

Contrarian Investing

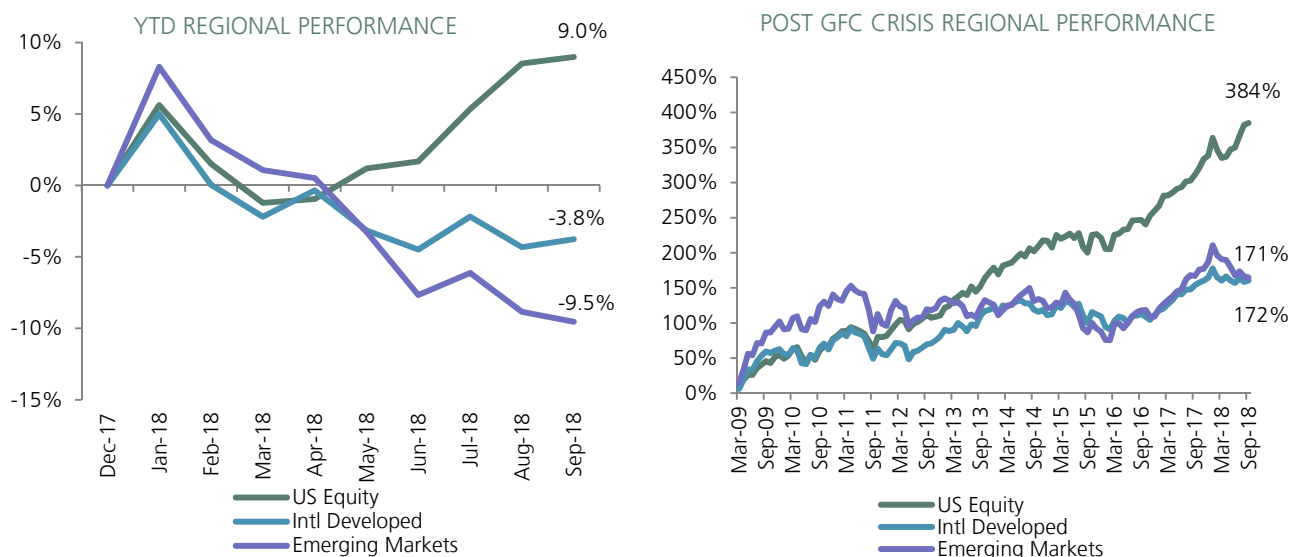
Portfolios built for “easy” times are poorly designed for hard times

Since the Global Financial Crisis, one could classify investing as “easy” and “comfortable”, an environment where investors’ inherent behavioral biases and herd mentality have been rewarded year over year. The idea of contrarian investing, defined as taking positions against the prevailing sentiment of time, which is easily accepted in principal, has become increasingly difficult amidst the trending market where prevailing sentiment continues to be rewarded.

Post- Global Financial Crisis, US domiciled equities with a Growth style orientation, primarily those companies with a consumer technology focus, have been the dominate driver of returns. This has created wide dispersion where the winners have won a lot, and losers have lost a lot, making contrarian investors increasingly uncomfortable **(Exhibits 1 and 2)**. This is an environment where diversification outside of US Growth equities has not paid off. However, taking history as a guide, we know that while markets can get stretched, they always eventually revert. Even though timing these reversions is difficult to impossible, valuations can serve as a gauge of future expected returns **(Exhibit 3 and 4)**. From this standpoint, a contrarian strategy incorporating International and Emerging markets with a renewed focus on valuation and fundamentals looks particularly compelling. More importantly, the potential for diversification benefits has increased as correlations across geographies have decreased **(Exhibit 5)**.

