Dynamic Allocation Strategy

NDR
NED DAVIS RESEARCH

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Macro/Market Update

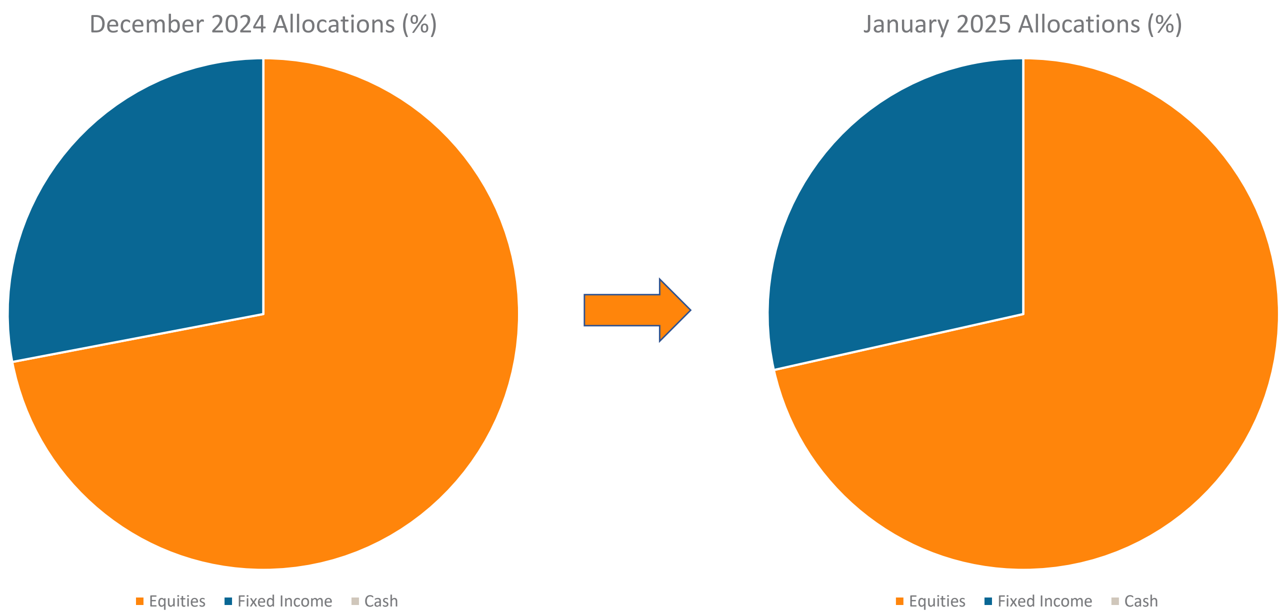
Global economic momentum saw continued growth in November, as the global composite (services and manufacturing) Purchasing Managers' Index (PMI) has risen for three of the last four months. The PMI resides well above levels associated with global recession, as the economy has reasserted itself to the upside.

Leading indicators within the report point to further improvement at the aggregate level. Both the new orders index and the future output index rose to their highest levels in six months. While services have continued to lead the expansion, which has the been the case for over two years, we see burgeoning signs of a turning point in global manufacturing based on leading indicators within the report.

The global economy appears positioned for an ongoing expansion, as easier global monetary policy, positive real wage growth, and increased fiscal support from some of the world's largest economies provide compelling evidence for this trend. However, there are potential downside risks emanating from the geopolitical sphere, most notably the risk of higher tariffs from the U.S. and an ensuing trade war.

During December, the MSCI All Country World Index (ACWI) underperformed the Bloomberg Barclays Global Aggregate Bond Index by over 18 basis points (bps). Stocks have outpaced bonds for eleven of the last fourteen months. Easing central banks, accommodative fiscal policy, receding inflation, and lacking recessionary evidence continue to support the equity cyclical bull market.

