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It's time to switch from a short-term thesis to a longer-term thesis, in our view. The popular tactical trade that has mostly benefitted growth companies for the last six months should give way to a more balanced approach. That also includes value stocks, dividend stocks and stocks with low volatility. We think most of the current uncertainties that are causing many investors to stay on the sidelines will be gone in the next six months.

We are fairly confident of the following:

- We should have a vaccine sometime soon, perhaps in the next six months, per most experts.
- The Supreme Court will have a ninth member sometime in the next six weeks to six months.
- All the elections in the Senate and the House and executive branch will have an outcome, almost certainly, before the end of November, but probably sooner.
- Importantly, one of the certainties with us today that should benefit the equity markets will not change even when the uncertainties fade away. That is, the Fed will keep rates low for a long time and will provide support to the economy as well.

Then, I think there are two key words here: First, *TINA*, the acronym for "There Is No Alternative." There is no real return on your cash without taking some level of risk. Second, *Temporary*, as in we believe the critical uncertainties weighing on the markets are temporary and about to be behind us, including the approximate 20% earnings decline in the S&P 500 Index in 2020 that should be mostly concentrated in the second quarter.

So, the conclusion we have drawn from thinking further out is the following: use equities as the primary vehicle to position your risk assets. Also, we think dividend equities provide some of the best opportunities to capture income with some upside potential. Finally, we believe it is time to move away from the tactical trade by shifting some dollars from sectors and industries with high valuations and high expectations to sectors with very low expectations and low valuations.

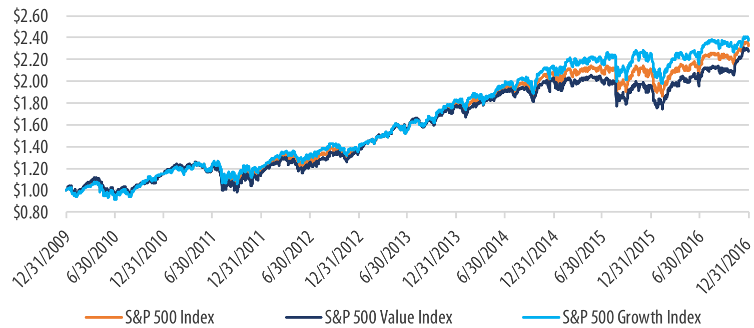
It seems like it has been "all growth all the time." When will value make a comeback?

It does seem that way and there is no question growth has dominated value for a while now. From 12/31/2009 through 9/30/2020, the S&P 500 Large Cap Growth Index's cumulative return is 378% versus the Large Cap Value Index's return of only 179% over the same period. That's massive—an average annual return of 15.7% a year for growth versus 10.0% for value over the 10 years and 9 months period.

But, almost all of that outperformance is since the end of 2016. From the start of the decade (12/31/2009) until 12/31/2016 growth returned 137% and value returned 127%. So, just a small amount of outperformance, for growth versus value stocks for the first 7 years of the decade. (See Figures 1 and 2)

Figure 1 S&P 500 Growth vs. Value Performance

12/31/09 – 12/30/16	S&P 500 Large Cap	S&P 500 Large Cap Value	S&P 500 Large Cap Growth
Cumulative Total Return	132.85%	127.32%	137.42%
Difference vs. Value	5.53%		10.09%



12/31/09 – 9/30/20	S&P 500 Large Cap	S&P 500 Large Cap Value	S&P 500 Large Cap Growth
Cumulative Total Return	276.53%	178.57%	378.16%
Difference vs. Value	97.67%		199.60%

