Chief Investment Office • MARCH 2017

The Madness of March

With the "madness" of March upon us, some would argue the same description applies to the financial markets and global economy. 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 February to its highest level in almost five years, and emerging markets have climbed out of a long five-year bear market. Better-than-expected profit growth in the emerging markets and Japan, greater stability in Europe's economy and rising nominal growth in China and the U.S. are leading to an old-fashioned synchronized global expansion. We expect global nominal growth to continue to surprise to the upside in the coming months.

With global inflation 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 hike the benchmark rate at this week's meeting and at least two more times in 2017. This "normalization" coupled with the momentum in the profits cycle has led us to believe we are firmly in the beginning of the late-cycle stage. This stage should last into 2018 and continue to be characterized by a catch-up trend on rates, a steep yield curve, some subtle increases in pricing power and economic surprises in the emerging markets, which were the last economies to recover, primarily due to the after-effects of the strong dollar and collapse in commodity and oil prices from late 2014 to early 2016.

Late-cycle phases tend 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 typically recovers in greater magnitude than other large economic zones and markets. We expect very similar performance trends this time around. However, some growth pockets across sectors are also attractive. These tend to be found in the Technology and Health Care sectors. Financials remain one of our more favored sectors as well.

The "madness" in profits should be evident in first-quarter earnings announcements, which are released beginning in early April. We expect positive profit revisions and elevated business confidence to underpin a move to record highs in equities through April. Moreover, one should not dismiss the possibility of a blow-off move towards the top end of the Year

The CIO View

ISC Viewpoint provides a comprehensive monthly update on the market outlook for clients of Merrill Lynch, including the tactical asset allocations summarized below.

For the complete version of the table see page 13. ▶

ASSET CLASS	CHIEF INVESTMENT OFFICE VIEW				
	Negative		Neutral		Positive
Global Equities				●	
U.S. Large Cap				●	
U.S. Mid & Small Cap				●	
International Developed				●	
Emerging Markets				●	
Global Fixed Income		●			
U.S. Treasuries		●			
U.S. Municipals				●	
U.S. Investment Grade				●	
U.S. High Yield		●			
U.S. Collateralized		●			
Non-U.S. Corporates	●				
Non-U.S. Sovereigns	●				
Emerging Market Debt			●		
Alternatives*			●		
Commodities			●		
Hedged Strategies			●		
Real Estate			●		
Private Equity			●		
U.S. Dollar			●		
Cash			●		

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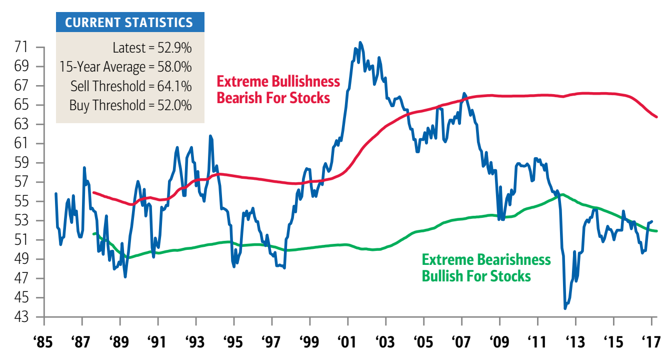
Ahead (sentiment-driven) S&P 500 range of 2300-2700 based on a further synchronized global expansion, expectations for U.S. fiscal stimulus measures (namely tax reform) later in the year, and an active but still patient Fed. One of our contrarian indicators, BofAML Sentiment indicator, shows that strategists' allocations to equities are at bearish levels that historically have been a bullish signal for equities (see Exhibit 1). Our central tendency target for the full year remains 2450 given current valuation levels, which are fair to a slight premium in absolute terms, in our view. On a relative basis versus fixed income, global equities continue to be a high overweight across all profiles in our multi-asset portfolios.

Let the madness begin.

