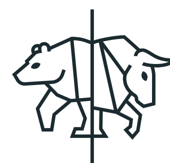
Market Digest – March 2021



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Impact of rising rates

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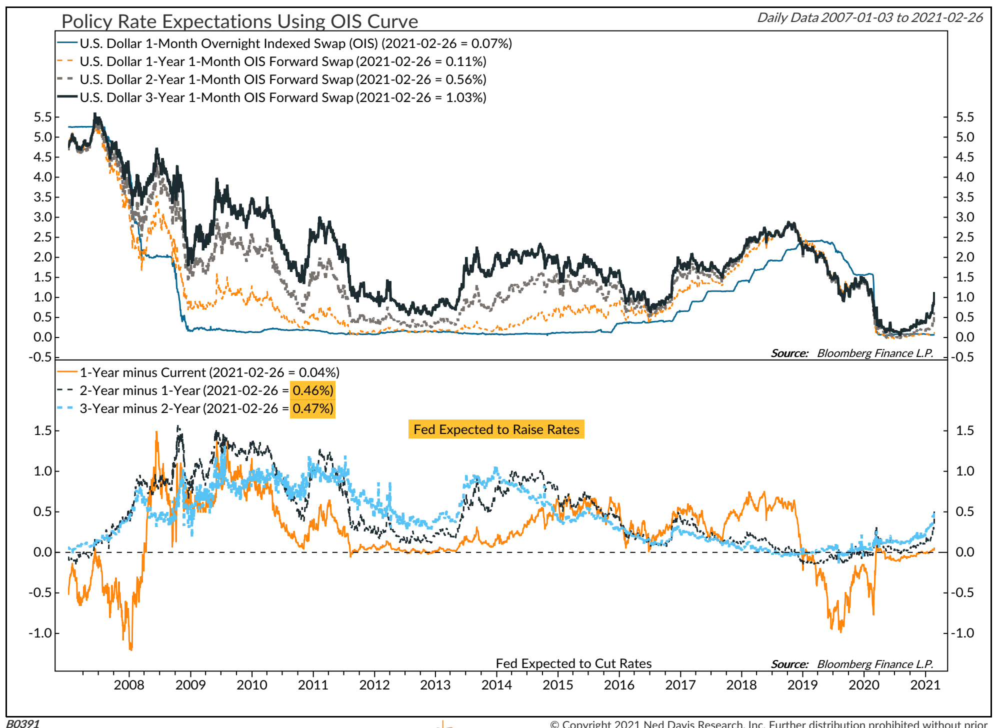
MARCH 15, 2021

Executive Summary

In early March, the 10-year Treasury yield blew through our 1.50% support and soaring to as much as 1.60%. The so-called "belly" of the curve moved even more than bonds, causing the market to price in two rate hikes over the next two years **(chart above)**. As long as yields are rising for the right reasons such as increased confidence in the economic outlook, progress on vaccine deployment, and additional fiscal support, the Fed appears to be complacent with its current policy. Over the past few weeks, we have made some position changes to align us better with the economic recovery.

Market looking for two rate hikes in next two years



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Global and U.S. Economy. Global growth accelerated in February, according to the latest PMIs, accompanied by higher price pressures. Manufacturing continued to lead the recovery, but the services sector is showing signs of life. The U.S. jobs market continues to rebound and housing continues to be a bright spot for the U.S. economy.

Global Asset Allocation. On February 18, we increased our recommended stock allocation to the maximum of 70%, shifting 5% from bonds (underweight at 20%) to stocks and 5% from bonds to cash (marketweight at 10%) which got us in line with our global balanced account model. On March 4, we also downgraded gold to neutral.

Fixed Income. With the 10-year yield rising, we took the opportunity on March 3 to reduce duration again to 85% of benchmark. We also downgraded investment grade credit to marketweight and upgraded MBS and ABS to overweight. Additionally, we made some minor shifts in our global bond allocation.

U.S. Stock Market. On March 3, we shifted from neutral to favoring Value on a tactical, short-term basis. The 2021 earnings recovery should be driven by cyclical Value stocks, regardless of the yield curve's slope.

U.S. Sectors. On March 11, we upgraded Energy to overweight and downgraded Health Care to underweight, which got us more in line with our upgrade of Value stocks.

Thematic Opportunities. Plunging COVID cases helped make Travel-related the top performing theme. Themes with strong momentum including Clean Energy, EVs, and Cannabis cooled off in 2H February. Tech-driven themes could underperform if the growth-scarcity premium reverses.

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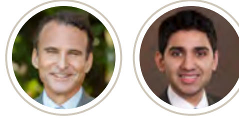

TIM HAYES, CMT CHIEF GLOBAL INVESTMENT STRATEGIST
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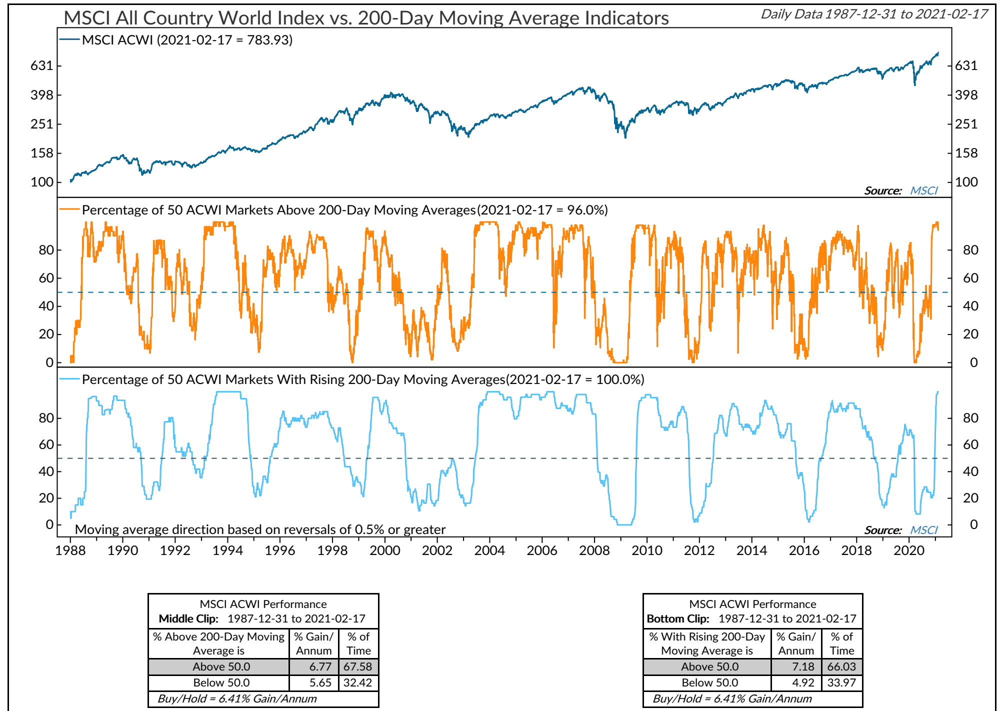
MARCH 15, 2021

Upgraded to maximum overweight stocks

Key Takeaways

- Now at max overweight stock exposure of 70%, underweight bonds at 20%, and marketweight cash at 10%.
- Downgraded gold to neutral recognizing death cross signal and influence of rising bond yields.
- Leaders became laggards in rotation, now global breadth is improving again as concentration is receding.

Bullish global market breadth



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Final upgrade

On February 18, we increased our recommended stock allocation to the maximum of 70% — the fourth and final in a series of upgrades that started when we shifted from underweight to marketweight June 2020.

The move was in response to the intra-month estimates from our Global Balanced Account Model and the indicator improvement reflected by our Rally Watch report. An implication of this broad-based indicator improvement is that we've seen a reset of the secular bull market that started in 2009. For the first time since the secular bull started, we saw all 50 All Country World Index (ACWI) component markets above their 200-day moving averages and were rising at the beginning of February **(chart above)**.

Another sign of the secular bull reset is the ACWI response to the excess liquidity — which has risen at a 17% per year pace since the initial reading in June 2019.

The current rally is also looking more consistent with a bull market than a bear — corrections have tended to be less frequent during secular bulls. The S&P 500 has now advanced for 72 days without a 5% correction, and 227 days without a 10% decline.

While it now appears likely that another secular bull upleg is underway, the secular potential may again be in question if reflation leads to overheating, moving the central bankers and bond vigilantes to lower the temperature. Fortunately, between now and then there should be substantial time and upside potential for stocks to continue trending higher.

Above excerpted from: "Final upgrade in a secular bull reset" by Tim Hayes, February 18, 2021

Neutral on gold

Since the bond yield lows last August, the yield ascent has been bad news for gold, which has been retreating to lower lows as yields have been rising to higher highs. The **chart at right** shows gold and the Global Aggregate Bond Yield maintaining an inverse correlation that has strengthened.

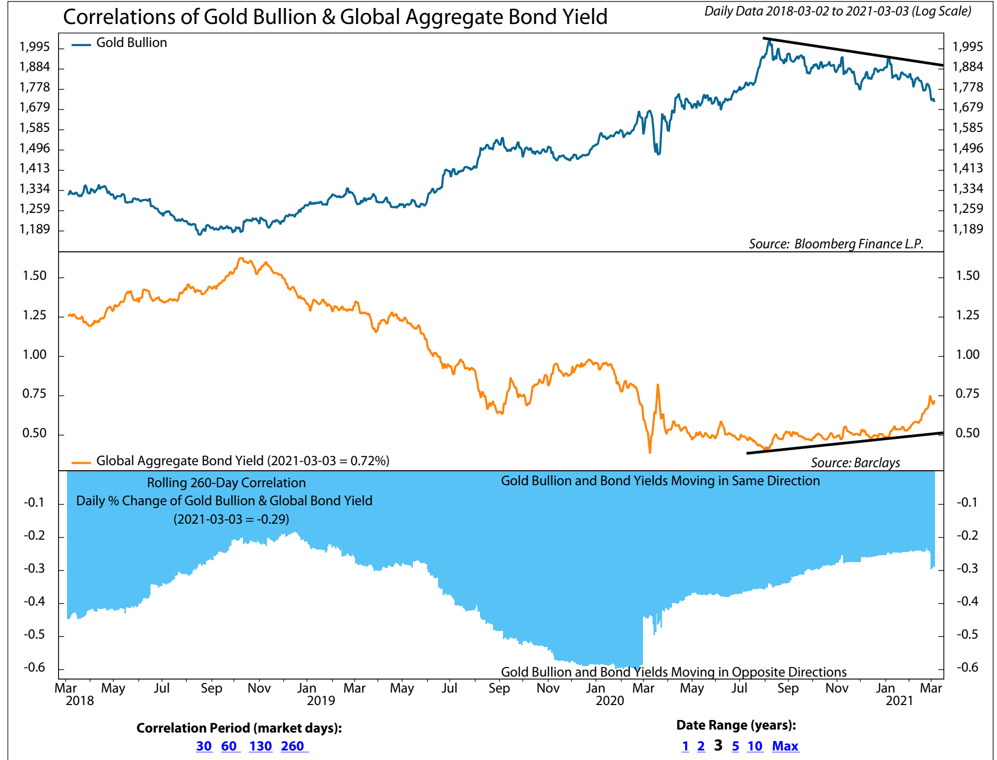
In descending to its lowest levels since June, gold has broken below both its 50- and 200-day moving averages — a bearish “death cross” signal **(chart below)**. Given the inverse correlation, gold should remain under pressure if bond yields continue to trend higher — which we expect — but it hasn’t become evident gold is heading into a sustained down-trend. The long-term uptrend remains intact.

Considering the status of gold’s long-term uptrend and the dollar’s continuing downtrend, we have cut back to neutral but not bearish, also recognizing sentiment, commodity performance, economic liquidity, real rates, and inflation expectations in assuming the neutral position. These considerations support the prospects for an eventual recovery and reassertive advance.

It’s currently more likely that our next move will return our gold position to bullish than drop it further to bearish once the Gold Watch report bullish indicators return to a majority.

Above excerpted from: “In the midst of mixed messages, now neutral on gold” by Tim Hayes, March 4, 2021

Gold has declined as yields have risen



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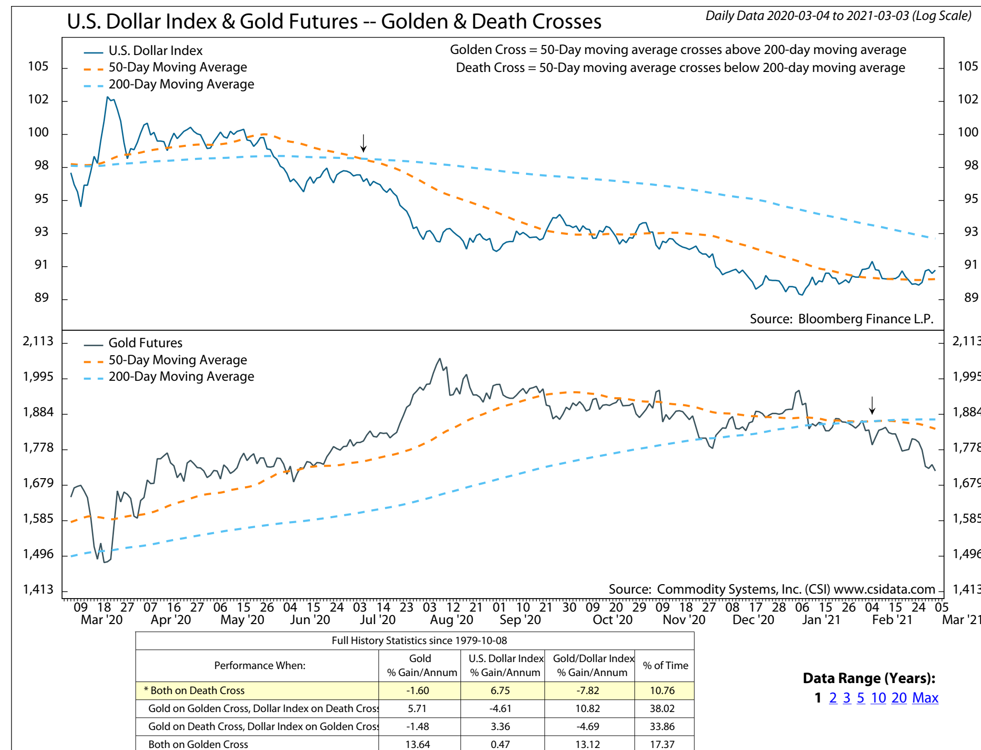
Long-term trends still intact



Full History Statistics since 1979-10-08

Performance When:	Gold % Gain/Annum	U.S. Dollar Index % Gain/Annum	Gold/Dollar Index % Gain/Annum	% of Time
* Both on Death Cross	-1.60	6.75	-7.82	10.76
Gold on Golden Cross, Dollar Index on Death Cross	5.71	-4.61	10.82	38.02
Gold on Death Cross, Dollar Index on Golden Cross	-1.48	3.36	-4.69	33.86
Both on Golden Cross	13.64	0.47	13.12	17.37

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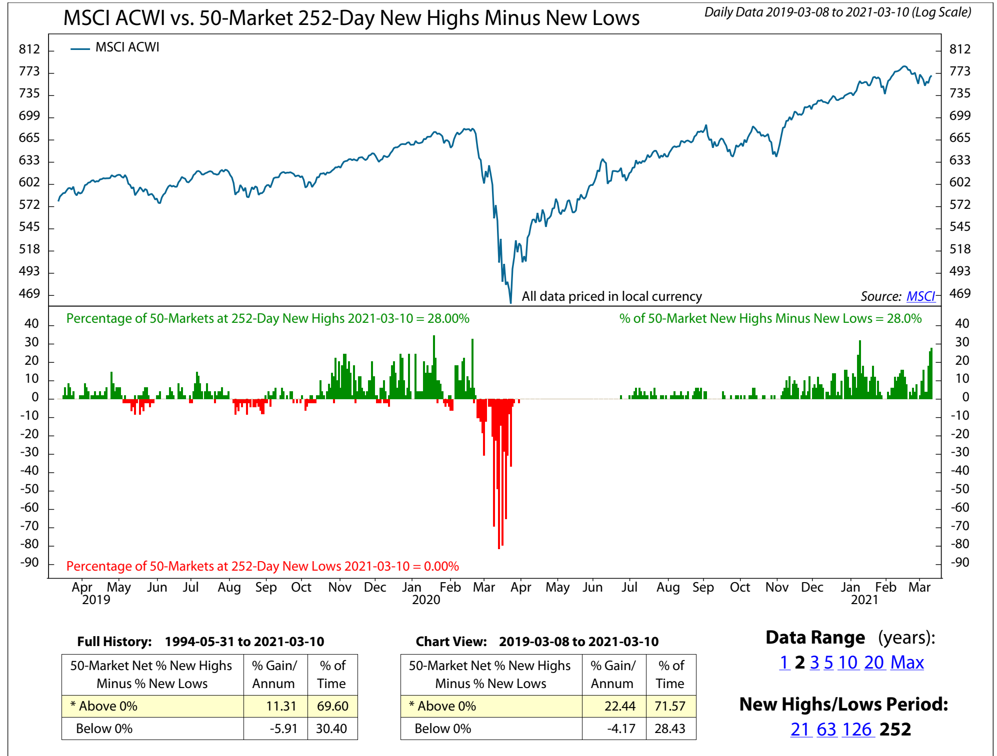
Convergence and global breadth

The indicator improvement thus far in 2021 led to lingering optimism, leaving the outperformers vulnerable to a negative surprise. That turned out to be the acceleration of bond yields, which sparked the rotation that started last month. But a broad-based decline has not materialized. And after limited deterioration, the global breadth has been improving again, with more than a quarter of the ACWI markets back at one-year highs **(chart right)**.

