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GLOBAL STRATEGY

November 4, 2024

Global Tactical Asset Allocation ai 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.*

In This Report

October 2024 Performance Review

The GTAAI model ended October with a 1.5% loss, underperforming a hypothetical balanced portfolio[1] by 0.6% (**Chart 1**). The model's allocation was slightly tilted toward stocks over bonds. Most of the underperformance was due to the model assigning a larger allocation to fixed income than the hypothetical portfolio.

Global risk assets rallied at the beginning of October but lost those gains toward the end of the month. Most indicators show resilient U.S. growth, although earnings beats were somewhat softer than expected. Global bonds sold off on expectations of larger fiscal spending. Tit-for-tat exchanges between Iran and Israel have not been more escalatory, easing some tensions. Overall, sentiment remains cautious as investors await the results of the upcoming U.S. elections and further details of Chinese stimulus.

For the equity component, the GTAAI model's country choices outperformed the MSCI Global Equity Index by 0.2% in October, with the index itself shedding 1.2%. The model was concentrated in Italian, Swiss, and U.S. equities. Italian stocks outperformed, but Swiss equities lagged.

For the bond component, the GTAAI model's selections underperformed the BofAML Global Investment Grade Government Index by 0.6%, which recorded a 1.7% loss (**Chart 2**). The model was underweight JGBs 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.

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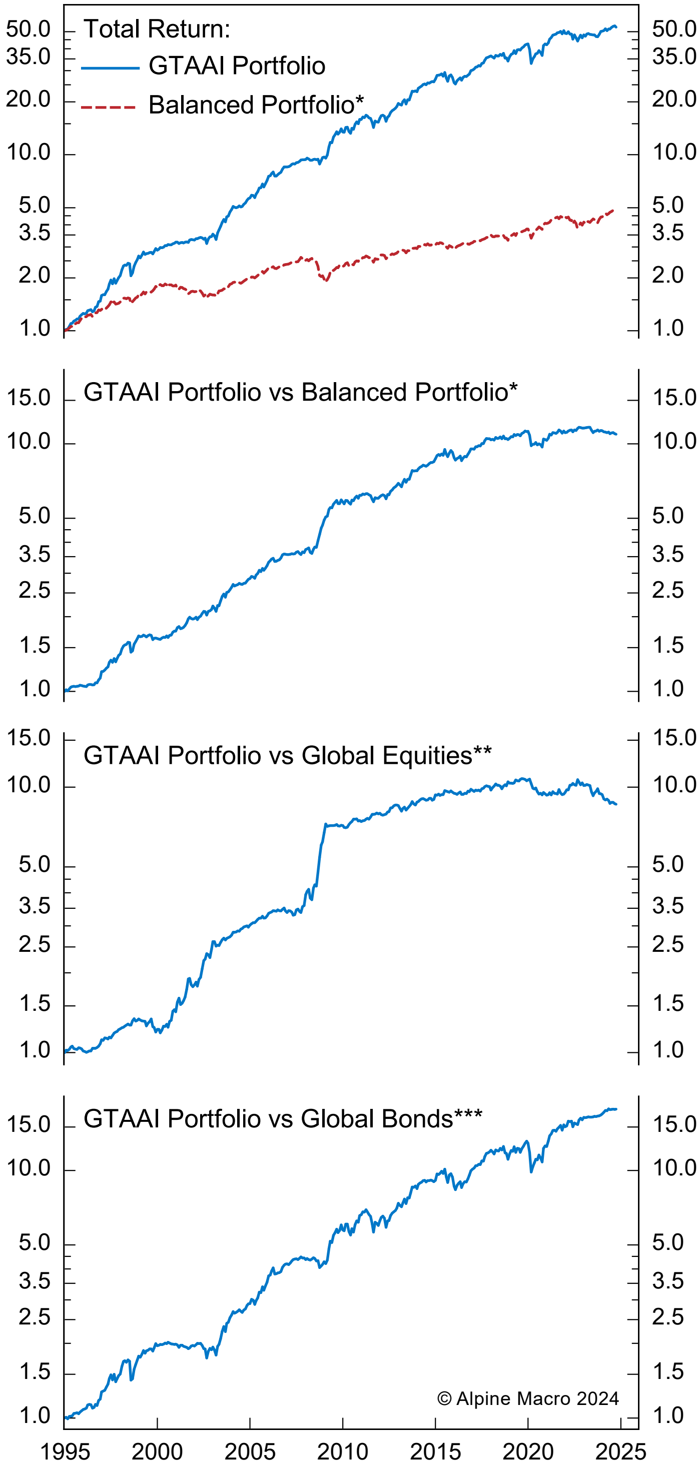
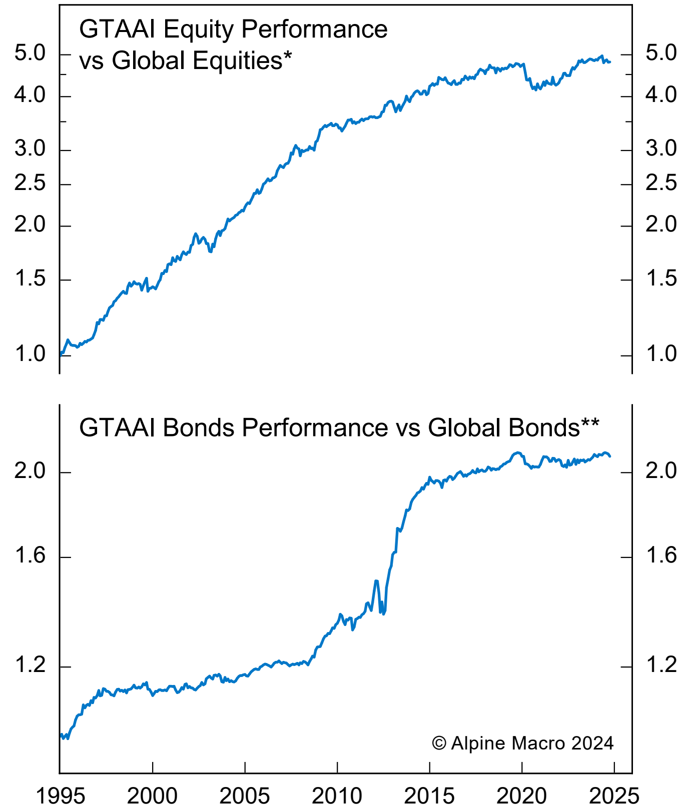
Chart 1 GTAAI Model Performance



