Dynamic Allocation Strategy

AUGUST 2021

Macro/Market Update

The global economy remained in strong growth mode in June, according to the latest global macroeconomic indicators. Even so, rising COVID cases in some parts of the world and ongoing supply chain issues, which have contributed to higher costs, present risks to the near-term outlook.

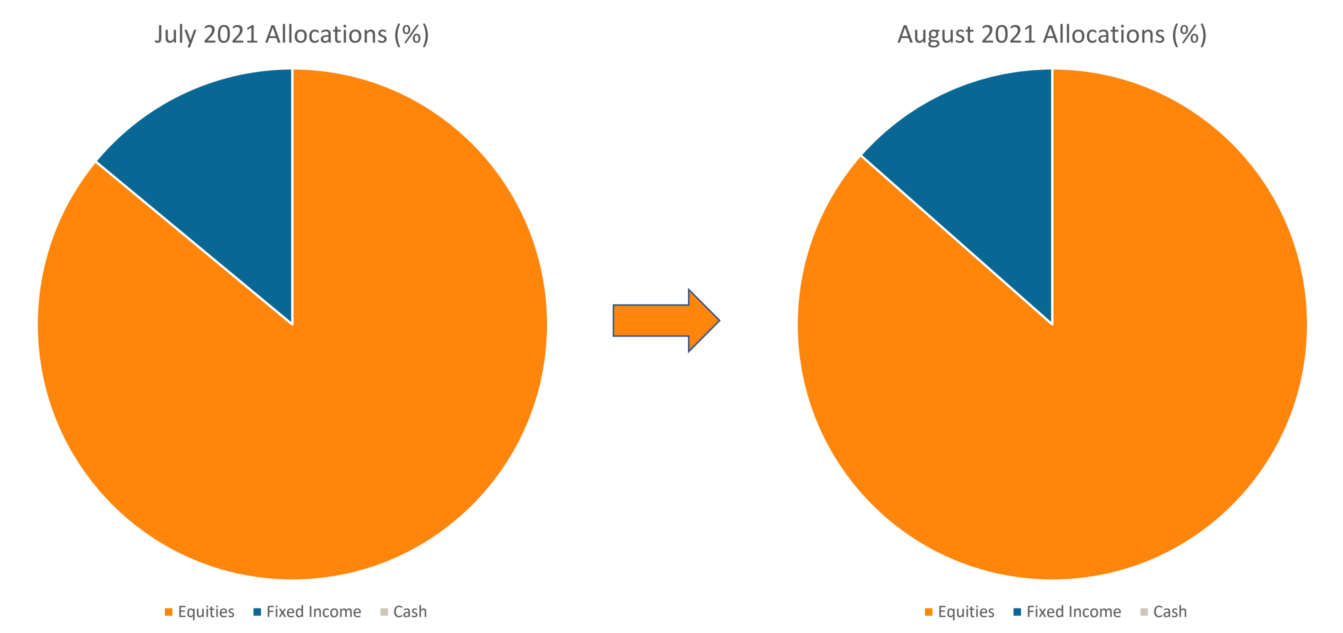
The global composite Purchasing Managers' Index (PMI) slipped 1.8 points in June to 56.6. It was the first decline in five months and the largest drop since the April 2020 lockdowns. However, the PMI is still hovering around its highest level on record and historically consistent with an extremely robust 5.3% annual global real Gross Domestic Product (GDP) growth rate.

New orders and employment, also eased from the prior month, but remained near their historical peaks. The composite future output index, however, climbed to its highest level since January 2014, indicating that businesses anticipate accelerating trends over the coming year.

Due to the imbalances in supply and demand, global prices continued to surge. The composite PMI's input and output price indexes both hovered around their highest levels on record. But in a possible sign that the imbalances are slowly abating, the input price index fell for the first time in nine months, while the output index slipped for the first time in six months.

During July, the MSCI All Country World Index (ACWI) underperformed the Barclays Global Aggregate Bond Index by more than 50 basis points (bps). This broke an eight-month winning streak for stocks relative to bonds. Global equities have been following a script in which the rallying leads to excessive optimism. The lingering optimism leaves investors complacent and vulnerable to a new negative, most recently the upturn in COVID-19 variant cases. The selling relieves the optimism, makes the market oversold, and attracts new buying by investors recognizing that the macro influences are still conducive to a stock market uptrend.

