Economic & Capital Markets Outlook

BNY INVESTMENT STRATEGY
& SOLUTIONS GROUP

THIRD QUARTER 2016

BNY MELLON

Executive Summary

ISSG CMC SUMMARY ASSET ALLOCATION

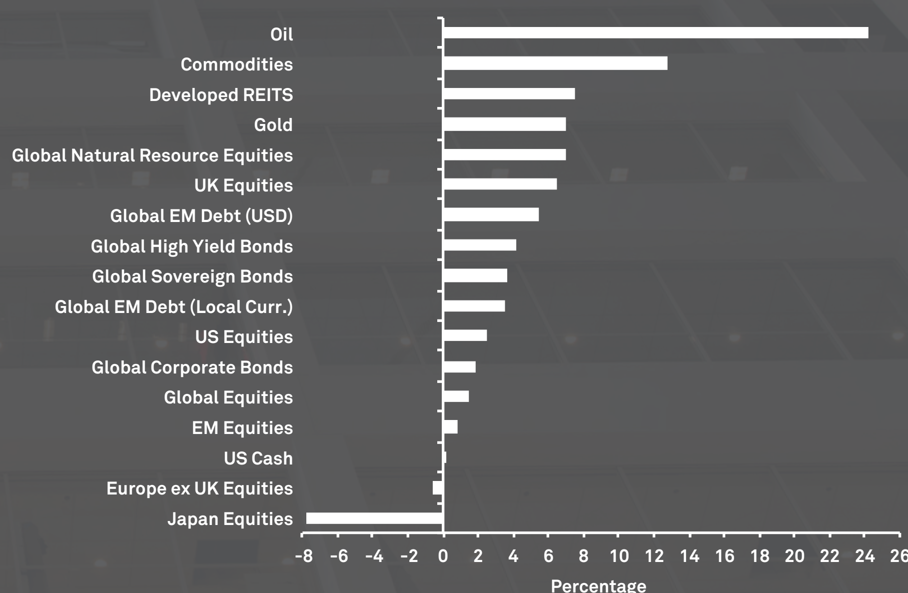
	Current	Benchmark
Global Equities	50.4%	50%
Global Bonds	45.2%	50%
Cash	4.4%	0%

- Further reduction in equity weight post "Brexit".
- Capital preservation remains a focus via cash overweight given persistent negative sovereign yields.

FIVE THINGS TO WATCH IN Q3 2016

1) Post "Brexit" developments across global markets.
2) Banking sector stresses in Italy and Germany as indicators of systemic contagion.
3) Forward rate curve in relation to inflation expectations in the US.
4) Renminbi stability relative to a stronger dollar and pending Special Drawing Rights (SDR) inclusion.
5) Post-Olympic growth trajectory in Brazil.

FIG. 1: GLOBAL ASSET PERFORMANCE
% change over 3 months to 30 JUN 16

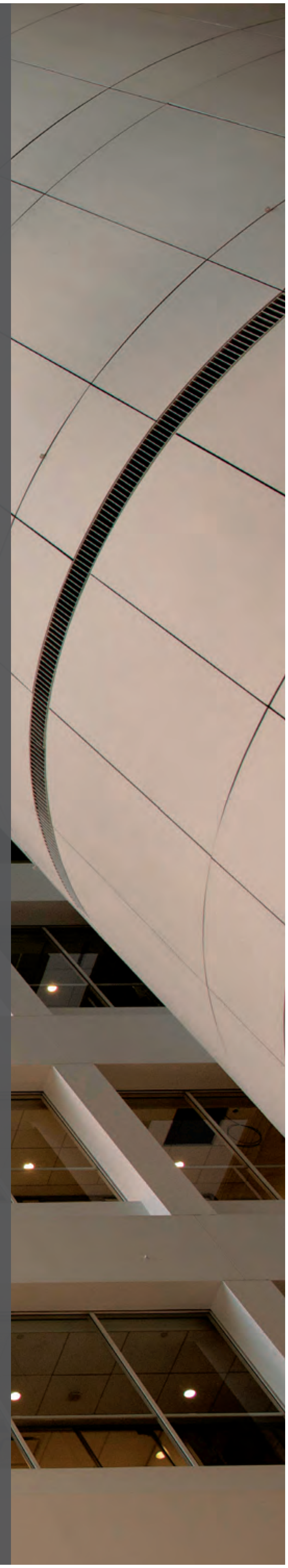


Source: Thomson Reuters Datastream & ISSG

ABOUT THE INVESTMENT STRATEGY & SOLUTIONS GROUP

BNY Investment Strategy & Solutions Group (ISSG) designs, develops and manages asset allocation strategies to help clients achieve their specific investment objectives. We combine a multi-faceted approach to risk with a forward-looking, long term perspective on economic and markets to identify opportunities while harnessing the broad and deep expertise of a global network of specialized investment affiliates to deliver sophisticated investment solutions.

The ISSG Capital Markets Committee (CMC) provides baseline, global asset allocation policy and assesses the market outlook for the global multi-asset strategies and solutions managed by ISSG.



