Dynamic Allocation Strategy

JANUARY 2024

Macro/Market Update

The global economy grew modestly in November, as the S&P Global Purchasing Managers' Index (PMI) global composite (services and manufacturing) indicated moderate global growth. It was the first increase in the PMI in six months, indicating some stabilization in the economy, and putting the PMI further away from severe recession.

Forward-looking indicators reflect slower global growth in 2024, but no recession. Overall new orders moved out of contraction territory for the first time in three months, but the future outlook index was little changed. While well above its cycle low in 2022, this index is still below its long-term average, indicating modest growth expectations.

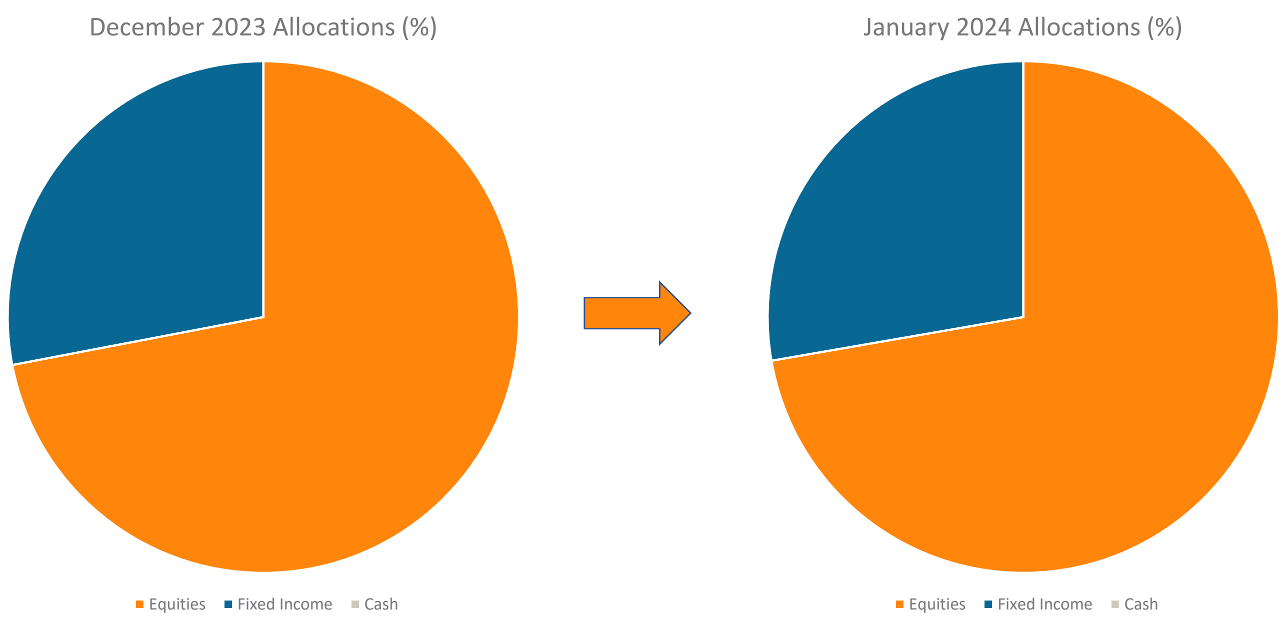
Both the manufacturing and services indexes saw modest improvement, something not seen in tandem since February. But manufacturing continued to contract, while services is growing at a fraction of the pace from earlier this year.

Due to easing global supply chain pressures and waning pandemic-related imbalances, global price growth has eased significantly from its peak in 2022. Both the global composite input and output price indexes are at or close to their lowest levels since late 2020. However, the composite price indexes are still above pre-pandemic levels as progress in bringing down inflation has slowed this year.

Among major countries and regions, growth trends in the U.S. and China remained mildly positive, while the economic decline in Europe eased somewhat. The global powerhouses continue to be emerging economies outside of China, led by India and the Middle East.

During December, the MSCI All Country World Index (ACWI) outperformed the Bloomberg Barclays Global Aggregate Bond Index by over 50 basis points (bps). Stocks outpaced bonds during two-thirds of the months in 2023. The drivers of the recent equity market advance could continue to support the market in 2024. Those include the transition from global inflation to disinflation, the likely aversion of a global recession, earnings continuing to beat expectations, and the anticipation that global central banks will be cutting rates.

