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QUARTERLY MARKET INSIGHTS

2ND QUARTER 2020

THE FAAMG ERA

A small group of massive, high profile, technology-oriented companies with ubiquitous brands and business footprints has dominated headlines, major U.S. equity indexes and the imaginations of many investors for nearly a decade. We believe the best representation of this phenomenon is the quintet of Facebook, Apple, Amazon, Microsoft and Alphabet (formerly known as Google). Taken together, "FAAMG" currently comprises roughly 21% of the S&P 500 Index's market capitalization. Over the five-year period ending June 30, the average cumulative return of the FAAMG stocks was 297.8% compared to the 66.2% return for the broad index. This group's combined average weight in the index over the last five years was 13.7%, but its members accounted for approximately 36.6% of the benchmark's cumulative gain during the period. In the first six months of 2020, the average return of the five FAAMG stocks was 24.1% compared to a decline of 3.1% for the S&P 500.

Elevated levels of concentration at the top of the S&P 500 Index as currently demonstrated by the FAAMG stocks is not unprecedented. In a recent report, Northern Trust Asset Management observed that the "Nifty Fifty" era of the 1960s and 1970s coincided with elevated S&P 500 Index concentration. In 1970, IBM, AT&T, General Motors, ExxonMobil and Kodak accounted for approximately 22% of the index. In 2000, toward the end of the "dot-com bubble," five stocks (Microsoft, General Electric, Cicso Systems, Walmart and ExxonMobil) accounted for about 17% of the S&P 500. What is unique, however, about the FAAMG companies compared to previous periods of market concentration is the group's dominance of various technology-related industries and the increasing tendency of its members' stocks to exhibit elevated cross correlations.

Upon first glance, the technology-heavy profile of the FAAMG stocks might give investors cause for concern, especially if they lived through the pain of the "dot-com" market bubble and subsequent bust. Yet, the technology landscape of 2020 is much different than the one that existed in 2000 with regard to maturity, scale and adoption. Each of the FAAMG companies are global leaders in one or more of what most investors, economists and policymakers view as powerful secular trends which originate in the technology sphere, but then branch out into other areas of the economy including finance, manufacturing and retail. These trends include e-commerce, cloud computing, digital advertising and digital payments.

In recent months, the FAAMG companies have seen their share prices enthusiastically supported by investor expectations that this group will benefit from the increased demand for cloud computing and e-commerce related to a broader adoption of remote working and online shopping amid the COVID-19 pandemic. As the FAAMG stocks have increasingly been at the forefront of the market's recovery from its March lows, they have drawn criticism for their elevated valuations according to traditional measures like the price-to-earnings-per-share (P/E) ratio. While none of this group is cheap relative to the broad market, a more nuanced discussion of their valuations seems useful. The stocks of three of the five - Alphabet, Apple and Microsoft – indeed trade at very large premiums relative to their recent forward-looking P/E ratio history. Meanwhile, shares of Facebook have traded at a discount to its five-year average P/E ratio for most of 2020. Finally, for better or worse, shares of Amazon have nearly always exhibited substantially elevated valuations based on earnings per share.

While investors should keep one eye on FAAMG stocks' valuations, a potentially underrated but more impactful short-term risk could be elevated stock price correlations across the group. As Gina Martin Adams, head of the Bloomberg Intelligence Equity Strategy team points out, "The average pairwise correlation in mega-cap tech was about 0.2 at the 2013 dawn of the FAAMG wave, indicating a weak relationship between stock prices for each pair. The correlation recently bottomed out at 0.52, but the correction and subsequent recovery has helped push it back to an all-time high 0.78."

Looking further out on the horizon, regulatory risk may be the biggest long-term concern for FAAMG companies and their shareholders. Charges of anti-competitive behavior aimed at Amazon, Facebook and Alphabet seem to be the most likely area where increased regulatory risk could emerge. More specifically, the issues of data privacy regulation and content curation for Facebook and Alphabet could be the highest risk regulatory items across the FAAMG cohort in coming years. European concerns for protecting the data of technology platform's users was codified into European Union law with the General Data Protection Regulation (GDPR). These apprehensions could migrate to the U.S. where, according to Pew Research Center data, a growing percentage of American voters believe that technology companies should be subject to greater oversight.