*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 did not work out as the dollar strengthened. The dollar appreciated by 2.7% and 2.5% against the euro and the Swiss franc, respectively.

Model Allocations For November 2024

For November, the model trims some risk exposure, reducing the equity allocation to 49% from 56% in October. The bond allocation rises by 7% to 49%, and the gold weight increases to 3%. The GTAAI assigns almost no weight to commodities (Chart 3). Table 1 provides the model's allocation details.

Chart 3 GTAAI Asset Class Allocation

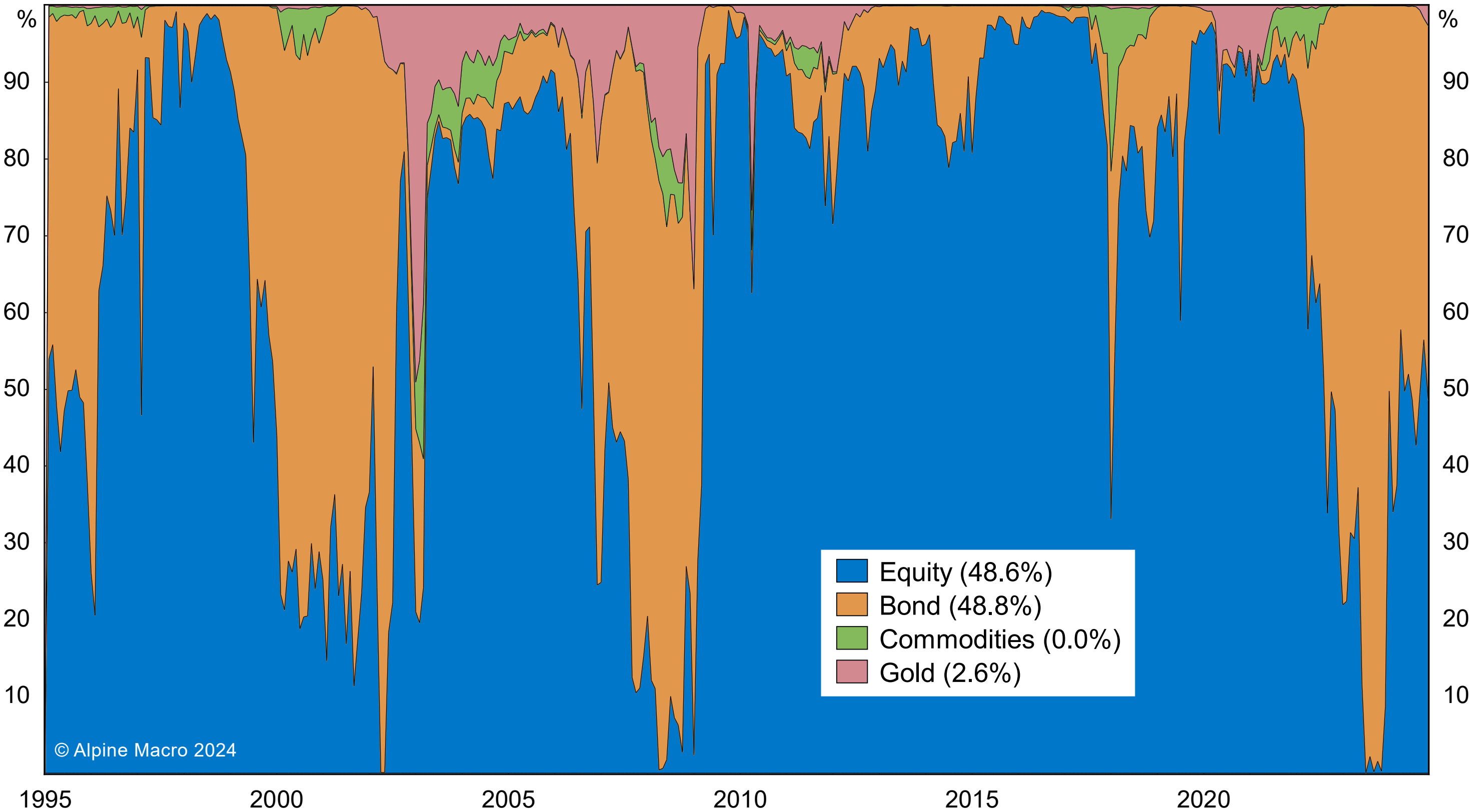


Table 1 Current GTAAI Model Allocations

	November 2024				October 2024			
	Equity (%)	Bond (%)	GSCI (%)	Gold (%)	Equity (%)	Bond (%)	GSCI (%)	Gold (%)
Australia	0.2	5.9			0.1	3.8		
Canada	0.2	2.4			0.5	2.4		
Switzerland	15.5	0.8			11.8	0.8		
Germany	0.5	8.7			0.5	7.8		
Emerging Markets	0.0	2.7			0.0	1.5		
Spain	1.7	0.0			1.7	0.0		
France	2.2	3.6			4.5	3.1		
U.K.	0.0	9.7			0.1	8.3		
Italy	15.8	0.1			18.9	0.1		
Japan	0.0	5.4			0.0	4.1		
Norway	1.3	5.2			0.2	5.7		
Sweden	0.3	0.6			0.1	0.9		
U.S.	10.9	3.8			18.0	3.3		
Total	48.6	48.8	0.0	2.6	56.4	41.9	0.0	1.7

Rounded to the nearest decimal point

The model remains lighter on stocks than its historical average. It is bullish on only a few equity markets but expects solid returns on bonds. The model believes global bond markets are oversold after the recent up leg in yields. Bond yields outside of the U.S. still have some distance to return to fair value.

The key bullish indicators for overall equities are the cycle indicator and improving money impulse. However, valuations are somewhat expensive, and momentum is overbought in certain countries.

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 And German Bonds

British gilts and German bunds are the model's preferred bond markets, together accounting for 40% of the overall fixed income allocation.