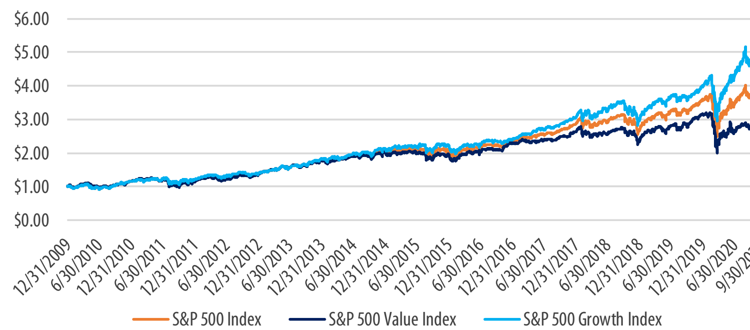
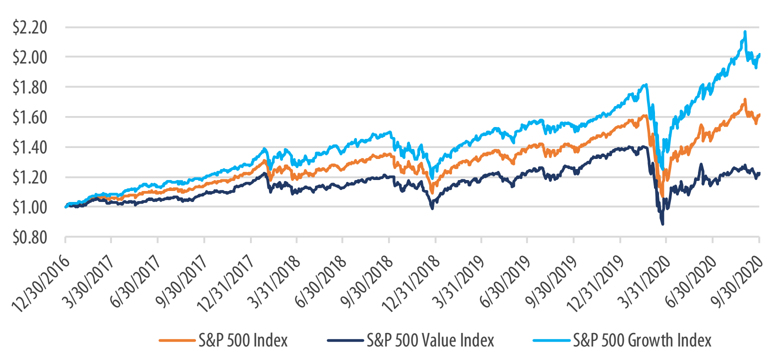


Figure 2 S&P 500 Growth vs. Value Performance

12/30/16 – 9/30/20	S&P 500 Large Cap	S&P 500 Large Cap Value	S&P 500 Large Cap Growth
Cumulative Total Return	61.66%	22.63%	101.50%
Difference vs. Value	39.03%		78.87%



Source for Chart Data: Bloomberg. All data is as of 9/30/2020. The charts are for illustrative purposes only and not indicative of any investment. Indexes do not chart management fees or brokerage expenses and no such fees or expenses were deducted from the performance shown. **Past performance is not a guarantee of future results.**

It has really just been the last three years and nine months where we have seen a one-way dominant trade, with growth up 102% and value up only 23%. So, it is more of a recent phenomenon than many may realize. Different people will have different explanations as to why growth is dominating—low interests rates favor growth companies, growth companies are scarce and have a bigger audience, better balance sheets and fundamentals, long-term secular stories, new economy, etc. That can be true for a lot of growth companies, and remember, we still like the growth trade. But, it is important to understand the rest of the reasons the gap between value and growth became so wide. (Figures 3 and 4) A substantial part of the outperformance these last three years and eight months was multiple expansion, not just superior earnings.

The message is simple. First, be careful about future certainties just based on the recent past. Second, beware of crowded trades, especially when valuations are increasing rapidly in a very short time frame.

Figure 3 S&P 500 Growth & Value Indexes' Top 10 Largest Holdings as of 12/30/16

S&P 500 Value

Ticker	Name	Weight	Market Cap	P/E Ratio
XOM	Exxon Mobil Corp	4.13%	$374,280.54	42.2
BRK/A	Berkshire Hathaway Inc	3.41%	$401,644.41	22.5
JPM	JPMorgan Chase & Co	3.41%	$308,768.41	15.2
T	AT&T Inc	2.88%	$261,176.73	19.0
WFC	Wells Fargo & Co	2.75%	$276,779.13	13.7
BAC	Bank of America Corp	2.46%	$223,321.54	15.1
CVX	Chevron Corp	2.45%	$222,190.45	115.8
C	Citigroup Inc	1.87%	$169,359.47	11.5
CSCO	Cisco Systems Inc	1.67%	$151,697.11	14.6
GE	General Electric Co	1.63%	$279,545.91	31.0
		Weight	**Total**	**Average**
		26.68%	$2,668,763.70	20.5*

S&P 500 Growth

Ticker	Name	Weight	Market Cap	P/E Ratio
AAPL	Apple Inc	6.05%	$617,588.49	14.1
MSFT	Microsoft Corp	4.73%	$483,160.29	22.7
AMZN	Amazon.com Inc	2.90%	$356,313.13	171.4
FB	Facebook Inc	2.64%	$332,401.77	40.8
GOOGL	Alphabet Inc	4.54%	$538,572.17	28.5
JNJ	Johnson & Johnson	1.87%	$313,432.46	18.3
CMCSA	Comcast Corp	1.61%	$165,225.07	20.0
HD	Home Depot Inc/The	1.60%	$163,331.03	21.9
UNH	UnitedHealth Group Inc	1.49%	$152,328.67	23.9
V	Visa Inc	1.43%	$203,445.07	27.1
		Weight	**Total**	**Average**
		28.87%	$3,325,798.15	24.1*

Source for Figures 3 and 4: Bloomberg as of 9/30/2020. All market capitalization numbers are in USD$ Millions.
*Average P/E ratios exclude Chevron (CVX) and Amazon (AMZN).

