

THIRD QUARTER 2023

MAXIMUM GROWTH

Global equities followed a choppy trajectory throughout the third quarter with July gains giving way to losses in August and September as interest rates pushed higher globally later on in the quarter. In the U.S., the broader economic narrative continued around resilient – but slowing – growth and moderating inflation, with both investors and the Federal Reserve interpreting these dynamics as more likely to lead to higher-for-longer monetary policy. Outside the U.S., Europe and to a greater extent, China, faced incremental growth headwinds. Central banks globally are approaching peak policy rates as policymakers have to carefully assess future growth concerns and the lagged impacts from their prior tightening with still-elevated core inflation. Overall, financial market returns were largely negative for the quarter with a few asset classes such as cash, high yield fixed income and natural resources seeing slight-to-modest gains.

We made one change in asset allocation in the quarter. In August, we increased high yield fixed income and decreased developed ex-U.S. equities in conjunction with our annual strategic asset allocation update. The tactical changes were primarily designed to account for the strategic asset allocation update and slightly reduce the risk profile of the portfolio. High yield fixed income remains our largest tactical overweight, while developed ex-U.S. equities were decreased to more fully align with our existing underweights to U.S. and emerging market equities. Currently, the portfolio has overweights in high yield fixed income and natural resources, funded by underweights across U.S. equities, developed ex-U.S. equities and emerging market equities. The portfolio ended the quarter with a moderately lower risk level than its strategic starting point (the strategic allocation is 100% risk assets).

The portfolio outperformed in the quarter as benefits from strategic positioning and tactical positioning outweighed modest drag from fund implementation. Strategic positioning benefited performance given natural resources and high yield fixed income outperformed global equities. Tactical positioning helped performance primarily due to benefits from the overweight to high yield fixed income and the overweight to natural resources. Our global natural resources (GUNR), our global quality real estate (GQRE) and our quality low volatility emerging markets equity (QLVE) were the main detractors in terms of fund implementation, while our quality low volatility developed markets ex-U.S. equity (QLVD) was the main contributor.

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P-102023-3174367-021724