Tactical Asset Allocation

This report reflects the current opinions of the Sendero Investment Committee on various asset classes used or considered for client portfolios versus their strategic allocation. The comments reflect opinions as of the specific date listed and can change quickly based on market conditions.

As of September, 2022

SENDERO®

Navigating wealth *beyond* investments

STABILITY

ASSET CLASS	OVERWEIGHT	NEUTRAL	UNDERWEIGHT
CASH	○		
TIPS	○		
FIXED INCOME			○

GROWTH

ASSET CLASS	OVERWEIGHT	NEUTRAL	UNDERWEIGHT
U. S. EQUITIES		○	
DEVELOPED MARKETS			○
EMERGING MARKETS			○

DIVERSIFIER

ASSET CLASS	OVERWEIGHT	NEUTRAL	UNDERWEIGHT
HEDGE FUNDS	○		
COMMODITIES & CRYPTOCURRENCIES		○	
REAL ESTATE	○		
CREDIT L/S	○		

Market Highlights

- Investors have experienced an extraordinary 2022, including the worst performance year on record so far for a combined stock and bond portfolio going back to the 1970s, the sharpest interest rate hiking cycle in 50 years, the strongest increase in the U.S. dollar, and 40-year-high inflation.
- Going forward, the sharp hawkish shift in interest rate policy in recent months has amplified global growth risks and contributed to rising stresses in global financial markets. The Federal Reserve will need to be increasingly alert to signs of further financial stress and the potential stronger economic fallout.

CASH OVERWEIGHT

We believe cash should be held to take advantage of market volatility and for near-term liquidity needs.

TIPS OVERWEIGHT

Base effects, supply-chain disruptions, and fiscal stimulus have combined to push inflation higher globally. Upside risks may persist into 2023, especially from stubborn food and energy prices. We are also watching wage growth and productivity for structural changes in inflation expectations going forward. We prefer short-term duration exposure given break-even rates.

FIXED INCOME UNDERWEIGHT

The case for for higher yields continues as the Fed is still getting out from behind the inflation curve, and the market currently expects the Fed to hike rates by another 100 bps in the next 12 months. Quantitative tightening also started this month, at a much faster pace than last time. Conversely, a potential downshift in economic activity from higher commodity prices and a pick up in unemployment potentially make the case for lower yields in the second half of 2023. Municipal bond valuations have normalized from earlier this year and we continue to prefer low/intermediate duration and higher quality munis.

U.S. EQUITIES NEUTRAL

While the Value factor remains attractive relative to Growth, we are inclined to focus on balance sheet quality and secular growth themes. Even with stock valuations becoming more attractive, earnings growth and corporate margins could be revised down further. As such, we expect volatility to stay high for the remainder of 2022 and 2023 as financial conditions tighten some more. Active concentrated managers should be rewarded for stock selection in such an environment. We maintain an overweight to small-cap equities, given their cyclical nature and correlation to interest rates and inflation.

DEVELOPED MARKETS UNDERWEIGHT

Despite attractive below-average valuations, we have a lower allocation given the regional impact of the ongoing war in Ukraine, headwinds to economic growth and corporate profits from higher energy prices, and elevated inflation and a more hawkish ECB. We prefer active exposure within international managers to navigate a challenging environment going into 2023.

EMERGING MARKETS UNDERWEIGHT

While EM equities trade at a discount to global markets, the financial and commodity repercussions from the war in Ukraine have the potential to create another wave of political instability in Emerging and Frontier economies. Along with our longstanding deglobalization theme, we see further challenges stemming from slower economic growth in China and rising U.S. interest rates potentially impacting EM credit.

HEDGE FUNDS OVERWEIGHT

We favor equity long/short strategies for differentiated sources of return due to anticipated equity dispersion and increased volatility. Global macro and managed futures strategies, currently seeing a wide opportunity set, may help investors seeking to diversify equity and fixed income allocations.

COMMODITIES & CRYPTOCURRENCY NEUTRAL

Persistent supply chain disruptions, elevated geopolitical risk and rising commodity prices from oil to corn and wheat all appear to have staying power. Commodity allocations have the potential to perform well versus stocks and bonds when the labor market is tight and inflation is high. Global economic growth and a decade of underinvestment should also continue to support demand for commodities longer term. Research on crypto strategies continues, given the opportunities in blockchain, but regulatory risks remain.

REAL ESTATE OVERWEIGHT

The pandemic has accelerated already-present underlying real estate trends. We continue to place emphasis on direct investments in properties located in strong regions that exhibit attractive rent-roll and cash-flow characteristics. This allocation continues to provide some income as well as a long-term hedge against rising inflation.

CREDIT OVERWEIGHT

We expect default rates to rise and recoveries to suffer in the coming years, which should create a favorable environment for dislocations/opportunities for active long/short managers.

Note: Positioning versus Strategic allocation.

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