CHIEF INVESTMENT OFFICE

Capital Market Outlook

November 30, 2020

All data, projections and opinions are as of the date of this report and subject to change.

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- Macro Strategy—With the help of fiscal stimulus, many U.S. consumers have lived well within their means during the pandemic. The personal savings rate is relatively high at the same time wealth is rising and financial obligations are low, a powerful setup for consumer spending in 2021. Real consumer spending growth in the year ahead could be the fastest we have seen in decades.
- Global Market View—When it comes to foreign trade and immigration, the administration of President-elect Joe Biden is expected to embrace more market-friendly, pro-growth policies. Both variables are important determinants of long-term economic growth and U.S. corporate earnings.
- Thought of the Week—Since the start of the economic recovery, investors have not fully embraced the market rally with sentiment remaining relatively bearish. But on the back of positive vaccine developments and greater clarity around the outcome of the elections, investor sentiment has turned more bullish in November.
- Portfolio Considerations—Headline risk is likely to keep investor risk aversion and cash allocations high, and we expect this to lead to a "seesaw" investment environment until end of November. We would use major weakness in equity markets as a buying opportunity for those who have at least a six-month-or-longer time horizon.

MACRO STRATEGY

Jonathan Kozy
Director and
Senior Macro Strategy Analyst

GLOBAL MARKET VIEW

Joseph P. Quinlan
Managing Director and
Head of CIO Market Strategy

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Vice President and
Investment Strategist

THOUGHT OF THE WEEK

Kirsten Cabacungan
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Data as of 11/30/2020, and subject to change

MACRO STRATEGY

U.S. Consumer: Locked and Loaded for 2021

Jonathan Kozy, Director and Senior Macro Strategy Analyst

A key pillar of support for the U.S. economy has been the resilience of consumer spending in sectors that are relatively immune to coronavirus-induced economic restrictions. This includes online spending and spending on durable consumer goods, including housing-related goods. Given the rising infection case count, the outlook for 2021 in these sectors will likely be particularly important until vaccinations can unleash massive pent-up demand for spending in leisure and service industries. There are high-level reasons to be optimistic. Specifically, the outlook for various sources of funding for U.S. personal consumption expenditures (wages, fiscal stimulus, savings, household wealth and debt) looks to be very positive heading into 2021. Over the last 40 years, the fastest pace of annual real personal consumption expenditure growth was 5.7% in 1983. In our view, there is a decent shot we surpass that in 2021.

Wage and Salary Income: Anchoring U.S. personal income and consumer spending are private sector wages and salaries, which represent 40% to 45% of overall income. Private sector income rose again in October and has now recovered at least 99.5% of pre-coronavirus levels. Similarly, the index of aggregate weekly payrolls, from the Bureau of Labor Statistics Payroll survey also suggests private wages and salaries are over 97% of pre-coronavirus levels. If vaccines are effective in aiding in economic normalization, income in the leisure and hospitality sector has significant upside from its current levels, which are only 77% of February levels. Put simply, the jobs that went away the fastest will likely come back very fast, supporting aggregate wage and salary income.

Looking at higher-frequency data, the labor market remains on track to support incomes despite concerns around the recent coronavirus wave. While the four-week average of initial claims for unemployment insurance is flattening out at a still-high level, continuing claims for unemployment insurance continue to move lower, suggesting the headline unemployment rate is likely to tick lower heading into year-end. We would still broadly characterize the labor market as improving but with lots of churn.

Fiscal Stimulus: An additional fiscal stimulus package is also possible in 2021. The initial pandemic-induced fiscal package included both direct payments to many individuals and enhanced unemployment benefits that sent overall personal income soaring to levels that were higher than income would have been without the pandemic. BofA Global Research expects a package of $500 billion to $1 trillion in the first half of 2021, and the stimulus will likely include enhanced unemployment insurance benefits, directly boosting personal incomes. Additionally, President-elect Biden has talked about additional consumer stimulus including easing student loan burdens.

Personal Savings: November 23 Chief Investment Office Capital Market Outlook pointed out that many U.S. consumers are sitting on a massive savings glut. With the personal savings rate around 13.6%, heading into 2021 consumers have $1.0 trillion in excess savings relative to a normalized personal savings rate of 6.6%. A significant portion of this savings could be characterized as “liquid.” In addition to wages, government transfer payments, and forbearance programs boosting savings, consumers are also benefitting from lower gasoline prices and low borrowing rates. Commuters now working from home are also saving on transportation costs. While savings is not equal across income cohorts, an issue policymakers will likely look to address in the year ahead, the overall personal saving backdrop is supportive of spending in 2021.

