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Glovista Global Perspectives

This Issue:

2020 Review and 2021 Year Ahead Outlook: Ending of Annus Horribilis to Give Way to Uneven Recovery and Further US$ Weakness; Glovista Favors High Quality, Value Oriented Exposures in Equities, Short Duration in Fixed Income and Precious Metals

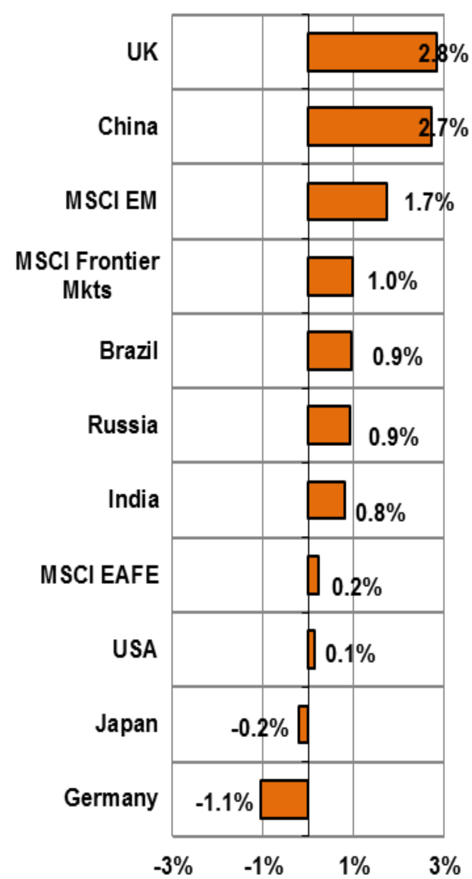
Without doubt, 2020 is guaranteed to go into the annals of history as one of the most traumatic years owing to the effects of the most expansive and synchronous global pandemic in recorded history. The 2020 pandemic has proved traumatic at the human, societal, economic, political and financial levels. Specifically:

- At the human level, the loss of life combined with the widespread disruption of activity has been among the largest and most traumatic in decades, including human suffering tied to social distancing (particularly in the elderly and chronically ill segments of the population). Other forms of suffering include diminished economic and mental wellbeing resulting from the considerable and possibly long-term loss in personal and business aspirations;

- At the societal level, the pandemic has disrupted large swaths of global service sector activity, particularly those entailing close interpersonal contact;

- At the economic level, outside unusually rare periods of depression in history, the pandemic has amounted to an unprecedented contraction in aggregate demand owing to the disruption in the demand for a large cross section of services, particularly in the discretionary space, the most obvious of which is tied to the leisure sector ecosystem. It is no accident that some of the most adversely impacted regions of the world and US economies include urban areas which, by nature, exhibit a disproportionately high representation of service industries;

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



Source: MSCI & Bloomberg

**As of December 24th, 2020*

GLOVISTA INVESTMENTS

S&P500 Monthly Sector Performance – December MTD 2020*

Sectors	% Change	FY1 PE Ratio
Energy	9.67%	NA
Materials	1.63%	27.1
Industrials	2.03%	42.2
Cons Disc	-0.12%	43.1
Cons Stap	0.21%	22.0
Technology	-1.38%	27.7
Healthcare	-0.81%	17.3
Financials	2.81%	17.7
Utilities	2.35%	19.2
Telecom	0.40%	24.9
Real Estate	0.82%	50.5
S&P500	0.38%	25.9

**As of December 24th, 2020*

Source: Bloomberg

- At the political level, the pandemic has brought out multiple episodes of unbrotherly, non-cooperative behavior including the hoarding of vaccines and PPE material as well as a lack of cooperative measures even within well established cooperative structures such as the Eurozone region. At this juncture, it is premature to ascertain the long-term nature and magnitude of the damage caused to the international order;

- At the financial level, the global pandemic challenged policymakers at a level unseen since the 2007-2009 Great Recession period. In particular, the much larger and broader magnitude of the collapse in global aggregate demand that unfolded in late February and March dwarfed the collapse in global trade flows in the late part of 2008, an event that helped bring about the introduction of unprecedented non-traditional monetary policy tools. In this occasion, the response of the world's largest central banks was even stronger, faster and broader than those enacted on the heels of the 2007-2009 crisis. Moreover, and as importantly, fiscal policy responses were considerably larger and broader at a global level, resulting in massive fiscal relief programs implemented by countries around the world, primarily developed.

Against the backdrop of such rare global calamity, the remainder of this column aims at providing a brief review of global macro and market developments in 2020 along with Glovista's principal global macro and investment thesis for the upcoming year, 2021.

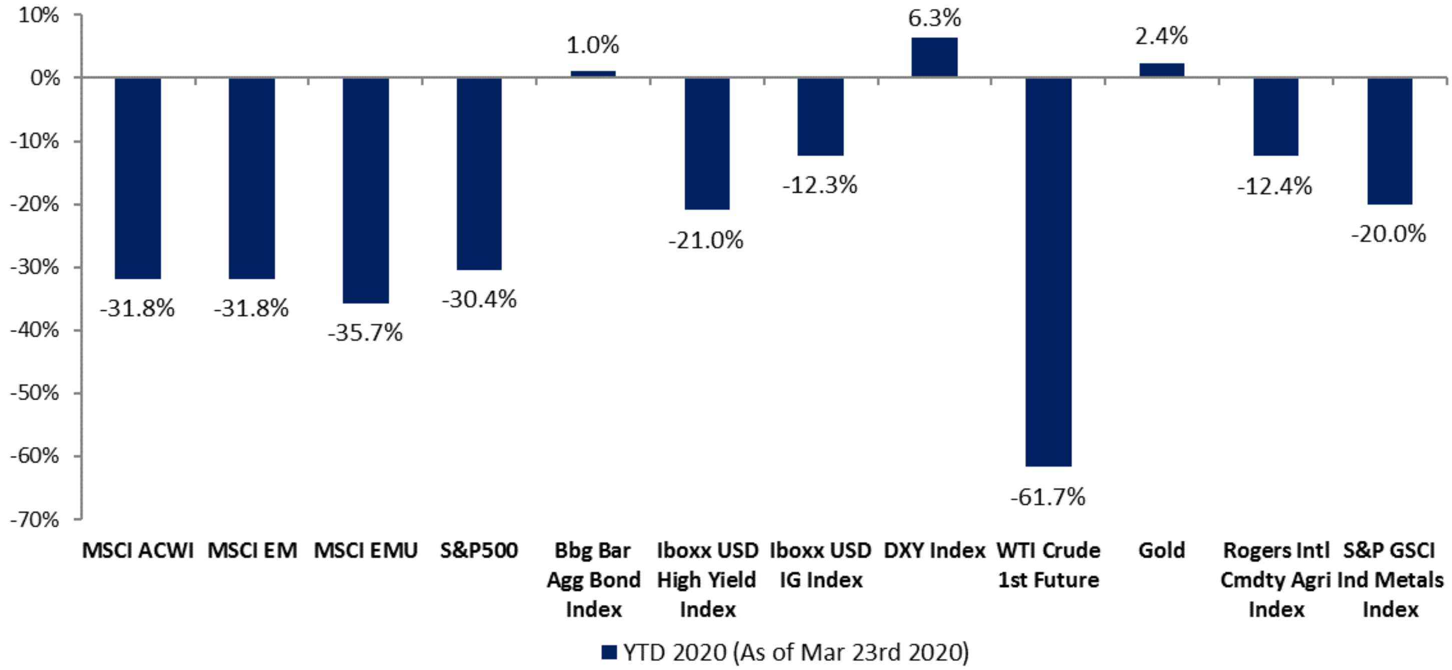
2020 Year Review: A Tale of Two Market Cycles - a Crash Fueled by Pandemic Driven Collapse in Demand followed by Sharp Bull Phase Anchored on Unprecedent Policy Support along with Fast and Effective Vaccine Development

A cursory review of this year's most salient global market developments leads to a "tale of two market cycles" account of 2020 in which the first cycle culminated in mid-March with the market trough reached by global risk indices following the sudden and outsized collapse in global aggregate demand set off by the pandemic's onset starting in late February. Figure 1 highlights the percentage declines recorded during that phase by some of the world's principal risk indices across the equities, credit and commodities domains.

In our view, the magnitude of the January-March declines in risk asset prices was well justified given then prevailing investor concerns surrounding the magnitude and duration of the collapse in aggregate demand resulting from the pandemic as well as the unprecedented nature of the accompanying uncertainty tied to such event. In addition, uncertainty surrounding the nature, magnitude and effectiveness of governments' policy response to an unprecedented shock added further impetus to the asset price declines via the corresponding spike in asset risk premium levels cutting across the equities and fixed income divides (Figure 2).

