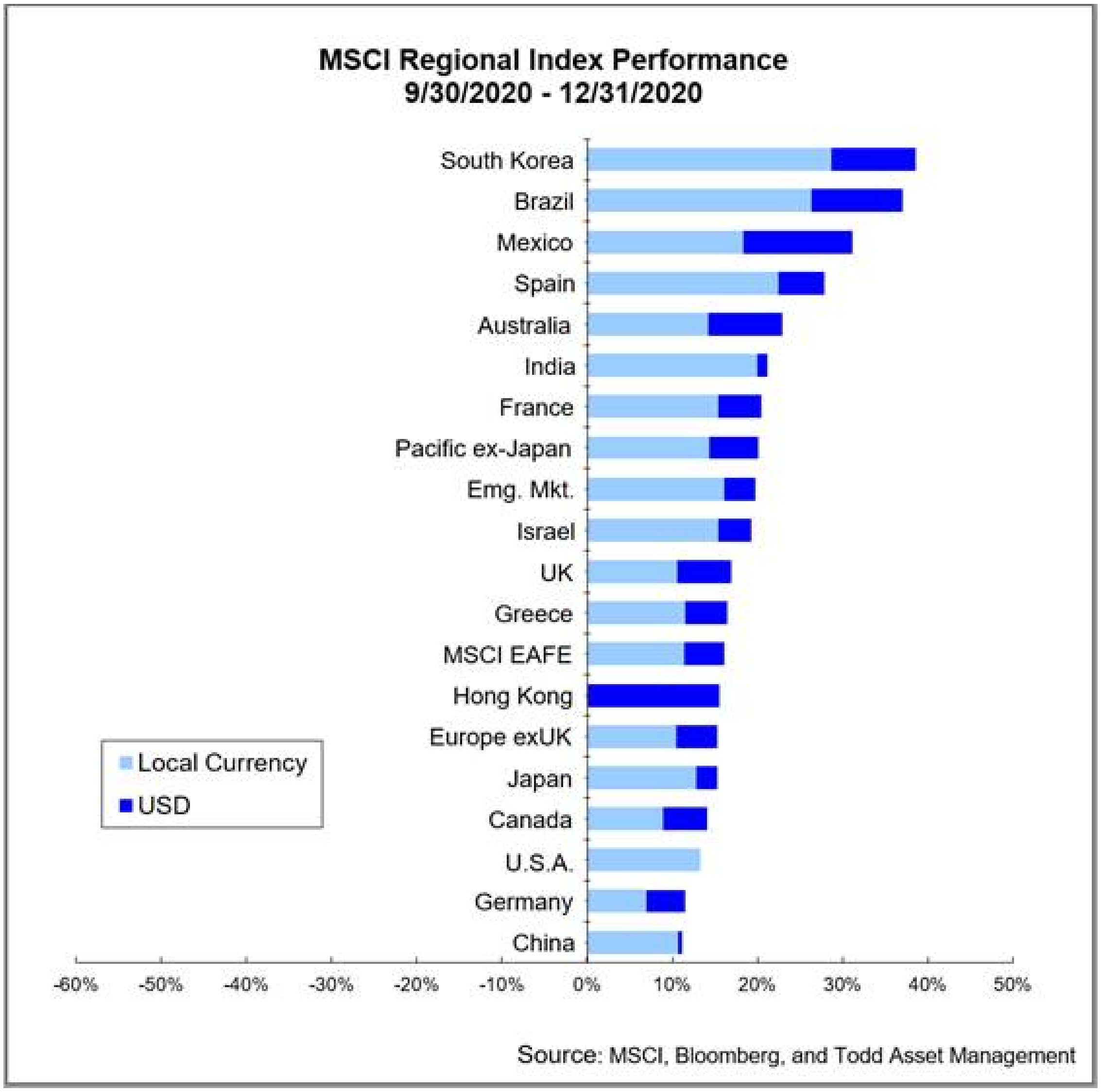




The rotation we highlighted above was most evident in the factors leading during the fourth quarter (chart left, top). All valuation metrics except dividend yield were rewarded during Q4, while growth and most momentum measures were not. Comparing that with the year to date period (chart left, bottom) you can see that this was a dramatic shift. With the improved visibility surrounding economic growth, we believe this shift is going to have some legs to it and should last some time.