The convergence is evident when comparing returns from the ACWI's high on February 16 to its low on Monday, March 8, a period in which the previous leaders became laggards. Among global markets, China has had the most dramatic reversal in fortune. Like the other former leaders that became laggards during the recent rotation, the Chinese market can be expected to return as a participant in the broad global advance.

Breadth improving again



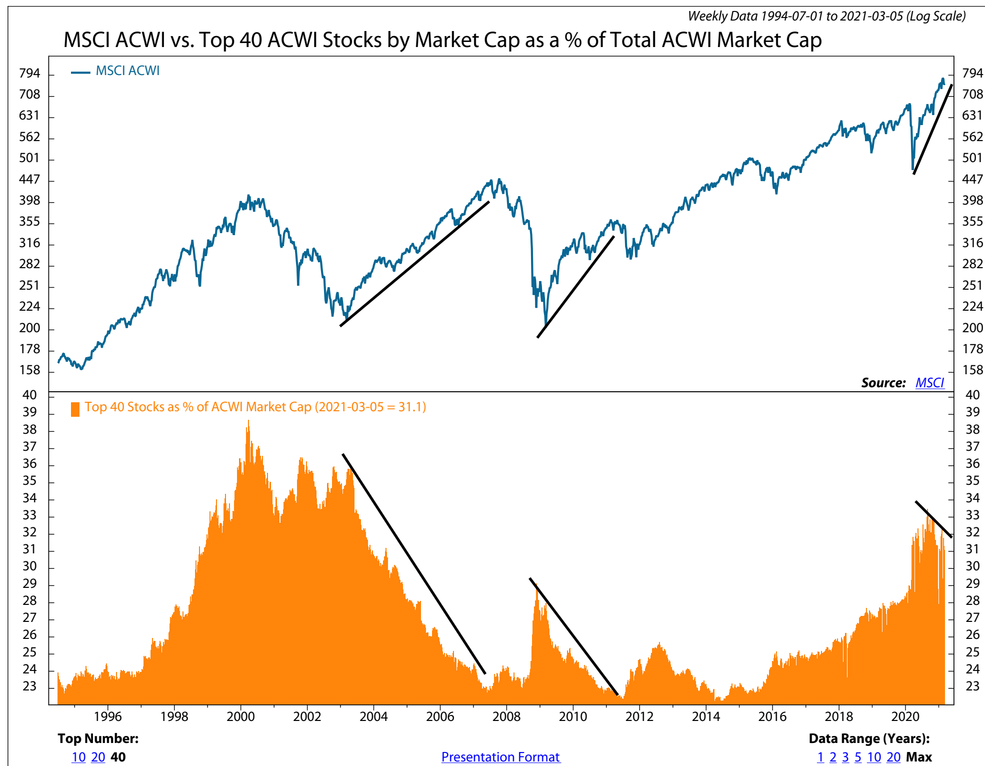
Full History: 1994-05-31 to 2021-03-10

50-Market Net % New Highs Minus % New Lows	% Gain/ Annum	% of Time
* Above 0%	11.31	69.60
Below 0%	-5.91	30.40

Chart View: 2019-03-08 to 2021-03-10

50-Market Net % New Highs Minus % New Lows	% Gain/ Annum	% of Time
* Above 0%	22.44	71.57
Below 0%	-4.17	28.43

Concentration receding



Fortunes also reversed among the 11 ACWI sectors, causing a healthy convergence of relative strength momentum. A continuation of this trend would be consistent with a broad advance, much as it was after the secular bottom in 2009.

As the global advance has broadened, it has become less dependent on the megacaps to pull it higher **(chart left)**. It would be encouraging to see a continuation of this trend.

Above excerpted from: "Convergence and global breadth" by Tim Hayes, March 11, 2021

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MARK PHILLIPS NDR EUROPEAN EQUITY ANALYST

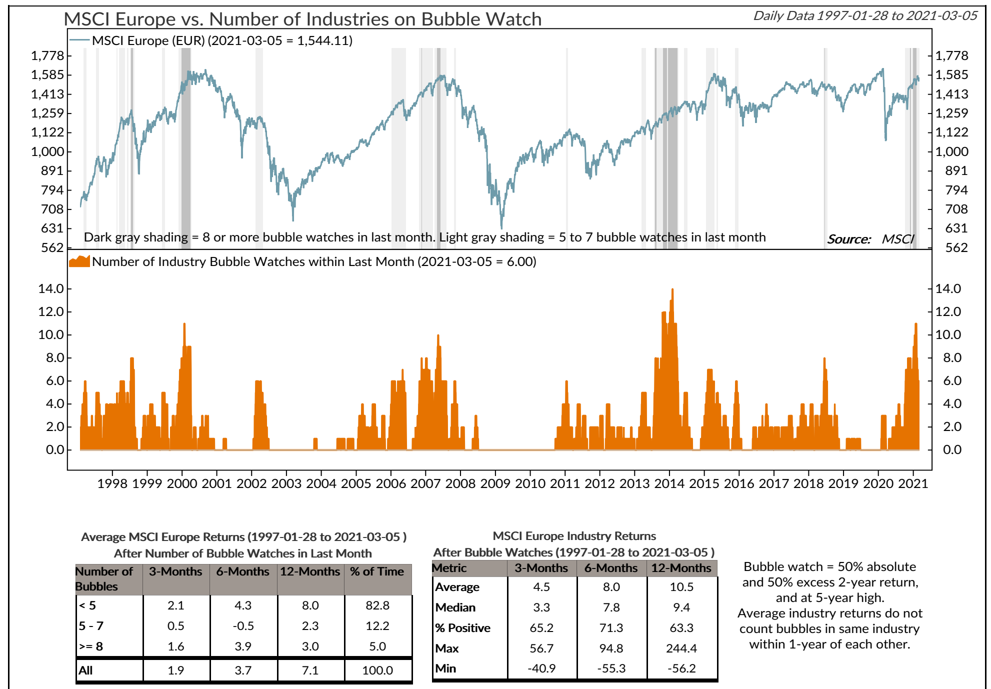
MARCH 15, 2021

Bubbles forming in Europe

Key Takeaways

- We identified three industry bubbles last month, which could potentially signal risk for the broader European stock market.
- However, technical and macro indicators still support the bullish case for European stocks.
- Outperformance by the European Materials sector has been driven by the Metals and Mining industry.

Comparisons with 2000 and 2007?



Average MSCI Europe Returns (1997-01-28 to 2021-03-05)
After Number of Bubble Watches in Last Month

Number of Bubbles	3-Months	6-Months	12-Months	% of Time
< 5	2.1	4.3	8.0	82.8
5 - 7	0.5	-0.5	2.3	12.2
>= 8	1.6	3.9	3.0	5.0
All	1.9	3.7	7.1	100.0

MSCI Europe Industry Returns
After Bubble Watches (1997-01-28 to 2021-03-05)

Metric	3-Months	6-Months	12-Months
Average	4.5	8.0	10.5
Median	3.3	7.8	9.4
% Positive	65.2	71.3	63.3
Max	56.7	94.8	244.4
Min	-40.9	-55.3	-56.2

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We identified three European industry bubbles in the last month — all of which are technology related — and three other industries meeting our Bubble Watch criteria. Such a high number of potential bubbles suggests a high degree of speculation like that around the stock market peaks in 2000 and 2007, and some caution could be warranted.

The **chart above** shows that since 1999, industries which have been in a bubble and at a five-year peak posted an average negative 7.7% total return in the following year. Further, periods when there were two or more industry bubbles within the last month were followed by an average negative total return of 6.3% in the MSCI Europe index.

Presently, economic conditions and trend indicators remain favorable for European stocks. The situation today is different from the deterioration in trend indicators and economic outlook we saw in 2000 and 2007, and which portended to significant drawdowns in stocks.

Recent stock market turbulence has been preceded by a rapid increase in bond yields and risk assets becoming overbought. Further, diverging breadth could suggest that some near-term weakness or consolidation is possible.

Strong technical and economic indicators are supportive for the tactical outlook for European stocks and we do not see the high number of industry bubbles in the European market as cause for concern just yet.

We remain constructive on European stocks.

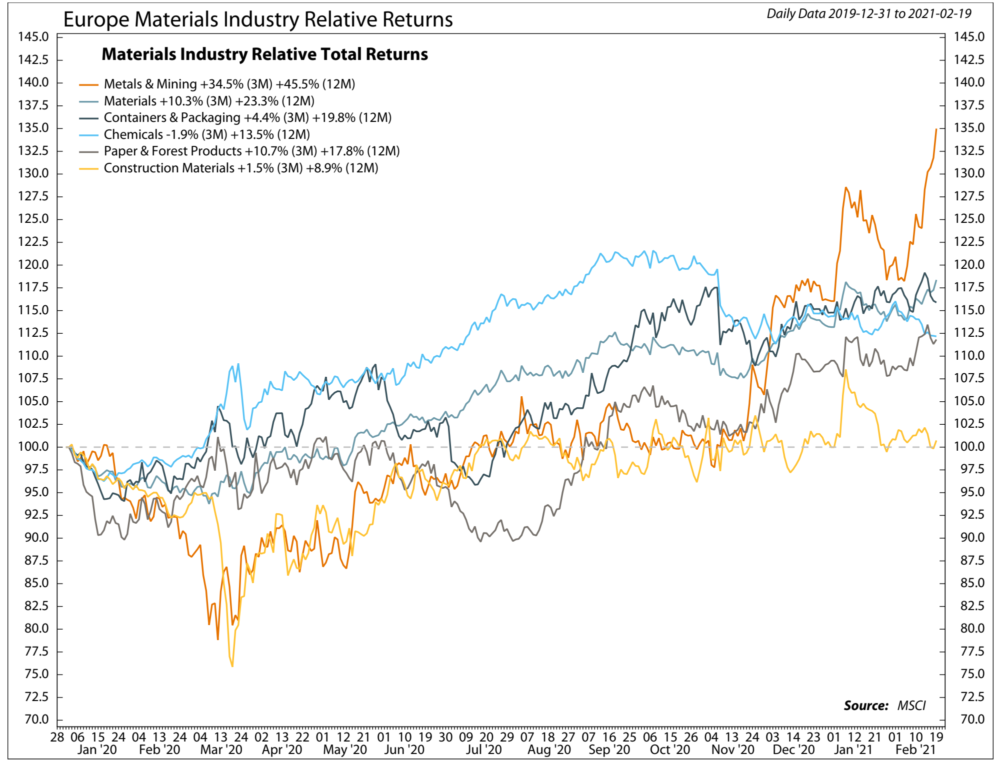
Above excerpted from: "European industry bubbles and market" by Mark Phillips, March 9, 2021 (available through NDR's new Europe Strategy product)

Metals and mining boom

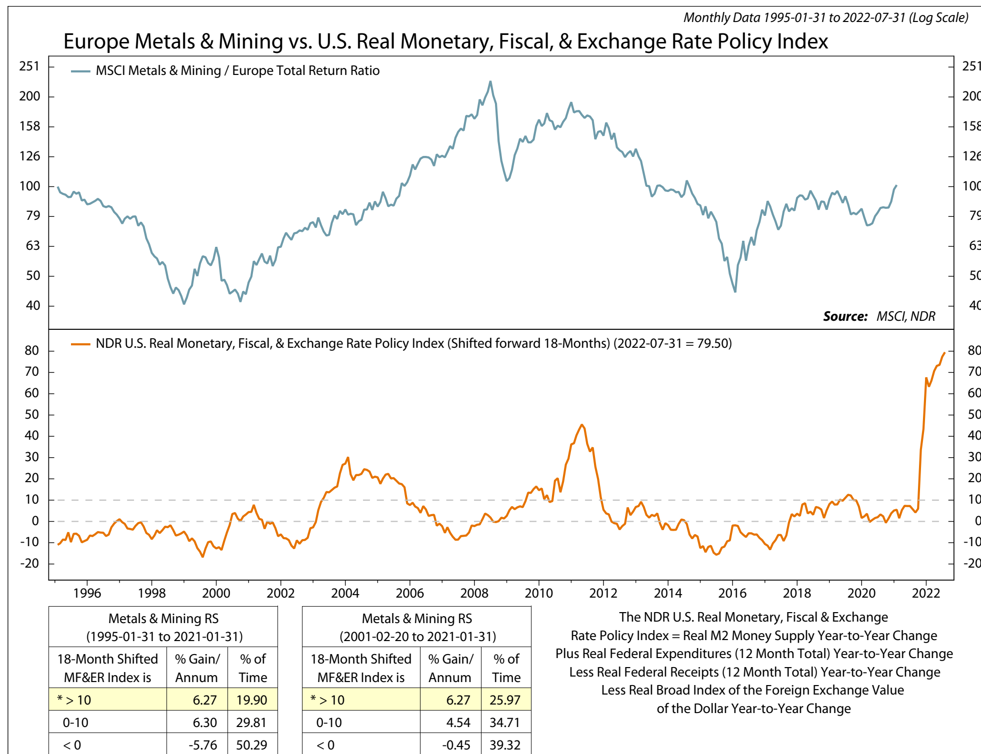
The **chart at right** shows that the MSCI Europe Materials sector has outperformed the broader market by 10% over the last three months, with four out of five of its industries outperforming.

It also illustrates the divergence between the two largest sectors — a 35% outperformance by the Metals and Mining industry in the last three months being offset by a -2% underperformance from the Chemicals industry.

Metals and Mining outperforms by 35%



Monetary and fiscal stimulus bullish



Metals & Mining RS (1995-01-31 to 2021-01-31)		
18-Month Shifted MF&ER Index is	% Gain/ Annum	% of Time
* > 10	6.27	19.90
0-10	6.30	29.81
< 0	-5.76	50.29

Metals & Mining RS (2001-02-20 to 2021-01-31)		
18-Month Shifted MF&ER Index is	% Gain/ Annum	% of Time
* > 10	6.27	25.97
0-10	4.54	34.71
< 0	-0.45	39.32

We see the current reflationary environment as broadly favoring the Materials sector. An improving economic outlook is particularly favorable for the Metals and Mining industry, but less so for the Chemicals industry.

The technical, macro, and fundamental picture is positive for the Metals and Mining industry, and we view further outperformance as likely. Monetary and fiscal stimulus in the U.S. and Europe offers further support to the bullish case for the European Metals and Mining industry **(chart left)**.

