GLOVISTA INVESTMENTS

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Glovista Global Perspectives

This Issue:

Risk Markets Rise further in July, fueled by US$/Inflation Declines, Goods Sector Stabilization and China Policy Actions; We Sustain Overweight Quality Factor Tilt while Raising Non-US Exposures

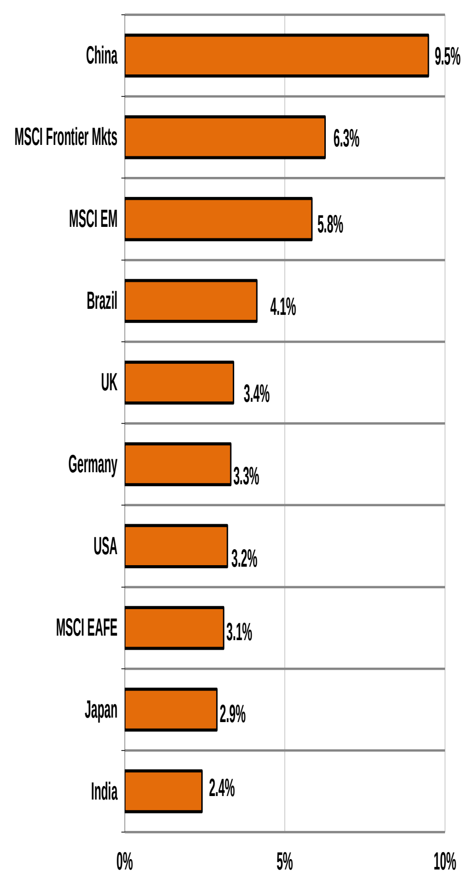
In July, risk markets have posted gains boosted by benign G10 macro data releases and policy actions out of China. In addition, value-oriented sectors (e.g. energy, materials and financials) have outperformed growth peers, under the auspices of declines in the US Dollar and core CPI inflation, along with incipient signs of stabilization in the long-running manufacturing sector slowdown at a global level.

Despite continued softening trends in global (ex-US) activity surprise indicators, the month of July has proven supportive of risk markets given the unfolding of a set of economic releases leading to expanded equity and credit market valuations. Some of those indicators have included declines in core inflation readings for the world's major economies (including the USA) along with policy stimulus measures announced by China's government.

While a number of major economies (most notably Germany) hover in recession territory, the US stands out for the resilience of its year-to-date activity momentum. As discussed in our June column, we attribute such US economic resilience to a pair of economic phenomena specific to the USA and transitory in nature; specifically:

- the US economy's exceedingly low interest rate sensitivity to the large succession of policy rate hikes seen over the past year and a half. Such unusually low sensitivity results in highly favorable (tax-cut like) effects on US households and corporates stemming from the broad-based borrowing rate locks entered during 2020 and 2021. Such rate locks were especially and uniquely supportive of the US economy in 2023 contrary to Europe and much of the rest of the world as the overriding majority of US households' and also corporates' debt is fixed-rate and long-term. This dynamic implies the Fed's interest policy's "long and variable lag" on the real economy is assured to be vastly longer than usual in the current cycle.

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



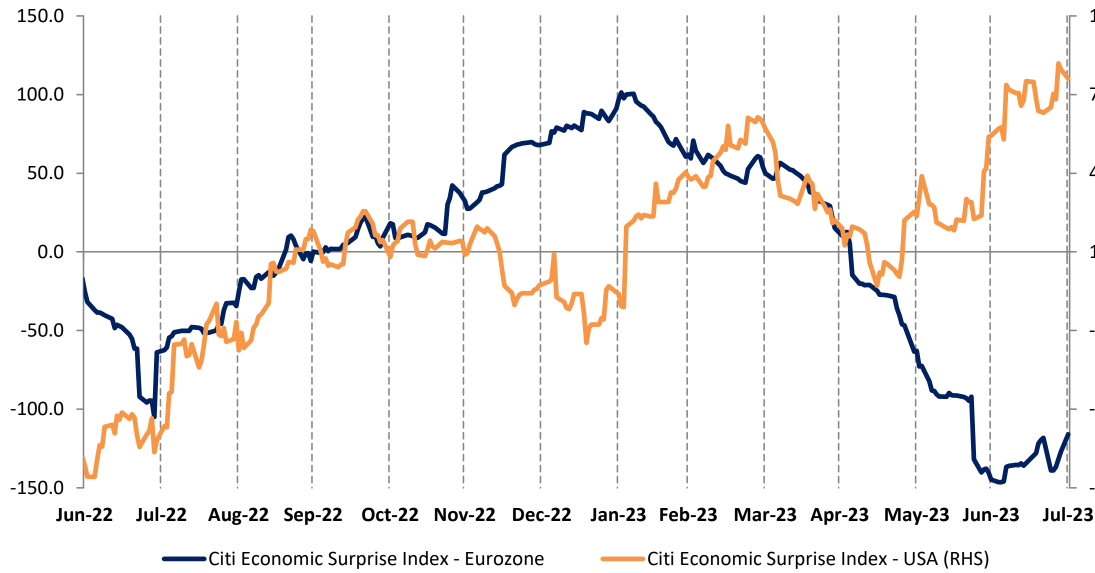
Source: MSCI & Bloomberg

**As of July 28th, 2023*

S&P500 Monthly Sector Performance – July MTD 2023*		
Sectors	**% Change**	**FY1 PE Ratio**
Energy	**5.18%**	**11.8**
Materials	**2.83%**	**19.1**
Industrials	**2.62%**	**20.6**
Cons Disc	**1.84%**	**27.5**
Cons Stap	**2.46%**	**21.3**
Technology	**2.50%**	**31.3**
Healthcare	**1.66%**	**19.3**
Financials	**4.24%**	**14.6**
Utilities	**2.32%**	**18.1**
Telecom	**6.77%**	**19.1**
Real Estate	**0.48%**	**36.8**
S&P500	**2.96%**	**21.3**

