



Life with inSight podcast series

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Navigating the Financial World in the Face of a Turbulent Geopolitical Landscape

Mark: Hello everyone. I'm Mark Teitelbaum of Equitable's Advanced Markets Team, and I'm happy to be hosting this edition of Equitable's award-winning podcast series Life with inSight. Our goal is to provide you with timely, informative, and valuable information that you can use in your practice when meeting with clients and other financial professionals.

We focus on state-of-the-art subject matter delivered by some of the most distinguished people in our industry today. Joining me today is one of those individuals, our own Ken Kozlowski. Let me provide a little background on Ken. Ken Kozlowski is both a certified financial planner, CLU and CHFC. Mr. Kozlowski is also a Managing Director of the Equitable Life Insurance Company and has served as Executive Vice President and Chief Investment Officer of the Equitable Investment Management Group since June, 2012. He's had the primary responsibility for the asset allocation, fund selection, and the rebalancing of Equitable's funds since 2003.

Ken, thanks for joining us today.

Ken: Thanks, Mark. It's great to be here.

Mark: Our topic of the discussion in this session is navigating the financial world in the face of a turbulent geopolitical landscape. And as we all have seen in recent months, there's been a very volatile stock market affected by a number of outside influences, not the least of which are the lingering effects of the pandemic inflation and the recent war on Ukraine and its impact on the world's economy.

For starters, in light of all this, what underlying themes are you encountering in the market today?

Ken: Thanks again, Mark. It's great to be here. And I just came from an Equitable board meeting for our trust last week. And I opened that meeting with a quote, and the quote is, "There are decades when nothing happens and weeks when decades happen."

And this is a quote from Lenin, and it's not John Lennon; it's the other Lenin. But so much has happened over the last number of weeks. We've got a shooting war in Europe. We've got an incredible spike in energy prices with WTI, you know, hovering over a hundred dollars and with its subsequent impact on inflation and CPI right now has a seven or eight handle, and in the mix, we've got an announcement by the Fed that says, you know, the next seven meetings, they're going to be raising rates. And all this kind of points to challenges going forward, and how do we navigate that? And I think that when you look at different metrics... For one, I'll start with the shape of the yield curve.

I mentioned that the seven interest rate hikes that are mapped out over the next year. And what you're seeing with the yield curve is a very distinct high on the short end and the spread between the 10-year and the 30-year right now is under 20 basis points. And what is that telling you? And when you look out, I think one of the things you gotta be cognizant of is it may be telling you that growth is going to become scarce at some point in the future.

And the yield curve generally is a forward-looking indicator. And that's something to, you know, think about. And we've had a very pronounced growth versus value theme that we're monitoring, as you know, growth over the long-term, the last five years, and even 10 years has outperformed value.

And that's a function of the performance that you've seen in some of those FAANG names. And the fact that if you look at the Russell 1000 growth, if you look at the top five or six names, they make up 40% of the benchmark, and a couple of things contributed to that. You've got the stimulus, you had very accommodative monetary policy, and now with the announcement and you saw this trend late in 2021, where you started to see value outperform, and you saw the yield curve on the front end go up, and you saw the flattening that occurred, there wasn't a parallel shift in the yield curve. And then you had these external events, like the war in Ukraine with its impact on energy and those items beginning late fall last year, you saw a tremendous shift from growth to value where value really started to outperform growth. So that's something to keep in mind. You've got energy, the best performing sector in the S&P, you've got the financial sector doing very, very well. Also, in terms of sectors within the S&P, that's a function of interest rates going up and banks getting a bid.

So that's one theme, the shape of the yield curve, and inflation. Inflation kind of goes hand in hand with the shape of the yield curve, because. What the yield curve's telling you is some people are interpreting it as, well, maybe inflation won't be as sticky as people thought, because middle of last year you had Chairman Powell talk about the fact that the inflation that we're seeing must be transitory. But obviously with the seven interest rate increases, you know, he's doing his best to combat that. And we're all feeling it at the pump at the grocery store and a couple of themes there in terms of the fact that unemployment still remains relatively low.

The unemployment rate right now is about 3.8%. The consumer hasn't really had any indication of changing their behavior in a big way. And we all know that the consumer is 70% of the economy, but the yield curve is telling you something with growth. Looking out into next year, inflation looks like it's going to be stickier than people anticipated.

We're hearing from a lot of our sub-advisors that they're starting to lower their estimates for growth going into next year. And what you're seeing in commodities, and it's not only energy, but I think one of the things to keep in mind, too, that really isn't talked too much about is that in Mariupol, they had a huge steel factory, that was a, a very large producer of steel. Steel has tripled in the last two and a half years. And 60% of every automobile made is still made out of steel. So you're seeing inflation in a lot of places. Not only in energy and food, but other commodities as well, which is impacting everybody.

Right now, we've got almost relatively full employment. People that want to have a job in most cases can find a job, but as always, we're looking out and looking at how these themes can impact your investment strategy. So those are the major high-level themes that we're looking at currently. And those are the items that we're really focusing on.

Mark: So given that, Ken, are there areas that an investor can look at during this period?

Ken: Sure. And I think people are... What I hear is most people are concerned about fixed income. Because for decades now, you've had interest rates coming down since what happened in the '70s, and that is not the case. And when you look at, again, the shape of the yield curve and the fact that inflation is high and probably will be for the near term, anyway, what do you do in the fixed income space? And I know there's been a lot of talk about the challenges of a 60/40 portfolio and is fixed income going to give you that diversification that you need within a strategy.

