Dividends and International Value

Volatile markets have made investors weary of paying up for expensive stocks with limited profits and no dividends. Significant attention is being paid to high-quality companies with strong cash flows, profits, and the ability to pay high dividends, while also trading at reasonable valuations. Often, this type of company can be found outside of the U.S. Some of the best performing companies during 2022 were the type of companies in our investment wheelhouse—those with a global focus, strong cash flows, profits, and dividends.

Inflation and Fixed Income

40 years of declining interest rates came to an end as inflation soared to 9%+ during 2022. While uncomfortably high inflation was not a welcome turn of events, especially when combined with the Fed's response of undergoing one of the fastest rate hike cycles in memory, the positive trade off is rates paid by fixed income investments available for purchase are now three times more than what could have been obtained just one year ago. The fixed income portion of portfolios can now contribute meaningful levels of income towards overall portfolio return.

Market Leadership

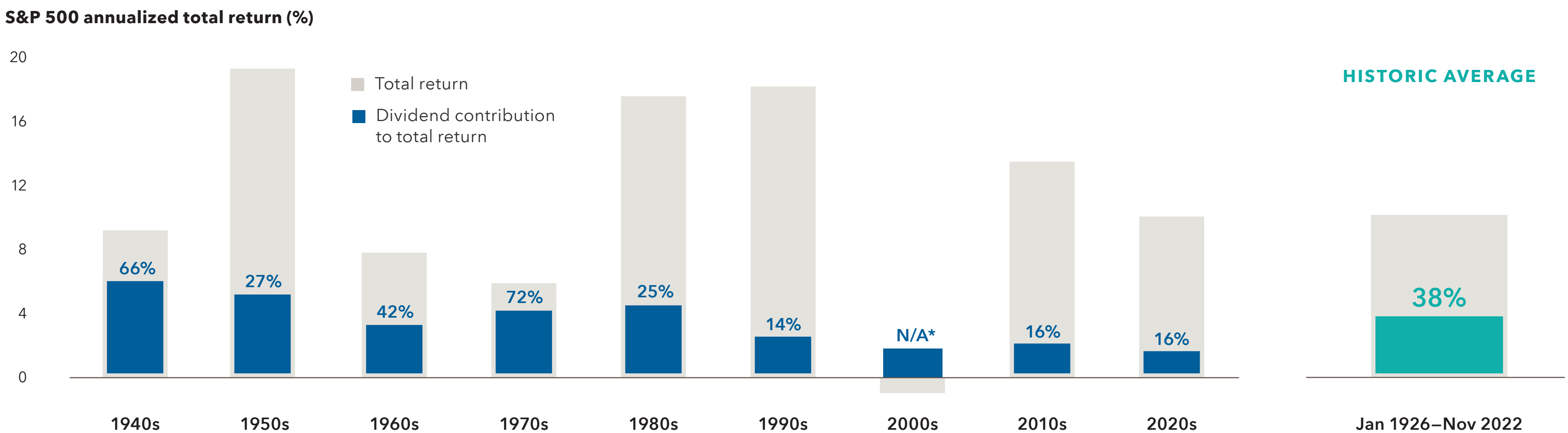
Markets have been dominated by a handful of mega-cap internet-related giants that traded at extreme prices compared to historical norms. Moving forward, we see greater emphasis being placed on a larger variety of companies, including those that produce physical assets. With a decade of loose monetary policy coming to an end, quality balance sheets and reasonable prospects will once again be of importance to investors. While digital companies are not going away, a wider range of market leadership could provide a tailwind for stock pickers.

During 2022, we were busy taking advantage of market volatility by positioning portfolios with a mix of quality global value equities and Treasury securities paying attractive yields. We believe quality international value equities, combined with higher fixed income yields, should provide a solid allocation for the year ahead.

The Barry Team

Look for dividends to account for a larger portion of total returns

Dividend contributions to returns by decade



Over the past decade, most investors spent little time thinking about dividends. With U.S. tech and consumer companies generating double-digit returns and dominating the lion's share of total market return, dividends appeared downright boring.

Today boring is beautiful, according to equity portfolio manager Caroline Randall. "With growth slowing, the cost of capital rising and valuations for less profitable tech companies declining, I expect dividends to be a more significant and stable contributor to total returns," Randall says.

