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GLOVISTA INVESTMENTS

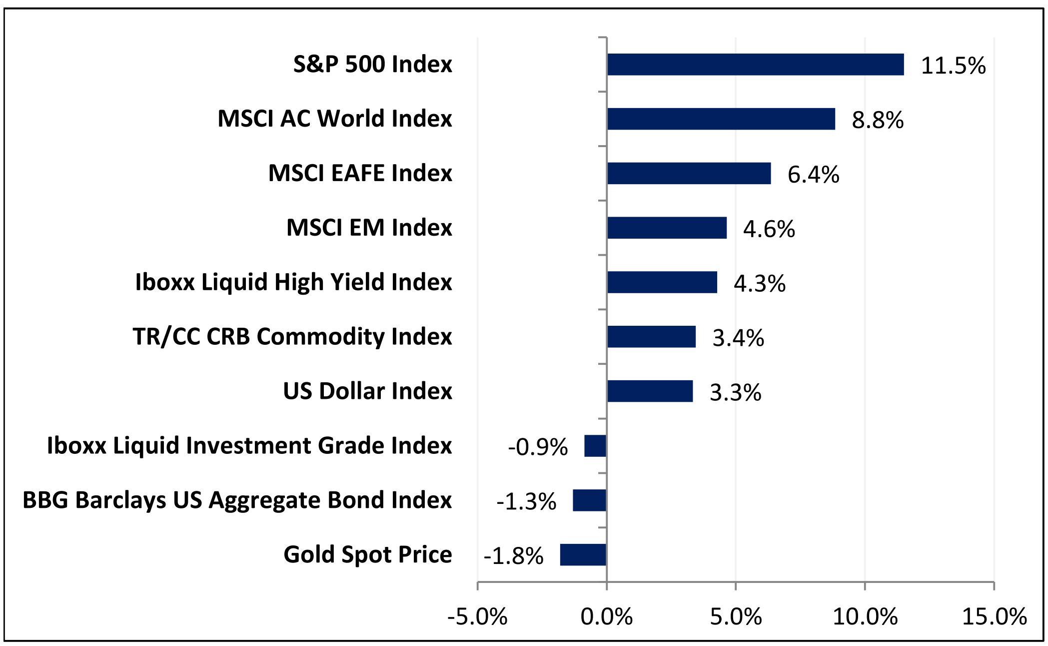
Glovista Global Perspectives

This Issue:

Markets Rise Further on Reduced Risks of US Protectionism and Solid Q4 Earnings; Glovista Raises Portfolios' Defensive Positioning on Valuation Considerations and Impending Europe Political and China Economic Risks

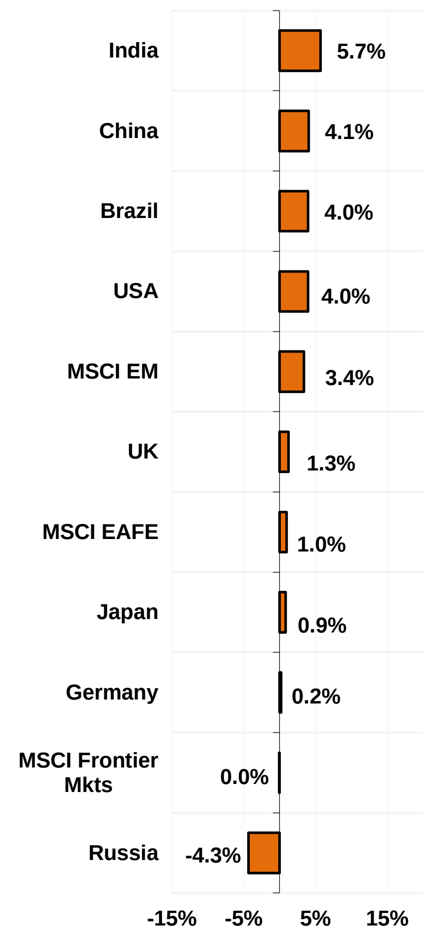
The month of February has marked an extension of the sharp rally in risk markets that began in the aftermath of the past US November 2016 elections. For example, Figure 1 illustrates percentage return performance figures for a number of risk indices globally covering the February 2017 month-to-date (MTD) along with the post-November 2016 US election periods.