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 traded this month as it reallocated within each asset class.
- The equity allocation remains above 80%.
- The fixed income allocation continues to be less than 20%.
- Cash has no weighting within the model.
- The global breadth indicator measures the percentage of global equity markets trading higher than their 50-day moving averages. At the end of June, more than two-thirds of global markets traded above their intermediate-term trends. However, breadth deteriorated during July as less than half of the markets were above their trends intra-month. The indicator was primed to favor bonds for August, but it rallied at the end of the month to barely hold on to its stocks signal (chart, below).
- Five of the six top-level indicators favor 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 remains at more than 10% above its one-year moving average, but it continues to decline from its all-time high set earlier this year.
Global Market Breadth	Favors Equities	52% of global equity markets are trading above their 50-day moving average. This indicator is near the threshold for favoring bonds.
OECD Leading Indicator	Favors Equities	The four-week change in the OECD Composite Leading Indicator (CLI) is still positive after hitting an all-time high one year ago.
PMI Breadth Factor	Favors Fixed Income	The four-week change in economies with expanding manufacturing industries is near its key threshold, but still favors fixed income.
Baltic Exchange Dry Index	Favors Equities	The Baltic Dry Index is more than 8% above its 13-week moving average. During July, the indicator had fallen to less than 2% above its intermediate-term trend.
Central Bank Policy	Favors Equities	In order to favor fixed income, this indicator requires a significant drop in global short-term rates.

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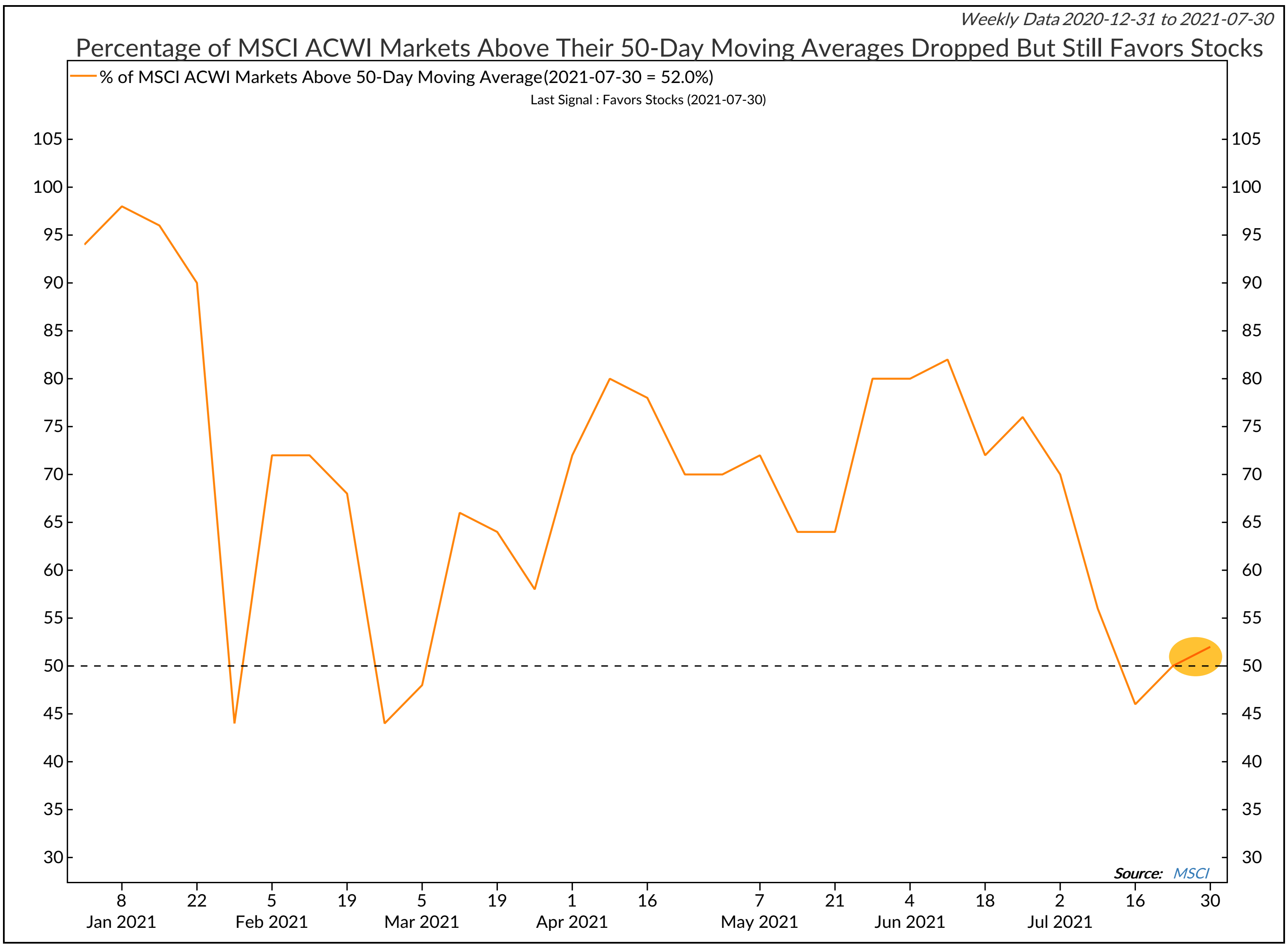

