



USAA MANAGED PORTFOLIOS

2019 First Quarter Update



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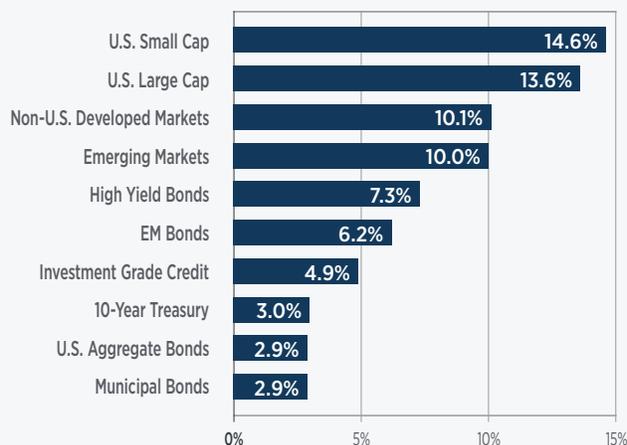


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FIGURE 1
STRONG 1Q FOR U.S. EQUITIES
YEAR TO DATE TOTAL RETURN



Indexes used: Bloomberg Barclays U.S. Municipal, Bloomberg Barclays U.S. Aggregate Bond, U.S. Benchmark 10-Year Govt, Bloomberg Barclays U.S. Credit, Bloomberg Barclays U.S. Corporate High Yield Bond, Standard & Poor's 500, J.P. Morgan Emerging Markets Bond Index Plus (EMBI+), Russell 2000, MSCI EAFE, MSCI Emerging Markets
Source: Thomson Reuters Datastream as of 3/29/2019

1Q RECAP

A stock recovery that started just after Christmas was a gift that kept on giving in the first quarter, with free delivery provided by the newly patient policymakers at the Federal Reserve. U.S. large caps and small caps got off to their fastest start in years despite a bleak outlook for earnings growth in the first quarter. Overseas equities shared in the bounty.

In late March, the Treasury yield curve inverted for the first time since 2007, and in doing so, instantly made recession risk a front-of-mind issue for many investors. On the other hand, strong stock returns helped ease the perceived risks for corporate bonds during the quarter.

MARKET OVERVIEW

The Obama family was still learning their way around the White House, the Great Recession had a few more months to run, and the Philadelphia Phillies were preparing to defend their first World Series title in nearly three decades (spoiler alert: they didn't) — this was all part of the American backdrop when the current bull market for stocks began on March 9, 2009.

FIGURE 2

U.S. STOCKS OFF TO BEST START SINCE FINANCIAL CRISIS

S&P 500 PERFORMANCE (TOTAL RETURN), 2009-2019



Source: Thomson Reuters Datastream

At 10 years and counting, it is just a couple of months shy of being the longest bull market in U.S. history and a fruitful one as well — on a total-return basis, the Standard & Poor’s 500 Index has gained more than 300% since hitting bottom amid the wreckage of the financial crisis. And age doesn’t appear to be an issue: The 13.6% return in the first quarter of 2019 (Figure 2) was the best start to a year since 1998.

The bull hasn’t charged along on its own — it has had plenty of help from a Federal Reserve that held interest rates at essentially zero for seven years, along with massive stimulus in the form of fiscal spending (remember “Cash for Clunkers”?) and later large-scale tax cuts. And while several market events left it wheezing — the 2013 “taper tantrum” when the Fed first hinted at monetary tightening, the dollar-led tumble in oil prices in 2014-16, and last year’s panic about slowing global growth — the bull managed to stay on its feet.

Growth worries have carried over into 2019, with a string of weak data coming out of Europe and China in recent weeks. The U.S. is feeling the slowing trend, with GDP growth stepping down each quarter since mid-2018 as the impact of the 2017 tax cuts fades. The latest estimates from the New York Fed calls for 1.3% real growth in the first quarter of 2019.

Nervous investors have rushed into the Treasury market, pushing up bond prices and driving down yields for longer-maturity bonds. In late March, the Treasury yield curve inverted for the first time since 2007 — the 3-month Treasury bill offered a higher income return than a 10-year Treasury note.

A yield-curve inversion generates attention because one has preceded every U.S. recession in the past half-century, but the timing variations limit its predictive power for investors. The period between inversion and recession has ranged from less than a year to more than two years, with the average gap around 14 months.

While we look to be late in the business cycle, we don’t see a recession on the horizon. The Fed’s clear signal that it intends to pause interest rate increases in 2019 appears to be relieving some market anxiety — after the yield curve inverted in January 2006, the Fed hiked rates four times. The apparent progress toward a U.S.-China trade deal could also be a positive.

