Issue
125
May/20

Monthly Market Newsletter

Glovista Global Perspectives

This Issue:

Global Perspectives **P.1**

Emerging Markets Perspectives **P.6**

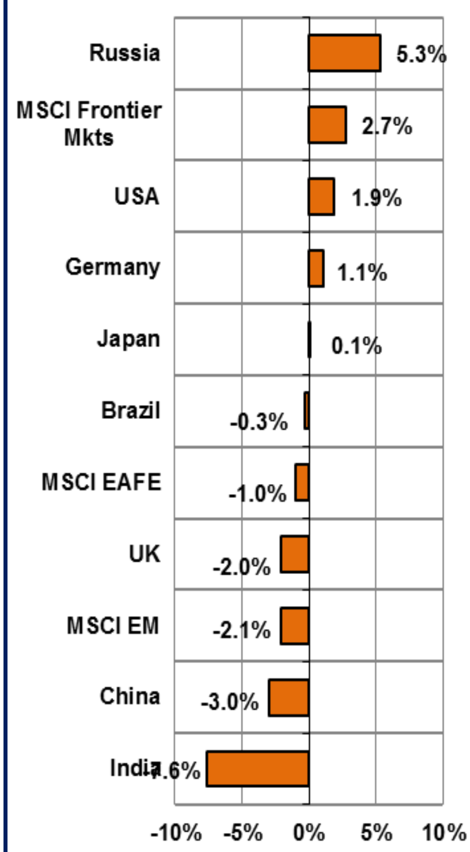
Risk Markets Post Uneven Recovery in May, Fueled by Further Relief Assistance, Investor Positioning and Broadening Reopening Measures as Virus Incidence Abates; Glovista Sustains High Quality Equities Exposure along with Short Bond Duration

In May, risk markets have consolidated the solid performance gains recorded in April. The make-up of May return performance has been uneven across risk asset groups, as illustrated in Figure 1. As discussed immediately below, we attribute risk markets' constructive May return performance largely to non-economic factors, tied to market technical/policy/virus related issues, the combined effects of which have helped bring about further reductions in asset risk premium levels.

As we look back at the past several weeks, we attribute the flat to strengthening return performance recorded by risk asset markets globally to the consolidation to continued decline recorded across various risk premium levels (Figure 2) as opposed to material upward revisions to world economic growth or consumer sentiment expectations. Specifically, we identify several developments as underlying such continued stability in risk premium levels:

- Further intensification in economic relief measures announced by both developed and developing country governments. For example, the past several weeks have witnessed the following announcements:
  - 10 percent of GDP economic stimulus measures by India's national government;
  - 500 billion Euro Economic Recovery Fund announced by the Eurozone region;
  - signaling by major US political leaders in support of a CARES Part 2 assistance program (of a magnitude in excess of US$700 billion) to be unfolded in the coming months should the pace of economic recovery disappoint;

Country-wise Monthly Performance in USD terms (May 2020)*



Source: MSCI & Bloomberg

***As of May 22nd, 2020**

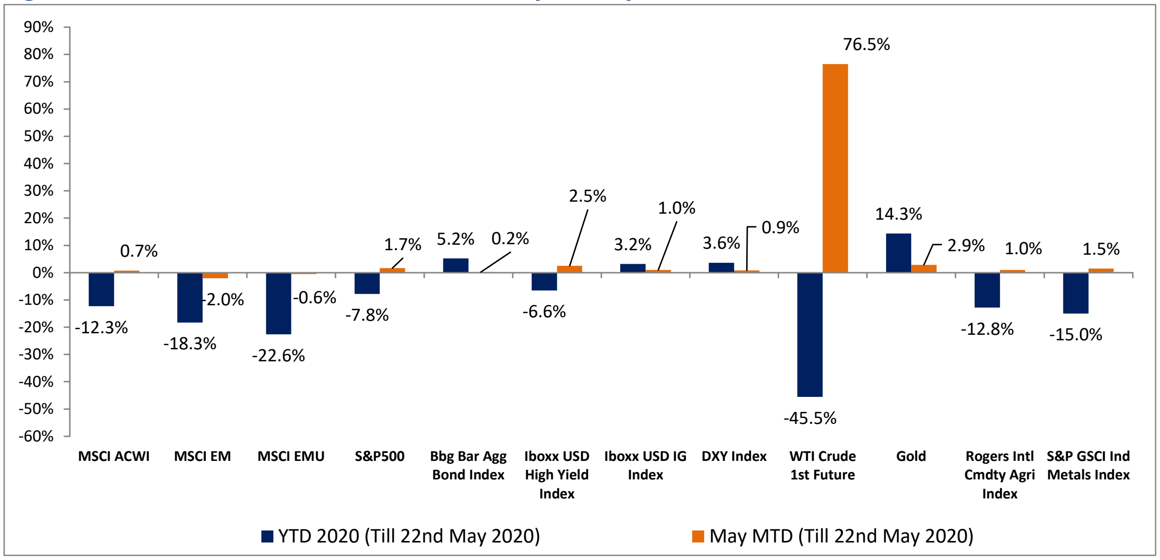
S&P500 Monthly Sector Performance – May MTD 2020*

