DUCK, DUCK, GOOSE

All in all, the 2nd quarter felt a little like a tale of two cities, that of Wall Street (best of times?) and that of Main Street (worst of times?). While we officially entered a recession in February of 2020, some estimate that we may have emerged in May, which would make this the shortest recession of all time. The S&P 500 Index notched its best quarter since 1998 with a 20.5% return, nearly erasing its first quarter loss. Developed and emerging market equity indices also posted returns approaching 20%, and high yield bond and emerging market debt markets recovered significantly, up over 10%. Oil prices also recovered after going negative, closing at roughly $40 a barrel (WTI). A number of promising statistics point to a rebound — but as Mark Twain said, "there are 3 kinds of lies: lies, damned lies, and statistics!" Retail sales grew by a record 18%, durable goods orders delivered +16%, pending home sales were up 44%, and personal spending rose 8% in May…but all of these data points are from significantly depressed levels. Furthermore, many segments of the economy have yet to participate in the recovery and are likely to be impacted for some time. Hotels, restaurants, airlines, and many small businesses have been among the hardest-hit.

Thus while Wall Street appeared to turn a blind eye, much of Main Street continued to suffer. Against the backdrop of stellar asset price performance, rising cases of the virus in the US tempered optimism going into quarter-end. Some cities have reversed their re-openings as new COVID-19 cases have mounted, creating more uncertainty, and the light at the end of the tunnel is increasingly looking like a train. First quarter GDP contracted 5.0%, but the second quarter is expected to be far worse, with estimates spanning a wide range (-30% to -40% annualized) and changing by the day. Despite efforts from PPP loans, 19 million jobs were lost in May, and June unemployment was 11.1%. While jobless claims have decelerated, they continue to hover around 1.5 million per week, with those receiving state benefits at roughly 18 million. Further evidence of the ongoing stress is reflected in downgrades and defaults across bonds and loans, which total $100 billion thus far in 2020, already the most since the entire year of 2009.

The Fed continues to be extremely accommodative and has hit this virus with a strong inoculation of liquidity combined with fiscal stimulus cocktail, now approaching $3 trillion, or nearly 14% of GDP. While some of these programs have been controversial, collectively they have been incredibly effective in restoring liquidity and confidence to the markets. Fed Chair Jerome Powell stands committed to this challenge, stating that in a recent meeting, "A full recovery is unlikely until people are confident that it is safe to reengage in a broad range of activities." However this is not our fight alone, but a global one as central banks and government around the world do their part to flatten the curve and find a cure.

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Meanwhile, many of us have been sheltered in place and therefore our global perspective may be a little closer to home. I myself live on the San Antonio River, where I have the pleasure of soaking up the local flora and fauna on my daily dog walks. Springtime here is especially vibrant, as the famed Riverwalk comes alive with beautiful bursting flowers, enthusiastic tourists (well, not this year!), and the hatching of hundreds of adorable baby ducklings. People "ooh and ah" over the fuzzy little babies as mom and dad proudly swim about showing off their progeny. Sadly this happy moment is short lived, as every year I witness the quickly dwindling numbers of hatchlings as the days click by. What may start as a flock of a dozen quickly plummets to 8, then 6, and then down to 1 or 2 (or sometimes none at all). No, it's not a "duck pandemic" that is taking the lives of these cute critters but other predators, such as turtles that pull the ducklings down by their feet and drown them, or perhaps the occasional hawk swooping down from overhead. Needless to say, there is a lot of herding that mom and dad have to do to keep their little ones safe – not to mention dodging swiftly moving river barges that occasionally separate these web-footed families with their strong wakes.

This spring however was remarkably different in more ways than one! First, there was COVID, which resulted in gym closures, forcing me to do the unthinkable…run outside. The iconic San Antonio river barges were also victims of the virus, and were temporarily placed in dry-dock. The upside of my self-imposed outdoor activities —I was afforded more duckling observation time. While I'm no scientist and can't draw any Darwinesque conclusions, I can share what I witnessed…the ducklings flourished! Instead of watching babies vanish, they blossomed, and mothers were able to raise their full brood to a self-sustainable size and weight. Perhaps the river barges are a distraction, and complicate the ducks' abilities to protect their newborn hatchlings from amphibious marauders? Or perhaps the ducks are simply more at peace without the added stress of river boat traffic. Either way, it would appear that increased levels of parenting could be one positive outcome of Corona.

And speaking of children, economists are predicting the next baby boom given the recent restrictive "stay at home orders"! Yes, many Americans have had a lot of time on their hands, and idle hands, well, you get my point. If these predictions come true, this could provide a sorely-needed beneficial boost to the economy in a country plagued by aging demographics, and falling replacement rates. Another benefit of the pandemic -- many of us have learned that we are quite capable of working from home, and in many cases are more productive. Technology has evolved and has empowered the work place to take on a different look and feel, and will continue to have more permanent ramifications. My hope is that many mothers (and fathers) will benefit from continued telecommuting, and not have to choose between a career and being a parent. Perhaps this will also afford many parents who were forced to leave the work force long ago the ability to return —from home.

Work from home still presents its own set of challenges as parents compete for broadband and toddlers photo bomb Zoom meetings. Nothing is perfect, and distractions for duck and human parents alike will always exist. In fact, just as the ducks have been multiplying and frolicking with their chicks, a stranger has come to town, seemingly going unnoticed. This imposter may look like a duck, but is actually an invasive Egyptian Goose, that is slowly making its way through Texas. They are larger than their brethren, highly territorial, and tend to push out local species. Which begs the question, how many ducklings will survive next year?

In conclusion, we believe innovation is here to stay not only in technology, but healthcare as well, which has seen a surge in telehealth consultations. In addition, we predict we will see a resurgence in on-shore manufacturing as companies re-strategize their supply chains, and factories will be revolutionized with state of the art robotics and AI machines, creating innovative job opportunities for future generations. To that end, we constantly strive to look forward and position our client portfolios to take advantage of long-term trends, while still casting one-eye in the rear view mirror to ensure an unexpected "goose" isn't encroaching.

CLOSING THOUGHTS

This year is far from over, and yet it already feels like we've lived a lifetime. We've entered a recession, we've seen unemployment hit levels not seen since the Great Depression, we've seen schools, parks, and businesses shuttered, and experienced unprecedented actions from the Federal Reserve and Congress. In the wake of our nation's birthday, we've had many freedoms we took for granted, taken away, and long-standing socio and economic issues come to light. And while the stock market has essentially made a round trip, we remain steadfast and watchful, as there is much we still don't know about this virus, and like our ducks, must adapt to the changing currents.

Regards,

John P. Ulrich, CFP®
President

Whitney E. Solcher, CFA®
Chief Investment Officer

Equity Markets

U.S. stock markets posted double-digit returns in the second quarter, with some segments erasing all of the first quarter's sharp losses. Growth, benefiting from its 44% exposure to Technology, sharply outperformed value (R1000 Growth: +27.8%; R1000 Value: +14.3%) and the spread is even larger on a ytd basis (R1000 Growth: +9.8%; R1000 Value: -16.3%). Small caps outperformed large (RMicrocap +38.8%; R2000: +25.4%; R1000: +21.8%). Within the S&P 500 (+20.5%), several sectors posted returns over 30% (Energy, Consumer Discretionary, Technology) while Utilities (+2.7%) fared the worst. It is worth nothing that the "FAAMG" stocks accounted for nearly 30% of the return for the S&P 500; collectively the group was up 35% for the quarter.

Outside of the U.S., double-digit returns were broad-based across developed and emerging markets (MSCI ACWI ex-USA: +16.1%; MSCI EM: +18.2%) but both remain down roughly 10% over the six-month period. As in the U.S., growth outperformed value.

Credit Markets

U.S. Treasury yields were range-bound in the second quarter; the 10-year U.S. Treasury yield closed the quarter at 0.66%; down only 4 bps from March 31 but off far more sharply from the year-end level of 1.92%. As a result, the Bloomberg Barclays US Treasury Index was up a modest 0.5% for the quarter. Other sectors recovered from sharp underperformance in the first quarter as investor confidence improved. For the quarter, the Bloomberg Barclays US Aggregate Bond Index gained 2.9%, with non- Treasury sectors faring the best. This is a stark contrast to the first quarter, when U.S. Treasuries were virtually the lone sector to post a positive return. The Bloomberg Barclays US Corporate Bond Index rose 9.0% in the second quarter but has underperformed like-duration U.S. Treasuries by 540 bps ytd. The Bloomberg Barclays High Yield Bond Index posted a double-digit return (+10.2%) in Q2 but remains down 3.8% ytd.

Rates were lower overseas, fueled by rate cuts across a broad swath of countries and strong performance from corporates. The Bloomberg Barclays Global Aggregate ex-US Bond Index rose 3.4% (unhedged). Emerging market debt indices posted lofty results (EMBI Global Div: +12.3%; GBI-EM Gl Div: +9.8%) but remain down single digits from year-end. Municipal bonds also rebounded from relatively poor performance in the first quarter; the Bloomberg Barclays Municipal Bond Index rose 2.7% in the second quarter but is up only 2.1% ytd.

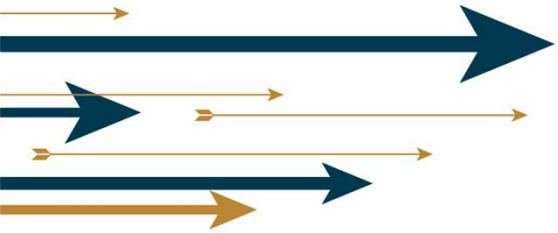
Returns for Various Periods - June 30, 2020

