Dynamic Allocation Strategy

OCTOBER 2021

Macro/Market Update

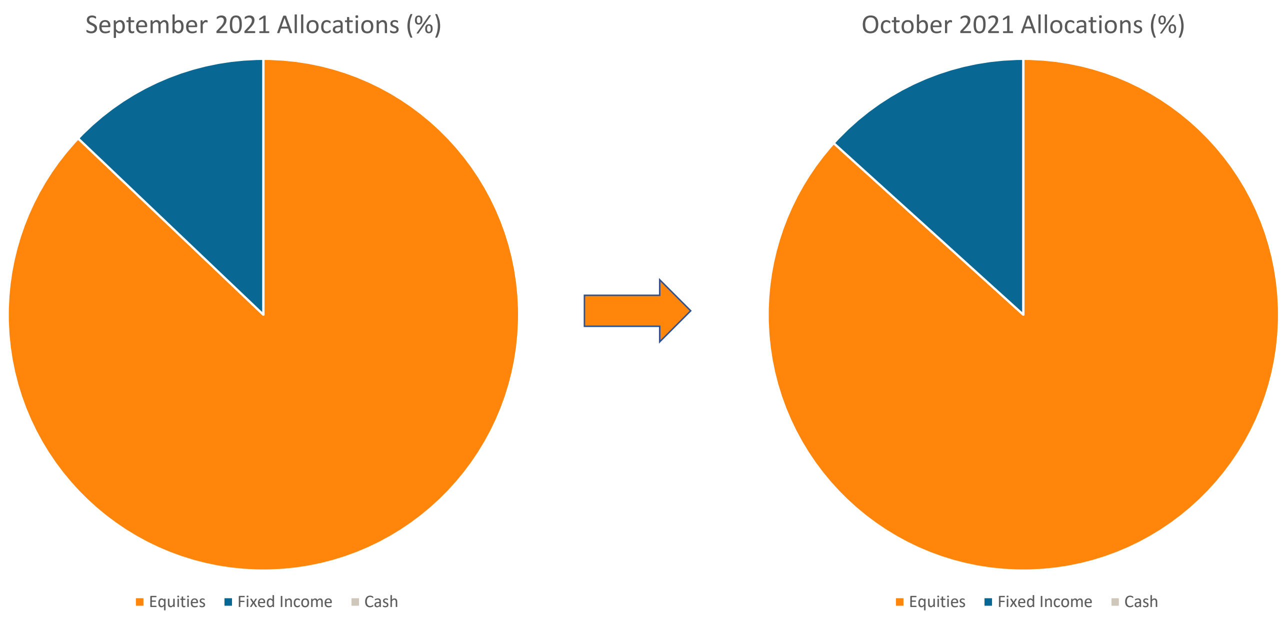
Global economic growth slowed notably in August, according to the latest Purchasing Managers' Index (PMI) data. The global composite PMI slumped 3.1 points to 52.6. It was the sharpest decline in the index since April 2020, during the worst of the COVID lockdowns, to the lowest level since the beginning of this year.

Global economic growth likely peaked in the second quarter of this year. The rising risk of COVID, intensified by the Delta variant, coupled with COVID-induced supply-chain disruptions and resource shortages that are impeding output and increasing costs, have put a damper on the global recovery.

However, the PMI remains firmly in positive territory, indicating that recession is not a near-term risk. The current reading in the composite is historically consistent with 2.6% annual global Gross Domestic Product (GDP) growth.

During September, the MSCI All Country World Index (ACWI) underperformed the Barclays Global Aggregate Bond Index by more than 230 basis points (bps). Stocks dropped by more than 400 bps, their worst month since October 2020. This broke a seven-month winning streak for stocks. Although global bond yields have risen, the stock/bond relative strength uptrend remains intact. The indicators and seasonal tendencies support a year-end rally scenario.

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 model did not trade this month as the turnover reduction algorithm rebalance threshold was not breached.
- The equity allocation remained above 80%.
- The fixed income allocation continued to be less than 20%, while cash had no weighting.
- The Purchasing Managers' Index (PMI) indicator whipsawed back to favoring fixed income this month as China's contribution dropped below 50.
- NDR's Chief Economist, Alejandra Grindal, noted that "China's economy slumped in August due to widespread restrictions triggered by China's zero-COVID tolerance policy...But the outlook is likely to improve somewhat in the coming months as COVID cases have nearly ground to a halt, which may prompt the government to ease restrictions."
- Five of the six top-level indicators favored equities over fixed income (table, below).