Figure 1. February 2017 Marks Continuation of Rally in Risk Indices Set Off on the Heels of November 2016 US Election Results (November 9st, 2016 to February 27th, 2017)



Source: Bloomberg

Country-wise Monthly Performance in USD terms (Feb MTD 2017)*



Source: MSCI & Bloomberg

**As of February 27th, 2017*

In our view, the extension into February of the rally in risk market indices that began in the aftermath of the US November 2016 results reflects a number of considerations, including the following:

- signs of diminished risks of an overly virulent protectionist scenario under President Trump. Said signs include the absence of major pronouncements on trade policy by President Trump on the occasion of recent US visits made by leaders of major US trading partners such as Canada, the UK and Japan. Likewise, on a recent visit to Mexico City, US Treasury Secretary Mnuchin delivered a speech on US-Mexico trade that was deemed constructive by Mexican officials;

- reduction of geopolitical tensions with China, following President Trump's recent validation of the longstanding "One China Policy" in a telephone communication with the Chinese leadership;

- solid 2016Q4 earnings results out of the world's major economic regions, with year-on-year earnings growth of around 8 percent for the US and around 12 percent for Europe and Japan;

- continued strengthening in business confidence indicators out of the world's major economic blocs.

The above noted developments have boosted risk asset prices on account of market participants' focus on continued positive activity momentum and a diminution of risk premium levels following the recent de-escalation of US protectionist scenarios and geopolitical tensions with China.

S&P500 Monthly Sector Performance – Feb MTD 2017*

Sectors	% Change	FY1 PE Ratio
Energy	-2.49%	30.6
Materials	0.48%	18.1
Industrials	3.91%	18.2
Cons Disc	2.48%	19.1
Cons Stap	4.63%	20.0
Technology	5.29%	17.5
Healthcare	6.46%	14.8
Financials	5.19%	13.9
Utilities	3.74%	17.4
Telecom	0.05%	13.9
Real Estate	4.73%	37.8
S&P500	3.99%	17.6

**As of February 27th, 2017*

Source: S&P

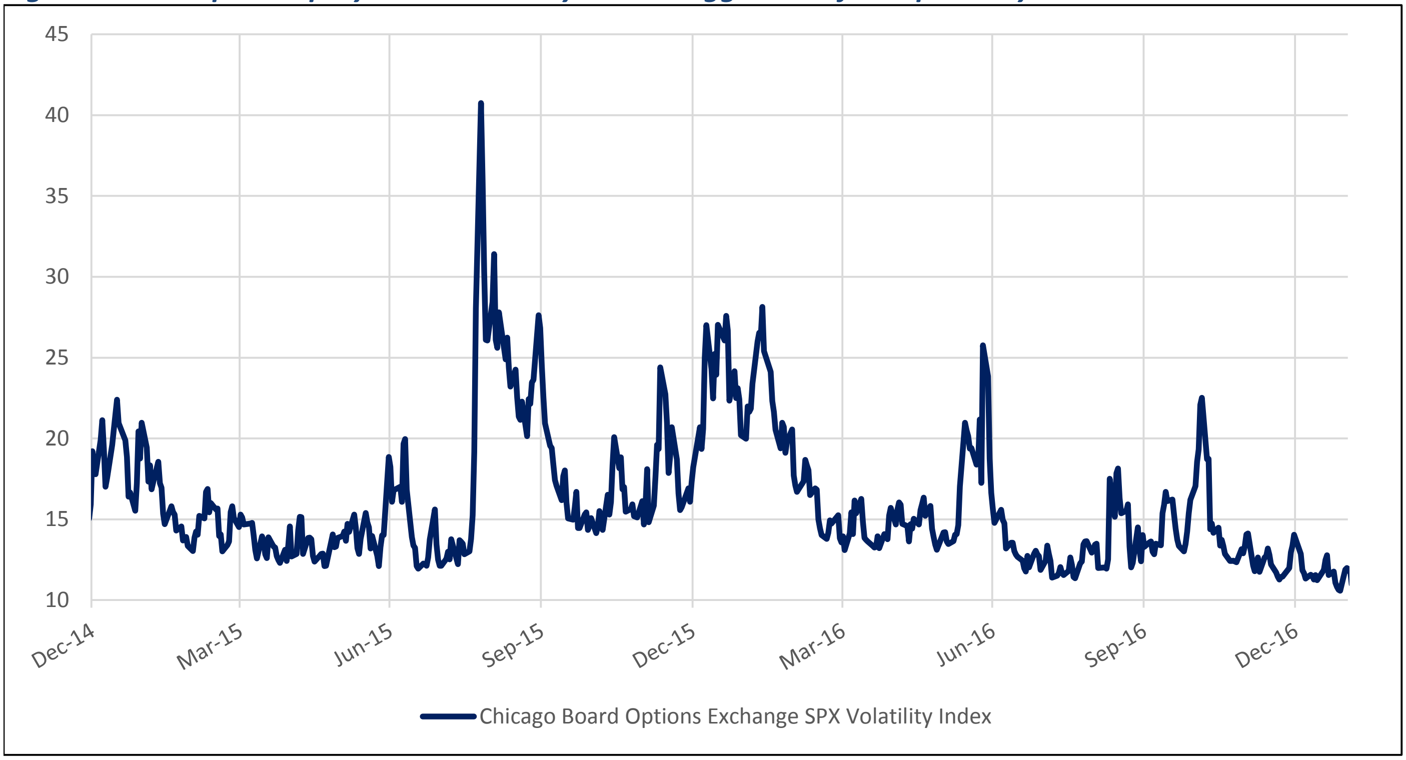
Near-term Market Outlook Conditioned by Key Hurdles including Overbought Condition, Impending Definition of Trump's Policy Agenda, European Elections and China Economic Risks