	Last Quarter	Year to Date	Last Year	Last 3 Years	Last 5 Years	Last 10 Years	Last 15 Years
MSCI:ACWI	19.22	(6.25)	2.11	6.14	6.46	9.16	6.42
Russell:3000 Index	22.03	(3.48)	6.53	10.04	10.03	13.72	8.78
Russell:3000 Growth Index	27.99	8.98	21.94	18.21	15.23	16.92	11.15
Russell:3000 Value Index	14.55	(16.74)	(9.42)	1.41	4.41	10.23	6.15
MegaCap							
Russell:Top 50	22.10	2.73	15.40	14.16	13.16	14.67	9.01
Russell:Top 200	20.91	(0.49)	11.20	12.48	11.91	14.57	9.04
Russell:Top 200 Growth	27.22	11.26	26.39	20.15	17.29	17.96	11.67
Russell:Top 200 Value	11.71	(15.35)	(7.32)	3.02	5.31	10.49	5.97
Large Cap							
S&P:500	20.54	(3.08)	7.51	10.73	10.73	13.99	8.83
Russell:1000 Index	21.82	(2.81)	7.48	10.64	10.47	13.97	8.91
Russell:1000 Growth	27.84	9.81	23.28	18.99	15.89	17.23	11.32
Russell:1000 Value	14.29	(16.26)	(8.84)	1.82	4.64	10.41	6.24
MidCap							
S&P:400 Mid Cap	24.07	(12.78)	(6.70)	2.39	5.22	11.34	8.21
Russell:Midcap Index	24.61	(9.13)	(2.24)	5.79	6.76	12.35	8.51
Russell:Midcap Growth	30.26	4.16	11.91	14.76	11.60	15.09	10.32
Russell:Midcap Value	19.95	(18.09)	(11.81)	(0.54)	3.32	10.29	7.00
Small Cap							
S&P:600 Small Cap	21.94	(17.85)	(11.29)	0.56	4.48	11.24	7.65
Russell:2000 Index	25.42	(12.98)	(6.63)	2.01	4.29	10.50	7.01
Russell:2000 Growth	30.58	(3.06)	3.48	7.86	6.86	12.92	8.85
Russell:2000 Value	18.91	(23.50)	(17.48)	(4.35)	1.26	7.82	4.97
Russell:Microcap	30.54	(11.21)	(4.77)	0.85	2.86	9.93	5.65
Non-US Equity							
MSCI:ACWI ex US	16.12	(11.00)	(4.80)	1.14	2.26	4.97	4.44
MSCI:EAFE	14.88	(11.34)	(5.13)	0.81	2.05	5.73	4.09
MSCI:EAFE Growth	16.95	(3.53)	4.15	5.91	5.52	7.78	5.71
MSCI:EAFE Value	12.43	(19.27)	(14.48)	(4.43)	(1.59)	3.53	2.35
MSCI:EAFE Small Cap	19.88	(13.11)	(3.52)	0.53	3.81	8.02	5.66
MSCI:EM	18.08	(9.78)	(3.39)	1.90	2.86	3.27	6.33
Fixed Income							
Blmbg:Aggregate	2.90	6.14	8.74	5.32	4.30	3.82	4.39
Blmbg:TIPS	4.24	6.01	8.28	5.05	3.75	3.52	4.00
Blmbg:Long Gov/Credit	6.23	12.82	18.91	10.32	8.98	7.84	7.08
Blmbg:Long Credit A	9.19	8.44	15.19	8.86	8.69	7.79	6.50
Blmbg:HY Corp Cash Pay	10.18	(3.79)	0.05	3.34	4.79	6.69	6.84
Blmbg:Muni 1-10 Yr	2.69	2.12	3.83	3.29	2.97	3.09	3.58
Blmbg:Glb Agg xUSD	3.38	0.61	0.71	2.52	2.89	1.98	2.85
Blmbg:Glb Agg xUSD Hdg	1.76	2.28	4.00	4.94	4.49	4.20	4.26
JPM:EMBI Plus	9.06	(0.40)	1.23	2.66	4.91	5.53	6.45
Other Assets							
Blmbg:Commodity TR Idx	5.08	(19.40)	(17.38)	(6.14)	(7.69)	(5.82)	(4.34)
S&P GSCI	10.47	(36.31)	(33.90)	(8.71)	(12.54)	(8.53)	(8.40)
S&P:Gold Spot Price Ix	12.77	18.21	27.36	13.17	8.97	3.75	9.90
FTSE:NAREIT Equity Index	11.82	(18.71)	(13.04)	0.03	4.06	9.05	6.02
Alerian:MLP Index	50.18	(35.71)	(41.43)	(16.79)	(12.85)	(1.41)	2.64

Source: Callan PEP database as of 6/30/2020

CAPITAL MARKETS REVIEW & OUTLOOK

Second Quarter 2020



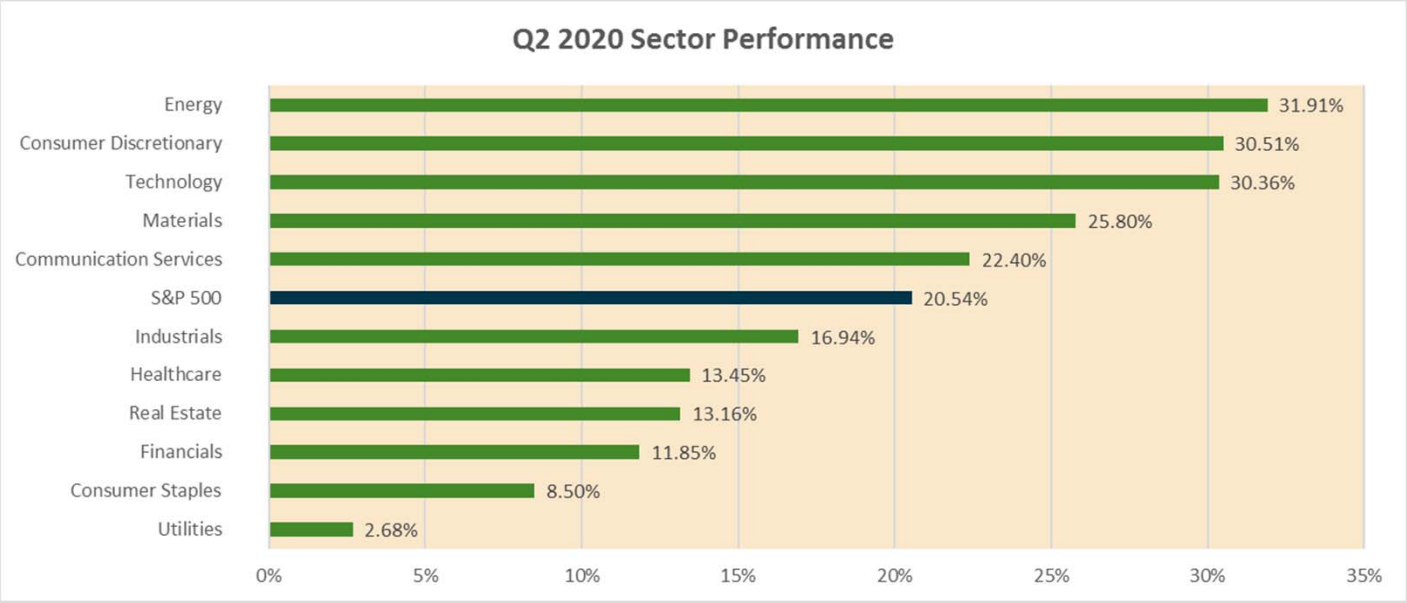
MAJOR MARKET INDICES (AS OF 6/30/2020)

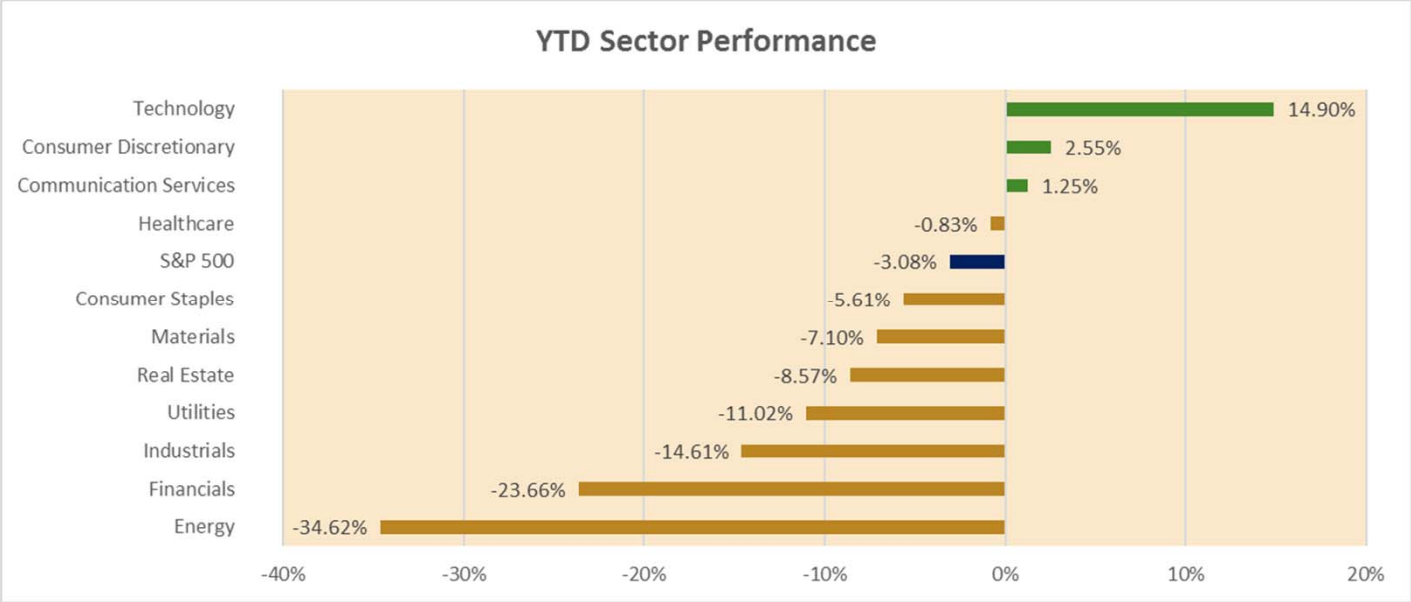
Domestic Equity	2020 Q2	YTD	Annualized 1 Year	5 Year	10 Year	P/E Ratio TTM
S&P 500	20.5%	-3.1%	7.5%	10.7%	14.0%	22.7
Russell 3000	22.0%	-3.5%	6.5%	10.0%	13.7%	22.0
Russell 1000 Value	14.3%	-16.3%	-8.8%	4.6%	10.4%	17.0
Russell 1000 Growth	27.8%	9.8%	23.3%	15.9%	17.2%	32.3
Russell 1000	21.8%	-2.8%	7.5%	10.5%	14.0%	22.4
Russell 2000	25.4%	-13.0%	-6.6%	4.3%	10.5%	15.9
Russell 2500	26.6%	-11.1%	-4.7%	5.4%	11.5%	17.1
International Equity	**2020 Q2**	**YTD**	**Annualized 1 Year**	**5 Year**	**10 Year**	**P/E Ratio TTM**
MSCI ACWI Ex US	16.3%	-10.8%	-4.4%	2.7%	5.5%	16.3
MSCI EAFE	15.1%	-11.1%	-4.7%	2.5%	6.2%	17.5
Emerging Markets	18.2%	-9.7%	-3.0%	3.2%	3.6%	14.5
Fixed Income	**2020 Q2**	**YTD**	**Annualized 1 Year**	**5 Year**	**10 Year**	**Yield**
Barclays Aggregate	2.9%	6.1%	8.7%	4.3%	3.8%	1.3%
Barclays Universal	3.8%	5.2%	7.9%	4.4%	4.1%	1.8%
Other	**2020 Q2**	**YTD**	**Annualized 1 Year**	**5 Year**	**10 Year**	**Value**
US Dollar	-1.7%	1.0%	1.3%	0.4%	1.2%	$97.39
WTI	93.4%	-35.8%	-33.5%	-7.2%	-6.0%	$39.27
Gold	10.5%	16.5%	28.7%	8.8%	4.0%	$1,781

- Q2 saw a stark reversal from the March 23rd market lows, aided by monetary and fiscal stimulus.
- As markets rebounded, Growth was the clear winner with heavy weightings to technology and communication stocks. The performance divergence between Growth and Value are reaching record highs.
- Small caps have underperformed for the year, but did rebound stronger in the second quarter, and domestic equities continue to outperform international.
- Despite severe dislocation in many parts of the bond market, the Barclay's Aggregate produced positive returns.
- Oil recovered from an historic negative price in the futures market and hovers around $40 as supply/demand imbalances work themselves through the system.
- Gold has continued to rally as a safe haven, despite the equity market recovery.

