Independence | Asset Advisors

2018 GLOBAL MARKETS OUTLOOK & 2017 REVIEW

DECEMBER 31, 2017

DISCLAIMER

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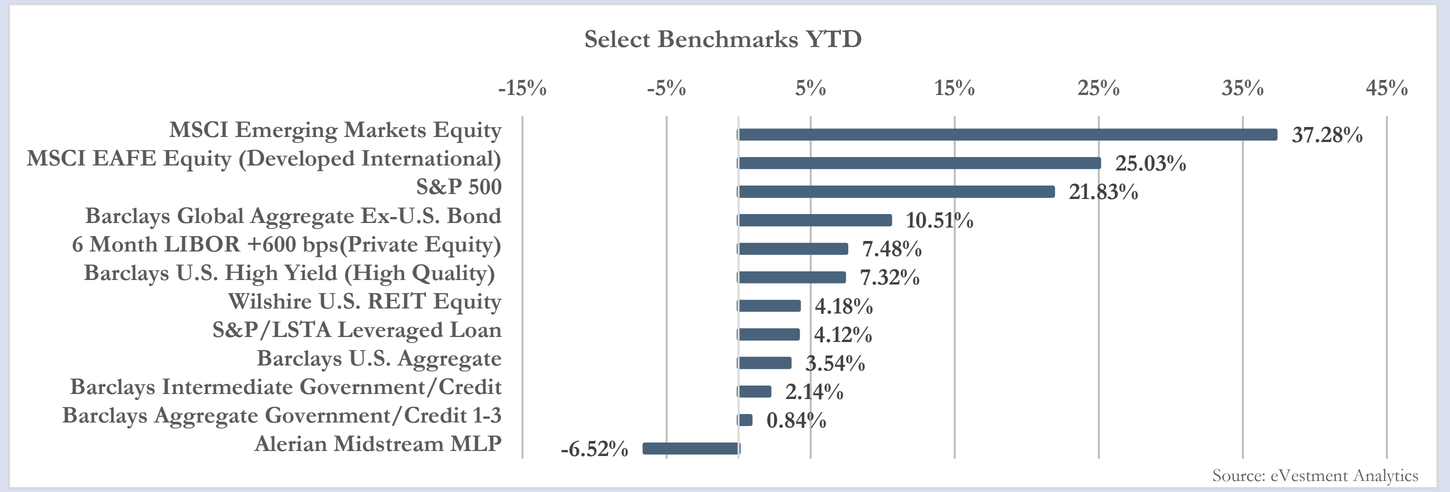
I. GLOBAL MARKETS REVIEW – 2017 FULL YEAR

SELECT BENCHMARKS – YEAR TO DATE AT DECEMBER 31, 2017



2017: A Remarkable Year

Global equity and fixed income markets performed well in the fourth quarter, capping off a strong year for most major global indices. U.S. equities performed exceptionally well, gaining 6.6% during the fourth quarter and 21.8% for the year. The double-digit annual return was not record setting; however, the combination of consistency and low volatility made 2017 a particularly remarkable year. Specifically, this was the first time since 1958 that the S&P 500 delivered positive returns in every month of a calendar year. The Energy sector and Energy Infrastructure MLPs posted negative returns for the year but rose 4.7% in December and into the new year as oil and gas prices strengthened.

Emerging markets and international developed (ex-U.S.) equities gained 7.4% and 4.2% in the fourth quarter, respectively. Both asset classes performed exceptionally well on a full year basis, as they outperformed U.S. equities by 15.5% and 3.2%, respectively. These impressive returns were the result of a bullish macroeconomic backdrop, supported by better earnings growth amid improved bottom-up credit, leverage and fiscal conditions.

Global bond markets gained overall in the fourth quarter and for the year. Domestically, corporate high yield and investment grade municipal bonds provided the strongest returns. Floating rate loans gained 4.1% over the year and ended 2017 yielding more than 5%. Emerging markets debt returned nearly 13% in 2017, with currency appreciation providing the majority of the total return.

2017 was one of the least volatile years in three decades. The CBOE Volatility Index (VIX), a popular measure of market volatility, set a new record low. It is interesting to note that while market volatility remained close to the historic low, political volatility simultaneously increased.

President Trump marked his first full year in office. Since his inauguration, global markets have experienced a period of synchronized expansion. While his administration's proposed and subsequently passed tax cuts had an undeniably positive affect on U.S. equities, political turmoil and trade policy proposals have been viewed as risky. Catalysts supporting global growth such as above-trend earnings growth, upwardly revised GDP results, lower unemployment, a robust housing market (U.S.), accommodative global trade, and accelerating infrastructure growth (outside the U.S.) have been driven by nine years of stimulative global monetary policy combined with modest fiscal policy actions (most notably in Japan and Asia). We give Republican leadership well deserved credit for reducing U.S. corporate taxes, which should provide a catalyst for near-term U.S. economic and earnings growth.

