ALPINEMACRO
A Unique Mind On The Markets

GLOBAL STRATEGY

October 2, 2024

Global Tactical Asset Allocation With Artificial Intelligence

Disclaimer: *Clients are advised to use our Global Tactical Asset Allocation model with AI (GTAAI) as a quantitative reference point – not as the sole reference point. As a mechanical process, the model cannot account for unanticipated events such as natural disasters or major political or policy disturbances. As such, we recommend investors overlay their discretionary views of these risks on top of our GTAAI allocations.*

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September 2024 Performance Review

The GTAAI model ended September with a 0.6% gain, underperforming a hypothetical balanced portfolio[1] by 1% (**Chart 1**). The model yielded 1.3% returns after including our hedging strategy. The model's allocation was evenly split between stocks and bonds. Most of the underperformance was due to country choices within equities.

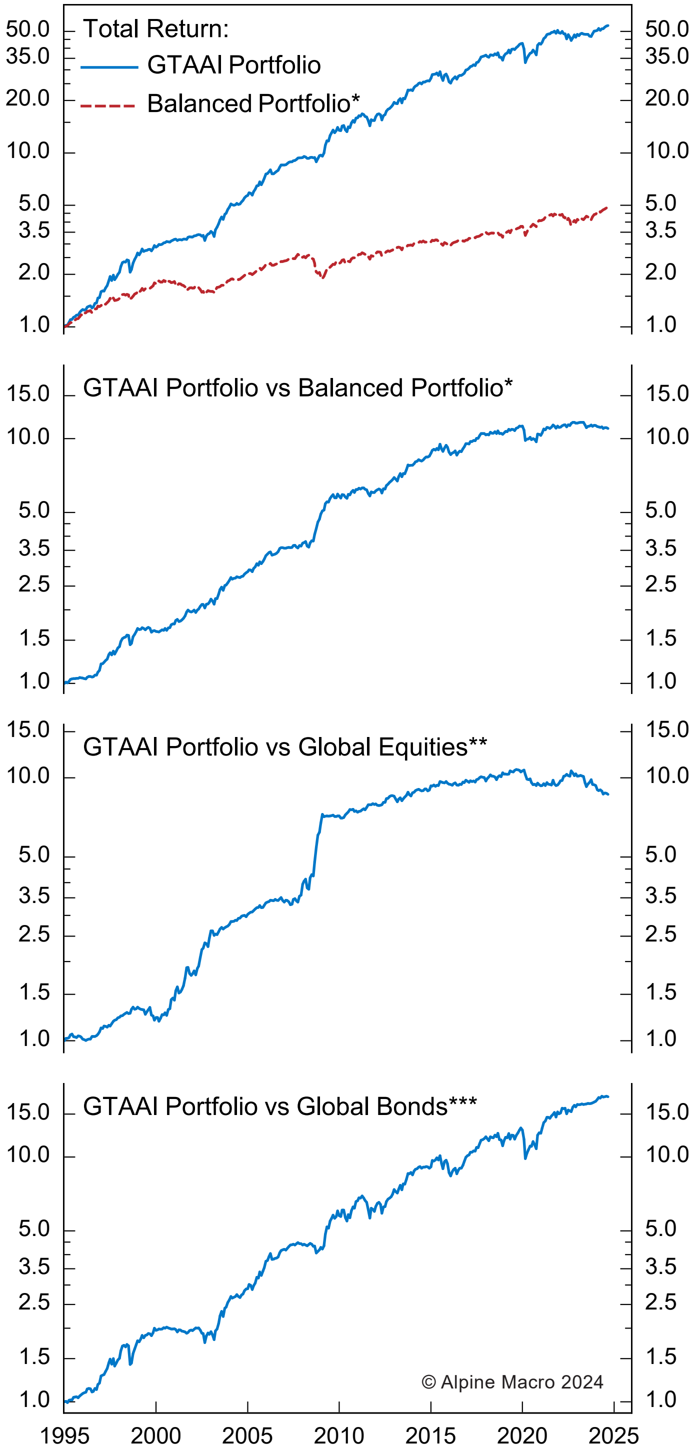
Global risk assets sold off at the beginning of September but rebounded sharply through the rest of the month. A jumbo rate cut by the Fed and announcements of forceful stimulus by Chinese policymakers buoyed risk assets. Some of the optimism was curtailed by the escalation of military conflict in the Middle East.