The gilt allocation rises to 10% from 8% in October. Gilt yields rose sharply in October after the U.K.'s new budget led markets to discount a larger deficit. The model does not directly account for fiscal policy, but this is reflected in a more pro-growth cycle indicator and higher fair value yields over time. The OECD leading economic indicator (LEI) for the U.K. is strengthening, although the model currently places limited weight on this factor.

The model views gilts as 1.8 sigma cheap versus fair value. The model takes into account a moving average of inflation and the policy rate. Inflation has fallen to 1.7% year-over-year basis. This should allow the Bank of England to further ease policy.

Moreover, gilts are 0.7 standard deviations oversold following the recent rise in yields. The currency indicator is also a minor headwind for this market.

German bunds receive an upgrade to a 9% weight for November. The valuation indicator suggests bunds are 1.1 standard deviations cheap. The model expects bund yields to trend lower toward fair value as the ECB cuts rates and eurozone disinflation continues.

Momentum for German bunds is near neutral, down from a peak of 2.4 sigma oversold. LEIs suggest that Germany's business cycle has peaked, which the model reads as a bullish signal for bunds.

Retain Allocation To Australian, Japanese And Norwegian Bonds

For November, the model's second-tier bond choices are Australian, Japanese and Norwegian bonds.

Australian bonds have cheapened after the recent selloff and are currently 1.5 sigma undervalued (Chart 4). Momentum is also slightly oversold at 0.4 standard deviations.

However, both the cycle and currency indicators are bond bearish. The Australian business cycle has been improving significantly, which puts upward pressure on yields.

The JGB allocation rises to 5% for November. Japanese bonds have cheapened significantly in recent quarters as JGB yields have increased. Although the BoJ is hiking rates and Japanese inflation is above 2%, the model does not see a

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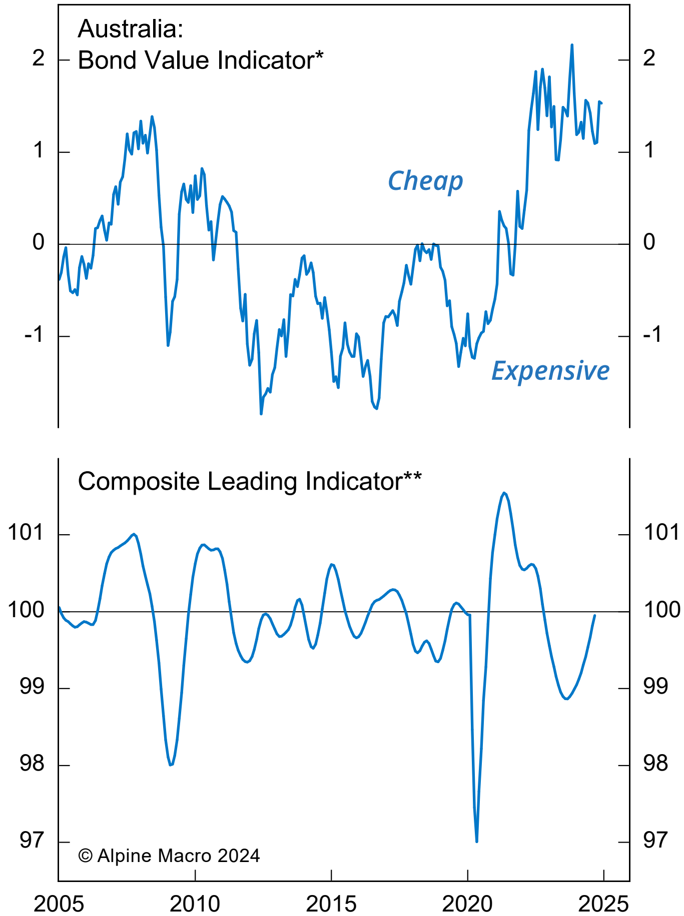
Chart 4 Australian Bonds Are Cheap But Face Cyclical Headwinds



*Alpine Macro proprietary indicator
**Amplitude adjusted; source: OECD

major rise in fair-value JGB yields. The model views Japanese bonds as 1.5 standard deviations cheap.

Momentum for JGBs is 0.8 standard deviations oversold. However, the yen contributed 11% against the decision to allocate to this market.

The Norwegian bond allocation drops to 5% from 6% in October. Valuations are 1.6 sigma cheap. Momentum is near neutral, but the currency is a significant headwind that limits a larger allocation to this market.