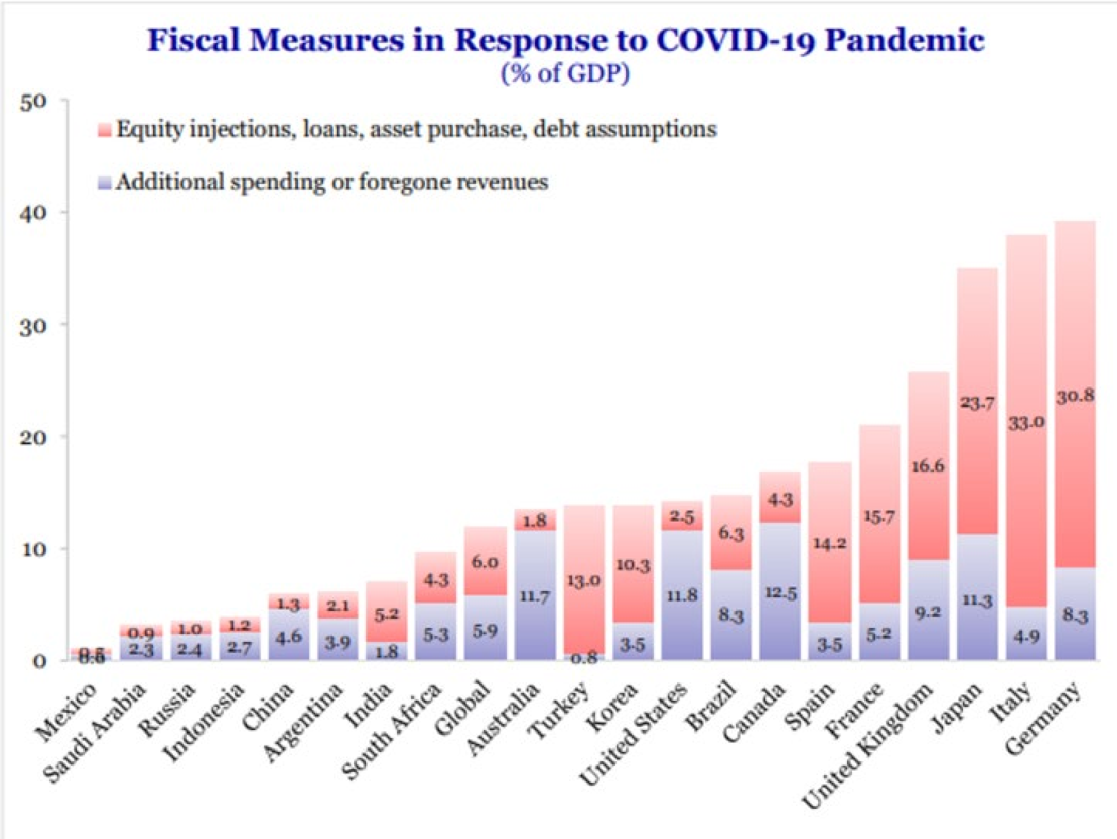
Source: Bloomberg, William O'Neill + Co. and Todd Asset Management

***Regional Performance***




All markets gained during the last quarter, and pay attention to the scale that they gained on. The largest developed markets look like they were weak links on the chart above, but still gained 0ver 10% for the three month period! Commodity driven markets (Latin America, Australia) were the leaders in the fourth quarter as commodity prices improved and an inventory build on electronic components led to more confidence in the South Korean market. Those markets gained on the order of 25-40% during the quarter.