ECONOMY

U.S. ECONOMY REOPENS AND BEGINS RECOVERY

U.S. economic growth in the first quarter contracted at an annual rate of 5.0%, slightly steeper than the 4.8% drop first estimated. As of July 2, the Atlanta Fed's GDPNow estimate for second quarter U.S. GDP is -35.2%, which reflects a historic slowdown through April and early May. The second quarter should be the low point for GDP in 2020, and we expect to see a second half recovery as global economies reopen. The unprecedented size and quickness of the fiscal and monetary response by the U.S. Federal Reserve and Congress has had a positive effect on recent economic readings as the domestic economy reopens and should continue to add to the expected economic rebound in the second half of the year.

Despite a recent increase in the number of COVID-19 cases, consumer confidence has risen in recent months. The Consumer Confidence Index rose to 98.1 in the month of June after a May reading of 85.9. Economists expected an increase as states loosened shelter-in-place orders, but the increase was more than anticipated. While the Confidence Index is well below its pre-pandemic levels, June's number marks a significant increase from May. Despite the show of improved confidence, economic experts say it is too early to say consumers are ready to start spending like they were before the pandemic.

The Commerce Department said consumer spending, which accounts for more than two-thirds of U.S. economic activity, jumped 8.2% in May, the largest increase since the government started tracking the series in 1959. Americans stepped up their spending in May despite a 4.2% decline in personal income, which had soared by 10.8% the previous month. But that spending is not likely to be sustained, as income is expected to decline further as millions of workers could lose access to at least a portion of the expanded unemployment insurance payments under the CARES Act by the end of July. As we move into the second half of the year, we are monitoring downside risks from a second wave of COVID-19 infections and any deterioration of U.S.-China trade relations. Conversely, news of an effective vaccine could drive consumer confidence and spending higher well in advance of doses becoming widely available.

ECONOMIC INDICATORS	LATEST	3MO PRIOR	CHANGE*
REAL GDP (QoQ ANNUALIZED)	-5.0%	2.1%	▼
TRADE BALANCE	-54.6	-34.7	▼
UNEMPLOYMENT RATE	11.1%	4.4%	▼
NON-FARM PAYROLLS	4800K	-1373K	▲
ISM MANUFACTURING	52.6	49.1	▲
ISM NON-MANUFACTURING	57.1	52.5	▲
RETAIL SALES (LESS AUTOS)	12.4%	-0.2%	▲
INDUSTRIAL PRODUCTION	1.4%	0.1%	▲
HOUSING STARTS	974M	1567M	▼
CONSUMER PRICE INDEX (YoY)	0.1%	2.3%	▲
CONSUMER CONFIDENCE	98.1	118.8	▼
EXISTING HOME SALES	3.91M	5.76M	▼
CONSUMER CREDIT	-18.28B	20.8B	▼
CRUDE OIL PRICE	39.27	20.48	▼

Source: Bloomberg. Past performance does not guarantee future results. *The change arrow is indicative of a positive or negative change in the economic nature of the data series. For example, a downward-pointing change arrow assigned to the crude oil price field will correspond with an increase in the actual price of crude oil over the last three months. This is because a short-term increase in the price of crude oil has historically been detrimental to U.S. economic growth.

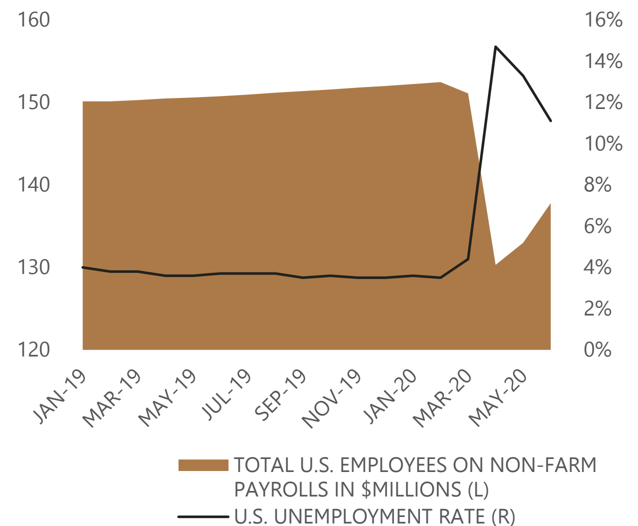
EMPLOYMENT AND MANUFACTURING

The U.S. labor market added 4.8 million jobs in June versus economists' expectation for 2.9 million, while the unemployment rate fell to 11.1% in June from 13.3% in May. Strong rehiring activity was driven by many U.S. states gradually reopening their economies in the first half of June. In May and June, the labor market recovered roughly a third of the 22.2 million jobs lost during March and April. Yet, the June employment data may not accurately represent the current employment situation because the data was gathered mid-month. The resurgence in COVID-19 cases in some southern and western states may have disrupted rehiring efforts in late June.

