

# UBS House View

*Investment Strategy Guide*

September 2016

CIO Wealth Management Research

**US edition**



## The bright side of Brexit?

**In Context:** The morning after

**In Focus:** As the consumer turns

**Videos:** Rob Samuels on the consumer and Mike Ryan on US elections

- 1 Tactical preferences**
- 2 Feature**  
The bright side of Brexit?  
by Mark Haefele
- 8 In context**  
The morning after  
by Mike Ryan
- 10 Preferred investment views**
- 11 At a glance**
- 11 Month in review**
- 12 Top themes spotlight**  
Golden years for Baby Boomers  
by Laura Kane and Stephen Freedman
- 14 Global economic outlook**
- 16 Asset classes overview**  
Equities  
Fixed income  
Commodities  
Foreign exchange
- 22 In focus**  
As the consumer turns  
by Rob Samuels and Brian Rose
- 24 Top themes overview**
- 26 Key forecasts**
- 27 Detailed asset allocation**
- 34 Performance measurement**
- 37 Appendix**
- 41 Publication details**



## Dear reader,

In our conversations with investors, we find that confusion has now given way to outright bewilderment. How, many clients asked us, can we see markets continue to reach new all-time highs even as the US is poised to choose between two presidential candidates with negative approval ratings, the UK has opted for a historical split from the rest of Europe, and nearly half of developed world sovereign debt trades at interest rates below 0%?

Into this age of anxiety comes this month's Investment Strategy Guide, emerging just in time to provide our readers with a bit of clarity.

In the **Feature** article, we again focus our attention on the fallout from the Brexit vote. While the decision to part company with the European Union has ushered in an era of ambiguity, it doesn't necessarily spell disaster for the UK. We discuss how a Swiss-style arrangement (which we dub "Britzerland") could lead to a more stable equilibrium. Meanwhile, more accommodative monetary policy and prospects for fiscal relief have helped bolster UK markets.

We also tackle the issue of the unsettled (and unsettling) political environment within the US in the **In Context** article. What we found here may come as something of a surprise to investors. Despite a heightened level of anxiety about the upcoming elections, it is our view that the most likely outcomes (which largely reflect

maintenance of the status quo) are apt to be greeted positively by investors. But even the alternative risk scenarios are less downbeat than some might expect given the checks and balances built into the US political system.

This month's **Top Themes** Spotlight centers on one of the most influential demographic segments of the population – not the Millennials, the Baby Boomers. Since birth, this generation has profoundly altered the economic, cultural, social, political and investment landscapes. As they continue to age, they are now poised to have a significant (and positive) impact upon healthcare, consumer, and financial services stocks.

Lastly, in this month's **In Focus** we discuss how continued solid employment growth is providing strong fundamental support for consumer spending. We look for an excellent environment for consumer discretionary stocks as they approach the crucial holiday spending season.

So despite the apparent paradoxes that have led to investor confusion, we retain our overweight to risk assets with preferences for US and emerging market equities.

Mike Ryan, CFA  
Chief Investment Strategist, WMA

**Video feature** Mike Ryan comments on how various election outcomes might impact sectors and policy. Click to play.



We prefer US equities and investment grade corporates, and favor emerging markets over Swiss equities.



## Equities

We remain overweight US and emerging markets, and underweight Swiss stocks.

## Fixed income

We remain overweight US investment grade corporates and underweight non-US bonds.

## Currencies

We have closed our preference for the US dollar versus the Australian dollar.

### LEGEND

**+** Overweight: Tactical recommendation to hold more of the asset class than specified in the moderate risk strategic asset allocation (see page 25)

**-** Underweight: Tactical recommendation to hold less of the asset class than specified in the moderate risk strategic asset allocation (see page 25)

**=** Neutral: Tactical recommendation to hold the asset class in line with its weight in the moderate risk strategic asset allocation (see page 25)

Each bar represents a +/- 2% tactical tilt or part thereof (i.e., one bar = 0.5% to 2%, 2 bars = 2.5% to 4%, 3 bars = over 4%). **NOTE: TACTICAL TIME HORIZON IS APPROXIMATELY SIX MONTHS**

# The bright side of Brexit?

## Post-Brexit rally

Many feared the UK vote to exit the EU would represent a setback for global markets. Instead we have seen price gains for assets across the risk spectrum.

## Bond yields

The UK's shift back toward monetary easing has contributed to lower global yields. This can help restrain the pace of US rate rises, since the Fed is eager to avoid a harmful appreciation of the US dollar.

## Fiscal options

The Brexit vote has also promoted renewed debate about the limits of monetary policy and the need for alternative means to stimulate faster economic growth.


## Asset allocation

We have closed our preference for the US dollar versus the Australian dollar.



**Mark Haefele**

Global Chief Investment Officer  
Wealth Management

 **Follow me on LinkedIn**  
[linkedin.com/in/markhaefele](https://www.linkedin.com/in/markhaefele)

What was initially reported as armed robbery turns out to be a misunderstood negotiation. No, I am not talking about what occurred in Brazil with four US Olympic swimmers. I am talking about Brexit. Many had feared that a UK vote to exit the EU would represent a significant setback for global markets. Instead, aside from the impact on the UK pound, the post-Brexit plunge lasted only a few days, as the reassuring Bank of England (BoE) response and stronger data elsewhere have allowed markets to focus on global growth. Now, all three US stock benchmarks are near record highs. Emerging market (EM) equities are at one-year peaks. High yield bonds have held up in spite of volatile oil prices. And, at the other end of the risk spectrum, the demand for developed market government debt is such that 40% of it now trades with a yield below zero.

Our diversified portfolios and overweight positioning in US equities have benefited from the post-Brexit rally. Over our six-month tactical investment horizon we remain confident that markets still hold upside. We are overweight US equities and US investment grade debt over government debt, as well as emerging market equities over Swiss equities.

But can we go further and point to something beyond a neutralization of the Brexit concerns? What might it take to see a potential bright side to the much-discussed vote? At a global level, the Brexit experience is promoting the debate on the limits of monetary policy, which could prove beneficial if it leads to more coordinated monetary and fiscal stimulus. And for the UK itself, Brexit might offer a historic opportunity to improve its economic fortunes, if the country follows the right role models.

Switzerland has proven it is possible to succeed outside the EU club.

The UK and Swiss economies have much in common, including a heritage of business-friendly regulation.

Swiss companies benefit from light regulation and an adaptable workforce.

### Britzerland?

The UK must choose its own path toward the brighter economic future promised by pro-Brexit politicians. However, there are proven roadmaps for successfully negotiating with the EU and improving economic prosperity.

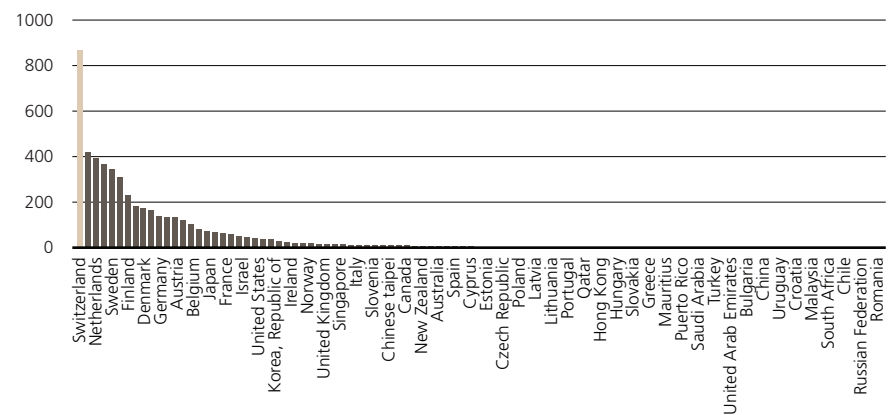
When Swiss voters opted to remain outside the European Economic Area in 1992, the pro-European economy minister described it as a “dark day” for the nation. Yet, economically, Switzerland has shown itself to be a success story. It now occupies the top spot in the World Economic Forum’s Global Competitiveness report, up seven notches since 2004. The Swiss model of light regulation and a focus on skills has helped make the Alpine state a magnet for multinationals and start-ups alike. It filed more patents per capita last year than any other country in the world (Fig. 1). And it also leads the EU in the adaptability of its workforce.

If UK politicians want to follow Switzerland’s lead, some uncomfortable choices likely loom. For instance, while rejecting membership in the European club, Switzerland remained open to foreign workers, helping it secure access to the common market and fuel economic growth. Switzerland also runs what in the UK might be seen as permanent austerity. Between 2006 and 2014, the Swiss have run an average general government surplus of 0.5% of GDP, relative to the UK’s average deficit of 6.5% of GDP, according to OECD data.

But the UK has many of the basic ingredients needed to follow Switzerland’s path if it chooses. Like Switzerland, it benefits from relatively light business regulation, a highly skilled workforce, and a tradition of innovation. And outside the EU, the UK will have even greater freedom to create the kind of business-friendly climate that helps explain Switzerland’s success.

**Fig. 1: Switzerland is an innovation hub, filing more patents per head than any other country.**

European patent applications per million inhabitants in 2015.



Source: European Patent Office, UBS. Data as of March 2016



If UK politicians make the right policy choices, the UK might just realize and enjoy a sustained “bright side to Brexit.”

### The global bright side

*For now*

The “bright side to Brexit” we’ve seen in the markets is not based on better-than-expected UK economic data; it will take months before data clearly indicates how the nation’s economy is coping with the vote. More important has been the outsized effect of the BoE’s actions on global yields. In effectively ending carry trades in gilts by announcing renewed quantitative easing, the BoE has contributed to a revived global “hunt for yield.” Subsequent downward pressure on US Treasury yields in particular has supported asset prices.

Post-Brexit declines in global government bond yields favor US companies, and lower debt costs in emerging markets.

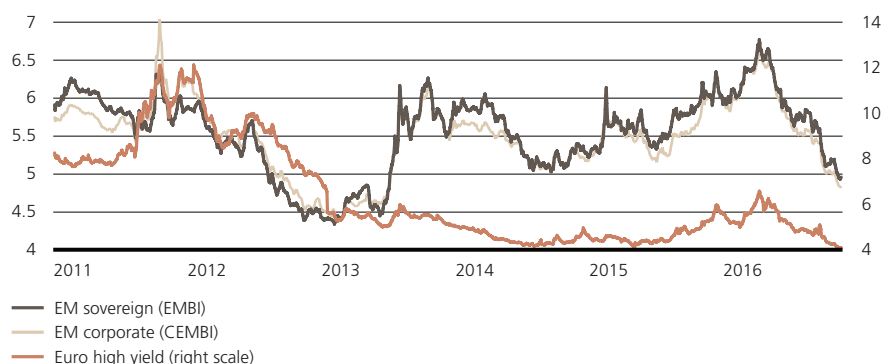
Lower yields reduce the cost of corporate debt in the US, boosting profit margins in the world’s largest economy. Emerging markets are also enjoying lower servicing costs on their foreign-currency liabilities; the yield on the JP Morgan EMBI and CEMBI indices for governments and corporates recently touched 4.81% and 4.92%, their lowest levels in three years (Fig. 2). And stronger EM exchange rates relative to a weaker US dollar contain EM inflation, reducing the need for local central banks to hike rates.

Lower global yields might also restrain the pace of US Federal Reserve tightening, since officials will be keen to avoid a damaging appreciation of the dollar. We expect only one Fed rate rise this year, and not until December.

EM nations can borrow in dollars at the cheapest rate in around three years.

**Fig. 2: Lower US yields pushed down borrowing costs on EM debt and European high yield.**

Yield to maturity for EM sovereign and corporate debt (USD), and for euro high yield.



Source: Bloomberg L.P., UBS. Data as of 22 August 2016

BoE chief Carney boosted market sentiment by ruling out sub-zero rates in the UK.

The UK referendum result has encouraged lawmakers to revisit the case for fiscal stimulus.

### *For later*

Although markets were reassured that another round of central bank stimulus managed to push risk assets higher, this post-Brexit easing has underlined the fact that we are approaching the limits of this plan. BoE Governor Mark Carney was keen to stress that the lower bound for rates will remain positive in the UK even though 40% of developed market government debt now carries a negative yield. Markets looked favorably on his disavowal of negative rates as an effective policy measure, which in turn will pressure Europe and Japan in particular to move beyond further rate cuts to stimulate growth.

Already, UK Chancellor Philip Hammond has flagged an end to the fiscal belt-tightening espoused by his predecessor, George Osborne. The European Commission's post-Brexit decision not to levy fines on deficit-limit breakers Spain and Portugal implies some fiscal leniency on the part of European policymakers, potentially linked to concerns about European unity. And Japan, also facing the limits of monetary policy, has introduced a JPY 28trn (USD 276bn) spending package.

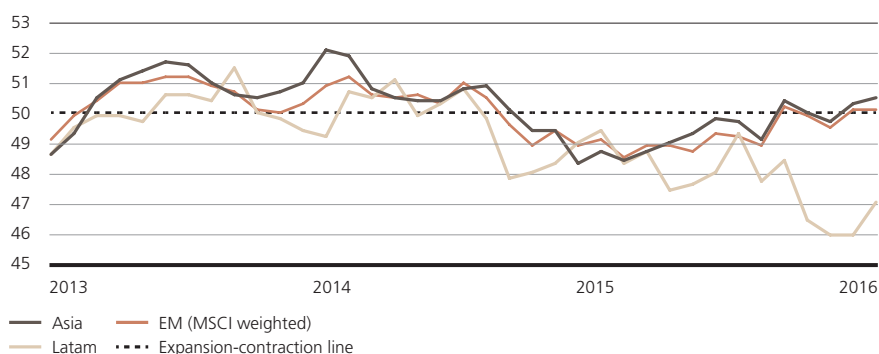
I am not suggesting that fiscal spending is a panacea for low growth and productivity, but I can see signs that Brexit could serve as the catalyst for politicians to engage in more growth-friendly policies, giving their central bank counterparts a break.

The door remains open for a Brexit outcome that is positive for both the UK and global markets. But it won't stay open forever.

Stronger economic growth should benefit our overweight EM equities position.

**Fig. 3: Leading indicators of emerging market growth are stabilizing.**

Manufacturing purchasing managers' indices for EM, Asia, and Latin America.



Source: Thomson Reuters Datastream, UBS. Data as of 2 August 2016.

US economic growth remains well supported by strong domestic consumption.

EM stocks benefit from stronger leading indicators of growth, and more stable earnings. More defensive Swiss stocks look set to underperform.

### Tactical asset allocation

Trends in global economic growth, central bank policy, and corporate profits have justified our risk-on stance.

US consumers remain in good health; average wages are growing at 3.4% according to the Atlanta Fed, close to the highest level since March 2009, and US household net worth is at a historical peak. Domestic demand growth in the second half of the year should help revive earnings per share growth to 3% for the full year. An end to the energy sector's capital expenditure destruction also bodes well for US industrial activity.

Since US borrowing costs should rise gradually, corporate debt costs will remain low for US and EM firms. This supports our overweight positions in US and EM equities in global portfolios. US stocks still look attractive relative to government bonds, despite trading at a trailing price/earnings ratio premium of 15% versus the average since 1960. In credit markets, we remain overweight US investment grade debt, whose spreads of 109 basis points still offer attractive carry versus government bonds.

We also remain overweight EM equities relative to Swiss stocks. We have seen encouraging signs of stabilization in emerging economies, with purchasing managers' indices pointing to rising activity in emerging Asia and Latin America (Fig. 3). Earnings also appear to have leveled off after a 30% slide since early 2012. In contrast, Swiss equities, which are heavily weighted toward defensive sectors, stand to benefit less from reviving global growth.

We made one change to our foreign exchange allocation this month, removing our preference for the US dollar versus the Australian dollar. In the wake of the Reserve Bank of Australia's second rate cut in early August, the near-term risks for AUDUSD look more balanced. The Australian dollar held its value due



to stronger-than-expected industrial performance in China and other emerging markets, signs that Australia will face fewer short-term setbacks to domestic growth, and the perceived Fed reluctance to raise rates at a time when other central banks remain in easing mode.