For the equity component, the GTAAI model's country choices underperformed the MSCI Global Equity Index by 1.3% in September, with the index itself gaining 1.8%. The model was concentrated in Italian, Swiss and U.S. equities. The star performers last month were Chinese and other EM stocks. Markets like Canada and Australia with high beta to EM also outperformed.

For the bond component, the GTAAI model's selections underperformed the BofAML Global Investment Grade Government Index by 0.2%, which recorded a 1% gain (**Chart 2**). The model was underweight Treasurys and overweight gilts. The former outperformed while the latter did not.

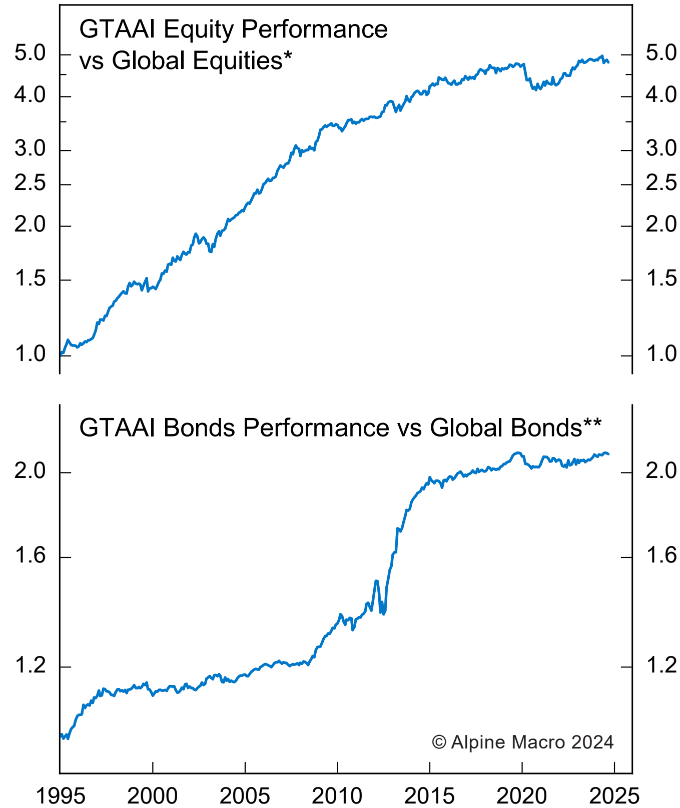
1 45% in global equities, 40% in global bonds, 7.5% in commodities and 7.5% in gold.

Chart 1 GTAAI Model Performance



*Portfolio with allocations to equities, bonds, commodities and gold at 45%, 40%, 7.5% and 7.5%, respectively
**MSCI All Country World Total Return Index in local currency
***BofAML Global Government Bond Index

Chart 2 GTAAI Alpha Performance



*MSCI All Country World Total Return Index in local currency
**BofAML Global Government Bond Index

We advised clients to retain foreign currency exposure. This strategy improved returns by 0.7%. The DXY depreciated by 0.6%. The dollar was particularly weak against the sterling, the Aussie dollar, and the yen.

Model Allocations For October 2024

For October, the model increases risk exposure, raising the equity allocation to 56% from 50% in September. The bond allocation falls by 8% to 42%. The gold weight rises to 2%. The GTAAI assigns almost no weight to commodities (Chart 3). Table 1 provides the model's allocation details.

