SOLAS WEALTH

PLANNING • INVESTING • COACHING

NOVEMBER 2022 PORTFOLIO UPDATE

ASSET ALLOCATION UPDATE

Current Asset Allocation – November 2022

		← Less Exposure			More Exposure →	
		Strategic Only	Under-weight	Baseline Allocation	Over-weight	Max Allocation
Equities	U.S. Large Cap	■				
	Foreign Developed	■				
	Emerging Market	■				
Quasi-Equity	Real Estate	■				
Bonds	U.S. Treasury	■				
	International Treasury	■				
	Inflation-Protected	■				
Alternatives	Hedge Strategies	■				
Liquid	Short-Term & Cash Equivalents					■

Adjustments can vary across strategies depending on each strategy's objectives.
What's illustrated above most closely reflects allocation adjustments for the Growth Strategy.

■	No change month-over-month
▲	Increase month-over-month
▼	Decrease month-over-month

U.S. Equities: Exposure will not change from its minimum allocation, as both the intermediate- and long-term timeframes remain in downtrends.

International Equities: Exposure will not change from its minimum allocation, as both foreign developed and emerging markets remain in downtrends across both timeframes.

Real Estate: Exposure will not change from its minimum allocation, as both the intermediate- and long-term timeframes remain in downtrends.

U.S. & International Treasuries: Exposure will not change and is at its minimum allocation due to downtrends across both timeframes.

Inflation-Protected Bonds: Exposure will not change and is at its minimum due to downtrends across both timeframes.

Alternatives: Exposure will not change and is at its minimum allocation due to downtrends across both timeframes.

Short-Term Fixed Income: Exposure will not change, as it is already at its max allocation due to previously taking on exposure from equities, real estate, alternatives, and longer-duration fixed income.

MONTHLY NOTE

"…learn enough from history to bear reality patiently, and to respect one another's delusions." –Will Durant

There's been a lot of talk this year about uncertainty. Specifically, about how markets hate it. We think it's beneficial for all investors to remember that the market is comprised of market participants (i.e., people), and it is actually us humans who hate uncertainty. Psychology even defines certainty as an emotional state, not an intellectual one.

In our view, it is wasted effort to attempt to create certainty, especially in the short run around outcomes. We can however create certainty of process, and this is our goal at Solas Wealth. The irony is that by focusing on process, you may ultimately improve outcomes. Focusing on process only may not be as emotionally satisfying in the short term, but one's long-term results are likely to be improved and more consistent.

In this month's note, we provide context to the longer-term trend in equities through the lens of our systematic investment process. At the end of the day, we think our strategies can add tremendous value, especially when considered as infrastructure, like a utility that's left to run behind the scenes, dependably and repeatably.

But first, here's a summary of our take on what transpired in the markets in October.

Asset-Level Overview

Equities & Real Estate

After making a new annual low early in the month, U.S. equities posted positive returns in October, led by the energy and industrial sectors. However, with the exception of the energy sector, all equity sectors in the U.S. remain entrenched in downtrends. As a result, all our portfolios will continue to have minimal exposure at the asset class level. Within strategies and products that incorporate single stocks, exposure will increase, particularly within U.S. small- and mid-caps.

Looking internationally, developed economies experienced rising equity prices in October. Conversely, emerging markets will experience yet another down month, led by weakness in Chinese stocks, which close the month near 15-year lows. Our portfolios continue to be minimally exposed to international stocks and will be until conditions improve.

Real estate securities have managed to eke out a small gain on the month, but conditions continue to be difficult. As inflation continues to run historically high, correspondingly

higher interest rates have had a considerable negative affect on U.S. and global real estate. Our portfolios remain at their minimum exposure to this asset class.

Fixed Income & Alternatives
What can you say about fixed income, except that things are UGLY? While some pockets, such as inflation-protected and global bonds, stopped dropping at least for now, U.S. bonds are on pace for yet another down month. This asset class seems intent on challenging stocks for worst-performing, which surprises many investors given its historically low-volatility characteristics. As a result, our portfolios remain at minimum exposure across all areas of fixed income except ultra-short duration.

