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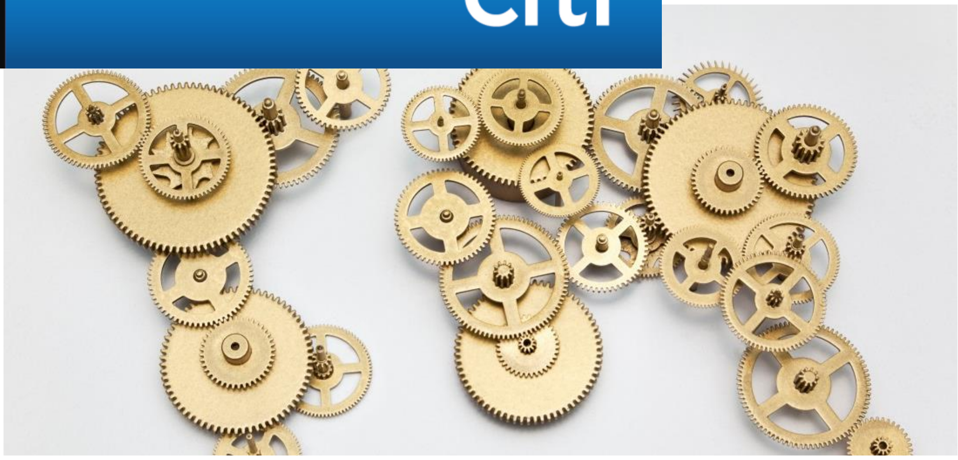

Europe Strategy

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Buy European equities now, UK equities later in 2020

- **Europe and the UK continue to face challenging unlocking phases despite COVID-19 treatment progress.** However, we do not expect the regional virus resurgences to result in new widespread and prolonged lockdowns.

- **Europe's economic recovery is gathering momentum, which is also reflected in gradually improving market perception. The UK still faces headwinds, including important EU trade deal talks**. Nevertheless, the UK's outlook should look clearer by year-end.

- **Government financial support programs can extend further.** France and Germany are currently supporting their economies aggressively, while the UK is likely to announce further measures in the autumn.

- **Central banks are expected to remain very accommodative.** We expect both the European Central Bank (ECB) and the Bank of England (BoE) to expand their asset purchase programmes in size and breadth.

- **While GDP recoveries are firmly underway, the high frequency data is losing some momentum and activity levels are still below normal levels.** We expect corporate earnings will fall by over 40% this year, before rebounding by a similar amount next year.

- **We are slightly overweight European equities, neutral UK equities, with a preference for 'COVID-cyclicals', value, and mid-caps.** We are focused on companies with balance sheet strength and progressive dividend growth.

- **European high yield corporate bonds have further to rally on a selective basis**, underpinned by the increasingly challenging investor search for positive yield.

- **Euro and Sterling have recently benefited from the broad US dollar weakness. The Euro is well supported by domestic drivers, Sterling now needs Brexit clarity.**

- **The virus's impact reinforces some of our recommendations from the start of the year**. These include staying invested, diversifying sensibly, and embracing higher volatility. Our long-term "Unstoppable Trends" like fintech and cybersecurity still offer attractive equity potential.

Contents

Europe – macro outlook improving

The European recovery story is clear-cut and only in its early stages, underpinned by more aggressive and more cohesive policymaking. This is reflected in several areas:

1. **The ECB has been decisive** in handling the threat to its bond buying program from the German Constitutional Court. This removed a risk to the European Court of Justice's primacy. We expect the ECB to add a further €350 billion to its already-committed €1.35 trillion PEPP (Pandemic Emergency Purchase Program), possibly including high yield corporate bonds. This is keeping costs low for the huge fiscal financing, and also helping the periphery with Greek bonds included in the PEPP.

2. **The €750 billion EU Recovery Fund is a vital catalyst, in four ways:**

   Firstly, the proposed size of €750 billion starts in 2021 and would add fiscal stimulus of about 1.4% of GDP.

   Secondly, there is €390 billion within it allocated to grants that should support the weaker periphery countries **– figure 1.**

   Thirdly, it demonstrates solidarity among EU leaders, which bodes well for the necessary long-term EU structural reforms that lie ahead. The solidarity in agreeing the Recovery Fund will extend to issuing EU sovereign bonds, as well as supporting the Euro.

