Our Outlook for 2015

Divergence in economic conditions and monetary policies appears to be the overarching theme for the year ahead.

The U.S. Federal Reserve is moving toward an interest-rate increase while other central banks are searching for ways to stimulate the economies of their respective countries.

U.S. stocks are expected to continue to outperform broad international benchmarks. On the fixed income side, higher-quality bonds should continue to perform well. Riskier assets, such as emerging market bonds, may underperform as investors demand higher yields to offset risks.

- Fiscal policy may be more important to investors than monetary policy.
- The rapid drop in oil prices will likely bolster global economic growth in the short term.
- Emerging market stocks are at a turning point because of attractive valuations.

- This secular bull market is likely in a more mature phase.
- Fed tightening cycles tend to usher in volatility and pullbacks but don’t typically upend bull markets.
- Lower energy prices put downward pressure on overall inflation, a plus for the U.S. economy and stock market.

- A stronger dollar is likely to hold down inflation and long-term interest rates.
- We expect a moderate rate hike by midyear and increased volatility.
- We are concerned about liquidity in the bond market as banks and dealers cut back on their inventory of bonds.

- Options traders generally perceive more upside for U.S. stocks.
- While volatility has receded in the short term, nothing lasts forever and volatility could increase.
2015 Global Investment Outlook

For 2015, we forecast another year of gains for global stocks. Supporting factors are revenue from slightly stronger global economic growth, boosted by central bank stimulus, along with supportive fiscal policy — for the first time in a while. Also, global growth could get a boost from the recent 25% decline in oil prices. The gains for stocks may be accompanied by volatility stemming from a number of risks. These risks include those posed by central bank actions that are complicated by varying levels of growth around the world, flare-ups in geopolitical hot spots and the potential for natural disasters, pandemics or other uncertain events to tip sluggish global growth into a recession.

Where will stocks offer investors the best potential return in 2015?

Many factors influence the relative performance of U.S. and international stocks. One indicator that has a solid track record of signaling when international stocks may outperform U.S. stocks is the “current account.”

The current account is driven by trade and money flows in and out of the United States. In general over the past 40 years, when the U.S. current account as a percentage of gross domestic product (GDP) was improving, U.S. stocks outperformed international stocks. The opposite was true when the current account worsened: International stocks outperformed U.S. stocks. Changes in the current account have led relative stock market performance by about three quarters of a year.

The U.S. current account has flattened after improving steadily in recent years and could be near a change in direction. The key to the direction in 2015 may be the dollar. If the U.S. current account were to deteriorate, driven by a significant rise in the U.S. dollar, it would suggest that international stocks may finally begin to outperform U.S. stocks in 2015.

The current account data for the third quarter will be released December 17, 2014. We will be watching this closely for signs of a change in direction. But, given where the key drivers stand today, we expect developed international stocks to lag those in the United States and emerging markets for several reasons: weaker economies, slower application of stimulus in Europe and valuations that don’t account for the risks — in addition to the trend in the current account.

Low oil prices could lead to upside surprises

The rapid drop in oil prices may act as a significant short-term boost to global economic growth. With the amount spent on oil amounting to 4% of world GDP, the global price decline from around $110 in recent years to about $80 is about 25%, which amounts to 1% of world GDP.

This does not translate directly into a 1% boost to global growth because the windfall to consumers is a cost to producers. But it can have a sizable effect in the short term. Producers are unlikely to make major cuts to their expenditures in the short term, while consumers have consistently proven to spend most of what they save at the pump. Historically, moves in oil have tracked closely with economic-surprise indexes and may point to some upside surprises in coming months that could help to lift stocks globally as 2015 gets off to a solid start.

Policy is a key theme for 2015

The potential boost to global growth from lower oil prices may act like fiscal stimulus in a way that is similar to a tax cut. Fiscal policy may be more important than monetary policy in 2015. Monetary policy may not change all that much from 2014. The Fed and Bank of England may raise rates in 2015, but central banks in Europe, China and Japan are ramping up stimulus for the year ahead. They are not alone.
In the past month, central banks in South Korea, Sweden, Vietnam, Iceland and Romania all have cut interest rates. While monetary policy garners a lot of attention, it is likely to remain broadly stimulative. More interesting for investors may be the change in fiscal policy next year.

