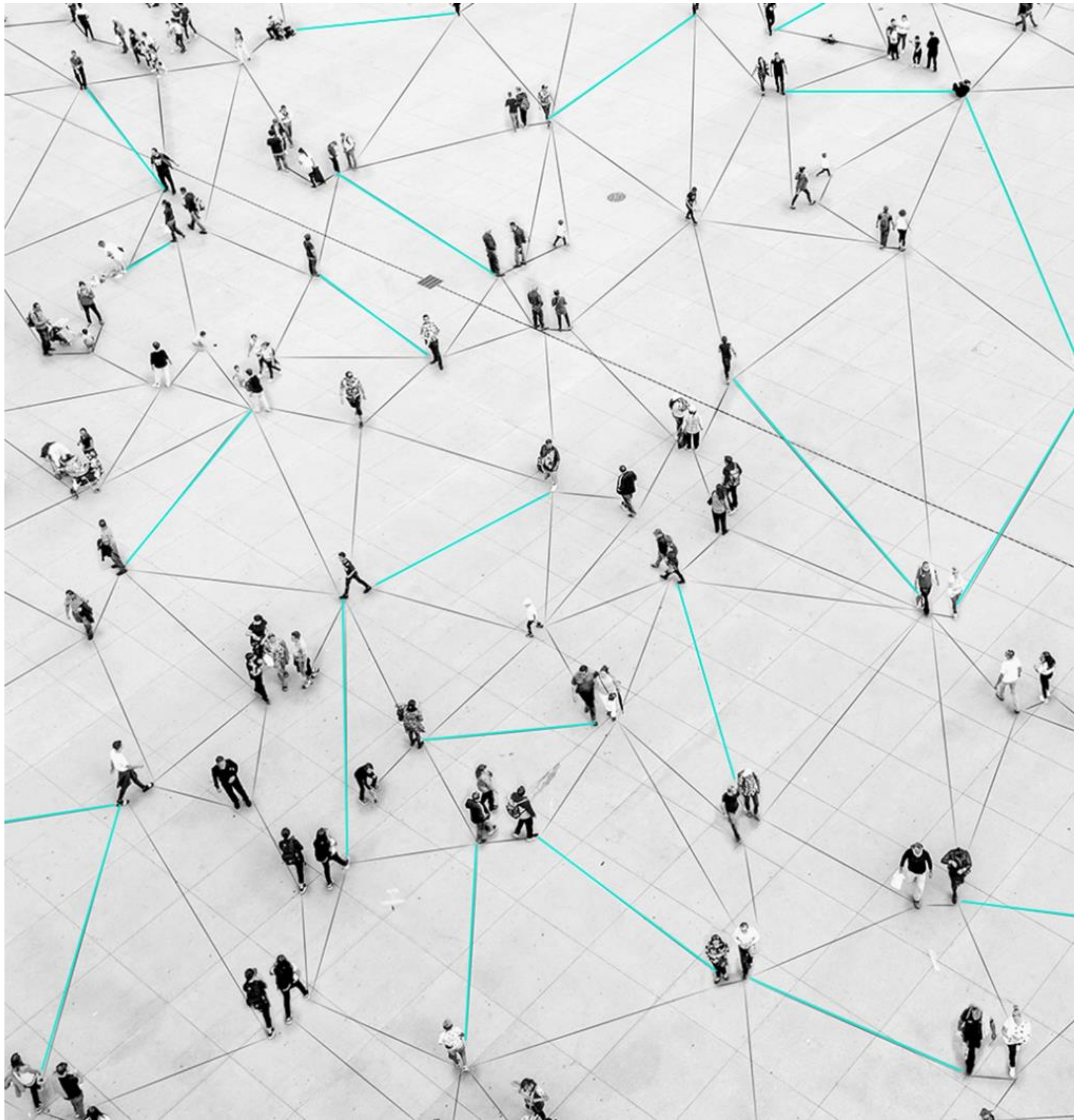
AlTi TIEDEMANN GLOBAL

July 2023

Quarterly Market Update and Outlook



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Executive summary

A strong quarter for stock market returns; positive for other risk assets.

- The second quarter saw strong gains across global equities, led by the US. The S&P 500 rose 8.3%, its biggest quarterly advance since the fourth quarter of 2021.
- Through June 30, the S&P 500 gained 16.9%, its best first half since 2019. Global markets were also strong but lagged the US.
- US stock market gains were highly concentrated 7: technology companies accounted for the lion's share of the S&P's return.
- Bond returns were driven mainly by income as intermediate and long duration government bond yields were mostly unchanged.
- On the Diversified asset side, gold, high yield bonds and hedge funds had modest gains.

Lots of good news everywhere in the face of investors cautiously positioned.