   Fourthly, the fund includes revenue-generating proposals in long-term growth areas like digital technology and green energy.

3. **A stronger periphery lessens the Eurozone breakup risk,** which is in turn a key underpinning of the Euro's strength. For underweight overseas investors looking to diversify from the US, the likely critical buyers in the months ahead, the firmer currency is generally viewed as a positive, as it removes the need to hedge, more than offsetting the impact on exporters. Our equity section (pages 4-6) outlines why we have confidence in attractive returns in selective areas despite the currency strength.

4. **Signicant domestic fiscal easings** are driving high frequency economic data pickups. This data is indicating firming growth, and our GDP growth forecast has been raised to 4% for next year.

   The locomotives of Europe have been particularly aggressive – figure 2:

   France announced a €100 billion Recovery Plan this week, following their €106 billion package during the second quarter. The recovery packages combined equate to around 8% of GDP. The latest package extends to 2024. €30 billion will be for ecological transition, €35 billion to boost firms' competitiveness and to support re-onshoring, and €35 billion to support the labour market and the health sector. 40% will be funded from France's share of the EU Recovery Fund's grants.

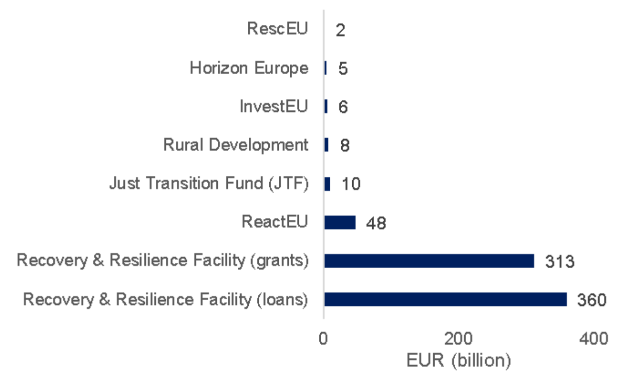
   Germany breached its debt and deficit guidelines with its €130 billion and €156 billion emergency fiscal packages. While these packages were focused on supporting workers and consumption, there is expected to be more focus on further supporting businesses looking forward.

The third fiscal support package announced last week is fiscally neutral, implying that the coalition has confidence that the worst phase of the COVID-induced economic downturn was in the second quarter. Neverthless, it does extend some existing emergency measures to help underpin the recovery. The key extension is that furloughing now has a maximum of 24 months (was previously 12 months) until 31 December 2021. This could be supportive for the ruling coalition ahead of the 2021 federal election. In addition the €25 billion business grant scheme has been extended until the end of this year. The EU recovery fund money will be focussed mainly on digital education.

5. **Better COVID-19 responses** (in terms of treatments, better clarity on preventative measures, as well as more hospital capacity) have enabled unlocking during the busy summer months with only modest viral resurgences. This has supported the growth upturns, and also improved perception towards Europe as an investment area.

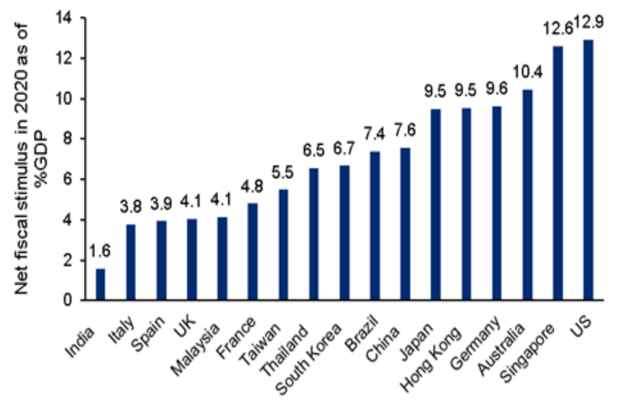
6. **Europe will benefit from Asia's economic revival.** The EU linkage is more significant with Asia than with Latin America, in terms of trade and revenue exposures. While 8.7% of Europe's total trade is with developing Asia, these linkages with Asia are even greater than the EU linkages with the US. Additionally, in terms of direct revenue exposure, Europe has the highest exposure to Asia (and Latin America) at 29.5%. (By comparison, the US only has 20.9%). This is positive for the EU given that Asia is coming out of the pandemic crisis first and the region's GDP growth next year is expected to exceed our forecast for global growth of 4.2%.