II. GLOBAL MARKETS OUTLOOK – 2018 FULL YEAR

2018: A Favorable Outlook
The U.S. economy is entering 2018 well positioned for additional growth. GDP growth has modestly accelerated to the 2.3% to 2.6% range (a sustainable rate), the labor market has improved, commodity prices are recovering, the housing sector is stable, consumer and business confidence have reached historically high levels, and the Leading Economic Indicator (LEI) increased again, signaling continued growth. Tax cuts and loosened regulation are favorable tailwinds. Tax cuts are projected to add $8 to $10 to S&P 500 per-share earnings in 2018. Globally, broad-based fundamental improvements and signs of synchronized growth are taking place for the first time since the financial crisis. The International Monetary Fund (IMF) revised upward its estimate for global economic growth to 3.5% in 2017 and 3.7% in 2018. The subdued global inflation trend is expected to tick slightly higher, which would be viewed favorably. With such a favorable consensus forecast, the single most significant risk may be an unexpected acceleration in inflation, leading to significant monetary policy tightening.

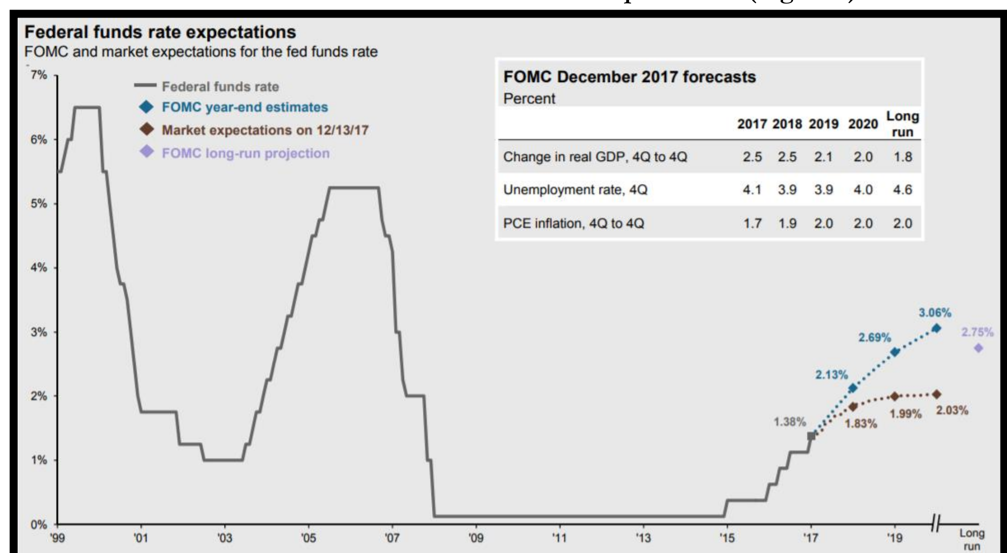
The macroeconomic backdrop, both fundamental and technical, is generally favorable across global fixed income markets as we begin the new year. Generally speaking, corporate fundamentals are strong and improving, technical conditions in the form of supply and demand are supportive, and central banks remain accommodative (ex-U.S.). However, valuations are unfavorable across the fixed income universe. In 2018 we expect fixed income to provide steady income to investors amid falling bond prices and increasingly higher yields. The returns will likely be driven by yield rather than any price appreciation, but positive overall absent a spike in inflation.

While our outlook for 2018 is favorable overall, there are significant headwinds that we expect will carry over from 2017. Heightened geopolitical tensions, currently with North Korea, are likely to continue, and natural disasters may remain a seasonal challenge to markets. Fortunately, events such as hurricanes, while devastating to local economies, often result in only short-lived market volatility. Any contagion effect of cryptocurrency volatility has thus far been muted, but bitcoin and other blockchain currency crashes could temporarily upset markets.

As the rest of the world prepares to begin interest rate "normalization" initiatives in 2018, the U.S. Federal Reserve (Fed) is already well on its way, having been the initiator in both interest rate hikes and balance sheet reduction.

The market assumes the Fed will remain relatively aggressive in 2018, as the market has already priced in three 0.25% rate hikes in 2018 (Figure 1). The Fed's balance sheet reduction program, which launched in 2017, will gain increasing traction over the course of 2018 as reinvestment is set to decline over time. Consensus suggests the balance sheet will have contracted by $400bn by the end of 2018.