- Sentiment was highly bearish entering 2023 and many investors lightened their equity exposure in favor of attractive cash yields.
- We had continued to maintain that 2023 would be a good year for risk assets and that investors should remain fully invested.
- The second quarter took many by surprise as was marked by significantly better news versus expectations: resilient growth, lower inflation, excitement around Generative AI, less banking stress, and resolved US debt deal.
- Good news sent investors and strategists scrambling to adjust positions.

Does this mean continued strength in risk assets ahead?

- After strong gains, the US market needs to consolidate, and breadth needs to widen.
- We still believe the US economy will slow into the back end of this year as Central Banks continue to tighten. Liquidity may be pressured by reduced lending.
- Risks to near term economic and earnings growth remain.
- However, when the S&P 500 gains more than 10% in the first half, the rest of the year tends to be positive (albeit with volatility).

An improving picture as we look forward to 2024.

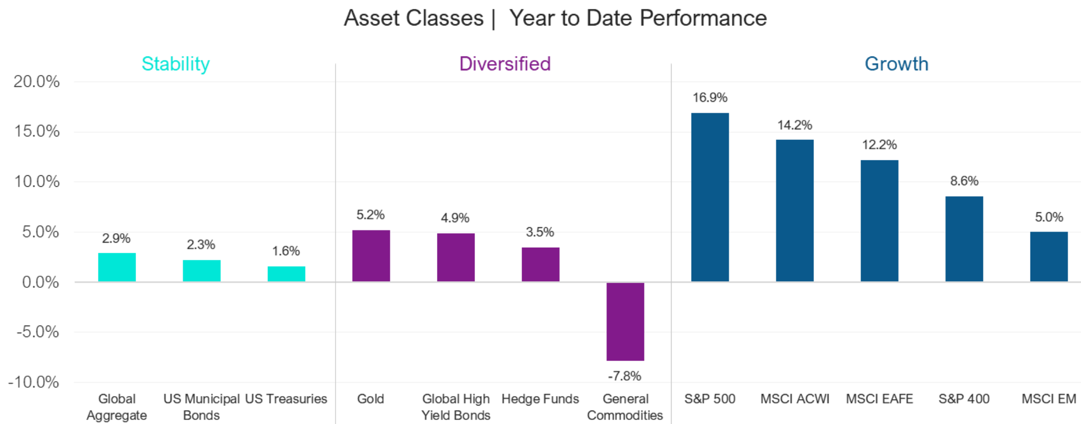
- We weigh the above near-term concerns with our more optimistic forward-looking view into 2024.
- The global economy may slow but from a higher base, providing more resilience than expected.
- We believe inflation will continue to ease as the year progresses.
- Hence, we think the worst of the 2022 bear market is behind us.

Insight detail

A strong quarter for stock market returns; more muted for other risk assets.

- Growth assets were strong. The S&P 500 returned a hefty 16.9% in the first half of 2023. Non-US markets gained 12.2% as measured by MSCI EAFE. Mid cap, value and emerging market indices ended the first half in positive territory but lagged US large cap gains.
- Diversified and Stability assets, while largely positive, showed more muted returns.

Asset Classes | Year to Date Performance



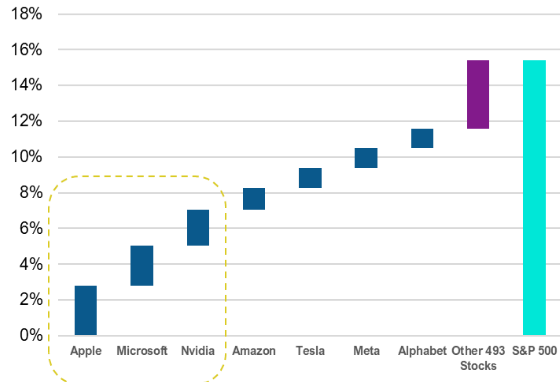
Source: Bloomberg LP; Total Return as at 06/30/2023. Gold performance is based on USD Spot price; Hedge Funds are HFRI Fund Weighted Composite + HFRX Global (month to date); all other indices are Bloomberg's own, unless otherwise stated.

Past performance is not a guide to future performance, nor a reliable indicator of future results or performance. Indices are unmanaged and do not reflect the deduction of fees and expenses, and are not available for direct investment. Refer to Indices and Definitions section for more information.

- The leading catalyst for strong US stock market performance has been news around Generative AI, which has propelled gains from seven stocks (Microsoft, Amazon, Apple, Google, Meta, Tesla, and Nvidia). They have accounted for close to 80% of the S&P 500's 2023 gain and now make up more than 25% of the index's market cap (the highest concentration in the index since 1972).
- This can be shown by the significant difference in performance between the cap-weighted and equal-weighted S&P 500 and waterfall of contribution to S&P gains YTD (below).