Sectors	% Change	FY1 PE Ratio
Energy	-0.25%	NA
Materials	1.93%	22.7
Industrials	-0.83%	28.6
Cons Disc	2.78%	48.5
Cons Stap	-1.60%	20.0
Technology	5.34%	25.2
Healthcare	-0.30%	17.4
Financials	-3.90%	16.0
Utilities	-1.73%	17.6
Telecom	5.38%	22.3
Real Estate	-3.87%	43.5
S&P500	1.48%	23.7

*As of May 22nd, 2020

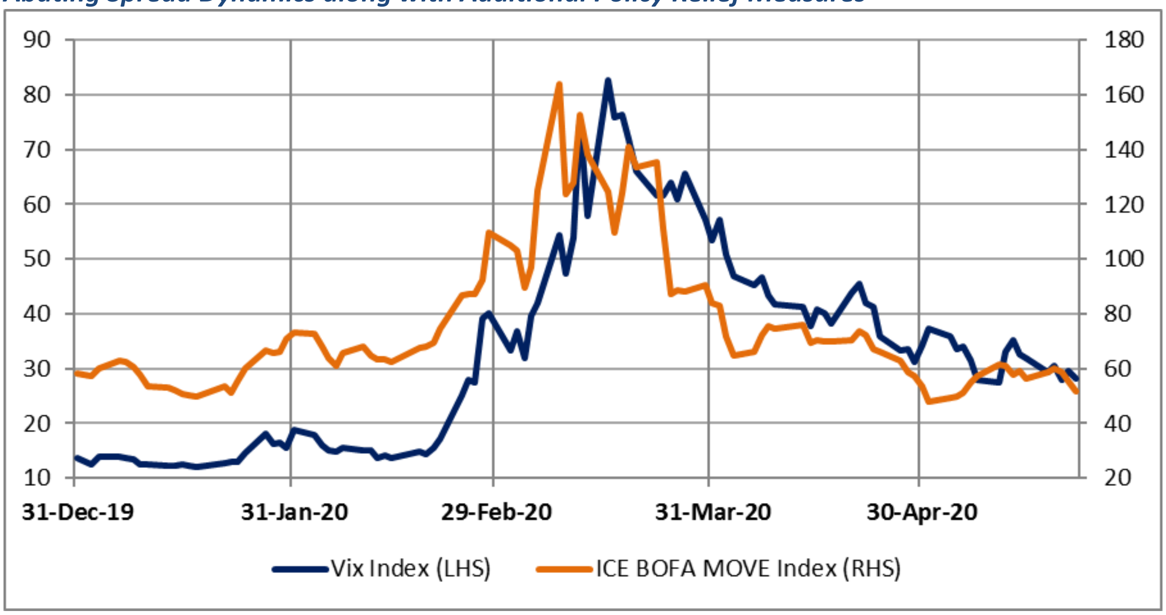
Source: Bloomberg

Figure 1. Risk Markets Post Uneven Recovery in May



Source: Bloomberg & Glovista Calculations

Figure 2. Equity and Bond Market Volatility Levels Decline Sharply in May, Fueled by Virus' Abating Spread Dynamics along with Additional Policy Relief Measures