U.S. Federal Reserve: Actions & Expectations (Figure 1)



	2017	2018	2019	2020	Long run
Change in real GDP, 4Q to 4Q	2.5	2.5	2.1	2.0	1.8
Unemployment rate, 4Q	4.1	3.9	3.9	4.0	4.6
PCE inflation, 4Q to 4Q	1.7	1.9	2.0	2.0	2.0

Source: JP Morgan Guide to the Markets

III. GLOBAL ASSET CLASS OUTLOOK – 2018 FULL YEAR

Asset Class	View	Tailwinds	Headwinds
U.S. Equity	----------X------	Sustainable GDP growth; tax cut & deregulation; $U.S. weakness	Trade & immigration policy risk; expensive
	U.S. equity markets are well positioned to continue their positive growth trend; no recession forecast in 2018; less room for growth due to high P/E multiples; mid to high single digit returns expected.		
Europe ex.-UK Equity	-------------X---	Economic recovery & earnings acceleration	Euro appreciation; qualitative easing expiration
	Valuations are attractive relative to U.S. equities; higher relative returns expected in 2018 amid further strengthening fundamentals, continued U.S. dollar weakness and higher corporate earnings.		
EM Equity	------------X----	Sustainable earnings; improved fiscal conditions, local consumption	Global trade critical; Chinese growth deceleration
	Emerging markets equity rally is expected to continue; fundamentals are forecasted to remain strong and the outlook is compelling; impractical to assume a repeat of 2017's stellar returns.		
REIT Equity	-------X---------	Strong fundamentals; occupancy & rent growth	Rising rates; sector supply/demand imbalances
	U.S. REIT prices are expected to begin 2018 as fairly discounted; returns are expected to bounce back after lagging in 2017; the high relative 4.1% yield is expected to increase slightly.		
Midstream MLP	-----------X-----	Improving fundamentals; institutional flows, low valuations	Oil price volatility; negative sentiment; retail flows
	Highest potential upside of any global equity asset class; macroeconomic backdrop remains favorable; proposed deregulation (plus recently passed tax bill) should be supportive; 6+% yield.		
U.S. Treasuries	--X--------------	Safe-haven; demand for duration	Rising inflation; reduced foreign demand; weaker dollar => inflation
	Expect further flattening of the yield curve as the Fed prepares to raise short-term rates three times in 2018; yields are expected to move higher amid falling prices; low total return.		
IG U.S. Bonds	-----X-----------	Low default rates; low volatility	Narrow credit spreads; increased duration risk
	Municipal bonds offer a better after-tax yield compared to tax-equivalent bonds; total returns are expected to be lower in 2018, but positive; corporate bonds are attractive; municipals are expensive.		
HY U.S. Bonds	--------X--------	Low default risk; search for higher yield; lower tax rate	Bonds trading at a premium to par; price risk
	Expect high yield bonds to benefit for the synchronized global expansion; foreign demand should remain high in 2018; total return will come from yield not gain; no signs of increased credit risk.		
Floating Rate Bonds	-----------X-----	Trading at discount to par; "no" rate risk, Fed rate increases	Volatility ties to high yield market
	The loan market should benefit for proposed Fed tightening; default rate is expected to remain low; coupon-clipping environment in 2018; total return forecast of 4.5-5.0%.		
Global ex.-U.S. Bonds	----------X------	Healthy global economy; currency appreciation vs. weakening $U.S.	Uncertain rate environment; flight to quality currency risk
	Emerging markets debt expected to do well in 2018; developed world growth should lead to greater commodity/goods demand; EM currencies and debt spreads should react positively.		

Quarter-over-Quarter Color Guide: Green = Positive / Black = Neutral (no change) / Red = Negative

IV. 2017 FIXED INCOME MARKETS

SELECT BENCHMARKS – GLOBAL FIXED INCOME MARKETS – **UPDATED DECEMBER 31, 2017**

	4Q17	YTD	1-Year	3-Years	5-Yers	10-Years
US Aggregate Bond	0.39	3.54	3.54	2.24	2.10	4.01
US Municipal Bond	0.75	5.45	5.45	2.98	3.02	4.46
US Corporate High Yield	0.47	7.50	7.50	6.35	5.78	8.03
US High Quality High Yield	0.39	7.32	7.32	6.21	5.81	8.40
S&P/LSTA Leveraged Loans	1.11	4.12	4.12	4.44	4.03	4.85
Global Agg. Ex-U.S.	1.63	10.51	10.51	1.77	-0.20	2.40

Source: eVestment Analytics

U.S. INVESTMENT GRADE TAXABLE BONDS [2017 + 3.54%]

REVIEW: The Barclays U.S. Aggregate Bond Index gained 3.5%, a solid result but unfavorable when compared to the rest of the global fixed income universe. During the fourth quarter, the yield curve compressed to its flattest level since before the financial crisis, and corporate credit spreads diverged between investment grade and high yield (investment grade tightened & high yield widened). The result was muted returns for shorter-duration indexes, whereas longer-duration indexes outperformed. Volatility during the year spiked at times, but on the whole remained subdued.