Source: Koyfin, Morningstar

SECTOR PERFORMANCE

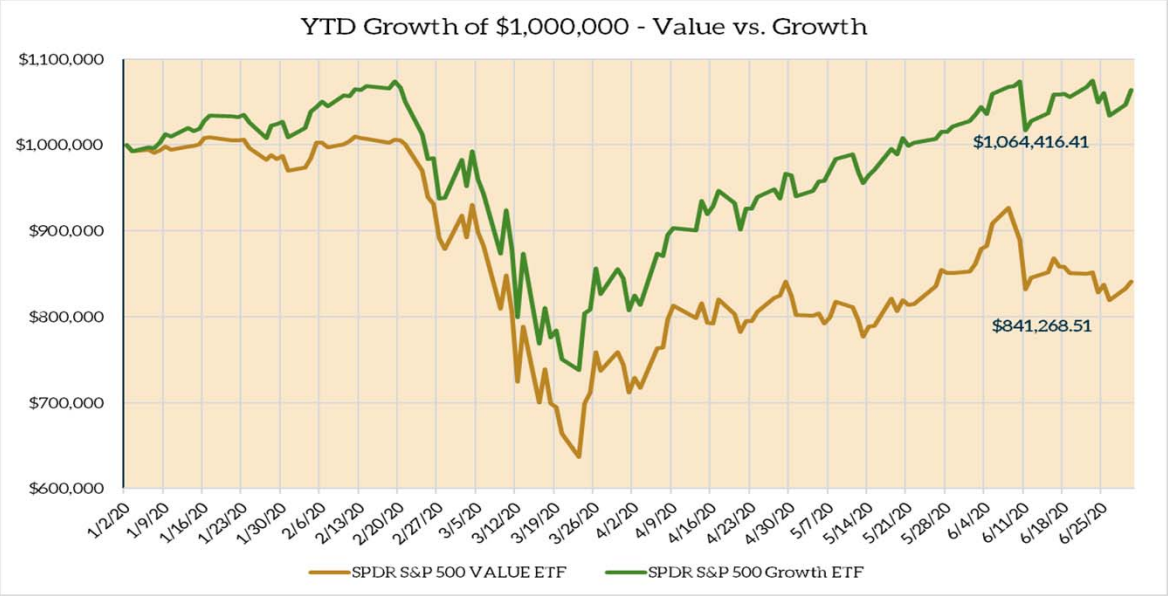




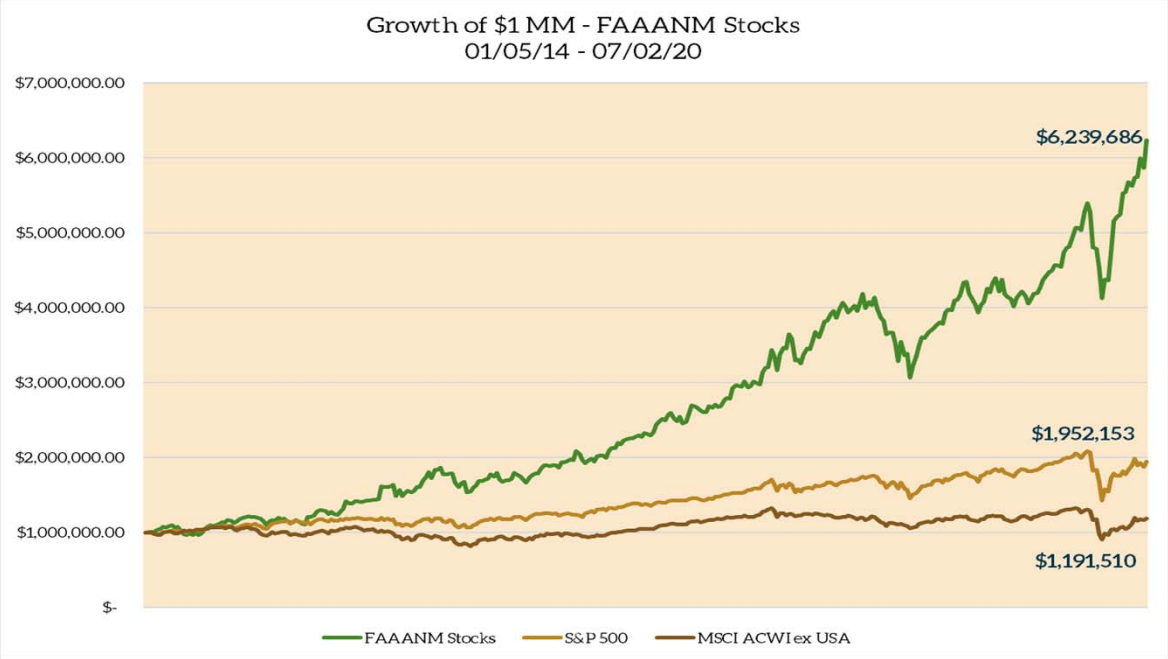
- Energy became the best performing sector for the quarter, but is still on par to be the worst sector year to date.
- Technology, communication services, and consumer discretionary remain the only positive performing sectors for 2020.

Source: Morningstar

HOW LONG CAN THIS LAST?

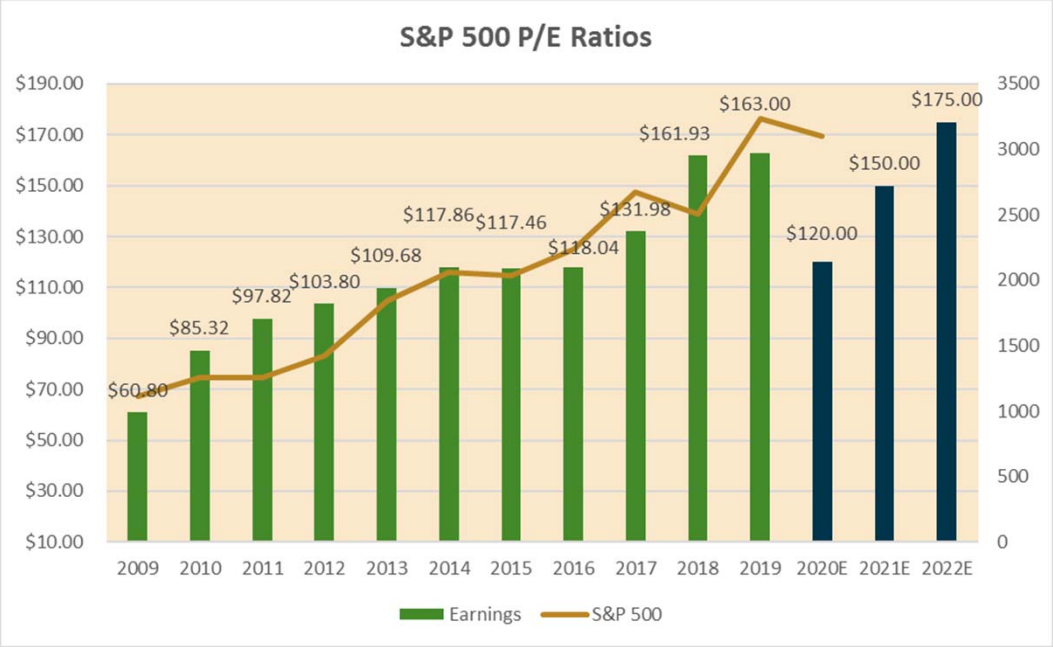


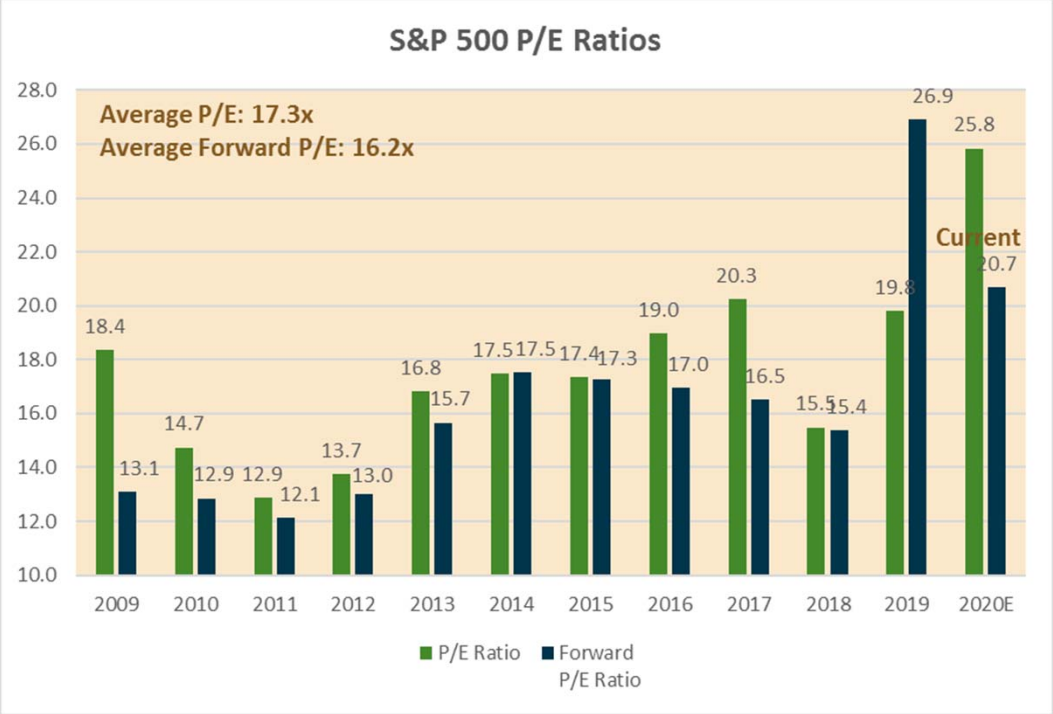
- Technology now composes roughly 28% of the S&P 500
- Since 2015, the vast majority of the stock market's performance has been concentrated in only six stocks.



