CAPITAL MARKET OUTLOOK

Chief Investment Office

The opinions are those of the author(s) and subject to change.

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IN THIS ISSUE

MACRO STRATEGY

U.S. economic policies broadly appear to be favorable for growth and risk assets in 2019. Fiscal policy remains stimulative, and the size of the deficit is far down our list of risks to the U.S. economy given the wide spread between nominal growth in the economy and interest rates.

GLOBAL MARKET VIEW

Global water scarcity remains one of our key long-term investment themes, as the world's limited freshwater supply is still under acute pressure. On both the supply and demand side of the equation, global water stress continues to build, setting the stage for a massive build-out of the global water infrastructure over the next decade and beyond.

THOUGHT OF THE WEEK

Investors across the spectrum from retail to institutional can be influenced by a variety of sentiment factors but whatever their motivation, sniffing out shifts in sentiment can help to avoid market imbalances.

PORTFOLIO CONSIDERATIONS

Given our expectation of elevated volatility, we suggest higher-quality exposure, large- over small-caps, companies with pricing power, cash on their balance sheets, the ability to grow dividends, and less leverage.

MACRO STRATEGY

U.S. ECONOMIC POLICY: DOVISH PIVOT, DEREGULATION, DEFICITS AND TRADE WARS

Jonathan W. Kozy, Senior Vice President and Senior Macro Strategy Analyst

Brian Wilczynski, Assistant Vice President and Investment Analyst

U.S. economic policy is set to remain pro-growth for the balance of 2019, in our view. Monetary policy is the biggest new tailwind, yet price inflation is likely going nowhere fast, putting little pressure on the Federal Reserve (Fed) to raise rates again. On the regulatory side, the Council of Economic Advisers (CEA) continues to sift through burdensome regulations, running cost-benefit analysis in an effort to boost growth. 2019 will likely be even better for growth than 2018 on the deregulatory front. While the fiscal deficit and the amount of debt are gaining more attention, for a number of reasons, including our belief that nominal growth is likely to continue to run well above interest rates for the foreseeable future, a fiscal crisis is far down our list of risks to the U.S. economy. Lastly, we continue to believe that there is an end in sight to the trade wars. In the end, the terms will likely be more favorable for the U.S. and global economy in terms of tariff and nontariff barriers, joint venture requirements, intellectual property protection and enforcement.

Fed on hold: We continue to believe that the policy shift away from monetary tightening is a significant reason that risk assets have turned higher, and we think the Fed will remain on hold at least until the end of 2019 for the following reasons: 1) Inflation has been declining and generally remains below the Fed's 2% target, and the Fed is considering a symmetric objective that would require lower rates for longer. 2) The strongest argument for further Fed rate hikes comes from the tightness of the labor market and upward pressure on wages, but the Fed does not target wage inflation. The Fed targets price inflation. While wage inflation is picking up, price inflation pressures remain benign. 3) Importantly, inflation expectations are also tame. After-tax profit margins remain very high, leaving many companies plenty of cash to manage tighter labor markets without letting price inflation get out of hand. Those companies also have the cash to invest in future productivity. 4) Productivity growth is trending higher and also serves to dampen inflation pressures. The determinants of productivity growth suggest this is likely to continue. 5) A relatively strong dollar is also helping keep commodity prices and overall inflationary pressure muted.

Data as of 03/25/2019 and subject to change.