Economic activity in the manufacturing sector grew in June, according to the latest report from the Institute for Supply Management. The ISM Manufacturing Index was better than expected with a reading of 52.6, marking a significant jump from 43.1 in May. An ISM reading above 50 indicates that many businesses are beginning to see an expansion of manufacturing activity for the first time since the pandemic emerged. Thirteen of eighteen industries surveyed reported growth for the month, with the strongest expansion coming in textile mills, wood products and furniture and related products. New orders rose 24.6 points to 56.4, and production surged 24.1 points to 57.3.

HOUSING

U.S. existing home sales, which are recorded at closing, plunged 9.7% in May. This marked the third straight monthly decline and offered evidence of the challenges COVID-19 has presented to the housing market. The National Association of Realtors said that the monthly decline pushed sales down to a seasonally adjusted annual rate of 3.91 million units, the slowest pace since a homebuyers tax credit expired in October 2010. Meanwhile, U.S. Census Bureau data indicated that sales of new single-family homes, which are recorded at signing, jumped 16.6% in May from April, to a seasonally adjusted annualized pace of 676,000. May sales were nearly 13% higher than a year ago as record-low mortgage rates have helped fuel the rebound with new properties being in high demand. Rising home values and stricter lending standards have also meant that homeowners are sitting on historically high amounts of home equity.



Source: Bloomberg. Past performance does not guarantee future results.

BEAR MARKET EMERGES FROM AN 11-YEAR HIBERNATION

Coming off one of the most rapid declines into a bear market in modern history, the U.S. stock market rebounded at a record pace in the second quarter in response to the unprecedented stimulus from the U.S. Federal Reserve and U.S. Congress and investors' optimistic outlook for the reopening of the economy. It only took 12 days for the S&P 500 to enter what is traditionally defined as a bull market in early April after bouncing off the market low on March 23. A widely recognized definition of a bull market is when stocks rise more than 20% from their bear market low and continue to rise. This was the S&P 500's second quickest bear market low to a bull market since the Great Depression; the fastest was 10 days in March 2009. The market rebound has resulted in the S&P 500 gaining 39.91% through the end of June since the market bottom on March 23 and has recovered 75% of the drawdown from the prior peak on February 19. During the rebound, the S&P 500 experienced the largest 50-day advance in history at 37.70% in early June. The S&P 500 closed out the quarter with a 20.54% return, the best quarter since 1998 and fourth occurrence with a quarterly return above 20% since the Great Depression. Foreign equity markets also enjoyed a strong rebound during the quarter, although they trailed their domestic counterparts.

The bulk of the market's recovery took place in late March and April in response to the stimulus programs from the U.S. Federal Reserve and U.S. Congress. The combined programs thus far from the Fed and Congress represent almost 25% of U.S. 2019 GDP. Stocks rallied after these aggressive stimulus actions based on investors' expectations that these measures would ease liquidity strains and possibly prevent a worst-case scenario of widespread bankruptcies. Stocks rose further in May and June as investor optimism was fueled by the gradual easing of COVID-19 lockdown policies in many U.S. states and improvement in economic data. During the final weeks of the quarter, stocks lost some momentum amid investors' growing concerns about the rising number of COVID-19 cases in the U.S. The escalation in new case numbers in several southern and western U.S. states prompted some governors to delay or reverse their business reopening plans.

In the U.S. equity market, all 11 S&P 500 sectors rose during the quarter, in stark contrast with the first quarter when all sectors declined by double digits. Consumer discretionary was the best performing sector, rising 32.86% in the quarter. Amazon (AMZN), which accounts for almost 25% of the

