With stability in our regional fundamental indicators, we maintain our existing regional allocation preferences. Global revisions remain strong, with no signs of a global slowdown visible in bottom-up revisions metrics, suggesting the recent investor tilt toward bonds and Growth stocks may not last.

We continue to have a strong overweight in the US, and outside the US we still prefer the Eurozone. We are underweight Emerging Markets and developed Asia. As noted last month, Canada and UK offer favorable regional bets for those seeking Value-oriented exposure. Emerging Markets still look weak in our work, and only moderately better when excluding China.

<table>
<thead>
<tr>
<th>Regional Pair</th>
<th>Favored</th>
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<tbody>
<tr>
<td>Emerging vs Developed</td>
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<tr>
<td>N. America vs EAFE</td>
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<tr>
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<td>US vs Canada</td>
<td>US</td>
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<tr>
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<td>Eurozone</td>
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<tr>
<td>Japan vs Asia ex Japan</td>
<td>Asia ex Japan</td>
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</table>
Regional allocation recommendations

Exhibit 1 below and at right shows our updated regional allocation framework and our current recommendations. Our hierarchical framework highlights a set of pair-wise regional allocation decisions that capture most of the key decisions that clients are making. It allows for flexibility by providing both simple independent binary (i.e., in or out, over- or underweight) decisions at several levels, as well as a complete set of recommended allocation weights for those looking to see how all of the recommendations combined can fit together.

The benchmark (neutral) weights are based partly on relative capitalization weightings, but simplified and adapted for our purposes. In particular, no region has a benchmark weight less than 10% regardless of the actual cap weighting. Our recommended weights, however, can vary more and will generally be kept in increments of 5%, including zero weights potentially.

At right is a summary list of the views shown below.

Exhibit 1: We maintain our allocation preferences, still overweight US and Europe ex UK, underweight EM and Asia

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</table>

Recommended allocations are shown in **bold** in each box, neutral (benchmark) weightings shown in *italics* in parentheses. Favored regions within each pair are highlighted in **green**.

*Source: Mill Street Research, Factset, Bloomberg*
**Strong revisions activity globally still led by US and Europe ex UK**

**Estimate revisions activity globally has held at historically strong levels even amid worries about the spread of the Delta variant of COVID-19.**

**The US and Europe ex UK still lead on our revisions metrics.**

In recent months we have highlighted the improvement in aggregate earnings estimate revisions breadth in Europe ex UK. The region is now just behind the US on our broad equal-weighted revisions breadth measures (lower chart at right).

The US has maintained its relative revisions leadership, and we could see another round of better-than-expected earnings reports for Q2.

Canada and the UK have also shown improvement recently, and are now very close to the global average on revisions metrics. Both have a Value/Cyclical tilt in their sector composition, and Value-oriented sectors remain a source of fundamental strength in our work.

Asia and Emerging Markets are weakest on our indicators. Developed Asia ex Japan and Emerging Markets have the lowest aggregate revisions readings, and both are seeing particularly strong impacts from COVID in key countries right now (e.g. Australia, Brazil, India, etc.).

COVID continues to have an impact on relative regional revisions activity, but has not had a recent significant impact on the overall level of revisions globally.

Investors appear to be worrying about weaker economic growth as bond yields fall and Growth stocks outperform Value stocks.

As we discuss further on page 5, there is little sign that analysts are finding reason to slow their estimate increases, much less cut forecasts outright. Thus we suspect the "growth scare" of recent weeks may not be sustainable.

**Exhibit 2: Global estimate revisions breadth remains extremely high, still led by the US and Europe ex UK**

*Source: Mill Street Research, Factset, Bloomberg*
Regional ETF Ranking and Top-Ranked Global Large-Caps

Exhibit 3 at right shows the cap-weighted aggregate MAER ranking for the constituents of the seven ETFs that track the major regions that we follow. While there can be a tendency for the aggregate rankings to cluster near the neutral 50% level at times due to the broad, heterogeneous composition of these indices, we can get a feel for where there are areas of bottom-up strength and weakness based on our six-factor composite MAER ranking model.

The regional ETF ranking shows the Eurozone now at the top along with Canada, followed by the UK and US. Emerging Markets remain weakest by a considerable margin.

Exhibit 4 below is a list of the top 25 largest global stocks that rank within the top decile of the combined universe of all constituents of the seven ETFs shown here. Thus these stocks are some of the most attractive names in our work globally that are also heavy weights in the cap-weighted indices (ETFs). There remains a strong cyclical tilt in the sectors represented, and less US exposure than before.

