Perspectives from GSAM Strategic Advisory Solutions

GSAM INVESTMENT THEMES

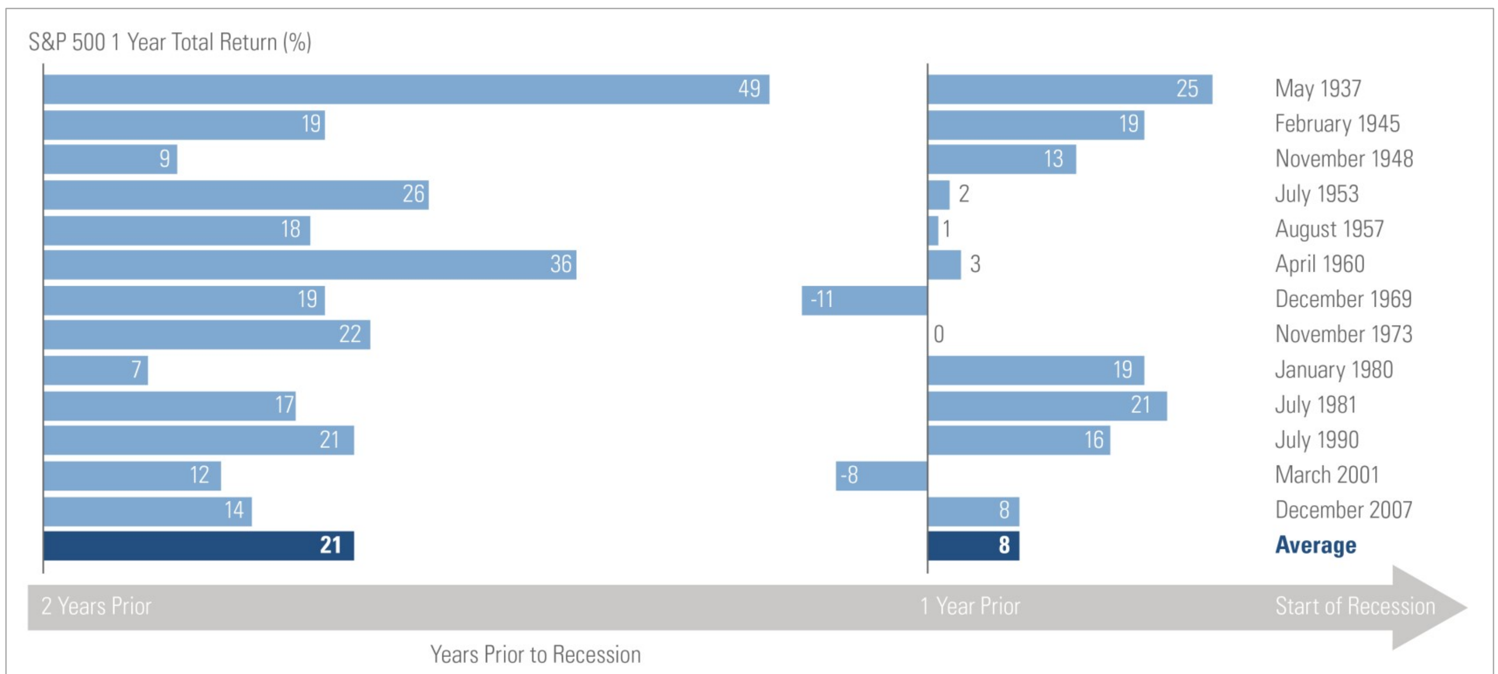
EARLY WITHDRAWAL RISK: Although the current economic recovery is of advanced age, the fundamentals suggest "age is just a number." Not only have 94% of countries experienced positive growth, but growth is accelerating in 61% of them. We think investors who question the sustainability of the recovery and equity returns risk premature withdrawal from the market. Historically, the two years prior to a recession have averaged an annualized ~15% return. We prefer to deploy a durable risk management framework, and remain invested.

THE ROLE OF ALTERNATIVES: Over the last two decades, investors have somewhat surprisingly found themselves in either a rising rate or falling equity environment (or both) almost half the time. Broadly diversified alternative strategies have outperformed during these challenging periods over 70% of the time. When alternative strategies were underperformers, they lagged by less than half as much as equities.[1] Given the difficulty of anticipating performance for individual alternative strategies, we believe comprehensive exposure is critical.

