



## Markets & Economies

# What's Driving the Strength in Global Equities?

***Macroeconomic and industry-specific trends are providing tailwinds. Given the scope of the opportunity set, we think selectivity will be the key to investment success.***



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Global equity markets have continued their strong showing through the third quarter of 2024, building on the rally that began in late 2023. Year to date through September 30, the S&P 500® Index advanced 22%, while the MSCI ACWI (All Country World Index) climbed 19%. Here, we'll look at some of the factors driving that strong performance and offer some insights about how investors might approach the asset class in the fourth quarter and beyond.

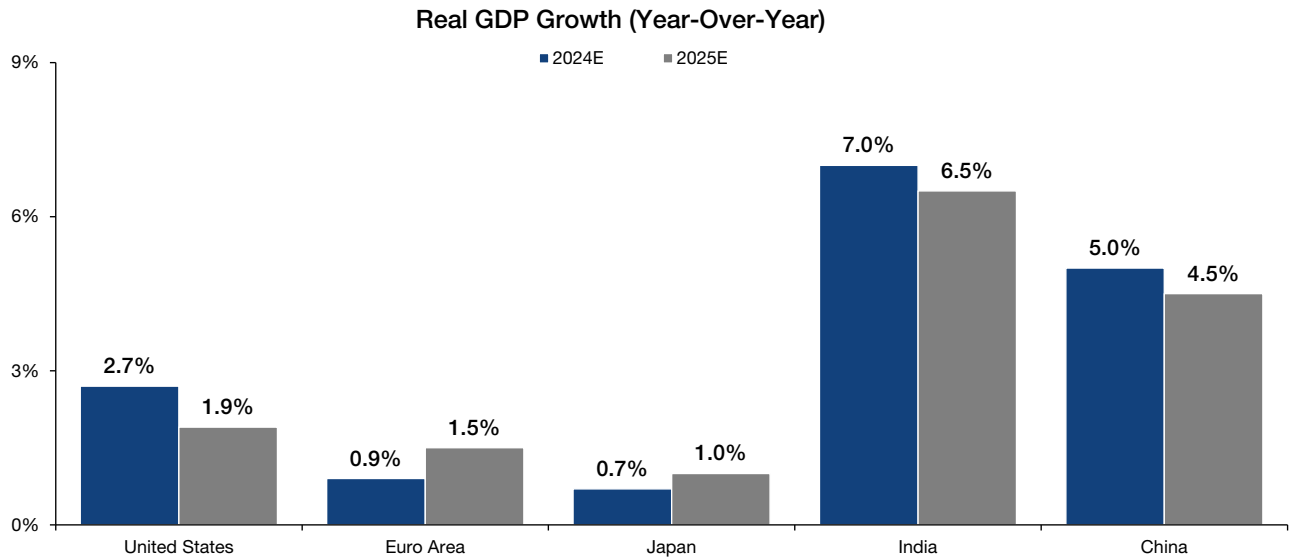
One development supporting markets in 2024: The global disinflation narrative is intact. The annualized August U.S. core consumer price index (which excludes food and energy prices) decreased to 3.3%, year over year, in September after peaking at 6.1% in September 2022. Many economies overseas are ahead of the U.S. on this front, with headline inflation in the Eurozone, Germany, the U.K., and Canada now at 1.8%, 1.6%, 2.2%, and 2.0%, respectively. (All inflation data are sourced from government agencies of the respective areas.)

This moderation in inflation has allowed central banks globally to begin easing monetary policy, with the U.S. Federal Reserve notably cutting rates by 50 basis points (bps) on September 18, the European Central Bank delivering two 25-bp cuts in the last three months, and the Bank of Canada cutting rates three times since June, with more cuts expected.

Meanwhile, economic growth is expected to moderate but stay positive in most developed markets, while maintaining a stronger profile in emerging markets (see Figure 1), bringing a so-called "soft landing" into view. Historically, this type of environment tends to be positive for risk assets, as evidenced by the performance of the major indexes referenced above. (There can be no assurance that such conditions will continue in the future.)



**Figure 1. GDP Data Point to a Soft Landing in Developed Markets, Strong Growth in Emerging Markets**  
*Real (inflation-adjusted) gross domestic product growth, year-over-year for indicated periods*



Source: International Monetary Fund World Economic Outlook (July 2024 update). E=Estimated. For illustrative purposes only.

