Q2Commentary & Outlook – June 2024

Key Takeaways

- ***Equities:*** ***The equity markets in the US continue to be fixated on the "AI association", especially Nvidia. Newer market participants also may not realize or forget that there have been several times when leading innovations have captured the allure of the population and resulted in a concentrated stock market. Most of the time, markets are diversified, meaning the current state cannot last long. We remain diversified across global markets and defensive at this stage of the market cycle.***
- ***Bonds:*** ***We also believe there are fewer macro-opportunities in bond markets, but increasingly, opportunities for active fixed income. We currently are minimizing duration and credit risk with a much shorter than Aggregate Bond Index duration with a bias to higher quality. We also have a portion of the bond portfolio allocated to short-term TIPs.***
- ***Alternatives:*** ***We continue to witness a positive correlation between the stock and bond markets. Political and geopolitical uncertainty coupled with a bear market in equity market diversification also points us to lower correlated asset classes with the potential for positive inflation-adjusted returns, hence continued exposure to long-short managed futures (ex equities), opportunistic commodities, and gold.***

Markets Review and Outlook:

Equities:

- The 3rd quarter, marked a quick reversal back to performance dominance of what is now the Mag 5. This group dominates the US large-cap growth indexes, up 9.57% during the quarter. The market also continues to reward "quality" stocks as defined by the quality factor and punish small-cap and large cap dividend-paying stocks.
- Overseas developed equity markets lagged due to a strong US dollar and lower growth expectations. The emerging markets, where many of the currencies are tied to the US dollar and low valuations, attracted new capital.
- Economic growth indicators show that the US economy is slowing at the same time US earnings expectations are expected growth 9% on year over year basis next. This optimistic forecast, combined with high valuations, suggests that we are nearing a peak in the market.

Bonds:

- Bond markets held steady during the quarter as interest rates held steady. Leveraged loans and high yield bonds remained in a leadership position, despite narrow spreads and increased default risk.
- High interest rates remain, as the Fed waits for further evidence of slowdown in the economy, specifically in the labor markets. However, recent news in the job markets of slight lower wage growth was indication that the Fed may soon reverse its monetary policy.

Alternatives:

- Many liquid alternative assets were either flat or slightly negative for the quarter, mainly due to the lack of any short-term trending (most commodity and managed futures strategies employ momentum as the primary driver of the process.
- We still embrace active credit, hedged equity, long-short managed futures, gold, and opportunistic commodity strategies, as well as gold. We believe that the diversification and non-correlated benefits are still present and non-

Market Performance

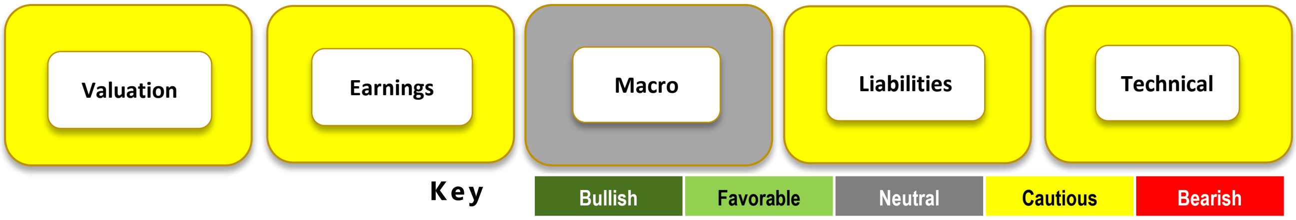
Bullish | Favorable | Neutral | Cautious | Bearish

`	June	Recent Qtr	YTD	1 Year	Current View
U.S. Large Cap	3.57	4.25	15.21	24.39	Cautious
U.S. Mid Cap	-1.59	-3.48	6.01	13.22	Favorable
U.S. Small Cap	-2.28	-3.10	-0.72	8.66	Cautious
U.S Momentum	4.57	4.02	24.40	36.01	Cautious
U.S Growth	6.97	9.57	23.51	32.45	Cautious
U.S.Multi Factor	-1.49	-2.92	7.48	19.94	Neutral
U.S. High Beta	1.75	-3.57	3.06	11.62	Cautious
U.S. Quality	3.17	4.08	16.38	27.99	Favorable
U.S. Buyback	-0.54	-3.83	5.39	17.42	Cautious
U.S. Equal Weight	-0.07	-2.71	5.27	13.86	Neutral
U.S. Value	-0.66	-2.11	5.75	15.22	Neutral
U.S. Dividend Aristocrats	-1.41	-4.66	2.00	4.31	Neutral
U.S. Low Volatility	-0.19	-0.88	4.85	5.95	Neutral
U.S. Low Volatility High Div	-1.16	0.97	6.74	12.32	Neutral
U.S. Select Dividend	-2.06	-1.11	4.83	11.00	Neutral
International Developed	-2.33	-0.48	4.83	10.81	Neutral
Emerging Markets Equity	2.23	5.30	7.33	11.95	Neutral
Fixed Income					
U.S. Total Bond	**0.93**	**0.13**	**-0.62**	**2.61**	Neutral
U.S. Government	0.99	0.17	-0.72	1.51	Neutral
U.S. Corporate	0.60	-0.53	-1.29	3.74	Neutral
U.S. High Yield	0.95	1.03	2.18	9.69	Cautious
U.S.Leveraged Loans	0.26	1.85	3.61	9.44	Cautious
Non-U.S. Developed	0.61	-0.60	-0.51	4.43	Cautious
Alternatives					
REITs	1.97	-1.89	-3.06	4.73	Cautious
Commodities	1.32	0.40	10.50	13.83	Favorable
Managed Futures	-1.42	-2.58	1.32	-4.33	Favorable
Hedge Funds	-0.08	0.13	2.13	5.24	Favorable

Source: Morningstar, data as of 06/30/2024

Risk Examination – June 2024

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



Valuation

- U.S. equity valuations that dominated the concentrated indexes are overvalued. Pockets of equity exposure remain attractive on a relative basis but may lack the catalyst to justify an immediate investment. Value, small, and midcap stocks are a case in point. However, many companies in the large-cap value universe (which have some overlap with quality stocks) are beginning to look attractive.

Earnings

- We believe earnings expectations are too optimistic, priced for perfection, and poised for disappointment. For example, market leader Nividia trades at a P/E multiple of 41x expected earnings, up from 24x expected earnings in January.

Macroeconomic

- There are several signs of economic slowdown in the US economy evidenced by weakness in the household and private services sector. Rising credit card debt, lower retail sales, and a slump in the new residential housing markets are just a few of the indicators pointing to lower real economic growth. Real time economic growth forecasts from the Atlanta's Fed GDP Now are at 1.5%.

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, the Middle East, 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%**

Risks

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

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 ▪ Continued exposure to emerging market equities with a cutback in smaller cap non-US equity markets. ▪ Entry point into US large-cap value stocks as we migrate into the next phase of the business cycle.	▪ 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 in developed markets and passive and active exposure to emerging 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" ▪ New emphasis on short-term TIPs	▪ 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 ▪ Continued exposure to selective innovation themes	▪ 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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Index definitions:

"U.S. Large Cap" represented by the S&P 500 Index.
"U.S. Small Cap" represented by the Russell 2000 Index.
"International" is 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" is 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" are 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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