BIG DEAL: Modern economies are creating more data than ever before, at an ever-increasing rate. As much as 90% of all data has been created in the last few years. Even so, less than 1% of this data is actually being used or analyzed. Faster computers and bigger databases do not, on their own, provide the best insights. We believe that sound guidance and judgment by experienced individuals are the key to uncovering valuable data-driven investment insights. Data analysis is likely to evolve in the coming years, but the march of technology simply deepens the need for human oversight and intuition.

TAX POLICY UNCERTAINTY: The timing and magnitude of any potential tax policy changes are a topic of much discussion. We believe the market would react favorably to any semblance of legislative clarity, since today, skepticism reigns. In the two months following the US election, market returns for S&P 500 companies taxed at higher corporate rates outperformed the overall index by 4.5% as of the middle of January, as markets anticipated disproportionate benefits for that segment. This pattern which could re-emerge with any positive surprise. We explore this topic in greater detail on page 2.

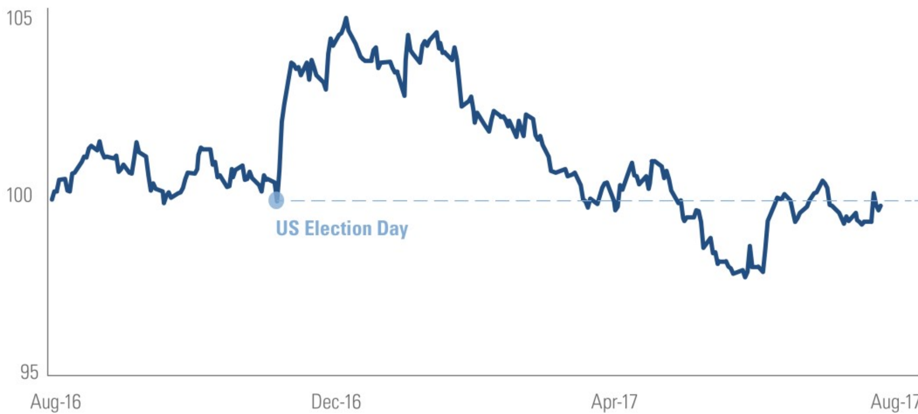
De-risking is a Risk



Text Source: GSAM. [1]Time period of analysis is from January 1, 1990 to December 31, 2016. Alternative strategies are represented by the HFRI FOF index, equities are represented by the S&P 500 Index, and Bonds are represented by the Bloomberg Barclays US Agg Bond Index. **Past performance does not guarantee future results, which may vary.**
Chart Source: NBER, Bloomberg, and GSAM. Data from January 1928 to July 2017, the largest available dataset for the S&P 500 Index. Chart shows S&P 500 Index total returns for the both 12 month period 2-year prior and the 12 month period 1-years prior to the start of a recession. Recession periods are as defined by the National Bureau of Economic Research as a significant decline in economic activity spread across the economy, lasting more than a few months, normally visible in real GDP, real income, employment, industrial production, and wholesale-retail sales. **Past performance does not guarantee future results, which may vary.**

US TAX POLICY CHANGES: NEVER SAY NEVER

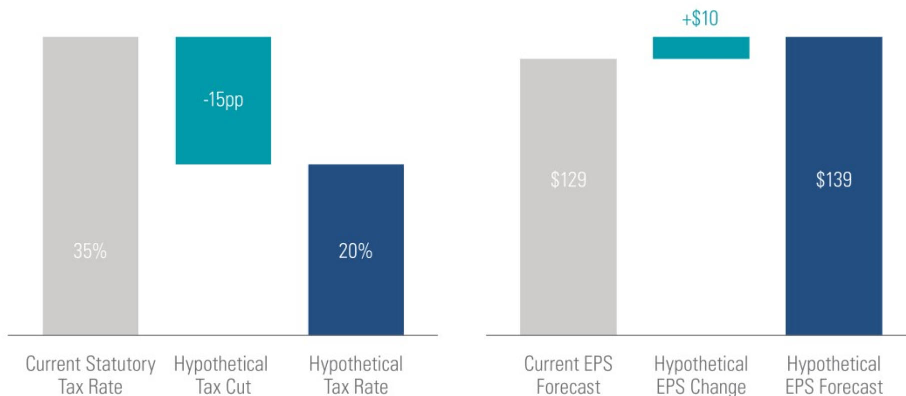
In a stark reversal from the first two months after the US election, equities today appear to be pricing a low probability that corporate tax legislation becomes law. Low probability aside, the House of Representatives' framework to reduce the rate from 35% to 20%, in our view, could potentially add to US large cap earnings meaningfully. In fact, even a modest change from the status quo could be positive for equities, precisely because of the market's low expectations.