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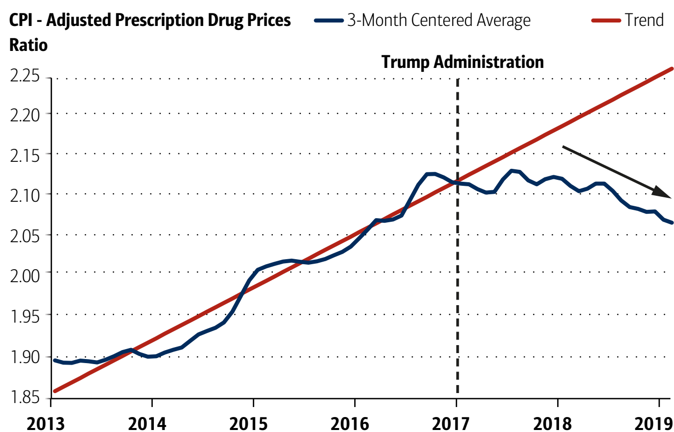
Deregulation: It's no secret that the Trump administration has made a strong deregulatory push, but the removal of impediments to competition and productivity from deregulation and its quantifiable impact on output gets far less attention than it deserves, in our view. There is more to deregulation than just a boost to confidence. For example, a report by the non-partisan Office of Management and Budget estimated that the Trump Administration saved $33B in regulatory costs in its first 21 months in office, compared to an increase of $245B in the same period during the Obama administration. The CEA is an advisory (not policymaking) branch of the government and is currently tasked with running cost-benefit analysis on U.S. regulations with the goal of quantifying the impact of regulations on growth. We think deregulation was a significant tailwind for growth in 2018 that is likely to increase in 2019 as the deregulation push continues. As an example, the CEA has released analysis on the benefits of easing FDA regulations on generic drugs. Drug prices fell for the first time in over 40 years last year (Exhibit 1). This is money in consumers' pockets. Lower drug prices were accomplished partly by removing entry barriers for generics that spurred a jump in the number of cheaper drugs approved by the FDA. Further support for the positive impact from deregulation comes from National Federation of Independent Business (NFIB) small business confidence data that show that government requirements have been much less of a problem since 2016.

Exhibit 1: Consumer Price Index (CPI) – Adjusted Prescription Drug Prices.



Note: Trend covers the second term of the Obama Administration. Sources: Bureau of Labor Statistics; Haver Analytics. Data as of March 15, 2019.

Deficits: Pro-growth tax reform has also raised fears of runaway deficits. We are not in the camp that says that deficits never matter, but the recently growing fiscal deficit is not near the top of our list of risks to the U.S. economic outlook and financial markets. Cross-country analysis suggests this view has some historical support. For example, the United Kingdom had debt in excess of gross domestic product (GDP) for most of the 20th century without a significant financial crisis or solvency event. Japan, the third largest economy in the world, has a debt-to-GDP ratio of over 200%, but interest rates are near zero. And there are plenty of other examples of countries where arbitrarily assigning debt-to-GDP thresholds has turned out to be overly alarmist.

In theory, growing debt can lead to a "crowding out" of private investment because of higher interest rates. While one could argue that interest rates in the U.S. would be lower today if the fiscal deficit was narrowing or overall debt was lower (in the absence of the tax cuts, for example), U.S. rates remain very low in absolute terms. In our 2/18/2019 Capital Market Outlook The Fiscal Bogeyman, we noted that the level of interest rates relative to nominal GDP growth is also a factor in judging the sustainability of government debt. GDP growth in excess of interest rates allows for more stable debt-to-GDP ratios. In the U.S., nominal GDP has averaged 4% over the course of this expansion, while the 10-year Treasury yield has averaged 2.6%. And we expect growth to surprise to the upside. The Congressional Budget Office has indicated that if productivity is 0.5% higher than their estimate, over the next ten years deficits could average 3.7% of GDP instead of the projected 4.4%. In other words, higher growth is a significant swing factor.

Lastly, foreign financing matters very little for the U.S. because we borrow in U.S. dollars. Emerging markets who borrow in U.S. dollars suffer when the dollar strengthens because the value of debt rises in their own currency. This is not the case for the U.S. given our "exorbitant privilege." It is true that foreigners hold over a third of U.S. Treasuries according to Haver Analytics, often raising concerns over foreign demand drying up. But their net purchases have trended lower the last few years, and U.S. rates nevertheless remain low. Other buyers simply fill the gaps because Treasuries remain a relatively safe, liquid, low-risk investment. In fact, one of the biggest risks to financial markets and the U.S. economy from the deficit may be that the "unsustainability" of deficit spending is exaggerated and austerity policies could lead to a recession. There is, for example, evidence that this fear of deficits has stymied the European Union's performance since the financial crisis.

