

15 Picks Based on Experts' Forecasts

Experts think foreign stocks, especially emerging markets, are attractive. Here are Morningstar's favorites for those themes.

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Sensible investors quite reasonably go on the defense when they hear "market forecast."

After all, it's incredibly difficult to predict which way the market will go--so much so that most firms take a strategic (long-term and hands-off) approach to asset allocation rather than managing their client portfolios' asset allocations tactically.

But the fact is, you need to plug in some kind of return assumptions for the major asset classes when putting together a financial plan. You could simply stick with historical returns for stocks and bonds--8% to 10% or so for stocks and 5% to 6% for bonds. The risk of that approach, however, is that these markets' returns over your particular planning horizon might look different than those long-term forecasts, either better or worse.

My now-annual compendium of various asset managers' asset-class forecasts is meant to help investors make realistic assumptions of what their portfolios might return over the next decade. Of course, most individuals are planning for a time horizon of more than 10 years. But if the prognostications are notably pessimistic, as they have been recently, that suggests that investors should trim their portfolio's long-term return assumptions, too. (The shorter the investors' time horizon, the bigger that haircut should be.)

The expert forecasts can also come in handy when thinking about whether your portfolio needs to be repositioned. Indeed, the forecasts may well amplify portfolio shifts you've been contemplating already. For example, many hands-off investors have seen their foreign-stock holdings shrink in importance relative to U.S., thanks in large part to strong

performance from domestic markets. Not only are their own Morningstar Portfolio X-Ray views suggesting that it's time to rebalance, but bullish forecasts for foreign stocks provide further impetus to do so.

With that in mind, I've highlighted some of the key themes from last week's article, as well as some corresponding mutual fund, exchange-traded fund, and even individual stock picks that correspond with those themes. For mutual funds and ETFs, I've focused on Morningstar Medalist funds; for individual stocks, I've focused on those that earn Morningstar Ratings of 4 or 5 stars currently.

Core Foreign Stocks

The Bull Case: Foreign markets had a terrific year in 2019. While most foreign-stock funds underperformed their U.S.-focused counterparts, that differential owed primarily to the dollar's strength relative to foreign currencies, not underlying weakness in the markets themselves. But judging from our expert forecasts, there's still gas in the tank for foreign stocks: Every firm we sampled expected better returns from foreign stocks than U.S. names over the next seven to 10 years. (Time horizons for the forecasts varied by firm.)

The Picks: If you've decided it's finally time to up your portfolio's allocation to foreign stocks, there are a few key ways to do so.

For individual stock investors, Morningstar's research corroborates the notion that foreign stocks look inexpensive relative to U.S. stocks: Fully two thirds of the stocks that currently receive 4- or 5-star ratings are domiciled outside the United States. When I screened for non-U.S. names with 4 or 5 stars, wide moats, and low fair value uncertainty ratings, four stocks fit the bill: Anheuser Busch (BUD), British

American Tobacco (BTI), Imperial Brands (IMBBY), and Roche Holdings (RHHBY). The tobacco makers currently rate 5 stars, but they may not appeal to all investors for ethical reasons.

For investors who would rather not pick individual stocks, plenty of mutual funds provide broad-based exposure to non-U.S. names. One of my favorite active funds is American Funds International Growth and Income (IGIFX), which I've used as the core non-U.S. holding in my "bucket" model portfolios for retirees. The fund had a standout year in 2019, owing in part to its heavy exposure to technology stocks. But the fund, which has a Morningstar Analyst Rating of Gold, also has long-term appeal thanks to its reasonable costs and sensible strategy. (Sibling American Funds EuroPacific Growth (AEPGX) is also Gold-rated.)

For investors who can withstand some volatility, Oakmark International (OAKIX) is a topnotch, contrarian-minded choice that is currently open to new investors. (It has been periodically closed over the years.)

If you're in search of a single non-U.S. fund that covers the waterfront, it's hard to go wrong with a broadly diversified foreign-stock index fund. Morningstar has several Gold-rated passive foreign-stock funds: iShares Core MSCI Total International Stock (IXUS) and Vanguard Total International Stock Market Index (VGTSX) are among the best. (The iShares fund is ETF-only, whereas the Vanguard fund is available as an ETF or traditional index fund.)

Emerging-Markets Stocks

The Bull Case: A handful of the firms in our roundup of market forecasts believe that the emerging-markets subgroup of the foreign-stock universe is particularly attractive today. Grantham Mayo Van Otterloo, for example, is pessimistic about the prospects for U.S. stocks and bonds, anticipating that both asset classes will end up in the red in inflation-adjusted terms over the next seven years. But its outlook for emerging-markets equities--4.5% real returns--is robust by comparison. Research Affiliates is similarly pessimistic about U.S. stocks and bonds but sanguine about emerging-markets equities: At year-end, its valuation-

dependent model was forecasting a whopping 6.8% real return from emerging-markets equities over the next decade.

The Picks: Of course, many investors own emerging-markets equities through broadly diversified foreign-stock funds. For example, total international index funds stash more than 20% of their portfolios in emerging-markets names. That said, some investors may choose to overweight emerging markets even more, or might wish to maintain discrete emerging/developed-markets funds to facilitate rebalancing.

On the active side, some of the best funds are closed or otherwise limiting purchases for new investors, including T. Rowe Price Emerging Markets Stock (PRMSX) and Harding Loevner Institutional Emerging Markets (HLMEX), both Silver-rated. But a handful of worthy active funds are still accepting new cash, including Seafarer Overseas Growth and Income (SIGIX) (Silver), GQG Partners Emerging Markets Equity (GQGRX) (Silver), Brandes Emerging Markets Value (BEMIX) (Silver), and Causeway Emerging Markets (CEMIX) (Bronze).

Among Morningstar's top-rated passive options for emerging-markets exposure are iShares Core MSCI Emerging Markets (IEMG), Schwab Emerging Markets Equity (SCHE), and Vanguard FTSE Emerging Markets (VWO). The Vanguard fund is available as either a traditional index mutual fund or ETF.



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