Comparative Performance of S&P 500
Capitalization weighted versus S&P equally weighted

Waterfall of contribution to S&P 500 gains YTD
(as of end June)



Source: Bloomberg LP, June 30th 2023

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- We believe that Generative AI will be transformational over the medium to long term and lead to significant improvements in productivity. However, we have seen a significant multiple expansion in these leading technology companies, which are now valued at over 30x earnings on average.
- A lot of good news has already been discounted and we are reminded of Amara's Law: 'we tend to overestimate the impact of technology in the short term and underestimate the effect in the long run'.
- For the US market to move higher we need to see greater participation from the other 493 companies in the S&P.

What explains the advance? Lots of good news everywhere in the face of investors cautiously positioned.

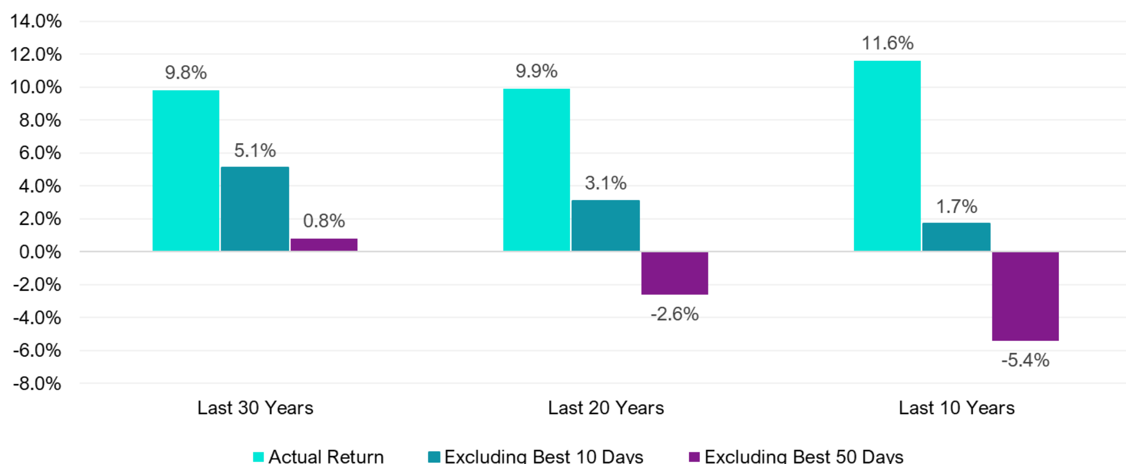
Few predicted the magnitude of gains this year, particularly in a year in which:

- The Fed continued to raise rates: over 500 basis points from 2022 and the fastest tightening cycle in 40 years.
- Short-term money market fund yields topped 5%, providing legitimate competition for equities.
- Four major banks failed amongst significant financial stress in the banking sector.
- The US yield curve is inverted by over 1%, traditionally a sign of economic weakness ahead.
- Most investors expected an imminent recession that would weigh on earnings.

However, a string of good news has propelled equity markets higher.

- The feared recession has yet to materialize, and economic growth has remained highly resilient, largely led by the global consumer. The US economy has been particularly strong.
- Q1 earnings beat expectations by a wide margin, leading some forecasters to expect increased earnings revisions ahead.
- Generative AI fever gripped markets on the transformational power of this technology to accelerate growth and improve productivity.
- The US resolved the debt crisis through bi-partisan compromise and with less fiscal drag than expected.
- Inflation, while sticky and above the Fed's target, continued to move lower.
- Q1 stresses from the banking crisis waned. Annual stress tests on larger banks at quarter end saw adequate capital buffers.

We are reminded of the importance of remaining invested despite an uncertain outlook. Doing so allows one to participate in the unexpected days that provide the lion's share of performance, as shown in the chart below.



Source: Goldman Sachs, June 2023

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Does this mean continued strength in risk assets ahead?

- Markets always experience volatility, particularly after periods of strong gains. Looking forward, we would not be surprised to see markets consolidate or pull back somewhat, a normal and healthy event.
- Risks that could undermine the positive sentiment:
  - Central Banks globally are continuing to tighten, with the Fed signaling possibly two more rate hikes in July and September. The Bank of England, the European Central Bank and the Central Banks of Canada, Norway, Switzerland, and Australia are also still moving rates higher.
  - Growth in China has slowed significantly after a spurt after Covid reopening.
  - Bank stresses continue. Banks with more than $100bn in assets may need to hold more capital, many regional banks face risks from increases in funding costs and refinancing risks in commercial real estate, and large banks face increased capital requirements per Basel III.
  - There is a possibility of a global synchronized slowdown that becomes negatively self-reinforcing, exacerbated by potential tightening in credit conditions in the US.
  - The US market has seen a significant multiple expansion and at 19.7x forward earnings is expensive relative to history.

For now, our base case is still an economic slowdown in the latter half of 2023. Whether this is a shallow recession, mild slowdown, or soft landing remains to be seen.

An improving picture as we look forward to 2024.

We see an improving economic picture as we look forward to 2024 as we expect inflation to moderate and growth expectations to improve.