Wealth: Household wealth is a source of both direct spending power and consumer confidence, which remains firm despite the recent coronavirus wave. Major sources of wealth such as home prices and equities, including in retirement accounts such as 401(k), are increasing in value. Household net worth, as measured by the Bureau of Economic Analysis and Board of Governors, reached a record high in the second quarter. According to Empirical Research, the top 1% of consumers possess $27 trillion in household wealth, equivalent to 15 years of annual income. Empirical Research also noted that an elevated savings rates at the same time wealth is rising is a rare combination.[1]

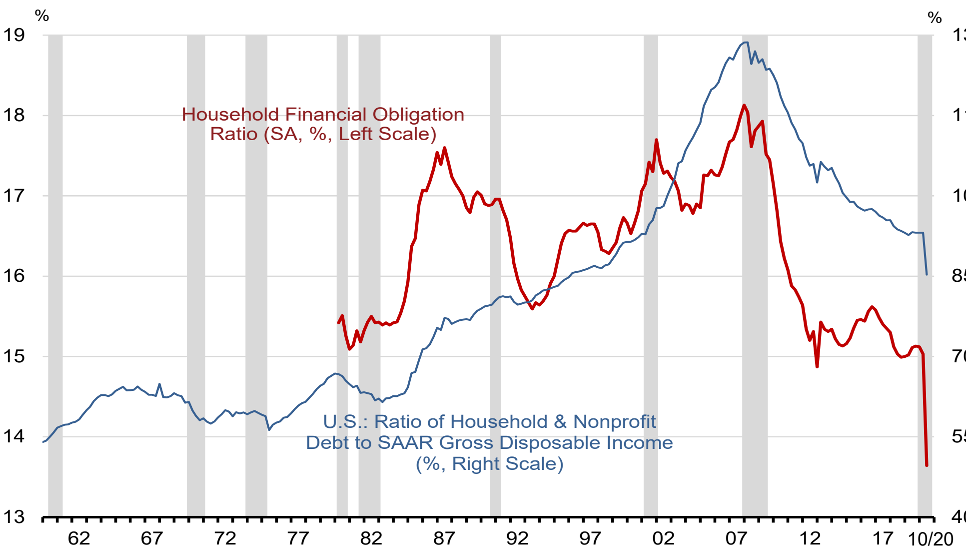
Home equity could be a buffer for high income earnings in the event of tax increases under the new administration, and the data on housing continue to be positive. Last week, data released from the National Association of Home Builders showed builder confidence is at a record high. Once homes are built, there is typically an associated boost to household durable goods like furniture, electronics, autos and do-it-yourself home improvement goods.

Debt: In aggregate, U.S. consumers are over a decade into a deleveraging cycle that has brought the ratio of debt to disposable income back to levels last seen in the mid-1990s. Notably, leverage was falling without the fiscal stimulus payments. Looking to 2021, business cycle expansions typically include a household re-leveraging cycle.

[1] Empirical Research Partners. Consumer Strategy: The Savings Glut. November 17, 2020.

At the same time, private sector interest rates are hitting record lows, pushing the financial obligations ratio to an all-time low (Exhibit 1). There are a few channels here where consumers can support spending through a releveraging cycle. One is through revolving credit, like credit cards. Secondly, consumers could lock in lower interest rates and extend maturities to lower payments by refinancing existing mortgages. In 2021, we are likely to see the backlog of mortgage refinancing and new refinancing pay dividends. A refinance typically entails some upfront cost followed by immediate monthly cash flow debt savings from lower rates.

Exhibit 1: Record-Low Financial Obligations as a Share of Disposable Personal Income.



Sources: Federal Reserve Board/Haver Analytics. Data as of October 2, 2020.

Of course, banks have to be willing to lend. In the fourth quarter, the Federal Reserve's (Fed's) Senior Loan Officer Survey showed the net share of banks tightening standards on residential mortgages improved from 61% to 16%.[2] Standards for other consumer loans also showed improvement but are still in "net tightening" territory as banks factor in the risks of the coronavirus and economic restrictions. While the data are currently mixed, if the economy gains traction and banks loan loss reserves are released, we will likely see improving lending standards on balance next year. And so far, tighter lending standards from commercial banks have not inhibited spending on houses or consumer durable goods, as nonbank lenders fill the gaps.