Exhibit 1: Sell Side Consensus Indicator (as of 28 Feb 2017)

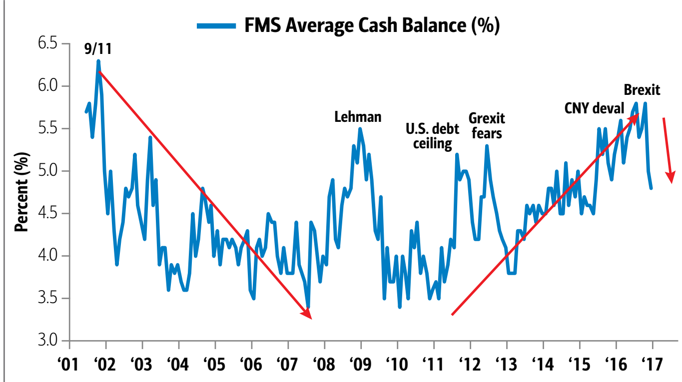


Source: BofA Merrill Lynch Global Research US Equity & Quant Strategy
Note: Buy and Sell signals are based on rolling 15-year +/- 1 standard deviation from the rolling 15-year mean. A reading above the red line indicates a Sell signal and a reading below the green line indicates a Buy signal.

Portfolio Strategy and Asset Allocation

- **We continue to expect equities to outperform fixed income:** We expect equities to remain in an uptrend as U.S. and global expansions gradually continue. Relative valuations versus fixed income in general remain attractive and corporate profits continue to improve. In the shorter term, we have moved from a "get paid to wait" core portfolio theme to a more cyclical-and value-oriented theme in multi-asset portfolios. We continue to see fund managers reducing cash levels to reallocate into cyclical sectors of the markets (see Exhibit 2). We also advise increasing less-correlated investments and committing to an increased level of tax-efficiency and rebalancing. Information Technology remains our favored sector for long-term growth.

Exhibit 2: Global FMS Cash balances as % AUM



Source: BofAML Global Investment Strategy, FMS

- **We are overweight U.S. equities:** U.S. equity market valuations appear slightly extended at approximately 20 times consensus S&P 500 earnings on a trailing basis, and around 18 times 2017 calendar-year earnings. 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 to 2700 reflecting the potential for fiscal stimulus and tax reform. Within U.S. equities, we maintain a slight overweight to large-cap stocks and value over growth investments. We are also overweight U.S. small-caps as we believe they will be beneficiaries of stronger U.S. growth.

- **We are overweight emerging market equities:** We maintain emerging market equities at overweight. They continue to face a range of challenges, including low commodity prices, gradual normalization of Federal Reserve interest rate policy and the structural downshift in China's growth rate. However, we believe they will benefit from the recent pick-up in global cyclical momentum, and valuations are attractive. We still view markets such as India—that 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.

- **We recommend a slight overweight in international developed equities with a preference for Japan:** We acknowledge that Japan's economy has structural impediments to growth such as high debt levels and 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 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 the triggering of Brexit looming in the first quarter.

- **We are underweight fixed income:** 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 in terms of yield. Allocations to HY should be with an active manager favoring higher-quality securities. Current valuations lead us to be cautious on allocations to index-based solutions in high-yield, as we prefer to be "up-in-quality" at this point in the cycle.

  We recommend active management to improve potential risk-adjusted returns in a rising rate environment. A barbell strategy of owning bonds with both longer and shorter maturities should perform better than a bulleted strategy.

- **We are neutral commodities:** Commodity prices are likely range-bound in the near-term, weighed down by global economic policy uncertainty but held up by stable global cyclical momentum. We think oil prices will finish the year 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 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 situation and private credit. We favor a steady commitment strategy and manager selectivity in diversified PE portfolios.

- **We remain neutral in 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.

- **The dollar:** The dollar is overvalued on a broad trade-weighted basis, but interest rate differentials are favorable and we believe further dollar appreciation is likely.

- **"A Transforming World" investment themes (Earth, people, innovation, markets, government):** We favor themes such as robotics, cloud computing, big data, cybersecurity, agriculture, water scarcity, financial technology, emerging market internet users, alternative energy and defense.