On the economy:

- The expected slowdown in economic growth is starting from a higher base. The first quarter in the US showed upward revisions to GDP growth, with US consumer contributing a gain of

4.2% versus 1.0% in the fourth quarter of 2022. The second quarter looks to be equally solid with the service economy still in expansionary territory.

- The US consumer still enjoys excess savings post pandemic and has low levels of debt. The travel sector continues to show signs of post-pandemic strength, as evidenced by airline and cruise company bookings.
- While manufacturing remains weak, there are some signs that the housing market (in recession last year) is starting to recover. New home sales in the US surged 12% and home prices rose +0.9% on a month-over-month basis in May despite mortgage rates climbing to 7.2% for a 30-year fixed loan.
- US corporations are in good shape with interest coverage ratios at 6.5x, well above the long-term average and significantly higher than levels on the eve of the covid pandemic. Companies also have limited near-term refinancing requirements, having extended the maturity of their debt until way into 2025.
- Government spending is likely to remain supportive. The US has committed over $1.7 trillion in various fiscal programs (the Inflation Reduction Act, the Chips Act, and the Infrastructure Investment and Jobs Act) and the EU has pledged $400bn in various stimulus program aimed at energy independence and climate transition. While these are multi-year programs, they can lead to near term multiplier effects in the public and private sector.
- We believe that China will continue to add stimulus in the form of fiscal and monetary support and Asia will enjoy improved growth from Japan. After years of moribund economic performance, Japan's GDP grew by 2.7% annualized in Q1.

On inflation:

- Central Banks are gaining credibility as they look jointly to quell inflation. We think the combined efforts of global tightening could contribute to a higher degree of inflation reduction success.
- Inflation expectations have continued to remain benign. The University of Michigan's indicator for one-year inflation expectations fell to 3.3% in June 2023, compared with 4.2% the previous month and the lowest level since March 2021.
- The Personal Consumption Expenditures Index, the Fed's favored measure, grew at 3.8% on a year-over-year basis, below the downwardly revised 4.3% in April. Both goods and services inflation decelerated over the month, further affirmation we may be slowly moving towards the Fed's target.
- The June US inflation number was also a positive surprise at 3.0% year on year, though the Fed would view core inflation (excluding food and energy) at 4.8% still too high. We note core inflation-ex housing is now under 3%
- We think that sometime in 2024 Central Banks will get inflation under control and be able to pause their rate hiking cycle and possibly pivot to easing.

Hence, we suspect that growth, while slowing into year-end 2023, should recover at some point next year.

Looking forward: Asset allocation positioning.

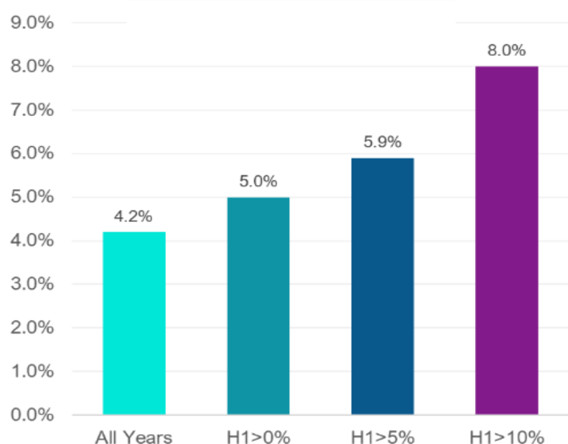
What does all this mean?

We divide our remarks into what we see as the near-term outlook and how we think about some of the macro regime shifts from a long-term perspective.

Near term:

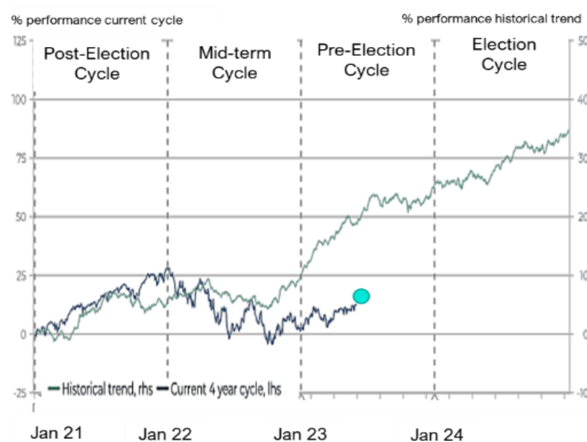
- We could well see a period of consolidation after strong first half gains, as markets discount the impact of potential economic weakness and/or mild recession on earnings of companies in the quarters ahead. We do not expect linear gains from here.
- Central Banks globally are still tightening. It may be that the combination of rising interest rates and tighter credit slows the economy more than expected or cause markets to wobble.
- Any pullback, in our view, would be an opportunity to lean into areas of strong conviction. We take comfort from the fact that strong first half gains typically result in solid returns for the second half of the year, with a median average gain of 8%.
- Moreover, the 3rd and 4th year of US Presidential electoral cycles tend to be positive for risk assets.

