Confidence must be earned

Amundi ASSET MANAGEMENT

October 2020

Time to reconsider US growth and value?

INVESTMENT TALKS

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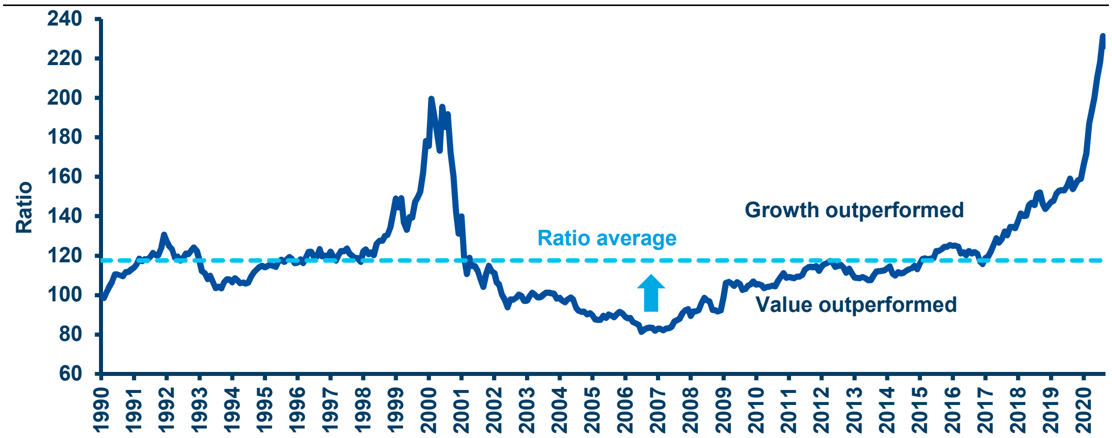
- *The outperformance of growth stocks over value stocks has reached record levels, as has the valuation gap.*
- *The environment for growth stocks has been ideal: interest rates have plummeted, and US technology companies have become increasingly dominant in the United States and abroad. However, we believe this ideal environment is unlikely to last. Inflation -- which has been dormant for years -- may rise as a result of stimulus measures. Historically, value has outperformed growth during inflationary periods.*
- ***We expect that select quality value stocks that can manage through this difficult economic period could benefit as the US and the global economy rebound and inflation returns.***
- *Given the uncertainty regarding the timing of a reflation of the US economy and the potential for a corresponding increase in interest rates,* ***we believe increasing exposure to both high-quality value stocks and growth stocks may be prudent, while reducing exposure to hyper-growth and deep-value stocks.***

Thirty-year outperformance of growth over value has exceeded previous peak in 2000



Source: Amundi based on Bloomberg data as of 30 September 2020. **Past performance is no indication of future results**. The chart shows the ratio of Russell 1000 growth index to Russell 1000 value (price). Indices are unmanaged and their returns assume reinvestment of dividends and, unlike mutual fund returns, do not reflect any fees or expenses associated with a mutual fund. It is not possible to invest directly in an index.

Why growth has outperformed value

We see two primary reasons for the outperformance of growth stocks:

- **Declining inflation and interest rates:** the monthly consumer price index (CPI) YoY growth reached 3.5% in October 2007 and has bee below that since then, hitting 1.3% in August 2020. This trend negatively impacted companies that have commodity exposure, many of which are in the value universe. Meanwhile, the ten-year US Treasury rate plummeted from 4.5% on 1 October 2007 to 0.68% as of 30 September 2020. This has been a negative for financial stocks, which have continued to dominate the value universe and rely on a healthy interest rate spread to generate profits. Conversely, falling interest rates have been a positive for growth stocks, as a lower

