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Freedom portfolio positioning in a more volatile market

Heightened volatility such as we have seen early in 2022 – and may continue to see – is an important consideration in the Freedom portfolio construction process.

The equity markets are off to a bumpy start in 2022, with concerns for elevated inflation, shifting monetary policies, ongoing supply-and-demand pressures and geopolitical tension contributing to increased market volatility. Understanding that volatility is part of investing, the Asset Management Services Investment Committee (AMS IC) positions Freedom portfolios in an attempt to maximize return potential while considering the amount of downside risk a client can accept.

KEY TAKEAWAYS

The capital markets experienced increased volatility to start 2022, driven by uncertainty around inflation, supply chains, monetary policy and the war in Ukraine.

Freedom portfolios are purposefully constructed to target a certain level of return based on the amount of downside risk a client can accept.

With the expectation economic growth will continue, albeit at a slower pace, Freedom portfolios are overweight U.S. equity, underweight international equity and underweight fixed income.

After three years of double-digit gains, the S&P 500 index experienced a double-digit loss – what analysts refer to as a correction – through the first two-plus months of 2022. The index, which tracks the 500 largest U.S. companies, was down roughly 12.0% for the year on March 14, though it recouped nearly half of its losses in the following days.

This patch of heightened volatility, which is affecting most areas of the market, has been driven by a number of factors. The inability of global supply chains to keep pace with the increased demand for goods has continued to drive inflation at rates not seen in decades, prompting the U.S. Federal Reserve to raise interest rates. These existing pressures have been intensified by the war in Ukraine: Nations around the world have used economic measures to voice their disapproval of Russia, resulting in even tighter supply chains and climbing oil prices.

While the scenes from Ukraine are unsettling, it is important to remember that such events do not typically drive sustained market downturns. Since 1941, we have experienced 12 similar geopolitical events and the average return for the S&P 500 six months later was roughly 5.0%.

FREEDOM POSITIONING

Arguably the most important element in constructing Freedom portfolios is asset allocation – the mix of asset classes that serves to mitigate risk and minimize volatility. Many factors must be considered in determining the appropriate allocation for a portfolio's objective, be it conservative, balanced or growth. Our goal is to attempt to maximize return for each objective's risk budget – the amount of risk the client is willing and able to accept.

While each objective has an allocation target, the AMS IC occasionally decides to purposefully overweight or underweight individual asset classes when it is considered strategically appropriate.

For equities, the committee's investment process prefers asset classes with attractive fundamentals, good quality and profitability, and positive sentiment. Fixed income weightings, when it comes to corporate bonds, are managed by positioning for the right maturities and exposures along the quality spectrum.

Currently, Freedom portfolios own a little more equity than normal and a little less fixed income. The equity overweight is to domestic equity, primarily U.S. large caps but also U.S. small- to mid-caps, based on the expectation the U.S. economy is well-positioned for additional growth relative to the rest of the world. Portfolios are underweight non-U.S. developed markets such as Europe and Japan, as well as emerging markets such as China.

A slight underweight to fixed income reflects the AMS IC's belief that equities are positioned to outperform, though bonds remain attractive as a diversification tool, especially during an equity downturn.

LOOKING AHEAD

The AMS IC favors a resilient growth outlook for the U.S. relative to the rest of the developed world, though the pace of U.S. growth is likely to be slower than it was in 2021. The war in Ukraine is likely to affect Europe more than the U.S. or other world economies. With the U.S. Federal Reserve ready to raise interest rates in support of a strengthening economy, and to help curb inflation, bond prices are expected to see further pressure.

The AMS IC evaluates Freedom portfolios on a regular basis and will continue to monitor these factors and more. Any additional changes would occur in an attempt to earn the best possible return for the amount of downside risk the committee is willing to tolerate, in alignment with portfolio objectives and client goals.

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It is important to review the investment objectives, risk tolerance, tax objectives and liquidity needs before choosing an investment style or manager. All investments carry a certain degree of risk and no one particular investment style or manager is suitable for all types of investors; you may incur a profit or a loss. Past performance is no guarantee of future results. There is no assurance that any investment strategy will be successful.

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- Fixed income securities (or "bonds") are exposed to various risks, including but not limited to credit (risk of default or principal and interest payments), market and liquidity, interest rate, reinvestment, legislative (changes to the tax code), and call risks.
- There is an inverse relationship between interest rate movements and fixed income prices. Generally, when interest rates rise, fixed income prices fall and when interest rates fall, fixed income prices generally rise. Short-term bonds with maturities of three years or less will generally have lower yields than long-term bonds, which are more susceptible to interest rate risk.
- Please note these portfolios may be subject to state, local and/or alternative minimum taxes. You should discuss any tax or legal matters with the appropriate professional.
- International investing involves special risks, including currency fluctuations, different financial accounting standards, and possible political and economic instability.
- Investing in emerging markets can be riskier than investing in well-established foreign markets. Emerging and developing markets may be less liquid and more volatile because they tend to reflect economic structures that are generally less diverse and mature and political systems that may be less stable than those in more developed countries.
- Investing in small-cap stocks generally involves greater risks and, therefore, may not be appropriate for every investor.
- Stocks of smaller or newer or mid-sized companies may be more likely to realize more substantial growth as well as suffer more significant losses than larger or more established issuers.
- These portfolios may be subject to international, small-cap and sector-focus exposures as well. Accounts may have overweighted sector and issuer positions, and may result in greater volatility and risk.
- Companies in the technology industry are subject to fierce competition, and their products and services may be subject to rapid obsolescence.

In a fee-based account, clients pay a quarterly fee, based on the level of assets in the account, for the services of a financial advisor as part of an advisory relationship. In deciding to pay a fee rather than commissions, clients should understand that the fee may be higher than a commission alternative during periods of lower trading. Advisory fees are in addition to the internal expenses charged by mutual funds and other investment company securities. To the extent that clients intend to hold these securities, the internal expenses should be included when evaluating the costs of a fee-based account. Clients should periodically reevaluate whether the use of an asset-based fee continues to be appropriate in servicing their needs. These additional considerations, as well as the Freedom fee schedule, are listed more fully in the Client Agreement and the Raymond James & Associates Wrap Fee Brochure.

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