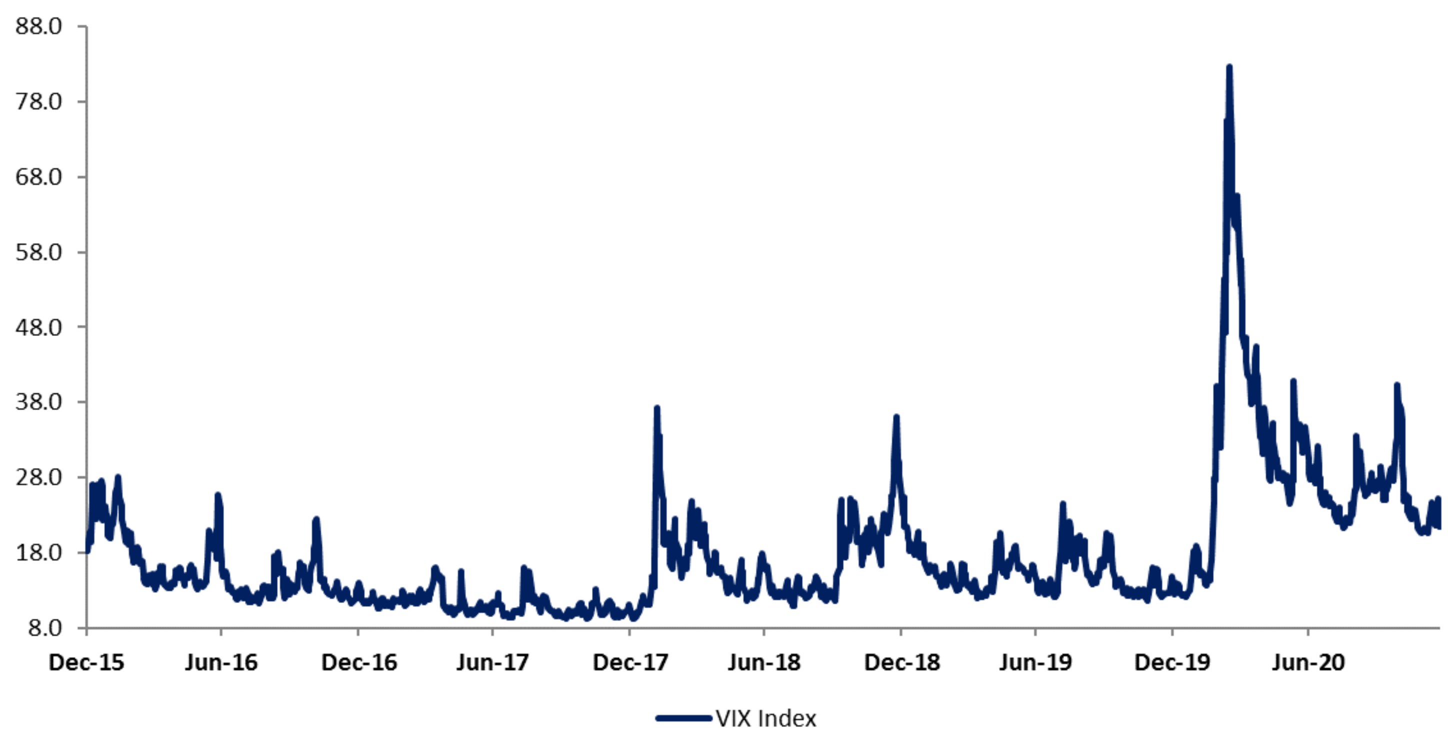
The sharp spike in investor concerns was further exacerbated by prevailing overbought conditions around mid-February, setting off reinforcing selling and hedging dynamics that were reflected across various financial indicators, such as the widening of equity volatility of volatility metrics to all time high levels (Figure 3).

Figure 1. Risk Markets' 2020 Crash Period's Return Performance: January 1-March 23



Source: Bloomberg and Glovista Calculations

Figure 2. Nature of Pandemic-fueled Shock to Global Demand Outlook Fueled Outsized Spike in Equity Risk Premium Levels: US Implied Risk (VIX)



Source: Bloomberg

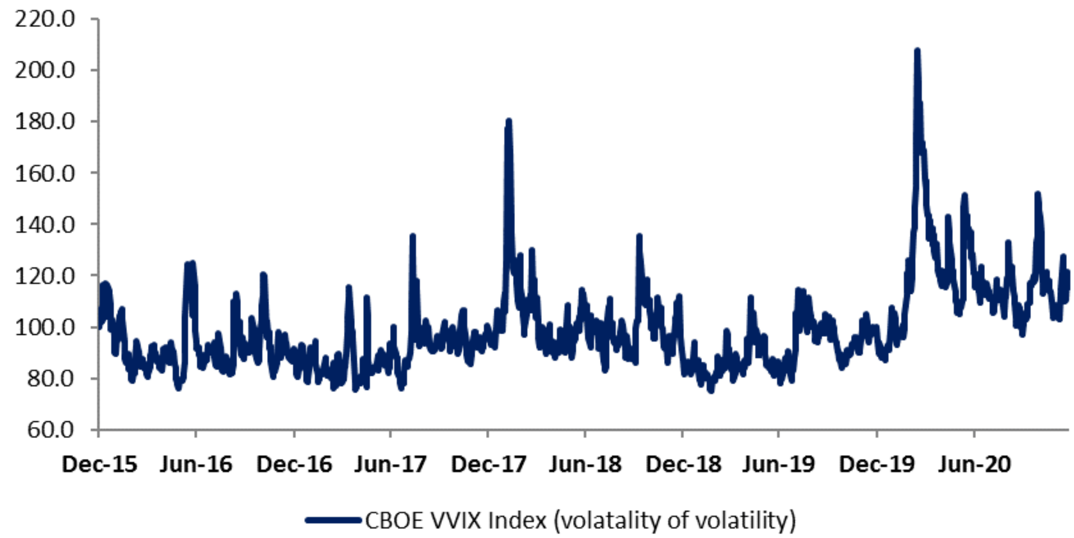
	December 24th 2020	December MTD Change
Gold	1807.59	1.7%
Silver	23.269	2.8%
Oil	44.91	-0.9%
EUR	1.1892	-0.3%
JPY	104.44	-0.1%
GBP	1.3357	0.3%
CHF	0.9113	-0.3%
CAD	1.2998	0.0%
AUD	0.7361	0.2%
BRL	5.375	-0.3%
MXN	20.0267	0.8%

Source: Bloomberg

Rates	December 24th Levels
1 Yr CD	0.39%
5 Yr CD	0.58%
30 Yr Jumbo Mortgage	2.97%
5/1 Jumbo Mortgage	2.8%
US Govt. 10 Year	0.88%
10 Yr Swap Spread	0.003%

Source: Bloomberg

Figure 3. Investor Concerns along with Overbought Conditions as of February Exacerbated Selling and Hedging Dynamics, as Revealed by Rise in Volatility of Equity Volatility to All Time High Levels