Asset Allocation Summary

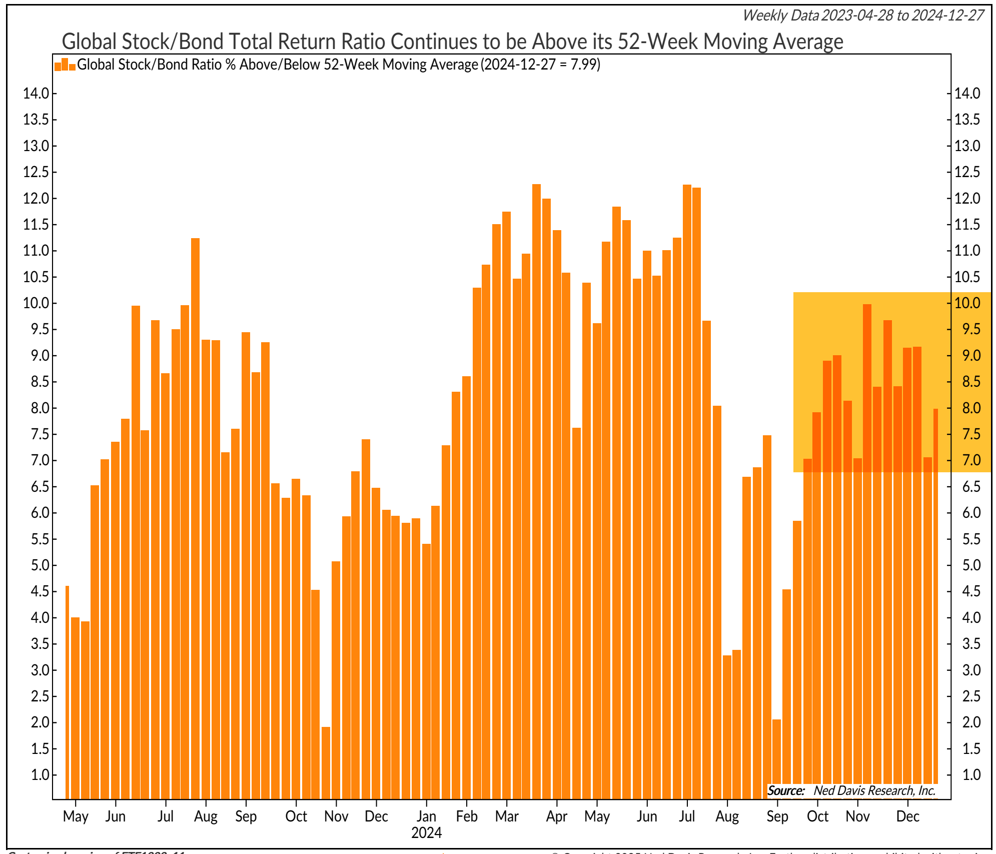


* See Equity Allocation Summary for how the equity allocation is distributed
** See Fixed Income Allocation Summary for how the fixed income allocation is distributed

The equity allocation continues to be above benchmark weighting, as the model did not trade this month. The model uses a turnover reduction mechanism, which reduces trading. The proposed allocations did not deviate enough from the existing weightings to warrant a model rebalance. Two-thirds of the indicators, which weigh the relative attractiveness of stocks and bonds, favor stocks.

The stock/bond relative strength indicator, which receives the greatest weighting in the model, compares the stock/bond ratio to its 52-week moving average. The stock/bond relative strength ratio remained stable during December, as it is approximately 8% above its 52-week moving average (chart right). This indicator has favored equities for over one year.

Following the trend is important as it can help to keep you on the right side of major market moves. The trend also can reduce behavioral biases. Ned Davis has said that following the trend is important because "the degree of unprofitable anxiety in an investor's life corresponds directly to the amount of time one spends dwelling on how an investment should be acting rather than the way it actually is acting."