Above excerpted from: "European equities – metals and mining boom" by Mark Phillips, February 23, 2021 (available through NDR's new Europe Strategy product)

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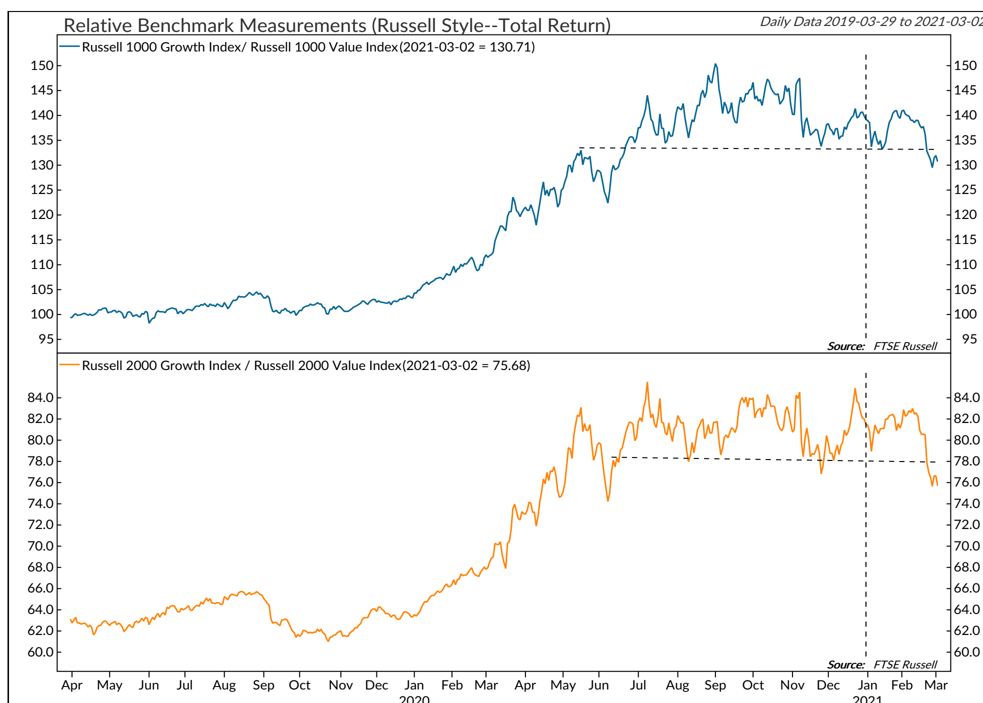
MARCH 15, 2021

Shifted to favoring Value

Key Takeaways

- We shifted from neutral to favoring Value on a tactical, short-term basis.
- The cyclical Value sectors we have favored for months are strong enough to support broader Value benchmarks over Growth benchmarks.
- The 2021 earnings recovery should be driven by cyclical Value stocks regardless of the yield curve's slope.

Growth/Value ratios breaking key support



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Next step in a process

On March 3, we shifted our tactical, short-term style recommendation from neutral to favoring Value over Growth. Consistent readers of our work should find this change unsurprising, as we have been listing indicators to watch in publications for months. The rotation to Value has been happening in stages. Even though we have been highlighting that cyclical Value sectors have been outperforming for months — Rob Anderson has been overweight Financials and Industrials — the broader Russell Value benchmarks had been in a trading range versus their Growth counterparts before breaking key support **(chart above)**.

Multiple reasons

Consistent with the NDR approach, our shift to Value is not based on one data point, but enough indicators lining up to tilt the weight of the evidence. Technical models, the interest rate environment, and economic conditions all favor Value. Importantly, the singular emphasis on the yield curve is missing a broader message.

Models lining up

Our trend models have continued their gradual shift to Value and are likely to continue to do so.

The intermediate-term trend models for the Russell 1000 Growth/Value ratio and Russell 2000 Growth/Value ratio were the first to favor Value in mid-2020. The long-term trend model exited its favoring-Growth zone for the first time since December 2019 this month.

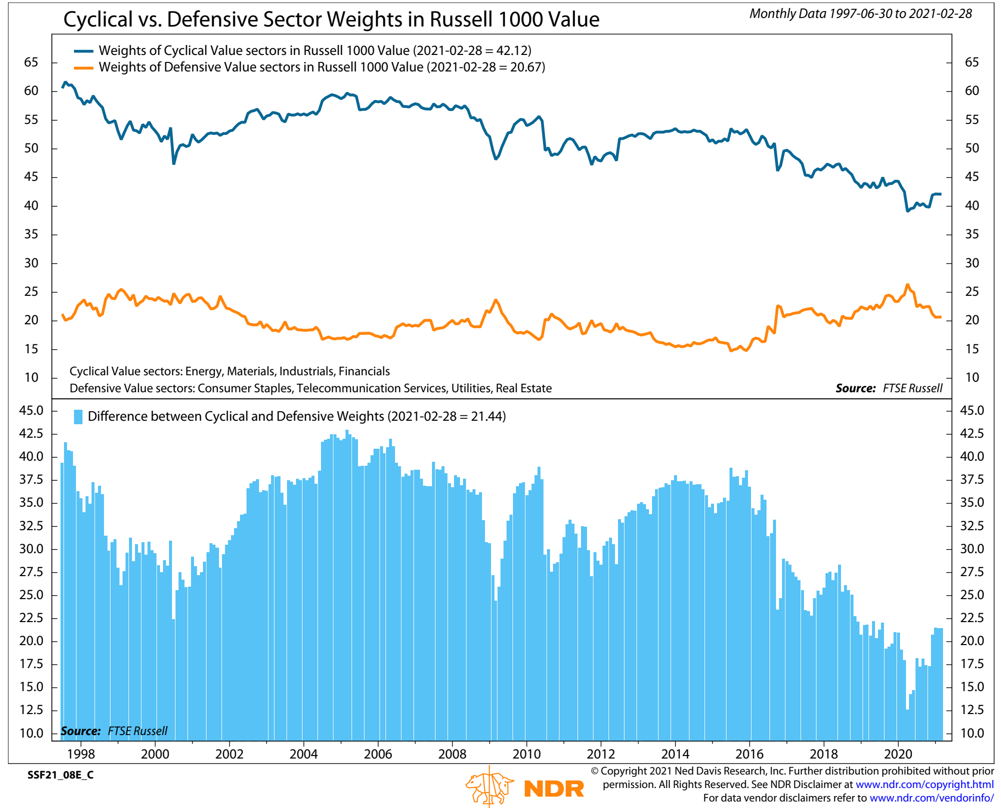
The internal composite within our flagship Growth/Value model continues to favor Growth. However, four indicators are close to switching: the Growth/Value ratio, Growth/Value moving averages, percentage of stocks above their 200-day moving averages, and net new highs.

Cyclical vs. defensive Value

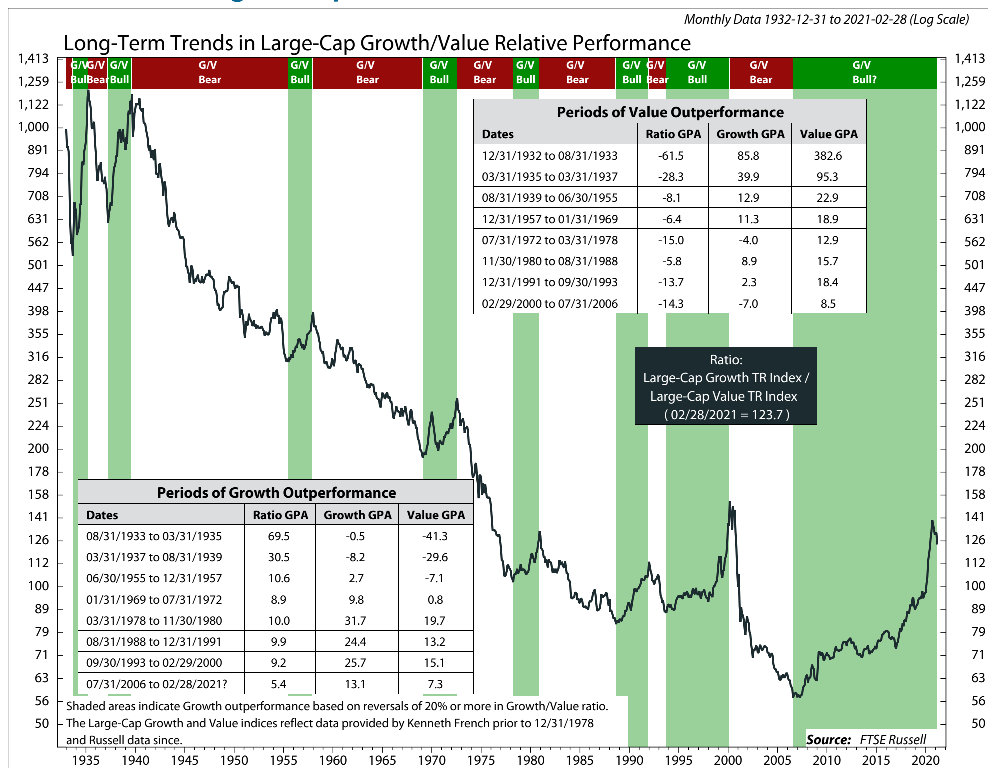
Benchmarks are often considered static, but in reality, they change over time. This is especially true for style benchmarks. For example, the Russell 1000 Value Index has grown less cyclical in the past 15 years. The **chart at right** shows the weights of cyclical Value sectors (Energy, Materials, Industrials, and Financials) and defensive Value sectors (Consumer Staples, Utilities, Real Estate, and the Telecom industry) in the Russell 1000 Value Index.

Cyclical sectors have had a bigger weight since at least 1997, but the spread shrank from 43.0% in February 2005 to 12.6% in March 2020. Consequently, the rebound in cyclical Value sectors in recent months has had a smaller impact on the Russell 1000 Value than in previous years. That may change going forward, but it explains why the Russell benchmarks traded sideways for eight months even as what some would think of as a generic concept of "Value" outperformed.

Cyclical sectors a smaller weight in Russell 1000 Value Index



Is Value exiting a 15-year secular bear vs. Growth?



Periods of Value Outperformance

Dates	Ratio GPA	Growth GPA	Value GPA
12/31/1932 to 08/31/1933	-61.5	85.8	382.6
03/31/1935 to 03/31/1937	-28.3	39.9	95.3
08/31/1939 to 06/30/1955	-8.1	12.9	22.9
12/31/1957 to 01/31/1969	-6.4	11.3	18.9
07/31/1972 to 03/31/1978	-15.0	-4.0	12.9
11/30/1980 to 08/31/1988	-5.8	8.9	15.7
12/31/1991 to 09/30/1993	-13.7	2.3	18.4
02/29/2000 to 07/31/2006	-14.3	-7.0	8.5

Periods of Growth Outperformance

Dates	Ratio GPA	Growth GPA	Value GPA
08/31/1933 to 03/31/1935	69.5	-0.5	-41.3
03/31/1937 to 08/31/1939	30.5	-8.2	-29.6
06/30/1955 to 12/31/1957	10.6	2.7	-7.1
01/31/1969 to 07/31/1972	8.9	9.8	0.8
03/31/1978 to 11/30/1980	10.0	31.7	19.7
08/31/1988 to 12/31/1991	9.9	24.4	13.2
09/30/1993 to 02/29/2000	9.2	25.7	15.1
07/31/2006 to 02/28/2021?	5.4	13.1	7.3

Secular vs. tactical

Growth has been in a long-term, secular bull market versus Value since 2006 **(chart left)**. During the last 15 years, Value has staged a few tactical rallies, but not anything resembling a secular shift. Whether this is a secular rotation to Value will depend on big picture macro factors like potential GDP, the interest rate regime, demographics, and mega-cap Growth stocks' fortunes. At this point, there is not enough evidence to support a secular rotation.

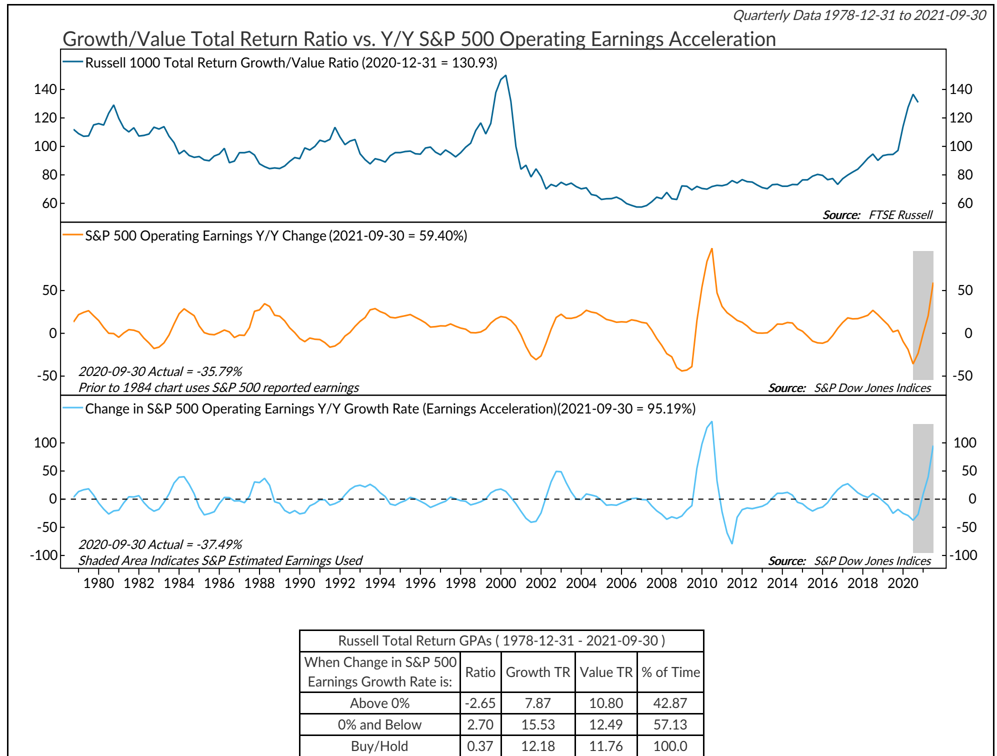
Above excerpted from: "Fully rotating into Value" by Ed Clissold, March 3, 2021

Earnings recovery

The spike in the 10-year yield has been blamed for the shift from Growth to value. However, a steeper yield curve is not universally bullish for Value and bearish for Growth. While cyclical Value sectors like Financials are the most positively sensitive (a steeper yield curve is bullish), defensive Value sectors are the most negatively sensitive.

Regardless of the yield curve, the earnings rebound should support Value over Growth. Earnings growth is set to skyrocket this year, as year/year comparisons match the shutdown in the first half of 2020 with the reopening in 2021. Accelerating earnings (EPS growth faster than a year ago) has historically favored Value over Growth **(chart right)**.

Accelerating EPS favors Value over Growth



Russell Total Return GPAs (1978-12-31 - 2021-09-30)

When Change in S&P 500 Earnings Growth Rate is:	Ratio	Growth TR	Value TR	% of Time
Above 0%	-2.65	7.87	10.80	42.87
0% and Below	2.70	15.53	12.49	57.13
Buy/Hold	0.37	12.18	11.76	100.0

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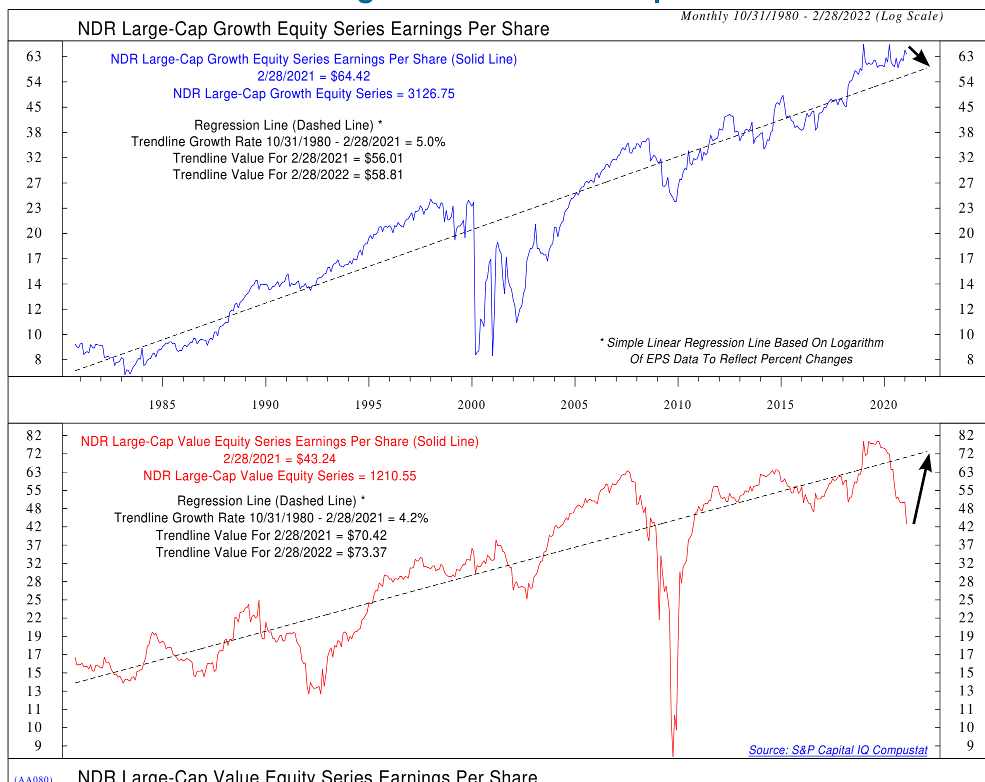
Value has more earnings mean reversion potential



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The reason is that cyclical Value sectors tend to have more volatile earnings, so they drive both declines and rebounds in overall EPS changes.