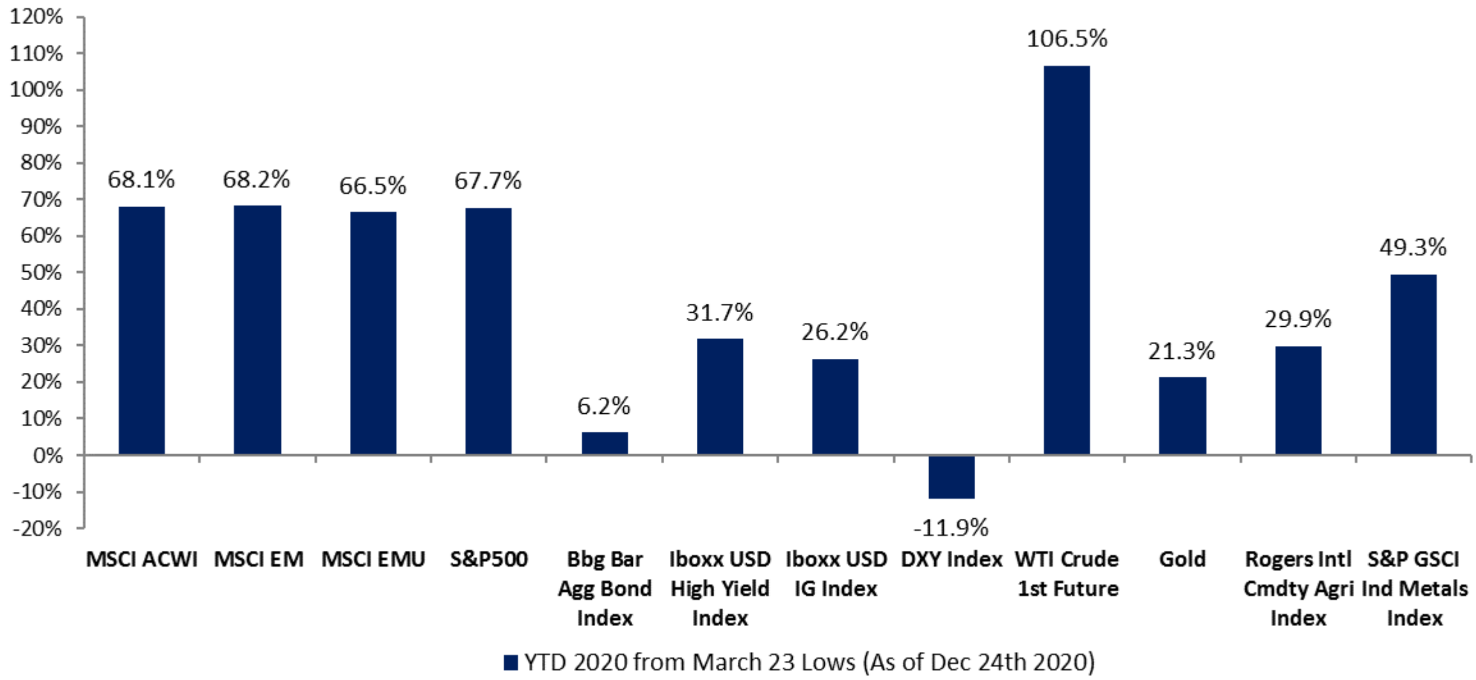
Source: Bloomberg

Happily for the global economy and world population, the speed, magnitude and breadth of governments' policy responses was unprecedently fast, large and wide. Arguably, recent memory from the similar, though far smaller, 'sudden stop'-like crisis that afflicted the world economy in 2007-2009 along with the unprecedented nature of the pandemic shock combined to produce such highly supportive government policy response around the world. As is well known, the array of government policy measures put forth in short order following the end February period in which the pandemic took hold included both monetary, fiscal and financial measures including outsized policy interest rate cuts, central banks' asset purchase programs, fiscal relief measures for firms and households, extension of massive swap and credit facilities between developed country central banks with counterparts in the developing world, among others. In some developed countries, annualized government budget deficits were allowed to expand to annualized levels to the tune of 30 percent of GDP. Such unprecedented government supports were commensurate with annualized GDP contractions recorded by some of the world's largest economic blocs (such as the USA and the Eurozone) during the second quarter of the year (of around 30 pct of GDP).

As the year progressed, the unprecedented contractions of economic activity during the second quarter gave way to outsized recoveries during the third quarter as governments sponsored a gradual reopening of their economies via the lifting of strict shutdown measures implemented during the second quarter. In the fourth quarter of the year, economic activity has continued to recover albeit at a significantly smaller pace as second infection waves have taken hold around the world, especially in the USA and Europe. As we look ahead to the first quarter of 2021, we expect a continuation of soft economic activity momentum owing to the persistently high infection levels in the USA and parts of Europe that are likely to remain elevated as the northern hemisphere's winter season progresses.

Notwithstanding the moderation of economic recovery in the fourth quarter of 2020 and the likelihood of continued softness in the first quarter of 2021, financial markets have been well supported during the fourth quarter, particularly in November and December owing to two principal developments that unfolded in the month of November: US general election results, likely to result in divided government (historically the most investor friendly political power configuration) and the surprisingly positive developments concerning the availability of highly efficacious vaccines (including Pfizer's and Moderna's) that have begun to be admitted to the general public starting in December.

Figure 4. Risk Markets' Sharp and Sustained Recovery since March Low Levels Reflect the Economic Recovery fueled by Unprecedented Government Policy Responses and Vaccine Developments



Source: Bloomberg & Glovista Calculations

Against the above mentioned backdrop, the sharp third and fourth quarter government-led economic recovery that ensued the onset of the pandemic along with the highly encouraging developments concerning the availability of efficacious vaccines have combined to put forth a sustained, outsized recovery in asset prices since the March low levels. As is typical during early cycle economic recoveries, risk premium levels have come down sharply during this period on account of the visibility afforded by the magnitude and breadth of economic relief measures but also reinforced by the unprecedented size of central banks' asset purchase programs (especially in the USA and Europe) that have encompassed a significant number of asset groups previously excluded from central banks' ownership mandates. Figure 5 illustrates the sharp compression in risk premium levels for equities and credit throughout the year.

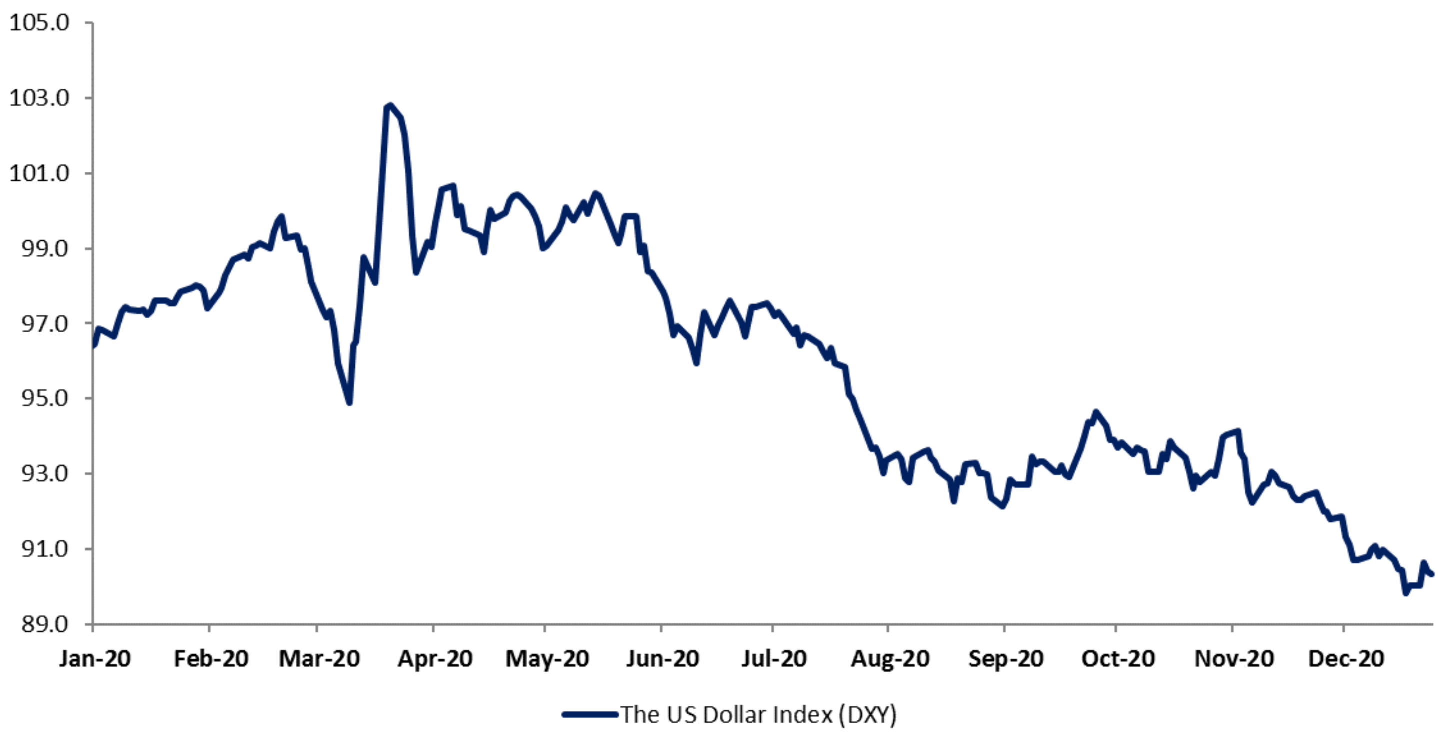
Developed country central banks' policy responses have resulted in exceedingly potent positive feedback effects on global liquidity and economic recovery dynamics on account of the combined effects from the following:

- *Weaker US Dollar:* vastly lower policy interest rates in the developed world (and the promise to keep rates low over at least the next two years) carry unambiguously bearish implications on the US Dollar, a dynamic that carries benign risk market implications at the global level given the reflationary effects accruing the global economy from a weaker US Dollar (Figure 6 and Figure 7). Beyond its favorable reflationary effects at a global level, a weaker US Dollar also impacts positively global economic growth dynamics given the outsized level of US Dollar denominated liabilities in the rest of the world as well as the higher consumption propensity in the developing world versus the US;

Figure 5. Asset Risk Premium Levels Compressed Sharply since March on the Back of Vastly Increased Visibility of Economic Recovery, Fueled by Government Policies