These examples are for illustrative purposes and do not represent any actual investment.

Past performance is no guarantee of future results.

Clearly, it's difficult to articulate a great story for value when it has been almost four years of huge underperformance versus growth. If you look at history and the value factor, however, value has been a long-term winner. In the decade ended 2009, the top 10% of value stocks as measured by price-to-book ratio beat the top 10% of growth stocks by 8.3% per year (see Figure 5). Last decade it reversed and growth beat value by 7.8% per year. Again, if you look at the last 20 years through the end of 2019, large value still outperformed large growth for those two decades by 75 basis points (0.75%) per year. The other thing to remember is that the future for value stocks needs to be worse than what's been forecasted and expectations are already extremely low.

Figure 4 S&P 500 Growth & Value Indexes' Top 10 Largest Holdings as of 9/30/20

S&P 500 Value

Ticker	Name	Weight	Market Cap	P/E Ratio
BRK/B	Berkshire Hathaway Inc	3.89%	$ 508,935.41	40.9
UNH	UnitedHealth Group Inc	2.73%	$ 296,286.19	17.5
VZ	Verizon Communications Inc	2.27%	$ 246,172.83	11.1
JNJ	Johnson & Johnson	2.10%	$391,974.75	26.5
PFE	Pfizer Inc	1.88%	$ 203,937.50	15.6
T	AT&T Inc	1.87%	$203,133.75	12.2
WMT	Walmart Inc	1.79%	$396,470.39	26.9
BAC	Bank of America Corp	1.69%	$208,718.12	11.5
CSCO	Cisco Systems Inc	1.54%	$166,754.62	13.9
JPM	JPMorgan Chase & Co	1.41%	$293,392.88	12.7
		Weight	**Total**	**Average**
		21.16%	$2,915,776.41	18.9

S&P 500 Growth

Ticker	Name	Weight	Market Cap	P/E Ratio
AAPL	Apple Inc	10.94%	$1,980,644.72	35.2
MSFT	Microsoft Corp	9.35%	$1,591,704.42	36.2
AMZN	Amazon.com Inc	7.88%	$1,577,166.31	121.1
GOOGL	Alphabet Inc	5.12%	$998,274.50	32.4
FB	Facebook Inc	3.70%	$746,104.88	32.0
V	Visa Inc	1.98%	$440,539.22	34.9
NVDA	NVIDIA Corp	1.96%	$333,932.72	88.0
MA	Mastercard Inc	1.76%	$338,528.76	46.4
ADBE	Adobe Inc	1.38%	$235,268.59	61.9
PYPL	PayPal Holdings Inc	1.36%	$231,175.26	87.0
		Weight	**Total**	**Average**
		45.44%	$8,473,339.30	50.4*

Figure 5 Value Factor (P/B) Performance through the Decades

Decade	Top-Decile Value	Top-Decile Growth	Excess Return
1930	-9.4%	-0.1%	-9.4%
1940	18.0%	6.4%	11.6%
1950	20.4%	19.5%	0.9%
1960	10.5%	8.4%	2.1%
1970	14.6%	1.6%	13.0%
1980	23.8%	11.6%	12.2%
1990	17.9%	20.3%	-2.4%
2000	4.8%	-3.6%	8.3%
2010	8.4%	16.2%	-7.8%

Data source: Kenneth R. French data library using the CRSP database. Universe includes all NYSE, AMEX & NASDAQ stocks. Stocks are market cap weighted.

Is it different this time? Is value dead, or at least a permanent laggard?

Again, as mentioned, if you look at the last 20 years through the end of 2019, value still outperformed growth. Currently, growth has remarkable momentum year-to-date in 2020 and is significantly outperforming value (32% through September), and also has outperformed value by 86 basis points (0.86%) per year for 20 years and 9 months. That's amazing that this year has flipped the 20 year value outperformance. But investing is always about looking forward. Many investors do think value is dead, but we expect cyclical value companies to perform much better when there is a normalized environment. Capital intensive companies have higher costs and higher debt levels and are usually more on the value side of the market—that is a negative right now. But since there is little new investment in those industries, the companies may end up with less competition. Energy is a good example: massive cuts in capital spending , no new entrants in the space, the lowest rig counts since 2005 (in fact massively lower). No one is increasing spending in energy exploration, so when demand comes back, we believe it's likely that energy companies will benefit.

