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NED DAVIS RESEARCH

Dynamic Allocation Strategy

FEBRUARY 2022

Macro/Market Update

The global economic expansion softened somewhat at the end of 2021, according to the latest Purchasing Managers' Index (PMI) data, as the COVID pandemic continues to present challenges to the outlook. The global composite (services and manufacturing) PMI fell 0.5 points in December to 54.3. It was the first decline in four months and the lowest level since September. However, the latest reading remains above its long-term average of 53.4 and historically consistent with 3.9% global real GDP growth.

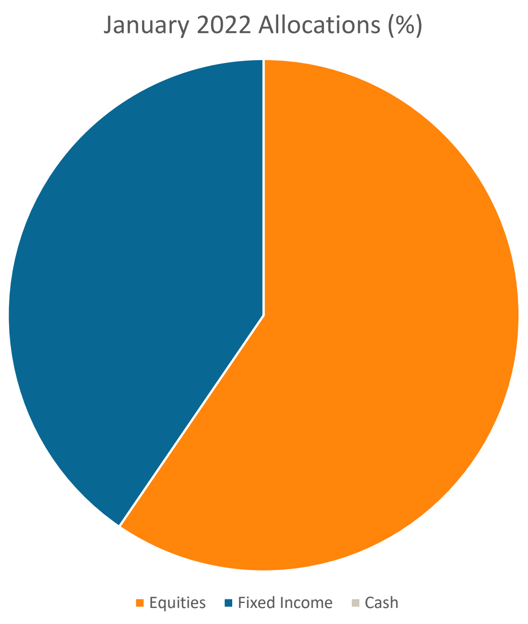
The global manufacturing PMI was essentially unchanged at 54.2 for a third straight month. Although down from its May peak of 56.0, it's still significantly above its historical average of 51.5. Output growth accelerated to a five-month high, but the expansion in export orders edged down moderately.

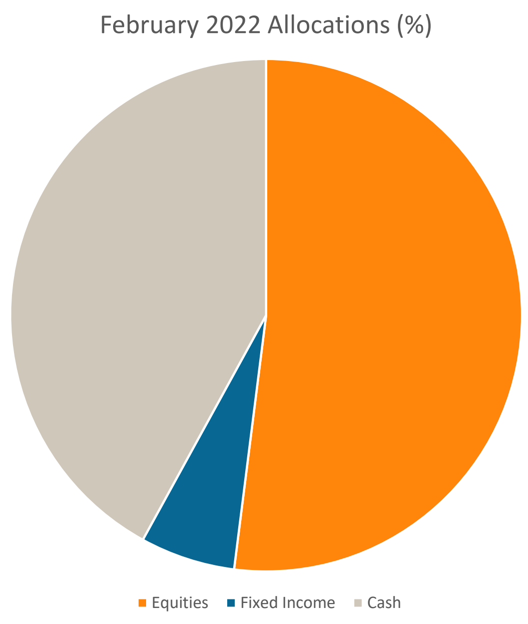
The COVID pandemic continues to present the greatest risk to the global outlook as it impacts spending patterns, supply chains, and inflation. Supply chain issues remained elevated, as delivery times are still near historical highs. The supplier delivery times index increased 1.4 points, up in five of the past six months, to 37.8. Global input and output prices remained historically elevated, but they are showing initial signs of easing.

The global composite input price index fell for the first time in four months and by the most since June. Meanwhile, output price growth slowed for a second straight month.

During January, the MSCI All Country World Index (ACWI) underperformed the Barclays Global Aggregate Bond Index by more than 250 basis points (bps). The spread between stocks and bonds has whipsawed between negative and positive values each month since July. It was the worst month for global stocks since March 2020. Risks are rising as the prospects for reversals in economic growth, earnings growth, and central bank policies, are likely to lead to greater volatility in global equities.