A TALE OF TWO QUARTERS

SELECTED S&P 500 QUARTERLY RETURNS SINCE 1940

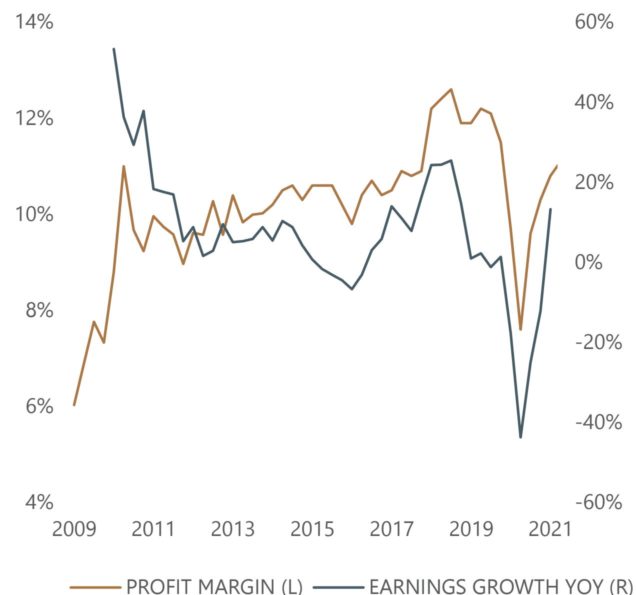
	BEST QUARTER		WORST QUARTER	
	QUARTER	RETURN	QUARTER	RETURN
1	Q1 1975	22.90%	Q3 1974	-25.05%
2	Q1 1987	21.32%	Q4 1987	-22.54%
3	Q4 1998	21.30%	Q4 2008	-21.94%
4	Q2 2020	20.54%	Q2 1962	-20.56%
5	Q1 1943	19.14%	Q1 2020	-19.60%
6	Q4 1982	18.21%	Q3 1946	-18.01%
7	Q2 1997	17.46%	Q2 1970	-17.99%
8	Q4 1985	17.14%	Q3 2002	-17.28%
9	Q3 1970	16.87%	Q2 1940	-16.49%
10	Q2 2009	15.93%	Q3 2001	-14.68%

Source: Morningstar. Past performance does not guarantee future results.

discretionary sector's weight, gained 41.50% as the work-from-home situation drove a jump in demand for the company's services including e-commerce and cloud computing. Improvement in the housing market and retail sales was supportive of other consumer discretionary stocks. Home builders Lennar (LEN) and D.R. Horton (DHI) surged over 60% while retailers including Home Depot (HD), Target (TGT), and Macy's (M) rose by around 30% or more.

The battered energy sector saw some relief as the price of U.S. West Texas Intermediate (WTI) crude oil recovered 91.75% during the quarter to around $40 per barrel. Despite the S&P 500 energy sector's 30.51% return in the quarter, the sector still has a 35.34% loss this year due to its 50.45% drop in the first quarter. The price of WTI oil has been on an extremely volatile ride this year. WTI started the year at $61 and sank 66.46% to $20.48 per barrel by the end of the first quarter due to the collapse in oil demand from COVID-19 lockdown measures. WTI briefly went into negative territory in April for the first time ever and steadily climbed higher through the rest of the quarter. Oil's resurgence was spurred by record oil production cuts from the Organization of the Petroleum Exporting Countries (OPEC) and its non-OPEC allies, including Russia, and higher fuel demand after some economies loosened COVID-19 lockdown measures.

Turning to the earnings outlook for the remainder of the year, the upcoming second quarter earnings reporting season is expected to mark the low point for S&P 500 earnings growth with a 43.65% year-over-year contraction followed by declines of 24.96% and 12.15% in the third and fourth quarters, respectively. Analysts project a very strong 26.13% earnings growth rebound next year driven heavily by margin expansion. The S&P 500's profit margin is projected to shrink in the second quarter by around 2.0% to 7.6%, marking its lowest level since 2009. The disruption of supply chains from COVID-19 shutdowns and the decision by a group of companies including Amazon (AMZN) and Home Depot (HD) to significantly increase spending in order to modify operations for the current environment are cited by analysts as major drivers of this profit margin compression. Scenario analysis from Bloomberg's Chief Equity Strategist Gina Martin Adams shows that S&P 500 earnings may still grow above 20% in 2021 even if a second wave of COVID-19 cases causes rolling lockdowns and takes a larger toll on earnings in the second half of this year.



Source: Bloomberg. Past performance does not guarantee future results.

