Ned Davis Research

Future Trends in Developed Capital Markets

Kevin Bates

Product Specialist

September 2024

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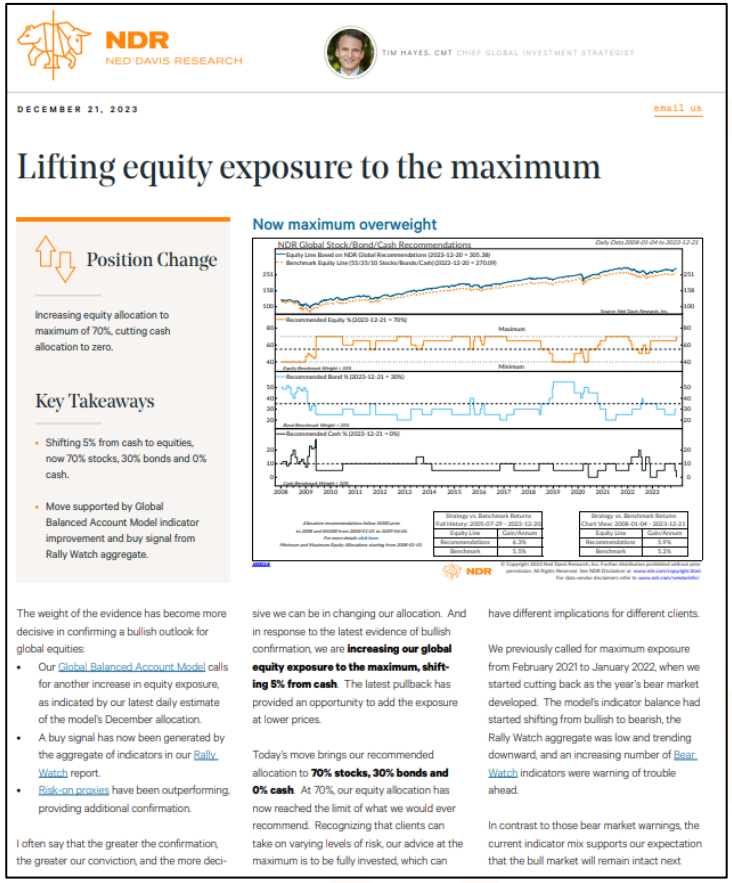

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TIM HAYES, CMT CHIEF GLOBAL INVESTMENT STRATEGIST

DECEMBER 21, 2023

email us

Lifting equity exposure to the maximum

Position Change

Increasing equity allocation to maximum of 70%, cutting cash allocation to zero.

Key Takeaways

- Shifting 5% from cash to equities, now 70% stocks, 30% bonds and 0% cash.
- Move supported by Global Balanced Account Model indicator improvement and buy signal from Rally Watch aggregate.

Now maximum overweight

NDR Global Stock/Bond/Cash Recommendations

The weight of the evidence has become more decisive in confirming a bullish outlook for global equities:

- Our Global Balanced Account Model calls for another increase in equity exposure, as indicated by our latest daily estimate of the model's December allocation.
- A buy signal has now been generated by the aggregate of indicators in our Rally Watch report.
- Risk-on proxies have been outperforming, providing additional confirmation.

I often say that the greater the confirmation, the greater our conviction, and the more decisive we can be in changing our allocation. And in response to the latest evidence of bullish confirmation, we are **increasing our global equity exposure to the maximum, shifting 5% from cash**. The latest pullback has provided an opportunity to add the exposure at lower prices.

Today's move brings our recommended allocation to **70% stocks, 30% bonds and 0% cash**. At 70%, our equity allocation has now reached the limit of what we would ever recommend. Recognizing that clients can take on varying levels of risk, our advice at the maximum is to be fully invested, which can have different implications for different clients.

We previously called for maximum exposure from February 2021 to January 2022, when we started cutting back as the year's bear market developed. The model's indicator balance had started shifting from bullish to bearish, the Rally Watch aggregate was low and trending downward, and an increasing number of Bear Watch indicators were warning of trouble ahead.

In contrast to those bear market warnings, the current indicator mix supports our expectation that the bull market will remain intact next

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- Market commentary and recommendations
- Platform of charts, indicators and models
- Global multi-asset coverage

NDR Investment Solutions

- Direct access to NDR's TAA models
- Tailored model portfolios
- Expand your product offering and AUM

Please see important disclosures at the end of this report.

