MARCH 2017

Too Much Growling and Howling

Buffaloes Stampede Bears

Can you hear the bears growl? Have you heard the wolves howl? Both have recently drowned out the subtle grunts of the bulls or—as we have been known to call their less attractive family members—the buffaloes.

The latest, overly short-term, investment headlines have centered on the potential start to a 5% or more correction. Many are discussing the notions that the so-called Trump rally is over, equity valuations are too rich, and the "reflation trade" and bank stocks have had their day in the sun, given that long-term yields have exhaled recently.

In our opinion, this is more of a pause than a wholesale switch in positioning. We don't think it makes sense to get caught up in the daily headlines and noise that populate the airwaves and can be disproportionately based on pure speculation rather than on sound, specific analysis.

Perhaps we are in for a 5% correction. If this were to occur ahead of earnings, it would be a buying opportunity and would represent a re-set in the uptrend, in our view. The simple reason is that we are not basing our diversified portfolio view on the passage of new stimulus alone. The passage of tax reform and a new health care bill, in our opinion, would be additive to the present environment and would support animal spirits, but we are of the view that the profit cycle is more important.

We agree that investors have been increasing their risk asset allocation based on the potential for pro-growth policies this year. We estimate that the approximate 5% rise in U.S. equities year-to-date (through March 24) is mostly in anticipation of profit-enhancing

Chief Investment Office

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HIGHLIGHTS

We have moved from a "get paid to wait" core portfolio theme to a more cyclical- and value-oriented theme in multi-asset portfolios.

- Equities remain attractive versus fixed income on a relative basis, in our opinion.
- Within equities, we favor global large caps, U.S. small caps and Emerging Markets. We also favor value over growth and more cyclical assets versus defensives.
- Within fixed income, we prefer credit to Treasuries. We would also consider an allocation to Treasury Inflation-Protected Securities (TIPS), where appropriate.

The Wealth Allocation Framework

LIFE PRIORITIES

The Wealth Allocation Framework helps you put your goals and aspirations at the center of decisions about allocating your financial resources. **Asset categories within the framework include:**

- **Personal:** Individual investors have a desire for safety and personal financial obligations they want to meet regardless of market conditions. To safeguard essential goals, investors can hold lower-risk assets—but they have to accept lower returns in exchange.
- **Market:** When we invest, we strive to capture market growth most efficiently. Today, access to a broadening array of asset classes and types makes diversifying beyond stocks and bonds easier than ever before.
- **Aspirational:** Investors seek significant wealth mobility. To pursue goals that require higher-than-market returns, investors often need to take higher and concentrated risks.

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tax reform. However, there is more to the story than this "thick icing on the cake" stimulus. In our view, global investors are still climbing the wall of worry; skepticism regarding the rally is still high; a wave of long-term investing pools (pension funds, sovereign wealth funds, Millennial investment programs, prescriptive goals-based allocation re-balancing) has yet to begin a full-scale rotation; the supply of stock continues to decline versus 10 years ago; and, as long as profits remain healthy and climbing (even if there is a delay in reform), we favor equities and would re-balance portfolios higher in the asset class (with slightly more emphasis on non-U.S. equities).

What about the medium-term outlook? Since bond yields bottomed in the summer of 2016, we have experienced waves of the reflation trade (cyclical investments such as Japan, Emerging Market equities, commodities, and the Financials and Materials sectors) and bouts of erratic roaming behavior in the more defensive investment areas (such as Treasury bonds and the Utilities and Consumer Staples sectors). The underlying "core foundation" of the latest uptrend has been characterized primarily by a rising profit cycle driven by a global synchronized recovery. In addition to this traditional type of expansion, in which the leading economic indicators continue to turn up and positive earnings revisions are occurring across most sectors, an "overlay of animal spirits" has dominated most of the first quarter of 2017. The expectation that fiscal stimulus would support further growth in economic profits has moved market multiples up slightly in the last few months but not to levels that are uncomfortably overvalued, in our opinion. We still anticipate better-than-expected earnings growth, even without additional stimulus in 2017, which would justify current market multiples and an "equilibrium" S&P 500 level of around 2450. We believe a majority of the recent "animal spirits" are based on the global economic expansion. Therefore, if tax reform (even in a more conservative sense) is passed this year, the likelihood of a higher multiple, in combination with additional earnings growth, could boost the S&P 500 into a range of 2500-2600 in the back half of the year. The "animal spirits" would come more from the bull family in this case, versus the recent "wolves that have been howling."

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>
> **Christopher Hyzy**
> Chief Investment Officer, Bank of America Global Wealth and Investment Management

Consider this. Growth is gathering momentum around the world, led by the U.S., as business and consumer confidence have increased significantly in the past few months. Moreover, the global manufacturing Purchasing Managers' Index (PMI) rose in the first quarter to its highest level in almost 10 years, and Emerging Markets have climbed out of a long five-year bear market. Rising small business and consumer confidence in the U.S., better-than-expected profit growth in the Emerging Markets and Japan, greater stability in Europe's economy, and higher nominal growth in China and the U.S. have continued.

With global inflation slowly picking up, led by subtle increases in pricing power, plus a slowdown in the dollar's advance and higher wage growth in the U.S., we expect the Federal Reserve (Fed) to raise interest rates at least two more times in 2017. In this case, the Fed would still be accommodative, in our opinion. This "normalization," coupled with the momentum in the profit cycle, has led us to believe we are firmly in the beginning of the late-cycle stage. This stage should last well into 2018 and continue to be characterized by a catch-up trend in rates, a still steep enough yield curve, modest increases in pricing power, and positive economic surprises in the Emerging Markets, which were the last economies to recover, primarily due to the after-effects of the strong dollar and of the collapse in commodity/oil prices from late 2014 to early 2016.

Late-cycle phases have tended to lead to outperformance of cyclical stocks over defensives, value over growth, small capitalization equities over large caps and Emerging Markets over more developed areas. In addition, Japan has typically benefitted more than other large economic zones and markets. We expect very similar performance trends this time around, even though small caps have struggled year-to-date. We also view some growth pockets across sectors as attractive. These tend to be found in Technology and Health Care. Financials remain one of our favored sectors, as well.

The continued optimism over profits should be evident in first-quarter earnings announcements, which will be released beginning in early April. We expect positive profit revisions and elevated business confidence to underpin a move to record highs (after this pause) in equities through April. One of our contrarian sentiment indicators shows that strategists' allocations to equities are at bearish levels that historically have been a bullish signal for equities over the medium term.

However, the latest Bank of America Merrill Lynch (BofAML) Global Fund Manager Survey Macro indicator flipped to neutral territory after flashing a buy signal last month and with a record number of investors (net 34%) thinking equities are overvalued. After the latest rally, a pause in the uptrend is to be expected.

Again, for those who are fully invested at this time, we would re-balance equities higher on market weakness. We continue to believe that, on a relative basis versus fixed income, global equities deserve to be a high overweight across all profiles in our multi-asset portfolios. For portfolios that have high cash exposure, we would be actively adding to our preferred areas in the coming weeks and over the summer months, when policy debates will likely boil up again.

Let's take a nap during the howling and growling at night and allow the bulls to run during the day.

Conviction, discipline and diversification are better than speculation, indifference and market timing.

In the next sections, we provide our high-conviction viewpoints on the macro outlook, portfolio strategy, themes and trends, and we answer some of the more frequent client questions relating to the current global environment.

Portfolio strategy and asset allocation

We continue to expect equities to outperform fixed income as the U.S. and global expansions proceed. Equity valuations relative to fixed income remain attractive and corporate profits continue to improve. In the shorter term, we have moved to a more cyclical and value-oriented approach in multi-asset portfolios. We still see fund managers reducing cash levels to invest in cyclical sectors of the markets. We also advise increasing less correlated investments and incorporating an increased focus on tax efficiency and rebalancing. Information Technology remains our favored sector for long-term growth.

Within equities we remain overweight U.S. equities. Valuations appear slightly extended but earnings are growing and we are maintaining our 2017 earnings per share (EPS) target range of $129-$138 for the S&P 500. We maintain an S&P 500 target range of 2300-2700 (with an equilibrium target of 2450), reflecting the potential for fiscal stimulus and tax reform. Within U.S. equities, we maintain a slight overweight to large cap stocks and small cap stocks and favor value over growth investments.

Looking abroad, we remain overweight Emerging Market equities. They continue to face a range of challenges, including low commodity prices, gradual normalization of Fed interest rate policy, and the structural downshift in China's growth rate. However, we believe they will benefit from the recent pickup in global cyclical momentum, and also believe valuations relative to developed markets are attractive. We still view markets such as India—which are less trade- and commodity-dependent and have more domestic support from internal reform—as the best-positioned. On a structural basis, we continue to expect strength in demand from the Emerging Market consumer, as incomes and spending power increase over the longer term.

In the international developed space, where we are slightly overweight, we continue to favor Japan. We acknowledge that Japan's economy has structural impediments to growth, such as high debt levels and challenging demographics. However, cyclically, growth there should accelerate on rising global activity, improving domestic demand and a weaker currency. The Bank of Japan's recent monetary policy stance of fading negative deposit rates and targeting the yield curve has been well received by investors. Along with monetary policy, fiscal policy will be supportive of growth. European equities can also produce positive returns, given that they are cheap, and earnings could surprise on the upside, driven by margin expansion and top-line growth. However, we maintain a cautious stance, given ongoing stress in the banking sector and a full political calendar over the next six months with crucial votes in Germany and France, and Brexit, which formally started with the triggering of Article 50 of the Lisbon Treaty on March 29.

As mentioned, we are underweight fixed income and recommend active management. Slightly short duration is warranted, balancing expectations for higher short-term rates and inflation in the U.S. with overwhelming demand for fixed income globally. We continue to prefer credit over Treasuries, with an emphasis on investment-grade corporates, particularly banks and municipals, although the relative value of credit has moderated. Some allocation to Treasuries for liquidity and relative safety is advised, and Treasury Inflation-Protected Securities (TIPS) should be considered, where appropriate.

We advocate an underweight for corporate high yield (HY)—valuations are very rich, especially for lower-rated credit tiers. Within HY, an allocation to leveraged loans is advised due to the floating-rate coupon, secured status and minimal yield give-up to unsecured bonds.

We are neutral commodities. Commodity prices are likely range-bound in the near term, weighed down by ample production capacity but held up by rising global cyclical momentum. We think oil prices will rise in the $50–$70 range and move slightly higher next year.

We are neutral hedge funds. We see the environment for active management and, hence hedge funds, improving in 2017 and continue to recommend a diversified approach when investing in this heterogeneous asset class. We have upgraded our view on global equity long-short funds from neutral to moderately positive.

We are neutral private equity. The combination of high headline multiples, increased deal competition, and the large capital overhang creates an investment environment that requires a disciplined approach to allocating capital across private equity strategies. Currently, we see opportunities in special situations and private credit. We favor a steady commitment strategy and manager selectivity in diversified private equity portfolios.

We remain neutral real estate as an asset class. The U.S. commercial real estate (CRE) markets are in the mature phase of the current real estate cycle, with continuing positive signs indicating that supply and demand for space are well balanced for most property types. CRE investors should look to current income returns with value growth now mostly driven by increases in rents and cash flow over time.

QUESTIONS & ANSWERS

QUESTION 1: Describe the macro landscape currently and for the balance of the year. What are the main catalysts? The main risks? The potential surprises?

Our outlook for a cumulative, synchronized global expansion in 2017 has been confirmed by a host of economic data over the past few months. Economic surprises continue mainly to the upside, as gauged by quantitative indicators like the Citi Economic Surprise measures. They show rising strength in both real growth and inflation. The combination of stronger activity and prices is a windfall for corporate revenues and profits, which have broken out to the upside in recent quarters. As a result, global equities have also gone to new highs, with most of the "wall of worry" now shifting from the recession fears of a year ago to "how good it will get." In particular, sentiment indicators, or so called "soft data," have surged ahead of "hard data," causing the main debate between doubters of faster growth and proponents of a new, faster growth outlook spurred on by pervasive pro-business reforms from the new U.S. administration. Based on historical relationships, sentiment indicators are leading indicators and are pointing toward real growth of 3% or more in the U.S.

