Why Global Equity?

By Gary P. Motyl, CFA®

The Case for Global Equity Mandates

At a time when the opportunities available to investors are broader than ever, the long-standing practice of separating domestic and nondomestic equity portfolios at the asset allocation level looks increasingly flawed. Consultants have produced scores of studies showing that skillful asset allocation can drive the overall performance of a total portfolio.

We would argue, however, that a global view of equities enables the investment manager to cross borders between emerging and developed countries and to conduct analysis and comparisons between companies in similar sectors around the globe, contributing to more astute and opportunistic investment decision-making. Consequently, we believe the global approach has the potential to drive strong returns over the long term.

Including Emerging Markets

The flexibility inherent in a global view of equities broadens the opportunity set to include emerging market equities. The fundamental case for this asset class is based on high economic growth combined with valuations that remain attractive despite strong performance in recent years. Gross domestic product (GDP) growth in developing countries recently has been double that of developed markets, and we believe strong...
growth in these countries will continue (figure 1).

Other factors working in favor of emerging markets are generally low correlations with developed markets, substantial progress in reducing risk factors for volatility, improving corporate governance, increasing use of generally accepted accounting principles, and favorable demographics that can drive strong growth among emerging-market consumers.

Region, Country, Sector, and Valuation Considerations

Regardless of the country of domicile, companies are increasingly exposed to global influences—whether through their customers, suppliers, or competitors. As a result, sector influences largely have surpassed both regional and country factors in asset allocation decision-making, and global equity returns have been driven increasingly by sector exposure.

In recognition of this development, many large investment firms have reorganized their research units around global economic or industrial sectors with a regional overlay. We believe this approach to research makes sense because it provides a natural structure in support of global mandates, facilitating analysis and comparisons between companies in similar sectors around the world.

This approach also lays the groundwork for more astute decision-making when it comes to finding areas of neglect or inefficiency and, hence, potential undervaluation. We believe those managers who are most successful in determining the magnitude and allocation of forward cash flows and identifying companies where those flows are incorrectly priced should benefit over the long term.

Going Global

A global approach to investment management reflects the rapidly changing and integrating global economy. It also is justified by simple logic: The wider the opportunity set, the better the chances for finding good investments. Indeed, it may be possible to realize higher alpha through a single global equity allocation rather than through the division of assets between separate non-U.S. and U.S. allocations. Viewing equities as a single, global asset class allows for the analytical comparison of valuations and other factors across geographic borders, which can lead to a more attractive risk/return trade-off.

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