Chart 3 GTAAI Asset Class Allocation

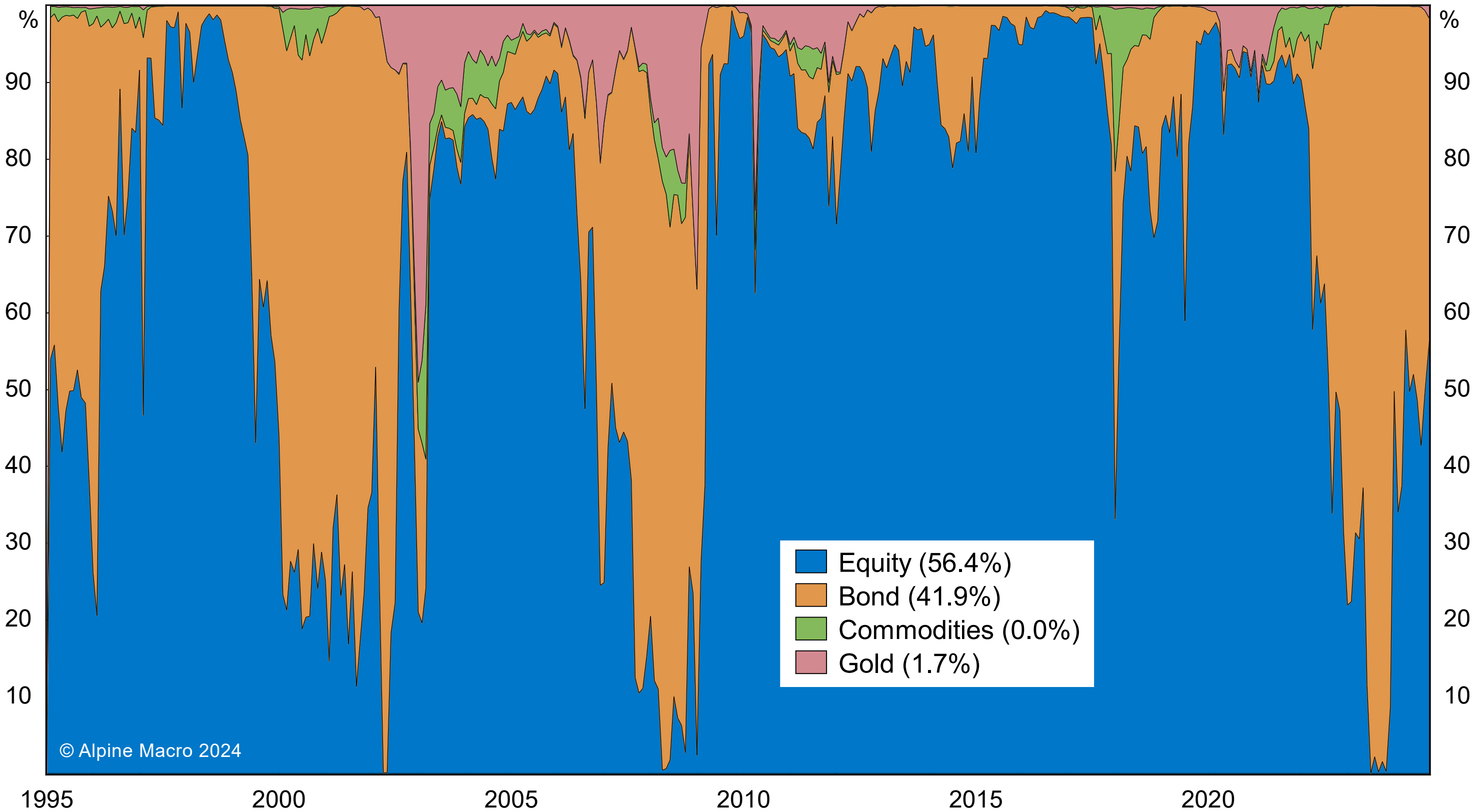


Table 1 Current GTAAI Model Allocations

	October 2024				September 2024			
	Equity (%)	Bond (%)	GSCI (%)	Gold (%)	Equity (%)	Bond (%)	GSCI (%)	Gold (%)
Australia	0.1	3.8			0.7	4.5		
Canada	0.5	2.4			0.3	4.0		
Switzerland	11.8	0.8			7.8	3.1		
Germany	0.5	7.8			1.5	7.6		
Emerging Markets	0.0	1.5			0.0	2.2		
Spain	1.7	0.0			0.9	0.0		
France	4.5	3.1			5.2	3.6		
U.K.	0.1	8.3			0.9	7.9		
Italy	18.9	0.1			14.3	0.2		
Japan	0.0	4.1			0.0	4.3		
Norway	0.2	5.7			0.9	6.8		
Sweden	0.1	0.9			0.4	1.9		
U.S.	18.0	3.3			16.6	3.8		
Total	56.4	41.9	0.0	1.7	49.6	49.8	0.0	0.6

Rounded to the nearest decimal point

The model is lighter on stocks than its historical average, but it is taking on slightly more risk versus September. It believes global bond markets have further to rally, and bond valuations have yet to return to fair value outside of the U.S.