Similarly, global measures are breaking out to the upside, as business leaders around the world come to realize that "pro-business" U.S. policies are likely to benefit them as well, much as they did during the last pro-market revolution, in the Reagan-Thatcher years. This spread of the new approach has been tipped by the reaction of foreign leaders in meetings with President Trump where they show a desire to do business with the new administration.

This should not be surprising, given the fact that the U.S. is the biggest national economy, with the wealthiest consumer market in the world. The new trend is also apparent in the latest G-20 communique, which has replaced the previous anti-protectionism and climate change focus with a focus on fair-trade and pro-business measures.

Naturally, the main debate in the market now is between those who believe in the efficacy of the new policy approach and those who think the policies cannot work or won't be implemented because of political roadblocks to their enactment. The same debate dominated the first Reagan administration—the last time the U.S. enjoyed strong 5% average real gross domestic product (GDP) growth over a 12-quarter stretch.

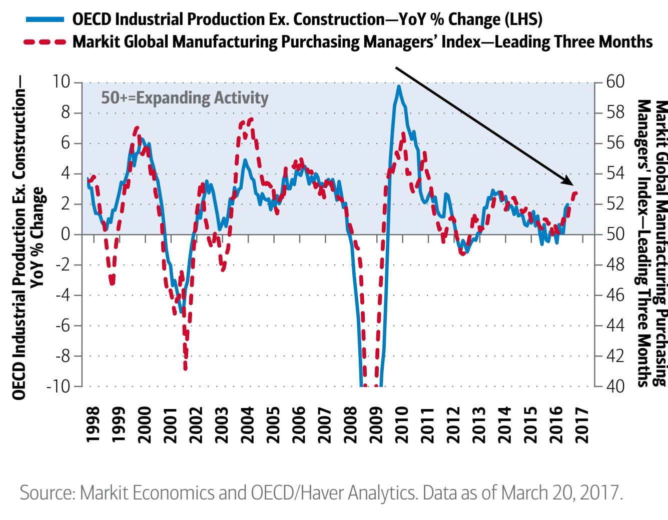
Assuming the optimistic view is correct, the bear crowd will dominate equity market action during correction phases and the believers will likely dominate what appears to be a secular bull market. It is not a coincidence that the strongest secular bull market in U.S. history started when the first Reagan administration ended the stagflation era. Ending the secular stagnation era should have a similarly positive effect on the global economy and equity markets. This is especially true outside the U.S., where growth has been even more restrained relative to potential, causing bigger deviations from historical equity-market valuations. This is doubly true about Emerging Markets, where many countries are coming out of a multi-year recession and corresponding bear markets.

U.S. leads synchronized global expansion

One major theme since the 2008 global financial crisis has been the shift of global leadership from China back to the U.S. Essentially, China's boom depended on growing trade deficits in strong consumer economies like the U.S. which allowed the Middle Kingdom to rack up progressively bigger trade surpluses. Those days are over, especially in this new era. The U.S. also benefitted from a more timely and aggressive monetary policy than Europe—for example, where political barriers delayed the appropriate monetary policy response. As a result, the U.S. expansion is the most advanced and the most prone to eventual late-cycle concerns such as margin squeezes and inflation from accelerating labor costs in a tight labor market. Nevertheless, inflation is coming off very low levels and growth is increasingly driven by technology and capital, as opposed to labor input. We still expect this will turn out to be the longest expansion in U.S. history. It will turn eight years old in June. In July 2019, should it persist, it will surpass the record run of the 1990s.

Exhibit 1 shows the global manufacturing purchasing managers' index (PMI), which has risen sharply over the past year, leading a pickup in the manufacturing output of the Organisation for Economic Co-operation and Development (OECD). Based on its recent performance, the rise in global production should continue at an accelerating pace in the months ahead. This is a clear example of a tight relationship between a leading sentiment indicator and hard data that seems to be following its usual script despite bears' claims that this time is different.

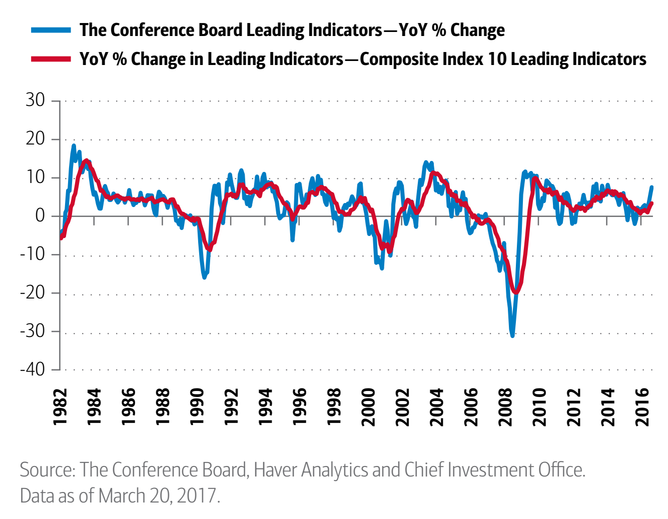
Exhibit 1: Surge in global manufacturing sentiment has in fact been followed by hard data. Sentiment points further up.



Source: Markit Economics and OECD/Haver Analytics. Data as of March 20, 2017.

U.S. leading indicators have also clearly accelerated (Exhibit 2). They represent a mix of hard and soft data, both of which are signaling strengthening growth. U.S. consumer spending softened a tad during the 2015 mid-cycle slowdown, but the underlying trend of the past three years has been a 3% average pace. Deviations below that have generally been temporary and offset by overshoots, keeping the 3% trend intact. For example, a record warm February caused a major decline in heat consumption that will likely cause a first-quarter undershoot.

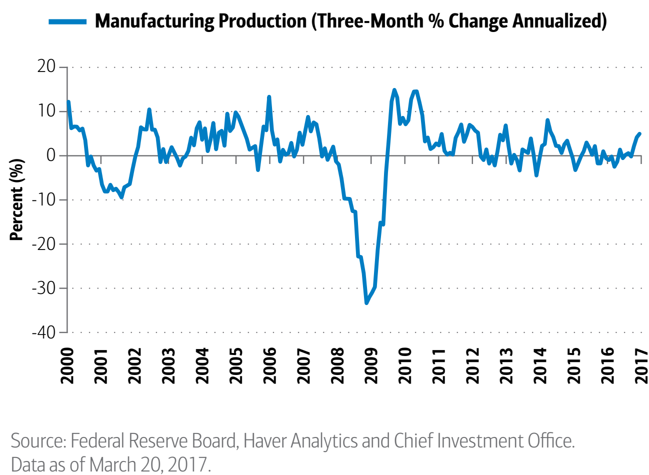
Exhibit 2: Growth momentum is picking up sharply, according to the U.S. index of leading indicators. Leading indicators point to stronger growth.



Source: The Conference Board, Haver Analytics and Chief Investment Office. Data as of March 20, 2017.

While the trend in U.S. consumer spending has been fairly steady, capital spending (capex) has been a different story. Partly, that's because the Energy sector accounted for such a large share of investment during the boom that oil prices reached more than $100 per barrel by mid-2014. By some measures, the Energy sector accounted for about half of overall global capex at its peak. The subsequent plunge took overall capex down, a major drag on U.S. GDP growth in 2015 and 2016. Energy capex is now recovering with the doubling of oil prices and rig count from their early 2016 troughs. Encouragingly, non-Energy capex by S&P 500 companies increased at a double-digit rate on a year-over-year basis in the fourth quarter. It is thus not surprising that the Fed's Federal Open Market Committee (FOMC) policy statement following its March 15 meeting cited some firming in business fixed investment after a long series of more negative assessments at prior meetings. Stronger capex is one of the reasons, along with solid consumer spending and expanding global trade, that U.S. manufacturing production grew almost 5% annually from November, 2016 through February, 2017 (Exhibit 3).

Exhibit 3: Mid-cycle slowdown over



Source: Federal Reserve Board, Haver Analytics and Chief Investment Office. Data as of March 20, 2017.

Animal spirits are also lifting business activity. They have surged in the last four months. For example, small business sentiment was stuck in recession territory during the decade up to the elections. Since then, it has jumped to levels typically associated with strong growth (Exhibit 4), including growth in investment. One reason seems to be the 180-degree turn in government regulatory policy also reflected in the National Federation of Independent Business (NFIB) survey response to the question about independent businesses' single-most

important problem, which for many businesses in recent years has been government requirements. Small business concern over government regulation has fallen dramatically since the election (Exhibit 5). Less regulation and more investment are two critical ingredients to boost productivity. Low productivity growth has been a major factor behind the era of secular stagnation. Faster productivity growth is an antidote for secular stagnation and the key factor behind the current plans to get U.S. GDP growth back above 3%.

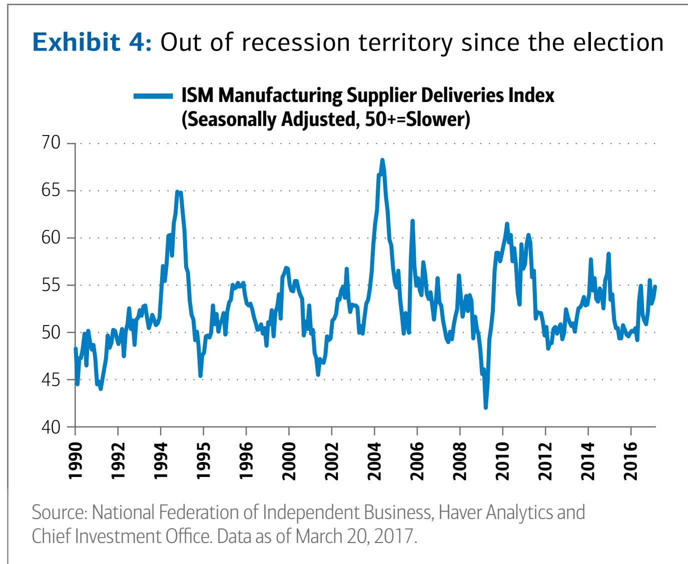


Exhibit 4: Out of recession territory since the election

Source: National Federation of Independent Business, Haver Analytics and Chief Investment Office. Data as of March 20, 2017.

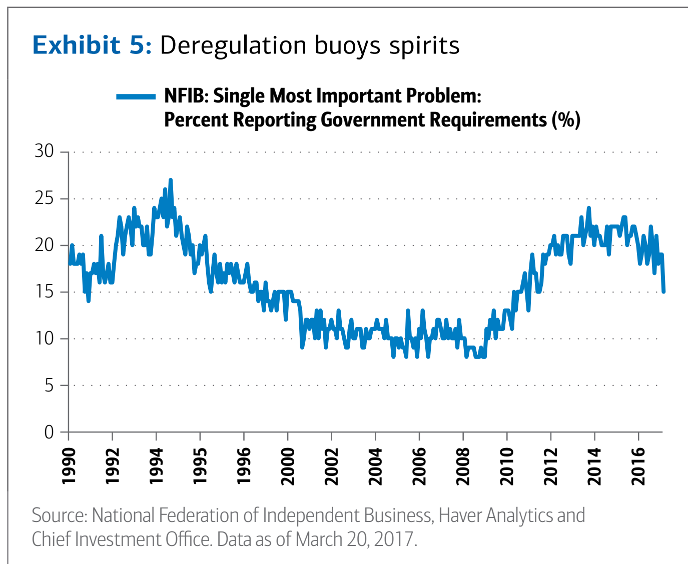


Exhibit 5: Deregulation buoys spirits

Source: National Federation of Independent Business, Haver Analytics and Chief Investment Office. Data as of March 20, 2017.

Interestingly, larger corporate CEOs seem to have gotten on board with newly found optimism (Exhibit 6). They also tend to be more exposed to global growth and are reflecting the improving trend in world GDP and trade growth.

