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Global Equities: Looking to a Brighter Future

With the US election now settled and a COVID-19 vaccine closer than ever, investors can look to a brighter future. And while large market moves could return given the current environment, volatility has often provided an opportunity to build long-term allocations to equities.

Where Are We Now?

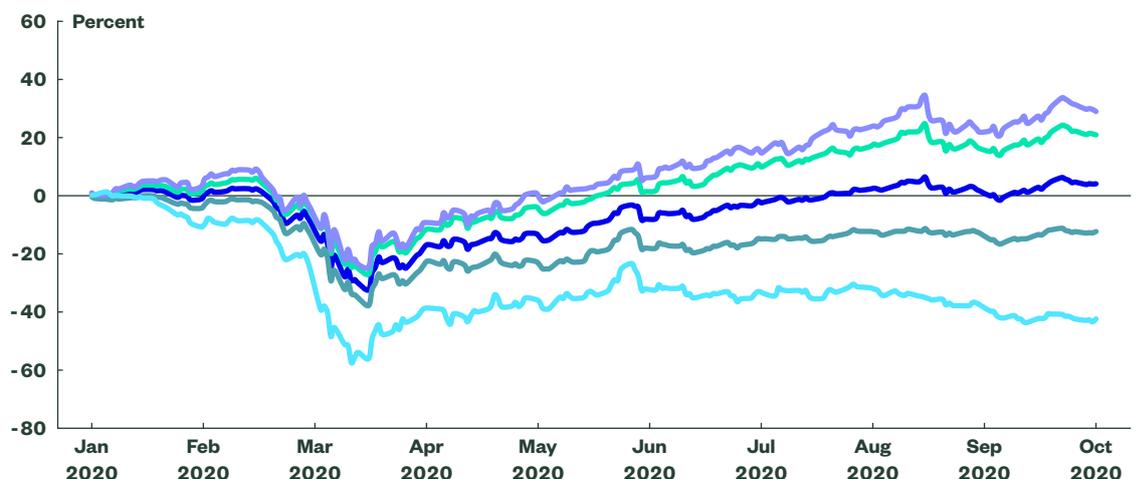
We believe “Business as Usual” returned to equity markets in May when, thanks to support of central banks, financial operations returned to a stable footing, credit spreads narrowed and relatively normal trading volumes resumed. Since then, we have seen a relatively orderly market cognisant of fundamentals. Global equities have followed a broadly upward trajectory on vaccine optimism and better-than-expected economic and corporate earnings results.

Since the market lows, the MSCI ACWI has risen by 53%, giving a net rise of 4% year to date. Within that, global Technology has risen by 32% (NTR) against versus Energy, which has fallen 42% (see Figure 1). Emerging markets are now back to the level where they started the year, with developed markets, driven by the US, performing better.¹

Notably, index recovery has been rather narrow, led by the FAANGs and their related sectors (Technology, Consumer Discretionary and Communication Services). Large dispersions in returns have occurred across equity markets, by sector, country and size; although, the styles of Growth/Momentum/Quality have worked particularly well all year, through up and down markets.² On several occasions there have been sharp sector rotations in favour of cyclicals and Value, but these rotations have not broken through to longer trends, with the necessary growth conditions still missing. Such large dispersions have created opportunities for active investment in equities and could continue to do so for some time.

Figure 1
A Year of Big Moves and Dispersion in Global Equity Markets

- MSCI ACWI
- MSCI ACWI Growth
- MSCI ACWI Value
- MSCI ACWI Energy
- MSCI ACWI Info.Tech



Source: Bloomberg Finance L.P., as of 22 October 2020. Past performance is not a guarantee of future returns.

