ASTOR INVESTMENT MANAGEMENT | FUNDAMENTALLY DRIVEN.

A Q&A into what we saw and where we are going.

FAQ

Frequently Asked Questions
2022 - 2023

Inside:

- **2022** Summary: *Biggest Contributor and Detractor*
- **2022** Performance: *Attributions, Market Overview*
- Outlook into **2023:** *Market anticipation, Fixed Income market insights, Equity market, and Inflation predictions*
- Astor's Positioning: **2022 - 2023**

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I. a. What has been the biggest attributor to performance throughout 2022?

Dynamic Allocation - Commodities, broadly, were a positive contributor. Overall asset allocation was the main driver of relative performance against the benchmark. The strategy began the year ~0.8 beta (to the S&P 500). As of this writing, we sit at just under 0.2 beta. While these adjustments did not occur at one point in time, the cumulative effect of methodical shifts away from risk assets helped reduce exposure to equities as markets. Within the fixed income part of the portfolio, a shift to lower duration exposure helped to reduce the impact of fixed income losses in longer duration positions.

I. b. What has been the biggest detractor to performance throughout 2022?

Dynamic Allocation - Even as the exposure was reduced in the strategy through the year,equities detracted the most from returns for the strategy. Broad technology exposure was the worst performer overall in the equity category of the strategy's holdings.

2022: Performance/Attributions/General Market Comments

II. a. Is there a segment of the market that has surprised you this year?

In general, broad asset categories (fixed income, equities, commodities) performed as you may expect given how the macro environment evolved in 2022.

Some things that could be categorized as a surprise however:

- The extent to which fixed income duration rallied in the second half of the year. While inflation may have hit its high point, higher prices persist.
- While not a total surprise given the run its had and the large increase in discount rates, it has been interesting to see the years long tech supremacy come to at least a temporary end. Tech still seems like the most dynamic part of the economy with little appetite on the part of the federal government to reign it in so we expect it will bounce back at some point.
- Energy stocks – a strong move in energy prices in the first part of the year supported strong returns in energy stocks, even as broad equity markets waned. Energy stocks have been resilient in the back half of the year even as energy prices have declined.

II. b. What do you think was the catalyst behind the market drawdown?

To simplify it, higher interest rates and inflation. These two worked hand in hand. Early-year declines were based on valuation adjustments on higher discount rates. Market multiple compression enhanced the sell-off as higher rates and overall costs threatened corporate margins. As these issues took hold, concern about the overall economy and direction of growth began to scare investors. Worsening economic growth and adeteriorating external environment (China, Europe) were close companions.

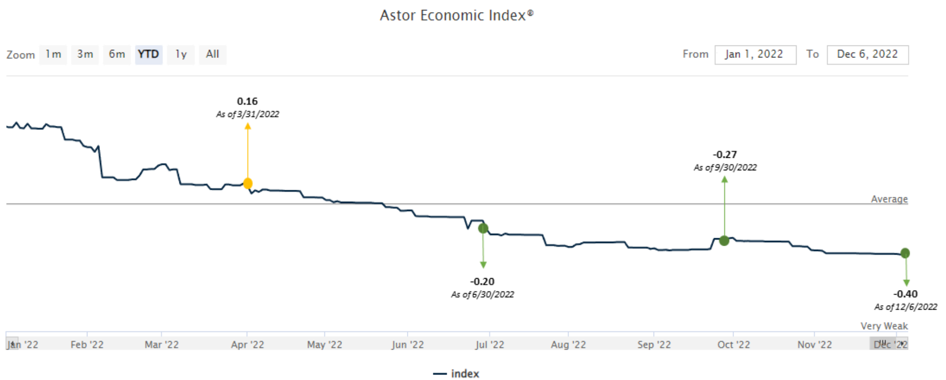
II. c. Why hasn't it rallied like in 2020?

- 2020 was an acute, exogenous event that resulted in a very sharp sell-off against the unknown. The present was uncertain and vaccine uncertainty was the biggest risk, the outlook for 2021 remained positive, interest rates were extremely low, and the government provided consumers with cash to spend. This year has been the opposite. Higher rates, higher costs, tightness in the labor market and uncertainty on how much and when the Fed reaches its terminal rate. The outlook for 2023 remains subdued.

- With all of this, market participants are faced with a wide range of potential outcomes over the next few months, with plausible scenarios for both easing or further tightening in monetary policy, as well as the potential for a benign slowdown in output or a hard landing. High conviction calls for equity appreciation are difficult against this macro backdrop. The Fed has also noted their plans to keep rates higher for longer, which was an absent factor in 2020.

II. d. What parts of the economy have affected the Astor Economic Index® (AEI) the most?

A moderating (although still tight) labor market, declining expectations for future growth, and weaker soft data (such as PMIs) all contributed notably to weakness in the Astor Economic Index® (AEI).