Gold specifically and commodities more broadly continued to drift relatively sideways to lower, for the most part, with the obvious exception being energy. While relatively less weak than other assets, gold has not done enough to warrant uptrends. As a result, all portfolios remain at their minimum allocation.

3 Potential Macro Catalysts for Trend Changes

Rinse, Repeat: The Federal Reserve is set to increase the baseline interest rate by 0.75% for the fourth time at their Nov. 1-2 meeting. However, officials plan to begin discussing whether to slow the pace of rate increases in the future, according to a report by The Wall Street Journal. Some members of the Federal Reserve are wary that they may be pushing the economy too far, which might tip the United States into a recession.

Elevator Down: The housing market continues to trend down. Rising mortgage rates and concerns about recession have caused buyers to scale back, sending home sales downwards and bringing down prices. The S&P CoreLogic Case-Shiller National Home Price Index fell 1.1% in August from July, the biggest decline since 2011.

Bigger Deductions! One positive side-effect of rampant inflation is that the IRS is raising tax brackets and standard deductions by 7%. The standard deduction will go to $27,700 for married couples and $13,850 for individuals, allowing more earnings to be shielded from income taxes. The threshold for the estate tax also jumped to $12.92 million for 2023.

Under the Surface of a Bear Market Rally

"We must all suffer one of two pains: the pain of discipline or the pain of regret." –Jim Rohn

Perhaps right on cue from last month's Co-Founders' Note, U.S. stocks produced a noticeable bear market rally in October. On the surface, this was a reprieve from the steady drumbeat of declining prices experienced so far in 2022.

However, it takes only a cursory look beneath the surface to realize that little has changed over the last 30 days. From a fundamental perspective, inflation data continues to come in higher than expected. Rates continue to rise as a result. Russia continues to wage its war with Ukraine. Oil prices remain relatively high with plenty of support for even higher prices. Oh, and throw in the uncertainty of a coming election in the U.S.

You have plenty ingredients for continued weakness in capital markets.

Our systematic investing approach, which take a quantitative look at price trends, reinforces the unfavorable economic and political climate. In fact, our trend signals turned down before the fundamental data reflected the dire conditions. Since the end of January, we have been generally underweight equities. In fact, we have been at our minimum allocations since the end of April.

Despite the increases in October, major indexes year-to-date continue to repeat the same patterns of new lows followed by lower highs. Until this cycle is broken, our research and systematic investing rules tell us that moving equity exposure back to even our baseline allocations is simply too much risk for the potential reward.

When you are exposed to falling asset prices and have no plan for how to respond, years like 2022 can be agonizing. That's typical of bear markets.

Our strategies are different because they follow repeatable rules for making allocation decisions, and we are able to clearly communicate the how and why behind our positioning, now and for future environments. This is important because investors sometimes incorrectly project future performance based on what they feel right now. If they see one of our strategies down double digits, they might infer a certain level of negative performance for the future. This despite that most of our risk-managed asset allocation and single stock strategies are beating their appropriate benchmarks year-to-date by, in many cases, several hundred basis points.

It is important for our clients to understand that even though we fell by a certain amount in January, it doesn't mean that's how we are positioned now. The beauty of systematic investing powered by trend following is that our positioning can change quickly depending on market conditions. And since we're transparent about our process and positioning, you can verify we're walking the walk for yourself: just ask to see how different

our positioning for January 2022 was compared to where we'll be in November, and we'll happily show you.

We can't predict if declines will continue. However, historical data makes us believe that a portfolio with low equity exposure and mostly allocated to ultra-short term bonds, like we have now, will experience only a fraction of the decline if markets close 2022 in the same manner they have acted all year. We are content with our allocations because we know that, just like we quickly reduced exposure earlier this year, we will increase it if things suddenly improve. Not only does this keep us positioned well, in our opinion, but also give us great peace of mind.

We view one of the most impactful elements of our investment process to be its repeatable, consistent infrastructure. An analogy we often use is that we want to operate like a utility. For example, electricity makes our lives better in countless ways, and we only stop to think about it when it's missing. That is how we want our investment process to work in terms of ubiquitous risk management: it should deliver few negative outlier events or times when the lights don't turn on. We also want our service model to operate like a utility for our client partners: dependable, consistent, and trustworthy.Best,

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