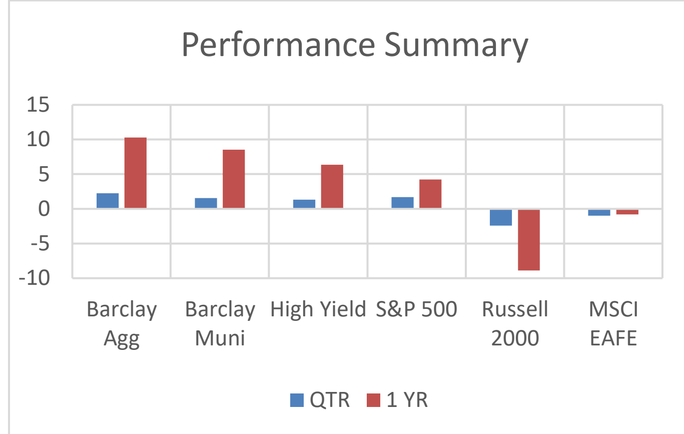
The third quarter was full of ups and downs for stocks as slowing economic growth became a reality. Growth in the second quarter slowed to 2.3% after averaging 2.9% in 2018. Recent economic data suggests growth will slow further, while increasing political and trade uncertainty are also weakening business and consumer confidence. The S&P 500 rose 1.7%, posting positive returns for the third straight quarter. Although, returns have diminished each quarter this year as Economic Policy Uncertainty Indices reach new highs. Small-cap stocks struggled, finishing the quarter down 2.4% and international stocks were down 1.0%. Core bonds were star performers, up 2.3%, as interest rates dropped in the face of the Federal Reserve cutting interest rates for the first time in a decade and global central banks moving towards easy monetary policy. Below are thoughts on a few big picture topics likely to impact financial markets in the year(s) ahead.



What a Second Fed Rate Cut Means for the Markets:

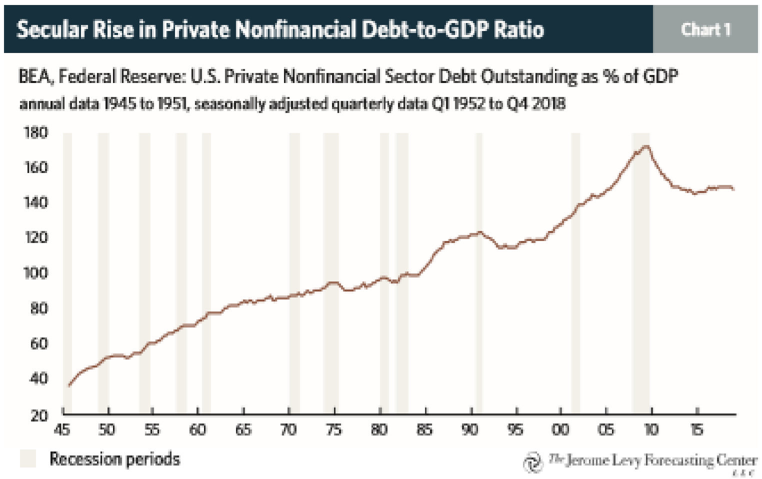
In mid-September the Federal Reserve cut interest rates for the second time, here are some thoughts on how that may impact the markets:

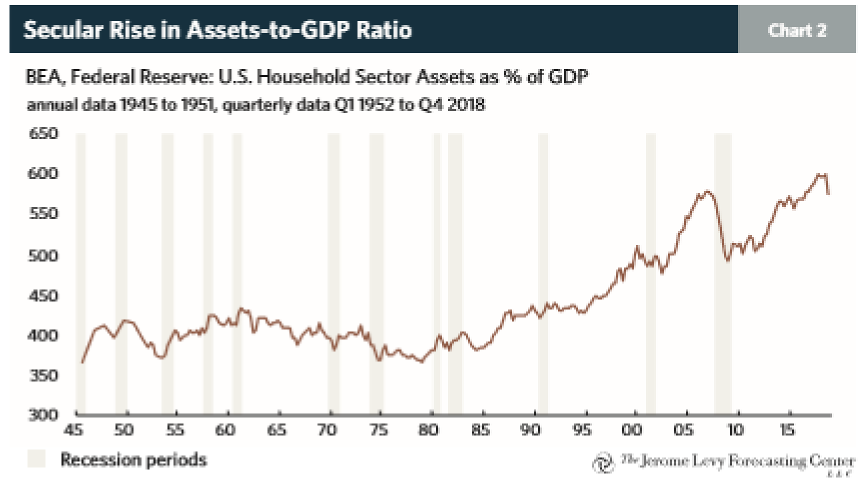
Stocks- historically a second rate cut is positive for the stock market. According to Ned Davis Research (NDR) there has been 19 instances of a second rate cut since 1921 and on average the stock market (DJIA) was up 20.3% one year later. The weakest stock market performances occurred when the Fed tried, and failed, to prevent a recession. The most recent examples being the recessions in 2001 and 2007, both of which had negative returns 12 months after the second rate cut. With the U.S. economy walking a tightrope, the future direction of economic growth will likely dictate stock performance in the coming year. If the economy reaccelerates we expect the recent cuts will lead to solid returns, however if the economy continues to slow and head towards recession, stocks are likely to correct. Given the current environment of economic and political uncertainty, combined with high stock valuations we suggest investors exercise some caution when allocating assets.

Bonds- the impact of a second rate cut on bonds has been mixed. The team at NDR studied the 11 instances since 1970, and found that 3 months after the second rate cut 10-year bond yields were higher in 9 of the 11 instances. While six months later 10-year yields were higher in 7 instances. With the 10-year yield approaching its all-time low yield in early September it makes sense to keep bond duration below benchmark. In simpler terms, interest rates have the potential to move higher in the year(s) ahead, suggesting it's not a great time to take a lot of interest rate risk. Keeping in mind that when interest rates rise the value of a bond decreases, which can lead to losses in bond portfolios.

