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5 Reasons International Equities Are a Compelling Opportunity Now

History is full of surprises and the events of this year are no exception, catching many investors off guard. We expect volatility to remain high due to the economic uncertainty and the fiscal and monetary stimulus that continues to drive equity markets. But while it's impossible to predict the future, it is possible to be prepared.

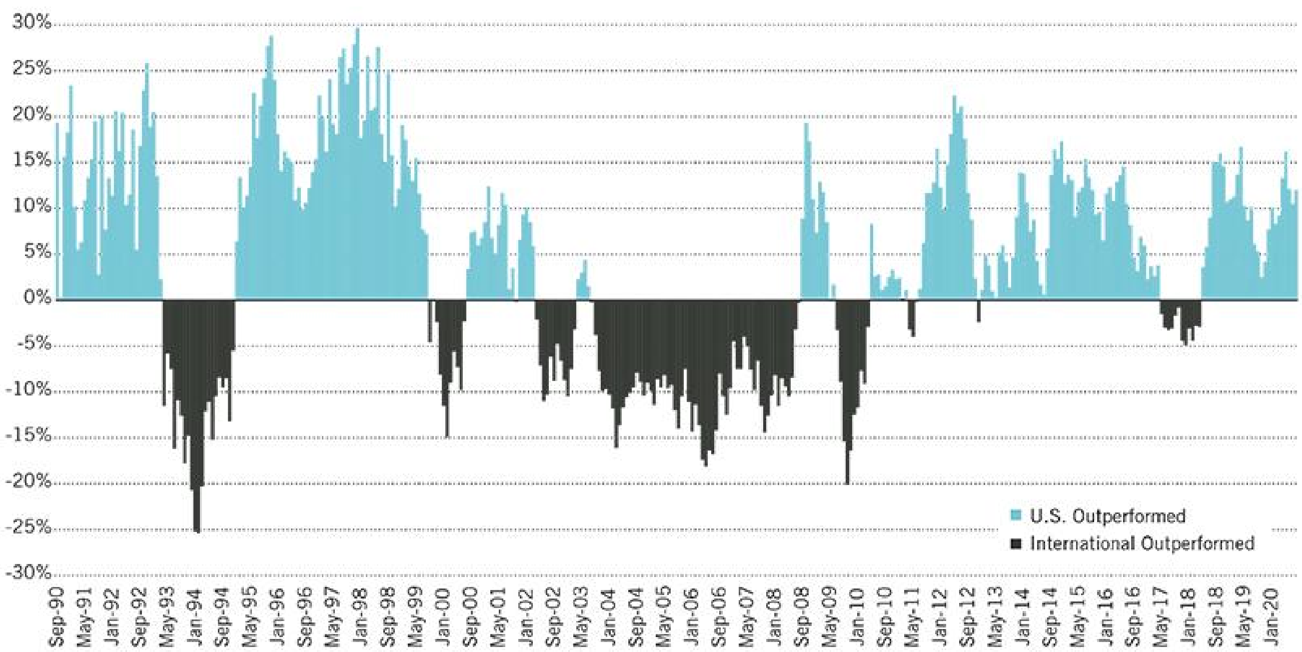
Warren Buffett, the CEO of Berkshire Hathaway who is famed for his preference for investing in America, recently surprised the markets after his company disclosed an allocation of $6 billion to the five biggest trading companies in Japan.

International investing is not just for the Oracle of Omaha. While the U.S. is one of the most dynamic economies in the world and home to leading global companies like Amazon and Alphabet, it is not the be-all and end-all for investors seeking a well-diversified equity portfolio. Although U.S. stocks have outperformed international stocks in recent years, we don't know when market sentiment will shift once again and a change in market leadership will occur.

Historically, international and U.S. stock markets are cyclical in nature. Looking back over the last 30 years, international stocks have at times outpaced U.S. stocks over long stretches. Timing these shifts in market sentiment are virtually impossible. By including both U.S. and non-U.S. exposure in an equity portfolio, investors are optimally positioned to take advantage of growth opportunities around the world.

TAKING TURNS AT THE TOP: U.S. VS. INTERNATIONAL EQUITIES

Rolling 1-Year Excess Returns (S&P 500® vs. MSCI ACWI ex USA)



S&P 500 Index minus MSCI ACWI ex USA Index, as of September 16, 2020. Source: FactSet. **Past performance is not indicative of future results.**

5 reasons why international equities are especially compelling now.