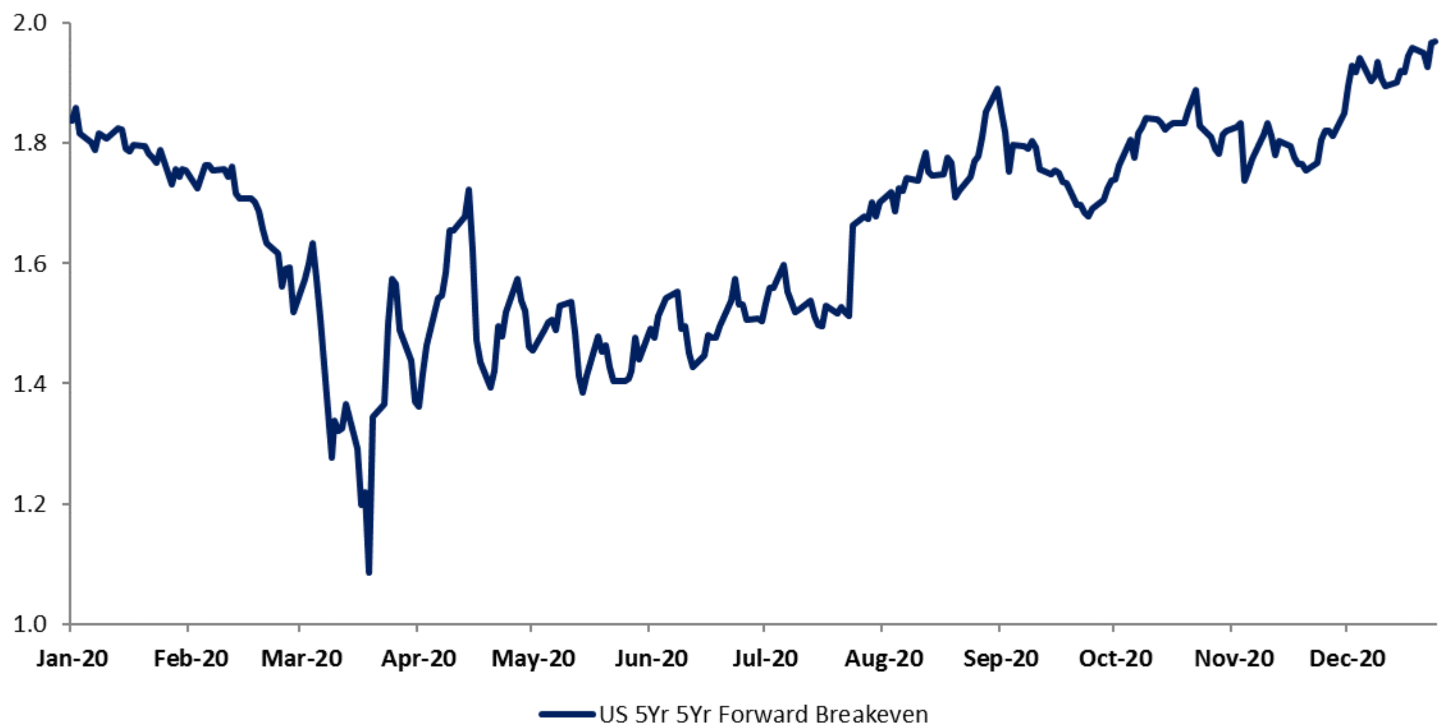
Source: Bloomberg

Figure 6. US Dollar Records Broad-based Weakening versus Most Global Peers, fueled by Exceedingly Accommodating US FED Policy and Strengthening Economic Cycle in 2020H2



Source: Bloomberg

Figure 7. US Medium-Term Inflation Expectations Record Sustained Recovery over the Course of 2020 as G3 Central Banks Implement Massive Expansionary Programs



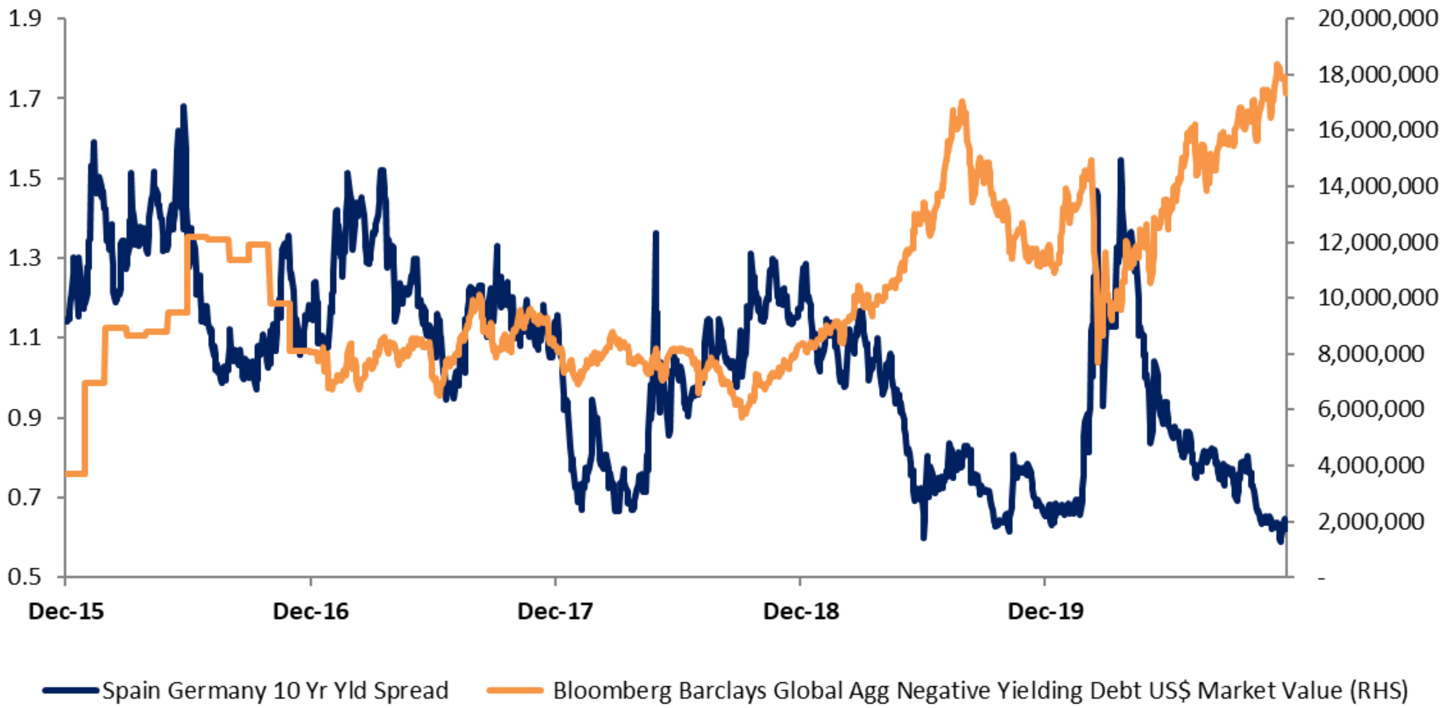
Source: Bloomberg

- *Central Banks' Direct Targeting of Lower Asset Risk Premium Levels*: Since the onset of the pandemic, developed country central banks (especially the US FED) have targeted explicitly the reduction of asset risk premium levels via the inclusion of junk rated securities within their vastly enlarged asset purchase programs. In that vein, it is no accident that asset risk premium levels have undergone massive compressions since their March peak levels (Figure 5). In turn, such compression of credit and other asset risk premium levels across the developed world have exerted powerful knock-on effects at a global level in the form of sustained reduction of yield levels around the developing world, including in certain pockets of global markets with questionable creditworthiness – both at the sovereign and corporate levels and both in developed and emerging economies (Figure 8).

Over the course of the year, the asset price recovery process has been led by growth sectors (especially so-called 'stay at home' sectors, such as technology stocks) on account of the lingering (until early November) uncertainty surrounding the potential availability of efficacious vaccines. Such virus specific risk factors accounted for the massive explosion in relative valuation premium commanded by growth stocks versus value peers during the period ending in early November, precisely the time when Pfizer and Moderna publicly released exceedingly favorable results of their phase 3 tests. Thus, it is no accident that growth stocks reached peak relative return performance versus value peers in early November (Figure 9).