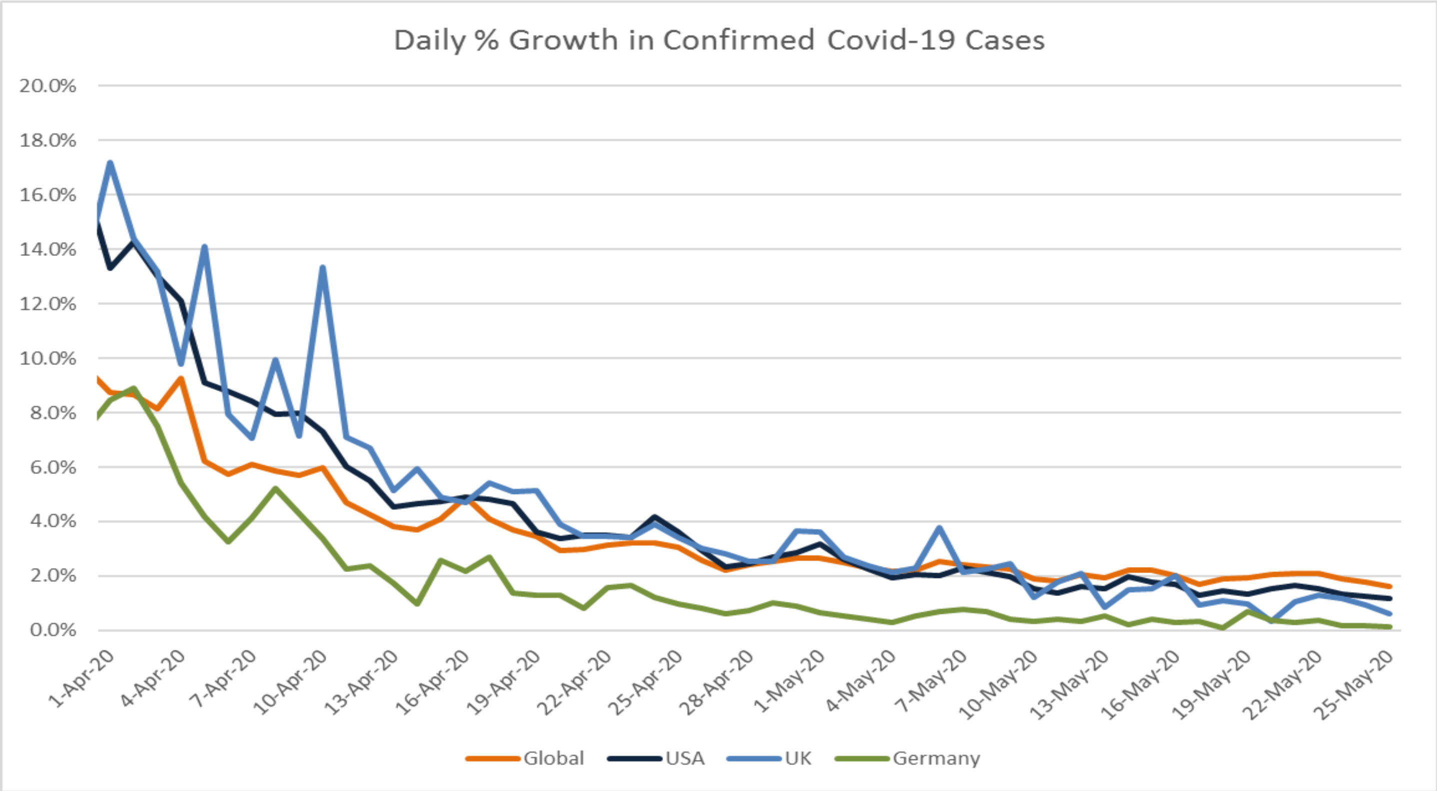
Source: Bloomberg

- US Federal Reserve leadership's explicit reiteration, at scheduled congressional testimonies by the US Federal Reserve Chair, of the Fed's version of former ECB President Draghi's "whatever it takes" stance;

- Chinese government's intensification of their infrastructure expenditure program in support of overall national economic activity.

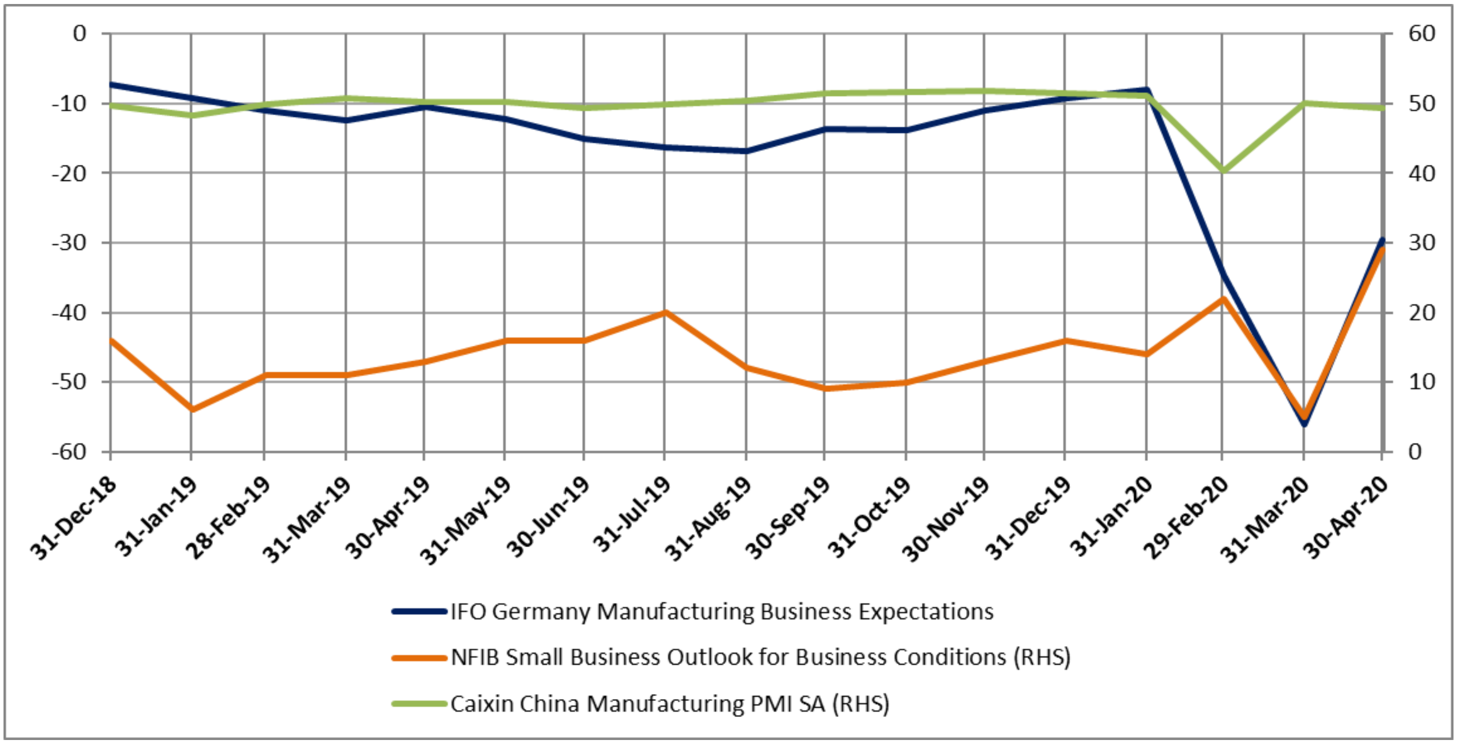
- Considerable abatement in the pace of the virus' new case infection curve across a large cross section of the world's major economic blocs, including the US, Eurozone and North Asia (Figure 3) along with and despite a growing pace of reopening phases being implemented across such regions in Europe and the USA since the end of April. The pace of recovery in economic activity has varied across countries. For example, Apple's mobility data shows US driving conditions currently hover a few percentage points above early January levels while walking conditions have close to recovered fully from the declines recorded since early January. However, transit traffic has recovered far more modestly from March and early April low levels. In Europe, the recovery to normalcy conditions has been far more significant in the core (Germany, Netherlands, France, for example) than in the periphery (especially Spain).