Trade wars: We also believe that there is relief coming from the trade wars. In the end, the terms will likely be more favorable for the U.S. economy in terms of tariff and nontariff barriers, joint venture requirements and intellectual property protection. According to Strategas Research: "Coming into 2018, China had a 10 percent average tariff rate. By comparison, the average U.S. tariff rate was 3.4 percent. Trump made it clear that China cannot

have one of the largest economies in the world and such a high tariff rate. Accordingly, China has been reducing its tariffs on non-U.S. countries as a way to diversify away from the U.S. during the trade spat. Our back-of-the-envelope calculation suggests that its average tariff rate is now 7.5 percent and is likely to drop further as the deal goes through. This is an example of where the post-deal policy is better than before Trump imposed tariffs." Additionally, Larry Kudlow recently suggested that there was a tentative agreement with China on an enforcement mechanism. While timing of a deal remains uncertain, progress is being made. Progress that helps the global economy, not just the U.S.

Bottom line: Many of these issues present notable headline risk as the market frets about trade negotiations with China, rhetoric from the Federal Reserve, and continued handwringing about the deficit. But these underlying policy shifts should ultimately be a net positive for growth and risk assets in 2019.

GLOBAL MARKET VIEW

WATER BLUES: THE CHALLENGES (AND INVESTMENT PLAYS) OF A THIRSTY PLANET

Joseph P. Quinlan, Head of CIO Market Strategy

Cameron Dawson, CFA®, Vice President and Industrial Equity Investment Analyst

Global water scarcity remains one of our key long-term investment themes. From a distance, the Earth's water supply appears abundant. But on closer inspection, much of it is unfit for use by farmers, businesses and households. Of the 71% of the Earth's surface covered by water, around 97% is saltwater found in oceans and seas, with some 2% frozen in snow and ice caps. This leaves just a tiny fraction of liquid fresh water in rivers, lakes, streams and underground aquifers.

And if that wasn't bad enough, the world's limited freshwater supply is still under acute pressure; a third of the world's biggest groundwater systems are in danger of drying out, for instance.[1] Global water demand is six times greater today than it was a century ago—and expected to jump by up to 50% by 2050.[2] What's more, as The Economist recently reported, "The world's water endowment is already highly unequal—just nine countries account for 60% of all available fresh supplies. China and India have about 36% of the world's people, but only about 11% of its fresh water."[3]

Now consider this: Water-linked conflicts between nation-states have spiked in recent years, with the dispute over water between Pakistan and India, two nuclear powers, the most serious potential water conflict in the world. Other potential water adversaries: Egypt and Ethiopia; Turkey versus Iraq and Syria; India and Bangladesh verus China; and the U.S. versus Mexico. Pick your spot: There doesn't appear to be a continent in the world not pressed by acute water challenges.

Finally, add in a global population that is growing and becoming more prosperous, and the premium on fresh water has never been as great as today. Another 1 billion people are expected to crowd the earth between 2015 and 2030 according to the United Nations and, crucially, even more will join the ranks of the world's consumers. Indeed, in an historic inflection point, half the world is now considered middle class, or live in households with enough discretionary income not to be considered poor or destitute. Against this backdrop, think more demand for discretionary items such as cars, household appliances, electronics and higher-protein diets, translating into more demand for natural resources—including water.

According to National Geographic it takes 1,857 gallons of water to produce a pound of beef; 371 gallons for a pound of fresh cheese. Meanwhile, the water intensity of producing one pair of blue jeans requires nearly 2,900 gallons of virtual water. Regarding other products: sausage—1,382 gallons; a pound of processed chicken—589 gallons, and a pound of bananas 103 gallons (Exhibit 2).

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[1] See, "Thirsty Planet," The Economist, March 2, 2019.
[2] Ibid.
[3] Ibid.