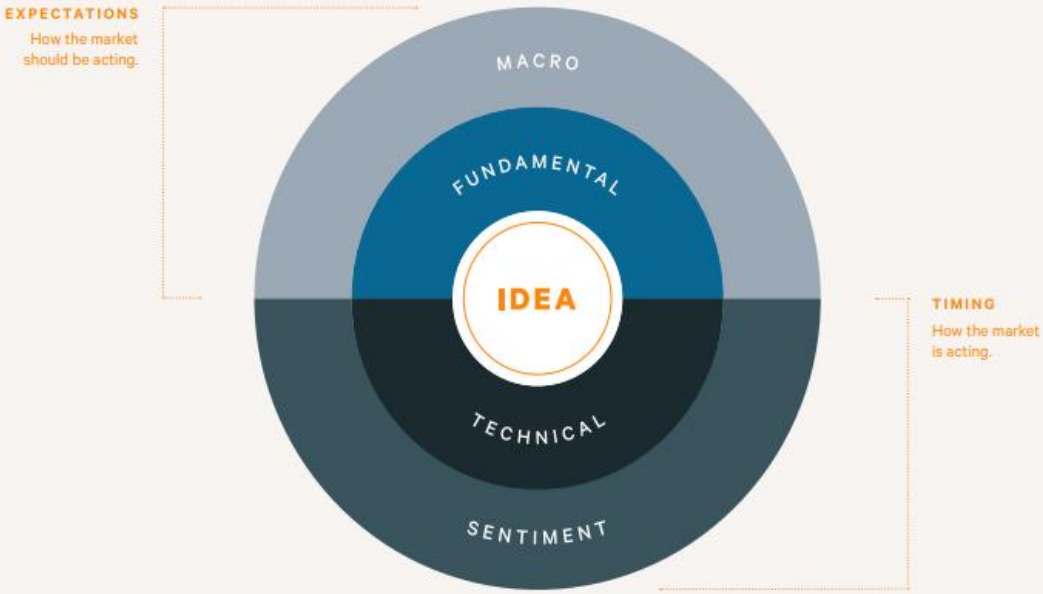
Agenda

- NDR's investment approach
- Macro vs. 60/40 portfolios
- Modeling developed markets
- Future development
  - Alternative Data
  - AI Implementation
  - Thematic investing
- Combining quant signals with human expertise

Ned Davis An early adopter of technology

Ned Davis "Weight of the evidence" approach

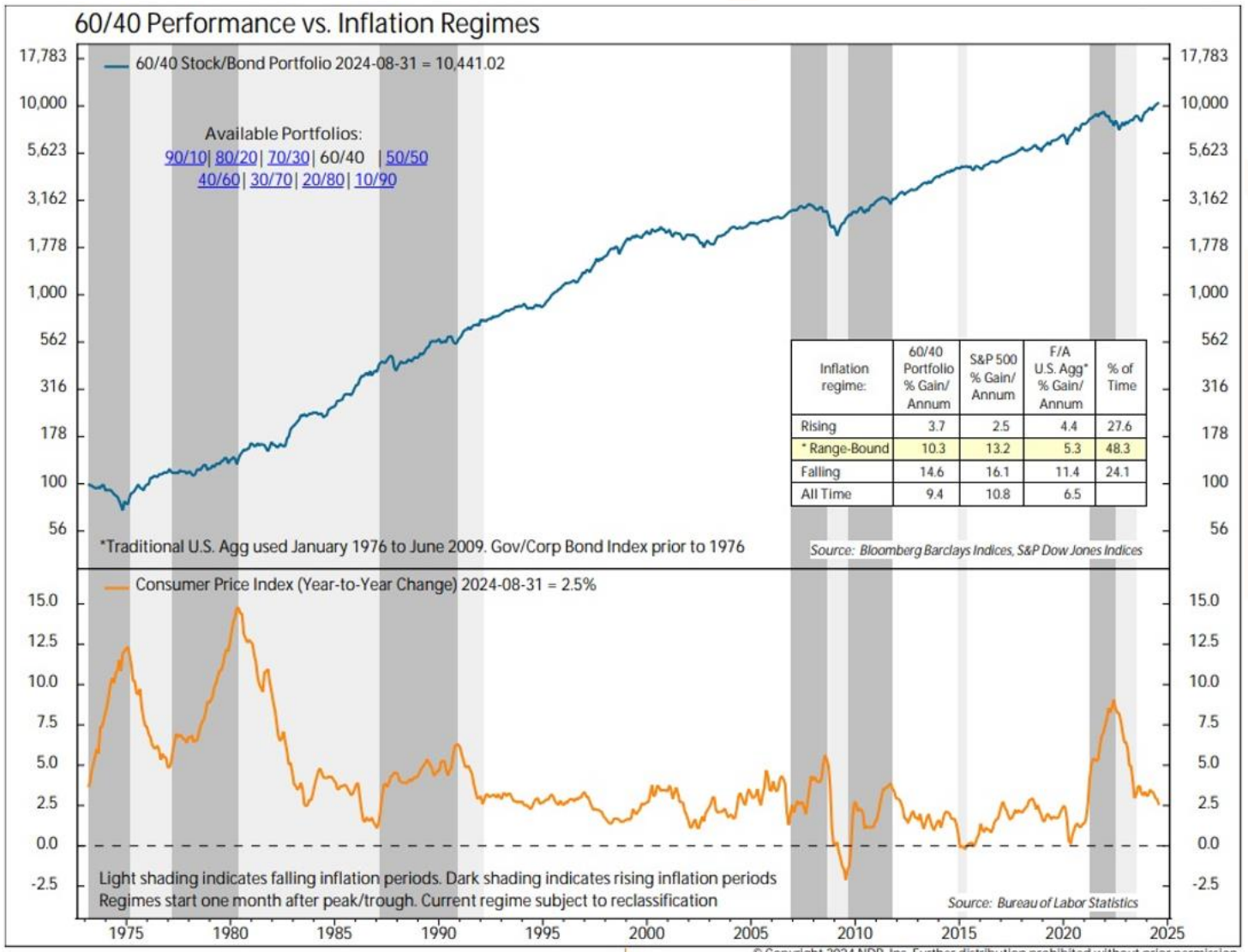
NDR 360° Methodology



"We are in the business of making mistakes. Winners make small mistakes, losers make big mistakes. Focus on risk management to keep mistakes small."

Ned Davis
NDR's Founder and Senior Advisor

Macroeconomic influences inflation vs. 60/40 portfolios



Inflation regime:	60/40 Portfolio % Gain/ Annum	S&P 500 % Gain/ Annum	F/A U.S. Agg* % Gain/ Annum	% of Time
Rising	3.7	2.5	4.4	27.6
* Range-Bound	10.3	13.2	5.3	48.3
Falling	14.6	16.1	11.4	24.1
All Time	9.4	10.8	6.5	

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"During 'The Golden Age of 60/40,' from 1982 to 2020, 60/40 portfolios performed extremely well as inflation fell. If inflation settles in a range above the Federal Reserve's 2% inflation target, investors will find it harder to make money through a passive 60/40 approach."