Source: Morningstar, Yahoo Finance, The Wall Street Journal

EARNINGS AND VALUATION

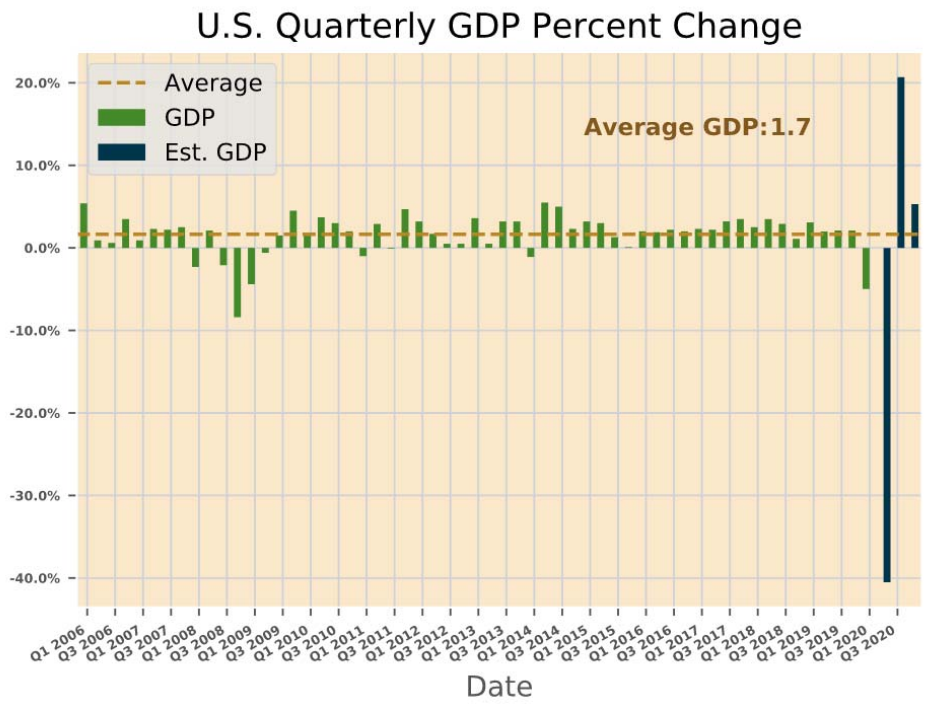




- Earnings are completely unpredictable at this point in time with 40% of S&P 500 companies pulling forward guidance for 2020.
- At a price of 3100, the S&P is currently pricing in a 20.6x forward P/E for 2021 at earnings of $150.

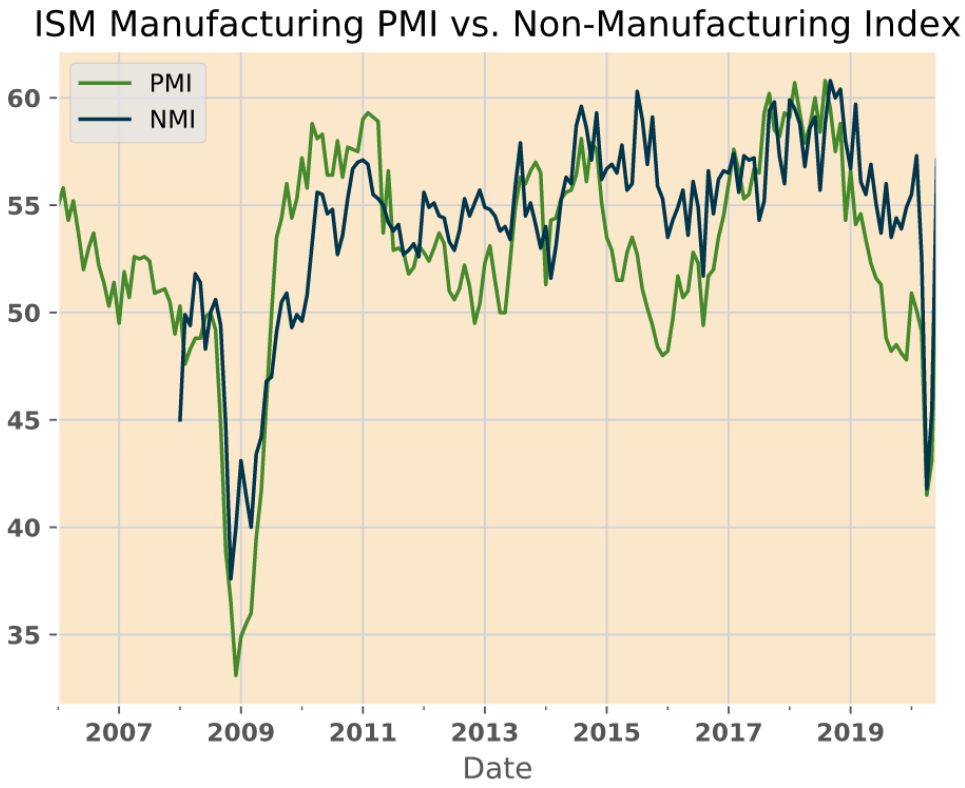
Source: Yardeni Research, Yahoo Finance

GROSS DOMESTIC PRODUCT



Estimates:
2020 Q2 – -40.5%
2020 Q3 – 20.7%
2020 Q4 – 5.3%

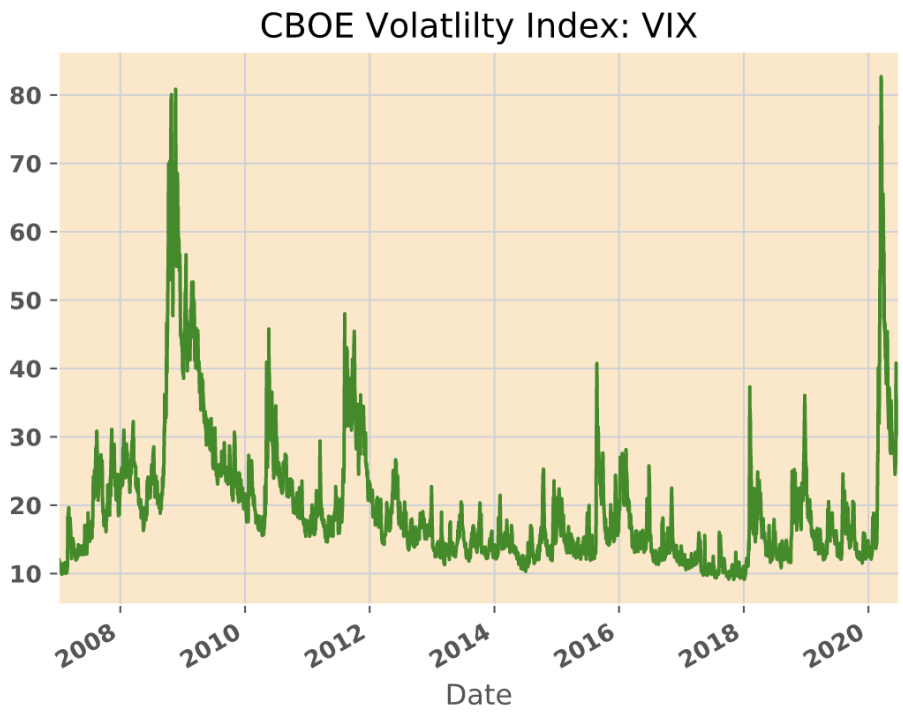
- GDP has fallen sharply, though increased fiscal and monetary stimulus will provide some support.



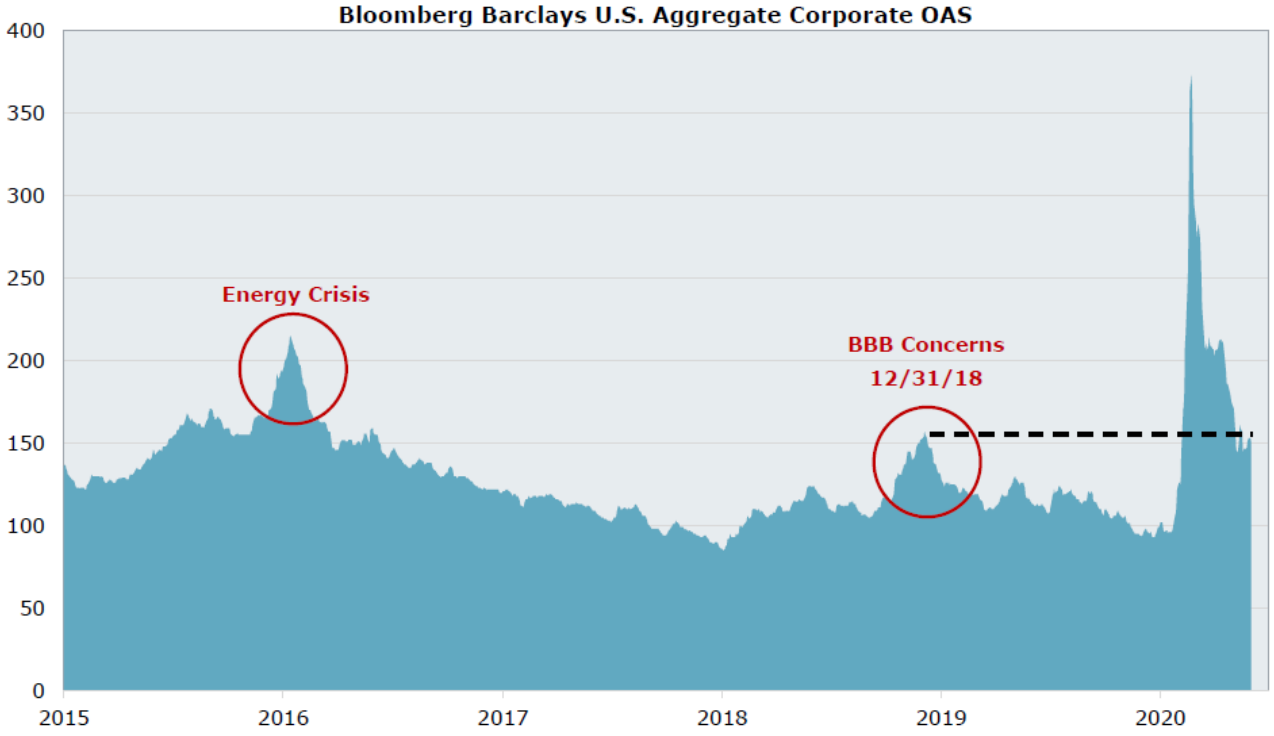
- Both manufacturing and service industries sharply contracted in Q2 due to forced closures and decreased demand.