Exhibit 2: Virtual Water Use.

Gallons of Water to Produce Each Item

Common Goods	Product	Gallons of Water
	1 Pair Blue Jeans	2,900
	1 Cotton Bed sheet	2,800
	1 Cotton T-Shirt	766
	1 Hamburger	634
	1 Glass of Wine	32
	1 Cup of Tea	9
Meat[1]	**Product**	**Gallons of Water**
	Pound of Beef	1,857
	Pound of Pork	756
	Pound of Chicken	469
Fruits/Vegetables[2]	**Product**	**Gallons of Water**
	Pound of Figs	379
	Pound of Plums	193
	Pound of Bananas	103
	Pound of Apples	84
Animal Products[3]	**Product**	**Gallons of Water**
	Pound of Sausage	1,382
	Pound of Processed Chicken	589
	Pound of Eggs	400
	Pound of Fresh Cheese	371
	Pound of Yogurt	138

Source: National Geographic. Data as of 2017.
[1] Virtual water in cattle, pigs and fowls is the water they drink and water used to grow, feed and clean the waste.
[2] Includes both rainwater and irrigation water.
[3] Virtual water totals include water used to raise animals and process the edible and product.

You get the picture—the direct and indirect demand on the globe's water infrastructure is staggering. Nearly every economic activity requires some water intake, making the water the most precious commodity in the world. In the context of "virtual water," the underlying global demand for water is immense.

That's also true for electricity generation for lighting homes and offices, running industrial machinery and charging electronic devices. This survey states it takes, for example, an estimated one liter of water to light one 60-watt lightbulb for 12 hours alone. Add to that the impact of agricultural subsidies commonly offered to farmers by governments around the world, as well as the estimated effects of climate change, and the scope of the looming water scarcity challenge becomes clear.

As demand increases for agricultural, industrial and consumer use, the 2030 Water Resources Group projects a nearly 40% global shortfall in available fresh water by 2030, based on current levels of water productivity and scheduled investments in water infrastructure. And the United Nations predicts that around 50% of the world's population will be living in areas of high water stress by 2030. The key question for investors is how this gap will close and who will benefit as it does so.

Exacerbating the issues of rising demand and static supply is the crumbling water-related infrastructure around the world that results in high levels of waste for already scarce treated water. Old and toxic lead pipes can cause clean water to become contaminated, while leaks and illegal siphoning result in non-revenue water, water that is treated by utilities but lost in transit to customers, accounting for a wasteful 25%–35% of all treated water volumes in developed markets and even higher levels in developing markets. Infrastructure investment and adoption of new technologies can prevent this waste, with Singapore being the model country at only 5% non-revenue water.[4] Making these investments is costly, however, as the American Water Works Association estimates that the U.S. will need to spend $1 trillion over the next 25 years just to replace aging drinking-water pipes, let alone necessary upgrades to wastewater and storm-water infrastructure.

INVESTMENT CHALLENGES

We expect demand for water services to increase over the coming years and decades, both in emerging and developed economies. This should potentially benefit companies involved in a range of related industries such as water monitoring, wastewater treatment and liquid purification services, as well as those that provide industrial equipment for fluid handling such as pumps, valves, filters, seals and water analysis instruments.

We suggest companies that enable water providers to essentially do more with less. High-quality industrial companies that provide "smart water" and digitization technologies are expected to be key players in solving both the developed and developing world's water challenges, with a key focus on reducing non-revenue water. Smart water solutions include both the connected hardware and software that enables water providers to anticipate problems in the infrastructure and then perform predictive maintenance before problems become very costly to fix. The connected hardware includes everything from water valves and pumps outfitted with sensors to smart buoys constantly testing water quality to smart maintenance devices that can be dropped into water pipelines to locate leaks. This hardware collects an immense amount of data that is then processed and monitored with software that is rapidly growing in functionality. These connected devices are complemented by broader company digitization that is enabling a growing number of workflows to be automated, such as customer service and water-quality testing, creating the potential for significantly lower labor costs. Though the water industry has a history of being slow to adopt new technology, we are seeing more rapid adoption of these smart technologies now that their efficacy has been demonstrated and the potential cost reduction benefit is clear.