What areas of value should you avoid, and which areas could be the best option?

In our view, you should avoid the deepest value areas that had the highest headwinds pre-COVID: traditional retail, old media, and old advertising. It's not necessarily going to get appreciably better, and they probably won't ever receive a big multiple. Number two we believe you should avoid: those names with the worst balance sheets and poor margins. Mixing some quality factors with value factors almost always makes sense because many value stocks tend to have worse balance sheets and margins than growth stocks, in our opinion.

We currently favor utilities. They are in the value camp but also provide lower volatility. Plus, they give an investor yield. There are 28 utility stocks in the S&P 500 Index and the yield is 3.5% for the S&P 500 Utilities Index as of 9/30/20. That is almost 5 times higher yield than the 10-year Treasury. Earnings are actually expected to be flat this year for the utilities sector and expected to be up 6% next year. The only other sectors with that stability this year and growth next year are health care and technology. Also, other sectors with good dividends as well as lots of value companies, like industrials and financials, are expected to lead in earnings growth next year. (See Figure 6)

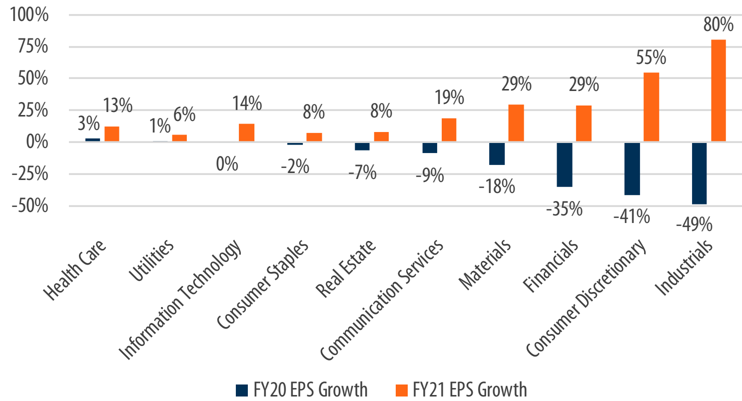
You have mentioned lately how much cash is on the sidelines? Over $8 trillion in checking accounts and money markets. When does that money move and where does it go? (Figures 7, 8 and 9)

Bond proxies are going to be a big story in 2021, in our opinion, as money moves off the sidelines looking for income. If you add low volatility to yield, utilities will keep popping up on your screen. They are also the fourth worst performing sector year-to-date, down almost 8% (price return) through the end of September. The safest way to play value, in our opinion, is to find quality secure dividends with an overweight in sectors with low volatility. Utilities certainly qualify, in our view.

These examples are for illustrative purposes and do not represent any actual investment.

Past performance is no guarantee of future results.

Figure 6 S&P 500 Index: Expected Earnings Growth Rates

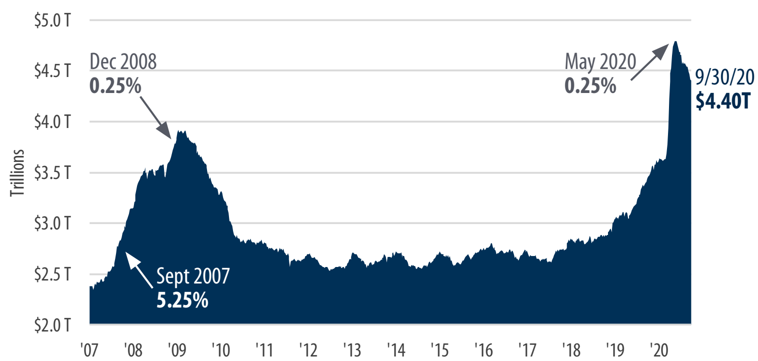


Source: Bloomberg. As of 9/30/2020. Earnings growth rates are based on aggregate sell-side estimates. FY is fiscal year. The S&P 500 Index is an unmanaged index of 500 stocks used to measure large-cap U.S. stock market performance. Investors cannot invest directly in an index. Earnings per share (EPS) is calculated as a company's profit divided by the outstanding shares of its common stock. The resulting number serves as an indicator of a company's profitability. EPS growth illustrates the growth of earnings per share over time.