Asset Allocation Summary

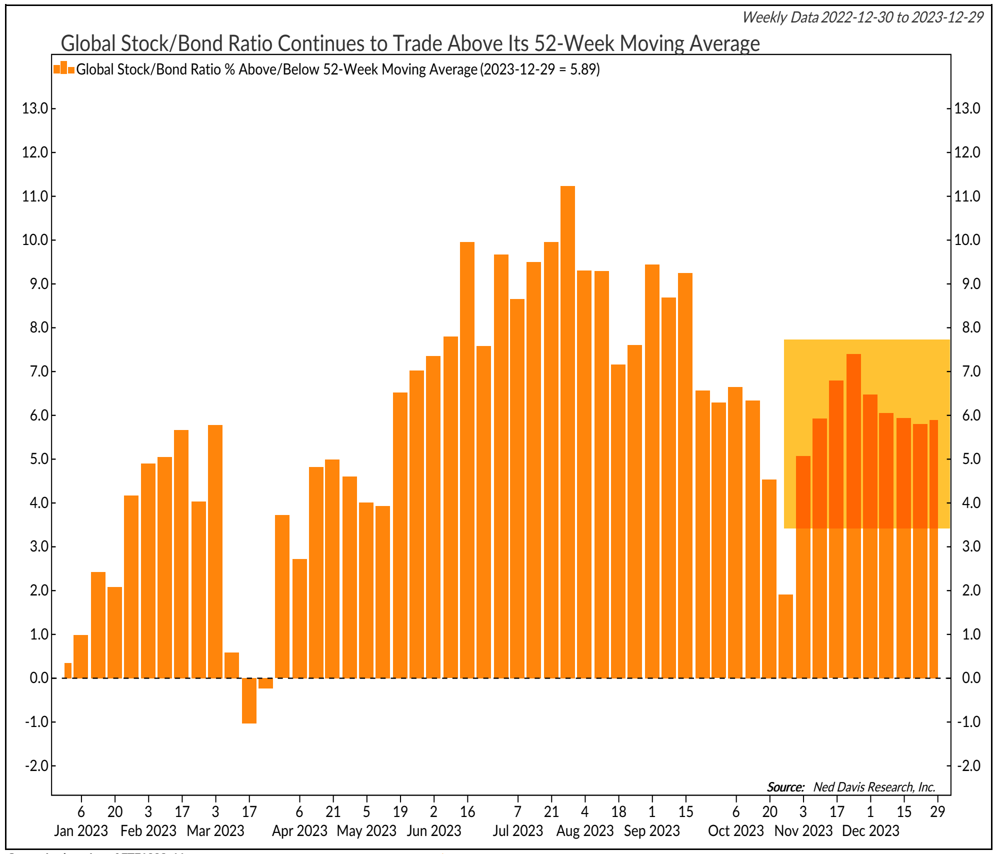


* See Equity Allocation Summary for how the equity allocation is distributed
** See Fixed Income Allocation Summary for how the fixed income allocation is distributed

The equity allocation remained 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.

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 ratio resides about 6% above its one-year moving average (chart right). It has favored equities since last March.

