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Are Value stocks the only & best solution going forward?

Nordea 1 – Global Stable Equity Fund

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Highlights

- Record high inflation levels and hawkish monetary policies have given further support to the Value-style comeback, seen since the release of the Covid vaccines
- Nevertheless, Value stocks are sometimes cheap for a reason and the sustainability of the currently favourable environment is everything but guaranteed
- A blend of Value with other styles could be the best option in an environment where macro/geopolitical uncertainties mount and risk control becomes paramount
- The Nordea 1 – Global Stable Equity Fund offers investors a unique blend of Value, Low Risk and Quality, with a proven track record of downside risk control¹

As yields' outlook glooms, the Value style booms

Equity styles relative performance can widely vary across different phases of the cycle, hence, making it particularly tempting for investors to try to time the allocation. In late 2020, and after many years of Growth outperforming Value, the first Covid-vaccines sparked a strong style rotation towards Value. The market anticipated that the re-opening of the main economies and the end of the "free money" era would lead to higher interest rates and would take a toll on Growth stocks' stretched valuations.

As 2021 went by, the rotation towards Value took a pause, and volatility among styles increased. Then again, since the start of 2022, 40-year high inflation levels (partially driven by the supply shock related to Russia's invasion of Ukraine) generated much more hawkish tone and policies from monetary authorities. This has fueled a second round of Value's style outperformance (as they are less impacted by higher discount rates for long term cash flows) and has made investors wonder if Value stocks are the way to go forward.

Equity Market/Styles Performance

| | Covid-Vaccine Value Rotation (31.10.2020 – 10.05.2021) | Growth/Quality Come-back (10.05.2021 – 11.12.2021) | Hawkish-Fed Value Revival (11.12.2021 – 30.04.2022) | Overall Period (31.10.2020 – 30.04.2022) |
|-------------------------------|--|--|---|--|
| Table 1 | | | | |
| MSCI World NR LCL | 28.56% | 10.54% | -10.03% | 27.86% |
| MSCI World Quality NR LCL | 22.93% | 16.34% | -14.37% | 22.46% |
| MSCI World Value NR LCL | 37.38% | 3.67% | 3.31% | 40.46% |
| MSCI World Growth NR LCL | 20.18% | 17.77% | -18.45% | 15.41% |
| MSCI World Minimum Vol NR LCL | 15.88% | 5.69% | -3.23% | 18.51% |

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There is value beyond Value

Value stocks have historically been more cyclical and it might be worth asking if central banks' aggressive response to the current – mostly supply driven – inflation spike will be able to put a stop to prices, or if in the other hand, could lead to an economic slowdown or even a recession. Would Value continue to outperform if the latter materializes? The aim of this paper is not trying to come-up with an answer to this question, but namely to present investors with an analysis on how the different equity styles have historically performed during market sell-offs.

Which styles have navigated better market volatility and shown lower drawdowns? Do they do better in isolation or a blend approach could offer a more resilient value proposition? Table 2 below sheds some light on these two questions. As it can be seen, looking at the last 20 calendar years (including the first 4 months of 2022) and focusing on the years where the equity market largest drawdown was larger than -10%, the Value factor has historically averaged the highest downside capture ratio vs the overall equity market, with growth closely following and Quality slightly outperforming. Unsurprisingly, the Low Risk factor (Min Vol Index) is the one that performs better in this type of environment, in terms of downside risk. But what about risk adjusted performance? From this perspective, the Quality factor is the one that delivers the highest risk adjusted return among all equity styles seen in isolation.

¹ The performance represented is historical; past performance is not a reliable indicator of future results and investors may not recover the full amount invested. The value of shares can greatly fluctuate as a result of the sub-fund's investment policy and cannot be ensured, you could lose some or all of your invested money.

Dowside Capture Ratio for calendar years with a Maximum Drawdown larger than –10% (vs MSCI World Index Lcl in EUR)

