Q1Commentary & Outlook – March 2024

Key Takeaways

- ***Equities:*** ***We remain overweight quality stocks as defined by solid balance sheets, with lower-than-average debt and higher-than-average operating cash flow. We also believe that tail risk has increased for risker equity assets due to constrained profit margins moving forward and elevated geopolitical uncertainty. We continue emphasizing risk management via momentum overlays for our riskiest positions.***
- ***Bonds:*** ***Bond exposure remains centered on high-quality credits with lower than market average duration. While the U.S. economy grows slightly slower, interest rates remain elevated, and inflation is stubbornly constant. This has delayed any near-term shift in Fed policy.***
- ***Alternatives:*** ***The stock and bond market is currently in a regime of positive correlation. With returns for both asset classes moving lower, the challenge continues to focus on the search for non-correlated independent sources of positive return. Global tensions in Europe and the Middle East coupled with uncertainty across the globe with respect to democratic elections only feeds higher uncertainty. We believe in this environment hedged strategies, gold and opportunistic commodities will provide the added diversification investors are searching for.***

Markets Review and Outlook:

Equities:

- Global equities were off to a strong start during the 1st quarter of 2024, a repeat of a stellar performance in 2023. The dominant attribute contributing to this momentum into the new year was the Magnificent 7, even though there were clear signs of dispersion within this Mega cap group. For Q1, the S&P 500 was up over 10%, with the Mag 7 up 13% and the S&P ex the Mag 7 up only 6%. This vs. the Mag 7 up 76% during 2023, the S&P 500 up 24%, and the S&P 500 ex Mag 7 up only 8%!
- Despite the Mega Cap dominance (the top ten stocks now account for 33.5% of the S&P 500, the highest level since the Depression), a slowdown in earnings growth and high valuations show some signs of stress. The top stocks' peak earning contribution of 34% of the market during late 2022 has slowed to just over 25% of the market.
- Market leadership was still concentrated on momentum and growth stocks (Technology and Communication Services). Still, a reversal of this trend was evident during the month of March with Energy and Value taking the lead.

Bonds:

- The total bond market declined during the quarter as Central Bank policymakers delayed a shift in policy toward rate cuts. Inflation news came in higher than expected, and the U.S. labor markets continued to remain strong.
- Lower-quality credits (high-yield bonds and leveraged loans provided positive results during the quarter as investors raced to lock in higher yields.

Alternatives:

- Commodities strengthened during the quarter as oil prices and precious metals rose. Increasing geopolitical risk combined with high oil demand contributed to the gains.
- Gold moved higher as a general risk hedge as investors increased their concerns over the direction of the global economy and increased conflicts overseas. Central banks have also continued to increase gold gains with continued purchases of gold reserves.

Market Performance

Bullish	Favorable	Neutral	Cautious	Bearish

`	March	YTD	1 Year	Current View
U.S. Large Cap	3.22	10.56	29.88	Cautious
U.S. Mid Cap	5.60	9.95	23.33	Favorable
U.S. Small Cap	3.24	2.46	15.93	Neutral
U.S Momentum	4.16	22.55	49.04	Cautious
U.S Growth	2.13	12.75	33.73	Cautious
U.S.Multi Factor	4.04	10.21	25.18	Neutral
U.S. High Beta	4.32	6.92	26.93	Cautious
U.S. Quality	3.72	12.23	29.73	Favorable
U.S. Buyback	5.06	10.19	25.66	Cautious
U.S. Equal Weight	4.46	7.91	19.38	Favorable
U.S. Value	4.55	8.05	25.58	Neutral
U.S. Dividend Aristocrats	4.72	7.09	14.07	Neutral
U.S. Low Volatility	3.09	5.84	8.49	Neutral
U.S. Low Volatility High Di	5.12	5.79	10.52	Neutral
U.S. Select Dividend	6.62	6.10	9.73	Neutral
International Developed	3.29	5.78	15.32	Neutral
Emerging Markets Equity	2.48	2.37	8.15	Neutral
Fixed Income				
U.S. Total Bond	**0.92**	**-0.78**	**1.70**	Neutral
U.S. Government	0.64	-0.93	0.13	Neutral
U.S. Corporate	1.23	-0.41	4.15	Neutral
U.S. High Yield	1.18	1.47	11.15	Cautious
U.S.Leveraged Loans	0.83	2.52	12.40	Cautious
Non-U.S. Developed	0.21	-4.30	-2.01	Cautious
Alternatives				
REITs	2.06	-0.20	10.54	Cautious
Commodities	4.20	4.92	4.29	Favorable
Managed Futures	0.48	0.89	-1.07	Neutral
Hedge Funds	2.06	3.50	8.57	Favorable