The Big Balance Sheet Economy:

Private sector balance sheets (non-government) have grown sharply relative to private sector income for several decades. The large growth in private balance sheets was led by huge growth in both debt and assets. To understand the magnitude of the growth in debt and assets in the U.S. it's easiest to compare them to the size of the economy (GDP), see the charts below. **It can be argued the disproportionate growth in balance sheets (debt and assets) relative to income changed the behavior of investors, making financial activity increasingly more volatile and encouraging riskier behavior.** Leading to each successive business cycle in the Big Balance Sheet Economy experiencing increasingly reckless behavior that led to even bigger balance sheets and ultimately leading to financial crisis ('00-'02 & '07-'09). Which made each successive recession more difficult to recover from, and required the government to engineer dramatic new lows in interest rates, heavy fiscal stimulus, and other measures to stabilize economic conditions. We are watching the growth in today's large balance sheets and watching for any signs of stress in the financial markets. Any underlying stress in the financial markets is likely to reveal itself when the next recession arrives and would warrant a shift to a more conservative asset allocations.





How Will the Fed Fight the Next Recession?

The Federal Reserve's recent rate cuts and the decline in longer-term rates have raised fears that the Fed's ability to ease financial conditions during the next recession will be limited. Historically, the Fed's primary tool to fight a recession has been to cut interest rates, with the average rate cutting cycle having been around 500 basis points (5%). Clearly, given the starting point of today's Fed Funds Rate (1.75-2.00%) that level of rate cuts isn't likely to happen. So what can the Fed do if a recession emerges and are risks higher than ever? Ultimately the Fed still has tools at its disposal, they may just need to be different. **The first line of defense will still be interest rate cuts,** however that will be limited, because the Fed has a stated preference not to pursue negative rates like its central bank counterparts in Europe and Japan. **The second tool will be forward guidance**. Which simply means they will explicitly announce economic thresholds to manage market expectations. For example, policy may remain loose until unemployment and/or inflation reach a certain target. **A third tool could be a return to quantitative easing (QE)** or the systematic purchasing of bonds to suppress interest rates. Lastly, if needed the Fed could implement new tools such as yield curve control or even take interest rates negative. **The bottom-line is today's low level of interest rates will make the Fed's job more challenging when the next recession arrives, however they still have tools at their disposal to help the economy recover.** Our biggest concern is the use of these tools could continue to inflate the Big Balance Sheet Economy discussed above. Of course, our elected officials could utilize fiscal policy to stimulate the economy, however that would require a level of bipartisan cooperation that's hard to envision in today's political climate. See the next page for details on our outlook for the major asset classes.

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 overweight value, Quality-at a-Reasonable-Price (QARP) and dividend 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, an improvement in LEIs and easy 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 peak in the next couple of years, fundamentals and valuations are reasonable, and expect EM to outperform both US and foreign developed markets long-term. Near-term, EM will be vulnerable if there is a global recession.

Fixed Income		
Investment Grade	↓	With the 10- year treasury yield near 1.5% we are maintaining our under-weight rating, and would move some bond exposure to 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	↔	This asset class can experience big performance swings and direct exposure may only be appropriate for higher risk tolerant investors.

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 performed well this year and may be overbought, however a small position still seems like a reasonable hedge in portfolios.

U.S. Stocks

Market Performance, Third Quarter 2019

Index	Q3 2019	1 YR
S&P 500	1.70%	4.25%
Russell 1000	1.42%	3.87%
Russell 1000 Value	1.36%	4.00%
Russell 1000 Growth	1.49%	3.71%
Russell Midcap	0.48%	3.19%
Russell 2000	(2.40%)	(8.89%)

Source: Morningstar

- Stocks were up and down during the quarter as concerns about slowing economic growth, political uncertainty and trade concerns grew. Small-cap stocks lagged as they often do late cycle when growth slows.
- The performance of growth and value stocks was comparable. 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, Third Quarter 2019

Index	Q3 2019	1 YR
MSCI EAFE	(1.00%)	(0.82%)
MCSI EME	(4.11%)	(1.63%)
MSCI BRIC	(4.48%)	3.02%

Source: Morningstar

- Foreign developed markets were down 1% for the quarter amid slower economic growth and geopolitical concerns. 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, Third Quarter 2019

Index	Q3 2019	1 YR
Vanguard Total Bond Index	2.40%	10.33%
Barclays Muni Bond	1.58%	8.55%
Barclays US Corp High-Yield	1.33%	6.36%
JPM GBI- EM Global Diversified	(0.79%)	10.13%
iShares TIPS Bond	1.39%	6.94%
BofA Merrill Lynch 3 month Treasury Note	0.56%	2.36%

Source: Morningstar

- Core and municipal bonds had strong gains as interest rates continued to fall. 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 lagged core bonds but had decent returns for the quarter. Given low yields and relatively tight spreads over high quality bonds we recommend an underweight position.

Alternative Assets

Market Performance, Third Quarter 2019

Strategies	Q3 2019	1 YR
PIMCO All Asset All Authority	(1.77%)	1.98%
AQR Diversified Arbitrage	0.54%	4.27%
Gateway	1.23%	(0.76%)
Vanguard REIT	7.42%	19.92%
BNY Mellon Global Real Return	0.59%	7.92%

Source: Morningstar

- REITs had a very strong quarter, up 7.4%. However, given the low level of interest rates and relatively high valuations we would use the recent rally to reduce 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.