Top Level Factors

Indicator	Current Signal (Red = New Signal)	Comment
Equities/Fixed Income Relative Strength (indicator receives a heavier weighting)	Favors Equities	The relative strength ratio remained at more than 10% above its one-year moving average. The spread reached an all-time high earlier this year.
Global Market Breadth	Favors Equities	54% of global equity markets were trading above their 50-day moving average. This was a significant decline from the 78% reading last month. Further deterioration in this indicator would likely cause it to change signal.
OECD Leading Indicator	Favors Equities	The four-week change in the OECD Composite Leading Indicator (CLI) was still positive, but at its lowest level since hitting an all-time high one year ago.
PMI Breadth Factor	Favors Fixed Income	This indicator whipsawed back to favoring fixed income. The four-week change in economies with expanding manufacturing industries returned to a negative reading due to weakness from China.
Baltic Exchange Dry Index	Favors Equities	The Baltic Dry Index was more than 25% above its 13-week moving average, which firmly favored equities relative to fixed income.
Central Bank Policy	Favors Equities	To favor fixed income, this indicator required a significant drop in global short-term rates.

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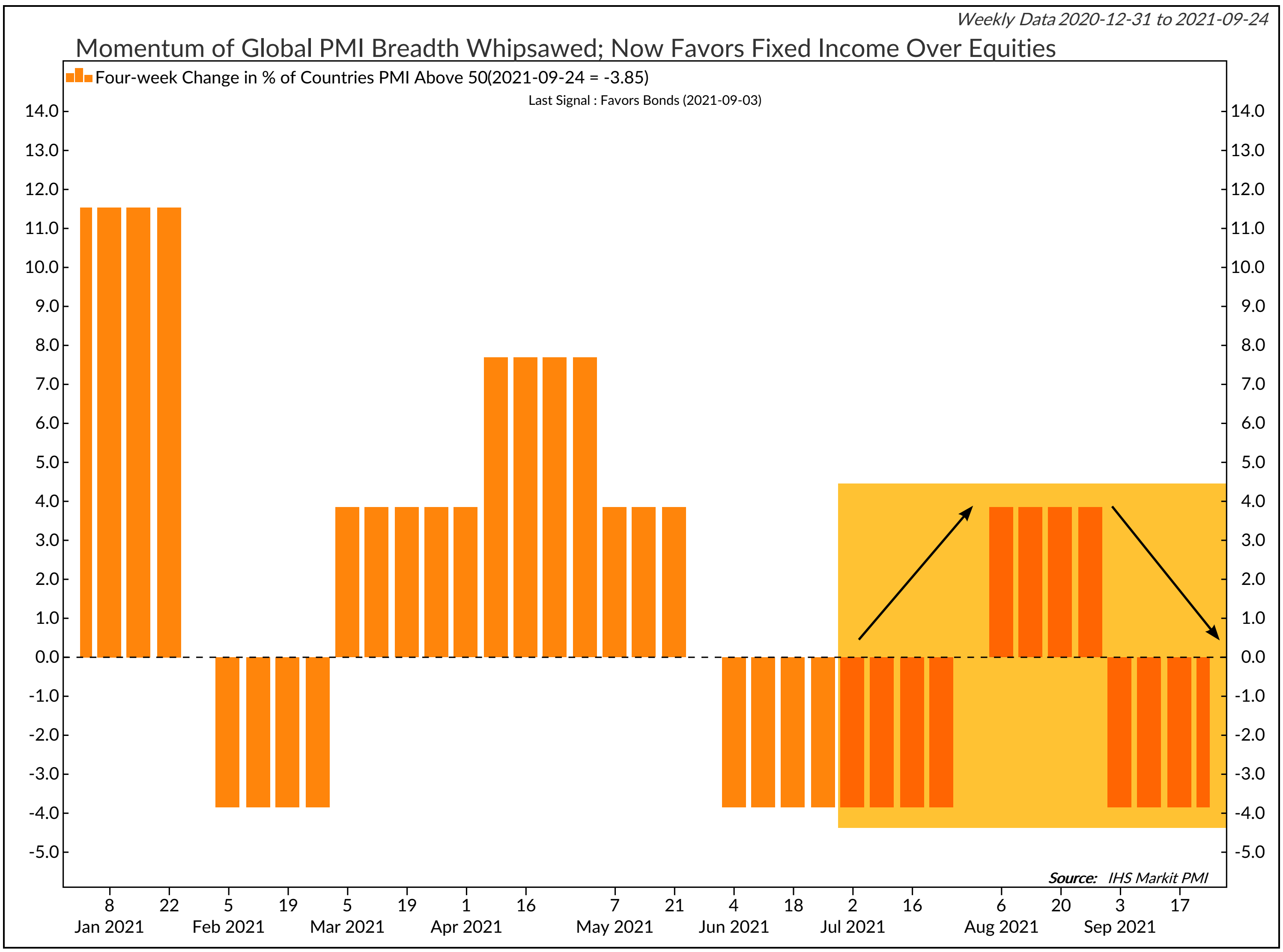