And I think that it's a great time to focus on an active fixed income strategy. And it's probably a great time to talk to your financial advisor to get an active fixed income strategy that has that flexibility to be able to move in different sectors, going up and down the duration spectrum and have that flexibility rather than just looking at a benchmark or an index.

To be able to navigate that time, I think active fixed income is really a great place to focus on. And when I talked earlier about value versus growth, the shape of the yield curve is showing you that growth is going to become more scarce. And when growth becomes more scarce, typically that's a time to look at more high-quality growth.

And when you look at how growth has outperformed value, I think some of that has been attributable to the massive liquidity that easy monetary policy has afforded it. And that growth, you're going to be a bit more selective

in terms of those areas of growth. That you could focus on. And when I say high-quality growth, I mean companies or asset classes that have a very strong record of earnings, sustainability, equity income strategies, strategies where you have dividend payers, those strategies were out of favor for very long, because everybody was just focusing on the high flyers and the FAANG stocks.

And now, with growth, relatively starting to underperform value, and we'll see how long this trend lasts, but when you look at other metrics in the marketplace, now those two areas could be fertile areas to navigate this particular environment

Mark: Ken, thanks. One of the things that I've seen with Equitable's investment management group is some of the work that you've done to reexamine the 60/40 portfolio, and what I've seen validates this as still a very viable mix, particularly for retirees. Would you care to comment on that?

Ken: Sure. The 60/40 portfolio, and I know in the press there's been some articles about "is the 60/40 still valid," especially given the points I just made about fixed income. And having a diversified portfolio, where, for example, under one roof, if you invest in a moderate allocation portfolio with a 50/50 mix of equity and fixed income, over time, it's going to enable you to avoid a lot of bad behaviors that we see with the average investors. And by bad behaviors, I mean not rebalancing periodically, not having that discipline, having too much emotion. Because, what we've seen with... If... For example, if you look at cash flows from the Investment Company Institute, that institute is an industry group. They provide metrics on investor cash flows, looking at brokerage accounts. They have a great chart that shows that, for example, in periods like 2008, where you have a very stressed market, people tend to just get out of the market and, they don't get back in until the market's up 1x or 2x, and by that time, they've missed an opportunity to rebalance. And with a 60/40 portfolio, for example, we make sure, and my team manages about 55 billion of allocation portfolios, and what we do is we set the asset allocation, we pick the underlying fund investments, and we do the rebalancing. And rebalancing... it's a powerful tool to make sure that if you fill out, for example, a risk tolerance questionnaire, and work with your financial advisor to determine what your risk tolerance is, at 60/40 with market movements, you can easily become a 65 or 70 equity exposure within your own portfolio.

And that's not what your risk tolerance says that you are. And our job in an, a 60/40 allocation portfolio is to keep you where you should be along that risk-return spectrum, and I think it takes out the emotion. It's a very disciplined process. And as I mentioned earlier, with fixed income, look for those opportunities to have portfolios that have some on the fixed income side, active fixed income managers that have the flexibility to navigate these times. There are also investment options that have 60/40 portfolios, where there would be an allocation to alternatives, which could provide you additional diversification. And again, you should talk to your financial advisor to come up with the right solution for you, but that could provide additional diversification.

And, given where interest rates are headed with the Fed, it might be a great time to look at those opportunities to get that additional diversification by adding some alternatives within your 60/40 portfolio and looking for those 60/40 portfolios that include some exposure to alternatives. We're very disciplined, long-term, patient investors. And if you look back over the last 22 years, a typical 60/40 portfolio has had three negative years during those periods. And I know that recently, given what fixed income has done, there's been some discussion about this, but if you're a patient, long-term investor, a 60/40 portfolio, I believe still has a great place within the average investor's investment mix.

Mark: With the volatility and uncertainty in today's markets, do you have any additional thoughts in terms of how Equitable Investment Management is positioning things? And then additionally, do you have any comments that you'd care to offer financial professionals relative to conversations they might be having with clients?

Ken: So, at Equitable Investment Management, we invest for the long-term. We're patient investors. We believe in the power of diversification to have exposure in many different asset classes that have relatively low correlation with each other. And that's how we position ourselves to weather storms. And in terms of FPs having conversations with our clients, and I'm sure everybody on the phone has been talking with our clients over the last few weeks, try to keep emotions out of the equation. Volatility happens, and it's happened over the years, many different times, and having a diversified portfolio where you systematically rebalance over all of those asset classes, and it's something that will force you to rebalance out of asset classes or areas of the market that have done relatively well, for example, equities over the past five years into an asset class that has done relatively less, better, like fixed income on an absolute basis. So that discipline and that rebalancing is one thing that will quell volatility.

And having that in mind, as I said earlier, reduces the emotion when you talk with your clients, and showing them how to navigate that as part of a diversified portfolio is something I know that everybody here is very focused on, and over the last several weeks has spent a lot of time on, and those are the themes I believe will benefit shareholders in the future.

And just to mention again, that we believe diversification is something that timeless has served investors well and will continue to do so in the future.

Mark: Well, thanks, Ken. This has been a great discussion. Speaking for all of us, we really appreciate your insight into the challenges that this market is facing today, and this helps us greatly in developing strategies to help steer us through these current market conditions.

I also want to thank our listeners for joining us today and remember to subscribe to our podcast. Equitable Life with inSight is available wherever you obtain and download your podcasts. Please subscribe so that you never miss an episode. And I look forward to you joining us next time.

Ken: Thanks mark. It's been great spending time with you today.

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