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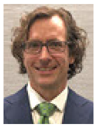
The Incredible Shrinking US Equity Market

The US public equity market is shrinking while the international equity market is growing—in terms of both size and potential opportunity for investors.



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IN THE LAST DECADE, THE US EQUITY MARKET SHRANK WHILE THE NON-US EQUITY MARKET GREW. From a numbers perspective, it can be explained simply: There just aren't enough US companies going public to replace the companies going private, merging, or being removed from an index (FIGURE 1).

But numbers can be misleading. Whether it's due to low liquidity (which makes it difficult to sell an investment at the desired time/price), low trading volume, or simply a foreign market that's difficult for US investors to access, not all non-US equities are readily available to US investors.

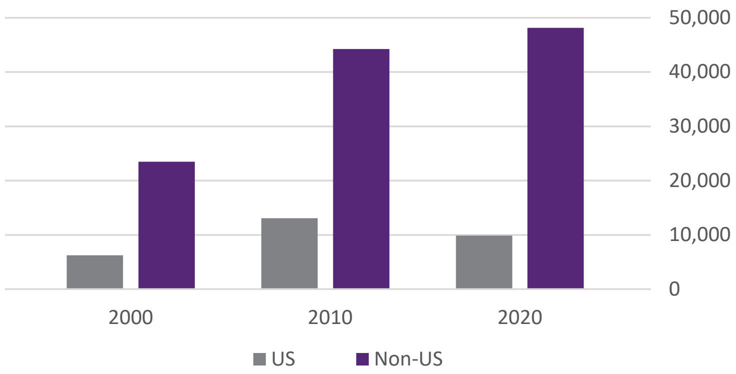
So rather than focusing on how many US stocks vs. international stocks there are, the real question is this: Is a shrinking US market being offset by a growing international opportunity set?

Here are three reasons why I believe the international market is not just growing, but becoming more accessible and investable for US investors.

Key Points

- The US equity market is losing more listed companies than it's gaining.
- About three times as many international companies have gone public than US companies in the last decade.
- US investors now have access to the China A-share market, but it's just the tip of a very large iceberg.

FIGURE 1
The US Equity Market Is Shrinking as the International Equity Market Grows
Number of publicly listed companies per exchange



As of 12/31/20. Source: Bloomberg, 3/21.

The pace of initial public offerings outside the US has been truly staggering.

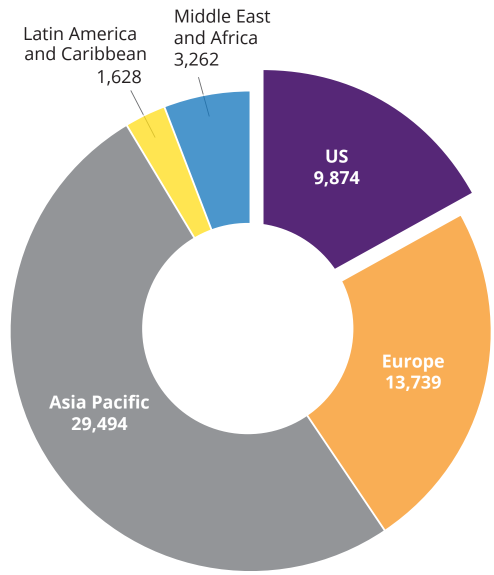
1. **Initial Public Offerings (IPOs):** According to data from Bloomberg, the pace of IPOs outside the US has been truly staggering. From 2011–2020, there were about 8,000 US IPOs. Over that same time period, there were more than 25,000 IPOs outside the US, a 3:1 ratio in favor of international equities.

3x MORE INTERNATIONAL COMPANIES HAVE GONE PUBLIC IN THE LAST DECADE

Why? In developed markets such as the US, private-equity investing[1] is one option for companies to access capital. In developing markets (those that are much smaller in size than developed markets), IPOs can be an attractive way to access investor capital on a more global scale. The standout in terms of IPOs has been the Asia Pacific region and China in particular. During the last decade, more than 70% of non-US IPOs came from the Asia Pacific region.