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 is slightly under 60%.
- The fixed income allocation plummeted to under 10%.
- Cash allocation surged from zero to over 40%. It was the largest allocation to cash in the model's history.
- The Purchasing Managers' Index (PMI) breadth indicator returned to favoring equities as the China PMI rose into the expansion zone. Over the last six months, the China PMI has oscillated around the key threshold and spent equal time within the expansion and contraction zones.
- Equity market breadth produced a new signal supporting fixed income. At the end of last week, less than 40% of global equity markets traded above their intermediate trends.
- The top-level indicators are evenly split between equities and 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 is less than 3% above its one-year moving average, its lowest spread in more than one year.
Global Market Breadth	Favors Fixed Income	This indicator now favors fixed income. Less than 40% of global equity markets are trading above their 50-day moving average. Last month, 58% of markets were in uptrends.
OECD Leading Indicator	Favors Fixed Income	The four-week change in the OECD Composite Leading Indicator (CLI) declined for a third straight month to its lowest levels since the spring of 2020.
PMI Breadth Factor	Favors Equities	This indicator now favors equities. The four-week change in economies with expanding manufacturing industries improved into expansion territory, as China crossed above the key threshold of 50 last month.
Baltic Exchange Dry Index	Favors Fixed Income	The Baltic Dry Index fell to more than 40% below its 13-week moving average, its lowest level since the spring of 2020 (chart at bottom).
Central Bank Policy	Favors Equities	To favor fixed income, this indicator required a significant drop in global short-term rates.