Figure 1. €750 billion Recovery Fund breakdown



Source: Bloomberg as of September 4th 2020

Figure 2. Net fiscal response (% GDP)



Source: Bloomberg as of September 4th 2020

European equities

At a global level, we increasingly prefer "COVID Cyclicals" over "COVID Defensives" and value over growth. (Double Header: "Redefining Value" and "Opportunity: Brazil"), European markets are well positioned for this with an average weighting of 54% "COVID Cyclicals" and much stronger correlation with value compared to other regions. *(COVID cyclicals: Financials, industrials, energy, materials, real estate, consumer discretionary. COVID defensives: IT, healthcare, communication services, consumer staples, utilities, Amazon)*

We have developed a new value framework, very different from the traditional method of seeking low share prices in relation to book value. This is partly because the pandemic has accelerated the usage of technology, and the companies using technology have prospects that are not fully reflected in their book values.

We see four different approaches to consider when investing in value:

1. **Dividend growers.** This includes firms that can sustain dividend growth as well as continuing to fund business expansions. They may emerge from this crisis stronger. Dividend growers in Europe have shown long-term outperformance characteristics – over the last 10-years, dividend growers in Europe have outperformed both broader Europe and even high dividend strategies (annual returns of 7.8% versus 6.9% and 5.7% respectively over a 10-year period).

2. **Growth at a reasonable price:** This approach uses the PEG ratio for valuation (PE/EPS growth). This helps to avoid both "value traps" and overpriced growth stocks.

3. **Companies less sensitive to rising rates:** We look in particular at companies exposed to higher rates, as evidenced by their correlations to German Bunds. Meanwhile areas such as REITs, utilities and telecoms benefit from lower rate environments given their attractions as "bond substitutes". Traditional value sectors like banks are likely to benefit most from the cyclical upturn leading to upward rate pressure. European banks are down 35% year-to-date, and we see we see selective opportunities at the individual bank level.

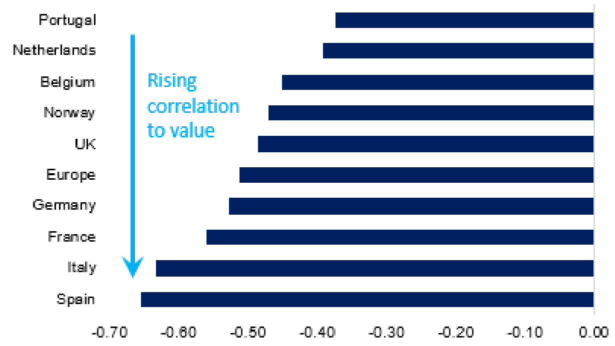
4. **We look at which countries are most exposed to the value rebound.** Both the UK and Europe have a relatively higher value bias versus other markets such as the US. Within Europe, Spain, Italy and France have the highest correlation to value **– figure 3.**

Our favoured stocks in these areas of value, have average expected total returns of 27% and dividend yields of 4.2% in the coming 12 months.

European small and mid-Cap equities (SMID) also continue to offer attractive investment opportunities. While SMID are up 45% since their 23 March 2020 lows and up 7% since our recent recommendation on 1 July, they have further to go in absolute and relative terms. There are several factors supporting this view:

1. The critical assumption is that the European economic outlook is gradually gathering momentum, as we discuss on page 3.
2. European SMID typically outperforms during the 12-months after market lows. Following the prior five European market corrections in excess of 20%, SMID stocks have outperformed large cap stocks by over 11% in the subsequent 12-month period (46% versus 35%).
3. European SMID has high exposure to both "COVID cyclicals" and value, areas that we favour at a global level. "COVID cyclicals" account for nearly two-thirds of European SMID, with the largest three sectors (industrials, financials and consumer discretionary) accounting for just under 50%.
4. Firmer Euro is supportive for the European domestic sectors & SMID – **figure 4**.
5. European SMID companies are only modestly geared. The huge volume of corporate bond issuance over recent weeks does not show a disproportionate proportion of stressed SMID companies seeking to raise capital.
6. European SMID valuations are reasonable, especially in relative terms. Current and prospective multiples for European SMID are in line with European large caps.
7. Ownership levels for all European equities including SMID are low.