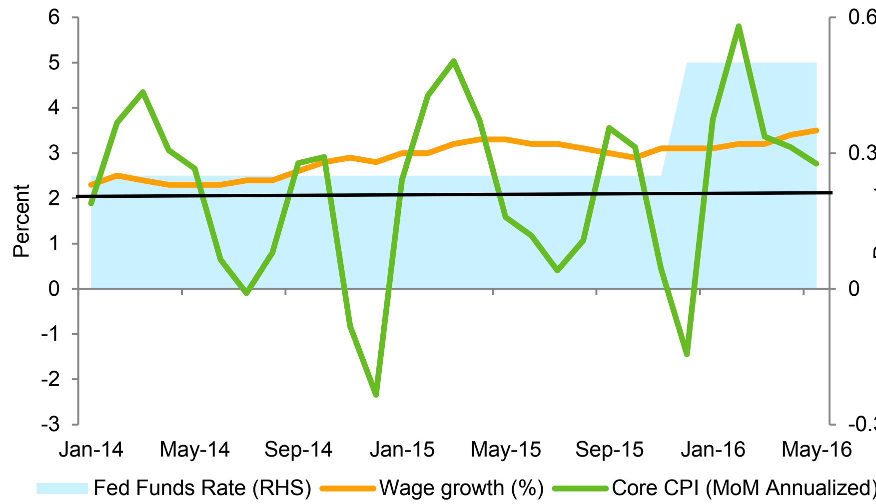
What We Are Watching

Theme	ISSG View	Asset Class Impact	Risks to View	Recent Considerations For ISSG View
Global Growth	Growth prospects for the DM universe face continued headwinds into H2 2016, as rising political uncertainty, geopolitical tensions and tightening labour markets weigh on corporate sector profits and capital spending plans. EM growth prospects for H2 2016 have benefited from the firming in prices across parts of the commodity complex and should benefit from more DM policy.	Against a backdrop of tepid economic growth expectations and rising uncertainty, the corporate sector will face increasing challenges to grow both top and bottom line numbers, a trend evidenced in analyst downgrades in H1 2016. Elevated sensitivity to economic news flow will continue to fuel bouts of volatility throughout H2 2016, and may be further compounded by liquidity concerns.	The risk of DM policy mistakes has stepped up sharply following the UK referendum vote to leave the European Union, as markets work to determine the appropriate "dis-integration premium" in the face of a prolonged period of uncertainty as the economic and political bases of this important relationship are rewritten.	A lacklustre growth backdrop in H2 2016 should see policy support continue across major DMs as downside risks to the economy remain the point of focus in the absence of inflationary pressures – indeed DM policymakers are likely to tolerate some inflationary pressures in their quest for sustainable growth. Consumer sector spending and sentiment will be a key pillar of support for H2 2016.
Global Inflation	The US inflation picture for the remainder of the year is increasingly conflicted – core inflation back in a normal range on the back of an increasingly tight labour market, whilst headline inflation measures are also poised to tick up in H2 2016 on the back of baseline effects, increasing the complexity of policy calibration.	Whilst disinflationary forces continue to be the central scenario priced in to the wider global markets for H2 2016, risk assets will continue to search for the catalysts required to drive top line growth, whilst DM government bonds should continue to benefit from bouts of risk off trading.	Another round of currency wars unleashes further disinflationary pressures, clouding the inflation outlook in DM countries. On the other hand, positive inflation surprises in H2 2016 could result in a rapid shift into inflation sensitive assets.	The fading prospect of a prolonged deterioration in energy prices should provide some support for headline inflation levels in H2 2016. However, FX policies continue to be a source for disinflationary pressures, with post-referendum GBP weakness the latest in an ongoing series of recent seismic shifts in major currencies.
Monetary Policy	DM accommodative policy to persist in H2 2016 as incremental risks to global activity levels introduced by the UK referendum result put policymakers on a more cautious footing. Further policy action from both the Bank of England (BOE) and the Bank of Japan (BOJ) look increasingly likely in H2 2016 as economic activity weakens.	Supportive monetary policy will continue to underpin the yield pickup trade in H2 2016 as DM investors are faced with a rising stock of negative yielding debt in European and Japanese markets, though this will be tempered by an increasingly volatile outlook for the FX markets. Watching CNY in run up to its inclusion in the SDR basket at the end of Q3 2016.	With DM policy rates already at record lows and efficacy of further monetary policy action diminishing, central banks face growing challenge to maintain their credibility with markets. Risks of counter cyclical policy action in UK rising for H2 2016 as BOE seeks balance between economic activity and inflation risks following the sharp currency devaluation.	The UK referendum has created a prolonged period of uncertainty for the European economy, taking a particular toll on the banking sector. The scale of additional stimulus programs in H2 2016 from the BOE and the ECB (already part way through a program) remain to be seen. Expectations for tighter US policy pushed out in to 2017.
Fiscal Policy	DMs reassessing fiscal stimulus options as limits of monetary policy increasingly apparent, though rising budget deficits and elevated debt/GDP levels increasing pressure on rating agencies as fiscal sustainability risks rise. EM markets face balancing act in H2 2016 as benefits of easier DM monetary policy could be offset by rapid changes in DM capital flows.	A rise in DM fiscal policy responses should be supportive for risk asset prices which are already under pressure from a weak growth backdrop, though deteriorating fiscal positions could add further pressures to bond and FX markets, particularly in the event that rating downgrades materialise in H2 2016.	Fiscal policy measures increasingly focused on domestic economies as global measures become more difficult to coordinate against a backdrop of rising nationalist and protectionist sentiment. Governments under increasing pressure to support/ protect faltering export industries, raising the risks of policy mistakes.	The impact of the UK referendum result has led to the government abandoning plans to achieve a balanced budget by the end of the current parliament as further fiscal stimulus in H2 2016 looks increasingly likely. Japan has also committed to a significant fiscal stimulus program, details of which will be announced in H2 2016.
Emerging Markets	EMs have benefitted from stabilisation in China, a major trading partner and source of demand, which itself is looking a less likely source for a significant market dislocation in H2 2016. EM economic fundamentals continue to show signs of improvement going into H2 2016, but may face weakness in DM export demand in the wake of developments in Europe.	EM assets remain attractive vs DM on a relative valuation basis and as a source for the yield pick-up trade, but will remain vulnerable to sharp changes in capital flows, particularly in countries where weaker economic fundamentals persist. Selected domestic bond markets may benefit from scope for policy rate cuts in H2 2016.	Whilst the pause in the DM policy rate path for H2 2016 has increased the relative attractiveness of the EM assets, EM FX volatility remains particularly prone to the risk-off trade and may crowd out the asset class returns available. Eastern European EM markets unlikely to escape negative developments in post-UK referendum Europe.	The differentiated outcomes we have seen in the first half of the year are likely to persist throughout the remainder of the year and into 2017 as growth, inflation and policy dynamics continue to diverge. EM FX and economic fundamentals will be key determinants of EM investment outcomes in an environment where contagion risks are elevated.
"Tail Risk Monitor"	Political and economic risks have stepped up a level in H2 2016, as the journey towards a new British leadership, a new UK-European relationship and a new US president are just a few of the "known unknowns" that will unfold. Rising protectionist sentiment could see latest round of global trade deals derailed.	The elevated political and geopolitical risk environment raise the prospect of sharper sell offs and prolonged periods of elevated volatility across asset classes, as well as diminished benefits from diversification relationships that may have previously held. Weak corporate sector spending may slow even further.	Increased uncertainty and deteriorating fundamentals drive a pickup in defaults and/or rating agency downgrades, FX pegs come under increasing pressure following further DM policy action, geopolitical risks continue to skew political views and systemic risks threaten banking sector stability.	Liquidity risks to remain elevated across lower quality/less liquid asset classes in H2 2016, as risks of policy errors raise the probability of a prolonged sell-off period. Sharp changes in capital flows could see significant rallies in perceived safe haven assets, increasing pressure on policy makers to provide a response.

Key Charts: Economics and Markets

- Strong employment trends in the US continue to put upward pressure on wages.
- Core inflation readings are already above the 2% target of US policymakers.
- Global growth concerns against a strong US labor market place the Fed in a rates conundrum should inflation continue to trend upward.

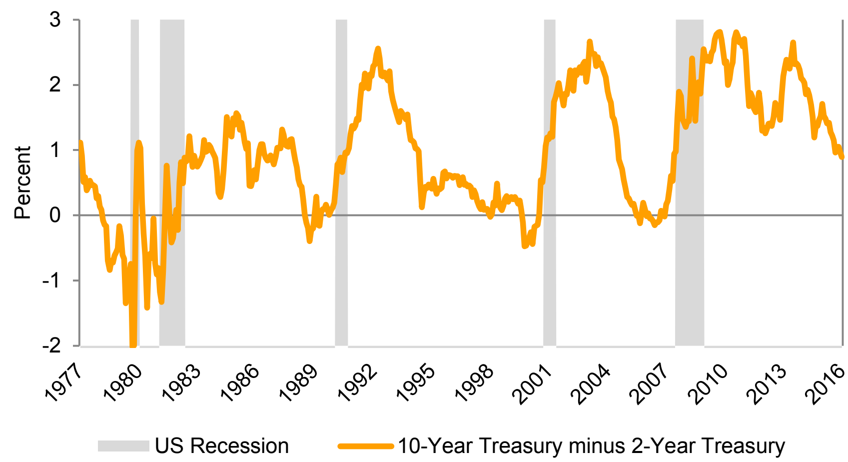
Fig. 2: Inflation pressure continuing to build



Source: Bloomberg, U.S. Bureau of Labor Statistics

- As the yield curve continues to flatten, bank profitability continues to come under pressure as does the credit cycle.
- We continue to watch the health of the overall credit cycle as fuel for the remainder of this economic cycle.
- Near term wage pressures as a result of continued employment strength may push short term rates higher and flatten the yield curve further.

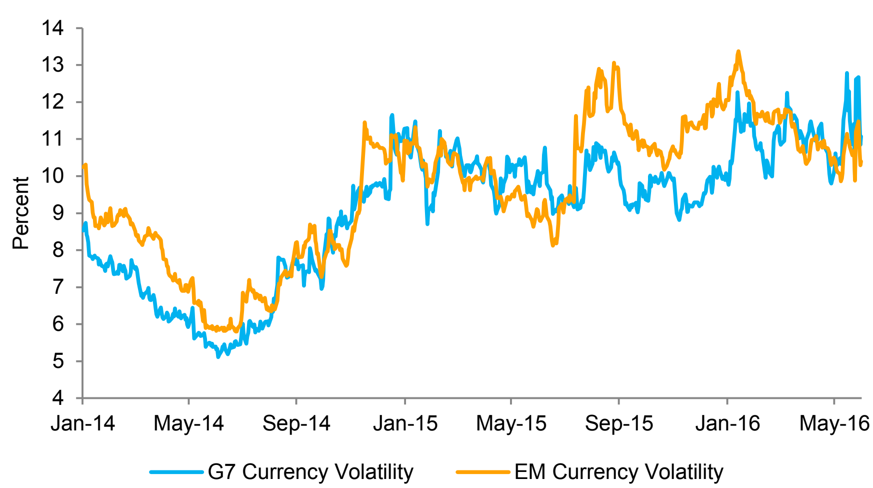
Fig. 3: Yield curve continues to flatten



Source: Bloomberg, The National Bureau of Economic Research

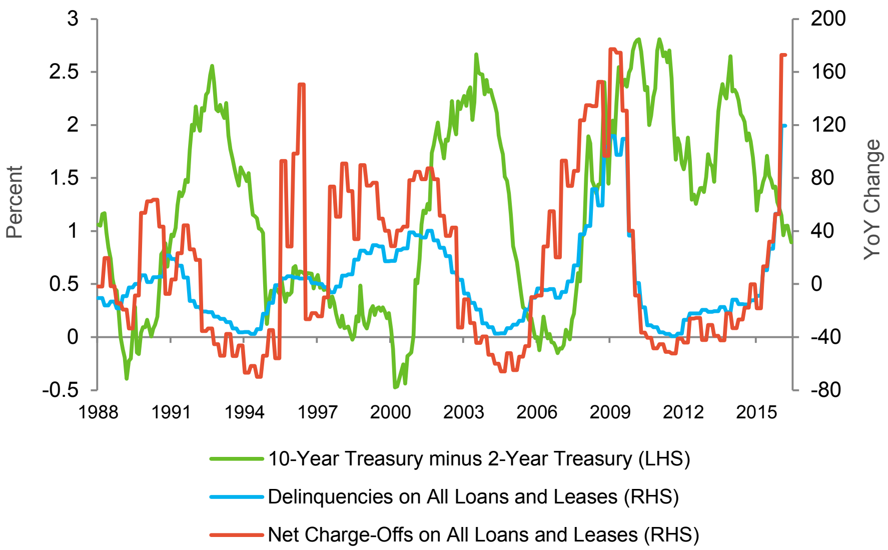
- With the onset of "Brexit" currency volatility has increased significantly in both developed and emerging markets.
- Interestingly, developed market currency volatility is significantly higher than that of emerging markets given the uncertain future of the EMU as well as the effectiveness of developed market monetary policy.
- Meanwhile, with negative revisions to inflation expectations in many emerging markets, policy may be finding traction as a precursor to growth.