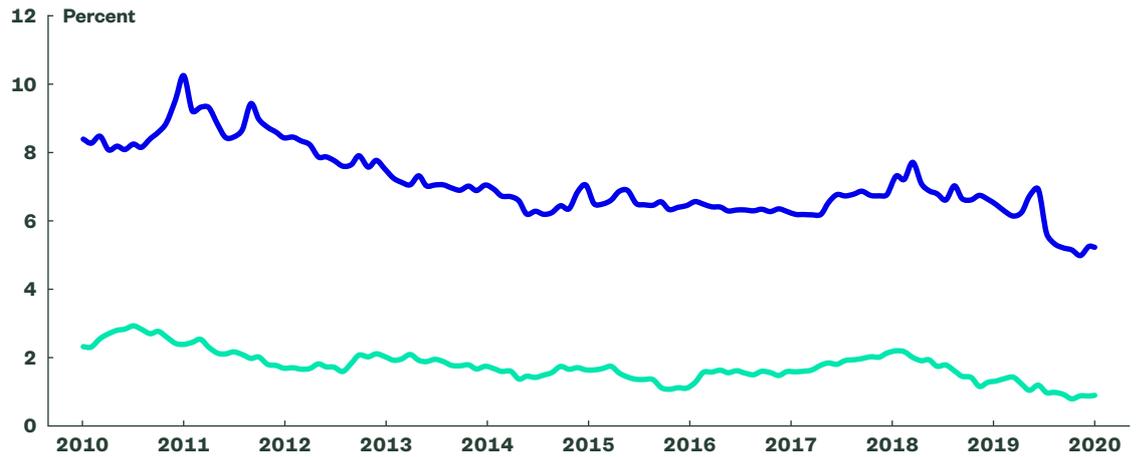
Forecast Returns

Looking to the longer term, equities continue to be a relatively attractive asset class. There has been a strengthening of structural, technological trends during the COVID-19 crisis that could benefit various industries. There is a reasonable amount of slack in economies, which means they can run at a faster pace than would normally be expected over the next few years. Furthermore, there is an opportunity for companies to increase efficiency through a greater reliance on technology.

From a valuation perspective, historically low bond yields offer a cushion against elevated uncertainty, thus allowing companies to access financing more easily. Figure 2 shows that the spread between the earnings yield on global equities and the yield on global bonds is approximately 4%.

Figure 2
Relatively Attractive Spread Remains Between Equities Earning Yield and Bond Yield to Worst (%)

■ Global Equities Earnings Yield 12m Fwd
■ Global Bonds Yield to Worst



Source: Bloomberg Finance L.P., State Street Global Advisors, as of 22 October 2020. Global Equities represented by MSCI ACWI Net Total Return USD Index, Global Bonds represented by Bloomberg Barclays Global-Aggregate Total Return Index Value Unhedged USD. Earnings Yield 12m fwd is reciprocal of 12m fwd BEST P/E. Yield to Worst is Index Yield to Worst. The above targets are estimates based on certain assumptions and analysis. There is no guarantee that the estimates will be achieved.

State Street Global Advisors produces forecast returns for key equity regions using the modelling capabilities of our Investment Solutions Group (ISG). The forecasts take into account core aspects of valuation and do not seek to capture more dynamic factors that can impact pricing. Hence, despite the momentous changes in economic outlook this year, there has not been significant change in forecast returns over longer time periods.

Figure 3
**Absolute Total
Return and Risk
Forecasts
for the Main
Equity Categories**

Asset Class	Short Term 1 Year (%)	Intermediate Term 3–5 Years (%)	Long Term 10+ Years (%)	Long-term Risk (Std Dev) (%)
Equities				
US Large Cap	6 . 6	5 . 6	5 . 7	15 . 2
US Mid Cap	6 . 3	5 . 8	6 . 0	18 . 0
US Small Cap	6 . 0	6 . 1	6 . 2	19 . 5
Europe	5 . 5	6 . 0	6 . 4	16 . 0
European Small Cap	–	6 . 7	7 . 1	16 . 7
Euro	5 . 4	5 . 9	6 . 2	19 . 8
United Kingdom	6 . 0	6 . 4	7 . 0	14 . 9
Japan	2 . 7	2 . 1	3 . 1	20 . 0
World (Global Developed)	6 . 0	5 . 5	5 . 8	14 . 7
Emerging Markets (EM)	8 . 3	8 . 6	8 . 6	21 . 1
EM Small Cap	–	9 . 1	9 . 1	20 . 9
EM Asia	8 . 8	8 . 9	8 . 7	22 . 1
China	10 . 0	10 . 2	9 . 0	33 . 6
Global Equities (ACWI)	6 . 3	5 . 8	6 . 1	14 . 7
Global Equities Small Cap	7 . 1	6 . 6	6 . 9	16 . 8