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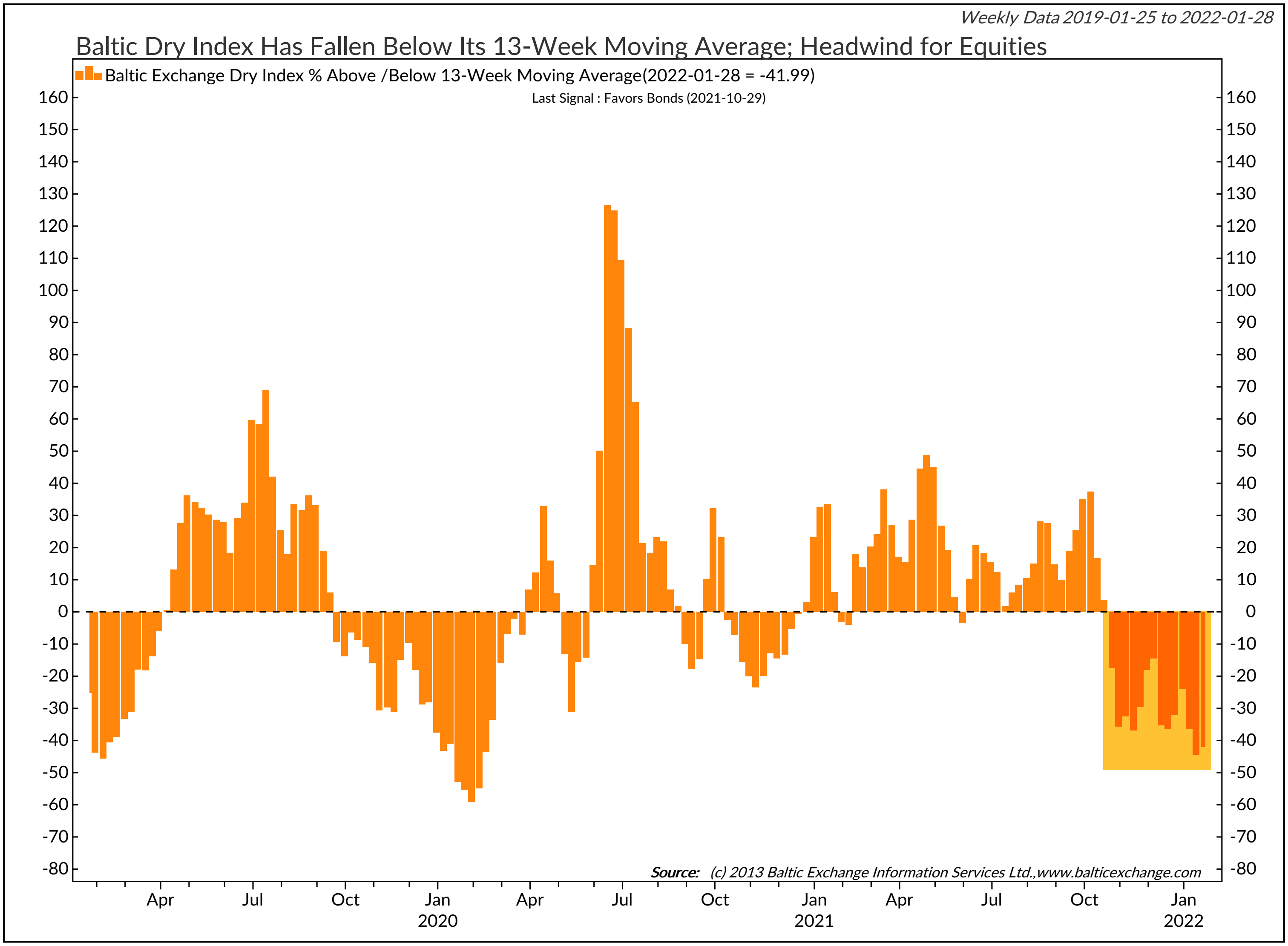