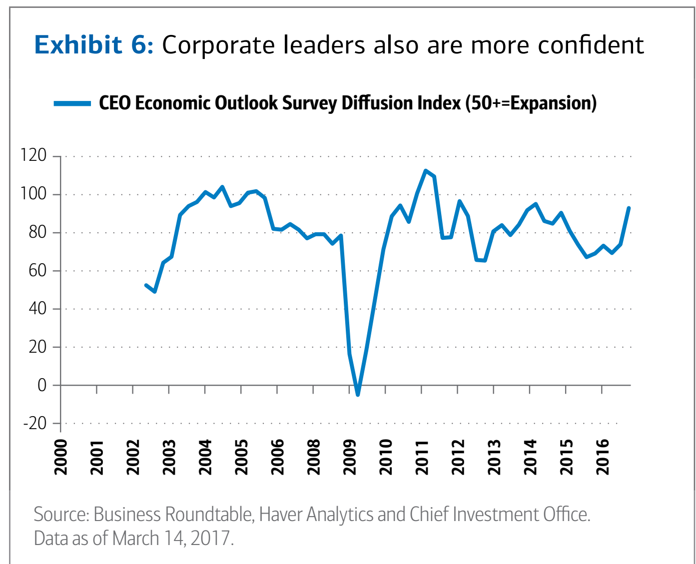


Exhibit 6: Corporate leaders also are more confident

Source: Business Roundtable, Haver Analytics and Chief Investment Office. Data as of March 14, 2017.

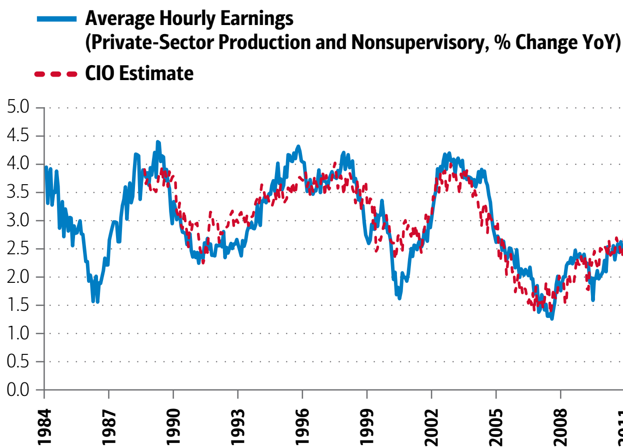
There was a lot of concern that a Trump presidency would prove protectionist. This was the main reason the conventional wisdom predicted he would be worse for the economy than his opponent. By emphasizing fair trade and the need to correct abuses by countries like China, he has largely assuaged those fears, leaving his pro-business agenda to surprise markets to the upside. By itself, the regulatory relief already anticipated has had a powerful stimulative effect on business spirits in the U.S. and perhaps the world.

Finally, we would note the underappreciated strength in the U.S. housing market. Unusually warm winter weather in the past two years has played havoc with typical seasonal patterns. This caused 2016 housing activity to look much weaker than the actual underlying trend because the spring rebound was pre-empted by early-winter warm-weather strength. As that effect passed through the data, the strong trend has re-emerged. Single-family starts of residences have averaged 13.5% gains over the past three years. That dropped to just 3.2% over the past year. Over the past six months, it jumped over 40%. Abstracting from the weather noise effects, we remain confident that the trend for the next few years remains in the double digits. Demographic and economic fundamentals support a strong housing view.

Ultimately, the longevity of expansions is determined by labor-market tightness, the resultant inflation pressures, and the Fed's tolerance for inflation. The U.S. expansion is transitioning from maximum Fed accommodation to normal Fed accommodation. This is easily seen in Exhibit 7, which shows the yield gap between 10-year Treasuries and the policy rate. Maximum

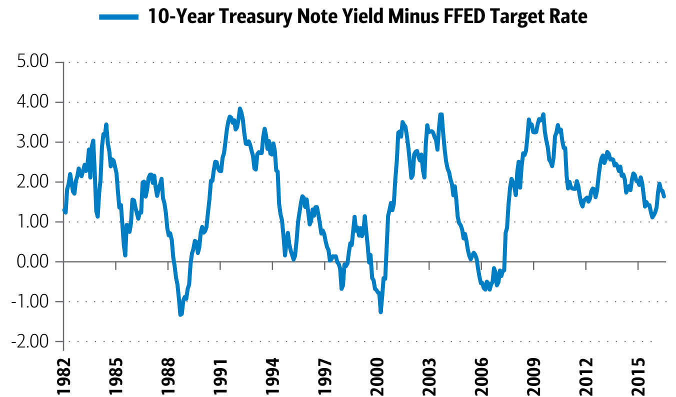
accommodation in the last three business cycles occurred with a gap of roughly 300 basis points (bps). Recessions ensued after the gap went negative. Our research suggests that, even when the planned rate hikes evident in the Fed's forward guidance are incorporated, the yield gap remains positive in normal territory through the end of the year. As seen in Exhibit 8, the behavior of the yield curve depends on labor cost pressures and the Fed's response to them. Given the moderate pressure anticipated on wages this year, the Fed's need to move from normal to restrictive does not appear pressing.

Exhibit 7: Employment can grow about 170,000 to 200,000 per month as high confidence spurs more labor force participation rate gains. Average hourly earnings growth likely to remain in check, keeping the Fed on a gradual tightening course, consistent with low downward pressure on the yield curve.



Source: Bureau of Labor Statistics, Haver Analytics and Chief Investment Office. Data as of March 15, 2017.

Exhibit 8: Labor market is not tight enough to cause market expectations of much Fed restraint. As a result, the yield curve appears likely to remain quite steep this year.



Source: Federal Reserve, Haver Analytics and Chief Investment Office. Data as of March 16, 2017.
Past performance is no guarantee of future results.

QUESTION 2: What is happening in the non-U.S. economies and markets? What are the main trends, surprises and risks?

The U.S. pickup over the past year is reinforced by improving economic conditions in Emerging Markets. Markets like Korea, Hong Kong and Taiwan, which are most sensitive to global trade, are showing strong growth in exports. It is not surprising, given six years of underperformance associated with long recessions, that Emerging Markets are now outperforming most developed markets, where historical valuations are less attractive.

One big worry earlier this year was the strong dollar. As other economies have picked up and the inflation outlook has moved higher, the anticipated gap between U.S. and other countries' monetary policies has started to shrink and take pressure off the dollar. Generally, when relative economic momentum shifts from the U.S. to the global economy, as is happening now, the dollar softens and other markets outperform. Basically, we believe there is more room to catch up to potential outside the U.S. This typical cyclical shift is complicated by the potential escape from secular stagnation if the U.S. administration's policies are adopted and work. Taken together, these facts suggest the global economy should keep improving in 2017 and 2018. Put another way, upside risks are growing.

QUESTION 3: Have the Emerging Markets turned the corner from their long slump? What is your view on growth and profits for the next year, and on any potential risks to that view?

Emerging Markets began to recover from their five-year relative price decline against developed market stocks early last year, and have remained ahead so far in 2017. The turnaround was briefly interrupted by the U.S. election result last November, but we expect the outperformance to persist as the cycle progresses, particularly with valuations still low on a relative basis.

Several supportive trends favor Emerging Markets over developed markets. The stabilization and partial rebound in commodity prices after a synchronized bear market across energy, metals and agriculture between 2011 and 2015 was a major boost for valuation in Latin America and emerging Europe (which led the early phase of the Emerging Market recovery) last year, and remains a support for year-on-year earnings in both regions. And this has since been followed by an expected move back to positive economic growth in 2017 for the two largest regional markets—Brazil and Russia—after each went through a two-year recession in 2015 and 2016.

Having underperformed last year, emerging Asia has been leading the Emerging Market rally in 2017. And as emerging Asia is by far the largest weight in the index at 71% of Emerging Market market capitalization, fuller participation by the region is a further support for Emerging Markets overall. Trade-oriented North Asian markets such as Korea, Taiwan and China have been among the top performers. The earnings outlook for all three has improved with stronger final demand in the U.S. and Europe, and a pickup in global trade from virtually flat a year ago to around 3% at the end of 2016. Korea and Taiwan in particular have also been supported by greater stability in the Chinese yuan, which has relieved competitive pressure on both markets after the material depreciation of the currency in 2015 and 2016. The People's Bank of China has delivered greater currency stability over recent months via tighter capital restrictions, and we expect this policy shift to be sustained in the runup to the national leadership transition later this year.

We expect Asia as a whole to continue leading the Emerging Market recovery. On top of the support from stronger trade and earnings, and relief from yuan depreciation, the outlook for commodities and U.S. rates will also be a relative tailwind. Resource importers in Asia will be the main beneficiaries should commodity prices remain range-bound near current levels, as we expect. And the region will be better insulated from further rate increases by the Fed, given its large aggregate current account surplus.

India remains our favored emerging country, especially with the recent electoral victory for the ruling party in a key state reinforcing our constructive view on internal reforms. And despite commanding higher valuations, we expect consumer-driven sectors such as Discretionary, Staples, Health Care and Technology to continue to outperform, as they have throughout the cycle so far. The key risks in the current environment remain a shift toward protectionist policy by the U.S. administration, a more aggressive series of Fed interest rate hikes than currently expected, more exchange rate instability in China, and new emerging geopolitical tensions in Asia (as discussed in question 15).

QUESTION 4: Describe the main catalysts for continued upside in U.S. equity markets. What's driving the uptrend? Describe your thoughts on profits and valuation and whether you have built a new base.

Since last summer, different catalysts emerged to drive equity markets higher, including improving economic data along with the bottoming of inflation and interest rates. The U.S. presidential election proved to be a game changer, as bulls took charge on a global basis, lifting sentiment and equity valuations. Since the election, small business owners and CEOs of Fortune 500 companies reported a record increase in optimism; economic activity, particularly in manufacturing, further strengthened; and, finally, corporate profits turned positive, rising strongly in the fourth quarter by 5% year-over-year, while sales rose 4%.

Going forward, to keep equity markets moving higher, we will need to see continued improvement in economic activity, sales and profit growth, and sentiment. Potentially the biggest hurdle or catalyst for equities going forward is corporate tax reform. EPS for the S&P 500 is projected to grow 8-10% in 2017, before adjustment for any tax reform benefit. If the administration can get tax reform approved by Congress this year or show enough progress to warrant optimism for early next year, it should continue to lift sentiment and would add to an earnings outlook that is already improving.

Investors also want to see ongoing improvement in the top line for the corporate sector, especially as margins come under pressure from rising wages and share buybacks become less of a support for earnings and the markets. Sales growth has improved for the second consecutive quarter after slowing for two years, and rising nominal growth should help keep this trend in place.

U.S. equity market valuations are slightly extended, at approximately 18-19 times earnings on a trailing-12-month basis for the S&P 500 index. However, relative valuations versus fixed income in general remain attractive. We believe continued upside in equities from current levels is likely to come from profit growth and not multiple expansion. Improving earnings expectations for 2017 and 2018 should support above average price/earnings multiples until we see a change in outlook or a slowdown in earnings growth.

QUESTION 5: Describe the latest developments around fiscal stimulus and what could be the impact of tax reform on growth and profits, and in what timeframe.

The fiscal landscape of the United States remains encouraging, albeit at a smaller and slower scale than previously anticipated, owing to the complex nature of pushing multiple pieces of legislation through Congress. The Trump administration is pursuing an ambitious fiscal agenda, chief of which remain tax reform and health care, in coordination with a budget that prioritizes defense and less regulation. However, in an effort to maintain or even reduce the deficit, we anticipate spending outlays to be matched with cuts elsewhere. Finally, President Trump has signaled his intention to submit an infrastructure bill later in the year, having recently solicited a list of shovel-ready projects from governors.