Source: Federal Reserve Economic Database, Yardeni Research

UNPRECEDENTED PANIC

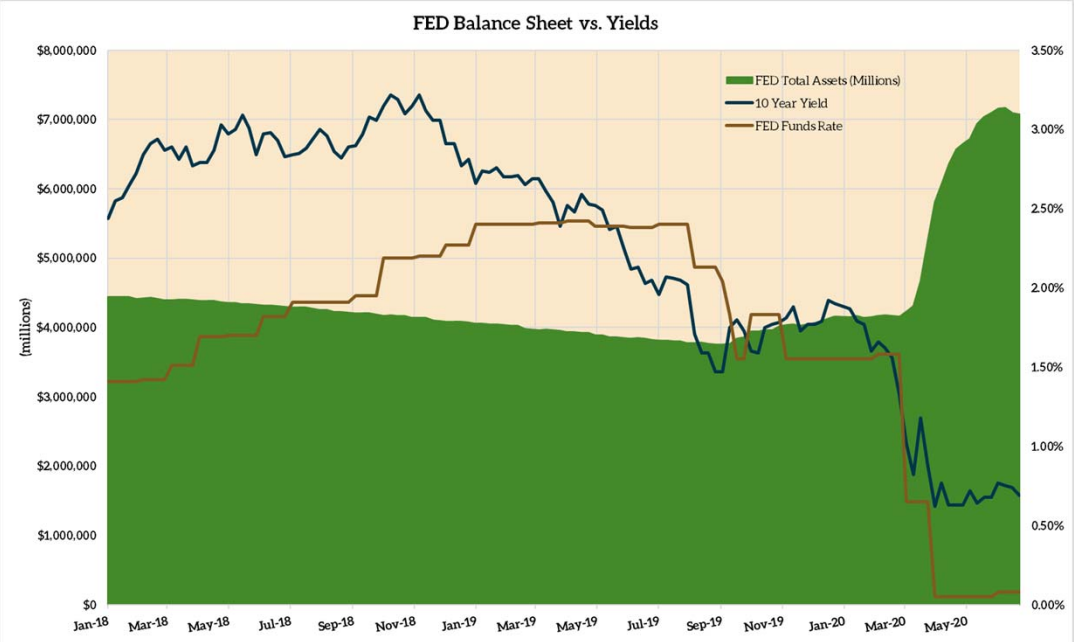


- Equity and bond markets alike, experienced enormous shock
- Volatility and credit spreads spiked, but reversed under Fed intervention, but still remain elevated from more normalized levels

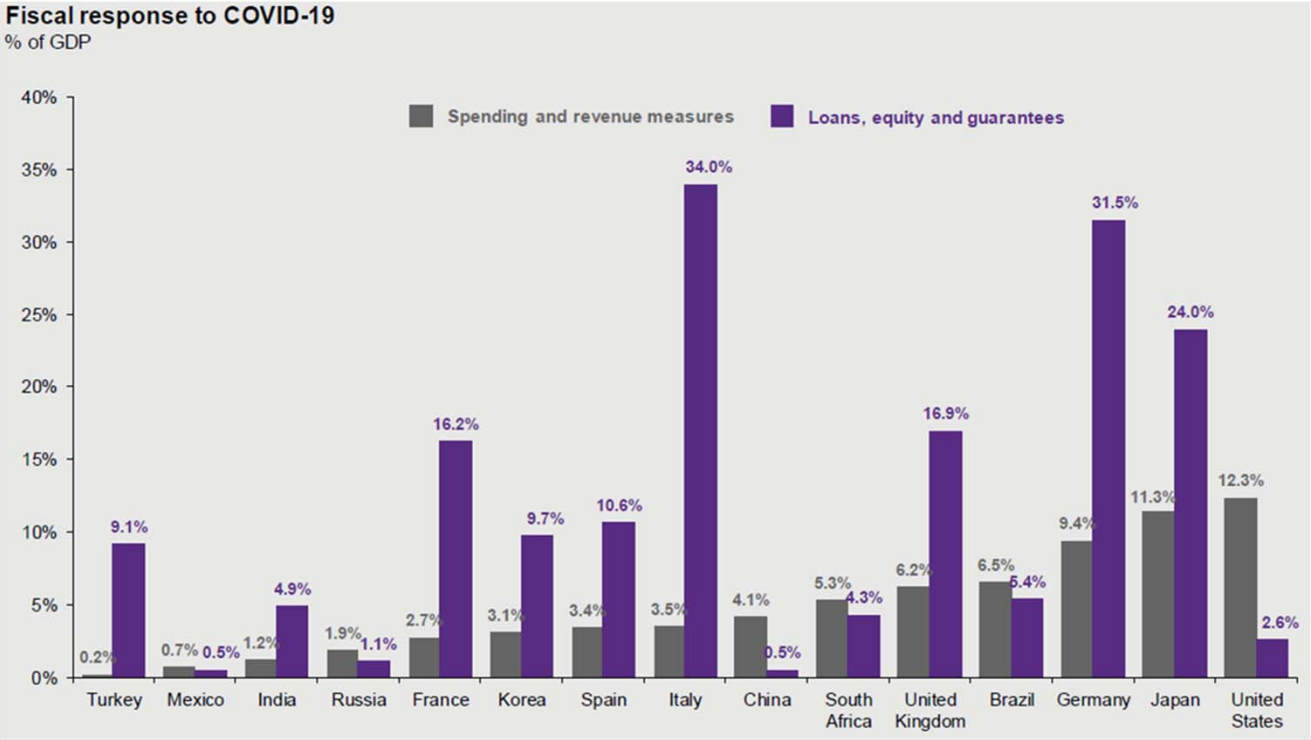


Source: Yahoo Finance, Baird Advisors

UNPRECEDENTED RESPONSE



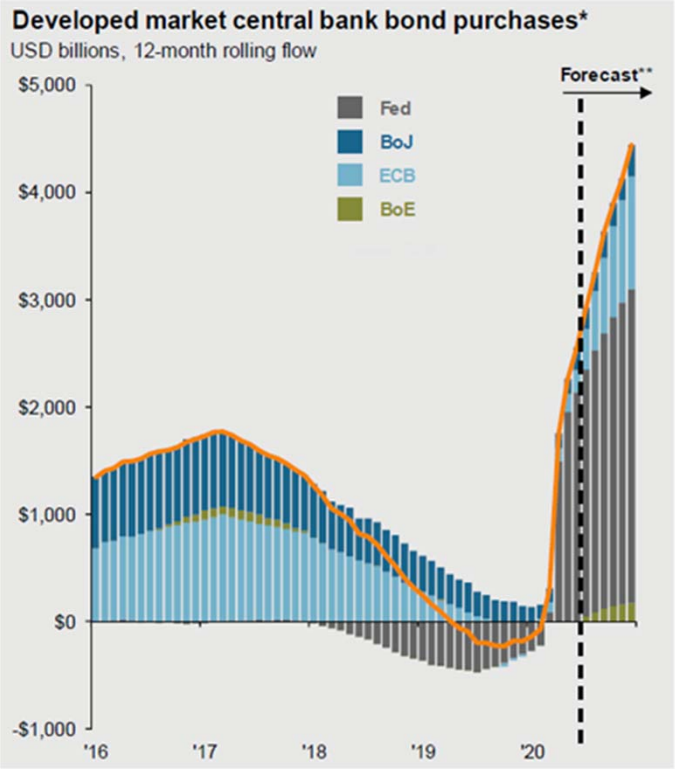
- The Fed has nearly doubled the size of its balance sheet in response to COVID and severe market dislocation.
- Global fiscal response is unprecedented, with the US currently contributing roughly 15% of GDP through fiscal and monetary response.



Source: Federal Reserve Economic Database, U.S Department of the Treasury, and JP Morgan

GLOBAL ECONOMICS & TRADE

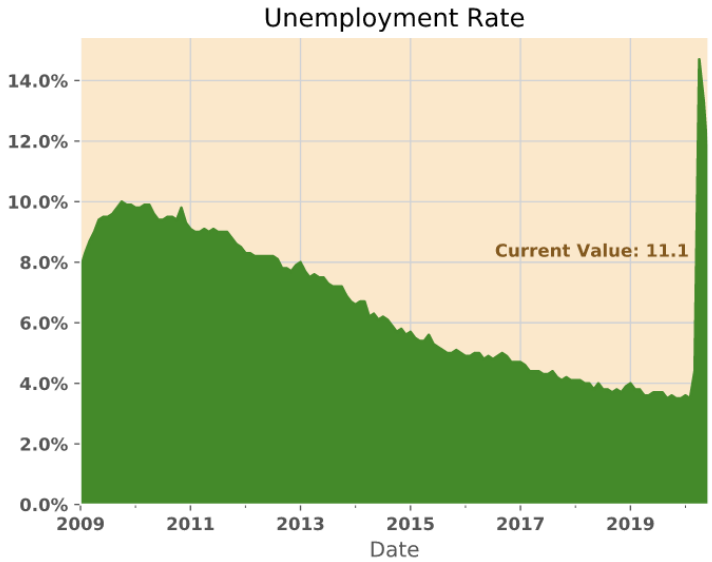
	GDP QoQ	GDP YoY	Core CPI YoY	Retail Sales	Industrial Production	Policy Rate	10Y Yield	Govt Debt/GDP	Jobless Rate
United States	-4.80%	0.30%	1.20%	-6.10%	-15.30%	0.25%	0.63%	106.90%	11.10%
Euro Zone	-3.80%	-3.30%	0.90%	-19.20%	-28.00%	-0.42%	n/a	84.10%	7.40%
China	-9.80%	-6.80%	1.10%	-2.80%	4.40%	3.85%	2.90%	50.50%	5.90%
Japan	-0.90%	-2.00%	-0.20%	-13.70%	-14.40%	-0.10%	0.03%	238.20%	2.90%
Germany	-2.20%	-2.30%	1.20%	-6.50%	-25.30%	-0.42%	-0.45%	59.80%	3.90%
United Kingdom	-2.00%	-1.60%	1.20%	-13.10%	-24.40%	0.10%	0.16%	81.70%	3.90%
France	-5.80%	-5.40%	0.60%	-31.10%	-34.20%	-0.42%	-0.13%	98.10%	7.80%
India	1.10%	3.10%	n/a	n/a	-16.70%	4.00%	5.89%	69.62%	11.00%
Italy	-4.70%	-4.80%	0.80%	-26.30%	-42.50%	-0.42%	1.34%	134.80%	7.80%
Brazil	-1.50%	-0.30%	2.16%	-16.80%	-27.20%	2.25%	6.84%	75.79%	12.90%
Canada	-2.10%	-0.90%	0.70%	-32.50%	-5.17%	0.25%	0.53%	90.60%	13.70%
Russia	0.60%	1.60%	2.90%	-19.20%	-9.60%	4.50%	5.95%	14.60%	6.10%
South Korea	-1.30%	1.30%	0.30%	-2.30%	-4.50%	0.50%	1.36%	36.60%	4.50%
Australia	-0.30%	1.40%	1.80%	2.30%	2.50%	0.25%	0.89%	45.10%	7.10%
Spain	-5.20%	-4.10%	1.10%	-31.60%	-33.60%	-0.42%	0.51%	95.50%	14.41%
Mexico	-1.60%	-1.60%	3.60%	-23.80%	-29.30%	5.00%	5.82%	45.50%	2.90%
Indonesia	-2.41%	2.97%	2.65%	-16.90%	-0.80%	4.25%	7.21%	29.80%	4.99%
Turkey	0.60%	4.50%	10.32%	-19.30%	-31.40%	8.25%	11.50%	33.10%	13.20%
Switzerland	-2.60%	-1.30%	-0.60%	-19.90%	0.80%	-0.75%	-0.43%	41.00%	3.40%
As of:	3/31/2020	3/31/2020	5/31/2020	5/31/2020	5/31/2020	6/30/2020	6/30/2020	12/31/2019	6/30/2020