We are maintaining our six-month AUDUSD forecast at 0.71, and have raised our 12-month view to 0.71 (from 0.68). We would consider this preference again if the AUD appreciated further, China's "old economy" suffered a more abrupt slowdown, or the market brought forward its expectations for the next Fed rate hike.



Mark Haefele  
Global Chief Investment Officer  
Wealth Management

UBS Global Research is produced independently. All views expressed herein are the views of the named analyst(s) and were prepared in an independent manner including with respect to UBS. The views expressed by the analyst do not necessarily represent the views of UBS as an institution.

# The morning after



**Mike Ryan, CFA**

Chief Investment Strategist  
Wealth Management Americas

In the excitement and frustration of our country's uniquely long and ever-divisive political contest, rich with policy proposals and promises, it can be easy to forget the yawning chasm between political rhetoric and policy reality. Even if a candidate is successful in securing the presidency, his or her promises will still need to travel a long road of practicality and compromise.

As investors, it is our responsibility therefore to consider the rhetoric through a prism of checks and balances established by our founding fathers, placing the candidates' promises within a plausible range of political outcomes, and evaluating their potential impact on both the real economy and on financial markets in each scenario.

This is the subject of the latest edition of our *ElectionWatch* report ([click here](#)), developed in conjunction with our colleagues in the UBS US Office of Public Policy.

In the report, we put ourselves into the mindset of an investor awaking on 9 November, the morning after the US elections. We look at the range of potential results, their consequences for policy and economic fundamentals, and the resulting investment implications.

## Assessing the scenarios

Of the six plausible electoral combinations for the White House and Capitol Hill, we have opted to focus on the implications of the three most probable outcomes:

### 1. Voting for the status quo (60% probability)

President Hillary Clinton assumes office alongside a very narrow Democratic majority in the Senate and a reduced Republican majority in the House of Representatives.

According to our analysis, this is the most probable outcome, resulting in the least

chance for radical policy shifts, as Clinton continues to shepherd the current administration's policy objectives (plus a few of her own) through a recalcitrant legislature.

While regulatory pressures would remain high for certain sectors of the economy, this scenario would likely be seen as a modest positive for both US equity and bond markets, as it reduces policy uncertainty and suggests only gradual rate increases.

### 2. Trump shocks the world (25% probability)

Donald Trump wins the presidency and carries the Republican Party to narrow majorities in both the Senate and the House.

This less-likely outcome entails the most policy uncertainty. The wide range of possible policy outcomes could trigger negative short-term reaction from both equity and fixed income markets.

While fiscal stimulus would be welcome, the threat of trade wars, protectionism, and ballooning deficits would preoccupy markets in the immediate aftermath of this election result.

### 3. Hillary runs the table (8% probability)

The Democratic Party captures the presidency and a narrow majority in both legislative chambers.

The presidency, House, and Senate have been united just 30% of the time in the past 40 years. Of the three most probable outcomes, this result holds the largest potential for sweeping policy changes.

Although a Clinton presidency is generally viewed more favorably than a Trump administration, the prospects for a leftward lurch in economic and regulatory policy if the Democrats take control of Congress

would likely weigh on markets. This represents a “risk scenario” with the biggest impact on financial markets.

There are still more than two months remaining until the US electorate makes its final determination and the votes are counted, and we will continue to evaluate and refresh our forecast probabilities and commentary in future *Election-Watch* reports.

### Insights and conclusions

The results of this exercise have confirmed some of our preconceptions, but they have also uncovered some surprises.

- **Markets prefer certainty.** A Clinton presidency is generally viewed more favorably than a Trump Administration overall – at least as far as financial markets are concerned. Given market abhorrence to uncertainty, the narrower range of potential policy and economic outcomes from a Clinton presidency is viewed more constructively.

- **For some sectors, “it’s gonna be huge.”** There are a number of asset classes and market sectors that could actually fare better under a Trump presidency; for example, higher interest rates and lightened regulatory burdens would provide significant benefits to the financial and energy sectors.
- **Easy to oversimplify.** There are some asset classes that at first seem to be a straightforward beneficiary of a given outcome, but a closer analysis reveals a more muddled outlook. For example, a Democratic sweep and a corresponding increase in marginal tax rates would be expected to benefit municipalities, but a proposed cap on the municipal exemption to 28% would mute the impact.
- **Well-defended defense.** Regardless of the electoral outcome, we find that defense spending is likely to be sustained in response to growing threats from state and non-state actors.
- **Bark worse than bite.** Perhaps the biggest surprise is that our overall assessment of even the worst-case scenarios for this election is relatively

upbeat. The US political system is designed to preserve order through periods of political discord, and to ensure that governing power would never be entrusted to one person or a single political institution.

### Potent portent?

Fortunately, the ability to forecast political outcomes is not a requirement for strong investment returns. Long-term investment value is created by assessing changes in economic growth, central bank policy and earnings trends.

Policy changes can impact these fundamentals, and drastic policy shifts can create short-term opportunities, but the highest and most durable returns accrue to investors who respond to such events with discipline.

**Bottom line:** For all of its drama and spectacle, it can be easy to oversimplify or overreact to potential outcomes of the election. While policy changes are possible in 2017, partisan politics will provide a check on extreme views and major policy shifts.

### Summary of the six plausible election outcomes and their impact

Scenario	Probability	President	Senate	House	US equities	US fixed income
1	60%	Clinton	D	R	+	++
2	25%	Trump	R	R	--	--
3	8%	Clinton	D	D	--	-
4	3%	Clinton	R	R	n	n
5	3%	Trump	D	R	-	+
6	1%	Trump	D	D	-	+

#### Legend

++	Positive
+	Modest positive
n	Neutral
-	Modest negative
--	Negative

# Preferred investment views

↑ Recent upgrades  
↓ Recent downgrades

---

## Most preferred

### Equities

- US
- Emerging markets
- India
- North American energy independence
- Transformational technologies
- e-Commerce
- Golden years for Baby Boomers

---

### Bonds

- US investment grade
- Beyond benchmarks

---

### Currencies

- NOK

---

### Cash

---

## Least preferred

- Switzerland

- 
- Government bonds

- 
- EUR
- 

As of 25 August 2016

# At a Glance

## Economy

Economic momentum in the US has advanced since Q2, supported by solid consumer spending as labor market conditions continue to strengthen. Meanwhile, leading indicators point to ongoing improvement in the manufacturing sector. Emerging market economic activity is stabilizing. Global monetary policy remains highly accommodative, with new easing measures recently introduced by the Bank of England and the Bank of Japan. We expect the next rate hike by the US Fed likely to occur in December. Markets have started to price in Fed rate hikes again, and while we are late in the cycle, the fundamental improvements and our outlook for EPS growth support our continued tactical overweight in US equities against government bonds. Positive earnings growth is expected in 2H amid fading headwinds from the strong dollar and weak oil prices. Top-line growth is bottoming and margins are stabilizing.

## + Equities

We also hold a tactical overweight in emerging market (EM) equities against Swiss equities. Emerging markets are showing signs of stabilizing economic activity, while earnings are improving. Swiss equities are expected to benefit less from improving global growth than the more cyclical emerging markets, while Swiss financial sector earnings face the challenge of low interest rates. We are removing our underweight position in Australian equities against EM equities, where applicable, following surprisingly weak news-flow on Australian banks and the stronger AUD pressuring already weak earnings growth further. Investors who previously held an underweight in Australian equities should underweight Swiss equities against EM equities instead.

## ● Fixed income

Improving global growth prospects and continued accommodative monetary policies have supported a search for yield, benefiting risky credit assets in particular. We maintain a tactical preference for USD investment grade (IG) corporate bonds over government bonds. USD IG bonds benefit from an attractive yield pickup with a current yield-to-maturity of 2.2%, while credit risks are compensated for at current spread levels. Meanwhile, government bond yields remain close to historical lows, with flat returns expected over the next six months. We maintain a neutral position in US high yield and EM bonds, since we consider the extent of further credit spread tightening and price upside limited.

## Foreign exchange

We favor the Norwegian krone over the euro. The Norwegian economy continues to show strong momentum, with rising growth and inflation supporting our case that the easing cycle in Norway is ending. Meanwhile, Eurozone inflation remains far from the European Central Bank's 2% target, and we expect the ECB to engage in further monetary easing.

# Month in Review

US economic data remained mixed this month. Nonfarm payrolls grew by 255,000 in July, above the 180,000 consensus, and data on the manufacturing sector was generally positive. However, GDP growth was weak in 2Q, and core CPI showed only a small rise in July, leaving open questions for the Fed. Better-than-expected 2Q earnings results continued to push US equities higher this month, with the S&P 500 Index temporarily reaching a record high of 2,190 on 15 August.

The Bank of England announced its decision to cut interest rates by 25 basis points at its August meeting. Additionally, the central bank introduced a package of measures to boost growth and inflation in the wake of the Brexit vote, most notably, restarting its asset purchase program. The Eurozone shrugged off Brexit-inspired blues from July, with the German ZEW economic sentiment indicator rising to 57.6 from 50.2, and the Manufacturing Purchasing Managers Index rising to 53.3.

In Asia, Japanese growth disappointed after a promising first quarter, with annualized GDP increasing by just 0.2% in 2Q. Data in China this month pointed to slower growth as well. Activity and credit data indicated slower output growth, while trade data signaled weakening demand.

Oil prices rose more than 20% in the first three weeks of August following talks of a production freeze by OPEC. Prices fell toward the end of the month as these expectations faded and a report on US crude stockpiles showed an unexpected increase of 2.5mn barrels during the week of 19 August.

# Golden years for Baby Boomers

**Laura Kane, CFA**, Thematic and Sustainable Investing Strategist

**Stephen Freedman, PhD, CFA**, Head of Thematic and Sustainable Investing Strategy

When we think of the most influential generations of our time, Millennials often first come to mind. While these digital natives have undeniably reshaped consumer preferences, there is another segment of the population that is comparable in size, is going through a significant demographic transition, and has the added benefit of more discretionary dollars at its disposal. Born between 1946 and 1964, the Baby Boomers comprise about a quarter of the US population and control the largest share of household wealth. Due to its sheer size, this generation has shaped consumption patterns in the US every time it has moved to a new phase in its life cycle.

During the 1950s, young Boomers fueled unprecedented demand for baby food and toys. Next, we saw dramatic shifts in preferences in fashion, music, and entertainment as the Boomers were caught up in the countercultural movement of the 1960s. The '80s brought the first personal computers, setting new standards for business, government, and communication. By the '90s, Boomers were immersed in raising their families and looking after their homes.

Baby Boomers are now moving into their next distinct chapter. In 2011, the first among them turned 65, and this

will continue at a pace of approximately 10,000 per day for the next 15 years. By 2030, almost a quarter of the US population will be over the age of 65. This is significant as 65 is typically the age at which most people retire and become eligible for Medicare coverage. We think that the aging and retirement of the Boomers will have significant implications for spending patterns – particularly within the health-care, consumer, and financial sectors. In our new top theme, *Golden years for baby boomers*, we highlight companies that are well-positioned toward these trends.

## Healthcare

As the Boomers reach retirement age, they will likely spend more on healthcare as they manage the deleterious effects of old age. Unsurprisingly, the 2014 Survey of Consumer Expenditures (SCE) showed that older individuals spend a larger portion of their total expenditures (12.2% for those ages 65-74) on healthcare than younger generations (8.8% for those ages 55-64).

Within the healthcare sector, we expect managed care organizations (MCOs), or health insurers, to benefit from increased demand. As Boomers turn 65, they are eligible for Medicare enrollment, which will drive an increase in the insured population. In addition, MCOs are benefiting



from moderate healthcare inflation and ongoing consolidation in the sector. Among the MCOs, we prefer those with strong positioning in the Medicaid and Medicare market because of their relatively higher growth potential. For this theme, MCOs with higher exposure to Medicare are most relevant.

Another potential beneficiary of an aging population is pharmaceutical companies that manufacture drugs aimed at prolonging or improving the quality of life for sufferers of chronic illnesses, such as cancer, Alzheimer's, diabetes, and heart disease, which are more prevalent in the elderly. Recent political talk of high drug prices has put some pressure on the pharmaceutical industry. While this political headwind may persist through the election season, we view this short-term pullback as an attractive entry point for these stocks.

Finally, we see some upside for select medical supply manufacturers. In particular, we find medical suppliers specializing in products that treat cardiovascular disease well-positioned to benefit from an aging Boomer population.

### Consumer

As the Boomers enter retirement, we think they will spend more discretionary dollars on enjoying their golden years and managing their transition to old age. For example, personal care products firms, such as cosmetics companies that lead in anti-aging skin care, may experience an increase in demand as Boomers seek to maintain their youthful appearance.

We also expect an increase in spending on travel and leisure. One specific opportunity we see is the cruise lines – since they tend to appeal to an older demographic. In fact, over 25% of cruise line passengers are over the age of 60. Moreover, the cruise lines represent a relatively underpenetrated vacation market, with a US penetration rate of only 3.5%.

The nature of housing spending may also change as Boomers retire and become empty-nesters. For example, they may decide it's time to downsize and move to a retirement community that offers leisure activities catering to their demographic. We see an opportunity to invest in homebuilders that are industry leaders

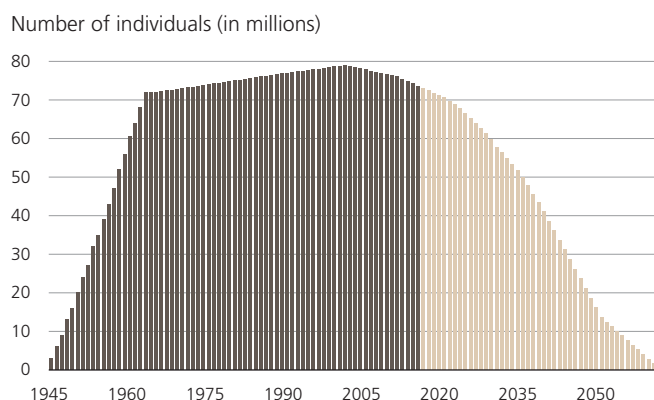
in developing lifestyle communities to serve active baby boomers as they move toward retirement.

Finally, Boomers may spend more dollars at the pharmacy. Individuals over the age of 65 utilize prescriptions at more than twice the rate of their younger counterparts (defined as ages 19-64), based on CVS estimates. The Centers for Medicare and Medicaid Services (CMS) projects that US prescription drug expenditures will grow by more than 6% annually over the next 10 years, supported by the demographic tailwind of an aging Boomer population.

### Financials

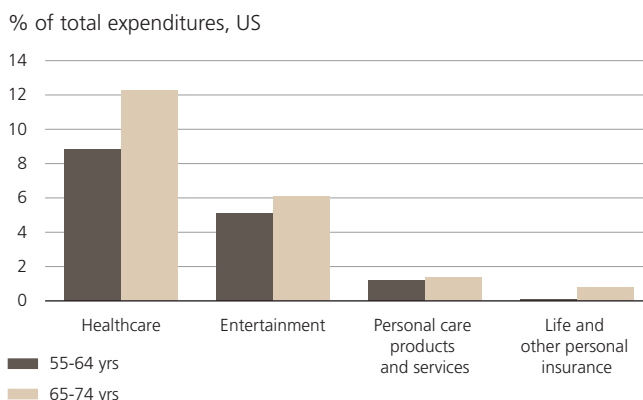
Financial services will be needed to help manage their wealth and ensure a smooth transition to life without a regular paycheck. The wealth concentration within portions of the Baby Boomer cohort, together with the need for different financial advice and products than prior to retirement, suggests that select asset managers and insurers will benefit.

**Fig. 1: Population of Baby Boomers in the United States**



Source: U.S. Census Bureau, UBS, as of May 2014

**Fig. 2: Spending patterns change after retirement**



Source: 2014 Consumer Expenditures Survey, Federal Reserve, UBS

# Global economic outlook

The Brexit vote is hurting the UK economy, while the global impact has been limited. US GDP growth has disappointed over the past three quarters, but with the labor market tightening, we still expect the Fed to hike rates in December. The Eurozone recovery is continuing at a modest pace, and Japanese data has been weak. Emerging market economies are looking somewhat better than they did early in the year. Inflation is subdued, and monetary policy is extremely accommodative in most countries.