Figure 3. May Witnesses a Considerable Abatement in the Virus' New Case Infection Incidence Globally



Source: Bloomberg and Glovista Calculations

Figure 4. May Witnesses Upturn in Business Sentiment Indicators out of World's Largest Economic Blocs



Source: IFO Institute, National Federation of Independent Business & Markit

- Incipient upturn in business sentiment diffusion indicators out of several of the world's largest economic blocs (Figure 4).

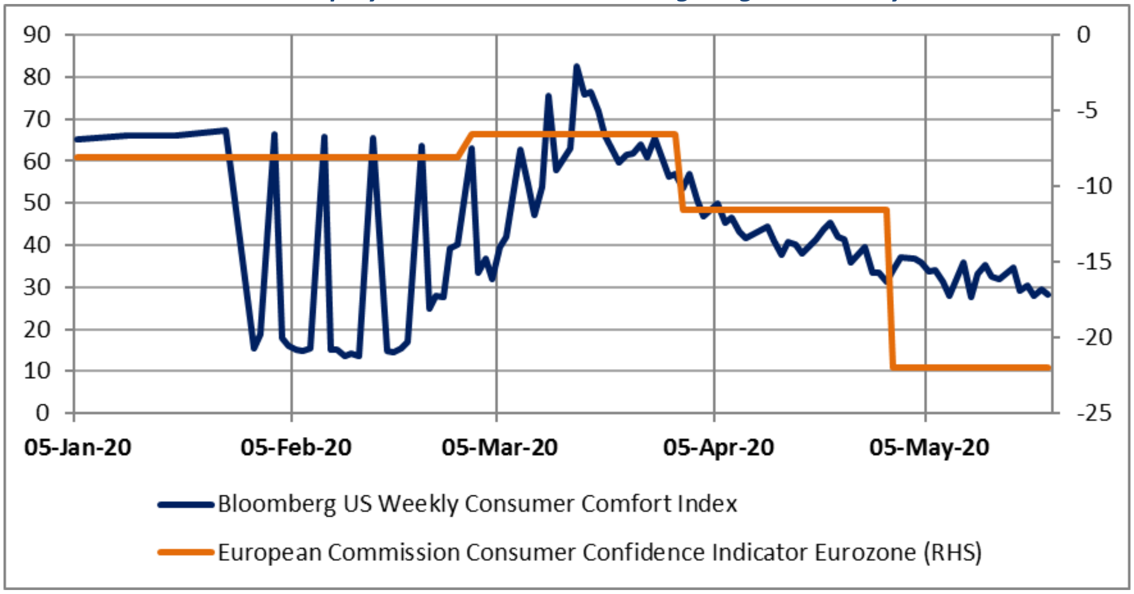
	May 22nd 2020	May MTD Change
Gold	1734.68	2.9%
Silver	17.2133	15.0%
Oil	33.25	76.5%
EUR	1.0901	-0.5%
JPY	107.64	-0.4%
GBP	1.2173	-3.3%
CHF	0.9712	-0.6%
CAD	1.3996	-0.4%
AUD	0.6537	0.4%
BRL	5.5334	-0.9 %
MXN	22.7324	6.0%

Source: Bloomberg

Rates	May 22nd Levels
1 Yr CD	0.61%
5 Yr CD	0.8%
30 Yr Jumbo Mortgage	3.72%
5/1 Jumbo Mortgage	3.06%
US Govt. 10 Year	0.6591%
10 Yr Swap Spread	0.00%

Source: Bloomberg

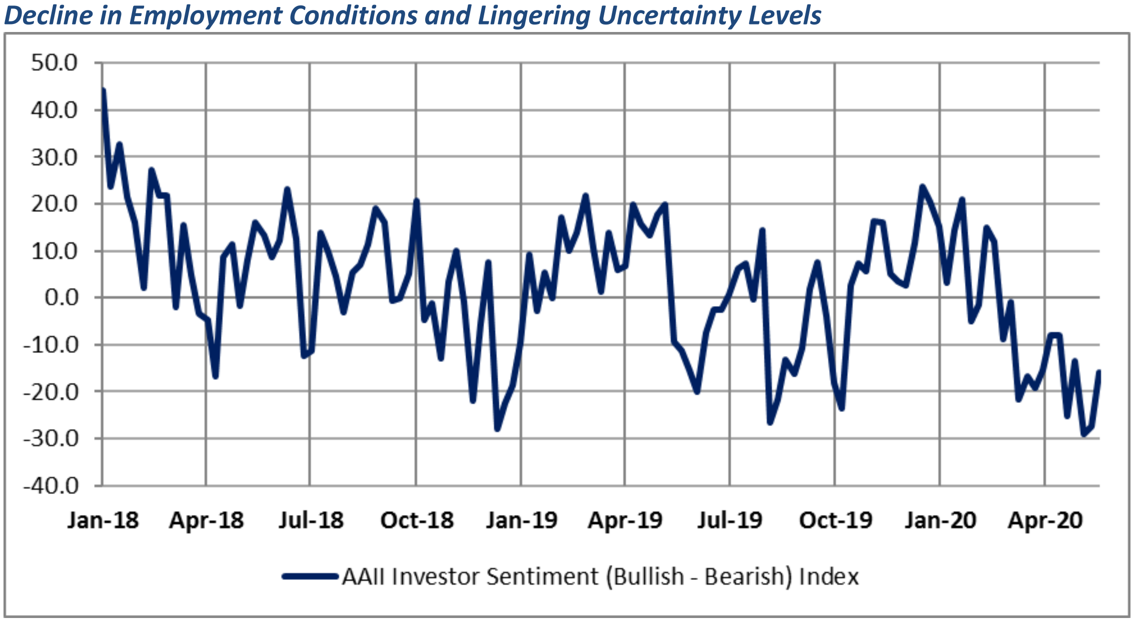
Figure 5. Consumer Sentiment Indicators Hover at Depressed Levels, Likely the Result of the Considerable Decline in Employment Conditions and Lingering Uncertainty Levels