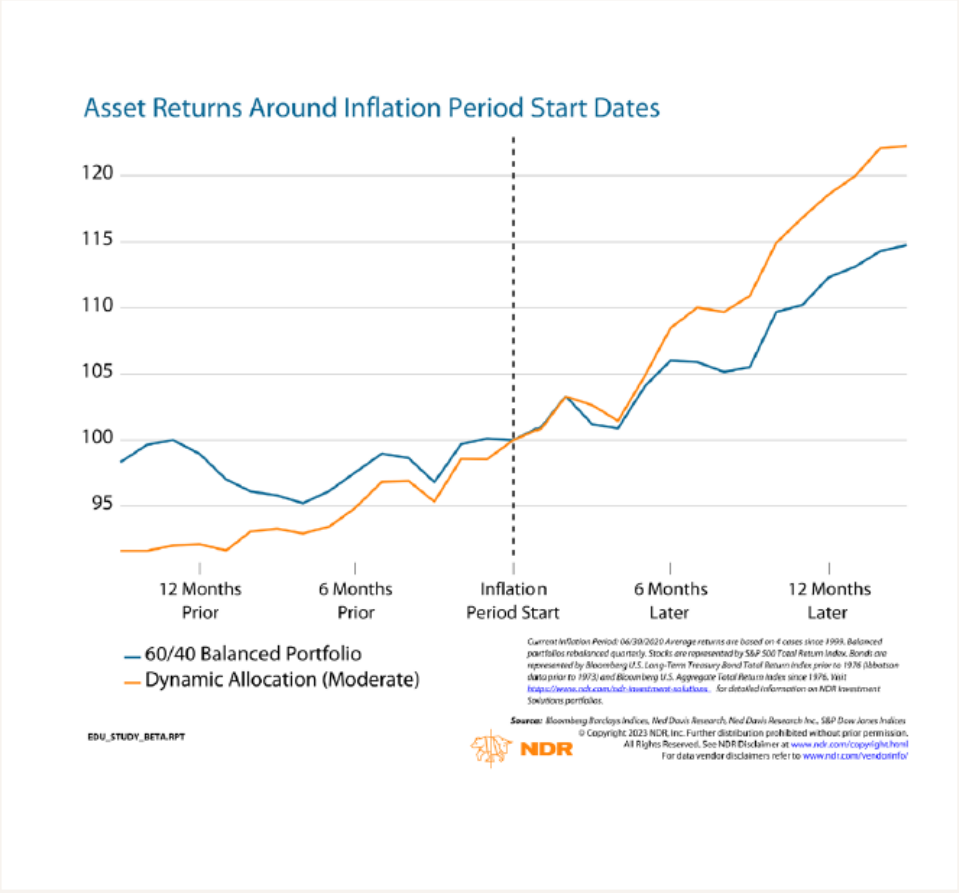
Joe Kalish, NDR's Chief Global Macro Strategist

Macroeconomic influences inflation vs. 60/40 portfolios

"A more active approach in terms of asset allocation, geographical positioning, and sector/industry/security selection will pay a greater role in generating returns."

Joe Kalish

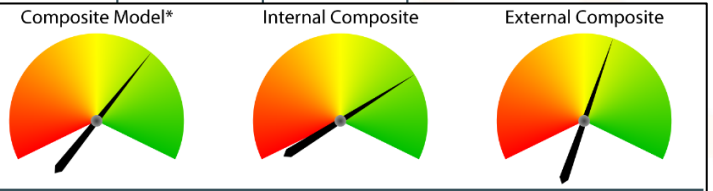
NDR's Chief Global Macro Strategist



Modeling developed markets U.S. Sector example

U.S. Sector Model Weights				
Sector	Model Weight vs. Benchmark Weight*	Month-End Readings		
		2024-08-30	2024-07-31	2024-06-28
Energy %	3.9	4.1	3.8	3.8
Materials %	2.3	0.8	1.1	0.8
Industrials %	8.5	8.6	9.2	9.0
Consumer Discretionary %	10.7	11.2	11.2	10.9
Consumer Staples %	6.6	7.8	6.3	5.1
Health Care %	12.4	14.4	13.8	14.2
Financials %	12.5			
Information Technology %	29.5			
Communication Services %	9.1			
Utilities %	2.2			
Real Estate %	2.3			