| | 2022 | 2021 | 2020 | 2019 | 2018 | 2017 | 2016 | 2015 | 2014 | 2013 | 2012 | 2011 | 2010 | 2009 | 2008 | 2007 | 2006 | 2005 | 2004 | 2003 | 2002 | Average |
|-----------------------------------|------|------|------|------|------|------|------|------|------|------|------|------|------|------|------|------|------|------|------|------|------|---------|
| MSCI World NR LCL | 1.00 | – | 1.00 | – | 1.00 | – | 1.00 | 1.00 | – | – | 1.00 | 1.00 | 1.00 | 1.00 | 1.00 | 1.00 | 1.00 | – | – | 1.00 | 1.00 | 1.00 |
| MSCI World Quality NR LCL | 1.27 | – | 0.90 | – | 1.04 | – | 0.79 | 0.88 | – | – | 0.79 | 0.73 | 0.86 | 0.80 | 0.81 | 0.95 | 0.84 | – | – | 0.89 | 0.90 | 0.89 |
| MSCI World Value NR LCL | 0.62 | – | 1.11 | – | 0.98 | – | 0.97 | 1.08 | – | – | 1.07 | 1.09 | 1.04 | 1.19 | 1.00 | 1.21 | 0.91 | – | – | 1.13 | 1.07 | 1.03 |
| MSCI World Growth NR LCL | 1.49 | – | 0.91 | – | 1.14 | – | 1.03 | 1.00 | – | – | 0.97 | 0.95 | 0.96 | 0.81 | 1.00 | 0.99 | 1.10 | – | – | 0.87 | 0.93 | 1.01 |
| MSCI World Minimum Vol NR LCL | 0.69 | – | 0.88 | – | 0.58 | – | 0.56 | 0.67 | – | – | 0.48 | 0.56 | 0.50 | 0.81 | 0.69 | 0.88 | 0.59 | – | – | 0.78 | 0.61 | 0.66 |
| 33% Qalue 33% Quality 33% Min Vol | 0.81 | – | 0.96 | – | 0.83 | – | 0.74 | 0.84 | – | – | 0.76 | 0.75 | 0.79 | 0.93 | 0.84 | 0.88 | 0.76 | – | – | 0.93 | 0.85 | 0.83 |

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Does this mean that pure Quality or even Low Risk are the way forward? It could be, but it would greatly depends on what investors might be looking for or, better yet, what they might be more concerned about. High inflation, increasing rates and lots of geopolitical uncertainty might require a more diversified approach. Would a passive blend allocation to Value, Quality and Low Risk factors offer a better value proposition? Table 3 suggests that such a passive blend portfolio would not necessarily do better than some/most of the individual styles. Yes, it improves the average maximum drawdown capture ratio p.a. compared to all styles but Low Risk, but it fails to deliver a higher risk-adjusted return over the last two decades, when compared to Low Risk and Quality.

Risk Adjusted Returns (last 20 years)

| | Return p.a. (%) | Std Dev (%) | Sharpe Ratio |
|-----------------------------------|-----------------|-------------|--------------|
| MSCI World NR LCL | 7.07 | 14.07 | 0.48 |
| MSCI World Quality NR LCL | 9.02 | 12.71 | 0.66 |
| MSCI World Value NR LCL | 6.00 | 14.65 | 0.40 |
| MSCI World Growth NR LCL | 7.93 | 14.33 | 0.53 |
| MSCI World Minimum Vol NR LCL | 7.08 | 9.96 | 0.63 |
| 33% Qalue 33% Quality 33% Min Vol | 7.45 | 11.94 | 0.57 |

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Stable Equities: an active blend approach to deliver better outcomes

Nordea's Multi-Assets Team has more than a decade managing active global equity portfolios that blend the Low Risk, Value and Quality factors, in order to try to outperform the market with an overall lower level of risk². Its process, focuses on finding stable companies with stable underlying fundamentals (earnings, free cash flows, EBITDAs, dividends, etc.) with explanatory power over their relatively less volatile prices, but adds a fundamental layer that aims to avoid low quality and/or very expensive stocks.

As it can be seen on Table 5, if we look at the Nordea 1 – Global Stable Equity Fund (BI-EUR) risk adjusted return since its inception, in 15.01.2010, and focus on its average capture ratio to the maximum equity drawdowns larger than –10% seen each calendar year (Table 4), there seems to be a lot of value of being an active manager with a blend exposure to a diversified set of risk factors/styles. In fact, Nordea's strategy has delivered the highest Sharpe Ratio vis-à-vis any single style and the passive blend option, coupled with a very low downside capture ratio, that is only a close second to that of the Low Risk Factor.

Dowside Capture Ratio for calendar years with a Maximum Drawdown larger than –10% (vs MSCI World Index Lcl in EUR)