Conclusions, Caveats and Investment Implications: Putting it all together, real consumer spending growth in the year ahead could be the fastest we have seen since the early 1980s when real consumer spending grew close to 6%. Overall gross domestic product (GDP) growth is likely to also benefit from an associated inventory build over the next few quarters. The U.S. Bureau of Economic Analysis' (BEA's) business inventory to sales ratio is at its lowest level since 2012. Businesses are likely planning for the back half of 2021 when vaccines could be gaining traction.

While the aggregate data on the consumer backdrop are positive, the story does not apply to every cohort, and policymakers should work to address the gaps. The unemployment rate remains elevated, with millions of people relying on government programs for income. And it is worth repeating that working from home does not work for all.

For investors, interest rate-sensitive sectors like autos and housing should continue to benefit from lower rates and strong consumer fundamentals. As mentioned, the housing cycle expansion will also support durable goods spending on furniture, electronics, autos and home improvement goods. Additionally, vaccines provide significant upside to the leisure and hospitality sectors.

[2] Calculated by Haver Analytics as of November 24, 2020.

GLOBAL MARKET VIEW:

Two Planks for Growth Under the New Administration

Joseph P. Quinlan, Managing Director and Head of CIO Market Strategy

Lauren J. Sanfilippo, Vice President and Investment Strategist

When it comes to foreign trade and immigration, the administration of President-elect Joe Biden is expected to embrace more market-friendly, pro-growth policies—aka, favor a more multilateral approach to trade and a more liberal/open stance toward immigration. Both variables—as we discuss below—are important determinants of long-term economic growth and U.S. competitiveness.

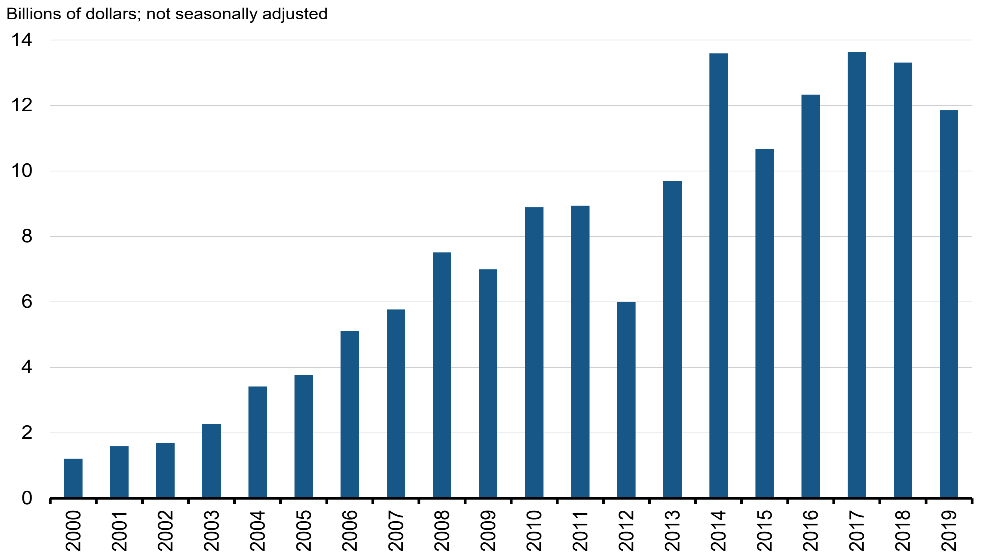
Don't be fooled by the trade numbers

The rap on U.S. exports is that as a driver of growth, they are inconsequential, since U.S. exports (goods and services) accounted for just 11.7% of GDP in 2019; the share of imports—14.6%—was slightly higher, curating the impression that foreign trade matters little to the consumption-led U.S. economy.