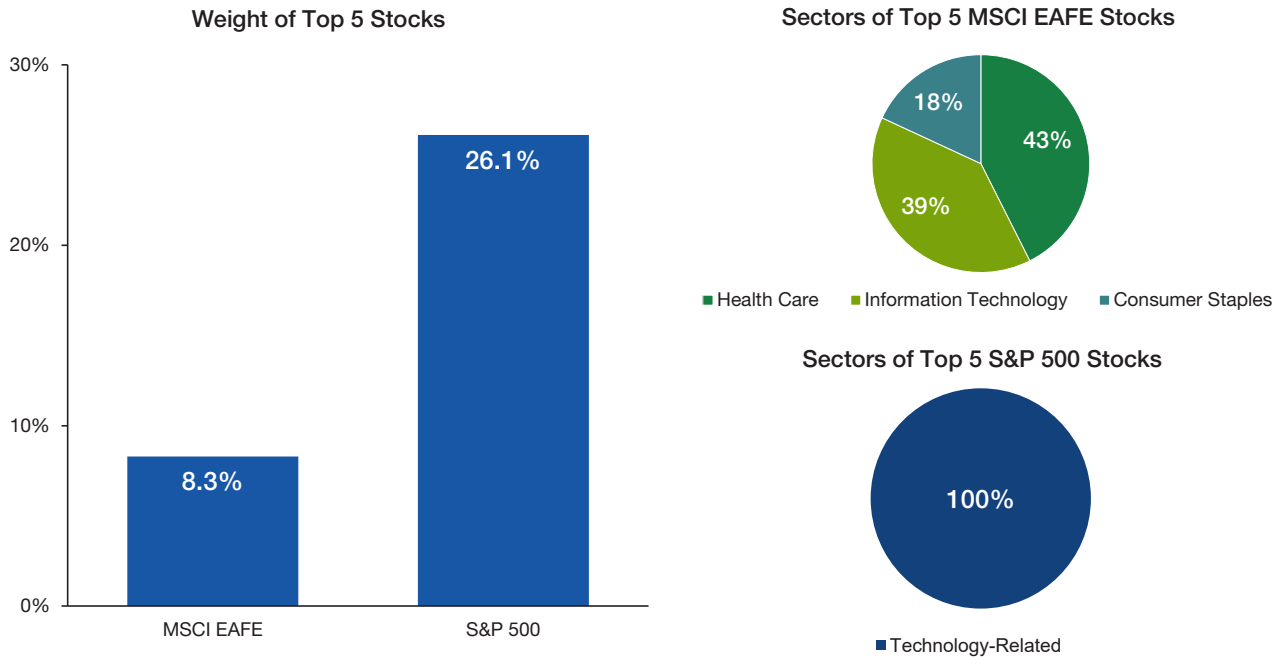
In a setting where yields are declining, European companies—having a larger share of floating-rate debt—are positioned to gain, as the interest payments on this debt periodically adjust according to current market interest rates. Reduced interest expense should lead to improved profitability and enhanced cash flow for corporate borrowers, freeing up capital that can be used to reduce debt, reinvest into the business, or return to shareholders through dividends and buybacks.

While we believe the U.S. equity market rally still has momentum, given a resilient U.S. economy and the continued investment in, and increasing adoption of, generative artificial intelligence (Gen AI), it is prudent to look at non-U.S. equity markets as well for their diversification benefits, cyclical and secular tailwinds. International markets are much more diverse, providing potential opportunities for active managers to win in different environments.

That diversity is evident when one looks at the composition of major equity indexes. The U.S. equity market has, over the years, become very tech-concentrated, resulting in an equity allocation that is skewed toward growth and dominated by just a handful of the biggest companies. In fact, the S&P 500's five largest stocks make up over a quarter of the market capitalization of the index (as of September 30) and are all technology-related. This growth skew has been a key driver of returns in U.S. markets recently. On the other hand, the five largest stocks in the MSCI EAFE make up less than 10% of the index and represent multiple industries and regions (see Figure 2), while also being significantly more value-oriented. We think a diversified portfolio of U.S. and international equities makes a lot of sense given the widely differing composition of these markets.



Figure 2. Diversification Across Geographies Can Present Opportunities for Equity Investors  
Composition data for indicated indexes as of September 30, 2024



Source: Factset. **Past performance is not a reliable indicator or guarantee of future results.** The historical data shown in the chart above are for illustrative purposes only and do not represent any specific portfolio managed by Lord Abbett. Indexes are unmanaged, do not reflect the deduction of fees or expenses, and are not available for direct investment.

The appeal of a broader geographic exposure becomes evident when one considers the many secular drivers that are positioned to benefit companies outside the United States. For example, the increasing adoption of AI could benefit AI-adjacent companies in Japan, many of which are smaller concerns that play in other parts of the supply chain outside of chip manufacturing. The increasing use of GLP-1 drugs to treat both diabetes and obesity could provide a boost to global pharmaceutical firms. There are also companies benefiting from the shifting of global supply chains in a post-pandemic world. In fact, according to Morgan Stanley Research, the percentage of U.S. imports from China has come down from a peak of just over 20% in 2018 to approximately 12% in 2024.

