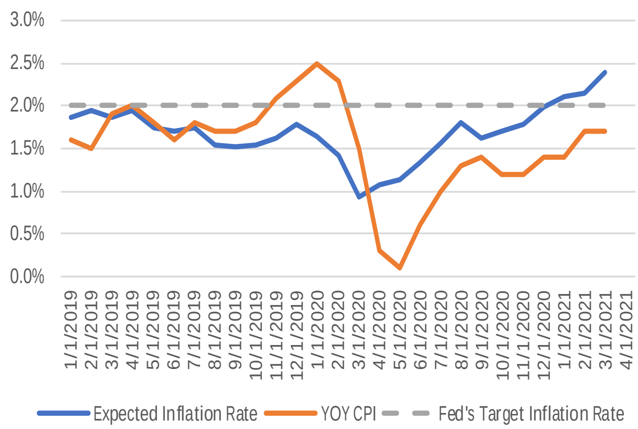
Global Market Positioning

April 2021

Real-time insight on how DuPont Capital has positioned its portfolios as a function of key factors driving the markets.

Key Market Factors (as of April 2021)

Inflation

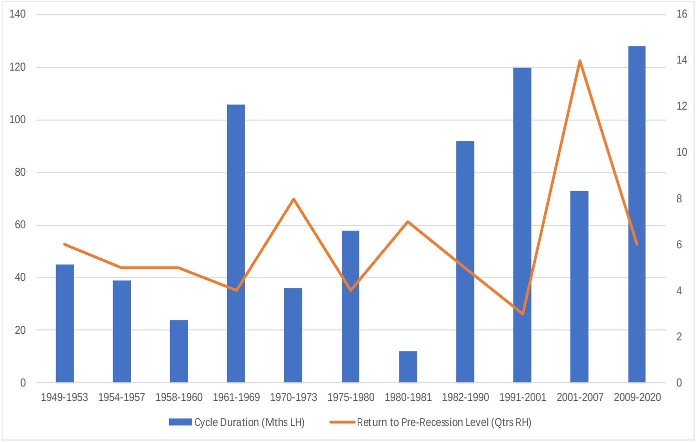


Source: Bloomberg
As of March 31, 2021

Will Inflation Be Transitory?

- Inflation expectations rose above the Fed's 2% target due to higher projected economic growth, massive fiscal stimulus, and a very accommodative Federal Reserve.
- Inflation will most likely rise well above 2% over the coming months, but the Federal Reserve believes the higher inflation will be transitory and decline toward its target over time without any action.
- Treasury yields rose for intermediate and longer maturities in the 1st quarter with the ten-year rising by 81 basis points from 0.93% to 1.74%.
- The yield curve steepened. The spread between the two-year and ten-year rose from 80 bps at year end to 158 at the end of the 1st quarter.
- Credit spreads were less volatile with investment grade corporates and EMD sovereigns ending close to unchanged for the quarter while high yield tightened.

U.S. Economic Expansions/ Recoveries Duration



Source: NBER. Morgan Stanley.

Sizing the Cycle

- Despite the severity of the pandemic-induced economic downdraft, the U.S. is projected to recovery sharply. Real GDP set to reclaim prior levels within six quarters – a similar repair period to many historic "normal" recessions.
- Historically, rapid U.S. recoveries – those characterized by a snapback in the manufacturing index (ISM) of less than 12 months – have been associated with (i) healthy market performance in the subsequent several quarters and (ii) subsequently more muted momentum in Treasury yields.
- Investors should be open-minded to the possibility that this economic cycle may not be quite as protracted as the 100-month average of the previous two. The interplay of fiscal and monetary policies merits attention once more.
- A shorter or more rapidly evolving cycle would suggest selectivity within Value exposures (operational leverage over market beta) and not shifting too aggressively away from higher Quality names if structural advantages are inherent.

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Current Positioning (as of April 2021)

Global Equity

- Investors anticipate a robust economic recovery with the possibility that dormant inflation expectation could be fully reignited. The reflation trade of the last several months has been equally as evident within equities as among other asset classes. Value and small cap names have assumed market leadership and have outperformed in parallel with higher yields and commodity prices.
- However, much of the early cycle rebound has already become reflected in prospective valuations. As the first quarter progressed, we saw an intra-style rotation out of deep value characteristics (such as Price to Book and Beta) toward less aggressively risk-seeking ones like Price to Free Cash Flow. There is an array of near-term inflation impulses from deferred demand, constricted supply chains and potential infrastructure capex stimulus, but structural economic trends and digital/demographic dynamics will persist. A sustainable multi-year change in market regime may prove illusory.
- In terms of positioning, we tend to see more favorable risk-reward stances in expansion-driven reflation opportunities than in pursuing a scenario of runaway or self-fueling inflation. This entails maintaining pro-cyclical tilts, while discriminating from a bottom-up perspective around the trajectory and duration of company-specific earnings drivers. Relative valuations need to be considered across a range of horizons. Near-term they are attractive for well-capitalized Financials with the strongest balance sheet flexibility, from a two year perspective recovering Aerospace and tech-transitional Auto end markets offer potentially undervalued quality exposures.
- The U.S. market continues to trade at a notable premium to other regions, despite the recent outperformance of value categories, which provides a compositional benefit to international markets. Geographically, some European hubs and several Emerging Markets are currently vaccine and/or lockdown laggards. These overhangs should be addressed over the coming months, with the expectation that economic recovery rates will re-converge into the second half.

Fixed Income

- The Federal Reserve's projection is that the Funds Rate will likely remain near 0% until 2023 and it will aim to achieve inflation moderately above 2% so that inflation averages 2% over time. Most of our portfolios have durations that are shorter than the benchmarks.
- Investment grade corporate spreads were close to unchanged during the quarter and are tighter than long term averages. We increased our allocation to corporates in 2020 when spreads were much more attractive. We did not make many changes in the 1st quarter of 2021 despite a significant amount of new issuance. We favor the basic industry, insurance, consumer cyclical, energy, and electric utility sectors.
- In Long Duration, we had very little exposure to long corporates at the beginning of 2020 and greatly increased our allocation from March through July due to the much more attractive spread levels. In 2021, we have not been active as we are not finding new opportunities with good value.
- High yield spreads tightened this quarter and are much tighter than long term averages. We were very selective in adding positions in the 1st quarter and will remain cautious.
- Emerging Markets Debt (EMD) declined along with Treasuries with spreads close to unchanged for the quarter. In the spring of 2020, we added numerous positions to our EMD portfolios when spreads widened, but we have been much less active over the last nine-to-twelve months. We believe that EMD is more attractive than other sectors of fixed income, particularly the high yield portion of EMD. Our main overweights are in Mexico, Brazil, Ukraine, Turkey, and Argentina.