Favor Italian And Swiss Equities

The model's equity allocations remain heavily concentrated in Italy, the U.S., and Switzerland.

The Italian equity allocation decreases to 16% from 19% last month, mainly due to a shift in momentum. Following last month's outperformance, momentum is now 0.6 sigma overbought versus a 1.2 sigma oversold reading in October.

Nevertheless, the money impulse indicator for Italy continues to improve. This reflects signs of endogenous credit creation and is the most important factor driving allocation to this market.

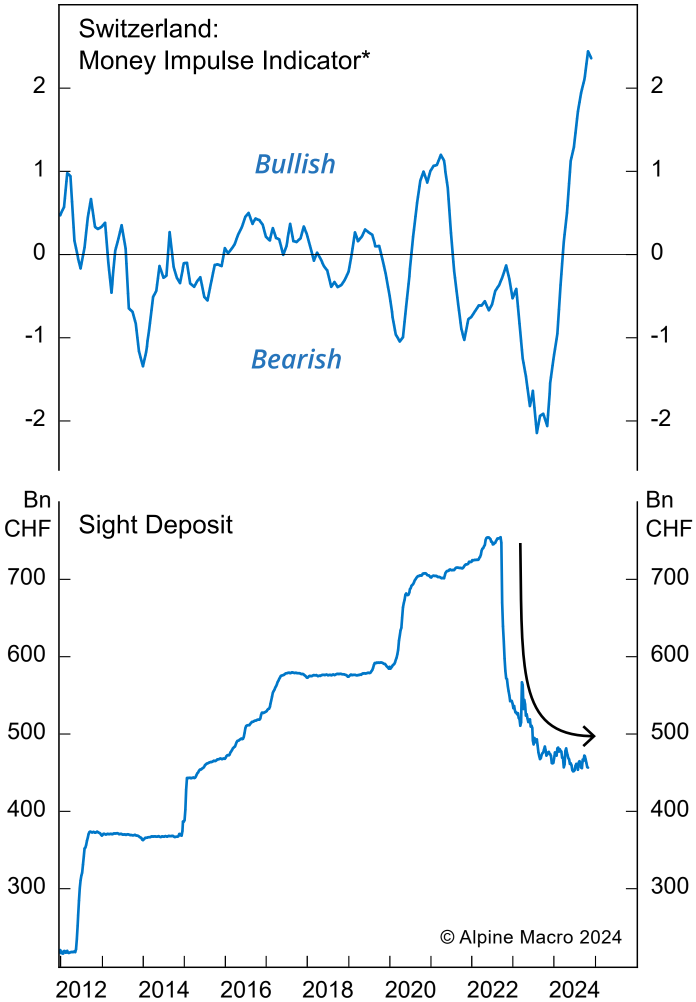
The liquidity indicator contributes 20% to the decision to allocate to this market. However, there has been some deterioration in this indicator over the past month. BTP-bund spreads have also risen by over 15 basis points.

Italy's earnings growth outperformance has plateaued after several quarters. The indicator is still positive but now only 0.3 sigma bullish. The Italian business cycle indicator shows a similar reading.

Swiss stocks receive a 16% 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 (**Chart 5**). Sight deposits have stabilized after months of decline.

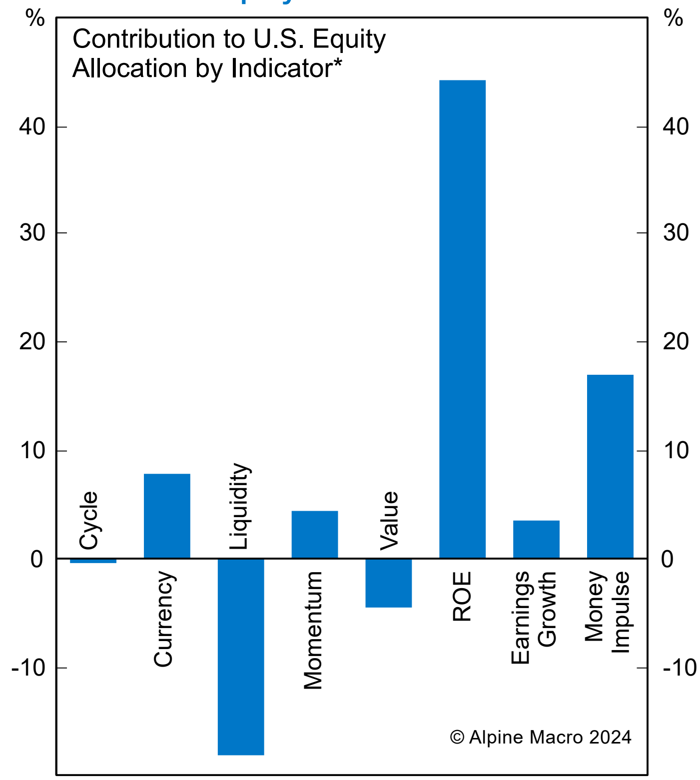
The model favors this market primarily for its strong return on equity (ROE) indicator. Momentum is no longer overbought. Recent currency dynamics have become a tailwind, as CHF weakness should boost local currency returns.