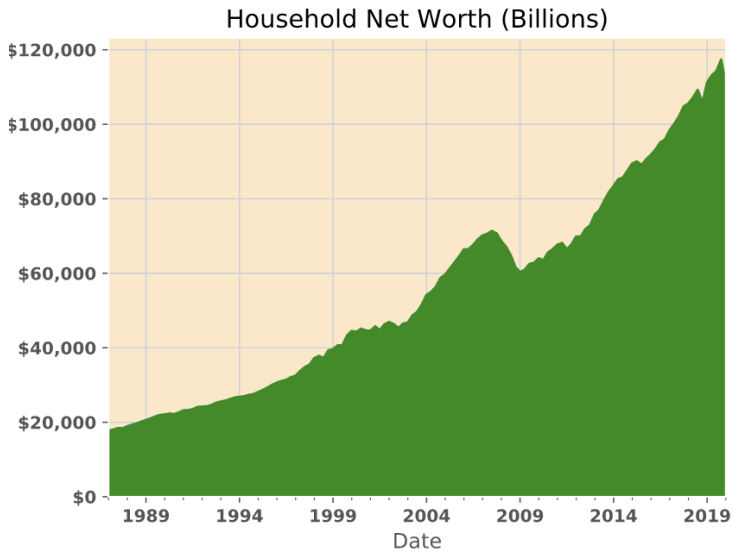


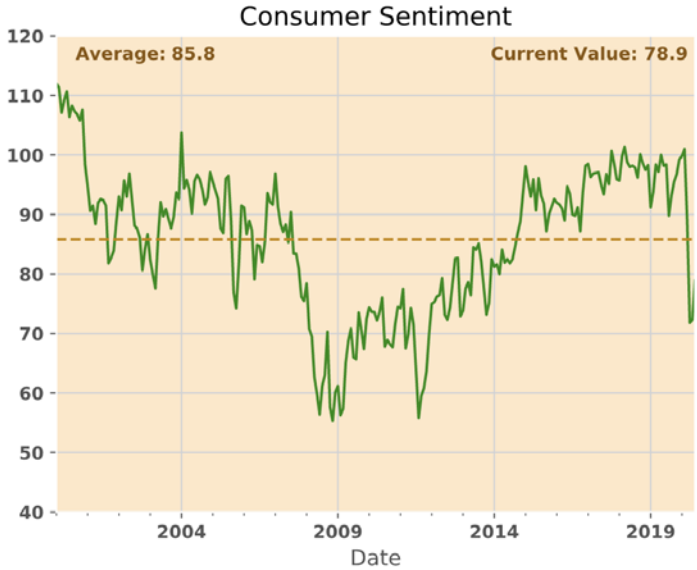
- Global GDP, Retail Sales, and Industrial Production are falling in lockstep due to the virus.
- Central banks around the world are forced to increase their balance sheets through bond purchases, reversing the trend seen since 2017.

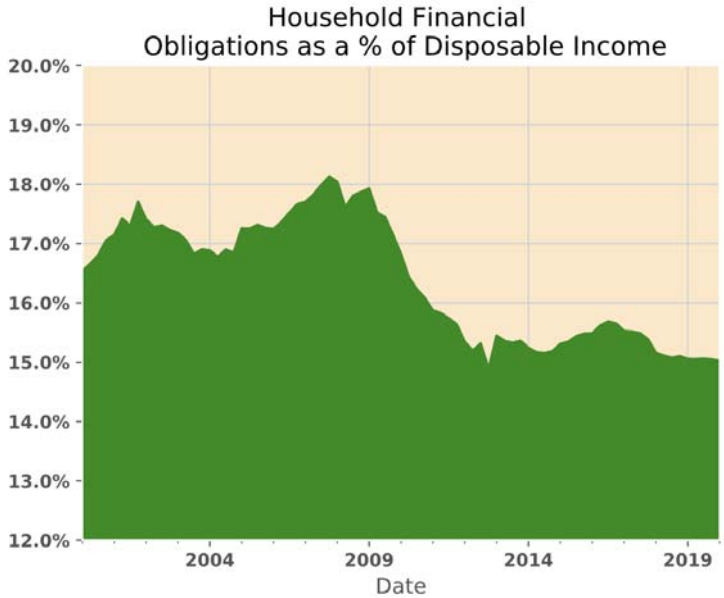
Source: Koyfin, J.P. Morgan

THE STATE OF THE US CONSUMER







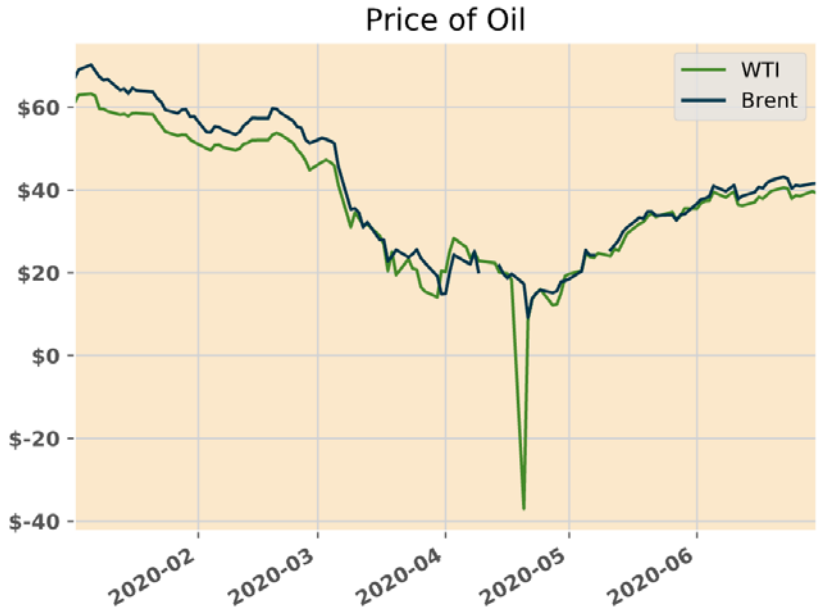


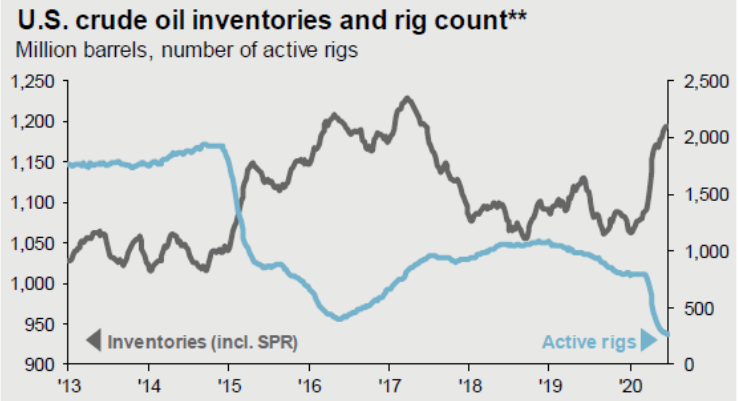
- Unemployment and Consumer Sentiment made a sharp reversal to their multi-year trends, which have steadily improved since the Great Recession.
- On a positive note, the consumer was much healthier entering this crisis, with household net worth at all time highs and lower debt levels.

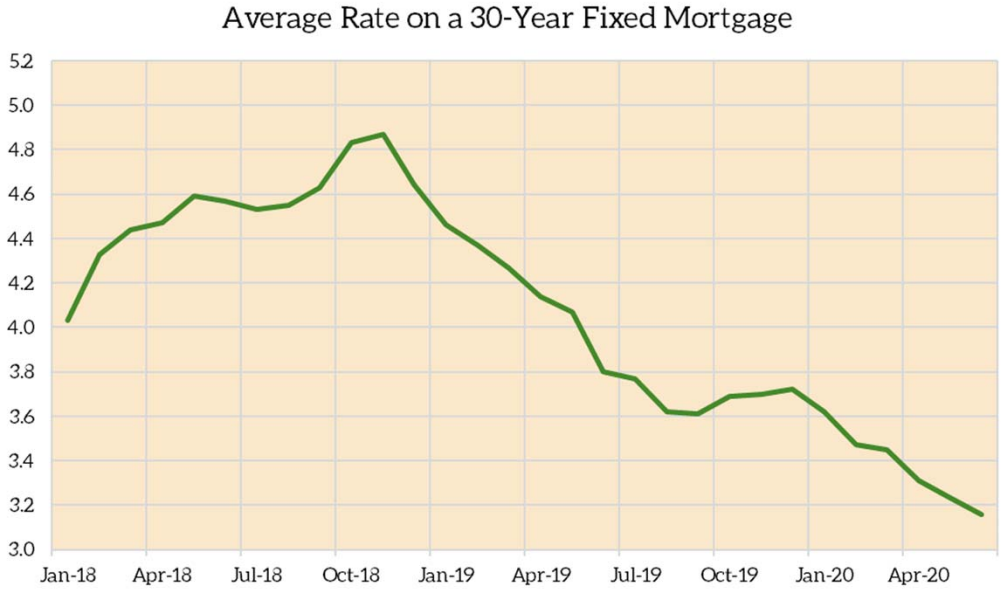
Source: Federal Reserve Economic Database

ADDITIONAL CONSUMER SUPPORT

- While the energy industry is struggling, low oil prices are beneficial to a struggling consumer.
  - US Rig counts have fallen quickly and the global supply imbalance is now only oversupplied by 2 million bbd, which should reduce as air travel increases.
- In addition, mortgage rates are at all time lows, helping to stimulate refinancing and new home purchases.