Strong first half augurs well for rest of year
S&P 500 Price Gains During Second Half (H2) since WWII



Source: CNBC June 28, 2023

Stocks below historical norms for a presidential cycle
S&P 500: Presidential election cycle



Source: MacroBond, data going back to 1942

Past performance is not a guide to future performance, nor a reliable indicator of future results or performance

Long term:

As we look ahead, our views remain unchanged. Most notably, while the Fed may get inflation lower, it will likely remain structurally higher than in the past (in the 3%+ range) due to interconnected and self-reinforcing factors:

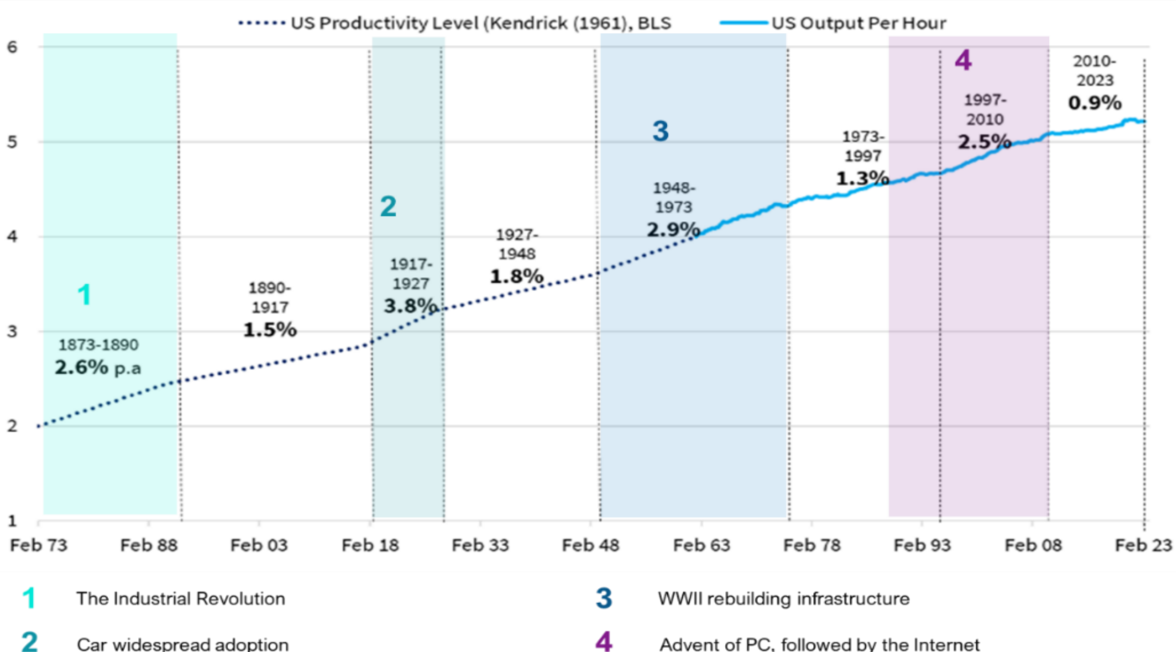
- The developed world is experiencing aging demographics. Labor remains in relatively short supply as baby boomers retire, keeping upward pressure on wages.
- The onshoring of supply chains could exacerbate labor shortages. The world is moving from hyper globalization where the global economy provided an endless supply of cheap labor to a world focused on national interests above global efficiency.

- We have entered more of a beggar-thy-neighbor regime, with particular strain between the US and China as each competes for access to key commodities and technology. Underinvestment in certain of these areas may keep costs elevated if demand outstrips supply.
- We are entering a world where once traditional allies fracture into new alliances, with China playing a more activist foreign policy role and wanting to assert its influence over many countries traditionally tied to the US.
- We suspect that nations are likely to use fiscal spending to accelerate national priorities, be it supporting priority investments, the energy transition, access to innovation and critical minerals, and/or investing in new areas of cyber protection and/or traditional forms of defense.
- A more activist and interventionist public sector is likely to keep debts and deficits high and put upward pressure on yields to support financing needs.

All these factors potentially raise the cost of production and could serve to challenge profit margins.

- The antidote to these profitability challenges is corporate investment in automation and technology. Indeed, we think we're on the verge of a strong capex cycle lasting several years.
- The opportunity of Generative AI is no doubt being evaluated by every company today; the technology opportunity, growth in automation, and need for energy efficiency are driving factors supporting increased corporate investment.
- Past periods of strong capex and innovation have tended to coincide with dramatic improvements in labor productivity.
- In the last four significant productivity booms (the Industrial Revolution, mass adoption of the automobile, rebuilding of economies-post WWI, and the advent of the personal computer and the Internet) led to productivity gains of 2.5% on average.
- Contrast this with the very poor productivity of the last decade (+0.9%) during an era of free money, low capex spend, less transformative innovation, and endless supply of cheap labor.