The efficacy and timing of tax reform and health care are challenged by their sheer complexity, partisanship, lack of a supermajority within the Senate, and divisions within the Republican Party itself. Consequently, it is likely that these reforms will be enacted via "reconciliation," a mechanism allowing for a Senate majority to sidestep a filibuster on a limited basis. Given the failed negotiations for health care reform, it is likely that the tax reform package will prove challenging as well. As a result, the stimulative effects of reform may not be enjoyed until 2018. The infrastructure proposal has more potential to garner bipartisan support and is expected to near one trillion dollars, with much of this capital sourced in partnership with private entities, combined with tax credits to reduce the reliance on federal outlays.

While we remain convinced that the ultimate implications of discretionary spending and key reforms will support economic growth, we would advise investors to temper expectations as to the magnitude of any stimulus and to appreciate the multiple paths of certain provisions in shaping ultimate outcomes.

Corporate tax reform, for example, will consist of additive measures that will have varying effects on earnings, through their implementation. BofAML Global Research outlines these provisions under multiple scenarios (Exhibit 9).

Exhibit 9: Estimated impact of tax reform on S&P 500 EPS

Tax Policy	15%	20%	25%
Tax rate change	10.50	8.00	5.00
Ending interest deductibility-initial impact	-0.50 to -1.00	-0.50 to -1.00	-0.50 to -1.00
Border adjustments	-4.00	-5.50	-6.50
Share count reduction from buybacks (50%)	4.00	4.00	4.00
Total initial impact	9.50 to 10.00	5.00 to 6.00	0.50 to 2.00
Ending interest deductibility-recurring impact	-3.50	-5.00	-6.00
Recurring impact	7.00	1.50	-3.50
One-time repatriation tax (875%), GAAP chart	-8.50	-8.50	-8.50

Source: BofA Merrill Lynch Global Research, U.S. Equity & Quant Strategy. Data as of March 22, 2017.

It is important to note that significant uncertainty remains surrounding the final corporate tax rate, interest rate deductibility going forward, depreciation expenses, and if border adjustment tax (BAT) will be included in the final proposal.

Furthermore, the impacts of reform will not be uniform; rather, there will be certain pockets of the economy that benefit to varying degrees and across different timeframes. For example, the proposed BAT would reward export-oriented industries, including agriculture, while punishing importers, such as retailers and oil refiners. Alternatively, elimination of the deductibility of interest may be phased in over time, ultimately detracting from capital-intensive sectors including Utilities and Telecoms, while less levered sectors, such as Technology, would encounter less pressure.

Tax reform is also expected to provide outsized benefits to small cap companies, which are typically subject to higher

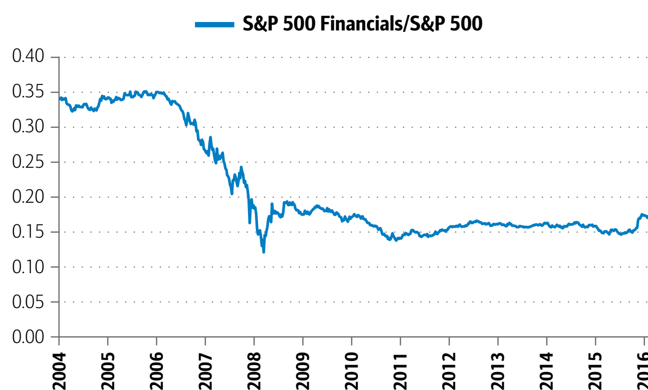
average tax rates while also deriving a greater portion of their revenues domestically. Finally, deregulation has the potential to materially improve the profitability of American firms, with new regulation measures having added approximately $108 billion in yearly costs since 2009, according to the Heritage Foundation. Certain sectors, including Energy and Financials, were impacted particularly hard by increased regulation and stand to benefit from deregulation. Through executive order, the Trump administration has issued a cap on regulation without offsetting cost reductions. Financial markets have since cheered beneficiaries to some extent, and we remain supportive of the Energy and Financial sectors as the benefits of deregulation and additional reform continue to serve as tailwinds moving forward.

QUESTION 6: How has sentiment evolved since the turn of the year, and what are the most interesting charts according to technical analysis across financial markets and sectors?

At the turn of the year, the BofAML Global Research Fund Manager Survey (FMS) indicated a low percentage of portfolio managers overweight global equities. Furthermore, the Sell Side Indicator (SSI), a proprietary gauge measuring strategist asset allocation recommendations, signaled widespread bearishness, which we viewed as a contrarian "buy" signal. Since then, improving economic data and earnings worldwide and the prospect of enactment of President Trump's pro-business legislative agenda have driven global equities to record highs. Global investors have shifted from a somewhat cautious investment stance towards a more optimistic one. Today, the FMS reports the highest net overweight to global equities in almost two years and well above the long-term average. The SSI now flags "neutral," hitting a 16-month high. Yet, at its current level, equities have historically appreciated. While sentiment still favors further gains for equities, it is no longer a notable tailwind.

On March 16, the Fed raised its policy interest rate by 25 basis points and reiterated its forecast of hiking two more times this year. Markets took the announcement in stride, seeing it as a signal of a strengthening economy. We view Financials as an intriguing investment for long-term investors, supported by President Trump's legislative push for deregulation. In addition, a stronger economy and rising interest rates would respectively yield greater opportunity to make loans and increase profit margins. While some investors may argue that the S&P 500 Financials sub-index is less than 20% from its record high, having already priced in the aforementioned developments, we would instead suggest viewing the sector compared to the broader S&P 500 (Exhibit 10). When viewed in this context, we feel Financials have the potential to outperform the S&P 500, given that they remain significantly below their relative highs of 2006 and 2007.

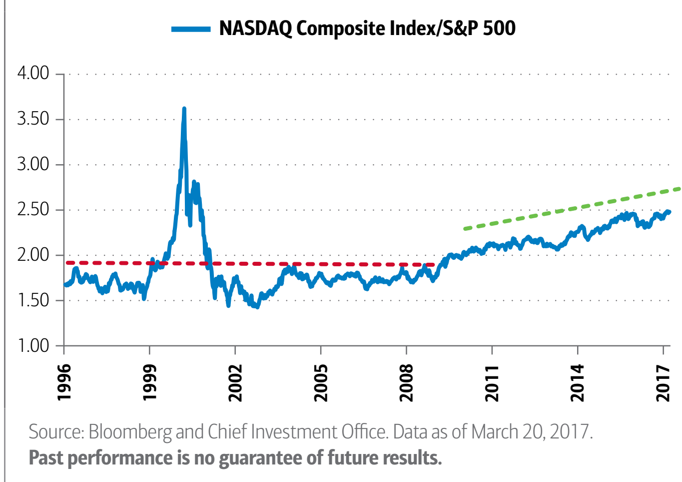
Exhibit 10: Financials have lots of runway



Source: Bloomberg and Chief Investment Office.
Data as of March 20, 2017.
Past performance is no guarantee of future results.

While we see a catch-up opportunity for Financials, we view Technology as a leader. The rise of smartphones, online social platforms, cloud computing, augmented and virtual reality, self-driving cars, and other advancements signals a shift to the "Digital Era." In our platform titled "A Transforming World," we view Technology at the forefront of our "Innovation" theme. From a time perspective, we see the Digital Era under the same lens as the Industrial and Agriculture Eras, with a shelf life spanning not years, but decades. In this light, we see the NASDAQ Composite as an index with the potential to represent this new age. When comparing the NASDAQ Composite to the S&P 500 (Exhibit 11), we can see its relative strength dating back to 2009. Given our belief that we are in the nascent stage of this new era, we are optimistic about the Technology sector's long-term potential. While on an absolute basis, the NASDAQ Composite index surpassed its 2000 peak, its relative position versus the S&P 500 remains below its respective peak.

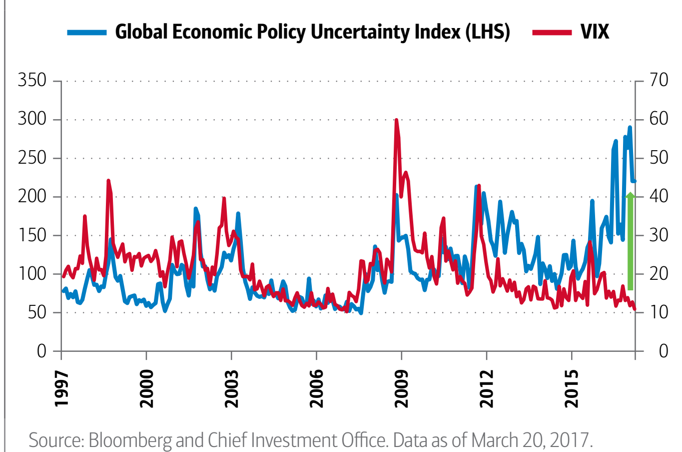
Exhibit 11: Relative Strength Seen in Technology



Source: Bloomberg and Chief Investment Office. Data as of March 20, 2017.
Past performance is no guarantee of future results.

We also stress the importance of maintaining a well-diversified portfolio, tailored to one's risk tolerance to guard against periods of heightened volatility and uncertainty. President Trump's "America First" platform, of which a key plank is the reshaping of U.S. trade relations with the rest of the world, has led to increased uncertainty on the path forward for globalization. Meanwhile, the U.K. triggered Article 50 on March 29, initiating the process of withdrawing from the European Union, after which France and Germany hold elections. However, investors have generally not seen these events as obstacles for the global economy and for corporate profits. The VIX index, a key measure of implied volatility in equities, remains low compared to the economic policy uncertainty index (Exhibit 12). Although the chances of a significant negative event occurring remain low, the divergent nature of these readings suggests that investors may be caught flatfooted if they come to fruition, leading to notable volatility.

Exhibit 12: Elevated uncertainty hasn't spilled into markets



Source: Bloomberg and Chief Investment Office. Data as of March 20, 2017.

QUESTION 7: Has the Fed entered a state of normalization? What is your view on rates and any impact on investment strategy?

Yes and no. The FOMC's average rate hike cycle over the past 30 years is roughly 300 bps. The latest and third rate hike in March put the Fed into the second quarter of an average hiking cycle. Hence, by conventional interest rate measures, the Fed is in the early stages of normalization. We expect two more 25 bp increases in 2017 and possibly three in 2018. Other measures also suggest that the Fed is entering a more normal state: short- and long-term rates have begun to drift higher, and Treasury term premiums are rising again.

By other measures, the Fed is still not quite normal. The Fed continues to maintain a balance sheet of $1.7 trillion mortgage-backed securities and $2.5 trillion in Treasuries. Just to maintain the balance sheet this year, it will buy some $300 billion in assets to replace its maturing securities. Hence, the Fed is still putting a substantial bid in two of the largest and most liquid fixed income markets in the U.S., while other major central banks are still actively net purchasing assets through quantitative easing.

We suspect the Fed views the tightening cycle cautiously. The overall level of rates is still low and the zero lower bound is not far. In the event of a negative shock, the Fed would have few rate cuts to ease before it would be forced to resort to the same unorthodox monetary policies it wheeled out during the financial crisis, including asset purchases and forward guidance. Bottom line: The Fed is entering a state of normalization but is not confidently past the risks of the zero lower bound, and its balance sheet is far from "normal."

As a result, the investment strategy today is not much different from before. Equity markets likely still receive some implicit support from the low level of rates and the bloated balance sheet, while fixed income yields may be slightly weighed down. Our investment strategy factors in the rising rate environment, which offers higher coupons but also poses duration risk and should be addressed by a barbell strategy. Our investment strategy also takes account of the impact of rising rates on equities. But we look for equities to rise as earnings continue to recover with the acceleration in nominal GDP growth. [Typically the early hikes by the Fed are associated with a rising equity market, as the faster economic activity is what prompts the Fed to hike in the first place.]

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QUESTION 8: Many are suggesting the bond markets could go through a tantrum if U.S. monetary policy diverges from the more accommodative stance of the European Central Bank and the Bank of Japan. Thoughts?