**as of July 28th 2023*

Figure 1. The Relative Resilience of the US Economy Evidenced in the Contrasting Economic Surprise Indicators from the Eurozone and the USA



Source: Citigroup & Bloomberg

- the overly loose (for periods outside recession) fiscal policy stance currently pursued in the US, with the federal government deficit hovering at close to 8.5% of GDP in 2023. Such loose policy stance reflects a number of factors including generous upward resets in social security payments earlier this year, industrial policy-oriented government programs, higher interest expenses paid by the US government, among others.

As we look ahead, despite underwhelming activity surprise indicators for most of the world, incipient signs of stabilization in the long-running manufacturing sector decline - particularly with recently announced China fiscal and monetary policy stimulus – bode favorably for a turn in relative economic momentum away from the US to the rest of the world's economies. We believe the recent downturn in the US Dollar cycle discounts such impending turn in economic cycle leadership away from the US, with favorable implications on non-US equity markets versus US peers. In addition, such a scenario of geographic broadening of economic activity should support an upturn in value sectors' relative performance versus growth peers.

On the policy front, recent G3 central bank policy actions have been somewhat consequential, especially out of the Bank of Japan. First, as widely expected, the FED and the ECB raised its reference policy rates by 25 basis points during the month of July. Both the US FED Chair and the ECB President emphasized that any further rate hikes would be data-dependent. Nevertheless, both expressed their staffs' expectation of continued deceleration in inflation pressures along with a weakening of economic momentum, with the FED staff discarding a recession scenario for 2023. In the case of the Bank of Japan, the actions taken during its scheduled July meeting proved more important as parameters governing its longstanding yield curve control (YCC) protocols were loosened, equating to a defacto 50 basis points raise in the target 10-year government bond yield. Notwithstanding such action, the Bank of Japan expects inflation to decelerate further in 2024 and 2025. We believe such policy actions, when viewed on a combined basis, are US Dollar bearish.

The second quarter corporate earnings season has attracted much investor attention as corporates have beaten downsized consensus estimates (from those prevailing at the beginning of the year). While 2023 earnings estimates remain considerably below those prevailing at the beginning of this year, 2024 and 2025 estimates have been upwardly revised, reflecting corporates' increased confidence in the economic outlook. Given our assessment on the likely transitory nature of recent dynamics supporting US growth, we believe global investors are likely to be disappointed on their US market earnings outlook versus international peers. In that light, US equities' (particularly large cap) valuations more than reflect such a rosy scenario. The opposite appears to hold true for non-US peers. A similar dynamic affects the divide between US high grade and high yield debt sectors.

Given the above considerations, the Glovista investment team sustains overweight exposure to high quality, low valuation equities and credit. At a global level, we have raised exposure to non-US markets during the month of July while sustaining exposure to gold and gold equities. Within the fixed income market, we continue to favor exposure to intermediate-duration high grade debt.

Emerging Market Perspectives

Emerging Market Equities Outperform US and EAFE Peers in July, Boosted by US$ Dollar Weakness, China Policy Actions and Signs of Goods Cycle Bottoming

In July, global and China country developments exerted unambiguously favorable effects on emerging market equities' relative performance versus developed country peers, with the MSCI EM index posting July returns of 5.84% against 3.21% for the MSCI US and 3.09% for MSCI EAFE peers. Specifically, a weakening US Dollar along with signs of an incipient upturn in the global goods cycle reinforced the EM equities' performance impetus stemming from recent policy easing measures announced by Chinese policymakers. Some of the recent policy announcements from the Chinese authorities include:

1. On July 10th, financial regulators extended the loan relief program for developers particularly focused on delivering homes for which they have already accepted deposits from consumers;
2. The Peoples Bank of China (PBOC) has been injecting liquidity in the economy by conducting reverse repo operations on a daily basis;
3. On July 18th, thirteen government departments outlined a plan to boost consumer spending on a list of items and improve access to credit for households;
4. On July 19th, the Communist party issued a rare statement committing to improving business conditions for private businesses including consulting tech entrepreneurs on drafting policies;
5. The Communist party Politburo signaled an easing of policies for the property sector at its annual meeting in July. The official comment excluded President Xi's standard slogan "Houses are for living, not for speculation.";
6. On July 27th, China's housing minister called for homebuyers who have paid off their mortgages to be treated as first time home buyers;
7. On July 28th, three government agencies outlined a plan to increase small and medium sector manufacturing by taking steps to increase sales of green and smart home goods in the rural area;
8. On July 31st, the National Development and Reform Commission released a document focusing on removing government restrictions on consumption such as car purchase limits and improving infrastructure.

As we look ahead, we reaffirm our expectation for a strong outlook facing the EM asset class based on the potential for policy interest rate cuts from a host of EM countries, relative growth acceleration versus developed regions, currency appreciation and increased investor appetite to the asset class from prevailing underweight allocation levels.

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GLOVISTA INVESTMENTS

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