Source: Goldman Sachs Global Investment Research, Bloomberg, and GSAM.

The performance of high tax stocks – defined as the 50 most heavily taxed S&P 500 stocks – may be the clearest sign of the market's tax-reform skepticism.

The initial surge of stocks with high exposure to tax policy has given way to parity with other market segments over the course of 2017. This leg of the bull market has instead relied on broader investor confidence in the global economic expansion.



Source: Goldman Sachs Global Investment Research, S&P Capital IQ, and GSAM.

If tax reform were to pass under currently discussed scenarios, it could add as much as 8% to S&P 500 earnings.

The House of Representatives' tax plan would cut the highest corporate tax rate to 20%, a large potential boost for S&P 500 Index earnings. We believe small cap stocks could see even greater upside, with a median Russell 2000 Index tax rate of 32% versus 26% for the S&P 500 Index.

Top Section Notes: As of July 31, 2017. Chart shows the relative performance of a portfolio of high tax rate S&P 500 stocks versus the broader S&P 500 Index to represent how the market may be pricing the probability for corporate tax reform. Hypothetical S&P 500 High Corporate Tax Rate Stock Portfolio allocation (an illustrative portfolio of high corporate tax rate equities): an equal weight blend of the 50 S&P 500 Index equities with the highest 10-year median corporate tax rate. The 10-year median corporate tax rate refers to the median effective corporate tax rate paid over the last 10 years. The median is the value separating the higher half of a data sample, a population, or a probability distribution, from the lower half. These illustrative results do not reflect any GSAM product and are being shown for informational purposes only. No representation is made that an investor will achieve results similar to those shown. The performance results are based on historical performance of the index used. The result will vary based on market conditions and your allocation. Please see end disclosures for additional definitions. GROWTH OF $100: A graphical measurement of a portfolio's gross return that simulates the performance of an initial investment of $100 over the given time period. The example provided does not reflect the deduction of investment advisory fees and expenses which would reduce an investor's return. Please be advised that since this example is calculated gross of fees and expenses the compounding effect of an investment manager's fees are not taken into consideration and the deduction of such fees would have a significant impact on the returns the greater the time period and as such the value of the $100 if calculated on a net basis, would be significantly lower than shown in this example. **Past performance does not guarantee future results, which may vary.** Bottom Section Notes: As of July 2017. Chart shows the House Republican tax reform proposal and the estimated impact a corporate tax rate cut of this size would have on earnings of the S&P 500 Index. EPS refers to Earnings per Share. The economic and market forecasts presented herein are for informational purposes as of the date of this presentation. There can be no assurance that the forecasts will be achieved.

Pro-Growth, Pro-Equity, Pro-Reality

Pro-Growth: We believe the increasingly synchronized global recovery will continue. Drivers may include loose financial conditions, a strong US labor market, fading political risk in Europe, and a consumer resurgence in emerging markets. So far, geopolitical uncertainties remain more bark than bite, inflation is low, and central banks appear keen to normalize policy carefully.

Pro-Equity: The most important implication of synchronized global recovery may be a likelihood of stronger earnings. This may be particularly true in non-US and emerging markets (EM) that are more levered to macro acceleration. Furthermore, history suggests that equites perform well in the latter stages of an economic cycle.

- **US**: Market sentiment on policy has swung too far in a negative direction, resulting in an almost full unwinding of the "Trump trade." With expectations so low, we think US equities have near-term upside potential, as any progress on reform would be additive to already solid earnings results.
- **Europe**: We are finally seeing a much-awaited earnings rebound, led by cyclicals. Europe's higher exposure to global revenues, leverage, and fixed costs potentially amplify sensitivity to improving global conditions.
- **Emerging Markets**: The EM economic growth premium to developed market (DM) continues to widen and inflationary pressures are moderating, potentially supporting an earnings rebound. We are constructive on the EM consumer, due to improving macro conditions, particularly in Asia. Following five years of underperformance versus DM, we believe macro underpinnings can sustain additional EM outperformance.