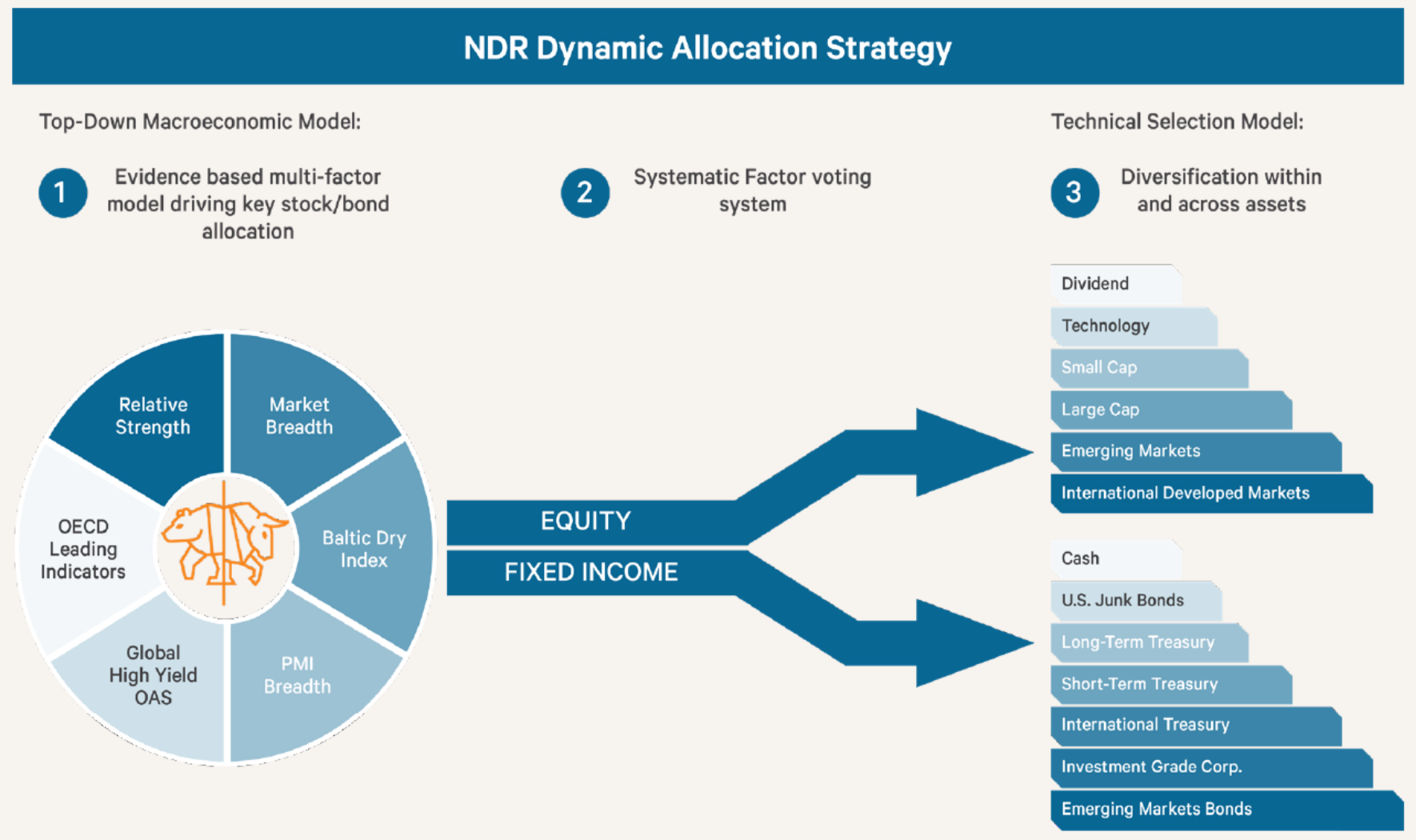
- Provides a view on 11 S&P 500 sectors
- Easily implementable with ETFs (Sector SPDRs)



Health Care Model Readings				
Indicator	Intra-Month Reading	Month-End Readings		
		2024-08-30	2024-07-31	2024-06-28
Health Care Composite	66.7	62.5	83.3	62.5

Health Care Sub-Model Readings				
Indicator	Intra-Month Reading	Month-End Readings		
		2024-08-30	2024-07-31	2024-06-28
Health Care Internal Composite	75.0	66.7	100.0	50.0
Health Care External Composite	58.3	58.3	66.7	75.0

Model Portfolios for Wealth Managers

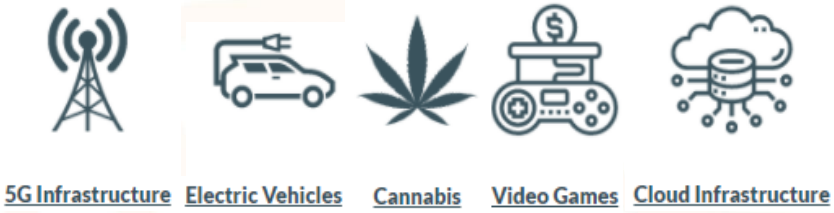


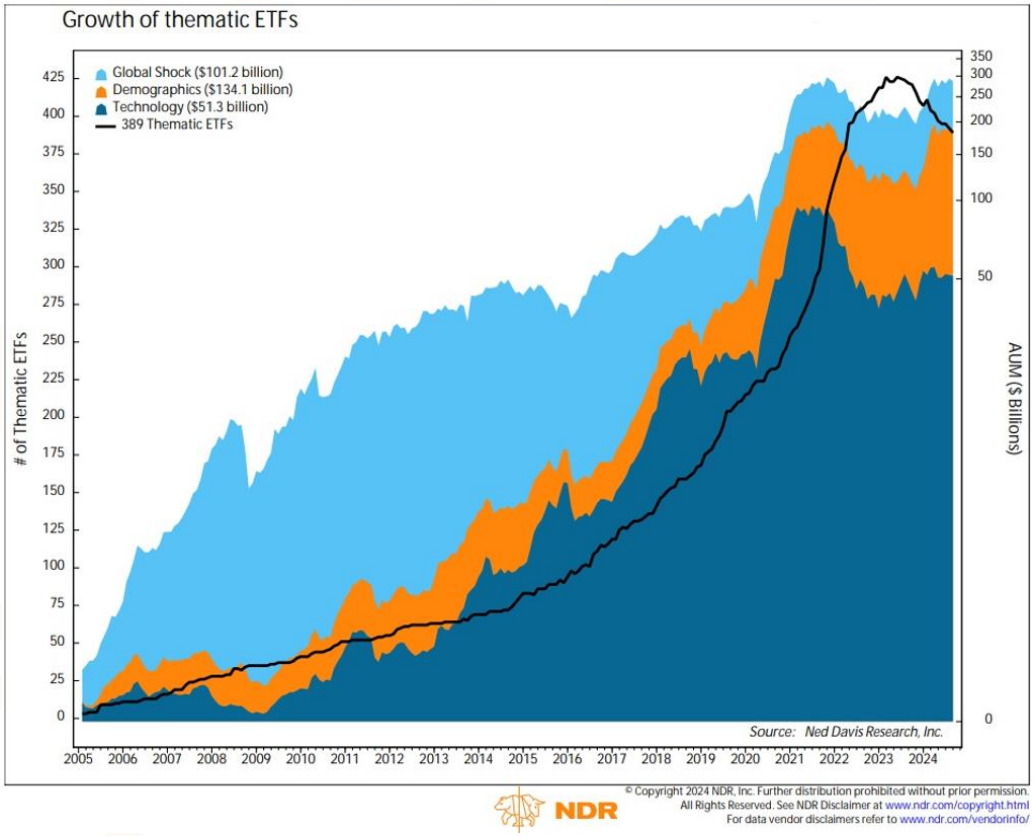
Modeling developed markets – Future development