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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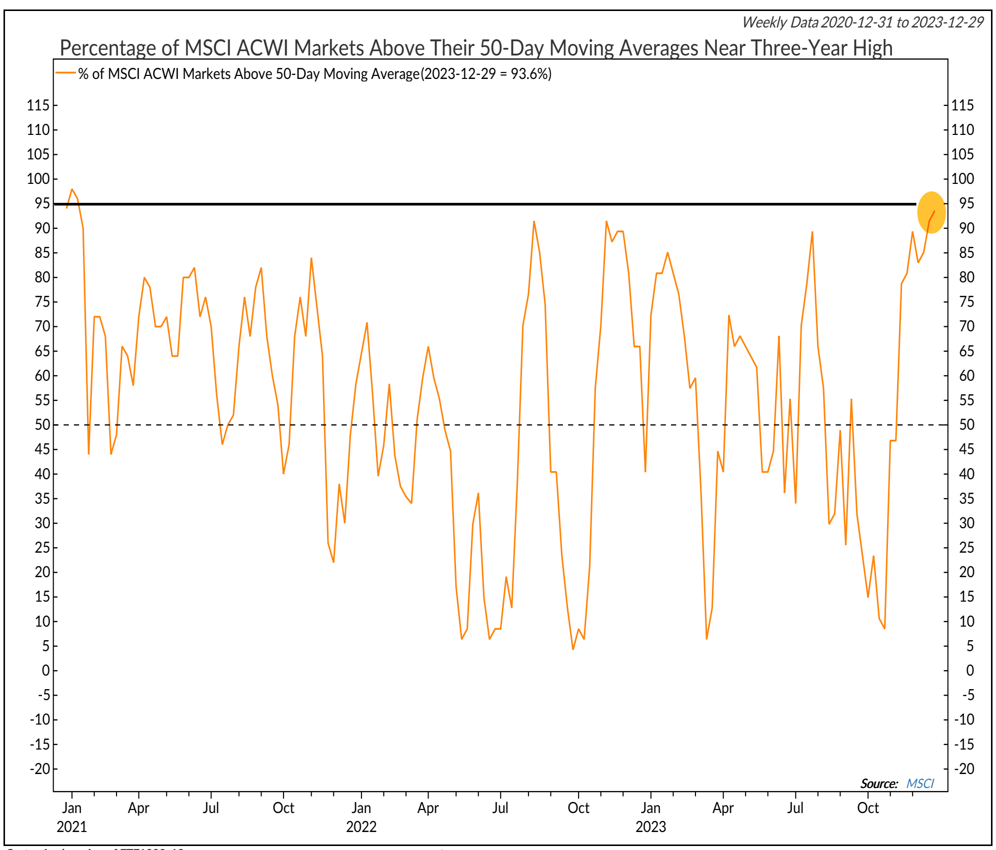

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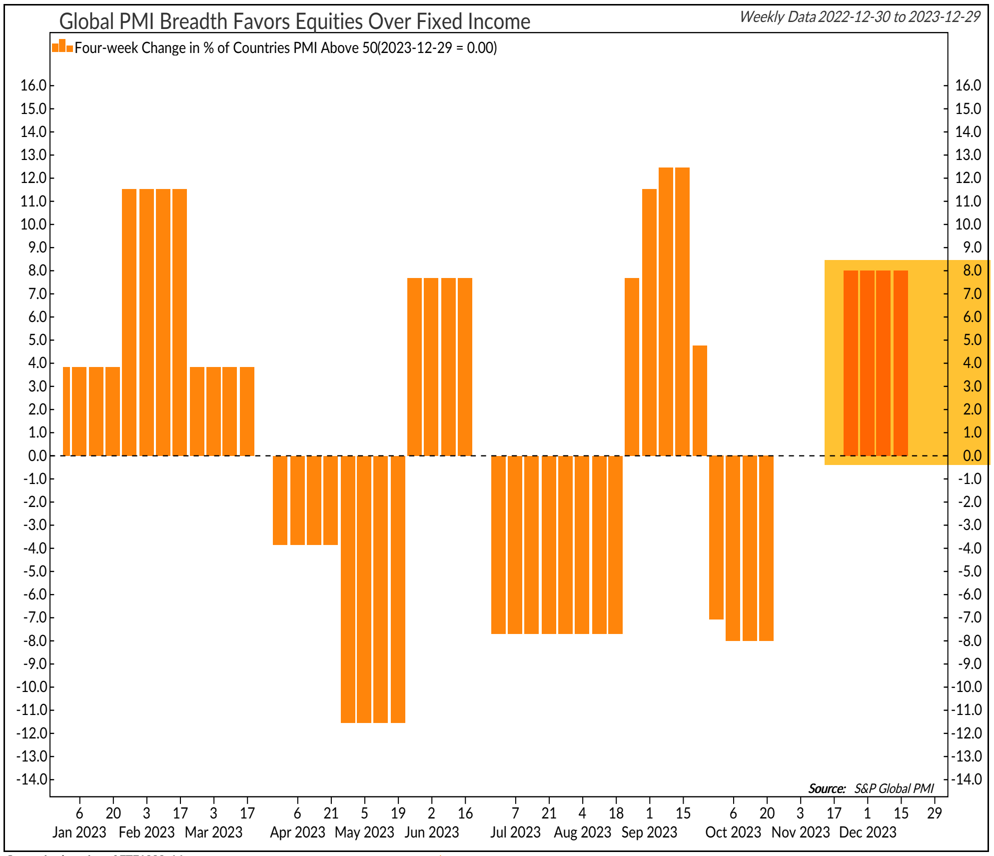
Global equity market breadth rebounded to its highest level since January 2021. The percentage of global equity markets trading above their 50-day moving averages experienced significant volatility in 2023. After declining to less than 10% at the end of October, more than 93% of markets now reside above the intermediate-term trends (chart left).