Pro-Reality: In our view, the composition of macro data suggests the current economic expansion should persist, though the pace of recovery has likely peaked. Valuation across most risk assets is top-decile, potentially constraining longer-term returns. In the short-run, however, any movement in pro-cyclical fiscal policy may provide a meaningful EPS boost. Consequently, we believe US equity markets still possess macro and policy upside, but require increased selectivity. The 2Q17 earnings season is one reason why 55% of companies beat estimates, but those companies averaged a mere 3bps of outperformance on the day of their announcement. Conversely, those companies that missed analyst forecasts underperformed the broader market by 225bps. Identifying the winners was productive, but avoiding the losers may have been more so.

Global GDP Growth Forecasts[1]

% yoy	2015	2016E	2017E	2018E
USA	2.9	1.5	2.1	2.3
Japan	1.1	1.0	1.8	1.2
Euro Area	1.9	1.7	2.0	1.5
UK	2.2	1.8	1.6	1.2
China	6.9	6.7	6.8	6.3
BRICs	5.0	5.4	5.7	5.9
Advanced Economies	2.2	1.7	2.1	1.9
World	3.5	3.2	3.7	3.8

Source: Goldman Sachs Global Investment Research.

Asset Class Forecasts[1]

	Current	3m	12m	% Δ to 12m
Equities				
S&P 500 ($)	2477	2425	2450	-1.1
STOXX Europe (€)	376	390	410	9.0
MSCI Asia-Pacific Ex-Japan ($)	534	500	530	-0.7
TOPIX (¥)	1620	1600	1700	5.0
10Y Rate (%)				
US	2.2	2.7	3.1	89.2 bp
Euro area (Germany)	0.4	0.7	1.0	59.0
Japan	0.0	0.1	0.2	22.5
Currencies				
Euro (€/$)	1.19	1.15	1.15	-3.2
Pound (£/$)	1.30	1.29	1.20	-7.5
Yen ($/¥)	110.2	112.0	115.0	4.4
Commodities				
Brent Crude Oil ($/bbl)	52.8	50.0	58.0	10.0
NYMEX Nat. Gas ($/mmBtu)	3.07	3.00	3.00	-2.3
London Gold ($/troy oz)	1320	1200	1250	-5.3
LME Copper ($/mt)	6776	6200	5500	-18.8

Source: Goldman Sachs Global Investment Research.

Impact on S&P 500 EPS

	Current Level	Hypothetical Level	EPS Impact to S&P 500
Margins	8.7%	9.9%	$10
Corporate Tax Rate	35%	20%	$10
US Dollar Index	93	84	$4
US GDP	2.1%	3.1%	$4
World GDP	3.7%	4.7%	$2
Brent Crude Oil	$49	$59	$1
Inflation	1.9%	2.9%	$1
10-Year Treasury	2.2%	3.2%	$0.5

Source: Goldman Sachs Global Investment Research and GSAM.

Text Source: GSAM. Left Chart Notes: The economic and market forecasts presented herein are for informational purposes as of the date of this presentation. There can be no assurance that the forecasts will be achieved. Please see additional disclosures at the end of this presentation. Right Chart Notes: For illustrative purposes only. The chart shows the impact of a hypothetical change of different economic variables to S&P 500 earnings per share. Margins represent the S&P 500 Index net margins, Corporate Tax Rates represent US Corporate Tax Rates, Inflation is represented by US Core CPI Inflation, 10-Year Treasury is represents the US 10-year Treasury yield. Please see additional disclosures at the end of this presentation. **Past performance does not guarantee future results, which may vary.** Text Notes: GDP refers to Gross Domestic Product.

Important Information

1 Page 3 Source 1: “Global equities gain 0.1%; US outperforms” – 9/04/2017.

Risk Considerations

Equity securities are more volatile than bonds and subject to greater risks. Small and mid-sized company stocks involve greater risks than those customarily associated with larger companies. Foreign and emerging markets investments may be more volatile and less liquid than investments in U.S. securities and are subject to the risks of currency fluctuations and adverse economic or political developments. Investments in commodities may be affected by changes in overall market movements, commodity index volatility, changes in interest rates or factors affecting a particular industry or commodity. The currency market affords investors a substantial degree of leverage. This leverage presents the potential for substantial profits but also entails a high degree of risk including the risk that losses may be similarly substantial. Currency fluctuations will also affect the value of an investment.