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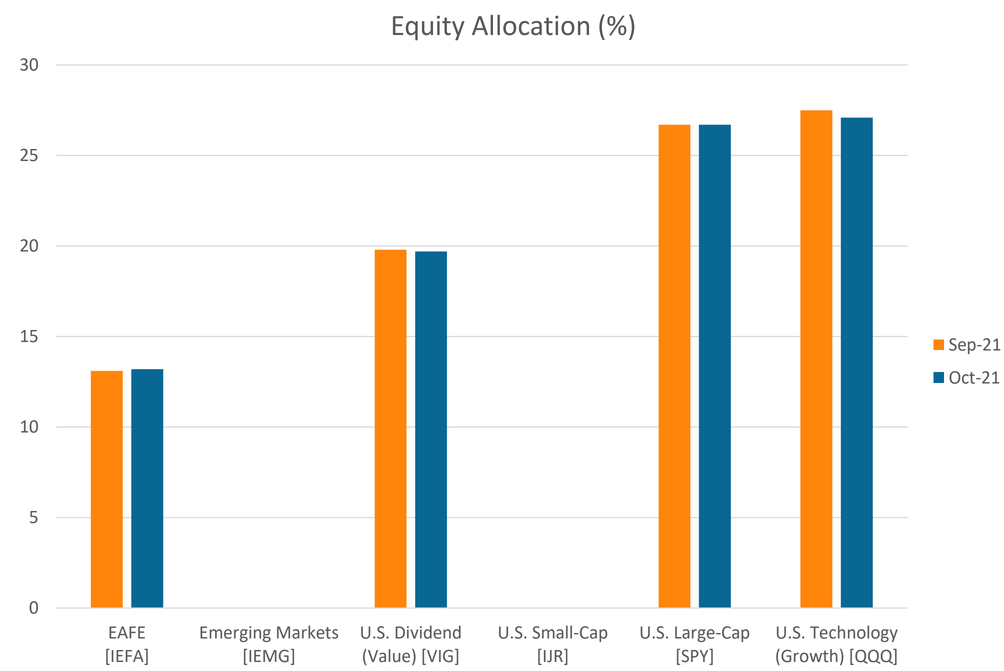
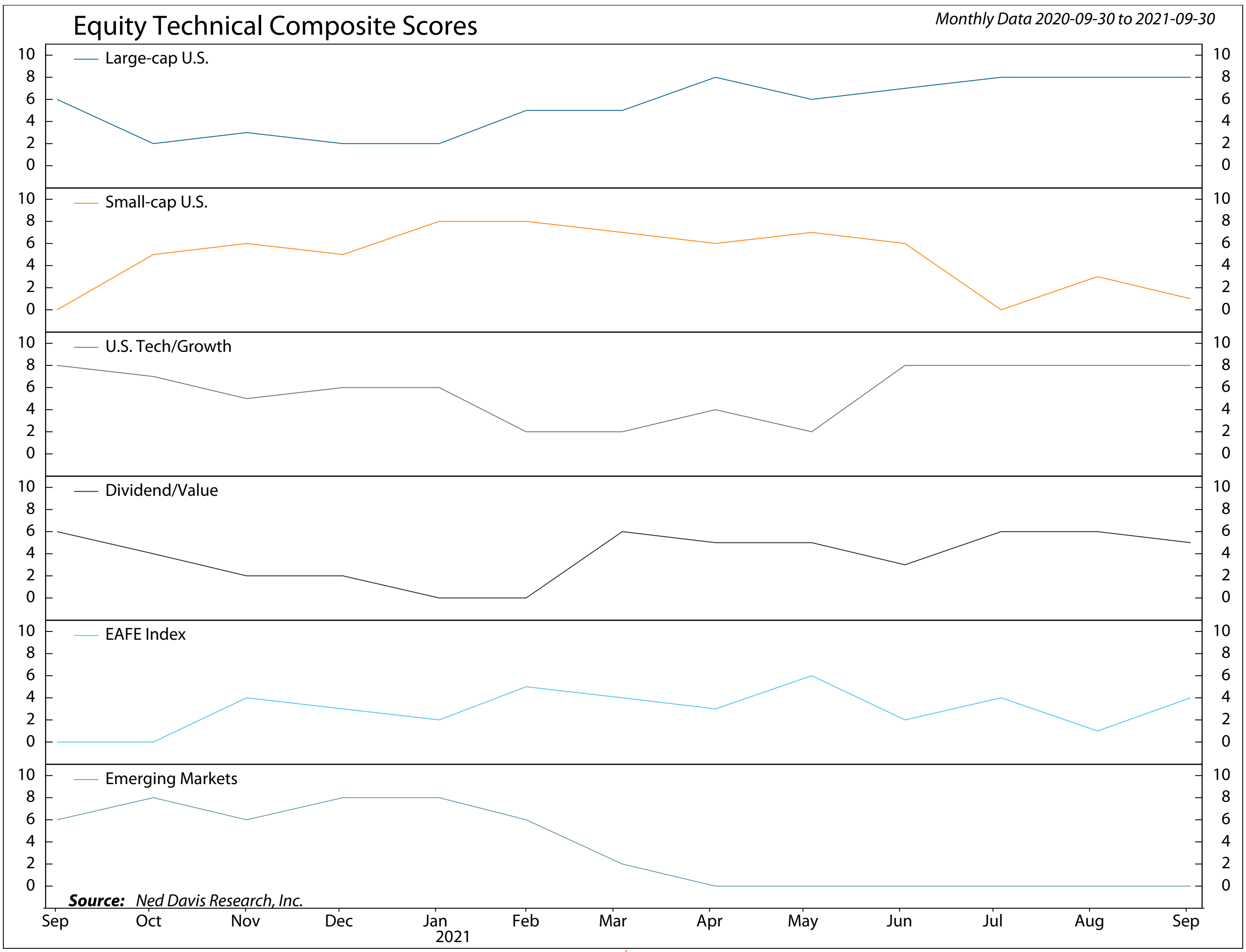
Equity Allocation Summary