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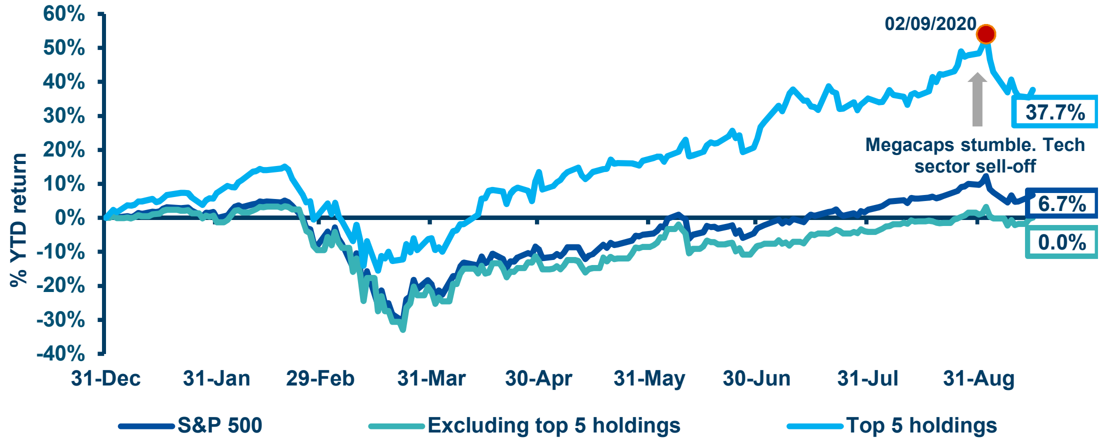
"The success of the top five holdings of the S&P 500 propelled the index to record highs, even amid the pandemic."

discount rate has been applied to future expected cash flows, increasing the net present value of those cash flows.

- **US dominance in technology-related industries with strong secular growth:** Alphabet, Amazon, Apple, Facebook, and Microsoft, among other companies, have emerged as dominant in their industries, which have been growing due to the digital transformation of the global economy. The success of these companies propelled the S&P 500 index to record highs, even amid the pandemic.

2020 YTD returns of the S&P 500 with and without the top five holdings



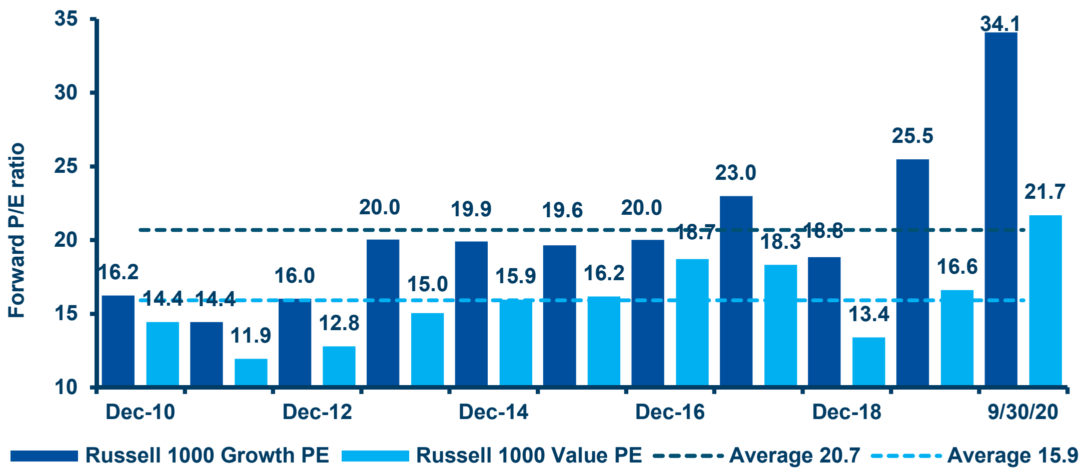
Source: Amundi based on Bloomberg data as of 30 September 2020. **Past performance is no guarantee of future results**. Top five holding include: Alphabet, Amazon, Apple, Facebook, and Microsoft. Indices are unmanaged and their returns assume reinvestment of dividends, and unlike investment product returns, do not reflect any fees or expenses. You cannot invest directly in an index. Securities listed are not meant to represent any current or future holding of an Amundi portfolio, and should not be considered recommendations to buy or sell any security.

We believe it may be time to shift towards value

The reasons why we believe now may be a good time to make this shift include:

- **The valuation gap between value and growth stocks is wide:** as of 30 September 2020, the Russell 1000 growth index was trading at approximately at 50% premium on price-to-earnings, which is the highest valuation gap in recent history.