History of US labor productivity from 1873-2023



Source: Aletheia Capital, The Missing Link, May 29th 2023

- A period of improved productivity would have powerful implications for disinflation and provide ample opportunities for companies who invest to potentially enhance growth and/or reduce costs.
- We see a world of winners and losers ahead. Companies that take advantage of the opportunity of digitalization will best fortify competitive positioning.

Asset allocation positioning

As we think about how these trends impact our Stability, Diversified and Growth strategy categories, we find continued fertile ground for diversification and where appropriate exposure to alternatives, such as real estate, private credit, and private equity.

Some of the trends we are interested in from a portfolio perspective include:

Stability assets

- On a risk-adjusted basis, current yields on inflation-protected, high-grade government, and corporate bonds are more attractive than they have been in more than a decade.
- However, if we are right about the outlook for growth and inflation into 2024, short rates are likely to head lower in 2024 and the long end will settle around the long term expected inflation rate (circa 3%) plus a real return of around 1%.
- This suggests that both the short and long end of bond markets may be under pressure and remain volatile if yield curves steepen.
- Stability assets should be a source of dry powder for increased allocations to higher returning diversified and growth.
- We have already made a move in this direction by reducing Stability in favor of an increased allocation to mid-cap and value companies in the US.

Diversified assets

- **Credit:** We see areas of credit becoming more interesting, particularly where we can secure close to long-term equity-like returns. We are evaluating a range of managers and expect allocations to increase in this area. We also have exposure to dynamic credit managers who can take advantage of changes in yield curve and inflation expectations.
- We continue to think that markets could remain volatile. **Absolute return** strategies fare particularly well in turbulent markets as temporary price dislocations provide opportunity for gains.
- We like **real assets** such as gold and have recently added a timber allocation, as both provide good sources of inflation protection and asset class diversification. For clients able to accept a degree of illiquidity, real estate can provide a natural inflation hedge with attractive, sustainable, and tax-efficient income and attractive after-tax returns.

Growth assets

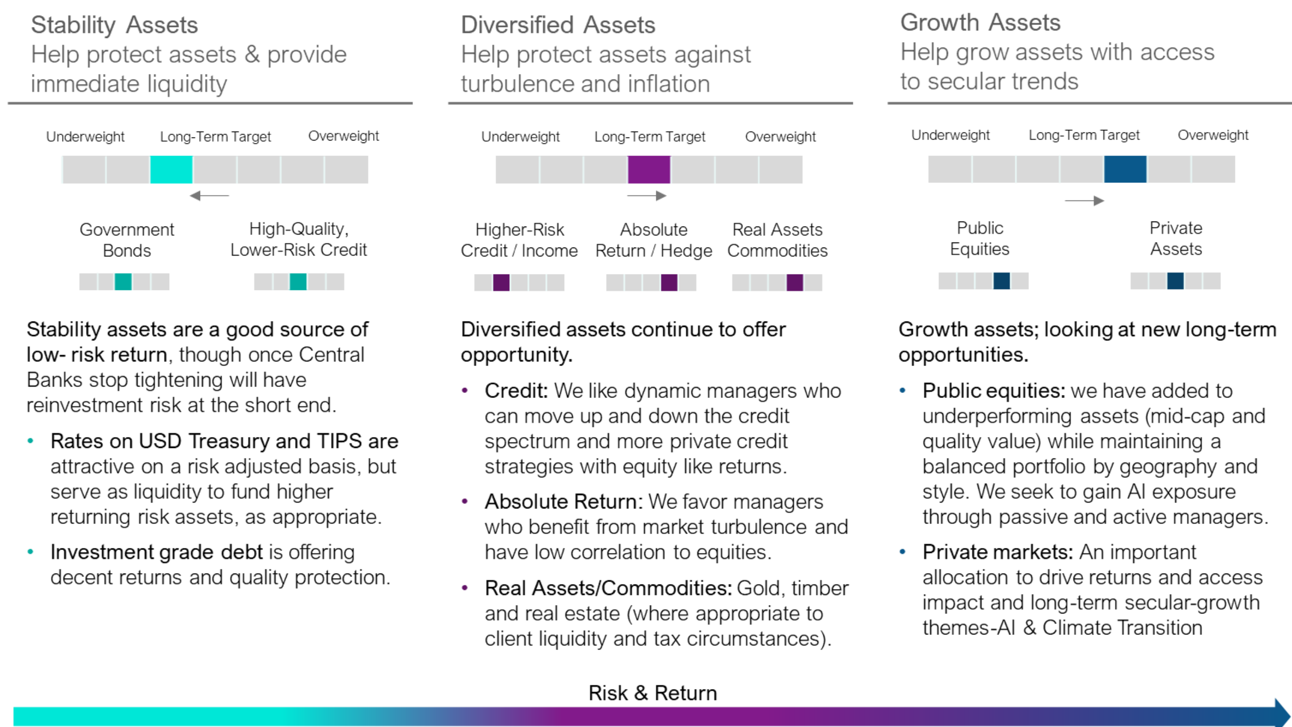
- In the US, we hold significant exposure in passive form. In the early days of AI adoption, the winners and losers across industries and sectors may be harder to predict. Passive exposure means that we are never under or overweight the wrong shares.
- We have increased our allocation to the mid-cap sector in the US as we expect these companies to benefit from earnings uplift from the onshoring of US manufacturing activity. Mid-caps have also underperformed the rally and now trade at a substantial discount to their own history and to US large-capitalization companies.