Macro strategy

- Purchasing Managers' Indexes around the world show the global expansion has become more synchronized as emerging markets begin to pick up after a five-year slowdown. The global manufacturing Purchasing Managers' Index rose in February to its highest level in almost five years.
- The U.S. is leading the global pickup. Business and consumer surveys continue to show a dramatic increase in economic confidence and optimism since the elections. We believe that the relationship between confidence and economic growth points to much stronger growth and profits.
- With inflation moving gradually higher, we expect the Fed to raise rates a few more times this year, but policy will generally remain accommodative. Housing is an important tailwind for the U.S., and residential investment appears to be rebounding, along with business spending on equipment.

Longer-term themes and trends				
Water	Agricultural Commodities	Climate Change	Global Obesity	Global Healthcare
Robotics and Global Information Technology	Rise of the Emerging Market Middle-Class Consumer	Womenomics	Global Commercial Real Estate	Global Defense and Cyber Security

Table 1: Economic and Market Forecasts (as of March 14, 2017)

	Q2 2016	Q3 2016	Q4 2016 E	2015	2016 E	2017 E
Real global GDP (% y/y annualized)				3.1	3.1	3.5 – 4.0
Real U.S. GDP (% q/q annualized)	1.4	3.5	1.9	2.6	1.6	2.0 – 3.0
CPI inflation (% y/y)*	0.7	0.9	1.3	0.1	1.3	2.0 – 3.0
Core CPI inflation (% y/y)*	2.1	2.2	2.2	1.8	2.2	2.0 – 3.0
Unemployment rate, period average (%)	4.9	4.9	4.7	5.3	4.9	4.5
Fed funds rate, end period (%)	0.37	0.37	0.62	0.37	0.62	0.87 – 1.37
10-year Treasury, end period (%)	1.49	1.60	2.45	2.27	2.45	2.62 – 3.12
S&P 500, end period	2099	2168	2239	2044	2239	2300 – 2700
S&P operating earnings ($/share)	29	30	32	118	119	129 – 138
€/$, end period	1.10	1.12	1.05	1.09	1.05	1.0 – 1.10
$/¥, end period	103	101	117	120	117	115 – 125
Oil ($/barrel), end period	48	48	54	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.
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.

The Chief Investment Office (CIO), in conjunction with the Research Investment Committee (RIC), is introducing a new asset allocation framework. This new framework is designed to 1) enhance the quality of goals-based advice to clients, 2) incorporate many secular and cyclical changes to market, macro and demographic conditions, and 3) provide unified and enhanced investment guidance by leveraging all CIO views and BofA Merrill Lynch Global Research. The CIO derives the Capital Market Assumptions (CMA) and Strategic Asset Allocations (SAA), which are constructed for a 20- to 30-year planning horizon, as described below. The Tactical Asset Allocation process remains the same and uses the Strategic Asset Allocation from the CIO as the starting point.

The new Capital Market Assumptions, which inform the long term Strategic Asset Allocation percentages as the foundation for goals-based advice, have been adjusted to take into account a number of key changes that have occurred during the latest economic cycle. In addition, the CMAs are geared, more importantly, to reflect significantly evolving long term demographic trends, industry developments regarding asset class correlation and their trends, the level of interest rates (both short and long), inflation, and volatility. The shift in long term demographics, which is just beginning to unfold, is likely to have a more dramatic impact on asset class returns, yields, risk and volatility than experienced in prior cycles, in our view.

Table 2: Strategic & Tactical Allocations For US Clients (Tier 0 liquidity)