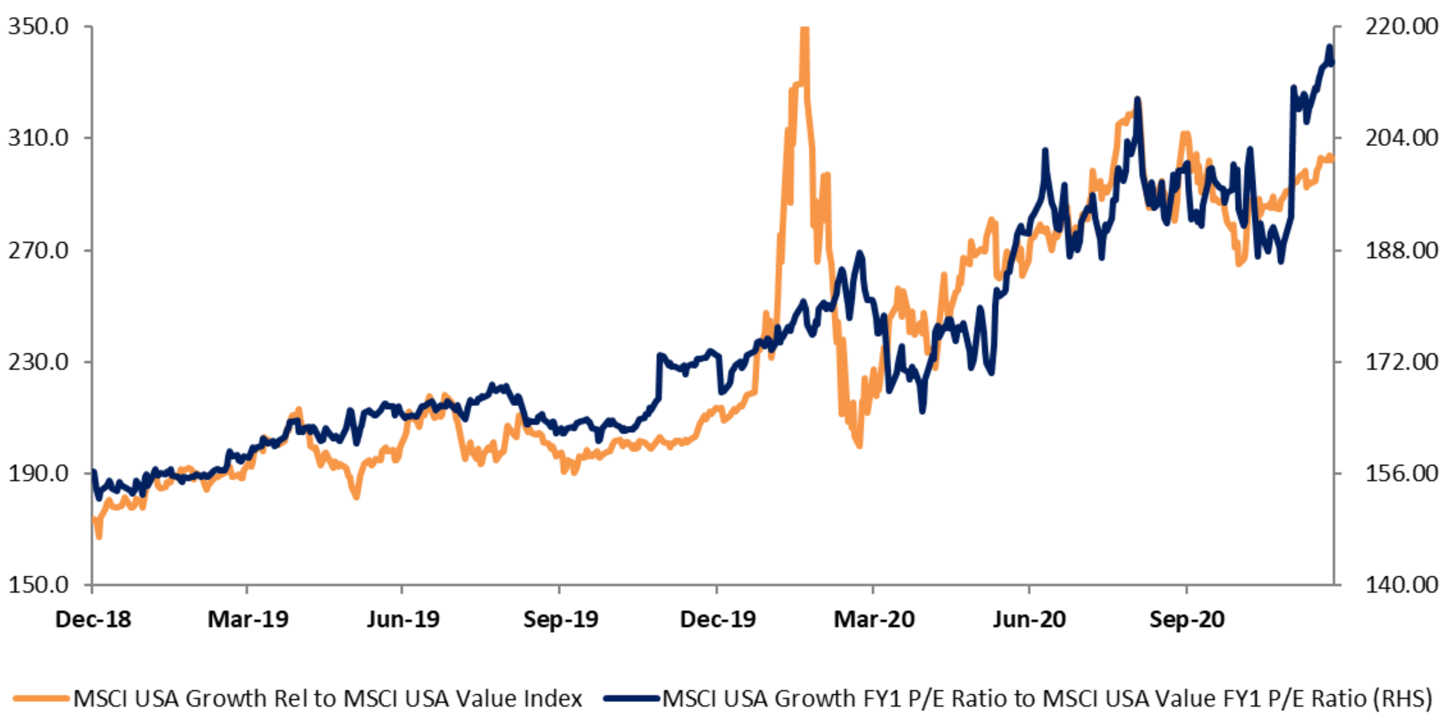
Interestingly, the above-mentioned dynamics conditioning the relative return performance between US growth and value sectors throughout 2020 were also present at a global level. For example, value sector heavy stock indices (primarily those in Europe) recorded a sharp return performance reversal versus growth sector heavy indices (primarily those in the USA) around the same period in November (Figure 10).

Figure 8. Exceedingly Abundant Global Liquidity Conditions Fuel Low Differentiation Across Significantly Different Segments of Global Markets and a Greater Proportion of Negative Yielding Bonds



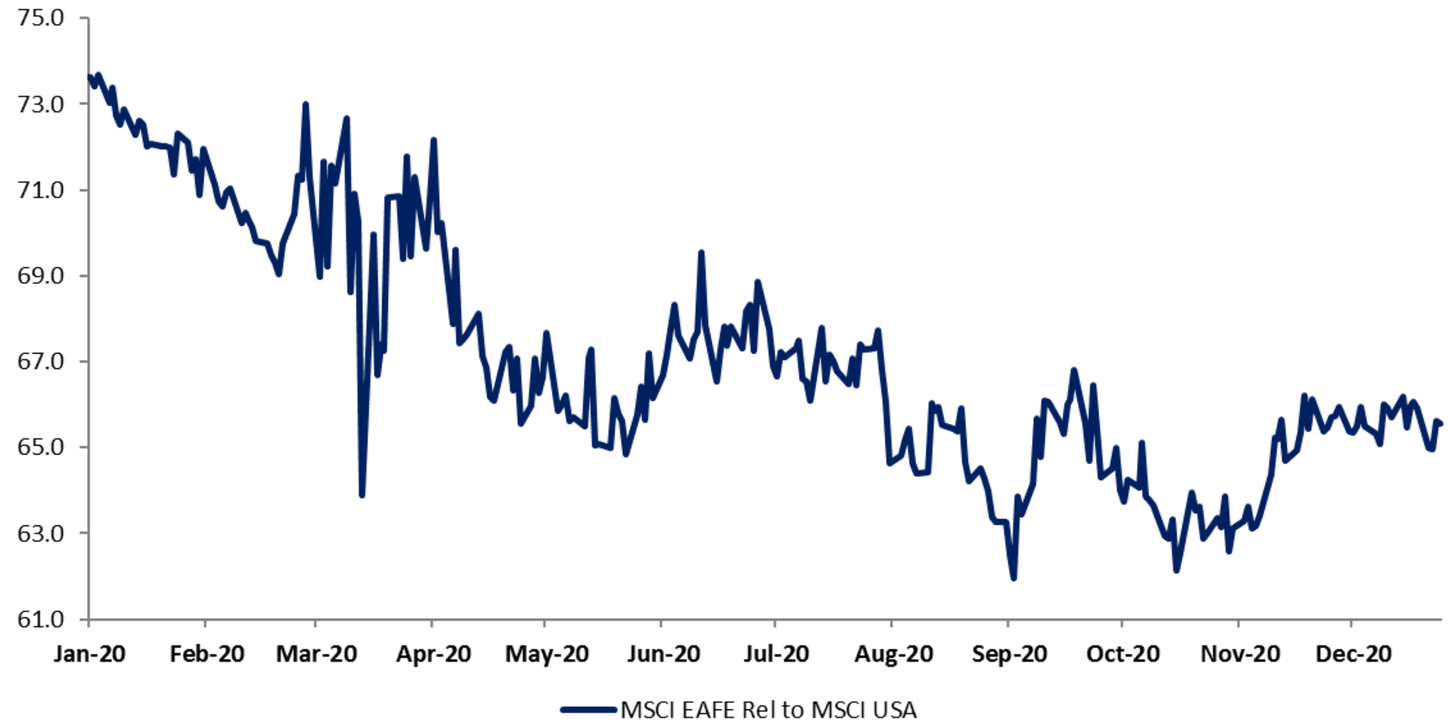
Source: MSCI, Bloomberg and Glovista Calculations

Figure 9. Vaccine Availability and Efficacy Uncertainty Factors Propelled Growth Assets' Relative Valuations to Exceedingly High Levels versus Value Peers Til the Release of Pfizer's and Moderna's Encouraging Phase 3 Vaccine Test Results



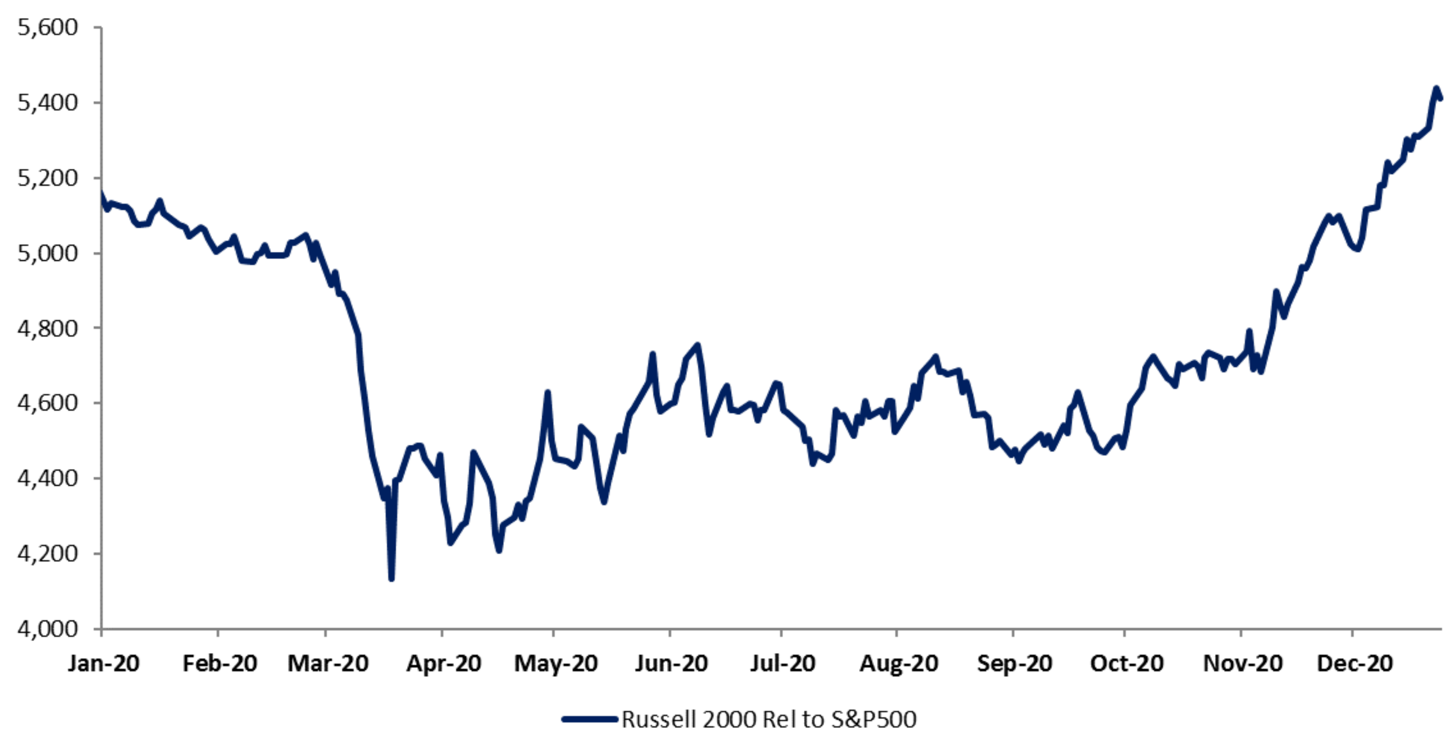
Source: MSCI, Bloomberg and Glovista Calculations