Asia Accounts for More Than Half the World's Publicly Traded Companies

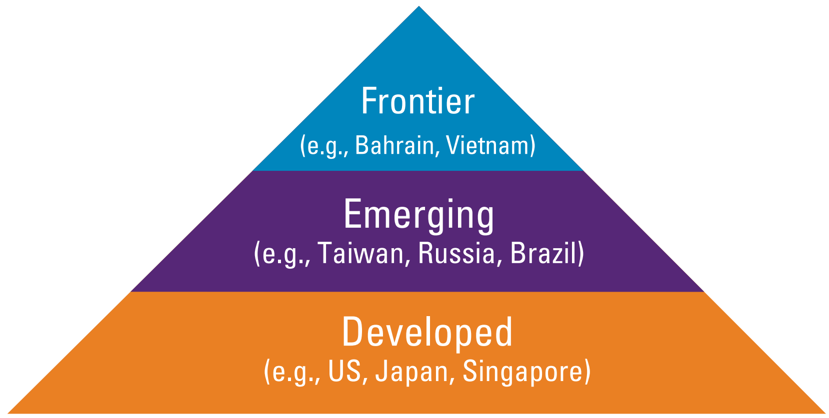
Number of publicly listed companies per exchange



As of 12/31/20. Source: Bloomberg, 3/21.

2. **New Markets:** Though the US and other developed markets are clearly defined, the definitions of developing markets (emerging and frontier) are more fluid. Generally speaking, the most broadly accessible markets fit within the developed and emerging categories, with frontier markets tending to present limitations in terms of liquidity and/or market access.

Typical Life Cycle of Equity-Market Classification



With a few notable exceptions, equity markets typically launch as frontier,[2] graduate to emerging, and then advance to developed as they mature and become more universally accessible. This process provides another avenue for adding companies to the non-US investable universe. We saw this in 2019 and 2020 when the largest international index provider, MSCI, moved Argentina, Kuwait, and Saudi Arabia to its emerging-markets indices.

Until the last decade, the China A-share market was only available to residents of mainland China.

3. **China A Share:**[3] This could certainly be considered a subset within the previous category, but it's such a big source of new equity names that it deserves its own category. There is a fair bit of confusion around what China A share actually is and how it differs from Chinese stocks.

   Chinese equities that were historically available outside of mainland China tended to be listed and traded in Hong Kong (or, in more limited cases, traded in the US as ADRs).[4] However, another equity market also existed that, until the last decade, was only available to residents of mainland China—the China A-share market.

   In 2014, China launched the Stock Connect program to allow certain stocks on the mainland exchanges to be traded by foreign investors through the Hong Kong Stock Exchange. Though it was a bit clunky initially, this program has become more widely accepted and utilized. In the process, index providers have begun adding China A-share stocks to their indices. In particular, MSCI currently includes the 481 China A-share stocks available through the Stock Connect program in the MSCI Emerging Markets Index.[5] China A-share stocks are also available in some actively managed mutual funds, including the Hartford Schroders China A Fund (HSHIX).

ONLY 11% OF MAINLAND CHINA-LISTED EQUITIES ARE AVAILABLE TO INTERNATIONAL INVESTORS

As of 6/30/21. Source: MSCI and World Federation of Exchanges.

There are more than 4,000 stocks currently traded on the mainland China exchanges in Shanghai and Shenzhen, so there is runway available to expand Stock Connect eligibility and dramatically increase the investable global equity universe.

Is This a Long- or Short-Term Phenomenon?

Pent-up demand and central-bank support from the pandemic, along with the pandemonium around SPACs[6] earlier this year (special acquisition companies, also known as “blank-check” companies) may have helped build some short-term momentum for new public equities in the US.

However, increased regulatory scrutiny and disappointing performance has already begun to deflate the enthusiasm around SPACs. That’s why I think the three variables listed above could continue to tip the scales in favor of non-US equities long term.

Conclusion

In short, it seems the US may continue to be the incredible shrinking market. But rather than viewing this as an alarming trend, I see this as a positive for investors because it’s being offset by a growing investable international universe. What’s more, through professionally managed mutual funds, investors can leverage the research, resources, and experience needed to potentially benefit from this growing international opportunity.