The model is cyclically constructive on stocks, and the money impulse is improving. However, more aggressive allocation is held back by overbought momentum and a weakening dollar that may impede global equity returns in local currency terms.

The GTAAI model is not benchmarked to any market capitalization or debt outstanding index. The weight of large markets in those indices will typically be higher than in the model, which only considers absolute return.

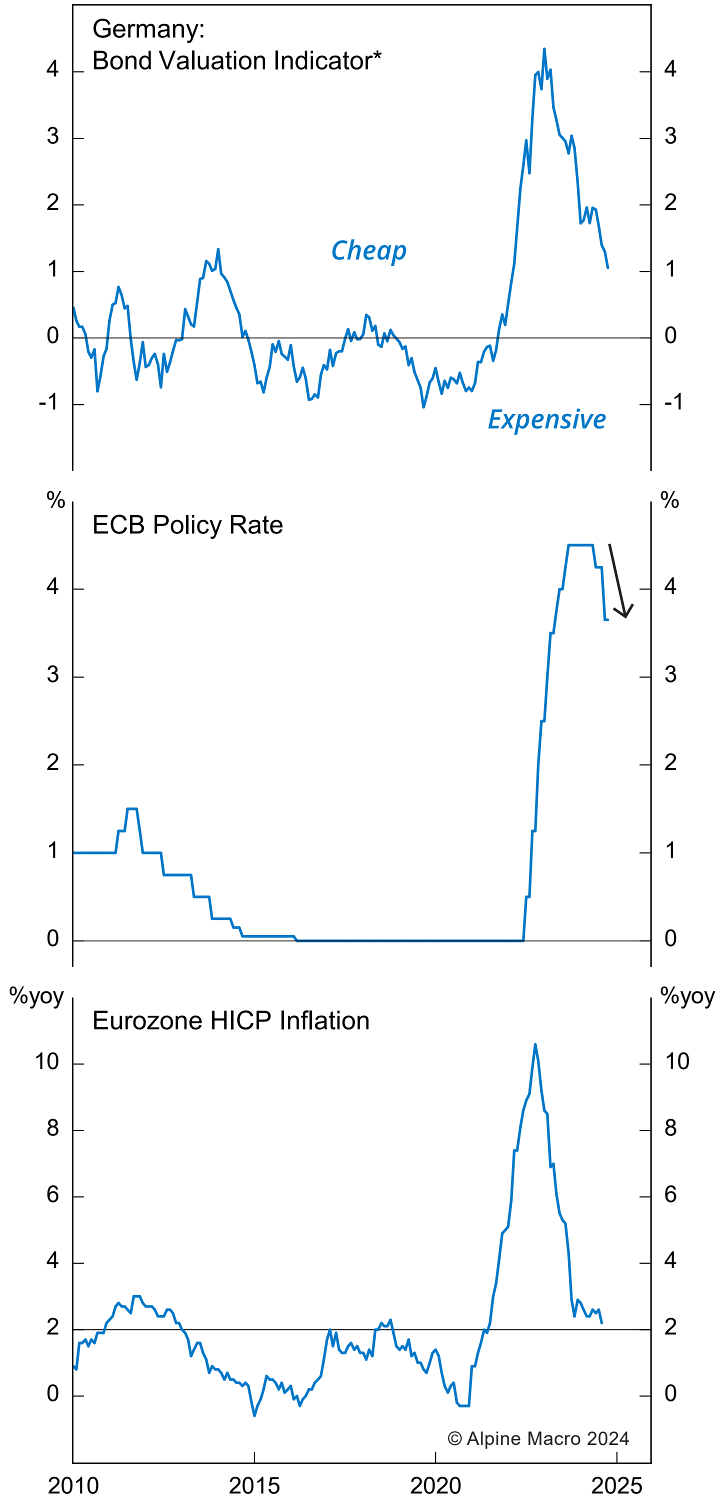
Favor British, German And Norwegian Bonds

The model further concentrates its bond allocation in a handful of markets, continuing a trend that started a few months ago. The three markets receiving the largest allocations are British, German, and Norwegian bonds.

