SEQUENT
REAL ESTATE + WEALTH MANAGEMENT

Investment Report: Spring 2023

Alternatives in your portfolio may help boost returns, manage risks, and help fight the inflation dragon.

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“The 60/40 portfolio faces new challenges after serving investors well over a 40-year deflationary time period.” – Ray Dalio, Bridgewater Associates

First, alternative investments can provide access to new opportunities that may not be available through traditional investments. For example, private equity and venture capital can provide exposure to companies that are not yet listed on public markets. Private real estate on the other hand, which will be a focus of this report, can offer the potential for income and capital appreciation.

Second, alternative investments often have low or negative correlations with traditional asset classes like stocks and bonds. As seen in the chart below, real estate has shown over time to have very low correlations to the stock and bond market. This means that when traditional asset classes are performing poorly, alternative investments may provide a buffer against losses. This can help investors maintain the overall value of their portfolio over the long term, even during times of market volatility.

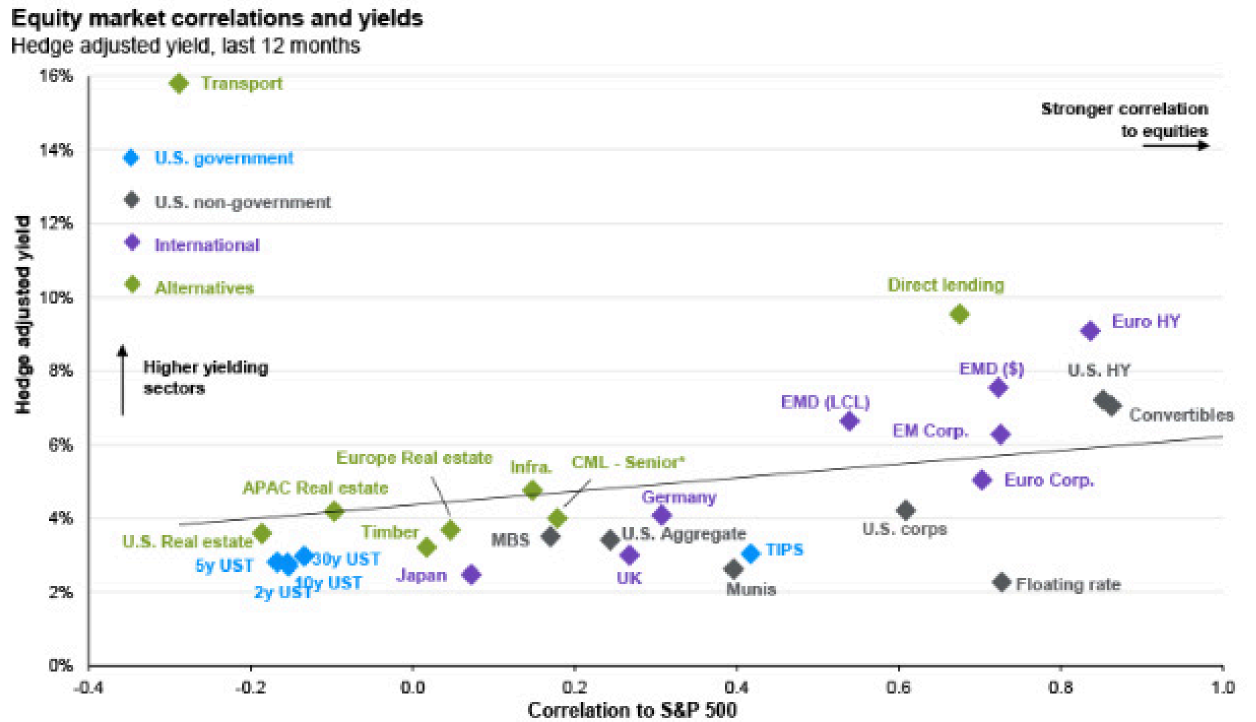
In this new inflationary environment, how are large institutions positioning their portfolios differently from individual investors?

One key lesson when observing how large institutions invest is that they tend to look beyond the public markets & traditional asset classes to build a more robust portfolio. Amongst professional investors it is well known that institutional investors, endowments & foundations have long looked past traditional stocks & bond investing for broader diversification, risk management and seek to obtain enhanced returns. For example, the University of California “General Endowment Pool” has almost 50% of its $18 billion total value invested in what are commonly named “Alternative Assets” as of 6/30/2022.

In addition, Pension & Investments Online highlighted a survey released late in 2022 by professional services firm Ernst & Young. Among other revelations, the 2022 EY Global Alternative Fund Survey found that some 75% of institutional investors felt their alternative asset managers “met or exceeded performance expectations during a challenging and volatile market period, successfully protecting capital in down markets while positioning for long-term income generation.”[1]

1 Past performance is not a guarantee of future results. Potential cash flows/returns/appreciation are not guaranteed and could be lower than anticipated.