Alternative data

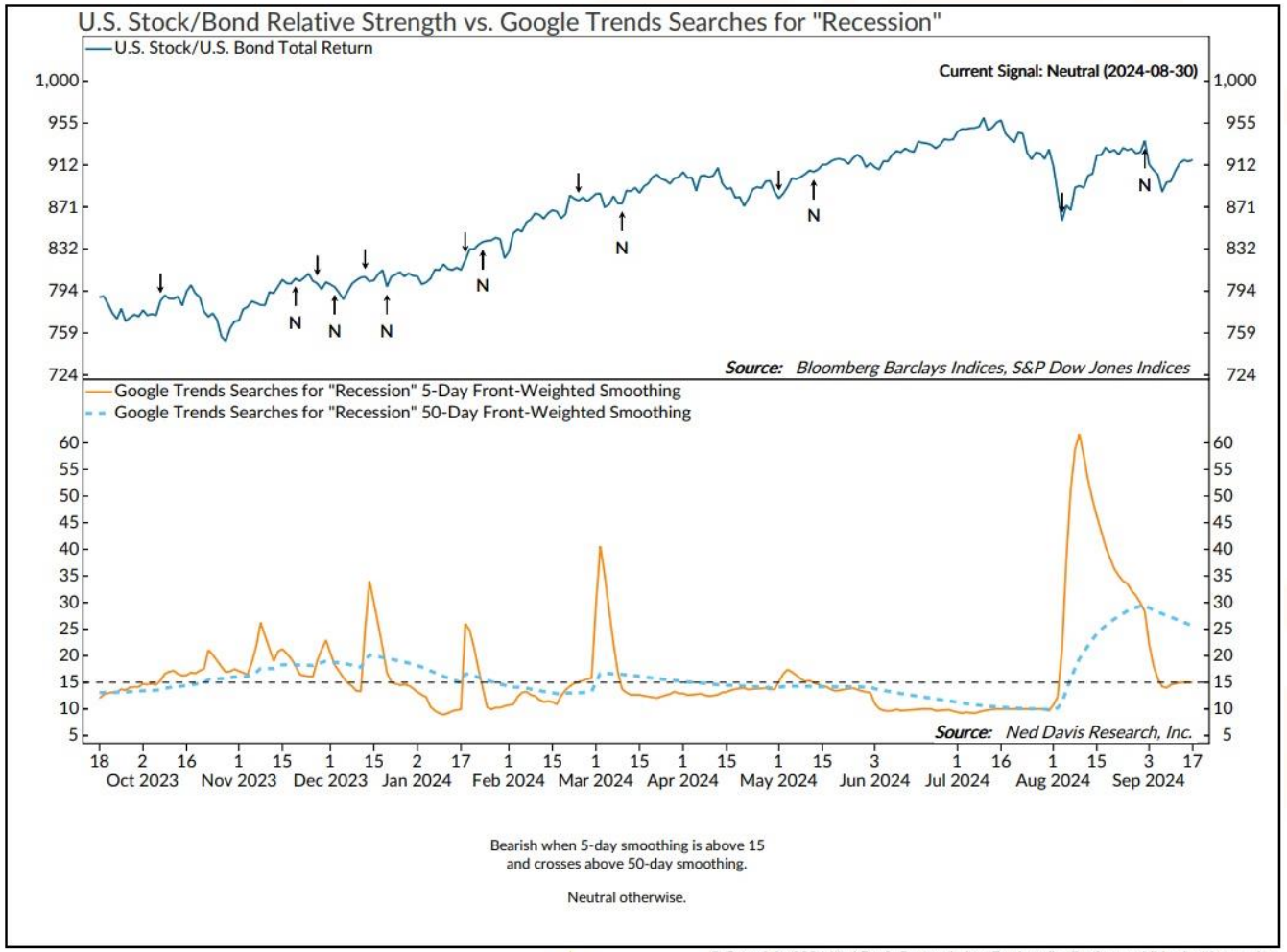
AI implementation / NLP

Thematic Investing





Alternative Data U.S. Stock / Bond Allocation vs. Google Search



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- Part of U.S. Asset Allocation Model
- Rising volume of Google searches for “recession” coincide with U.S. equity drawdowns

AI Implementation – Natural Language Processing (NLP)

- NLP, or Natural Language Processing, is a form of Artificial Intelligence that enables machines to break down and interpret natural human language.

- Natural human language is full of ambiguity and is constantly evolving language (especially on social media).

- NLP leverages the latest Deep Learning techniques to take unstructured data (like news articles, chats, tweets, etc.) and enable the machine to 'learn' the meaning from the text.