This indicator describes the underlying health of global equities, since it tracks the number of markets participating on the upside. Elevated breadth is important because if many stocks rally, even if a few run into trouble, enough stocks remain in uptrends that they can support the popular averages.

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 widening improvement in the economic outlook. This economic momentum breadth indicator (chart right) turned bullish on equities as China rose above 50.



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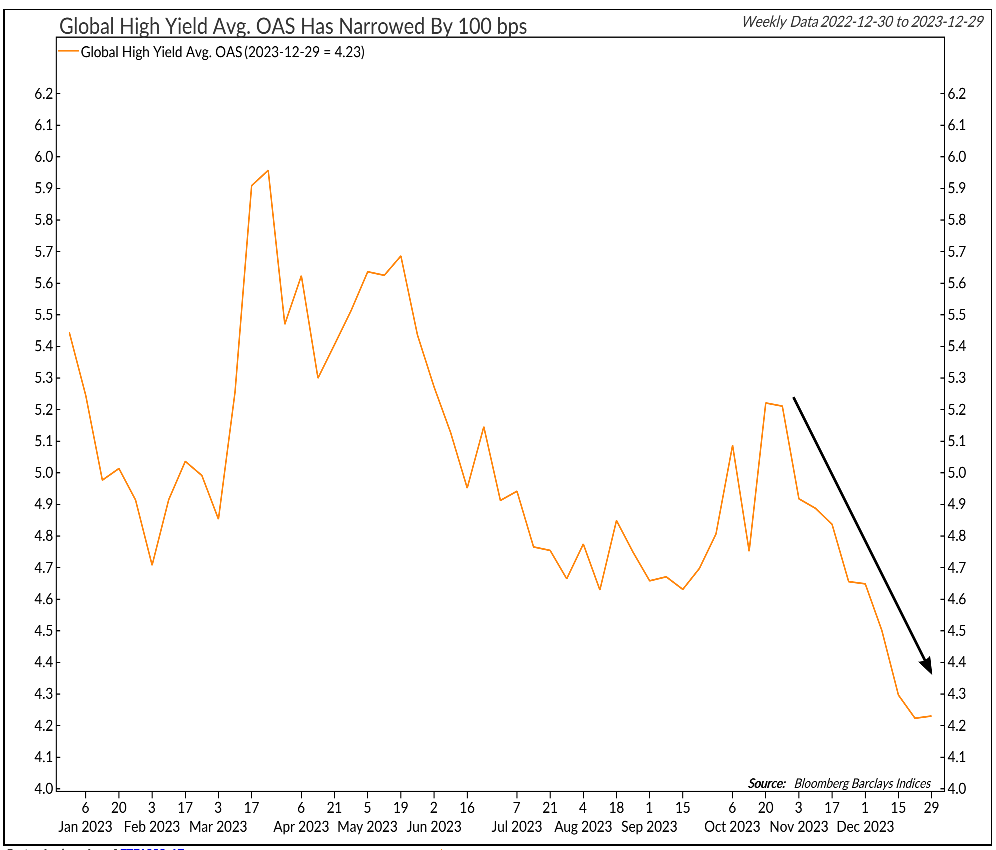