Reason 1: Attractive Valuations

In the post COVID-19 environment, U.S. equities have become relatively expensive, with the MSCI U.S. Index trading at an average of over 20x forward earnings. As a result of the run-up in valuations, international benchmarks are trading at the widest discount to U.S. indices of any point in the last 20 years.

VALUATION GAP BETWEEN MSCI USA AND EX USA INDICES

Forward P/E, September 2000 - August 2020

Source: FactSet.

Reason 2: Diversify Idiosyncratic Risk

The pandemic demonstrates just how severe unknown risks can be, not to mention how widely the effects can vary. While the pandemic is global in nature, not all countries have been impacted to the same extent. Damage to the U.S. economy this year is projected to be greater than to Germany and many Asian economies, and the global recovery will be uneven.

REAL GDP ANNUAL PERCENTAGE CHANGE

		Projected	
	2019	**2020**	**2021**
United States	2.3	-8.0	4.5
Germany	0.6	-7.8	5.4
China	6.1	1.0	8.2
India	4.2	-4.5	6.0
ASEAN-5	4.9	-2.0	6.2

Source: IMF, World Economic Outlook, June 2020. Economies are listed on the basis of economic size. Note: For India, data and forecast are presented on a fiscal year basis with FY2020/2021 starting in April 2020. India's growth is -4.9% in 2020 based on the calendar year

Reason 3: Diversify Currency Exposure

Exposure to international equities can be a good hedge against the risk of U.S. dollar depreciation. Over the past 50 years, U.S. stocks have performed well during periods of U.S. dollar strength, outperforming international equities by 108.7% on average. But during periods of U.S. dollar weakness, international equities have outperformed domestic equities by an average of 31.8%. The dollar peaked at the end of 2016 and has since weakened by approximately 9%. This suggests a good entry point given the average U.S. dollar cycle is 7 years and 9 months. It is reasonable to expect that the currency's decline may continue for another few years, and international equities have actually lagged so far in the current cycle.

USD SPOT (DXY) INDEX

	USD Performance	MSCI EAFE/ ACWI ex US Performance	S&P 500 Performance
9/30/69-6/30/80	-31.2%	95.4%	92.6%
6/30/80-12/31/84	75.0%	23.3%	83.2%
12/31/84-9/30/92	-46.4%	224.7%	226.8%
9/30/92-6/29/01	47.2%	78.2%	248.5%
6/29/01-3/31/08	-39.9%	116.6%	21.9%
3/31/08-12/30/16	42.3%	8.9%	104.7%
12/30/16-7/31/20	-8.6%	25.7%	56.8%

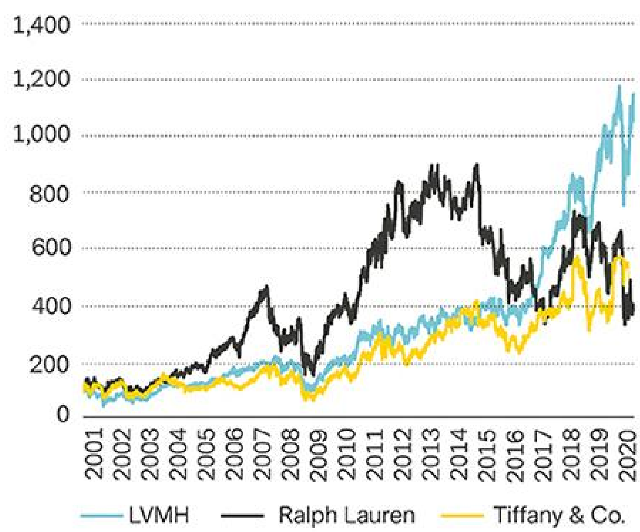
Past performance is not indicative of future results.
See index definitions below. Source: Bloomberg.

Reason 4: Non-U.S. Companies Dominate Certain Sectors

The U.S. is home to many top-performing companies in the information technology and communication services sectors. However, some of the world's most compelling companies in the consumer staples, consumer discretionary, and industrials sectors can be found in Europe, thus providing opportunities for business diversification in a U.S.-biased portfolio. As examples, consider the performance of French luxury conglomerate LVMH or Hong Kong-based hand and power tools manufacturer Techtronic versus their U.S. peers.