Figure 3. Country correlation to value



Source: Bloomberg as of September 4th 2020

Figure 4. Europe SMID performance versus Euro

Source: Bloomberg as of September 4th 2020. Indices are unmanaged. An investor cannot invest directly in an index. They are shown for illustrative purposes only. Past performance is no guarantee of future returns. Real results may vary.

Euro outlook and the impact of Euro strength on equities

We have been bullish on the Euro since $1.11 in May and still are. The early move was driven by the broad USD decline as well as by the European periphery risks falling. The improved outlook is also reflected in market positioning turning net long.

While the trade-weighted Euro has only just exceeded it's 10-year average level, relative valuation models suggest the single currency is still 15% undervalued relative to the US dollar. The Euro still has further upside potential, driven by four primary factors: (1) improving Euro-area growth pickup versus the US, (2) underweight global investors increasing positioning in Europe, (3) higher real yields than the US, (4) and better relative virus containment versus the US.

Key technical levels are at $1.1850 and $1.20 (the February 2018 high was $1.25). **We advise using pullbacks to add to positions.** Medium term, assuming the EU recovery continues and US dollar faces further pressure, the Euro could be supported through $1.20 and above.

Impact of Euro strength on equities

Meaningful further Euro appreciation beyond the recent 10% Euro rally could see some headwinds for profit margins for European exporters. However, more important than the absolute level of the Euro, is the pace of any Euro appreciation and the strength of the economic recovery. In addition, the Euro strength is more than offset by the other factors supporting European markets highlighted elsewhere (policy support, valuation, underweight global investors).

While small- and mid-cap companies and domestically orientated sectors (such as banks, utilities, telecoms) would benefit, sectors with a cost base in Euros and a large proportion of revenues generated in US dollars would more likely be impacted. These include industrials, autos, aerospace and luxury sectors.

Fixed Income

We continue seeing selective opportunities in the European high yield market

Since the March 2020 lows, European HY has rallied 22% (compared to the 8.5% rally in IG), yet the average yield of 4.3% and the average spread of 426 basis points (bp) remain attractive as investors are increasingly challenged in finding positive yield. This is reflected in the heavy issuance being mostly heavily oversubscribed. Across European HY and IG, issuance has exceeded €1.57 trillion in 1H 2020 (over 50% up from 1H 2019).

Defaults in Euro HY have remained muted versus the US, and this can also be attributed to lower overall levels of leverage and a smaller energy sector weighting. In their latest forecasts, S&P ratings agency expect the trailing 12m default rate to rise to 8.5% by June 2021 (compared to 3.35% in June 2020). This baseline implies 62 defaults from Euro HY companies. As the cycle matures further, there will be an inceasing need to be more selective in the sector.

Periphery bonds also look attractive

Greece recently issued a €2.5 billion sovereign bond, which attracted bids of €18 billion. This was despite the yield of 1.22% being substantially less than the 1.57% for Greece's previous sovereign issue in June. This is demonstrating the ongoing scramble for bonds that are positive yielding, as well as showing rising confidence that the EU Recovery Fund will materially reduce economic and financial risks in the periphery countries like Greece. The oversubscription was doubtless also helped by the ECB's Pandemic Emergency Purchase Program including Greek bonds (the previous ECB QE programs did not).

United Kingdom – short-term headwinds

The economy

The UK suffered more than most developed countries during the second quarter when GDP growth fell by 20%. This was largely due to a delayed lockdown as well as the services sector (nearly 80% of output) having a particularly tough downturn. With government support the outlook is improving, but **it is too early for strong optimism due to economic and Brexit uncertainties on the immediate horizon.**

The economic issue is the sustainability of the upturn, in particular to what extent the weak consumer sector weighs on companies. The Government furlough support program ends at the end of October. The OBR (office for budget responsibility) has forecast that 20% of furloughed workers might be made redundant, taking the UK unemployment rate to 12%. A recent survey from YouGov & CEBR (centre for economic and business research) showed consumer confidence falling to 99.5 after three successive months of improvement. The GfK market research group has also highlighted that consumer confidence is falling due to weakening job prospects.