- In light of the surprisingly weak Q3 GDP, Japan is set to delay the planned 2015 consumption-tax increase. Elsewhere in Asia, China continues to provide targeted fiscal stimulus programs, including the most recent announcement of new rail projects that are intended to keep the economy from slowing more sharply.
- In Europe, the fight over the French and Italian budgets is pretty much over, with the EU not requiring the nations to hit previously agreed upon budget targets for 2015 through significant tax increases and spending cuts. In addition, Europe will likely approve and begin to implement some version of President Juncker’s plan to provide 300 billion euros in spending initiatives.
- Even here in the United States, Federal outlays have increased for five months, after being flat for five years, and were up 5.5% year-over-year in October.

Globally, we are starting to see a shift from fiscal drag to fiscal stimulus in what is still going to be a very stimulative monetary-policy environment. These policies are likely to continue to push asset prices higher around the world in 2015 despite still-sluggish global growth.

**Why are emerging market stocks attractive now?**

Here are three key points on why now is the time for emerging market stocks:

- Emerging market stocks — recent performance laggards — may be at a turning point due to attractive valuations.
- Despite the risks presented by the slowdown in Europe and geopolitical spillovers, emerging market economies may benefit from an improvement in global growth.
- If growth continues to be sluggish, low valuations on emerging market stocks and correspondingly low expectations may limit their downside.

Valuations on emerging market stocks are relatively inexpensive when compared with stocks in the United States and other developed markets. Emerging market stocks — as measured by the MSCI Emerging Markets Index — are trading at a price-to-earnings (P/E) ratio of only about 10. In comparison, U.S. stocks — as measured by the Standard & Poor’s 500-stock index — traded at a P/E of more than 15. Other developed market stocks as represented by the MSCI EAFE Index (excluding Japan) had a P/E of about 14. The relatively low valuation implies that investors have already priced in a pessimistic outlook for emerging market stocks, making them better positioned than stocks of developed international markets.
Global Markets

Also, emerging market stocks may benefit from an improvement in global growth. Global exports appear ready to accelerate from the recent quarterly pace of about 1%. Emerging market stocks historically have outperformed their developed-country counterparts when global exports improve. Over the past 10 years, when global exports grew faster than 2.5% in a quarter, returns from emerging market stocks were almost double than those of international developed country stocks.

We may have reached a turning point for EM stocks. In 2014, we’ve seen solid stock market gains from even the most economically challenged emerging market countries. Stock markets in Venezuela, South Africa and Turkey have produced positive total returns year-to-date through November 25, 2014. That’s despite issues like a sky-high “misery index” – the sum of a country’s inflation rate and its unemployment rate. After years of underperformance, EM stock markets appear to have started to climb a “wall of worry” despite negative events, with the MSCI Emerging Markets Index up 13% from this year’s February 5 low, as of November 25.

How can emerging market stocks perform well even amid a strong dollar?

Emerging market stocks often are considered at risk when the dollar rises and commodity prices fall. A strong dollar, weak commodity prices and solid emerging market stock performance, however, can coexist in the environment we foresee for a few key reasons:

• There are now far more commodity consumers than producers among emerging market stocks. The emerging market sector mix has changed over time. Nearly 50% of the value of the companies in the MSCI Emerging Market Index is now in the financials and technology sectors. The materials sector, the largest sector 20 years ago, now accounts for less than 10% of the emerging market universe and even combined with the energy sector accounts for less than 20% of the index’s value. By and large, emerging market companies are not the commodity producers they are often believed to be—or were in the past.