At year-end the Barclays U.S. Aggregate Index was priced at $103, offering a yield to worst of 2.7% with a six-year duration. U.S. corporate bonds were the highest returning component of the aggregate, gaining 6.4% and yielding 3.3%. U.S. asset backed bonds were the laggard, returning only 1.6% while offering a meager yield of 2.3%.

OUTLOOK: U.S. investment grade bonds received less attention than normal during the year as investor attention remained drawn to the exceptional global equity return environment. Despite predictions about rising rates and the end of the bond bull market, the U.S. investment grade market experienced another solid year. Looking ahead into 2018, we expect returns to remain positive, but subdued, with return coming from yield. Corporate credit appears to offer the best value (yield earned for price paid), is poised for a higher total return as credit metrics improve, and investors expect the positive impact of tax cuts from higher earnings.

U.S. MUNICIPAL BONDS [2017 + 5.45%]

REVIEW: The Barclays Municipal Bond Index gained 5.5%, a welcomed result considering the general uncertainty surrounding tax and healthcare policy reforms. As was the case with the U.S. Treasury curve, the municipal bond curve also flattened during the year, the direct result of lower 30-year municipal bond yields that fell 46 bps to 2.62%.

OUTLOOK: Looking ahead to 2018, the outlook for municipal bonds is favorable from a tax-equivalent yield perspective. Ultimately, the final version of the “Tax Cuts and Jobs Act” left the existing tax laws unchanged; however, the inundation of new issue surplus in December will likely result in depressed supply in early 2018.

Municipal bonds continued to offer an after-tax advantage to investors, with a 2.4% year-end yield-to-worst requiring an equivalent 3.9% taxable yield to break-even. The opportunities to source this yield from investment grade taxable bonds are scarce, with the Barclays U.S. Aggregate Index yielding just 2.7% at year-end. However, with a price of $109 at year-end, the asset class is far from cheap.

HIGH YIELD [2017 + 7.50%]

REVIEW: High yield bonds posted a total return of 7.5%. Leverage did creep up over the course of the year; however, corporate debt service coverage ratios remained solid with improvement in both revenue and EBITDA metrics during the year. Lending standards remain "easy" with prospective financing options for levered issuers.

In terms of valuation, high yield bonds ended the year in a very different place compared to 2016. As of December 31, 2017, the high yield market had an average price of $101, and an average yield to worst of 5.8%. This is drastically different compared to February 2016, when high yield bonds yielded 10% following the sell-off of risk assets, the result of a broad collapse in commodity prices. High yield bonds experienced heightened levels of volatility in 2016, whereas 2017 saw near historically low levels of price movement.

OUTLOOK: Fundamentally, the asset class is well positioned heading into 2018. The year-end default rate of 1.3% was well below the 30-year average of 3.8%, and analyst consensus suggests the rate will tick only slightly higher in 2018 (estimates of 2%). U.S. high yield bonds provided a more "normal" return to investors with mid-single digit return comprised predominantly of interest return (yield). Looking ahead, we expect high yield bonds to benefit from continued synchronized global growth. Valuations are not particularly attractive, but the strong fundamental and technical backdrops continue to be supportive. Our prediction is that the asset class will generate a slow and steady upward return that will closely mirror the yield of its underlying high yield bonds.

FLOATING RATE [2017 + 4.12%]

REVIEW: Floating rate loans gained 4.1%. There was minimal price appreciation potential heading into 2017, yet the Index generated a total return that was within 1% of its 5.2% eight-year average return since the credit crisis.

OUTLOOK: As is the case for high yield bonds, the fundamental backdrop for bank loans is supportive heading into 2018. The U.S. economy is expected to improve and we expect new loan issuers to subsequently increase revenues, earnings and cash flows. The loan market default rate ended the year at 2.1%, well below the long-term historical average. Analyst consensus suggests little change in default rates, as low single-digit growth in the U.S. should be supportive to credit risk assets. Note that most leveraged loans are secured and loss ratios are a fraction of default rates.

Investors anticipate three U.S. Fed rate hikes in 2018, and the resetting floating rate component of the loan market makes the asset class particularly appealing to yield seeking investors. Loan prices start 2018 in the mid $98s, but roughly 70% of the market continues to be priced at par or higher. We agree with the analysts at Eaton Vance, whose base case forecast calls for a coupon-clipping environment going forward. Given minimal price appreciation potential in 2018, their total return forecast is 4.5% based on our rising rate assumptions.

