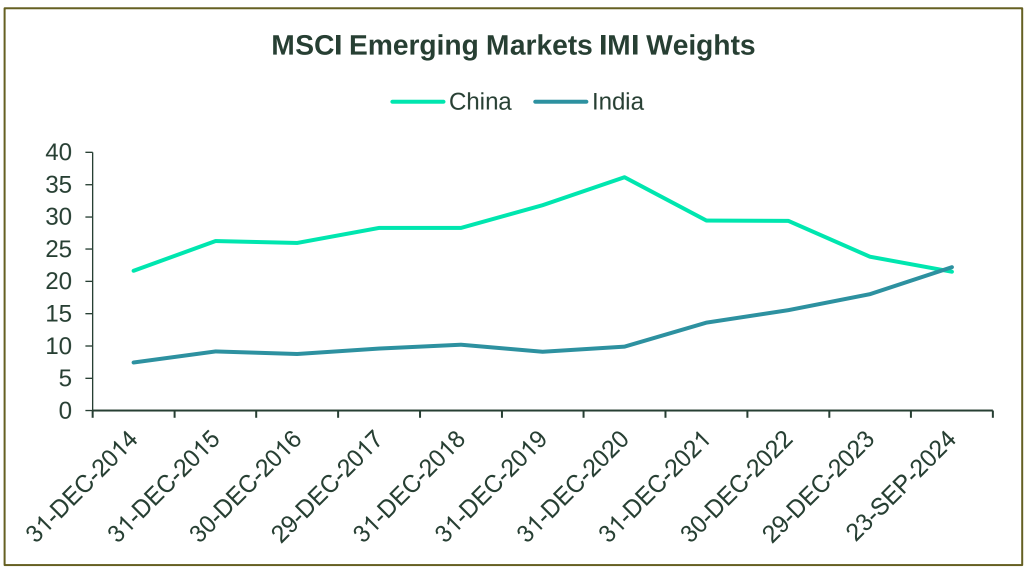
September 26, 2024
Commentary

Weekly Market Update

Insight of the Week

India's Ascent: Overtaking China in Global Markets

Two of the largest emerging markets have taken very different paths, echoing their economic and demographic divergence. For the first time, India just recently overtook China as the largest weight in the MSCI Emerging Markets IMI Index, which is an index composed of small, mid, and large cap companies. While this achievement highlights India's rising prominence and investor confidence, it also points to deeper economic challenges China is currently facing.



Source: MSCI, Factset as of 09/24/2024.

India is the world's fastest-growing major economy and remains on track to overtake Japan and Germany to become the world's third largest economy by 2027[1]. India's nominal GDP growth rate is running in the low teens, more than thrice the economic growth in China, generating a profound divergence in earnings growth.

In contrast, China's reduced weight in the index partly stems from a mix of economic and structural challenges. China's property market (which accounts for nearly 30% of GDP) remains the primary source of volatility as home prices remain unstable. This, paired with frictions with major trading partners and years of abrupt domestic policy changes, has led to more muted economic growth than observed in the past. Consumers have pulled back on spending as retail sales remain weak with consumer confidence near all-time lows. However, last week, China cut

[1] IMF World Economic Outlook, Jan. 2024. Forward-looking estimates may not come to pass.

interest rates and bank reserve requirements in an attempt to support the economy. We don't think these measures alone will be enough to turn around the situation, however the acknowledgement and attempt may improve short term sentiment. The question remains if they will follow through with further support, enough to boost the local consumer.

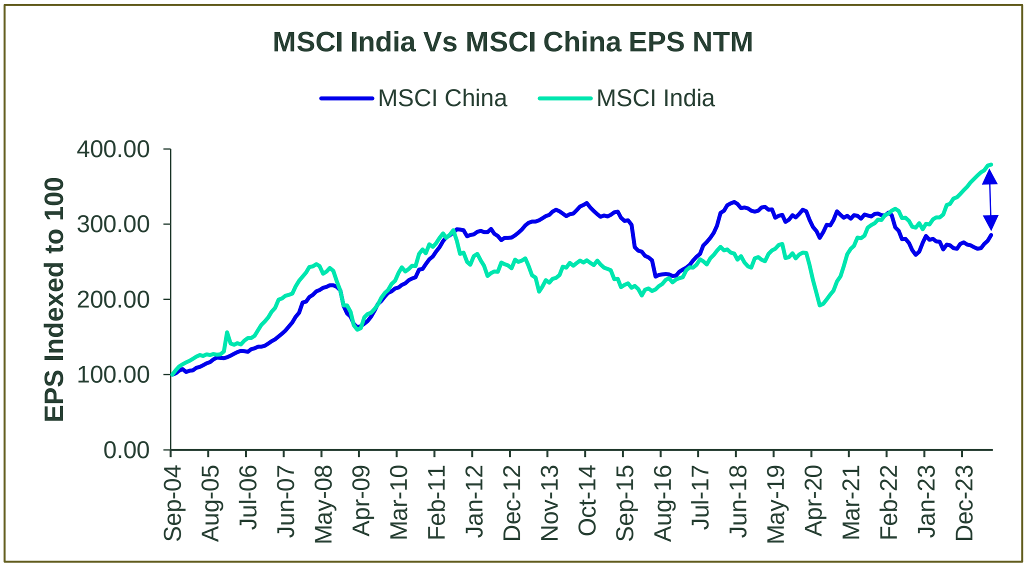
Source: State Street Global Advisors, FactSet.