Thematic Opportunities Score

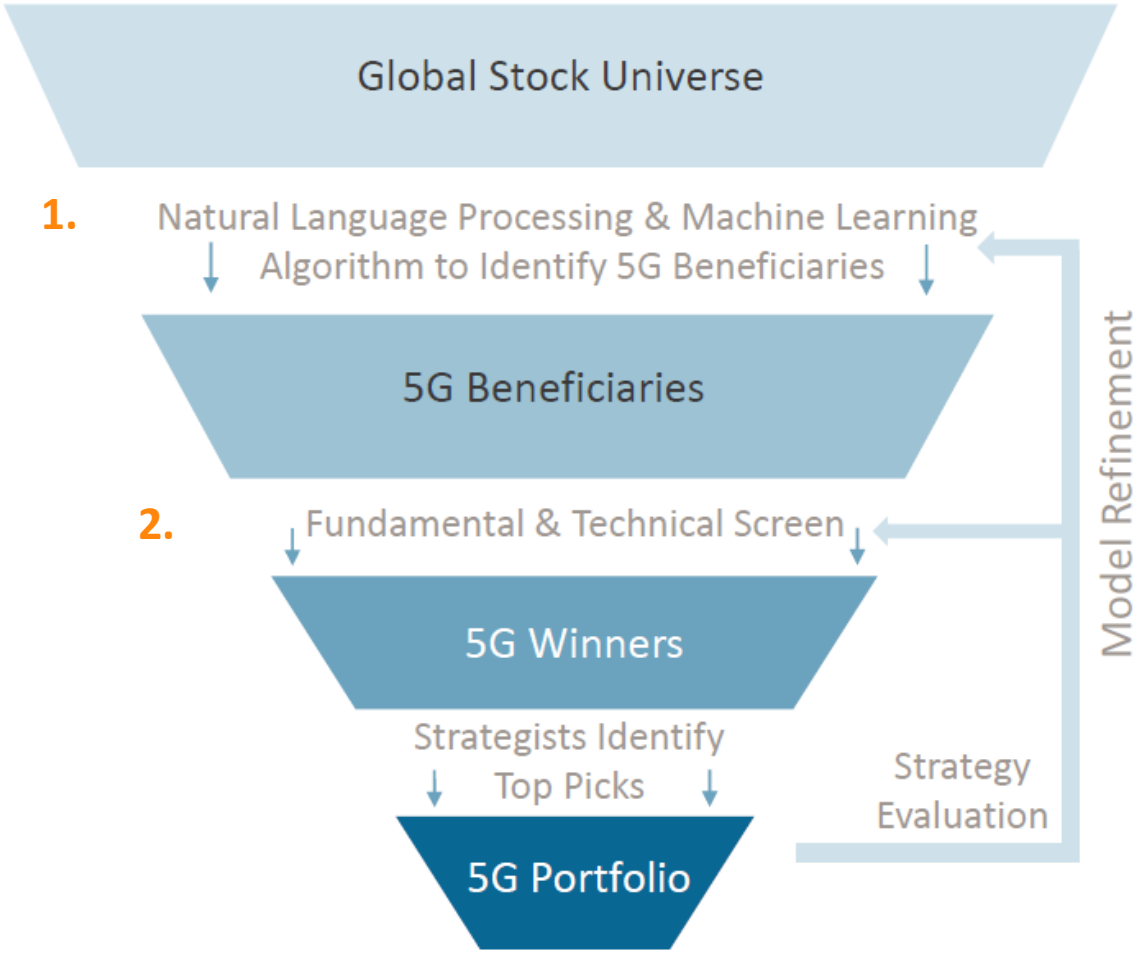
NDR Thematic Opportunities Score quantifies how closely a company's business description aligns with a user-defined theme.

- Proprietary NLP-based algorithm compares the descriptions of over 60,000 global companies to the selected target
- Score ranges from 0 (not at all related) to 100 (perfectly aligned with theme)
- "Themes" can be topics like "electric cars" or "cloud computing" …or more abstract like "travel to Mars"
- Themes are defined by target companies (like Tesla for "electric cars") and/or keywords (like "battery")

Thematic Scoring Example 5G Winners Portfolio

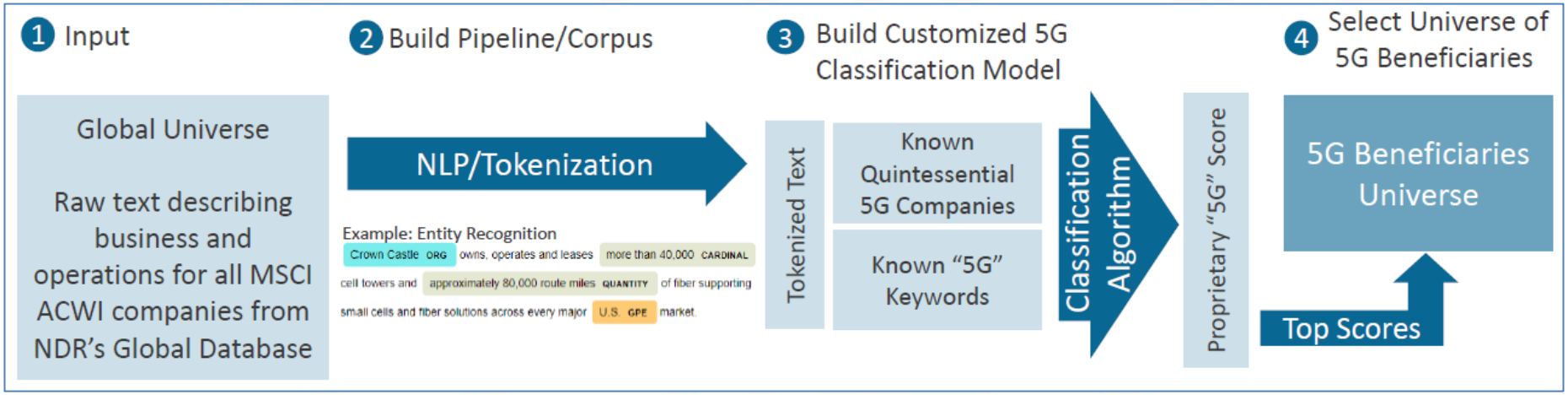
Objective:

Select companies best positioned to capitalize on the "5G" movement

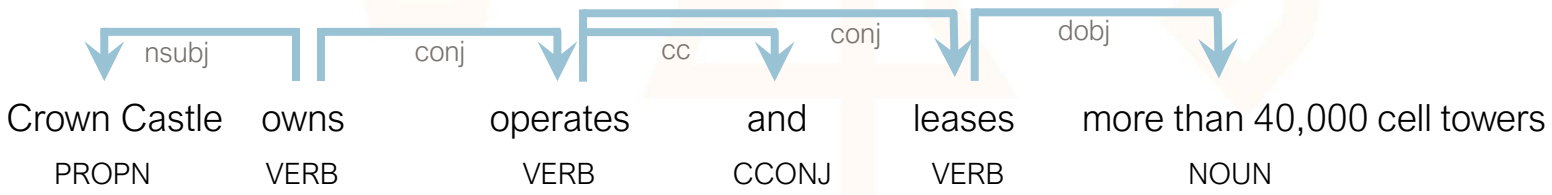


Thematic Scoring Example 5G Winners Portfolio

1. Use NLP and Machine Learning to identify companies that support and/or benefit from the growth of 5G communication



Example: Text Relationships and POS Tags



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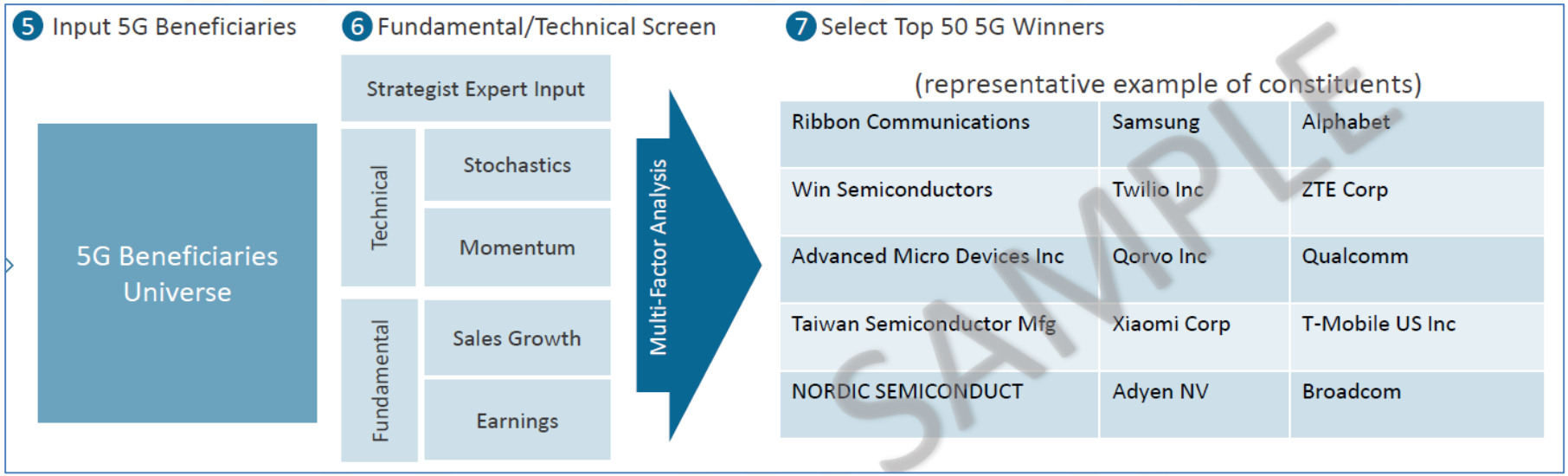
Thematic Scoring Example 5G Winners Portfolio

2. Expert developed fundamental and technical selection criteria used to distinguish best positioned companies from 5G Beneficiaries Universe



SAMPLE

Thematic Opportunities Score - Implementation

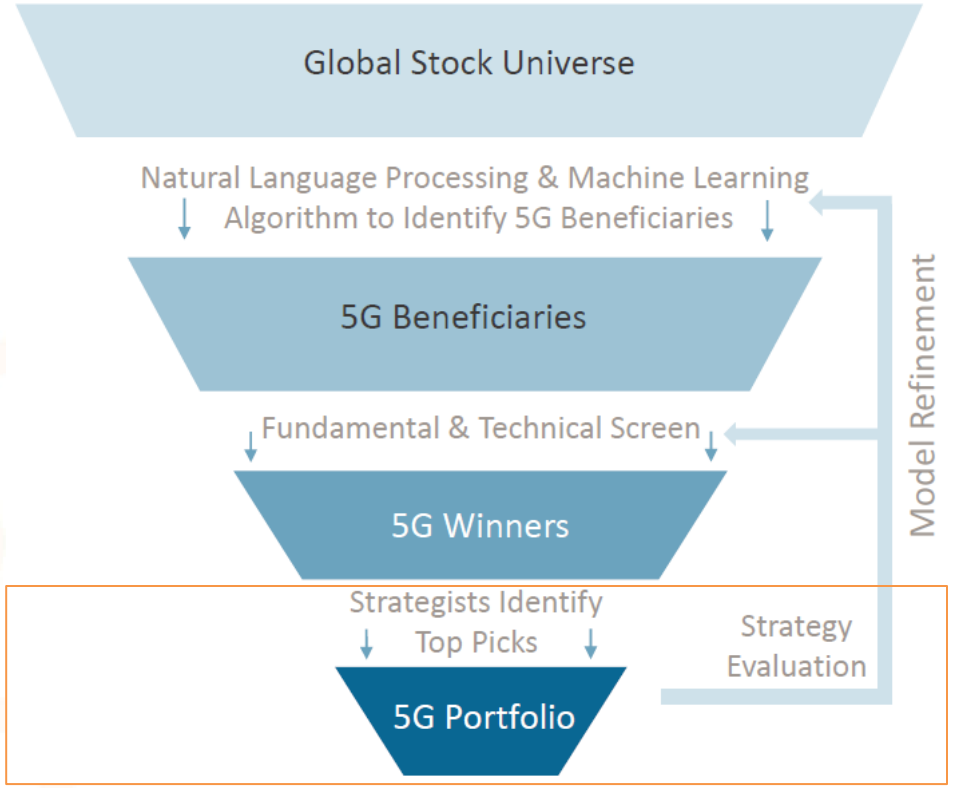
The Thematic Opportunities Score augments NDR's traditional 360° approach with cutting-edge NLP algorithms to quantify alignment to specified themes with maximum efficiency.