Global growth in 2016 expected to be **2.9%**

	Real GDP growth in %			Inflation in %		
	2015	2016F	2017F	2015	2016F	2017F
US	2.6	1.4	2.4	0.1	1.3	2.2
Canada	1.2	1.9	2.5	1.1	1.7	1.9
Brazil	-3.8	-3.4	0.8	10.7	6.4	4.7
Japan	0.6	0.5	1.2	0.8	-0.2	0.5
Australia	2.5	2.8	3.0	1.5	1.2	1.8
China	6.9	6.6	6.3	1.4	1.9	2.0
India	7.6	7.4	7.6	4.9	5.4	4.5
Eurozone	1.6	1.5	1.3	0.0	0.3	1.5
UK	2.3	1.3	0.5	0.0	0.8	3.4
Switzerland	0.8	0.9	1.3	-1.1	-0.3	0.4
Russia	-3.7	-0.6	1.5	15.5	7.1	5.0
World	3.2	2.9	3.3	2.7	2.7	2.8

Source: Reuters EcoWin, IMF, UBS, as of 24 August 2016

Note: In developing the CIO economic forecasts, CIO economists worked in collaboration with economists employed by UBS Investment Research. Forecasts and estimates are current only as of the date of this publication, and may change without notice.

## Central bank policy

**Brian Rose, PhD**

US Economist

**Ricardo Garcia-Schildknecht**

Economist

### House view

Probability: 45%

The Brexit vote has had little direct impact on the US economy, and contagion via financial markets has not been an issue. Recent US data has been mixed, with strong job and weak GDP growth, but the former is more important for the Fed. The economy is approaching full employment and inflation is not far from the 2% target. Uncertainty will likely prevent the Fed from raising rates at its next couple of meetings, but we expect a rate hike in December.

### ➤ Positive scenario

Probability: 40%

#### **Worse macro backdrop**

The Fed is forced to stay on hold, but a rate cut remains unlikely. The European Central Bank launches additional monetary easing rapidly to address the downside risks emanating from the UK referendum. This may include more QE and/or a deposit rate cut, among other measures.

### ➤ Negative scenario

Probability: 15%

#### **Macro risks fade**

Diminished risks allow the Fed to hike rates twice by year-end. The ECB ignores the fallout from Brexit and refocuses rapidly on the inflation rebound, signaling a full exit from its QE program.

# Crude oil market rebalancing

**Giovanni Staunovo**

Analyst

**Dominic Schnider**

Analyst

**Wayne Gordon**

Analyst

## House view

Probability: 70%

The oil market is rebalancing and still has a ways to go since OPEC crude output is at its highest since 2008 and disrupted Canadian supply has returned. Expected counter-seasonal oil inventory buildup in 2H16 should make oil prices vulnerable to declining in the near term.

### ➤ Positive scenario

Probability: 10–20%

#### Sharper-than-expected contraction

Along with geopolitical events, political destabilization in oil-exporting countries, like Venezuela and those in the Middle East, and/or an emergency OPEC meeting that leads to a production cut are factors to consider. Alternatively, US crude oil production could contract more sharply than projected by key energy agencies.

### ➤ Negative scenario

Probability: 10%

#### Resilient production

Cost reductions, efficiency gains, and industry consolidation could lead to more resilient US oil production, keeping the oil market oversupplied and inventories on the rise – potentially reaching storage capacity limits. Also, receding unplanned crude production outages in OPEC countries like Libya could exacerbate the short-term production surplus.

# US earnings growth to resume

**Jeremy Zirin, CFA**

Head, Investment Strategy, WMA

**David Lefkowitz, CFA**

Senior Equity Strategist

## House view

Probability: 60%

While headline 2Q16 S&P 500 earnings-per-share (EPS) likely contracted slightly by 2-3% on a year-over-year basis, results compared favorably to the 6% decline experienced in the first quarter. This improving trend should continue with headline S&P 500 earnings growth resuming in the second half of the year.

### ➤ Positive scenario

Probability: 20%

#### Business confidence accelerates

Higher interest rates and rising commodity prices, driven by improving global growth prospects, could produce stronger-than-anticipated S&P 500 EPS growth as energy and financials experience meaningful gains. Increased confidence in the global economic expansion could spur greater capital investment, improving the outlook for industrials. Technology end-markets improved in 2Q16, and continued strength could result in earnings upside. Regardless of the November presidential election outcome, tax-reform momentum is expected to build. Lower taxation on repatriated foreign earnings could boost S&P 500 EPS via higher share buybacks.

### ➤ Negative scenario

Probability: 20%

#### Growth slump or stagnation

A downturn in US and global growth could lead to weaker-than-projected revenues for S&P 500 companies. Wage pressures, unaccompanied by improving consumer and business demand, could pressure profit margins and earnings growth rates. Persistently low short-term interest rates and continued declines in long-term interest rates could pressure financial sector earnings.

# Key dates

29 August 2016

## Personal income and spending for July

In addition to the important data on income and spending, this report includes the personal consumption expenditures (PCE) price index, the inflation measure that the Fed focuses on.

1 September 2016

## ISM Manufacturing for August

The ISM Manufacturing PMI has topped 50 since March, a sign that the manufacturing sector is on the mend after a soft patch.

2 September 2016

## Labor report for August

Nonfarm payrolls increased by 255,000 in July, the second straight month of strong gains. However, it still appears that the underlying trend has slowed somewhat in 2016. We will look at details of the report for evidence that the labor market is getting tighter.

6 September 2016

## ISM Non-Manufacturing for August

The ISM Non-Manufacturing PMI is an important indicator of current economic conditions. The PMI slipped to 55.5 in July, still a good level, but a further drop could raise some concerns.

15 September 2016

## Retail sales for August

With consumer spending driving overall economic growth, retail sales data is even more important than usual. Sales were strong in 2Q, but July was somewhat disappointing.

# Equities

Jeremy Zirin, CFA; David Lefkowitz, CFA; Markus Irngartinger, PhD, CFA

Performance has been mostly positive year-to-date. US equities have surged to new record highs, and emerging markets (EM) have gained, but the stronger yen has restrained the Japanese market, and negative interest rates have weighed on Eurozone financials. We are overweight US and EM equities, and underweight Swiss equities. Easier comparisons from oil prices and the dollar, coupled with continued strength in consumer spending, should help S&P 500 earnings-per-share (EPS) advance in the quarters ahead.

## Eurozone

⊖ neutral

We are neutral on Eurozone equities. Solid domestic consumer demand and ongoing monetary easing support a continued economic recovery. Leading economic indicators - especially for manufacturing activity - have stabilized in expansionary territory. While currency depreciation supported earnings last year, the euro has modestly appreciated this year. Earnings dynamics are rather weak when compared to other regions.

<b>EURO STOXX</b> (index points, current: 326)	Six-month target
<b>House view</b>	<b>335</b>
➤ Positive scenario	375
➤ Negative scenario	270

## Japan

⊖ neutral

We are neutral Japanese equities. Earnings growth should be moderate at 3% in FY16 (which ends in March 2017) and 4% in FY17, in our view. The yen has strengthened by more than 15% this year, and USDJPY trades around 100 currently, versus an average rate of 120 in FY15. We don't expect the yen to strengthen further in the next 12 months. Thus, the currency headwind for corporate earnings might fade toward the end of the year. Our preferred ideas within Japan equities include share-buyback and high-dividend-yield stocks.

<b>TOPIX</b> (index point, current: 1,307)	Six-month target
<b>House view</b>	<b>1,350</b>
➤ Positive scenario	1,500
➤ Negative scenario	1,100

## Emerging markets

⊕ overweight

We are overweight emerging market (EM) equities in our global portfolio. EM economic activity numbers are stabilizing, and manufacturing sentiment is turning more positive from low levels. Corporate earnings growth is improving, especially compared with several developed markets. The recent rise in commodity prices is encouraging, and the global liquidity backdrop remains supportive. Also, EM equities are trading at a discount to their developed market counterparts. We prefer China, Brazil, South Korea, and India to Mexico, Malaysia, the Philippines, and Taiwan.

<b>MSCI EM</b> (index points, current: 897)	Six-month target
<b>House view</b>	<b>940</b>
➤ Positive scenario	1,075
➤ Negative scenario	725

## UK

⊖ neutral

We are neutral on the UK. A weakening economic backdrop after the UK vote to leave the EU is likely to lead to downgrades in UK earnings, particularly for cyclical and domestic areas, including financials. Meanwhile, international companies will likely see upgrades to earnings, based on benefits from the weaker pound. Sterling has dropped about 11% on a trade-weighted basis since Brexit. Earnings are likely to fall by up to 5% this year and by a double-digit rate next year.

<b>FTSE 100</b> (index points, current: 6,836)	Six-month target
<b>House view</b>	<b>7,025</b>
➤ Positive scenario	7,500
➤ Negative scenario	5,600

Note: Current values as of 24 August 2016

# US equities

We are overweight US equities. Second-quarter earnings season confirmed that the worst of the year-long earnings slump is behind us. Easier year-over-year comparisons for energy earnings and multinationals, coupled with continued strength in consumer spending, should help drive S&P 500 EPS growth in the quarters ahead. Valuation remains attractive versus very low-yielding bonds. We do not expect the election outcome to materially impact our current economic or profit assumptions.

## US equities overview

+ overweight

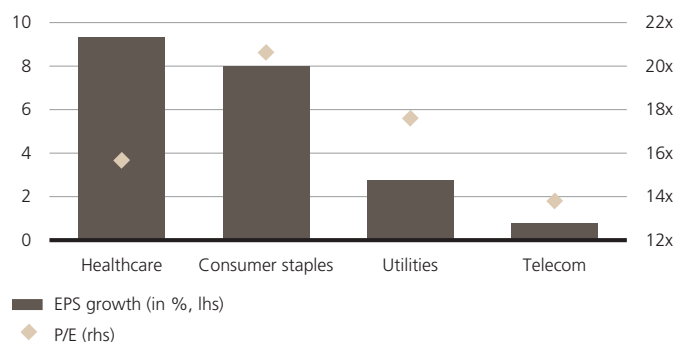
US equities have drifted higher, with little volatility, during the latter stages of the summer. We continue to believe that the US bull market is well-supported, and further gains are likely as year-over-year S&P 500 earnings growth turns positive in the second half of the year. The combination of reasonably healthy economic growth and low interest rates should keep US equity valuations above historical averages. The Fed is likely to raise rates later this year in December, but the risk of an aggressive Fed tightening cycle is low. Our rolling six-month S&P 500 target is 2225, or 17 times our forward 12-month EPS forecast.

## US sectors

While defensive sectors with high dividend yields were the top sector performers during the first half of the year, trends have reversed thus far during the third quarter. Robust earnings from technology and other cyclical sectors during second-quarter earnings season helped drive a rotation out of the "safe-haven" sectors, such as utilities and telecom. We expect this rotation to continue, and favor the consumer discretionary, technology, and energy sectors. Within defensive sectors, healthcare offers the most attractive combination of solid earnings growth and reasonable valuation.

### Healthcare offers the best combination of growth and valuation within defensive sectors

Next 12 months EPS growth and P/E, consensus estimates



Source: FactSet, UBS, as of 24 August 2016

## US equities – size

Improving domestic economic momentum, combined with a benign credit backdrop, has helped drive strong gains in small-cap stocks over the past few months. Year-to-date, both small- and mid-caps have modestly outperformed large-caps. Our recommended stance within US equities is a balanced tactical tilt across all size segments. Faster earnings growth should support smaller-size segments over the next few quarters; however, higher leverage suggests small-caps could be more vulnerable should growth disappoint.

## US equities – style

Growth stocks have modestly outperformed value stocks thus far in the third quarter, but continue to trail year-to-date. We have a neutral view between these two style segments of the US equity market. Our sector preferences for technology, consumer discretionary, and healthcare support a growth bias; however, rebounding energy stocks and the prospects for a Fed rate hike later this year benefit the broad value index, balancing the outlook.

S&P 500 (index points, current: 2,175)

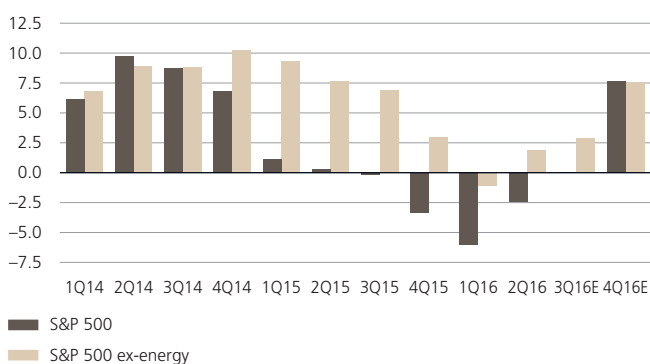
Six-month target

<b>House view</b>	<b>2225</b>
➤ Positive scenario	2450
➤ Negative scenario	1875

Note: Current values as of 24 August 2016

### Earnings growth is resuming

S&P 500 EPS, year-over-year change, in %



Source: FactSet, UBS, as of 24 August 2016

# Bonds

Leslie Falconio; Kathleen McNamara, CFA, CFP; Barry McAlinden, CFA; Philipp Schoettler; Frank Sileo

We expect Treasury yields to move modestly higher as the economic recovery continues and the Fed gradually raises rates. Strong June and July labor reports suggest that the economy is in good shape and inflation should gradually trend higher. Risks include market disruptions due to factors such as Brexit or a slowing Chinese economy. Although somewhat higher rates will result in minimal returns for government bonds, we maintain a neutral duration stance. Duration exposure is important to a well-diversified portfolio.

## Government bonds

⊖ underweight

The monthly trading range in 10-year yields is the lowest that the market has witnessed since 2006. With volatility low and the Treasury yield not rising above 1.6% since the end of June, complacency has entered the market. Although foreign central bank buying of US Treasuries remains strong, too many investors are leaning the same way. If/when interest rates do begin to trend higher, then the markets may witness a run for the exit out of the safe-haven assets.

US 10-YEAR YIELD (Current: 1.6%)		Six-month target
<b>House view</b>		<b>1.7%</b>
➤ Positive scenario		1.5%
➤ Negative scenario		1.9%

## US high yield corporate bonds

= neutral

High yield has returned 14% year-to-date, and 10.5% when excluding commodity sectors. While these price gains are unlikely to be repeated, we look for HY to deliver coupon-driven returns over the next six months. We see spread levels at 513bps as being expensive based on fundamentals, and look for spreads to trade sideways to gradually upward. We expect default rates to moderate to 4-5% over the next year as energy defaults peak. The low rate of non-commodity issuer defaults should only increase significantly under a negative scenario where recessionary risks rise.

USD HY SPREAD (Current: 513bps*)		Six-month target
<b>House view</b>		<b>625bps</b>
➤ Positive scenario		500bps
➤ Negative scenario		1,100bps

\*Data based on BAML High Yield indexes

## US investment grade corporate bonds

⊕ overweight

We continue to like the risk/reward profile of investment grade corporates despite the low yield levels. Year-to-date, IG's total return is 9%, which is 3% better than duration-matched Treasuries. The global search for yield will keep foreign demand elevated as overseas investors take advantage of the larger scale that US IG offers. Among IG sectors, we see better relative value in US IG financials, which have improved somewhat versus non-financials, but still offer relative value. Along the IG curve, we favor intermediate credit maturities in the 5- to 10-year range.

US IG SPREAD (Current: 140bps*)		Six-month target
<b>House view</b>		<b>150bps</b>
➤ Positive scenario		125bps
➤ Negative scenario		275bps

\*Data based on BAML IG corporate index

## Emerging market bonds

= neutral

Emerging market credit spreads further tightened over the last month by 14bps and 16bps and total returns were 1.4% and 1.3% for sovereign and corporate debt, respectively. The global liquidity backdrop remains supportive, the EM business cycle appears to have bottomed out, hard-landing fears in China are fading, stronger EM currencies and stable commodities are helping, and EM default rates have probably peaked. Despite the favorable performance, we remain neutral for EM sovereign and corporate bonds in USD within a global portfolio, and reiterate our 360bps six-month spread forecasts for both.