Fig. 4: "Brexit" impacting global currency volatility



Source: Bloomberg

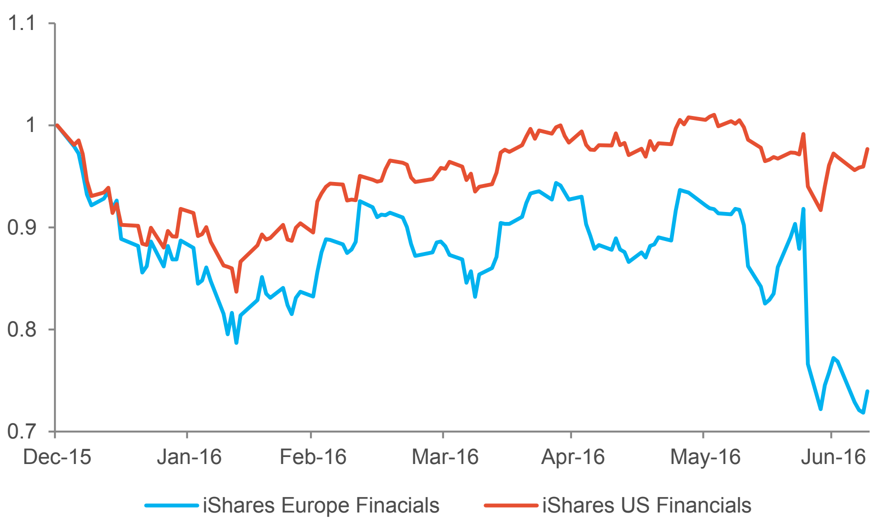
Fig. 5: Possible cracks in the credit cycle



Source: Bloomberg, Federal Reserve Bank of St. Louis

- Beyond the steepness of the yield curve we continue to watch the health of the credit cycle as fuel for the remainder of this economic cycle.
- Persistently low rates throughout this cycle have allowed leverage to be increased on a global basis against a global search for yield.
- As growth remains muted, defaults, charge-offs, and non-performing loans should be monitored closely.

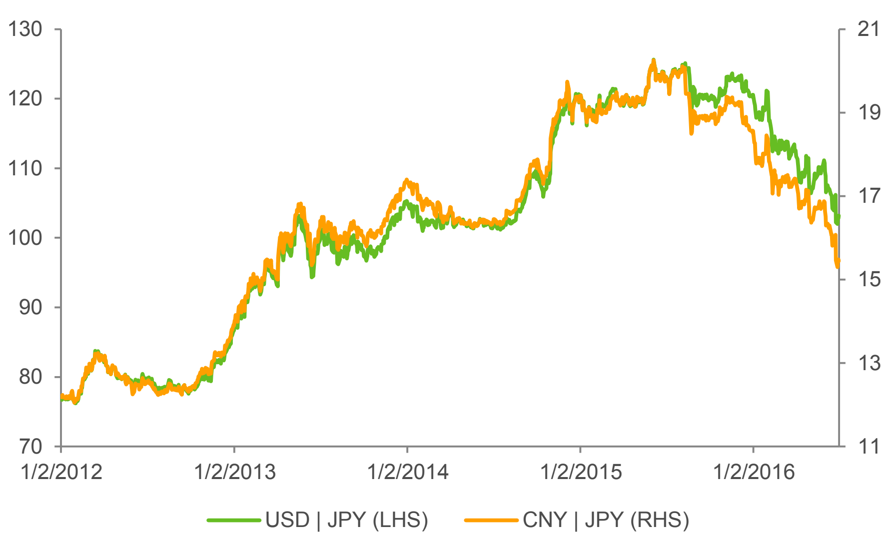
Fig. 6: European financials coming under pressure



Source: Bloomberg

- The threat of “Brexit” and its potential longer term impact have weighted on the European banking system.
- Continued uncertainty and concerns over the health of regional banks could cause further delay in lending, M&A, and business activity and put further stress on the regional banks which could serve to depress growth further.
- Attention should be paid to further updates on European Bank Stress tests.

Fig. 7: Asian currency dynamics intensifying



Source: Bloomberg

- The currency dynamics in the Asia-Pacific region continue to have global impact.
- Post “Brexit” the Yen has become a safe haven currency of choice in addition to the dollar and as a result has strengthened significantly despite policy efforts to depreciate it to spur exports.
- Simultaneously, the RMB continues to be pegged to a basket of currencies anchored, in part, by a strengthening USD.
- With both countries attempting to spur growth through exports, currency wars between China and Japan could have global implications.

Economic Outlook

Investor sentiment and economic developments in Q2 2016 were centered around two themes. The first was the reflation trade, spurred by the nascent recovery in commodities prices, simulative monetary policy globally, and exceedingly tight labor markets in the US. The second was political uncertainty. "Brexit" was the dominant question mark over most of Q2, however, there were other political motivations for the flight to safe havens, such as the winnowing US presidential candidate field and Spanish elections, as nationalist and populist sentiments rose to the forefront.

Indeed, with the conventional wisdom favoring "remain", the markets were ill-prepared for the "Brexit" outcome. European equities and GBP sold off hard on the exit vote, with ramifications felt in nearly all markets globally. Since June 23, many markets have repaired themselves, with the US equity market fully recovered and making new highs. Still, there are lingering doubts about the durability of the market rally for a number of fundamental reasons, namely weak global demand, lack of fiscal stimulus & capex spending, commodities overcapacity, and lofty valuations on the backs of low-to-negative interest rates.

As we enter H2 2016, most of these concerns remain in place against the backdrop of sluggish global growth and tepid inflation. The erratic nature of some short-horizon data points has led to market overreactions in either direction, as we see in the probabilities of Fed rate hikes after each most recent employment report. Yet, overall, global growth and inflation expectations & revisions showed little change from their trajectory one quarter ago (Figs. 8 & 9). Global GDP growth is forecast modestly above the critical 2% level, with only a marginal uptick in growth expectations. Indeed revision to this growth forecast remains biased to the downside, as we await clarity on growth prospects in a post-"Brexit" Europe which was already facing numerous headwinds given anemic growth, weak demographics, the ECB's inability to spark inflation, and banking woes from Non-Performing Loans and negative rates.

As we look regionally (Fig. 10), in the US, GDP forecasts are improving and inflation expectations are stabilizing as the reflation in energy prices appears to be taking a pause, and the one-time effects of a low base slowly work their way out of year-on-year comparisons. While in Japan, inflation expectation revisions turned strongly negative, yet GDP estimate revisions are starting to tick upward. Finally among the EM BRICs, we see revisions to expected GDP slowing down, and revisions to inflation expectations picking up as a function of commodities and currency.