Gilts continue to hold an 8% weight for October, unchanged from September. Gilt yields have been flat for the past two months and offer the highest carry in all DM bond markets. The valuation indicator accounts for two-thirds of the reason the model favors this market.

The model expects gilt yields to converge towards fair value, which accounts for a moving average of inflation, policy rate, and NAIRU. Inflation has fallen back to 2%, NAIRU has drifted lower since the pandemic, and policy easing will continue.

Chart 4 German Bund Yields Will Converge Towards A Falling Fair Value



*Alpine Macro proprietary indicator

However, momentum is now less oversold. The model does not consider the cycle indicator or the currency to be important drivers of allocation at the moment.

German bunds also receive an 8% weight. The valuation indicator suggests that bunds remain 1.1 standard deviations cheap, and yields are about 100 basis points above fair value (**Chart 4**). Fair-value yields for bunds have risen due to higher ECB policy rates and inflation since the reopening. However, as the ECB continues to ease and eurozone inflation undershoots the target, the remaining undervaluation will likely be absorbed through lower yields as both inputs decline.

The momentum indicator for bunds currently suggests that this market is 0.3 sigma oversold, down from a peak of 2.4 sigma. Both the business cycle and currency inputs are slightly bearish for bunds.

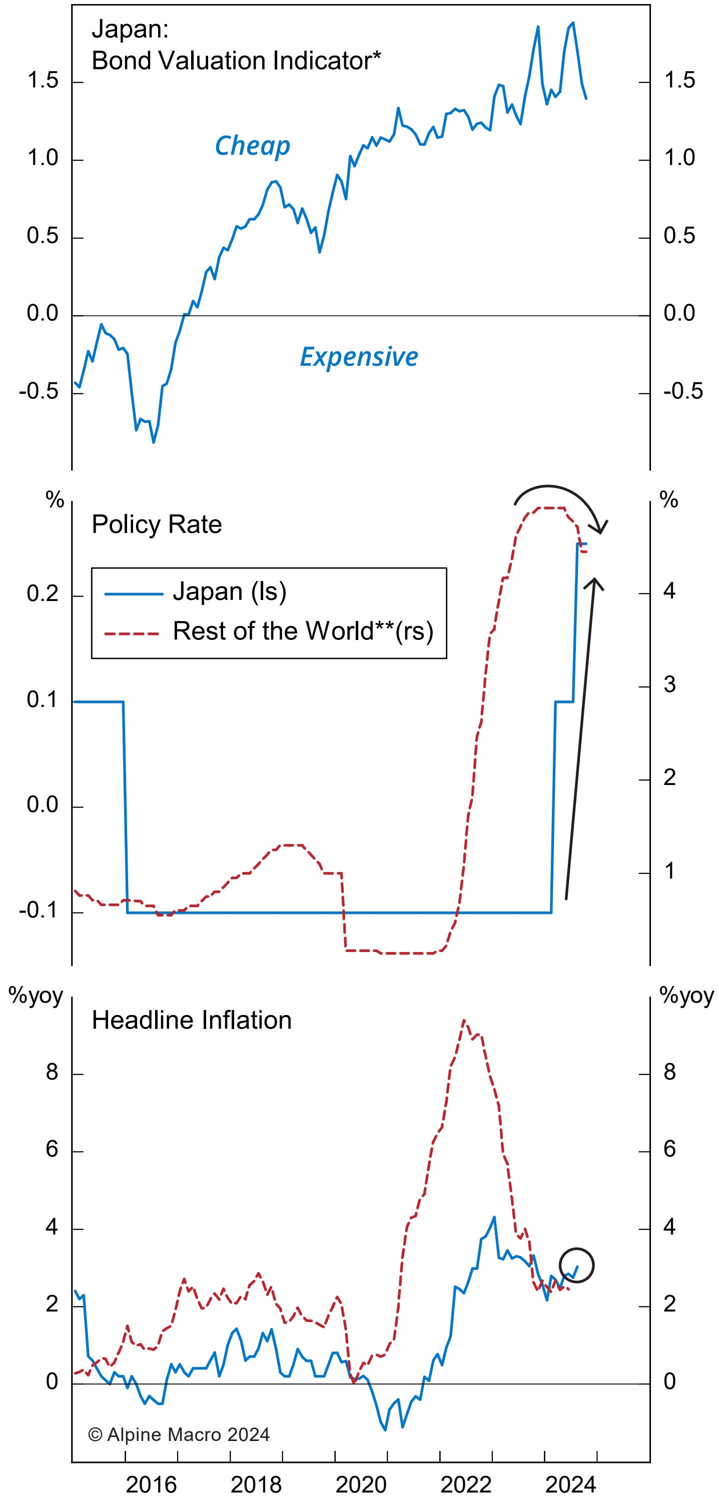
The GTAAI model downgrades Norwegian bonds to a 6% allocation from 7% in September. The main reason for the downgrade is a swing in the currency indicator, which contributes 7% *against* the decision to allocate to this market. Valuations are still 1.2 standard deviations cheap, but momentum has returned to neutral.