	Single Asset Class All Fixed Income		Conservative		Moderately Conservative		Moderate		Moderately Aggressive		Aggressive		Single Asset Class All Equity	
	Strategic	Tactical	Strategic	Tactical	Strategic	Tactical	Strategic	Tactical	Strategic	Tactical	Strategic	Tactical	Strategic	Tactical
Equities	0%	0%	21%	24%	37%	42%	53%	60%	69%	74%	84%	89%	98%	98%
U.S. Large Cap Growth	0%	0%	5%	4%	9%	8%	12%	11%	16%	15%	19%	18%	23%	22%
U.S. Large Cap Value	0%	0%	8%	10%	14%	16%	19%	22%	25%	27%	29%	31%	36%	36%
U.S. Small Cap Growth	0%	0%	1%	1%	1%	2%	2%	3%	2%	3%	3%	4%	3%	3%
U.S. Small Cap Value	0%	0%	1%	2%	1%	2%	2%	4%	2%	3%	3%	4%	4%	5%
International Equity	0%	0%	5%	5%	9%	10%	13%	14%	17%	18%	21%	22%	24%	24%
Emerging Markets	0%	0%	1%	2%	3%	4%	5%	6%	7%	8%	9%	10%	8%	8%
Fixed Income	98%	98%	55%	52%	61%	56%	45%	38%	29%	24%	14%	9%	0%	0%
Governments	28%	27%	17%	15%	17%	14%	14%	10%	9%	6%	5%	2%	0%	0%
Mortgages	23%	23%	12%	11%	15%	14%	11%	9%	7%	6%	3%	2%	0%	0%
Corporates	24%	28%	10%	12%	15%	17%	14%	16%	9%	10%	4%	5%	0%	0%
High Yield	7%	5%	4%	3%	5%	3%	4%	2%	3%	2%	1%	0%	0%	0%
Intl Fixed Income	16%	15%	12%	11%	9%	8%	2%	1%	1%	0%	1%	0%	0%	0%
Cash	2%	2%	24%	24%	2%	2%	2%	2%	2%	2%	2%	2%	2%	2%

Source: Chief Investment Office and BofAML Global Research.

Table 3: Strategic and tactical allocations for U.S. clients (Tier 1 liquidity)

Tier 1 (higher liquidity): Up to 15% of the portfolio may be unavailable for 3–5 years.

	Single Asset Class All Fixed Income		Conservative		Moderately Conservative		Moderate		Moderately Aggressive		Aggressive		Single Asset Class All Equity	
	Strategic	Tactical	Strategic	Tactical	Strategic	Tactical	Strategic	Tactical	Strategic	Tactical	Strategic	Tactical	Strategic	Tactical
Equities	0%	0%	19%	22%	35%	40%	50%	57%	66%	71%	80%	82%	98%	98%
U.S. Large Cap Growth	0%	0%	4%	4%	8%	7%	11%	10%	16%	15%	18%	16%	23%	22%
U.S. Large Cap Value	0%	0%	7%	9%	13%	15%	18%	21%	24%	26%	28%	29%	36%	36%
U.S. Small Cap Growth	0%	0%	1%	1%	1%	2%	1%	2%	2%	3%	3%	4%	3%	3%
U.S. Small Cap Value	0%	0%	1%	2%	1%	2%	2%	4%	2%	3%	3%	4%	4%	5%
International Equity	0%	0%	5%	5%	9%	10%	13%	14%	16%	17%	20%	20%	24%	24%
Emerging Markets	0%	0%	1%	1%	3%	4%	5%	6%	6%	7%	8%	9%	8%	8%
Fixed Income	98%	98%	55%	52%	50%	45%	33%	26%	17%	12%	3%	1%	0%	0%
Governments	28%	27%	18%	16%	14%	11%	10%	6%	6%	3%	1%	0%	0%	0%
Mortgages	23%	23%	12%	11%	13%	12%	8%	6%	4%	3%	1%	0%	0%	0%
Corporates	24%	28%	9%	10%	13%	14%	10%	12%	5%	6%	1%	1%	0%	0%
High Yield	7%	5%	4%	3%	4%	3%	3%	1%	1%	0%	0%	0%	0%	0%
Intl Fixed Income	16%	15%	12%	12%	6%	5%	2%	1%	1%	0%	0%	0%	0%	0%
Cash	2%	2%	15%	15%	2%	2%	2%	2%	2%	2%	2%	2%	2%	2%
Alternatives	0%	0%	11%	11%	13%	13%	15%	15%	15%	15%	15%	15%	0%	0%
Hedge Funds	0%	0%	8%	8%	10%	10%	11%	11%	11%	11%	11%	11%	0%	0%
Private Equity	0%	0%	0%	0%	0%	0%	0%	0%	0%	0%	0%	0%	0%	0%
Real Assets	0%	0%	3%	3%	3%	3%	4%	4%	4%	4%	4%	4%	0%	0%

Source: Chief Investment Office and BofAML Global Research.
Real Assets is defined to include commodities and private real estate.