***Interesting Charts we saw this quarter***



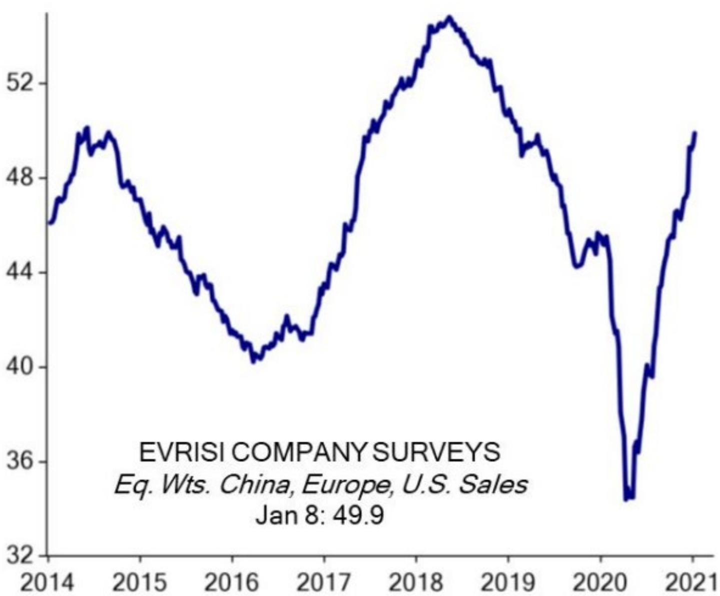

Source: IMF

Many nations aggressively addressed the pandemic with government aid. The scale of these support operations was unprecedented, and should have long tailed impacts for the economy and markets.


Global central banks are being supportive and short term interest rates have set new lows recently. They are backing up low rates with further bond purchases as well. Rates are likely to remain low until economic growth sustainably picks up.