Source: State Street Global Advisors Investment Solutions Group, as of 30 September 2020. The above universes are based on the MSCI ACWI IMI. The forecasted returns are annual arithmetic averages, data is reported on a gross of fees basis. Additional fees, such as advisory fee, would reduce return. For example, if an annualised gross return of 10% was achieved over 5 years and a management fee of 1% p.a. charged and deducted annually, the resulting return would reduce from 61% to 53%. Performance includes reinvestment of dividends and other corporate earnings and is calculated in the local currency. It does not take into consideration currency effects. The forecasted performance is not necessarily indicative of future performance, which could differ substantially. The above targets are estimates based on certain assumptions and analysis. There is no guarantee that the estimates will be achieved.

These forecasts are forward-looking estimates of real return potential, derived from historical and current dividend yields, forecast real earnings growth rates and potential for expansion or contraction of valuation multiples. The State Street Global Advisors estimates of real earnings growth rates incorporate forecasts of labour, capital and productivity levels. Thus variations in labour, capital and productivity levels result in region-specific differences in estimates, allowing for more region-appropriate forecasts for both developed and emerging market equities.

Another important feature of these forecasts is the inclusion of elements of ESG through leveraging State Street Global Advisors R-Factor® scores. Improvements in a country's aggregated and normalised R-Factor® scores are used to incrementally reduce its risk expectations within the forecast and the other way around.

Asset Allocation

US Equities

The US continues to offer the relatively safest near-term opportunity and is currently the favoured region in ISG's Tactical Asset Allocation model.³ This positioning is supported by the US bias towards corporate quality, in particular balance sheet strength, which we believe is helpful in a more difficult economic environment. There are also important near-term benefits from the country's huge domestic market and diversified economy. While some policy action could be disrupted in the short term by the presidential election, long-term strengths may prevail, helped by the ability to channel necessary fiscal and monetary policies.

In the near term, State Street Global Advisors prefers large cap over small cap equities, given their quality bias and weighting in technology shares, which has helped performance. However, in the longer term there may be more upside from small and mid cap indices, albeit with an increase in risk.