To make the situation even more challenging, Chancellor of the Exchequer (or Finance Minister) Sunak is considering ways to turn around the fiscal deficit (which could rise to over £350 billion in the current financial year, around 17% of GDP). He is reportedly considering four possibly measures in his autumn budget: 1. A rise in corporation tax from 19% to 24%. 2. Equalising rates of capital gains tax and income tax. 3. Reconsidering the law guaranteeing 0.7% spending on foreign aid. 4.

Removing the ‘triple lock’ on pensions. The ‘triple lock’ guarantees annual pension rises equal to the highest of wage growth, price inflation, and 2.5%. While these are all tentative at this stage, a premature tightening is a risk factor.

Brexit trade discussions

Having left the European Union on 31 January 2020, the UK is next due to leave its one-year transition period on 31 December 2020. During the transition, the UK’s trading relationship, financial contributions, and legal obligations are the same as they were during its formal membership. The UK’s Prime Minister Johnson has chosen not to seek an extension.

There were signs of progress in early summer, with signals that the UK could accept a single agreement, and the EU could accept a lesser role for the European Court of Justice.

These are the main remaining points of contention:

1. Sovereignty. The UK believes that it is entitled to the same type of agreement as other sovereign countries like Canada.
2. EU market access. The EU wants a “level playing field” in labour, environment, state aid, and competition rules, in exchange for UK market access to the single market.
3. Governance. The EU would prefer a single agreement covering everything, overseen by the European Court of Justice.
4. Irish border. The two sides need to agree on the detailed logistical arrangements for customs checks on goods entering Northern Ireland from the British mainland.
5. Fishing rights. The EU would like to maintain its existing fishing rights to the UK’s Exclusive Economic Zone (up to 200 nautical miles from the UK coastline) in perpetuity.
6. UK financial services. The sector contributes 12% of UK output and generates more tax revenue than any other sector. The UK accepts that “passporting” – full access for its financial services firms to all European single market nations – is unlikely. However, the UK is aiming instead for “mutual recognition” of closely aligned regulatory standards. But “mutual recognition” is more than the EU offers any other third country. So, the EU is instead seeking “equivalence”. This is where the two sides would each set their own standards and regulations, while recognising each other’s regulations as effectively the same. The negative of “equivalence” is that it could be withdrawn by Brussels at short notice.

The key issue is the need to agree a “level playing field” plan for state aid – item 2. above. The EU insists that the UK cannot gain an unfair competitive advantage, and wants the UK to lay out its state aid plans before a trade deal is agreed. They highlight that the Withdrawal Agreement states the desire for “common high standards.” The UK has historically given state aid amounting to only 0.34% of GDP.

Should no trade deal be agreed, the UK would leave with the EU on World Trade Organisation (WTO) terms at the end of this year. Preparation time for this scenario would be very limited, resulting in significant administrative challenges. After the transition period, the EU will classify the UK as a “third country”, meaning that it is no longer an EU member and no longer benefits from its current trade access to EU countries and the outside world.

Ultimately, the COVID-19 economic impact on both the EU and the UK is raising the pressure for a deal. In addition, a trade deal is also a priority for Angela Merkel as Germany assumes the presidency of the EU Council until the end of this year.

A deal is still desired by both sides, is still possible in the time remaining, and on balance is very slightly more likely than "no deal."

If a deal is struck, it would be a very basic free trade agreement, largely WTO-based, with the likelihood of being added to in years to come. A basic deal could be with basic implementation provisions to smooth the transition.

The immediate economic benefit of such a basic deal would be small, however the symbolism and prospect of an amicable ongoing partnership in crucial areas like security and the environment would be very positive.