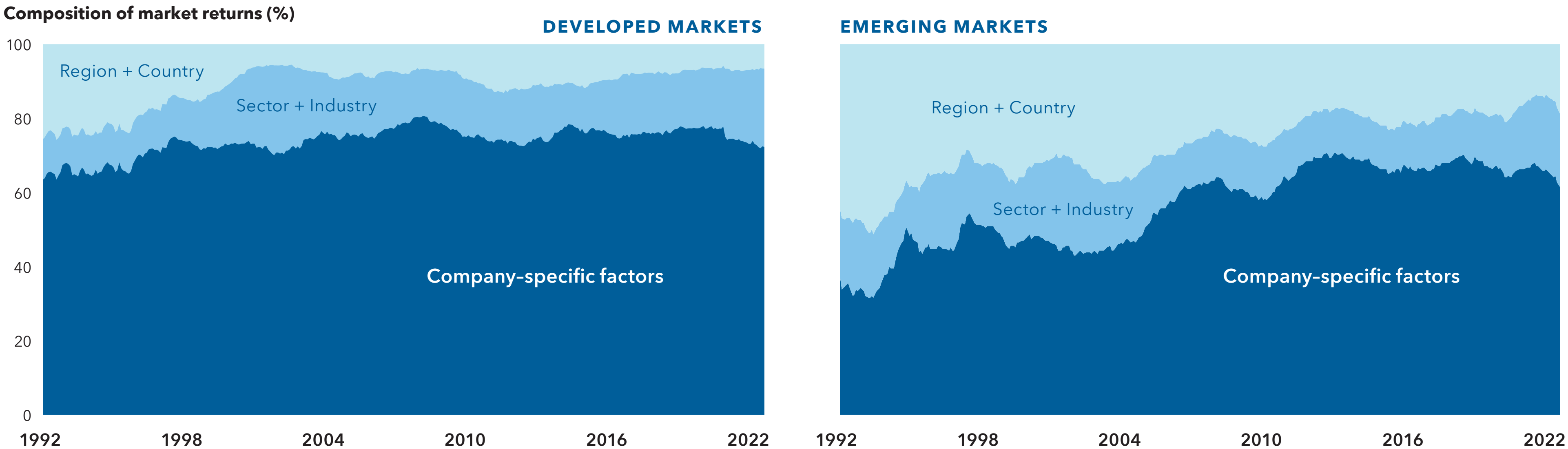
While dividends accounted for a slim 16% of total return for the S&P 500 Index in the 2010s, historically they have contributed an average 38%. In the inflationary 1970s they climbed to more than 70%. "When you expect growth in the single digits, dividends can give you a head start," Randall adds. "They may also offer a measure of downside protection when volatility rises, but it is essential to understand the sustainability of those dividends."

Companies that have paid steady and above-market dividends can be found across the financials, energy, materials and health care sectors, among others. Examples include Zurich Insurance, metals and mining multinational Rio Tinto, biopharmaceutical giant AbbVie, personal care company Kimberly-Clark, and tobacco makers Imperial Brands and British American Tobacco.

SOURCE: S&P Dow Jones Indices LLC. 2020s data is from 1/1/20 through 11/30/22. Past results are not predictive of results in future periods.
*Total return for the S&P 500 Index was negative for the 2000s. Dividends provided a 1.8% annualized return over the decade.

International outlook: Company fundamentals are more important than macro headwinds

During the past three decades, company-specific factors have had a large and growing impact on returns



There's no doubt investors have been frustrated in recent years with the persistent lagging returns of international equities. A strong U.S. dollar, weak economies in Europe and Japan, and various troubles in emerging markets have created a cloudy near-term outlook.

However, investors would do well to remember that there's a difference between top-down macroeconomic views and the fundamental, bottom-up prospects for individual companies. Company fundamentals are driving returns outside the U.S., placing added importance on individual stock picking.

For many multinational companies headquartered in economically struggling areas, national conditions often have little or no impact on revenues, except perhaps when it comes to regulation and taxes.

"In Europe, for example, investing in Airbus has a lot to do with demand for airplanes in the U.S. and China," says Capital Group portfolio manager Gerald Du Manoir, "while investing in LVMH has a lot to do with U.S. consumer demand for luxury goods.