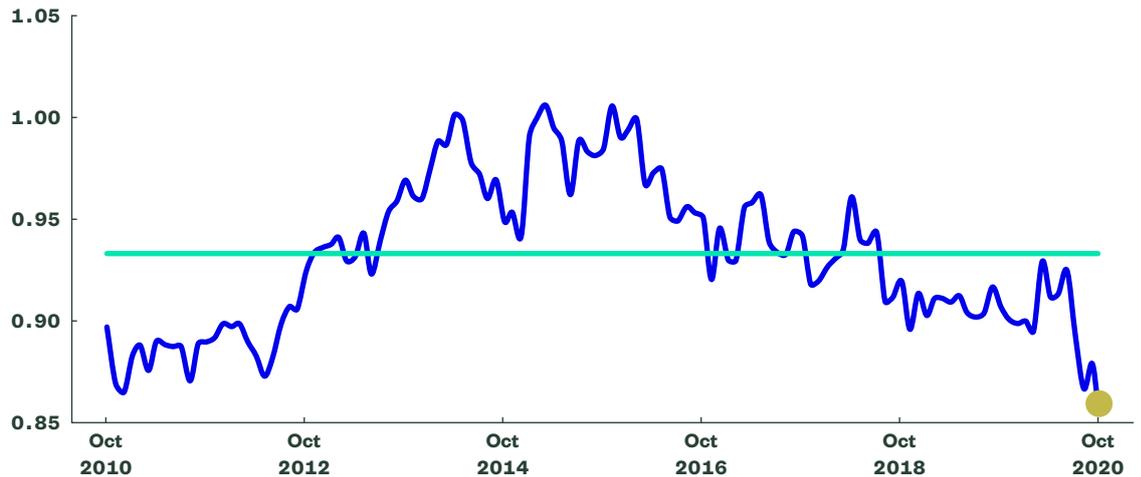
Europe and UK Equities

Europe, with or without the UK, presents a more complex case. The region would be an immediate beneficiary of any cyclical bounce, as seen in market excitement over the summer months this year when the EU announced a EUR 750 billion recovery package. However, the European region is more vulnerable than the US to a renewed economic downturn in light of its greater reliance on trade and foreign economies.

Given its sectoral composition, the European region has a value bias. Figure 4 shows that European equities are trading at a significant discount to their 10-year average P/E relative to global equities.

Figure 4
**European Equities
Appear Undervalued
Against Global Equities**

■ Relative P/E
■ Average Relative P/E
■ Current Relative P/E



Source: Bloomberg Finance L.P., State Street Global Advisors, as of 22 October 2020. Europe Equities represented by MSCI Europe Net Total Return Index, Global Equities represented by MSCI ACWI Net Total Return Index. Earnings Yield 12m fwd is reciprocal of 12m fwd BEST P/E.

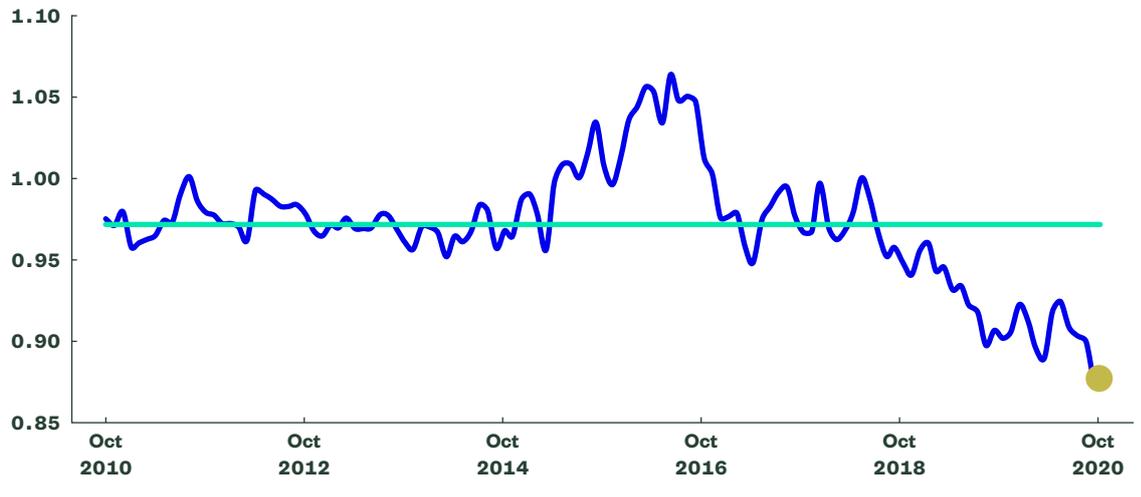
As with other regions, we believe sectors and smart beta factors in Europe may provide opportunities for outperformance alongside pure country selection. Smaller European companies are forecast to return a higher rate than larger companies given business lifecycle dynamics.

Even though forecast returns for the eurozone improve over time, there is still a large, unresolved geopolitical risk surrounding the European Union and, critically, dealing with the exit of the UK.

UK equity markets are at an interesting juncture. The country has experienced a very difficult economic and political period in 2020, causing a derating even deeper than that of Europe (see Figure 5). Forecast returns are better than the eurozone for each time period. As an open economy, the UK could benefit from future global trade improvements. Also, a weak GBP (see Figure 6) may support exports in the new post-Brexit world.