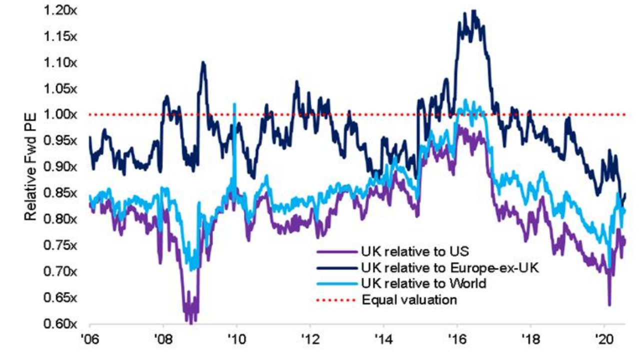
UK equities view – short-term challenges, long-term positive

UK equities remain down 20% so far in 2020, underperforming broader Europe and the US. With close to 70% of overseas revenue exposure, UK equities have been hit hard by a combination of Brexit uncertainty and US dollar weakness. In addition, with 80% of output derived from the stressed services sector, services equities have dragged back the index.

Earnings are rebounding from depressed levels (consensus expectations show UK earnings are set to rebound 35% in 2021, following declines of 37% in 2020), and dividend pressures are lessening. The FTSE 100 currently offers an attractive average dividend yield of 4.1% and trades on a forward price-to-earnings multiple of 18x which is relatively attractive. – **figures 4 and 5.** We see selective opportunities in cyclical areas like energy and financials, as well as in mid-caps as the economy begins to rebound. UK equities could also benefit from a value rebound more broadly, given its higher relative correlation to value versus growth - **figure 3**.

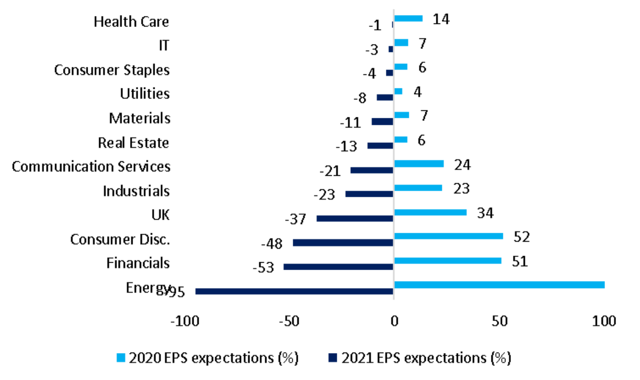
While UK equities may face some further headwinds near-term, more Brexit and policy clarity, as well as improved virus containment in the autumn, could lead to a more compelling UK equity outlook in 2021.

Figure 5. Relative forward 12m PE



Source: Bloomberg as of September 4th 2020. Forecasts are expressions of opinion, are not a guarantee of future results, are subject to change without notice and may not meet our expectations due to a variety of economic, market and other factors.

Figure 6. UK EPS expectations 2020 and 2021



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Asset allocation definitions