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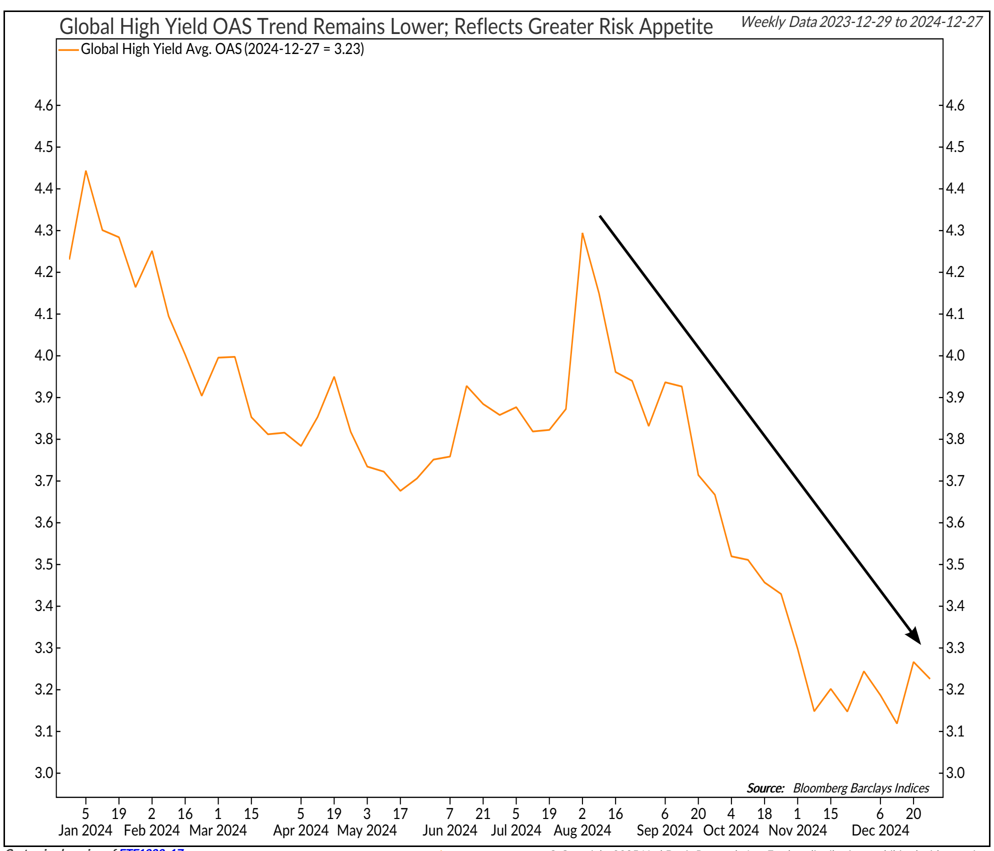

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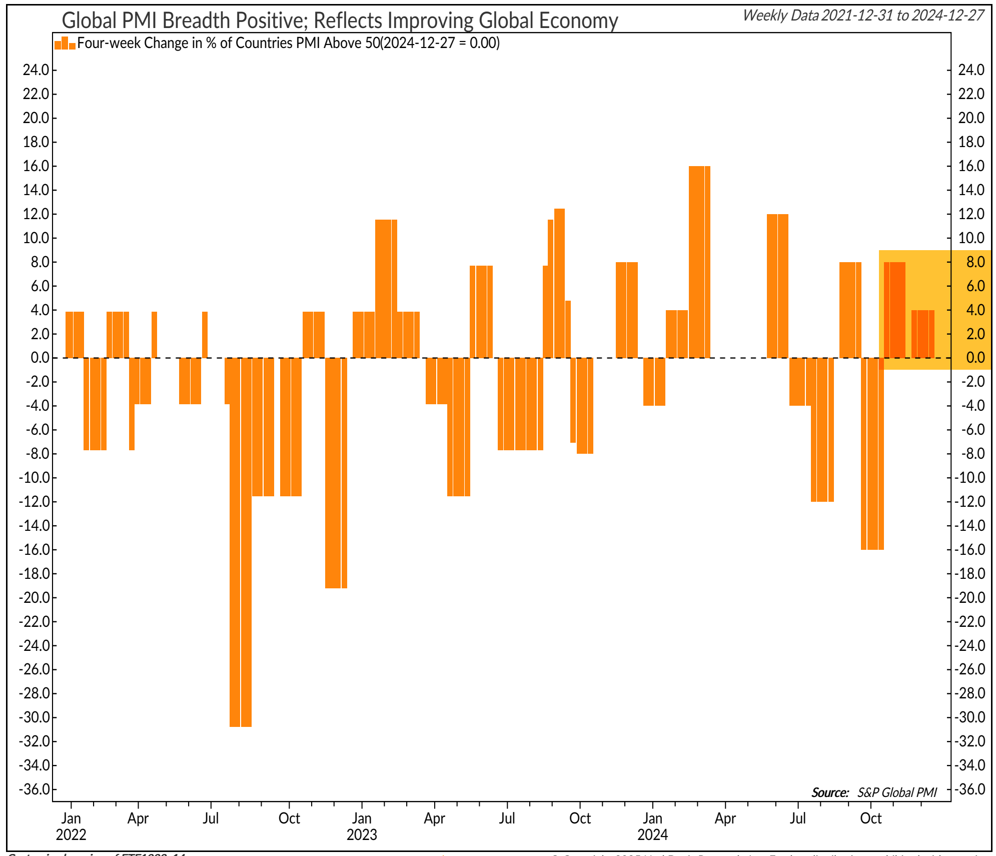
Global high yield option-adjusted spreads (OAS) have moved significantly lower since experiencing large volatility in August. During the beginning of August, OAS jumped almost 50 bps. Since then, OAS have reversed by over 100 bps (chart left), indicating improved risk appetite by fixed income investors.

