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NED DAVIS RESEARCH

Dynamic Allocation Strategy

APRIL 2023

Macro/Market Update

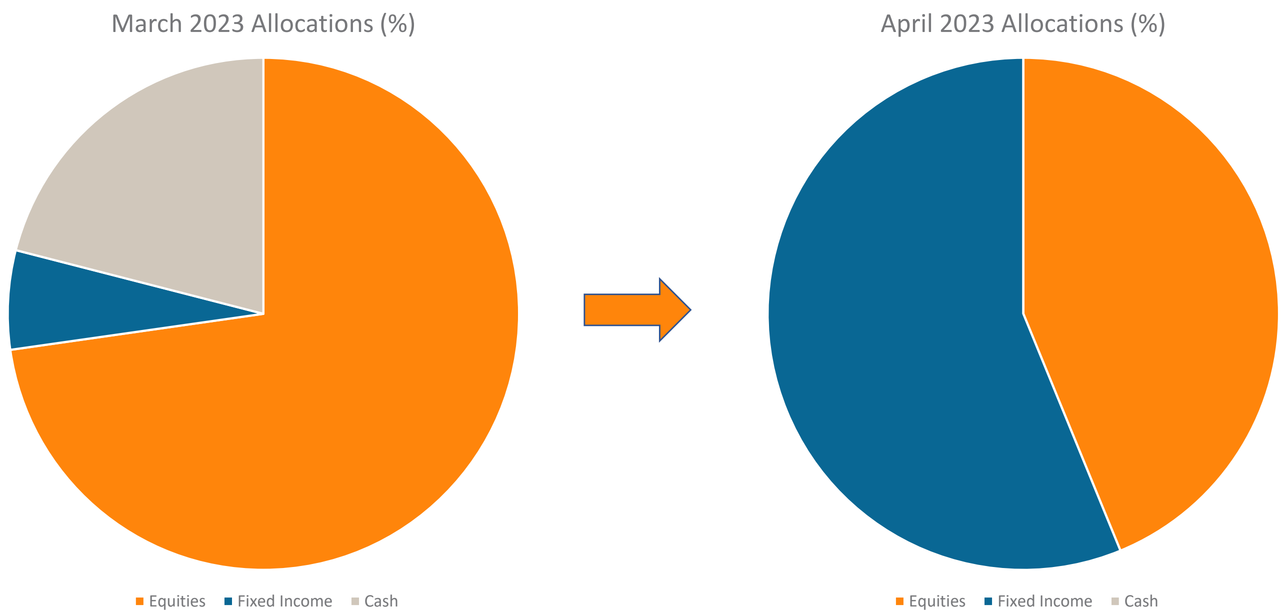
The global economy continued to show signs of improvement, according to the February S&P Global Purchasing Managers' Index (PMI) readings. The global composite PMI jumped 2.3 points, its third straight increase and the most since July 2020, to 52.1, the highest level and first expansion since mid-2022.

Global new orders expanded for the first time in seven months, while the future output index climbed to its highest level in nearly a year. China contributed greatly to the global figure as the end of its zero-COVID policy has seen growth surge. However, even outside of China, the expansion broadened across the globe, as the global composite PMI excluding China also rose to an eight-month high.

Despite these favorable signs, downside risks remain elevated. History suggests that tight monetary policy will continue to limit potential upside in the global economy for the foreseeable future. Moreover, stubbornly high inflation may keep central banks tighter for longer, effectively increasing the risk of recession.