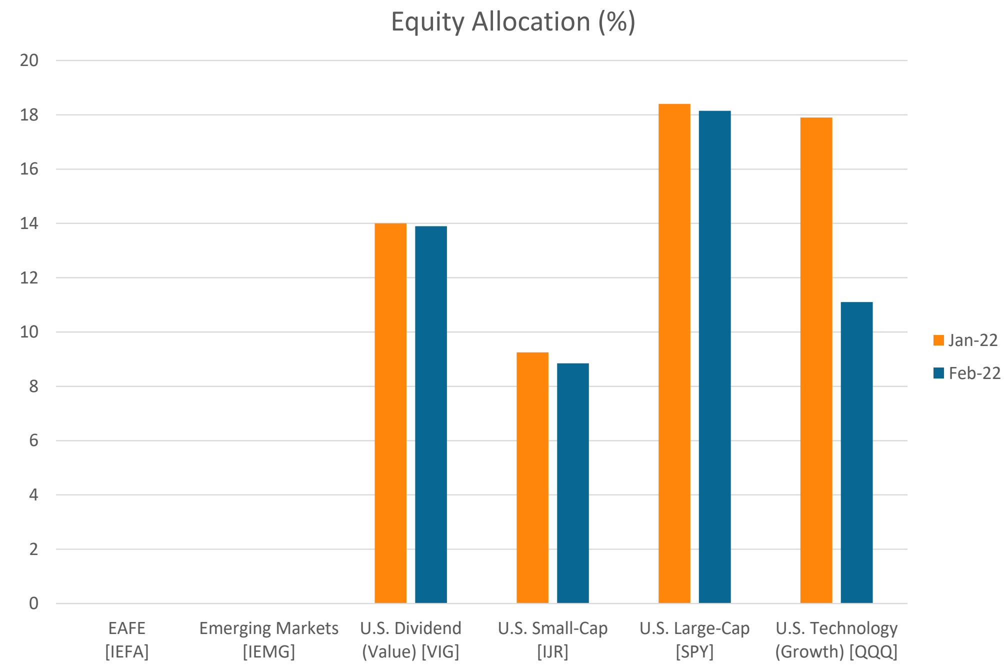
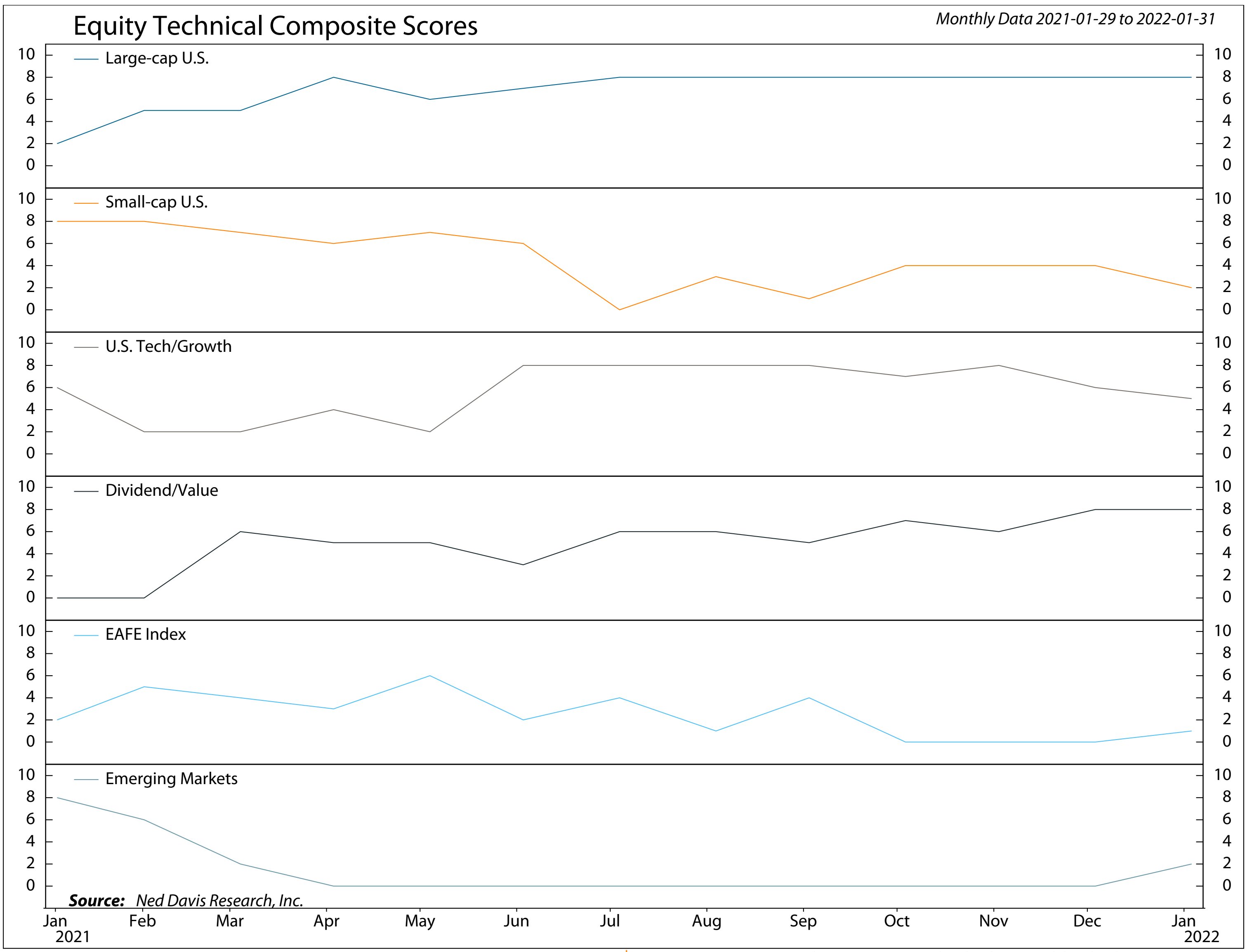


