SSI Investment Management

December 2022

Flexible Allocation: Environment and Portfolio Positioning

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Environment

- After moving significantly higher for two consecutive months, equity markets reversed course in December, with the S&P 500 falling 5.77%
- The yield on 10-Year US Treasuries rose 27 basis points to 3.88%, contributing to the 0.45% decline in the Bloomberg U.S. Aggregate Bond Index

- **Economy** – slowdown occurring / mild recession most likely
  - Inflation: continued to decline from peak levels
    - Reflected in November and December CPI report
  - Federal Reserve: slowed the pace of rate hikes to 50 basis points in December
    - Additional rate hikes are likely to be limited, with the pace possibly slowing to 0.25% and a pause coming sooner rather than later
    - How quickly will they pivot if inflation slows further and/or economy weakens significantly?
  - Economic data generally weaker
    - Real GDP should be positive for Q4 but growth is expected to slow, and could turn negative, in 2023
    - Most employment indicators remain healthy, although there are signs of a modest slowdown in some areas
    - Earnings estimates have been declining and corporate profits may turn down in the fourth quarter or early in 2023
    - Globally, China reversed their zero-covid policy and economic activity is expected to strengthen, while Europe has stabilized and may be able to avoid a recession

- **Market Trend** – pulled back in December
  - Longer term support levels in place
  - Significant $ remain on the sidelines

- **Valuation** – attractive (especially certain segments)

Portfolio Positioning

- SSI's disciplined process and "constrained" approach helped Flexible Allocation portfolios limit drawdowns

- Although markets pulled back in December, the investment environment has become more constructive over the last couple months
    - Portfolio is no longer defensively positioned
    - Equity allocations remain steady and close to relevant benchmarks

- **Equity** portfolio generated returns similar to the S&P 500
    - Reduced energy position (XLE), which helped returns throughout 2022
    - Increased international equity position (VXUS / HEFA)

- **Fixed Income** portfolio held up relatively well, outperforming the Bloomberg Aggregate Bond Index
    - Given the highly volatile rate environment, we continue to focus on fixed income securities with limited interest rate sensitivity
    - Outlook for fixed income has improved significantly with mid-to-high single digits available across many fixed income market segments

- **Alternatives** outperformed the remainder of the portfolio
    - Convertibles offer attractive risk/reward - opportunity for upside participation combined with the potential for downside protection

- If the environment continues to improve, the portfolio will be adjusted to further capitalize on opportunities and participate in market upside

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