Bond Diversification Choices

For October, the model's second-tier bond choices are diverse, with Australian, U.S., French, and Japanese bonds receiving between 3-5% allocations.

The JGB allocation falls to 4% for October. Japanese bonds are the cheapest market based on our indicators (**Chart 5**). The Japanese economy and

Chart 5 JGBs Have Cheapened As Japan Moves Out Of Sync With ROW



*Alpine Macro proprietary indicator
**Average of U.S., Europe, Australia, Canada, and U.K.

monetary policy are out of sync with the rest of the world (ROW). Japanese inflation is rising, and the BoJ has been raising rates while the ROW is cutting.

Australian bonds are 1.1 standard deviations undervalued. Valuation is the main driver of the allocation to this market. This indicator is counterbalanced by an improving cycle indicator, which points to higher yields. Recent strength in the AUD is also a slight headwind.

U.S. Treasury valuations are approaching neutral. Momentum is no longer oversold but may undershoot into overbought territory. The model views recent currency dynamics as a sizable headwind for outperformance.

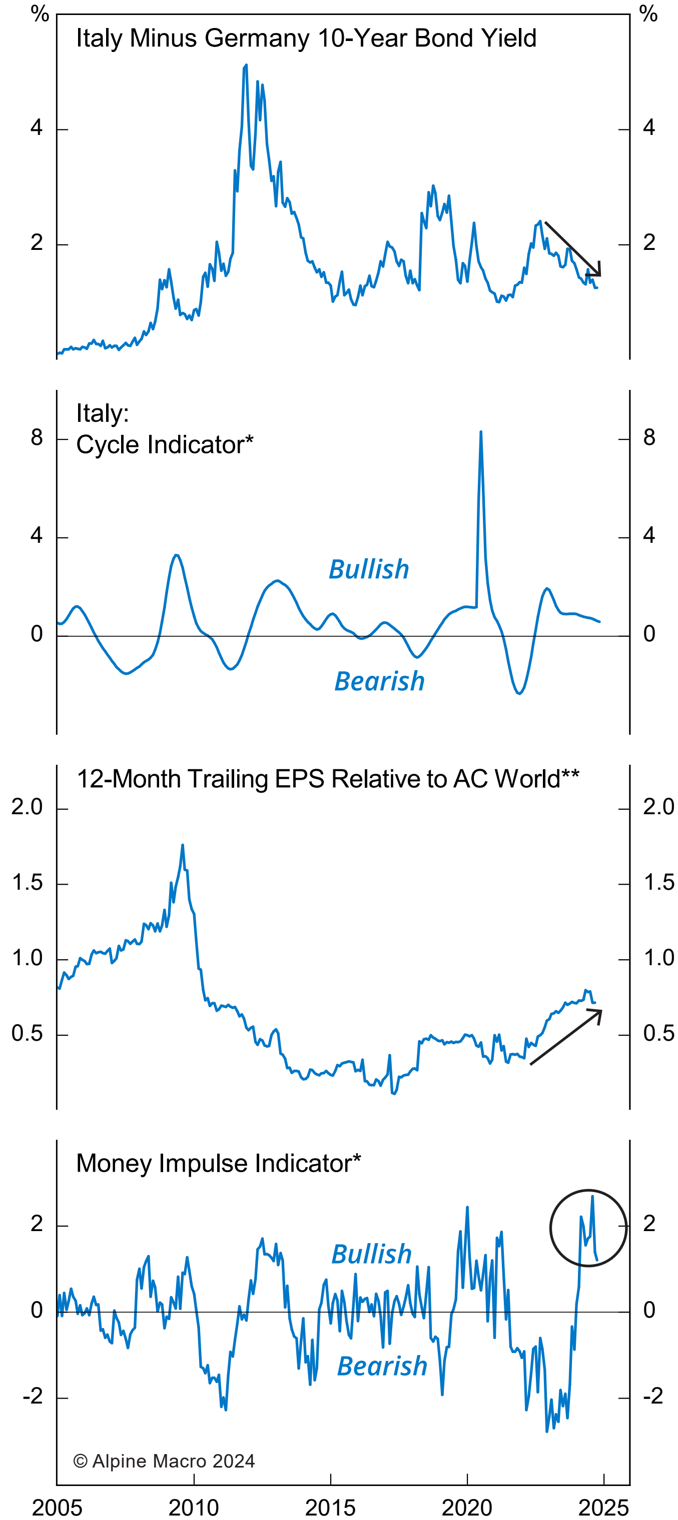
Favor Italian And Swiss Equities

The model's equity allocations are heavily concentrated in Italy, the U.S., and Switzerland. Most of the upgrade to equities this month is also distributed between these three markets.

The Italian equity allocation rises to 19%. It is the model's preferred market for October. Four main factors support the Italian allocation (**Chart 6**):

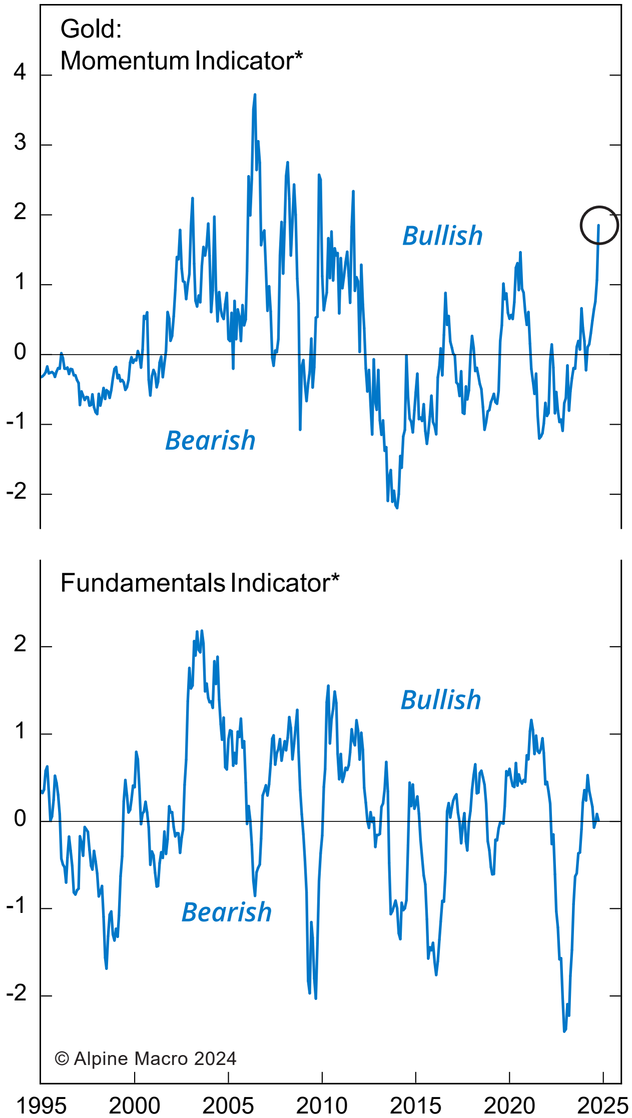
- Liquidity is supportive, with the indicator at 0.5 sigma bullish. This indicator contributes to a third of the decision to allocate to this market.
- The Italian business cycle is 0.6 sigma bullish, contributing to one-fifth of the allocation decision.
- Italy's earnings growth still outpaces the ROW although the indicator has slightly retraced in recent months.

Chart 6 Several Factors Support Italian Stocks



*Alpine Macro proprietary indicator
**Source: MSCI Large, Mid & Small Cap Index

Chart 7 **Upgrade Gold On Strong Momentum**



*Alpine Macro proprietary indicator

- Money impulse has become supportive with the indicator at 1.2 sigma.