Nothing could be further from the truth. The U.S. economy is large, but the rest of the world is larger and more populated. U.S. GDP accounted for just 24% of the global total in 2019, while America's population is less than 5% of all of humanity. Beyond our shores, in other words, there is a great deal of earnings potential for Corporate America, although tapping this potential has become more challenging over the past few years against a backdrop of rising U.S. tariffs and retaliatory actions taken by our trading partners. Add in rising U.S.-Sino trade tensions, pressure on U.S. firms to "reshore" production, and the U.S. walking away from one of the largest trade deals in history (the Transpacific Partnership Agreement), and it's hardly been smooth sailing for U.S. firms leveraged to foreign markets over the past few years.

The tone of trade in the next administration, however, will likely be different. It should be multilateral in scope; it should be more conciliatory toward U.S. allies, notably the European Union, the largest overseas market for U.S. goods and services; and it should be tough on China but also open to de-escalating trade and investment tensions between the world's two largest economies, while working with China in tackling climate change and the pandemic. In that China has emerged as a key source of U.S. earnings over the past two decades (Exhibit 2), any ratcheting down of trade tensions between the U.S. and China would be welcomed by Corporate America. When it comes to U.S. corporate earnings, China matters.

Exhibit 2: U.S. Affiliate Income Earned in China.



Source: Bureau of Economic Analysis. Data available through 2019-latest available data.

That said, the benefits of expanding trade ties go beyond just corporate earnings. As multiple empirical studies have concluded, the greater the volume of trade of a country, the greater the competition, the higher the level of productivity, and the more efficient allocation of resources. Trade begets more innovation, economies of scale, and high-end specialization. It's a catalyst for more crossborder investment, employment and higher incomes. And finally, more trade also means lower prices for consumers and more competitively priced choices.

All of the above is another way of saying that the new administration's approach to trade is expected to be more supportive of U.S. growth and corporate earnings. Improving U.S. trade relations with the rest of the world is bullish for U.S. equities.

Immigration matters to growth and innovation

Like trade, immigration policies under the President-elect Biden administration are likely to become more liberal and open, in contrast to the tougher entry policies of the current administration. Under the latter, legal immigration has been cut nearly in half since 2017.[3] The denial rate on new H-1B petitions for foreign skilled workers jumped from 6% in full year (FY) 2015 to 30% in FY 2020.[4] Refugees and asylum seekers have not been spared either: For FY 2020, the ceiling for refugees was 84% lower than the final year of the Obama administration.[5] Meanwhile, the number of military naturalizations and naturalizations in general have all declined in the past few years—with all of the above emblematic of the more restrictive immigration policies.

Enter the President-elect Biden administration, which has pledged to "modernize America's immigration system." What this means in reality remains to be seen. However, the general consensus is that U.S. immigration policies—for humanitarian and economic reasons—are expected to be less restrictive and more strategic under the new administration. In our opinion, this is a bullish indicator for the U.S. given the importance of immigrants to the U.S. labor force and economy, as detailed in Exhibit 3.

Exhibit 3: The Heavy Lifting of Immigrants.

Share of Foreign-Born Workers (%)	
All Occupations	**17.5%**
Healthcare	
Home Health Aides	35.2%
Physicians	28.5%
Personal Care Aides	24.7%
Pharmacists	22.4%
Nursing Assistants	20.9%
Surgeons	18.9%
Registered Nurses	15.0%
Respiratory Therapists	13.1%
Miscellaneous	
Farming, fishing and forestry	41.8%
Building and grounds cleaning/maintenance	36.9%
Construction and extraction	30.0%
Computer and mathematics	26.8%
Transportation and material moving	20.6%
Architecture and engineering	19.6%
Installation, maintenance and repair	14.7%

Employed foreign-born persons 16 years and over, 2019 annual averages.
Sources: Bureau of Labor Statistics; National Foundation for American Policy. Data as of May 15, 2020.

Whether at the high end of skills or low end, the foreign-born workforce of America is critical. Of the total U.S. workforce, 18% of workers are foreign-born, or 27.5 million workers. This reliance on foreign labor spans various industries, from architecture and engineering (20% foreign-born) to