The Purchasing Managers' Index (PMI) breadth indicator measures the four-week point change of the percentage of economies with a PMI greater than 50 (expanding activity). The PMI is based on a survey sent to executives regarding their outlook on areas such as inventories, production, and employment.

A change greater than zero favors stocks, while a change less than zero supports bonds. Equities typically outperform fixed income when there is strength in the economic outlook. This economic momentum breadth indicator remained positive, as the PMIs for Hungary and South Korea rose above 50 (chart right).



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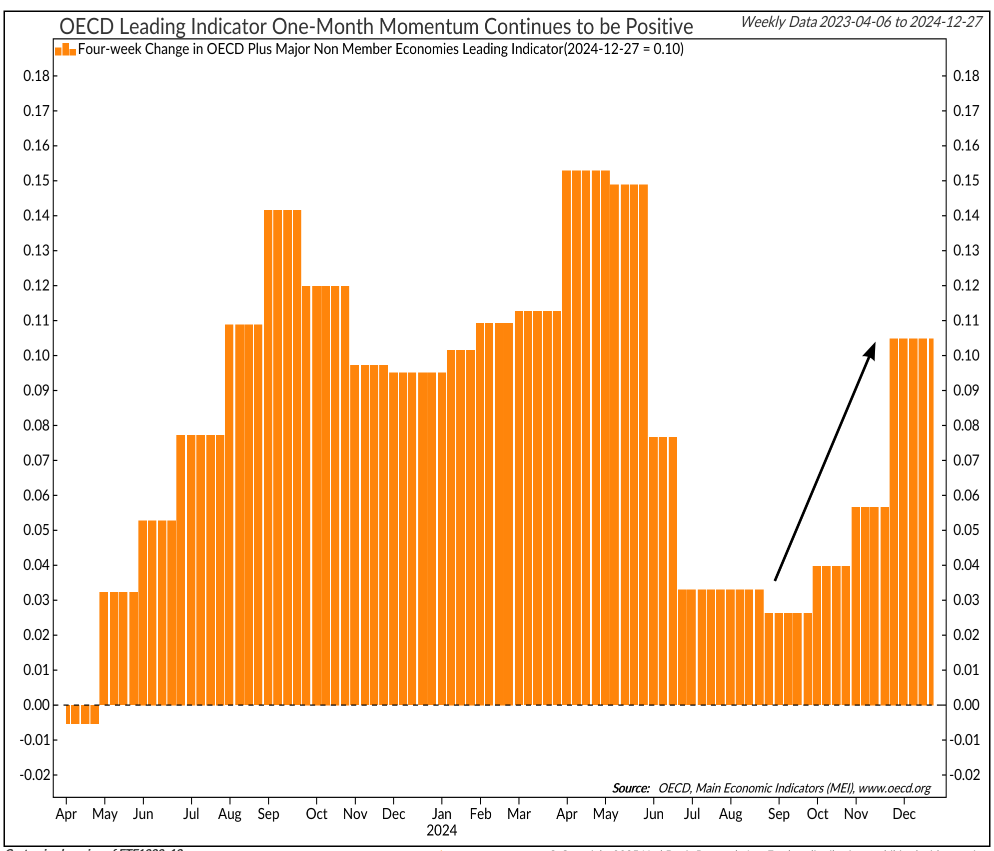