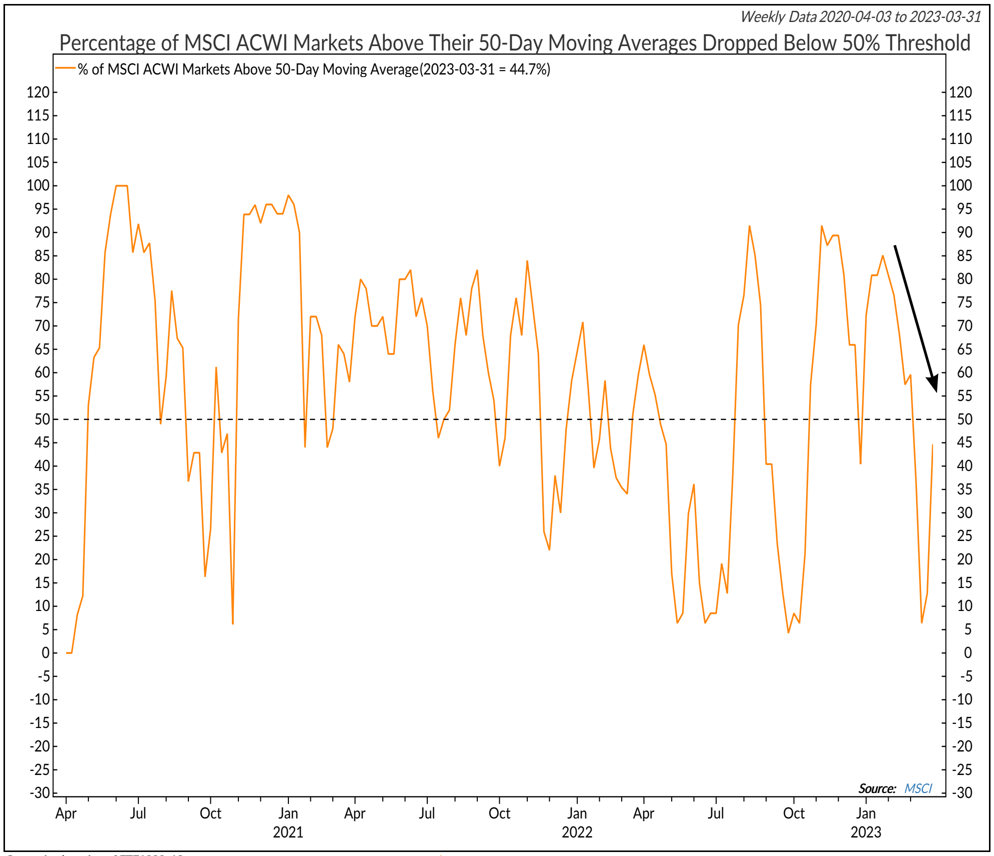
During March, the return for the MSCI All Country World Index (ACWI) was in line with the Bloomberg Barclays Global Aggregate Bond Index. Global stocks have outpaced bonds for six of the last nine months. However, global equity market upside participation has weakened, making the equity market vulnerable to a mega-cap stock downturn, as it was at the start of 2022.

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 dropped below benchmark allocation for April, as two-thirds of the top-level indicators favor fixed income over equities. The global equity breadth indicator calculates the percentage of global equity markets trading above their 50-day moving average. This indicator recently has experienced significant volatility. Last month, more than 57% of global equity markets traded above their 50-day moving averages. By mid-March, the reading dropped to less than 10%. As of the beginning of April, almost 45% of markets traded above their intermediate-term trend (chart at right).



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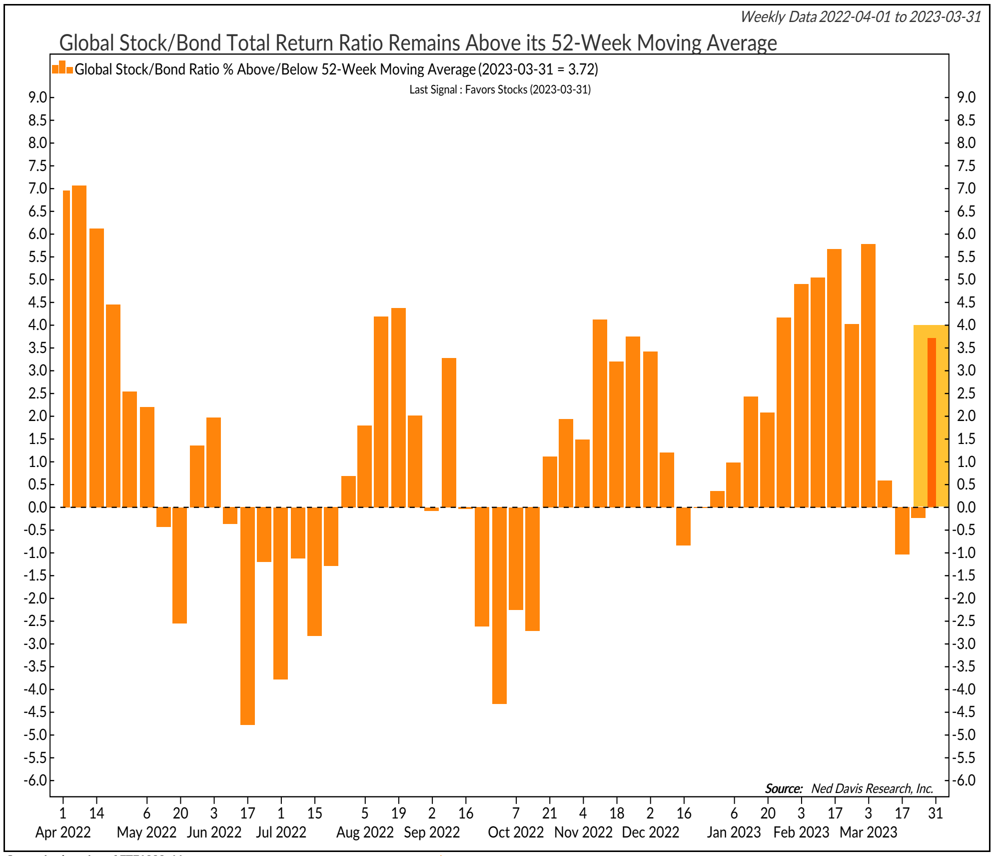
Customized version of ETF1000_17