Fig. 8: Expected Global Growth and Growth Revisions

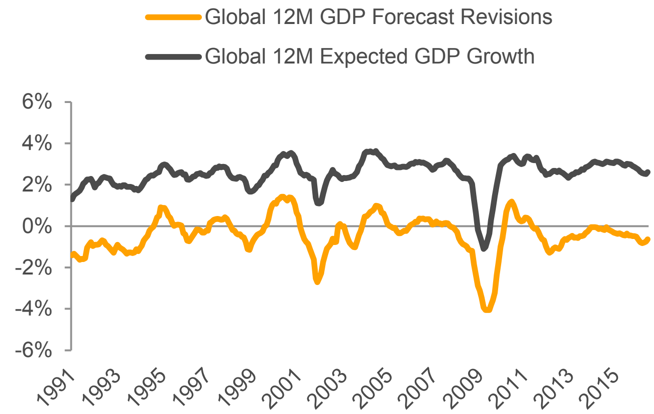


Fig. 9: Expected Global Inflation and Inflation Revisions

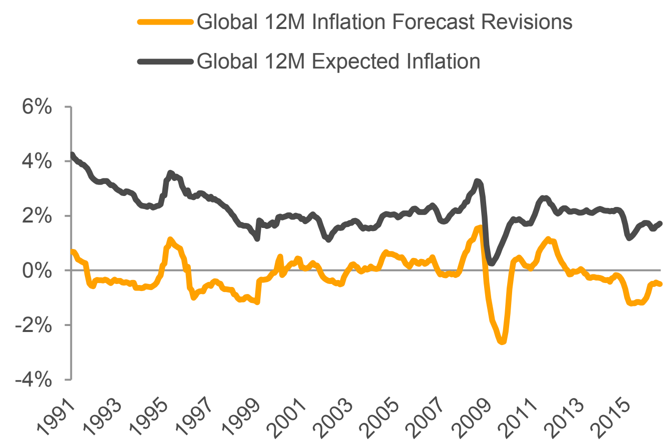
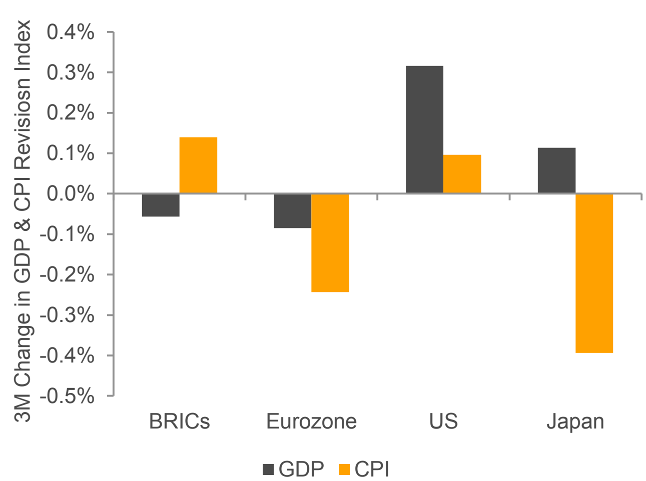
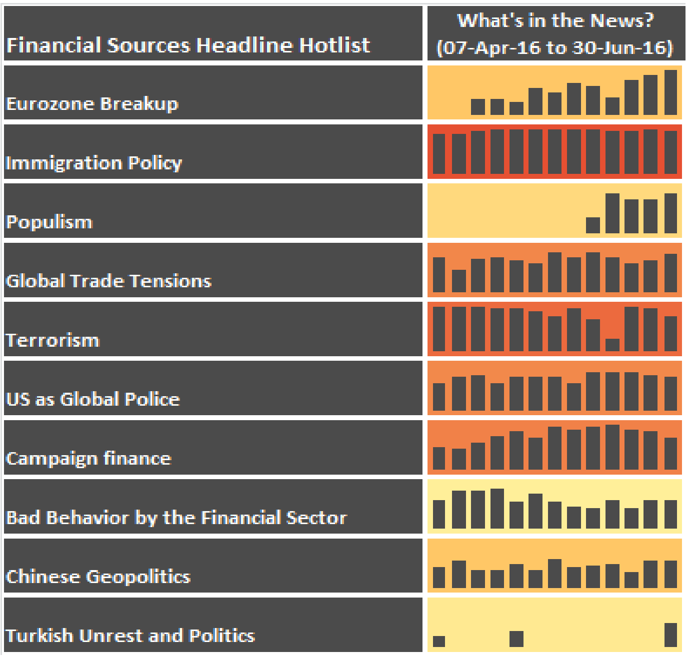


Fig. 10: Quarterly Regional Revisions For Growth and Inflation Forecasts



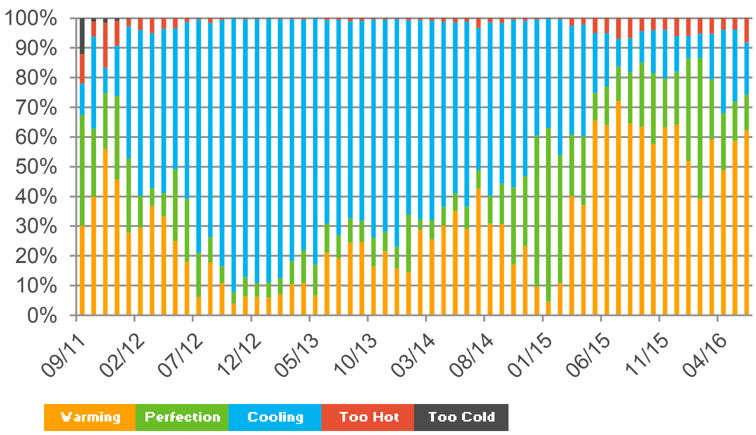
Source for Fig. 8,9,10: Consensus Economics, ISSG

Fig. 11: Global Headline Hotlist



The above graphic shows the top ten most mentioned themes that are relevant to financial markets in order of their ranking on June 30, 2016. The bar height shows the frequency of the coverage of each theme in the news for each of the last 13 weeks, with the furthest right bar representing the most recent ranking. The color of the background denotes the average intensity over the past quarter. Using financial media and influential blogs identified by multiple teams at BNY Mellon, those stories are used to highlight the hottest topics each week across over 3,000-6,000 news items. Story summaries are classified using a Bayesian classifier which is trained on stories from the last six months. Training stories are manually tagged and classified by a senior strategist.

Fig. 12: RBAA* Regime Probabilities



Source ISSG as of 30 June 2016

*Regime Based Asset Allocation (RBAA) is a proprietary asset allocation model created by the ISSG which considers asset returns in the context of regimes created by underlying changes in growth and inflation expectations. Contact the ISSG for detailed information on this research. Please see appendix for information regarding regime categories.

In our proprietary analysis of news flow – the Global Headline Hotlist (Fig. 11) – we have seen a steady build-up of news around the sustainability of the Eurozone and speculation of follow-on exit votes from other members. Indeed this topic dominates the current news volume, with immigration policy, rising populist sentiment, and global trade tensions all highly-ranked in terms of news flow. Global trade tensions cover multiple trending topics which are expected to persist, including post-"Brexit" trade renegotiations, the South China Sea dispute, and competitive currency dynamics. Stories around financial impropriety and Chinese politics have slowed somewhat over the quarter. Based on the recent outcome by the international tribunal in the Hague around China's island building efforts, expect to see renewed "sabre rattling" and consequent geopolitical concerns once again originating out of the region.

Our Regime Probability Outlook (Fig. 12) is indicating growing probability for both the "warming" and "too hot" regimes. While the probability of "too hot" is quite minimal, the "warming" regime is clearly dominating and this is to be expected given the recovery in commodities prices, tight labor markets, currency biases, and accommodative policy stances that are currently at work across the global economy. It remains to be seen if all these forces will persist as robustly into 2017, especially as the year-on-year base effects of low commodities prices work their way out of comparisons and global demand fails to materialize in light of realignments in Europe, political change, or a yet unknown left tail event. It is also interesting to note that the probability of "perfection" has largely diminished, while the "cooling" regime probability has expanded slightly in the past year. This indicates that conditions are poised for a binary economic outcome to one side of the range or the other, rather than a "goldilocks" scenario of renewed growth amid low inflation. These binary environments, as we are currently observing, are typically favorable toward diversification and "barbell" positioning as they benefit from asymmetrical returns under bi-modal outcomes, with less risk than a one-way directional bet.

Asset Class Outlook

Global Equity Markets:

	ISSG CMC View	Valuation Model	Momentum Model	RBAA Model	
US Equity	Overweight	Favorable	Favorable	Favorable	The active overweight in US equity continues to decline. While continued strength in employment should support consumer activity, global growth concerns and the headwind of a stronger dollar merit the reduction in weight.
Europe ex-UK Equity	Neutral	Favorable	Favorable	Favorable	The "tug-of-war" between expected policy responses from the ECB in the aftermath of the "Brexit" vote contrasted with growing uncertainty as to the Eurozone's future keep us at neutral. Growing concerns in the Italian banking sector and pending elections in Italy as well as other countries only add to the uncertainty going forward.
Pacific ex-Japan Equity	Neutral	Favorable	Favorable	Neutral	The overarching theme in the region continues to be the state of Chinese economic growth and resulting currency impacts from policy actions by regional central banks or expectations thereof. The dollar being seen as a "safe haven" currency could add pressure to commodity sensitive countries.
Japan Equity	Neutral	Favorable	Unfavorable	Unfavorable	Japan remains neutral. The BOJ remains in a difficult position with inflation running below target despite policy efforts. Given uncertainty from "Brexit", the Yen is being seen as a "safe haven" currency and thwarting depreciation attempts from the BOJ.
UK Equity	Neutral	Favorable	Neutral	Favorable	We remain at neutral in the UK for similar reasons as Europe with a "tug-of-war" between expected policy responses from the BOE in the shadow of "Brexit" and the uncertainty of what the implications of an exit from the Eurozone might be. Inflation expectations have been accelerating given the depreciation in the Sterling.
EM Equity	Neutral	Favorable	Neutral	Favorable	A dramatic reduction in the expectations for rate hikes in the US has reignited the "search for yield" and eased the pressure on capital outflow from EM countries despite the recent strength in the USD. Despite these developments, we remain neutral given ever present fundamental concerns in Latin America and China.
REIT Equity	Neutral	Neutral	Favorable	Favorable	We remain neutral to REITs as the yield spread differential with Treasuries remains at more normalized levels. With US policy makers sounding more dovish, the asset class should benefit from a momentum tailwind as investors search for yield once again. Although, such a move would pressure valuations.
Global Natural Resource Equity	Neutral	Favorable	Unfavorable	Unfavorable	While valuations of the sector remain attractive given the sell off in commodities during this market cycle, the supply / demand dynamics going forward keep us at neutral. Capacity across the entire commodity complex has been rationalized but a strengthening dollar post "Brexit" combined with global growth that may be slowing, also post "Brexit", create significant headwinds despite the capacity reductions.