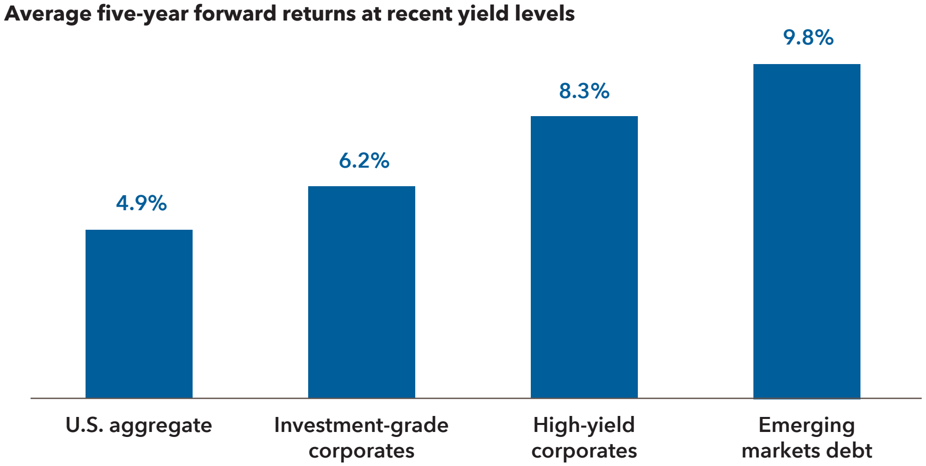
"In emerging markets," he adds, "investing in Taiwan Semiconductor Manufacturing has a lot to do with global demand for computer chips. Granted, the outlook for some economies doesn't look too compelling right now, but I feel confident that we can still find promising companies in Europe, Japan and emerging markets to populate our investment portfolios."

SOURCE: Empirical Research Partners. As of 9/30/22. Analysis provided by Empirical Research Partners using their developed market and emerging market stock universes that approximate the MSCI World Index and MSCI Emerging Markets Index, respectively. Data shows the percentage of market returns that can be attributed to various factors over time, using a two-year smoothed average. Past results are not predictive of results in future periods.

Income is back in fixed income

Investing at current yields has provided attractive returns

Average five-year forward returns at recent yield levels

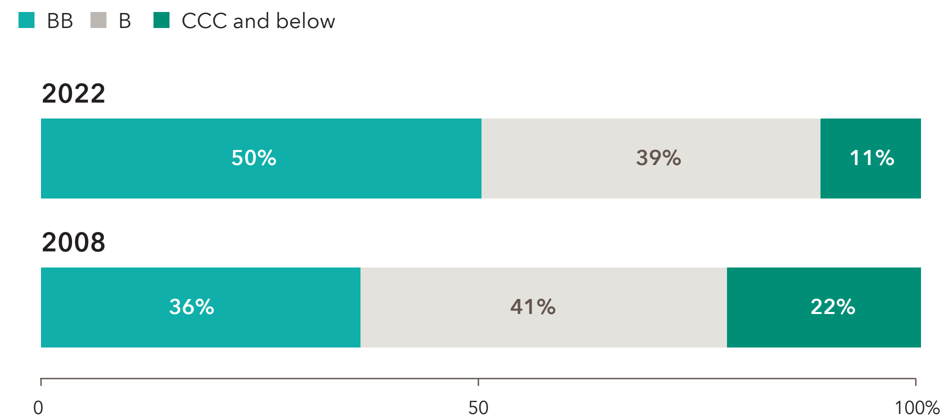


Starting yield (%)

U.S. aggregate	Investment-grade corporates	High-yield corporates	Emerging markets debt
4.56	5.31	8.63	7.68

CCC-rated and below are now 11% of high-yield universe

Bloomberg U.S. Corporate High Yield Index weight by credit quality



High inflation and hefty rate hikes by the Fed have given rise to a bond market rout. While painful, these losses can set the stage for higher income down the road. The yield on 10-year U.S. Treasury bonds climbed to 4.27% in October, the highest level since June 2008. Yields, which rise when bond prices fall, have soared across sectors. Over time, income levels should increase since the total return of a bond fund is made up of price changes and interest paid – and the interest component is now much higher.

One surprising element has been the resilience of consumers. Consumer spending accounts for roughly 70% of the economy, and spending has been robust.

"This has helped keep corporate balance sheets in pretty good shape," says fixed income portfolio manager Damien McCann. "But I expect credit quality to weaken as the economy slows. In that environment, I prefer defensive sectors such as health care over homebuilders and retail."

High-yield bonds are relatively well positioned for an economic slowdown as bond prices have already declined sharply as rates rose. An uptick in defaults, which markets have already priced in, could still increase in a deep recession.

"We went through a significant default cycle with the pandemic," says David Daigle, fixed income portfolio manager. "The underlying credit quality of the asset class has improved markedly since 2008."

SOURCES: Capital Group, Bloomberg, Bloomberg Index Services Ltd., J.P. Morgan. For left chart: Yields and monthly return data as of 11/30/22, going back to January 2000 for all sectors except emerging markets debt, which goes back to January 2003. Based on average monthly returns for each sector when in a +/–0.30% range of yield to worst shown. Sector yields above include Bloomberg U.S. Aggregate Index, Bloomberg U.S. Corporate Investment Grade Index (BBB/Baa and above), Bloomberg U.S. Corporate High Yield Index, 50% J.P. Morgan EMBI Global Diversified Index/50% J.P. Morgan GBI-EM Global Diversified Index blend. Yield to worst is a measure of the lowest possible yield that can be received on a bond that fully operates within the terms of its contract without defaulting. Past results are not predictive of results in future periods. For right chart: As of 11/30/22.