Until the issue of wasteful non-revenue water is minimized, essentially the low-hanging fruit of water needs, adoption of alternative water source technologies such as desalination and reuse will likely remain narrow and dependent on specific regional needs and regulations.

Another way to gain exposure to domestic water infrastructure investment is through high-quality water utilities that are rolling up the highly fragmented and widely inefficient water utility industry. Though the physical water infrastructure has to be localized, these utilities can potentially reduce costs by consolidating back office services and bringing a higher level of technology and operating expertise to increase efficiency. These cost savings could be substantial, which frees up capital to be invested in infrastructure and maintenance, reducing risk of water-quality crises. The above-mentioned smart devices and digitization are also enabling these water utilities to come up with lower-cost, creative solutions for truly crumbling infrastructure, where completely rebuilding would be too expensive for local communities to support with higher rates. We look for companies with strong balance sheets, healthy cash flow, and highly skilled management teams that allow for continued consolidation of and higher operating efficiency in the regulated water industry.

[4] Source: Xylem Inc, as of 2018.

The bottom line: The case for water has only become more compelling since we first suggested investment exposure to this resource in 2005 for investors to consider. On both the supply and demand side of the equation, global water stress continues to build, setting the stage for a massive build out of the global water infrastructure over the next decade and beyond.

THOUGHT OF THE WEEK

HOW IS THE MARKET FEELING?

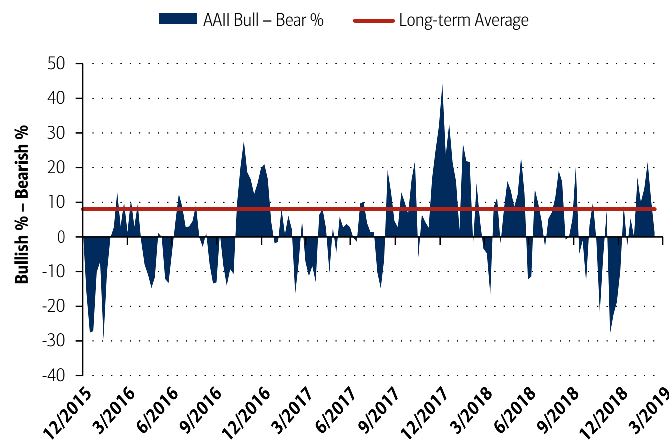
Nick Giorgi, CFA®, Vice President and Investment Strategist

Over a longer timeframe, approaching ten years, asset prices typically converge toward what might be deemed fair value. However, in the near term, markets may diverge from value and be driven by technicals, namely sentiment. Investors across the spectrum from retail to institutional can be influenced by a variety of sentiment factors but whatever their motivation, sniffing out shifts in sentiment can help to avoid market imbalances.

Within the past twelve months there have been two episodes during which many indicators suggested stretched sentiment, characterizing a market feeding off of "euphoria" or "fear." In late January 2018, the bull was running at full speed to the extent that the BofA Merrill Lynch Global Research Bull & Bear[5] indicator flashed a contrarian "sell" signal based upon record equity inflows, bullish hedge fund positioning, and extreme global equity index breadth. Conversely, January 2019 began with a contrarian "buy" signal triggered by poor equity breadth, government bond inflows, and panic levels of index option positioning. For investors, evidence of excess greed in the marketplace often represents an opportune time to reduce risk, while excess fear can present attractive entry points. Both recent instances resulted in a reversal of market trend soon thereafter, effectively busting each sentiment imbalance.

