

Asset Allocation Overview

Thoughts on Markets, the Economy, and Positioning

Geopolitics took center stage in Q1, as the conflict in Iran widened. The Strait of Hormuz garnered daily headlines, as Iran effectively closed one of the world's most important shipping lanes. Approximately 20% of the world's oil supply passes through the Strait, with refined energy products, fertilizer, helium, plastics, and other goods also disrupted. The price of crude oil spiked from a Q4 low of \$55 per barrel, reaching close to \$100 per barrel. Equity volatility followed suit, albeit modest in comparison. The S&P 500 declined -5% in March offsetting year-to-date gains in the process. Assets that were more sensitive to oil prices or equity risk fared worse in March, including growth equities, small caps, and international stocks. Traditional bonds fared better than stocks in March on a relative basis, but still fell -1.8% for the month, erasing year-to-date gains. The Bloomberg US Aggregate Bond Index finished the quarter effectively unchanged. Finally, the Federal Reserve opted to hold interest rates at current levels during their March meeting. The crosswinds of a multi-year, cooling labor market and price pressures stemming from energy will likely weigh on policy makers in the coming months. For now, the Fed is guiding a single rate cut through the end of 2026.

Key Talking Points

Real assets have been added to our asset allocation framework, beginning in Q2. Orion's investment team supports the conviction underpinning the asset class, including long-term diversification benefits, protection from unexpected inflation, and assets that have lower correlations to traditional stocks and bonds. These include natural resources, real estate, precious metals, industrial metals, global infrastructure, and broad commodities. Numerous secular tailwinds support the asset class in the near-term, including demand for AI related infrastructure, retrofitting and optimizing the US power grid, renewed defense infrastructure in Western Europe, Japan, and at home. An unsettled geopolitical backdrop also supports inflation-resistant assets and an overweight allocation to portfolios. Orion's investment team has been pleased with positioning and outlook elsewhere, including small cap stocks, which have outperformed large cap stocks over the trailing twelve months. We remain cautiously optimistic on risk assets, driven by healthy corporate earnings growth, tailwinds from AI, a resilient US consumer, low stress in credit markets, and an accommodative Federal Reserve.

POSITIONING - STOCKS	CHANGE	UNDERWEIGHT	NEUTRAL	OVERWEIGHT	RATIONALE
Domestic Equity			●		Healthy earnings growth, AI tailwinds, resilient consumer, lower interest rates
International Equity			●		Energy supply uncertainty; fiscal spending boost, weaker USD, improving earnings expectations
Emerging Markets			●		Trade impacts muted, record exports in China, tailwind for commodity exporters
Large Cap			●		AI capex, productivity gains, healthy earnings growth and balance sheets; elevated valuations
SMID Cap			●		Lower borrowing costs, AI broadening, attractive valuations; unsettled inflation
Growth			●		Growth has become expensive of late but remains attractive over the long-term
Value			●		Value stocks offering attractive downside protection during recent volatility

POSITIONING - REAL ASSETS	CHANGE	UNDERWEIGHT	NEUTRAL	OVERWEIGHT	RATIONALE
Real Assets				●	Unsettled geopolitical backdrop; secular tailwinds including reshoring of defense, AI infrastructure, and a renewed focus on energy optimization

POSITIONING - BONDS	CHANGE	UNDERWEIGHT	NEUTRAL	OVERWEIGHT	RATIONALE
Government Bonds			●		Improving rates, safe haven from equity market volatility; expanding US debt
MBS			●		Mortgage yields and spreads remain attractive, relative to Treasuries
Corporate Credit		●			Improved default risk for high yield, but credit spreads remain tight
Duration			●		Long-dated yields remain range bound over the past 12 months

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CALL

385.375.8650

EMAIL

contact@townsquarecapital.com

¹Source: Proprietary Orion data, as of 6/18/2024.

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