SANCTUARY
WEALTH

Sanctuary Asset Management

Investment Outlook
December 2023

Active Asset Allocation Views

Overview

This month's view underscores a dynamic investment environment shaped by government policies, economic indicators, and legislative developments. These movements are likely engineered to have a substantial impact on the economy, which is not seen as coincidental. Fiscal stimulus measures continue to play a critical role in driving real GDP growth. The council raised concerns about a possible 'look back' recession, a term for a retroactively declared economic downturn, once data is fully assessed. This scenario warrants caution for investors, as it suggests a need for strategic portfolio adjustments to mitigate potential downturn impacts. Significant legislation passed during the Biden Administration is expected to create notable ripples in the economic landscape. The timing of these policies, aligning with the presidential election cycle, adds a layer of complexity. Investors should be vigilant in analyzing how these changes might engineer specific political outcomes, affecting market sentiment and investment trends.

Economy

Key indicators such as the OECD leading indicator and ISM point towards upward trends, suggesting potential investment opportunities in sectors benefiting from economic growth. However, this optimism is tempered by consumer pessimism driven by inflation and high costs, indicating a cautious approach for consumer-driven markets. A critical aspect for investors is the potential for a negative Consumer Price Index (CPI) if shelter costs are excluded. This scenario could prompt the Federal Reserve to consider lowering interest rates, a move that would have significant implications for bond markets and interest-sensitive sectors. Investors should monitor developments in housing and shelter costs closely, as changes here could influence broader market dynamics. The interplay between consumer sentiment, inflation, and unemployment rates is complex. Despite a strong labor market, persisting inflationary pressures may lead to unanticipated economic shifts. Investors should be prepared for volatility, particularly in industries sensitive to consumer spending and inflation. Balancing portfolios to mitigate risks associated with inflation while capitalizing on growth in a strong labor market could be a prudent strategy.

Equities

The equities market is currently dominated by the 'Magnificent 7' tech stocks, significantly swaying market indices and overall performance. This concentration raises concerns about market health and diversification strategies. These tech giants have outperformed the broader market, which shows sluggish growth in their absence, signaling a need for investors to reassess portfolio balance. Valuation expansion of these tech stocks points towards a shift in investment strategy, favoring stock pickers. This environment could herald increased opportunities in small-cap and quality stocks, sectors often overlooked in tech-heavy portfolios. Investors should consider rebalancing to capitalize on potential growth in these areas. However, caution is advised due to uncertainties around valuation timing and market irrationality. The possibility of a super cycle, deviating from historical trends, presents both risks and opportunities. Investors need to stay vigilant, continuously analyze market dynamics, and be prepared to adapt strategies to mitigate risks associated with overreliance on a narrow segment of the market while exploring emerging opportunities outside the tech sphere.

Fixed Income

The ongoing reduction in bank reserves, because of the Fed's balance sheet contraction, is scrutinized for its potential impact on the labor market and wage dynamics. Investors should monitor these changes closely, as they could significantly influence bond yields and fixed income investments. The labor force participation rates and the JOLTS index are key indicators of labor market health. Their trends are vital for understanding wage pressures, which in turn affect overall economic growth and investment strategies. Regarding the 10-year Treasury, there's active debate. Worries about treasury supply versus a continued decline in inflation are driving the debate about whether we will see a higher or lower level on 10-year in the coming year, or years. In some cases, there is a wide difference between forecasts and opinions as the market continues to adjust to ever changing dynamics. These predictions should be weighed against potential wage pressures, which might persist until labor force participation fully recovers. Investors also face the challenge of a possible rate cut by the Federal Reserve, should inflation drop significantly or economic growth slow down.

Alternatives

Reduced capital accessibility and higher borrowing costs has been favorable for private lending, offering attractive risk-adjusted returns. Current optimism is fueled by decreasing inflation, solid employment figures, and steady economic growth, factors crucial for investment decision-making. Despite positive indicators, cautiousness is advised due to the potential lingering effects of inflation. This climate presents unique opportunities to provide capital under favorable terms, especially relevant in the private equity sector where market stress could escalate. Investors should exercise careful selection in private equity investments, where increased stress is likely. The secondary market for private equity is experiencing robust growth, propelled by a lack of liquidity options for Limited Partners (LPs) and General Partners (GPs), as well as a scarcity of quality assets. This situation presents a strategic opportunity for investors to leverage these market conditions, considering the evolving landscape and potential for high returns in carefully selected private market investments.