Global high yield option-adjusted spreads (OAS) now favor fixed income (chart at left). Global high yield option-adjusted spreads widened by 125 basis points (bps) from early February until mid-March during the banking sector weakness. With global high yield OAS widening, bond investors demanded higher yields for taking on more risk. However, last week the indicator narrowed almost 50 bps.

Not all indicators are bearish on 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 indicator was going to favor fixed income, but the rally during the last week of March prevented the signal change. The stock/bond ratio is more than 3.5% above its one-year moving average (chart at right).



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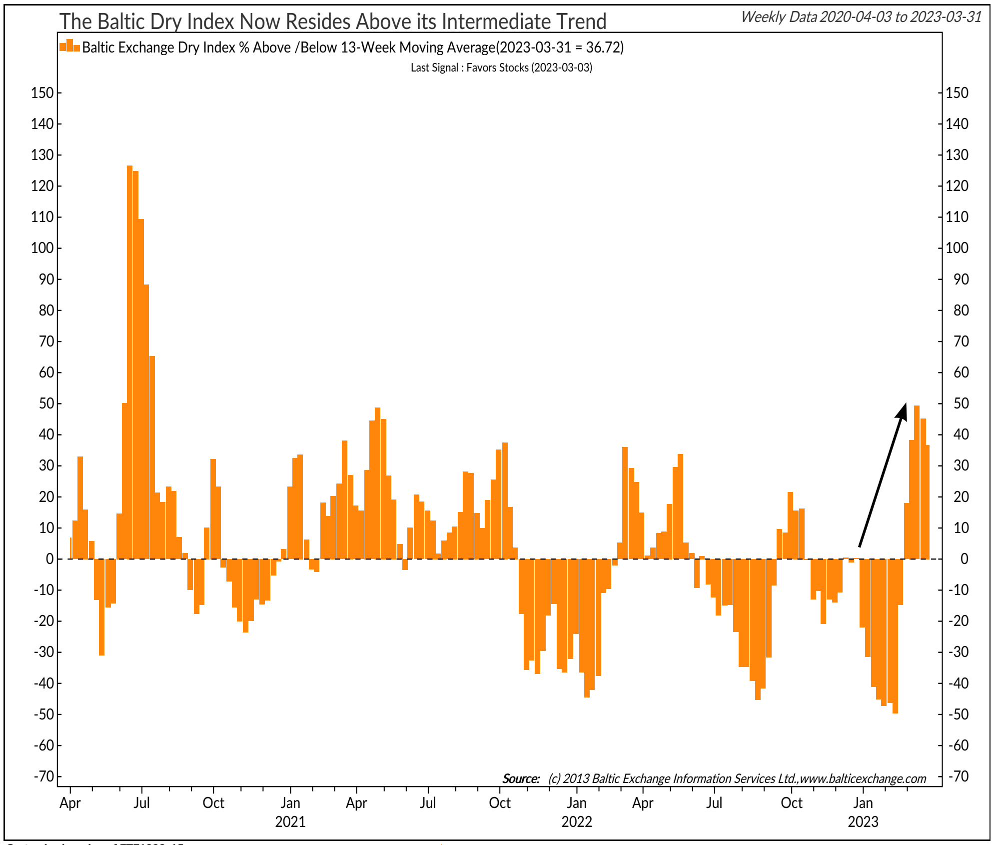