BULGING ISSUANCE AND NARROWING SPREADS

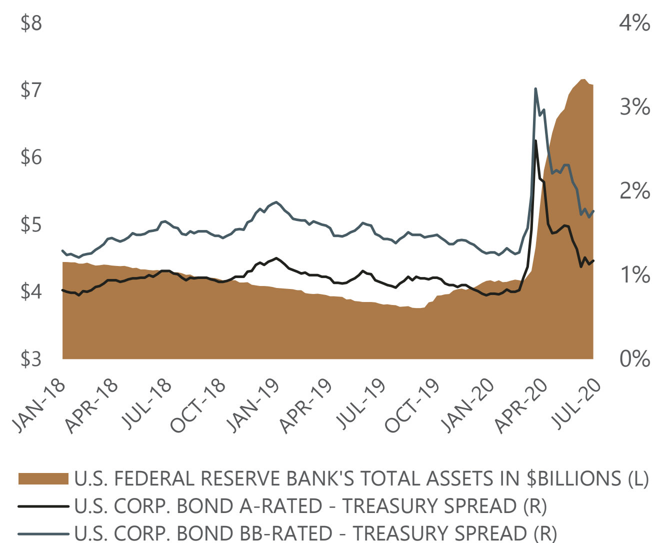
The final weeks of the first quarter brought forth a flurry of emergency U.S. Federal Reserve programs to combat the economic and financial impacts of the COVID-19 pandemic. That storyline carried through to the second quarter with the central bank expanding its massive intervention in lending markets to further quell the surge of illiquidity and sharp, downward repricing that permeated the bond world in March. The central bank entered the municipal debt markets with its April 9 establishment of the Municipal Liquidity Facility to help state and local governments manage cash flow stresses caused by the economic shutdowns by offering up to $500 billion in lending to states and municipalities. All told, the Fed's purchase programs resulted in the expansion of its balance sheet from approximately $4.3 trillion in mid-March to $7.1 trillion on June 30.

In addition to their outright purchases, Fed officials stepped up their efforts in the second quarter to communicate their commitment to protect the economy. In a statement following its late-April meeting, the central bank's policy-setting body indicated "The Committee expects to maintain this target range until it is confident that the economy has weathered recent events and is on track to achieve its maximum employment and price stability goals. In a May interview on CBS news magazine 60 Minutes, Fed Chairman Jerome Powell stated his view that the central bank "(is) not out of ammunition by a long shot." He added "...there is really no limit to what (it) can do with these lending programs...to support the economy..."

This policy backdrop allowed for a substantial narrowing of credit spreads in domestic corporate and municipal bond markets during the period, as investors exhibited considerably less concern over default risk at the end of the quarter than they did at the beginning. Yield spreads across the corporate credit rating scale tightened in the quarter, as the yield differential between A-rated U.S. corporate bonds and U.S. Treasury bonds with a similar maturity narrowed from 2.02% at the beginning of the quarter to 1.12% on June 30. Meanwhile, yield spreads for their lower quality counterpart, U.S. high yield corporate bonds, fell 1.70% from 8.79% on March 31 to 6.19% at the close of the quarter.

A reduction in pressure on the broad high yield market was helped by an improving environment for the distressed energy sector. As the price of U.S. West Texas Intermediate (WTI) crude oil nearly doubled in the quarter to approximately $39 per barrel, the additional yield

FED BALANCE SHEET EXPANSION AND CREDIT SPREADS



Source: Bloomberg. Past performance does not guarantee future results.

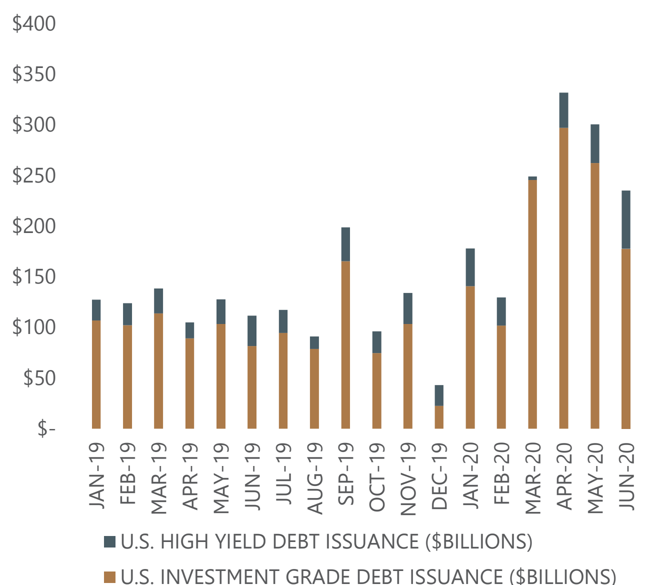
required by investors to purchase below investment grade energy sector bonds compared to a similar maturity Treasury bond declined significantly. As oil prices moved closer to what is perceived to be levels where large U.S. energy companies can offset their cash outflows with inflows, stress on those firms' balance sheets has declined dramatically for the time being.