Asset classes	Benchmarked against
Global equities	MSCI All Country World Index, which represents 48 developed and emerging equity markets. Index components are weighted by market capitalization.
Global bonds	Bloomberg Barclays Capital Multiverse (Hedged) Index, which contains the government -related portion of the Multiverse Index, and accounts for approximately 14% of the larger index.
Hedge funds	HFRX Global Hedge Fund Index, which is designed to be representative of the overall composition of the hedge fund universe. It comprises all eligible hedge fund strategies; including but not limited to convertible arbitrage, distressed securities, equity hedge, equity market neutral, event driven, macro, merger arbitrage and relative value arbitrage. The strategies are asset-weighted based on the distribution of assets in the hedge fund industry.
Commodities	Dow Jones-UBS Commodity Index, which is composed of futures contracts on physical commodities traded on US exchanges, with the exception of aluminum, nickel and zinc, which trade on the London Metal Exchange (LME). The major commodity sectors are represented including energy, petroleum, precious metals, industrial metals, grains, livestock, softs, agriculture and ex-energy.
Cash	Three-month LIBOR, which is the interest rates that banks charge each other in the international inter -bank market for three-month loans (usually denominated in Eurodollars).
Equities	
Developed market large cap	MSCI World Large Cap Index, which is free-float adjusted and weighted by market capitalization. The index is designed to measure the equity market performance of the large cap stocks in 23 developed markets. Large cap is defined as stocks representing roughly 70% of each market's capitalization.
US	Standard & Poor's 500 Index, which is a capitalization -weighted index that includes a representative sample of 500 leading companies in leading industries of the US economy. Although the S&P 500 focuses on the large cap segment of the market, with over 80% coverage of US equities, it is also an ideal proxy for the total market.
Europe ex UK	MSCI Europe ex UK Large Cap Index, which is free-float adjusted and weighted by market capitalization. The index is designed to measure large cap stock performance in each of Europe's developed markets, except for the UK.
UK	MSCI UK Large Cap Index, which is free-float adjusted and weighted by market capitalization. The index is designed to measure large cap stock performance in the UK. FTSE 100 Index: Capitalisation weighted index of the 100 most highly capitalised companies traded on the London Stock Exchange FTSE 250 Index: Capitalisation weighted index of the 250 most highly capitalised companies outside of the FTSE 100 traded on the London Stock Exchange
Japan	MSCI Japan Large Cap Index, which is free-float adjusted and weighted by market capitalization. The index is designed to measure large cap stock performance in Japan.
Asia Pacific ex Japan	MSCI Asia Pacific ex Japan Large Cap Index, which is free-float adjusted and weighted by market capitalization. The index is designed to measure the performance of large cap stocks in Australia, Hong Kong, New Zealand and Singapore.
Developed market small and mid-cap (SMID)	MSCI World Small Cap Index, which is a capitalization-weighted index that measures small cap stock performance in 23 developed equity markets.
Emerging market	MSCI Emerging Markets Index, which is free-float adjusted and weighted by market capitalization. The index is designed to measure equity market performance of 22 emerging markets.
Bonds	
Developed sovereign	Citi World Government Bond Index (WGBI), which consists of the major global investment grade government bond markets and is composed of sovereign debt, denominated in the domestic currency. To join the WGBI, the market must satisfy size, credit and barriers-to-entry requirements. In order to ensure that the WGBI remains an investment grade benchmark, a minimum credit quality of BBB–/Baa3 by either S&P or Moody's is imposed. The index is rebalanced monthly.
Emerging sovereign	Citi Emerging Market Sovereign Bond Index (ESBI), which includes Brady bonds and US dollar -denominated emerging market sovereign debt issued in the global, Yankee and Eurodollar markets, excluding loans. It is composed of debt in Africa, Asia, Europe and Latin America. We classify an emerging market as a sovereign with a maximum foreign debt rating of BBB+/Baa1 by S&P or Moody's. Defaulted issues are excluded.
Supranationals	Citi World Broad Investment Grade Index (WBIG)—Government Related, which is a subsector of the WBIG. The index includes fixed rate investment grade agency, supranational and regional government debt, denominated in the domestic currency. The index is rebalanced monthly.
Corporate investment grade	Citi World Broad Investment Grade Index (WBIG)—Corporate, which is a subsector of the WBIG. The index includes fixed rate global investment grade corporate debt within the finance, industrial and utility sectors, denominated in the domestic currency. The index is rebalanced monthly.
Corporate high yield	Bloomberg Barclays Global High Yield Corporate Index. Provides a broad-based measure of the global high yield fixed income markets. It is also a component of the Multiverse Index and the Global Aggregate Index.

Securitized	Citi World Broad Investment Grade Index (WBIG)—Securitized, which is a subsector of the WBIG. The index includes global investment grade collateralized debt denominated in the domestic currency, including mortgage - backed securities, covered bonds (Pfandbriefe) and asset -backed securities. The index is rebalanced monthly.

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Bond rating equivalence
Alpha and/or numeric symbols used to give indications of relative credit quality. In the municipal market, these designations are published by the rating services. Internal ratings are also used by other market participants to indicate credit quality.