During the Taper Tantrum of 2013, Treasury yields spiked more than 100 bps, Emerging Market debt sold off, and measures of implied volatility rose markedly. Back then, comments by key Fed policymakers triggered concerns that investors would be caught with too much duration. Now the concern is that yields could spike if the Fed has to tighten more than expected. After nearly a decade of central banks holding rates abnormally low, the fear is "normalization" could happen more abruptly.

Expectations of rising rates due to faster growth, higher inflation, and tightening by the Fed will likely persist. By contrast, the European Central Bank (ECB) is only likely to cease its quantitative purchase program next year at the earliest, while the Bank of Japan (BoJ) has committed to accommodation until it surpasses its 2% inflation goal. As a result, the Fed, which could reach its 2% inflation goal this year or next, looks to be well ahead of its peers in terms of its exit strategy. But a tantrum presupposes a surprise in the market. Will markets now be surprised if the Fed pulls further ahead of the ECB or BoJ? We doubt it. In fact, recently, the surprises have been in the opposite direction, as better growth abroad has narrowed the outlook for policy divergence.

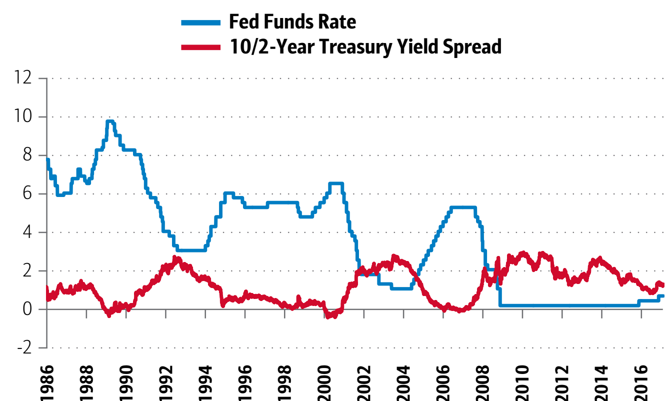
QUESTION 9: Describe the fixed income landscape, your view, and potential risks and direction of the yield curve and duration.

Our year-ahead outlook highlighted that the most important 2016 event was a change in the central banker mindset—moving away from an era of zero rates along a path towards policy normalization. Encouragingly, this trend remains in place, and the rate of progress has accelerated. There was a one-in-three chance of a March rate hike at the beginning of the year, but better-than-expected economic data and favorable FOMC speeches caused markets to eventually price in a certain rate hike as the March meeting approached. The Fed did carry through with the March rate hike—only the third time the FOMC has raised the targeted federal funds rate since the financial crisis.

Increased Fed policy transparency, combined with its sensitivity to market sentiment and improving economic fundamentals, has led to a gradual and expected reaction in fixed income markets: higher nominal rates, higher real rates, a dearth of volatility, tightening investment grade spreads, a continued high yield rally, with both yields and spreads dropping and steady municipal returns.

We expect an increase in the 10-year Treasury yield in 2017, although not in a straight line, but in fits and starts. We are forecasting a yield of 2 5/8% to 3 1/8% by the end of 2017, based on what now looks to be three Fed rate hikes in total for 2017, including the recent move. Using history as a guide, the 10-year Treasury yield has risen an average of 130 bps from the beginning of a rate hike cycle until the last hike, which implies about a 3.6% yield at the end of this cycle. Therefore, we favor fixed income strategies that are slightly short in terms of duration. History also tells us that the curve invariably flattens in a rate hike cycle; FOMC rate hikes have a more pronounced effect on the short end of the curve than on the long end. The flattening of the yield curve in the hiking cycle reflects the restraining effect of Fed policy on the economy in order to keep inflation in check. The two- to 10-year Treasury curve has flattened an average of 122 bps over the last four rate hike cycles (1986, 1994, 1999 and 2005); if history repeats itself, almost all of that flattening is still to come in 2017 and 2018. A higher and flatter curve favors a barbell strategy, as the belly of the curve usually underperforms, and that is still our recommendation.

Exhibit 13: Yield curve flattens when the Fed raises rates

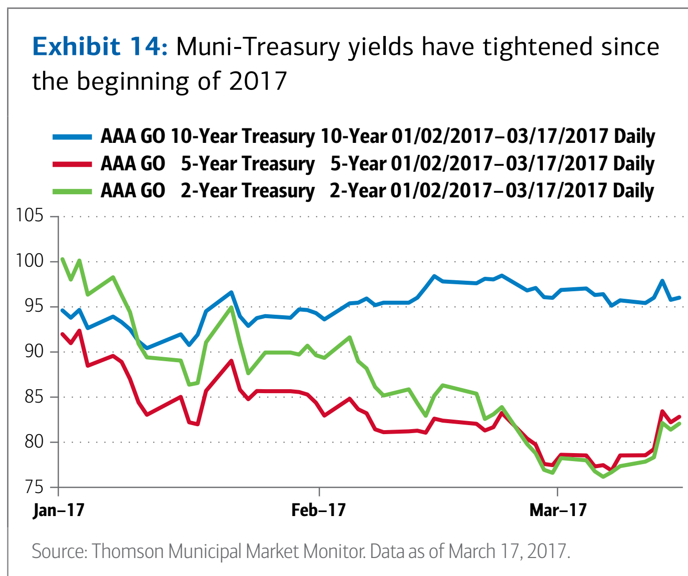


Source: Bloomberg and Chief Investment Office.
Data as of March 20, 2017.
Past performance is no guarantee of future results.

Investment Grade: We have become slightly more cautious on credit, as valuations have become more stretched. For Investment Grade, we remain slightly overweight. The improving economic backdrop, a transparent Fed, potential for pro-business fiscal policies, and positive yield differentials versus the rest of the world are important themes that remain relevant. Further modest spread tightening supporting low-single-digit excess returns is possible, but we feel that spreads are unlikely to tighten to 2005 levels, given the higher durations in the market and deterioration in credit quality over the last decade. We caution that spreads appear closer to fair value, and excess returns are near to our full-year targets already. Therefore, with rates having more room to rise, investors should prepare for increasing volatility of total returns.

High Yield: We have moved to underweight on corporate High Yield. Based on average credit losses through the cycle, prospective returns for the buy-and-hold investor have hovered in the low- to mid-3% range. Spreads are well through average levels for the High Yield market as a whole, and for every credit category within High Yield. Overall, yields are quite low by historical standards and barely cover average credit losses for the CCC and below sector. Combined with higher-than-average leverage levels—which may portend higher credit losses in the next cycle than experienced historically—this leaves us feeling that the risk-reward tradeoff is unfavorable, and there is little margin of safety for the risk-averse, long-term investor. For the portion of funds still invested in High Yield, stay up-in-quality, favoring BBs and Bs over CCCs and lower. This also means having a portion of High Yield funds dedicated to the leveraged loan space, which offers above-average spreads relative to unsecured bonds, slightly less credit risk, given their position in the capital structure, and—because they are floating-rate—a shorter duration profile.

Exhibit 14: Muni-Treasury yields have tightened since the beginning of 2017



Source: Thomson Municipal Market Monitor. Data as of March 17, 2017.

Municipals: For the high tax-bracket investor in taxable accounts, municipals retain their status as a key foundational portfolio element, and we remain overweight on the asset class. Municipal-to-Treasury yield ratios have tightened on shorter-maturity munis since the beginning of 2017, although the shorter munis got a little cheaper after the Fed hiked rates. Ten-year munis have widened in 2017 and continue to look attractive.

Based on the relative cheapness of longer-term munis, it would appear investors are demanding additional compensation for the risk that the value of the municipal bond tax exemption will be weakened by tax reform. President Trump's tax plan calls for a decrease in the top tax bracket, from 39.6% to 33%, and the 3.8% investment surtax could be repealed. However, House Republican plans to cut the tax rate on taxable interest income even further are unlikely to pass, in our view, and the muni bond tax exemption itself is very likely to remain in place. If so, demand—which has been volatile since Election Day—is likely to improve on the longer end of the muni curve, and spreads should tighten. If tax reform stalls and individual income tax cuts are more modest, the upside for munis could be even greater. In terms of supply, new money municipal issues have trailed overall municipal volume, so outstanding municipal bonds have actually decreased since 2010, one of the only major fixed income asset classes to do so. In addition, overall volume has been down over the last few months. These are positive technical factors. We believe credit spreads for A-rated bonds provide an attractive risk-adjusted opportunity, while on the short end, variable rate demand notes provide a competitive return.

QUESTION 10: What is the outlook for oil prices in an environment of robust demand, given strength in the global economy and a supply picture whereby U.S. shale revival is threatening production discipline?

Global oil demand has surprised to the upside over the past three years and should continue to increase at a robust pace in 2017, as both export- and consumer-based economies have overcome their recent slowdowns and global economic indicators point to robust economic growth going forward. Coupled with more discipline on the supply side, as reflected in the recent OPEC agreement to bring inventories into better balance, this should keep prices from falling more this year.

OPEC's November 30, 2016, agreement to curb production, its first such decision since 2001, was enhanced by promises of additional cuts from 11 non-OPEC countries, including Russia.

The purpose of the 1.8 million barrels per day combined planned cut from December supply levels was to reduce the crude oil inventory surplus. However, this action is being countered by three important supply factors:

1. production from large projects committed to earlier in the decade, such as in Brazil, which is surprising to the upside;
2. the successful application of horizontal drilling to mature fields, as in Russia, for example, which is boosting supply prospects; and
3. the revival of shale oil.

North America is seeing a surge in oil rigs, most of which are for horizontal drilling by shale oil producers. BofAML Global Research calculates that 84% of non-OPEC supply gains are due to U.S. shale production. Improved technology and cost cutting during the most recent industry slump have lowered breakeven costs to around $55 per barrel for major shale producers, a key reason the U.S. has replaced Saudi Arabia as the world's swing producer. As a result, the International Energy Agency has significantly increased its global oil production capacity estimates through 2019, a major cause of the significant drop in crude oil prices over the past month.

The oil-price slump since mid-2014 helped strengthen global gasoline demand to a record high last year, with even economically vulnerable regions, such as the European Union, contributing to the trend. As evidence of a synchronized global expansion is mounting, including BofAML's surging Global Wave and robust manufacturing Purchasing Managers' Indexes, petroleum demand should remain strong, even in the face of structural tailwinds: better vehicle fuel efficiency, alternative energy sources, aging populations, urbanization, and China's transition toward a more service-based economy.

Thus, we expect higher than previously anticipated levels for both demand and supply in coming quarters. Strong adherence to the OPEC-plus-Russia agreement to keep a cap on supply through June is critical for market conditions and the direction of prices. When OPEC meets again on May 25, the relative benefits and costs of short-term price stability versus longer-term loss of market share will likely be high on the agenda. It is worth noting that preserving market share was one of the main drivers of the surge in production that started in mid-2014.

Even then, because of an upwardly revised supply outlook elsewhere, oil prices are likely to remain closer to the lower half of our $50-$70-per-barrel estimate this year. Prices should then start to move up, as supply growth is seen diminishing substantially after 2018-2019. Given the multitude of moving parts affecting both supply and demand, high oil-price volatility should not be surprising ahead.

We see both downside and upside risks to our view of moderately rising oil prices. Rising U.S. interest rates, a potentially stronger U.S. dollar, and a flatter yield curve could restrain global growth and hurt demand from Emerging Markets in particular, therefore depressing oil prices. So could better-than-expected supply from improving and expanding shale extraction technologies, or another price war led by OPEC to preserve market share. On the other hand, unforeseen geopolitical events and supply disruptions, as well as stronger global demand and higher inflation, could tilt price forecasts upwards.

QUESTION 11: The U.S. dollar seems to have lost some momentum after the Trump rally. What's your outlook for it for the rest of the year?

The dollar continues to be supported by wide and widening interest rate differentials, but the peak of monetary policy divergences may be behind us. This is likely what the recent dollar consolidation is reflecting. The European Central Bank and the Bank of England, for example, appear to be signaling they will be backing off the monetary accelerator in the next year or so, which should slow the pace of interest rate divergence going forward. Japan remains the exception, given its commitment to peg rates until its inflation target is in sight. Meanwhile, it is unlikely the Fed will need to tighten policy much faster than the three to four hikes per year that are already priced in. Thus, we see some potential for monetary policy recoupling over the next few years, assuming the European Monetary Union avoids a breakup and positive global cyclical dynamics stay on track. Valuation is also a medium-term headwind for the dollar. On a standardized basis, the real broad trade weighted dollar is around one standard deviation overvalued.