• The China-driven commodity boom that coincided with strong emerging market performance is ending. From the late 1990s through the late 2000s, the close relationship between commodities and emerging market stocks was tied to China and its massive scale and rapid pace of construction activity. China became the importer of nearly half of the world’s supply of copper and other materials. This period, often referred to as the commodity super-cycle, is now ending as China refocuses its growth. The transformation of where growth is coming from in China has been dramatic. Resource-heavy State Owned Enterprises now represent only about 25% of China’s GDP. Resource-light companies, including some world-class e-commerce firms, are thriving and becoming decoupled from state control as they go global in raising capital. A testament to the decoupling of Chinese stock market performance from commodity prices is the fact that over the past three years ending November 25, 2014, commodity prices, measured by the Commodity Research Bureau index, are flat to down while the Hang Seng Index of Chinese stocks is up about 50% on a total return basis. So while the commodity super-cycle may be ending, emerging market stocks have moved on.

• Lessons have been learned and put into practice since the dollar-driven disasters of the 1990s. Emerging market countries have made structural changes. Smaller trade and budget deficits, larger foreign currency reserves, debt denominated in local currencies, and flexible exchange rates are leaving these countries much less vulnerable to an extended rise in the dollar than they were in the past.

The effect of a rising dollar on any nondollar investment can act as a drag. But low valuation accounts for much of the risk and leaves plenty of room for solid performance.
2015 U.S. Stock Market and Economic Outlook

Our view, which we have held since the market bottomed in 2009, is that the current bull market is secular, not cyclical. Secular bull markets—like from 1949 to 1968 and 1982 to 2000—are extended bull markets characterized by above-average annualized returns and generally less-dramatic downside risk.

This does not mean this market is immune to corrections, but it shares characteristics of past secular bull markets. For one, the Standard & Poor’s 500-stock index has posted an annualized return of 22% in the first four years of this bull market. This closely mirrors the first four years of prior secular bull markets, which had similar annualized S&P 500 returns. Economic characteristics of past secular bull markets at their outset include secular valuation lows, secular unemployment rate highs and negative real interest rates. All three characteristics also were in place at the beginning of the current bull market.

Since we put the bull market in an economic context, we will share a high-level outlook for the U.S. economy. Unique in this recovery is the large spread between the average quarterly real growth of gross domestic product (GDP), which has been a relatively paltry 2.3%, and that for the private sector, which has been a healthier 3.2%. We believe this spread is set to narrow, with the overall growth rate catching up to the private sector’s growth rate, due to waning fiscal drag.

Consumer spending is picking up

The “deleveraging” period since 2008, when consumers were focused on paying off debt, is largely over. This is why consumer spending has been recovering. It is not likely to reach prior lofty levels due to the lingering memory of the debt crisis and a general increase in frugality. But with consumer free cash flow on the rise, due in part to lower energy prices, consumer spending (accounting for 68% of U.S. GDP) should remain relatively healthy and could even accelerate more than income growth.

In addition, the economic expansion appears to be in a phase of higher capital expenditures, or capex. Investment-led expansions tend to last longer than those that are led by consumer spending. Since the mid-2000s, corporate cash has tended to be used for stock buybacks and dividend payments rather than capital expenditures. But the tide appears to be turning toward a greater focus on capex. Capacity utilization, a capex leading indicator, is nearing the critical 80% level, which has historically meant demand is sufficiently high to warrant the expansion of capital investments. And, prior underinvestment in fixed assets and the old age of those assets also suggest a sustained expansion in capex.

Capacity utilization of greater than 80% is a key for capex

[Graph showing capacity utilization and real nonresidential fixed investment]

Capacity Utilization as of 10/14. Nonresidential Fixed Investment as of 3Q14. Source: FactSet, Ned Davis Research (NDR), Inc. (Further distribution prohibited without prior permission. Copyright 2014 (c) Ned Davis Research, Inc. All rights reserved.), Strategas Research Partners LLC.
But every bull market—secular or cyclical—has stages and we are likely in a more mature phase. What is remarkable about this bull market is that euphoria hasn’t set in, even after a 240% appreciation in stock prices since March 2009. Investors remain skeptical of this bull market.