Table 4: Strategic and tactical allocations for U.S. clients (Tier 2 liquidity)

Tier 2 (moderate liquidity): Up to 30% of the portfolio may be unavailable for 3–5 years.

	Single Asset Class All Fixed Income		Conservative		Moderately Conservative		Moderate		Moderately Aggressive		Aggressive		Single Asset Class All Equity	
	Strategic	Tactical	Strategic	Tactical	Strategic	Tactical	Strategic	Tactical	Strategic	Tactical	Strategic	Tactical	Strategic	Tactical
Equities	0%	0%	17%	20%	32%	37%	46%	53%	60%	65%	73%	75%	98%	98%
U.S. Large Cap Growth	0%	0%	4%	4%	7%	6%	10%	9%	14%	13%	16%	14%	23%	22%
U.S. Large Cap Value	0%	0%	6%	8%	12%	14%	16%	19%	21%	23%	26%	27%	36%	36%
U.S. Small Cap Growth	0%	0%	1%	1%	1%	2%	2%	3%	2%	3%	3%	4%	3%	3%
U.S. Small Cap Value	0%	0%	1%	2%	1%	2%	2%	4%	2%	3%	3%	4%	4%	5%
International Equity	0%	0%	4%	4%	8%	9%	12%	13%	15%	16%	18%	18%	24%	24%
Emerging Markets	0%	0%	1%	1%	3%	4%	4%	5%	6%	7%	7%	8%	8%	8%
Fixed Income	98%	98%	55%	52%	51%	46%	35%	28%	19%	14%	3%	1%	0%	0%
Governments	28%	27%	18%	16%	15%	12%	11%	7%	6%	3%	1%	0%	0%	0%
Mortgages	23%	23%	12%	11%	13%	12%	8%	6%	5%	4%	1%	0%	0%	0%
Corporates	24%	28%	9%	10%	12%	13%	11%	13%	5%	6%	1%	1%	0%	0%
High Yield	7%	5%	4%	3%	4%	3%	3%	1%	2%	1%	0%	0%	0%	0%
Intl Fixed Income	16%	15%	12%	12%	7%	6%	2%	1%	1%	0%	0%	0%	0%	0%
Cash	2%	2%	16%	16%	2%	2%	2%	2%	2%	2%	2%	2%	2%	2%
Alternatives	0%	0%	12%	12%	15%	15%	17%	17%	19%	19%	22%	22%	0%	0%
Hedge Funds	0%	0%	6%	6%	8%	8%	9%	9%	9%	9%	11%	11%	0%	0%
Private Equity	0%	0%	2%	2%	3%	3%	4%	4%	6%	6%	7%	7%	0%	0%
Real Assets	0%	0%	4%	4%	4%	4%	4%	4%	4%	4%	4%	4%	0%	0%

Source: Chief Investment Office and BofAML Global Research.
Real Assets is defined to include commodities and private real estate.

Table 5: Strategic and tactical allocations for U.S. clients (Tier 3 liquidity)

Tier 3 (lower liquidity): Up to 45% of the portfolio may be unavailable for 3–5 years.

