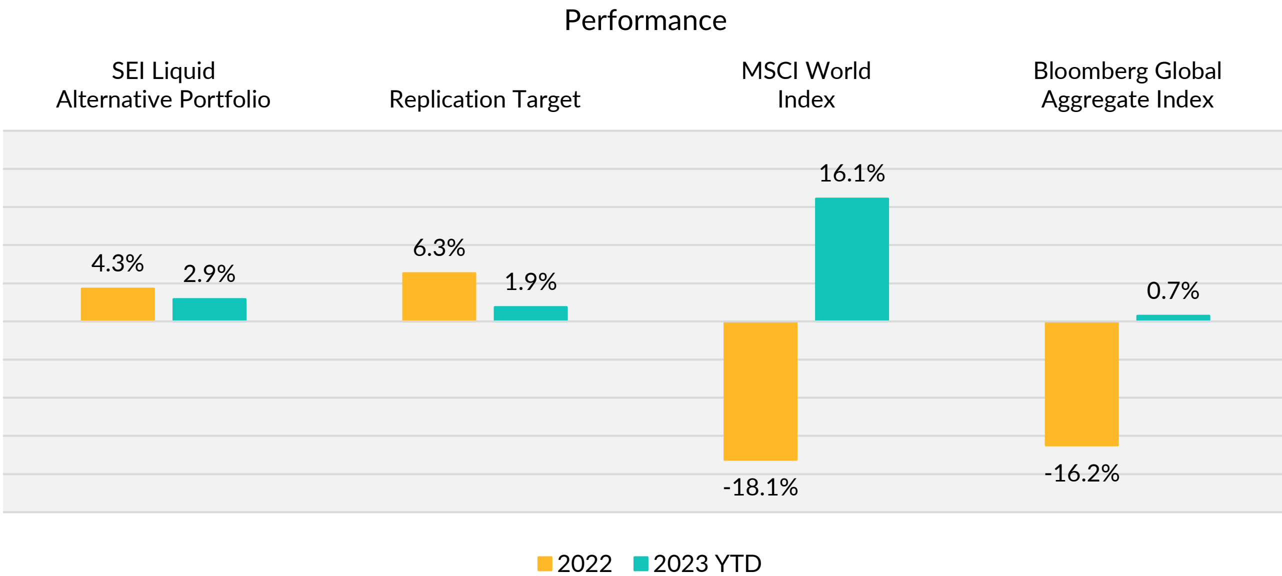
SEI LIQUID ALTERNATIVE FUND

August 2023 Update

Dear Colleagues:

The Portfolio[1] returned **-0.1%** in August and is now up **2.9%** in 2023, approximately 100 bps ahead of the Target portfolio of seventy leading hedge funds. This compares to a loss last month of -2.4% in the MSCI World Index and -1.4% in the Bloomberg Global Aggregate Index.



*Source: DBi and Bloomberg. Data as of August 31st, 2023

Higher for longer. What if it's "higher forever"?

The return of inflation was consistently met with disbelief by the vast majority of allocators. In early 2021, after we wrote a note about Stan Druckenmiller's prescient call, most allocators confidently told us he was wrong. By mid-year, early signs were dismissed as transitory. By Fall,

[1] Performance of the portfolios managed by DBi, net of sub-advisory fees. Please consult SEI directly for performance of individual share classes.

most expected one or perhaps two rate hikes the following year. During 2022, as the evidence became indisputable, allocators jumped on the idea that the Fed would quickly pivot. By January, the taper trade dominated markets. Then in February, inflation exceeded expectations, short rates rose but longer rates held fast and the yield curve inverted. A few months later, the recession scare post-SVB also was quickly run over by this Teflon economy. Today, the narrative is "higher for longer" – with "longer" simply defined as a "taper" a bit farther out.

Commentators have described this disbelief as a matter of heuristic bias: that humans, used to one state of the world, resist change. We think it is a bit more nuanced. In early 2021, most diversified portfolios were anchored around a single bet: low rates forever. This showed up in both stocks (overweight FAANGs) and bonds (*de minimus* yields on long dated paper). Research reports and client communications reflected this. Even for an allocator open to the idea of a regime shift, what do you do? No consultant would recommend a wholesale change to a ten-year asset allocation model in year two. An advisor who reflexively dumps all bonds risks, if the data is a false positive, blowing up his or her business. Clients want their professional allocators to be the steady hand at the wheel, and hence most move slowly regardless of whether it is economically rational.

There is a new issue at play, one we did not appreciate in 2021. What if this is permanent? What would this new world order do to "diversified" portfolios? The assumption that stocks and bonds hedge each other anchors trillions upon trillions of dollars of diversified portfolios. Yet there is strong evidence that, when inflation is higher, stock-bond correlations turn positive. This was the state of the world order before the past two plus decades. That would upend a cornerstone of asset allocation. Overnight, a back-of-the-envelope analysis suggests a 25% increase in risk in a 60/40 portfolio. Clients who expect a smooth train ride might be strapped on a comparatively scary rollercoaster.

While we have no crystal ball as to how this plays out, we believe allocators should plan for this world. That means increasing exposure to strategies with low beta to both stocks and bonds. Since inception, the Portfolio has had a beta to the MSCI World and Bloomberg Global Aggregate Bond Index of **0.2** and **0.0**, respectively. The successful allocators of 2030 may well be the ones who embraced, rather than fought, a long-term shift in the market structure.

The **Strategic Alpha** (Multi-Strategy) replication portfolio returned **-0.6%** in August and is up **6.4%** year to date. The Target portfolio of Equity Long/Short, Relative Value and Event-Driven hedge funds gained 0.3% last month and up an estimated 4.0% year to date. Since inception, we believe the replication portfolio has delivered over 90% of pre-fee returns, with a correlation of around 0.80, and approximately 122 bps per annum of alpha. The portfolio continues to benefit from rising rates through a short position in the 30 Year Treasury. Intermonth rebalancing helped to contain losses in equities as the portfolio shifted exposure from emerging markets to international developed and from small caps to tech.

The **Tactical Alpha** (Managed Futures) replication portfolio returned **0.6%** in August and is down **-2.1%** year-to-date; the Target portfolio of hedge funds declined -0.5% last month and is down -1.6% this year. Since inception, the replication portfolio has generated a cumulative return of 51%, nearly double that of the Target hedge funds, with a correlation of approximately 0.80. A reduction in net equity exposure helped to minimize losses while shorts in commodity linked currencies and interest rates generated gains. A spread trade between the Euro and Yen was flat during the month. The portfolio increased its conviction in short rates while reducing exposure to equities and maintaining the stance in currencies.

Please note that we have rebranded the firm as DBi. Please take a moment to visit our new website at www.dbi.co (no “m”!). We look forward to any questions or comments.

All the best,

The DBi Team