Figure 7 Money Market Fund Assets Are Surging

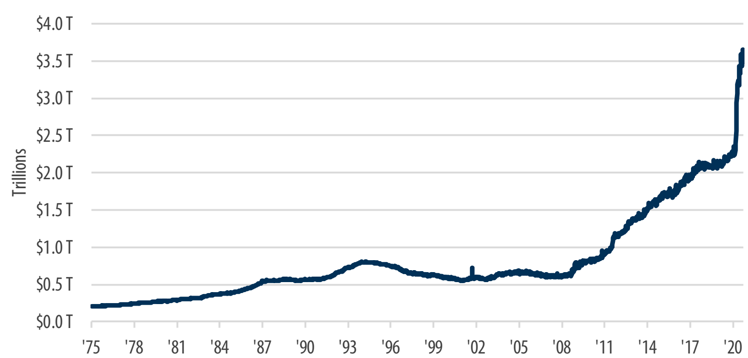
ICI All Money Market Funds (Total Net Assets)

Money market fund assets totaled $4.40 trillion for the week ended 9/30/20, up from $3.63 trillion at the start of 2020.



Source: Investment Company Institute (ICI). Weekly data from 2007-9/30/20.

Figure 8 Total Checkable Deposits



Source: Federal Reserve Bank of St Louis. Weekly data from 1975 – 9/30/20, seasonally adjusted.

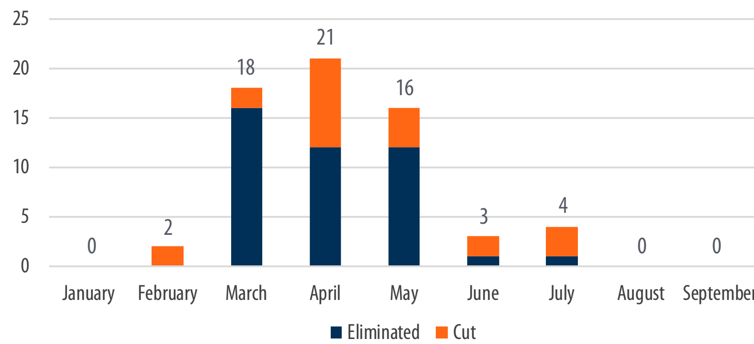
Checkable deposits consist of any demand deposit account against which checks or drafts of any kind may be written.

Do you think investors are confident that dividends are safe? (Figures 9 and 10)

Investors were right to be concerned that dividends were not safe, however, dividend cuts are mostly past us, in our opinion. Fifty-five S&P 500 members cut or eliminated their dividends from March to May this year, but there were no cuts or eliminations in August or September (Figure 9). Furthermore, the majority of cuts were in the hardest hit areas. We believe investors are getting this wrong, which creates a nice opportunity when they realize that dividends are safe. So, we believe if you find quality dividends and rising dividends, you will find yield and low valuation in a lot of names.

Finally, look at history. If you look at factor performance, (Figure 10) you can see how poorly value and yield have performed as factors over the last four years. However, the aftermath of prior recessions like 2000 and 2009 tell us that value and yield led the recovery.

Figure 9 S&P 500 Index: 2020 Dividend Eliminations & Cuts by Month



Source: Capital IQ & Bloomberg. As of 9/30/20. Includes current and S&P 500 Index members that have left the index this year.

Figure 10 Yearly Factor Performance

	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008
Top	Value 34.65%	Mom 18.49%	Mom 75.03%	Yield 24.61%	Yield 10.13%	Low Vol -2.50%	Value 46.88%	Value 23.49%	Mom 18.90%	Yield 21.08%	Mom 17.82%	Low Vol -26.42%
2	Yield 34.51%	Quality 14.93%	Size 23.92%	Low Vol 24.32%	Value 7.33%	Yield -4.40%	Size 41.89%	Yield 21.07%	Value 11.83%	Low Vol 19.28%	Quality 14.03%	Yield -32.83%
3	Low Vol 34.01%	S&P 500 EW 12.19%	Quality 23.81%	Value 22.05%	Low Vol 5.30%	Quality -9.34%	S&P 500 EW 40.97%	Quality 20.46%	Quality 10.24%	Value 18.01%	Size 4.54%	Mom -35.93%
4	S&P 500 EW 29.05%	Low Vol 6.44%	S&P 500 EW 12.03%	S&P 500 EW 9.64%	Quality 1.53%	Mom -11.62%	Mom 35.81%	Low Vol 19.32%	Size 9.24%	S&P 500 EW 15.80%	S&P 500 EW 1.53%	Size -36.46%
5	Mom 28.13%	Yield 4.62%	Value -0.82%	Quality 7.96%	S&P 500 EW -0.39%	Value -17.57%	Quality 34.61%	S&P 500 EW 16.95%	S&P 500 EW 8.06%	Quality 15.04%	Low Vol 1.22%	S&P 500 EW -39.72%
6	Quality 27.30%	Size 4.21%	Yield -4.86%	Size -1.06%	Size -2.72%	S&P 500 EW -18.18%	Yield 32.82%	Size 16.54%	Yield 6.13%	Size 14.81%	Yield -6.72%	Quality -40.31%
Bottom	Size 20.39%	Value 3.92%	Low Vol -5.03%	Mom -8.43%	Mom -11.35%	Size -19.05%	Low Vol 28.72%	Mom 14.81%	Low Vol 5.89%	Mom 9.83%	Value -7.64%	Value -41.69%