	Single Asset Class All Fixed Income		Conservative		Moderately Conservative		Moderate		Moderately Aggressive		Aggressive		Single Asset Class All Equity	
	Strategic	Tactical	Strategic	Tactical	Strategic	Tactical	Strategic	Tactical	Strategic	Tactical	Strategic	Tactical	Strategic	Tactical
Equities	0%	0%	17%	20%	32%	37%	46%	53%	60%	65%	73%	75%	98%	98%
U.S. Large Cap Growth	0%	0%	4%	4%	7%	6%	10%	9%	14%	13%	16%	14%	23%	22%
U.S. Large Cap Value	0%	0%	6%	8%	12%	14%	16%	19%	21%	23%	26%	27%	36%	36%
U.S. Small Cap Growth	0%	0%	1%	1%	1%	2%	2%	3%	2%	3%	3%	4%	3%	3%
U.S. Small Cap Value	0%	0%	1%	2%	1%	2%	2%	4%	2%	3%	3%	4%	4%	5%
International Equity	0%	0%	4%	4%	8%	9%	12%	13%	15%	16%	18%	18%	24%	24%
Emerging Markets	0%	0%	1%	1%	3%	4%	4%	5%	6%	7%	7%	8%	8%	8%
Fixed Income	98%	98%	55%	52%	51%	46%	35%	28%	19%	14%	3%	1%	0%	0%
Governments	28%	27%	18%	16%	15%	12%	11%	7%	6%	3%	1%	0%	0%	0%
Mortgages	23%	23%	12%	11%	13%	12%	8%	6%	5%	4%	1%	0%	0%	0%
Corporates	24%	28%	9%	10%	12%	13%	11%	13%	5%	6%	1%	1%	0%	0%
High Yield	7%	5%	4%	3%	4%	3%	3%	1%	2%	1%	0%	0%	0%	0%
Intl Fixed Income	16%	15%	12%	12%	7%	6%	2%	1%	1%	0%	0%	0%	0%	0%
Cash	2%	2%	16%	16%	2%	2%	2%	2%	2%	2%	2%	2%	2%	2%
Alternatives	0%	0%	12%	12%	15%	15%	17%	17%	19%	19%	22%	22%	0%	0%
Hedge Funds	0%	0%	6%	6%	8%	8%	9%	9%	9%	9%	11%	11%	0%	0%
Private Equity	0%	0%	2%	2%	3%	3%	4%	4%	6%	6%	7%	7%	0%	0%
Real Assets	0%	0%	4%	4%	4%	4%	4%	4%	4%	4%	4%	4%	0%	0%

Source: Chief Investment Office and BofAML Global Research.
Real Assets is defined to include commodities and private real estate.

Table 6: Strategic and tactical allocations for Global clients without alternatives (Tier 0 liquidity)

	Single Asset Class All Fixed Income		Conservative		Moderately Conservative		Moderate		Moderately Aggressive		Aggressive		Single Asset Class All Equity	
	Strategic	Tactical	Strategic	Tactical	Strategic	Tactical	Strategic	Tactical	Strategic	Tactical	Strategic	Tactical	Strategic	Tactical
Equities	0%	0%	22%	25%	37%	42%	52%	59%	66%	71%	81%	86%	98%	98%
North America	0%	0%	13%	15%	21%	24%	30%	35%	38%	41%	46%	49%	56%	57%
Europe (ex UK)	0%	0%	3%	3%	5%	5%	7%	7%	9%	9%	11%	11%	13%	13%
UK	0%	0%	2%	2%	4%	3%	5%	4%	6%	5%	8%	7%	8%	7%
Japan	0%	0%	1%	2%	1%	2%	2%	3%	3%	4%	3%	4%	8%	8%
Asia Pacific (ex Japan)	0%	0%	1%	1%	2%	3%	3%	4%	4%	5%	5%	6%	5%	5%
Emerging Markets	0%	0%	2%	2%	4%	5%	5%	6%	6%	7%	8%	9%	8%	8%
Fixed Income	98%	98%	54%	51%	61%	56%	46%	39%	32%	27%	17%	12%	0%	0%
Global Governments	55%	53%	30%	28%	33%	29%	23%	18%	15%	12%	8%	5%	0%	0%
Global Corporate	18%	21%	8%	9%	10%	11%	9%	11%	7%	8%	4%	5%	0%	0%
Global Mortgages	18%	18%	12%	11%	13%	12%	10%	8%	7%	5%	4%	2%	0%	0%
Global HY, EM debt	7%	6%	4%	3%	5%	4%	4%	2%	3%	2%	1%	0%	0%	0%
Cash	2%	2%	24%	24%	2%	2%	2%	2%	2%	2%	2%	2%	2%	2%

Source: Chief Investment Office and BofAML Global Research.

Table 7: Strategic and tactical allocations for Global clients with alternatives (Tier 1 liquidity)

Tier 1 (higher liquidity): Up to 15% of the portfolio may be unavailable for 3–5 years.