Both the U.S. Treasury and American corporations took advantage of a much calmer second quarter environment than existed in March to engage in enormous amounts of debt issuance during the period. Fed policy support for credit markets helped clear a path for more than $800 billion of corporate debt issuance in the second quarter according to SIFMA data. This was highlighted by several notably massive new deals including ExxonMobil's $12.3 billion issuance on April 13, Boeing's $25 billion issuance on April 30 and AT&T's $12.5 billion issuance on May 21. For its part, the U.S. Treasury engaged in approximately $2.75 trillion of net government debt issuance in the second quarter, according to SIFMA data, in order to finance the CARES Act's colossal pandemic-related relief programs. This compares to a combined $2.68 trillion of net U.S. Treasury debt issuance from 2017 through 2019.

Despite the surge of issuance in the quarter, yields on the 10-year U.S. Treasury note traded in a relatively tight range during the period. Breakouts above 0.75% were short-lived in large part due to steady demand for safe haven assets in a period of elevated economic uncertainty. The short-end of the U.S. Treasury yield curve was held down by widely held market expectations that the Fed's policy rate will remain at the zero bound of 0.00% - 0.25%. Meanwhile, large-scale Fed purchases and generally healthy private market demand for Treasury bonds kept a ceiling on the longer end.

In the current environment, we believe it makes sense to focus fixed income portfolio exposure on those areas of the bond market within the scope of the various Federal Reserve facilities implemented in recent months. From a credit perspective, we believe it remains sensible to focus on upgrading the quality of portfolio exposure with balance sheet durability and business model resiliency top of mind. We believe a near-benchmark duration profile can help balance the downside risk of future surges in demand for safe haven assets related to elevated economic uncertainty with the upside risk of potential inflationary pressures driven by deficit spending and COVID-19 pandemic-related supply chain constraints.

THE SURGE IN CORPORATE DEBT ISSUANCE



Source: SIFMA. Past performance does not guarantee future results.

BUILDING CROSSCURRENTS

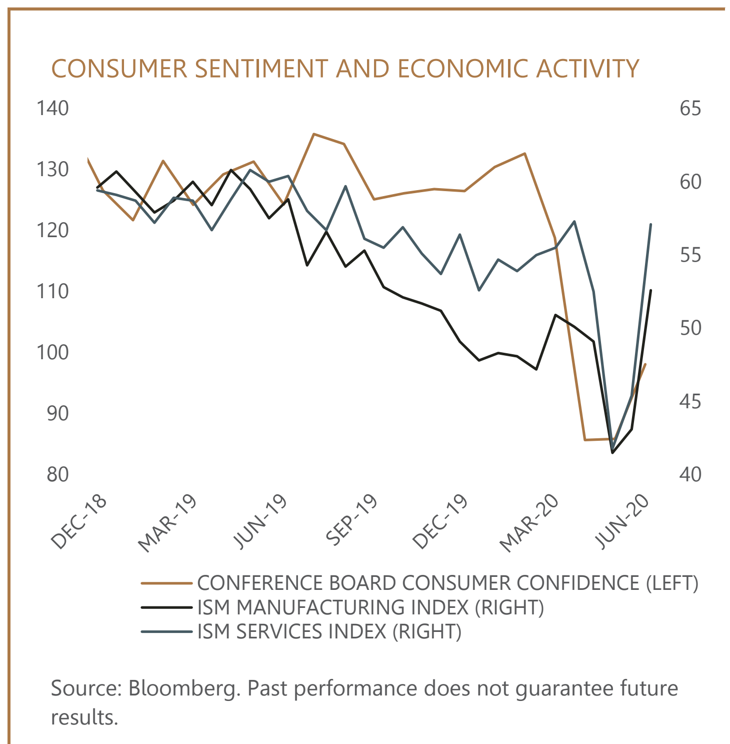
As the second quarter drew to a close, investors were confronted with an increasingly complicated set of crosscurrents to navigate. On the one hand, further signs of improvements in the domestic economic picture amid the phased reopenings in most U.S. states were viewed positively. Set against this backdrop were mounting concerns surrounding the potentially adverse impacts of a recent surge in COVID-19 cases in several large southern and western U.S. states. While the S&P 500 Index recorded one of its strongest quarters in history over the April to June period, the pace of the rally slowed noticeably in the second half of June amid rising virus case counts in Arizona, California, Florida and Texas.

On the economic front, it seems reasonable to expect a continuation of improvements in a majority of domestic economic data from often historically weak levels. This would be similar to what we have seen with the better-than-expected May and June non-farm payrolls reports and gradual declines in weekly continuing jobless claims from an early-May high. More recent examples of this trend include the June releases for both the ISM manufacturing and ISM Non-Manufacturing (Services) Purchasing Managers Indexes climbing back into expansion territory.