Equities

India's Resemblance of China

As mentioned in the above Insight of the Week, India's overtaking of China in the MSCI EM IMI Index illustrates how structural differences effects performance. Prior to COVID, investors deployed vast amounts of capital into China, chasing outsized returns due to its impressive economic growth. China was uniquely different from the rest of the emerging markets due to its size and business cycle. Investors embraced China for its potential to deliver outperformance. China now faces several structural challenges in the form of real estate defaults, market downturns and struggling consumer confidence.

As per India, given its large population, size of its economy and increasing geopolitical influence, the outlook resembles that of China from years past. India offers investors strong macro fundamentals and structural advantages that could propel its future success. The divergence in Earnings Per Share between the two countries displays India's growing advantage.



Source: FactSet. Data as of September 26,2024.

India and China have several structural differences that directly impact their future global influence. India doesn't have a history of surprise regulatory intervention. It's organized as a democracy vs China's "People's Democratic Dictatorship". Demographically, India's population is younger and China's median age is 10 years higher – a consequence of its 'one child policy'.

Currently these two countries have many differences, and India's current growth resembles that of China during its best years. Will India ultimate succumb to the same fate? We don't believe so because India is more structurally sustainable.

Source: State Street Global Advisors, FactSet.

Fixed Income

Approaches to Fixed Income Investment Management

Last month, our SSGA fixed income colleagues wrote a paper highlighting the different approaches to investment management within fixed income, and within the various sectors of the fixed income asset class. Their conclusion was that the ultimate choice between active, index, or systematic fixed income investment strategies depends on an investor's return objectives, risk constraints, and fee budget, among other considerations.

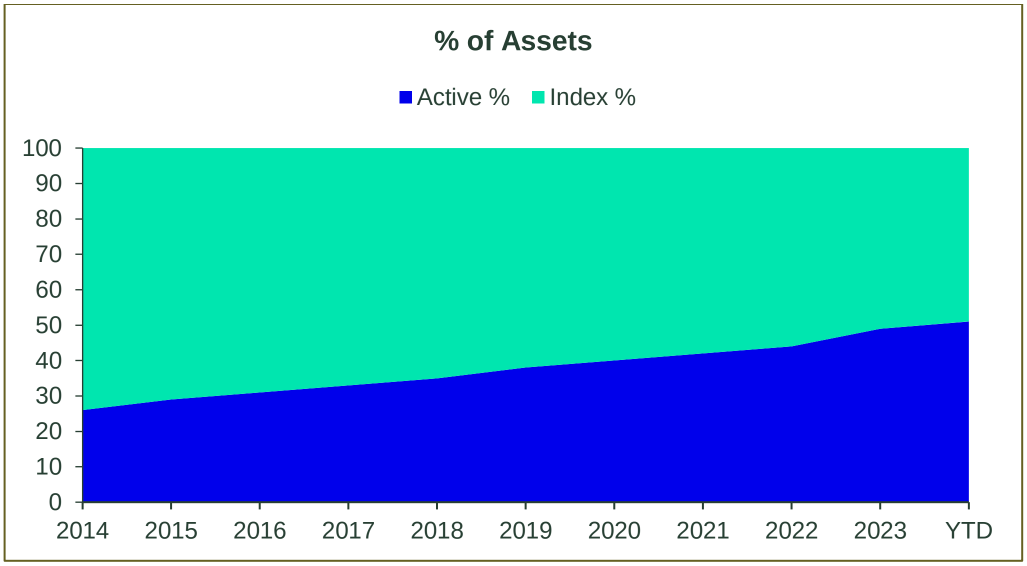
The complete paper titled "The Role of Active, Index and Systematic Investing in Fixed Income Portfolios" can be found on the SSGA website or by visiting:

"https://www.ssga.com/us/en/institutional/insights/active-index-systematic-investing-in-fixed-income"

Active investment management relies on the belief that inefficiencies within markets provide the opportunity to generate excess return on a risk adjusted basis. Active investing in bonds makes sense when managers can identify structural efficiencies, cyclical fluctuations and can turn those into tactical opportunities through asset allocation and security selection. Sectors that can benefit from an active investment approach are the credit and securitized sectors where combination a of a top-down/bottom-up alongside robust fundamental research can produce excess returns.

Index investing, on the other hand, was founded on the belief that markets are efficient and contends that securities always trade at their fair market value and that persistent excess return is impossible over time. Indexing is associated with low costs and low tracking errors. Within fixed income, indexing works best when alpha potential is low, for example in government bonds. Managers can create efficiencies in index investing through processes such as stratified sampling, low turnover, and participation in new issuance.

After a slow launch in the 1970s, indexing began to soar in the decades since. According to Morningstar, the total assets under management in exchange traded funds and notes, along with index managed mutual funds surpassed active assets for the first time in December 2023 (index$13.29 trillion versus active at $13.23 trillion). In addition, index funds have attracted more inflows than active funds for the past nine years.



