ENVESTNET PMC

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STRATEGAS insight

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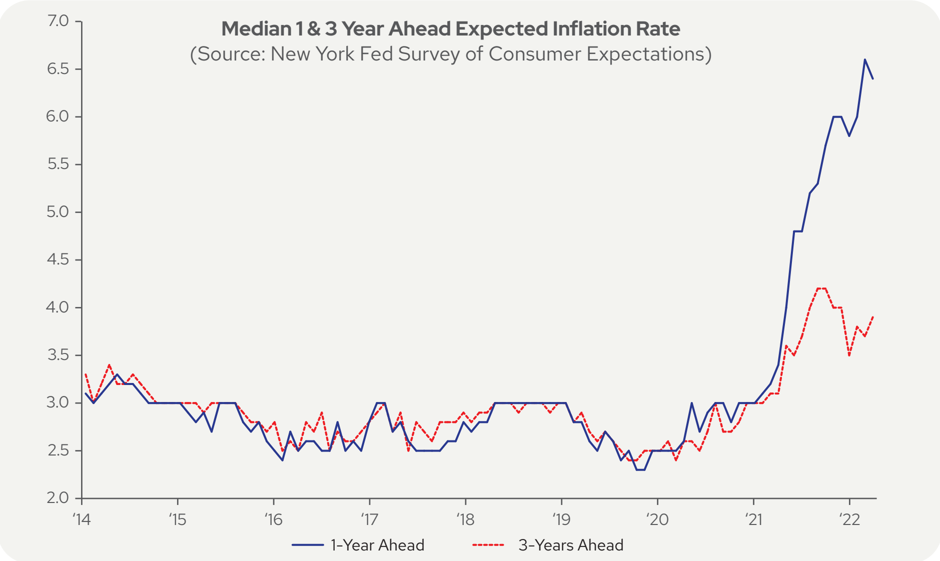
More to Come

The consensus continues to assign higher odds to a "soft landing" than to other economic outcomes—notably, recession—and equity positioning, though lower relative to total portfolio, still reflects this bias through a modest preference for growth shares. Interesting if one considers the environment…

April inflation readings surpassed expectations, and though "peak inflation" is more of a mathematical construct, prices are still expected to remain elevated. China's local lockdowns in pursuit of its "Zero COVID" policy is causing further disruption in the global supply chain. Europe appears to be heading for an economic downturn—if it is not in one already—given Russia's invasion of Ukraine and related sanctions. Global rates have continued their push higher, weighing on equities, and the U.S. Treasury 2/10 curve inverted in April. The US dollar has risen to levels last seen nearly 20 years ago. (The euro is nearly at parity with the greenback.)

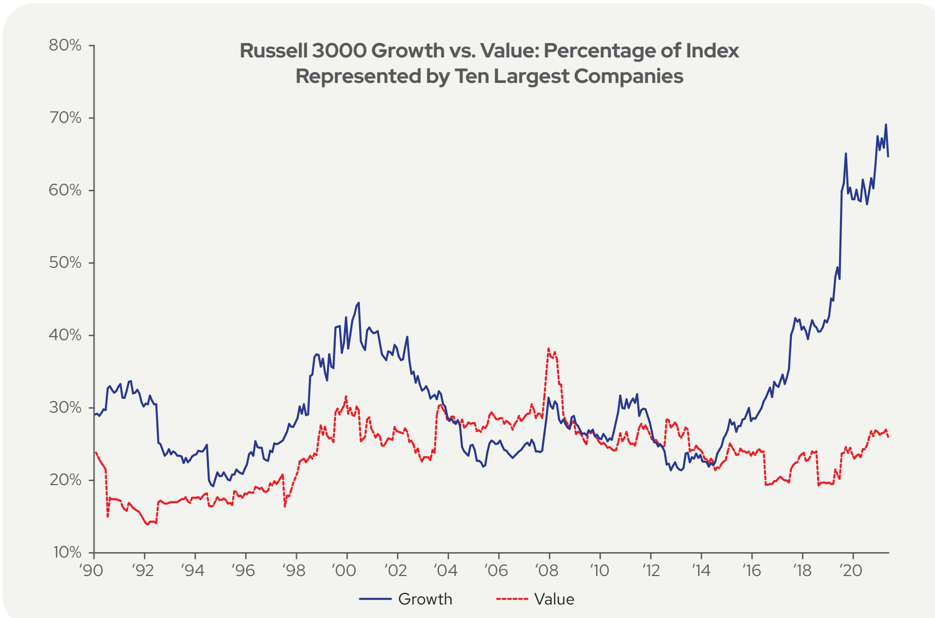
After a month plus of heightened volatility punctuated by acute bouts of panic selling, it will not be surprising to see tactical buyers emerge. Looking ahead, should the current market drawdown persist into quarter end, particularly in growth stocks, we would not be surprised if asset allocators—as a class—became net buyers of equities in late June/early July to build risk-adjusted positioning back to model. In both cases we remain cautious. Though it is always possible—indeed likely—that a strong countertrend move will metathesize, we would be inclined to pare back further from early-cyclical and "long-duration" growth positions, should a period of market strengthening emerge in the near term, and would reallocate in the comfort of higher-quality and more defensive shares for the intermediate term. Thus, we have positioned the Strategas Macro Thematic Opportunities ETF (NYSE: SAMT), anticipating continued momentum in four thematic areas: "Inflation for Longer," "Quantitative Tightening," "Cyclical Defensives," and "De-Globalization."