Still, the dollar will benefit significantly from interest rate differentials even if the pace of widening slows. Balancing these headwinds and tailwinds leaves us with a more neutral base case for the dollar, with some upside from euro breakup risk and U.S. fiscal and/or trade policies, which are difficult to predict. Absent the euro-breakup risk, we would not be inclined to recommend hedging European equity exposure, but we deem the risk to be

significant. In our base case, we think the euro will finish the year near its current level of between 1.00 and 1.10.

The yen continues to be an attractive carry trade currency. This will leave the currency vulnerable to bouts of volatility like we saw last year, when the yen appreciated from 120 against the dollar at the beginning of the year down to 100 in the middle of the year, then depreciated sharply at the end of the year to close around 118 against the dollar. Our base case is for the yen to finish the year between 115 and 125 (a slight depreciation from these levels, as foreign rates rise while Japan's stay fixed), but we expect periods of risk-off sentiment will create volatility.

QUESTION 12: How do you see the European political landscape?

This year marks the 60th anniversary of the Treaty of Rome, the agreement that established the European Economic Community and would later lay the basis for the creation of the European Union. However, the political calendar for the E.U. in 2017 will be defined more by its challenges than its celebrations. Leadership elections in the Netherlands ended in defeat for the far-right anti-EU Freedom Party, but investors will remain focused on a series of other events that have the potential to destabilize European markets. Voters in France will go to the polls on April 23 and May 7 in a two-round presidential election, with parliamentary elections to follow on June 11 and June 18. Italy's ruling party may still call for early elections this summer following the resignation of its former Prime Minister late last year. Federal elections will take place in Germany on September 24. And the U.K. has formally entered its two year period of negotiation with the European Commission on March 29 as it prepares to leave the EU. Though we do not foresee any major shock results of the type witnessed last year, political developments in Europe will need to be closely watched.

The French election in particular has the potential to cause the most market volatility should the result go against expectations. Current polling shows the centrist candidate Emanuel Macron well ahead of his far-right, anti-EU opponent Marine le Pen in simulated second-round voting, though market uncertainty is reflected in the fact that French government debt spreads briefly surpassed those of Ireland as recently as the end of February. As a founding member of the EU and a part of the eurozone currency bloc, a victory for le Pen could be far more damaging to the rest of the union than the Brexit vote. But the constitutional limits placed on the French president without support from parliament (a majority for le Pen's National Front party is highly unlikely) mean that any near-term market weakness would probably be short-lived. Though le Pen's policy agenda includes withdrawing from the euro, renegotiating the terms of EU membership and increasing protectionist measures, EU rules and legislative opposition would prevent her from enacting these measures. Parliamentary approval by both chambers would, for example, be required to pass the constitutional amendment needed to call a referendum on EU membership. And individual EU countries cannot set protectionist trade terms unilaterally. However, an anti-EU French leader would clearly deal a major blow to the prospect of closer economic and political union among member states.

In Italy, even if early elections go ahead, no single party has enough popular support to govern alone—even under proposed new election rules that would hand a parliamentary majority to any party gaining 40% of the vote. And in Germany (as in France), the far-right opposition is also expected to make gains, but the odds of defeat for the ruling coalition are much lower. Indeed, the biggest risk is likely to be on the upside, given the growing support for the Social Democratic Party—Chancellor Merkel's center-left junior coalition partner. Its leader, former President of the European Parliament Martin Schulz, has been rising in popularity since taking over the party leadership earlier this year and has pledged support for more pro-growth policy. His leadership, therefore, could help to reverse the deflationary effects of current eurozone austerity policy. As a central case, we do not expect any major or persistent market disruption around these events, but they will nonetheless bear close watching as the key dates draw nearer. Unexpected outcomes could threaten an already fragile economic recovery in Europe and cause local markets to underperform.

QUESTION 13: Any emerging trends in the industry that we must watch?

There are numerous emerging trends in the investment management industry that deserve a close eye. Three of the most interesting investing trends include the significant gap between bond fund flows and equity fund flows since the credit crisis, the fund flows into passive vehicles, and the size and duration of the "bull run" in equity financial assets since the credit crisis.

Since the beginning of 2009, according to the Investment Company Institute and Bloomberg Data, there have been almost $1.5 trillion in cumulative U.S. fund inflows—not including Exchange-Traded Funds (ETFs)—into fixed income versus an outflow of approximately $180 billion in U.S. equity fund flows (not including ETF flows). This stark contrast in flows has occurred in a period in which U.S. equities have returned nearly 300% (since the lows in early March 2009), longer-dated bond yields have been stuck in a lower-for-longer range, and the Fed has hiked the federal funds rate only three times in 11 years! With our expectation that bond yields are going to grind higher in the next few years, the so-called great rotation, which has yet to occur, could be the main driver that closes the bond versus equity fund flow gap. This "rotation" would extend the current bull market further, in our view. In this case, the fund flows are more than likely to rotate to the areas that have not participated as much in the post-crisis rally, such as financial stocks and non-U.S. equities, including Emerging Markets.

Another major gap has developed in the trend of flows into passive versus active funds. Since the beginning of 2009, according to BofA Merrill Lynch U.S. Equity & U.S. Quant Strategy, passive funds have received over $1.5 trillion, while active funds have had an outflow of over $500 billion. There are many reasons for this, including price sensitivity, difficulty in outperforming, and the build of programmatic investing platforms. However, given the assets-under-management (AUM) split of U.S. funds, which is still 64% in active funds, with the balance in passive, this flow movement is likely to continue for some time. In an environment where event risk is elevated, we believe a mix of active managers and passive vehicles makes the most sense when building a portfolio for the long term.

According to Bloomberg Data, this bull market, as measured by the S&P 500, is about 3.5 times higher than its low point in March 2009, and is the second-longest, after the approximately decade-long move during the 1990s' technology craze. Although the gains for both periods are impressive, a striking difference between the 1990s' advance and the current one is that market multiples rose to the high 20s at their peak nearly 20 years ago. Today, multiples are much lower, at around 18-19 times a 2017 earnings base of $129-130, which is at the low end of the expected earnings range. Given that interest rates are still close to record low levels and not expected to return soon to the average risk-free yields experienced in the post-World War Two era—current market multiples are not too high, in our opinion.

Multiples are merely at a slight premium with the potential to rise slightly as bond yields grind higher and the rotation of some of the excessive bond fund flows shift to equity. In addition, even if the market multiple remains sticky or drops slightly, we believe that stronger-than-expected earnings growth could provide the catalyst for higher equity prices in the near future. Long-term investors should consider developing a disciplined re-balancing portfolio strategy that increases the allocation to equities over the next few months and not wait for the proverbial 5-10% pullback. In the long run, allocating across time periods on a disciplined basis has been a much more successful strategy than waiting for the right time to catch the pull-back. Just missing 10 of the best days per decade can wipe out most of the potential gains during that span (Exhibit 15).

Exhibit 15: Panic-selling and pullback timing result in missing the best days

Decade	Price return	Excluding best 10d per decade	Excluding worst 10d per decade	Excluding best/ worst 10d per decade
1930	-42%	-79%	39%	-50%
1940	35%	-14%	136%	51%
1950	257%	167%	425%	293%
1960	54%	14%	107%	54%
1970	17%	-20%	59%	8%
1980	227%	108%	572%	328%
1990	316%	186%	526%	330%
2000	-24%	-62%	57%	-21%
2010	95%	34%	200%	106%
Since 1930	**10055%**	**31%**	**1124980%**	**14442%**

Source: S&P; BofA Merrill Lynch U.S. Equity & Quant Strategy.
Data as of March 27, 2017.

QUESTION 14: What are investment flows telling us? Any trends we should know about across markets, asset classes and sectors?

Fund flows over the last decade have been decisively into fixed income versus equities. As interest rates normalize and move higher, fund flows into equities should increase and support the equity bull market. Despite the notable improvement in the economic outlook and the Fed tightening, flows have seen only a minor adjustment from the past couple of years. Equities have started the year with stronger inflows, but not at the expense of fixed income flows, which remained positive year-to-date.

Despite the lack of conviction within overall year-to-date equity and fixed income flows, asset class and sector data reveal some defining trends, although it is still early in the year. Financials dominated equity sector inflows and, surprisingly, utilities continued to see strong flows despite headwinds from rising rates. Reflationary assets such as value, infrastructure, Master Limited Partnerships, materials, Japan and Emerging Markets have also attracted steady inflows.

Looking into trends, following the election we saw a significant tilt in market performance towards value and Financials, which significantly outperformed the broader market through year-end. However, during the first quarter of 2017, we witnessed some reversion in these trends. We believe that Financials, and especially banks, have the ability to outperform the market based on our expectation for rising yields, improvement in the domestic economy, increased operating leverage and prospects for reduced regulatory burden. Technology has emerged as the best-performing sector year-to-date and, among defensives, Health Care has outperformed (as of March 16). Both areas remain favored sectors for long-term investors.

The value segment of the market is heavily weighted towards Financials, Energy and pharmaceutical companies. The growth segment's bias towards Technology, Consumer Discretionary and Health Care has lifted it above the Value index. We still believe value can outperform growth this year as Financials strengthen and Energy stocks recover.

Small cap stocks have also strongly outperformed since the election but have lagged over the past couple of months. The basis for our positive view on small caps has only strengthened over the past couple of months, as economic data and small business sentiment indicators have improved. However, small caps may need a catalyst to resume their outperformance versus large caps, which may come from potential corporate tax cuts.

QUESTION 15: What are the geopolitical hot spots?

The major focal points of geopolitical risk have shifted among the Middle East, Eastern Europe and the Asia-Pacific over recent years, with all three areas containing flashpoints that potentially threaten regional stability.

In the Middle East, Syria (despite current efforts to maintain a ceasefire) remains a cauldron of competing interests, with Iran and Russia aligned behind the Syrian regime, an opposition supported by the U.S. and its allies in Turkey and the Gulf states, and non-state militant groups opposed by both sides.

In Eastern Europe, the hot war in Ukraine has subsided, but the conflict between Kiev and eastern separatists continues. The Ukrainian government recently imposed an embargo on goods flowing in and out of rebel-held territory in the east and introduced new sanctions on Russian companies operating in the country.

But, for the time being at least, the main locus of global geopolitical risk has shifted to Asia—by far the most consequential of the three regions for global economic activity. In South Asia, small-scale military skirmishes over disputed territory between India and Pakistan have increased over the past 12 months, with India threatening trade sanctions and even a review of the countries' common waters treaty if the Pakistani government fails to control attacks by militant groups. And North Asia has arguably become the greatest source of potential geopolitical escalation. On his recent visit to Japan, Korea and China, the U.S. Secretary of State, Rex Tillerson, placed the security threat from North Korea high on the agenda following recent nuclear test launches by the Pyongyang regime, encouraging China to toughen its stance. The U.S. and China are already embroiled in a geopolitical standoff over Chinese island building in the South China Sea, and an increasingly belligerent North Korea could further strain Sino-U.S. relations. Not only is the U.S. likely to increase pressure on China to impose firmer sanctions on Pyongyang, but tensions could also rise over the proposed positioning of a new U.S. missile defense system in South Korea, which is firmly opposed by the Chinese government.

The risk of open conflict between the world's two largest economies remains remote, but a further deterioration in relations could increase the likelihood of higher trade barriers, which would potentially undermine the global economic recovery. At the very least, rising geopolitical tensions in the Asia-Pacific region could increase the risk premium on regional Asian equity markets, which have been leading the Emerging Market recovery so far in 2017.

QUESTION 16: Can you discuss the growing momentum of environmental, social and governance (ESG) investing and explain the term Impactonomics®?