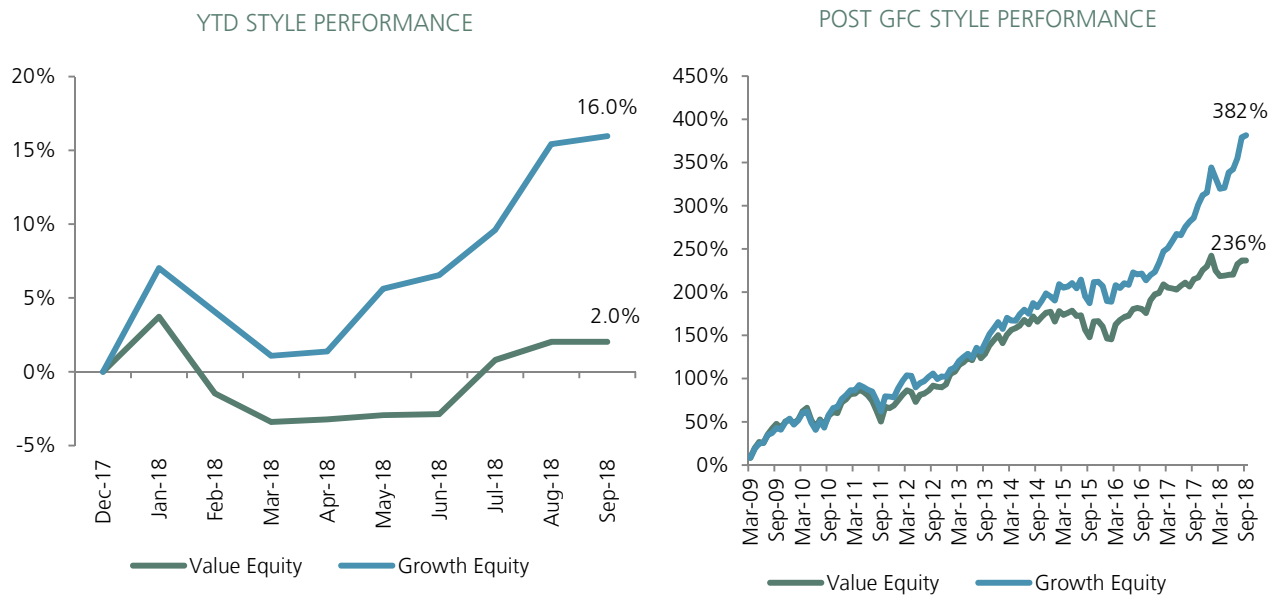
How much more room do you think Growth and US equities have to grow? While the US Growth trend has persisted over the last nine-plus years, a possible reversion in the market may be a stark reminder of the potential benefits of diversification, as portfolios constructed to fully take advantage of the current expansion may need to be repositioned for a change in market environment.

EXHIBIT 1: US vs THE WORLD — INCREASING REGIONAL DISPERSION



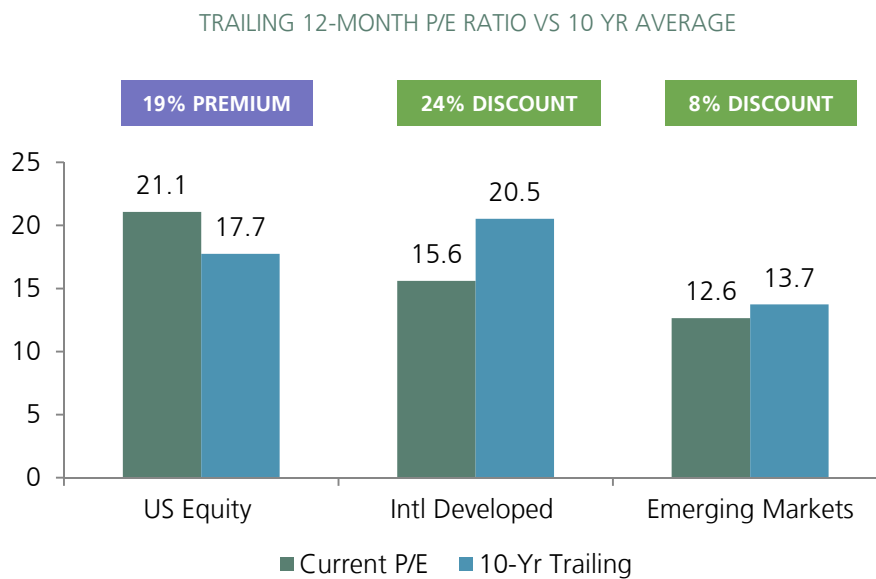
Source: Bloomberg as of 9/30/2018. US Equity (S&P 500 Index), International Developed (MSCI EAFE), Emerging Markets (MSCI EM).