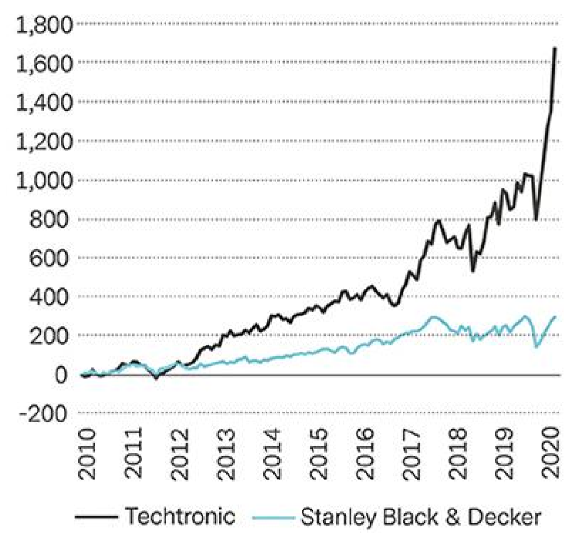
NON-U.S. COMPANIES VS. U.S. COMPETITORS

LVMH VS. RALPH LAUREN CORP. AND TIFFANY & CO.
Total Return January 2001 - August 2020



Source: FactSet.

TECHTRONIC VS. STANLEY BLACK & DECKER
Total Return February 2010 - August 2020



Source: Bloomberg.

Reason 5: A Complement to U.S. Equities

A handful of stocks are increasingly driving performance of the S&P 500® Index. With more people working from home and e-commerce on the rise due to the pandemic, this trend has accelerated even further. As the U.S. market narrows and the S&P 500 continues its climb, a large number of international equities can sensibly complement domestic exposures. It is worth considering that:

- In the U.S., as of September 30, 2020, the "FANGMAN" stocks (Facebook, Amazon, Netflix, Alphabet (Google), Microsoft, Apple, and NVIDIA) have accounted for 32.5% of the S&P 500 returns over the past 5 years, 49.3% over the past 3 years, and 83.8% over the past year.
- In any given year between 2011 and 2019, 38.1% of MSCI ACWI ex USA companies on average beat the S&P 500 while only about half (54.7%) of S&P 500 companies beat the international index on the same metrics during this period when U.S. markets significantly outperformed. This indicates that there are many non-U.S. companies that can enhance a U.S.-only portfolio.

An Active Approach to International Equities

Investors focused on U.S. equities alone are missing out on a world of attractive growth and diversification opportunities. The Virtus Vontobel Foreign Opportunities Fund, subadvised by Vontobel Quality Growth Boutique, uses an active, bottom-up approach to identify great businesses around the world. Vontobel's high-quality approach seeks to provide superior alpha capture with lower risk over full market cycles. By diversifying both idiosyncratic risks and currency exposure, this strategy offers investors the potential for lower overall portfolio volatility and a hedge when the U.S. is lagging broader global markets.

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Index Definitions

The **U.S. Dollar Index (USDX)** indicates the general international value of the USD by averaging the exchange rates between the USD and major world currencies. The ICE US computes this by using the rate supplied by some 500 banks. The **MSCI AC World ex USA Index (net)** is a free float-adjusted market capitalization-weighted index that measures equity performance of developed and emerging markets, excluding the U.S. The **S&P 500® Index** is a free-float market-capitalization weighted index of 500 of the largest U.S. companies. The index is calculated on a total return basis with dividends reinvested. The **MSCI EAFE® Index (net)** is a free-float-adjusted market-capitalization weighted index that measures developed foreign market equity performance, excluding the U.S. and Canada. It was developed with a base value of 100 as of 12/31/1987. The **MSCI USA Index (net)** is a free float-adjusted market-capitalization weighted index that measures the performance of the large and mid-cap segments of the U.S. equity market. MSCI indexes are calculated on a total return basis with net dividends reinvested. All indexes are unmanaged, their returns do not reflect any fees, expenses, or sales charges, and they are not available for direct investment.

Important Risk Considerations

Equity Securities: The market price of equity securities may be adversely affected by financial market, industry, or issuer-specific events. Focus on a particular style or on small or medium-sized companies may enhance that risk. **Geographic Concentration**: A fund that focuses its investments in a particular geographic location will be highly sensitive to financial, economic, political, and other developments affecting the fiscal stability of that location. **Foreign & Emerging Markets:** Investing internationally, especially in emerging markets, involves additional risks such as currency, political, accounting, economic, and market risk. **Market Volatility:** Local, regional or global events such as war, acts of terrorism, the spread of infectious illness or other public health issue, recessions, or other events could have a significant impact on the fund and its investments, including hampering the ability of the fund's portfolio manager(s) to invest the fund's assets as intended. **Prospectus:** For additional information on risks, please see the fund's prospectus.

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