During September, all six equity areas declined. Only U.S. Small Caps (IJR) fell by less than 300 bps. Europe, Australasia, and the Far East [EAFE] (IEFA) and Emerging Markets (IEMG) both dropped by less than 400 bps. U.S. Large Caps (SPY) and U.S. Value [Dividends] (VIG) each declined by less than 500 bps. This broke a seven-month winning streak for SPY. Only QQQ plummeted more than 500 bps. It was the worst month for VIG, SPY, and QQQ since March 2020. However, QQQ, SPY, and VIG continued to receive more than 15% allocation for October due to their elevated technical composite scores (image at bottom).





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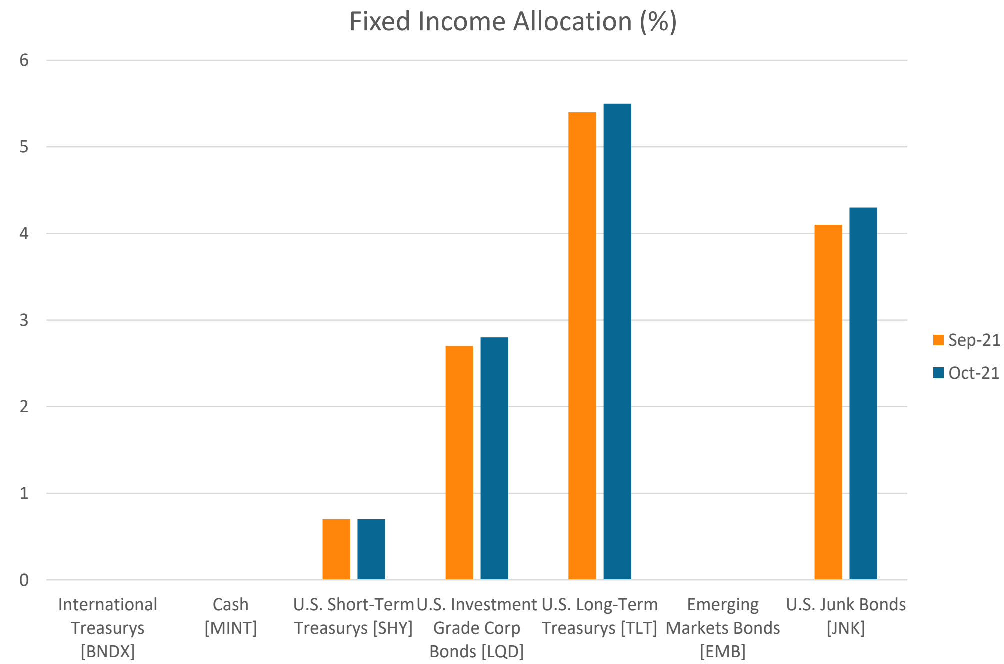
