

# Easing Into Slowing Growth

We are in a late cycle environment in which macro conditions are increasingly signaling deterioration, and this fact alone calls for nuanced portfolio construction. However, our macroeconomic analysis suggests that the economic softening so far has been largely offset by central banks around the world pivoting to easing, which has loosened financial conditions considerably. Looking forward, it still remains unclear if the loosening of financial conditions will manage to turn the outlook around.

Here is how we are positioning asset allocation portfolios in light of our outlook for the global economy and markets.



## OVERALL RISK

Given broadly slowing growth, increasing geopolitical uncertainty, and generally higher levels of volatility, we are modestly underweight risk relative to our benchmark, and building liquidity to take advantage of tactical buying opportunities.

## POSITIONING

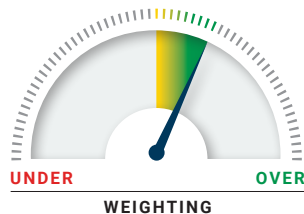


### EQUITIES

U.S.	-	+
Europe	-	+
Japan	-	+
Emerging markets	-	+

We expect volatility and slowing profit growth to continue to restrain investor appetite for equities in 2019. Therefore, we have a modest underweight to equities with an emphasis on liquidity and high quality, defensive sectors. We favor large caps over small caps, U.S. equities over European equities, and have increased our weighting in high-dividend-yielding equities, which we believe should benefit from lower sovereign bond yields.

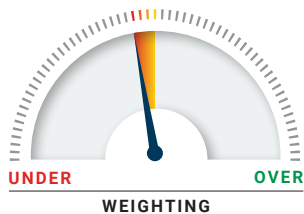
## OPPORTUNITIES



### RATES

U.S.	-	+
Europe	-	+
Japan	-	+
Emerging markets	-	+

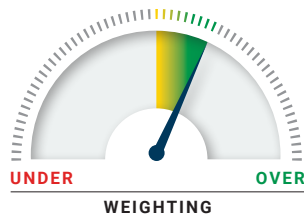
We prefer high quality duration as we move toward the later part of the cycle, as we still believe that fixed income offers an attractive diversifier for risk in portfolios, particularly given the dovish pivot of global central banks. However, we are selective in our exposures. Recognizing the significant moves lower recently, we still find U.S. rates the most attractive in developed markets.



### CREDIT

Securitized	-	+
Investment grade	-	+
High yield	-	+
Emerging markets	-	+

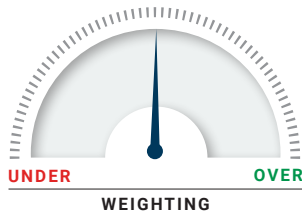
Given our late cycle view, we expect corporate credit will underperform over the coming year. Within corporate credit, we prefer shorter-dated bonds from high quality issuers, especially in defensive and noncyclical sectors, which is in keeping with our quality and liquidity theme. The high yield underweight reflects in particular the glut of low quality leveraged loan issuance. We continue to favor non-agency mortgage-backed securities (MBS) as they remain a relatively stable alternative to corporate credit. We are also selectively receiving rates in select emerging market (EM) external credits where valuations look compelling, and that we believe will benefit from global developed market central banks pivoting to a more dovish rate path.



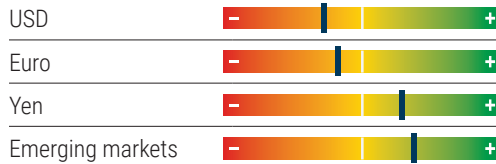
### REAL ASSETS

Inflation-linked bonds	-	+
Commodities	-	+
MLPs	-	+
Gold	-	+

Historically, real assets tend to perform well in late cycle environments; however, that relationship has become less stable in recent periods. That said, we still view real assets as an effective tail risk hedge against rising inflation as well as a portfolio diversifier, and we therefore maintain a modest allocation to what we feel are attractively valued opportunities, including U.S. Treasury Inflation-Protected Securities (TIPS).