	Single Asset Class All Fixed Income		Conservative		Moderately Conservative		Moderate		Moderately Aggressive		Aggressive		Single Asset Class All Equity	
	Strategic	Tactical	Strategic	Tactical	Strategic	Tactical	Strategic	Tactical	Strategic	Tactical	Strategic	Tactical	Strategic	Tactical
Equities	0%	0%	19%	22%	34%	39%	48%	55%	63%	68%	77%	81%	98%	98%
North America	0%	0%	10%	12%	19%	22%	27%	32%	36%	39%	44%	46%	56%	57%
Europe (ex UK)	0%	0%	3%	3%	5%	5%	6%	6%	9%	9%	11%	11%	13%	13%
UK	0%	0%	2%	2%	3%	2%	5%	4%	6%	5%	7%	6%	8%	7%
Japan	0%	0%	1%	2%	2%	3%	2%	3%	2%	3%	3%	4%	8%	8%
Asia Pacific (ex Japan)	0%	0%	1%	1%	2%	3%	3%	4%	4%	5%	5%	6%	5%	5%
Emerging Markets	0%	0%	2%	2%	3%	4%	5%	6%	6%	7%	7%	8%	8%	8%
Fixed Income	98%	98%	53%	50%	49%	44%	35%	28%	20%	15%	7%	3%	0%	0%
Global Governments	55%	53%	30%	28%	26%	22%	17%	12%	9%	6%	3%	0%	0%	0%
Global Corporate	18%	21%	8%	9%	8%	9%	7%	9%	5%	6%	2%	3%	0%	0%
Global Mortgages	18%	18%	12%	11%	11%	10%	8%	6%	4%	2%	1%	0%	0%	0%
Global HY, EM debt	7%	6%	3%	2%	4%	3%	3%	1%	2%	1%	1%	0%	0%	0%
Cash	2%	2%	13%	13%	2%	2%	2%	2%	2%	2%	2%	2%	2%	2%
Alternatives	0%	0%	15%	15%	15%	15%	15%	15%	15%	15%	14%	14%	0%	0%
Hedge Funds	0%	0%	11%	11%	11%	11%	11%	11%	11%	11%	10%	10%	0%	0%
Private Equity	0%	0%	0%	0%	0%	0%	0%	0%	0%	0%	0%	0%	0%	0%
Real Assets	0%	0%	4%	4%	4%	4%	4%	4%	4%	4%	4%	4%	0%	0%

Source: Chief Investment Office and BofAML Global Research.
Real Assets is defined to include commodities and private real estate.

Table 8: Strategic and tactical allocations for Global clients with alternatives (Tier 2 liquidity)

Tier 2 (higher liquidity): Up to 30% of the portfolio may be unavailable for 3–5 years.

	Single Asset Class All Fixed Income		Conservative		Moderately Conservative		Moderate		Moderately Aggressive		Aggressive		Single Asset Class All Equity	
	Strategic	Tactical	Strategic	Tactical	Strategic	Tactical	Strategic	Tactical	Strategic	Tactical	Strategic	Tactical	Strategic	Tactical
Equities	0%	0%	17%	20%	30%	35%	43%	50%	56%	61%	68%	70%	98%	98%
North America	0%	0%	9%	11%	17%	20%	24%	29%	33%	36%	38%	39%	56%	57%
Europe (ex UK)	0%	0%	2%	2%	4%	4%	6%	6%	8%	8%	9%	9%	13%	13%
UK	0%	0%	2%	2%	3%	2%	4%	3%	5%	4%	7%	5%	8%	7%
Japan	0%	0%	1%	2%	1%	2%	2%	3%	2%	3%	3%	4%	8%	8%
Asia Pacific (ex Japan)	0%	0%	1%	1%	2%	3%	3%	4%	3%	4%	4%	5%	5%	5%
Emerging Markets	0%	0%	2%	2%	3%	4%	4%	5%	5%	6%	7%	8%	8%	8%
Fixed Income	98%	98%	53%	50%	48%	43%	32%	25%	17%	12%	3%	1%	0%	0%
Global Governments	55%	53%	30%	28%	25%	21%	17%	12%	8%	5%	1%	0%	0%	0%
Global Corporate	18%	21%	8%	9%	8%	9%	6%	8%	4%	5%	1%	1%	0%	0%
Global Mortgages	18%	18%	12%	11%	11%	10%	7%	5%	4%	2%	1%	0%	0%	0%
Global HY, EM debt	7%	6%	3%	2%	4%	3%	2%	0%	1%	0%	0%	0%	0%	0%
Cash	2%	2%	14%	14%	2%	2%	2%	2%	2%	2%	2%	2%	2%	2%
Alternatives	0%	0%	16%	16%	20%	20%	23%	23%	25%	25%	27%	27%	0%	0%
Hedge Funds	0%	0%	8%	8%	10%	10%	11%	11%	12%	12%	14%	14%	0%	0%
Private Equity	0%	0%	3%	3%	4%	4%	6%	6%	7%	7%	8%	8%	0%	0%
Real Assets	0%	0%	5%	5%	6%	6%	6%	6%	6%	6%	5%	5%	0%	0%