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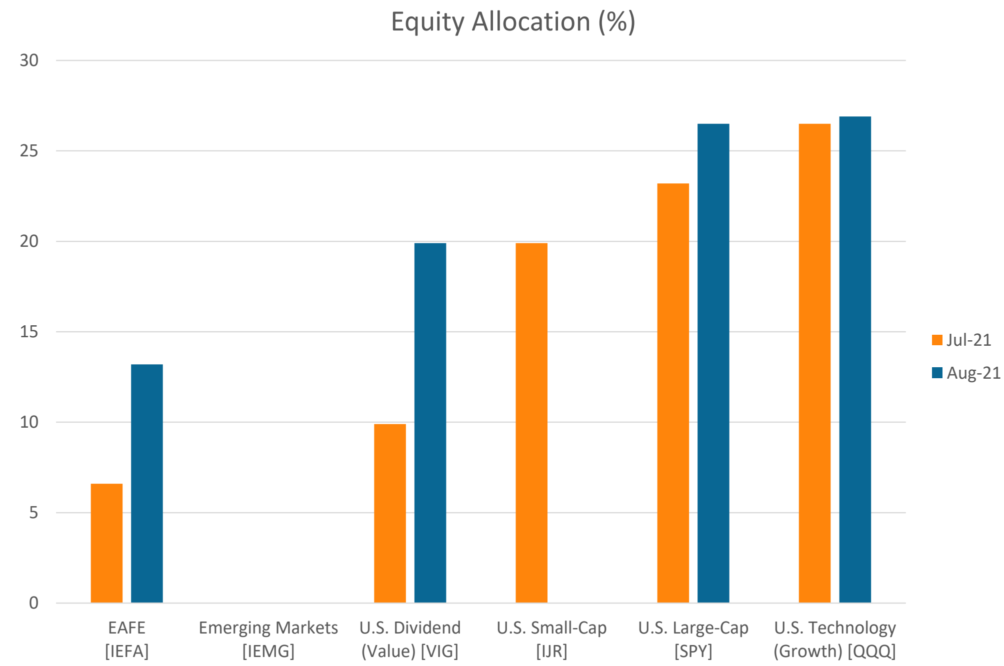
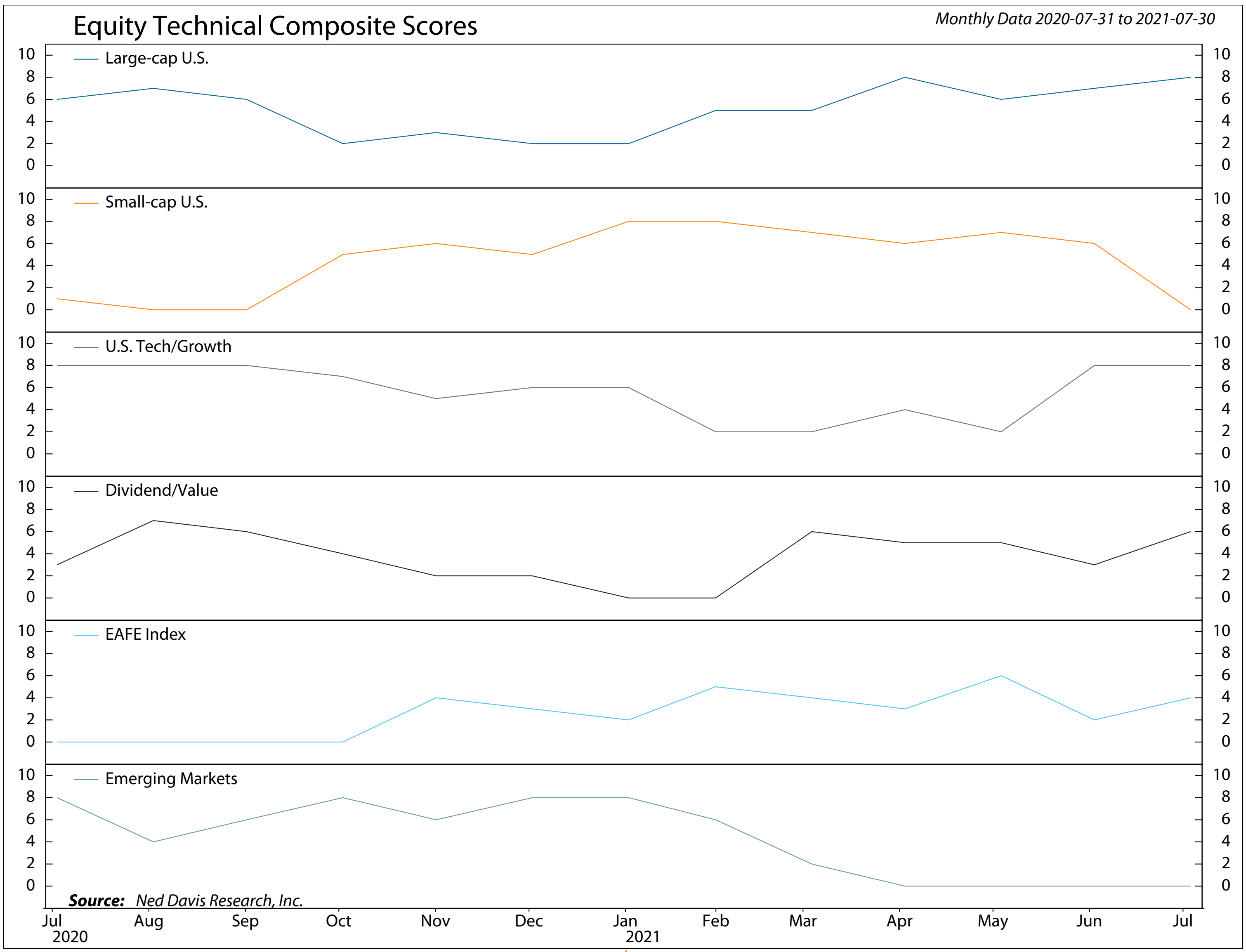
Equity Allocation Summary