- We have added exposure to value-oriented equities, focused on quality companies that are showing an improving return on capital invested and free cash-flow generation. These trade at a substantial discount to growth companies. These companies can provide both diversification and additional upside from growth and multiple expansion.
- We maintain exposure to non-US equities. Once the Fed stops raising rates and pivots to an easier stance, we see further US dollar weakness which in the past has led to strong gains for international markets. Macro and micro dynamics in Europe and Japan have supported solid earnings growth and provide diversification benefits.

In private markets:

- Our focus is to leverage our access and experience to partner with managers who add strategic and operational value to drive enhanced profitability. We think the trend of increased investment in automation and technology is supportive of enhanced returns.
- Value-adding buyout managers can use opportunities in digitalization to enhance revenue and drive increased profitability. M&A consolidation can accelerate further efficiency gains.
- Many of our growth and venture managers are laser focused on the opportunity of Generative AI. While public companies like Nvidia and cloud providers like Amazon and Microsoft are likely to dominate the AI infrastructure layer (the proverbial picks and shovels of this platform advancement) the application layer across all industries is still in nascent stage.
- We think this market gap may well be addressed by new technology leaders in private markets. Media, industrial, financial and health care sectors are particularly prime for AI and technology disruption.
- We also see ample opportunities through our managers to invest in the energy transition. In our view, climate is one of the most important investment opportunities of the next decade. We are positioned with managers that we believe can help identify leaders in the decarbonization journey ahead.

Our positioning is summarized in the chart below.



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Indices and Definitions

The 10-YEAR TREASURY YIELD INDEX measures the return on investment, expressed as a percentage, on a debt obligation (note) issued by the United States government with a maturity of 10 years upon initial issuance.

The 5-YEAR TREASURY YIELD INDEX measures the return on investment, expressed as a percentage, on a debt obligation (note) issued by the United States government with a maturity of 5 years upon initial issuance.

ASSET ALLOCATIONS: Tiedemann will change asset allocations over time and from time to time. Changes to the asset allocations may cause the Targeted Asset Class Returns to change, perhaps materially.

ALERIAN MLP TR U.S.D INDEX measures the performance of energy segment U.S. equity securities. It is a composite of the most prominent energy Master Limited Partnerships (‘MLPs’). The index is calculated using a float-adjusted, capitalization-weighted methodology.

BLOOMBERG MUNI INTER-SHORT 1-10 TR INDEX measures the performance of tax-exempt municipal bonds with more than one year and less than ten years remaining until maturity.

BLOOMBERG AGGREGATE BOND INDEX is an unmanaged broad base index comprised of intermediate term, investment grade bonds including Treasury bills, Government agency bonds, mortgage-backed bonds, Corporate bonds, and foreign bonds. The index is considered representative of the fixed income market as a whole.

BARCLAYS U.S. TIPS is an unmanaged index comprised of U.S. Treasury Inflation Protected Securities with one or more years remaining maturity with total outstanding issue size of $500mm or more and measures the performance of U.S. TIPS market.

BARCLAYS MUNI 1-YR is an unmanaged index comprised of investment grade, tax-exempt Municipal bond issues with maturities of one to two years, and is considered representative of the short-term Municipal bond market.

BARCLAYS MUNI 5-YR is an unmanaged index comprised of 4–6-year duration, fixed-rate, intermediate-duration, tax-exempt bonds representative of the municipal bond market of intermediate duration.

BLOOMBERG HIGH YIELD MUNICIPAL BOND INDEX is an unmanaged index composed of non-investment-grade, unrated, or rated below Ba1 bonds.

BLOOMBERG U.S. CORPORATE HIGH YIELD BOND INDEX measures the U.S.D-denominated, high yield, fixed-rate corporate bond market. Securities are classified as high yield if the middle rating of Moody's, Fitch and S&P is Ba1/BB+/BB+ or below. Bonds from issuers with an emerging markets country or risk, based on the indices' EM country definition, are excluded. The U.S. Corporate High Yield Index is a component of the U.S. Universal and Global High Yield Indices.

CRSP U.S. MEGA CAP GROWTH INDEX classifies growth securities using the following factors: future long-term growth in earnings per share (EPS), future short-term growth in EPS, 3-year historical growth in EPS, 3-year historical growth in sales per share, current investment-to-assets ratio, and return on assets.