The **chart at left** indicates that Value should power the EPS rebound this year. Large-cap Growth EPS is 15.0% above its long-term trendline, while large-cap Value is 38.6% below. Earnings mean reversion potential is more prevalent in Value than Growth, as is typical in the early stages of an earnings recovery.

Above excerpted from: "More to Value rotation than interest rates" by Ed Clissold, March 9, 2021

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MARCH 15, 2021

Shifting more toward Value

Key Takeaways

- Upgraded Energy to overweight and downgraded Health Care to underweight.
- Macro environment and earnings recovery support the positioning.
- Energy has the best track record during periods of rising inflation.

Cyclical Value sectors with best breadth readings

Percent of Issues Above Moving Averages

Sector		Days: 10	50	100	SORT 200
Energy	**Cyclical Value sectors**	93.3	93.3	96.7	96.7
Financials		92.3	90.8	91.5	94.3
Materials		96.6	84.7	88.1	93.2
Industrials		88.3	81.6	85.3	91.3
Consumer Discretionary	**Cyclical Growth sectors**	80.2	69.8	80.8	89.5
Communication Services		58.7	58.7	76.1	86.7
Technology		37.6	33.0	58.2	81.5
Real Estate	**Defensive/bond proxy sectors**	79.8	69.0	78.6	79.8
Consumer Staples		87.9	74.1	72.4	71.9
Health Care		42.5	31.4	49.0	66.9
Utilities		96.1	74.5	45.1	66.7

Excerpted from report ESS_1500.

Source: S&P Capital IQ and MSCI, Inc. (GICS), NDR Multi-Cap Institutional (Universe)

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Sector shifts

When we added Energy to our shortlist of 2021 sector bounce-back candidates on December 23, we didn't anticipate such a strong move to begin the year. Back then, Energy was still trading almost 40% below its 52-week high, with one-fourth of the sector's constituents trading more than 50% below their one-year highs.

Fast forward to today, and Energy is leading the reopening trade, rising over 35% year-to-date. With NDR favoring Value over Growth and Energy's technical- and macro-based composites now bullish in our sector model, on March 11, we shifted further toward cyclical Value by adding 1% point of allocation to Energy and upgrading the sector to overweight.

We removed 2% points of allocation from Health Care and downgraded the sector to underweight, matching the sector model's February month-end downgrade. We also added 1% point of allocation to Materials, with the sector remaining an official marketweight recommendation.

Better breadth

Energy, along with all cyclical Value sectors, has seen improvement in long-term breadth readings. The **table above** shows all four cyclical Value sectors with greater than 90% of issues trading above their 200-day moving averages.

Cyclical Growth sector breadth has held up well despite the rotation from Growth to Value.

The weak links have been defensive and bond proxy sectors. Health Care currently has the second-lowest 200-day reading and the lowest 50-day reading.

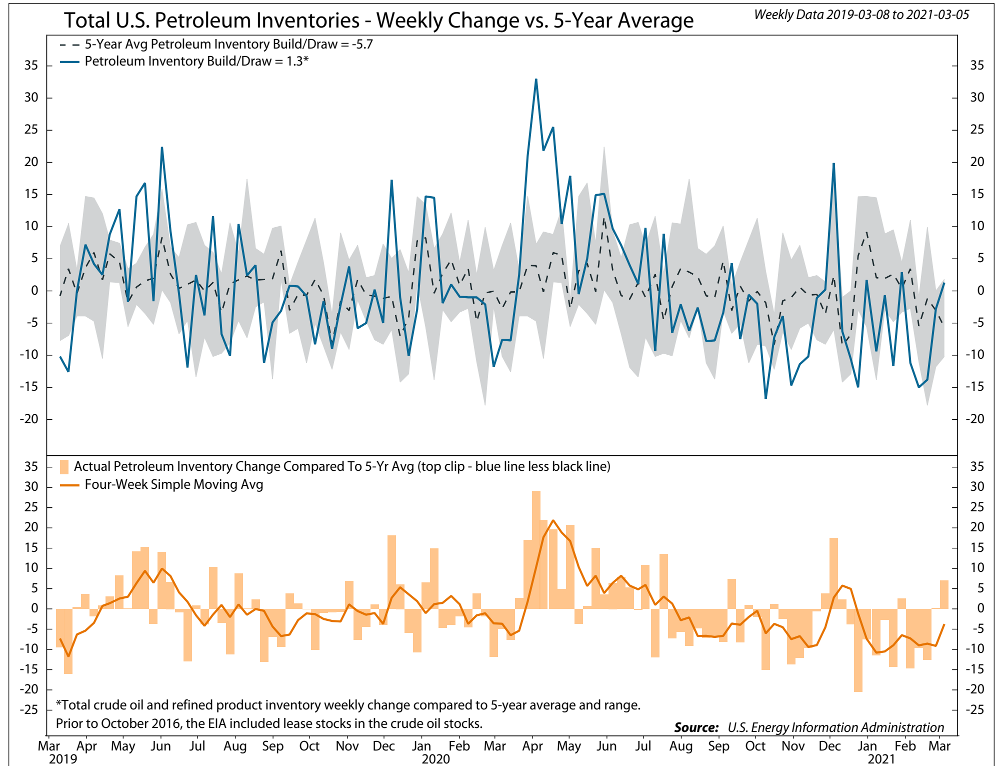
Cyclical Growth sectors have also seen weakening short-term breadth. Technology, for example, only has 33.0% of issues trading above their 50-day moving averages.

Bullish oil inventory reports

Energy's outperformance has been accompanied by rising crude oil prices, with the sector and the commodity maintaining their strong correlation despite the pandemic. WTI, after briefly falling into negative territory last April, has risen above its pre-pandemic level.

Behind the Energy and crude rallies is the winnowing out of huge stockpiles of oil that accumulated during the early stages of the pandemic. The **chart at right** shows that most 2021 U.S. petroleum inventory reports have been coming in below their seasonally adjusted averages. As a result, U.S. inventory of total petroleum products has fallen back to its five-year average.

Inventory readings mostly bullish to begin year



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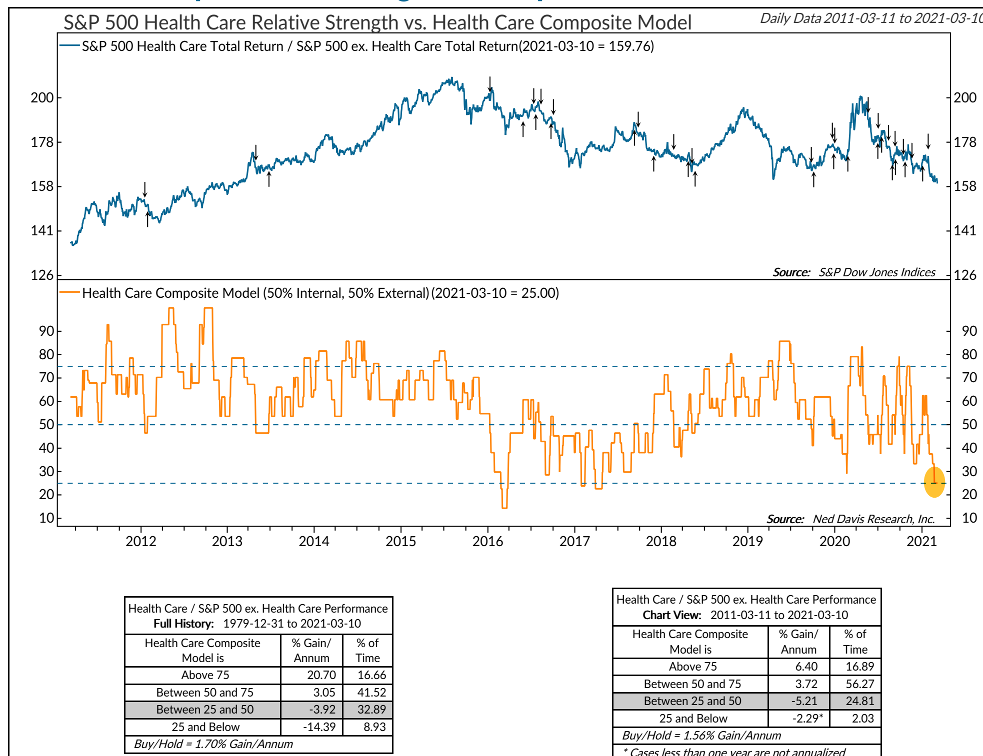
Lowest composite reading since April 2017



Health Care / S&P 500 ex. Health Care Performance
Full History: 1979-12-31 to 2021-03-10

Health Care Composite Model is	% Gain/ Annum	% of Time
Above 75	20.70	16.66
Between 50 and 75	3.05	41.52
Between 25 and 50	-3.92	32.89
25 and Below	-14.39	8.93

Buy/Hold = 1.70% Gain/Annum

Health Care / S&P 500 ex. Health Care Performance
Chart View: 2011-03-11 to 2021-03-10

Health Care Composite Model is	% Gain/ Annum	% of Time
Above 75	6.40	16.89
Between 50 and 75	3.72	56.27
Between 25 and 50	-5.21	24.81
25 and Below	-2.29*	2.03

Buy/Hold = 1.56% Gain/Annum
** Cases less than one year are not annualized*

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Sector model's message

Health Care's composite model score has been on the opposite trajectory of Energy and is now at its lowest level since April 2017 **(chart left)**. All six of Health Care's technical indicators in the sector model are bearish, and the sector has the lowest overall composite score among all sectors.

We viewed Health Care as a top upgrade candidate coming into 2021, with near-record low relative valuations and a Biden administration set on lowering the percentage of uninsured Americans. The sector model never got bullish enough for us to make the move. We still like the long-term prospects for the sector and will likely be quick to upgrade on model improvement.

Above excerpted from: "Shifted more toward Value" by Rob Anderson, March 11, 2021

Inflation and sector leadership

Whether or not the massive fiscal spending programs to aid in the economic recovery will lead to problematic levels of inflation for the stock market and the economy has been frequently debated. Our macro team has highlighted strong structural forces that are both inflationary and disinflationary and expects only a moderate pickup of 2.2% in CPI inflation in 2021.

The CPI Index reached a cycle low in May 2020 with a Y/Y growth rate of 0.1% and has since jumped to 1.4%. With inflation likely to continue higher, the **table at right** looks at sector performance during periods of rising CPI since 1972.

Energy has been the most consistent outperformer, beating the S&P 500 in seven of the prior nine cases by a median of 13.9%.

Energy consistently outperformed when inflation has been rising

Sector Performance During Periods of Rising CPI Inflation*

SORT

S&P 500 Sector	% Cases Outperforming**	Median Return**
Energy	77.8	13.9
Communication Services	66.7	9.5
Health Care	55.6	3.3
Consumer Staples	55.6	7.7
Information Technology	44.4	-4.4
Industrials	44.4	10.5
Materials	44.4	6.4
Consumer Discretionary	33.3	12.5
Utilities	33.3	5.7
Financials	22.2	-9.0
S&P 500 Index	na	9.8
CPI Rise***		

* CPI Y/Y change rises 200 basis points or more

** % cases outperforming and median return exclude recent case (case 10)

***CPI rise is the increase in the Y/Y growth rate, trough to peak, in basis points

Source: S&P Dow Jones Indices.

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Price recovery varies greatly among categories

Y/Y CPI for Select Categories (%)

SORT

Category	1/31/21	5/31/20	% Pt Change
Energy	-3.6	-18.9	15.3
Airline Fares	-21.3	-28.8	7.5
Apparel	-2.5	-7.9	5.4
Lodging Away from Home	-11.4	-15.2	3.8
Tobacco & Smoking Products	6.7	4.3	2.3
Gas & Electricity	2.1	-0.2	2.3
New Vehicles	1.4	-0.3	1.7
CPI Index	**1.4**	**0.1**	**1.3**
Household Furnishings	2.9	1.6	1.2
Food Away from Home	3.9	2.9	1.0
Nursing Homes	2.8	2.6	0.2
Alcoholic Beverages	2.4	2.2	0.2
Food at Home	3.7	4.8	-1.1
Prescription Drugs	-2.4	1.4	-3.8
Health Insurance	2.9	19.7	-16.8

Source: Bureau of Labor Statistics.

Ned Davis Research T_IF21_07.3

Many of our sector and industry indicators look at inflation on a more granular level, as the CPI Index can often mask individual inflationary or deflationary pressures that can be important for leadership trends.

The CPI categories hit hardest by COVID, like airline fares, lodging, energy, and apparel are still experiencing lower prices compared to a year ago **(table left)**. While most CPI categories are seeing higher growth compared to the May trough, health insurance, prescription drugs, and food at home categories are all lower. How prices respond to the reopening of the economy will help determine which sectors and industries lead, and which lag.

Above excerpted from: "Rising inflation and sector leadership" by Rob Anderson, February 18, 2021

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PAT TSCHOSIK, CFA, CMT, SENIOR PORTFOLIO STRATEGIST
MATT BAUER, CFA, SENIOR RESEARCH ANALYST

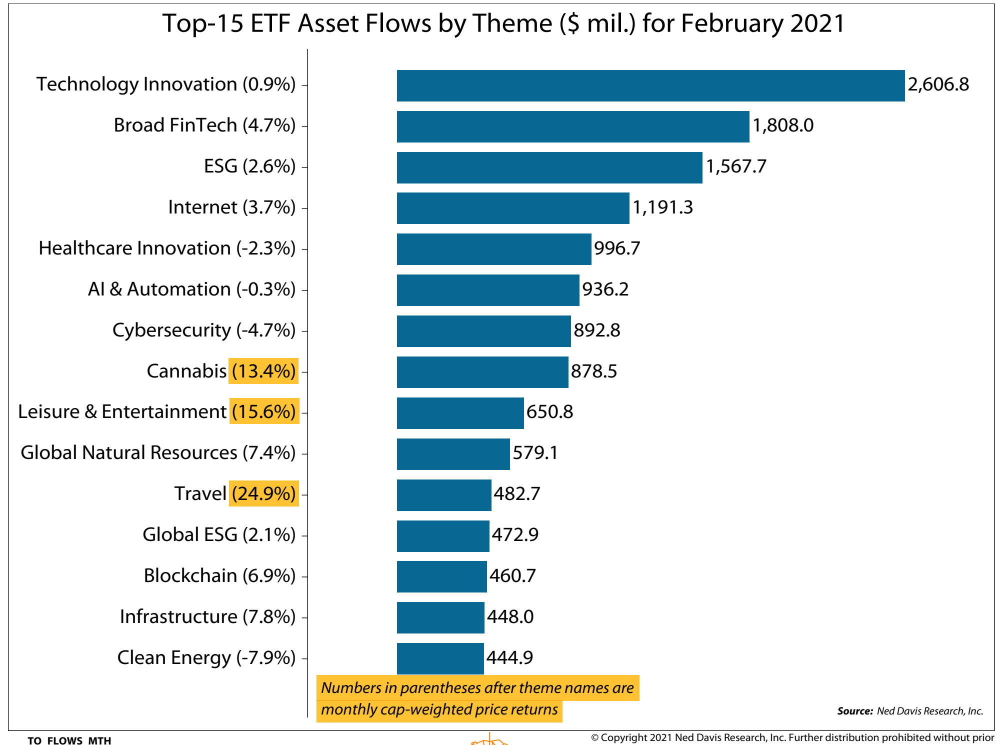
MARCH 15, 2021

Travel heats up while others cool off

Key Takeaways

- Plunging COVID cases helped make Travel-related the top performing theme.
- Themes with strong momentum including Clean Energy, EVs, and Cannabis cooled off in 2H February.
- Tech-driven themes could underperform as Value sectors outperform Growth.

Falling COVID cases lifted travel-related



The plunge in new COVID cases and rollout of the vaccine in February caused Travel ETFs to jump. The jumped helped make Travel-related the top performing theme **(chart above)**. Global Natural Resources and Natural Resources themes performed well, but this was oil in disguise.

Highflyers grounded

Cannabis ETFs — up over 60% in January — were the third-best performing theme in February. However, the Cannabis returns mask a strong reversal. Cannabis wasn't the only high-flying theme to experience a significant reversal after a recent peak. Our NDR EV stock index is down more than 19% since its January 26 peak. Global Clean Energy and Clean Energy were the worst- and second-worst performing themes in February.