As we look ahead at the next quarter, a number of important hurdles appear to be lined up against further upside potential for risk asset prices. Some of those hurdles include the following:

- *Overbought market conditions.* Most short-term indicators suggest equity and credit asset prices are short-term overbought. Such indicators include low implied equity index volatility levels (Figure 2), relative strength indicator levels (Figure 3) and the leadership exerted by retail investor flows in the post-November equities rally confirmed by the prevalence of equity inflows via passive equity index ETFs.

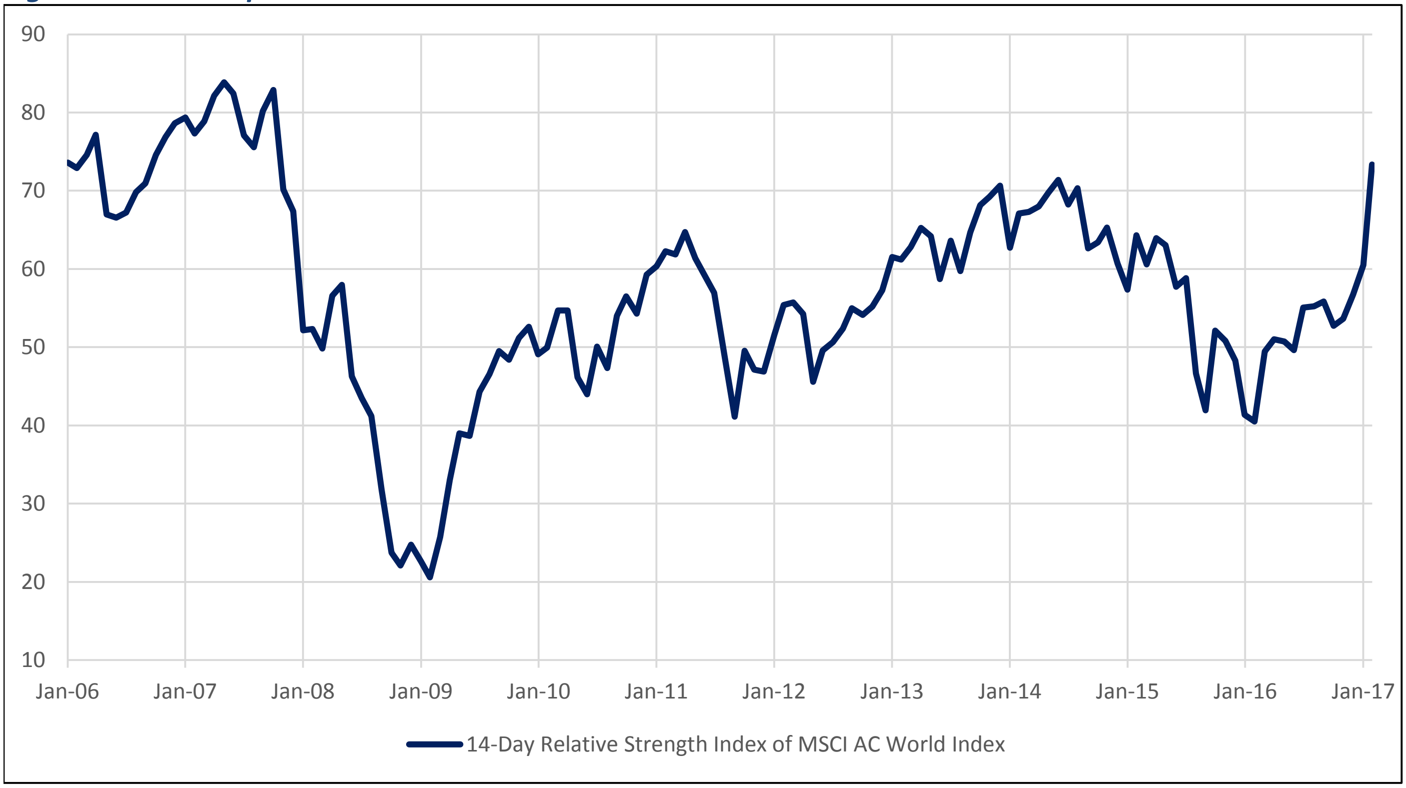
- *Impending definition of Trump's policy agenda.* US President Trump is scheduled to deliver his first major policy address before the US Congress this coming Tuesday, February 28 (post the release of this monthly update). The analysts' community broadly expects Mr. Trump to provide a more detailed picture of the policy agenda his administration will be submitting before Congress over the coming weeks, including tax, trade, healthcare and infrastructure expenditure reform measures. In all likelihood, such announcement will prove material not only for the broader market but also for specific sectors of the market, especially on issues such as border tax adjustments.