EMBIG div / CEMBI div SPREAD (Current: 337bps / 337bps)		Six-month target
<b>House view</b>		<b>360bps / 360bps</b>
➤ Positive scenario		300bps / 300bps
➤ Negative scenario		550bps / 580bps

Note: Current values as of 24 August 2016



## Municipal bonds

neutral

Over the past month, the market technicals remained favorable. The tax-exempt sector has now witnessed 46 straight weeks of net cash inflows to muni funds. Net issuance was negative, representing an important tailwind for the market. On a year-to-date basis, munis have gained 4.6%. At current levels, we believe that tax-exempt paper holds value versus US Treasury securities. Beyond September, volatility may increase due to uncertainty surrounding the final outcome of the US elections. Current AAA 10-year muni-to-Treasury yield ratio: 90.3% (last month: 91.9%).

## Non-US developed fixed income

underweight

Over the past month, bond yields moved mostly lower in countries outside of the US, and the dollar fell against most other major currencies, boosting the value of non-US assets when measured in dollars. This generated strong returns for non-US developed fixed income. However, non-US bond yields are at very unattractive levels with many bonds offering negative yields, and we expect the dollar to strengthen in the near term as the Fed prepares to raise rates. We therefore recommend an underweight position on the asset class.

## Additional US taxable fixed income (TFI) segments

### Agency bonds

Although Agency bonds have returned a respectable 3.6%, according to the BAML Agency Index, they are underperforming most other fixed income assets. Although we still anticipate that spread product will outperform Agency debt heading into the second half of the year, a pickup in volatility may warrant small exposure to the fixed income safe-haven assets. Current spread is +18bps to the 5-year (versus +16bps last month).

### Preferred securities

Valuation in the USD 25 par preferred market remains historically tight with spreads narrowing to post-crisis lows. ETF flows could prolong imbalances, but current valuation may impede outperformance, and create vulnerability to potential shocks and volatility. We maintain a neutral position. There are opportunities to take profits in overextended USD 25 par preferreds and redeploy proceeds into select USD 1000 par fixed-to-float preferreds with call protection and high back-end spreads, or select high-coupon fixed-rate coupons. Current spread: 74bps vs. 82bps last month.

### Mortgage-backed securities (MBS)

MBS seem resilient to all market moves, whether oil or Brexit, as spreads remain range-bound. We remain neutral on MBS until the upper or lower band of the 95bps-115bps spread range is broken. With volatility more than likely going higher into the election and the possibility of a rate hike in December, we do not anticipate significant outperformance of the sector. MBS are currently a carry play, and their AAA rating keeps liquidity investors, such as banks and mutual funds, continuously involved. Current spread is +102bps to the 5-year and 10-year Treasury blend (versus +100bps last publication).

### Treasury inflation-protected securities (TIPS)

TIPS breakeven inflation rates fell during August declining to 1.28%, as oil prices declined earlier in the month. As oil recovered back to the USD 47 range, 5-year TIPS increased slightly to 1.33%. We remain neutral on the TIPS market, and the recent weak CPI report justifies our view for not currently having an overweight. We are targeting a low 120's breakeven inflation as a possible re-entry point, but for now, we remain sidelined.

Note: Current values as of 24 August 2016

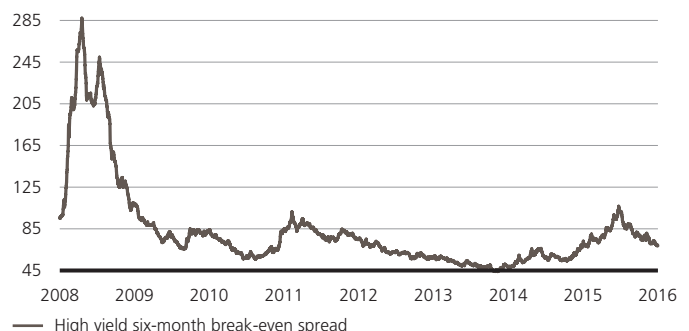
#### UBS WMR interest rate forecast

Americas	24-Aug-16	3 mths	6 mths	12 mths
USD 3M Libor	0.8	1.2	1.3	1.6
USD 2Y Treas.	0.8	0.9	1.0	1.1
USD 5Y Treas.	1.1	1.2	1.3	1.5
USD 10Y Treas.	1.6	1.5	1.7	1.9
USD 30Y Treas.	2.2	2.3	2.5	2.7

Source: UBS, as of 24 August 2016

#### Currently high yield has 68bps of spread cushion before underperforming US Treasuries

Six-month break-even spreads for HY, in bps



Source: Factset, UBS, as of 22 August 2016

# Commodities and other asset classes

Dominic Schnider, CFA, CAIA; Giovanni Staunovo; Thomas Veraguth; Wayne Gordon

Broadly diversified commodity indices, like the Bloomberg Commodity Index and UBS Bloomberg CMCI Index, managed to gain strength in August due to a recovery in crude oil prices. We believe the return outlook for the asset class remains un compelling – a view we have held the entire year. On a spot basis, we expect the asset class to deliver returns of around 0% over the next six months.

## Commodities

neutral

**Precious metals** Gold prices have benefited from three factors this year: higher financial market volatility, political uncertainties, and lower US real rates, which stem partly from the Fed's slower hiking path. If it appears that the Fed will turn more hawkish in coming weeks, gold will come under greater pressure. That said, we continue to like its insurance attributes, and expect prices to steady and trade around USD 1,325/oz in six months and USD 1,275/oz in 12 months. We see persistently low real rates as keeping a floor under gold near these levels in the longer term.

<b>GOLD</b> (Current USD 1,324/oz)	Six-month target
<b>House view</b>	<b>USD 1,325/oz</b>
Positive scenario	USD 1,500/oz
Negative scenario	USD 1,050/oz

**Crude oil** Supply availability of crude oil has improved with the return of disrupted Canadian oil supply and with OPEC crude production at its highest level since 2008. This makes oil vulnerable to lower prices, in our view, as inventories build counter-seasonal in 2H16. We remain confident that a combination of contracting non-OPEC supply and rising oil demand in emerging markets will result in a balanced oil market next year, which should bring with it Brent oil prices of USD 55/bbl or higher in 12 months. Price setbacks offer an opportunity to increase exposure to the oil market, in our view.

<b>BRENT</b> (Current: USD 49/bbl)	Six-month target
<b>House view</b>	<b>USD 45/bbl</b>
Positive scenario	USD 70/bbl
Negative scenario	USD 30/bbl

**Base metals** Our expectations of firmer industrial activity in the coming months favor higher base metal prices. While supply should be able to accommodate greater demand, drawing down inventories should initially support prices. We like aluminum, nickel, and lead. The sensitivity to manufacturing and supply and production cost considerations favor higher prices.

We are less comfortable with a long position in copper and zinc. Ample supply remains a price burden, while zinc prices have already rallied. We believe this gives copper and zinc an unattractive risk/reward profile. We see copper prices being capped at USD 5,000/mt over the next three to six months.

**Agriculture** The diminishing probability of a La Niña event disrupting the summer cropping season in South America and the recent record US Department of Agriculture corn and soybean yield predictions of 175.1 bushels/acre and 48.9 bushels/acre, respectively, in the US are major dampeners of sentiment ahead. With global weather agencies toning down climate risks, unless South American yield potential is undermined by regional weather issues, in our view, grains and oilseeds markets could face further downside pressure on prices. Soft commodities, including cotton, have shown greater resilience. Cotton is sensitive to setbacks and profit-taking as speculative accounts are overextended, which makes it one of our least preferred commodities.

## Other asset classes

**Listed real estate** Earnings growth remains solid at 4.5% for 2016-17. A 3.5% dividend yield makes an 8% full-year return possible, provided overall bond yields stay low. Listed real estate has already delivered more than 12.5% this year and is unattractively valued. It trades at a 1.8% premium to net asset value compared to a historical -6.4%. Financial conditions for real estate stabilized after deteriorating at the beginning of the year, but are now slowly worsening again. Spread expansion presents the biggest risk at these extremely low bond yields, despite the current good spreads.

<b>FTSE EPRA/ NAREIT Developed</b>	Six-month target
<b>TR USD</b> (Current: 4,796)	
<b>House view</b>	<b>USD 4,500</b>
Positive scenario	USD 4,800
Negative scenario	USD 4,000

Note: Current values as of 24 August 2016

# Foreign exchange

Thomas Flury

We expect the Fed to hike rates in December, while money markets are only pricing for one increase at the end of 2017. The USD should be supported once markets start to reprice the probability of an earlier rate hike. We continue to expect the JPY, AUD, and NZD to weaken as central banks in these countries ease. We favor the NOK versus EUR. Rising growth and overshooting inflation in Norway support our case that Norges Bank won't cut its policy rate again, while further monetary easing in the Eurozone remains likely.

## USD

⚖ neutral The events in the upcoming months will be crucial for the USD. The US elections and the monetary policy of the Federal Reserve could expose the USD to larger swings. We continue to expect the Fed to hike interest rates in December, while money markets are only pricing for one increase at the end of 2017. The USD should be supported once markets start to reprice the probability of an earlier rate hike.

## EUR

⚖ underweight We expect EURUSD to fall as markets prepare for a US rate hike this year. Even if the world economic outlook deteriorates in the coming months, we still see some upside for the USD versus the EUR. On a 12-month view, we expect EURUSD to rise, as the euro is strongly undervalued and has decent recovery potential once the European Central Bank shifts its policy stance from easing to tightening.

## GBP

⚖ neutral The referendum in the UK led to a significant shift of political powers with breathtaking speed. The outcome of the Brexit negotiations between the UK and the EU is likely to affect the attractiveness of UK assets for foreign investors. We see the economy weakening further, with more stimulus from the Bank of England likely to keep the pound weak for the next six months.

## CHF

⚖ neutral The CHF is near equilibrium against the USD, but it is strongly overvalued against other G10 currencies. We expect the USD to appreciate first, as the Fed is expected to tighten first. In the long term, though, USDCHF should follow its multi-decade downtrend, as Swiss inflation stays well below US inflation.

## JPY

⚖ neutral Prime Minister Shinzo Abe's party has announced another fiscal package to support the economy, as was widely expected. But even this fiscal stimulus is unlikely to boost inflation closer to the 2% target. We expect further monetary stimulus from the Bank of Japan in coming months, and still expect USDJPY to rise to 107 in 12 months.

## Other developed market currencies

+ overweight We expect the NOK to strengthen fundamentally as the combination of Norway's growth rebound and high inflation rates speaks for a tighter policy path of the Norges Bank relative to the ECB. We prefer the NOK over the EUR.

### UBS CIO FX forecasts

	3M	6M	12M	PPP*
EURUSD	1.08	1.10	1.10	1.26
USDJPY	104	104	107	78
USDCAD	1.30	1.28	1.25	1.21
AUDUSD	0.74	0.71	0.71	0.70
GBPUSD	1.25	1.28	1.32	1.60
NZDUSD	0.70	0.68	0.65	0.60
USDCHF	1.00	1.00	1.02	1.00
EURCHF	1.08	1.10	1.12	1.25
GBPCHF	1.25	1.28	1.34	1.60
EURJPY	112	114	118	98
EURGBP	0.86	0.86	0.83	0.78
EURSEK	9.50	9.30	9.00	8.89
EURNOK	9.00	8.70	8.70	9.98

Source: Thomson Reuters, UBS, as of 24 August 2016

Note: Past performance is not an indication of future returns.

\*PPP = Purchasing Power Parity

# As the consumer turns

Signs point to a happier holiday season



Rob Samuels  
Equity Sector Strategist



Brian Rose, PhD  
US Economist

The macroeconomic backdrop for consumers is more favorable than at any time since the financial crisis. By far, the most important factor supporting consumer spending is the improvement in the labor market. Job growth has averaged more than 200,000 per month over the last five years, which has pushed the unemployment rate below 5%. Job openings are near record-high levels, while initial jobless claims are at historic lows. With the economy approaching full employment, labor shortages are spreading and wages are starting to rise at a faster pace. The growth in labor income provides the fuel to keep consumer spending growing, and improving labor market conditions have helped to lift consumer confidence.

Financial conditions are also supportive of consumer spending. The stock market is near record highs and house prices are steadily rising, providing a boost to household balance sheets. Thanks to low interest rates, household debt service has fallen to 10% of disposable income, close to a record low. There are of course some negatives, such as the large number of people struggling with student loans, as well as baby boomers trying to save more for retirement. There is also a possibility that the upcoming election could weigh on sentiment and spending, but at least so far there isn't any evidence that this is happening. Overall, we expect consumer spending to rise at least as fast as income, and income should continue to increase at a robust pace.

Solid consumer fundamentals combined with low relative sector valuations support our overweight of the S&P 500 consumer discretionary sector. Earnings grew nearly 15% in the second quarter, the strongest of any sector, and positive trends are expected to continue into the first half of 2017. Let's dig a little bit deeper into what we learned during the past quarter.

Coming out of first quarter retail earnings season, analysts covering the US retailers felt like a boxer who had just come out of a 12-round fight with Mike Tyson in his prime bruised and battered from the horrendous results that were reported, especially within the department store space. Inventories were bloated, deep promotions were prevalent and investors were questioning if consumers would ever return to the mall to shop. What a difference a quarter makes. Second quarter earnings season just wrapped up, and while numbers were far from perfect, companies did manage to beat lowered expectations. Same-store sales came in much better than feared, and management commentary suggested that these trends accelerated throughout the quarter, with a healthy start to back to school.

Perhaps one of the better data points to come out of two weeks of earnings conference calls was around inventory management. It appears as if department stores remain very cautious with their ordering patterns given last winter's warm weather, and inventory seems to be much better aligned to sales than a year ago. In fact, inventory hasn't been in this

good shape across the mall since the first quarter of 2013. While mall traffic continues to be sluggish and unlikely to improve given the continued growth of online and mobile shopping, the improved inventory positioning means that we could see fewer markdowns this upcoming holiday season and more full-priced selling -- a positive for retailer's profit margins.

Another positive call-out for the quarter was the strength of denim and an encouraging start to the important back-to-school shopping season. Denim is a key apparel category and any signs of a potential emerging trend should be viewed as a positive for apparel sales.

The path forward suggests that there is room for continued improvement for retailers. Looking forward, year-over-year comparisons appear very favorable given last year's disappointing winter selling season, which was dampened by very warm weather and its deleterious impact on winter apparel sales.

Overall, consumer discretionary stocks carry reasonable valuations, should deliver solid earnings growth compared to the broader market, and for many retailers, same-store sales comparisons are very easy through the middle of next year. The tailwinds are in place to make this a truly happy holiday season.

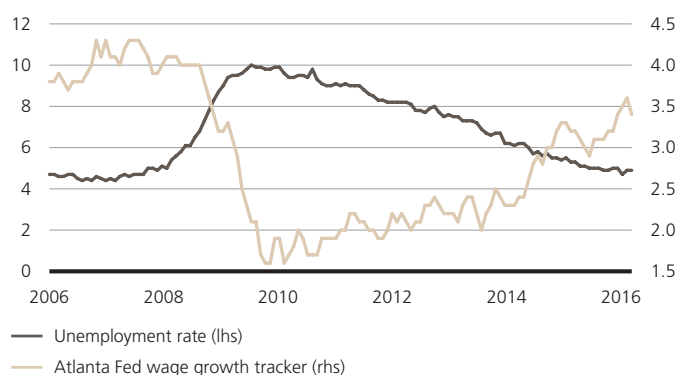
#### Video feature

Click the play button to watch



**Fig. 1: Improving labor market supports consumer spending**

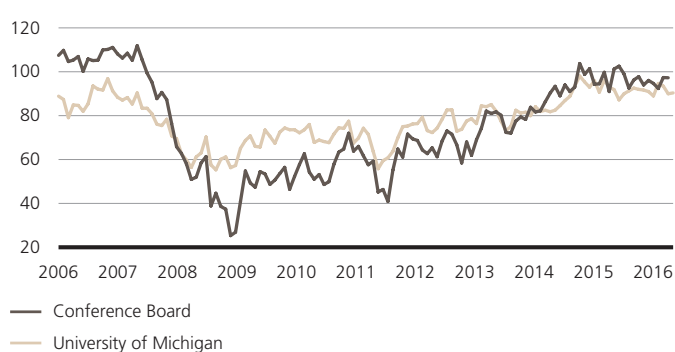
Unemployment rate in % (lhs), wage growth y/y % (rhs)



Source: Bloomberg, UBS, as of 24 August 2016

**Fig. 2: Consumer sentiment holding steady**

Conference Board consumer confidence and University of Michigan consumer sentiment



Source: Bloomberg, UBS, as of 24 August 2016

# Top themes overview

Our Top themes list represents our currently recommended thematic ideas

## e-Commerce: Beyond Amazon

As consumers of traditional retail shift their shopping and spending online, opportunities abound for true omnichannel retailers and related companies. We believe that long-term positive drivers of digital growth, including the rapid adoption of mobile devices, will continue to hasten market share shifts online. We recommend taking a look at select opportunities in consumer-focused industries that take an omnichannel approach and that utilize digital marketing strategies to complement their online efforts.

