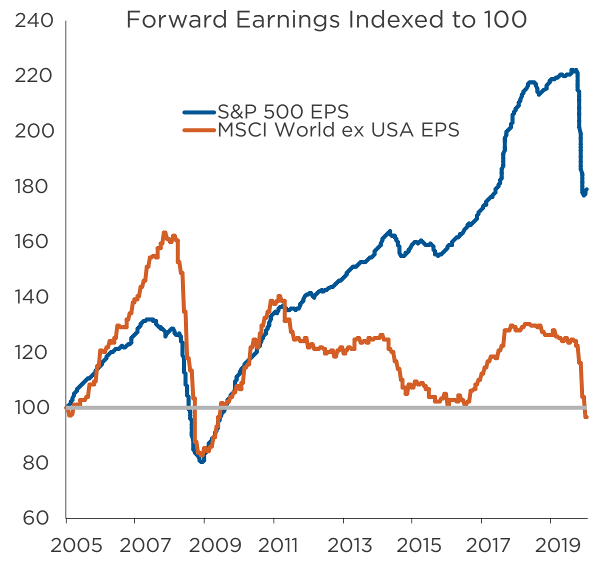
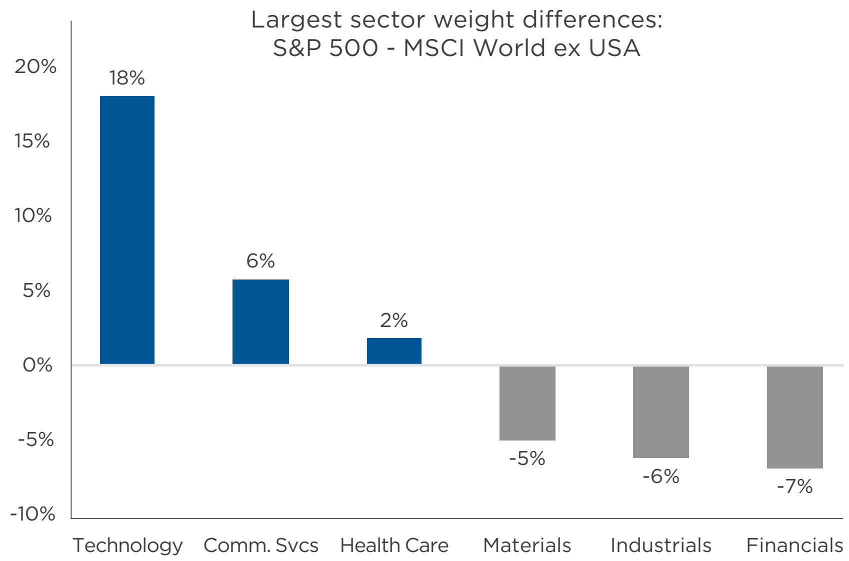
U.S. Likely to Maintain Its Earnings Advantage If Recovery Is Gradual and Uneven





Source: FactSet; S&P 500, MSCI World ex USA next 12-month earnings per share. Sector composition as of 5/31/2020.

QUARTERLY MARKET OUTLOOK: **THIRD QUARTER 2020**

International Outlook

Q2 likely marked the steepest drop in global economic growth since WWII, with 95% of countries projected to experience a decline in GDP.* Absent a medical breakthrough, we expect the recovery to be gradual, uneven and likely slower than the consensus assumes.

From recession to recovery – Most major economies will likely experience a sharp snapback in activity in Q3, but we expect growth to be gradual and uneven as pent-up demand fades. Economic activity will likely take years to reach pre-pandemic levels. The pace of the recovery will largely depend on how well countries manage the ongoing health crisis, which will determine how fast consumer confidence and jobs return.

Fiscal and monetary policy to stay supportive – World governments and central banks have taken sizable measures to provide relief, but more support is likely needed. U.S. policymakers are considering additional fiscal relief on top of stimulus measures that accounted for 14% of U.S. GDP. Europe is also stepping up its efforts, announcing a proposal for common bond issuance among member countries for the first time in the EU's history.

Balancing earnings against valuation differences – Corporate earnings outside the U.S. struggled to gain traction during the last economic expansion and have now taken a hit because of the pandemic. International indexes are weighted more heavily toward cyclical sectors such as financials and industrials that depend on above-average global growth for improved relative performance. The U.S. equity market is likely to maintain its earnings advantage as its equity market is tilted toward sectors with more resilient earnings streams. We believe discounted international valuations will unlock value in the long term, but we don't currently see a catalyst for this.

▶ *Action for Investors*

We recommend a neutral allocation to international equities and an underweight allocation to international fixed income. While international equities are trading at discounted levels, the macroeconomic backdrop and relative earnings trends act as headwinds, in our view. Global diversification can help moderate volatility and position portfolios for long-term growth.

*Sources: IMF, World Economic Outlook Update, June 2020.

Special risks are inherent to international investing, including those related to currency fluctuations and foreign political and economic events.

Diversification does not ensure a profit or protect against loss in a declining market.

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