Looking beyond traditional
Equity & Bond Market Correlations and Yields



Source: Bloomberg, Gilberto-Levy, NCREIF, MSCI, FactSet, ICE, J.P. Morgan Asset Management. *CML is commercial mortgage loans. Fixed income shown above are represented by Bloomberg indices except for EMD and ABS – U.S. Aggregate; MBS: U.S. Aggregate Securitized - MBS; U.S. corps: U.S. Corporates; Munis: Municipal Bond; U.S. HY: Corporate High Yield; TIPS: Treasury Inflation-Protected Securities (TIPS); Floating Rate: U.S. Floating Rate; Convertibles: U.S. Convertibles Composite; ABS: J.P. Morgan ABS Index; EMD ($): J.P. Morgan EMBIG Diversified Index; EMD (LCL): J.P. Morgan GBI EM Global Diversified Index; EM Corp: J.P. Morgan CEMBI Broad Diversified Index; Euro Corp: Euro Aggregate Corporate Index; Euro HY: Pan-European High Yield Index; U.S. Real Estate: NCREIF Property Index – ODCE ; Europe Real Estate: Market weighted-avg. of MSCI Global Property Fund Indices - U.K. & Cont. Europe; APAC Real Estate: MSCI Global Property Index - Asia-Pacific; Global infra.: MSCI Global Quarterly Infrastructure Asset Index (equal weighted blend; U.S. Direct Lending: Cliffwater Direct Lending Index; Timber: NCREIF Timberland Property Index (U.S.); Transport returns and yield are derived from a J.P. Morgan Asset Management index; CML – Senior: Gilberto-Levy Commercial Mortgage Performance Aggregate Index. Convertibles yield is based on the U.S. portion of the Bloomberg Global Convertibles. Country yields are represented by the global aggregate for each country. Yield and return information based on bellwethers for Treasury securities. U.S. Real Estate yield is calculated using the MSCI Global Property Fund Index – North America. Correlations are based on quarterly return over the past 10 years through 9/30/2022. All non-alternative yields are as of 11/30/2022. Alt yields are as of 9/30/2022. Quarterly return correlations and yields for infrastructure are as of 6/30/2022.
Data is based on availability as of November 30, 2022.

Last, diversifying with alternative investments can help improve the overall diversification of an investment portfolio. By holding a mix of asset classes that have low correlations with one another, investors can potentially reduce the overall volatility of their portfolios which may help increase their chances of achieving their investment goals over the long term. Below shows how by adding the right mix of alternatives to portfol os, historically, it enhanced investor returns and helped to lower volatility.

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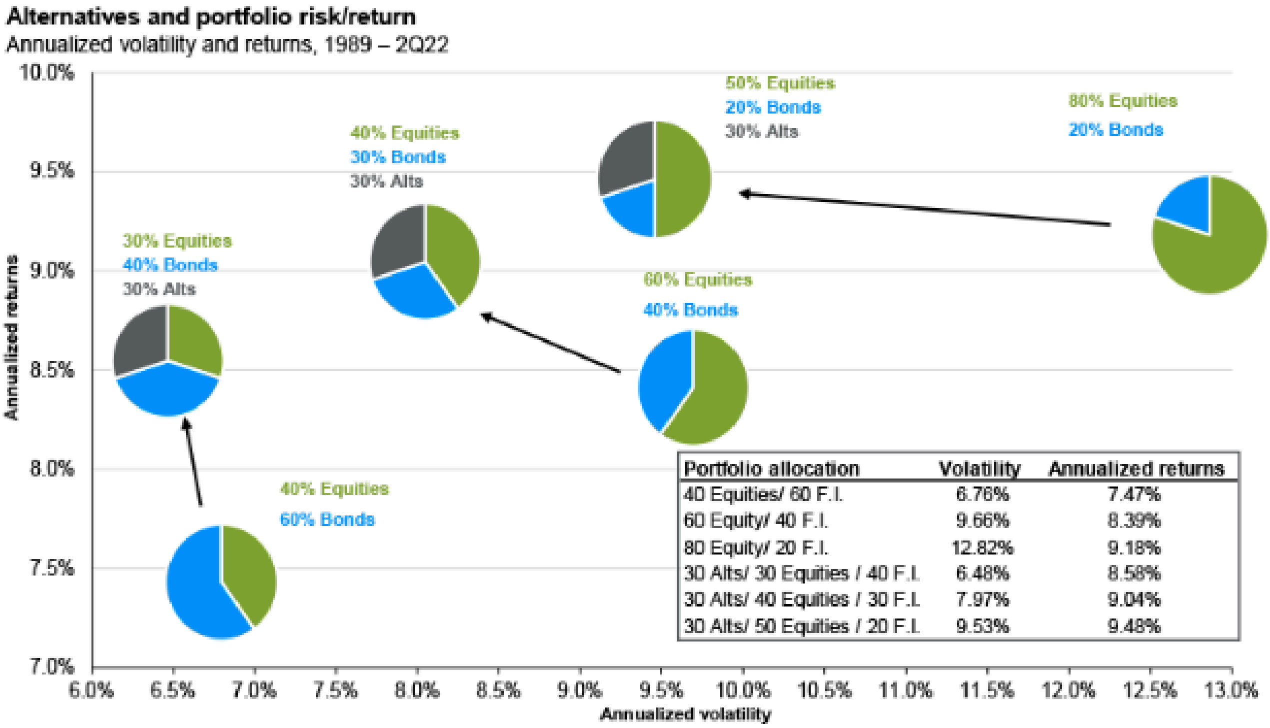
What can we learn from Advanced Portfolio Diversification?