Chart 5 Swiss Money Impulse Is Improving



*Alpine Macro proprietary indicator

Chart 6 Drivers Of The U.S. Equity Allocation



*Absolute value sums up to 100%; positive contribution means the indicator favored allocation to this market

Downgrade U.S. Stocks

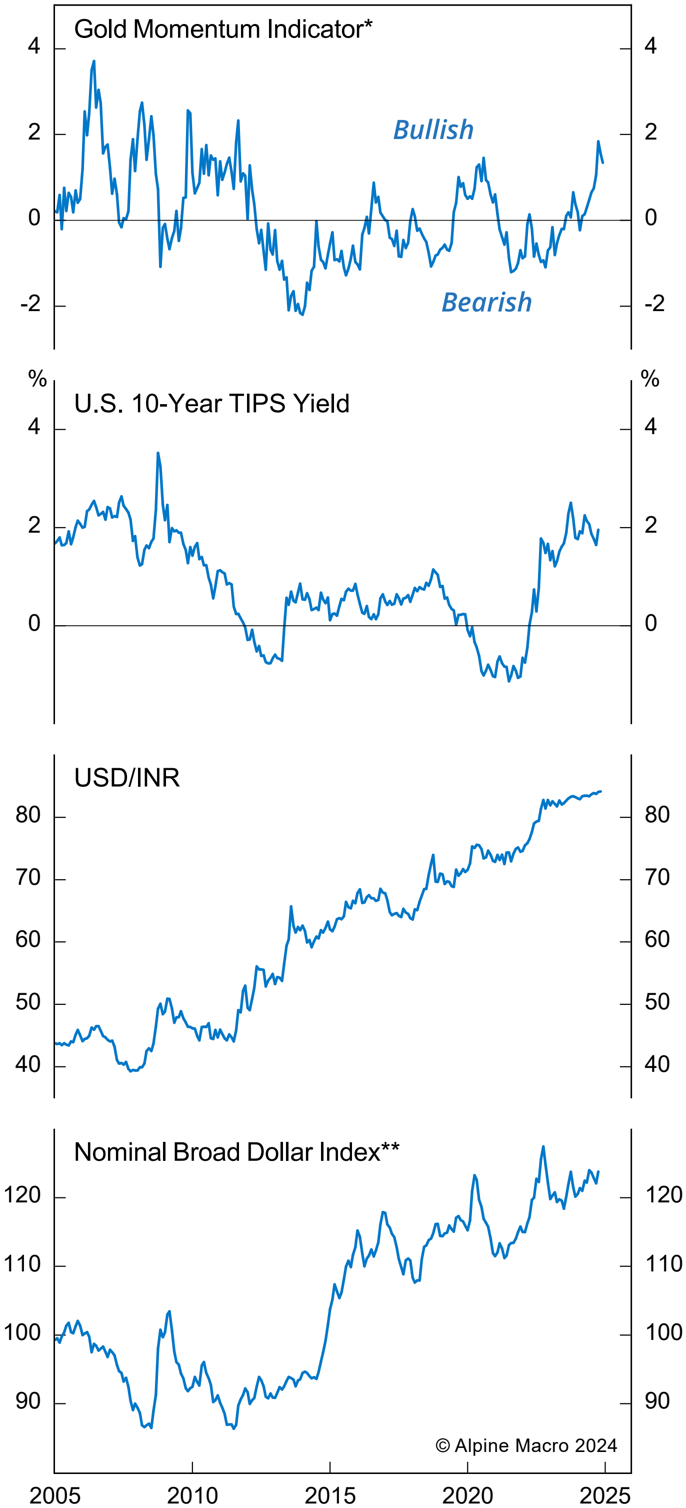
The model downgrades the U.S. equity allocation to 11%, down 7% from October. Here is the model's assessment of this market (**Chart 6**):

