Citi Global Wealth Investments

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Answers To Your Top Questions:

What's Next for Global Equities? And What About Tech?

Key Takeaways

- More than 75% of global equity markets are trading above their 200-day moving average. Broadening of equity performance is occurring beyond the US. Global inflation is falling, and central banks are poised to dial back tight monetary policy. This will mean a stronger world economy in 2025. Forward-looking equity investors should consider that returns may be earned more broadly across the world in such an environment.
- It is not too late to consider tech. In fact, technology should remain a cornerstone of suitable investor portfolios. Plenty of tech stocks have lagged high-flying mega caps since the start of 2023. For long term investors, we see virtue in semiconductor manufacturers, robotics and select software players.
- The combination of lower policy interest rates, slowing inflation, uninterrupted economic growth and rising corporate profits is as close to an ideal setting for financial markets. As this data and policy became clear, global equity markets rallied without a setback for the past five months. Looking forward, they may still benefit from the mere confirmation of this forecast path but will likely appreciate at a slower pace unless there are further positive surprises.

Potential Portfolio Implications

Our focus is to identify growth opportunities and associated risks across the world. We ask investors to consider a global view, keeping in mind the value of diversification. US shares cannot outgrow the rest of the world by a much larger margin than in the past.

Separately, we still believe tech should remain a cornerstone of portfolios for suitable investors. In a global economy increasingly propelled by technological innovation, we believe investors should seek exposure to technology in their portfolios. In particular, Artificial Intelligence (AI) linked thematic plays in the semiconductor space, robotics, and select software plays are timely.

Answers to Your Top Questions

Q1: Given the Performance of US Equities, Why Should Investors "Go Global"?

Given the performance of US equities over the past 15 years and the strength of the dollar, US investors wonder whether there is value in international diversification. Many non-US investors who have built US portfolios feel similarly. For the most part, we think US firms have earned most of the premium in valuation that has arisen over the past decade (see **FIGURE 1**). But that is not a forward-looking view.

Our focus is to uncover growth opportunities and to manage portfolio risk at the same time. A "bottoms-up" approach to asset allocation in a global portfolio leaves us overweight US equity sectors by 5.5% compared to a -3.5% position for non-US shares today. As we described the September Quadrant, fast growing companies outside the US are doing well, but there are fewer of them.

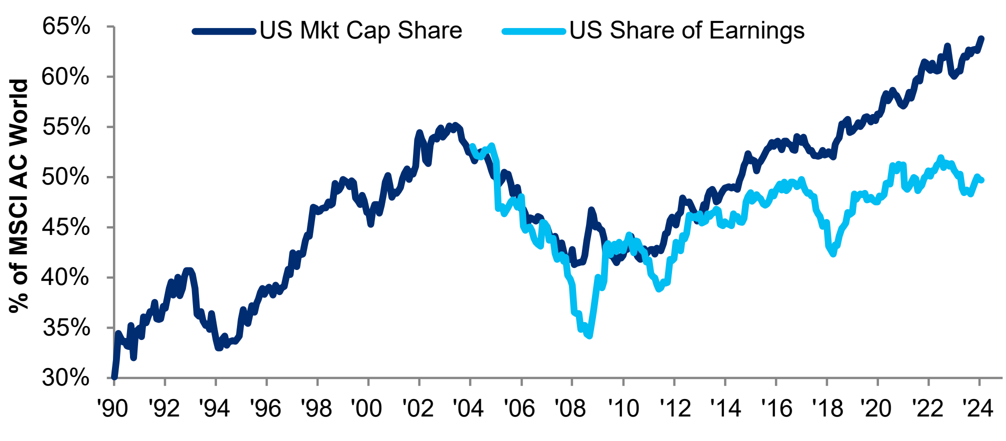
If you simply extrapolate past performance into the future, some trends become unsustainable. Looking at data since 1970, US equities have never been a larger share of the world equity market as measured in US dollars. US Equities have risen from about 40% of world equity market cap in 2010 to 65% today. But to repeat the outperformance of US shares, domestic markets would have to rise to 90% of the world equity market in the next 15 years. This seems highly unlikely.