Portfolio allocation	Volatility	Annualized returns
40 Equities/ 60 F.I.	6.76%	7.47%
60 Equity/ 40 F.I.	9.66%	8.39%
80 Equity/ 20 F.I.	12.82%	9.18%
30 Alts/ 30 Equities / 40 F.I.	6.48%	8.58%
30 Alts/ 40 Equities / 30 F.I.	7.97%	9.04%
30 Alts/ 50 Equities / 20 F.I.	9.53%	9.48%

Source: Bloomberg, Burgiss, HRFI, NCREIF, Standard & Poor's, FactSet, J.P. Morgan Asset Management. Alts include hedge funds, real estate, and private equity, with each receiving an equal weight. Portfolios are rebalanced at the start of the year.
Data is based on availability as of November 30, 2022

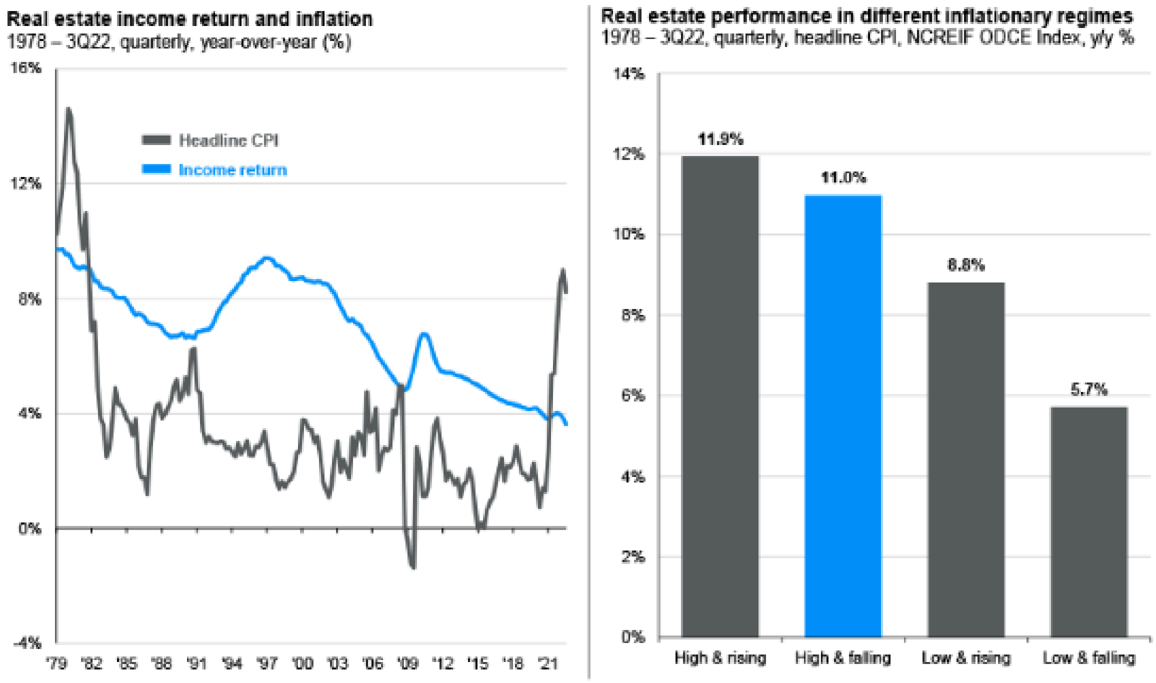
Overall, diversifying with alternative investments may help provide investors with several benefits, including the potential for higher returns, better diversification, and improved risk management. While these types of investments can be complex and may not be suitable for all investors, they can be an important part of a well-diversified investment portfolio.