Source: Bloomberg & European Commission

Despite the considerable bounce recorded in business sentiment indicators, the addition of new economic relief measures across a large number of major economies and the abatement of the virus' incidence across the world, consumer sentiment indicators continue to hover at depressed levels (Figure 5) along with continued elevated levels of investor risk aversion (Figure 6).

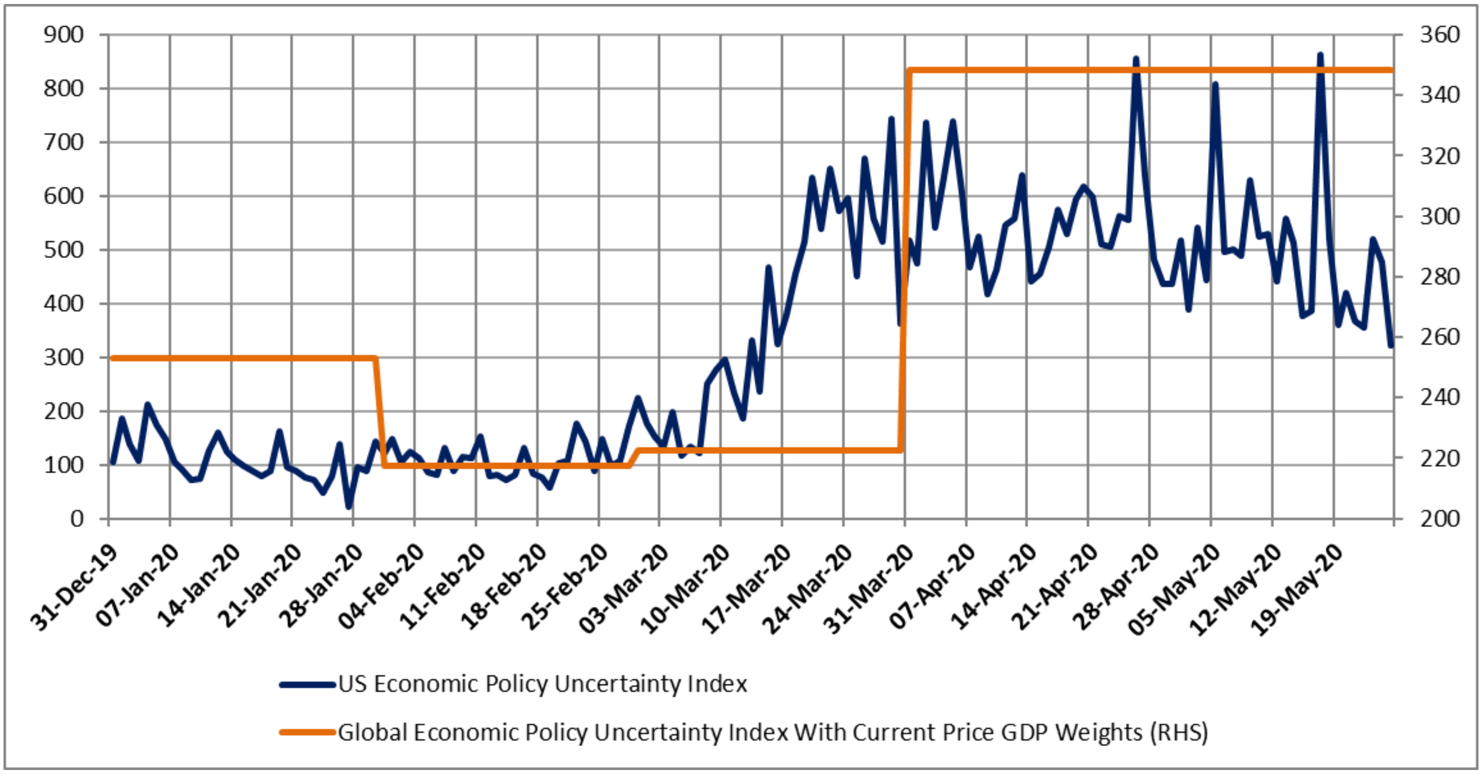
Figure 6. Investor Sentiment Remains Bearish, Likely the Reflection of the Considerable Decline in Employment Conditions and Lingering Uncertainty Levels