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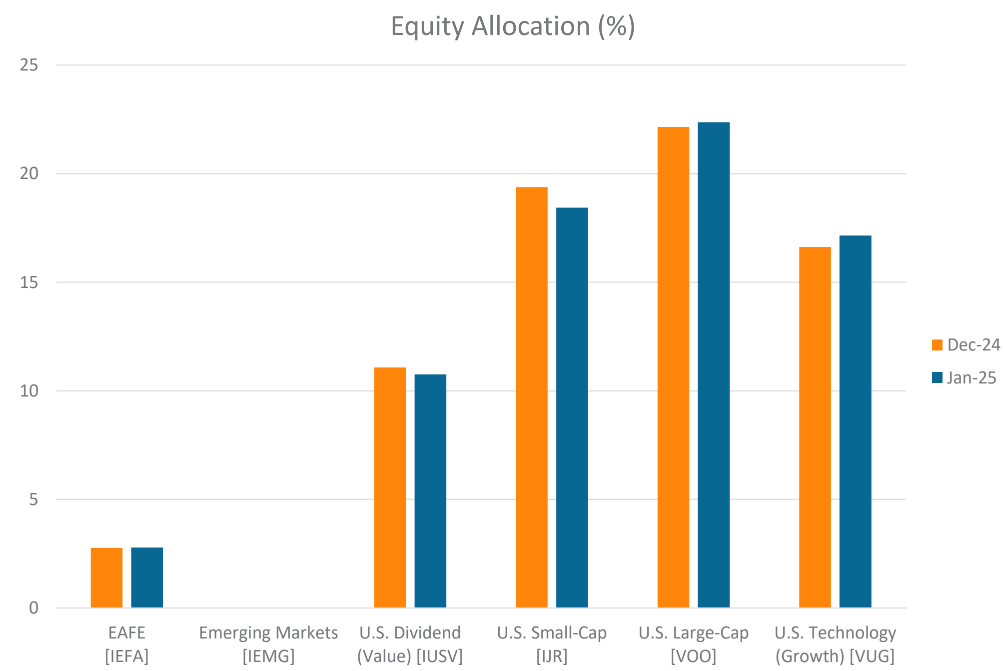
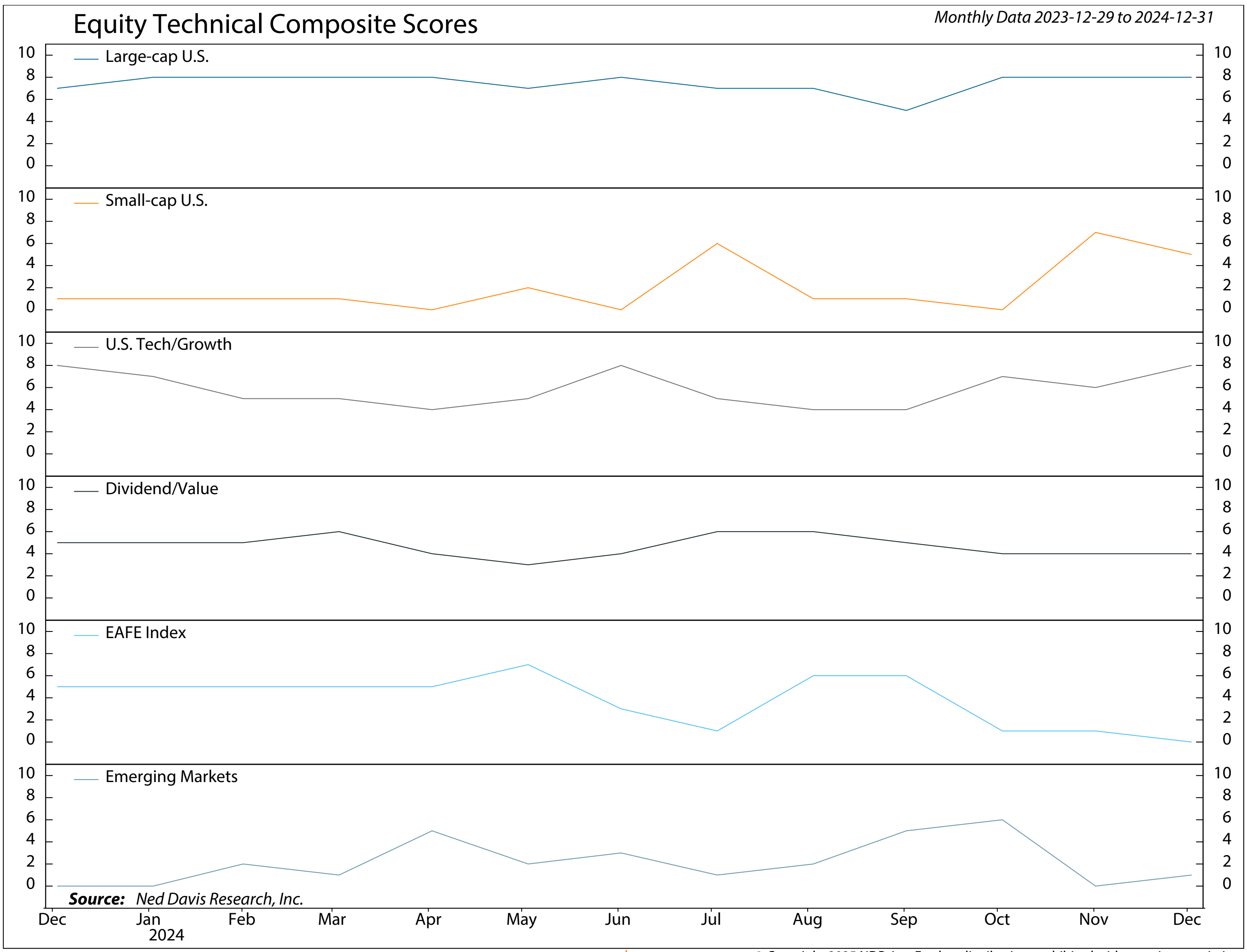
After declining for 18 consecutive months, the four-week change in the Organization for Economic Cooperation and Development (OECD) Composite Leading Indicator (CLI) has increased for the past 19 months (chart left).

