MEKETA
INVESTMENT GROUP

GLOBAL MACROECONOMIC WORKING GROUP

Near-term Market Assessment December 2020

Purpose

This document provides summary observations made by a group of Meketa investment professionals on a monthly basis that are based on a variety of market and economic factors. It is meant to be a high level overview of our aggregated views on current market trends. These views are used in a variety of ways to inform near-term portfolio construction.

Current Market Conditions

As the month of November progressed, markets gained clarity on the US presidential election results and COVID-19 vaccines. The election outcome became increasingly clear by mid-month. At the same time, positive outcomes from vaccine trials for COVID-19 were announced. With these two developments, the market volatility from late October rapidly declined, catalyzing a burst higher across global equity markets, with a rotation away from growth and large cap, which have done well in the pandemic environment, toward value and small cap. While the near-term direction of fiscal policy remains uncertain, market participants clearly view the combination of recent events as positive for risk. Looking forward, the backdrop for equities remains favorable given policy support, the COVID-19 vaccine allowing economies to slowly reopen, and price momentum remaining favorable. However, valuations remain stretched in some cases, so prudent risk taking is merited. Fixed income continues to offer defensive characteristics, but yields remain low and spreads are tight, reducing the appeal of underlying fixed income asset classes on a relative basis.

High Level Views

	Strongly Negative (●)	Negative (●)	Neutral (●)	Positive (●)	Strongly Positive (●)
Rate Sensitive			●		
Credit			●		
Equities				●	
Real Assets			●		

Most Recent Changes

	Strongly Negative (●)	Negative (●)	Neutral (●)	Positive (●)	Strongly Positive (●)
Within Rate Sensitive					
Cash/ST Gov't Bonds			●		
Long-Term Gov't Bonds			●		
TIPS		○	→ ●		
Core Bonds			●		
Within Credit					
EM Debt Local			●		
High Yield Bonds			●		
Within Equities					
US Equity				●	
EAFE Equity			○	→ ●	
EM Equity				●	
Within Real Assets					
REITs			●		
Public Natural Resources			●		
Commodities Futures			●		
Pairs					
Stocks vs. Bonds			○	→ ●	
US Equities vs. Int'l Equities			●		
Short vs. Long Duration			●		
Nominal Bonds vs. TIPS			●		
High Quality vs. High Yield			●		
Risk Assets vs. Cash			●		

→ Indicates change in view from previous month

○ Indicates former position of previous month's view

Asset Class	Rationale Supporting Our Position
Within Rate Sensitive	
Cash/ST Gov't Bonds ●	Economic uncertainty related to the virus and risks related to the roll-out of the vaccine create the potential for increased market volatility making these safe-haven assets attractive, offset by a lower yield offering as a result of Fed rate cuts.
Long-Term Gov't Bonds ●	While long-term government bonds offer a yield pick-up over cash, that pick up is diminished by the Fed's commitment to "lower for longer" interest rates. Furthermore, if rates increase there is the risk of meaningful price declines.
TIPS ●	Inflation expectations have increased but remain below long-term averages, and central banks have largely failed to reach their inflation targets post-GFC. TIPS are also exposed to duration risk (see Long-Term Gov't Bonds). TIPS do provide cheap insurance against an unexpected acceleration in inflation, a potential risk as economic growth likely increases next year and given policy support.
Core Bonds ●	The Fed has pledged unprecedented support for corporate issuers, but a vast increase in corporate leverage and a rapid narrowing of spreads have reduced the risk-reward benefit of core bonds.
Within Credit	
EM Debt Local ●	Trade tensions, de-globalization, and volatility in EM currencies relative to the US dollar creates headwinds for the asset class, but the spread pick-up in EM debt is considerable and continued weakness in the US dollar should benefit local currency bonds.
High Yield Bonds ●	Spreads have narrowed to below long-term averages, but risk continues to be backstopped by the Fed's commitment to provide liquidity at any sign of credit market strain. In this low rate environment the pick-up in relative yield is also attractive, but comes with some risk.
Within Equities	
US Equity ●	We are cautiously optimistic on continued strong performance from US equities, with clarity on both the election and the development of several COVID-19 vaccines. Volatility, which rose in October, has declined, corporate profits have been resilient, and incremental economic data indicates a gradual recovery from the early 2020 collapse.
EAFE Equity ●	The backdrop for global equities is increasingly positive. We view EAFE equities as the most effective way to gain exposure to "value" factors within our three equity categories. The major EAFE economies exhibit more favorable aggregate valuations, tend towards more pro-cyclicality, and have struggled to cope with the COVID-19 pandemic. A recovery in activity, coupled with increasing appetite for "value" factors, should be supportive. Additionally, continued weakness in the US dollar should act as a tailwind for US investors.
EM Equity ●	China's first-in/first-out experience with COVID-19, coupled with aggressive shutdown measures, and fiscal/monetary easing, have left the country in a strong relative economic position; however, continued tensions with the US mean investors should moderate short-term expectations. The emerging market space, ex-China, struggled to cope with the pandemic, leading to weaker relative performance; as risk sentiment improves, countries that have been particularly impacted by the pandemic should benefit from capital inflows. Continued weakness in the US dollar would particularly benefit emerging markets.
Within Real Assets	
REITs ●	Significant impairment from rental losses and an uncertain path of the new normal in key REIT sectors like industrial property weigh on the space, which has lagged the recovery in global equities. However, REIT yields remain attractive, and the possibility of an acceleration in the recovery provides a potential tailwind.
Public Natural Resources ●	Lower demand resulting from COVID-19 restrictions creates temporary headwinds. As the gradual re-opening of economies occurs, the resource demand recovery could surprise positively off a low base, providing a tailwind for the space.
Commodities Futures ●	Supply/demand imbalances have been magnified as a result of COVID-19, with the oil market getting hit particularly hard as a result of both supply and demand shocks in early 2020. The supply side remains uncertain across the commodity complex, but demand should at least gradually recover off a low base from the depths of the 2020 contraction.

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