Source: Source: Morningstar as of March 2024; [Active vs. Passive Funds: Performance, Fund Flows, Fees | Morningstar.]

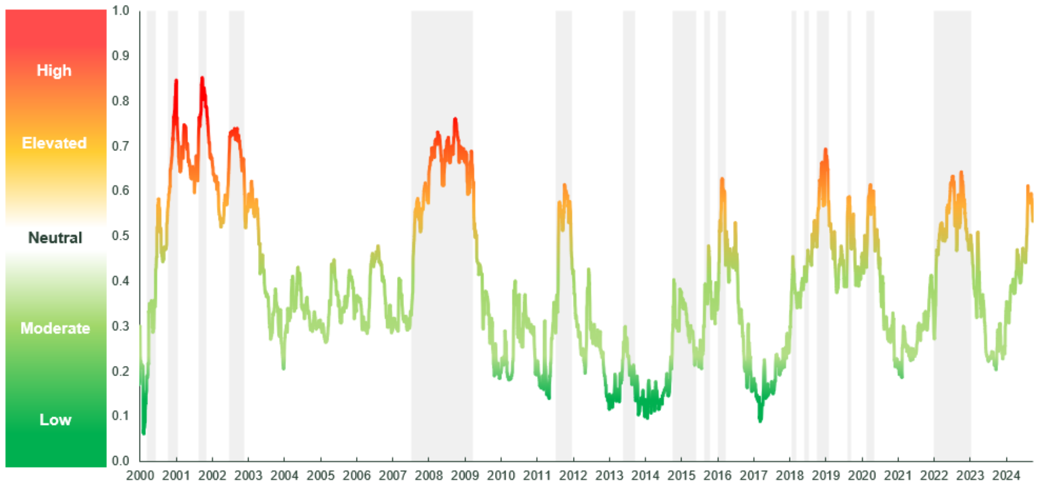
Systematic investing is a relatively new approach that uses data driven models to determine a security's attractiveness in terms of specific factors. Like active investment management, systematic investment management also relies on the belief that inefficiencies in markets can lead to opportunities to generate alpha. However, unlike active investment management, systematic investing relies on a rules based/ model approach that is consistent and repeatable and removes investment manager biases. Systematic investing is possible when there is enough market data/market signal information available across multiple economic cycles and makes sense when managing large portfolios where scalability, efficiency, risk management and cost controls are important.

Ultimately the approach that is suitable for an investor would depend upon their objectives and constraints. Investors need to seek out investment managers that have the skills, expertise, and breadth to cover each approach, as well as a strong understanding of the risk factors that drive alpha between sectors.

Source: State Street Global Advisors, Morningstar.

Market Regime Indicator

The Market Regime Indicator (MRI) represents a proprietary multi-asset class model designed to characterize risk appetites within the capital markets.



Source: State Street Global Advisors, Investment Solutions Group (ISG). As of September 25, 2024. The data displayed is not indicative of the past or future performance of any SSGA product. The above data represents a back-test of the MRI model, which means that those results were achieved by means of the retroactive application of the model which was developed with the benefit of hindsight. Data displayed beyond this date is not backtested, but is still generated by the model referenced. All data shown above does not represent the results of actual trading, and in fact, actual results could differ substantially, and there is the potential for loss as well as profit. The Market Regime Indicator (MRI) is a quantitative framework that attempts to identify the current market risk environment based on forward-looking market indicators. We believe the factors used are good indicators of the current risk environment as they are responsive to real-time market impacts and in theory should include all current and forward views of those markets. These factors are combined to create a single measure and used to identify one of four risk regimes: Low Risk, Moderate, Normal, Elevated and High Risk..

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*Pensions & Investments Research Center, as of 12/31/23.
†This figure is presented as of June 30, 2024 and includes ETF AUM of $1,393.92 billion USD of which approximately $69.35 billion USD is in gold assets with respect to SPDR products for which State Street Global Advisors Funds Distributors, LLC (SSGA FD) acts solely as the marketing agent. SSGA FD and State Street Global Advisors are affiliated. Please note all AUM is unaudited.

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Equity securities may fluctuate in value and can decline significantly in response to the activities of individual companies and general market and economic conditions.

Bonds generally present less short-term risk and volatility than stocks, but contain interest rate risk (as interest rates raise, bond prices usually fall); issuer default risk; issuer credit risk; liquidity risk; and inflation risk. These effects are usually pronounced for longer-term securities. Any fixed income security sold or redeemed prior to maturity may be subject to a substantial gain or loss.

Currency Risk is a form of risk that arises from the change in price of one currency against another. Whenever investors or companies have assets or business operations across national borders, they face currency risk if their positions are not hedged.

Generally, among asset classes, stocks are more volatile than bonds or short-term instruments. Government bonds and corporate bonds generally have more moderate short-term price fluctuations than stocks, but provide lower potential long-term returns. U.S. Treasury Bills maintain a stable value if held to maturity, but returns are generally only slightly above the inflation rate.

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Exp. Date: 3/31/2025