Despite positive directional trajectories from a growing number of U.S. economic data sets, most major global economies will almost certainly experience sharp growth contractions for the full year 2020 in the wake of widespread economic shutdowns in March, April and May. According to the median Bloomberg consensus forecast, U.S. GDP is expected to contract by 5.6% in 2020. A majority of investors appear to be looking past 2020 into 2021, however, when U.S. GDP is expected to resume growth at a clip of 4.0%.

Nonetheless, market participants should be prepared for truly stunning domestic quarterly GDP prints for both the second quarter and third quarter. The median Bloomberg consensus forecast is for a 34.7% contraction of GDP on an annualized quarter-over-quarter basis in the second quarter and a 19.9% expansion in the third quarter. We view these forthcoming data points as surrounded by a healthy dose of noise and primed for significant revisions. Thus, it seems most useful for investors to spend more of their time thinking about broad trends in economic growth and the shape of the likely 2021 recovery than trying to extrapolate meaning from the extraordinary quarterly GDP numbers they will no doubt encounter in coming months.

Turning to the prospects for equity markets, downward earnings revisions for the S&P 500 Index have appeared to stabilize over the last six to eight weeks. This is a positive development that we believe has been a contributing factor to the extension of April's equity market gains into May and June. Nonetheless, the Bloomberg median consensus for 2020 S&P 500 earnings per share (EPS) 2020 has declined 29% from roughly $175 on January 29 to $125 on June 30.



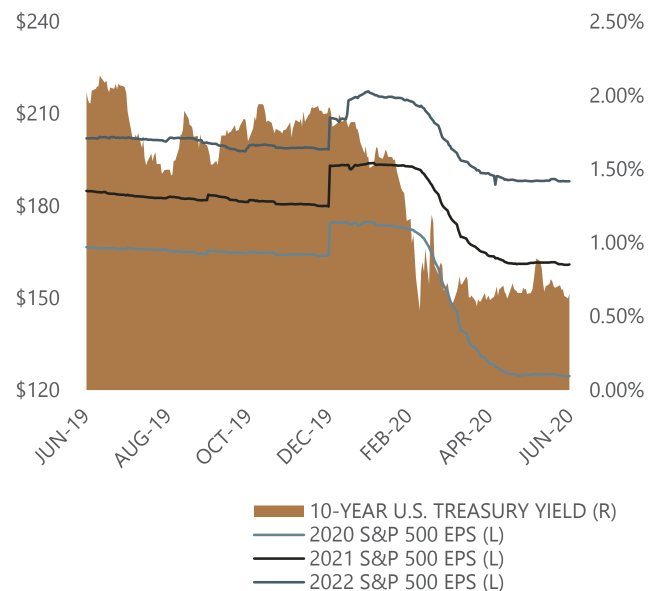
Source: Bloomberg. Past performance does not guarantee future results.

Given the S&P 500 Index's 39% rally since its March 23 low, its valuation based on expected profits over the next 12 months is more expensive now than when it recorded an all-time closing high on February 19. In absolute terms, then, stocks are clearly expensive when compared to their own history. From a relative perspective, however, the recent increase in the S&P 500's valuation has been more than offset by the sharp decline in U.S. government bond yields thus far in 2020. While the earnings yield of the S&P 500 Index based on expected twelve-month EPS ended June at roughly 4%, yields on the benchmark 10-year U.S. Treasury spent nearly all of the second quarter in a range between 0.60% and 0.80%.

In the second half of 2020, we do not expect any durable rise in government bond yields to materialize. We believe it makes sense for investors to focus on quality credit exposure and be near benchmark duration. Heading into 2021, we would argue that risk remains tilted toward higher yields due to a combination of the current ultra-low levels of interest rates, a Fed which we see as very unlikely to engage in negative interest rate policy and the potential for upside inflation surprises driven by pandemic-related supply chain constraints.

In the current environment of ultra-low bond yields and large-scale policy support, we believe the total return prospects of high-grade fixed income securities relative to their equity counterparts remain weak despite the powerful equity market rally. As such, our recommendation in late March to target modestly smaller fixed income allocations in client portfolios and commensurately larger equity allocations remains appropriate. Across asset classes in the second half of 2020 our focus will be on upgrading the quality of portfolio components in an effort to minimize exposure to areas of the economy which might face significant business model impairments.

S&P 500 EPS ESTIMATES AND BOND YIELDS



Source: Bloomberg. Past performance does not guarantee future results.