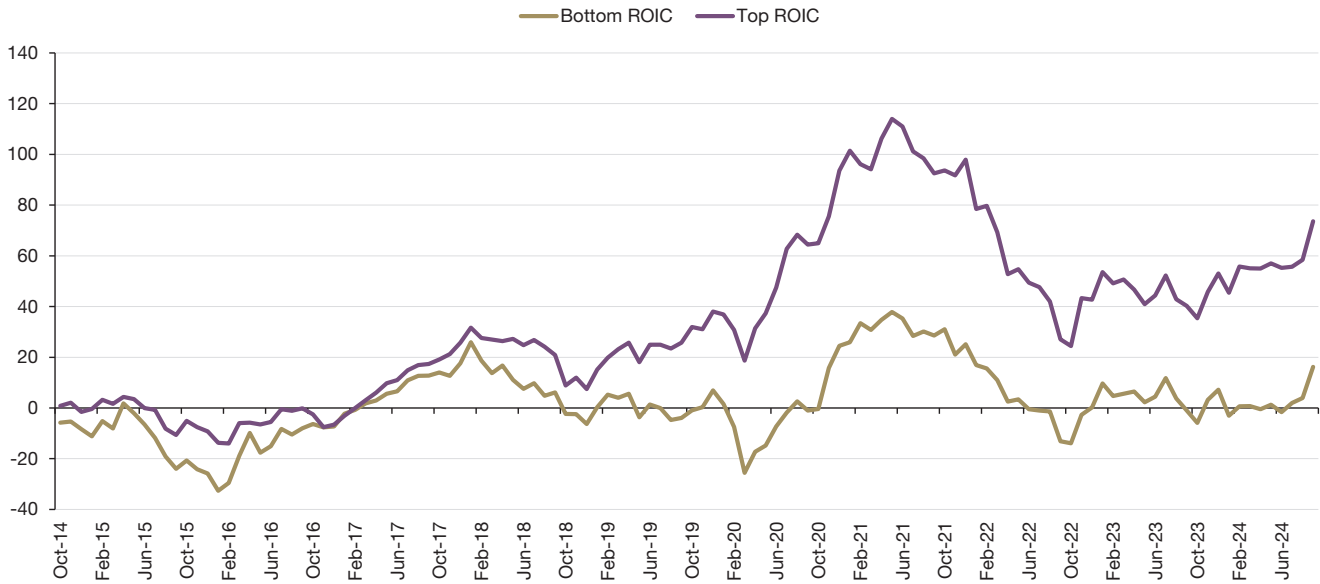
## Mapping a Global Equity Strategy

As we have observed, both cyclical and long-term factors make a compelling case for global equities. But what is the most effective way to invest in this asset class? While index investing is a common approach in U.S. equity markets, it may not be the best fit for international markets. Given the vast array of options, “owning the entire market” in a broader geographic universe also means holding companies with weak fundamentals, such as low returns on invested capital, negative earnings, poor or stagnant earnings growth, and high debt levels.

Therefore, we advocate a more selective approach to global equity investing, one that emphasizes identifying businesses with sustainable competitive advantages. These strengths enable firms to demonstrate robust quality indicators, including high returns on invested capital (ROIC), free cash flow, and healthy margins—traits that are characteristic of companies with a strong competitive “moat.” In fact, we have found that over the last decade, the top decile (top 10%) segment of the MSCI ACWI ex-USA Index, based on annual ROIC growth, outperformed the bottom decile by 57.4% (see Figure 3).



**Figure 3. Companies That Display a Key Measure of Competitive Strength Have Outperformed**  
*Performance of top- and bottom-decile companies on the MSCI All Countries World Index (ex-U.S.) based on return on invested capital (ROIC), September 30, 2014–September 30, 2024*



Source: FactSet. Return on invested capital, a measure of how effectively a company is creating value through its investments, is calculated by dividing a company's net operating profit after taxes by its total invested capital. **Past performance is not a reliable indicator or guarantee of future results.** The historical data shown in the chart above are for illustrative purposes only and do not represent any specific portfolio managed by Lord Abbett. Indexes are unmanaged, do not reflect the deduction of fees or expenses, and are not available for direct investment.

One final observation: Active management teams with deep and broad research and security valuation capabilities may be particularly well positioned to capitalize on the trends that could drive future growth across global equity markets.



## Glossary & Index Definitions

**Disinflation** is a decrease in the rate of inflation.

**Macroeconomics** is the study of large-scale or general economic factors and how they interact in economies.

**Market capitalization** is the total value of a company's outstanding shares of stock, which include publicly traded shares plus restricted shares held by company officers and insiders.

A "**moat**" is a type of sustainable competitive advantage that makes it difficult for a business' rivals to erode its market share.

**Return on invested capital** is calculated by taking into account the cost of the investment and the returns generated. Returns are all the earnings acquired after taxes but before interest is paid. The value of an investment is calculated by subtracting all current long-term liabilities, those due within the year, from the company's assets.

The **MSCI ACWI (All Country World Index)** is a free float-adjusted, market capitalization-weighted index that is designed to measure the equity market performance of developed and emerging markets.

The **MSCI EAFE Index** is an equity index which captures large and mid cap representation across 21 Developed Markets countries around the world, excluding the US and Canada. With 732 constituents, the index covers approximately 85% of the free float-adjusted market capitalization in each country. The **MSCI EAFE Ex-U.S. Index** excludes shares in the United States.

The **S&P 500®** Index is widely regarded as the standard for measuring large cap U.S. stock market performance and includes a representative sample of leading companies in leading industries.

Indexes are unmanaged, do not reflect the deduction of fees or expenses, and are not available for direct investment.

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