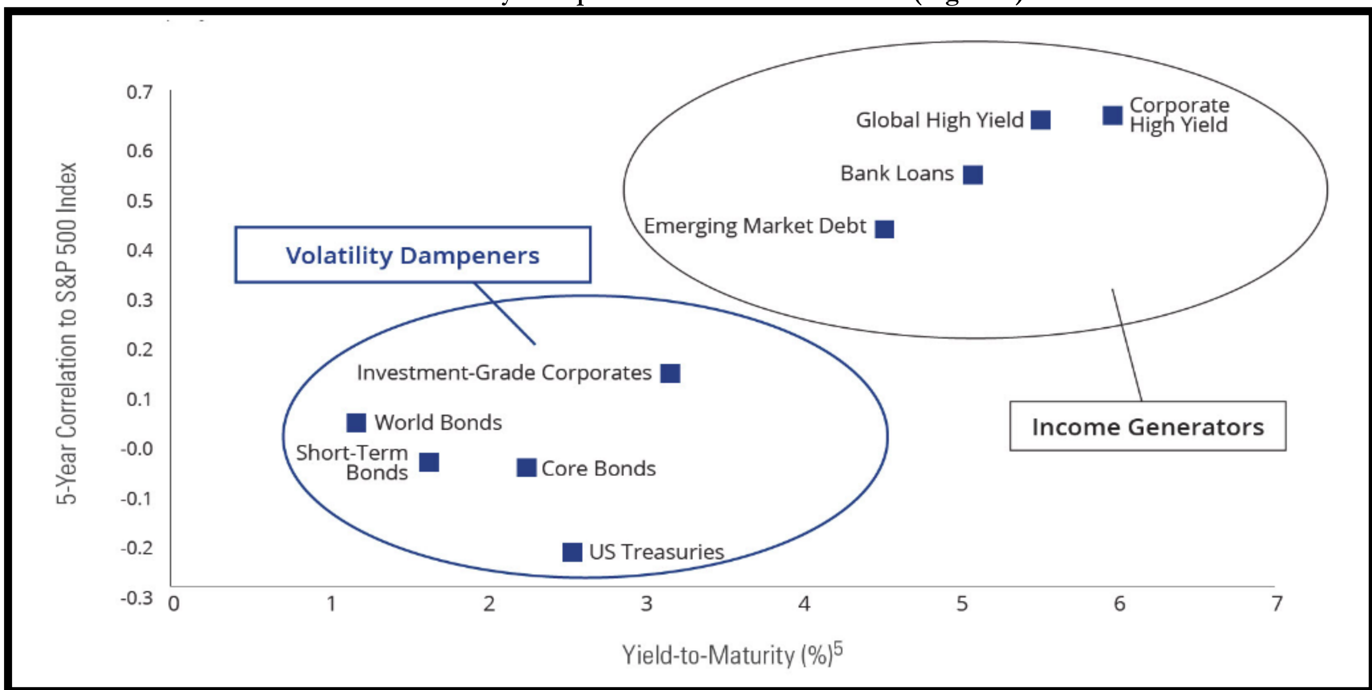
EMERGING MARKETS DEBT [2017 + 12.99%]

REVIEW: Emerging markets debt returned nearly 13%, as emerging markets currencies appreciated 5.8% against the U.S. dollar. The double-digit return came as a surprise to most investors, as they were against a backdrop of a U.S. monetary tightening cycle, accompanied by higher short-term yields, which is viewed as a negative for the asset class. Despite these headwinds, EM debt outperformed nearly all fixed income asset classes in 2017.

OUTLOOK: Looking ahead, it is likely we will see a continuation of the synchronized global growth trend that gained momentum in 2017. Specifically, consensus suggests the U.S. and European economies will grow in the mid-2% range, which is likely to positively affect emerging markets economies. It is probable that growth in the developed markets will lead to greater commodity/goods demand that has historically supported the exports of emerging markets countries. As a result, it is likely that emerging market currencies and debt spreads will react positively to the development.

We expect fixed income will serve as a positive contributor to portfolio return in 2018. We agree with the market

Volatility Dampeners vs Income Generators (Figure 4)



Source: Hartfordfunds, BarclaysLive, Morningstar

that the Fed will continue its normalization initiative. We also agree with consensus that bond prices will generally decline, and yields will correspondingly rise. The primary source of total return will be yield. It will be important for investors to remain well diversified and consider adding to less traditional fixed income markets including emerging markets debt. We favor fully allocating to fixed income sectors that respond atypically to rising interest rates, such as high yield and floating rate loans. However, adding to fixed income sectors with higher correlations to equities could result in additional volatility (Figure 4).