Short	Medium	Long	Decade

[Click for full report](#)

[e-Commerce: Beyond Amazon](#)

## **NEW** Golden years for Baby Boomers

The Baby Boomers – which represent almost a quarter of the US population – are aging and entering their retirement years. This generation, by its sheer size, has always had an outsized influence on society. As the Boomers enter into their hard-earned retirement and set out to enjoy their golden years, we expect various segments of the economy to benefit disproportionately, particularly segments of the healthcare, consumer, and financial sectors.

Short	Medium	Long	Decade

[Click for full report](#)

[Golden years for baby boomers](#)

## India – A land of many (re)turns

We believe Indian equities have the potential to outperform the broader market over the next year. Recent economic data points to a gradual pickup in growth that should create an environment conducive for a corporate profit revival. Further, valuations look attractive, as markets have priced out any major benefits from reform efforts. We see the potential for a moderate re-rating in recognition of the many credible efforts that the Narendra Modi-led government has already made.

Short	Medium

[Click for full report](#)

[India – A land of many \(re\)turns](#)

## North American energy independence: Reenergized

We continue to focus on the North American oil and gas business, where we project that growth will resume with the recovery in energy commodity prices; and in energy infrastructure, where we believe opportunities still exist due to evolving trends in the US. The strongest operators could emerge from the downturn with an enhanced competitive position. Meanwhile, lower oil prices and an advantaged regional natural gas price are beneficial to North American industrial energy consumers. We also see advances in renewable and alternative energy providing new approaches to satisfying energy demand.

Short	Medium	Long	Decade

[Click for full report](#)

[North American energy independence: Reenergized](#)



# Top themes overview

## Transformational technologies

We believe there are two areas of technological innovation that will be driving forces behind productivity gains during the next decade. The first is the set of business opportunities around the explosion of digital data. The second is automation and robotics. Both have the potential to transform the structure of our economy, disrupt existing business models, and create opportunities for those well-positioned to participate. Security underpins both digital data and industrial automation, and in our view, is the key enabling technology for the next wave of innovation across both information technology and the industrial sector.

Short	Medium	Long	Decade
-------	--------	------	--------

[Click for full report](#)

[Transformational technologies](#)

## Beyond benchmark fixed income investing



Over the next decade, we believe that US taxable fixed income investors will find themselves in a challenging market environment characterized by low starting yield levels, bouts of volatility, and a longer, drawn-out normalization cycle. For these investors, the most widely used benchmark is the Barclays Aggregate Index, which suffers from several flaws, in our view. We argue that investors can circumvent benchmark shortcomings by diversifying bond portfolios beyond a traditional benchmark and adopting a more flexible approach to active fixed income management.

Short	Medium	Long	Decade
-------	--------	------	--------

[Click for full report](#)

[Beyond benchmark fixed income investing](#)

### Drivers behind Top themes

	Resources/ Environment	Innovation/ Technology	Demographics/ Society	Int'l trade and investment	Government/ Regulation	Cyclical factors	Financial industry trends
Theme name							
 e-Commerce: Beyond Amazon		✓	✓			✓	
 India – A land of many (re)turns	✓			✓	✓	✓	
 North American energy independence: reenergized	✓	✓		✓	✓	✓	
 Transformational technologies	✓	✓	✓				
 Beyond benchmark fixed income investing					✓	✓	
 Golden years for Baby Boomers		✓	✓		✓		

Source: UBS

# Key forecasts

As of 24 August 2016

+ Overweight  
= Neutral  
- Underweight

						6-month forecast		
Asset class	TAA <sup>1</sup>	Change	Benchmark	Value	m/m perf. in % <sup>2</sup>	House View	Positive scenario	Negative scenario
EQUITIES								
USA	+	–	S&P 500	2175	0.0%	2225	2450	1875
Eurozone	=	–	Euro Stoxx	326	2.2%	335	375	270
UK	=	–	FTSE 100	6836	1.6%	7025	7500	5600
Japan	=	–	Topix	1307	-1.6%	1350	1500	1100
Switzerland	–	–	SMI	8200	0.1%	8365	9000	7000
Emerging Markets	+	–	MSCI EM	897	3.2%	940	1075	725
BONDS								
US Government bonds	–	–	10yr yield	1.6%	0.2%	1.7%	1.5%	1.9%
US Corporate bonds	+	–	Spread	140 bps	0.7%	150 bps	125 bps	275 bps
US High yield bonds	=	–	Spread	513 bps	1.6%	625 bps	500 bps	1100 bps
EM Sovereign	=	–	Spread	337 bps	1.5%	360 bps	300 bps	550 bps
EM Corporate	=	–	Spread	337 bps	1.7%	360 bps	300 bps	580 bps
OTHER ASSET CLASSES								
Gold	=	–	Spot price	1324 /oz.	0.1%	1325	1500	1050
Brent crude oil	=	–	Spot price	49.05 /bbl.	7.4%	45	70	30
Listed real estate	=	–	RUGL Index	4796	-0.4%	4500	4800	4000
CURRENCIES			Currency pair					
USD*	=	–		NA	NA	NA	NA	NA
EUR	–	–	EURUSD	1.13	2.6%	1.10	NA	NA
GBP	=	–	GBPUSD	1.32	0.9%	1.28	NA	NA
JPY	=	–	USDJPY	100	-5.4%	104	NA	NA
CHF	=	–	USDCHF	0.97	-2.0%	1.00	NA	NA

Source: Bloomberg, UBS

<sup>1</sup> TAA = Tactical asset allocation, <sup>2</sup> Month over month

Note: Current values as of 24 August 2016

\* For intra-month changes to the currency allocation, see CIO Note: Close US dollar vs. Australian dollar call, 3 August 2016.

**Past performance is no indication of future performance. Forecasts are not a reliable indicator of future performance.**

# Detailed asset allocation

## taxable with non-traditional assets

Investor risk profile		Conservative				Moderately conservative				Moderate				Moderately aggressive				Aggressive			
Change this month	All figures in %	Strategic asset allocation	CIO tactical deviation	Change this month	Current allocation <sup>1</sup>	Strategic asset allocation	CIO tactical deviation	Change this month	Current allocation <sup>1</sup>	Strategic asset allocation	CIO tactical deviation	Change this month	Current allocation <sup>1</sup>	Strategic asset allocation	CIO tactical deviation	Change this month	Current allocation <sup>1</sup>	Strategic asset allocation	CIO tactical deviation	Change this month	Current allocation <sup>1</sup>
<b>Cash</b>		0.0	+0.0		0.0	0.0	+0.0		0.0	0.0	+0.0		0.0	0.0	+0.0		0.0	0.0	+0.0		0.0
<b>Fixed Income</b>		69.0	-2.0		67.0	57.0	-2.0		55.0	46.5	-2.0		44.5	41.0	-2.0		39.0	33.0	-2.0		31.0
<b>US Fixed Income</b>		62.0	+0.0		62.0	51.0	+0.0		51.0	40.5	+0.0		40.5	34.0	+0.0		34.0	26.0	+0.0		26.0
US Gov't		7.0	-1.0		6.0	5.5	-1.5		4.0	4.0	-2.0		2.0	3.5	-2.0		1.5	2.0	-2.0		0.0
US Municipal		50.0	+0.0		50.0	39.0	+0.0		39.0	30.0	+0.0		30.0	24.0	+0.0		24.0	17.0	+0.0		17.0
US IG Corp		4.0	+1.0		5.0	3.5	+1.5		5.0	3.0	+2.0		5.0	2.5	+2.0		4.5	2.0	+2.0		4.0
US HY Corp		1.0	+0.0		1.0	3.0	+0.0		3.0	3.5	+0.0		3.5	4.0	+0.0		4.0	5.0	+0.0		5.0
<b>Int'l Fixed Income</b>		7.0	-2.0		5.0	6.0	-2.0		4.0	6.0	-2.0		4.0	7.0	-2.0		5.0	7.0	-2.0		5.0
Int'l Developed Markets		6.0	-2.0		4.0	4.0	-2.0		2.0	3.0	-2.0		1.0	3.0	-2.0		1.0	2.0	-2.0		0.0
Emerging Markets		1.0	+0.0		1.0	2.0	+0.0		2.0	3.0	+0.0		3.0	4.0	+0.0		4.0	5.0	+0.0		5.0
<b>Equity</b>		16.0	+2.0		18.0	27.0	+2.0		29.0	34.5	+2.0		36.5	45.0	+2.0		47.0	55.0	+2.0		57.0
<b>US Equity</b>		9.0	+2.0		11.0	15.0	+2.0		17.0	20.0	+2.0		22.0	26.0	+2.0		28.0	31.0	+2.0		33.0
US Large cap Growth		2.5	+0.5		3.0	4.5	+0.5		5.0	6.0	+0.5		6.5	8.0	+0.5		8.5	9.5	+0.5		10.0
US Large cap Value		2.5	+0.5		3.0	4.5	+0.5		5.0	6.0	+0.5		6.5	8.0	+0.5		8.5	9.5	+0.5		10.0
US Mid cap		3.0	+0.5		3.5	4.0	+0.5		4.5	5.0	+0.5		5.5	7.0	+0.5		7.5	8.0	+0.5		8.5
US Small cap		1.0	+0.5		1.5	2.0	+0.5		2.5	3.0	+0.5		3.5	3.0	+0.5		3.5	4.0	+0.5		4.5
<b>International Equity</b>		7.0	+0.0		7.0	12.0	+0.0		12.0	14.5	+0.0		14.5	19.0	+0.0		19.0	24.0	+0.0		24.0
Int'l Developed Markets		4.0	-0.5		3.5	7.0	-1.0		6.0	8.5	-1.0		7.5	11.0	-1.0		10.0	14.0	-1.0		13.0
Emerging Markets		3.0	+0.5		3.5	5.0	+1.0		6.0	6.0	+1.0		7.0	8.0	+1.0		9.0	10.0	+1.0		11.0
<b>Commodities</b>		4.0	+0.0		4.0	4.0	+0.0		4.0	4.0	+0.0		4.0	5.0	+0.0		5.0	5.0	+0.0		5.0
<b>Non-traditional</b>		11.0	+0.0		11.0	12.0	+0.0		12.0	15.0	+0.0		15.0	9.0	+0.0		9.0	7.0	+0.0		7.0
Hedge Funds		11.0	+0.0		11.0	12.0	+0.0		12.0	10.0	+0.0		10.0	3.0	+0.0		3.0	0.0	+0.0		0.0
Private Equity		0.0	+0.0		0.0	0.0	+0.0		0.0	5.0	+0.0		5.0	6.0	+0.0		6.0	7.0	+0.0		7.0
Private Real Estate		0.0	+0.0		0.0	0.0	+0.0		0.0	0.0	+0.0		0.0	0.0	+0.0		0.0	0.0	+0.0		0.0

"WMR tactical deviation" legend: **Overweight** **Underweight** **Neutral** "Change" legend: ▲ Upgrade ▼ Downgrade \*Refers to moderate-risk profile.

<sup>1</sup>The current allocation column is the sum of the strategic asset allocation and the tactical deviation column.

Source: UBS and WMA AAC, 25 August 2016. See appendix for information regarding sources of strategic asset allocations and their suitability, investor risk profiles, and the interpretation of the suggested tactical deviations from the strategic asset allocations.

# Detailed asset allocation

## taxable without non-traditional assets

Investor risk profile		Conservative				Moderately conservative				Moderate				Moderately aggressive				Aggressive			
Change this month	All figures in %	Strategic asset allocation	CIO tactical deviation	Change this month	Current allocation <sup>1</sup>	Strategic asset allocation	CIO tactical deviation	Change this month	Current allocation <sup>1</sup>	Strategic asset allocation	CIO tactical deviation	Change this month	Current allocation <sup>1</sup>	Strategic asset allocation	CIO tactical deviation	Change this month	Current allocation <sup>1</sup>	Strategic asset allocation	CIO tactical deviation	Change this month	Current allocation <sup>1</sup>
<b>Cash</b>		0.0	+0.0		0.0	0.0	+0.0		0.0	0.0	+0.0		0.0	0.0	+0.0		0.0	0.0	+0.0		0.0
<b>Fixed Income</b>		80.0	-2.0		78.0	66.0	-2.0		64.0	54.5	-2.0		52.5	44.0	-2.0		42.0	33.0	-2.0		31.0
<b>US Fixed Income</b>		72.0	+0.0		72.0	58.0	+0.5		58.5	47.0	+0.0		47.0	36.0	+0.0		36.0	26.0	+0.0		26.0
US Gov't		8.0	-1.0		7.0	7.0	-1.5		5.5	5.0	-2.0		3.0	3.0	-2.0		1.0	2.0	-2.0		0.0
US Municipal		58.0	+0.0		58.0	45.0	+0.0		45.0	35.0	+0.0		35.0	26.0	+0.0		26.0	16.0	+0.0		16.0
US IG Corp		4.0	+1.0		5.0	3.0	+2.0		5.0	3.0	+2.0		5.0	2.0	+2.0		4.0	1.0	+2.0		3.0
US HY Corp		2.0	+0.0		2.0	3.0	+0.0		3.0	4.0	+0.0		4.0	5.0	+0.0		5.0	7.0	+0.0		7.0
<b>Int'l Fixed Income</b>		8.0	-2.0		6.0	8.0	-2.5		5.5	7.5	-2.0		5.5	8.0	-2.0		6.0	7.0	-2.0		5.0
Int'l Developed Markets		6.0	-2.0		4.0	5.0	-2.5		2.5	4.0	-2.0		2.0	3.0	-2.0		1.0	2.0	-2.0		0.0
Emerging Markets		2.0	+0.0		2.0	3.0	+0.0		3.0	3.5	+0.0		3.5	5.0	+0.0		5.0	5.0	+0.0		5.0
<b>Equity</b>		16.0	+2.0		18.0	30.0	+2.0		32.0	40.5	+2.0		42.5	51.0	+2.0		53.0	62.0	+2.0		64.0
<b>US Equity</b>		9.0	+2.0		11.0	18.0	+2.0		20.0	23.0	+2.0		25.0	29.0	+2.0		31.0	36.0	+2.0		38.0
US Large cap Growth		3.0	+0.5		3.5	5.0	+0.5		5.5	7.0	+0.5		7.5	9.0	+0.5		9.5	11.0	+0.5		11.5
US Large cap Value		3.0	+0.5		3.5	5.0	+0.5		5.5	7.0	+0.5		7.5	9.0	+0.5		9.5	11.0	+0.5		11.5
US Mid cap		2.0	+0.5		2.5	5.0	+0.5		5.5	6.0	+0.5		6.5	7.0	+0.5		7.5	9.0	+0.5		9.5
US Small cap		1.0	+0.5		1.5	3.0	+0.5		3.5	3.0	+0.5		3.5	4.0	+0.5		4.5	5.0	+0.5		5.5
<b>International Equity</b>		7.0	+0.0		7.0	12.0	+0.0		12.0	17.5	+0.0		17.5	22.0	+0.0		22.0	26.0	+0.0		26.0
Int'l Developed Markets		4.0	-0.5		3.5	7.0	-1.0		6.0	10.0	-1.0		9.0	12.5	-1.0		11.5	15.0	-1.0		14.0
Emerging Markets		3.0	+0.5		3.5	5.0	+1.0		6.0	7.5	+1.0		8.5	9.5	+1.0		10.5	11.0	+1.0		12.0
<b>Commodities</b>		4.0	+0.0		4.0	4.0	+0.0		4.0	5.0	+0.0		5.0	5.0	+0.0		5.0	5.0	+0.0		5.0

"WMR tactical deviation" legend: **Overweight** **Underweight** **Neutral** "Change" legend: ▲ Upgrade ▼ Downgrade \*Refers to moderate-risk profile.

