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WHY INVESTORS SHOULD THINK GLOBALLY

FIRST PUBLISHED APRIL 2024

With US equities enjoying a sustained period of dominance over their international peers, some investors have questioned the wisdom of looking beyond US shores, preferring instead to stick exclusively with the world's dominant market. Whilst this approach is perhaps understandable, we think it risks leaving long-term opportunities on the table.

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The case for investing globally is often framed in terms of "why now", with proponents pointing to shifting macro conditions or other cyclical reasons to look beyond US shores at a given point in time. Today, the argument might focus on the likely persistence of many of the drivers of US outperformance over the past decade, whether valuation expansion, the epic run of the Magnificent Seven, or the strength of the dollar. Advocates of mean reversion, meanwhile, tell us that the stark outperformance of US equities is unlikely to last.

"We think investors risk leaving opportunities on the table by failing to look beyond US shores"

But whilst these are all legitimate, interesting and important questions to be asking, relative calls between markets are notoriously difficult to get right on a consistent basis, let alone time well consistently too. In our view, investors should have exposure to both the US and international equity markets at all times for two separate but closely connected reasons.

The first of these, diversification, is, or at least should be, well understood. In the seventy years since Harry Markowitz introduced the world to modern portfolio theory, diversification has become a bedrock of investor thinking. And with good reason. Done correctly, diversification can potentially allow investors to increase the expected return of a portfolio for the same level of risk.

Of course, when Markowitz labelled diversification as "the only free lunch in finance" he was speaking to the risk/return benefits that accrue from buying uncorrelated assets. Today, the correlation between the US and other developed equity markets is relatively high, so the benefits of diversification are certainly not what they were prior to our globalised era. Only when investors venture into emerging and more esoteric geographies do we see a more material benefit emerge. That said, there is a residual diversification benefit to investing globally that allocators should want to harness: the serving might not be as big but you're still getting your sides for free.

The second and most compelling argument for investing globally is the freedom to pursue the very best investment opportunities regardless of where they happen to be listed. Put bluntly, why would you not want to access to the broadest possible opportunity set? To be solely exposed to the US is to leave some outstanding opportunities on the table. No country has a monopoly on corporate excellence.

Many of the most interesting companies identified by our fundamental company analysis don't have US peers, or if they do they are a rather pale imitation. Just as there are no international equivalents of the Silicon Valley behemoths, there are no US analogues of the storied French and Italian luxury houses. Asian savings and protection? Industrial automation? Fashion and beauty? All long-term opportunities with market-leading exponents domiciled outside the US.

"Investors should have exposure to both the US and international equity markets at all times"

Nor are these businesses narrow plays on domestic economies. Overwhelmingly, they are global multi-nationals deriving a significant proportion of their sales and earnings from countries other than where they are listed. You're unlikely to be investing in a Japanese automation business for exposure to the Japanese economy or a Danish pharmaceutical firm solely for the domestic healthcare opportunities.

"Why would you not want to access to the broadest possible opportunity set?"

It goes without saying that this bottom-up approach to global equity investing demands rigorous analysis of all *stock-specific* opportunities and risks. This includes paying due consideration to the impact of geopolitics, an issue very much front of mind for US sceptics of global investing.

At a portfolio level, rather than look at events such as Ukraine or the Middle East through the prism of geography or sector, we think it more relevant to consider risk exposure by the potential for value impairment across stocks, and then aggregate this up. To think of China-Taiwan risk, for example, only as an Asian phenomenon is to overlook the severe ramifications for those US tech companies entirely dependent on Taiwanese chip manufacturers. Better to understand how risk is expressed across real-world businesses, then stocks, then the portfolio. Globalisation may be in retreat, but the world is still incredibly interconnected.

The myriad links and chains in the global economy are an inconvenient truth for those who question the wisdom of straying from US shores in an uncertain and volatile world. Ultimately, no amount of US exposure can offer immunity from geopolitical risk. What it can guarantee you, however, is a sizeable chunk of country-specific risk, whether you're 100% invested, overweight or even just at 'market' weight. Risk, just like opportunity, can be found anywhere.

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STOCK EXAMPLES

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