Source: Chief Investment Office and BofAML Global Research.
Real Assets is defined to include commodities and private real estate.

Table 9: Strategic and tactical allocations for Global clients with alternatives (Tier 3 liquidity)

Tier 3 (higher liquidity): Up to 45% of the portfolio may be unavailable for 3–5 years.

	Single Asset Class All Fixed Income		Conservative		Moderately Conservative		Moderate		Moderately Aggressive		Aggressive		Single Asset Class All Equity	
	Strategic	Tactical	Strategic	Tactical	Strategic	Tactical	Strategic	Tactical	Strategic	Tactical	Strategic	Tactical	Strategic	Tactical
Equities	0%	0%	17%	20%	30%	35%	43%	50%	56%	61%	68%	70%	98%	98%
North America	0%	0%	9%	11%	17%	20%	24%	29%	33%	36%	38%	39%	56%	57%
Europe (ex UK)	0%	0%	2%	2%	4%	4%	6%	6%	8%	8%	9%	9%	13%	13%
UK	0%	0%	2%	2%	3%	2%	4%	3%	5%	4%	7%	5%	8%	7%
Japan	0%	0%	1%	2%	1%	2%	2%	3%	2%	3%	3%	4%	8%	8%
Asia Pacific (ex Japan)	0%	0%	1%	1%	2%	3%	3%	4%	3%	4%	4%	5%	5%	5%
Emerging Markets	0%	0%	2%	2%	3%	4%	4%	5%	5%	6%	7%	8%	8%	8%
Fixed Income	98%	98%	53%	50%	48%	43%	32%	25%	17%	12%	3%	1%	0%	0%
Global Governments	55%	53%	30%	28%	25%	21%	17%	12%	8%	5%	1%	0%	0%	0%
Global Corporate	18%	21%	8%	9%	8%	9%	6%	8%	4%	5%	1%	1%	0%	0%
Global Mortgages	18%	18%	12%	11%	11%	10%	7%	5%	4%	2%	1%	0%	0%	0%
Global HY, EM debt	7%	6%	3%	2%	4%	3%	2%	0%	1%	0%	0%	0%	0%	0%
Cash	2%	2%	14%	14%	2%	2%	2%	2%	2%	2%	2%	2%	2%	2%
Alternatives	0%	0%	16%	16%	20%	20%	23%	23%	25%	25%	27%	27%	0%	0%
Hedge Funds	0%	0%	8%	8%	10%	10%	11%	11%	12%	12%	14%	14%	0%	0%
Private Equity	0%	0%	3%	3%	4%	4%	6%	6%	7%	7%	8%	8%	0%	0%
Real Assets	0%	0%	5%	5%	6%	6%	6%	6%	6%	6%	5%	5%	0%	0%

Source: Chief Investment Office and BofAML Global Research.
Real Assets is defined to include commodities and private real estate.

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 MBS and continued volatility should continue to weigh on market. Cap rates in CMBS have become less appealing. Select opportunities exist in properly structured CMBS and ABS.
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.

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Asset allocation and diversification do not assure a profit or protect against a loss during declining markets.

Alternative investments, such as hedge funds and private equity funds, are speculative and involve a high degree of risk. There generally are no readily available secondary markets, none are expected to develop and there may be restrictions on transferring fund investments. Alternative investments may engage in leverage that can increase risk of loss, performance may be volatile and funds may have high fees and expenses that reduce returns. Alternative investments are not suitable for all investors. Investors may lose all or a portion of the capital invested.

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.

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