Fig. 13: ISSG CMC Global Asset Class Views

ASSET CLASS	*ISSG VIEW*
Global Equities	**+0.4%**
U.S.	O/W
Europe Ex U.K.	Neutral
Pacific Ex-Japan	Neutral
Japan	Neutral
U.K.	Neutral
EM	Neutral
REITS	Neutral
Global Natural Res.	Neutral
Global Bonds	**-4.8%**
U.S. Sovereign Debt	U/W
U.K. Sovereign Debt	U/W
Japanese Sovereign Debt	U/W
German Sovereign Debt	U/W
Inflation Linked Bonds	O/W
High Yield	Neutral
U.S. IG Corp. Bonds	O/W
EM Local Cur. Debt	Neutral
EM USD Sovereign Debt	Neutral
Cash	**+4.4%**

Fig. 14: Global Equity Index Performance
% change vs MSCI AC World Index over 3 months to 30 Jun 16

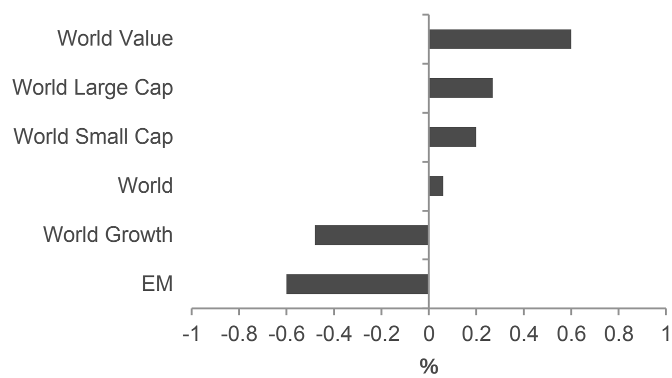


Fig. 15: Country Index Performance
% change over 3 month to 30 Jun 16

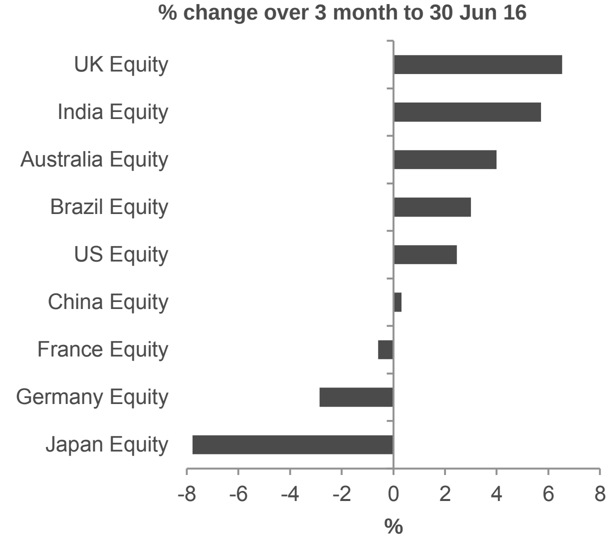


Fig 14, 15 Source: Thomson Reuters Datastream & ISSG

Fig. 16: Fixed Income Performance
% change over 3 months to 30 Jun 16

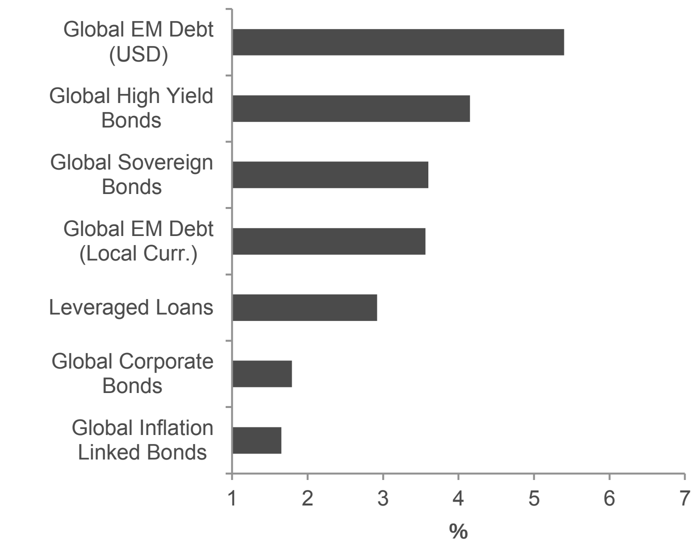


Fig.17: Commodities Performance
% change 3 month to 30 Jun 16

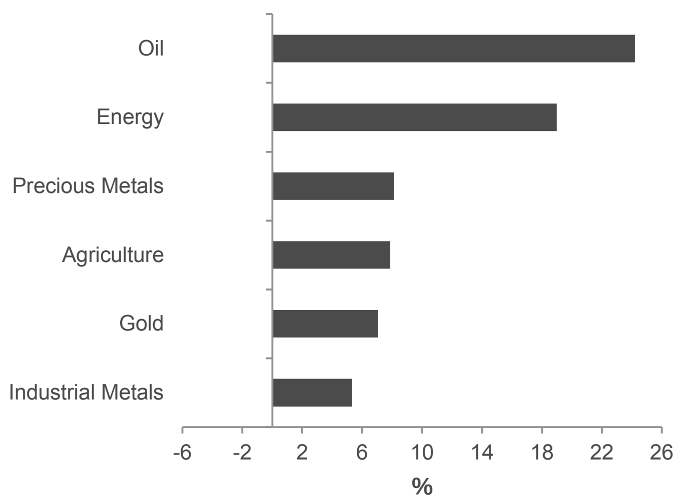


Fig. 18: FX Currency Pairs
% change 3 months to 30 Jun 16

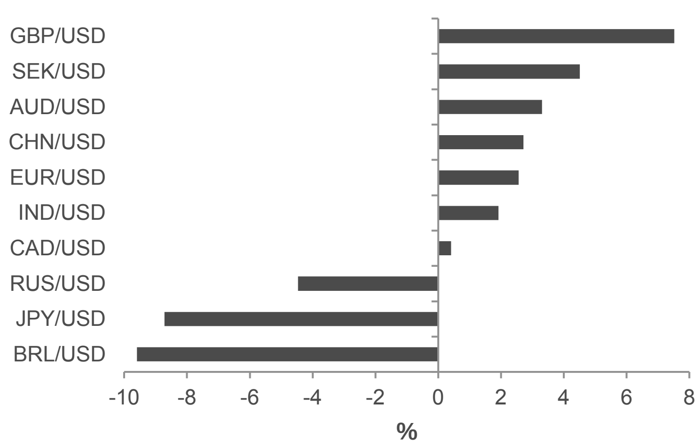


Fig 16, 17, 18 Source: Thomson Reuters Datastream & ISSG

Global Bond Markets:

	ISSG CMC View	Valuation Model	Momentum Model	RBAA Model
Developed Sovereign Bonds	U/W / Neutral	Unfavorable	Favorable	Unfavorable
	Significant portions of global sovereign debt have moved into negative yielding territory. Yet, given the post-"Brexit" landscape and uncertainty that exists because of the historic vote we move to a neutral in US treasuries as part of a portfolio risk reduction.			
Inflation Linked Bonds	Overweight	Neutral	Favorable	Neutral
	We remain overweight inflation-linked bonds and continue to prefer them to nominal bonds given the inflation adjusted capital preservation they offer portfolios at this point in an economic cycle.			
High Yield Bonds	Neutral	Favorable	Favorable	Unfavorable
	We remain neutral to high yield bonds given the uncertain landscape going forward globally. While oil prices appear to have stabilized, overall growth remains questionable at this point in the credit cycle.			
Investment Grade Corporate Bonds	Overweight	Unfavorable	Neutral	Unfavorable
	We move to overweight in investment grade bonds. Recent issuances have moved spreads out relative to their high yield counterparts. The credit quality in the sector combined with a spread component continue to make these bonds an attractive alternative to sovereign bonds.			
Emerging Markets – Local Currency Bonds	Neutral	Favorable	Unfavorable	Neutral
	EM currencies have weathered the "Brexit" storm relatively well and have remained stable. Capital flows pressure appears to have eased as well despite a strengthening dollar as investors look to the sector for yield. Non-financial corporate debt in China remains a concern.			
Emerging Markets – USD Bonds	Neutral	Unfavorable	Favorable	Favorable
	We remain neutral on EM dollar based debt. The dollar should continue to exhibit positive momentum as a safe-haven currency in the post "Brexit" market landscape which will be supportive of EM hard currency debt. While Russia appears to have stabilized given higher oil prices, Brazil remains a key concern for us. Post Olympics will be a critical time for Brazil to demonstrate growth.			
Cash	Overweight	N/A	N/A	N/A
	We have increased our cash overweight since last quarter. Preservation of capital remains paramount and given negative yields in many sovereign bonds cash remains a good liquid preservation vehicle for rapidly changing market dynamics.			

