Richard Bernstein Advisors

The Leaders In Pactive® Management

RBA Quick Insights

September 28th, 2023

Is investing really this easy?

At the start of the bull market, nobody wanted to invest in the US

Our firm began managing assets in 2010, in the wake of the Global Financial Crisis. Being the epicenter of the crisis, investor pessimism towards the US was extreme. Confidence in its financial institutions was shaken, and the all-powerful US consumer was facing the dual balance sheet pressures of excessive debt coupled with big declines in asset values stemming from the stock and housing markets. The US was coming off a decade of lost returns, and the US tech sector had underperformed the global stock market by the widest margin on record. As a result, the US traded at a steep discount and its share of global stock markets was at an extreme low.

People preferred to invest in the new engine of global growth

Emerging markets had supplanted the US as investors' most favored stock market, supported by healthier demographics, superior growth, and seemingly better government debt burdens. Emerging markets had also outperformed the rest of the world over the past decade by nearly the widest margin ever (94th percentile). All signals were aligned.

The tides have turned

Thirteen years later, the narrative could not be more different. The dominance of US tech has resulted in one of the best absolute and relative decades of performance in history, with nearly every other major category (especially emerging markets) lagging significantly. The US has had superior earnings growth, and its companies dominate almost every major industry. The tech sector is a juggernaut of innovation and growth, and its dominant profit margins have resulted in some of the strongest balance sheets in the world, with plenty of cash to buy up-and-coming technologies, future rivals and buy back their own shares.

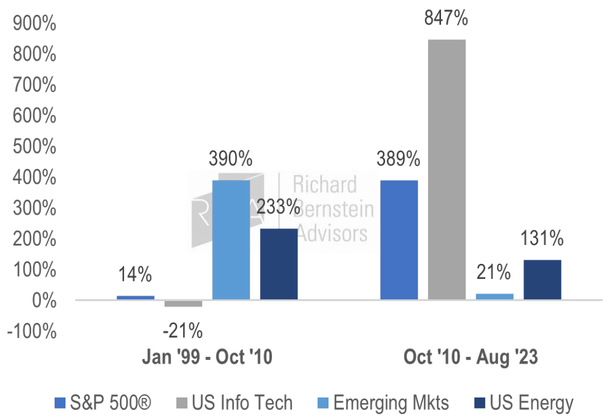
Be careful when Wall Street starts to feel like Easy Street

Since 2010, the S&P 500® and US Tech sector have returned 389% and 847% (14% and 21% per annum), respectively (Chart 1), with valuations (Chart 2) and household equity allocations now near all-time highs, suggesting that investors are positioned for more of the same. What concerns us about investors doubling down on the best trade of the past decade are the numerous historical precedents suggesting that a continuation of these extreme returns is unlikely. Either these time-tested rules no longer apply, and investing is now as easy as simply buying what has worked, or investors are improperly allocated for the next market cycle.

1. **Returns are greatest when capital is scarce:** Extremes in performance and valuations tend to reverse, as it becomes increasingly difficult for results to keep pace with the hype driving expectations. Conversely, investment opportunities that have been left for dead tend to have an easier time exceeding low expectations.
2. **New market cycles come with new leadership:** Major shifts in macroeconomic fundamentals tend to come with new market leadership. This changing of leadership across cycles tends to be accompanied by significant market volatility.
3. **It's never too early to sell a bubble:** It can be difficult to time major market reversals and leadership changes, but the unique aspect to a bubble is that it's never too early to sell. Even if you bought the Nasdaq-100 index a full year before its peak, initially doubling your money, it still took you roughly a decade to recoup your subsequent losses.

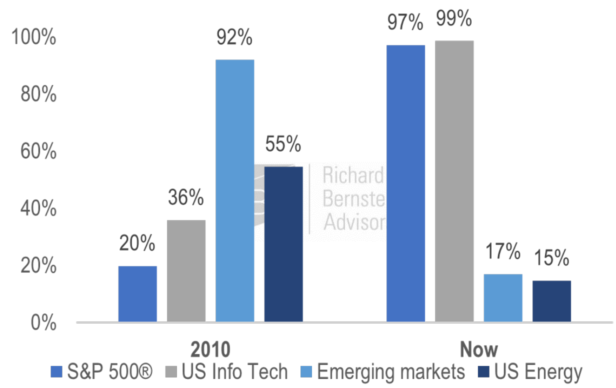
(*Continued on page 2*)

Chart 1: Select total returns: 1999 - 2010 vs. 2010 - Now



Source: Richard Bernstein Advisors LLC, Bloomberg, MSCI, S&P

Chart 2: Relative P/E vs. ACWI (%ile of history since 2005)



Source: Richard Bernstein Advisors LLC, Bloomberg, MSCI, S&P
Note: Percentile of history since 2005 of the forward P/E of each index relative to the forward P/E ratio of the MSCI ACWI index of global stocks.

Dan Suzuki, CFA
Deputy Chief Investment Officer