Source: Morningstar, data as of 03/31/2024

Risk Examination – March 2024

A quarterly update on our views of the complex risk factors in global markets

Valuation	Earnings	Macro	Liabilities	Technical

Key

Bullish	Favorable	Neutral	Cautious	Bearish

Valuation

- U.S. equity valuations remain elevated, and markets are concentrated. While valuation is not a short-term indicator of the market direction, it generally has a good long-term record of setting return expectations over the next decade. By most measures of valuation, ranging from forecasts of P/E to Price/Cash Flow, markets are trading at a premium to their long-term average.

Earnings

- Positive earnings momentum will be difficult to maintain in an environment where signs of an economic slowdown are evident. Consumer demand is feeling the pressure of higher inflation and the higher cost of servicing debt, especially credit card debt.

Macroeconomic

- The market has struggled with expectations of future economic growth. Many had forecast a recession in 2023, but it never arrived. Now the consensus expectation is for a soft landing. We still believe that the odds favor lower real growth and elevated inflation rates (stagflation).

Fundamental, Economic & Geopolitical Risks

- Our view is that balance sheet risk has risen due to higher debt ratios and elevated interest rates. The number of zombie companies (insufficient operating cash flow to service existing debt) is rising along with credit default risk, especially the lower-end spectrum of high-yield debt. Economic risks include slower growth, rising debt costs, and sticky inflation. Uncertainty is elevated due to politics both at home (election year) and abroad (Israel/Hamas war, Russia/Ukraine war, China, etc.).

Technical/Sentiment

- The uncertainty from the effects of the crisis in Ukraine and its broader geopolitical impact (i.e., the new Axis of Evil: Russia, China, and Iran), elevated inflation rates, and lower economic growth ahead will most likely continue to feed higher volatility in the public markets.
- Consumer households are starting to feel the headwinds of constraints on consumption that should lead to lower growth.

2024-2025 Economic and Investment Scenarios

Our assessment of potential macro scenarios

	Recession	**K – Shaped Recovery**	**Return to New Normal**	**Robust Recovery**
Economy / Geopolitical	▪ Negative growth precipitated by elevated interest rates, inflation, lower growth ▪ Civil unrest, election outcome ▪ Demand slowdown	▪ Weakness in consumer discretionary ▪ Strength in E-commerce/innovation ▪ Fed focus on 2% inflation & no room for fiscal stimulus	▪ Gradual recovery with radically different labor market ▪ Inward focus ▪ Steady growth/low inflation	▪ Inflation reverts to Fed target ▪ Job growth/higher consumption ▪ Infrastructure spend
Markets	▪ Prolonged sell-off in risky assets ▪ Rush to safe-haven assets such as the U.S. dollar, gold and cash	▪ Negative effect of elevated inflation ▪ Volatility dominates ▪ Highly valued & concentrated markets ▪ Focus on risk	▪ Extended recovery puts focus on value, small cap & higher inflation ▪ Pressure on Big Tech	▪ Negative real rates, a flood of new money = continued asset inflation ▪ Alternative assets & equities prosper
Focus	▪ Flight to quality: Short duration U.S. Treasuries, U.S. Dollar, & Gold benefit	▪ Premium on asset diversification = liquid alts ▪ Commodities & non-directional investments	▪ Focus shifts from sentiment driven markets to fundamentals	▪ Fully invested, but highly diversified
Probability	**40%**	**30%**	**20%**	**10%**