IV. 2017 U.S. EQUITY MARKET

SELECT BENCHMARKS – U.S. EQUITY MARKETS – **UPDATED DECEMBER 31, 2017**

	4Q17	YTD	1-Year	3-Years	5-Yers	10-Years
S&P 500	6.64	21.83	21.83	11.41	15.79	8.50
S&P Mid Cap 400	6.25	16.24	16.24	11.14	15.01	9.97
S&P Small Cap 600	3.96	13.23	13.23	12.00	15.99	10.43
Russell 1000 Value	5.33	13.66	13.66	8.65	14.04	7.10
Russell 1000 Growth	7.86	30.21	30.21	13.79	17.33	10.00
Alerian MLP	-0.95	-6.52	-6.52	-9.33	-0.06	6.05

U.S. LARGE CAP EQUITY [2017 + 21.83%]

REVIEW: 2017 turned out to be a very good year for U.S. equity investors. The S&P 500 gained 6.6% in the fourth quarter, resulting in a solid 21.8% return for the year. It was the first time the Index ended every single month of a calendar year with a gain (14-months of gains, a new record). U.S. equities rallied during the quarter on the advancement of the long-awaited tax reform bill. Markets reacted favorably to the announcement that permanent tax cuts for corporations would be the centerpiece of the package. U.S. equities were also supported by generally positive macroeconomic data, including better-than-expected third quarter GDP growth of 3.0% (annualized) and strong momentum going into year end.

"Growth" equity greatly outperformed "value" equity in 2018, as cyclical sectors such as Information Technology, Materials and Consumer Discretionary provided the majority of the Index's return. As measured by the S&P 500 Index, growth stocks gained 27.4% in 2017 while value earned less than 16%. This represents the largest variance between the U.S. large cap subsectors since 2000. This trend reversed in December, however, with value gaining 1.5% to growth's 0.8% gain. There are several warning signs that risk has concentrated in large-cap tech stocks. Five FAANG (Facebook, Apple, Amazon, Netflix, Google) stocks now represent 14% of S&P 500 market cap. The Tech sector represents a full 40% of the NASDQ for the first time since the 1999 Tech bubble.

OUTLOOK: It is possible the gap between growth and value will begin to narrow in 2018 as the FAANG stocks may struggle to maintain their dominance. We anticipate a rotation back to high quality value stocks, as markets tend to regress to mean valuations, although the timing and magnitude of that rotation are impossible to forecast.

ENERGY INFRASTRUCTURE AND MASTER LIMITED PARTNERSHIPS [2017 -6.52%]

REVIEW: The Alerian MLP Index declined 6.5% in 2017, a blemish on what was otherwise a terrific year for global equity markets. 2017 was a weak year for energy MLPs overall, a result of lethargic investor sentiment stemming from a momentum shift away from energy and value companies into large cap growth. Uncertainty regarding the possible impact of the U.S. tax act clouded a positive forecast for revenue and cash flow on improved balance sheets. At the retail level, capital flowed out of MLPs, while at the institutional level, inflows accelerated.

OUTLOOK: We believe energy infrastructure stocks and MLPs remain a mispriced asset class. A full allocation to MLPs offers investors a best-in-class yield (Figure 5) combined with sustainable long-term revenue and earnings growth prospects. Furthermore, the macroeconomic backdrop for MLPs is favorable, and proposed deregulation, cost-of-capital advantages (maintained in recently passed tax act) support accelerated growth for the next five or more years.

U.S. EQUITY OUTLOOK

Since 1963, the S&P 500 Index has returned more than 15% during a calendar year 19 times. However, over the last 50 years, the Index has gained an average of 7.5%. Uniquely, tax cuts add $8 per share to 2018 forecasted S&P 500 earnings. That represents an additional 6% increase in 2018 earnings from tax savings.