Figure 5
**UK Equities Have
 Been Derated Even
 More than Europe**

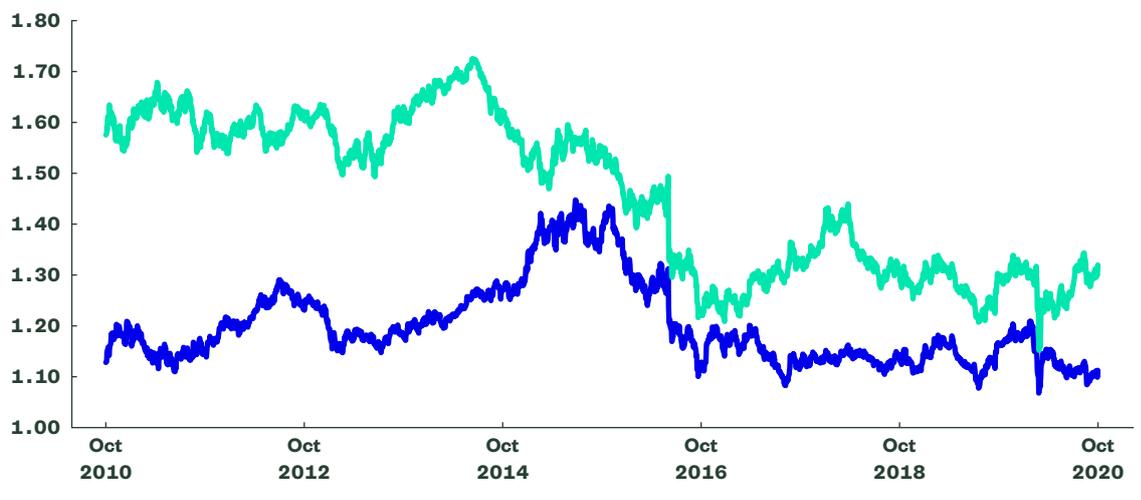
■ Relative P/E
 ■ Average Relative P/E
 ■ Current Relative P/E



Source: Bloomberg Finance L.P., as of 22 October 2020.

Figure 6
**Weak GBP May
 Support UK Exports**

■ GBP/EUR
 ■ GBP/USD



Source: Bloomberg Finance L.P., as of 22 October 2020.

Japan Equities

Even with a smooth transition to a new prime minister and continuation of Abe's policies, there remain large structural problems for the Japanese economy. This pressure weighs heavily on our forecast returns for the market. However, if economic activity recovers early in 2021 it would help exporters, and the postponed Olympic Games may provide additional support. The ability to tackle the virus successfully compared with other developed markets is a bright spot.

Emerging Markets

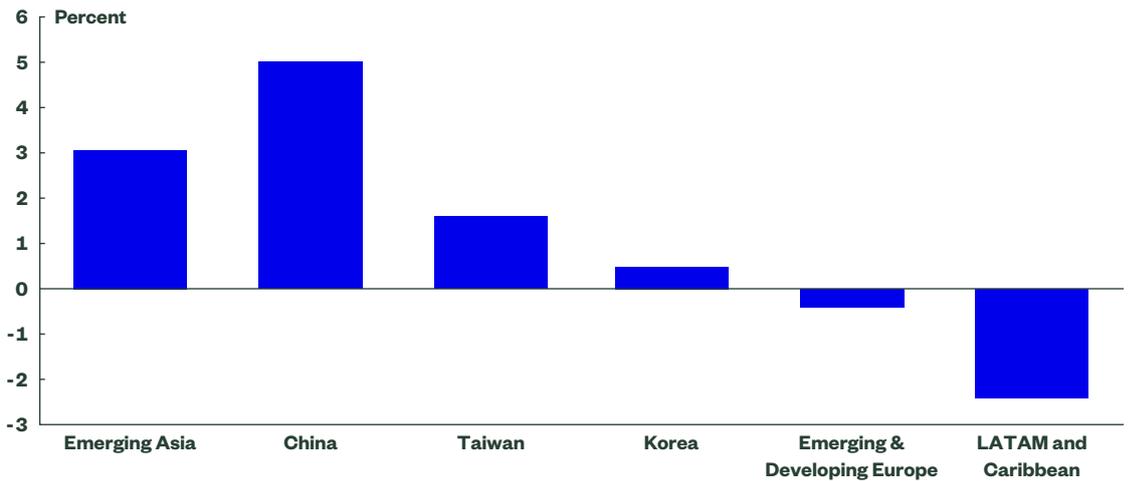
Emerging markets tend to have a greater dependency on commodities, including oil, and initially during the COVID-19 crisis saw large drops in GDP growth forecasts. During the worst of the crisis, steep capital outflows drove currency depreciation, leading debt servicing obligations to become more onerous and increasing the risk of default. However, the environment is now more settled, although as ever there is a wide discrepancy across the regions.