Sentiment levels are currently much more benign, as neither pessimism nor optimism appear overly extended. Fund manager cash levels are currently relatively high, and institutional positioning indicates caution but bond flows and credit market technicals demonstrate more risky behavior. The American Association of Individual Investors (AAII), which polls approximately 160k retail investors on a weekly basis, illustrates sentiment that has recently pulled back below its historical average but well above recent troughs (Exhibit 3). With sentiment roughly balanced, fundamentals appear primed to break the draw and determine if pessimism or optimism will help carry the market moving forward.

Exhibit 3: Individual Investors Have Recently Turned Cautious.



Source: American Association of Individual Investors, Chief Investment Office. Data as of March 14, 2019.

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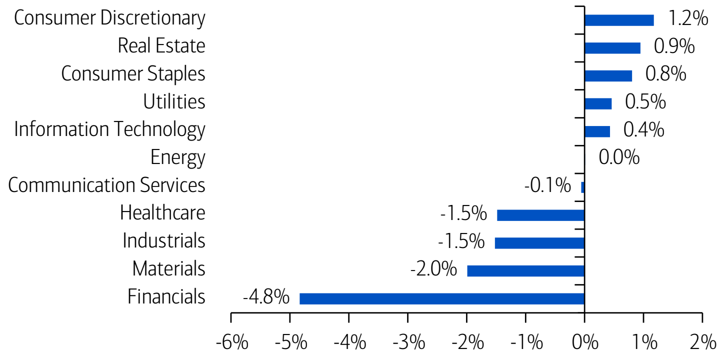
MARKETS IN REVIEW

Equities

	Current	Total Return in USD (%) WTD	MTD	YTD
DJIA	25,502.32	-1.3	-1.5	10.0
NASDAQ	7,642.67	-0.6	1.5	15.5
S&P 500	2,800.71	-0.7	0.7	12.3
S&P 400 Mid Cap	1,854.99	-2.1	-2.8	11.9
Russell 2000	1,505.92	-3.0	-4.3	12.0
MSCI World	2,094.81	-0.6	0.6	11.7
MSCI EAFE	1,882.97	-0.3	0.7	10.1
MSCI Emerging Markets	1,059.63	0.2	0.9	10.0

S&P 500 Sector Returns



Fixed Income[1]

	Current	Total Return in USD (%) WTD	MTD	YTD
Corporate & Government	2.91	1.0	1.7	2.8
Agencies	2.54	0.6	1.1	1.5
Municipals	2.38	0.7	1.2	2.5
U.S. Investment Grade Credit	2.97	0.9	1.6	2.6
International	3.67	1.1	2.0	4.6
High Yield	6.49	0.3	0.6	6.9

	Current	Prior Week End	Prior Month End	2018 Year End
90 Day Yield	2.39	2.39	2.38	2.36
2 Year Yield	2.32	2.44	2.52	2.49
10 Year Yield	2.44	2.59	2.72	2.69
30 Year Yield	2.88	3.01	3.08	3.02

Commodities & Currencies

Commodities	Current	Total Return in USD (%) WTD	MTD	YTD
Bloomberg Commodity	171.13	0.3	0.6	7.1
WTI Crude $/Barrel[2]	59.04	0.9	3.2	30.0
Gold Spot $/Ounce[2]	1,313.70	0.9	0.0	2.4

Currencies	Current	Prior Week End	Prior Month End	2018 Year End
EUR/USD	1.13	1.13	1.14	1.15
USD/JPY	109.92	111.48	111.39	109.69
USD/CNH	6.72	6.71	6.70	6.87

Sources: Bloomberg, Factset. Total Returns from the period of 3/18/2019 to 3/22/2019. Bloomberg Barclays Indices.[1] Spot price returns.[2] All data as of the 3/22/2019 close.
Past performance is no guarantee of future results.