Swiss stocks receive a 12% weight, up by 4% from last month. The upgrade is driven by a stronger money impulse, with the indicator rising to 2.4 standard deviations bullish. Recent currency dynamics have also become less of a headwind. The model mainly favors this market for its strong Return On Equity (ROE) indicator. However, momentum is overbought.

Upgrade U.S. Stocks

The model increases the U.S. equity allocation to 18%, up 2% from September. Most indicators lean bullish:

- The money impulse indicator, which tracks the second derivative of M2, is the main driver behind the upgrade. Money impulse has rebounded strongly on the back of credit creation.
- The ROE indicator for the U.S. is at 1.7 standard deviations bullish. The model, based on the adaptive expectations hypothesis, believes that ROE should capture structural factors such as the regulatory environment, tax policies, propensity for buybacks, and sector composition.
- Liquidity turns slightly bearish as money market spreads spiked on quarter-end window dressing.
- Momentum is 1 sigma oversold.
- The currency is turning into a slight tailwind.

Increase Gold Allocation

The model's gold allocation rises to 2%. The upgrade is mostly driven by momentum which is 1.8 sigma bullish (**Chart 7**).

Fundamentals remain near neutral. The recent fall in real yields is bullish for gold, but the dollar has yet to decisively weaken below its range of the past three years. The Indian rupee, a proxy for demand, has been softening.

Currency Considerations

While the model considers investments in local currencies, we offer discretionary hedging advice to enhance performance. The euro and the Swiss franc are the primary hedging currencies to consider this month.

We recommend retaining local currency exposures. Beijing has made a U-turn and is forcefully stimulating the economy. Markets are responding, and strengthening Chinese demand will benefit more cyclical currencies versus the dollar (Chart 8). At the same time, we expect the Fed to continue easing rapidly to ensure a soft landing. This will erode the dollar's yield advantage.

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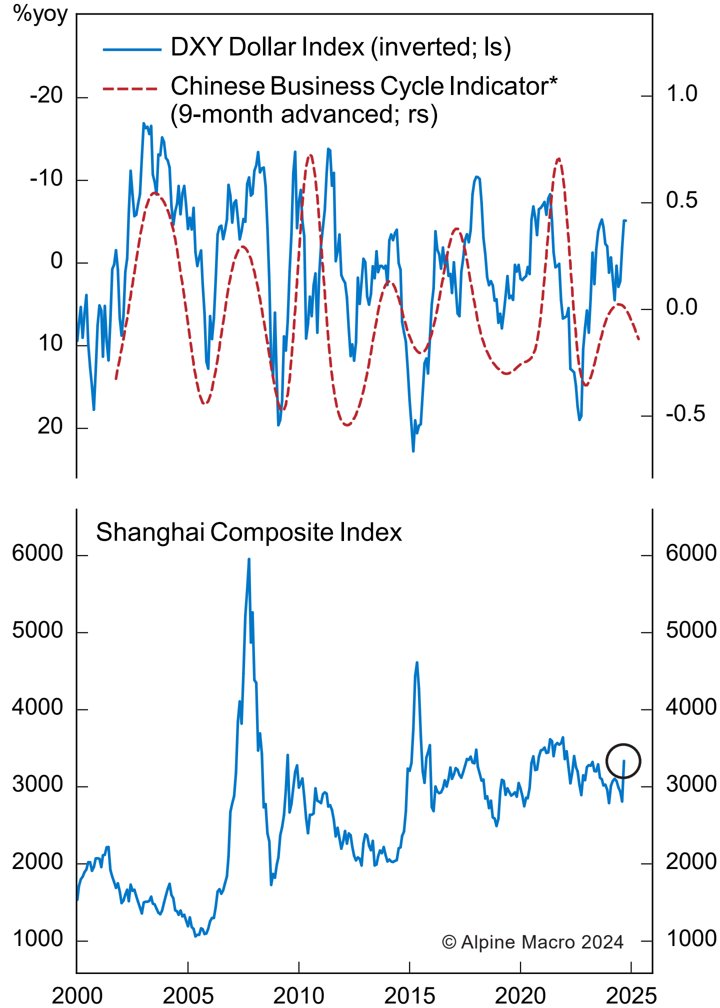
Chart 8 Chinese Stimulus Will Soften The Dollar



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