Commodities:

	Neutral
	We remain neutral to the commodity complex as the supply/demand picture for the asset class remains opaque. As mentioned previously, capacity reductions are helping to alleviate the supply overhang across the complex but questionable growth sustainability in China and stronger dollar are negatives for the demand picture.

Currency:

EUR/USD	Underweight
	Given the substantial role that the UK played in the European Monetary Union, we believe the Euro will continue to come under pressure due to the UK's exit and possible exit of other countries in the future.
JPY/USD	Neutral
	The Yen remains in a tough dichotomy between a "safe-haven" currency and a currency that is trying to be weakened by policy makers to spur export lead growth in Japan. For this reason we remain neutral.
EM: Asia/USD	Neutral
	Chinese economic policy continues to dominate the landscape of both EM Asia currencies, but also the Asia/Pacific region broadly. The RMB remains at its lowest point to the currency basket peg in several years thanks in large part to a strengthening dollar.
EM: LATAM/USD	Neutral
	Brazil contributes nearly half of the regional GDP to Latin America. The recent run in the Real, for us, lacks any fundamental catalyst. The search for yield will provide near term support to the region.

ISSG Global Heatmaps

Fig. 19: ISSG Global Macroeconomic Heat Map

Global Macroeconomic Heatmap (Last 3 years as of 30-Jun-16)	Inflation	Inflation Revisions	Growth (PMI)	Growth Revisions	Monetary Policy	Surprise vs. Consensus	Company Earnings
United States	1.0%	-0.6%	51.3	-0.7%	-0.2	-19.8	4%
United Kingdom	0.3%	-0.7%	50.1	-0.5%	-0.5	12.5	13%
Eurozone	0.1%	-0.9%	52.6	-0.2%	-0.7	5.0	4%
Japan	-0.4%	-1.2%	48.1	-0.9%	0.9	24.9	-16%
Brazil/Latam	9.3%	1.7%	41.6	-3.7%	0.5	36.8	4%
Russia/CEEMEA	7.3%	0.0%	49.6	-1.2%	0.0	-15.2	20%
India/Asia Pacific	0.8%	-0.5%	50.7	-0.5%	-0.2	-19.2	-24%
China	2.0%	-0.1%	50.0	-0.2%	-0.3	-36.5	-35%

This heat map is designed to display a wide spectrum of macroeconomic trends across the major global regions over the past three years. Green and red shading indicate what we believe to be positive and negative levels, respectively, of the indicated variables; while green and red borders indicate positive and negative changes over the last quarter. Yellow shading indicates neutral readings. The time series lines are shown merely for ease of comparing trends, and are not meant to convey any particular values or levels. See appendix for series definitions and sources.

As we head into the third quarter of 2016, there are several interesting developments in observing the ISSG Global Macroeconomic Heat map (Fig. 19). Revisions to inflation expectations have turned decidedly negative across the Eurozone and Japan despite significant policy efforts to increase the level of inflation in those countries. In contrast, inflation revisions have also turned negative in parts of emerging markets, namely Brazil and Russia, indicating a possible easing in inflationary pressures as a result of currency depreciation in addition to policy traction. Revisions to economic growth expectations have stabilized across much of the developed world in comparison to last quarter. Negative sentiment that was weighing on both global and regional growth outlooks heading into Q2 has been reduced which is commensurate with the rally in global equity markets and supportive policy expectations.

Fig. 20: ISSG Global Correlation Heat Map

Global Correlation Heatmap (Last 3 years as of 30-Jun-16)	World Equity	EM Equity	DM Bonds	EM $ Bonds	DM IG Corps Hedged	DM HY Corps Hedged	Commod	Dollar
World Equity	14.3%	0.80	-0.33	0.49	-0.05	0.67	0.45	-0.07
EM Equity		15.0%	-0.25	0.60	0.09	0.69	0.51	-0.17
DM Bonds			2.9%	0.12	0.76	-0.19	-0.25	0.06
EM $ Bonds				6.7%	0.42	0.72	0.40	-0.24
DM IG Corps Hedged					3.3%	0.31	-0.02	-0.03
DM HY Corps Hedged						6.0%	0.49	-0.15
Commod							14.3%	-0.45
Dollar								7.6%

The Global Correlation Heatmap is designed to convey levels and changes in correlation and volatility numbers across major asset classes. Numbers in the unshaded cells represent the current exponentially weighted volatility level, with green and red fonts representing low and high levels relative to a time-weighted 3 year mean. The lower left half of the Heatmap, displaying exponentially-weighted weekly correlation pair data for the last 3 years, is included to allow users to compare trends and is not meant to convey any particular values or levels. The upper right half of the Heatmap reflects the current observation for the same data series. Green and red shading indicate what we believe to be low and high levels, respectively, of the current observation relative to a time weighted 3 year mean, while green and red borders indicate a significant decrease or increase over the last quarter.

With interest rates around the world moving into lower, and even negative, territory the continued search for yield in having an impact on this quarters Global Correlation Heat map (Fig. 20). Correlations across much of the high yield credit, equity, and emerging markets have increased given investor need to move further out on the risk spectrum in order to generate needed yield and/or return. As a result, the diversification benefits of credit and emerging markets, both equity and debt, are continuing to decrease within portfolios as these asset classes continue to exhibit increasing positive correlations. In contrast, the diversification benefits of developed market bonds with high yield bonds continues to increase as investors seek safe haven assets to off set the need for increased risk across portfolios and developed market bonds play such a role.

Performance Monitor

Fig. 21: Capital Markets
% change over 1 year to 30 Jun 16

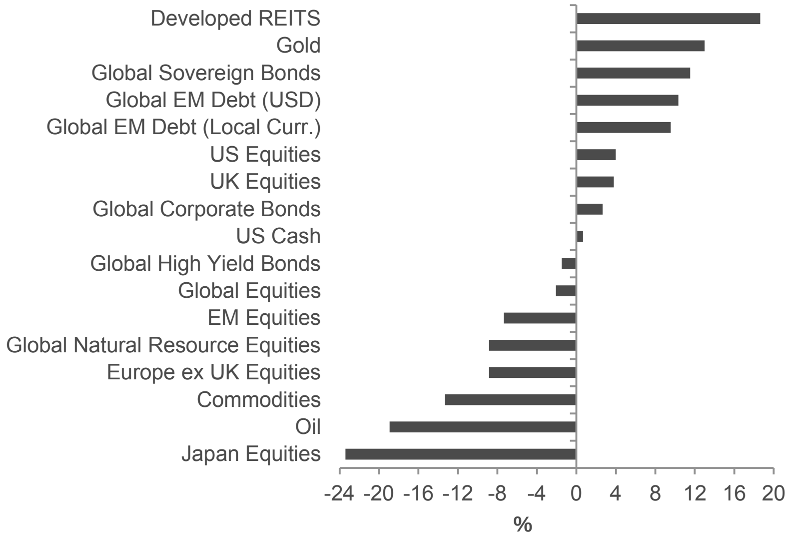


Fig. 22 : Equity Country Index Performance
% change over 1 year to 30 Jun 16

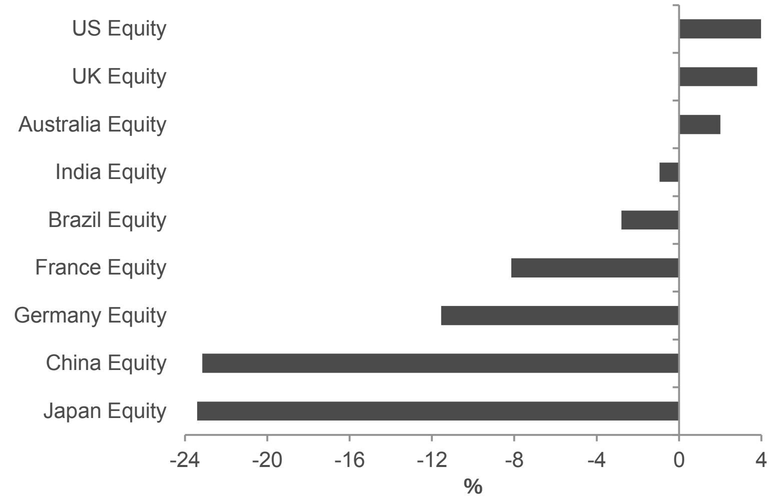


Fig. 23: Global Equity Index Performance
% change vs MSCI AC World Index over 1 year to 30 Jun 2016