Impact Investing, the practice of intentionally investing for both attractive financial and social returns, has seen unprecedented interest from both asset managers and asset owners. In its 2016 Trends report, the U.S. Sustainable Investment Forum recorded a 33% two-year growth in assets under management, primarily in active strategies, in a period otherwise dominated by passive investing. The biennial report surveys the assets under management, investing trends, and ESG criteria of U.S. asset managers and institutional investors using one or more sustainable investment strategies and pegs the total at $8.72 trillion, or one-fifth of all investments under professional management in the U.S.

The landscape could not be more different from the pioneering socially responsible investing (SRI) field, which suffered from narrow appeal and a mixed performance track record. Rapidly expanding data sets (over 80% of the companies in the S&P 500 Index now issue a Corporate Social Responsibility Report, up from 20% in 2011) enable fund managers to focus on incorporating ESG metrics into their analysis, comparing companies to find leaders and laggards, versus simply excluding those in historically objectionable industries. Industry groups such as the Sustainable Accounting Standards Board (SASB) have emerged to drive alignment on what data are material to each industry for the purpose of driving better economic outcomes. And academic and practitioner research increasingly points to the potential for such data to be additive to traditional fundamental analysis. With over 80% of the market value of the S&P 500 now attributable to intangible assets, the desire to gain insights into the management of a company's brand, intellectual property, employee base, and supply chain is understandable. In fact, the Department of Labor updated its guidance relating to ESG investing in 2015, advising that not only is consideration of ESG factors acceptable, it is a "proper component" of a fiduciary's responsibility. This seemingly subtle shift has resonated loudly in the institutional world, where a heretofore significant barrier has now been removed.

Client interest, driven by demographics and the availability of mainstream products, has also escalated. According to the 2016 U.S. Trust Insights on Wealth and Worth® Survey, 53% of women, 58% of ultra-high-net-worth investors, and 85% of Millennials own or are interested in owning Impact Investments. The portion of all investors who claim to have reviewed their investment portfolios for impact climbed from 23% in 2015 to 32% in 2016. These investors increasingly understand that with the mainstreaming of corporate ESG practices and the institutional-caliber Impact investment products now available, they do not have to choose between impact and return: 58% believe it is possible to invest based on ESG factors and achieve market rate returns.

Impactonomics® is a lens through which to examine the relationship between economic growth and investing for impact and profit, and the measurable social and environmental changes it can bring. Bringing together historically social factors such as the economic empowerment of women, the preservation of eco-diversity, comprehensive family benefits, or access to health care and the economic analysis of risk and return provides important insights. It operates at firm, sector and geographic levels. Using Impactonomics®, we continue to analyze fund managers' ability to integrate ESG and financial factors into the investment process in a manner that leads to fresh insights and economic and social benefit.

Table 2: Economic and market forecasts (as of March 29, 2017)

	Q4 2016	Q1 2017E	Q2 2017E	2015	2016	2017 E
Real global GDP (% y/y annualized)				3.1	3.1	3.5 – 4.0
Real U.S. GDP (% q/q annualized)	1.9	1.5 – 2.0	2.5 – 3.5	2.6	1.6	2.0 – 3.0
CPI inflation (% y/y)*	1.3	1.6	1.8 – 2.0	0.1	1.3	2.0 – 3.0
Core CPI inflation (% y/y)*	2.2	2.2	2.2	1.8	2.2	2.0 – 3.0
Unemployment rate, period average (%)	4.7	4.7	4.6 – 4.7	5.3	4.9	4.5
Fed funds rate, end period (%)**	0.62	0.87	0.87 – 1.12	0.37	0.62	1.12 – 1.62
10-year Treasury, end period (%)	2.45	2.40	2.50 - 2.60	2.27	2.45	2.62 – 3.12
S&P 500, end period***	2239	2350 – 2375	2350 – 2400	2044	2239	2300 – 2700
S&P operating earnings ($/share)	32	33	34	118	119	129 – 138
$/€, end period	1.05	1.07	1.04 – 1.08	1.09	1.05	1.00 – 1.10
¥/$, end period	117	112	114 - 118	120	117	115 – 125
Oil ($/barrel), end period	54	48	50 - 55	37	54	50 – 70

Percent calendar-year average over calendar-year average annualized unless stated. E = Estimate.

* Latest 12-month average over previous 12-month average.

** Fed funds rate, end period based on market indications.

*** Our 2017 S&P 500 end period forecast, 2450, is the equilibrium target, with 2700 being the highest bull case with pro-growth policies initiated and sentiment driving the earnings number to the upper end of the range.

Past performance is no guarantee of future results.

Economic or financial forecasts are inherently limited and should not be relied on as indicators of future investment performance.

Source: Global Wealth & Investment Management Investment Strategy Committee.

Table 3: Total returns (%, U.S. dollar terms as of March 24, 2017)

	YTD	Last 6 Months	Last 12 Months
Equity Indexes			
S&P 500	5.20	9.44	17.60
Dow Jones Composite	4.85	14.22	20.68
NASDAQ	8.56	10.55	23.67
Russell 2500	1.82	8.06	22.42
Russell 2000	0.08	8.73	27.31
UK (FTSE100)	5.07	4.20	10.12
Japan (TOPIX)	7.02	5.29	18.45
MSCI World	5.94	7.93	16.78
MSCI EAFE	7.37	6.01	14.81
Hang Seng	11.05	3.50	24.23
Euro Stoxx 50	7.62	10.19	15.89
Emerging Market	12.65	6.44	22.32
Asia ex-Japan	12.52	6.34	21.54
DJ US Select REIT Index	-0.90	-5.44	4.18
U.S. Size and Style			
U.S. Small Cap	1.54	8.63	23.95
U.S. Mid Cap	4.60	8.24	18.24
U.S. Value	2.69	9.50	18.55
U.S. Growth	8.12	9.04	17.28
Global Sectors			
Consumer Discretionary	5.99	7.75	12.77
Consumer Staples	8.04	1.31	6.86
Energy	-6.24	4.93	15.47
Financials	4.90	18.87	28.36
Health Care	8.51	1.33	10.01
Industrials	6.46	9.74	17.13
Information Technology	12.09	12.94	27.67
Materials	7.37	12.31	28.85
Telecommunications	2.10	-1.60	2.23
Utilities	7.75	1.87	7.63
Bonds			
10-Year Treasury	0.70	-6.05	-3.05
2-Year Treasury	0.21	-0.33	0.31
TIPS	1.40	-1.29	2.99
Municipals	1.22	-2.27	0.42
Corporate Bonds (Merrill Lynch Corporat e Bonds)	1.35	-1.52	4.12
High Yield Bonds	1.76	4.10	16.20
Emerging Market Bonds	4.37	0.85	12.95
Foreign Exchange			
U.S. Dollar	-2.70	5.14	2.05
British Pound	-0.47	-0.82	-9.81
Euro Stoxx 50	0.38	-0.47	1.12
Japanese Yen	4.30	-7.62	3.38
Swiss Franc	0.43	1.69	1.95
Australian Dollar	2.91	4.48	2.58
Canadian Dollar	0.23	-0.90	-0.23
Hedge Funds			
Global Hedge Fund Index	3.88	2.69	6.21
Hedge Fund Equal Weight	1.24	2.49	6.80
Commodities			
CRB Index	-4.57	0.45	6.98
Gold	7.91	-7.04	2.19
Oil	-14.42	0.54	7.65

Source: Bloomberg. Data as of March 24, 2017. **Past performance is no guarantee of future results.**

When assessing your portfolio in light of our current guidance, consider the tactical positioning around asset allocation in reference to your own individual risk tolerance, time horizon, objectives and liquidity needs. Certain investments may not be appropriate, given your specific circumstances and investment plan. Certain security types, like hedged strategies and private equity investments, are subject to eligibility and suitability criteria. Your financial advisor can help you customize your portfolio in light of your specific circumstances.

ASSET CLASS	CHIEF INVESTMENT OFFICE VIEW					COMMENTS
	Negative		Neutral		Positive	
Global Equities				●		Maintaining our overweight to global equities versus fixed income based on expectations for higher nominal growth and improving corporate profits.
U.S. Large Cap				●		Positive based on higher nominal growth, improving sales and earnings growth for S&P 500 companies, despite extended valuations. Favor cyclical sectors such as consumer discretionary, financials, energy, select industrials and factors like dividend growth, high quality. Prefer Value over Growth based on improving earnings and higher exposure to financials and energy.
U.S. Mid & Small Cap				●		Benefits from the potential for domestic focused fiscal stimulus, lower corporate taxes and easier regulatory environment, given Republican controlled white house and Congress agenda. Neutral mid cap equities.
International Developed				●		Prefer Japan over Europe. Cautious on Europe on busy election calendar in 2017 and rise of populist parties. Positive on Japan on fiscal and monetary stimulus, weaker Yen and potential for improving domestic demand.
Emerging Markets				●		Moderately positive given attractive valuations, improving economic activity, rising commodity prices. Republican sweep and prospect for rising interest rates and U.S. dollar, anti-trade measures have reduced our earlier conviction. Longer-term, reform-oriented countries and consumer spending exposures are preferred.
Global Fixed Income		●				Bonds provide portfolio diversification, income and stability, but low rates skew down-side risk. Slightly short duration is warranted balancing higher short term rates in the U.S and expectations for inflation with overwhelming demand for fixed income globally. Over 20% of Global Aggregate Index trades with negative yields.
U.S. Treasuries		●				Current valuations stretched. Some allocation for liquidity and safety is advised. We expect the Fed will be raising short rates and longer rates will be impacted by impending fiscal stimulus. An allocation to treasury inflation protected securities (TIPS) should be considered where appropriate.
U.S. Municipals				●		Currently cheap vs taxable bonds, based on historical valuations. This provides an opportunity for the intermediate-to-long term. However, we are cautious over the near term until discussions on tax reform bring greater clarity as to the eventual treatment of tax-exempt munis.
U.S. Investment Grade				●		Technical backdrop remains supportive of credit spreads given highly accommodative central bank policies which overshadow the continued softening in corporate fundamentals. Overweight to investment grade credit is biased towards U.S. banks.
U.S. High Yield		●				Valuations are rich. Expect a high degree of volatility. Prefer actively-managed solutions that are higher in credit quality. Fundamentals remain soft. Allocation to floating rate, secured bank loan strategies is advised.
U.S. Collateralized		●				Higher rates have extended durations in Mortgage Backed Securities and continued volatility should continue to weigh on market. Cap rates in Commercial Mortgage Backed Securities (CMBS) have become less appealing. Select opportunities exist in properly structured CMBS and Asset Backed Securities.
Non-U.S. Corporates	●					Select opportunities in European credit, including financials; however, any yield pickup likely to be hampered by a stronger dollar.
Non-U.S. Sovereigns	●					Yields are unattractive after the current run-up in performance; prefer active management.
Emerging Market Debt			●			Vulnerable to less accommodative Federal Reserve policy and lower global liquidity; prefer U.S. dollar-denominated Emerging Market debt. Local Emerging Market debt likely to remain volatile due to foreign exchange component; prefer active management.
Alternatives*			●			Select Alternative Investments help broaden the investment toolkit to diversify traditional stock and bond portfolios.
Commodities			●			Medium-/long-term potential upside on stabilizing oil prices; near-term opportunities in energy equities/credits.
Hedged Strategies			●			We currently emphasize hedge fund strategies that have low to moderate levels of market exposure and those managers that can generate a large portion of their return from asset selection and/or market timing.
Real Estate			●			We prefer opportunistic and value sectors.
Private Equity			●			We see potential opportunities in special situations/opportunistic and private credit strategies.
U.S. Dollar			●			Stronger domestic growth and a less dovish Federal Reserve policy (relative to the monetary policies of other Developed Market central banks) support a stronger dollar going forward.
Cash			●			We have a small cash position awaiting deployment when opportunities arise.

* Many products that pursue Alternative Investment strategies, specifically Private Equity and Hedge Funds, are available only to pre-qualified clients.