Source: AAII & Glovista Calculations

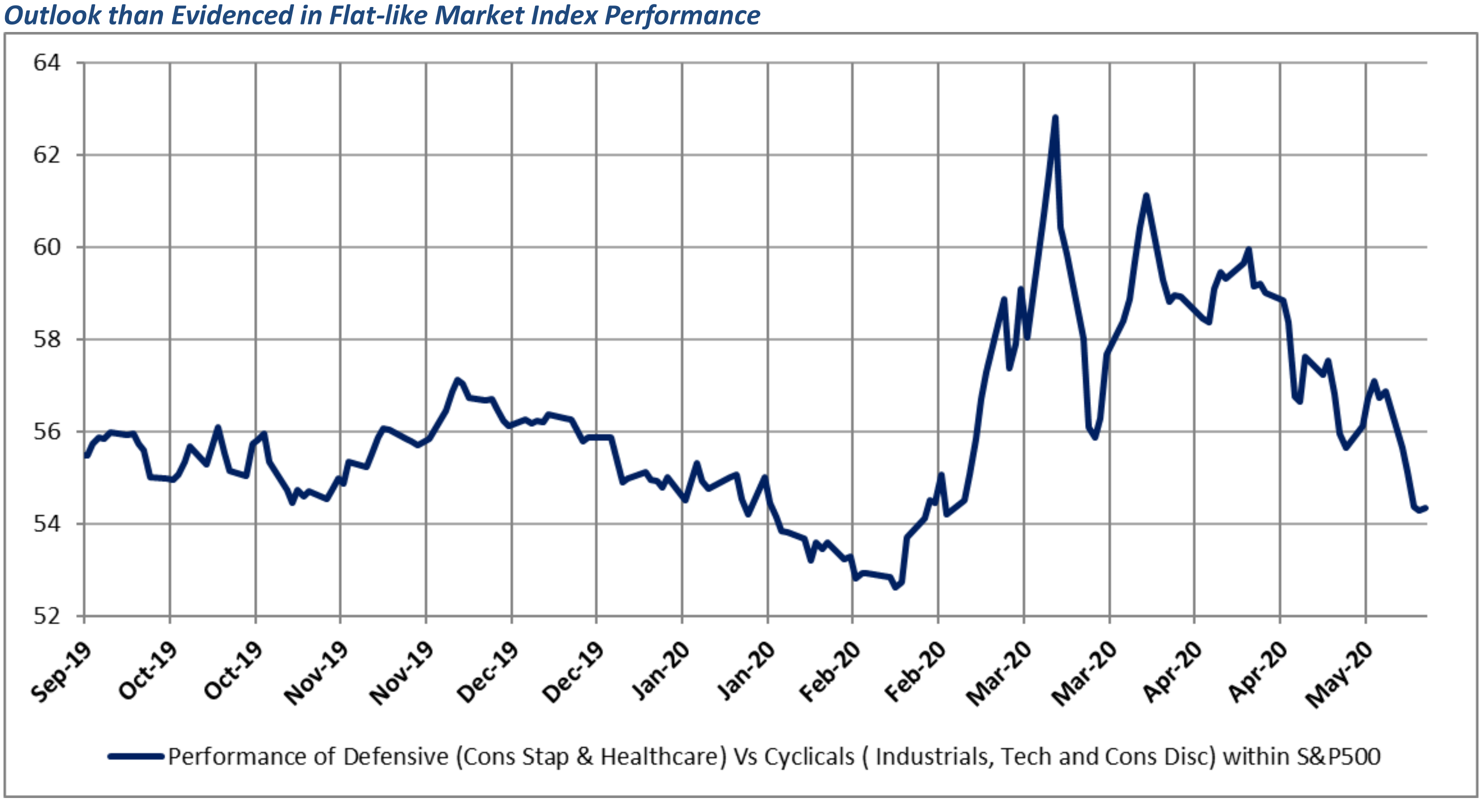
We attribute such lingering high levels of consumer sentiment and investor caution to (a) the unprecedentedly large order of magnitude and speed in the deterioration of employment conditions since March along with (b) uncertainty surrounding the outlook of policy direction later this year should a sizable second wave of viral infection crystalize. Figure 7 illustrates continued high levels of policy uncertainty both at the US and global levels.

Figure 7. Persistently High Levels of Investor Concerns Likely Reflect Lingering High Levels of Policy Uncertainty