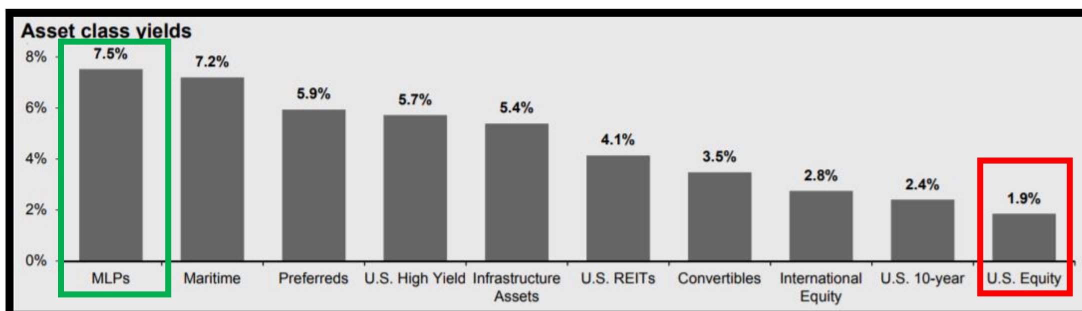
As we look ahead to 2018, we believe U.S. equity markets are well positioned to continue their positive growth trend. Employment data remains favorable, the housing market appears stable, growth forecasts are manageable, and the U.S. Federal Reserve's tightening actions are a sign of its confidence in continued economic progress. Furthermore, proposed lower corporate tax rates are expected to bolster corporate earnings growth. Our belief is that even a moderate pace of underlying growth, though perhaps less than the rate in 2017, along with a slight acceleration in the pace of inflation, could lead to stronger than expected revenue growth.

While our outlook for U.S. stock markets is favorable and we do not forecast a recession in the next 18 months, we do see potential headwinds. Perhaps the greatest is simply current valuations, which provide less room for higher growth as P/E multiples have risen and dividend yields have fallen (Figure 5). Headline risk will likely continue to play a greater role in the year ahead, and U.S. equity markets could experience increased outflows as investors transition capital to foreign equity markets in search of higher total returns. The more valuations stretch, the more vulnerable equities are to a market correction.

Given a backdrop of moderate economic growth, decent earnings growth, minimal inflation, and gradually rising interest rates, U.S. equities should be capable of generating mid to high single-digit returns in 2018. Our base case expectation is that U.S. equities will provide an average nominal return of 6% in the next 5 to 7 years. Returns will be generally comprised of 2% dividend yield and 6% earnings growth less -2% for P/E reversion to mean valuations of 15.6x earnings.

Current Asset Class Yields (Figure 5)

The best value across global equity markets remains Energy Infrastructure Master Limited Partnerships.



Source: JP Morgan Guide to the Markets

V. 2017 FOREIGN EQUITY MARKETS

SELECT BENCHMARKS – NON-U.S. EQUITY MARKETS – **UPDATED DECEMBER 31, 2017**

	4Q17	YTD	1-Year	3-Years	5-Yers	10-Years
MSCI ACWI	5.73	23.97	23.97	9.30	10.80	4.65
MSCI ACWI ex-U.S.	5.00	27.19	27.19	7.83	6.80	1.84
MSCI EAFE	4.23	25.03	25.03	7.80	7.90	1.94
MSCI EAFE Small Cap	6.05	33.01	33.01	14.20	12.85	5.77
MSCI Emerging Markets	7.44	37.28	37.28	9.10	4.35	1.68
MSCI EM Small Cap	9.23	33.84	33.84	8.44	5.41	2.78

INTERNATIONAL DEVELOPED EQUITY [2017 +25.03%]

REVIEW: Global equity markets gained 25% in 2017 in what has been characterized as a period of synchronized global growth. Beginning in mid-December 2016, the global economy collectively expanded with all major regions participating in the recovery. In fact, 96% of major global economies ended the year with a PMI[1] figure above 50 as a sign of economic acceleration.

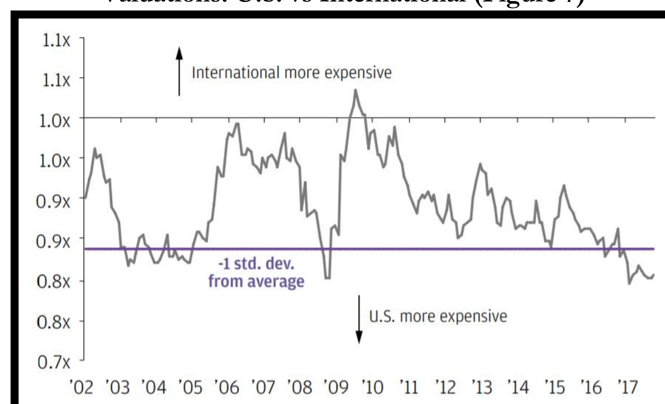
After having underperformed the U.S. for a number of years, international developed equities outperformed in 2017. Persistent fears about European elections and Brexit dissipated and were replaced by investor confidence as corporate earnings continued to strengthen (Figure 6) and the U.S. dollar weakened. Investor confidence was further reinforced by signs of rising inflation, which combined with improving economic growth, may give the European Central Bank (ECB) reason to begin tapering its supportive quantitative easing program.