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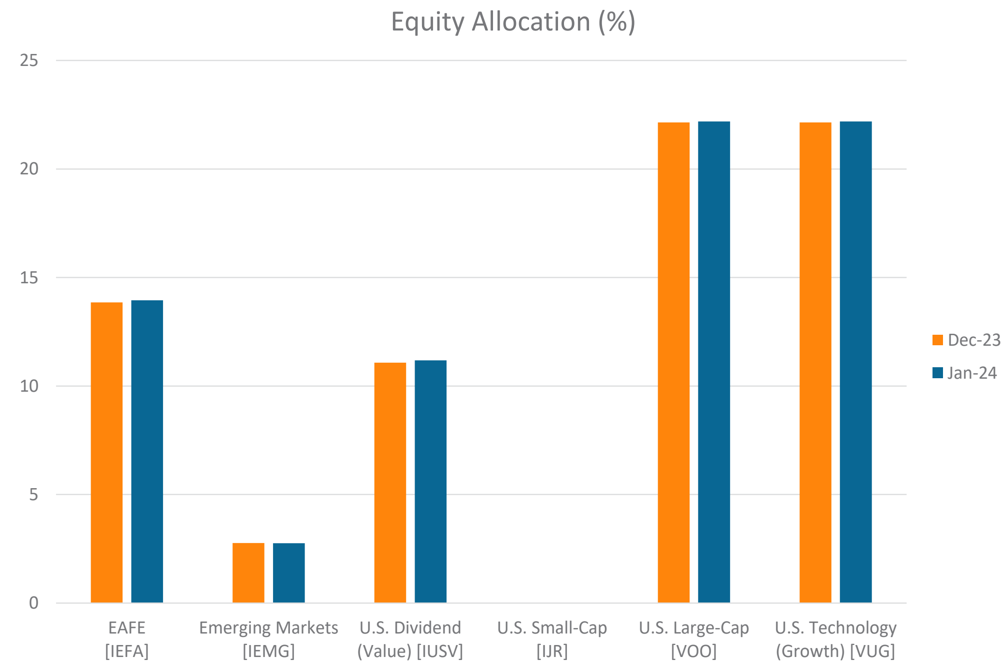
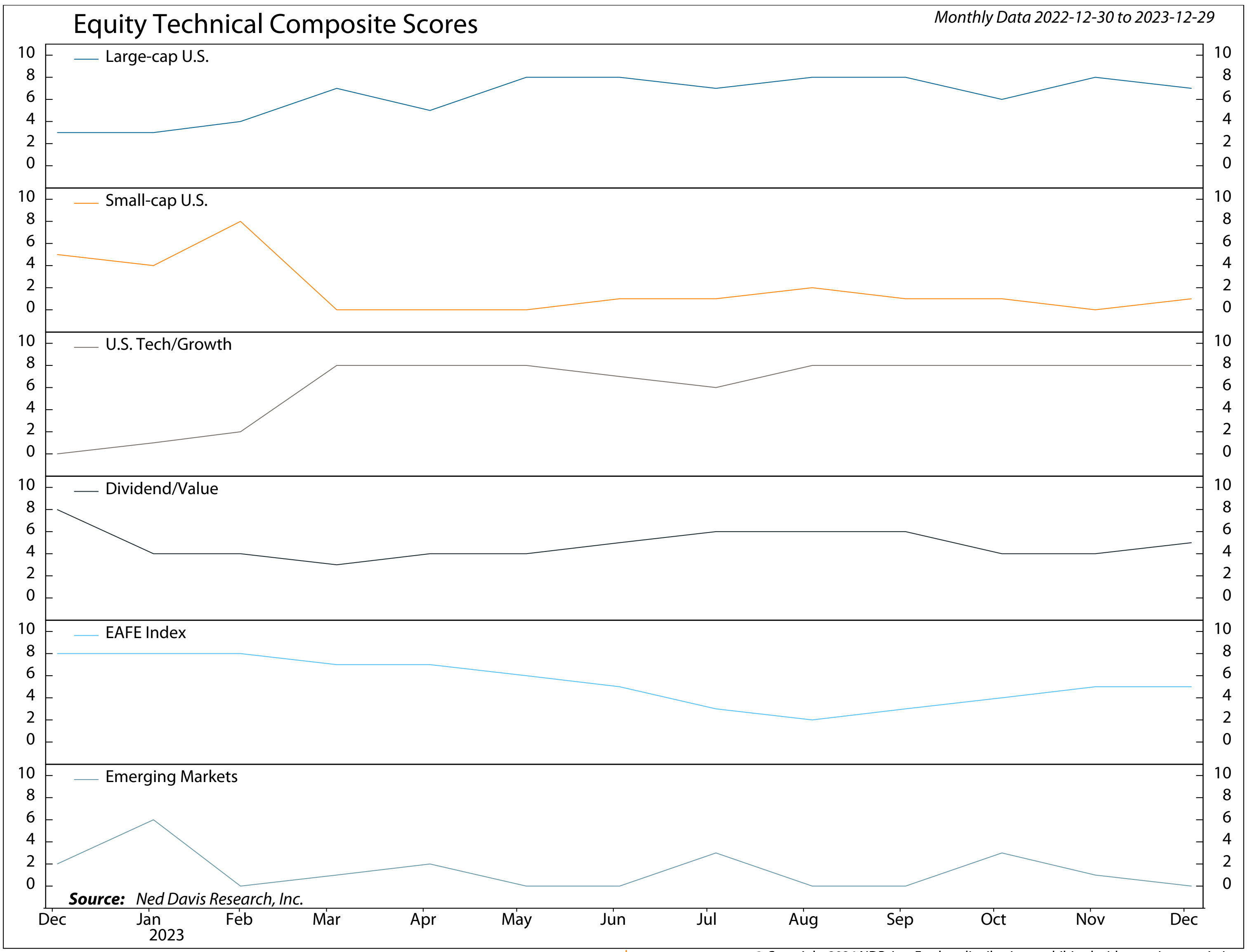
After rising by almost 60 basis points (bps) from mid-September through October, global high yield option-adjusted spreads (OAS) fell 100 bps during November and December (chart left), which reflects improving risk appetite.