Bond credit quality ratings	Rating agencies		
Credit risk	**Moody's[1]**	**Standard and Poor's[2]**	**Fitch Ratings[2]**
Investment Grade			
Highest quality	Aaa	AAA	AAA
High quality (very strong)	Aa	AA	AA
Upper medium grade (Strong)	A	A	A
Medium grade	Baa	BBB	BBB
Not Investment Grade			
Lower medium grade (somewhat speculative)	Ba	BB	BB
Low grade (speculative)	B	B	B
Poor quality (may default)	Caa	CCC	CCC
Most speculative	Ca	CC	CC
No interest being paid or bankruptcy petition filed	C	D	C
In default	C	D	D

1 The ratings from Aa to Ca by Moody's may be modified by the addition of a 1, 2, or 3 to show relative standing within the category.
2 The ratings from AA to CC by Standard and Poor's and Fitch Ratings may be modified by the addition of a plus or a minus to show relative standing within the category.

(MLP's) - Energy Related MLPs May Exhibit High Volatility. While not historically very volatile, in certain market environments Energy Related MLPS may exhibit high volatility.

Changes in Regulatory or Tax Treatment of Energy Related MLPs. If the IRS changes the current tax treatment of the master limited partnerships included in the Basket of Energy Related MLPs thereby subjecting them to higher rates of taxation, or if other regulatory authorities enact regulations which negatively affect the ability of the master limited partnerships to generate income or distribute dividends to holders of common units, the return on the Notes, if any, could be dramatically reduced. Investment in a basket of Energy Related MLPs may expose the investor to concentration risk due to industry, geographical, political, and regulatory concentration.

Mortgage-backed securities ("MBS"), which include collateralized mortgage obligations ("CMOs"), also referred to as real estate mortgage investment conduits ("REMICs"), may not be suitable for all investors. There is the possibility of early return of principal due to mortgage prepayments, which can reduce expected yield and result in reinvestment risk. Conversely, return of principal may be slower than initial prepayment speed assumptions, extending the average life of the security up to its listed maturity date (also referred to as extension risk).

Additionally, the underlying collateral supporting non-Agency MBS may default on principal and interest payments. In certain cases, this could cause the income stream of the security to decline and result in loss of principal. Further, an insufficient level of credit support may result in a downgrade of a mortgage bond's credit rating and lead to a higher probability of principal loss and increased price volatility. Investments in subordinated MBS involve greater credit risk of default than the senior classes of the same issue. Default risk may be pronounced in cases where the MBS security is secured by, or evidencing an interest in, a relatively small or less diverse pool of underlying mortgage loans.

MBS are also sensitive to interest rate changes which can negatively impact the market value of the security. During times of heightened volatility, MBS can experience greater levels of illiquidity and larger price movements. Price volatility may also occur from other factors including, but not limited to, prepayments, future prepayment expectations, credit concerns, underlying collateral performance and technical changes in the market.

Alternative investments referenced in this report are speculative and entail significant risks that can include losses due to leveraging or other speculative investment practices, lack of liquidity, volatility of returns, restrictions on transferring interests in the fund, potential lack of diversification, absence of information regarding valuations and pricing, complex tax structures and delays in tax reporting, less regulation and higher fees than mutual funds and advisor risk.

Asset allocation does not assure a profit or protect against a loss in declining financial markets.

The indexes are unmanaged. An investor cannot invest directly in an index. They are shown for illustrative purposes only and do not represent the performance of any specific investment. Index returns do not include any expenses, fees or sales charges, which would lower performance.

Past performance is no guarantee of future results.

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Investing in smaller companies involves greater risks not associated with investing in more established companies, such as business risk, significant stock price fluctuations and illiquidity.

Factors affecting commodities generally, index components composed of futures contracts on nickel or copper, which are industrial metals, may be subject to a number of additional factors specific to industrial metals that might cause price volatility. These include changes in the level of industrial activity using industrial metals (including the availability of substitutes such as manmade or synthetic substitutes); disruptions in the supply chain, from mining to storage to smelting or refining; adjustments to inventory; variations in production costs, including storage, labor and energy costs; costs associated with regulatory compliance, including environmental regulations; and changes in industrial, government and consumer demand, both in individual consuming nations and internationally. Index components concentrated in futures contracts on agricultural products, including grains, may be subject to a number of additional factors specific to agricultural products that might cause price volatility. These include weather conditions, including floods, drought and freezing conditions; changes in government policies; planting decisions; and changes in demand for agricultural products, both with end users and as inputs into various industries.

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