Growth vs. value valuation gap has reached historical highs

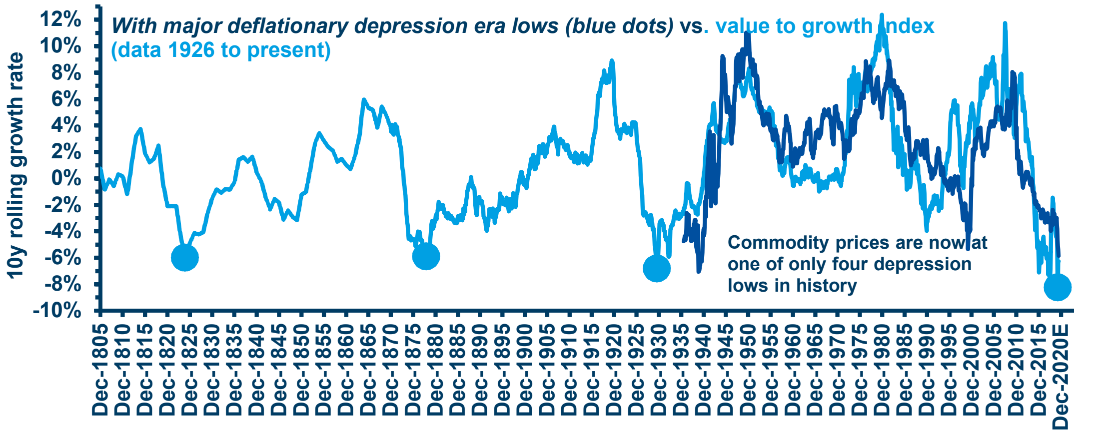


Source: Amundi based on Bloomberg data as of 30 September 2020. Indices are unmanaged and their returns assume reinvestment of dividends and, unlike mutual fund returns, do not reflect any fees or expenses associated with a mutual fund. It is not possible to invest directly in an index.

"Unprecedented levels of monetary and fiscal stimulus may result in a reflation of the US economy."

- **Possible reflation in the US economy**: unprecedented levels of monetary and fiscal stimulus may result in a reflation of the US economy. As seen in the chart below, commodity prices have been highly correlated to the value-to-growth index. This is because the value indices generally have much greater exposure to inflation-sensitive stocks than growth indices. For example, the energy, financials, industrials and materials sector represented 41% of the Russell 1000 value Index as of 30 September 2020 compared with 15% for the Russell 1000 growth index. In addition, commodity price trends have typically lasted for a decade or more. As of 30 June 2020, commodity prices were lower than they have been in over 200 years. While they could decline further, we believe stimulus efforts and gradual improvements in the economy are likely to push them higher, which could result in value outperforming growth.

High correlations – Commodities and the value-to-growth index



Source: Stifel Equity Research as of 30 June 2020 (latest data available). Blue line represents US commodity price index, a weighted average of selected commodity prices. Indices used in Stifel research: Warren & Pearson Commodity Index (1795-1912), WPI Commodities (1913-1925), equal-weighted (1/3 ea.) PPI Energy, PPI Farm Products and PPI Metals (Ferrous and Non-Ferrous) ex-precious metals (1926-1956), Refinitiv Equal Weight (CCI) Index (1956-1994), and Refinitiv Core Commodity CRB Index (1994 to present). Value vs.growth links the Fama/French (Dartmouth/Tuck web-hosted) series from 1926 to 1977 and the Russell 1000 total return index (1978 to present).

Increasing value exposure is not without risk

In our view, the risks to increasing value exposure are threefold:

- The first is that the US and global economies may be slow to recover from the pandemic, causing interest rates to remain low and investors to continue favouring growth stocks.
- The second risk is that a number of companies in the value universe are structurally impaired. For example, some airlines are likely to survive only with continued government assistance. Full-price department stores have lost share to online and discount retailers; this could continue even after the pandemic ends, as consumers remain budget conscious.
- Finally, a Biden victory could result in higher regulation in sectors such as energy and financials, which currently have larger weightings in value indices than in growth indices. Growth stocks could also be at risk under a Biden administration due to a proposal to increase taxes on foreign income from a minimum of 10.5% to 21.0%. This could disproportionally impact US technology companies disproportionally, which derived 43% of their revenue from the United States compared with 60% for the S&P 500 in 2019. The technology sector has a higher weighing in growth indices than in value indices. **In short, both value and growth stocks could be negatively impacted by a Biden victory. Offsetting this, at least in part, is the likelihood of additional fiscal stimulus under a Biden administration, especially in case of a Democratic sweep.** By comparison, a Trump reelection may result in cyclical stocks outperforming given a pro-business agenda, with large cap technology stocks a likely source of funds.

"Given these risks, we believe it is important to take an active approach to increasing exposure to value."

