STRATEGAS insight

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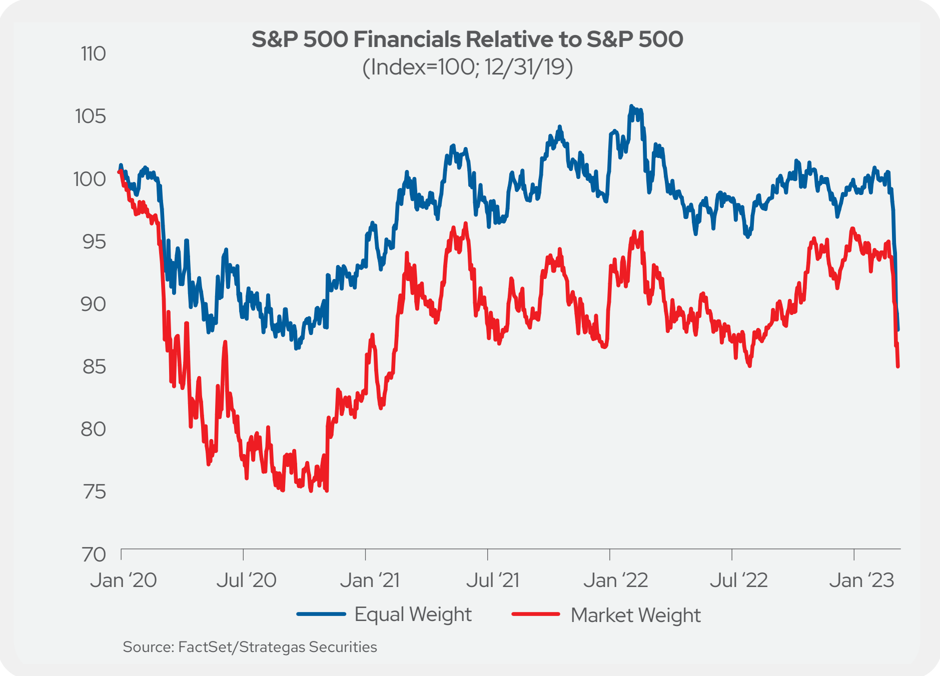
Another Financial Crisis



How quickly a situation can change! Less than a month ago, there existed a palatable tension between an economy rapidly weakening at the hands of policymakers' incessant attempts at reigning in unanchored inflation and the nullifying counterweight of a stubbornly strong labor market, improved consumer spending data, and the alluring pull of higher equity prices. Not surprisingly, investors' foundational optimism pulled them generally in favor of the later. Then, in very short order it seems, the lagged effects of tightening monetary policy caught-up with those banks employing less-than-stalwart risk controls and the next chapter of our global deleveraging saga was upon us.

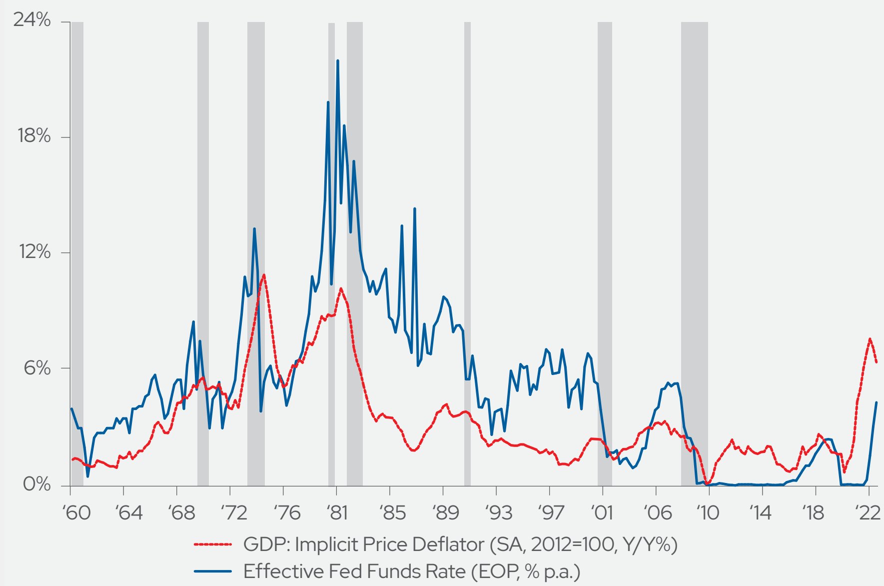
Ultimately, little has occurred that changes our base case. By our lights, we continue in the throes of a bear market typical for the pre-recession progression associated with economic deleveraging. We believe investors should be prepared for a longer-than-desired period of price compression catalyzed by a rolling global margin call in which increasingly impaired collateral necessitates further asset sales. We saw this first with the faddish stuff (SPACs/crypto) getting taken out, followed by longer-duration holdings (FANG & friends) and, now it appears the illiquid & HTM assets (commercial real estate, private debt/equity) are coming under pressure. Each of these phases has been punctuated with powerful, will-testing countertrend rallies. In conversations with clients, few seemed sanguine about the range of assets that would ultimately come under pressure or the time with which it will take to play out. As one prominent macro investor, who shares our view, put it, the process to work through this imbalance will be something akin to a "pig in a python."

Earlier this month, Strategas hosted its 16th annual Macro Conference in New York. As always, it was wonderful to see old and new friends, particularly after the disruptions of the last few years. The tone, as you might imagine, was decidedly cautious to bordering-on-negative given developments in the banking system over the preceding days. Through conference presentations and anteroom conversations, the focus was on the conditions which would result in no landing, a soft landing, or a hard landing. The all-encompassing question seemed to be, **are recent bank failures systemic, or not?** If **yes**, then policymakers should pause/cut, patch the banking system with more acronyms, gather more information and reassess the appropriate approach for combating the economy's many extant imbalances in the context of – yet another – financial crisis. If **no** then hike (as the ECB did), perhaps more clearly articulate desired target inflation levels and the terminal policy rate viewed as necessary to achieve it, and let the market gauge the offsetting economic pain. Last fall, we took the decision to reduce exposure to Equities in our tactical allocation portfolios to below benchmark. In light of recent developments, we are further reducing our share allocation, trimming exposure to U.S. Large-Cap Growth, i.e., long-duration operating franchises with a high reliance on access to both the public and private capital markets, and U.S. Mid-Cap Value, i.e., regional banks with outsized geographic (commercial real estate) and industry (tech, life-sciences, and green energy) exposures. We are also reducing, to Underweight, our recommended weighting of Financials within U.S. equity portfolios. In a phrase, we remain in a "cautious, wait-and-see" crouch, albeit more cautious than a week ago with respect to timing. Inasmuch we are increasing our Cash holding and while we are bullish on the outlook for Gold (and are overweight in our PA), we are holding our current position as it bumps up against the traditional upper bound of exposure.

New York Fed Probability Of Recession In The Next 12-Months

Source: New York Federal Reserve/Strategas Securities as of 3/17/23

U.S. GDP Deflator Y/Y Vs Fed Funds Effective Rate



Strategas Recommended Asset Allocation Mar'23

	Equities	Bonds
Overweight	Dev AC Core US LC Value US MC Value US SC Core	
Neutral	EM AC Core US MC Growth	ABS/CMBS US Dollar EMD IG Corporates
Underweight	US LC Core US LC Growth	US MBS U.S. Treasuries

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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