**Earnings growth is outpacing rise in valuations**

We can also look at the market’s underlying fundamentals. S&P earnings have tripled since March of 2009, while the stock market is up a lesser 240%. On both a trailing and forward basis, the market is about at historic median P/E ratios while most of the macro conditions supporting higher valuations remain in place. These include a “not-too-hot, not-too-cold” economic environment of trend growth and subdued inflation and the stronger dollar. In addition, the market’s best performance historically has come when earnings growth is positive, but not too hot.

Many have argued that multiples have risen “artificially,” meaning they have been pushed up by risk-seeking investors and record-low interest rates. Interestingly, though, multiple expansion in this bull market has been about average for bull markets since 1957. So why have stock market returns been so high? Earnings. Earnings growth in the current bull market has been 20% above the average level of growth for all bull markets since 1957.

**What could spark volatility?**

Investor sentiment is a shorter-term factor that will likely drive the market’s ups and downs in 2015. Much like when attitudinal measures of investor sentiment indicated high levels of optimism and complacency in September, the market is vulnerable to negative catalysts when sentiment is optimistic.

One catalyst in 2015 could be interest-rate uncertainty as the Fed moves toward an initial rate increase. The onset of Fed tightening cycles has not upended bull markets historically—quite the contrary—but it does often usher in bouts of volatility and pullbacks. Case in point would be the two most recent tightening cycles during the mid-1990s and mid-2000s. The stock market performed admirably, but with five corrections (or pullbacks) during each cycle. The corrections averaged -12% in the mid-1990s cycle, while the average pullback was -7% in the mid-2000s cycle.

Consider every initial rate increase since the early 1960s and the stock market’s behavior in the six months before and after that increase. The market’s weakest period tends to occur several months in advance of the initial increase but the trajectory of the market’s performance is largely higher over the full year.
How do falling oil prices affect the U.S. economy and stock market?

Consumer spending represents 68% of the U.S. economy. Oil and gas capex represents about 1% of U.S. GDP and less than 9% of U.S. total capex (which in turn represents about 12% of U.S. GDP). Therefore, the benefit of lower energy prices to the consumer and many businesses greatly outweighs the significant hit to energy companies and/or energy-oriented capex, especially in energy-oriented states.

U.S. domestic capex has grown by more than $600 billion over the past four years, with $100 billion of that being energy-oriented. One can argue that much of non-energy capex would benefit from reduced operating costs courtesy of lower energy prices.

Lower energy prices also hold down overall inflation, which is a plus for both the U.S. economy and stock market. Lower inflation has historically meant higher equity valuations. In fact, there is a direct inverse correlation between the energy sector’s weight in the S&P 500: a lower weight, typically as a result of lower energy prices, has led to higher overall S&P 500 P/E ratios, and vice versa.

Is a strong dollar good for the U.S. stock market and economy?

The conditions supporting the U.S. dollar resemble those that drove the dollar bull market of the 1990s, most of which also had a positive effect on the stock market; i.e., stocks and the dollar were positively correlated. The correlation between the dollar and stocks recently moved back into positive territory and we think it will likely remain there.

This is in contrast to the dollar bull market in the early 1980s when runaway inflation and double-digit interest rates drove the dollar higher—not positive conditions for the stock market. During the 2008 financial crisis, a higher dollar was the result of its safe-haven status amid a crumbling global financial system—also not a positive condition for the stock market. During these phases of dollar strength, the stock market was inversely correlated to the moves in the dollar.

As far as economic impact, while a stronger dollar makes exported goods more expensive, exports represent only 13% of U.S. GDP, compared with 68% for consumer spending. Since many commodities—notably oil—are priced in dollars, a stronger dollar means lower commodity prices, which is good for consumption-oriented economies of countries like the United States.

Could too much dollar strength be a bad thing? The answer probably rests with the bond market. The negative implications—the tightening effect—of a stronger dollar can be offset by a decline in longer-term interest rates. So far this year, the U.S. Dollar Index (DXY) has appreciated by about 10%, while the 10-year Treasury yield has fallen by about 70 basis points. As such, the bond market is at least partly doing its job as an offset to the negative implications of a stronger dollar.

Key Points:

- A stronger dollar means lower commodity prices, which is good for consumption-oriented economies like ours.
- Lower energy prices put downward pressure on overall inflation.
2015 Fixed Income Outlook

In 2015, we expect moderately higher interest rates, a stronger dollar, a flatter yield curve and heightened volatility.