ECONOMIC OUTLOOK AND INVESTMENT POLICY

ECONOMIC FACTORS	CURRENT OUTLOOK
U.S. GDP Growth	The Bloomberg consensus economists' expectations for full-year 2020 U.S. GDP growth declined to -5.6% in late June from -1.2% in early April.
Federal Funds Rate	As of the second week of July, Fed funds futures markets project 0% probability of any rate hikes before the fourth quarter of 2021.
Inflation	Bond market expectations for average annual U.S. inflation over the next five years increased to 1.17% on June 30 from 0.53% on March 31.
Employment	Another Congressional extension of Paycheck Protection Program funding for American businesses would likely assist the labor market recovery.
Consumer Confidence	Any signs of successful economic reopenings or further labor market improvements will likely boost consumer sentiment from low levels.
Oil	Despite Saudi Arabia and Russia's agreement to cut production, elevated economic uncertainty should continue to weigh on oil prices.
Housing	Ultra-low rates and the Fed's commitment to purchase unlimited agency mortgage-backed securities should support the housing market.
International Economies	Bloomberg consensus economists' expectations project the euro zone and Japanese economies to contract in 2020 by 8.0% and 4.9%, respectively.

	MINIMUM		NEUTRAL		MAXIMUM
FIXED INCOME		●			
Core Bonds			●		
TIPS				●	
Non-Investment Grade			●		
International	●				

CURRENT OUTLOOK

In an environment of ultra-low bond yields, we believe the total return prospects of high-grade fixed income securities relative to their equity counterparts remain weak despite the powerful equity market rally from late March through the second quarter. As such, our recommendation from late March to target modestly smaller fixed income allocations than we recommended during 2019 remains appropriate. Within our core fixed income sleeve, we believe a near-benchmark duration profile can help balance the downside risk of future surges in demand for safe haven assets related to elevated economic uncertainty with the upside risk of potential inflationary pressures driven by deficit spending and COVID-19 pandemic-related supply chain constraints. While stress in below investment-grade credit markets remains elevated compared to recent history, we believe a moderate level of exposure remains reasonable given our view that a significant amount of default risk is likely incorporated in current spreads exhibited by high yield bonds.

	MINIMUM		NEUTRAL		MAXIMUM
EQUITIES				●	
Large Cap				●	
Mid Cap				●	
Small Cap			●		
Developed International		●			
Emerging Markets		●			

CURRENT OUTLOOK

We believe the persistence of historically low government bond yields combined with the massive emergency stimulus measures taken by the U.S. Federal Reserve and Congress justifies a slightly higher allocation to equities than we recommended in 2019. While economic and market uncertainty remains elevated amid efforts to contain a resurgence of COVID-19 cases, the gap between expected future returns in equity markets and bond markets remains wide enough, in our view, to justify this stance for long-term investors. We view an overweight to U.S. large capitalization stocks as appropriate given their size, scale and diversification relative to other areas of the global equity market. While U.S. midcap stocks do not fit all of these criteria, we believe an overweight to this area of the market makes sense given particularly compelling relative valuations.

	MINIMUM		NEUTRAL		MAXIMUM
ALTERNATIVES*				●	

	CAP PRES	IWSG	BAL	GWSI	GROWTH
Global Real Estate			●	●	●
Global Infrastructure		●	●	●	●
Hedged Equity	●	●	●	●	●
Arbitrage	●	●	●		

CURRENT OUTLOOK

As most global equity markets entered bear market territory in March, price volatility surged to levels not seen since the depths of the 2008-2009 global financial crisis. Meanwhile, developed market bond yields have plunged to historically low levels as many investors scramble to increase their exposure to safe haven assets. We expect equity and credit market volatility to remain elevated in the second half of 2020, while government bonds are most likely more than fairly valued over long-term investment horizons. Considering this backdrop, we recommend that client portfolios include an overweight to alternative investments that have demonstrated an ability to provide enhanced portfolio diversification over full market cycles. Our diversified alternatives portfolios, as seen in the table to the left, are designed to decrease the risk profile of our five investment objective-based portfolios (CAP PRES, IWSG, BAL, GWSI, and GROWTH).

The above minimum/neutral/maximum recommendations represent MainStreet Advisors' current positions relative to our Strategic Asset Allocation ranges. Views expressed have a 6-12 month horizon and are those of the MSA Investment Committee.
*Cap Pres: Capital Preservation, IWSG: Income with some growth, Bal: Balanced, GWSI: Growth with some income

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