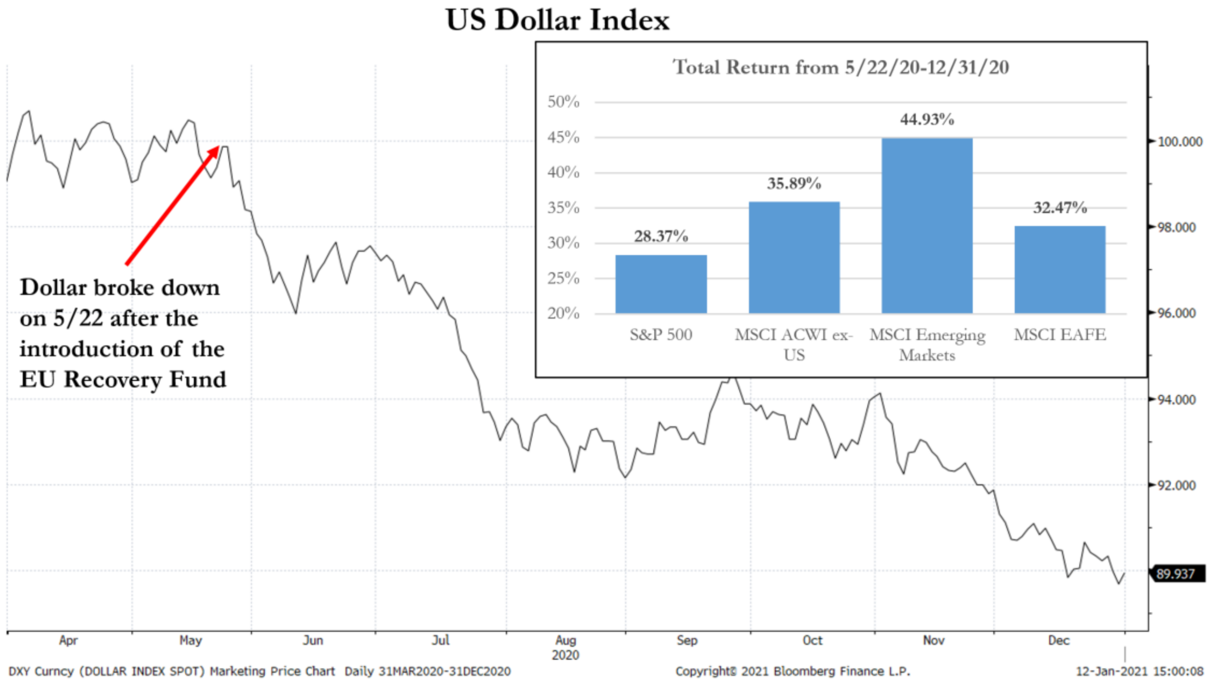
Source: Evercore ISI

**Synchronized Global Growth**

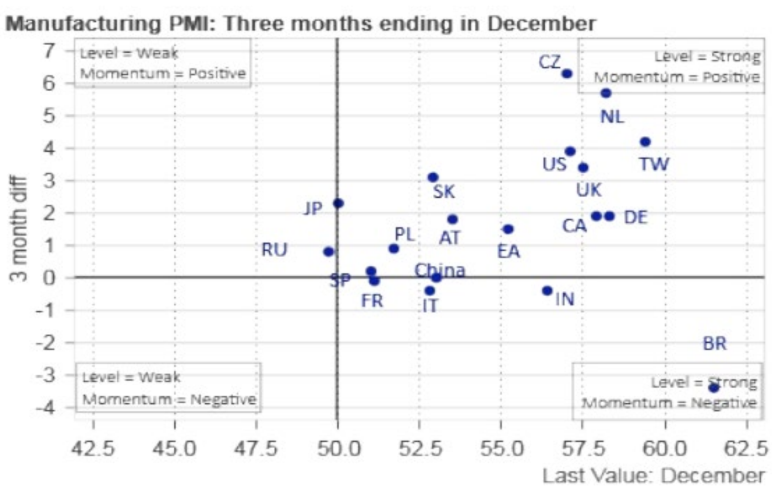



Global Company Surveys indicate that sales are generally improving compared to expectations. This is a precursor to globally synchronized growth, like we saw in 2016-2018. That episode was forcibly truncated by the trade war. Absent another trade war, we believe this episode could last longer since world economies are just exiting recession.

Source: Evercore ISI




In past reviews, we have noted that a weaker dollar has correlated with stronger international stock market performance. Following the EU Recovery Fund introduction in May, risk of the EU disintegrating lessened considerably. This (and greater US deficit spending) led the dollar to decline by approximately 10%. Since then, International markets have been beating the S&P 500, led by the Emerging Markets. We believe this outperformance can continue for quite a while.




Source : Deutsche Bank, Markit, Macrobond

Global Purchasing Manager Indexes (chart left) generally are showing manufacturing economies expanding (right of the crosshairs is expansion) and accelerating (above the crosshairs is accelerating.) When vaccines are widespread we expect the Services counterpart to this to improve as well.

***Summary***

Over the short term, there are some worrisome signs of frothy sentiment within the market. We've all seen bitcoin spike, new IPOs surge, and the recent memory of the FANG stocks is fresh in most investors' minds. We would not be surprised if the market pulled back or simply tracked sideways at some point early-mid 2021 as investors begin to wrestle with the implications of Europe and Britain implementing their separation agreement and a new administration in the US. As we look forward over the coming quarters and years, we are encouraged. The recession and bear market are probably behind us, and a durable economic expansion appears to be starting. We believe the start of this cycle should feature a rotation to favor sectors that have lagged over the past cycle, namely international, value oriented and smaller stocks.

As always, if you need any additional information, please feel free to contact any of us.

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Jack White, CFA
Jack Holden CFA
Shaun Siers, CFA

01/15/2021
MSCI ACWI ex-US (Net) – 285
MSCI ACWI (Net) – 333
MSCI ACWI ex-US Value - 174



***Refer to the following page for more information on the commentary presented. This is pertinent to this letter and should not be reproduced or duplicated without this disclosure.***

The indexes are unmanaged, and not available for direct investment; they include reinvestment of dividends; they do not reflect management fees or transaction costs.

MSCI ACWI ex-U.S. (net) Index is a float-adjusted market capitalization index that is designed to measure the combined equity market performance of developed and emerging market countries excluding the United States. The ACWI ex-U.S. includes both developed and emerging markets. For investors who benchmark their U.S. and international stocks separately, this index provides a way to monitor international exposure apart from U.S. investments. The Net Index takes into account the impact of foreign tax withholdings on dividend income.

MSCI ACWI (net) Index is a float-adjusted market capitalization index that is designed to measure the equity market performance of developed and emerging markets.

The MSCI ACWI ex-U.S. Value (gross) Index captures large and mid-cap securities exhibiting overall value style characteristics across 22 Developed and 26 Emerging Markets countries. The value investment style characteristics for index construction are defined using three variables: book value to price, 12-month forward earnings to price and dividend yield.

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