During July, U.S. Value [Dividends] (VIG) was the top-performing area within equities as it increased by more than 300 basis points (bps). U.S. Growth [Technology] (QQQ) and U.S. Large Caps (SPY) both grew over 200 bps. SPY has risen for six consecutive months. U.S. Small Caps (IJR) fell by more than 200 bps last month, while Emerging Markets (IEMG) plummeted by over 500 bps. This broke a nine-month winning streak for IJR. QQQ, SPY, and VIG all received more than 15% allocation for August due to their elevated technical composite scores (image at bottom).





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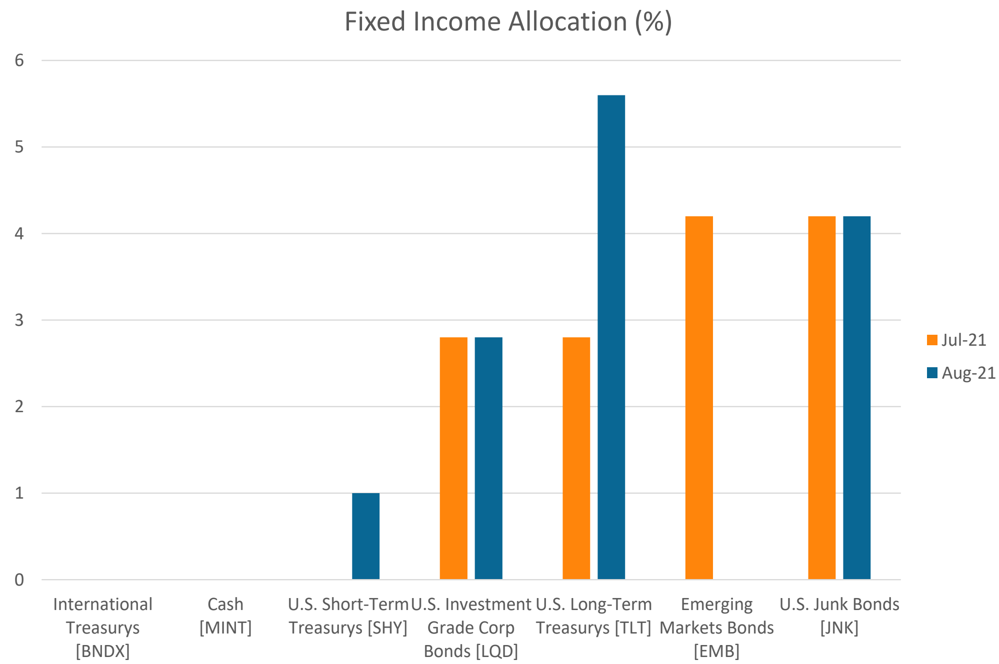
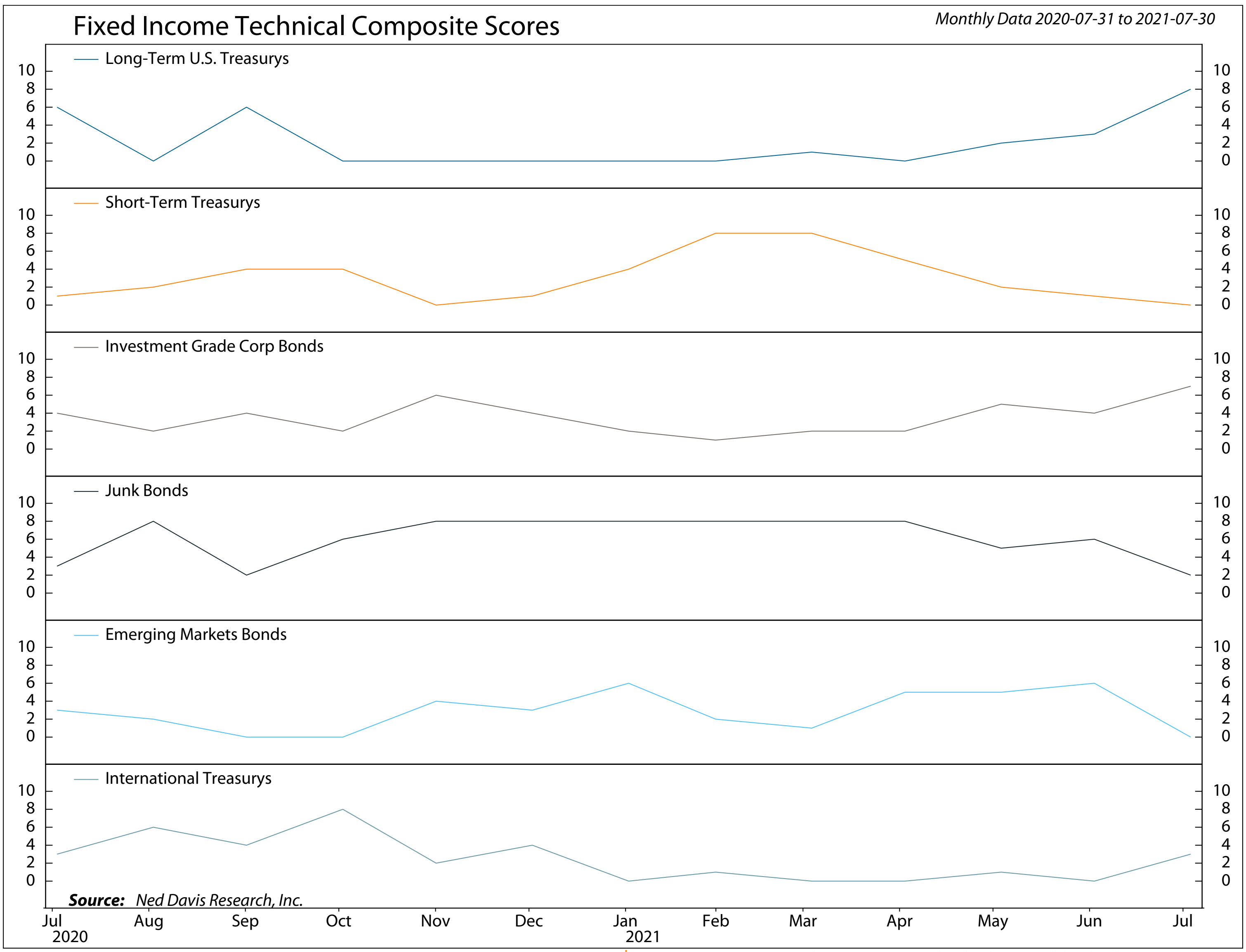
Fixed Income Allocation Summary

Last month, U.S. Long-Term Treasurys (TLT) was the best-performing sector within fixed income, as it gained over 300 bps. TLT has jumped by more than 300 bps for two consecutive months. U.S. Investment Grade (LQD) and International Investment Grade Bonds (BNDX) both increased by more than 100 bps. Emerging Market bonds (EMB), U.S. High Yield (JNK), and U.S. Short-Term Treasurys (SHY) each rose over 10 bps. LQD and EMB have produced positive returns for four straight months. JNK has been higher for each of the last six months. TLT and JNK both received more than 3% allocation for August (image at bottom).





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