Customized version of ETF1000_15

Equity Allocation Summary

During January, all equity areas declined. Emerging Markets (IEMG) fell by less than 100 basis points (bps). U.S. Large Caps (SPY), U.S. Value [Dividends] (VIG), and Europe, Australasia, and the Far East [EAFE] (IEFA) each dropped by more than 400 bps. U.S. Small Caps (IJR) and U.S. Growth [Technology] (QQQ) both plummeted by over 700 bps. VIG, QQQ, and SPY each received more than 10% allocation for February due to their elevated technical composite scores (image at bottom).





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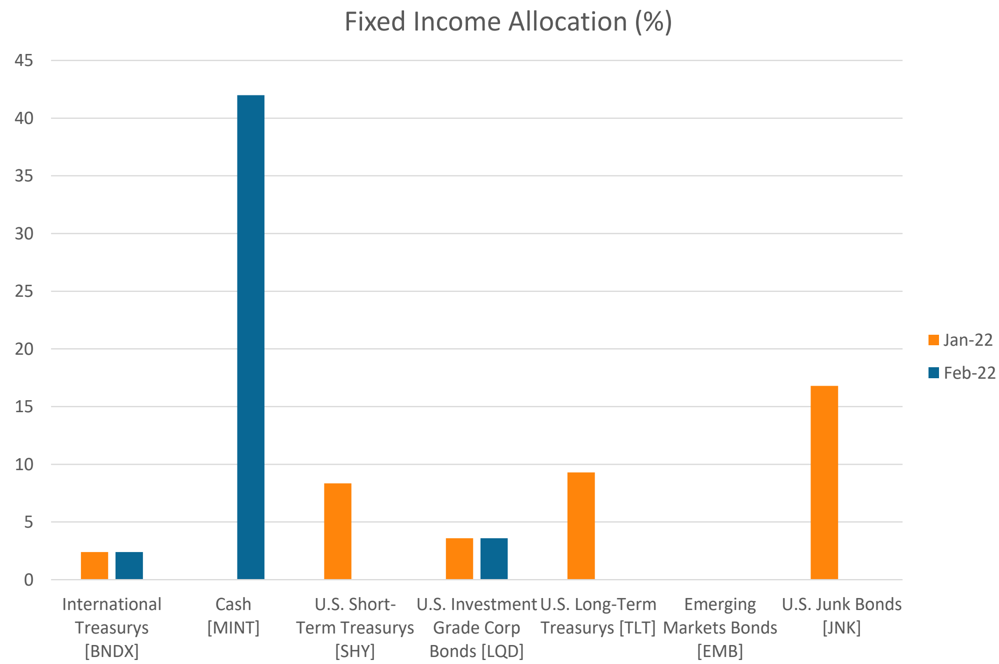
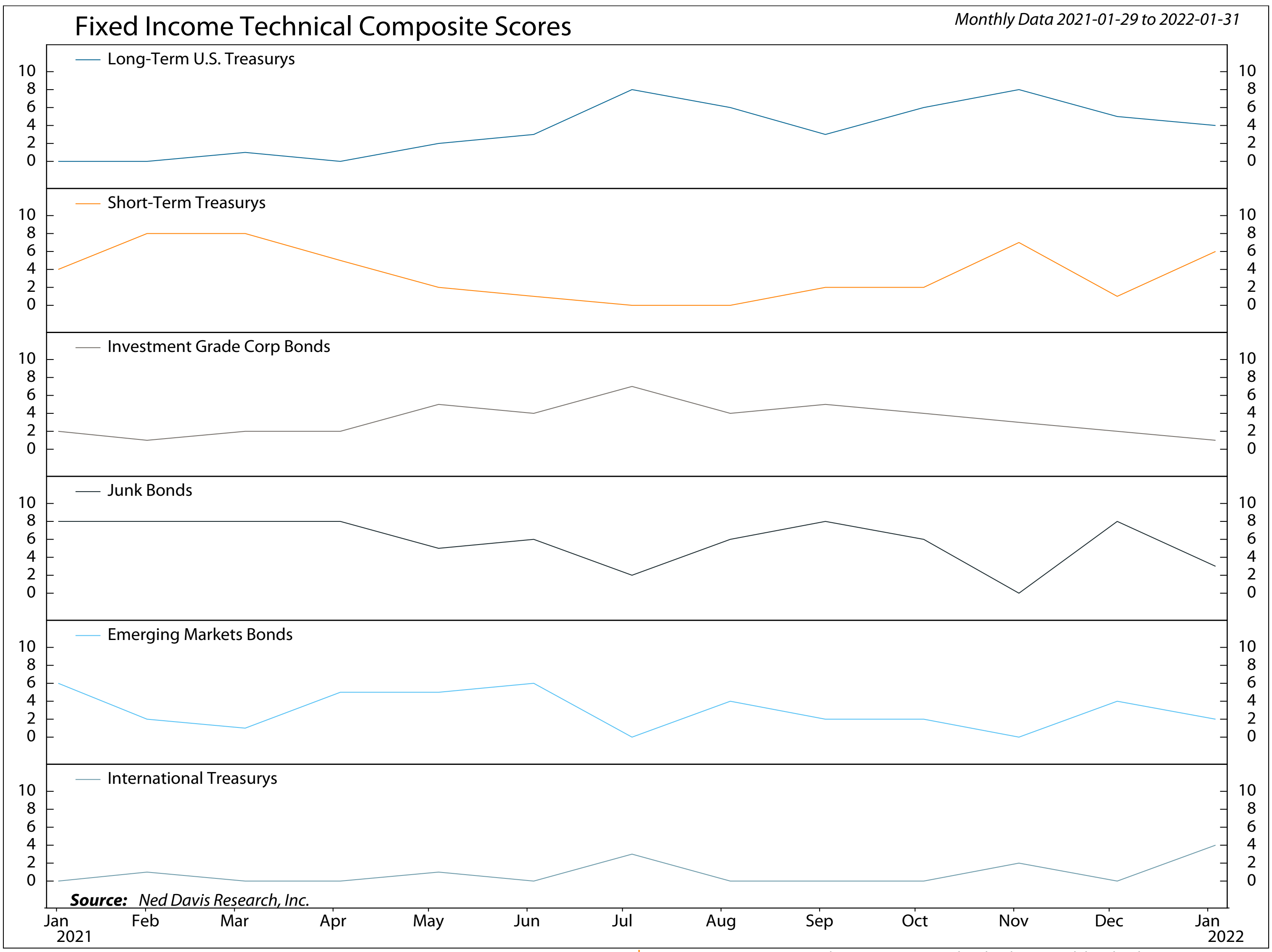
Fixed Income Allocation Summary

All fixed income areas fell during January. International Investment Grade Bonds (BNDX) and U.S. Short-Term Treasurys (SHY) declined by less than 200 bps. U.S. High Yield (JNK), Emerging Market bonds (EMB), U.S. Long-Term Treasurys (TLT), and U.S Investment Grade (LQD) all dropped by more than 250 bps. The bond intra-asset class model determines the opportunity for each area relative to cash and then relatively allocates across the segments with favorable attributes (image at bottom). At this time, no fixed income area exceeded the threshold to receive an allocation. The model recommends raising cash until a better opportunity presents itself.





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