<sup>1</sup>The current allocation column is the sum of the strategic asset allocation and the tactical deviation column.

Source: UBS and WMA AAC, 25 August 2016. See appendix for information regarding sources of strategic asset allocations and their suitability, investor risk profiles, and the interpretation of the suggested tactical deviations from the strategic asset allocations.

# Detailed asset allocation

## non-taxable with non-traditional assets

Investor risk profile		Conservative				Moderately conservative				Moderate				Moderately ag- gressive				Aggressive			
Change this month	All figures in %	Strategic asset allocation	CIO tactical deviation	Change this month	Current allocation¹	Strategic asset allocation	CIO tactical deviation	Change this month	Current allocation¹	Strategic asset allocation	CIO tactical deviation	Change this month	Current allocation¹	Strategic asset allocation	CIO tactical deviation	Change this month	Current allocation¹	Strategic asset allocation	CIO tactical deviation	Change this month	Current allocation¹
	Cash	0.0	+0.0		0.0	0.0	+0.0		0.0	0.0	+0.0		0.0	0.0	+0.0		0.0	0.0	+0.0		0.0
	Fixed Income	68.0	-2.0		66.0	56.0	-2.0		54.0	46.5	-2.0		44.5	39.0	-2.0		37.0	33.0	-2.0		31.0
	US Fixed Income	60.0	+0.0		60.0	49.0	+0.0		49.0	40.0	+0.0		40.0	32.5	+0.0		32.5	26.0	+0.0		26.0
	US Gov't	47.0	-1.0		46.0	36.0	-1.5		34.5	28.0	-2.0		26.0	19.5	-2.0		17.5	13.0	-2.0		11.0
	US Municipal	0.0	+0.0		0.0	0.0	+0.0		0.0	0.0	+0.0		0.0	0.0	+0.0		0.0	0.0	+0.0		0.0
	US IG Corp	9.0	+1.0		10.0	7.0	+1.5		8.5	5.0	+2.0		7.0	4.0	+2.0		6.0	2.0	+2.0		4.0
	US HY Corp	4.0	+0.0		4.0	6.0	+0.0		6.0	7.0	+0.0		7.0	9.0	+0.0		9.0	11.0	+0.0		11.0
	Int'l Fixed Income	8.0	-2.0		6.0	7.0	-2.0		5.0	6.5	-2.0		4.5	6.5	-2.0		4.5	7.0	-2.0		5.0
	Int'l Developed Markets	6.0	-2.0		4.0	4.0	-2.0		2.0	3.5	-2.0		1.5	2.5	-2.0		0.5	2.0	-2.0		0.0
	Emerging Markets	2.0	+0.0		2.0	3.0	+0.0		3.0	3.0	+0.0		3.0	4.0	+0.0		4.0	5.0	+0.0		5.0
	Equity	17.0	+2.0		19.0	28.0	+2.0		30.0	34.5	+2.0		36.5	42.0	+2.0		44.0	53.0	+2.0		55.0
	US Equity	10.0	+2.0		12.0	16.0	+2.0		18.0	20.5	+2.0		22.5	24.0	+2.0		26.0	31.0	+2.0		33.0
	US Large cap Growth	3.0	+0.5		3.5	5.0	+0.5		5.5	6.0	+0.5		6.5	7.5	+0.5		8.0	9.5	+0.5		10.0
	US Large cap Value	3.0	+0.5		3.5	5.0	+0.5		5.5	6.0	+0.5		6.5	7.5	+0.5		8.0	9.5	+0.5		10.0
	US Mid cap	2.5	+0.5		3.0	4.0	+0.5		4.5	5.5	+0.5		6.0	6.0	+0.5		6.5	8.0	+0.5		8.5
	US Small cap	1.5	+0.5		2.0	2.0	+0.5		2.5	3.0	+0.5		3.5	3.0	+0.5		3.5	4.0	+0.5		4.5
	International Equity	7.0	+0.0		7.0	12.0	+0.0		12.0	14.0	+0.0		14.0	18.0	+0.0		18.0	22.0	+0.0		22.0
	Int'l Developed Markets	4.0	-0.5		3.5	7.0	-1.0		6.0	8.0	-1.0		7.0	10.0	-1.0		9.0	13.0	-1.0		12.0
	Emerging Markets	3.0	+0.5		3.5	5.0	+1.0		6.0	6.0	+1.0		7.0	8.0	+1.0		9.0	9.0	+1.0		10.0
	Commodities	4.0	+0.0		4.0	4.0	+0.0		4.0	4.0	+0.0		4.0	5.0	+0.0		5.0	5.0	+0.0		5.0
	Non-traditional	11.0	+0.0		11.0	12.0	+0.0		12.0	15.0	+0.0		15.0	14.0	+0.0		14.0	9.0	+0.0		9.0
	Hedge Funds	11.0	+0.0		11.0	12.0	+0.0		12.0	10.0	+0.0		10.0	8.0	+0.0		8.0	3.0	+0.0		3.0
	Private Equity	0.0	+0.0		0.0	0.0	+0.0		0.0	5.0	+0.0		5.0	6.0	+0.0		6.0	6.0	+0.0		6.0
	Private Real Estate	0.0	+0.0		0.0	0.0	+0.0		0.0	0.0	+0.0		0.0	0.0	+0.0		0.0	0.0	+0.0		0.0

"WMR tactical deviation" legend: **Overweight** **Underweight** Neutral "Change" legend: ▲ Upgrade ▼ Downgrade \*Refers to moderate-risk profile.

<sup>1</sup>The current allocation column is the sum of the strategic asset allocation and the tactical deviation column.

Source: UBS and WMA AAC, 25 August 2016. See appendix for information regarding sources of strategic asset allocations and their suitability, investor risk profiles, and the interpretation of the suggested tactical deviations from the strategic asset allocations.

# Detailed asset allocation

## non-taxable without non-traditional assets

Investor risk profile		Conservative				Moderately conservative				Moderate				Moderately aggressive				Aggressive			
Change this month	All figures in %	Strategic asset allocation	CIO tactical deviation	Change this month	Current allocation <sup>1</sup>	Strategic asset allocation	CIO tactical deviation	Change this month	Current allocation <sup>1</sup>	Strategic asset allocation	CIO tactical deviation	Change this month	Current allocation <sup>1</sup>	Strategic asset allocation	CIO tactical deviation	Change this month	Current allocation <sup>1</sup>	Strategic asset allocation	CIO tactical deviation	Change this month	Current allocation <sup>1</sup>
<b>Cash</b>		0.0	+0.0		0.0	0.0	+0.0		0.0	0.0	+0.0		0.0	0.0	+0.0		0.0	0.0	+0.0		0.0
<b>Fixed Income</b>		78.0	-2.0		76.0	65.0	-2.0		63.0	55.0	-2.0		53.0	46.0	-2.0		44.0	36.0	-2.0		34.0
<b>US Fixed Income</b>		69.0	+0.0		69.0	57.0	+0.0		57.0	47.0	+0.0		47.0	38.0	+0.0		38.0	29.0	+0.0		29.0
US Gov't		55.0	-1.0		54.0	42.0	-1.5		40.5	32.0	-2.0		30.0	23.0	-2.0		21.0	13.0	-2.0		11.0
US Municipal		0.0	+0.0		0.0	0.0	+0.0		0.0	0.0	+0.0		0.0	0.0	+0.0		0.0	0.0	+0.0		0.0
US IG Corp		10.0	+1.0		11.0	8.0	+1.5		9.5	6.0	+2.0		8.0	4.0	+2.0		6.0	3.0	+2.0		5.0
US HY Corp		4.0	+0.0		4.0	7.0	+0.0		7.0	9.0	+0.0		9.0	11.0	+0.0		11.0	13.0	+0.0		13.0
<b>Int'l Fixed Income</b>		9.0	-2.0		7.0	8.0	-2.0		6.0	8.0	-2.0		6.0	8.0	-2.0		6.0	7.0	-2.0		5.0
Int'l Developed Markets		7.0	-2.0		5.0	5.0	-2.0		3.0	4.0	-2.0		2.0	3.0	-2.0		1.0	2.0	-2.0		0.0
Emerging Markets		2.0	+0.0		2.0	3.0	+0.0		3.0	4.0	+0.0		4.0	5.0	+0.0		5.0	5.0	+0.0		5.0
<b>Equity</b>		18.0	+2.0		20.0	31.0	+2.0		33.0	41.0	+2.0		43.0	50.0	+2.0		52.0	59.0	+2.0		61.0
<b>US Equity</b>		10.0	+2.0		12.0	18.0	+2.0		20.0	23.0	+2.0		25.0	28.0	+2.0		30.0	33.0	+2.0		35.0
US Large cap Growth		3.0	+0.5		3.5	5.5	+0.5		6.0	7.0	+0.5		7.5	8.5	+0.5		9.0	10.0	+0.5		10.5
US Large cap Value		3.0	+0.5		3.5	5.5	+0.5		6.0	7.0	+0.5		7.5	8.5	+0.5		9.0	10.0	+0.5		10.5
US Mid cap		3.0	+0.5		3.5	5.0	+0.5		5.5	6.0	+0.5		6.5	7.0	+0.5		7.5	9.0	+0.5		9.5
US Small cap		1.0	+0.5		1.5	2.0	+0.5		2.5	3.0	+0.5		3.5	4.0	+0.5		4.5	4.0	+0.5		4.5
<b>International Equity</b>		8.0	+0.0		8.0	13.0	+0.0		13.0	18.0	+0.0		18.0	22.0	+0.0		22.0	26.0	+0.0		26.0
Int'l Developed Markets		4.0	-0.5		3.5	8.0	-1.0		7.0	10.0	-1.0		9.0	12.0	-1.0		11.0	14.0	-1.0		13.0
Emerging Markets		4.0	+0.5		4.5	5.0	+1.0		6.0	8.0	+1.0		9.0	10.0	+1.0		11.0	12.0	+1.0		13.0
<b>Commodities</b>		4.0	+0.0		4.0	4.0	+0.0		4.0	4.0	+0.0		4.0	4.0	+0.0		4.0	5.0	+0.0		5.0

"WMR tactical deviation" legend: Overweight Underweight Neutral "Change" legend: ▲ Upgrade ▼ Downgrade \*Refers to moderate-risk profile.

<sup>1</sup>The current allocation column is the sum of the strategic asset allocation and the tactical deviation column.

Source: UBS and WMA AAC, 25 August 2016. See appendix for information regarding sources of strategic asset allocations and their suitability, investor risk profiles, and the interpretation of the suggested tactical deviations from the strategic asset allocations.



# Detailed asset allocation

## all equity and all fixed income models

	All equity				All fixed income, taxable				All fixed income, non-taxable			
All figures in %	Strategic asset allocation	CIO tactical deviation	Change this month	Current allocation <sup>1</sup>	Strategic asset allocation	CIO tactical deviation	Change this month	Current allocation <sup>1</sup>	Strategic asset allocation	CIO tactical deviation	Change this month	Current allocation <sup>1</sup>
<b>Cash</b>	<b>5.0</b>	<b>-2.0</b>		<b>3.0</b>	<b>5.0</b>	<b>+0.0</b>		<b>5.0</b>	<b>5.0</b>	<b>+0.5</b>		<b>5.5</b>
<b>Fixed Income</b>	<b>0.0</b>	<b>+0.0</b>		<b>0.0</b>	<b>95.0</b>	<b>+0.0</b>		<b>95.0</b>	<b>95.0</b>	<b>-0.5</b>		<b>94.5</b>
<b>US Fixed Income</b>	<b>0.0</b>	<b>+0.0</b>		<b>0.0</b>	<b>82.0</b>	<b>+3.5</b>		<b>85.5</b>	<b>81.0</b>	<b>+3.0</b>		<b>84.0</b>
US Gov't – total market	0.0	+0.0		0.0	9.0	-3.5		5.5	16.0	+4.5		20.5
US Gov't – 1~3 years	0.0	+0.0		0.0	0.0	+0.0		0.0	6.0	-1.5		4.5
US Gov't – 3~7 years	0.0	+0.0		0.0	0.0	+0.0		0.0	14.0	-2.5		11.5
US Gov't – 7~10 years	0.0	+0.0		0.0	0.0	+0.0		0.0	10.0	-1.5		8.5
US MBS	0.0	+0.0		0.0	0.0	+0.0		0.0	9.0	+0.0		9.0
US Munis – total market	0.0	+0.0		0.0	28.0	+2.0		30.0	0.0	+0.0		0.0
US Munis – short duration	0.0	+0.0		0.0	11.0	+0.0		11.0	0.0	+0.0		0.0
US Munis – long duration	0.0	+0.0		0.0	22.0	+1.0		23.0	0.0	+0.0		0.0
US Investment Grade	0.0	+0.0		0.0	5.0	+4.0		9.0	10.5	+4.0		14.5
US High Yield	0.0	+0.0		0.0	7.0	+0.0		7.0	15.5	+0.0		15.5
<b>Int'l Fixed Income</b>	<b>0.0</b>	<b>+0.0</b>		<b>0.0</b>	<b>13.0</b>	<b>-3.5</b>		<b>9.5</b>	<b>14.0</b>	<b>-3.5</b>		<b>10.5</b>
Int'l Developed Markets	0.0	+0.0		0.0	7.0	-3.5		3.5	7.0	-3.5		3.5
Emerging Markets	0.0	+0.0		0.0	6.0	+0.0		6.0	7.0	+0.0		7.0
<b>Equity</b>	<b>95.0</b>	<b>+2.0</b>		<b>97.0</b>	<b>0.0</b>	<b>+0.0</b>		<b>0.0</b>	<b>0.0</b>	<b>+0.0</b>		<b>0.0</b>
<b>US Equity</b>	<b>54.0</b>	<b>+2.0</b>		<b>56.0</b>	<b>0.0</b>	<b>+0.0</b>		<b>0.0</b>	<b>0.0</b>	<b>+0.0</b>		<b>0.0</b>
US Large-cap Growth	7.0	+0.5		7.5	0.0	+0.0		0.0	0.0	+0.0		0.0
US Large-cap Value	7.0	+0.5		7.5	0.0	+0.0		0.0	0.0	+0.0		0.0
US Large-cap Total Market	19.0	-6.0		13.0	0.0	+0.0		0.0	0.0	+0.0		0.0
Consumer discretionary	0.0	+3.0		3.0	0.0	+0.0		0.0	0.0	+0.0		0.0
Healthcare	0.0	+3.0		3.0	0.0	+0.0		0.0	0.0	+0.0		0.0
US Mid-cap Equity	14.0	+0.5		14.5	0.0	+0.0		0.0	0.0	+0.0		0.0
US Small-cap Equity	7.0	+0.5		7.5	0.0	+0.0		0.0	0.0	+0.0		0.0
<b>International Equity</b>	<b>41.0</b>	<b>+0.0</b>		<b>41.0</b>	<b>0.0</b>	<b>+0.0</b>		<b>0.0</b>	<b>0.0</b>	<b>+0.0</b>		<b>0.0</b>
Int'l Developed Markets	23.5	-1.0		22.5	0.0	+0.0		0.0	0.0	+0.0		0.0
Global EM Equity	17.5	-5.0		12.5	0.0	+0.0		0.0	0.0	+0.0		0.0
China	0.0	+3.0		3.0	0.0	+0.0		0.0	0.0	+0.0		0.0
India	0.0	+3.0		3.0	0.0	+0.0		0.0	0.0	+0.0		0.0

"WMR tactical deviation" legend: **Overweight** **Underweight** Neutral

<sup>1</sup>The current allocation column is the sum of the strategic asset allocation and the tactical deviation column.