EXHIBIT 2: GROWTH vs VALUE — INCREASING STYLE DISPERSION



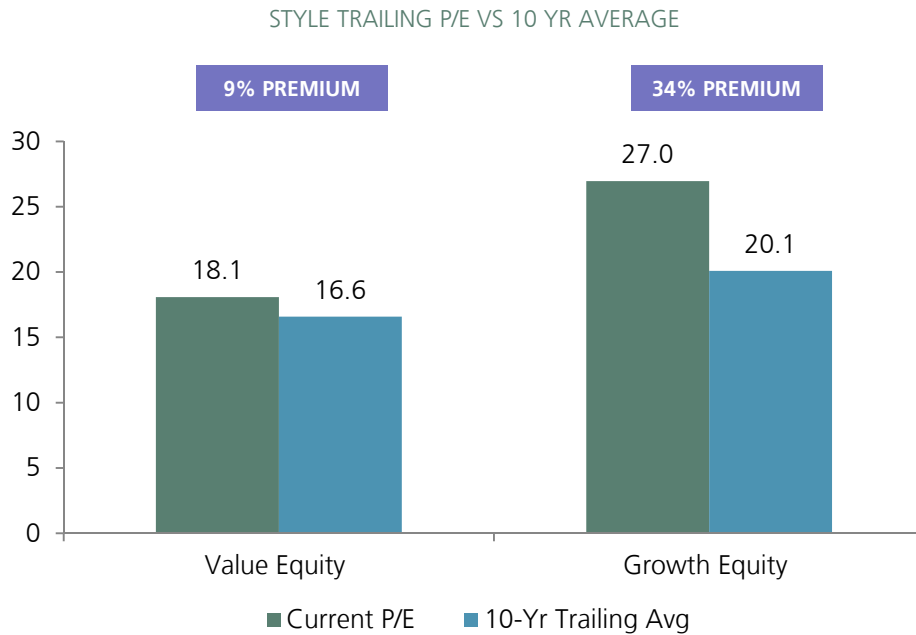
Source: Bloomberg as of 9/30/2018. Value Equity (Russell 1000 Value), Growth Equity (Russell 1000 Growth).

EXHIBIT 3: REGIONAL VALUATIONS — US EQUITIES ARE TRADING AT A SIGNIFICANT PREMIUM TO THEIR 10-YEAR AVERAGE P/E VALUATIONS, WHILE INTERNATIONAL DEVELOPED AND EMERGING MARKET EQUITIES ARE TRADING AT A DISCOUNT



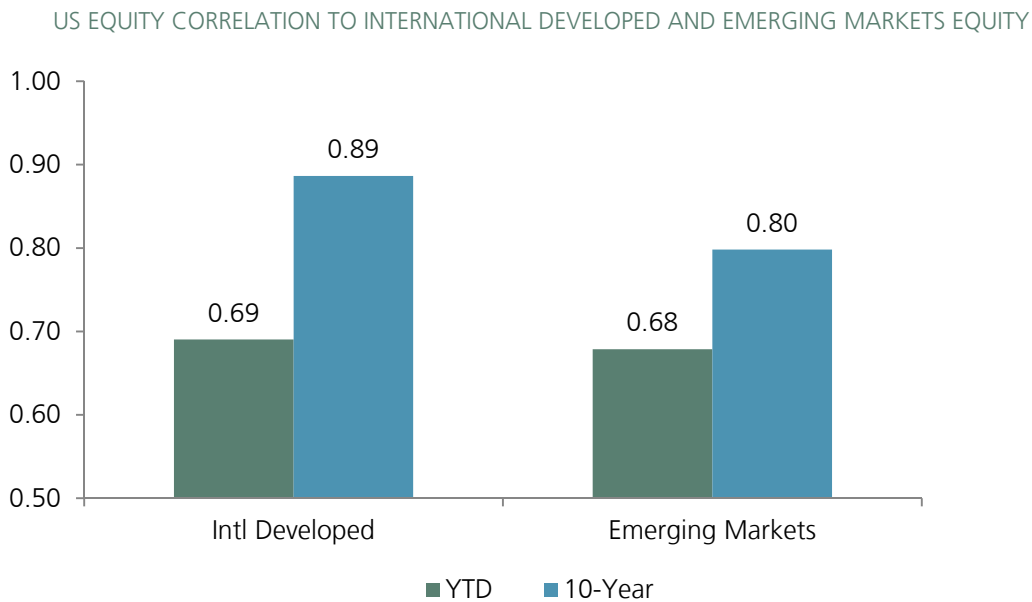
Source: Bloomberg as of 9/30/2018. US Equity (S&P 500 Index), International Developed (MSCI EAFE), Emerging Markets (MSCI EM).

EXHIBIT 4: STYLE VALUATIONS – GROWTH IS TRADING AT A 34% PREMIUM TO ITS 10-YEAR TRAILING P/E AVERAGE, WHILE VALUE IS TRADING RELATIVELY IN-LINE WITH ITS RESPECTIVE 10-YEAR TRAILING P/E AVERAGE



Source: Bloomberg. Trailing 12-month P/E Valuation as of 9/30/18.

EXHIBIT 5: CORRELATIONS — THE CORRELATION BENEFITS OF DIVERSIFYING ACROSS REGIONS HAVE INCREASED



Source: Bloomberg and eVestment as of September 30, 2018. US Equity (S&P 500 Index), International Developed (MSCI EAFE), Emerging Markets (MSCI EM).

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QSCR 18261 (October 2018)