

THIRD QUARTER 2020

GROWTH WITH MODERATE INCOME

Financial markets continued to rebound in the third quarter, helped by ongoing improvement in consumer and business-related economic data. Investors assessed a number of developments including COVID-19 in addition to the U.S. election outlook and prospects for additional fiscal stimulus in the U.S. Global equities exceeded pre-virus highs in the quarter – though a down month in September reduced the quarterly gain to about 8%. Across regions, U.S. equities generally topped their non-U.S. peers with help from continued strong performance in large technology companies. Central bank policy globally remains extremely accommodative with little in the way of policy changes in the quarter, though the Federal Reserve announced an update to its inflation targeting framework. U.S. interest rates remained stable throughout the quarter, while credit spreads declined overall despite a modest uptick in September.

We made one change in asset allocation in the quarter. In August, we increased our municipal investment grade fixed income, emerging market equity, global real estate and global listed infrastructure allocations, while decreasing our municipal high yield fixed income, inflation-linked fixed income, non-U.S. developed market equity and natural resources allocations. The tactical change reduced our large overweight to municipal high yield fixed income following strong performance in the asset class and reduced our underweight to emerging market equity, while also reflecting some adjustments directly related to our annual strategic asset allocation update. Currently, the portfolio has overweights in municipal high yield fixed income, municipal investment grade fixed income and global listed infrastructure, funded by underweights across inflation-linked fixed income, U.S. equities and emerging market equities. The portfolio ended the quarter with a moderately lower risk level than its strategic benchmark.

Performance for the quarter was negatively impacted by fund implementation, tactical positioning and strategic positioning. Strategic positioning weighed on performance due to headwinds from lower returns in municipal high yield fixed income and real assets compared to global equities. Tactical positioning detracted from performance due to the overweight to municipal high yield fixed income, the underweight to emerging market equities and the overweight to global listed infrastructure. Our quality low volatility U.S. equity strategy (QLV), our quality low volatility developed markets ex-U.S. equity strategy (QLVD) and our quality low volatility emerging markets equity strategy (QLVE) were the main detractors in terms of fund implementation, while our global listed infrastructure strategy (NFRA) and our municipal high yield fixed income strategy (NHVMX) were the main contributors.

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