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**Exhibit 3: Cap-weighted aggregate MAER ranking of constituents of key regional index ETFs.**

<table>
<thead>
<tr>
<th>Region (ETF)</th>
<th>Aggregate MAER Rank</th>
<th>1 Month Ago</th>
<th>2 Months Ago</th>
</tr>
</thead>
<tbody>
<tr>
<td>Eurozone (EZU)</td>
<td>62.5</td>
<td>54.7</td>
<td>57.2</td>
</tr>
<tr>
<td>Canada (EWC)</td>
<td>61.5</td>
<td>60.2</td>
<td>61.7</td>
</tr>
<tr>
<td>UK (EWU)</td>
<td>57.9</td>
<td>52.7</td>
<td>52.4</td>
</tr>
<tr>
<td>USA (SPY)</td>
<td>57.8</td>
<td>62.1</td>
<td>67.2</td>
</tr>
<tr>
<td>Pacific ex Japan (EPP)</td>
<td>47.4</td>
<td>47.8</td>
<td>50.4</td>
</tr>
<tr>
<td>Japan (EWJ)</td>
<td>47.3</td>
<td>49.1</td>
<td>49.1</td>
</tr>
<tr>
<td>Emerging Markets (EEM)</td>
<td>34.7</td>
<td>37.9</td>
<td>42.4</td>
</tr>
</tbody>
</table>

Source: Mill Street Research, Factset, Bloomberg
Falling US yields driving recovery in Growth vs Value globally, but may not last

A key feature of recent global equity market action has been the outperformance of Growth stocks relative to Value stocks. While especially pronounced in the US, it is a global trend.

One apparent driver of investor sentiment toward Growth and Value is the trend in US long-term bond yields, which are widely used as a global benchmark.

Falling bond yields suggest expectations of weaker economic growth and inflation, which are conditions that are viewed as relatively more favorable for Growth stocks than Value (cyclical) stocks.

The top chart at right plots the relative return of the MSCI ACWI Growth versus Value indices over the last two years, along with the return of long-term US Treasury bonds (proxied by the popular bond ETF with ticker TLT).

We can see the tendency for Growth/Value returns to move along with US Treasury bond returns, and the latest bout of outperformance by Growth is aligned with the latest rally in bond prices.

Is global growth in fact weakening sharply as one might infer from the drop in bond yields? While the extreme stimulus-driven peaks in global growth cannot be maintained, the level of economic activity is still quite healthy by recent years’ standards.

One straightforward measure of growth expectations from a bottom-up perspective is the trend in aggregate analyst earnings expectations.

The bottom chart at right plots the aggregate (cap-weighted) next-12-month (NTM) earnings per share estimates for Factset’s broad World universe over the last three years.

We see that estimates continue to rise at an aggressive pace, even in recent weeks, with no real signs of a pause, much less a downturn. This suggests global earnings and economic growth still has some momentum, and thus the recent preference for Growth stocks may not last much longer.

Source: Mill Street Research, Factset, Bloomberg
Value-tilted Canada and UK holding up versus ACWI ex-US markets

For exposure outside of the US, we have been somewhat more positive in Canada and UK recently as ways of getting exposure to Value-oriented regions.

Last month we added exposure to both Canada and UK, bringing Canada to benchmark weight and reducing our underweight in the UK. We remain comfortable with those moves, and view both markets as offering exposure to Value/Cyclical sectors for those looking to lean against the recent Growth tilt in returns globally.

Because of the heavy weight the US carries in the benchmark MSCI ACWI index (58% currently), we have created indicator charts for Canada (the ETF with ticker EWC) and UK (ETF ticker EWU) relative to the MSCI ACWI Ex-USA index below.

Canada has outperformed the ACWI ex US sharply this year, but has recently paused. Its relative revisions metrics remain favorable, though relative valuations have shifted from highly supportive to more neutral as a result. The UK, by contrast, has seen less relative return activity but revisions have improved further, allowing relative valuations to return to multi-year favorable readings for the UK. Thus both countries are reasonable ways to gain Value exposure for those seeking it.

Exhibit 6: Canada’s metrics are holding up vs ACWI ex US. UK is continuing to look better relative to ACWI ex US.
Emerging Markets remains a key underweight in our regional allocations, and we have noted in recent months the negative influence of China on the overall MSCI EM index.

Below we show our regional ETF indicator charts for the widely-followed MSCI Emerging Markets ETF (ticker EEM) relative to the global ACWI benchmark ETF, and also for the MSCI Emerging Markets ex China ETF (EMXC) to highlight the differences and similarities.

The relative revisions metrics for EEM remain very weak, and there has been little sign of a change in the trend of underperformance recently. Despite the underperformance, relative valuations for EEM vs ACWI have not moved much and remain near neutral readings.

The EMXC indicators are “less bad” than those for EEM, and certainly have a more favorable valuation profile. This suggests that the influence of Chinese stocks (34% of the weight in EEM) remains net negative both for revisions and for valuations. Non-China EM stocks in aggregate are cheap relative to their historical average, and relative revisions magnitudes (blue bars) are somewhat positive, but are still seeing well below-average revisions breadth. Overall we would remain underweight EM stocks with or without China, but would prefer ex-China for now.

Exhibit 7: EM metrics remain unfavorable relative to the broader ACWI. China’s large influence remains a net negative for EM, with EM ex-China looking much cheaper and somewhat less negative on revisions and returns.
Hypothetical Performance Tracking

Below we show hypothetical performance tracking results for the regional allocation recommendations as published in this report (page 2). See important disclosures below and on the following page.

The allocation weightings were first published July 16th, 2019. Results after March 18th, 2020 will reflect the revised regional framework used in this report. Results for short time periods should always be interpreted with caution.

Returns based on ETFs corresponding to each region using total returns in US dollars.

Note: Results shown here do not reflect any actual trading and are for informational purposes only. They do not include important considerations such as transactions costs, taxes, fees or other expenses. Past performance is no guarantee of future results.

Source: Mill Street Research, Factset, Bloomberg
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