Source: UBS and WMA AAC, 25 August 2016. See appendix for information regarding sources of strategic asset allocations and their suitability, investor risk profiles and the interpretation of the suggested tactical deviations from the strategic asset allocations.

### Publication note

The All Equity and All Fixed Income portfolios complement our balanced portfolios and offer more granular implementation of our House View. While we generally do not recommend that investors hold portfolios consisting of only stocks or only bonds, the All Equity and All Fixed Income portfolios can be used by investors who want to complement their existing holdings. It is also possible to combine the All Equity portfolio with one of the All Fixed Income portfolios to generate a balanced portfolio. The tactical tilts in the portfolios are based on the corresponding tilts in our balanced portfolios (moderate risk profile, without alternative investments).

A special feature of the All Equity portfolio is that it includes "carve-outs": 3% allocations to our preferred sectors within US large-caps as well as our preferred countries within both international developed markets and the emerging markets. A maximum of two sectors/countries of each type may be selected for carve-outs. The amount of cash in the All Equity portfolio will vary one-for-one with the overall overweight/underweight on equities in the balanced portfolio, subject to a 3% maximum. This allows us to express a tactical preference between stocks and bonds.

The All Fixed Income portfolios include both taxable and non-taxable versions. These are based on the fixed income portion of the balanced portfolios, with the non-taxable version incorporating an additional allocation to Mortgage Backed Securities. In addition, the All Fixed Income portfolios include allocations to government bonds (Munis in the taxable version, Treasuries in the non-taxable version) of different maturities, allowing views on duration to be expressed. Cash is set at 5% of the portfolios, with small deviations possible due to rounding.

# Portfolio analytics

The portfolio analytics shown for each risk profile's benchmark allocations are based on estimated forward-looking return and standard deviation assumptions (capital market assumptions), which are based on UBS proprietary research. The development process includes a review of a variety of factors, including the return, risk, correlations and historical performance of various asset classes, inflation and risk premium. These capital market assumptions do not assume any particular investment time horizon. The process assumes a situation where the supply and demand for investments is in balance, and in which expected returns of all asset classes are a reflection of their expected risk and correlations regardless of time frame. Please note that these assumptions are not guarantees and are subject to change. UBS has changed its risk and return assumptions in the past and may do so in the future. Neither UBS nor your Financial Advisor is required to provide you with an updated analysis based upon changes to these or other underlying assumptions.

In order to create the analysis shown, the rates of return for each asset class are combined in the same proportion as the asset allocations illustrated (e.g., if the asset allocation indicates 40% equities, then 40% of the results shown for the allocation will be based upon the estimated hypothetical return and standard deviation assumptions shown below).

You should understand that the analysis shown and assumptions used are hypothetical estimates provided for your general information. The results are not guarantees and pertain to the asset allocation and/or asset class in general, not the performance of specific securities or investments. Your actual results may vary significantly from the results shown in this report, as can the performance of any individual security or investment.

Risk Profile ==>>	Conservative	Moderately conservative	Moderate	Moderately aggressive	Aggressive
<b>Taxable with non-traditional assets</b>					
Estimated Return	4.4%	5.1%	5.9%	6.4%	7.0%
Estimated Risk	5.6%	7.4%	9.6%	11.5%	13.5%
<b>Taxable without non-traditional assets</b>					
Estimated Return	4.0%	4.8%	5.5%	6.1%	6.8%
Estimated Risk	5.4%	7.5%	9.5%	11.5%	13.5%
<b>Non-taxable with non-traditional assets</b>					
Estimated Return	4.3%	5.0%	5.8%	6.4%	7.0%
Estimated Risk	5.5%	7.4%	9.5%	11.4%	13.4%
<b>Non-taxable without non-traditional assets</b>					
Estimated Return	4.0%	4.8%	5.5%	6.1%	6.8%
Estimated Risk	5.4%	7.5%	9.5%	11.4%	13.5%

Asset Class	Capital Market Assumptions	
	Annual total return	Annual risk
US Cash	2.5%	0.5%
US Government Fixed Income	2.2%	4.3%
US Municipal Fixed Income	2.9%	4.7%
US Corporate Investment Grade Fixed Income	3.5%	5.9%
US Corporate High Yield Fixed Income	5.6%	11.7%
International Developed Markets Fixed Income	4.0%	9.0%
Emerging Markets Fixed Income	4.9%	9.1%
US Large-cap Equity	7.5%	16.8%
US Mid-cap Equity	8.4%	19.6%
US Small-cap Equity	8.6%	21.8%
International Developed Markets Equity	8.5%	19.7%
Emerging Markets Equity	10.0%	25.5%
Commodities	6.4%	18.9%
Hedge Funds	6.2%	6.7%
Private Equity	11.8%	24.4%
Private Real Estate	8.5%	11.8%

# Additional asset allocation models

## US equity sector allocation, in %

For US equity subsector recommendations please see the "Equity Preference List" for each sector. These reports are published on a monthly basis and can be found on the Online Services website in the Research > Equities section.

	S&P 500 Benchmark allocation <sup>1</sup>	CIO WMR tactical deviation <sup>2</sup>				Current allocation <sup>3</sup>
		Numeric		Symbol		
		Previous	Current	Previous	Current	
Consumer Discretionary	12.3	+2.0	+2.0	++	++	14.3
Consumer Staples	10.1	-1.0	-1.0	–	–	9.1
Energy	7.1	+1.0	+1.0	+	+	8.1
Financials	15.9	+0.0	+0.0	n	n	15.9
Healthcare	14.7	+2.0	+2.0	++	++	16.7
Industrials	10.0	+0.0	+0.0	n	n	10.0
Information Technology	20.9	+1.0	+1.0	+	+	21.9
Materials	2.9	-2.0	-2.0	--	--	0.9
Telecom	2.7	-1.0	-1.0	–	–	1.7
Utilities	3.3	-2.0	-2.0	--	--	1.3

Source: S&P, UBS, as of 25 August 2016

Note: The benchmark allocation, as well as the tactical deviations, are intended to be applicable to the US equity portion of a portfolio across investor risk profiles.

## International developed markets (non-US) equity module, in %

	Benchmark allocation <sup>1</sup>	CIO WMR tactical deviation <sup>2</sup>		Current allocation <sup>3</sup>
		Previous	Current	
EMU / Eurozone	28.0	+5.0	+2.0	30.0
UK	20.0	+5.0	+2.0	22.0
Japan	19.0	+5.0	+2.0	21.0
Australia	7.0	-7.0	+2.0	9.0
Canada	9.0	+0.0	+0.0	9.0
Switzerland	8.0	-8.0	-8.0	0.0
Other	9.0	+0.0	+0.0	9.0

Source: UBS, as of 25 August 2016

## International developed markets (non-US) fixed income module, in %

The US Taxable Fixed Income Allocation table appears in Fixed Income Strategist, which is published on a monthly basis and can be found in the Fixed Income section of the Online Services Research website.

	Benchmark allocation <sup>1</sup>	CIO WMR tactical deviation <sup>2</sup>		Current allocation <sup>3</sup>
		Previous	Current	
EMU / Eurozone	42.0	-5.0	-5.0	37.0
UK	9.0	+3.5	+0.0	9.0
Japan	32.0	+3.5	+0.0	32.0
Other	17.0	-2.0	+5.0	22.0

Source: UBS, as of 25 August 2016

### Footnotes

<sup>1</sup> For the first table on this page, the benchmark allocation is based on S&P 500 weights. For the second and third tables on this page, the benchmark allocation refers to a moderate risk profile and represents the relative market capitalization weights of each country or region.

<sup>2</sup> See "Deviations from strategic asset allocation or benchmark allocation" in the appendix for an explanation regarding the interpretation of the suggested tactical deviations from benchmark. The "current" column refers to the tactical deviation that applies as of the date of this publication. The "previous" column refers to the tactical deviation that was in place at the date of the previous edition of *UBS House View* or the last *UBS House View Update*.

<sup>3</sup> The current allocation column is the sum of the CIO WMR tactical deviation columns and (the S&P 500 benchmark allocation for the first table on this page) (the benchmark allocation for the second and third tables on this page).

# Tactical asset allocation performance measurement

The performance calculations shown in Table A commence on 25 January 2013, the first date upon which the Investment Strategy Guide was published following the release of the new UBS WMA strategic asset allocation (SAA) models. The performance is based on the SAA without non-traditional assets for a moderate risk profile investor, and the SAA with the tactical shift (see detailed asset allocation tables where the SAA with the tactical shift is referred to as "current allocation"). Performance is calculated utilizing the returns of the indices identified in Table B as applied to the respective allocations in the SAA and the SAA with the tactical shift. For example, if US Mid Cap Equity is allocated 10% in the SAA and 12% in the SAA with the tactical shift, the US Mid Cap Equity index respectively contributed to 10% and 12% of the results shown. Prior to 25 January 2013, CIO WMR published tactical asset allocation recommendations in the Investment Strategy Guide using a different set of asset classes and sectors. The performance of these tactical recommendations is reflected in Table C.

The performance attributable to the CIO WMR tactical deviations is reflected in the column in Tables A and C labeled "Excess return," which shows the difference between the performance of the SAA and the performance of the SAA with the tactical shift. The "Information ratio" is a risk-adjusted

performance measure, which adjusts the excess returns for the tracking error risk of the tactical deviations. Specifically the information ratio is calculated as the ratio of the annualized excess return over a given time period and the annualized standard deviation of daily excess returns over the same period. Additional background information regarding the computation of the information ratio figures provided below are available upon request.

The calculations assume that the portfolios are rebalanced whenever changes are made to tactical deviations, typically upon publication of the Investment Strategy Guide on a monthly basis. Occasionally, changes in the tactical deviations are made intra-month when warranted by market conditions and communicated through an Investment Strategy Guide Update. The computations assume portfolio rebalancing upon such intra-month changes as well. Performance shown is based on total returns, but does not include transaction costs, such as commissions, fees, margin interest, and interest charges. Actual total returns adjusted for such transaction costs will be reduced. A complete record of all the recommendations upon which this performance report is based is available from UBS Financial Services Inc. upon written request. Past performance is not an indication of future results.

**Table A: Moderate risk profile performance measurement (25 January 2013 to present)**

	SAA	SAA with tactical shift	Excess return	Information ratio (annualized)	Russell 3000 stock index (total return)	Barclays Capital US Aggregate bond index (total return)
25 January 2013 to 31 March 2013	0.79%	0.83%	0.04%	+0.9	5.59%	0.11%
2Q 2013	-2.18%	-2.14%	0.04%	+0.3	2.69%	-2.33%
3Q 2013	3.60%	3.86%	0.26%	+2.4	6.35%	0.57%
4Q 2013	3.05%	3.23%	0.18%	+2.9	10.10%	-0.14%
1Q 2014	2.56%	2.53%	-0.03%	-0.2	1.97%	1.84%
2Q 2014	3.44%	3.49%	0.05%	+0.3	4.87%	2.04%
3Q 2014	-1.54%	-1.71%	-0.16%	-1.2	0.01%	0.17%
4Q 2014	0.47%	0.73%	0.26%	+1.3	5.24%	1.79%
1Q 2015	1.38%	1.69%	0.31%	+2.1	1.80%	1.61%
2Q 2015	-0.18%	-0.19%	-0.01%	-0.1	0.14%	-1.68%
3Q 2015	-4.67%	-5.08%	-0.41%	-2.4	-7.25%	1.23%
4Q 2015	1.61%	1.67%	0.06%	+0.5	6.27%	-0.57%
1Q 2016	2.11%	1.72%	-0.39%	-3.7	0.97%	3.03%
2Q 2016	2.81%	2.88%	0.08%	+1.1	2.63%	2.21%
3Q 2016 to date	2.56%	2.63%	0.07%	+1.7	4.33%	0.55%
2016 year to date	7.66%	7.40%	-0.26%	-1.2	8.11%	5.89%
Since inception (25 January 2013)	16.56%	16.92%	0.35%	+0.2	55.23%	10.80%

Source: UBS, as of 24 August 2016

# Tactical asset allocation performance measurement

**Table B: SAA for moderate risk profile investor, and underlying indices (all figures in %)**

<b>25 Jan 2013 to present</b>	
US Large Cap Growth (Russell 1000 Growth)	7.0
US Large Cap Value (Russell 1000 Value)	7.0
US Mid Cap (Russell Mid Cap)	6.0
US Small Cap (Russell 2000)	3.0
International Dev. Eq. (MSCI EAFE)	10.0
Emerging Markets Eq. (MSCI EMF)	7.5
US Government Fixed Income (BarCap US Agg Government)	5.0
US Municipal Fixed Income (BarCap Municipal Bond)	35.0
US Investment Grade Fixed Income (BarCap US Agg Credit)	3.0
US Corporate High Yield Fixed Income (BarCap US Agg Corp HY)	4.0
International Dev. Fixed Income (BarCap Global Agg xUS)	4.0
Emerging Markets Fixed Income (50% BarCap EM Gov and 50% BarCap Global EM (USD))	3.5
Commodities (Dow Jones-UBS Commodity Index)	5.0

Source: UBS

The performance calculations shown in Table C, which start on 25 August 2008 and end on 24 January 2013, have been provided for historical information purposes only. They are based on prior SAAs (referred to as benchmark allocations) with non-traditional assets for a moderate risk profile investor, and on prior SAAs with tactical shifts as published in the Investment Strategy Guide during the same time period. Performance is calculated utilizing the returns of the indices identified in Table D as applied to the respective allocations in the SAA and the SAA with the tactical shift. See the discussion in connection with Table A, previous page, regarding the meanings of the “Excess return” and “Information ratio” columns and how the “Information ratio” column is calculated.

From 25 August 2008 through 27 May 2009, the Investment Strategy Guide had at times published a more detailed set of tactical deviations, whereby the categories “Non-US Developed Equities” and “Non-US Fixed Income” were further subdivided into regional blocks. Only the cumulative recommendations at the level of “Non-US Developed Equities” and “Non-US Fixed Income” were taken into account in calculating the performance shown in Table C opposite. Prior to 25 August 2008, WMR published tactical asset allocation recommendations in the “US Asset Allocation Strategist” using a less comprehensive set of asset classes and sectors, which makes a comparison with the subsequent models difficult.