Emerging markets could return more than US equities, including on a risk-adjusted basis, in all forecast time periods. Forecasted returns are even higher for emerging market small caps given the high exposure to structural growth trends.

Emerging Asia is particularly attractive on a relative basis, with its inherent structural advantages of demographic change and advanced technological industries. China has a weighting of c. 50% in the index and the country is expected to serve as the engine for global growth in years to come. The other important contributors are Korea and Taiwan (with China, the three countries make up c. 80% of market capitalisation). See Figure 7 for GDP growth projections for 2020 and 2021.

According to State Street Global Advisors, expected market returns for emerging Asia are higher than those for Latin America or Europe for the next year and three to five years; thereafter emerging Europe has a higher forecast, partially due to growth in Russia. Despite the growth attractions of emerging Asia, the earnings yield is only marginally lower than the broader region, as shown in Figure 8.

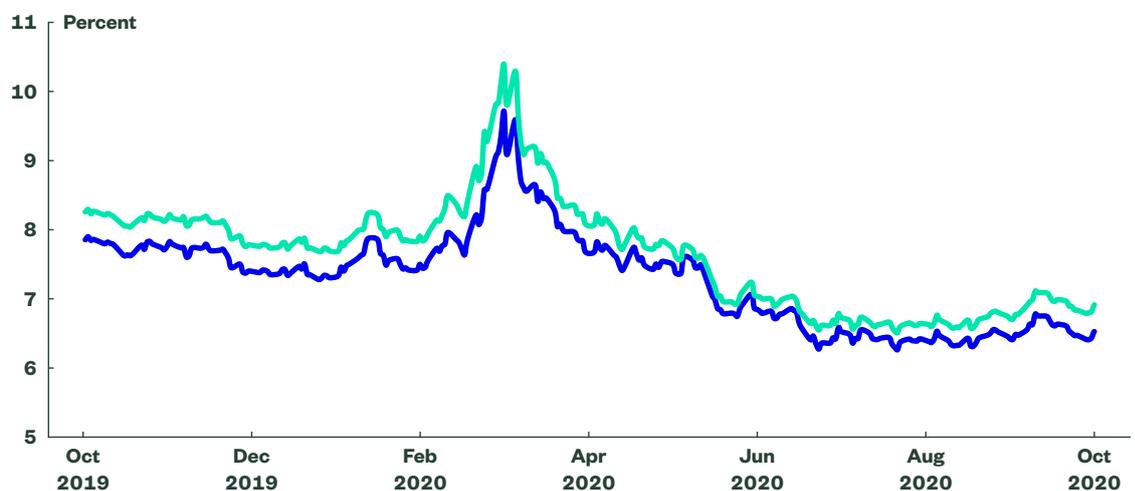
Figure 7
IMF Projections for GDP growth in 2020/21 Show EM Asia Driven by China (%)



Source: International Monetary Fund, World Economic Outlook, October 2020 Update. are geometrical averages of 2020 and 2021 projections for each country, calculated by State Street Global Advisors.

Figure 8
EM Asia on Similar Valuation to Broader EM Despite Better Forecast Returns

■ EM Asia Earnings Yield 12m Fwd
 ■ Broad EM Earnings Yield 12m Fwd



Source: Bloomberg Finance L.P., State Street Global Advisors as of 22 October 2020. EM Asia represented by MSCI Emerging Asia Net Total Return USD Index, Broad EM is represented by MSCI Emerging Net Total Return USD Index. Earnings Yield 12m fwd is reciprocal of 12m fwd BEST P/E. Past performance is not a reliable indicator of future performance. The above targets are estimates based on certain assumptions and analysis. There is no guarantee that the estimates will be achieved.