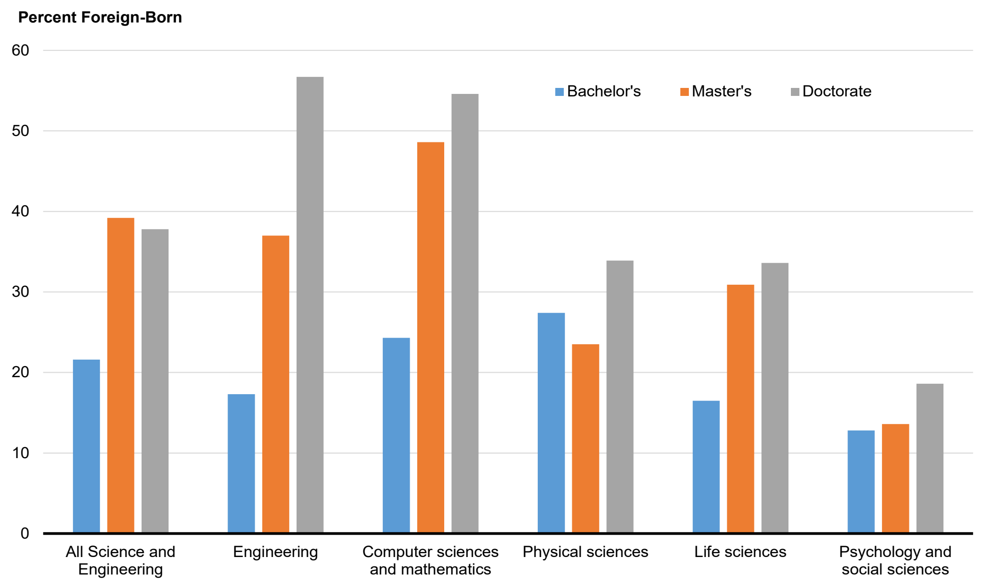
[3] See, "A Review of Trump Immigration Policy," Forbes, August 26, 2020.
[4] Ibid.
[5] Ibid.

farming (42%) and construction (30%). Sharing the pandemic's burden on our healthcare workers, more than 28% of our physicians are foreign-born, 22% of pharmacists, 15% of registered nurses and 19% of surgeons. Whether it's responding to medical needs during the pandemic or maintaining buildings for the return of school or work, the United States relies heavily on immigrants to contribute to the quantity and quality of labor supply here in the U.S.

In addition, immigrants not only fill jobs, they create jobs. America's world-class entrepreneurial ecosystem has long been driven by some of the world's best and the brightest immigrant founders and chief executives like Google co-founder Sergey Brin or CEO Sundar Pichai, Microsoft CEO Satya Nadella, and Elon Musk, the founder of Tesla and SpaceX. A National Foundation for American Policy report found that 55% of the country's $1 billion startup companies had at least one immigrant founder.[6] Immigrants are heavily represented in the ranks of U.S. unicorn key leadership roles.

And when it comes to higher education specific to the science and engineering fields, in many occupations the higher the degree level, the greater the proportion of the workforce who are foreign-born (Exhibit 4). In both engineering and computer sciences, more than half of doctorate holders are foreign-born, a disproportionate share considering only 17% of the college graduate population in the U.S. is foreign-born.

Exhibit 4: Degree Holders in Science and Engineering Occupations.



Source: National Center for Science and Engineering Statistics. Data as of January 2020.

In the end, immigrants matter. As does trade. And under the President-elect Biden administration, both policies are likely to be set to become more pro-growth and pro-earnings, adding more momentum to a market rally being powered by greater political clarity, prospects of a vaccine for coronavirus, and continued fiscal and monetary policy support.

[6]National Foundation for American Policy, October 24, 2018.

THOUGHT OF THE WEEK:

Merrier Investor Sentiment but No Euphoria

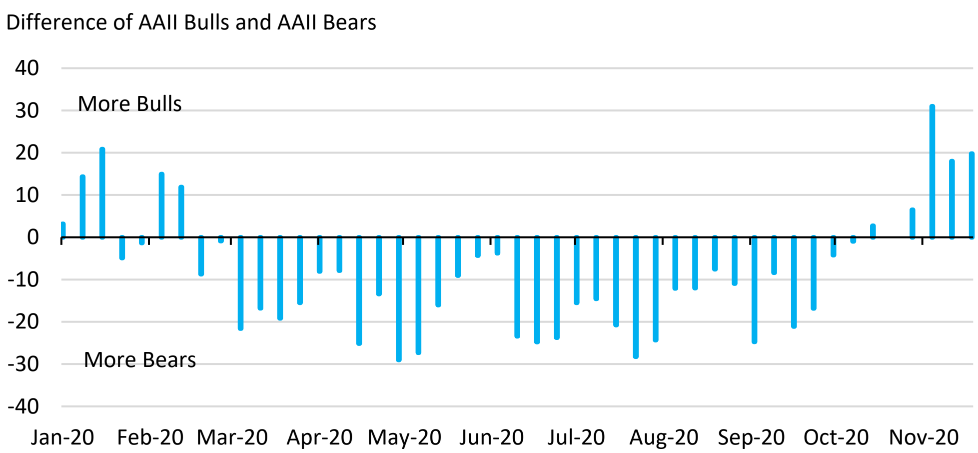
Kirsten Cabacungan, Investment Analyst

Since the start of the economic recovery, investors have not fully embraced the market rally, with sentiment remaining relatively bearish. But on the back of positive vaccine developments and greater clarity around the outcome of the elections, investor sentiment has turned more bullish in November.

Investors who maintained elevated levels of cash throughout the pandemic have redeployed some of this capital. Fund manager cash holdings fell in November to 4.1%, down from 5.9% in April, and now sit lower than the pre-coronavirus level in January at 4.2%, according to BofA Global Research. More cyclically oriented areas of the market have benefited, with all sectors positive for the month led by Energy, Financials and Industrials, and market breadth improving with roughly 93% of S&P 500 stocks trading above their 200-day moving average.

The Chicago Board Options Exchange (CBOE) Volatility Index (VIX), used as a gauge for investor uncertainty, has shown volatility moving lower and levels receding during market down days. The American Association of Individual Investors® (AAII) sentiment survey confirms the rise in bullishness with the second week of November bull reading at 55.8, a level only last seen in January 2018 (Exhibit 5). But could these more elevated sentiment indicators be a sign that optimism is turning overly exuberant?

Exhibit 5: Investment Sentiment Is Turning More Bullish.



Source: Bloomberg. Data as of November 30, 2020. Short term performance shown to illustrate more recent trend. **Past performance is no guarantee of future results.**

The bullish breakaway pulled back some with the AAII bull reading in the subsequent week roughly 12 points lower at 44.3, likely in the wake of rising coronavirus cases, and the ratio of AAII bulls to bears currently in the 73rd percentile is still not at a statistically worrisome level. Despite more cash reentering the market, money market assets under management still sits at $4.3 trillion, roughly $700 billion higher than the level at the end of 2019.

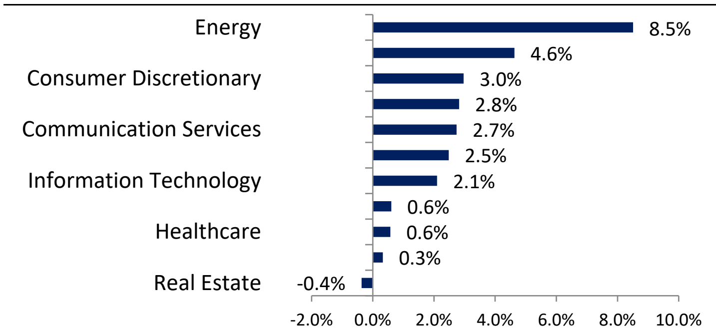
Although positive vaccine developments remain a bright spot, the rising level of coronavirus cases, record hospitalizations and heightened potential for further shutdowns are major near-term risks to sentiment. For now, investor sentiment remains closer to neutral, in our view, given that cash levels still remain elevated and near-term sentiment continues to fluctuate. We believe some consolidation could be healthy for the market but see the current backdrop of an accommodative Fed and continued progress in the economic recovery as supportive for higher equities into 2021.

MARKETS IN REVIEW

Equities

	Total Return in USD (%)			
	Current	WTD	MTD	YTD
DJIA	29,910.37	2.2	13.1	7.0
NASDAQ	12,205.8	3.0	12.0	37.2
S&P 500	3,638.35	2.3	11.4	14.5
S&P 400 Mid Cap	2,205.92	2.7	16.2	8.5
Russell 2000	1,855.27	3.9	20.7	12.5
MSCI World	2,601.45	2.4	13.6	12.0
MSCI EAFE	2,080.15	2.2	17.0	4.3
MSCI Emerging Markets	1,230.72	1.8	11.6	12.5