Appendix

Index Definitions

Indexes are unmanaged, and an investor cannot invest directly in an index.

Asia ex Japan—MSCI Index is a capitalization-weighted index that monitors the performance of stocks from the Pacific region.

Barclays Capital Aggregate Index represents securities that are U.S. domestic, taxable, and dollar-denominated. The index covers the U.S. investment-grade fixed rate bond market, with index components for government and corporate securities, mortgage pass-through securities, and asset-backed securities. These major sectors are subdivided into more specific indexes that are calculated and reported on a regular basis.

Barclays Capital Global High-Yield Index provides a broad-based measure of the global high-yield fixed income markets. The Global High-Yield Index represents that union of the U.S. High-Yield, Pan-European High-Yield, U.S. Emerging Markets High-Yield, CMBS High-Yield, and Pan-European Emerging Markets High-Yield Indexes. The Global High-Yield Index is a component of the Multiverse Index, along with the Global Aggregate Index. The Global High-Yield Index was created on January 1, 1999, with index history backfilled to January 1, 1990.

CEO Economic Outlook Survey Diffusion Index—The CEO Economic Outlook Index combines the responses on projected sales, capital spending and employment into an overall index that shows how the CEOs believe the U.S. economy will perform in the six months ahead. It is a diffusion index centered on 50, which means anything above 50 is expansion and anything below 50 is contraction.

Consumer Discretionary—S&P Global 1200 Consumer Discretionary Sector Index encompasses those industries in the S&P Global 1200 Index that are most sensitive to economic cycles, such as automobiles, household durable goods, textiles & apparel and leisure equipment & facilities. The index is market-cap-weighted, free-float-adjusted outside the U.S.

Consumer Staples—S&P Global 1200 Consumer Staples Index comprises companies in the S&P Global 1200 Index whose businesses are less sensitive to economic cycles, such as manufacturers and distributors of food & beverage and producers of nondurable household goods and food & drug retailing. The index is market-cap-weighted, free-float-adjusted outside the U.S.

CRB Index—The Reuters CRB Commodity Price Index is an arithmetic average of commodity futures prices with monthly rebalancing.

DJ EURO STOXX 50 is a capitalization-weighted index of 50 European blue-chip stocks from those countries participating in the Economic and Monetary Union (EMU). The equities use free-float shares in the index calculation.

DJ Wilshire REIT Float—The Dow Jones Wilshire REIT Index measures U.S. publicly traded real estate investment trusts. It is a subset of the Dow Jones Wilshire Real Estate Securities Index. It is weighted by full market cap as well as float-adjusted market cap and is quoted in U.S. dollars.

Dow Jones UBS Commodity Index is designed to be a highly liquid and diversified benchmark for commodities as an asset class. The DJAIG Index is composed of futures contracts on 19 physical commodities.

Dow Jones Composite is a price-weighted average of 30 blue-chip industry-leader stocks.

Emerging Market—MSCI Index of daily Total Return.

Energy—S&P Global 1200 Energy Sector Index comprises companies in the S&P Global 1200 Index that are dominated by the construction or provision of oil rigs, drilling equipment and other energy services or engaged in the exploration, refining and transport of oil, gas and other fuels. The index is market-cap-weighted, free-float-adjusted outside the U.S.

Financials—S&P Global 1200 Financials Sector Index consists of companies in the S&P Global 1200 Index involved in activities such as banking, mortgage finance, specialized finance, asset management and custody, corporate lending, financial investment, real estate and REITs. The index is market-cap-weighted, free-float-adjusted outside the U.S.

Global Economic Policy Uncertainty Index—The Global Policy Uncertainty Index tracks the general state of the economy as it relates to businesses. It can include broad economy-wide conditions or specific economic conditions of a particular industry.

Global Hedge Fund Index—The HFRX Global Hedge Fund Index is designed to be representative of the overall composition of the hedge fund universe. It comprises eight strategies: convertible arbitrage, merger arbitrage, equity hedge, equity market neutral, relative value arbitrage, event-driven, distressed securities and macro. The strategies are asset-weighted based on the distribution of assets in the hedge fund industry.

Hang Seng Index is a capitalization-weighted index of 33 companies that represent approximately 70% of the total market capitalization of the Stock Exchange of Hong Kong. The components of the index are divided into four subindexes: Commerce and Industry, Finance, Utilities, and Properties.

Health Care—S&P Global 1200 Health Care Sector Index encompasses companies that manufacture healthcare equipment and supplies or provide healthcare-related services and companies involved in research, development, production and marketing of pharmaceuticals and biotech products. The index is market-cap-weighted, free-float-adjusted outside the U.S.

Hedge Fund Research Inc. (HFRI) Fund of Funds Index is an equally weighted index consisting of domestic and offshore hedge funds of funds. The HFRI Indexes are based on information self-reported by hedge fund managers that decide, on their own, at any time, whether or not they want to provide, or continue to provide, information to HFR Asset Management, L.L.C. ("HFR"). Results for funds that go out of business are included in the index until the date that they cease operations. Therefore, these indexes may not be complete or accurate representations of the hedge fund universe and may be biased in several ways.

HFRI Global Macro Index is a subset of funds included in the broader HFRI Index. Global macro managers may carry long and short positions in any of the world's major capital or derivative markets. These positions reflect their views on overall market direction as influenced by major economic trends and/or events. The portfolios of these funds may include stocks, bonds, currencies and commodities in the form of cash or derivatives instruments. Most funds invest globally in both developed and emerging markets.

Index Definitions *(continued)*

HFRI Relative Value Index is a subset of funds included in the broader HFRI Index. Relative value arbitrage attempts to take advantage of relative pricing discrepancies between instruments including equities, debt, options and futures. Managers may use mathematical, fundamental or technical analyses to determine misvaluations. Securities may be mispriced relative to the underlying security, related security, groups of securities or the overall market. Many funds use leverage and seek opportunities globally. Arbitrage strategies include dividend arbitrage, pair trading, options arbitrage and yield curve trading.

Index of Leading Indicators (The Conference Board)—Starting in May 1990, the index consists of 10 macroeconomic and market sub-components of the Composite Index of Leading Indicators (2010=100).

Industrials—S&P Global 1200 Industrials Sector Index includes companies whose business is dominated by one of the following activities: manufacture and distribution of capital goods, including aerospace and defense, construction, engineering and building products, electrical equipment and industrial machinery. The index is market-cap-weighted, free-float-adjusted outside the U.S.

Information Technology—S&P Global 1200 Information Technology Sector Index covers technology software and services, technology hardware & equipment and semiconductors & semiconductor equipment manufacturers. The index is market-cap-weighted, free-float-adjusted outside the U.S.

ISM Manufacturing Supplier Deliveries Index—Reveals if deliveries from suppliers are faster or slower and is seasonally adjusted.

Japan (TOPIX) is a capitalization-weighted index of all companies listed on the First Section of the Tokyo Stock Exchange.

Markit Global Manufacturing Purchasing Managers' Index—The Global Report on Manufacturing & Services is compiled by IHS Markit based on the results of surveys covering over 18,000 purchasing executives in over 40 countries. Together, these countries account for an estimated 89% of global gross domestic product.

Materials—S&P Global 1200 Materials Sector Index comprises a breadth of commodity-related manufacturing industries, including companies that manufacture chemicals, construction materials, glass, and related packaging products, metals, minerals and mining companies and producers of steel. The index is market-cap-weighted, free-float-adjusted outside the U.S.

MSCI ACWI (All Country World Index) is a free-float-adjusted market-capitalization-weighted index that is designed to measure the equity market performance of developed and emerging markets.

MSCI ACWI FM (Frontier Markets) is a free-float-adjusted market-capitalization-weighted index that is designed to measure the equity market performance of developed and emerging markets. MSCI covers 24 developed, 21 emerging and 31 frontier markets. If there is no designation (such as 'EM' or 'AC') before a regional or composite index, the index consists of developed markets only.

MSCI EAFE is a stock market index that is designed to measure the equity market performance of developed markets (Europe, Australasia, Far East), excluding the U.S. and Canada.

MSCI World Index is a free-float-weighted equity index.

NASDAQ is a broad-based capitalization-weighted index of stocks in all three NASDAQ tiers: Global Select, Global Market and Capital Market. The index was developed with a base level of 100 as of February 5, 1971.

National Council of Real Estate Investment Fiduciaries (NCREIF) Property Index is a market-value-weighted index which measures the performance of investment-grade nonagricultural income-producing properties.

Oil—Bloomberg West Texas Intermediate Cushing Crude Oil Spot Price is usually at parity with the front-month Nymex crude oil contract, with the exception of its three-day delivery scheduling period after the front-month contract expires, also known as a roll.

Russell 1000 Growth® Index includes those Russell 1000 companies with higher price-to-book ratios and higher forecasted growth values.

Russell 1000® Index is a subset of the Russell 3000® Index that measures the performance of the 1,000 largest capitalization companies of the U.S. equity universe.

Russell 1000® Value Index includes those Russell 1000 companies with lower price-to-book ratios and lower expected growth values.

Russell 2000® Index is a subset of the Russell 3000® Index that measures the performance of the 2,000 smallest companies of the U.S. equity universe.

Russell 2000® Growth Index includes those Russell 2000 companies with higher price-to-value ratios and higher forecasted growth values.

Russell 2000® Value Index includes those Russell 2000 companies with lower price-to-book ratios and lower forecasted growth values.

Russell 3000® Index measures the performance of the 3,000 largest U.S. companies based on total market capitalization, which represents approximately 98% of the investable U.S. equity market.

Russell Midcap® Index represents the 800 smallest companies in the Russell 1000® Index.

Russell Midcap® Growth Index includes those Russell Midcap Index companies with higher price-to-book ratios and higher forecasted growth values.

Russell Midcap® Value Index includes those Russell Midcap Index companies with lower price-to-book ratios and lower forecasted growth values.

Russell Top 200® Index is a subset of the Russell 3000® Index that measures the performance of the largest 200 companies by market capitalization of the U.S. equity universe.

VIX—The CBOE Volatility Index (VIX), of the Chicago Board Options Exchange, reflects a market estimate of future volatility, based on the weighted average of the implied volatilities for a wide range of strikes. First- and second-month expirations are used until eight days from expiration, then the second and third are used.

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Alternative Investments such as derivatives, hedge funds, private equity funds, and funds of funds can result in higher return potential but also higher loss potential. Changes in economic conditions or other circumstances may adversely affect your investments. Before you invest in Alternative Investments, you should consider your overall financial situation, how much money you have to invest, your need for liquidity, and your tolerance for risk.

Investments have varying degrees of risk. Some of the risks involved with equities include the possibility that the value of the stocks may fluctuate in response to events specific to the companies or markets, as well as economic, political or social events in the U.S. or abroad. Bonds are subject to interest rate, inflation and credit risks. Investments in high-yield bonds may be subject to greater market fluctuations and risk of loss of income and principal than securities in higher rated categories. Income from investing in municipal bonds is generally exempt from federal and state taxes for residents of the issuing state. While the interest income is tax exempt, any capital gains distributed are taxable to the investor. Income for some investors may be subject to the federal alternative minimum tax (AMT). Investments in foreign securities involve special risks, including foreign currency risk and the possibility of substantial volatility due to adverse political, economic or other developments. These risks are magnified for investments made in emerging markets. Investments in a certain industry or sector may pose additional risk due to lack of diversification and sector concentration. Investments in real estate securities can be subject to fluctuations in the value of the underlying properties, the effect of economic conditions on real estate values, changes in interest rates, and risk related to renting properties, such as rental defaults. There are special risks associated with an investment in commodities, including market price fluctuations, regulatory changes, interest rate changes, credit risk, economic changes and the impact of adverse political or financial factors.

No investment program is risk-free, and a systematic investing plan does not ensure a profit or protect against a loss in declining markets. Any investment plan should be subject to periodic review for changes in your individual circumstances, including changes in market conditions and your financial ability to continue purchases.

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