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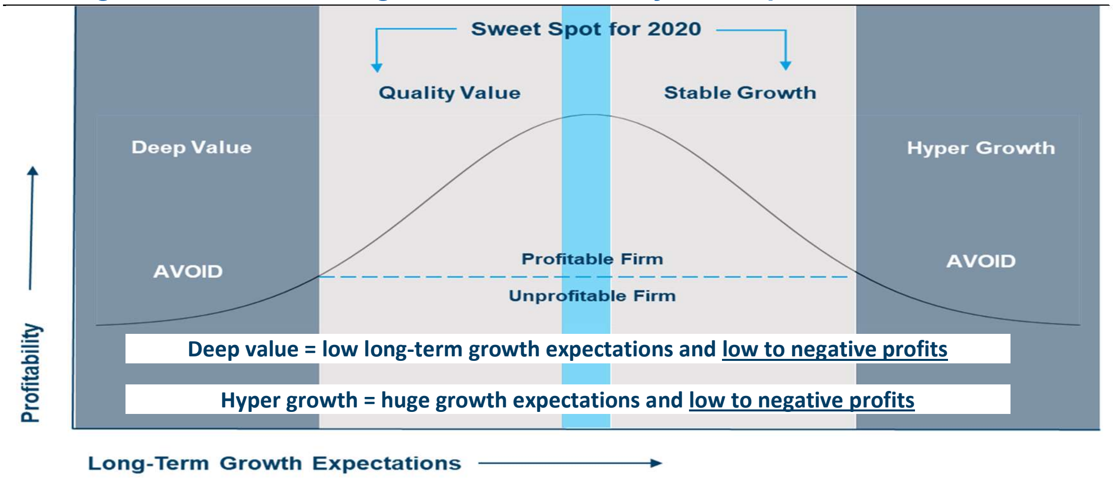
A path forward in US equities

In the current market environment, we see four distinct categories of stocks:

- **Hyper growth** companies that are wildly overvalued, approaching dot.com levels;
- **Stable growth** companies that have been highly profitable, but are also in some cases too highly valued (and dependent on low interest rates or low discount rates to maintain those valuations);
- **Quality value** companies that we believe can survive the economic downturn and emerge competitively stronger; and
- **Deep value** companies that are struggling to survive the pandemic and have a questionable future (i.e., airlines, full-price department stores, restaurants), even if they do survive.

Striking a balance between growth and value may be the path forward



Source: Cornerstone Macro. **For illustrative purposes only.**

"We believe the most appealing opportunities in US equities are in stable growth and quality value stocks."

We believe the most appealing opportunities in US equities are in stable growth and quality value stocks. Stable growth stocks can provide exposure to secular growth trends that are not dependent on economic growth. An example would be the shift to online retail. While a number of stable growth stocks may have high valuations, others may be more reasonably valued. Quality value stocks can offer cyclical exposure in companies that may be positioned to manage through the difficult economic period if the US and global economy take longer than expected to recover. **Therefore, we believe shifting portfolio exposure in US equities away from hyper growth stocks into stable/defensive growth and quality value -- while avoiding deep value -- is prudent.**

Given that the pandemic has increased the spotlight on labour practices and safety issues, **we also believe the more successful investment strategies in this environment may be those that focus on sustainability, holistically, meaning not just from a competitive and financial perspective, but also with ESG (environmental, social and governance) considerations in mind**. We believe that doing so could enable these strategies to pursue companies that could not only survive the current economic environment, but emerge from the pandemic stronger than they were before it began.

AMUNDI INVESTMENT INSIGHTS UNIT

The Amundi Investment Insights Unit (AIIU) aims to transform our CIO expertise, and Amundi's overall investment knowledge, into actionable insights and tools tailored around investor needs. In a world where investors are exposed to information from multiple sources we aim to become the partner of choice for the provision of regular, clear, timely, engaging and relevant insights that can help our clients make informed investment decisions.

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Definitions

- **Correlation:** The degree of association between two or more variables; in finance, it is the degree to which assets or asset class prices have moved in relation to each other. Correlation is expressed by a correlation coefficient that ranges from -1 (always move in opposite direction) through 0 (absolutely independent) to 1 (always move in the same direction).
- **Net present value (NPV):** Difference between the present value of cash inflows and the present value of cash outflows over a period of time.
- **Price-earnings ratio (P/E):** current price of a stock divided by the consensus analyst estimates of one-year projections of its earnings per share.
- **Russell 1000 growth index:** it measures the performance of large cap US growth stocks.
- **Russell 1000 value Index:** it measures the performance of large cap US value stocks.
- **S&P 500 index:** it is a commonly used measure of the broad US stock market.
- Indices are unmanaged and their returns assume reinvestment of dividends and, unlike mutual fund returns, do not reflect any fees or expenses associated with a mutual fund. It is not possible to invest directly in an index

Important information

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