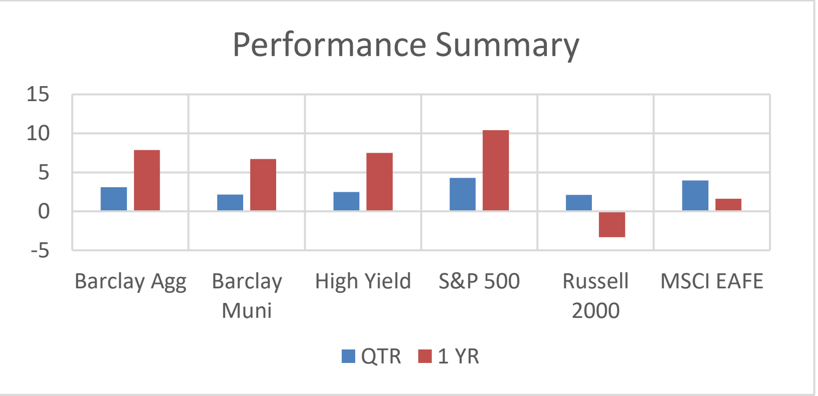
After a ‘risk off’ May, risk assets recovered losses quickly in June. Dovish central banks around the world led to lower interest rates and propelled the rally in risk assets. The major US equity indices were all positive for the quarter as the S&P 500, Russell Midcap and Russell 2000 increased 4.3%, 4.1% and 2.1% respectively. International stocks returns were mixed as developed markets gained 4.0% and emerging market equities eked out a 0.7% gain. Fixed income returns were positive across the board as core bonds, muni and high-yield bonds rose 3.0%, 2.1% and 2.5% respectfully. Global diversified bonds gained 5.6% for the quarter. Below are some of our thoughts for the 2nd half of 2019.



Thoughts on the 2nd half of 2019:

Economy- investors spend far too much time analyzing every wiggle and report about the economy. They would be better served by simply differentiating the trend from the cycle. Prior to the Great Recession, GDP growth of 3% or higher seemed normal for the US. However, the pace of economic growth since the Great Recession (GR) has been much slower, averaging only 2.3% thru the end of 2018. With growth the past two years averaging around 2.7%, many were led to believe the economy could return to its pre GR growth rates. However, it’s likely that recent tax cuts and spending policies simply pulled forward demand and growth trend is likely to revert back to a slower level. The Federal Reserve Bank of San Francisco, in a recent research paper, estimates the long-term growth rate in the US is in the range of 1.5 to 1.75%. These trends are likely to persist primarily due to easily predictable demographic trends, leading to slower labor force growth and ongoing slow productivity growth.

The Fed and interest rates- in late June, Jay Powell and the Federal Reserve signaled a clear change in tone, becoming more dovish. As of late June, the market is pricing in a high likelihood of three or more Fed rate cuts in 2019 and a fourth by the end of 2020. Near term, any rate cuts should keep interest rates well contained. However, if rates are held low for too long it increases the likelihood inflationary pressures will build, ultimately forcing the Fed to hike rates sooner than they otherwise would have. In general, we suggest an underweight allocation to bonds, staying underweight duration and holding some inflation protection securities.

Foreign and emerging market stocks- dovish central banks have driven global interest rates lower, and increased the odds the economy will recover in the 2nd half of 2019. With the Fed signaling future interest rate cuts, the US dollar is likely to be pressured lower, benefitting the performance of foreign assets. We are optimistic on the long-term return potential of foreign stocks, particularly emerging market value stocks.

Bull and Bear points of view- the current investment cycle is long in the tooth, and walking a fine line between extending the rally and the next bear market. The bull case is centered on an economic recovery in the 2nd half, with inflation and interest rates staying low. While the bear case is based on financial excess, central banks choking off growth, higher inflation and lower earnings. The battle rages on and is too early to call.

Trends/Risks- here is a quick rundown of the key trends and risks we are watching:

- **China-** slower economic growth, especially if the trade war escalates, could lead to problems for their heavily indebted economy.
- **Politics and Populism-** an increase in populism could pose a danger to the global economy. Escalating trade wars have the potential to reach a tipping point, causing business confidence and spending to retreat.
- **Demographics-** aging populations are weighing on global economies and can strain government finances in the major economies.
- **Financial Market Vulnerability-** debt, algorithmic trading, liquidity concerns and other excesses in the financial market have the potential to exacerbate any downturns.

Asset Class		* ↔ Neutral weight ↓ Underweight ↑ Overweight
Equities	***View****	***Comments***
U.S. Large Cap	↓	In global portfolios we are underweight US stocks in favor of other asset classes, primarily due to valuation. Within the category we would emphasize Quality-at a-Reasonable-Price (QARP), dividend paying stocks over non-paying stocks. If/when the risk of recession increases we would further reduce exposure to both large and small/mid cap stocks.
U.S. Small/Mid Cap	↓	We remain underweight small/mid-cap stocks due to relatively high valuations and concerns about high debt levels. Small/Mid-caps tend to perform best early to mid in the business cycle, and we view the current cycle as being in the later stages.
International Developed	↔	We are neutral on foreign developed stocks near-term. However, investors with a longer time horizon should be overweight based on reasonable valuations, a potential upswing in corporate earnings and looser monetary policy. On a five year time horizon we expect foreign developed markets to outperform US markets.
Emerging Markets	↑	For long-term global portfolios we would be overweight emerging markets, with an emphasis on value. We believe the US $ may be peaking, fundamentals and valuations are reasonable, and expect EM to outperform both US and foreign developed markets LT.