Figure 10. EAFE Stocks - Predominantly Value Sector Oriented - Record Similarly Timed Performance Reversal versus US Stocks - Predominantly Growth Sector Oriented - Around the November Period, Likely Reflecting the Expectational Effect from November Vaccine Test Results



Source: MSCI, Bloomberg & Glovista Calculations

Figure 11. US Large Cap Stocks' Strong Outperformance Leadership versus Small Cap Peers Reverses in October/November Period as Markets Discount More Heavily a Higher Tax Regime and Faster Return to Normal Conditions, Triggered by Democrats' November Win and November Vaccine Announcements, respectively.

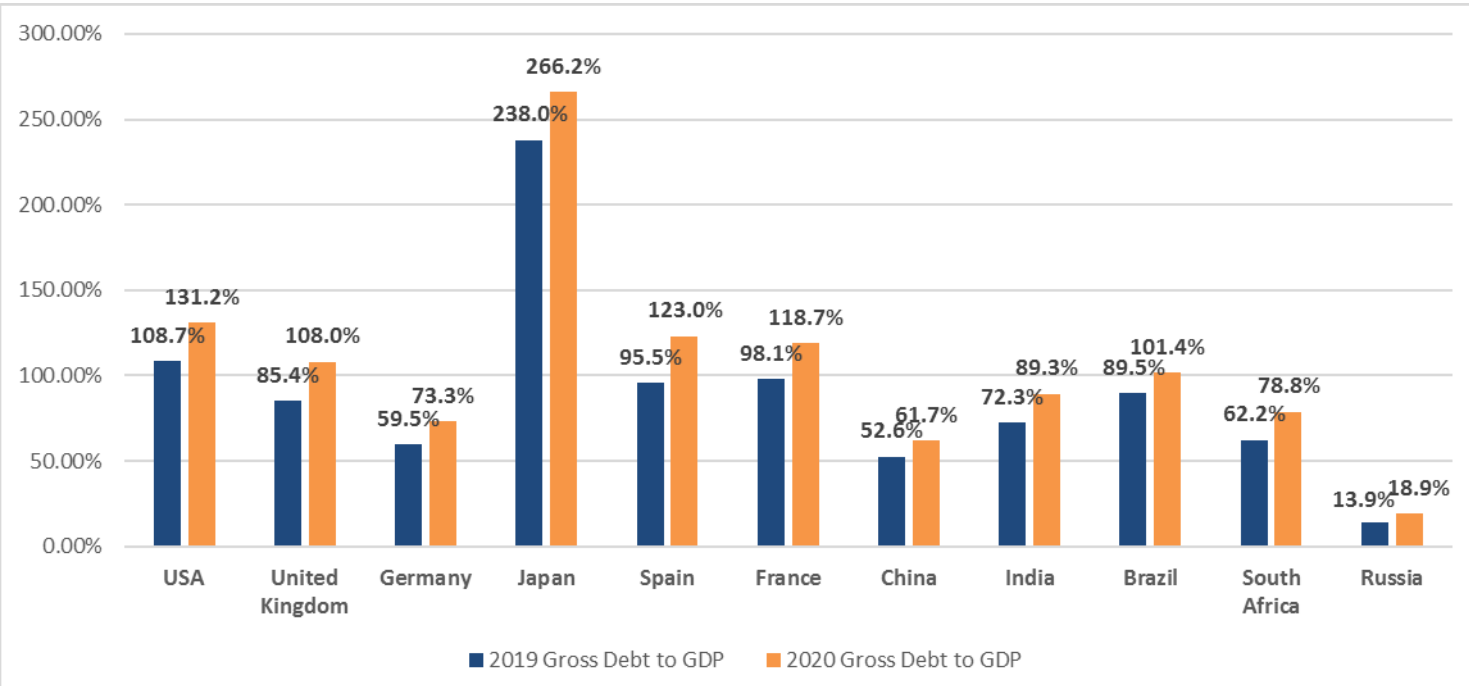


Source: MSCI, Bloomberg & Glovista Calculations

Another important dynamic taking hold throughout 2020 is found in the relative return performance between large and small capitalization stocks. Specifically, large cap stocks held strong relative performance leadership versus small cap peers throughout much of 2020, till the October/November period. Since then, small cap stocks have commanded one of the sharpest relative outperformance periods in recorded history (Figure 11).

Of course, one of the most significant legacy effects from the unprecedented government policy responses implemented in 2020 is given by the outsized growth of public debt levels, particularly around the developed world where the magnitude of fiscal relief packages was most extreme (Figure 12).

Figure 12. Major Legacy Effect from Government Responses to 2020 Pandemic: Deterioration of Public Indebtedness Levels



Source: IMF

Economic history reminds us that sharp spikes in public indebtedness levels carry adverse growth implications over the medium- and long-term, absent the presence of highly favorable productivity shocks that can serve as powerful compensating factors. As importantly, a cursory look at the current juncture in economic history leads to the identification of several factors that reinforce the adverse growth implications stemming from the increased public debt levels currently ailing the world. Such factors include:

- the ageing of the population;

- current low nominal and real (inflation adjusted) interest rate levels. For example, that nominal policy interest rates hover at or exceedingly close to the zero lower bound in the developed world implies the presence of asymmetrically large fiscal risks that could unfold under normalized interest rate scenarios in the years ahead;

- the ascendancy of nationalism and anti-globalization forces around the world. In that regard, it is important to remember that between 1990 and 2010 much of world economic growth was propelled by international trade growth. To the extent to which international trade of goods and services turns from a growth contributor to growth detractor, the hurdle facing global economic growth is even higher;

- Undoubtedly, the global pandemic has led to the acceleration in the behavioral disposition, rate and breadth of adoption of new labor-saving (e.g. virtualization, digitization, automation, genomics, among others) technologies – impacting the logistics, commerce, medical, financial, education service domains. Economic history reminds us that such rate of technological innovation is most likely to prove welfare enhancing over the long-term while the transitional welfare and economic costs could prove significant, with considerable implications at the economic growth, geopolitical and social levels.

<u>2021 Year Outlook</u>: Solid Second Half Recovery Awaits Challenging First Quarter; Glovista Favors High Quality Value Oriented Equities and Short Bond Duration Tilts; US$ Likely to Weaken Further

As we look ahead to 2021, we expect the sustained yet gradual broadening of Covid vaccine applications throughout the world to fuel a sustained cyclical economic recovery at the global level. However, we expect such dynamics to take hold starting in the year's second half. We hold a more cautionary short-term outlook on the global economy, encompassing the year's first quarter and possibly part of the second quarter, on account of two principal dynamics:

- Adverse fiscal impulse factor impacting much of the developed world on account of the sequential withdrawal of fiscal relief measures. Such dynamic amounts to fiscal tightening with adverse economic growth implications, especially at a juncture in which much of the developed world is being adversely impacted by a powerful second Covid infection wave;

- Troubling infection dynamics plaguing much of the developed world on account of the ongoing second virus infection wave along with increased confirmation of a notably more infectious strain is taking hold across a growing number of countries. Such state of affairs is likely to translate into more drastic shutdown measures by governments around the world in the short-term.

Against the above-mentioned considerations, Glovista is positioning its global portfolios with a high-quality factor (defensive) tilt as we enter 2021, possibly a contrarian investor opinion as of the publication of this report. However, we maintain a bullish outlook towards equities over the balance of the year on account of our macro thesis calling for recovery – particularly in the year's second half – and equities' highly attractive valuations versus fixed income. Glovista continues to embrace the view that fixed income remains an unattractive asset class over the long term on account of its lack of value given alternate asset classes, including equities, real estate and non-US $ currencies, particularly given our baseline case of no global recession in 2021.