< < < Downside < < < | **> > > Upside > > >**

Risks

Downside	Upside
Geopolitical risk of a misstep with Russia, China, Iran	Effective use of fiscal stimulus spurs economic growth
Sustained high-interest rates and higher energy prices	Globalization returns
Runaway debt growth on pace to equal Japan	A shift in focus and higher productivity
Higher rates of poverty and social displacement	Strong real economic growth and productive use of credit
Higher unemployment – weaker demand	Raises the wealth effect across multiple sectors
	Lower rates of inflation, above-trend real growth

Portfolio Asset Class Positioning

PORTFOLIO SEGMENT / SEGMENT OBJECTIVE	SEGMENT CONSTITUENTS	SEGMENT COMMENTS
Equity *Diversified risk factor exposure with an emphasis on quality, value, & innovation*	▪ Global exposure to high-quality companies and innovators in their field ▪ Diversified across size and high quality in both US and non-US markets. Exposure to a risk-managed approach to holding leading-edge innovation across sectors	▪ Systematic exposure in U.S. equity to an equal-weighted market index, & high-quality stocks with low debt ratios across global markets ▪ Diversified non-US exposure to high-quality and small-cap developed market stocks ▪ Continued emphasis on actively managed beta exposures
Fixed Income *Seek to Preserve Capital, and Diversify Equity Exposure*	▪ Emphasis on short to intermediate duration & and high credit quality issues ▪ Reduction in credit risk (ABS & senior bank loans) ▪ Not a time to "reach for yield"	▪ Reduction in cash exposure to high-quality credit (short-intermediate term duration) ▪ Favor high-quality credit over duration ▪ Issuer selection critical for active management
Opportunistic *Highest Conviction Ideas Based on 12-24 Month Proprietary Forecasts*	▪ Slight overweight in the energy sector ▪ Focus on risk management via our dynamic innovation overlay process to lessen the risk of large drawdowns ▪ Small-cap international equity developed markets	▪ Reflects our short-term model (value and momentum) ▪ Seeking participation in select themes with attractive return potential based on innovative technologies such as 3D printing, gene therapies, digital wallets, renewable energy, and AI ▪ Innovation: monthly rebalance of risk (high beta and risk-off low beta) based on momentum
Alternative *Anticipated Risk Mitigation with Alpha Opportunities*	▪ Opportunistic Commodities ▪ Hedged equity ▪ Global macro–credit ▪ Carbon credits ▪ Systematic L/S managed futures ▪ Gold	▪ Lower than average return and higher risk expectations for equities and bonds present the challenge of providing uncorrelated sources of risk and return. ▪ We favor exposure to risk-managed approaches to investing in liquid alternatives with an emphasis on actively managed long/short commodities, carbon credits, hedged equity, gold & managed futures

For additional information, please refer to the Disclosures at the end of this report.

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~~markets.~~ ***Past performance is not a guarantee of future results.*** All investments are subject to risk, including the loss of principal. Portfolio positions referenced are subject to change at any time, your portfolio may not reflect the information referenced.

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Index definitions:

“U.S. Large Cap” represented by the S&P 500 Index.
“U.S. Small Cap” represented by the Russell 2000 Index.
“International” represented by the MSCI Europe, Australasia, Far East (EAFE) Net Return Index.
“Emerging” represented by the MSCI Emerging Markets Net Return Index.
“U.S. Aggregate” represented by the Bloomberg U.S. Aggregate Bond Index.
“U.S. Government” represented by the Bloomberg U.S. Government Bond Index.
“U.S. Corporate” represented by the Bloomberg U.S. Credit Bond Index.
“U.S. High Yield” represented by the Bloomberg U.S. Corporate High Yield Index.
“Non-U.S. Developed” represented by the S&P International Treasury ex U.S. Index.
“Emerging Market Debt” represented by the JP Morgan GBI-EM Global Core Index
“REITs” represented by the FTSE North American Real Estate Investment Trust (REIT) Equity REITs Index.
“Commodities” represented by the Dow Jones Commodity Index .
“Managed Futures” represented by the Credit Suisse Managed Futures Index.
“Global Macro” represented by the Credit Suisse Global Macro Index

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