Figure 2. VIX Implied Equity Index Volatility Levels Suggestive of Complacency



Source: Bloomberg

Figure 3. World Equities' Price Momentum at Overextended Levels



Source: MSCI and Bloomberg

	Feb 27th 2017	Feb MTD Change
Gold	1252.77	3.5%
Silver	18.266	4.0%
Oil	54.05	2.3%
EUR	1.0587	-2.0%
JPY	112.7	0.1%
GBP	1.2442	-1.1%
CHF	1.009	-2.0%
CAD	1.318	-1.2%
AUD	0.7673	1.2%
BRL	3.1104	1.2%
MXN	19.911	4.4%

Source: Bloomberg

Rates	Feb 27th Level
1 Yr CD	0.57%
5 Yr CD	1.21%
30 Yr Jumbo Mortgage	4.45%
5/1 Jumbo Mortgage	3.4%
US Govt. 10 Year	2.365%
10 Yr Swap Spread	-0.0225%

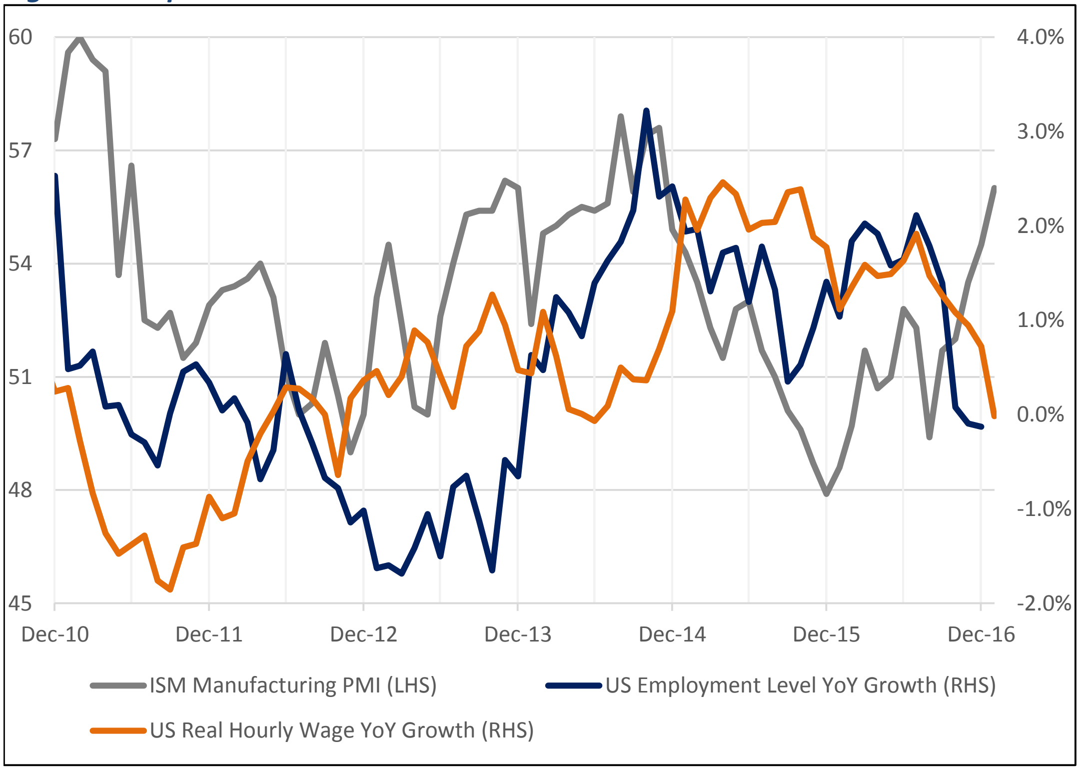
Source: Bloomberg

- *Increased two-sided risks associated with upcoming European elections, especially those in France and Germany.* Such risks appear to have increased owing to Marine Le Pen's rise in the French polls along with the SPD's in Germany's. Ultimately, these political developments are material to the European and global market outlook owing to the currency redenomination scenarios away from the Euro currency should a major Euro area country such as France or Germany opt to exit the currency union;

- *Chinese economic downside risks.* Over the past several weeks, it has become clear the Chinese economic authorities have sponsored a de-facto tightening of fiscal policies as the measures introduced a year ago to support the banking sector in implicitly 'off-loading' a share of its non-performing loan portfolios have been allowed to run their course. In the process, fiscal expenditure growth levels have come down by double digits in percentage terms on a year-on-year basis from levels prevailing at the end of 2015. As policy stimulus levels decline, the impact on the Chinese economy is likely to be felt across a number of cyclical sectors, impacting trading partners around the world. Such dynamics could bring about deflationary forces onto the global scene, with adverse implications on world risk asset markets;