Equity Allocation Summary

For a second consecutive month, all six equity areas increased by more than 390 bps. U.S. Small Caps jumped more than 12% in December, its best month since November 2020. U.S. Value and International Developed both gained over 500 bps. U.S. Large-Caps, U.S. Growth, U.S. Value, and International Developed received more than 10% allocation for January (chart right).





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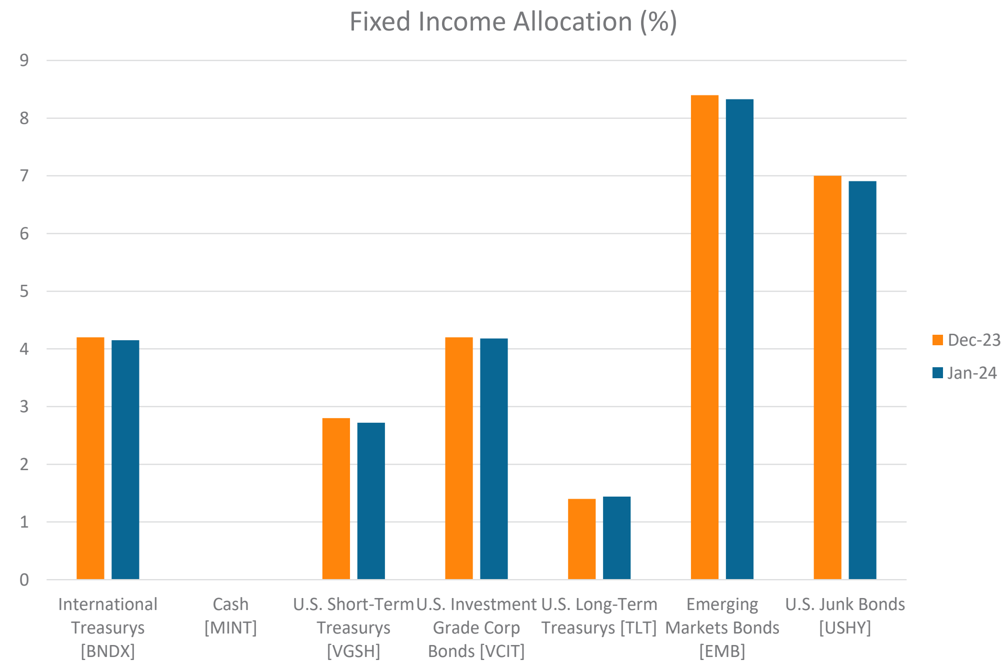
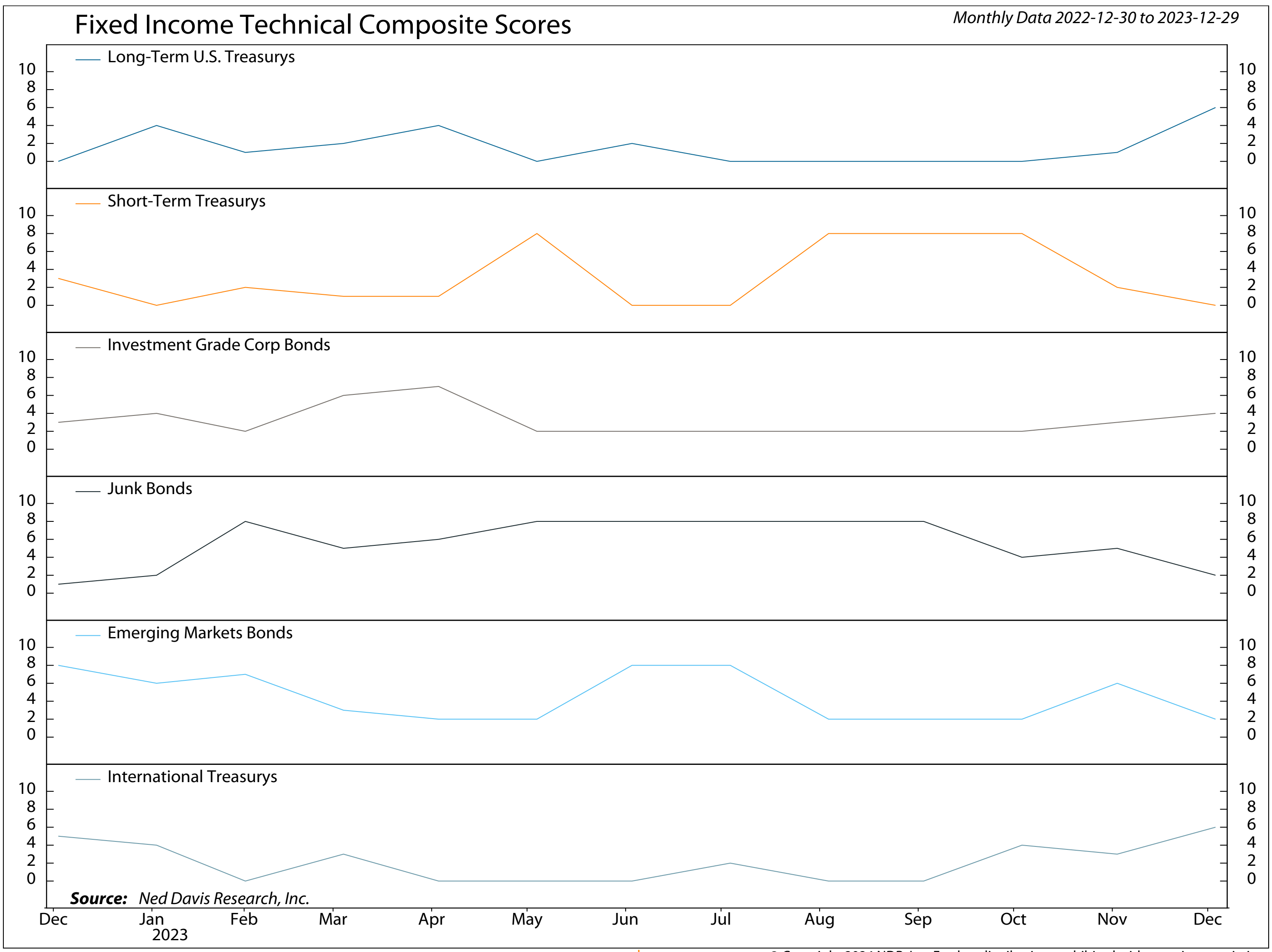
Fixed Income Allocation Summary

All fixed income segments increased more than 100 bps for a second straight month. U.S. long-term Treasurys (TLT) gained more than 800 bps during November and December. Such strength across two months last occurred in 2011. Emerging Market bonds and U.S. Investment Grade Corporates both rose more than 400 bps. Emerging Market bonds and U.S. High Yield were the only areas to receive more than 5% allocation for January (chart right).





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