Fixed Income		
Investment Grade	↓	With the 10- year treasury yield near or below 2% we are maintaining our under-weight rating, and would keep some bond exposure in cash reserves which offer competitive yields and good liquidity. We recommend keeping some exposure for disciplined risk management, diversification purposes and to hedge reinvestment risk.
High-Yield Bonds	↓	We are underweight high-yield and believe valuations are too high given the current late stage of the business cycle. We like to own high-yield early in the business cycle when spreads are wide and valuations are cheap, today spreads are tight and valuations rich.
Municipal Bonds	↔	We are neutral on municipal bonds, however they remain attractive for high tax-bracket investors and we would overweight them in taxable portfolios. The supply/demand outlook for municipal bonds is favorable and should benefit holders going forward.
TIPS	↑	Given the low level of unemployment and interest rates available on core bonds we are favorable on TIPs as a hedge against higher inflation. Especially in tax-deferred accounts.
Floating-Rate Loans	↓	We are underweight and remain concerned about the amount and quality of loans being issued, and don't believe they warrant the additional risk.
Emerging Markets	↔	We believe investors with a higher risk tolerance should consider adding some exposure to this asset class.

Alternatives		
Absolute-Return/Alternatives	↑	We like this asset class and believe it can improve the risk/reward profile of portfolios that hold traditional asset classes. Our expectation is this asset class will perform in-between bonds and stocks over a full market cycle.
REITs	↓	The decline in interest rates this year has led to a strong rally in REITs, reducing our outlook for future performance. With cap rates declining and debt levels increasing our expectation future returns will be lower. We are reducing exposure to this asset class.
Commodities/Gold	↔	We view commodities as an effective way for long-term investors to diversify their portfolios and hedge against higher inflation. We expect the performance of commodities to improve and believe small positions in gold are suitable as a hedge against geopolitical and monetary policy risk. Gold has broken out form a long-term base and the performance of gold stocks has improved

U.S. Stocks

Market Performance, Second Quarter 2019

Index	Q2 2019	1 YR
S&P 500	4.30%	10.42%
Russell 1000	4.25%	10.02%
Russell 1000 Value	3.84%	8.46%
Russell 1000 Growth	4.64%	11.56%
Russell Midcap	4.13%	7.83%
Russell 2000	2.10%	(3.31%)

Source: Morningstar

- Volatility increased sharply during the quarter. After a sharp sell-off in May markets reached new highs in June.
- Growth stocks regained their dominance over value stocks and have outperformed by over 5% YTD. As the next cycle emerges we believe value has the potential to outperform growth by a wide margin but investors will have to remain patient to capitalize.
- Our preference is to tilt portfolios towards quality-at a-reasonable-price (QARP) and dividend paying investment strategies.

International Stocks

Market Performance, Second Quarter 2019

Index	Q2 2019	1 YR
MSCI EAFE	3.97%	1.60%
MCSI EME	0.74%	1.61%
MSCI BRIC	(0.13%)	3.52%

Source: Morningstar

- Foreign developed markets lagged during the quarter and lag the major U.S. indices YTD. Slower economic growth and geopolitical concerns weighed on their relative performance. Longer-term we expect foreign stocks to outperform their US counterparts, although capitalizing on this trend will require patience.
- We continue to see signs the US $ may be peaking. Speculation among traders is aggressively predicting a higher US Dollar in 2019, this is usually a good contrary indicator. If the Dollar does sell-off we think it will be a catalyst for better foreign stock performance

Fixed Income

Market Performance, Second Quarter 2019

Index	Q2 2019	1 YR
Vanguard Total Bond Index	3.05%	7.75%
Barclays Muni Bond	2.14%	6.71%
Barclays US Corp High-Yield	2.50%	7.48%
JPM GBI- EM Global Diversified	5.64%	8.99%
iShares TIPS Bond	2.77%	4.59%
BofA Merrill Lynch 3 month Treasury Note	0.64%	2.27%

Source: Morningstar

- Core and municipal bonds generated solid gains as interest rates dropped. With interest rates at current levels we would be underweight core bonds, keep durations relatively short and overweight cash. The technical outlook for municipals continues to be favorable.
- High-yield bonds snapped back after a tough finish to 2018. Given relatively tight spreads over high quality bonds we suggest using the current rally as an opportunity to reduce exposure.