Within global equities, we enter 2021 with a balanced style exposure across the growth-value divide following value stocks' exceedingly strong Q4 relative performance along with Glovista's cautious outlook for 2021 Q1. We foresee rebalancing our equities portfolio over the course of the first half in favor of value-oriented sectors. In the international arena, we favor emerging market equities over EAFE on account of relative valuations, earnings and top line revenue growth performance outlooks as well as North Asia's dominant presence in EM, arguably the world's least virus impacted region. We discuss further below our EM equities outlook in greater detail.

Within the fixed income market domain, we favor short duration exposures given our constructive 2021 world economic outlook baseline case as well as current depressed bond term premium levels. Within the credit space, we favor a barbell exposure to short-term Treasury securities and senior loans along with US financial sector credit. In the commodities space, we continue to favor precious metals (especially gold and silver) on account of their sound diversification gains within a global balanced portfolio as well as favorable investor positioning.

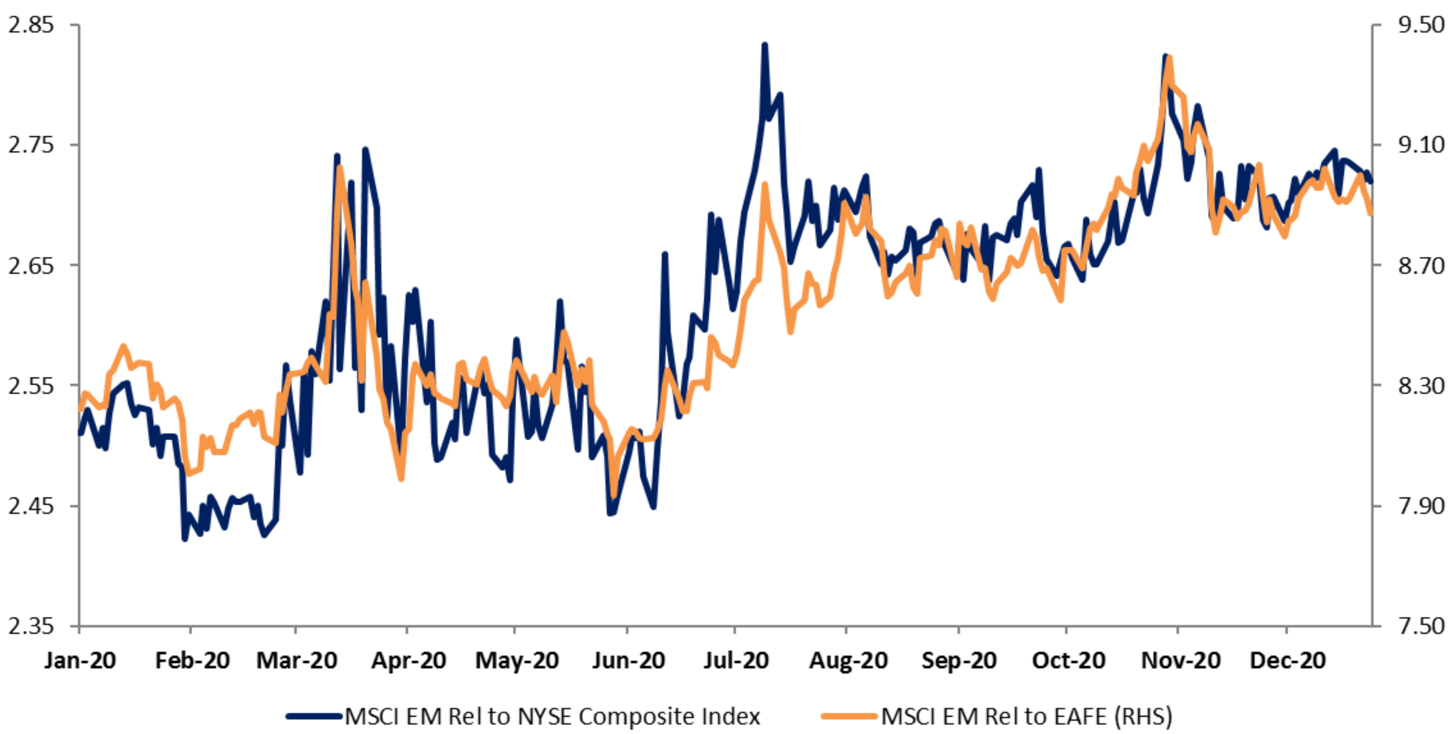
Of course, no outlook is bereft of risks. In that regard, we identify the following as the principal downside risk factors conditioning the 2021 outlook: adverse US investor fiscal expectations following a potential Democrats' win of the two Georgia senatorial seats at the upcoming January 5th run-off elections; unexpected unhinging of inflation expectations; unexpected credit shocks out of the Eurozone's periphery or the financial system; adverse geopolitical events (e.g. North Korea, Iran, Russia, China); policy mistakes by fiscal or monetary authorities; unexpected shifts in consumer behavioral patterns; exacerbated consumer or investment responses to de facto fiscal tightening likely to unfold in 2021.

Emerging Markets Perspectives

In 2021, EM Equities Look Poised to Extend Outperformance versus DM Peers on Blue Sky Valuation, Cyclical, US$ Cycle and Ownership Conditions; Value Oriented Markets Likely to Outperform

In 2020, emerging market equities have outperformed broad US and international non-US developed equity peers (EAFE) despite the onset of one of the most vicious volatility spikes in modern financial and economic history (Figure 13). That the EM asset class managed to post such solid return outperformance against such global shock backdrop and in the presence of lingering geopolitical tensions between the USA and the EM asset class' largest country constituent (China) speaks loudly to the asset class' solid fundamentals, attractive valuations and favorable investor ownership position.

Figure 13. EM Equities Post Solid Return Outperformance versus Broad-based US and EAFE Benchmarks in 2020, despite Global Pandemic Shock and Lingering USA-China Tensions



Source: Bloomberg

We credit the EM equities' asset class 2020 resilient return outperformance versus developed peers to the strength of the asset class' fundamentals, including the EM benchmark's heavy domestic demand sector and North Asia regional representations. In 2020, such traits proved highly accretive to return performance owing to technology sectors' considerably smaller sensitivity to government dictated shutdown measures while North Asian countries' stellar management of the pandemic translated into considerably shallower mid-year regional economic contractions than for most other economies around the world, resulting in far more resilient revenue and earnings growth recoveries in the year's second half.

The EM asset class' resilience in the face of the pandemic along with EM Asian economies' strong macro balance sheets paved the way to a number of favorable reinforcing dynamics on the asset class' 2020 performance, most notably with regard to currency revaluation of the Renminbi. Specifically, as the US and European central banks implemented aggressive policy rate cuts throughout the year, interest rate differentials with China's Renminbi turned highly supportive of US Dollar weakness versus China's currency. Accompanying such supportive yield differential backdrop on EM currencies was the sustained decline in GDP and financial volatility throughout the year, starting in the March market low period. Said process of US Dollar weakness versus EM currencies extended beyond the Renminbi to encompass a growing number of EM currencies (Figure 14). In the process, the EM currency revaluation process helped set off a virtuous cycle of loosening financial conditions and economic strengthening across a broadening swath of emerging market economies for which a large percentage of national bourses are represented by non-tradable, local economy service sector plays (Figure 15).

As we look ahead to 2021, we believe EM equities look poised to extend their 2020 return outperformance versus developed market (DM) peers on the basis of what we deem to be blue sky valuation, cyclical, US$ cycle and ownership conditions as well as the new US administration's stronger globalist credentials that are likely to reverberate favorably on global asset risk premium levels. For example, Figure 16 highlights EM equity valuations to hover at a sizable 23% percent P/E discount versus world peers while Figure 17 illustrates the projected acceleration in world GDP growth over the course of 2021 according to the Bloomberg consensus of economists. Finally, a compilation of multiple exchange and survey indicators shows global investors' allocations to EM equities to hover well below benchmark weightings. Specifically, while EM equities comprise around 13 percent of global equity index benchmarks, global investors' exposure levels hover at around 7 percent. Under our baseline case of continued, accelerated relative return outperformance by EM equities, market history suggests global investors are likely to increase allocations significantly to the asset class over the coming quarters.