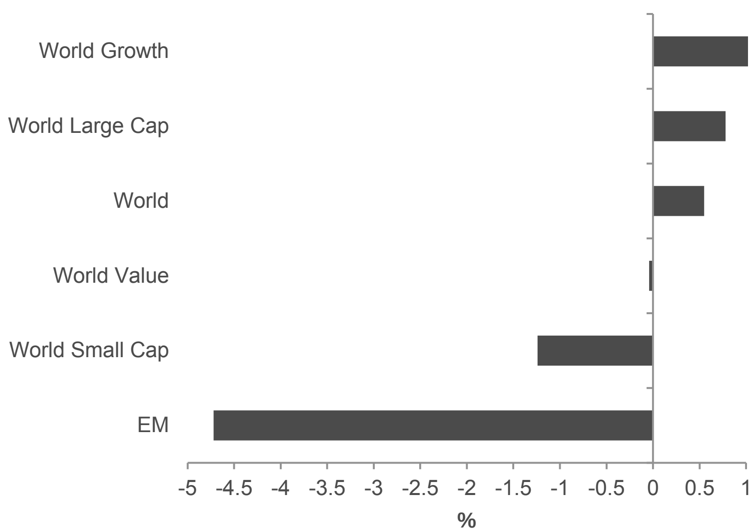


Fig. 24: Fixed Income Performance
% change over 1 year 30 Jun 16

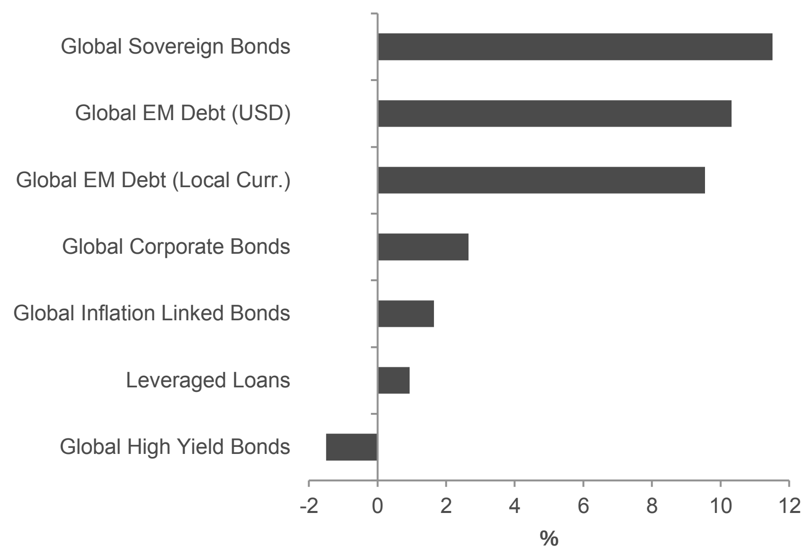


Fig. 25: Commodities Performance
% change 1 year to 30 Jun 16

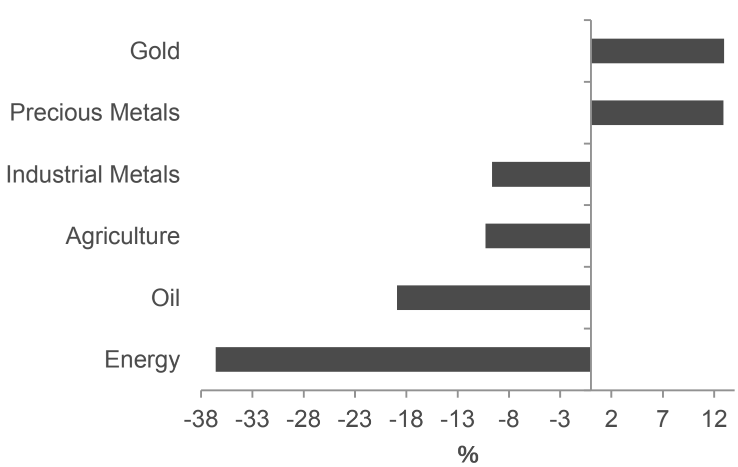
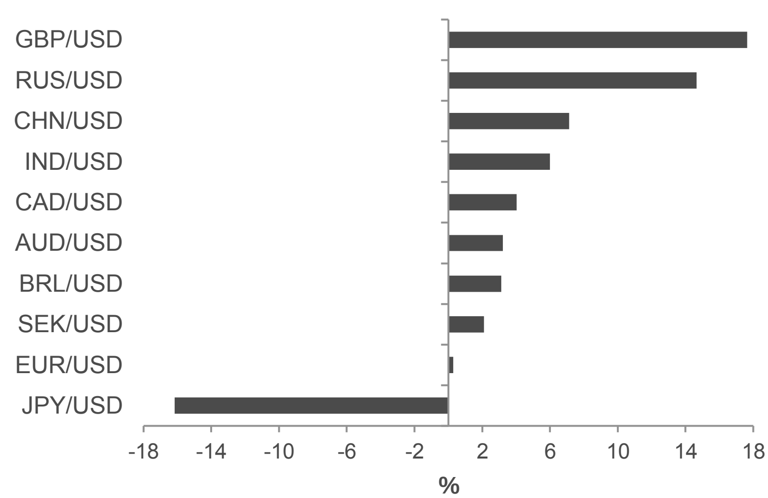