The OECD creates monthly CLIs for 35 economies to capture turning points in the growth cycle. Each CLI contains a wide range of indicators such as money supply, yield curve, building permits, consumer and business sentiment, share prices, and manufacturing production. Improvement in global economic momentum supports the trend.

Equity Allocation Summary

During December, only U.S. Growth produced a positive return, as it rose more than 44 bps. Non-U.S. markets dropped for a third consecutive month, which last occurred from August -October 2023. U.S. Small Caps and U.S. Value both suffered their worst monthly returns since September 2022. U.S. Large Caps, U.S. Growth, and U.S. Small Caps each received more than 15% allocation for January (image bottom).





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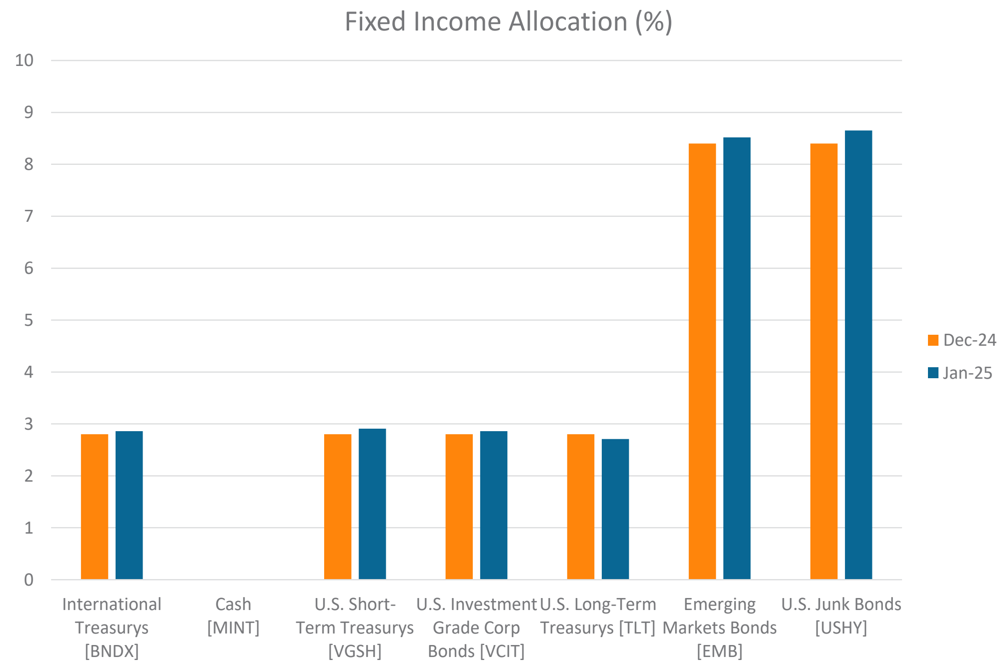
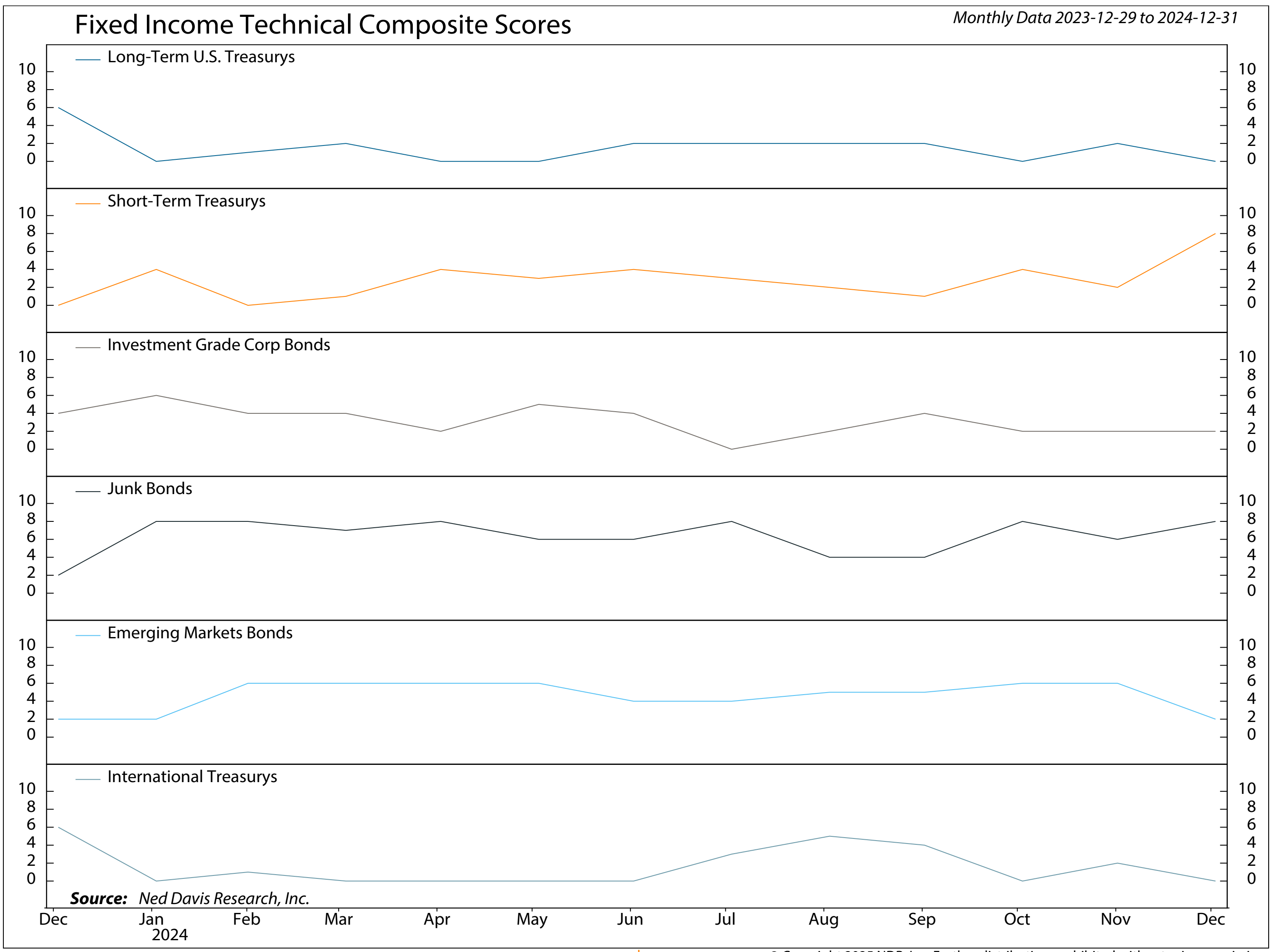
Fixed Income Allocation Summary

Only U.S. Short-Term Treasurys generated a positive return during December. U.S. Long-Term Treasurys plummeted over 600 bps, its worst month since April. Emerging Market bonds fell more than 220 bps. EM bonds have fallen more than 220 bps for two of the last three months. U.S. Investment Grade Corporate bonds have fallen by more than 150 bps for two of the last three months. U.S. High Yield and EM bonds received more than 8% allocation for January (image bottom).





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Using any graph, chart, formula, model, or other device to assist in deciding which securities to trade or when to trade them presents many difficulties and their effectiveness has significant limitations, including that prior patterns may not repeat themselves continuously or on any particular occasion. In addition, market participants using such devices can impact the market in a way that changes the effectiveness of such devices. NDR believes no individual graph, chart, formula, model, or other device should be used as the sole basis for any investment decision and suggests that all market participants consider differing viewpoints and use a weight of the evidence approach that fits their investment needs.

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