The strongest performing asset class or region in each decade is rarely the same one (see **FIGURE 2**). As we described in our 2024 Wealth Outlook, regional crises are more common than events that impact the whole world, such as the Pandemic. While investors can choose a home-biased portfolio, our preference is to continue seeking strong risk-adjusted returns globally with the value of diversification in mind.

For now, more than 75% of global equity markets are trading above their 200-day moving average. Broadening of equity performance is occurring beyond the US. Global inflation is falling, and central banks are poised to dial back tight monetary policy. This will mean a stronger world economy in 2025. Forward-looking equity investors should consider that returns may be earned more broadly across the world in such an environment.

Please see the latest Quadrant for more details.

FIGURE 1: Global Equities: US Share of Total Market Cap and US Share of EPS



Source: Bloomberg and FactSet as of March 26, 2024. Indices are unmanaged. An investor cannot invest directly in an index. They are shown for illustrative purposes only and do not represent the performance of any specific investment. Index returns do not include any expenses, fees, or sales charges, which would lower performance. **Past performance is no guarantee of future results**. Real results may vary.

FIGURE 2: The Strongest Performing Asset Class is Rarely the Same Year-After-Year or Decade After Decade

1950s	1960s	1970s	1980s	1990s	2000s	2010s	2020s	Avg Annualized Return	Risk-Adjusted Return
World ex-US Equities 20.8%	US Small Caps 15.5%	EM Govt USD Bond 14.4%	World ex-US Equities 22.8%	US Equities 18.2%	EM Govt USD Bond 12.9%	US Equities 13.6%	US Equities 12.1%	US Small Caps 11.6%	US Equities 0.50
US Equities 19.3%	US Equities 7.8%	US Small Caps 11.5%	US Equities 17.5%	US Small Caps 11.6%	G7 Govt Bond 6.4%	US Small Caps 10.5%	US Small Caps 6.4%	US Equities 11.4%	EM Govt USD Bond 0.41
US Small Caps 16.9%	World ex-US Equities 5.1%	World ex-US Equities 10.1%	US Small Caps 15.8%	G7 Govt Bond 8.0%	US Investment Grade 6.4%	EM Govt USD Bond 6.3%	World ex-US Equities 4.2%	World ex-US Equities 9.9%	World ex-US Equities 0.38
EM Govt USD Bond 5.3%	Cash 4.1%	Cash 6.5%	US Investment Grade 12.8%	US Investment Grade 8.0%	Cash 2.7%	World ex-US Equities 6.0%	Cash 1.8%	EM Govt USD Bond 7.5%	US Small Caps 0.38
Cash 2.0%	EM Govt USD Bond 3.5%	US Investment Grade 6.1%	G7 Govt Bond 12.8%	EM Govt USD Bond 7.7%	US Small Caps 2.2%	US Investment Grade 4.3%	US Investment Grade -0.1%	US Investment Grade 5.4%	US Investment Grade 0.17
G7 Govt Bond 0.4%	US Investment Grade 2.4%	G7 Govt Bond 6.1%	Cash 9.1%	World ex-US Equities 7.3%	World ex-US Equities 1.6%	G7 Govt Bond 3.7%	G7 Govt Bond -0.8%	G7 Govt Bond 5.3%	G7 Govt Bond 0.16
US Investment Grade 0.4%	G7 Govt Bond 2.4%	US Equities 5.8%	EM Govt USD Bond 6.4%	Cash 5.0%	US Equities -0.9%	Cash 0.6%	EM Govt USD Bond -0.8%	Cash 4.1%	

Source: Factset and Global Financial Data as of December 31, 2023. Bloomberg Emerging Markets USD Aggregate Index, Bloomberg Global G7 Index, Bloomberg US Corporate Investment Grade Index, MSCI USA, MSCI World ex US, Russell 2000, and Bloomberg US Treasury Bellweathers (3mo) Index were used as proxy. Indices are unmanaged. An investor cannot invest directly in an index. They are shown for illustrative purposes only and do not represent the performance of any specific investment. Index returns do not include any expenses, fees, or sales charges, which would lower performance. **Past performance is no guarantee of future results**. Real results may vary.