Hartford Funds 4- and 5-Star Overall-Rated Global and International Equity Funds*

	Morningstar Category	Overall Rating	# of Funds	3-Year Rating	# of Funds	5-Year Rating	# of Funds	10-Year Rating	# of Funds
Hartford Global Impact Fund (HGXIX)	World Small/Mid Stock	★★★★	135	★★★★	135				
Hartford Schroders International Multi-Cap Value Fund (SIDNX)	Foreign Large Value	★★★★	317	★★★	317	★★★	269	★★★★	180
Hartford International Opportunities Fund (IHOIX)	Foreign Large Blend	★★★★	691	★★★★	691	★★★★	591	★★★★	397
Hartford Schroders International Stock Fund (SCIEX)	Foreign Large Blend	★★★★★	691	★★★★★	691	★★★★★	591	★★★★★	397
Hartford International Value Fund (HILIX)	Foreign Large Value	★★★★	317	★★	317	★★★	269	★★★★★	180
Hartford Multifactor Diversified International ETF (RODE)	Foreign Large Value	★★★★	317	★★★★	317				

Past performance does not guarantee future results. Ratings based on Class I shares and ETFs. Ratings of other share classes may differ. As of 9/30/21. Source: Morningstar, 10/21. * For a full list of Hartford Funds, please visit hartfordfunds.com.

Talk to your financial professional to find the right balance of US and international equity exposure for your portfolio.

[1] Private equity consists of funds and investors that bypass public exchanges and directly invest in companies.

[2] Frontier markets are less-advanced capital markets in the developing world. They are considered more established than the least-developed countries but still less established than the emerging markets because they are viewed as too small, carrying too much risk, or are too illiquid to be considered an emerging market.

[3] China A shares are the stock shares of mainland China-based companies that trade on the two Chinese stock exchanges, the Shanghai Stock Exchange and the Shenzhen Stock Exchange. A shares are also known as domestic shares because they use the Chinese renminbi for valuation. They are different from B shares, which are quoted in foreign currencies, such as the US dollar, and are more widely available to foreign investors.

[4] American depository receipts (ADRs) are certificates issued by American depository banks representing a specified number of shares in a foreign company's stock. ADRs trade on US markets like a domestic share.

[5] MSCI Emerging Markets Index is a free float-adjusted market capitalization-weighted index that is designed to measure equity market performance in the global emerging markets.

[6] A special-purpose acquisition company (SPAC) is a company with no commercial operations that is formed strictly to raise capital through an initial public offering for the purpose of acquiring an existing company. SPACs are also known as "blank check" companies.

Important Risks: Investing involves risk, including the possible loss of principal. • Foreign investments may be more volatile and less liquid than US investments and are subject to the risk of currency fluctuations and adverse political, economic, and regulatory developments. These risks may be greater, and include additional risks, for investments in emerging markets or if a fund focuses in a particular geographic region or country.

Important risks for Hartford Schroders China A Fund: The Fund invests in China A shares through Stock Connect, which is subject to a number of restrictions that may affect the Fund's investments and returns. • Risks associated with investments in China include currency fluctuation, political, economic, social, environmental, regulatory and other risks, including risks associated with differing legal standards. Focusing investments in China subjects the Fund to more volatility and greater risk of loss than a fund with more geographically diverse investments. These risks may be greater, and include additional risks, for investments in emerging markets, such as China. • Small- and mid-cap securities can have greater risks and volatility than large-cap securities. • Derivatives are generally more volatile and sensitive to changes in market or economic conditions than other securities; their risks include currency, leverage, liquidity, index, pricing, regulatory and counterparty risk. • Because the Fund is non-diversified, it may invest in a smaller number of issuers, and may be more exposed to risks and volatility than a more broadly diversified fund. • To the extent the Fund focuses on one or more sectors, the Fund may be subject to increased volatility and risk of loss if adverse developments occur. • Integration of environmental, social, and/or governance (ESG) factors into the investment process may not work as intended.

Investors should carefully consider a fund's investment objectives, risks, charges, and expenses. This and other important information is contained in a fund's full prospectus and summary prospectus, which can be obtained by visiting hartfordfunds.com. Please read it carefully before investing.

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