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Monthly Market Newsletter

Glovista Global Perspectives

This Issue:

__2023 Mid-Year Outlook:__ We Sustain Defensive Portfolio Tilts, Raising Exposure to High Quality Equities and Bond Duration as Growth Decelerates Amidst Tightening Liquidity

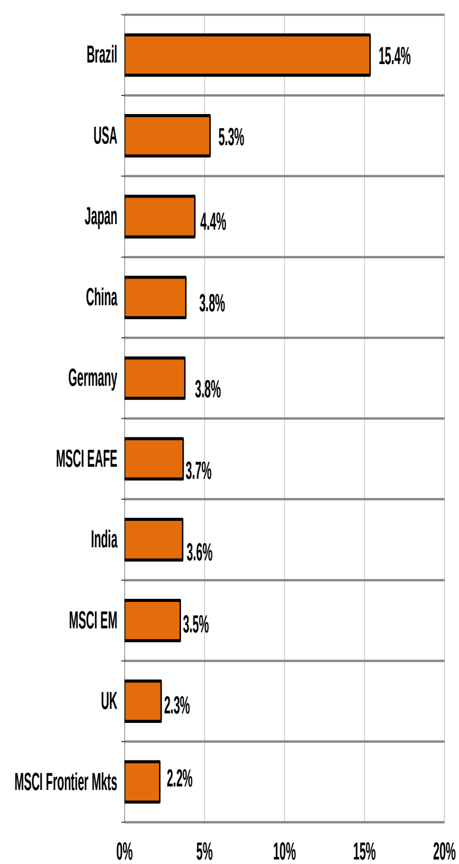
In June, the global activity calendar has underwhelmed consensus estimates, as reflected in broad-based declines recorded by economic surprise activity readings for most of the world's economic regions, with the exception of the United States. Similarly, long-term inflation expectations – as reflected via survey and market-based indicators - have declined during the month (Figure 1), resulting in a sizable fall in bond market volatility (e.g. MOVE index).

On the policy front, developed country central bank actions and guidance have proven more hawkish than expected, including larger than expected policy rate hikes out of the Bank of England, Bank of Canada and the Reserve Bank of Australia. In addition, at its June meeting, the US Federal Reserve upwardly revised its policy rate projections for the rest of 2023 while on June 28th Fed Chair Powell stated the 2 percent core PCE target is unlikely to be reached before 2025. The European Central Bank's more hawkish guidance than the US Federal Reserve's has led to a modest US dollar sell-off during the month of June. Likewise, increased concerns over a weaker than expected ongoing Chinese economic recovery - combined with a broad-based softening of global manufacturing activity – led to declines in industrial and energy commodity prices during the month.

From a market perspective, June macro and policy developments have led to modest bounces in risk asset prices, particularly for US indices, during the month via the supportive effects from: (1) a weaker US dollar, (2) lower bond market volatility, and; (3) reduced downside tail risks to the global activity outlook, courtesy of the boost to global households' income via the reduction of food and energy commodity prices.

From a portfolio strategy perspective, these macro developments reinforce our longstanding asset class tilts: underweight equities, overweight fixed income and