Q2: Is it too late to buy tech?

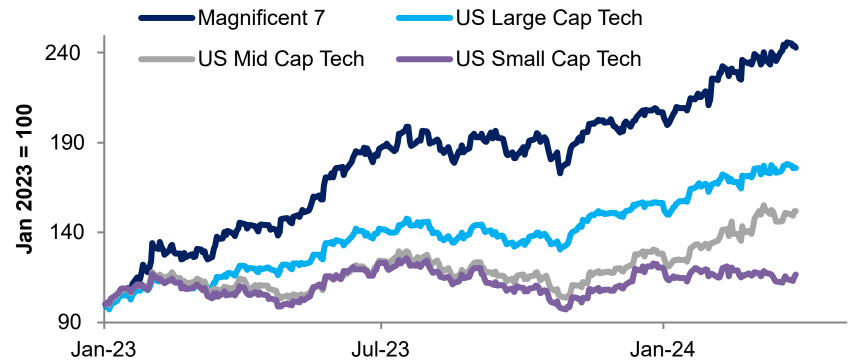
Last year, the "Magnificent 7"[1] propelled the Nasdaq 100 to a 55% return. This year, with the tech momentum trade shifting to AI Infrastructure, the Philadelphia Semiconductor Index (SOX) has surged nearly 17% in 3 months. Many investors are left wondering if it is too late to buy tech.

In a global economy that is increasingly propelled by technological innovation, we believe investors should seek to keep tech exposure in their portfolio. And there is still value to be found in tech on a relative basis. Plenty of tech stocks have lagged the high-flying mega caps since the start of 2023 (**FIGURE 3**). We think investors are beginning to dig deeper to find AI winners among medium and small companies.

The AI boom is also coinciding with a rebound in the "traditional" technology cycle. We see clear signs of a bottoming in demand for basic chips that go into PCs, smartphones, and industrial machinery (**FIGURE 4**). While recent market momentum has favored anything tied to AI, a durable recovery in everyday electronics demand should also be supportive for small and mid-sized tech firms who are vital parts of complex supply chains.

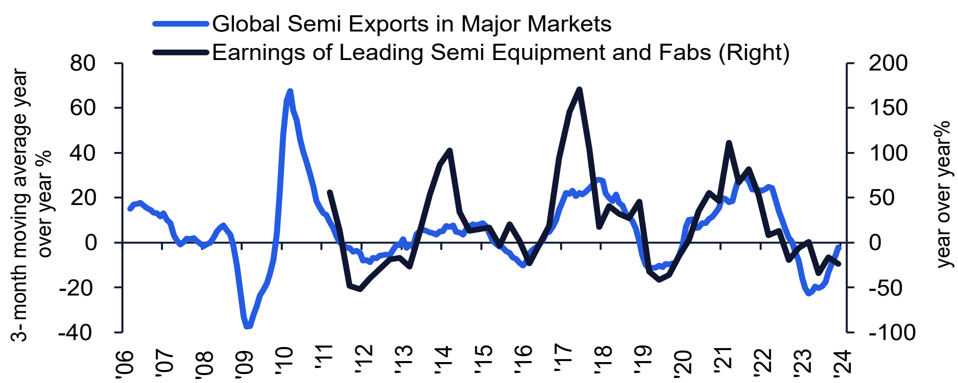
[1] The Magnificent 7 stocks include Amazon.com (AMZN), Apple (AAPL), Google parent Alphabet (GOOGL), Meta Platforms (META), Microsoft (MSFT), Nvidia (NVDA) and Tesla (TSLA). The securities or company names included herein are for illustrative purposes only and do not constitute a recommendation of or solicitation to purchase or sell any security.