OUTLOOK: Valuations of international developed equities are relatively attractive and remain below those of U.S. stocks (Figure 7). As the chart shows, non-U.S. developed equities are attractively priced, and we expect this trend to continue in 2018 amid further strengthening fundamentals, continued U.S. dollar weakness, and sustainably higher corporate earnings growth rates.

EPS Growth: U.S. vs International (Figure 6)

Source: JP Morgan, Compustat, FactSet

Valuations: U.S. vs International (Figure 7)



Source: JP Morgan, FactSet, MSCI, S&P

[1]PMI stands for the "Purchasing Managers' Index," which serves an indicator of the economic health of the manufacturing sector. A PMI reading over 50 represents expansion, while a reading under 50 signals contraction.

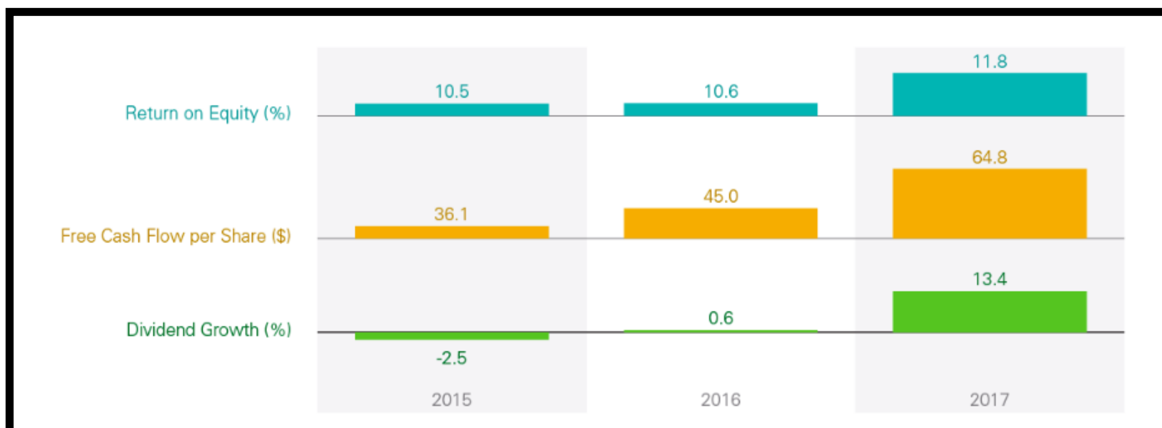
EMERGING MARKETS EQUITY [2017 +37.28%]

REVIEW: Emerging markets equities were undoubtedly the best performing traditional global investment in 2017. During the year, the asset class gained more than 37% (U.S. dollar terms), outperforming both U.S. and developed ex-U.S. equities by 15.5% and 12.3%, respectively. The emerging markets equity rally was supported by strong fundamentals, robust corporate earnings results and positive retail fund flows. Emerging markets equities ended the year with the strongest fundamentals in more than a decade (Figure 8).

Emerging markets equities finished 2017 valued at 12.5x forward 12-month earnings, slightly higher than one standard deviation above their 15-year average. Analyst consensus suggests this earnings multiple is fundamentally supported by earnings growth. Based solely on this criteria, the emerging markets equity asset class opportunity continues to look compelling relative to developed markets, which traded at 17.0x earnings at the end of the year. Emerging markets companies ended the year valued at a 25% discount to developed markets.

OUTLOOK: Heading into 2018, we expect that the emerging markets rally will continue. Fundamentals are strong and the earnings outlook is compelling. However, it is impractical to assume that the asset class has enough underlying support or momentum to replicate the stellar returns from 2017. One reason for our skepticism is that like in the U.S., more than 60% of the MSCI Emerging Market Index's return was driven by only a few sectors in 2017, Information Technology and Financials. Furthermore, while valuations are compelling compared to more expensive developed indexes, they are significantly fuller than they were a year ago.

Emerging Markets Equity Fundamentals (Figure 8)



Source: MSCI

FINAL THOUGHTS…

We conclude our 2017 Fourth Quarter Market Review and 2018 Outlook thankful for the tremendous returns recorded in the year just passed, and cautiously optimistic for additional growth in the year ahead. We believe fixed income will serve as a steady source of income. We see the best opportunities in emerging markets debt, as well as asset classes that perform atypically during tightening cycles, including high yield bonds and floating rate loans. We believe the strong macroeconomic backdrop will further support U.S. equity growth; however, we expect higher volatility in the second half and a longer-term return outlook of approximately 6% (4% real + 2% inflation). Domestically, the best equity opportunity remains in high quality energy infrastructure companies. Outside the U.S. we prefer international developed equities over emerging markets equities, as we are willing to sacrifice some return for what we perceive to be far less risk in the coming years.