SECOND QUARTER 2021

GROWTH WITH MODERATE INCOME

Equity markets performed well in the second quarter, with gains across each major global equity region as well as positive returns across most fixed income asset classes. The global growth backdrop remained constructive as economies moved towards reopening, while better-than-expected earnings growth also helped support equity market returns. Investor concerns focused on the inflation outlook and its potential implications on Federal Reserve policy. After rising to 1.74% by the end of the first quarter, interest rates declined in the second quarter, with the 10-year Treasury yield stabilizing around 1.50% in June and ending the quarter at 1.47%. The credit environment remained constructive with tightening credit spreads in the second quarter across both investment grade and high yield fixed income – helped by improving corporate fundamentals and continued investor demand for yield. In central bank policy, the European Central Bank remained highly accommodative, while Fed leaders reiterated a patient approach towards achieving the central bank's inflation and full employment goals after increased investor concerns that the Fed was becoming more hawkish following the June meeting.

We made no changes in asset allocation in the quarter. We remain constructive on risk assets as the global growth environment continues along a positive trajectory during the pandemic recovery, helped by accommodative monetary policy and our view that the rise in inflation is likely to prove transitory. Currently, the portfolio has broad-based overweights to risk assets including developed ex-U.S. equities, natural resources, global listed infrastructure, U.S. equities and emerging market equities, funded by underweights across cash, investment grade fixed income and inflation-linked fixed income. The portfolio ended the quarter with a higher risk level than its strategic benchmark.

Performance for the quarter was fairly close to benchmark as benefits from tactical positioning were offset by headwinds from strategic positioning. Strategic positioning weighed on performance as high yield fixed income and global listed infrastructure failed to keep pace with global equities. Tactical positioning benefited performance primarily due to the underweight to risk control assets including cash, inflation-linked fixed income and investment grade fixed income, partially offset by some negative impacts from the overweight to global listed infrastructure. Our broader-based U.S. market factor tilt strategy (TILT), our broader-based developed markets ex-U.S. factor tilt strategy (TLTD) and our global natural resources strategy (GUNR) were the main detractors in terms of fund implementation, while our quality large cap U.S. equity strategy (QLC), our global quality real estate strategy (GQRE) and our global listed infrastructure strategy (NFRA) were the main contributors.

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