FIGURE 3: Mega-cap, Large, Mid and Small Cap Tech since January 2023



Source: Bloomberg as of March 27, 2024. Magnificent 7 index constructed by Bloomberg. Large, Mid and Small Cap Tech correspond to S&P 500, 400, and 600 Technology Indices, respectively. Indices are unmanaged. An investor cannot invest directly in an index. They are shown for illustrative purposes only and do not represent the performance of any specific investment. Index returns do not include any expenses, fees, or sales charges, which would lower performance. **Past performance is no guarantee of future results**. Real results may vary.

FIGURE 4: Korea and Taiwan Chip exports and semi equipment earnings



Source: Haver Analytics as of March 27, 2024. Please note, Semi Exports and Leading Semi Equipment and Fabs is a basket of largest global semiconductor equipment firms, based on MSCI AC World Semiconductor Equipment index. Indices are unmanaged. An investor cannot invest directly in an index. They are shown for illustrative purposes only and do not represent the performance of any specific investment. Index returns do not include any expenses, fees, or sales charges, which would lower performance. **Past performance is no guarantee of future results**. Real results may vary.

Q3: And where is AI likely to boost shares next?

Small and medium-sized tech companies and especially those with an AI focus, present a potential opportunity for buy-and-hold investors. When it comes to AI, we believe investors should focus specifically on three thematic areas:

- **Semiconductor equipment:** While global semiconductor equipment stocks have rallied 29% this year, they have still lagged the world's leading chipmaker by 53%. Leading fabs in Taiwan and equipment players in Europe, Japan, and the US continue to point to full order books out several years.
- **Select software players with strong moats and lots of data:** As AI models get trained and deployed, we will see beneficiaries among leading software names who most effectively integrate AI into their existing products. But selectivity will be key in areas of software like cyber security, fintech, and SaaS where competition is heating up.
- **Robotics and tech hardware:** The key difference between the engines that power chatbots and robots is the input data. AI-powered chatbots digest lots of text while robots analyze data from cameras or sensors. As AI chips become more powerful and available at scale, sellers of industrial robots and automated driving software will soon be able to complete complex, human-like tasks. These advancements have the potential to revolutionize manufacturing and drive a surge in productivity as our commutes suddenly become "work time."

Q4: What does the Fed's new economic forecast mean for markets?

The big news at the Fed's March meeting was that the Fed expects an uninterrupted economic expansion through 2026 as inflation normalizes. And even as the expansion continues, it expects to move the Fed funds rate from todays near 5.4% level to 3.1% over the same time.

At the Federal Open Market Committee (FOMC) press conference, Fed Chair Powell confirmed that economic expansion would not be a barrier to moving monetary policy back from a restrictive stance to a more neutral stance. As we discuss in the latest Quadrant, the Fed is concerned that monetary policy – if maintained at its current stance – will lead to a weaker labor market than is necessary.

The combination of lower policy interest rates, slowing inflation, uninterrupted economic growth and rising corporate profits is as close to an ideal setting for financial markets (see **FIGURE 5**).

As this data and policy became clear, global equity markets rallied without a setback for the past five months. Looking forward, they may still benefit from the mere confirmation of this forecast path but will likely appreciate at a slower pace unless there are further positive surprises.

FIGURE 5: Latest Fed Projections show economic expansion and normalizing inflation

Fed March 2024 Summary of Economic Projections (%)*			
	2024	2025	2026
GDP	2.1	2.0	2.0
*(CGWI GDP Estimate)**	2.0	2.4	
Federal Funds Rate	4.6	3.9	3.1
Inflation (PCE)	2.4	2.2	2.0
Unemployment	4.0	4.1	4.0

Source: Fed, CGWI as of March 27, 2024. Note: Fed funds rate projection is for year-end. All forecasts are expressions of opinion and are subject to change without notice and are not intended to be a guarantee of future events. **Past performance is no guarantee of future results**. Real results may vary. No assurances can be given that the future results indicated, whether expressed or implied, will be achieved. While sometimes presented with numerical specificity, any projections and estimates are based upon a variety of assumptions that may not be realized, and which are highly variable.