# Tactical asset allocation performance measurement

**Table C: Moderate risk profile performance measurement (25 August 2008 to 24 January 2013)**

	Benchmark Allocations (SAA)	Benchmark Allocation (SAA) with tactical shift	Excess return	Information ratio (annualized)	Russell 3000 stock index (total return)	Barclays Capital US Aggregate bond index (total return)
25 Aug 08 to 31 Dec 08	-16.59%	-15.64%	0.96%	+2.0	-29.00%	3.33%
2009 Q1	-5.52%	-5.45%	0.07%	+0.3	-10.80%	0.12%
2009 Q2	11.18%	11.37%	0.18%	+1.0	16.82%	1.78%
2009 Q3	10.44%	11.07%	0.63%	+2.1	16.31%	3.74%
2009 Q4	2.99%	3.30%	0.31%	+1.1	5.90%	0.20%
2010 Q1	2.74%	2.56%	-0.18%	-0.9	5.94%	1.78%
2010 Q2	-4.56%	-4.87%	-0.31%	-1.4	-11.32%	3.49%
2010 Q3	8.34%	7.99%	-0.35%	-2.1	11.53%	2.48%
2010 Q4	5.18%	5.17%	-0.01%	-0.1	11.59%	-1.30%
2011 Q1	3.23%	3.15%	-0.08%	-0.4	6.38%	0.42%
2011 Q2	0.62%	0.47%	-0.16%	-0.9	-0.03%	2.29%
2011 Q3	-7.65%	-8.56%	-0.90%	-2.5	-15.28%	3.82%
2011 Q4	4.66%	4.39%	-0.27%	-0.8	12.12%	1.12%
2012 Q1	5.89%	5.41%	-0.48%	-2.3	12.87%	0.30%
2012 Q2	-1.59%	-1.57%	0.02%	+0.2	-3.15%	2.06%
2012 Q3	4.18%	4.08%	-0.10%	-1.1	6.23%	1.59%
2012 Q4	0.69%	0.65%	-0.04%	-0.7	0.25%	0.21%
01 Jan 13 to 24 Jan 13	2.17%	2.20%	0.03%	+2.5	5.19%	-0.23%
Since inception	24.86%	24.10%	-0.76%	-0.1	31.81%	30.76%

Source: UBS

**Table D: SAAs for moderate risk profile investor, and underlying indices (all figures in %)**

25 Aug 2008 to 23 Feb 2009		24 Feb 2009 to 24 Jan 2013	
US Large Cap Value (Russell 1000 Value)	12.5	US Large Cap Value (Russell 1000 Value)	11.0
US Large Cap Growth (Russell 1000 Growth)	12.5	US Large Cap Growth (Russell 1000 Growth)	11.0
US Small Cap Value (Russell 2000 Value)	2.0	US Mid Cap (Russell Midcap)	5.0
US Small Cap Growth (Russell 2000 Growth)	2.0	US Small Cap (Russell 2000)	3.0
US REITs (FTSE NAREIT All REITs)	1.5	US REITs (FTSE NAREIT All REITs)	2.0
Non-US Dev. Eq. (MSCI Gross World ex-US)	10.5	Developed Markets (MSCI Gross World ex-US)	10.0
Emerging Markets Eq. (MSCI Gross EM USD)	2.0	Emerging Markets (MSCI Gross EM USD)	2.0
US Fixed Income (BarCap US Aggregate)	30.0	US Fixed Income (BarCap US Aggregate)	29.0
Non-US Fixed Income (BarCap Global Aggregate ex-USD)	8.0	Non-US Fixed Income (BarCap Global Aggregate ex-USD)	8.0
Cash (JP Morgan Cash Index USD 1 month)	2.0	Cash (JP Morgan Cash Index USD 1 month)	2.0
Commodities (DJ UBS total return index)	5.0	Commodities (DJ UBS total return index)	5.0
Alternative Investments (HFRX Equal Weighted Strategies)	12.0	Alternative Investments (HFRX Equal Weighted Strategies)	12.0

Source: UBS

# Investment committee

## Global Investment Process and Committee description

The UBS investment process is designed to achieve replicable, high quality results through applying intellectual rigor, strong process governance, clear responsibility and a culture of challenge.

Based on the analyses and assessments conducted and vetted throughout the investment process, the Chief Investment Officer (CIO) formulates the UBS Wealth Management Investment House View (e.g., overweight, neutral, underweight stance for asset classes and market segments relative to their benchmark allocation) at the Global Investment Committee (GIC). Senior investment professionals from across UBS, complemented by selected external experts, debate and rigorously challenge the investment strategy to ensure consistency and risk control.

## Global Investment Committee composition

The GIC is comprised of 12 members, representing top market and investment expertise from across all divisions of UBS:

- Mark Haefele (Chair)
- Mark Andersen
- Jorge Mariscal
- Mads Pedersen
- Mike Ryan
- Simon Smiles
- Tan Min Lan
- Themis Themistocleous
- Paul Donovan (\*)
- Dawn Fitzpatrick (\*)
- Bruno Marxer (\*)
- Andreas Koester (\*)

(\*) Business areas distinct from Chief Investment Office/Wealth Management Research

## WMA Asset Allocation Committee description

We recognize that a globally derived house view is most effective when complemented by local perspective and application. As such, UBS has formed a Wealth Management Americas Asset Allocation Committee (WMA AAC). WMA AAC is responsible for the development and monitoring of UBS WMA's strategic asset allocation models and capital market assumptions. The WMA AAC sets parameters for the CIO WMR Americas Investment Strategy Group to follow during the translation process of the GIC's House Views and the incorporation of US-specific asset class views into the US-specific tactical asset allocation models.

## WMA Asset Allocation Committee composition

The WMA Asset Allocation Committee is comprised of five members:

- Mike Ryan
- Michael Crook
- Richard Hollmann (\*)
- Jeremy Zirin
- Stephen Freedman

(\*) Business areas distinct from Chief Investment Office/Wealth Management Research



# Explanations about asset classes

## Sources of strategic asset allocations and investor risk profiles

Strategic asset allocations represent the longer-term allocation of assets that is deemed suitable for a particular investor. The strategic asset allocation models discussed in this publication, and the capital market assumptions used for the strategic asset allocations, were developed and approved by the WMA AAC.

The strategic asset allocations are provided for illustrative purposes only and were designed by the WMA AAC for hypothetical US investors with a total return objective under five different Investor Risk Profiles ranging from conservative to aggressive. In general, strategic asset allocations will differ among investors according to their individual circumstances, risk tolerance, return objectives and time horizon. Therefore, the strategic asset allocations in this publication may not be suitable for all investors or investment goals and should not be used as the sole basis of any investment decision. Minimum net worth requirements may apply to allocations to non-traditional assets. As always, please consult your UBS Financial Advisor to see how these weightings should be applied or modified according to your individual profile and investment goals.

The process by which the strategic asset allocations were derived is described in detail in the publication entitled "UBS WMA's Capital Markets Model: Explained, Part II: Methodology," published on 22 January 2013. Your Financial Advisor can provide you with a copy.

## Deviations from strategic asset allocation or benchmark allocation

The recommended tactical deviations from the strategic asset allocation or benchmark allocation are provided by the Global Investment Committee and the Investment Strategy Group within CIO Wealth Management Research Americas. They reflect the short- to medium-term assessment of market opportunities and risks in the respective asset classes and market segments. Positive/zero/negative tactical deviations correspond to an overweight/neutral/underweight stance for each respective asset class and market segment relative to their strategic allocation. The current allocation is the sum of the strategic asset allocation and the tactical deviation.

Note that the regional allocations on the Equities and Bonds pages in *UBS House View* are provided on an unhedged basis (i.e., it is assumed that investors carry the underlying currency risk of such investments) unless otherwise stated. Thus, the deviations from the strategic asset allocation reflect the views of the underlying equity and bond markets in combination with the assessment of the associated currencies. The detailed asset allocation tables integrate the country preferences within each asset class with the asset class preferences in *UBS House View*.

## Scale for tactical deviation charts

Symbol	Description/Definition	Symbol	Description/Definition	Symbol	Description/Definition
+	moderate overweight vs. benchmark	–	moderate underweight vs. benchmark	n	neutral, i.e., on benchmark
++	overweight vs. benchmark	– –	underweight vs. benchmark	n/a	not applicable
+++	strong overweight vs. benchmark	– – –	strong underweight vs. benchmark		

Source: UBS

# Appendix

## Emerging Market Investments

Investors should be aware that Emerging Market assets are subject to, among others, potential risks linked to currency volatility, abrupt changes in the cost of capital and the economic growth outlook, as well as regulatory and sociopolitical risk, interest rate risk and higher credit risk. Assets can sometimes be very illiquid and liquidity conditions can abruptly worsen. WMR generally recommends only those securities it believes have been registered under Federal US registration rules (Section 12 of the Securities Exchange Act of 1934) and individual State registration rules (commonly known as “Blue Sky” laws). Prospective investors should be aware that to the extent permitted under US law, WMR may from time to time recommend bonds that are not registered under US or State securities laws. These bonds may be issued in jurisdictions where the level of required disclosures to be made by issuers is not as frequent or complete as that required by US laws.

For more background on emerging markets generally, see the WMR Education Notes “Investing in Emerging Markets (Part 1): Equities,” 27 August 2007, “Emerging Market Bonds: Understanding Emerging Market Bonds,” 12 August 2009 and “Emerging Markets Bonds: Understanding Sovereign Risk,” 17 December 2009.

Investors interested in holding bonds for a longer period are advised to select the bonds of those sovereigns with the highest credit ratings (in the investment-grade band). Such an approach should decrease the risk that an investor could end up holding bonds on which the sovereign has defaulted. Subinvestment-grade bonds are recommended only for clients with a higher risk tolerance and who seek to hold higher-yielding bonds for shorter periods only.

## Nontraditional Assets

**Nontraditional asset classes are alternative investments that include hedge funds, private equity, real estate, and managed futures (collectively, alternative investments).** Interests of alternative investment funds are sold only to qualified investors,

and only by means of offering documents that include information about the risks, performance and expenses of alternative investment funds, and which clients are urged to read carefully before subscribing and retain. An investment in an alternative investment fund is speculative and involves significant risks. Specifically, these investments (1) are not mutual funds and are not subject to the same regulatory requirements as mutual funds; (2) may have performance that is volatile, and investors may lose all or a substantial amount of their investment; (3) may engage in leverage and other speculative investment practices that may increase the risk of investment loss; (4) are long-term, illiquid investments; there is generally no secondary market for the interests of a fund, and none is expected to develop; (5) interests of alternative investment funds typically will be illiquid and subject to restrictions on transfer; (6) may not be required to provide periodic pricing or valuation information to investors; (7) generally involve complex tax strategies and

there may be delays in distributing tax information to investors; (8) are subject to high fees, including management fees and other fees and expenses, all of which will reduce profits.

Interests in alternative investment funds are not deposits or obligations of, or guaranteed or endorsed by, any bank or other insured depository institution, and are not federally insured by the Federal Deposit Insurance Corporation, the Federal Reserve Board, or any other governmental agency. Prospective investors should understand these risks and have the financial ability and willingness to accept them for an extended period of time before making an investment in an alternative investment fund, and should consider an alternative investment fund as a supplement to an overall investment program.

In addition to the risks that apply to alternative investments generally, the following are additional risks related to an investment in these strategies:

- **Hedge Fund Risk:** There are risks specifically associated with investing in hedge funds, which may include risks associated with investing in short sales, options, small-cap stocks, “junk bonds,” derivatives, distressed securities, non-US securities and illiquid investments.
- **Managed Futures:** There are risks specifically associated with investing in managed futures programs. For example, not all managers focus on all strategies at all times, and managed futures strategies may have material directional elements.
- **Real Estate:** There are risks specifically associated with investing in real estate products and real estate investment trusts. They involve risks associated with debt, adverse changes in general economic or local market conditions, changes in governmental, tax, real estate and zoning laws or regulations, risks associated with capital calls and, for some real estate products, the risks associated with the ability to qualify for favorable treatment under the federal tax laws.
- **Private Equity:** There are risks specifically associated with investing in private equity. Capital calls can be made on short notice, and the failure to meet capital calls can result in significant adverse consequences including, but not limited to, a total loss of investment.
- **Foreign Exchange/Currency Risk:** Investors in securities of issuers located outside of the United States should be aware that even for securities denominated in US dollars, changes in the exchange rate between the US dollar and the issuer’s “home” currency can have unexpected effects on the market value and liquidity of those securities. Those securities may also be affected by other risks (such as political, economic or regulatory changes) that may not be readily known to a US investor.

# Disclaimer

Chief Investment Office (CIO) Wealth Management (WM) Research is published by UBS Wealth Management and UBS Wealth Management Americas, Business Divisions of UBS AG (UBS) or an affiliate thereof. CIO WM Research reports published outside the US are branded as Chief Investment Office WM. In certain countries UBS AG is referred to as UBS SA. This publication is for your information only and is not intended as an offer, or a solicitation of an offer, to buy or sell any investment or other specific product. The analysis contained herein does not constitute a personal recommendation or take into account the particular investment objectives, investment strategies, financial situation and needs of any specific recipient. It is based on numerous assumptions. Different assumptions could result in materially different results. We recommend that you obtain financial and/or tax advice as to the implications (including tax) of investing in the manner described or in any of the products mentioned herein. Certain services and products are subject to legal restrictions and cannot be offered worldwide on an unrestricted basis and/or may not be eligible for sale to all investors. All information and opinions expressed in this document were obtained from sources believed to be reliable and in good faith, but no representation or warranty, express or implied, is made as to its accuracy or completeness (other than disclosures relating to UBS and its affiliates). All information and opinions as well as any prices indicated are current only as of the date of this report, and are subject to change without notice. Opinions expressed herein may differ or be contrary to those expressed by other business areas or divisions of UBS as a result of using different assumptions and/or criteria. At any time, investment decisions (including whether to buy, sell or hold securities) made by UBS AG, its affiliates, subsidiaries and employees may differ from or be contrary to the opinions expressed in UBS research publications. Some investments may not be readily realizable since the market in the securities is illiquid and therefore valuing the investment and identifying the risk to which you are exposed may be difficult to quantify. UBS relies on information barriers to control the flow of information contained in one or more areas within UBS, into other areas, units, divisions or affiliates of UBS. Futures and options trading is considered risky. Past performance of an investment is no guarantee for its future performance. Some investments may be subject to sudden and large falls in value and on realization you may receive back less than you invested or may be required to pay more. Changes in FX rates may have an adverse effect on the price, value or income of an investment. This report is for distribution only under such circumstances as may be permitted by applicable law.

Distributed to US persons by UBS Financial Services Inc. or UBS Securities LLC, subsidiaries of UBS AG. UBS Switzerland AG, UBS Deutschland AG, UBS Bank, S.A., UBS Brasil Administradora de Valores Mobiliarios Ltda, UBS Asesores Mexico, S.A. de C.V., UBS Securities Japan Co., Ltd, UBS Wealth Management Israel Ltd and UBS Menkul Degerler AS are affiliates of UBS AG. UBS Financial Services Incorporated of Puerto Rico is a subsidiary of UBS Financial Services Inc. UBS Financial Services Inc. accepts responsibility for the content of a report prepared by a non-US affiliate when it distributes reports to US persons. All transactions by a US person in the securities mentioned in this report should be effected through a US-registered broker dealer affiliated with UBS, and not through a non-US affiliate. The contents of this report have not been and will not be approved by any securities or investment authority in the United States or elsewhere. UBS Financial Services Inc. is not acting as a municipal advisor to any municipal entity or obligated person within the meaning of Section 15B of the Securities Exchange Act (the "Municipal Advisor Rule") and the opinions or views contained herein are not intended to be, and do not constitute, advice within the meaning of the Municipal Advisor Rule.

UBS specifically prohibits the redistribution or reproduction of this material in whole or in part without the prior written permission of UBS and UBS accepts no liability whatsoever for the actions of third parties in this respect.

Version as per September 2015.

© UBS 2016. The key symbol and UBS are among the registered and unregistered trademarks of UBS. All rights reserved.

# Publication details

**Publisher**

UBS Financial Services Inc.  
Wealth Management Research  
1285 Avenue of the Americas, 20th Floor  
New York, NY 10019

This report was published  
on 26 August 2016.

**Lead authors**

Mark Haefele  
Mike Ryan

**Authors** (in alphabetical order)

Leslie Falconio  
Stephen Freedman  
Thomas Flury  
Ricardo Garcia-Schildknecht  
Wayne Gordon  
Markus Irngartinger  
Laura Kane  
David Lefkowitz  
Barry McAlinden  
Kathleen McNamara  
Brian Rose  
Rob Samuels  
Dominic Schnider  
Philipp Schoettler  
Frank Sileo  
Giovanni Staunovo  
Thomas Veraguth  
Justin Waring  
Jeremy Zirin

**Editors**

Roslyn Myers

**Project Management**

Paul Leeming  
John Collura  
Matt Siegel

**Desktop Publishing**

George Stilabower  
Cognizant Group – Basavaraj Gudihal,  
Srinivas Addugula, Pavan Mekala  
and Virender Negi

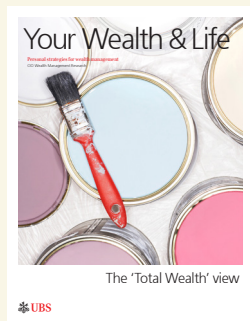
# UBS House View Monthly Call

A unique opportunity to hear the House View explained  
and to interact directly with CIO WMR's thought leaders.

**The next call will be on:  
Thursday, September 1 at 1:00 PM ET / 10:00 AM PT**

Dial in: 1-877-200-4456  
Passcode: 46502#

## Also from CIO WMR



©2016 UBS Financial Services Inc. All rights reserved. Member SIPC. All other trademarks, registered trademarks, service marks and registered service marks are of their respective companies.

UBS Financial Services Inc.  
[www.ubs.com/financialservicesinc](http://www.ubs.com/financialservicesinc)

UBS Financial Services Inc. is a subsidiary of UBS AG.

