SENDERO
WEALTH MANAGEMENT

TACTICAL ASSET ALLOCATION

as of September 30, 2018

This report reflects the current opinions of the Sendero Investment Committee on various asset classes used or considered for client portfolios versus their strategic allocation. The comments reflect opinions as of the specific date listed above and can change quickly based on market conditions.

STABILITY

ASSET CLASS	OVERWEIGHT	NEUTRAL	UNDERWEIGHT
CASH	O		
FIXED INCOME			O
ALTERNATIVE STRATEGIES	O		

GROWTH

ASSET CLASS	OVERWEIGHT	NEUTRAL	UNDERWEIGHT
U.S. MARKETS		O	
DEVELOPED MARKETS		O	
EMERGING MARKETS		O	
REAL ESTATE/REITs			O
PRIVATE EQUITY			O
ENERGY	O		

DIVERSIFIER

ASSET CLASS	OVERWEIGHT	NEUTRAL	UNDERWEIGHT
HEDGED STRATEGIES	O		

O OVERWEIGHT O NEUTRAL O UNDERWEIGHT

MARKET HIGHLIGHTS

- While we continue to believe that U.S. economic and market fundamentals are strong, we also note that political and policy risks have grown considerably. These risks will likely come to a head in the next 12–18 months, in our view, when the impact of fiscal stimulus from tax cuts will begin to fade and interest rates will probably be higher.

- The reality of broad trade tariffs and the uncertainty about the trajectory of trade policy should weigh more on market and corporate sentiment through 2019. The global economy could also become less supportive. While we continue to believe that current equity market valuations are justified, we also recognize that they are high relative to history.

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CASH

OVERWEIGHT

We have a higher allocation to cash awaiting deployment when opportunities arise. We are wary of overall equity valuations and higher volatility in the near-term amid political uncertainty globally.

FIXED INCOME

UNDERWEIGHT

Given our expectations of sustained nominal economic growth, further interest rate hikes this year and 2019 along with the Federal Reserve continuing to reduce it's balance sheet, we maintain our underweight positioning to Fixed Income. We still believe in the fundamentals of the asset class as a tail-risk hedge, but we still prefer short-duration benchmark exposure. We favor TIPs as an inflation hedge and managers that have the ability to capture both the long and short side of the fixed income opportunity set.

ALTERNATIVE STRATEGIES

OVERWEIGHT

We recommend full tactical allocations to Multi-Strategy and Market Neutral strategies to reduce portfolio risk. Overall performance has improved due to a higher level of dispersion across industries, sectors, geographies and currencies. What we continue to see is managers in the CTA, Systematic, Quant, risk parity spaces targeting volatility, which creates dispersion in momentum, value and growth factor return. Funds have generally gotten more defensive due to uncertainty about the direction of the U.S. equity market, particularly given the performance gap between the U.S. and the rest of the world.

U.S. MARKETS

NEUTRAL

We are maintaining our neutral tactical allocation to domestic equities. Broad measures of economic activity are still suggesting that US growth should remain on solid footing through the rest of 2018. While valuations are now more reasonable, we remain cautious on the overall equity markets due to the potential for higher volatility from uncertainties over the stronger dollar, trade and tariff policies, and concerns over earnings sustainability in the next few quarters. Our expectation for long only domestic equities is for muted returns with periods of heightened downside risks for 2019. With political and policy risks abound, we see an opportunity for active managers to continue to take advantage of dispersion between company and sector winners and losers.

DEVELOPED MARKETS

NEUTRAL

We continue to maintain our neutral tactical allocation to Developed Markets with an emphasis on active management not exposed to benchmark sectors, but quality companies. While valuations are attractive relative to U.S. equities, the full impact of potential trade wars is still a big unknown despite improvements in European fundamentals and continued positive earnings momentum.

EMERGING MARKETS

NEUTRAL

We are maintaining our neutral tactical allocation to Emerging Markets. Valuations are attractive given expected EPS growth rates, but country selection remains key, especially as trade risks and currency impact from a higher dollar evolve over the rest of the year and into 2019. Global election uncertainty and policy direction are key risks. Active managers should benefit in that dislocations will likely provide attractive entry points for quality companies in a higher volatility environment.

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REAL ESTATE/REITs

UNDERWEIGHT

We continue to recommend an underweight to REITs and CRE due to elevated valuation and lower AFFO expectations amid heightened short-term sensitivity to higher interest rates within a late cycle environment.

PRIVATE EQUITY

UNDERWEIGHT

Low interest rates and a low return environment have continued to drive investor interest in private equity. Funds selling into this setting have benefitted from investor demand; however, those with current to near-term vintages are not finding valuations as favorable for new capital. If purchased properly, allocations to private equity should help buffer higher interest rates and heightened market volatility.

ENERGY

OVERWEIGHT

We continue to be bullish on energy equities due to investor pessimism, a lack of global capex, improving technicals, and inventory levels. Both WTI and Brent are setting highs as OPEC producers maintain production targets and sanctions have caused Iran's supply to come off quickly. U.S. production growth could slow towards year-end and early into next year. The two main constraints are pipeline takeaway capacity and production from aging shale basins. Lack of capex during the recent energy downturn years coupled with the elimination of the inventory surplus, propels oil prices in the long-term. Main Risks to the downside include, dollar strength, US- China trade war affecting demand, and if OPEC spare capacity is larger than expected. We recommend a tactical allocation to energy equities as an overweight position.

HEDGED STRATEGIES

OVERWEIGHT

We also recommend a full tactical allocation to Hedged Equity to diversify overall risk and long only beta exposure as the market reprices risk from higher interest rates and desynchronized economic growth. While the drivers for this allocation are similar to our Multi-Strategy and Market Neutral recommendation, fundamentally based equity strategies should also benefit. The main risk to our recommendation is the market continues on an upward trend. In this scenario, funds with lower net exposure will likely underperform on a relative basis.

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