Source: Baker Bloom & Davis

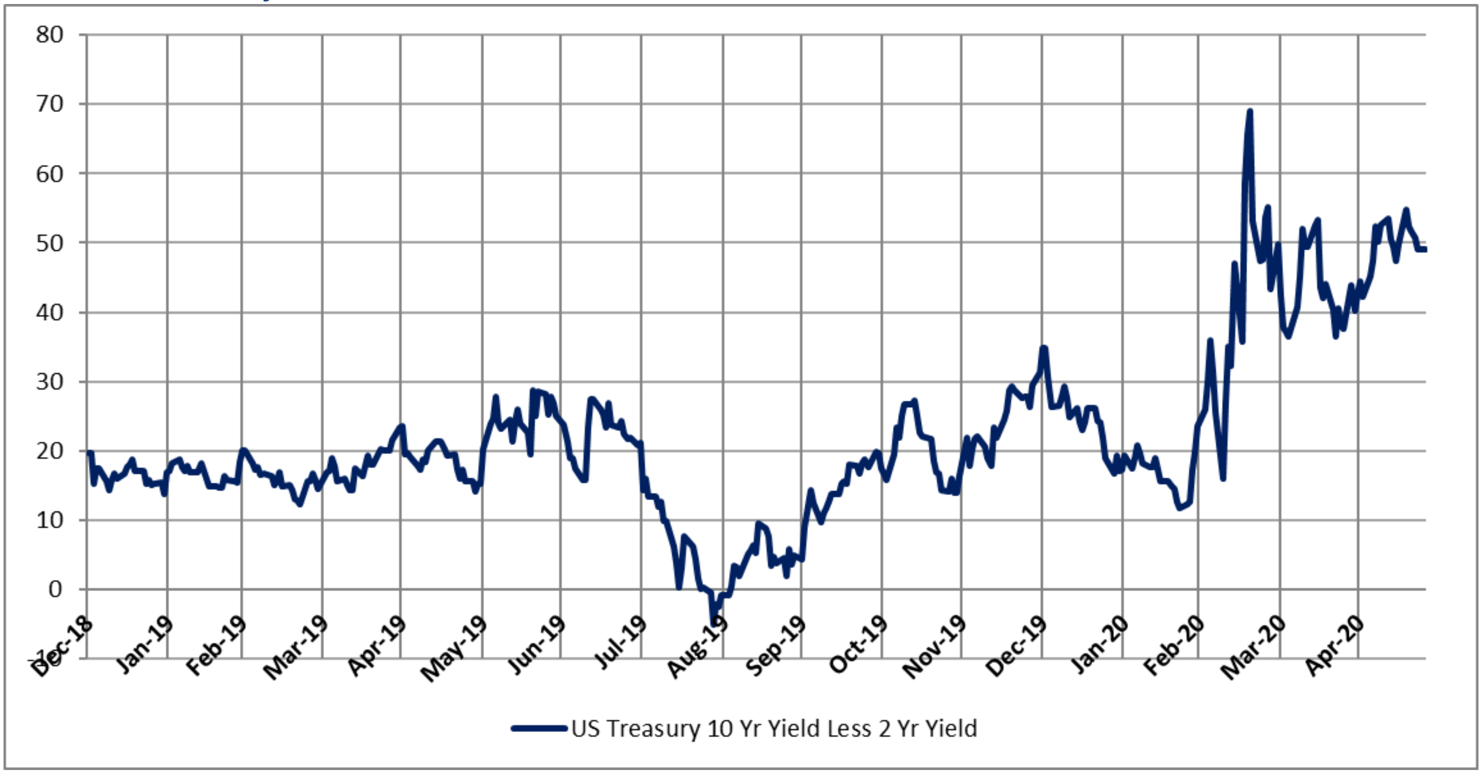
Figure 8. Cyclical Stocks' Performance Leadership Gains versus Defensive Peers throughout May Points to More Favorable Outlook than Evidenced in Flat-like Market Index Performance



Source: Bloomberg & Glovista Calculations

Despite continued high levels of investor and policy uncertainty, recent changes in global risk indices' internal dynamics illustrate a more constructive outlook for the investment outlook. For example, Figure 8 illustrates US defensive sector stocks' loss of performance leadership to cyclical peers throughout the month of May despite the flattish overall market index performance. Likewise, government yield curves have steepened moderately throughout the month of May, consistent with a thesis for impending economic recovery in the year's second half (Figure 9).

Figure 9. US Government Yield Curve Continues to Steepen in May, Likely a Reflection of Growth Recovery Expectations for the Year's Second Half



Source: Bloomberg

From a market technical perspective, continued high levels of investor caution represents a contrarian bullish signal as do the incipient signs of business sentiment levels. Consumer sentiment levels are understandably more likely to respond more gradually as non-economic factors tied to the virus' progression (including a possible second wave of infection this Fall) remain relevant over a longer time horizon. However, recent weeks have also brought about a new round of relief assistance measures to the business and consumer sectors from across a large number of countries, a supportive factor to the outlook. These policy developments, accompanied by the considerable abatement in the virus' incidence across the world, are helping lay the grounds for a strong recovery in the year's second half. Of course, the outlook is not without considerable risks.

These include the following, among several others:

- Potential shifts in consumer and enterprise behavior (a phenomenon called 'hysteresis', by economists);

- Policy uncertainty surrounding the response to a virus' second wave this Fall along with the longer-term implications (at the growth and inflation level) from the larger budget deficits (close to 20 percent of GDP at an annualized level for the US in 2020);

- Business behavioral implications stemming from governments' response to the pandemic – including a switch from 'just in time' inventory and manufacturing protocols to 'just in case' protocols that are likely to entail higher levels of resilience at the expense of lower efficiency level;

- Geopolitical implications, ranging from further escalation in US-China relations to heightened political tensions within the Eurozone on the back of the debate concerning the lack of an effective fiscal union.

In an upcoming monthly newsletter column, we will address the above listed risk factors in some detail. For the purposes of the current discussion, we will just state that such risk factors are likely to unfold in 'slow motion' and in ways that are likely to be offset – at least partially – through dynamics that may not be necessarily apparent.