Implementation Ideas

US Equities

SPDR S&P 500 UCITS ETF (**SPY5**)

SPDR S&P 500 ESG Screened UCITS ETF (**500X**)

SPDR Russell 2000 U.S. Small Cap UCITS ETF (**ZPRR**)

Europe

SPDR MSCI Europe Small Cap UCITS ETF (**EUSC**)

SPDR STOXX Europe 600 ESG Screened UCITS ETF (**ZPDX**)

SPDR FTSE UK All Share UCITS ETF (**FTAL**)

Emerging Market Equities

SPDR MSCI EM Asia UCITS ETF (**EMAD**)

SPDR MSCI Emerging Markets UCITS ETF (**EMRD**)

SPDR MSCI Emerging Markets Small Cap UCITS ETF (**SPYX**)

Global Equities

SPDR MSCI ACWI UCITS ETF (**ACWD**)

SPDR MSCI ACWI IMI UCITS ETF (**SPYI**)

SPDR MSCI World Small Cap UCITS ETF (**ZPRS**)

Figure 9
Performance

	1M (%)	3M (%)	YTD (%)	1 Year (%)	3 Years (%)	5 Years (%)	Since Inception
US Equities							
Inception Date 19/03/2012							
SPDR® S&P® 500 UCITS ETF (Dist)	-3.82	8.83	5.30	14.73	11.86	13.70	12.56
S&P 500® Index	-3.84	8.79	5.13	14.49	11.62	13.45	12.34
Difference	0.01	0.04	0.18	0.24	0.24	0.25	0.22
Inception Date 30/01/2012							
SPDR S&P 400 U.S. Mid Cap UCITS ETF (Acc)	-3.30	4.59	-9.03	-2.77	2.29	7.46	9.32
S&P MidCap 400® Index	-3.29	4.65	-8.97	-2.66	2.39	7.57	9.44
Difference	-0.01	-0.06	-0.07	-0.11	-0.10	-0.11	-0.12
Inception Date 30/06/2014							
SPDR Russell 2000 U.S. Small Cap UCITS ETF (Acc)	-3.46	4.73	-9.12	-0.19	1.28	7.52	4.90
Russell 2000® Index	-3.38	4.84	-8.96	-0.02	1.36	7.56	4.66
Difference	-0.08	-0.11	-0.16	-0.17	-0.08	-0.04	0.24
Europe Equities							
Inception Date 31/05/2001							
SPDR MSCI Europe UCITS ETF	-1.41	0.08	-12.70	-7.75	-0.23	3.34	2.44
MSCI Europe Index	-1.41	0.10	-12.75	-7.76	-0.34	3.21	2.53
Difference	0.00	-0.02	0.05	0.01	0.11	0.13	-0.08
Inception Date 30/09/2019							
SPDR STOXX Europe 600 ESG Screened UCITS ETF (Acc)	-1.35	0.78	-11.29	-5.86	-	-	-5.86
STOXX Europe 600 ESG-X Index	-1.36	0.78	-11.24	-5.82	-	-	-5.82
Difference	0.00	0.01	-0.05	-0.05	-	-	-0.05
Inception Date 31/03/2005							
SPDR MSCI Europe Small Cap UCITS ETF	-0.65	6.16	-10.44	0.07	0.65	4.95	7.70
MSCI Europe Small Cap Index	-0.59	6.23	-10.32	0.21	0.58	5.20	7.97
Difference	-0.05	-0.07	-0.12	-0.14	0.07	-0.25	-0.27
Inception Date 28/02/2012							
SPDR FTSE UK All Share UCITS ETF (Acc)	-1.71	-2.96	-20.01	-16.78	-3.45	3.22	4.40
FTSE All-Share Index	-1.69	-2.92	-19.92	-16.59	-3.21	3.46	4.54
Difference	-0.02	-0.04	-0.09	-0.19	-0.24	-0.24	-0.14