Interest rates

The focus of attention in the fixed income markets is likely to be on the Federal Reserve’s move toward tighter monetary policy, which we think will have significant effects on the markets, but not perhaps in the way most people think. It’s not just about interest rates – but more about volatility and valuation.

The Fed has already exited quantitative easing (QE) and assuming the economy continues to perform reasonably well, as we expect, then a rate hike seems likely midyear. But we think that the rate of Fed tightening will be slower than the Fed has indicated and more in line with the trend implied by the forward market. While we believe the domestic economy will continue to improve, there are strong disinflationary pressures coming from Europe and Asia, which could hold down inflation and bond yields. Additionally, we expect the dollar to continue to rise as the Fed shifts policy.

The market and the Fed are far apart

Yield to maturity

It is not clear that QE has been solely responsible for the drop in interest rates. We think falling inflation and inflation expectations have been a big contributor. In fact, the evidence suggests that during periods of QE, long-term rates have risen along with inflation expectations. When periods of QE have ended, rates and inflation expectations have generally trended lower. Therefore, the absence of QE doesn’t necessarily mean rates will rise by much unless there is stronger growth and/or an increase in inflation expectations. So our rate expectations would be for a moderate rise from current levels.

Stronger dollar

A stronger dollar is likely to hold down inflation and long-term interest rates as well. With the U.S. economy likely to outperform the economies of other developed countries, especially Europe and Japan, we’re expecting the dollar to continue to advance. It’s up about 8% on a trade-weighted basis since last summer and the diverging trends in growth and monetary policy between the United States and other major countries should mean the dollar gets stronger.
Higher relative interest rates make the dollar more attractive to hold. For example, two-year note yields in Germany and Japan are near zero or even negative, so even at current rates there is a positive cost of carry in holding dollars versus euros or yen. With the prospect of easier monetary policies in Europe and Asia, that spread is likely to widen even further. The upshot is that as long as U.S. growth remains on track and the Fed is still shifting away from the loose monetary policy of the past six years, the dollar should continue to rise and that should keep inflation and interest rates in check.

Yield curve

Our expectation is that as the Fed raises rates, the major trend will be a flatter yield curve, particularly if inflation remains below the 2% target level. The yield curve has already flattened quite a bit from the 5-year to 30-year maturities. With rate hikes, the front end of the curve – from 3-month bills to 5-year notes – should flatten. The market has already priced in a lot of the increase in rates. A flatter yield curve would be consistent with the pattern of the 2004 cycle, which was signaled in advance and unlike the early response to the 1994 tightening cycle, which was not.

Volatility

While the Fed’s impact on long-term interest rates can be debated (and will be) it does seem clear that the Fed’s various programs have suppressed volatility in the fixed income markets. Between the zero interest rate policy and the Fed’s messaging, volatility has been quite low by historical standards. The Merrill Lynch index of bond market volatility – the MOVE index – shows that current volatility readings of about 65 to 70 are well below the long-term average of 100-110. We don’t expect a spike on the magnitude of the 2008-09 time period, but we do think it is likely to rise from here.

Without the strong Fed backstop, we think investors will demand more risk premium to hold bonds, causing volatility to rise. Therefore, we expect some widening of credit spreads – more in high yield than in investment grade. Between rising volatility, a stronger dollar and tighter Fed policy, the riskier sectors of the markets – high yield, bank loans and emerging market bonds – may underperform as investors demand higher yields to offset these risks. Some spread widening has already occurred and we would expect that to continue.
What should investors do if liquidity is a concern in the bond market?

We are concerned about liquidity in the bond market. With banks and dealers cutting back on the inventory of bonds they hold, there are fewer market makers now than there were a few years ago before the financial crisis. Consequently, when the markets get volatile, there are more price gaps – there is just no one there to provide a reasonable price. We’re also concerned that vehicles like funds and ETFs, which are liquid structures, may give the impression that the underlying markets are more liquid than they really are and investors may not realize it.