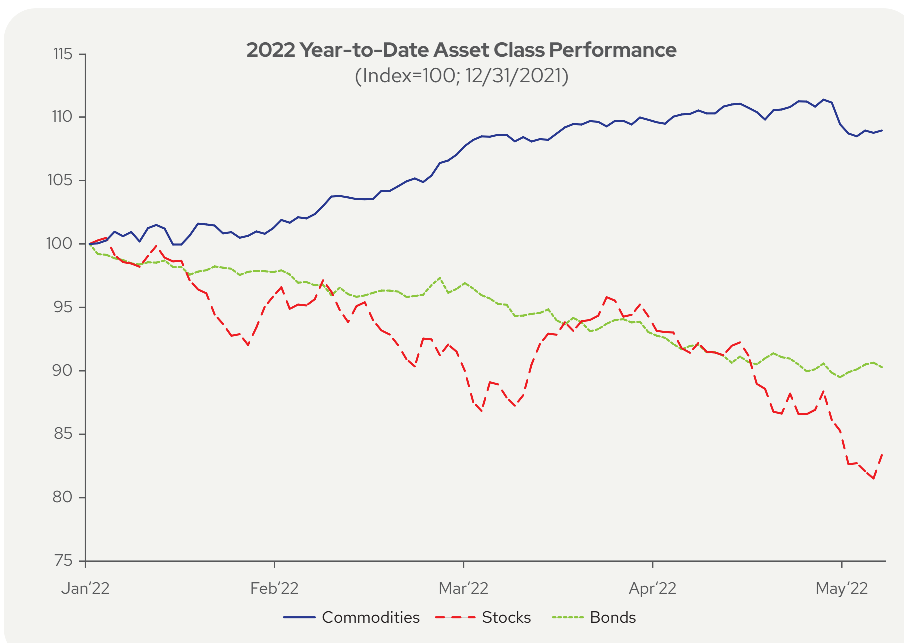


Though COVID-19 and its health effects remain much in the fore, a decade plus of post-GFC monetary leniency, compounded by necessary (less necessary and wholly unnecessary) fiscal provisioning, appears to have fostered such a sufficient misallocation of resources that recalibrating the global economy from disequilibrium is likely—in our view—to be protracted and, at times, painful. In conversations with clients, we have continued to recommend both a reduction of broad equity exposure and a rotation toward value. Last month (April 2022), we reduced equity exposure in our global asset allocation portfolios to a neutral 60% weighting from 62% (which we established in September 2021) and down from a post-pandemic rally high of 67% (January–August 2021). We are unchanged this month. Within equities, however, our portfolio construction since Q421 has increasingly tilted toward US domestic shares (particularly large cap value), with targeted neutral-to-underweight allocations to large cap growth, large cap core, developed international, and emerging markets.

We are adding to Treasurys this month, as we did in April. Like the material above-benchmark allocation to equities we had established following the brunt of the pandemic-induced sell-off, we maintained a significant below-benchmark position in broader fixed income and to U.S. Treasurys, given the application of fiscal and monetary policy during the same period. With the recent back-up in rates at the long end of the curve, we are increasing exposure to reduce this underweight and to reduce our underweight to duration. We anticipate natural buying from liability book managers to grab some portfolio yield while improving the quality of their holdings. We are increasing our broad allocation to fixed income by 200 basis points, to 32% from 30%, by deploying some of the portfolio's cash (we retain a 6% position to cash & equivalents, of which 4% is in gold). Within fixed income, we are reducing exposure to both bank loans and short-duration investment grade corporates, both of which have been steady outperformers over the last several quarters, and increasing long-duration investment grade holdings along with Treasurys.

Two summers ago (June 2020), anticipating that inflation would prove less transitory than policymakers hoped, we used a portion of our elevated cash balance to establish a small position in gold (2%). In June 2021, we increased our position to 4%. With the increased correlation between stocks and bonds making it more challenging to hedge one with the other, we have established a beachhead position in the ostensibly less correlated alternative asset sleeve, namely commodities. Though the recent run in nearly all commodity segments may make the timing seem spurious, we are compelled by both the risk management profile (particularly in more liquid corners), and the fundamental underpinnings we see in commodities, with increasingly structural dislocation in

