SENDERO®
Navigating wealth
beyond investments

Asset Allocation Viewpoints

as of May 2023

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.

	Asset Class	Positioning
Stability	Cash	Overweight (green)
	TIPS	Overweight (green)
	Fixed Income	Underweight (brown)
Growth	U.S. Equities	Neutral (yellow)
	Developed Markets	Underweight (brown)
	Emerging Markets	Underweight (brown)
Diversifier	Market Neutral | Managed Futures | Hedged Equities	Overweight (green)
	Commodities |Cryptocurrencies	Neutral (yellow)
	Real Estate	Neutral (yellow)
	Credit L/S	Overweight (green)

Overweight Neutral Underweight

Stability

Cash

We believe cash should be held to take advantage of market volatility and for near-term liquidity needs. The ability to now earn a positive substantial yield on cash is a welcome option after years of financial repression.

TIPS

While headline inflation readings have downshifted since September, core PCE is still more than double the Fed's 2% goal. Core services inflation excluding shelter has moved sideways for the last few months and some measures of underlying inflation are still trending up in a concerning manner. Short and long-term breakeven levels look attractive given where real yields are.

Fixed Income

Recently, banking sector stress has severely affected the credit market landscape. Banking issues will only further tighten lending conditions. Leading economic indicators remain weak, money supply growth is still negative, and yield curves remain inverted. With rates lower on this risk-off environment, we are currently neutral duration versus a stated benchmark but will continue to look for prudent opportunities to potentially extend duration in the future. Fixed Income should do a better job of diversifying multiasset class portfolios from this point forward, since higher yields offer not only higher income but also can potentially move down substantially if an economic downturn occurs. Bond valuations have normalized from last year and we continue to prefer higher quality munis as well as investment-grade credit.

Growth

U.S. Equities

While the value factor remains attractive relative to growth, we are inclined to focus on balance sheet quality and secular growth themes. Near-term risks for Equities come from a potential global slowdown in growth and profits, persistently elevated levels of inflation, the U.S. debt ceiling, and tightening credit conditions. 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. We continue to believe that market volatility will be elevated for most asset classes and expect the "grind-it-out" environment to persist for markets in the near term before stabilizing later this year. On the other hand, investor sentiment remains mostly bearish, a positive contrarian indicator.

Developed Markets

Despite attractive valuations, we have a lower allocation given the regional impact of the ongoing war in Ukraine, headwinds to economic growth and corporate profits, greater economic exposure to any potential broadening in banking sector stress, upward pressures on core inflation, and a hawkish European Central Bank (ECB). We prefer active exposure within international managers to navigate a challenging environment in 2023.

Emerging Markets

EM Equities appear attractively valued but remain vulnerable to high and still rising global interest rates, a still relatively strong U.S. dollar and any potential broadening in banking sector stress. We continue to expect a wide return dispersion between individual countries and regions. 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.

Diversifier

Market Neutral | Managed Futures | Hedged Equities

Despite a tepid start to the year, we see opportunities for Hedge Funds amid an uncertain market environment. We favor equity long/short strategies for differentiated sources of return due to anticipated equity dispersion and increased volatility. Higher interest rates and slowing global growth will likely result in declining corporate earnings, creating potential shorting candidates. Global macro and managed futures strategies may help investors seeking to diversify equity and fixed income allocations.

Commodities | Cryptocurrencies

Even with the potential for a recession this year, positive fundamentals remain in place and a moderate allocation to commodities could be additive from a return and a diversification perspective. Commodities tend to do well in periods of elevated geopolitical risk and inflation, both of which seem to be currently available in abundance. Global economic growth and a decade of underinvestment should also continue to support demand for commodities longer term. 2022 was probably the biggest year of upheaval in crypto history. Yet, research on crypto strategies continues, given the opportunities in blockchain and decentralized finance. Regulatory risks remain on the back of the headline FTX bankruptcy.

Real Estate

High interest rates, the potential for a recession later this year, concerns over lending growth due to the failures of several regional banks, and the impact to commercial real estate, we prefer a neutral allocation. We continue to place emphasis on direct investments in quality 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 during periods of inflation.

Credit L/S

Current corporate default rates remain low, but this may be changing: Forecasts for defaults in 2023 have now climbed to around 2.3% for HY compared to long-term averages of 3.2%. 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.

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