NORTHERN TRUST

DIVERSIFIED STRATEGIST PORTFOLIOS
QUALITY LOW VOLATILITY
(TAX SENSITIVE)
QUARTERLY COMMENTARY

THIRD QUARTER 2020

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, non-U.S. developed market equity and natural resources allocations, while decreasing our U.S. equity allocation. The tactical change reduced our underweight to non-U.S. equities given the stabilizing growth outlook, while also adjusting the portfolio for 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 and tactical positioning, though these headwinds were partially offset by benefits from strategic positioning. Strategic positioning was helped primarily by risk assets significantly outperforming risk control assets, partially offset by weaker returns in real assets compared to global equities. Tactical positioning detracted from performance due to the underweight to emerging market equities, the equal-weight to natural resources (previously underweight) and the equal-weight to non-U.S. developed market equities (previously underweight). Our municipal investment grade fixed income strategy (NOTEX), our quality low volatility U.S. equity strategy (QLV) and our quality low volatility developed markets ex-U.S. equity strategy (QLVD) were the main detractors in terms of fund implementation, while our global listed infrastructure strategy (NFRA) and our target duration TIPS strategy (TDTT) were the main contributors.

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