Fig. 26: FX Currency Pairs
% change 1 year to 30 Jun 16



Figs. 21, 22, 23, 24, 25, 26 Source: Thomson Reuters Datastream & ISSG

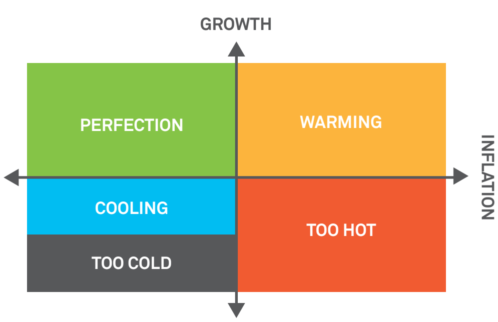
Appendix & Disclosures

ASSET	INDEX	DEFINITION
Commodities	Bloomberg Commodities Index Total Return (USD Index)	The Bloomberg Commodities index is an index that tracks the performance of broad based commodities.
Gold	Gold Bullion LBM USD/ozt	Tracks the performance of gold bullion spot prices.
Oil	Brent Crude Month FOB USD/BBL	Tracks the performance of Brent Crude Oil spot prices.
Global Sovereign Bonds	JPM Global GBI (USD Index)	Tracks the performance of global sovereign bonds.
Developed Sovereigns		US, UK, Japan, and German Sovereign Debt securities
US Equity	S&P 500 (USD Index)	Tracks the performance of 500 of largest market capitalization equities in the United States.
US Cash	JPM US Cash Index (3M) (USD Index)	Tracks the performance of US 3 month treasury bills.
US Dollar	JPM USD Index Real Broad	Tracks the performance of the US Dollar against a basket of broad currencies.
Global Corporate Bonds	Barclays Global Agg Corp (USD Index)	Tracks the performance of aggregate corporate bonds.
Developed REITS	FTSE E/N Dev REITS (Local Currency)	Tracks the performance of global real estate investment trusts in developed markets.
Global Natural Resource Equities	S&P Gbl Nat Resource Equities (USD Index)	Tracks the performance of global equities linked to natural resources.
Global Investment Grade Bonds	Barclays Inv Grade Corporates (USD Index)	Tracks the performance of aggregate investment grade corporate bonds.
Global Inflation Linked Bonds	Barclays Global Agg Infl-Lkd (USD Index)	Tracks the performance of global inflation linked bonds.
Global High Yield Bonds	Barclays Global High Yield (USD Index)	Tracks the performance of global high yield bonds rates below investment grade.
Global Equities	MSCI World (LC Index)	Tracks the performance of developed market global equities.
MSCI AC World	MSCI AC World Index	Tracks the performance of developed market global equities
Global EM Debt (USD)	JPM EMBI Global Composite (USD Index)	Tracks the performance of dollar based emerging market sovereign bonds.
EM Equities	MSCI Emerging Markets (LC Index)	Tracks the performance of emerging market equities.
UK Equities	FTSE 100 (LC Index)	Tracks the performance of equities domiciled within the United Kingdom.
Europe Ex UK Equities	MSCI Europe ex UK (LC Index)	Tracks the performance of equities domiciled in Europe and not including the UK.
Japan Equity	MSCI Japan (LC Index)	Tracks the performance of equities domiciled in Japan.
Pacific Ex Japan Equity	MSCI Pacific ex Japan (LC Index)	Tracks the performance of equities domiciled in the Asia - Pacific region but not including Japan.
Germany Equity	DAX 30 (LC Index)	Tracks the performance of 30 of largest equity market capitalization companies in Germany.
Eurozone Equity	EuroStoxx 50 (LC Index)	Tracks the performance of 50 of largest equity market capitalizations in the Eurozone.
France Equity	CAC 40 (LC Index)	Tracks the performance of 40 of the largest equity market capitalizations of France.
Australia Equity	ASX All Ordinaries (LC Index)	Tracks the performance of the largest equity market capitalizations of Australia.
Brazil Equity	MSCI Brazil (LC Index)	Tracks the performance of the equities domiciled in Brazil.
India Equity	MSCI India (LC Index)	Tracks the performance of equities domiciled in India.
China Equity	MSCI China (LC Index)	Tracks the performance of equities domiciled in China.
World Growth	MSCI World Growth (LC Index)	Tracks the performance of growth oriented equities as defined by MSCI.
World Large Cap	MSCI World Large Cap (LC Index)	Tracks the performance of large equity market capitalization companies.
World Value	MSCI World Value (LC Index)	Tracks the performance of value oriented equities as defined by MSCI.
World Small Cap	MSCI World Small Cap (LC Index)	Tracks the performance of small equity market capitalization companies.
Leveraged Loans	S&P Leveraged Loan Index (USD Index)	Tracks the performance of leveraged loans.
Global EM Debt (Local Curr.)	JPM GBI Emerging Markets (LC Index)	Tracks the performance of local currency denominated emerging market bonds.
Agriculture	S&P GSCI Agriculture Total Return (USD Index)	Tracks the total return performance of agricultural commodity futures.
Precious Metals	S&P GSCI Precious Metals Total Retn	Tracks the total return performance of futures for precious metals related futures.
Industrial Metals	S&P GSCI Industrial Metals Total Retn (USD Index)	Tracks the total return performance of futures for industrial metals related commodities.
Energy	S&P GSCI Energy Total Return (USD Index)	Tracks the total return performance of futures for energy related commodities.
EUR/USD	EUR/USD	Tracks the performance of the Euro / US Dollar exchange rate.
RUS/USD	RUS/USD	Tracks the performance of the Russian Ruble / US Dollar exchange rate.
CHN/USD	CHN/USD	Tracks the performance of the Chinese Renminbi / US Dollar exchange rate.
SEK/USD	SEK/USD	Tracks the performance of the Swedish Krona / US Dollar exchange rate.
GBP/USD	GBP/USD	Tracks the performance of the British Pound / US Dollar exchange rate.
AUD/USD	AUD/USD	Tracks the performance of the Australian Dollar / US Dollar exchange rate.
BRL/USD	BRL/USD	Tracks the performance of the Brazilian Real / US Dollar exchange rate.
CAD/USD	CAD/USD	Tracks the performance of the Canadian Dollar / US Dollar exchange rate.

ASSET	INDEX	DEFINITION
IND/USD	IND/USD	Tracks the performance of the Indian Rupee / US Dollar exchange rate.
JPY/USD	JPY/USD	Tracks the performance of the Japanese Yen / US Dollar exchange rate.
EM LATAM/USD		Considers the aggregate performance direction of a basket of currencies from Latin American countries as defined in the JPM GBI Emerging Markets Index
EM Asia/USD		Considers the aggregate performance direction of a basket of currencies from Asian countries as defined in the JPM GBI Emerging Markets Index
EUR FX		Tracks the performance of the Euro / US Dollar exchange rate.
GBP FX		Tracks the performance of the British Pound / US Dollar exchange rate.
JPY FX		Tracks the performance of Japanese Yen / US Dollar exchange rate.
EM FX		Tracks the performance of a basket of Emerging Markets currencies versus the US Dollar.
US 10Y Yield		Tracks the performance of the yield on the 10 year US treasury note.
Inflation	Headline Consumer Price Index	Tracks the performance of inflation as reported by respective national economic statistics bureaus.
Growth (PMI)		Tracks the performance of purchasing managers indices in each country to proxy GDP growth.
Company Earnings		A proprietary diffusion index of positive and negative analyst earnings estimate revisions.
Monetary Policy		Derived from the futures curve for short term interest rates as indicative of central bank policy.
Inflation Revisions		A proprietary measure of cumulative economist revisions for future levels of inflation in a country.
Growth Revisions		A proprietary measure of cumulative economist revisions for future real economic growth in a country.
US 10 Year Treasury	USGG10YR Index	Tracks the performance of the US 10 Year Treasury Index.
US 2 Year Treasury	USGG2YR Index	Tracks the performance of the US 2 Year Treasury Index.
US Recession		A significant decline in economic activity spread across the economy, lasting more than a few months, normally visible in real GDP, real income, employment, industrial production, and wholesale-retail sales.
Wage Growth	WDTROVER	Atlanta Fed Wage Growth Tracker Overall.
Federal Funds Rate	FDTR	Federal Funds Target Rate is interest rate at which depository institutions (banks and credit unions) lend reserve balances to other depository institutions overnight, on an uncollateralized basis.
Core CPI		Core Consumer Price Index (CPI) is equal to CPI minus energy and food prices and is used to measure core inflation.
G7 Currency Volatility	JPMVXYG7 Index	Tracks volatility of G7 currencies calculated based on currency 3 month ATMF vols which are combined with a set of fixed weights to produces the daily result.
EM Currency Volatility	JPMVXYEM Index	Tracks volatility of emerging market currencies calculated based on currency 3 month ATMF vols which are combined with a set of fixed weights to produces the daily result.
Delinquencies on All Loans and Leases	DALLCIACBEP	Delinquencies on All Loans and Leases, Commercial and Industrial, All Commercial Banks, Millions of Dollars, Quarterly, Not Seasonally Adjusted.
Net Charge-Offs on All Loans and Leases	NCOALLCIACB	Net Charge-Offs on All Loans and Leases, Commercial and Industrial, All Commercial Banks, Millions of Dollars, Quarterly, Not Seasonally Adjusted.
iShares MSCI Europe Financials	EUFN Equity	The ETF seeks results that correspond to the performance of the MSCI Europe Financial Sector.
iShares US Financials	IYF Equity	The ETF seeks investment results that correspond to the performance of the Dow Jones US Financial Sector Index.
CNY/JPY	CNYJPY Curncy	Tracks the performance of the Chinese Yuan / Japanese Yen exchange rate.

These benchmarks are broad-based indices which are used for comparative purposes only and have been selected as they are well known and are easily recognizable by investors. Comparisons to benchmarks have limitations because benchmarks have volatility and other material characteristics that may differ from the portfolio. For example, investments made for the portfolio may differ significantly in terms of security holdings, industry weightings and asset allocation from those of the benchmark. Accordingly, investment results and volatility of the portfolio may differ from those of the benchmark. Also, the indices noted in this presentation are unmanaged, are not available for direct investment, and are not subject to management fees, transaction costs or other types of expenses that the portfolio may incur. In addition, the performance of the indices reflects reinvestment of dividends and, where applicable, capital gain distributions. Therefore, investors should carefully consider these limitations and differences when evaluating the comparative benchmark data performance. The foregoing index licensers are not affiliated with The Bank of New York Mellon Corporation, do not endorse, sponsor, sell or promote the investment strategies or products mentioned in this presentation and they make no representation regarding advisability of investing in the products and strategies described herein. Valuation Model – The ISSG Valuation Model considers relative valuations across the asset classes that we rank. We consider the current values placed on future cash flows of the securities against their historical longer-term trend levels. Momentum Model – The ISSG Momentum Model considers relative price momentum across the asset classes that we rank. Our research shows that this can be an indicator of continued appreciation potential in the future. RBAA Model – The ISSG Regime Based Asset Allocation Model defines five macroeconomic regimes based on the interaction of growth and inflation expectations. We believe changes to these expectations drive regime shifts and influence asset returns.

BNY ISSG RBAA Regimes:



CORRELATION HEAT MAP DEFINITIONS

ASSET CLASS	INDEX — please see above for definitions
World Equity	MSCI AC World (LC Index)
EM Equity	MSCI Emerging Markets (LC Index)
DM Bonds	JPMorgan GBI Global Unhedged
EM $ Bonds	JPMorgan EMBI Global Composite (USD Index)
DM IG Corps Hedged	Barclays Global Aggregate Corp Index (USD Index)
DM HY Corps Hedged	Barclays Global High Yield (USD Index)
Commodities	Dow Jones – UBS Commodities Index Total Return (USD Index)
Dollar	US Dollar Index

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