- The money impulse indicator, which tracks the second derivative of M2, is 1.1 standard deviations bullish. The indicator has rebounded on the back of credit creation despite ongoing quantitative tightening by the Fed.
- The ROE indicator is a key driver of allocation for the U.S. 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 shows some tightness as money market spreads widened at the end of October.
- The currency is bullish and contributed 8% to the decision to allocate to U.S. stocks.

Increase Gold Allocation

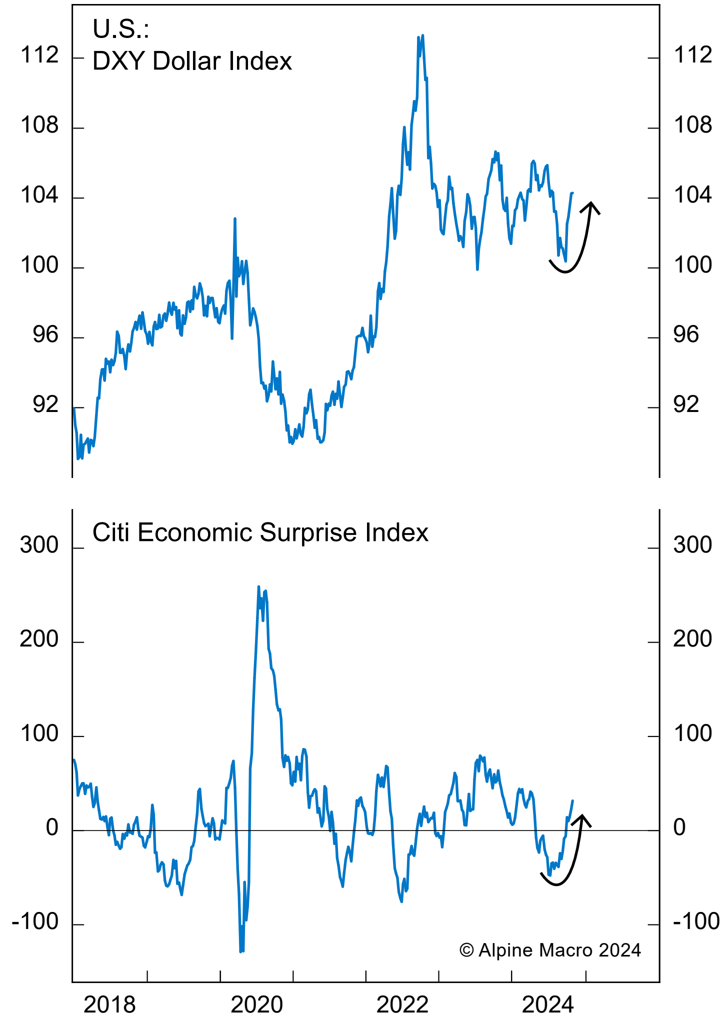
The model's gold allocation rises to 3% from 2% in October. Momentum is 1.5 standard deviations bullish (**Chart 7**). Gold tends to experience large cyclical swings, and the model expects this rally has further to run.

Chart 7 Gold Has Momentum But Fundamentals Have Yet To Improve



*Alpine Macro proprietary indicator
**Source: Federal Reserve

Chart 8 Strong U.S. Economy Is Supporting The Dollar



Fundamentals have not yet turned favorable, with TIPS yields rebounding and the dollar appreciating. The INR, a proxy for physical gold demand, has remained relatively flat.

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 hedging local currency exposures as the U.S. economy continues to surprise on the upside (**Chart 8**). The market is repricing the terminal Fed funds rate. With interest rate differentials moving in favor of the dollar, the greenback is likely to remain supported.

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