S&P 500 Sector Returns



Fixed Income†

	Total Return in USD (%)			
	Current	WTD	MTD	YTD
Corporate & Government	1.11	-0.03	1.23	8.72
Agencies	0.52	-0.01	0.20	5.34
Municipals	1.18	0.08	1.43	4.50
U.S. Investment Grade Credit	1.16	-0.03	0.91	7.28
International	1.82	0.13	2.57	9.18
High Yield	4.71	0.63	3.88	5.06

	Current	Prior Week End	Prior Month End	2019 Year End
90 Day Yield	0.07	0.06	0.09	1.54
2 Year Yield	0.15	0.16	0.15	1.57
10 Year Yield	0.84	0.82	0.87	1.92
30 Year Yield	1.57	1.52	1.66	2.39

Commodities & Currencies

	Total Return in USD (%)			
Commodities	Current	WTD	MTD	YTD
Bloomberg Commodity	159.70	0.9	4.1	-7.2
WTI Crude $/Barrel††	45.53	8.0	27.2	-25.4
Gold Spot $/Ounce††	1787.79	-4.4	-4.8	17.8
Currencies	Current	Prior Week End	Prior Month End	2019 Year End
EUR/USD	1.18	1.17	1.17	1.12
USD/JPY	105.62	105.29	105.48	108.61
USD/CNH	6.69	6.75	6.78	6.96

Sources: Bloomberg, Factset. Total Returns from the period of 011/23/2020 to 11/27/2020. †Bloomberg Barclays Indices. ††Spot price returns. All data as of the 11/27/2020 close.
Past performance is no guarantee of future results.

Asset Class Weightings (as of 9/1/2020)

	Under-Weight		Neutral	Over-Weight	
Global Equities				●	
U.S. Large Caps Growth				●	
U.S. Large Caps Value				●	
U.S. Small Caps Growth				●	
U.S. Small Caps Value			●		
International Developed			●		
Emerging Markets	●				
Global Fixed Income					
U.S. Governments		●			
U.S. Mortgages		●			
U.S. Corporates				●	
High Yield		●			
U.S. Investment Grade Tax Exempt			●		
U.S. High Yield Tax Exempt		●			
International Fixed Income	●				
Alternative Investments*					
Hedge Funds					
Private Equity					
Real Assets					
Cash					

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

CIO asset class views are relative to the CIO Strategic Asset Allocation (SAA) of a multi-asset portfolio.

Economic & Market Forecasts (as of 11/27/2020)

	2019A	Q1 2020A	Q2 2020A	Q3 2020A	Q4 2020E	2020E
Real global GDP (% y/y annualized)	2.9	-	-	-	-	-3.7
Real U.S. GDP (% q/q annualized)	2.2	-5.0	-31.4	33.1	4.0	-3.5
CPI inflation (% y/y)	2.3	1.5	0.6	1.3	1.1	1.2
Core CPI inflation (% y/y)	2.3	2.1	1.2	1.7	1.6	1.7
Unemployment rate(%)	3.5	3.8	13.0	8.8	6.5	8.0
Fed funds rate, end period (%)	1.55	0.08	0.08	0.09	0.13	0.13
10-year Treasury, end period (%)	1.92	0.67	0.66	0.68	0.90	0.90
S&P 500 end period	3231	2585	3100	3363	3250	3250
S&P earnings ($/share)	163	33	28	39	38	138
Euro/U.S. dollar, end period	1.12	1.10	1.12	1.17	1.18	1.18
U.S. dollar/Japanese yen, end period	109	108	108	105	103	103
Oil ($/barrel, avg. of period, WTI**)	57	46	29	40	44	40

The forecasts in the table above are the base line view from BofA Global Research. 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. Historical data is sourced from Bloomberg, FactSet, and Haver Analytics.

Past performance is no guarantee of future results. There can be no assurance that the forecasts will be achieved. Economic or financial forecasts are inherently limited and should not be relied on as indicators of future investment performance.

A = Actual. E/* = Estimate. S&P 500 represents the year-end target for 2020. **West Texas Intermediate.
Sources: BofA Global Research; GWIM ISC as of November 27, 2020.

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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.

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.

Chicago Board Options Exchange (CBOE) Volatility Index (VIX) is a real-time market index that represents the market's expectation of 30-day forward-looking volatility.

Indexes of Aggregate Weekly Payrolls are calculated by dividing the current month's aggregate by the average of the 12 monthly figures for the base year. Indexes are averages for production and nonsupervisory employees.

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