	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020
Top	Value 49.32%	Size 25.69%	Low Vol 10.00%	S&P 500 EW 17.65%	Mom 43.89%	Low Vol 18.39%	Low Vol 5.33%	Value 25.16%	Quality 23.53%	Low Vol -2.92%	Quality 32.69%	Mom 11.50%
2	S&P 500 EW 46.31%	Mom 24.72%	Yield 7.81%	Mom 17.62%	Size 39.43%	Yield 16.93%	Mom 2.76%	Yield 23.04%	Mom 20.55%	Mom -4.52%	S&P 500 EW 29.24%	Quality 2.46%
3	Size 43.35%	Value 22.70%	Quality 1.08%	Value 17.41%	Quality 38.23%	S&P 500 EW 14.49%	Yield -1.76%	Size 16.41%	S&P 500 EW 18.90%	Yield -7.25%	Size 28.44%	S&P 500 EW -4.75%
4	Quality 41.50%	Quality 22.37%	S&P 500 EW -0.11%	Size 16.90%	Value 36.60%	Quality 12.01%	S&P 500 EW -2.20%	S&P 500 EW 14.80%	Low Vol 18.79%	Quality -7.55%	Low Vol 27.52%	Low Vol -5.10%
5	Yield 34.45%	Yield 22.17%	Size -1.17%	Quality 16.72%	S&P 500 EW 36.16%	Value 9.45%	Quality -2.51%	Low Vol 14.21%	Size 16.36%	S&P 500 EW -7.64%	Value 27.43%	Size -7.36%
6	Low Vol 23.28%	S&P 500 EW 21.91%	Value -2.11%	Yield 15.93%	Yield 28.33%	Size 8.30%	Size -4.15%	Quality 11.74%	Yield 13.81%	Size -10.46%	Yield 26.96%	Yield -18.71%
Bottom	Mom 14.71%	Low Vol 17.08%	Mom -3.11%	Low Vol 14.08%	Low Vol 26.96%	Mom 7.75%	Value -6.16%	Mom 6.94%	Value 12.45%	Value -14.71%	Mom 24.81%	Value -22.95%

Data Sources: Capita IQ PIT data. Returns are total returns. Universe: largest 1,000 U.S. firms with $1 million in average daily volume over the previous 3 months. Top 30% of stocks by factor are selected. Stocks are then equally weighted. Past performance is no guarantee of future results. Data updated as of 9/30/2020.

Value: Lowest price-to-book **Momentum:** Highest 12-month price change **Quality:** Highest return-on-equity **Size:** Lowest market capitalization **Low Volatility:** Lowest 1-year price variability **Dividend Yield:** Highest dividend yield

Final Thoughts?

Sure. We think it's time to allocate some equity assets to parts of the market that we feel are positioned to perform better in the future. History shows us that value and yield performed well coming out of a recession, although past performance does not guarantee future results. We expect this time to be no different. Valuations and expectations are very low in equities with those factor exposures.

Dave McGarel is Chief Investment Officer, Chief Operating Officer and a Managing Director. As First Trust's Chief Investment Officer, Dave consults with the other members of the Investment Committee on market conditions and First Trust's general investment philosophy. As Chief Operating Officer, Dave is responsible for First Trust operations, including information systems, trust administration and First Trust administration.

Dave has over 20 years of experience and is a graduate of the University of Notre Dame with a BS in Accounting. He is a member of the CFA Society of Chicago and the CFA Institute. Dave is also a member of the American Institute of Certified Public Accountants.