At best, this is just profit taking after incredible runs in some of these high-flying ETFs. At worst, this is the beginning of thematic bubbles bursting. Our best guess is that several of the highflyers will continue to underperform while economic growth broadens out and cyclical value stocks lead.

Tech Titans lagging

Tech Titans have struggled relative to cyclical value sectors and the recent upgrade of Value over Growth has us thinking this could be a longer-term pullback that requires patience. This should present some great buying opportunities in technology-driven themes later this year.

Please contact your NDR-BCA sales representative for a complimentary trial to NDR Thematic Opportunities.

Above excerpted from: "Thematic update March 2021" by Pat Tschosik and Matt Bauer, March 3, 2021 (available through NDR's new Thematic Opportunities product offering)

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ALEJANDRA GRINDAL SENIOR INTERNATIONAL ECONOMIST
PATRICK AYERS INTERNATIONAL ECONOMIC ANALYST

MARCH 15, 2021

Global economic growth accelerates

Key Takeaways

- Global growth accelerated in February, according to the latest PMIs, accompanied by higher price pressures.
- Manufacturing continued to lead the recovery, but the services sector is showing signs of life.
- U.S. growth accelerated, Chinese growth softened, and Europe contracted at a slower pace.

Rebound ahead

The **table at right** summarizes our outlook by major country and region for this quarterly update. Since our last outlook in November, economic conditions have been mixed as several countries deal with rising COVID cases and restrictions. Industrial activity has rebounded markedly, a clear sign of adaptability to the pandemic, but the consumer has generally lagged. Inflation pressures are rising globally, but likely won't become a long-term issue in the developed world.

Above excerpted from: "G7 and BRIC outlook: Rebound ahead, but inflation on the horizon" by Alejandra Grindal, March 1, 2021

G7 and BRIC economic summary

Country/ Region	Outlook for Economic Growth	Summary
U.S.		• We reaffirm our projection of 4.6% real GDP growth in 2021, bolstered by Biden stimulus. • Expect weaker growth in the first half of the year, but stronger growth later on. • Price pressures in the U.S. will firm in 2021, but longer-term pressures contained.
Eurozone		• Double dip recession inevitable, exacerbated by slow vaccine deployment. • But strong 2H rebound likely due to pent-up demand and room for upside in beaten-down industries. • Short-term inflation to rise, but strong disinflationary trends persist, enabling an accommodative ECB.
U.K.		• Despite being clobbered by Brexit and COVID, fast vaccine deployment sets the stage for a sharp rebound. • But high unemployment and Brexit pose risks to the outlook. • CPI is likely to surpass the BoE's target this year, but the bank will likely remain accommodative due to excess capacity.
Japan		• The Japanese economy declined less in 2020 than most of the G7, but 2021 is off to a slow start amid a spike in COVID. • Weak consumption is offsetting a strong industrial rebound. • Inflation may rise in the short-term, but the BoJ struggles with strong disinflationary forces.
China		• Some recent data has brought up concerns of a soft patch in the economic powerhouse. • On balance, we expect trends to remain robust through at least the first part of the year. But data will be difficult to navigate in the coming months due to the LNY and COVID distortions. • Inflation, debt, and resumption of trade war remain risks for the year.
India		• India's economy has roared back after being one of the most negatively impacted by COVID. • Industrial activity is surging, while the consumer is slowly recovering. • Inflation risks are to the upside.
Brazil		• Brazil's economy fared relatively better than other Latin American economies in 2020. • But a fading of 2020's massive fiscal support has weighed on the economy. • High government debt and rising inflation also present risks to the outlook.
Russia		• After a brief lull in Q4 2020, Russia's economy has resumed upside momentum. • Following the poisoning of opposition leader Alexey Navalny, the country is at risk for additional sanctions. • Higher inflation may prompt the central bank to hike rates later this year.

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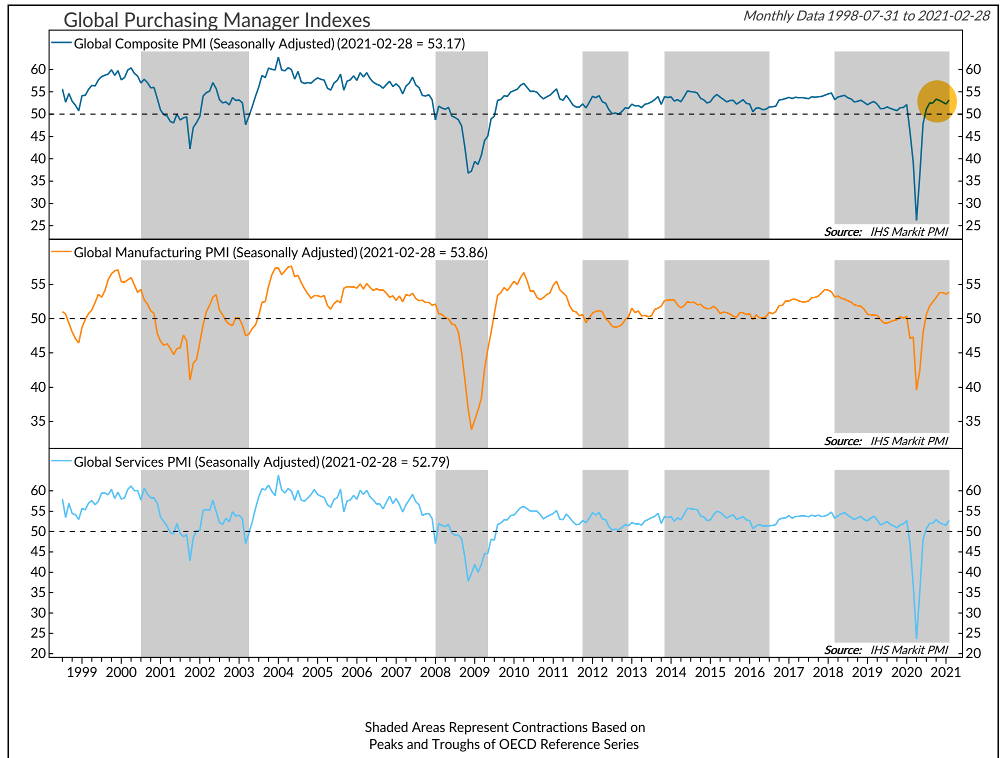
Growth accelerates

Global economic growth grew at a robust pace in February, according to the latest PMIs. The global composite PMI, which includes both the services and manufacturing sectors, rose 0.9 points to 53.2 in February. It was the first gain in four months and to its second-highest level since August 2018 **(chart right)**. Despite many economies still implementing COVID-related restrictions and the vast majority still in the early stages of vaccinations, the resiliency of the global economy speaks to the adaptability and ingenuity of humans during such unusual times.

Manufacturing leads again

Global manufacturing continued with its upside momentum, leading overall gains in the global economy. The global manufacturing PMI climbed to its highest level in two years and continued to broaden, indicating that the recovery remains firmly on track. The share of countries with expanding manufacturing industries rose to 80% in February — the largest share since October 2018 **(chart left)**. This supports our long-held view of a V-shaped recovery in the sector, which is more conducive to social distancing than the larger services sector.

The global economy remains resilient



IE250E

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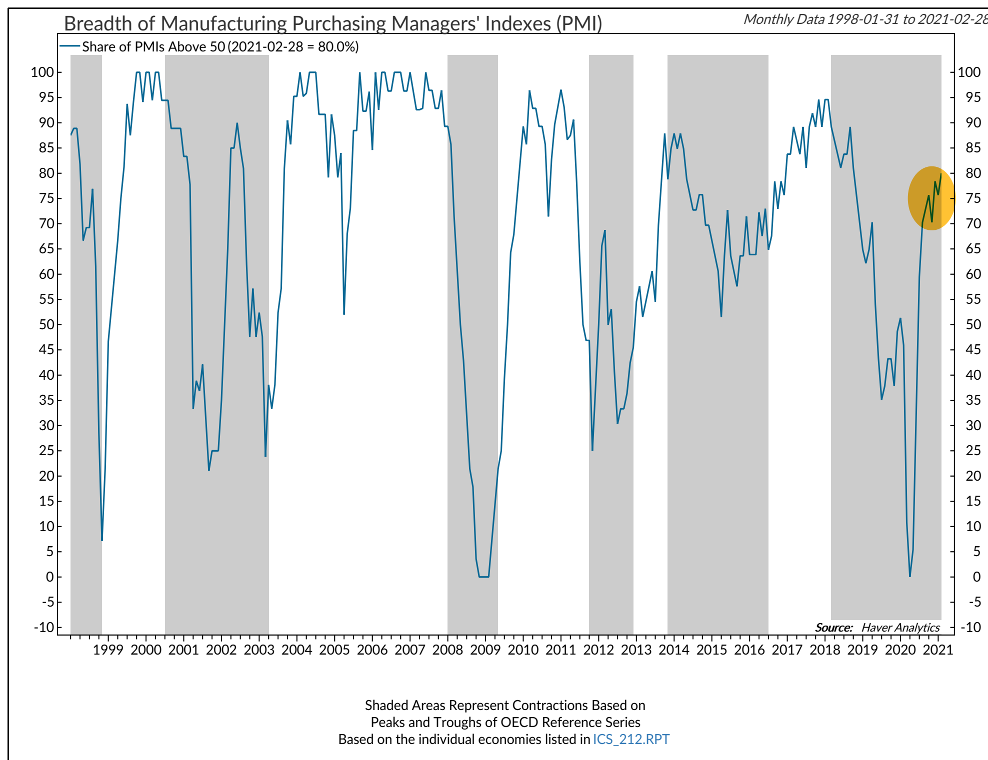
Manufacturing breadth at highest level since October 2018



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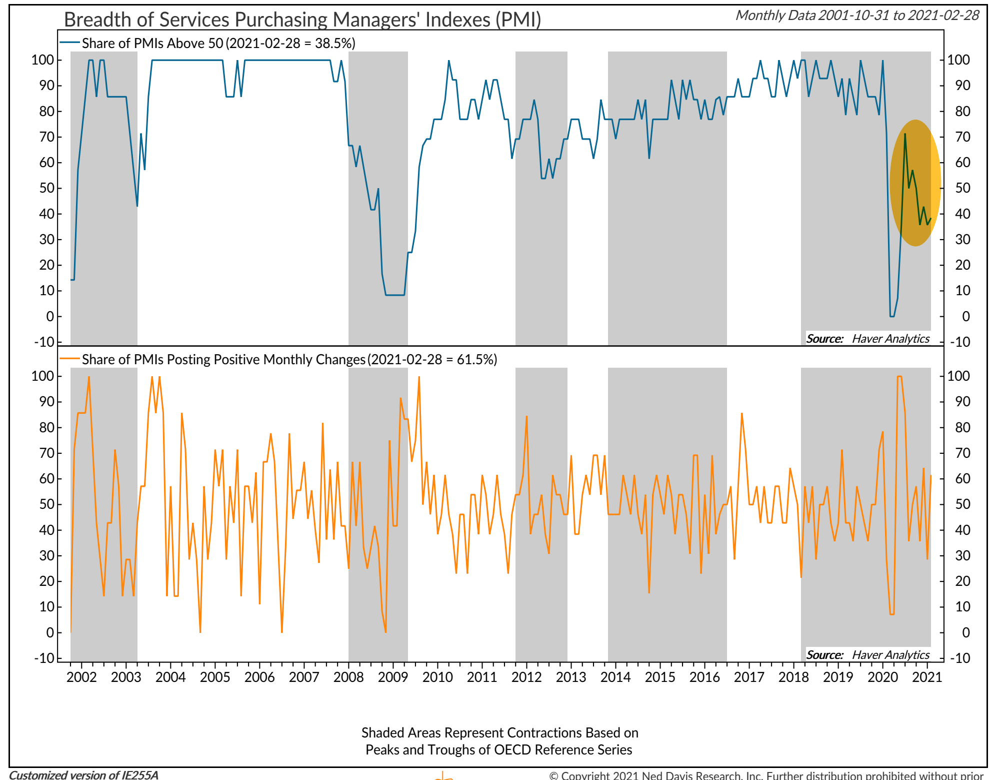
Services picking up

Although the services sector has consistently lagged manufacturing during the age of COVID, the sector showed some positive signs in February. The global services PMI jumped 1.2 points to 52.8, a four-month high. Not surprisingly, the key culprit dragging down the services sector is consumer services — which fell at a faster pace in February and for the 13th straight month.

Services breadth, however, remained in the

doldrums. The share of economies with expanding services industries edged up to 39%, a far cry from the 90%-plus readings observed during most expansions **(chart right)**. But the share of countries that reported month-to-month gains in their PMIs rose to over 60%, a sign that downside momentum is moderating.

Services breadth remains weak



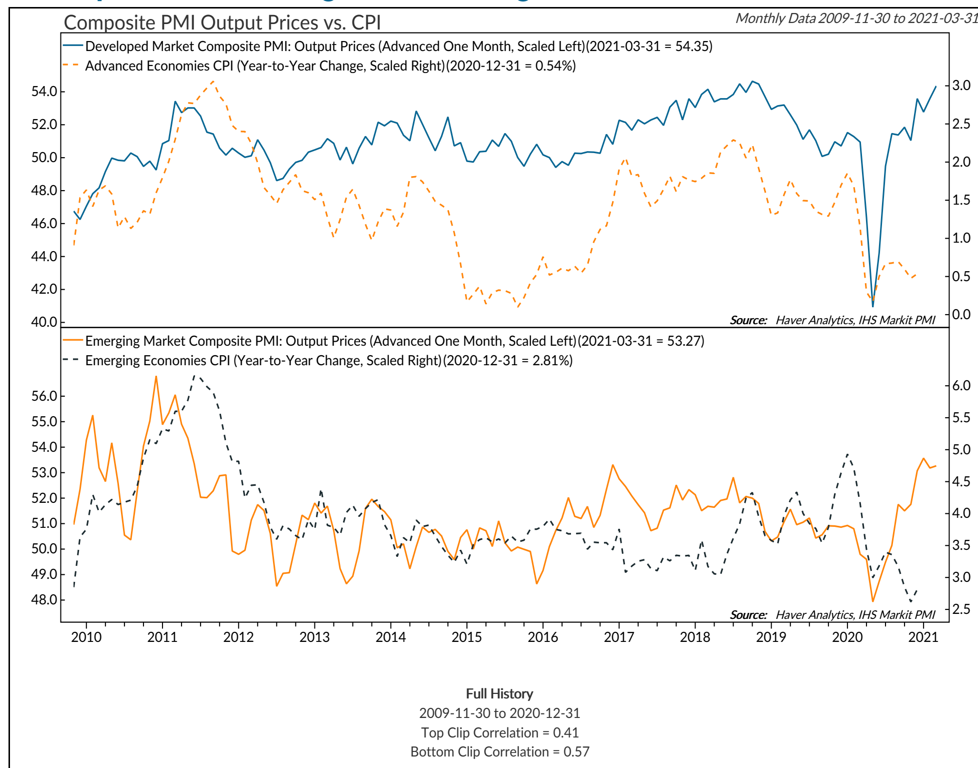
Global inflation rising

The global composite input price index surged to its highest level since September 2008, while the output price index jumped to the highest since records began in 2009. As shown in the **chart below**, the rising output price indexes will likely feed into consumer prices in the coming months, in line with our view of a pick-up in inflation this year.

China's growth eases again

The Markit composite PMI for China edged down to a 10-month low, as output slowed in both the manufacturing and services sectors — held down by some localized COVID outbreaks and distortions caused the Lunar New Year holiday. We expect these factors to be short lived, but if this weakness is sustained, it could pose trouble to the rest of the world — in particular manufacturing. China tends to lead global trends by a couple of months.

Price pressures rising across the globe



Europe recovering

Amid ongoing lockdowns, the eurozone economy continued to contract, albeit at a slower pace. Services continued to shrink — led by Ireland, France, and Spain. Manufacturing growth accelerated to a three-year high, as all countries, but Greece, reported growth.