Figure 14. G3 Central Banks' Loosening Policy Response Combined with Post-March Decline in Economic and Financial Volatility Set Off Virtuous EM Currency Revaluation Dynamics

Source: Bloomberg

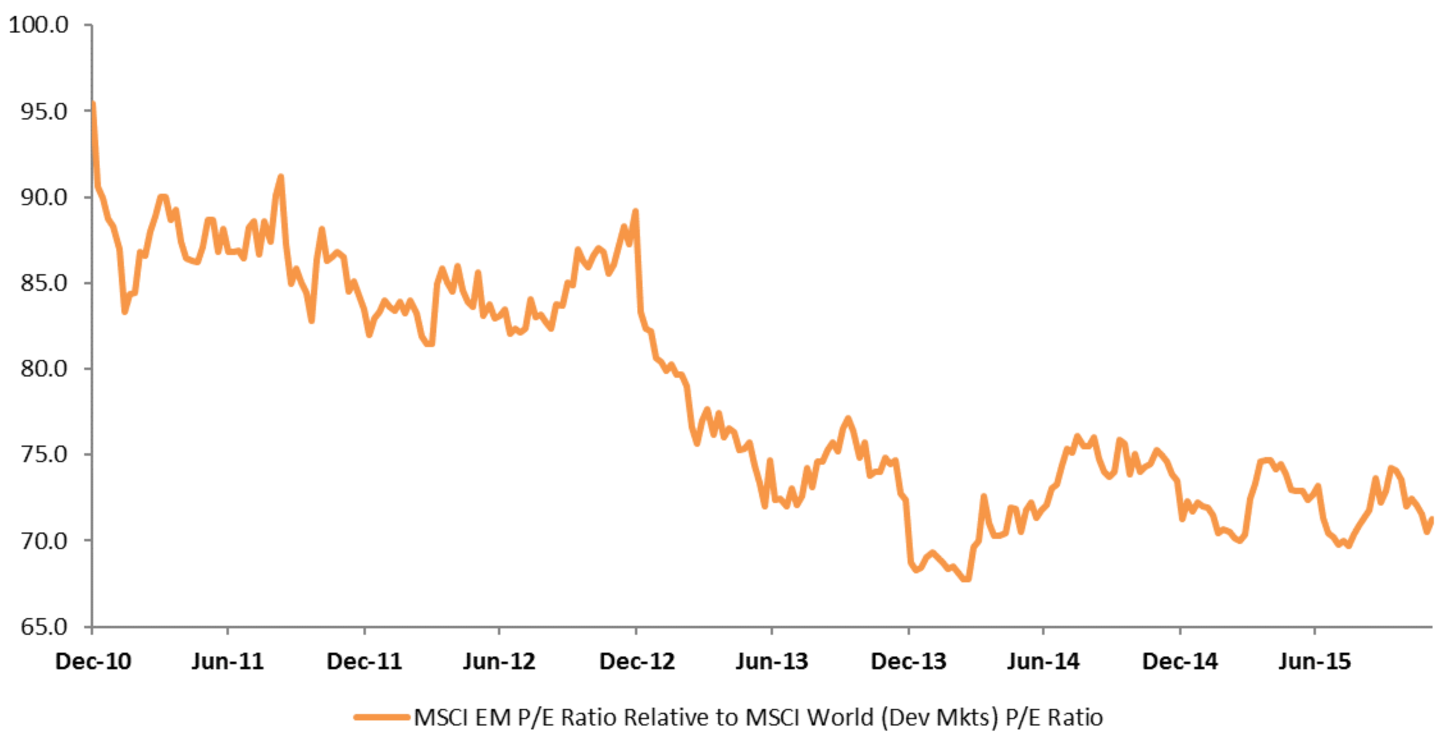
Figure 15. EM Equity Index Benchmark's Vastly Increased Domestic Sector and Asia Regional Representation over the Years

MSCI Emerging Markets: Selected Sector and Regional Benchmark Weights

	1997	2002	2007	2020
Sector Weights				
Energy	6.20%	10.70%	16.70%	5.10%
Materials	16.50%	12.50%	14.30%	7.50%
Consumer Discretionary	8.00%	6.70%	5.10%	18.60%
Technology	5.50%	17.40%	13.20%	19.70%
Financials	25.80%	19.30%	22.80%	18.20%
Telecom Services	11.20%	15.20%	9.70%	11.80%
Regional Weights				
EM Asia	36.7%	55.4%	54.6%	79.6%
Latin America	38.5%	17.6%	20.4%	8.0%
EMEA	24.7%	27.0%	25.0%	12.4%

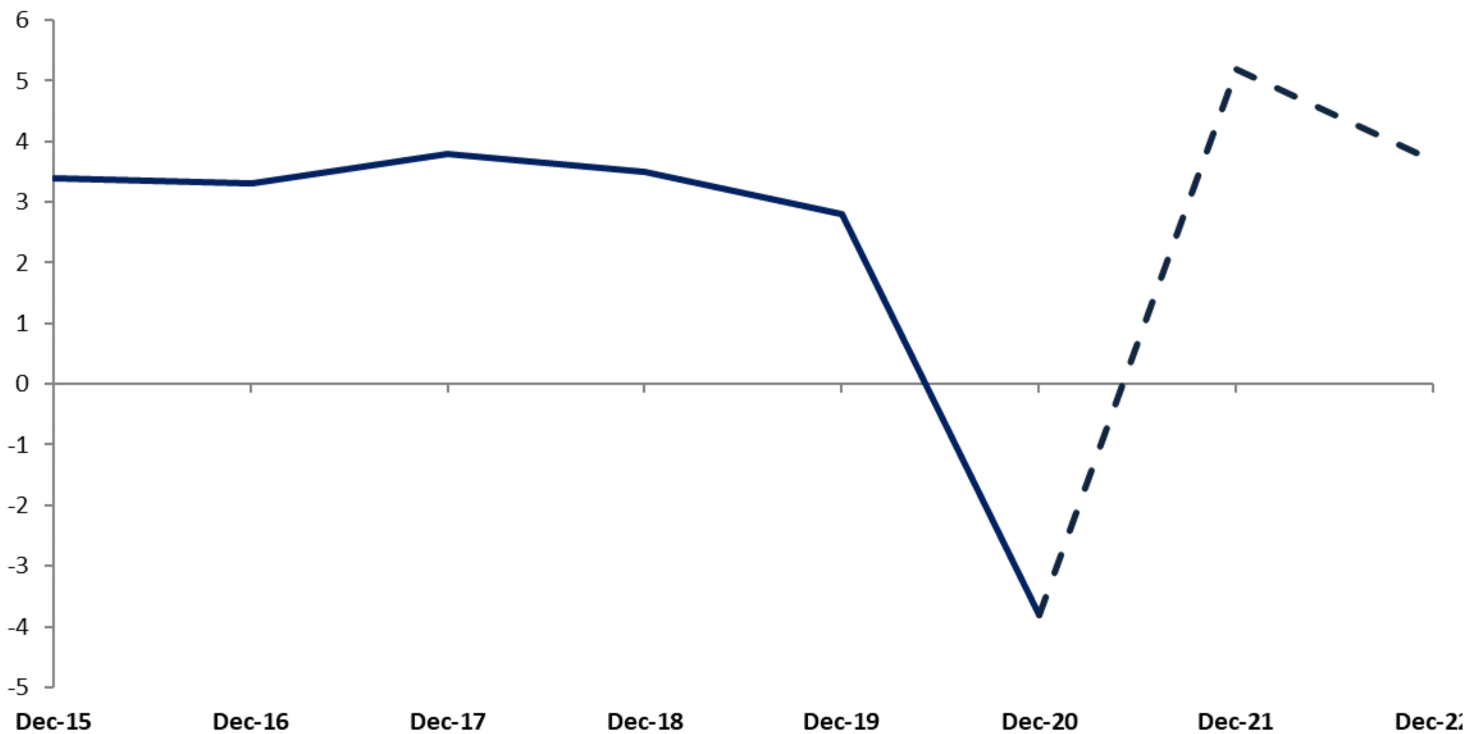
Source: Bloomberg; 2020 weights are estimates as of 16th December 2020

Figure 16. EM Equities Hover at 23 % Discounted Valuations versus World Peers at a Highly Auspicious Juncture of the Global Investment Cycle for the Asset Class: Weakening US$, Cyclical Upswing in Global Economy and Asset Class' Under-ownership Status



Source: MSCI, Bloomberg and Glovista Calculations

Figure 17. World GDP Growth Momentum Over 2021-2022: Bloomberg Consensus



Source: Bloomberg

Against such favorable backdrop for the EM asset class, the Glovista emerging markets strategy favors increased allocations to value oriented markets in the Latin America, South East Asia and EMEA regions on account of relative valuation and strengthened top line and margin growth prospects versus emerging Asia following EM North Asia equities' strong 2020 calendar year relative performance was boosted partly by that region's superior positioning to withstand the macro effects from the pandemic. As a growing share of the world's population is vaccinated over the course of 2021, the macro and financial environment is expected to turn increasingly more favorable for non-North Asia Emerging Market corporates. Within those regions, the Glovista investment team favors selected overweight exposures to Chile, Russia, India, Indonesia, Turkey as well as selected sector plays in Chile, Mexico, Brazil and Thailand. Within North Asia, we favor selected IT sector plays in South Korea, Taiwan and China.

As for potential downside risks conditioning the outlook on the asset class, we include the usual set of factors: geopolitical (especially China, Russia and the Middle East), adverse effects from potential G3 policy mistakes, unexpected global inflation acceleration or US$ strengthening process.

With the turn of such an precedented year for the world, filled with over a million lives lost to the pandemic and unspeakable hardships borne by so many, we extend our very best wishes to you and your loved ones, in the hope that 2021 be filled with good health, peace and joy.

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