Alternative Assets

Market Performance, Second Quarter 2019

Strategies	Q2 2019	1 YR
PIMCO All Asset All Authority	2.13%	3.02%
AQR Diversified Arbitrage	2.55%	4.36%
Gateway	1.16%	1.66%
Vanguard REIT	1.55%	12.41%
BNY Mellon Global Real Return	4.23%	9.74%

Source: Morningstar

- REITs were one of the best returning asset classes during the quarter. However, given the low level of interest rates and relatively high valuations we are reducing exposure to this asset class.
- We like alternative assets as a strategic way to reduce risk and increase absolute returns in portfolios. We plan to maintain a position in alternative assets unless we see a significant pullback in traditional assets (stocks and bonds).

Appendix:

Benchmark Definitions

U.S. Equity		Description
S&P 500	Index	The index includes 500 leading US companies and captures approximately 80% coverage of available market capitalization.
Russell 1000	Index	The Russell 1000 Index measures the performance of the large-cap segment of the U.S. equity universe and includes approximately 1000 of the largest securities. The Russell 1000 represents approximately 92% of the U.S. market.
Russell 1000 Value	Index	The Russell 1000 Value Index measures the performance of the large-cap value segment of the U.S. equity universe. It includes those Russell 1000 companies with lower price-to-book ratios and lower expected growth values.
Russell 1000 Growth	Index	The Russell 1000 Growth Index measures the performance of the large-cap growth segment of the U.S. equity universe. It includes those Russell 1000 companies with higher price-to-book ratios and higher forecasted growth values.
Russell Midcap	Index	The Russell Midcap Index measures the performance of the mid-cap segment of the U.S. equity universe. It includes approximately 800 of the smallest securities based on a combination of their market cap and current index membership.
Russell 2000	Index	The Russell 2000 Index measures the performance of the small-cap segment of the U.S. equity universe. It includes approximately 2000 of the smallest securities based on a combination of their market cap and current index membership.
International Equity		**Description**
MSCI EAFE	Index	The EAFE (Europe, Australasia, Far East) index consists of 21 developed market country indexes, excluding the US & Canada. It is a free float-adjusted market capitalization index that is designed to measure the equity market performance of developed markets.
MCSI EME	Index	The index is a free float-adjusted market capitalization index that is designed to measure equity market performance of emerging markets and includes 23 emerging market countries in the index.
MSCI BRIC	Index	The index is a free float-adjusted market capitalization weighted index that is designed to measure the equity market performance of the following four emerging market country indexes: Brazil, Russia, India and China.

Fixed Income		Description
Vanguard Total Bond Index	Index Fund	This index measures a wide spectrum of public, investment-grade, taxable, fixed income securities in the United States—including government, corporate, and international dollar-denominated bonds, as well as mortgage-backed and asset-backed securities, all with maturities of more than 1 year.
Barclays Aggregate Bond	Index	The U.S. Aggregate Index covers the USD-denominated, investment-grade, fixed-rate, taxable bond market of SEC-registered securities. The index includes bonds from the Treasury, Government-Related, Corporate, MBS (agency fixed-rate and hybrid ARM pass-through bonds), ABS, and CMBS sectors.
Barclays Muni Bond	Index	The U.S. Municipal Indices cover the USD-denominated long term tax exempt bond market. The index has four main sectors: state and local general obligation bonds, revenue bonds, insured bonds, and pre-refunded bonds.
Barclays US Corp High-Yield	Index	The index covers the USD-denominated, non-investment grade, fixed-rate, taxable corporate bond market and excludes Emerging Markets debt.
JPM GBI- EM Global Divers	Index	The index tracks returns for actively traded external debt instruments in emerging markets. Included in the index are US-dollar denominated Brady bonds, Eurobonds, and traded loans issued by sovereign entities.
iShares TIPS Bond	ETF	The iShares TIPS Bond ETF seeks to track the investment results of an index composed of inflation-protected U.S. Treasury bonds.
BofA Merrill Lynch 3 month Treasury Note	Index	The 3-month US Treasury Note Index is comprised of a single issue purchased at the beginning of the month and held for a full month. At the end of the month, that issue is sold and rolled into a newly selected issue.
Alternative Assets		**Description**
PIMCO All Asset All Authority	Mutual Fund	The investment seeks maximum real return, consistent with preservation of real capital and prudent investment management. The primary benchmark for the fund is the S&P 500, with a secondary objective of Consumer Price Index +650 basis points.
AQR Diversified Arbitrage	Mutual Fund	The investment seeks long-term absolute (positive) returns. It invests in a diversified portfolio of instruments, including equities, convertible securities, debt securities, loans, warrants, options, other types of derivative instruments.
Gateway	Mutual Fund	The investment seeks to capture the majority of the returns associated with equity market investments, while exposing investors to less risk than other equity investments. The fund invests in a broadly diversified portfolio of common stocks, while also selling index call options and purchasing index put options.

Alternative Assets		Description
Vanguard REIT	ETF	The investment seeks to provide a high level of income and moderate long-term capital appreciation by tracking the performance of a benchmark index that measures the performance of publicly traded equity REITs.
Dreyfus Global Real Return	Mutual Fund	The fund allocates its investments among global equities, bonds and cash, and, generally to a lesser extent, other asset classes, including real estate, commodities, currencies and alternative or non-traditional asset classes and strategies, primarily those accessed through derivative instruments.