Country-wise Monthly Performance in USD terms (June 2023)*



Source: MSCI & Bloomberg

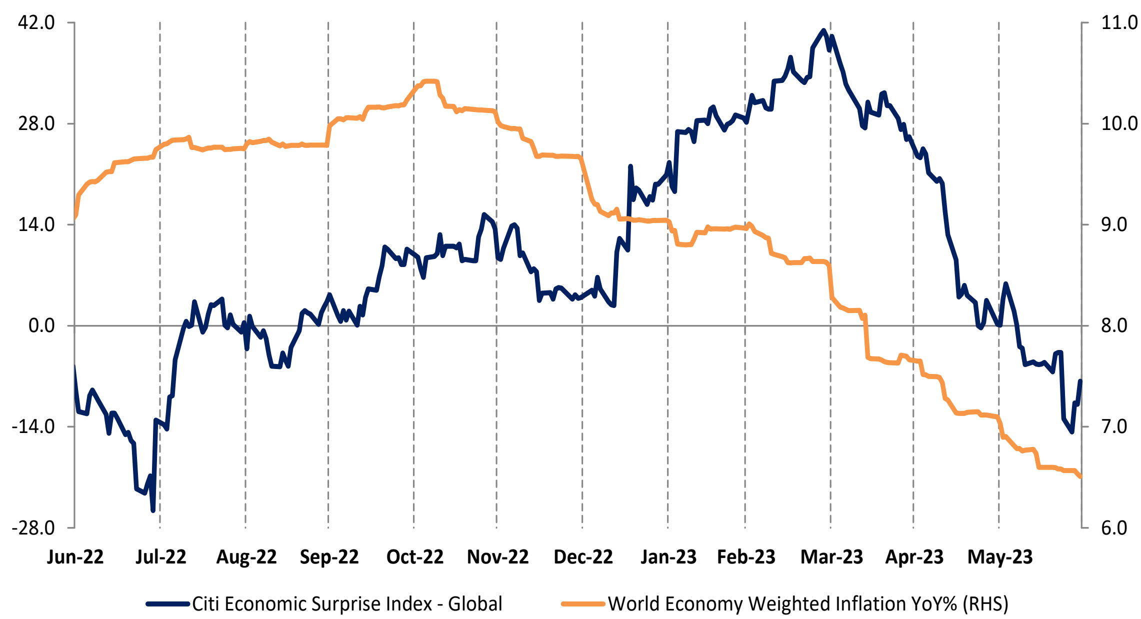
***As of June 29th, 2023**

Sectors	% Change	FY1 PE Ratio
Energy	5.81%	10.7
Materials	9.79%	18.0
Industrials	10.21%	19.9
Cons Disc	10.48%	26.9
Cons Stap	1.92%	20.6
Technology	4.64%	30.1
Healthcare	3.08%	17.9
Financials	5.58%	13.6
Utilities	0.25%	17.4
Telecom	1.56%	17.9
Real Estate	4.30%	36.3
S&P500	5.18%	20.1

S&P500 Monthly Sector Performance – Jun MTD 2023*

**as of June 29th 2023*

Figure 1. Underwhelming Global Activity and Declining Inflation Over the 2nd Quarter is at Stark Contrast with Hawkish Central Bank Guidance



Source: Citigroup & Bloomberg

selective ownership of precious metals, particularly gold. Within equities, we favor overweight exposure to high-quality, defensive factors. In fixed income, we favor overweight allocations to high-grade, long-duration paper with a barbell of short-term T-Bills.

Our asset class tilts reflect our expectation of continued deceleration of economic activity, particularly in the developed world and including the USA. A number of OECD economies have already entered recession (e.g. Germany, New Zealand and Sweden) while other large economies (e.g. China) have surprised negatively owing to the knock-on effects on manufacturing sector activity resulting from a combination of the normalization of global supply chains and firms' resultingly lower need to hold high inventory levels, particularly as working capital funding costs have reset higher following last year's succession of policy rate hikes across the developed world.

In the US economy's case, we expect continued deceleration of economic activity in the year's second half. Already, recent economic releases point to a material softening of labor market conditions, as reflected in the latest US ISM non-manufacturing sector index's employment readings and the US NFIB job openings indicator. In addition, the latest releases of private sector surveys evidence a marked decline in postings across most job categories outside healthcare, with most of the softness centered in the financial and information technology sectors.

As we look ahead to the year's second half, we sustain our baseline case of modest US recession late in 2023/early 2024 as a result of several considerations, including:

- lower employment growth resulting from an ongoing decline in corporate profit margins – as evidenced in the most recent NIPA figures – and weaker (especially nominal) top line growth, courtesy of lower inflation and lower household disposable income growth;

- decline in households' disposable income growth, particularly for cohorts with higher propensity to spend, as a result of the unwinding of several transitory phenomena that were highly supportive to aggregate demand during the year's first half, including:
    - the outsized upward adjustment in US Social Security payments starting in January, owing to the reset factor following last year's spike in headline CPI inflation which is unlikely to be repeated this year,
    - highly favorable weather conditions impacting the northern hemisphere during the winter period, resulting in sharp energy price declines,
    - highly stimulative effect of loosening liquidity conditions stemming from the US Federal Reserve's launch of liquidity facilities supporting the banking system on the heels of this past March's regional banking sector bankruptcies,
    - stimulative effects of loosening liquidity conditions resulting from the debt ceiling crisis that led to a sharp shrinkage in net debt issuance by the US Treasury that is now soon projected to reverse itself,
    - the fast-approaching end this Fall of the longstanding student loan debt relief introduced by the Biden administration,
    - projected drawdown of extraordinary savings pool accumulated by US households during the pandemic era, courtesy of Uncle Sam.