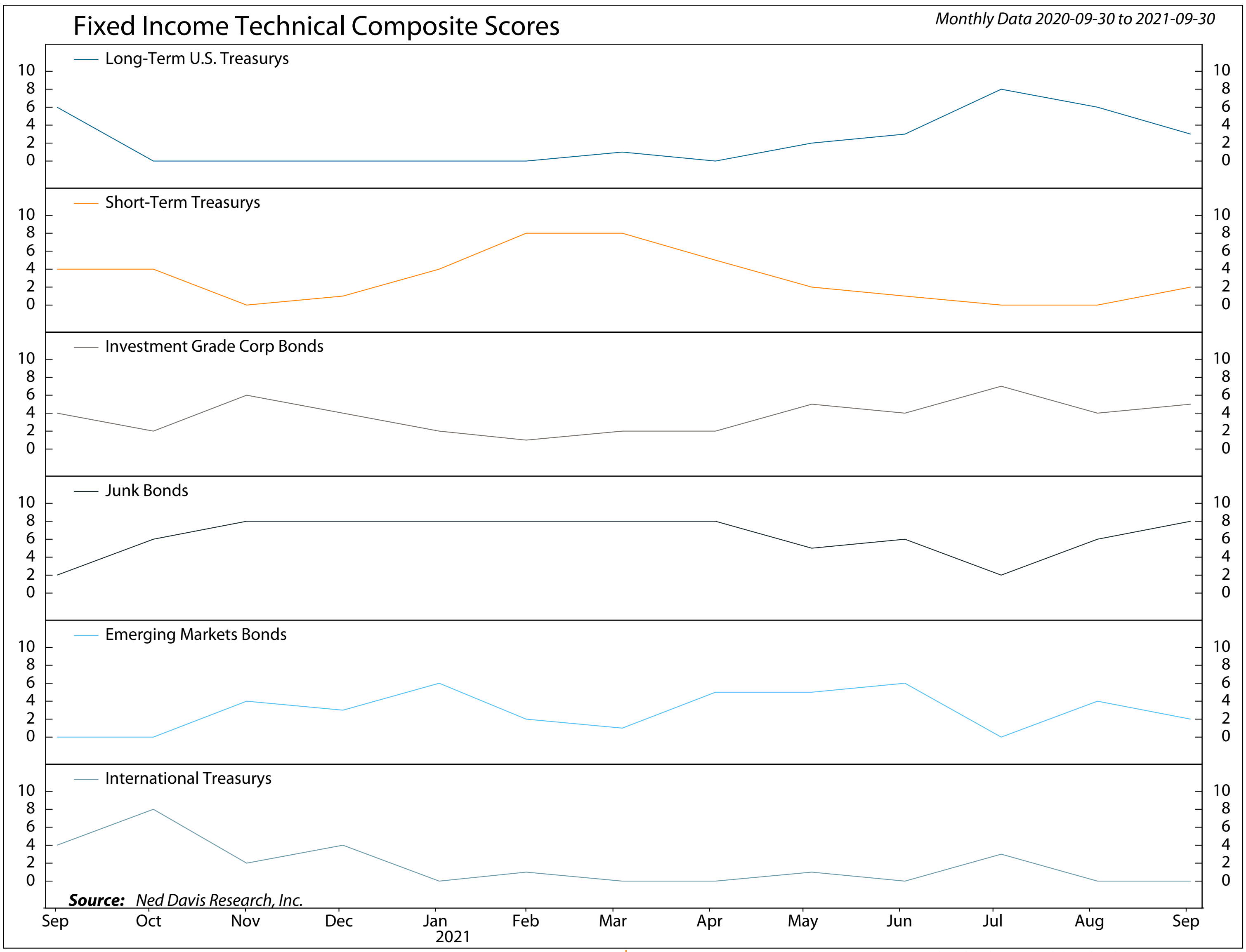
Fixed Income Allocation Summary

During September, all fixed income categories suffered losses. U.S. Short-Term Treasurys (SHY) and U.S. High Yield (JNK) both fell by less than 100 bps. It broke a seven-month winning streak for JNK. U.S. Investment Grade (LQD) and International Investment Grade Bonds (BNDX) each dropped by less than 200 bps. Emerging Market bonds (EMB) and U.S. Long-Term Treasurys (TLT) both declined by more than 200 bps. Prior to September, EMB had risen for the previous five months. TLT and JNK both received more than 3% allocation for October (image at bottom).





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