Above excerpted from: "Global growth accelerates" by Alejandra Grindal, March 4, 2021

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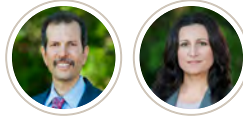


JOSEPH F. KALISH CHIEF GLOBAL MACRO STRATEGIST
VENETA DIMITROVA SENIOR U.S. ECONOMIST

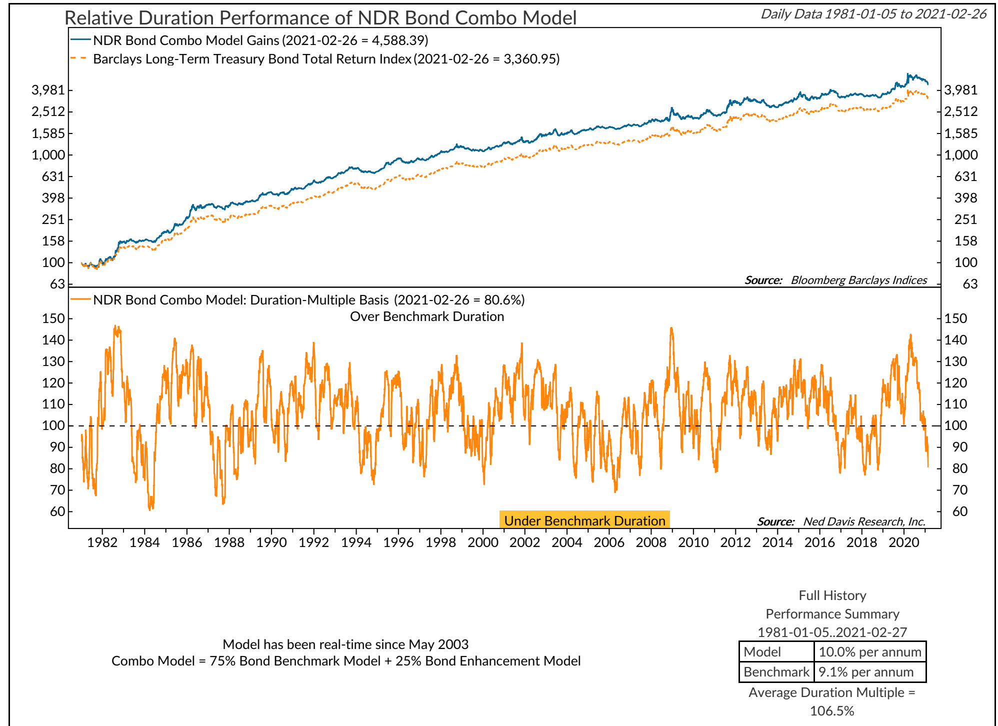
MARCH 15, 2021

Reduced duration, again

Key Takeaways

- We cut bond duration to 85% of benchmark, downgraded investment grade credit to marketweight, and upgraded MBS and ABS to overweight.
- The rise in yields has primarily been driven by rising inflation expectations.
- With the Fed and ECB unconcerned about higher bond yields, we made some adjustments to our global bond allocation and closed our European peripheral debt trade.

Lowest bond duration since October 2018



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As long as yields are rising for the right reasons such as increased confidence in the outlook, progress on vaccine deployment, and additional fiscal support, FOMC participants sounded unperturbed. At the latest FOMC meeting, Fed Chair Powell called the rise in bond yields a "statement of confidence," a message that has been confirmed by several other FOMC participants. The Fed doesn't want disorderly markets.

7-year auction disaster

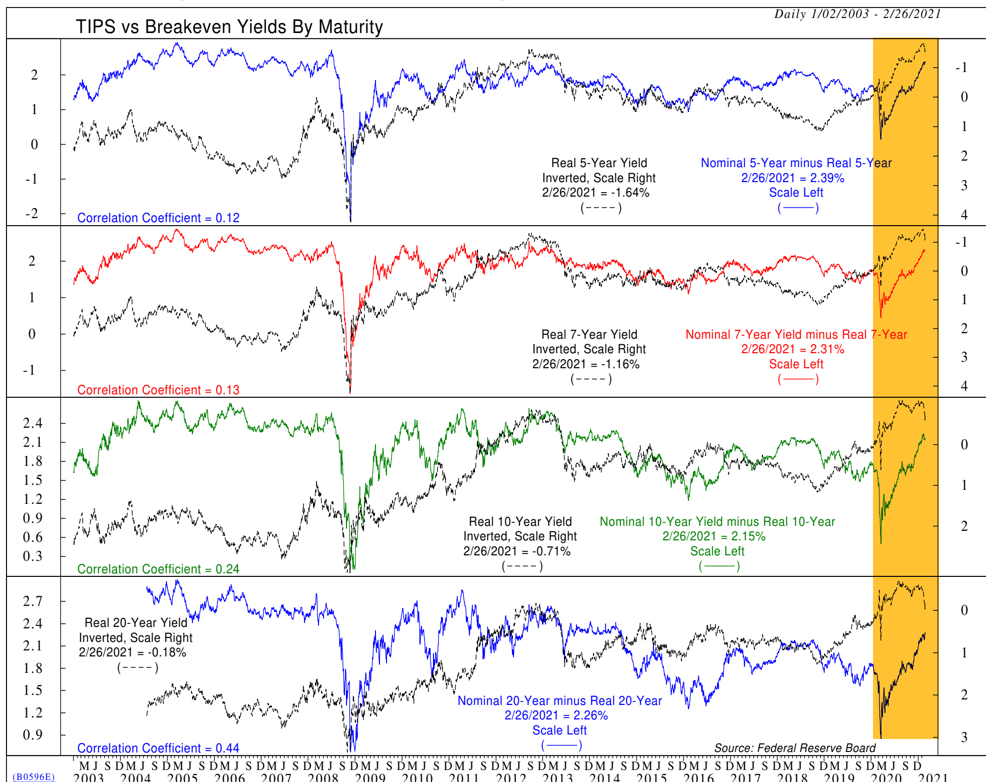
But, that message was crafted before the most recent disastrous 7-year Treasury note auction, which saw the worst bid/cover ratio on record. That led to forced technical selling and mortgage/convexity hedging. The Treasury market had a dysfunctional feel to it with the 10-year Treasury yield blowing through our 1.50% support and soaring to as much as 1.60%. Ten-year TIPS yields rose 40 basis points (0.40%) in eight trading days. And the so-called "belly" of the curve moved even more than bonds on Thursday, causing the market to price in two rate hikes over the next two years (late 2022/early 2023).

The Fed can't be happy with that kind of movement. The Fed is very interested in the smooth functioning of the Treasury market. Remember, the Fed will purchase at least $80 billion of Treasurys and $40 billion of agency MBS every month. They could purchase more if markets are illiquid.

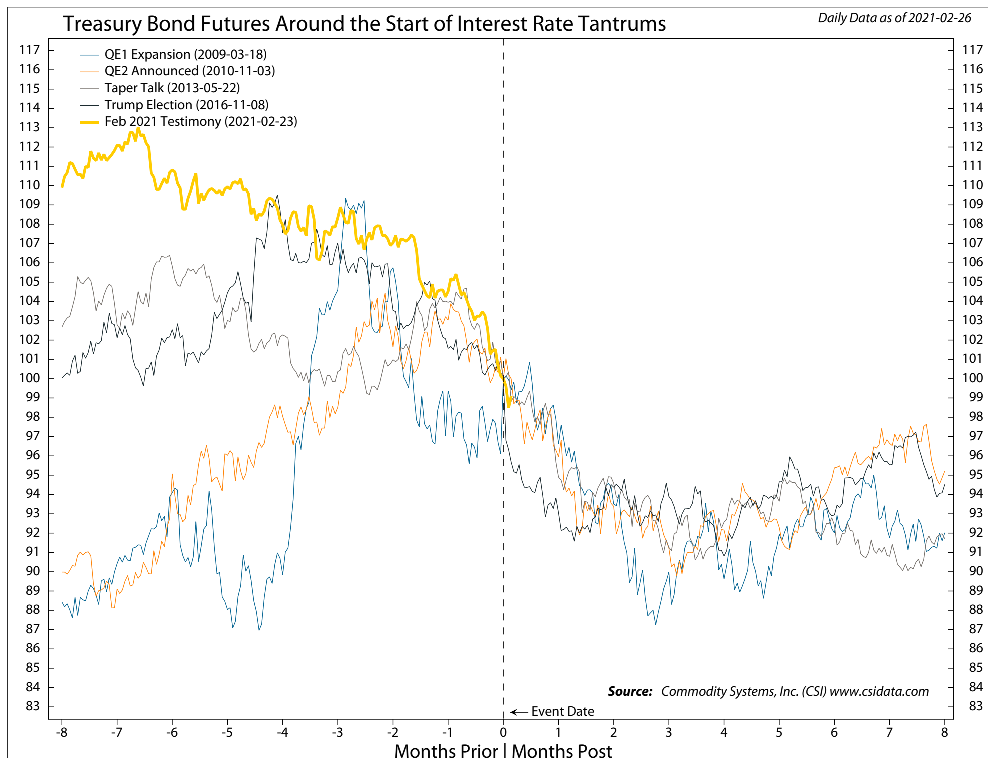
With a more gradual move to higher yields, **we further reduced our bond exposure by 5% to 85% of benchmark duration**, our lowest exposure since November 2018. It will also bring us closer to our Bond Combo Model, which has slipped to 81% of benchmark duration, its lowest reading since October 2018 **(chart above)**.

Inflation expectations stall, real yields rise

As we have noted recently, except for the past two weeks, most of the yield rise has been due to increasing inflation expectations **(chart right)**. The move in real yields reflects a better economic outlook.

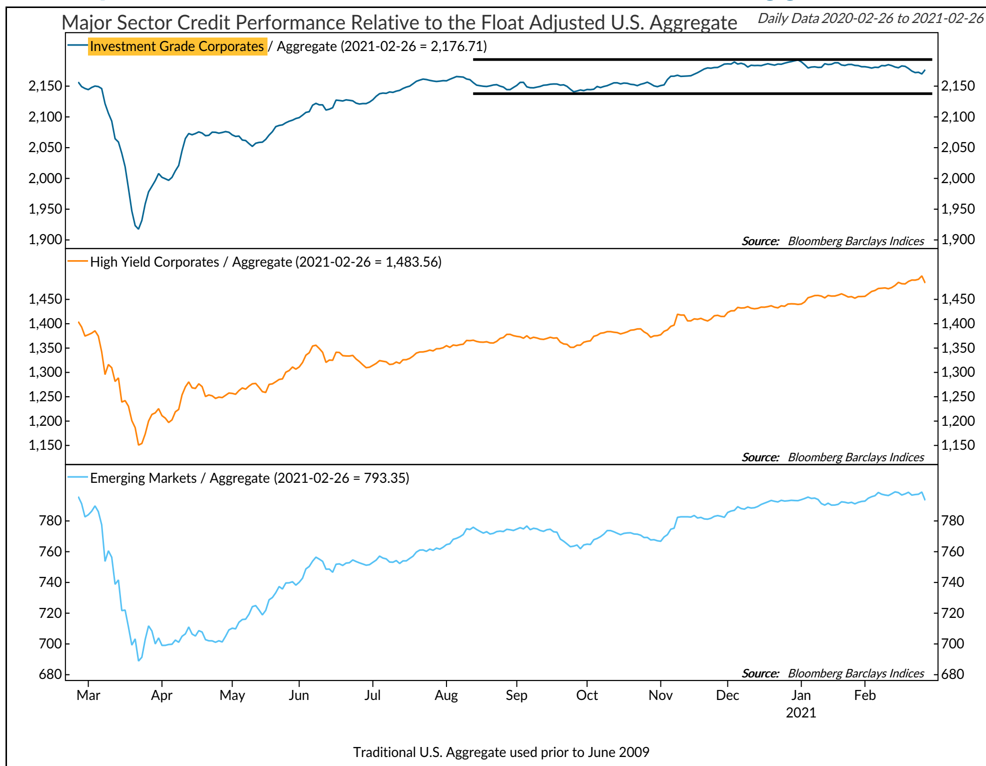


Downside risk to bond prices



We're also concerned that the history of recent policy-related bond routs is not encouraging for the next 3-4 months. The expansion of QE1 and QE2 ended as it began, with specific date-based guidance and specific purchase amounts. The "taper talk" was the effective end of QE3. Finally, Trump's surprising victory in 2016 caused a massive shift in policy expectations. All four cases ended in tears for bond investors **(chart left)**.

IG corporates have flattened out relative to the Agg



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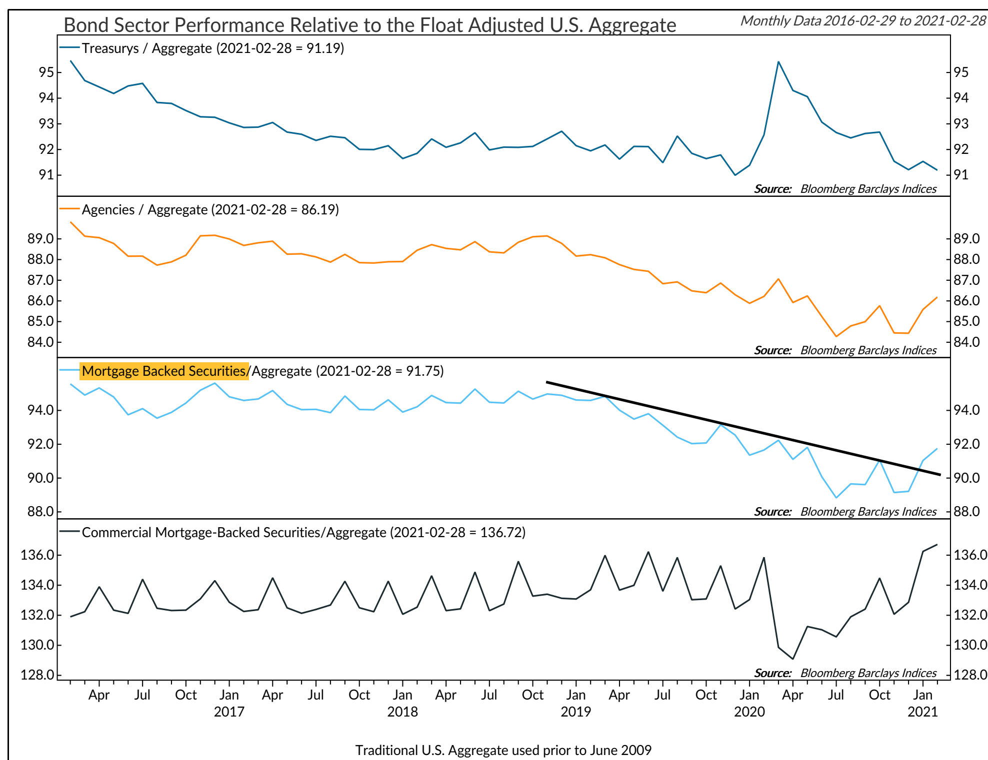
Sector changes

We also downgraded investment grade corporates to neutral from overweight, due to their higher duration. We remain overweight high yield and underweight Treasurys.

MBS outperforming as yields rise



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Additionally, we upgraded mortgage-backed securities (MBS) and asset-backed securities (ABS) to overweight for its shorter duration and a brighter consumer outlook.

Above excerpted from: "Fed officials give green light to higher yields" by Joe Kalish, March 2, 2021

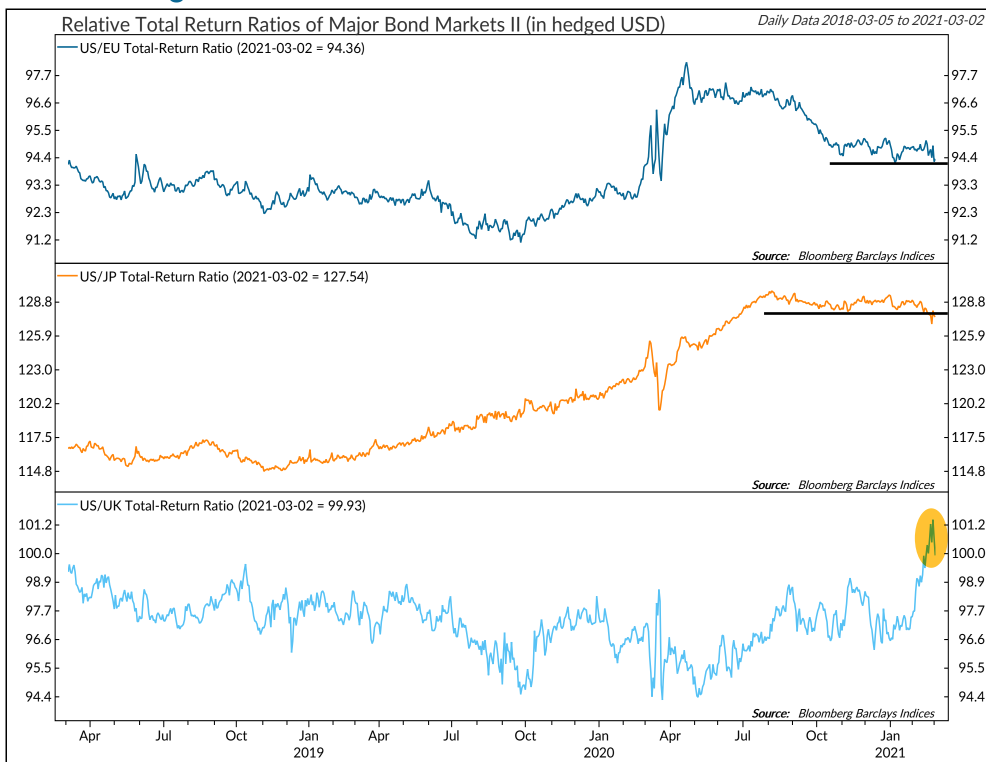
Reduced global bond risks

With the Fed and now the ECB seemingly unconcerned by rising bond yields, on March 4, we made a modest adjustment to our global bond allocation. We reduced our U.S. weighting by 2% to a marketweight 48% and increased our Japanese weighting by the same amount to a marketweight 17%.