Our advice to clients is to make sure that they understand liquidity risk. Investors should not keep funds that they need available in the near term in investments that may not be that liquid. Secondly, when investing in individual bonds, it may make sense to invest in larger issues which are going to have more liquidity. Finally, we think they should go over their portfolios with a bond specialist or their financial consultant and understand the liquidity risk. If they are buy-and-hold investors, it may not matter to them, but for many it probably will make a difference.

Why are you critical of junk bonds?

We have thought since last summer that the risk/reward in high yield just wasn’t that attractive. The yields are low – last summer yields dropped to record lows on the Barclays U.S. Corporate High Yield Bond Index – and credit quality was deteriorating. There are far more “covenant lite” bonds now, increasing leverage and fewer protections for investors. An additional factor recently has been the drop in oil prices. About 15% of the Barclays U.S. Corporate High Yield Bond Index is now comprised of energy companies. That compares to just 7% a few years ago. With oil prices dropping, it’s likely to put a strain on some of those companies that are highly leveraged and it may mean higher defaults or at a minimum more stress in the sector. That warrants a higher risk premium than exists in the market. Over the past few years, a lot of money has moved into the high yield market – into both bank loans and traditional high yield bonds – as yields have dropped. The trend is beginning to reverse. If the outflows continue or pick up, it could cause a drop in prices.

**Key Points:**

- We expect further widening in credit spreads, which makes the risk/reward in high yield bonds unattractive.
- Investors need to understand the risks that declining liquidity in the fixed income markets pose for their investments.
2015 Trader Outlook

As discussed earlier in this 2015 outlook, there are a number of more positive economic indicators for investors to consider. The four-week moving average for weekly jobless claims, for example, remains near a 14½ year low. Other employment related data, such as the monthly unemployment rate, the labor-participation rate and the labor-turnover rate, all indicate continued improvement in the labor markets. Retail sales posted a solid advance in October.

We believe this trend will continue, resulting in a very strong holiday shopping season. Consumer sentiment has also reached a seven-year high. When consumers feel good and lower gasoline prices are leaving money in their pockets, they are likely to go shopping.

Technically, the Standard & Poor's 500-stock index (SPX) remains on solid ground, at or near record highs. While many market watchers were quick to call the September 18, 2014, reading of 2011.36 as the year high, the SPX has blown solidly past that level. The rebound from the Ebola-induced scare has been astounding. The SPX has gained more than 9.5% in only 19 trading days.

Keeping an eye on put/call ratios

There has been a lot of discussion recently regarding put/call ratios. The SPX OIPCR (open interest put/call ratio) shows that the total number of outstanding puts on the SPX now outnumber the total outstanding calls by a margin of less than 2 to 1. This is the lowest level since mid-June and indicates that SPX option traders generally perceive that the SPX has more upside ahead. This ratio and the index often move in the same direction, but that has not been the case for the past 3 weeks. The ratio is very close to a six-month low. The last two times the ratio was this low, the SPX remained in an uptrend for several weeks.

The VIX OIPCR (open interest put/call ratio) indicates that the total number of outstanding call contracts just barely outnumber the total outstanding puts by a margin of more than 2 to 1. While this might sound high, it is important to note that calls outnumbered puts by a ratio of more than 4 to 1 before the October volatility spike. This is not only down sharply from the 12-month high of .53 on 10/23/14, we believe it illustrates that many traders see little risk of another sharp spike in the VIX in the near term. To further emphasize this point, the last time the VIX was at its current levels (before the October spike) this ratio was at .25. So while we are at the same level VIX, we are at a much lower put/call ratio.

While we are somewhat surprised by how quickly the VIX has dropped since the Ebola-induced increase, it does help to illustrate how that sharp rise was likely an irrational panic. Irrational panics not only are typically short-lived, they often represent excellent entry points for traders looking to buy on dips. While there are other put/call ratios, these two have some of the most reliable track records, and both are clearly bullish in the near term.