Valuable use cases:

- Thematic Index/ETF creation (Broad Exposure)
- Thematic Stock Portfolio creation (Targeted Exposure)
- Thematic Relevancy

Bottom Line – Quant Signal + Human Overlay

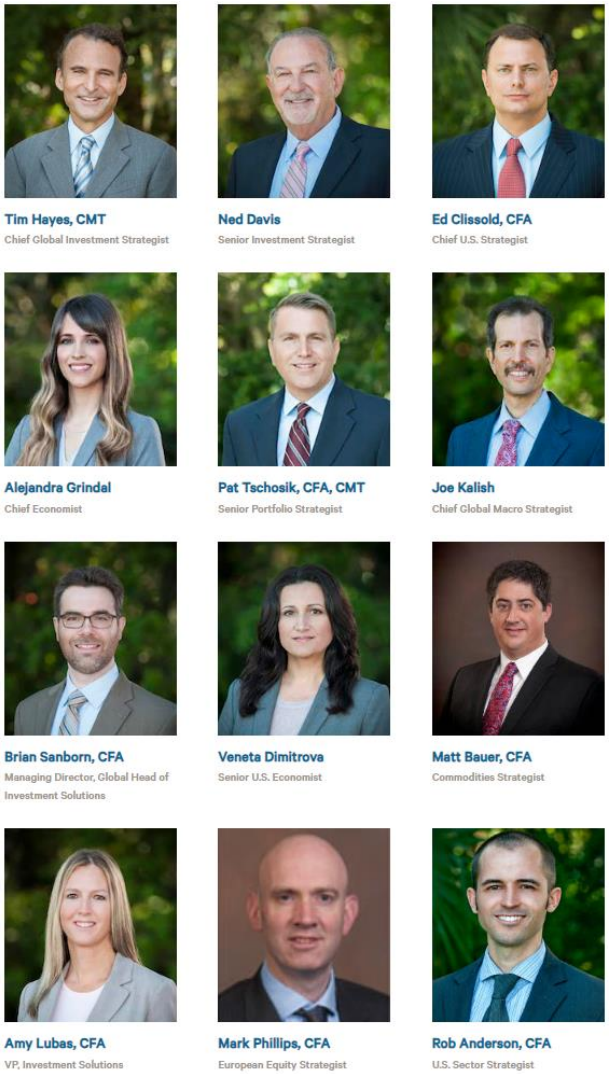
Final portfolio selection based on multi-factor quantitative model with Strategist oversight



Bottom Line – x5 major investment themes for the next decade

	Real GDP	Inflation	Potential impact
AI and innovation	↑	↓	• Increased investment and potential productivity gains • May take several years before economy-wide productivity boost • Starting in the U.S., but spillover to other economies
Deglobalization	↓	↑	• Reconfiguring supply chains, near-shoring, ally-shoring • Prioritizing security over efficiency • Reduced trade flows. Untapped comparative advantage => loss of productivity • Reduced foreign demand for financial assets, such as government bonds
Demographics	↓	↑↓	• Slower labor force growth • Tighter labor markets • Rising old-age dependency ratio • Reduced aggregate demand with aging
Fiscal challenges	↓	↑	• More burdensome debt service • Upward pressure on interest rates • Crowding out of private investment • Central banks may become more tolerant of higher inflation
Clean energy transition	↑↓	↑	• Reduced investment in fossil fuels • Increased demand for clean energy commodities, such as metals, used in EV batteries • Government incentives for clean energy development

Bottom Line – Tactical market outlook



Do expect

- Soft Landing
- Sluggish 2H GDP (< 2%)
- Volatility next few months
- Potential yearend rally

Do not expect

- Recession
- Major shift to bonds
- Secular bear market in equities

NED DAVIS RESEARCH

NDRsales@ndr.com
www.ndr.com
(800) 241-0621

SARASOTA

3665 Bee Ridge Road Suite 306
Sarasota, FL 34233
United States
800 241 0621 (U.S. & Canada)
941 412 2300

NEW YORK

1270 Avenue of the Americas
11th Floor
New York, NY 10020
(800) 241-0621

LONDON

4 Bouverie Street
Temple, London
EC4Y 8AX
+44 20 7779 8454

HONG KONG

12/F, 8 Queen's Road East
Wan Chai
Hong Kong
+852 3416 6676

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See the Signals.™

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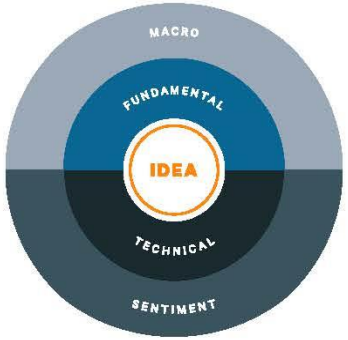

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