Q5: Why is lower inflation so important to a healthy economy?

Inflation, particularly unpredictable inflation, harms confidence in purchasing power. It can cause distortions in consumer behavior which in turn hampers production and investment in the economy.

When inflation is caused by supply shocks, it lowers the non-inflationary "potential" of the economy. Jumps in inflation have very often been the catalyst for recession (see **FIGURE 6**).

Insufficient supply means household incomes will not go as far. Throughout the world, unstable inflation has undermined confidence in government policy. Even with the sharp slowdown in inflation that began in 2022, the increase in consumer prices in 2021-2022 still appears to linger as a factor holding back consumer confidence from a full recovery (see **FIGURE 7)**.

Looking forward, we believe headline inflation measures will fall further over the course of 2024. Confidence in a lasting economic recovery may gain further traction with it. However, it is seeming less likely that the Fed will achieve its 2% inflation target in the coming ten years as it was in the post 2010 decade.

FIGURE 6: US CPI Year over Year % Change and Periods of Recession

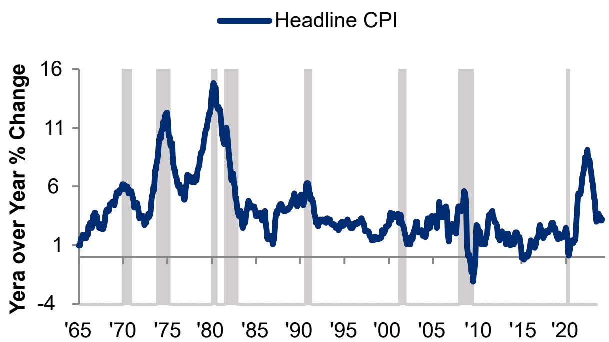
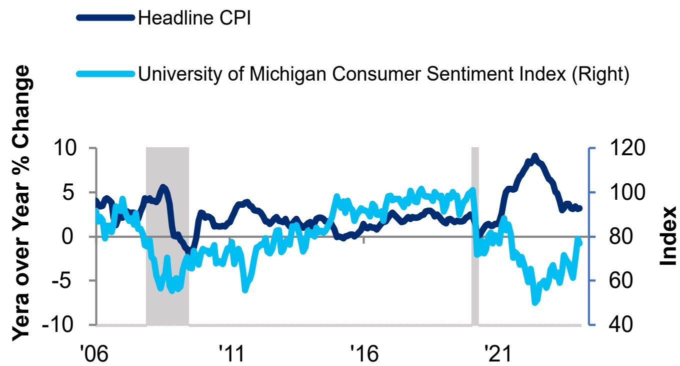


FIGURE 7: US CPI Year over Year % Change and Index of Consumer Sentiment



Source: Haver Analytics as of March 28, 2024. Shaded areas denote recession. Indices are unmanaged. An investor cannot invest directly in an index. They are shown for illustrative purposes only and do not represent the performance of any specific investment. Index returns do not include any expenses, fees, or sales charges, which would lower performance. **Past performance is no guarantee of future results**. Real results may vary.

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High quality (very strong)	Aa	AA	AA
Upper medium grade (Strong)	A	A	A
Medium grade	Baa	BBB	BBB
Not Investment Grade			
Lower medium grade (somewhat speculative)	Ba	BB	BB
Low grade (speculative)	B	B	B
Poor quality (may default)	Caa	CCC	CCC
Most speculative	Ca	CC	CC
No interest being paid or bankruptcy petition filed	C	D	C
In default	C	D	D

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- potential lack of diversification and resulting higher risk due to concentration of trading authority when a single advisor is utilized;
- absence of information regarding valuations and pricing;
- complex tax structures and delays in tax reporting;
- less regulation and higher fees than mutual funds; and
- manager risk.

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