| | 2022 | 2021 | 2020 | 2019 | 2018 | 2017 | 2016 | 2015 | 2014 | 2013 | 2012 | 2011 | 2010 | Average |
|---|-------------|------|-------------|------|-------------|------|-------------|-------------|------|------|-------------|-------------|-------------|-------------|
| MSCI World NR LCL | 1.00 | – | 1.00 | – | 1.00 | – | 1.00 | 1.00 | – | – | 1.00 | 1.00 | 1.00 | 1.00 |
| MSCI World Quality NR LCL | 1.27 | – | 0.90 | – | 1.04 | – | 0.79 | 0.88 | – | – | 0.79 | 0.73 | 0.86 | 0.91 |
| MSCI World Value NR LCL | 0.62 | – | 1.11 | – | 0.98 | – | 0.97 | 1.08 | – | – | 1.07 | 1.09 | 1.04 | 1.00 |
| MSCI World Growth NR LCL | 1.49 | – | 0.91 | – | 1.14 | – | 1.03 | 1.00 | – | – | 0.97 | 0.95 | 0.96 | 1.06 |
| MSCI World Minimum Vol NR LCL | 0.69 | – | 0.88 | – | 0.58 | – | 0.56 | 0.67 | – | – | 0.48 | 0.56 | 0.50 | 0.62 |
| 33% Qalue 33% Quality 33% Min Vol | 0.81 | – | 0.96 | – | 0.83 | – | 0.74 | 0.84 | – | – | 0.76 | 0.75 | 0.79 | 0.81 |
| Nordea 1 – Global Stable Equity BI EUR | 0.42 | – | 0.92 | – | 0.64 | – | 0.73 | 1.11 | – | – | 0.50 | 0.64 | 0.41 | 0.67 |

Source: © 2022 Morningstar, Inc. All Rights Reserved as at 04.05.2022. European Open End Funds database, Morningstar EAA Fund Equity Large-Cap Value – Global category. Performance in EUR and based on monthly observations. Period under consideration: 15.01.2010 – 30.04.2022. The performance represented is historical; past performance is not a reliable indicator of future results and investors may not recover the full amount invested. The value of shares can greatly fluctuate as a result of the sub-fund's investment policy and cannot be ensured, you could lose some or all of your invested money. For illustrative purposes only. Comparison with other financial products or benchmarks is only meant for indicative purposes.

Risk Adjusted Returns (since GSEF inception)

| Table 5 | Return p.a. (%) | Std Dev (%) | Sharpe Ratio |
|---|-----------------|--------------|--------------|
| MSCI World NR LCL | 10.01 | 17.53 | 0.88 |
| MSCI World Quality NR LCL | 12.27 | 18.00 | 1.03 |
| MSCI World Value NR LCL | 7.99 | 17.79 | 0.72 |
| MSCI World Growth NR LCL | 11.77 | 18.47 | 0.97 |
| MSCI World Minimum Vol NR LCL | 9.11 | 13.05 | 1.04 |
| 33% Qalue 33% Quality 33% Min Vol | 9.86 | 15.42 | 0.94 |
| Nordea 1 – Global Stable Equity BI EUR | 11.45 | 15.30 | 1.11 |

Source: © 2022 Morningstar, Inc. All Rights Reserved as at 04.05.2022. European Open End Funds database, Morningstar EAA Fund Equity Large-Cap Value – Global category. Performance in EUR and based on monthly observations. Period under consideration: 15.01.2010 – 30.04.2022. **The performance represented is historical; past performance is not a reliable indicator of future results and investors may not recover the full amount invested. The value of shares can greatly fluctuate as a result of the sub-fund's investment policy and cannot be ensured, you could lose some or all of your invested money.** For illustrative purposes only. **Comparison with other financial products or benchmarks is only meant for indicative purposes.** With effect from 14.12.2020, the official reference index of the fund is 70% MSCI World Index (Net Return) and 30% EURIBOR 1M (FX adjusted). Prior to this date, the fund did not have an official reference index. The performance of the reference index before this date is provided for convenience purposes. This reference index is used for performance comparison purposes.

Key takeaways

In a nutshell, our Nordea 1 – Global Stable Equity Fund is a unique investment solution to help investors face the current uncertain and challenging market environment:

- Navigate the current style rotation, from expensive Growth to more cyclical Value stocks, as its valuation overlay allows them to be less impacted by higher discount rates
- Historically offered higher and more stable returns when compared to the overall equity market and any single equity style
- Delivered superior capital preservation features, thanks to their lower downside capture ratio during large equity sell-offs
- Aims to offer lower inflation sensitivity thanks to their superior pricing power and their ability to pass inflation to consumers with almost no impact on margins³

Do you want to know more? Reach out to your Nordea AM Sales representative, who will be thrilled to share more information on these unique investment solution.

Investment Strategy:

This actively managed fund applies a unique process to construct a portfolio of boring equities with stable returns based on an objective, computer driven, quantitative stock screening model. The process identifies companies that operate in established lines of business, generating consistently stable earnings, dividends, cash flows, etc. This stability helps dampen price volatility of such companies, stocks, making them less risky than the broader market. Benchmark used for performance comparison only. Risk characteristics of the fund's portfolio may bear some resemblance to those of the benchmark. Benchmark: 70% MSCI World Index (Net Return) and 30% EURIBOR 1M (FX adjusted).

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