Glovista Raises High Quality Stocks' Exposure and Underweight Bond Duration Given Investor Positioning, Renewed Policy Support and Virus Incidence

We continue to favor exposure to high quality stocks owing to our thesis calling for global economic recovery – reinforced by recent data releases and improved business sentiment indicators, discussed above - along with stocks' value attractiveness versus developed country fixed income. It is important to note that while stocks' valuations are not cheap on a 12-month forward basis, they are on a so-called: "second 12-month" basis, particularly versus fixed income. Such differentiation is important given the unusual, extraordinarily large and exogenous nature of the shock (virus) that brought about such monumental dislocations in asset prices. Moreover, the compression in nominal and real bond yields is likely to erode fixed income instruments' diversification allure within the traditional balanced (50-50 or risk parity) investment paradigm for years to come, thus highlighting the importance of a richer factor-based approach to global investment solutions, entailing higher equity exposure levels.

Emerging Markets Perspectives

EM Asia Stocks Lag Peer Group in May, Fueled by Rising Geopolitical US-China Tensions; Glovista Raised Latin America Regional Allocation on Tactical Basis

In May, Emerging Market stocks have performed approximately in line with their International Developed EAFE peers, recording a -2.03% month-to-date (MTD til 22nd May 2020) return performance versus -0.71% for their EAFE peers. Such modest underperformance has been heavily tilted towards Chinese and other North Asian regional stocks, fueled by two principal dynamics:

- profit-taking considerations following the growth-sector oriented Asia regional stocks' strong relative year-to-date outperformance versus their value-sector oriented peers in the Latin America and CEEMA regions, and;

- renewed geopolitical tensions between China and the USA, entailing a number of events that include:

    - US Secretary of State Pompeo's public statements earlier in the month in support of the Taiwanese president's successful reelection campaign;

    - escalating pressures on Hong Kong by the Beijing national government whereby China is set to introduce a new security legislation for Hong Kong which will enhance China's influence on the legal framework and enforcement mechanism on residents of Hong Kong , and; the US Trump administration and Senate's decision to pursue the passage of potential delisting from US exchanges of foreign securities (with a presumption such actions are aimed at Chinese issues) whose issuers do not comply with US standards for audit. In addition, the planned legislation will require the listed companies to reveal whether they are owned or controlled by a foreign government.

Over the past several weeks, the Glovista investment team cut its overweight China allocation to underweight on the back of our concern of escalating tensions between China and the USA as well as our expectation value-oriented markets that had lagged the benchmark over the course of the year would likely be supported by an improved outlook concerning the virus' diffusion globally. Specifically, over the past several weeks those US states as well as European countries that have reopened (albeit partially) their economies have not encountered a reversal in the sustained decline in the virus' infection rates. Moreover, as discussed above, the past several weeks have witnessed a further acceleration in relief measures out of Developed and Emerging Market economies (such as India on the fiscal side as well as a growing number of emerging market countries' central banks that have cut reference policy rates by larger orders of magnitude than expected by the consensus). Such developments are supportive of the global economic outlook – and thus of emerging market economies', particularly of value-oriented markets whose macroeconomic dynamics exhibit far higher betas to the global economic cycle.

As a result of the above, we have raised country-level exposures to Brazil, Mexico and India, funding such raises with cuts out of our China and South Korea country allocations. As we look ahead, we are likely to maintain a cautious outlook towards the Chinese equity market owing to factors impacting risk premium levels. We view such factors to retain some relevance as we approach the US November presidential election period. On a longer-term basis, within the value-oriented market segment, we continue to favor Russia and India as our top picks. Finally, from an asset class perspective, we continue to expect emerging market stocks to post solid return outperformance versus global peers on account of their under-owned status (further intensified by the large year-to-date outflows recorded by the asset class, in both the ETF and mutual fund space), undisputed relative valuation attractiveness and balance sheet strength, especially in the Asia Pacific region.

Disclaimers:

1. *This newsletter from Glovista is for information purposes only and this document should not be construed as an offer to sell or solicitation to buy, purchase or subscribe to any securities.*
2. *This document is for general information of Glovista clients. However, Glovista will not treat every recipient as client by virtue of their receiving this report.*
3. *This newsletter does not constitute a personal recommendation or take into account the particular investment objectives, financial situations, or needs of individual clients. The securities discussed in this document may not be suitable for all investors.*
4. *The price and value of investments referred to in this newsletter and the income arising from them are subject to market risks. Past performance is not a guide for future performance*
5. *Certain transactions including those involving futures, options, and other derivatives as well as non-investment grade securities give rise to substantial risk and are not suitable for all investors. Please ensure that you have read and understood the current risk disclosure documents before entering into any derivative transactions.*
6. *This newsletter has been prepared by Glovista based upon publicly available information and sources, believed to be reliable. Though utmost care has been taken to ensure its accuracy, no representation or warranty, express or implied, is made that it is accurate or complete.*
7. *The opinions expressed in this newsletter are subject to change without notice and Glovista is under no obligation to inform the clients when opinions or information in this report changes.*
8. *This newsletter or information contained herein does not constitute or purport to constitute investment advice and should not be reproduced, transmitted or published by the recipient. This document is for the use and consumption of the recipient only. This newsletter or any portion thereof may not be printed, sold or circulated or distributed without the written consent of Glovista.*
9. *Forward-looking statements in this newsletter are not predictions and may be subject to change without notice. Neither Glovista nor any of its directors, employees, agents or representatives shall be liable for any damages whether direct or indirect, incidental, special or consequential including lost revenue or lost profits that may arise from or in connection with the use of the information included in this newsletter.*

1 Evertrust Plaza Suite 1102
Jersey City NJ 07302
Tel: 212-336-1540
Website: www.glovista.net