FIGURE 3

JOB OPENINGS OUTNUMBER JOB HUNTERS

AVAILABLE POSITIONS VS. UNEMPLOYED, 2004-2019 (IN MILLIONS)

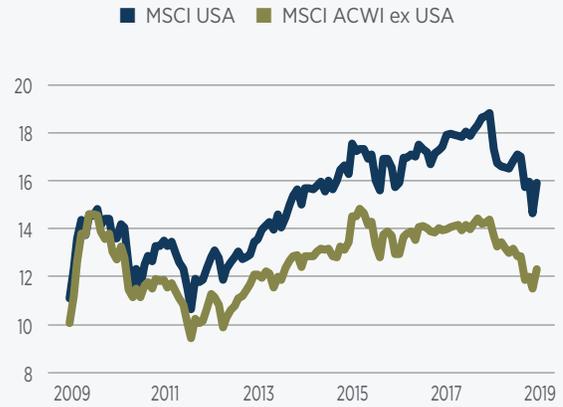


Source: Bureau of Labor Statistics

FIGURE 4

OVERSEAS EQUITIES APPEALING ON PRICE-TO-EARNINGS BASIS

MSCI USA INDEX VS. MSCI ALL-COUNTRY WORLD INDEX EX USA, 2009-19



Source: Thomson Reuters Datastream

Global equity markets look to be at a crossroads.

One fork leads back toward the “there is no alternative to U.S. stocks” mindset that prevailed for much of this decade. GDP growth trends are worse overseas and other key U.S. data looks stronger — unemployment under 4% with modestly rising wages, job openings outnumbering job seekers (Figure 3), and inflation closer to target rates. The U.S. manufacturing sector continues to expand, consumers continue to spend, and we have less exposure to a struggling China than other developed markets.

The other fork goes to a place where overseas markets overcome their current economic malaise and unruly politics, and in doing so, their favorable valuations (Figure 4) once again attract investor attention and investor cash. China engineers a soft landing for its economy with the helping hand of government and perhaps a trade deal, and this stimulates animal spirits among its investors that lift other emerging markets as well. Europe and Japan also benefit from a more robust China through export growth. Stability returns to the European Union, as Brexit and Italy’s various crises get solved.

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Current stock market behavior seems to be heavily driven by near-term positive sentiment for U.S. equities — volatility has dipped back into the docile zone last seen back in the fall, when the S&P 500 was at record levels.

But it’s important to remember that sentiment and volatility are prone to sharp swings, as we saw when stocks tanked at the end of 2018 and then fully rebounded in just a few weeks. No one knows where the market goes from here, but investors should be ready in case the ride turns out to be bumpy.

PORTFOLIO MANAGEMENT

Tactical positioning in USAA Managed Portfolios at the end of the first quarter favored fixed income assets over equities to reflect our cautious stance given heightened market uncertainties, particularly those related to global economic growth.

We shifted away from tactical positions in U.S. large cap and international developed stocks during the quarter, but maintained our tactical allocation to U.S. small caps. We believe small caps can benefit from the relative strength of the U.S. economy while being less exposed to China-related trade turmoil.

Our key themes heading into the second quarter:

U.S. EQUITIES

With the fast start out of the blocks, U.S. stocks are riding a wave of positive momentum as we move into 2Q. And as discussed above, even with GDP growth slowing from 2018's peppy pace, the U.S. outlook remains brighter than that of other major economies.

And with the Fed on hold and talk of boosting fiscal spending, we could easily envision the current rally continuing deeper into 2019. That said, we will be closely focused on 1Q earnings to see if the forecast of negative year-over-year growth comes to pass — equity prices tend to follow earnings.

FIXED INCOME

We had been concerned in late 2018 about the rising risk of a Fed overshoot on rates and its impact on corporate debt, but the central bank's decision to sit on its hands for a while has eased that concern. Slowing GDP growth, however, is still worrisome, as is the dour earnings growth outlook for U.S. equities. We leaned into high yield in January to take advantage of attractive prices available after December's selloff, and in February we bumped up our Treasury stake based on our view that U.S. equities may have gotten overextended.

As always, our guidance to members is to remain focused on the long-term investment plan that you have put so much thought into. For those USAA Managed Portfolio shareholders who may be uneasy about market risk in general or have concerns about current asset-class allocations, we suggest consulting with a USAA advisor.