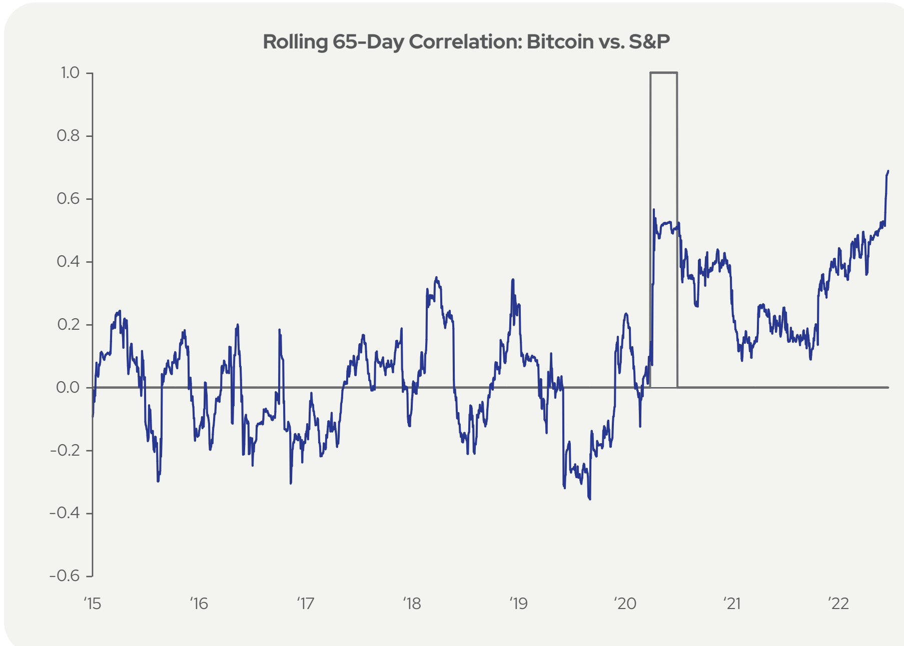




global supply chains and the thematic momentum behind de-globalization.

Though crypto currencies are not a position in our allocation portfolios, we are inclined, given the number of client questions on the topic in recent weeks, to note the acute sell-off in these assets. Particularly notable is the sharp increase in Bitcoin's rolling correlation with the broader equity market (and those of higher-beta alt coins). The (extremely) long-term case for digital currencies as part of an evolved global currency regime may have merit, but we are on the sidelines until the use case is proved outside a period of easy money.

The outlook remains uncertain. Our Chief Economist, Don Rissmiller, has discussed the existence of narrow paths to less severe resolutions of various components of disequilibrium in the economy. Those paths are indeed narrow and—in our view—narrowing. Stay focused.



About Strategas

Strategas is a global institutional brokerage and advisory firm. The Firm provides macro research, capital market and corporate advisory services, and investment management solutions to institutional investors and corporate executives in more than twenty countries around the world.

Founded in 2006 by Jason DeSena Trennert, Nicholas Bohnsack, and Don Rissmiller, the Firm was acquired by Baird Financial Group in 2018. Strategas operates independently as a wholly-owned subsidiary of Baird and offers institutional securities services through Strategas Securities, LLC, a broker-dealer, and investment management solutions, including this commentary, through Strategas Asset Management, LLC, a registered investment advisor.

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Index Overview & Key Definitions

Fed, The Fed or FED refers to the Federal Reserve System, the central bank of the United States. Fed Funds Rate, the interest rate at which a depository institution lends funds maintained at the Federal Reserve to another depository institution overnight. The Gross Domestic Product (GDP) rate is a measurement of the output of goods and services produced by labor and property located in the United States. Real Gross Domestic Product (GDP) is an inflation-adjusted measure that reflects the value of all goods and services produced by an economy in a given year. Nominal Gross Domestic Product is gross domestic product (GDP) evaluated at current market prices. The S&P 500 Index is an unmanaged index comprised of 500 widely held securities considered to be representative of the stock market in general. The Russell 1000 Index is a market capitalization weighted benchmark index made up of the 1000 largest U.S. companies in the Russell 3000 Index. The Russell 2000 Index is an unmanaged index considered representative of small-cap stocks. The PCE (Personal Consumption Expenditure) Index of Prices is a US-wide indicator of the average increase in prices for all domestic personal consumption. Using a variety of data including U.S. Consumer Price Index and Producer Price Index prices, it is derived from personal consumption expenditures; essentially a measure of goods and services targeted towards individuals and consumed by individuals. The Producer Price Index (PPI) program measures the average change over time in the selling prices received by domestic producers for their output. The prices included in the PPI are from the first commercial transaction for many products and some services. FAANG is an acronym for the five of the market's most popular tech stocks, namely Facebook, Apple, Amazon, Netflix and Alphabet's Google. The North American Free Trade Agreement (NAFTA) is an agreement signed by Canada, Mexico, and the United States, creating a trilateral trade bloc in North America. The Seasonally Adjusted Annual Rate (SAAR) is a rate that is adjusted to take into account typical seasonal fluctuations in data and is expressed as an annual total. SAARs are used for data affected by seasonality, when it could be misleading to directly compare different times of the year. The Atlanta Fed GDPNow forecasting model provides a "nowcast" of the official estimate prior to its release by estimating GDP growth using a methodology similar to the one used by the U.S. Bureau of Economic Analysis. GDPNow is not an official forecast of the Atlanta Fed. Rather, it is best viewed as a running estimate of real GDP growth based on available data for the current measured quarter.

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