- *D*ivergence between US sentiment indicators and labor demand conditions. Over the past several months, economic sentiment indicators have strengthened considerably. However, such improvement in sentiment levels has been at odds with labor demand conditions, including real wage growth (Figure 4). For example, year-on-year US real wage growth has decelerated to the 0 percent level while the year-on-year growth of employment levels has decelerated consistently over the past several months (Figure 4);

Figure 4. Improved US Economic Sentiment Levels at Odds with Labor Conditions



Source: Institute of Supply Management and Bureau of Labor Statistics

- *Divergence between US sentiment indicators and loan activity dynamics and lending standards.* Recently released Fed data shows a sequential decline in bank credit levels to the private sector since December 2016, amounting to the largest percentage decline in several years. In addition, the latest Fed's senior loan officer survey corresponding to the fourth quarter of 2016 shows lending standards on auto loans to have tightened for three consecutive quarters while credit card lending standards recently spiked into ranges that entail 'net tightening'. Such divergence between sentiment and consumer sector data are sobering given the large consumer expenditure share in the US economy, at close to 65 percent.

Over the past several weeks, US fixed income markets appear to have focused on the recent divergence between sentiment indicators and labor demand conditions as well as the potential disinflationary effects stemming from Chinese economic developments discussed above. Figure 5 illustrates the notable moderation in medium-term US inflation expectations over the past several weeks.

Figure 5. US Intermediate-term Inflation Expectations Moderate Considerably Early in 2017

Source: Bloomberg

Glovista Raises Defensive Portfolio Stance given Valuation Considerations, Rate Outlook, Policy and Political Uncertainty