FIGURE 5

UMP TACTICAL ALLOCATION AS OF 3/31/2019

ASSET CLASS	CHANGE	TACTICAL
US Large	▼	
US Small	—	✓
International Developed	▼	
Emerging Market	—	
Treasury	▲	✓
Investment Grade Credit	—	✓
High Yield	▲	✓
Emerging Market Debt	—	
Cash	—	

USAA MANAGED PORTFOLIOS INVESTMENT TEAM

Investment Philosophy

We believe in constructing global, actively-managed portfolios that aim to capitalize on market opportunities utilizing multiple asset classes, institutional managers, and investment factors including value, momentum, and corporate credit. We adhere to our disciplined research and portfolio construction process, even if it causes us to deviate from the crowd.

What We Do

- Build broadly diversified model portfolios to help you achieve your financial goals
- Set long-term allocations to help reduce risk and volatility along with a short-term allocation to maximize timely opportunities
- Monitor how investments and managers complement each other
- Rebalance to keep risk in-line
- Employ tax minimization strategies when warranted

We continually focus on global markets, economies and the geopolitical environment so you can focus on your life goals.

Core Competencies



\$21.4B

Assets Under Management*

147,000

Active Accounts*

* As of 12/31/18

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Diversification is a technique to help reduce risk. There is no absolute guarantee that diversification will protect against a loss of income.

Past performance is no guarantee of future results.

Asset allocation does not protect against a loss or guarantee that an investor's goal will be met.

Fixed income securities are subject to price volatility and a number of risks, including interest rate risk. Interest rates and bond prices move in opposite directions so that as interest rates rise, bond prices usually fall and vice versa. Interest rates are currently at historically low levels. Fixed income securities also carry other risks, such as inflation risk, liquidity risk, call risk, and credit and default risks. Lower-quality fixed income securities involve greater risk of default or price changes. Securities of non-U.S. issuers generally involve greater risks than U.S. investments and can decline significantly in response to adverse issuer, political, regulatory, market and economic risks. Fixed income securities sold or redeemed prior to maturity may be subject to loss. • Investments in foreign securities are subject to additional and more diverse risks, including but not limited to currency fluctuations, market illiquidity, and political and economic instability. Foreign investing may result in more rapid and extreme changes in value than investments made exclusively in the securities of U.S. companies. There may be less publicly available information relating to foreign companies than those in the U.S. Foreign securities may also be subject to foreign taxes. Investments made in emerging market countries may be particularly volatile. Economies of emerging market countries are generally less diverse and mature than more developed countries and may have less stable political systems.

The MSCI Emerging Markets Index is a free float-adjusted market capitalization index that is designed to measure equity market performance in the global emerging markets. • The MSCI EAFE Index covers 21 developed markets outside of North America: Europe, Australasia and the Far East. It aims to include in its international indices 85% of the free float-adjusted market capitalization in each industry group within each country. • The MSCI USA Index is designed to measure the performance of the large- and mid-cap segments of the U.S. equity market. The index covers approximately 85% of the free float-adjusted market capitalization in the U.S. • The MSCI World ex USA Index measure large- and mid-cap stock performance in 22 developed markets (U.S. excluded). The index covers approximately 85% of the free float-adjusted market capitalization in each country. • The Bloomberg Barclays U.S. Municipal Index covers the U.S. dollar-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. • The Bloomberg Barclays US Corporate High Yield Bond Index measures the U.S. dollar-denominated, high yield, fixed-rate corporate bond market. Securities are classified as high yield if the middle rating of Moody's, Fitch and S&P is Ba1/BB+/BB+ or below. Bonds from issuers with an emerging markets country of risk, based on Barclays EM country definition, are excluded. • The Standard & Poor's 500 Index is an unmanaged index of 500 stocks representing the large cap segment of the market, covering 75% of the U.S. equities market. • The S&P SmallCap 600 Index measures the small-cap segment of the U.S. equity market. The index is designed to track companies that meet specific inclusion criteria to ensure that they are liquid and financially viable. • The Russell 2000 Index is an unmanaged index that consists of the 2,000 smallest companies in the Russell 3000 Index. It is a widely recognized small cap index. • The Bloomberg Barclays U.S. Aggregate Bond Index is a widely recognized index used to track the performance of investment grade bonds in the U.S. • The Bloomberg Barclays U.S. Credit Index measures the performance of the investment-grade, taxable corporate and government-related bond market. It is composed of the Bloomberg Barclays U.S. Corporate Index and a non-corporate component that includes non-U.S. agency, sovereign, supranational and local authority bonds. • The JP Morgan Emerging Markets Bond Index Plus (EMBI+) tracks total returns for foreign currency-denominated, fixed-income securities issued in emerging markets.

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