Stocks typically recover before recessions end

Everyone wants to know when the next recession will start and how long it will last. While each recession is painful in its own way, one potential bright spot is that they don't historically last very long. Our analysis of 11 U.S. cycles since 1950 shows that recessions have ranged from two to 18 months, with the average lasting about 10 months.

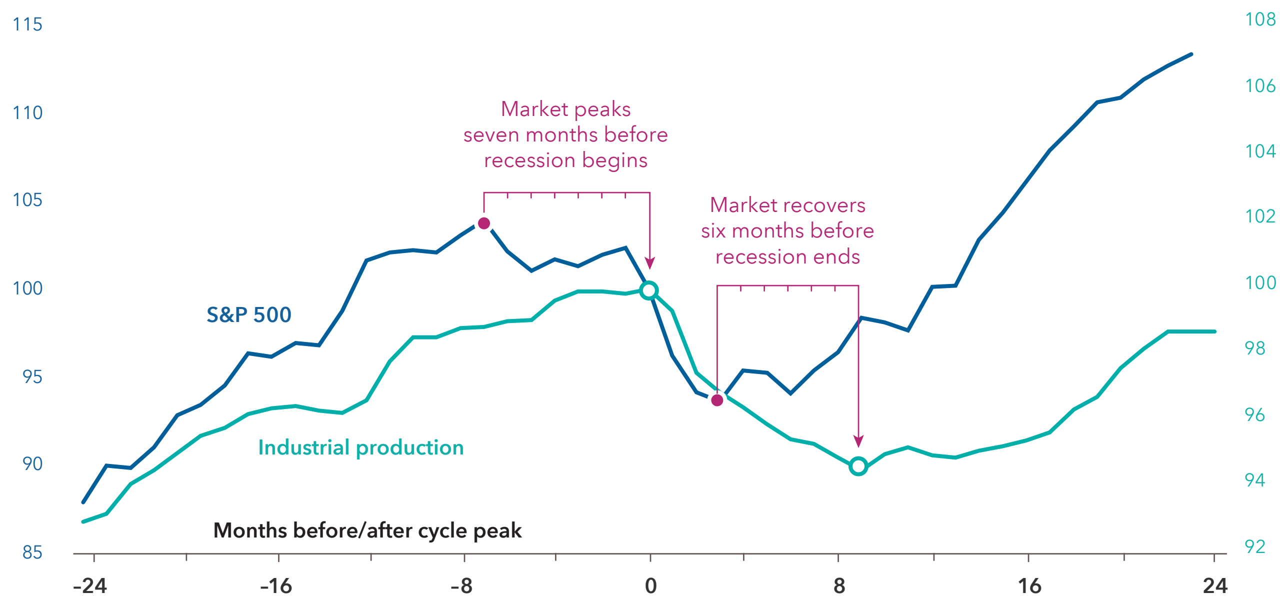
What's more, stock markets usually start to recover before a recession ends. Stocks have already led the economy on the way down in this cycle, with nearly all major equity markets entering bear market territory by mid-2022. And if history is a guide, they could rebound about six months before the economy does.

The benefits of capturing a full market recovery can be powerful. In all cycles since 1950, bull markets had an average return of 265%, compared to a loss of 33% for bear markets.

The strongest gains have often occurred immediately after a bottom. Therefore, waiting on the sidelines for an economic turnaround is not a recommended strategy.

"It's been a difficult year, and the pain may continue," says Capital Group economist Darrell Spence. "But it's important to keep in mind: One thing all past recessions and bear markets had in common was that they eventually ended. Ultimately, the economy and the markets should right themselves."

Stocks have been a leading indicator of the economy



	RECESSION	VS.	EXPANSION
Duration (months)	10		69
GDP growth	-2.5%		24.6%
Corporate earnings	-22%		96%
Net jobs added	-3.9M		12M

	BEAR MARKET	VS.	BULL MARKET
Duration (months)	13		67
Total return	-33%		265%

SOURCES: Capital Group, Federal Reserve Board, Haver Analytics, National Bureau of Economic Research, RIMES, Standard and Poor's. Data reflects the average of completed cycles in the U.S. from 1950 to 2021, indexed to 100 at each cycle peak. Corporate earnings calculated by Strategas for all completed cycles from 1/1/28–11/30/22. Other data includes all completed cycles from 1/1/50–11/30/22. Industrial production measures the change in output produced by manufacturers, mines and utilities and is used here as a proxy for the economic cycle. Past results are not predictive of results in future periods.