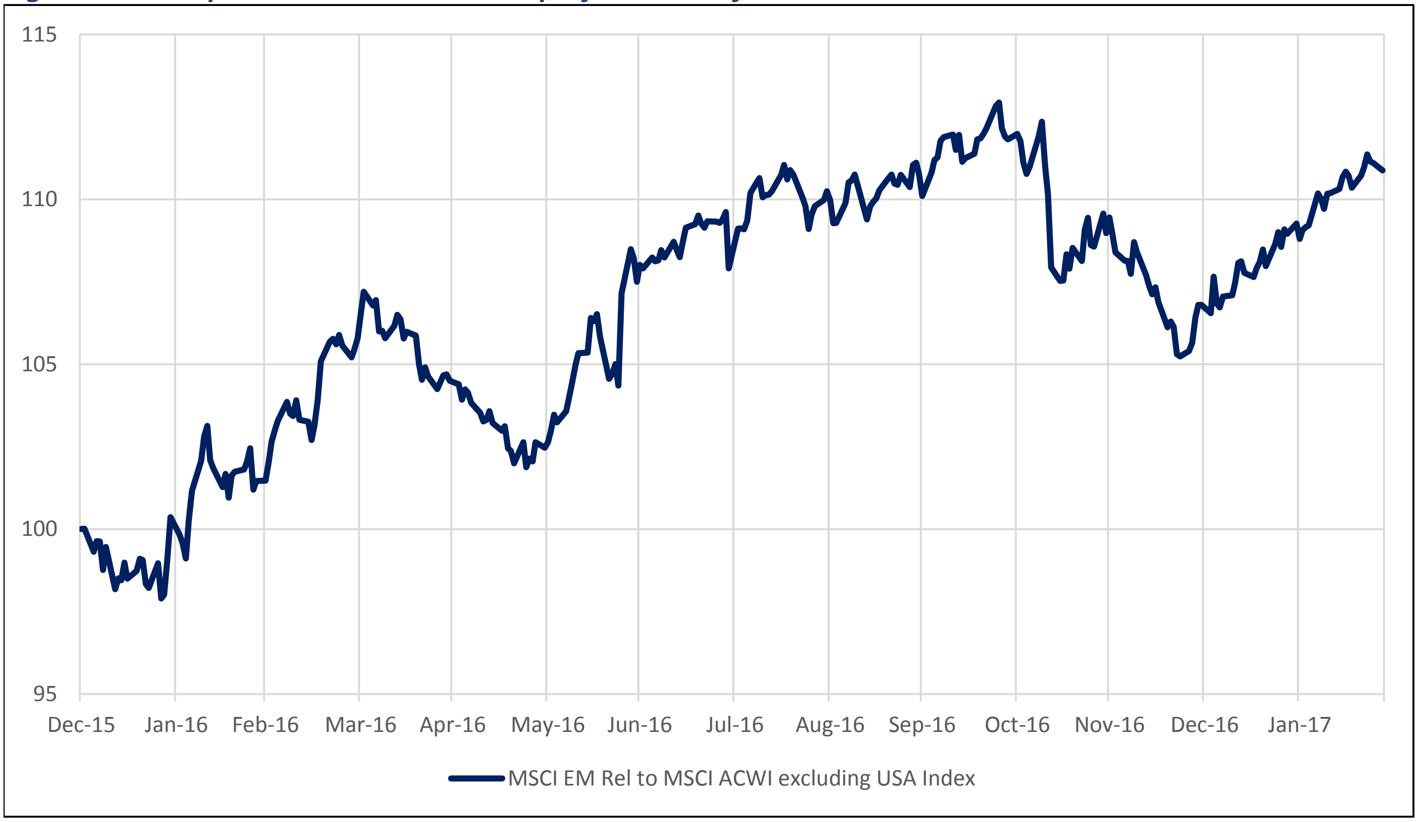
Over the past several weeks, Glovista has deemphasized its managed portfolios' cyclical tilts, opting to raise exposure to defensive equity sectors such as utilities, healthcare and consumer staples while retaining exposure to the technology sector. Within fixed income markets, we have raised duration exposure as we expect the US Federal Reserve to take a gradual path in raising further the Federal Funds rate given the continued moderation in inflation expectations together with the persistently high levels of policy uncertainty. Within the commodities sector, we remain constructive towards the soft and precious metals groups, taking on exposure to those groups on a tactical basis.

Emerging Markets Perspectives

EM Equities Extend Outperformance Vs. DM Peers, Boosted by Lower Risks of US Protectionism, High Real Yields and Cyclical Growth; Glovista Sustains Overweight Value Tilts

In February, Emerging Market (EM) equities have extended their multi-month long return outperformance of Developed Market (DM) peers (Figure 6). In our view, the EM equities' rally has been boosted by a number of factors, including:

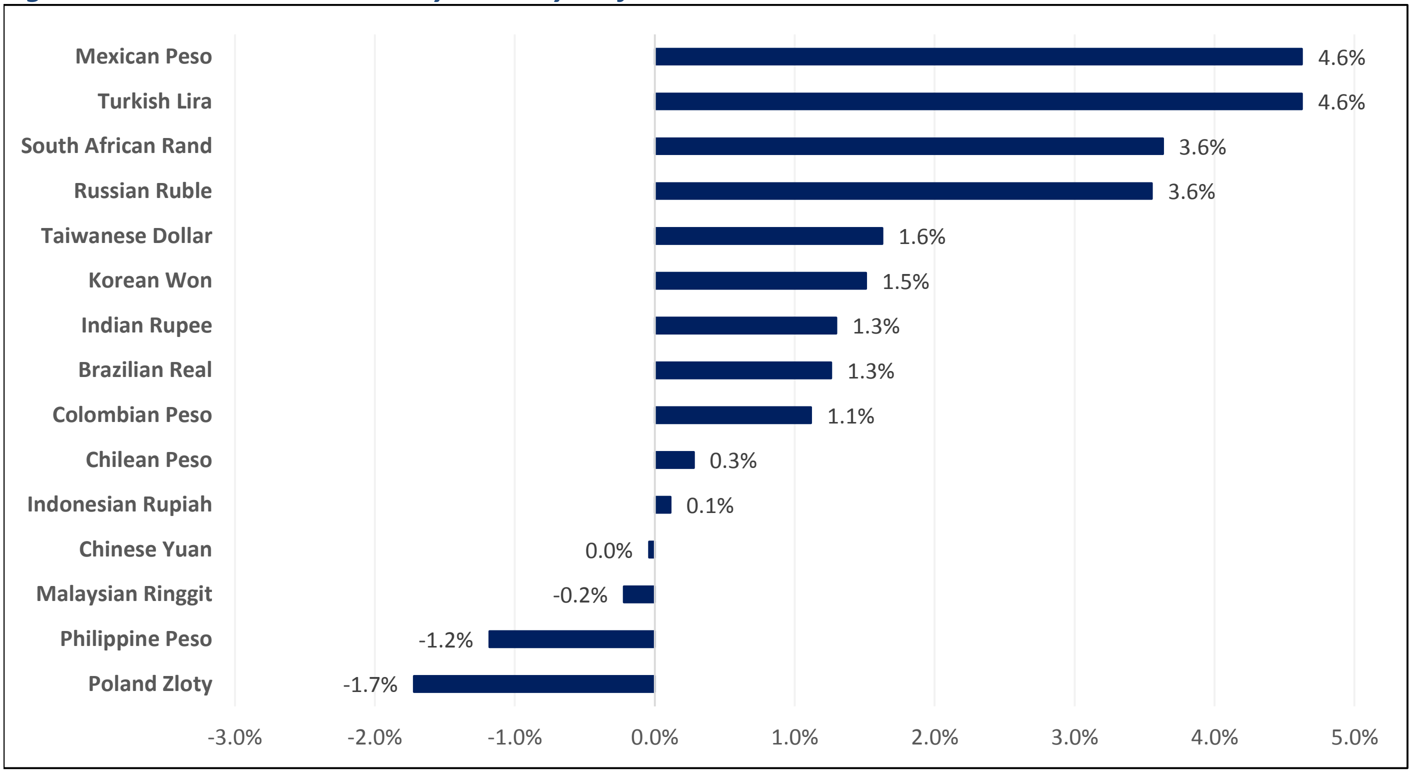
Figure 6. EM Equities Extend Return Outperformance of DM Peers



Source: MSCI, Bloomberg and Glovista Calculations

* reduced risks of an overly virulent protectionist agenda under President Trump, examples of which include the absence of major pronouncements on trade policy by President Trump on the occasion of US visits made by leaders of major US trading partners such as Canada, the UK and Japan. Likewise, in a recent visit to Mexico City, US Treasury Secretary Mnuchin delivered a speech on US-Mexico trade that was deemed constructive by Mexican officials. Consequently, it should not be altogether surprising for the Mexican Peso to be the strongest EM currency versus the Greenback during the month of February (Figure 7);