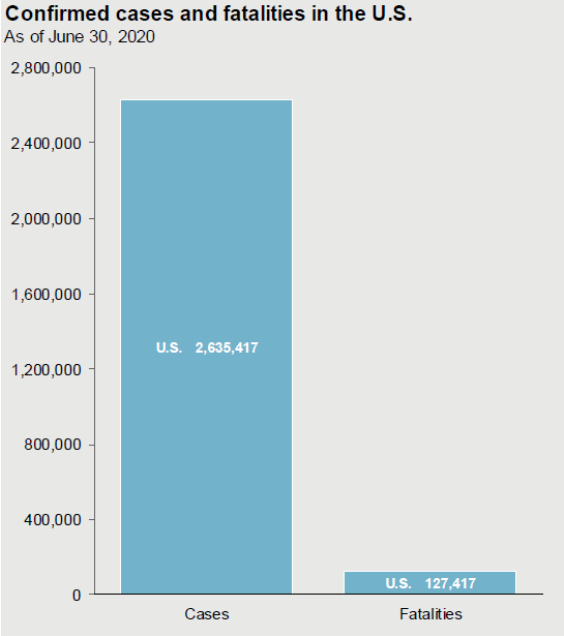


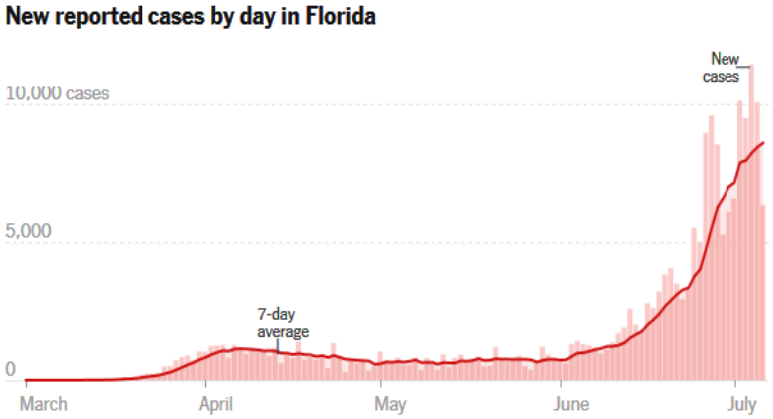


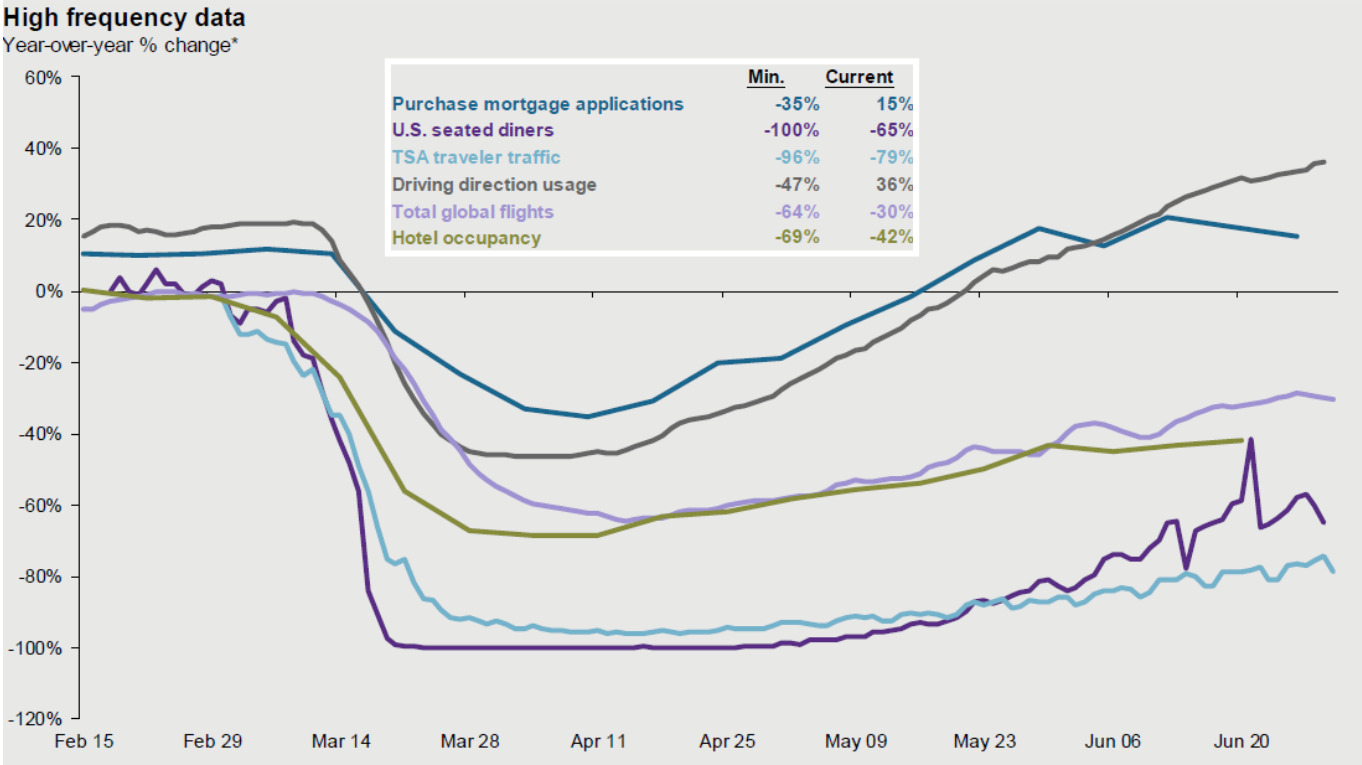
Source: Federal Reserve Economic Database, Freddie Mac, The Wall Street Journal, J.P. Morgan

BUT HOW LONG WILL THE RECOVERY TAKE?

- Recent spikes in cases, forcing cities to pause re-openings is tapping the breaks on a return to normalcy



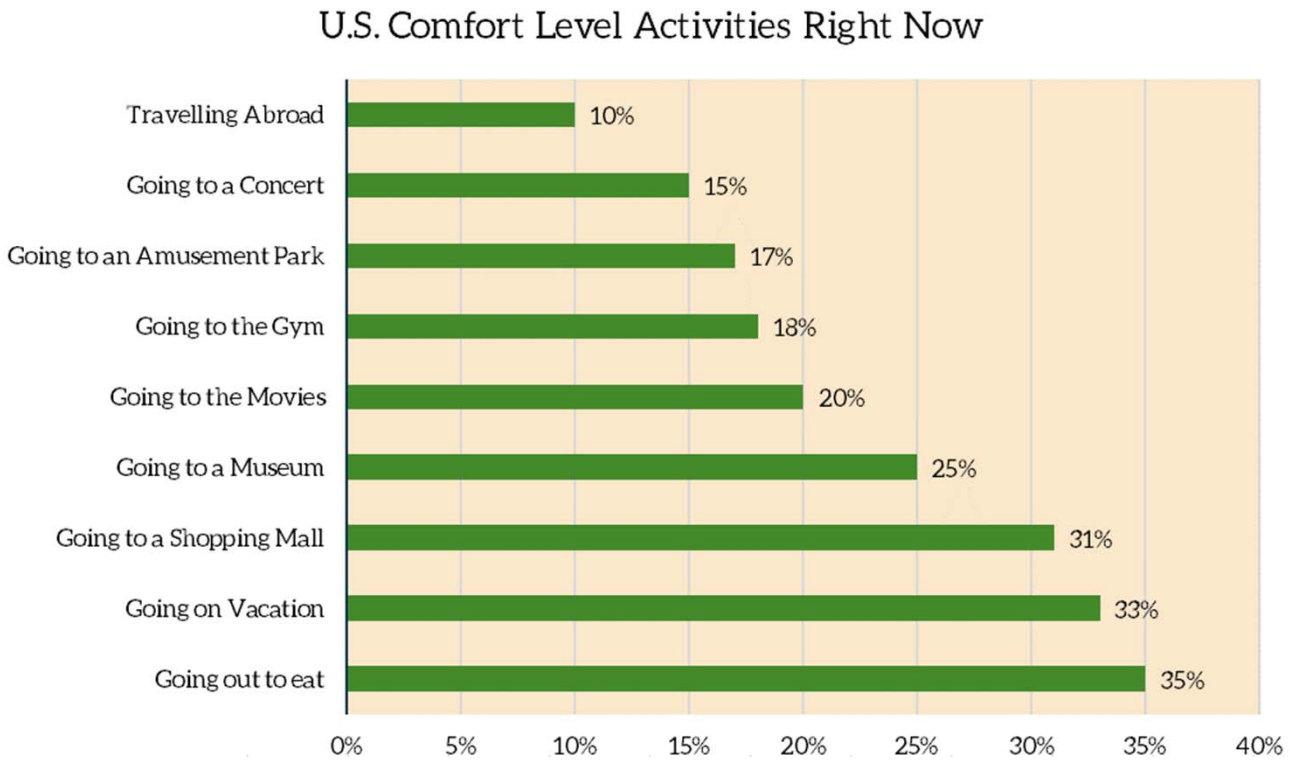




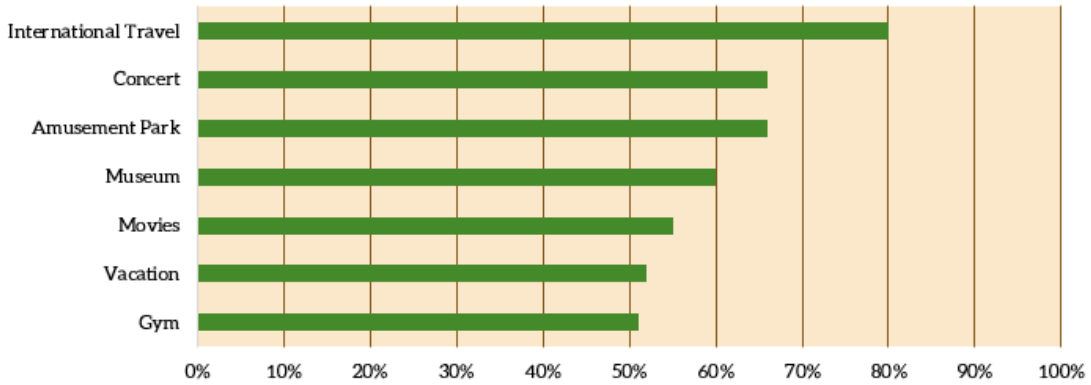
Source: Federal Reserve Economic Database, Freddie Mac, The Wall Street Journal, J.P. Morgan

THE ROAD TO RECOVERY

"A full recovery is unlikely until people are confident that it is safe to reengage in a broad range of activities." – Jerome Powell, Federal Reserve Chairman



% of Americans who answered "Six Months or Later" when asked "How much time will pass before you feel comfortable doing these activities?"