Source: State Street Global Advisors, as of 30 September 2020. Performance is net of fees. **Performance quoted represents past performance, which is no guarantee of future results. Investment return and principal value will fluctuate, so you may have a gain or loss when shares are sold. Current performance may be higher or lower than that quoted. All results are historical and assume the reinvestment of dividends and capital gains. The performance data do not take account of the commissions and costs incurred on the issue and redemption, or purchases and sale, of units. Visit ssga.com/etfs for most recent month-end performance.** Performance returns for periods of less than one year are not annualised. Index returns are unmanaged and do not reflect the deduction of any fees or expenses.

Figure 9

Performance (cont'd)

	1M (%)	3M (%)	YTD (%)	1 Year (%)	3 Years (%)	5 Years (%)	Since Inception
Emerging Market Equities							
Inception Date 16/05/2011							
SPDR MSCI Emerging Markets UCITS ETF	-1.65	9.43	-1.46	10.21	2.08	8.68	1.55
MSCI Emerging Markets Index	-1.60	9.56	-1.16	10.54	2.42	8.96	1.95
Difference	-0.04	-0.13	-0.29	-0.33	-0.34	-0.29	-0.39
Inception Date 11/05/2011							
SPDR MSCI EM Asia UCITS ETF	-1.13	11.88	7.82	21.10	5.18	10.79	4.33
MSCI EM (Emerging Markets) Asia Index	-1.12	11.92	8.01	21.52	5.67	11.29	4.92
Difference	-0.01	-0.04	-0.19	-0.42	-0.48	-0.51	-0.59
Inception Date 11/05/2011							
SPDR MSCI Emerging Markets Small Cap UCITS ETF	-1.62	11.70	-2.59	6.42	-1.27	4.77	0.34
MSCI Emerging Markets Small Cap Index	-1.64	11.85	-2.40	6.89	-1.09	4.60	0.48
Difference	0.02	-0.15	-0.19	-0.47	-0.19	0.16	-0.15
Global Equities							
Inception Date 13/05/2011							
SPDR MSCI ACWI UCITS ETF	-3.29	7.91	0.96	9.95	6.89	10.39	7.50
MSCI ACWI (All Country World Index) Index	-3.22	8.13	1.37	10.44	7.12	10.30	7.65
Difference	-0.07	-0.22	-0.41	-0.50	-0.23	0.09	-0.15
Inception Date 16/05/2011							
SPDR MSCI ACWI IMI UCITS ETF	-3.24	8.02	-0.02	9.04	5.97	9.85	7.70
MSCI ACWI IMI (All Country World Investable Market Index) Index	-3.10	8.11	0.48	9.57	6.47	9.97	7.51
Difference	-0.14	-0.09	-0.49	-0.53	-0.49	-0.12	0.19
Inception Date 25/11/2013							
SPDR MSCI World Small Cap UCITS ETF	-2.16	7.40	-6.74	2.26	2.12	7.69	5.67
MSCI World Small Cap Index	-2.16	7.46	-6.37	2.77	2.31	7.96	5.85
Difference	0.01	-0.06	-0.37	-0.52	-0.19	-0.27	-0.18

Source: State Street Global Advisors, as of 30 September 2020. Performance is net of fees. **Performance quoted represents past performance, which is no guarantee of future results. Investment return and principal value will fluctuate, so you may have a gain or loss when shares are sold. Current performance may be higher or lower than that quoted. All results are historical and assume the reinvestment of dividends and capital gains. The performance data do not take account of the commissions and costs incurred on the issue and redemption, or purchases and sale, of units. Visit ssga.com/etfs for most recent month-end performance.** Performance returns for periods of less than one year are not annualised. Index returns are unmanaged and do not reflect the deduction of any fees or expenses.

Endnote

- 1 Bloomberg Finance L.P., as of 15 October 2020.
- 2 Source: S&P Dow Jones Indices, as of 31 October 2020.
- 3 Source: State Street Global Advisors, as of 30 September 2020.

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