We are way out ahead of the model, having moved to a more neutral allocation two months ago. The model tries to lock onto longer-term trends, but we are concerned about several ratios breaking down.

The U.S. is close to breaking down against Europe, has broken support versus Japan, and appears to be reversing its gains against the U.K. **(chart right)**.

U.S. looking vulnerable



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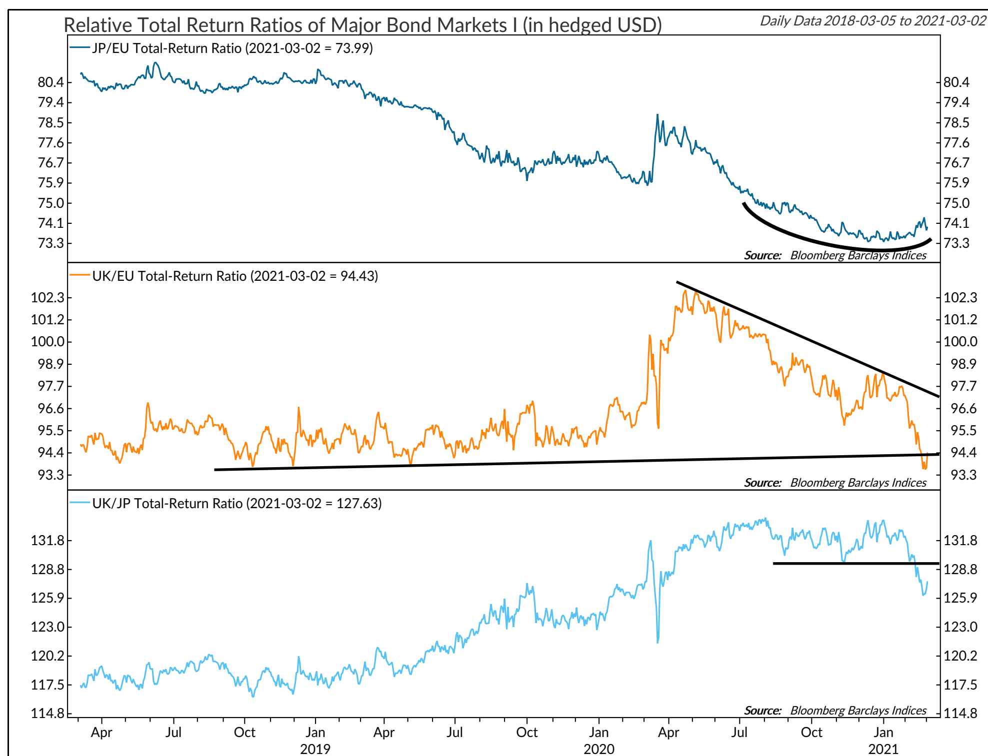
Japan looking better, U.K. worse



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Japan, where yield curve control remains in effect, looks like it is slowly turning up relative to Europe. Although the U.K. has bounced in recent days, it looks badly broken **(chart left)**.

Finally, with Mario Draghi now at the helm in Italy and yields starting to rise in Europe, we don't see any catalyst to hold onto the European peripheral debt trade we implemented on August 6, so we closed out that trade.

Above excerpted from: "Reducing global bond risks" by Joe Kalish, March 4, 2021

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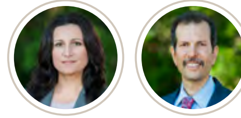


VENETA DIMITROVA SENIOR U.S. ECONOMIST
JOSEPH F. KALISH CHIEF GLOBAL MACRO STRATEGIST

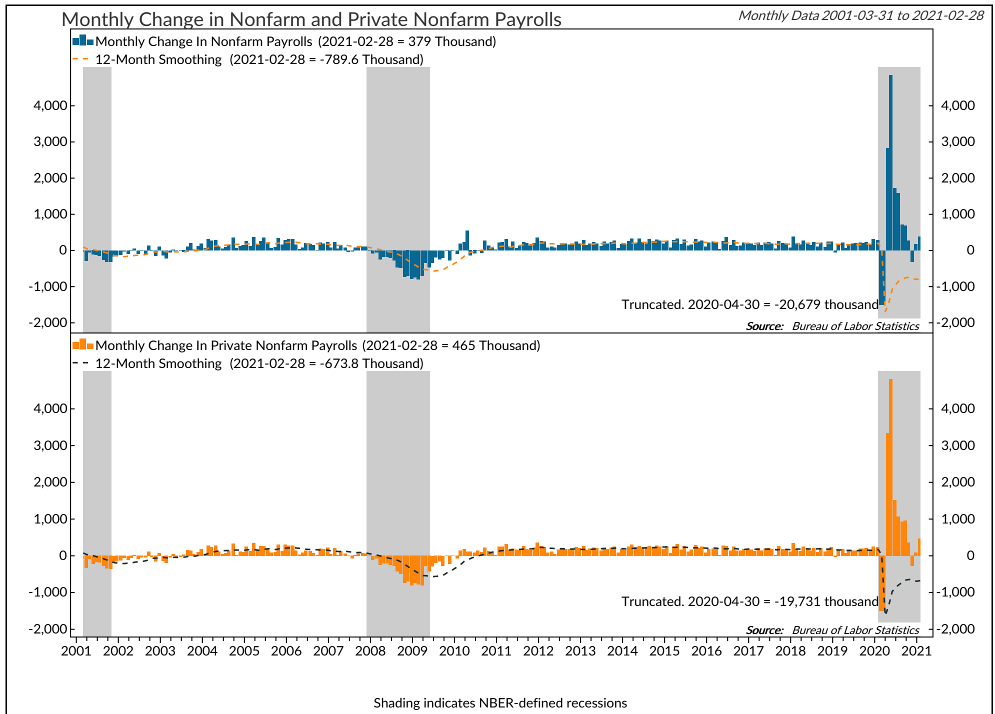
MARCH 15, 2021

Strength in jobs and housing

Key Takeaways

- Big recall of leisure and hospitality workers on temporary layoff drove the February gain in jobs.
- Jobs report won't change monetary or fiscal support near-term, but we expect tapering of asset purchases later in the year.
- Strong housing demand and a persistent housing shortage are driving up housing and commodity prices. Watch for a spike in mortgage rates.

Solid rebound, but still well below pre-pandemic level



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Strong jobs recovery

Led by a strong rebound in the leisure and hospitality industry, nonfarm payrolls expanded by 379,000 in February **(chart above)**, above the consensus of 210,000 and our forecast of 250,000. Additionally, the prior two months were revised up by 38,000. The unemployment rate ticked down to 6.2%, below the consensus of 6.3% and our estimate of 6.4%. One black mark was the reversal in the average workweek, which shortened to 34.6 hours from a downwardly revised 34.9 hours. There are two reasons for that. One, companies brought back staff rather than working their existing employees harder. Two, the severe winter storm hit late in the survey week.

Overall, this report is good news for the Fed, which won't stand in the way of rising bond yields, as long as the rise is orderly and for the right reasons. Nevertheless, the Fed remains far from its goals of maximum employment and price stability. If these trends continue, we expect the Fed to announce it will taper its asset purchases later in the year.

Private nonfarm payrolls increased 465,000, the most in four months, and a positive sign that the labor market recovery is regaining its footing, on the back of slower COVID case spread and a ramp-up in the vaccination rate. Even so, the private sector is still 8.1 million jobs, or 6.2%, below its pre-pandemic level, as the recovery has a long way to go to full employment.

The increase in February was led by leisure and hospitality (+355K), mostly at restaurants and bars, as COVID restrictions eased across more states. There were also notable gains in temporary help (+53K), health care and social assistance (+46K), retail trade (+41K), and manufacturing (+21K).

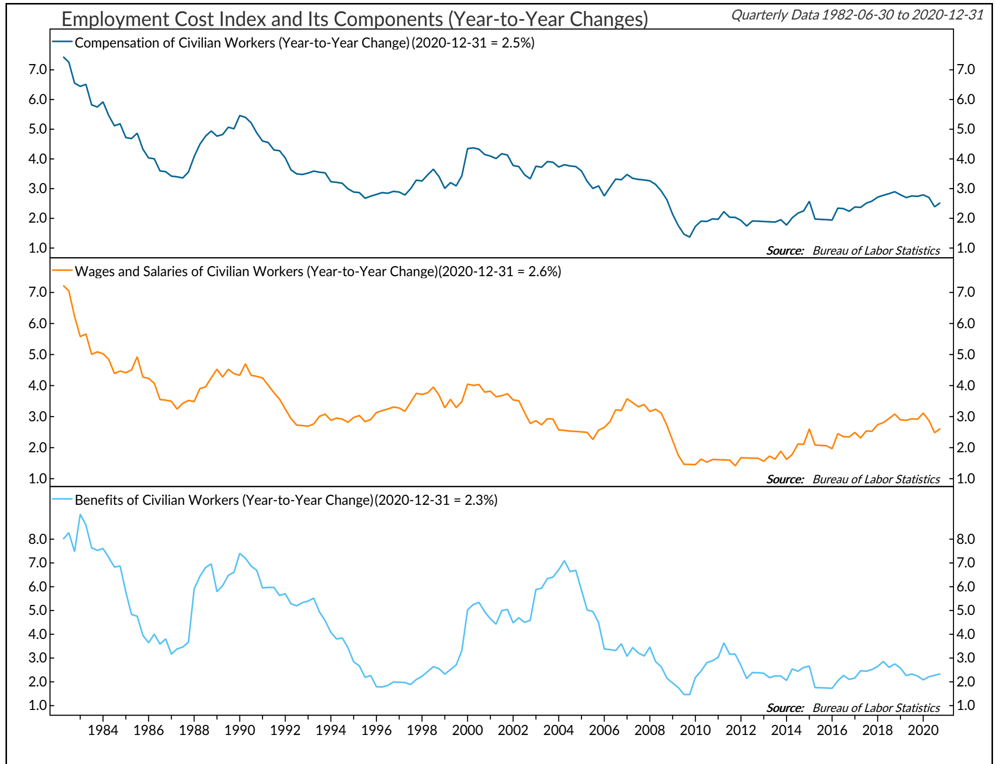
Average hourly earnings picked up 0.2% from the previous month and 5.3% from a

year ago, more than double the average pace of wage growth during the previous expansion. But this statistic remains distorted by the disproportionate loss of lower-paying jobs during the pandemic and does not adequately reflect the state of the labor market.

The Fed has focused on other compensation measures, such as the Employment Cost Index, which was up 2.5% y/y at the end of 2020 and below its pre-pandemic pace **(chart right)**.

Above excerpted from: "Strong jobs recovery" by Veneta Dimitrova, March 5, 2021

ECI better reflects wage growth



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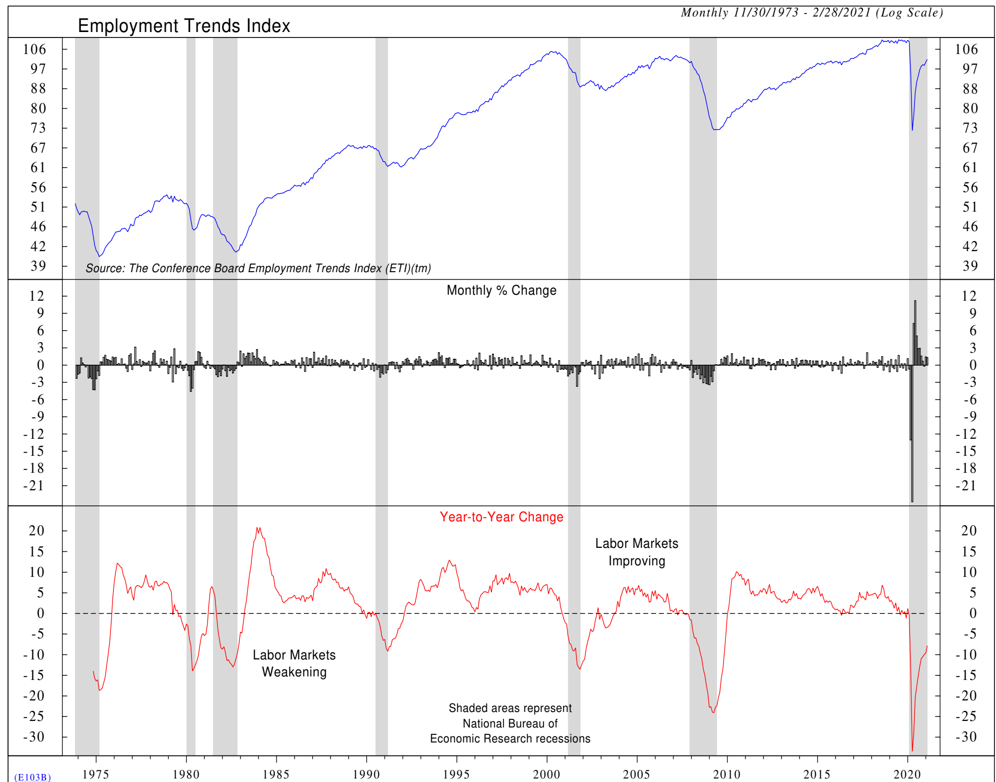
Employment trends improve

The Employment Trends Index (ETI) increased 1.3% in February, up in nine of the past 10 months **(chart below)**, as labor market conditions continued to improve from the pandemic slump. On a y/y basis, the ETI was still down 7.8%, but the negative momentum has eased substantially since the depth of the pandemic and corresponds to continued real GDP recovery.

Five of the eight ETI components made positive contributions last month, led by temporary help hires. The Conference Board expects the vaccine rollout to lead to more hiring in in-person services by late spring, particularly in leisure and hospitality, transportation, and childcare services, which could bring down the unemployment rate to about 5.0% by the end of this year.

Above excerpted from: "Employment trends improve" by Veneta Dimitrova, March 8, 2021

Trends up in nine of the past 10 months



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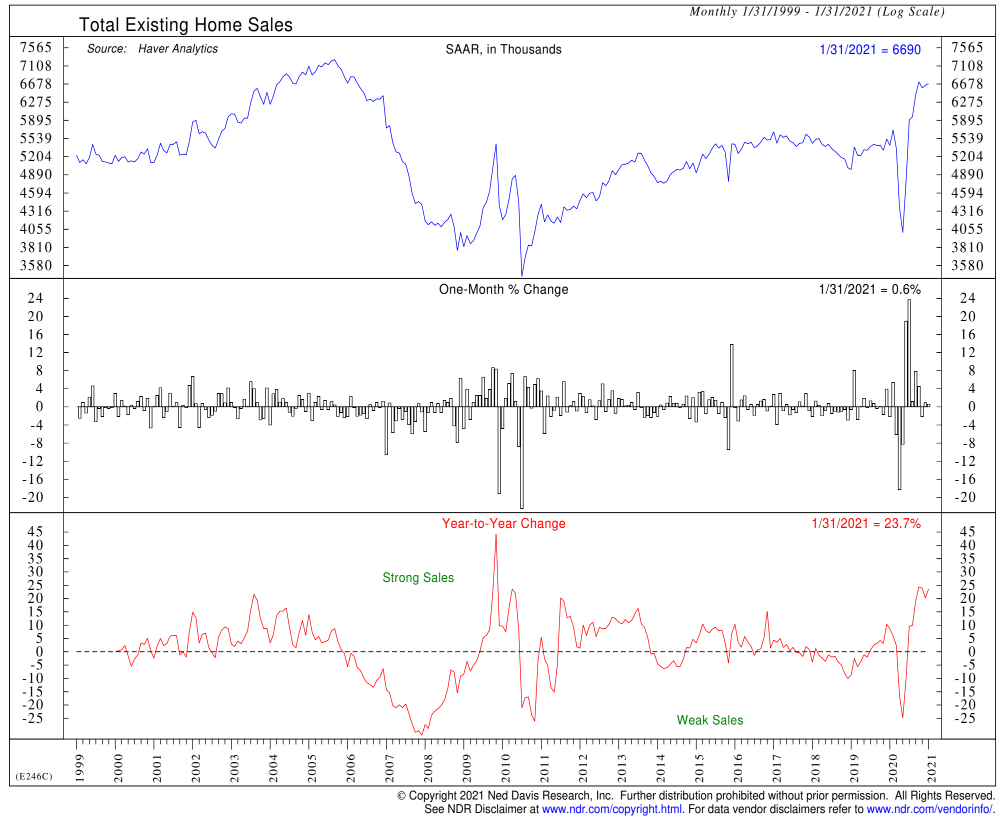
Strong housing demand

Even though the pandemic shut down most of the country in March and April of last year, the housing market perked up after reopening and activity has accelerated ever since. Housing demand has rebounded strongly, with existing home sales hitting a 6.69-million-unit annual rate in January, close to the highest level since April 2006, and up 23.7% from a year ago **(chart right)**. Similarly, new home sales at the start of this year were close to their highest level since late 2006 and were up 19.3% year/year.