Gym	Vacation	Movies	Museum	Amusement Park	Concert	International Travel
51%	52%	55%	60%	66%	66%	80%

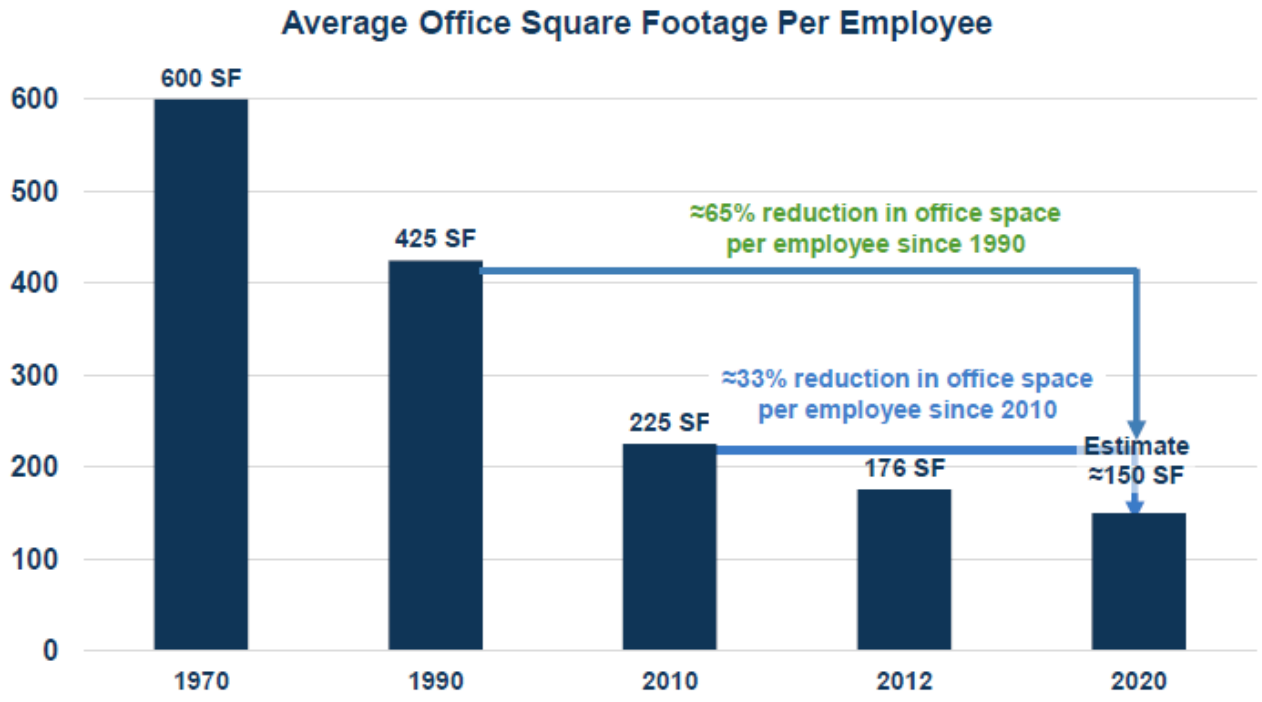
Source: The Wall Street Journal

THE FUTURE OF REAL ESTATE

- We see COVID resulting in longer term trends in real estate, which we are closely monitoring.
- While some companies will embrace more physical space, others will downsize and increase the usage of telecommuting.
- Retail has already been trending to online, and there will be increased demand for industrial data centers and towers for 5G.

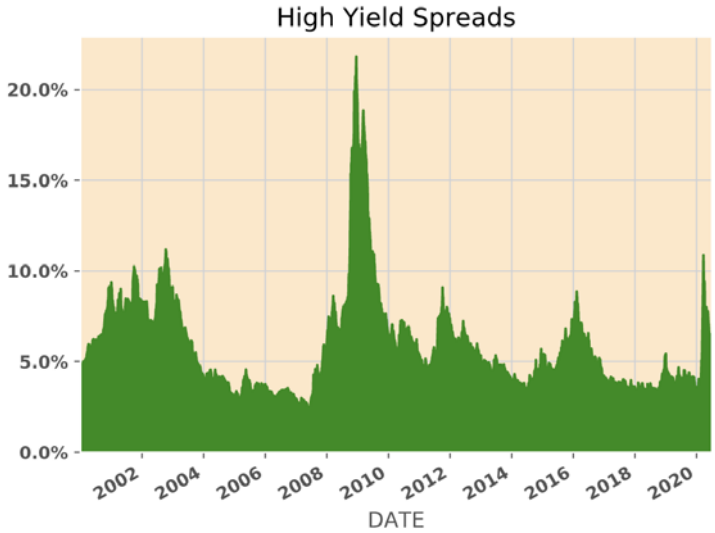
Office: The Impact of Social Distancing

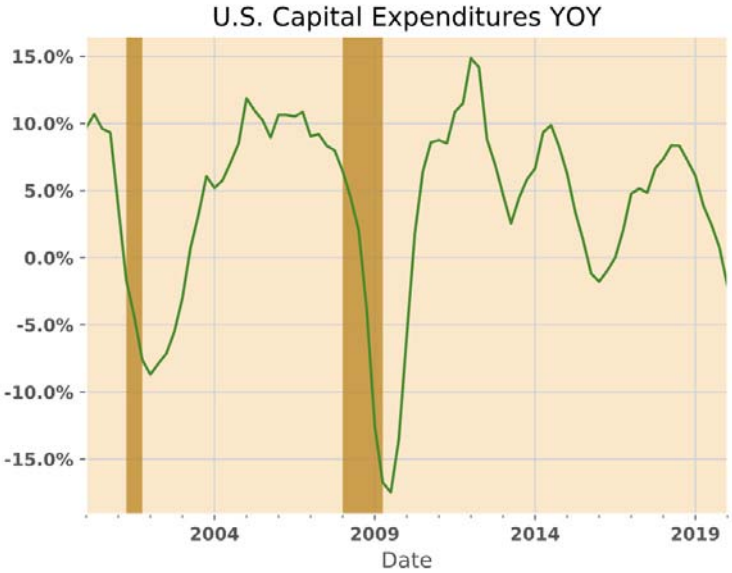
COVID-19 Will Likely Reverse the Decades-Long Trend of Compression in Space Per Employee

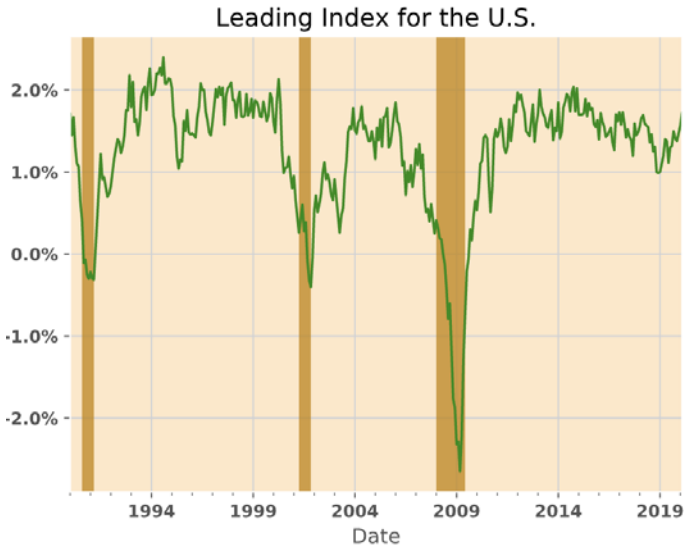


Source: UBS, Cushman & Wakefield, Brookfield Research

US ECONOMIC INDICATORS



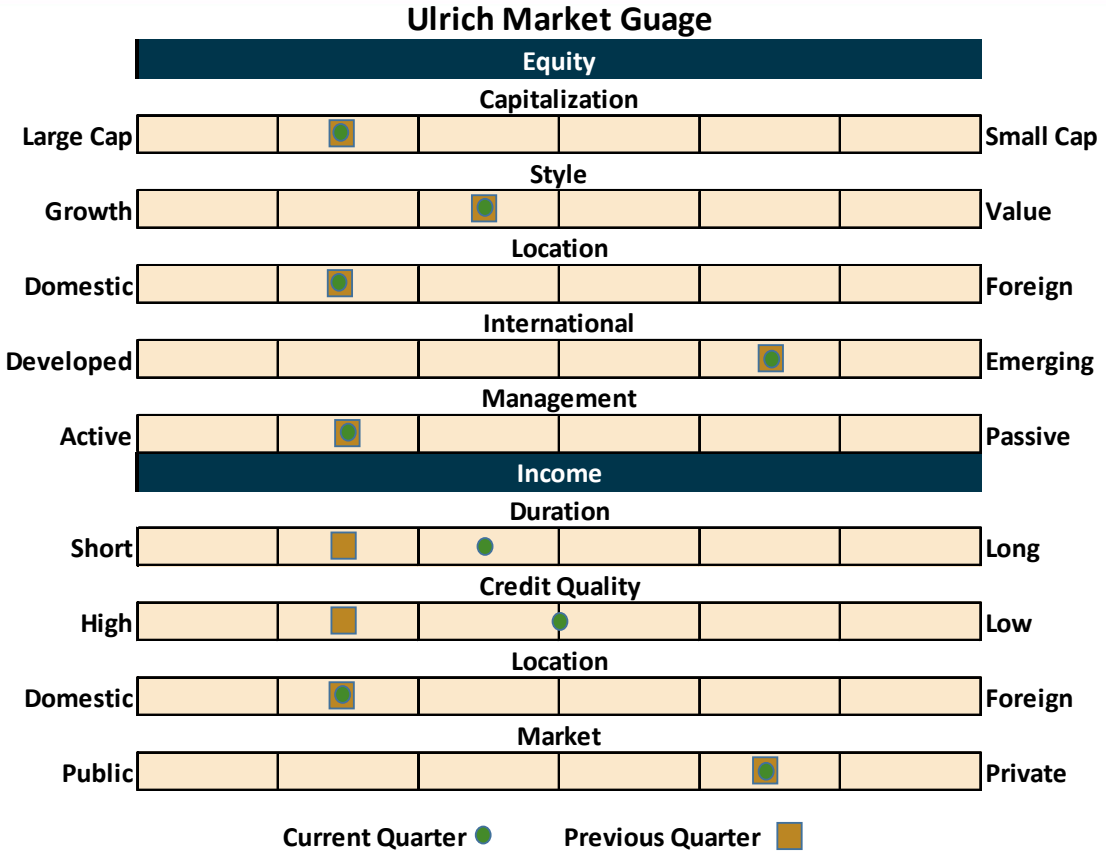




- While fundamentals are weak, we would expect a quicker recovery from this Coronavirus induced recession.

Source: Federal Reserve Economic Database

SUMMARY AND OUTLOOK



- Despite significant interruptions in the market place, our overall thesis regarding portfolio asset allocation is little changed.
  - We remain overweight to US equity over international, overweight equities to bonds, and overweight technology, innovation and consumer services.
  - We have tilted market cap downward, and will continue to do so.
  - Emerging markets look more attractive compared to developed countries based on growth expectations and current valuation.
  - Active management should become more important as earnings should be more of a driver going forward.
- Given the substantial run up in Growth, we will look to rebalance portfolios to bring them more in line with our target allocations.
- We continue to diversify our income producing assets to incorporate a broader range of asset classes that provide a more attractive risk/return profile.
- We do expect volatility to continue as more economic data emerges and as we near the 2020 election. We have increased cash holdings to position for this expectation.