With very low expectations for the lame duck session in Congress and no real threat of higher interest rates until at least March or April of 2015, the United States should be able to remain decoupled from the problems in Europe and continue to be the investing location of choice for at least the next few months. That doesn’t mean there won’t be another small pullback or two before the end of the year, but traders should view them as buying opportunities.
What are some market factors to watch for in the short term?
Since we are in a mature phase of this bull market, the consumer discretionary sector, which gained 30% in 2013, may not be a great long-term investment. But with low gasoline prices, consumer sentiment at a seven-year high and a fair amount of pent-up demand, we believe short-term gains in consumer discretionary stocks may continue over the holiday season. With the two big catalysts behind us — the end of the Fed’s tapering process and the midterm elections — the seasonally strong period from November through January looks like it may provide opportunities this year.

In 20 of the past 28 years when December finished higher, the subsequent January also finished higher. A notable exception, however, was that this did not happen in December 2013/January 2014, so as with any other statistical pattern, it is not completely reliable.

It is also worth noting that as we are approaching the end of the sixth year of this bull market, the historical averages suggest a total gain in the range of 15% to 20% for the 12-month period ending in mid-March 2015. That is about double the current gain of 8.6% since mid-March 2014. A move of this magnitude would put the S&P 500 in the range of 2160 to 2250.

On The Rise
The S&P 500 Index is up 9.5% over the past month.
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International investments involve additional risks, which include differences in financial accounting standards, currency fluctuations, geopolitical risk, foreign taxes and regulations, and the potential for illiquid markets. Investing in emerging markets may accentuate these risks.

Index definitions
MSCI Emerging Markets Index is a free float-adjusted market capitalization index that is designed to measure equity market performance in the global emerging markets. This index is a float-adjusted market capitalization index that consists of indices in 21 emerging economies: Brazil, Chile, China, Colombia, Czech Republic, Egypt, Hungary, India, Indonesia, Korea, Malaysia, Mexico, Morocco, Peru, Philippines, Poland, Russia, South Africa, Taiwan, Thailand, and Turkey.

CRB (Commodity Research Bureau) Continuous Commodity Index is a commodity index based on the futures prices of various commodities.

S&P 500® Index is a market-capitalization weighted index that consists of 500 widely traded stocks chosen for market size, liquidity, and industry group representation.

Hang Seng Index is a free float-adjusted market capitalization-weighted stock market index in Hong Kong. It is used to record and monitor daily changes of the largest companies of the Hong Kong stock market and is the main indicator of the overall market performance in Hong Kong. These 48 constituent companies represent about 60% of capitalization of the Hong Kong Stock Exchange.

The Merrill Lynch Index of Bond Market Volatility (MOVE) index is a yield curve weighted index of the normalized implied volatility on 1-month Treasury options.

Barclays U.S. Corporate High-Yield Bond Index covers the USD-denominated, non-investment grade, fixed-rate, taxable corporate bond market. Securities are classified as high-yield if the middle rating of Moody’s, Fitch, and S&P is Ba1/BB+/BB+ or below.

Chicago Board Options Exchange Market Volatility Index (VIX) a popular measure of the implied volatility of S&P 500 index options. Often referred to as the fear index or the fear gauge, it represents one measure of the market’s expectation of stock market volatility over the next 30 day period.

Trade Weighted U.S. Dollar Index: Other Important Trading Partners is an average of the exchange rates of a country’s currency with the currencies of its most important trading partners, weighted to reflect each trading partners’ importance to the country’s trade. A currency’s trade weighted index is also known as its effective exchange rate. The currencies in the U.S. dollar index are the euro, the yen, sterling, the Canadian dollar, the Swedish crown and the Swiss franc. It was launched in 1973 with a value of 100.00.

Barclays Emerging Markets USD Index includes USD-denominated debt from emerging markets in the following regions: Americas, Europe, Middle East, Africa, and Asia. As with other fixed income benchmarks provided by Barclays, the index is rules-based, allowing for an unbiased view of the marketplace and easy replicability.

Barclays International: Sovereign Index is a sub-index.

U.S. Dollar Index (DXY) is an index (or measure) of the value of the United States dollar relative to a basket of foreign currencies.
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