Survey after survey of housing market activity have pointed to life during and after COVID as a key driver of housing demand. Fiscal stimulus and record low mortgage rates have padded household budgets, particularly for those who kept their jobs, and raised affordability.

Sales at the highest annual rate since April 2006



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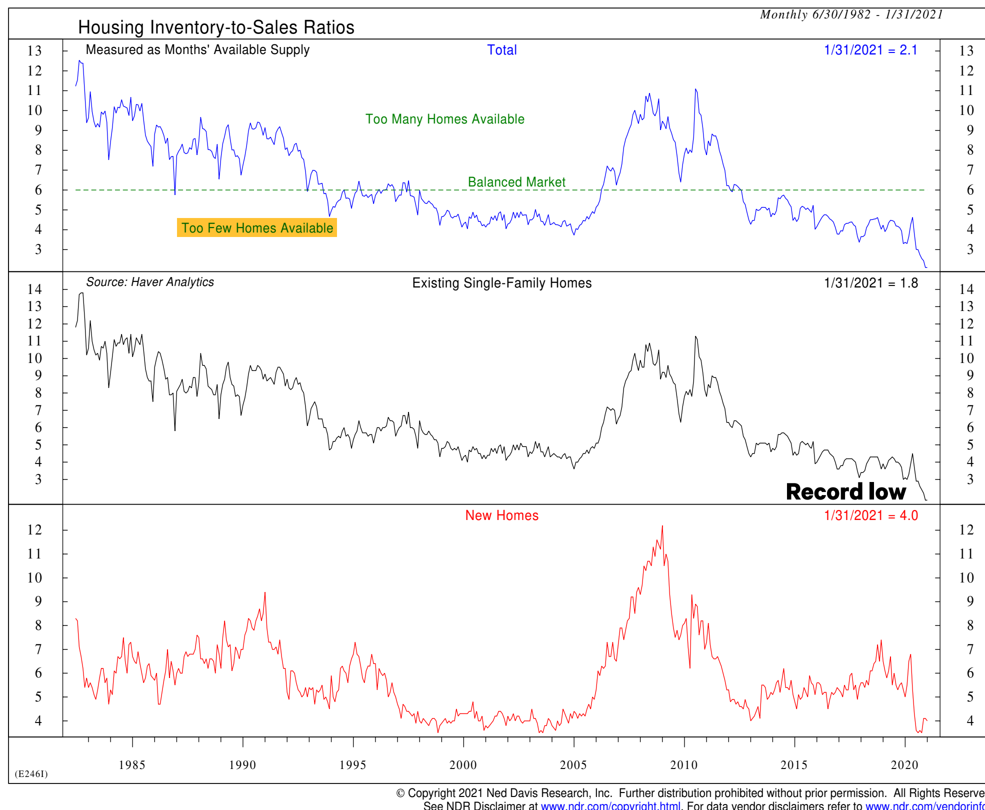
Record tight housing inventory



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Extreme housing shortage

Months' available supply for single-family homes was at 2.1 in January, a record low **(chart left)**. The shortage is putting upward pressure on prices, which are growing by double digits year/year. This is creating housing wealth for existing homeowners and is making it profitable for homebuilders to bring new construction to the market. But, with the backup in yields, we'll need to watch mortgage rates. Our analysis shows a backup of 75 basis points (0.75%) in mortgage rates from a local trough could be meaningful. But we're not there yet. The conventional mortgage rate needs to increase to about 3.5% before it negatively impacts home sales and starts.

Above excerpted from: "Why are lumber prices hitting record highs?" by Veneta Dimitrova, March 1, 2021

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MARCH 15, 2021

Rising rates and stock performance

Key Takeaways

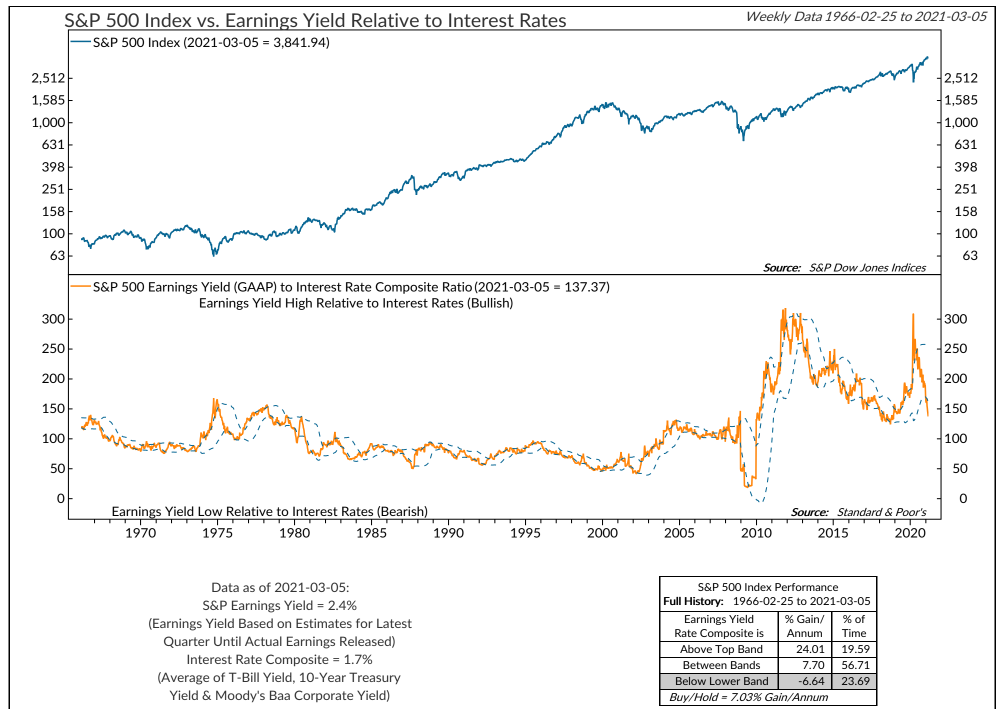
- With this much debt in the economy, rising rates can be a problem.
- I am particularly watching corporate bond yields and mortgage rates.
- NDR Monetary Composite has gone from bullish to neutral, but is not a problem yet.

In a debt-heavy economy, it does not take much of a rise in interest rates to hurt stocks or housing, and later put pressure on borrowers and the economy. But we want to watch some objective indicators to tell us if the rise is just noise or something significant.

Interest rates rising

The **chart above** suggests that stocks have risen enough or interest rates have risen already to begin to pressure stocks. However, because the ratio itself is still above average, I would like to see more to get seriously worried. I am watching is the six-month change in corporate bond yields which has moved from bullish to neutral, but it is not yet negative.

Earnings yields relative to rates still high, but falling



S&P 500 Index Performance
Full History: 1966-02-25 to 2021-03-05

Earnings Yield Rate Composite is	% Gain/ Annum	% of Time
Above Top Band	24.01	19.59
Between Bands	7.70	56.71
Below Lower Band	-6.64	23.69

Buy/Hold = 7.03% Gain/Annum

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Mortgage rates still low

For housing, I watch the relationship between mortgage rates and home sales. A 75 basis point (0.75%) rise in mortgage rates has historically been a problem for total single family home sales. This may be particularly true this cycle, as home prices have risen well above income, so a sell signal on this chart would suggest real affordability problems. Thus far, mortgage rates have only risen slightly.

Watching T-notes

Three-year Treasury yields may also be important, because these rates are more controlled by the Fed. A rise in T-note yields may be a way to tell if the Fed is beginning to remove its "emergency" ultra-easy policies.

Finally, I am watching our Fab Five Monetary Composite. It uses more than just interest rates. It is now neutral, but a negative reading could signal trouble for stocks.

Above excerpted from: "How will we know if interest rate rise might start to hurt stocks?" by Ned Davis, February 26, 2021 (available through the NDR Hotline product offering)

Glossary of terms

Asset Allocation: Ned Davis Research, Inc. constrains the recommended equity weighting (which can theoretically range from zero to 100%) to be limited to a minimum of 40% stocks and a maximum of 70% stocks. Due to the constraint on equity weighting, the combination of bonds and cash can be weighted no greater than 60% and no less than 30% in NDR's recommendations. The benchmark for bond allocation is 35% and for cash is 10%.

Benchmark Duration: The most commonly used measure of bond risk, quantifies the effect of changes in interest rates on the price of a bond or bond portfolio. The longer the duration, the more sensitive the bond or portfolio should be to changes in interest rates. Point of reference for a measurement.

Beta: A number describing the relation of an investment return with that of the financial market as a whole. Numbers greater than one suggest an investment will increase more than the broad market when it is rising, and have greater declines when the market is falling.

Breadth: A technical term used to demonstrate how broadly a market is moving.

Capital Market: Is a market for securities (debt or equity), where business enterprises (companies) and governments can raise long-term funds.

Commercial Mortgage-Backed Securities (CMBS): A type of mortgage-backed security backed by commercial mortgages rather than residential mortgages. When compared to a residential mortgage-backed security, a CMBS provides a lower degree of prepayment risk because commercial mortgages are most often set for a fixed term.

Core Inflation: Is a measure of inflation which excludes certain items that face volatile price movements, notably: food and energy.

Cyclical Bear: Cyclical swings in the market can last from several months to a few years, and are designed to be in line with the primary trend. A cyclical bear market is a cyclical swing when the market is in a downtrend.

Cyclical Bull: Cyclical swings in the market can last from several months to a few years, and are designed to be in line with the primary trend. A cyclical bull market is a cyclical swing when the market is in an uptrend.

Deflation: Is a slight decrease in the general price level of goods and services. Deflation occurs when the annual inflation rate falls but stays above 0%.

Demographics: Studies of population based on factors such as age, race, sex, economic status, level of education, income level, and employment.

Echo Bull/Bear: An echo bear market is a shallower correction which occurs in the equity market that does not coincide with an economic recession. An echo bull market is one that follows and echo bear market.

European Central Bank (ECB): Is the institution of the European Union (EU) which administers the monetary policy of the EU Eurozone member states. It is thus one of the world's most important central banks. The bank was established by the Treaty of Amsterdam in 1998, and is headquartered in Frankfurt, Germany.

Eurozone/European Union: Is an economic and monetary union (EMU) of the European Union (EU) member states which have adopted the euro currency as their sole legal tender. It currently consists of Austria, Belgium, Cyprus, Finland, France, Germany, Greece, Ireland, Italy, Luxembourg, Malta, the Netherlands, Portugal, Slovakia, Slovenia, and Spain.

Glossary of terms

Federal Open Market Committee (FOMC): A component of the Federal Reserve System, is charged under United States law with overseeing the nation's open market operations. It is the Federal Reserve committee that makes key decisions about interest rates and the growth of the United States money supply.

Gross Domestic Product (GDP): The total output of goods and services produced in a given country during a given period.

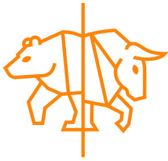
Lagging Indicator: An economic factor that changes after the economy has already begun to follow a particular pattern or trend; used to confirm long-term trends.

Leading Indicator: An economic factor that changes before the economy starts to follow a particular pattern or trend; used to predict changes in the economy.

Median P/E: Numeric value separating the higher half of a sample, a population, or a probability distribution, from the lower half. This is the middle price-to-earnings ratio of a series.

Mortgage-Backed Securities (MBS): A type of asset-backed security that is secured by a mortgage or collection of mortgages. These securities must also be grouped in one of the top two ratings as determined by an accredited credit rating agency.

MSCI Emerging Market Index: An index developed by Morgan Stanley Capital International, Inc. (MSCI) as an equity benchmark for emerging market stock performance. It is a capitalization-weighted index that aims to capture 85% of publicly available total market capitalization. Component companies are adjusted for available float.



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NDR HOUSE VIEWS (Updated March 11, 2021)

NDR recommends maximum overweight allocation to equities, underweight allocation to bonds and marketweight allocation to cash. It is likely that we have seen a reset of the secular bull market that started in 2009.

Equity Allocation

U.S. | We are marketweight the U.S. relative to other regions but are bullish on an absolute basis. The rally from the March 23 low has met the NDR criteria for a cyclical bull market, and we are shifting to risk-on assets as models confirm. We favor small-caps over large-caps and Value over Growth.

INTERNATIONAL | We are overweight Emerging Markets, underweight Japan, U.K. and Pacific ex. Japan, and neutral on all other regions within our seven-way regional allocation framework.

Macro

ECONOMY | The global economy fell into its deepest recession in the postwar era due to COVID-19, but as of Q2, it has begun to show signs of recovery. Even so, a V-shaped recovery is unlikely as spending behaviors will remain subdued until the virus subsides.

FIXED INCOME | We are 85% of benchmark duration. We are positioned for a steeper yield curve. We are overweight MBS, ABS, HY corporates, EM, and TIPS. We are underweight Treasurys.

GOLD | Weighed down by rising yields but long-term considerations still positive. We are neutral.

DOLLAR | Dollar technical composite total one of the lowest among major currencies. We are bearish.

Economic Summary

March 8, 2021

Near term activity: ● Accelerating ● Neutral ● Decelerating

Global Economy
(5.8%)

U.S. Economy
(4.6%)

U.S. Inflation
(2.2%)

Economic gauges reflect changes in near-term economic activity. Numbers in parenthesis refer to NDR 2021 forecasts.

Global Asset Allocation

● Overweight ● Marketweight ● Underweight

- ● Stocks (70%)
- ● Cash (10%)
- ● Bonds (20%)

Benchmark: Stocks (55%), Bonds (35%), Cash (10%)

Equities — Regional Relative Allocation

- ● Emerging Markets (17%)
- ● U.S. (57%) | Europe ex. U.K. (15%) | Canada (3%)
- ● Japan (4%) | U.K. (2%) | Pacific ex. Japan (2%)

Benchmark – U.S. (57.8%), Europe ex. U.K. (13%), Emerging Markets (12.6%), Japan (6.9%), U.K. (3.8%), Pacific ex. Japan (3.1%), Canada (2.7%)

Global Bond Allocation

- ● U.S. (48%) | Europe (30%) | Japan (17%) | U.K. (5%)

Benchmark: U.S. (49%), Europe (29%), Japan (16%), U.K. (6%)

U.S. Allocation

- ● Stocks (70%) | Small-Cap | Value
- ● Mid-Cap | Cash (10%)
- ● Bonds (20%) | Large-Cap | Growth

Benchmark: Stocks (55%), Bonds (35%), Cash (10%)

Sectors

- ● Financials (15%) | Industrials (12%) | Energy (4%)
- ● Health Care (11%) | Consumer Staples (5%) | Utilities (1%)

Benchmark: Technology (26.9%), Health Care (14.0%), Financials (9.9%), Communication Services (11.1%), Consumer Discretionary (12.0%), Consumer Staples (7.6%), Industrials (8.2%), Energy (2.4%), Utilities (2.9%), Real Estate (2.6%), Materials (2.5%)

U.S. Bonds — 85% of Benchmark Duration

Please see important disclosures at the end of this report.

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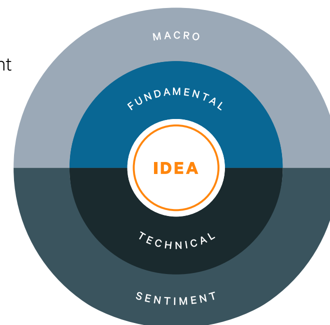

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