Figure 7. EM Currencies' February Monthly Performance versus the US Dollar



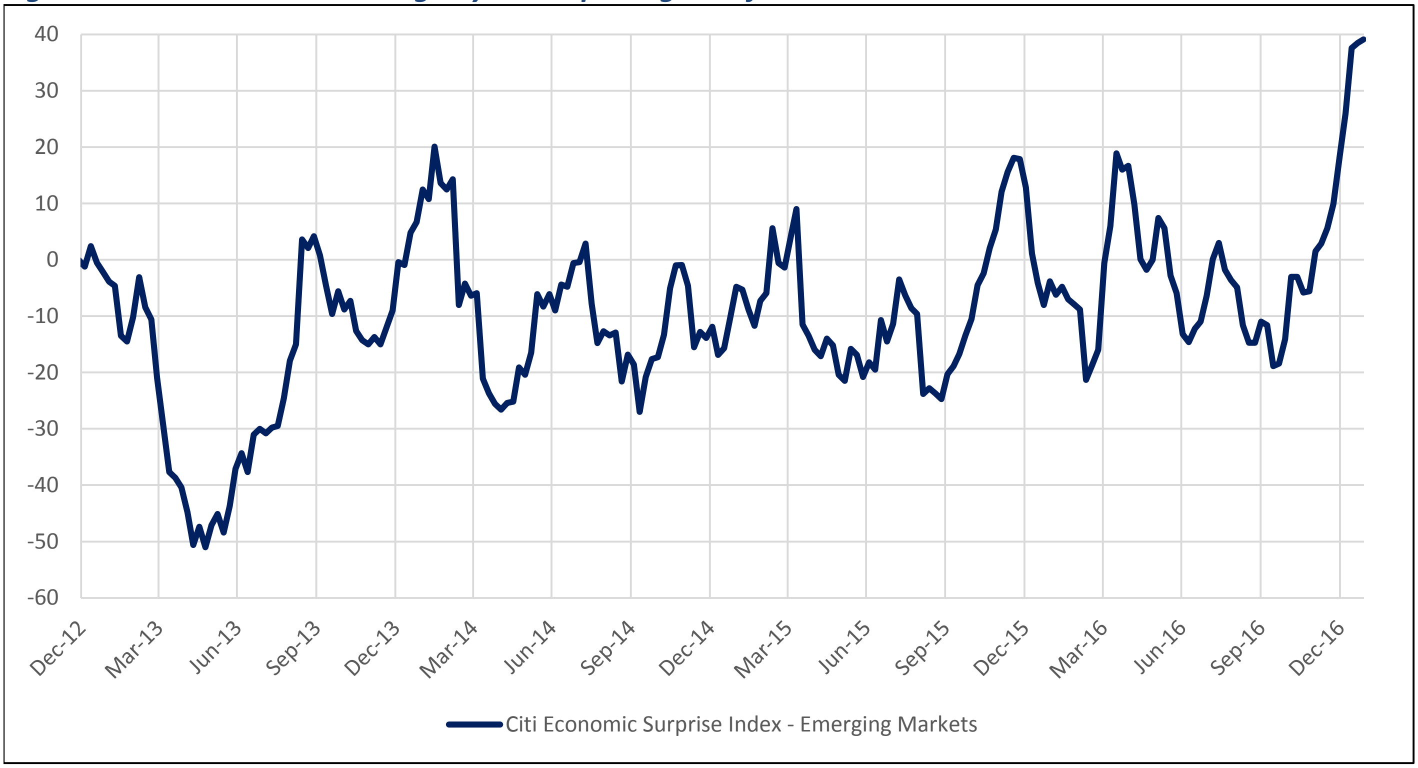
Source: Bloomberg

* Improved cyclical upswing facing EM economies, as indicated by Figure 8. Nevertheless, we remain cautious towards the Chinese economic outlook owing partly to a far less supportive fiscal policy backdrop in 2017. EM equity markets hold a higher beta to cyclical forces than DM peers. Consequently, EM equity market outperformance of DM peers around cyclical upturns is not at all surprising.

The recent abatement in global investor concerns surrounding the protectionist overtones of President Trump's agenda as well as reduced geopolitical risks helped push Mexican and Chinese equities into relative outperformance territory versus EM peers for the month of February. Polish and Turkish equities recorded strong relative outperformance during the month owing to a strong bid for value sectors, especially in the financial sector at a juncture in which energy prices have been consolidating.

Over the short term, we expect EM equities are likely to consolidate further or pull back modestly following a multi-month long period of relative outperformance. In the process, we believe continental economies with solid long-term fundamentals, such as India's, are likely to outperform their EM peer group. We remain steadfastly bullish EM equities on a stand-alone and relative basis versus DM peers both over the intermediate- and long-terms on account of cheap relative valuations, superior cyclical stance as it relates firms' profit margins and top line sales growth. Finally, investor positioning remains exceedingly underweight the EM asset class, thereby providing additional impetus for the asset class' strong relative outperformance over the coming quarters.

Figure 8. EM Economies Undergo Cyclical Upswing thus far in 2017



Source: Citigroup Global Markets

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