Inflation & Institutional Private Equity Real Estate: Key Considerations

The public markets were down substantially to the downside in 2022, but private market valuations have lagged and have been slower to adjust. We believe the private markets will lag two to three-quarters behind public markets as write-downs start to appear. We believe this suggests that declining valuations will bring opportunities that may begin to emerge in 2023.

Forecasts are inherently limited and should not be relied upon as an indicator of future results. Past performance is not a guarantee of future results.

REAL ESTATE AND INFLATION



Source: BLS, NCREIF, FactSet, J.P. Morgan Asset Management. "High" inflation is defined as any year-over-year headline CPI reading above the historical median, while "low" inflation is defined as any year-over-year headline CPI reading below the historical median. The median y/y headline CPI for period between 1978 to 3Q22 is 2.91%.
Data is based on availability as of November 30, 2022.

As we look ahead, private real estate assets seem well-positioned to deliver stable cash flows and public market diversification, even if capital values decline. During this next cycle, it is important to focus on a few important factors when investing in private real estate.

First, you should consider owning quality assets. High occupancy Class A properties in strong markets which are characterized as core and core plus.

Second, Commercial property types that perform well in different market cycle phases are often referred to as “needs-based” asset classes. These include properties like multifamily apartments, senior housing, manufactured housing, and healthcare, which most people consider essential during good times and bad.

This does not suggest other properties like industrial and self-storage will under-perform during late-cycle phases. Self-storage has always been considered reces-sion-proof. But needs-based assets have historically proven to be resilient.

Finally, investors can further insulate themselves from late-cycle economic conditions by diversifying their portfolio with commercial properties in different geographies. History has shown that only some primary or secondary markets are impacted similarly during slow growth periods. Creating a diversified commercial real estate portfolio to reduce location concentration will help manage risk.

In Conclusion

Recessions can take many forms, as we're learning in real-time today. The recession of 2008-09 looks much different than the recession we are entering because of the COVID-19 crisis. The direction and duration of this recession remain to be seen. We know that it will have an impact on the commercial real estate industry at large but suspect it may have a greater impact on some property types more so than others. It could take months for investors to really understand the full depth of the pandemic's impact on commercial real estate. Opportunistic buyers may find that price adjustments take even longer to materialize.

While few investors predicted a global health crisis, there were other indicators that a recession was looming on the horizon for some time now. Those who have carefully crafted a portfolio that seeks to be a recession-resilient portfolio may be better positioned to weather this downturn, regardless of how long it lasts. If suitable, we feel that allocating a percentage of your portfolio to private alternative real estate may have the potential to help you create a portfolio that helps you weather the market's ups and downs.

Eric Scaff
Founder, Managing Director

Charles Strickler
Managing Director

Disclosures:

Because investor situations and objectives vary this information is not intended to indicate that an investment is appropriate for or is being recommended to any individual investor.
This is for informational purposes only, does not constitute individual investment advice, and should not be relied upon as tax or legal advice. Please consult the appropriate professional regarding your individual circumstance.
Diversification does not guarantee a profit or protect against a loss in a declining market. It is a method used to help manage investment risk.

Statements concerning financial market trends are based on current market conditions, which will fluctuate. Past performance is not indicative of future results. Forecasts and estimates are inherently limited and do not guarantee future results.

Investing in alternative assets involves higher risks than traditional investments and is suitable only for sophisticated investors. Alternative investments are often sold by prospectus that discloses all risks, fees, and expenses. They are not tax efficient, and an investor should consult with his/her tax advisor prior to investing. Alternative investments have higher fees than traditional investments and they may also be highly leveraged and engage in speculative investment techniques, which can magnify the potential for investment loss or gain and should not be deemed a complete investment program. The value of the investment may fall as well as rise and investors may get back less than they invested.

All investments may not be suitable for all investors. Investments may involve a high degree of risk and should only be considered by investors who fully understand all potential associated risks. Prospective investors should perform their own due diligence carefully and review the “Risk Factors” section of any prospectus, private placement memorandum or offering circular before considering any investment.

All bonds carry some degree of “credit risk,” or the risk that the bond issuer may default on one or more payments before the bond reaches maturity. In the event of a default, you may lose some or all of the income you were entitled to, and even some or all of the principal amount invested. Other risks may include interest rate risk, inflation risk, reinvestment risk, and liquidity risk.

Indices are unmanaged and investors cannot invest directly in an index. Unless otherwise noted, performance of indices does not account for any fees, commissions or other expenses that would be incurred. Returns do not include reinvested dividends.
The S&P® 500 Index is a widely recognized capitalization-weighted index that measures the performance of the large-capitalization sector of the U.S. stock market.

The Consumer Price Index (CPI) measures the overall change in consumer prices based on a representative basket of goods and services over time and is the most widely used measure of inflation.

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