Source: Astor , NBER, Bloomberg, Data: 1/1/2022 - 12/31/2022. The Astor Economic Index® should not be used as the sole determining factor for your investment decision. There is no guarantee that the index will produce the same results in the future. An investment cannot be made in the index.

Outlook into 2023!

III. a. Could we see a repeat of 2022?

- A carbon copy is unlikely, but the markets could remain challenging as the Fed navigates a monetary storm. The weakness we saw in both equity and bond prices, as well as a surge in commodity prices, were pretty severe and reflected a dramatic paradigm shift from low inflation/cheap money.

- While the future is uncertain the Fed expects to tighten much less in 2023 than it did in 2022, this changes the economic background significantly. Market thoughts will probably drift toward easing in the second half of next year. The big unknown is how severe a slowdown we will see. The Fed expects a modest one, but it is a nice trick to slow things enough to subdue inflation but not enough to cause a severe recession.

- Recent positive returns in risk assets and longer duration fixed income suggest the market is pricing in something approximate to a soft landing, or, failing at that, a decline in inflation that would allow the Fed to moderate policy substantially.

- The risk to the consensus view (and thus the market) is that inflation proves to be persistent in 2023, or that growth stalls.

III. b. Is the worst over for the fixed income markets?

- The initial punch was severe. From here depends on the evolution of inflation. If, as seems most likely, the high for inflation is in, then the high for yields and rates may be in as well. The yield curve has moved to historic levels of inversion. If it is to move back positive, it is plausible longer duration Treasury rates could resume a move back toward 2022 highs.

- Should inflation prove persistent, we could expect a repricing back towards the levels seen in Q3 2022, but not necessarily of the same magnitude as earlier this year.

III. c. Is the worst over for the equity markets?

- This depends on rates, and how hard the economy puts on the breaks in early 2023. Much of the decline in equities markets in 2022 can be attributed to a higher discount rate (higher monetary policy), with some moderation in economic activity.

- While equity prices have removed some ‘fluff’, multiples are not extremely cheap. The consumer may be less likely to keep paying the higher prices passed down from corporate America if the macro backdrop falters.

- This could provide additional margin pressure and likely push market multiples lower for a time. It is plausible that the market has yet to consider the full impact of a recession in 2023 on equity prices. Lower earnings to go with lower multiples would not be a good combo.

III. d. What do you need to see to increase equity in 2023?

- We will need to see an uptick in growth expectations looking forward. Stronger fundamentals, irrespective of inflation, will be needed – a scenario that we believe is possible. The macro data trends have not been positive on the whole, especially in recent reports. Labor markets have held up relatively well. Whether that continues into 2023 remains to be seen.

- Note that risk assets could be added regardless of the path of inflation to the extent that the Fed’s reaction function does not crush future growth.

Positioning for now?

IV. a. As of the Investment Committees’ last meeting of the year (in December), you have 17% equity in ADA – why do you feel this is the appropriate amount of risk for now?

Hard to believe it’s been almost a year. The strategy started in 2022 with much

more equity (~80%). The outlook for the macro economy began to moderate early in the year as higher inflation and the prospects for higher rates and a reversal of course from QE took hold. Fast forward, we have seen the global economy weaken substantially.

Because of forward-looking data, we see the risks still outweigh the rewards inthe stock market today. We foresee a hard landing or stagflation somewhat more likely than a soft landing or "immaculate" disinflation. Expectations for lowered earnings estimates have increased, somewhat mirroring the forward-looking macro-outlook. At the inflection point, we would expect to see that change first.

IV/ b. As a PM of the ADA strategy- where do you see it fitting into a client portfolio?

Dynamic Allocation can be a core complement to traditional portfolios, with the ability to shift equity exposure based on the macro environment. With a base-case allocation balanced between equity and fixed income, its focus is on moderate risk, which has the potential to make it a fit for most client portfolios that are concerned about managing risk. Its long-term risk profile (since inception standard deviation) is lower than the 60/40 (S&P 500/Bloomberg USAggregate Bond) benchmark and has a substantially lower drawdown.

DISCLOSURES

BENCHMARK INFORMATION & DEFINITION:

Standard & Poor's 500 Total Return Index: *The S&P 500 Index measures the performance of 500 large cap stocks, which together represent approximately 80% of the total equities market in the United States. The Total Return calculation includes the price-plus-gross cash dividend return. The S&P 500 is registered trademark of McGraw Hill Financial. An investment cannot be made directly in an index.*

The Bloomberg U.S. Aggregate Bond Index: *U.S Agg is a abroad-based index representing the dollar-denominated, investment grade bond marke tand includes Treasuries, government securities, and mortgage securities.*

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