Asset Class Weightings (as of 3/6/19)

	Under-weight		Neutral		Over-weight
Equities	•	•	•	●	•
U.S. Large Caps	•	•	•	●	•
U.S. Mid Caps	•	•	●	•	•
U.S. Small Caps	•	•	•	●	•
International Developed	•	●	•	•	•
Emerging Markets	•	•	•	●	•
Fixed Income	•	●	•	•	•
U.S. Investment Grade Taxable	•	●	•	•	•
International	●	•	•	•	•
Global High Yield Taxable	•	●	•	•	•
U.S. Investment Grade Tax Exempt	•	•	●	•	•
U.S. High Yield Tax Exempt	•	●	•	•	•
Alternative Investments*					
Hedge Funds					
Private Equity					
Real Estate					
Tangible Assets / Commodities					
Cash					

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

Economic and Market Forecasts (as of 3/22/19)

	Q2 2018A	Q3 2018A	Q4 2018A	Q1 2019E	2018A	2019E
Real global GDP (% y/y annualized)	–	–	–	–	3.8*	3.4
Real U.S. GDP (% q/q annualized)	4.2	3.4	2.6	1.0	2.9	2.2
CPI inflation (% y/y)	2.7	2.6	2.2	1.6	2.4	1.8
Core CPI inflation (% y/y)	2.2	2.2	2.2	2.1	2.1	2.2
Unemployment rate (%)	3.9	3.8	3.8	3.9	3.9	3.7
Fed funds rate, end period (%)	1.91	2.18	2.40	2.38	2.40	2.63
10-year Treasury, end period (%)	2.86	3.06	2.68	2.65	2.68	3.00
S&P 500 end period	2718	2914	2507	–	2507	2900
S&P earnings ($/share)	41	43	41*	40	162.5*	170
Euro/U.S. dollar, end period	1.17	1.16	1.15	1.16	1.15	1.25
U.S. dollar/Japanese yen, end period	111	114	110	106	110	101
Oil ($/barrel, avg. of period, WTI**)	68	69	59	58	65	59

The forecasts in the table above are the base line view from BofAML Global Research team. The Global Wealth & Investment Management (GWIM) Investment Strategy Committee (ISC) may make adjustments to this view over the course of the year and can express upside/downside to these forecasts.

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A = Actual. E/* = Estimate. S&P 500 represents a fair value estimate for 2019. **West Texas Intermediate.
Sources: BofA Merrill Lynch Global Research; GWIM ISC as of March 22, 2019.

INDEX DEFINITIONS

Securities indexes assume reinvestment of all distributions and interest payments. Indexes are unmanaged and do not take into account fees or expenses. It is not possible to invest directly in an index. Indexes are all based in dollars.

Index term	Definition
S&P 500 Index	includes a representative sample of 500 leading companies in leading industries of the U.S. economy. Although the index focuses on the large-cap segment of the market, with approximately 75% coverage of U.S. equities, it is also an ideal proxy for the total market
Consumer Price Index (CPI)	is a measure that examines the weighted average of prices of a basket of consumer goods and services, such as transportation, food and medical care. It is calculated by taking price changes for each item in the predetermined basket of goods and averaging them.

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

It is not possible to invest directly in an index.

Asset allocation, diversification, dollar cost averaging and rebalancing do not ensure a profit or protect against loss in declining markets. Dollar cost averaging involves continual investment in securities regardless of fluctuating price levels; you should consider your willingness to continue purchasing during periods of high or low price levels.

Past performance is no guarantee of future results.

Stocks of small-cap companies pose special risks, including possible illiquidity and greater price volatility than stocks of larger, more established companies.

Companies may reduce or eliminate dividend payment to shareholders. Historically, dividends make up a large percentage of stocks' total return.

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Nonfinancial assets, such as closely-held businesses, real estate, oil, gas and mineral properties, and timber, farm and ranch land, are complex in nature and involve risks including total loss of value. Special risk considerations include natural events (for example, earthquakes or fires), complex tax considerations, and lack of liquidity. Nonfinancial assets are not suitable for all investors. Always consult with your independent attorney, tax advisor, investment manager, and insurance agent for final recommendations and before changing or implementing any financial, tax, or estate planning strategy.

Investments in tangible assets are highly volatile and are speculative. 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.

Alternative Investments such as private equity 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.

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The investments discussed 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. 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. 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).

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