DEBT TO EQUITY RATIO: a company's total long-term debt divided by total shareholders' equity. The result is a measure of a company's leverage.

ETF: An exchange traded fund (ETF) is a type of security that involves a collection of securities—such as stocks—that often tracks an underlying index, although they can invest in any number of industry sectors or use various strategies. ETFs are in many ways similar to mutual funds; however, they are listed on exchanges and ETF shares trade throughout the day just like ordinary stock.

EPS: Earnings per share (EPS) is calculated as a company's profit divided by the outstanding shares of its common stock. The resulting number serves as an indicator of a company's profitability.

FORWARD PRICE TO EARNINGS: The forward price to earnings (P/E) is the measure of a company's P/E ratio using its expected earnings, used by investors and analysts to determine the relative value of a market or company's shares against another or itself over time.

FTSE TREASURY BENCHMARK 10-YEAR is a market value-weighted index of public obligations of the U.S. Treasuries with maturities of ten years. The Index reflects no deduction for fees, expenses or taxes.

FTSE WORLD GOVERNMENT BOND INDEX (WGBI) measures the performance of fixed-rate, local currency, investment-grade sovereign bonds. The WGBI is a widely used benchmark that currently includes sovereign debt from over 20 countries, denominated in a variety of currencies, and has more than 30 years of history available. The WGBI provides a broad benchmark for the global sovereign fixed income market. Sub-indexes are available in any combination of currency, maturity, or rating.

HFRX ABSOLUTE RETURN INDEX is designed to be representative of the overall composition of the hedge fund universe. It is comprised of all eligible hedge fund strategies; including but not limited to convertible arbitrage, distressed securities, equity hedge, equity market neutral, event driven, macro, merger arbitrage, and relative value arbitrage.

JPMORGAN GBI EM INDEX is an index comprised of emerging market government debt denominated in local currencies.

*KBW Bank Index: This is a modified cap-weighted index consisting of 24 exchange-listed National Market System stocks, representing national money center banks and leading regional institutions.

MERRILL LYNCH HIGH YIELD MASTER II INDEX is an unmanaged index that tracks the performance of below investment grade U.S. dollar-denominated corporate bonds publicly issued in the U.S. domestic market.

A mortgage-backed security (MBS) is an investment similar to a bond that is made up of a bundle of home loans bought from the banks that issued them.

MSCI ACWI INDEX captures large and mid cap representation across 23 Developed Markets and 27 Emerging Markets countries.

MSCI CHINA INDEX is constructed based on the integrated China equity universe included in the MSCI Emerging Markets Index, providing a standardized definition of the China equity opportunity set. It captures large- and mid-cap representation across China A shares, H shares, B shares, Red chips, P chips and foreign listings (e.g., ADRs). With 704 constituents, the index covers about 85% of this China equity universe. Currently, the index includes Large Cap A and Mid Cap A shares represented at 20% of their free float adjusted market capitalization. China A shares will be partially included in this index, making it the de facto index for all of China.

MSCI EAFE is a free float-adjusted market capitalization index that is designed to measure the equity market performance of developed markets, excluding the U.S. & Canada.

MSCI EM is a free float-adjusted market capitalization weighted index that is designed to measure the equity market performance of emerging markets.

MSCI U.S. REIT Index is a free float-adjusted market capitalization weighted index that is comprised of equity Real Estate Investment Trusts (REITs)

OPERATING MARGIN measures how much profit a company makes on a dollar of sales, after paying for variable costs of production, such as wages and raw materials, but before paying interest or tax. It is calculated by dividing a company's operating profit by its net sales.

RU.S.SELL 1000 measures the performance of the large-cap segment of the U.S. equity universe. It includes approximately 1,000 of the largest securities based on a combination of their market cap and current index membership of the Russell 3000.

RU.S.SELL 2000 is a market cap-weighted index that measures the performance of the small-cap segment of the U.S. equity universe. It includes approximately 2000, or 10% in total market-capitalization, of the smallest securities of the Russell 3000 based on a combination of market cap and current index membership.

S&P 500 INDEX consists of approximately 500 stocks chosen for market size, liquidity, and industry grouping, among other factors. The S&P 500 is designed to be a leading indicator of U.S. equities and is meant to reflect the risk/return characteristics of the large-cap universe.

SPDR Barclays Capital High Yield Bond ETF is designed to measure the performance of publicly issued U.S. dollar denominated high yield corporate bonds with above-average liquidity.

US Consumer Price Index Shelter: The index for the service that a housing unit provides its occupants. Owners' equivalent rent of residences and rent of primary residence measure the majority of the change in the shelter cost consumers experience.

Zillow Observed Rent Index (ZORI): A smoothed measure of the typical observed market rate rent across a given region. The index is dollar-denominated by computing the mean of listed rents that fall into the 40th to 60th percentile range for all homes and apartments in a given region, which is once again weighted to reflect the rental housing stock.