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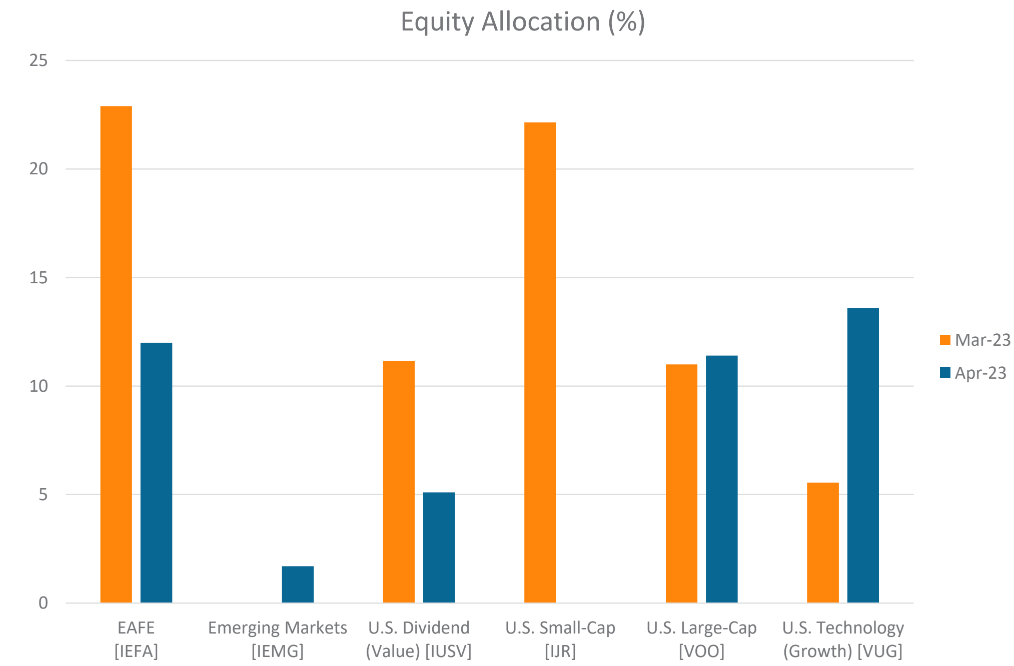
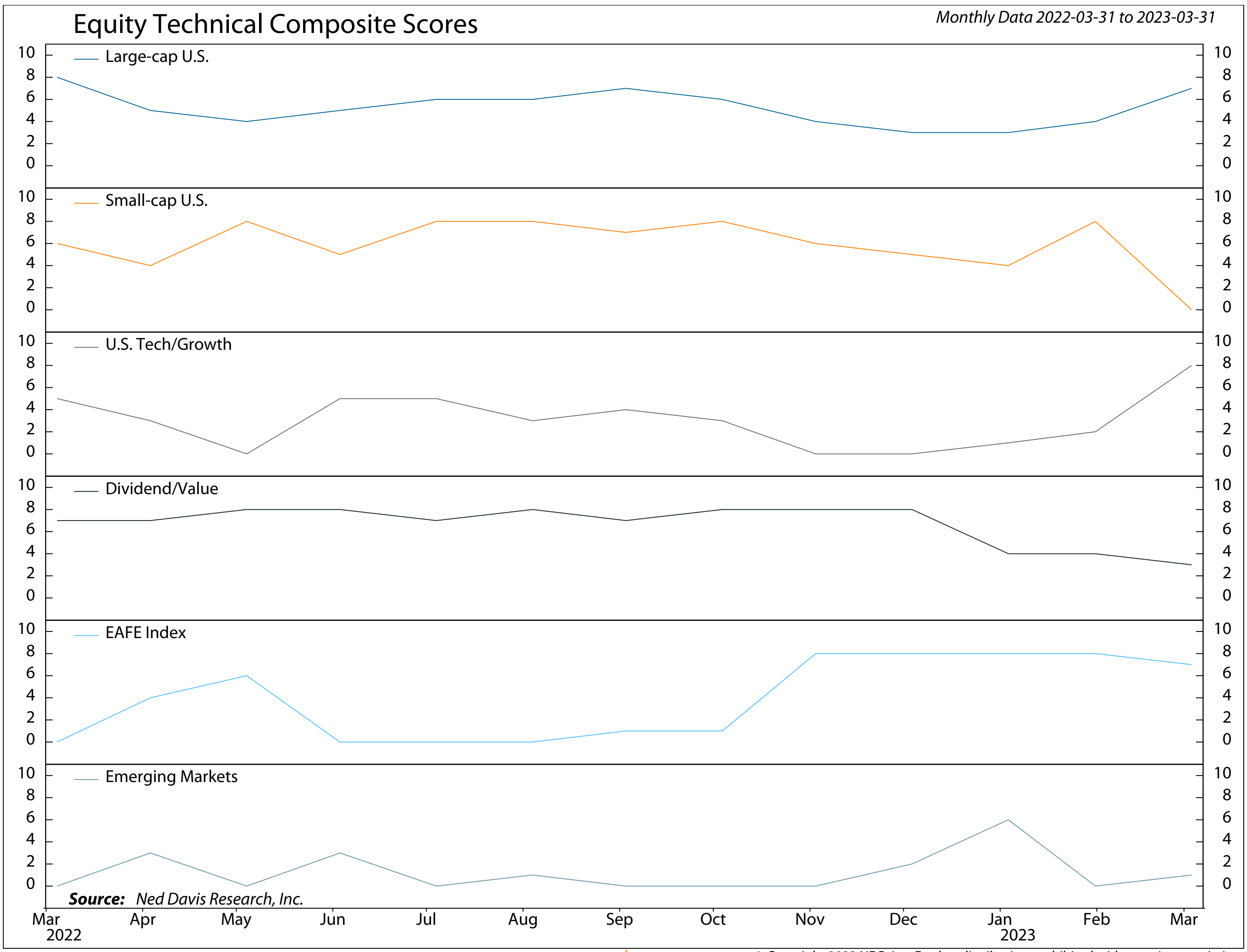
The Baltic Dry index (BDI) indicator now favors stocks. Last month, the BDI was more than 14% below its 13-week moving average. By mid-March, the indicator jumped to its highest reading since the economic reopening during 2020. The BDI now resides at more than 36% above its intermediate-term trend (chart at left).