Investments in fixed-income securities are subject to credit and interest rate risks. Bond prices fluctuate inversely to changes in interest rates. Therefore, a general rise in interest rates can result in the decline in the bond’s price. Credit risk is the risk that an issuer will default on payments of interest and principal. This risk is higher when investing in high yield bonds, also known as junk bonds, which have lower ratings and are subject to greater volatility. All fixed income investments may be worth less than their original cost upon redemption or maturity.

Emerging markets securities may be less liquid and more volatile and are subject to a number of additional risks, including but not limited to currency fluctuations and political instability.

The currency market affords investors a substantial degree of leverage. This leverage presents the potential for substantial profits but also entails a high degree of risk including the risk that losses may be similarly substantial. Such transactions are considered suitable only for investors who are experienced in transactions of that kind. Currency fluctuations will also affect the value of an investment.

Alternative strategies often engage in leverage and other investment practices that are speculative and involve a high degree of risk. Such practices may increase the volatility of performance and the risk of investment loss, including the entire amount that is invested. **Manager risk** includes those that exist within a manager's organization, investment process or supporting systems and infrastructure. There is also a potential for fund-level risks that arise from the way in which a manager constructs and manages the fund. **Bonds** and Fixed income investing involves interest rate risk. When interest rates rise, bond prices generally fall. **Leverage** increases a fund's sensitivity to market movements. Funds that use leverage can be expected to be more "volatile" than other funds that do not use leverage. This means if the investments a fund buys decrease in market value, the value of the fund's shares will decrease by even more. Alternative strategies often make significant use of over-the-counter (OTC) derivatives and therefore are subject to the risk that **counterparties** will not perform their obligations under such contracts. Alternatives strategies may make investments that are illiquid or that may become less liquid in response to market developments. At times, a fund may be unable to sell certain of its **illiquid** investments without a substantial drop in price, if at all. There is risk that the **values** used by alternative strategies to price investments may be different from those used by other investors to price the same investments. The above are not an exhaustive list of potential risks. There may be additional risks that should be considered before investment decision.

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Important Information

Definitions

The **S&P 500 Index** is the Standard & Poor's 500 Composite Stock Prices Index of 500 stocks, an unmanaged index of common stock prices.
The **Stoxx Europe 600 Index** represents the performance of large, mid and small capitalization companies across 17 countries of the European region.
The **MSCI AC Asia Pacific ex Japan Index** captures large and mid cap representation across 4 of 5 Developed Markets countries (excluding Japan) and 8 Emerging Markets countries in the Asia Pacific region.
The **TOPIX Index** is a market capitalization-weighted index that is calculated based on all the domestic common stocks listed on the Tokyo Stock Exchange First Section.
The **MSCI Emerging Markets Equity Index** is a free float-adjusted market capitalization index that is designed to measure equity market performance of emerging markets.
The **Bloomberg Barclays EM Local Currency Government Index** in an unmanaged country-constrained index designed to provide a broad measure of the performance of liquid local currency emerging markets debt.
The **Bloomberg Barclays Investment-Grade Corporate Bond Index** is designed to track a more liquid subset of the US Corporate Index, which measures the market for investment grade, fixed-rate, taxable corporate bonds.
The **Bloomberg Barclays Global High Yield Index** provides a broad-based measure of the global high-yield fixed income market.
The **Bloomberg Barclays US Government Index** represents the portion of the Barclays US Aggregate Index that is US Treasury or Agency securities.
The **MSCI EAFE Small Cap Index** is an equity index capturing small cap representation across Developed Markets countries around the world, excluding the US and Canada.
The **S&P Global Infrastructure Index** is designed to track 75 companies from around the world chosen to represent the listed infrastructure industry while maintaining liquidity and tradability.
The **MSCI EAFE Index** is designed to represent the performance of large and mid-cap securities across 21 developed markets, including countries in Europe, Australasia and the Far East, excluding the U.S. and Canada.
The **FTSE NAREIT Composite REIT Index** is a free-float adjusted, market capitalization-weighted index of U.S. Equity and Mortgage REITs.
The **Alerian MLP Index** is the leading gauge of energy Master Limited Partnerships (MLPs). The float-adjusted, capitalization-weighted index's constituents represent approximately 85% of total float-adjusted market capitalization.
Standard Deviation is a measure of the dispersion of a set of data from its mean.
BRIC refers to Brazil, Russia, India, and China.

Index Benchmarks

Indices are unmanaged. The figures for the index reflect the reinvestment of all income or dividends, as applicable, but do not reflect the deduction of any fees or expenses which would reduce returns. Investors cannot invest directly in indices.

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