As observers of the global economy, we attribute the stronger resilience displayed by the US economy during the year's first half – vis-à-vis other developed country peers – to two distinctive factors that are likely to fade over the coming months:

1. US households' balance sheets' lower interest rate sensitivity courtesy of the dominant use of fixed rate mortgage loans versus floating that are more widely used in Europe, the UK, Sweden and Australia, and;

2. The unparalleled balance sheet boost enjoyed by US households as a result of the overly generous transfer programs implemented by the US federal government during the pandemic period, the effects of which on current expenditure are expected to play out completely by the fourth quarter of this year.

The above macro considerations lead to several market implications, including:

- our reaffirmation that the US Dollar index's cycle top was recorded this past September 2022;
- intermediate- and long-term sovereign bond yields have already topped out;
- bond market volatility is likely to have topped out, certainly versus equity volatility;
- precious commodities are likely to outperform industrial and energy commodities over the coming quarters.

From an equities market perspective, our macro baseline case suggests overweight allocations to high-quality, cheaply valued stocks. The US market is the most expensively valued at a global level, particularly the top 7 names in the SP500. The bottom 493 SP500 index constituents trade at a 12-month forward earnings multiple of 15.8x, an attractive valuation when viewed against our macro baseline case. In the international scene, emerging market equities are especially attractively valued – at 12-month forward earnings multiple of around 12.7x – particularly against a backdrop of (a) resilient real wage growth, (b) likely decline in policy rates (from real levels considerably higher than those in the developed world), (c) global investors' under-owned status, and (d) potential continued US Dollar weakness versus high carry emerging market currencies. Although Eurozone equities are attractively valued at 13.0x 12-month forward earnings multiple, the cyclical backdrop as well as European corporates' stronger linkages to the Chinese economy lessen EAFE stocks' allure versus EM peers.

Finally, as always, the investment outlook is not bereft of risks. Our investment team identifies the following as the most top of mind: the potential for policy mistakes by G3 central banks; the potential for fiscal policy overtightening, particularly in the US; the risk of sudden dislocations in the world energy market, possibly as a result of Russia or OPEC related actions; the risk of a broadening of the Ukraine- Russia war outside Ukrainian territory; unhinging of households' inflation expectations.

Emerging Market Perspectives

India and LatAm Stocks Outperform Solidly in June, fueled by Resilient Local Growth Factors, Cheap Valuations and Low Geopolitical Risk Load; EM Asset Class' 2023 Second Half Outlook Especially Auspicious

Emerging market stocks, as represented by the MSCI EM index, performed in line with non-US developed market peers during the month of June. Latin America, Polish and Indian stocks posted especially strong outperformance during the month, propelled by resilient local growth factors, cheap valuations and low geopolitical risk load versus north Asian peers, in particular.

A review of recent macro developments across emerging market countries highlights a solid recovery in real wage growth for a number of Latin American countries, particularly Brazil, Mexico and Peru. Absolute and relative stock valuations for Latin American equities remain exceedingly cheap from a historical perspective, with LatAm stocks trading at close to 50% discount versus US equities against a historical average discount factor close to 25%. Indian equities continue to benefit from supportive local economic growth momentum as well as attractive risk premium given the country's low geopolitical risk load versus north Asian peers.

As we look ahead to the year's second-half, our investment team expects the emerging market equities' asset class to post especially robust outperformance versus developed peers on the back of several considerations, including:

- sharp upturn in relative economic growth momentum between EM economies versus developed European economies and the USA;
- exceedingly cheap relative valuations between EM equities and developed peers, lending attractive entry points to global investors at a cyclical juncture in which the US Federal Reserve is widely expected to bring its lasting rate hike cycle to an end;
- EM currencies' compelling carry characteristics at a juncture in which bond and equity market volatility has been edging lower on a sustained basis these past several months;
- Global investors' exceedingly underinvested status to the asset class;
- Considerable potential for an impending start to policy rate cuts by a large number of EM central banks as prevailing real interest rate levels are high by historical standards and running inflation momentum has been turning lower over the past several months;
- China, the epicenter of investor growth concerns in the EM space, has witnessed a recent succession of stimulative policy stimulus measures announced by the government. Likewise, indicators of consumer mobility have remained resilient, boding well for a resumption of service expenditure growth despite the likely continued softness in the property market.

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