Asset Allocation Views

		UW			N	OW				
		Conviction							Change	
BROAD ASSET CLASS	Equities			●					▼	Slight underweight valuations are more expensive and mega-cap technology leadership is unlikely to be sustained.
	Fixed Income					●			▲	Strategically overweight credit where we see opportunities in MBS and below-investment grade.
	Cash					●			▲	Maintaining benchmark weight to cash and reallocating into longer maturity investment grade fixed income.
ASSET CLASS – EQUITIES	U.S.				●					Slightly underweighted the benchmark weighting, discerning stock selection over sectors.
	U.S. Large Cap				●					Appears least risky among equities, but there is avoiding overhyped 'Magnificent 7' stocks.
	U.S. Mid Cap			●					▼	Underweight suggesting skepticism; potential growth prospects slightly challenged.
	U.S. Small Cap					●			▲	Selectively bullish on small caps, with regional bank focus.
	U.S. Growth			●					▼	Growth stocks likely overpriced; reducing exposure, particularly attributed to 7 stocks (i.e., "Magnificent 7").
	U.S. Value					●			▲	Value stocks remain attractively valued and could benefit in a 'no-landing' scenario.
	Intl. Developed				●					Economic headwinds feared in non-US developed markets.
	Intl. Emerging Markets				●					Geopolitical/economic concerns drive emerging market underweight.
ASSET CLASS – FIXED INCOME	Duration				●					
	Credit Quality					●				Attractive yields found in lower credit quality.
	Treasuries			●					▼	Slight underweight; anticipating policy-driven rates to have peaked.
	MBS					●			▲	High-quality agency MBS preferred within the benchmark with attractive yield.
	Corporate IG			●						Underweight to take advantage of tight credit spreads to fund increased risk-taking elsewhere.
	+ Corporate HY					●				Overweight in high-yield; recession risks deemed past, but we expect challenges in maturity wall in 2024/25.
	+ Intl. Developed				●					Avoiding international bonds from developed markets, due to currency risk concerns.
	+ Intl. Emerging Markets				●					Steering clear of the potential volatility in emerging markets debt.
ASSET CLASS – ALTERNATIVE	Hedge Funds					●				Favorable environment for many styles, including Macro, Long/Short, Event Driven, and Trend Following.
	Private Credit						●			Additional 300-500 basis points over SOF, as private lenders help fill a void left by a bank pullback.
	Private Equity					●				PE secondaries are being led YTD by Buyout, with Growth/Venture to follow are macro picture improves.
	Real Estate				●					We see areas like infrastructure equity as a relative bright spot, and a challenging environment for CRE
	Crypto				●					Bitcoin is the leading asset class YTD, despite broader market volatility.

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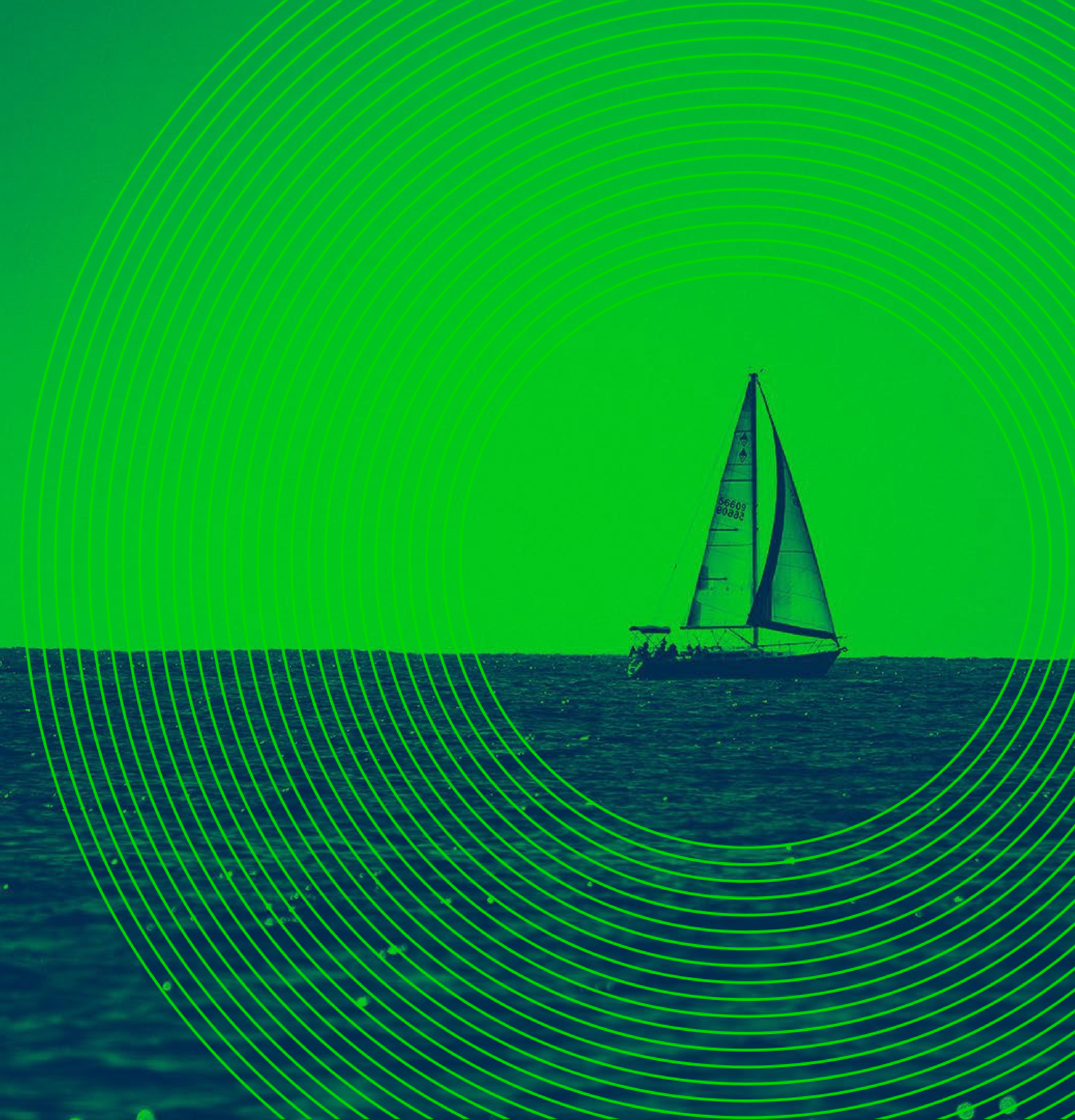


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