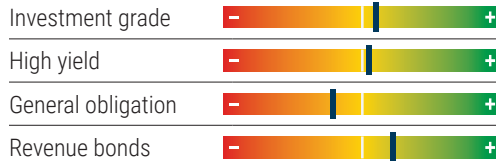
**CURRENCIES**



We have a nuanced view on currencies, and expect more significant alpha opportunities to emerge outside of the major currencies. The dovish pivot by developed market central banks argues for an overweight to those EM currencies that are both attractively valued and higher yielding. We have paired this risk with an underweight to export-heavy Asian currencies that are closely linked to China.



**MUNICIPALS**



We favor overweighting municipal allocations as U.S. tax reform has created a favorable technical dynamic for the market. Tax law changes have contributed to a drop in issuance while demand has remained steady, particularly in high-tax states where state and local tax deductions were curtailed. Additionally, in this macro environment, municipal bonds may offer investors a late-cycle refuge with attractive, tax-efficient income. However, credit selection will become more critical as economies cool. We continue to emphasize credits backed by dedicated revenue streams less subject to politics and pensions.

**Past performance is not a guarantee or a reliable indicator of future results.**

**All investments** contain risk and may lose value. Investing in the **bond market** is subject to risks, including market, interest rate, issuer, credit, inflation risk, and liquidity risk. The value of most bonds and bond strategies are impacted by changes in interest rates. Bonds and bond strategies with longer durations tend to be more sensitive and volatile than those with shorter durations; bond prices generally fall as interest rates rise, and the current low interest rate environment increases this risk. Current reductions in bond counterparty capacity may contribute to decreased market liquidity and increased price volatility. Bond investments may be worth more or less than the original cost when redeemed. **Sovereign securities** are generally backed by the issuing government. Obligations of U.S. government agencies and authorities are supported by varying degrees, but are generally not backed by the full faith of the U.S. government. Portfolios that invest in such securities are not guaranteed and will fluctuate in value. **Inflation-linked bonds (ILBs)** issued by a government are fixed income securities whose principal value is periodically adjusted according to the rate of inflation; ILBs decline in value when real interest rates rise. **Treasury Inflation-Protected Securities (TIPS)** are ILBs issued by the U.S. government. **Equities** may decline in value due to both real and perceived general market, economic and industry conditions. Investing in **foreign-denominated and/or -domiciled securities** may involve heightened risk due to currency fluctuations, and economic and political risks, which may be enhanced in emerging markets. **Currency rates** may fluctuate significantly over short periods of time and may reduce the returns of a portfolio. **Commodities** contain heightened risk, including market, political, regulatory and natural conditions, and may not be suitable for all investors. Investing in MLPs involves risks that differ from equities, including limited control and limited rights to vote on matters affecting the partnership. **MLPs** are a partnership organized in the US and are subject to certain tax risks. Conflicts of interest may arise amongst common unit holders, subordinated unit holders and the general partner or managing member. MLPs may be affected by macro-economic and other factors affecting the stock market in general, expectations of interest rates, investor sentiment towards MLPs or the energy sector, changes in a particular issuer's financial condition, or unfavorable or unanticipated poor performance of a particular issuer. MLP cash distributions are not guaranteed and depend on each partnership's ability to generate adequate cash flow. **Mortgage- and asset-backed securities** may be sensitive to changes in interest rates, subject to early repayment risk, and while generally supported by a government, government-agency or private guarantor, there is no assurance that the guarantor will meet its obligations. Income from **municipal bonds** is exempt from federal income tax and may be subject to state and local taxes and at times the alternative minimum tax. The **credit quality** of a particular security or group of securities does not ensure the stability or safety of the overall portfolio. **Diversification** does not ensure against loss.

**Management risk** is the risk that the investment techniques and risk analyses applied by the investment manager will not produce the desired results, and that certain policies or developments may affect the investment techniques available to the manager in connection with managing the strategy. There is no guarantee that these investment strategies will work under all market conditions or are suitable for all investors and each investor should evaluate their ability to invest long-term, especially during periods of downturn in the market. Investors should consult their investment professional prior to making an investment decision.

**Alpha** is a measure of performance on a risk-adjusted basis calculated by comparing the volatility (price risk) of a portfolio vs. its risk-adjusted performance to a benchmark index; the excess return relative to the benchmark is alpha.

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