Equity Allocation Summary

During March, all equity areas, except for U.S. Small Caps (IJR), gained. IJR has declined by more than 100 bps for three of the last four months. U.S. Growth (VUG) jumped more than 700 bps. VUG has increased by over 400 bps for four of the last six months. Emerging Markets (IEMG), International Developed (IEFA), and U.S. Large-Caps (VOO) each rose over 275 bps in March. VUG, IEFA, and VOO each received more than 10% allocation for April due to their technical composite scores.





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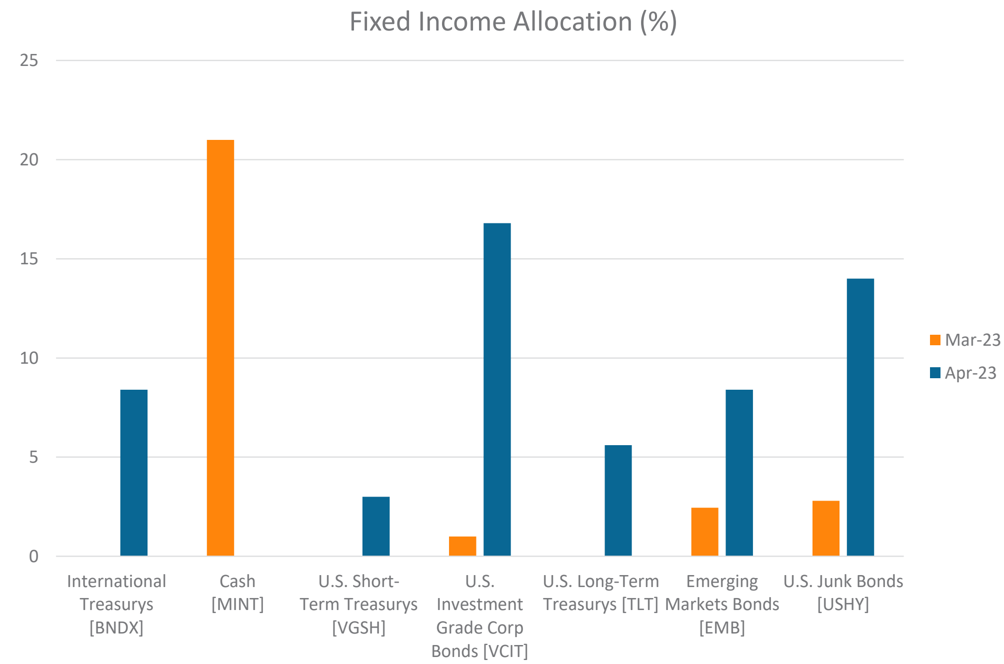
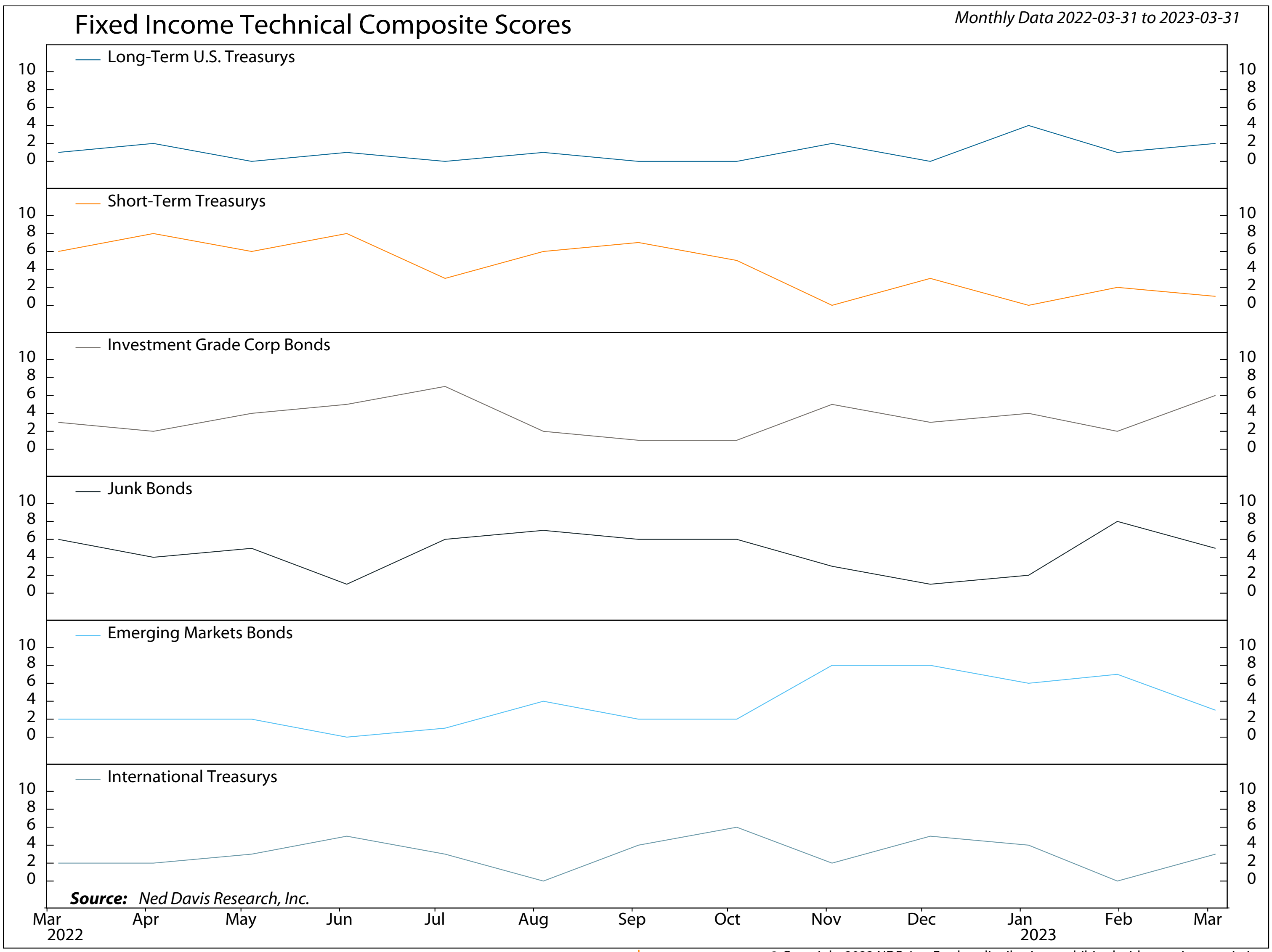
Fixed Income Allocation Summary

All fixed income areas increased during March. U.S. Long-Term Treasurys (TLT) and U.S. Investment Grade Corporates (VCIT) were the top performers as they jumped over 300 bps. U.S. High Yield (USHY) and International Investment Grade (BNDX) rose more than 200 bps. It was BNDX's best monthly return since July. Emerging Market bonds (EMB) and U.S. Short-Term Treasurys (VGSH) gained over 100 bps. It was the best monthly return in the history of VGSH. VCIT and USHY received at least 10% allocation for April due to their technical composite scores.





Source: *Ned Davis Research, Inc.*

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