Northern Trust | Matt Peron: Get Your Value On!

[MUSIC PLAYING]

2017 was a strong year for markets globally, but the standouts were growth and momentum companies with momentum outperforming in the US by over 10%. We saw a similar pattern in other markets. Given these strong returns many market observers today decry a lack of value in the markets. But if investors are seeking value, why not buy value directly? I'm referring to the cheapest part of the market often called a value style or risk factor.

From a top-down view, the current business cycle has been an unusual one. At the highest level, it has appeared to be one big cycle that started nine years ago. However, if you take a closer look, it resembles a series of smaller cycles. Typically, early in a cycle value outperforms and eventually hands off to growth, which leads until the cycle ends. However, we may be at the start of one of these sub-cycles as global growth broadens. If that's the case, value, which has underperformed significantly in the current cycle, may be positioned for outperformance before again yielding to growth.

Let's take a look from the bottoms-up. How does the value factor look from a historical perspective? From a valuation perspective the value factor is one standard deviation cheap versus its typical valuation relative to the market. While it has been cheaper than this in the past, it is still at an attractive discount if you believe the economic expansion still has room to run. Outside the US, the value factor could be even more potent as these markets are even earlier in their business cycles.

Putting it all together, there is a case for value globally, both from a top-down and bottoms-up perspective. However, it's very difficult to time factors, so patience may be required. On the other hand, there is risk that the cycle ends early, which would be a problem for value investors. We are keeping an eye on those risks closely, but at this stage we believe the benefits outweigh the risks.

[MUSIC PLAYING]