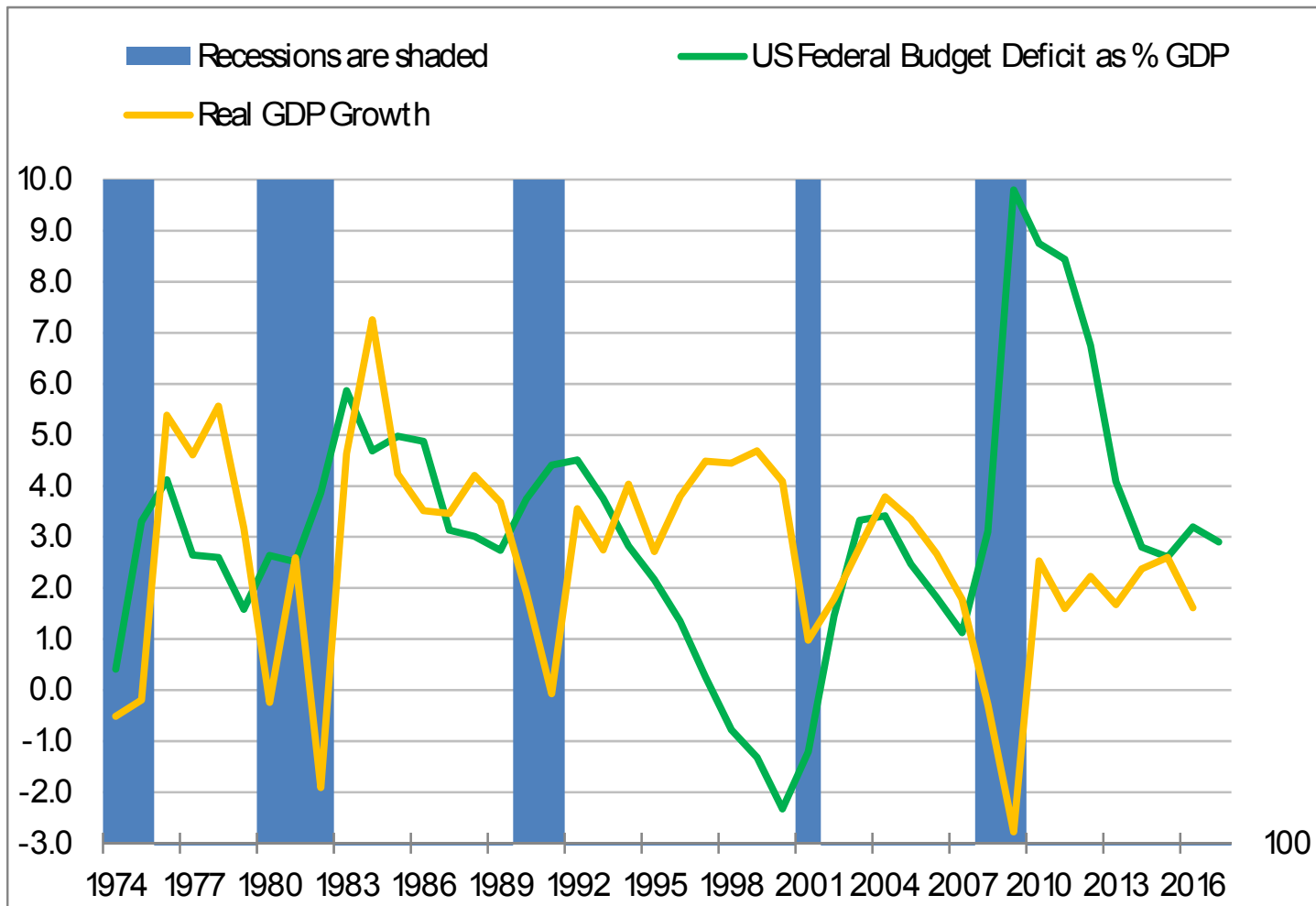
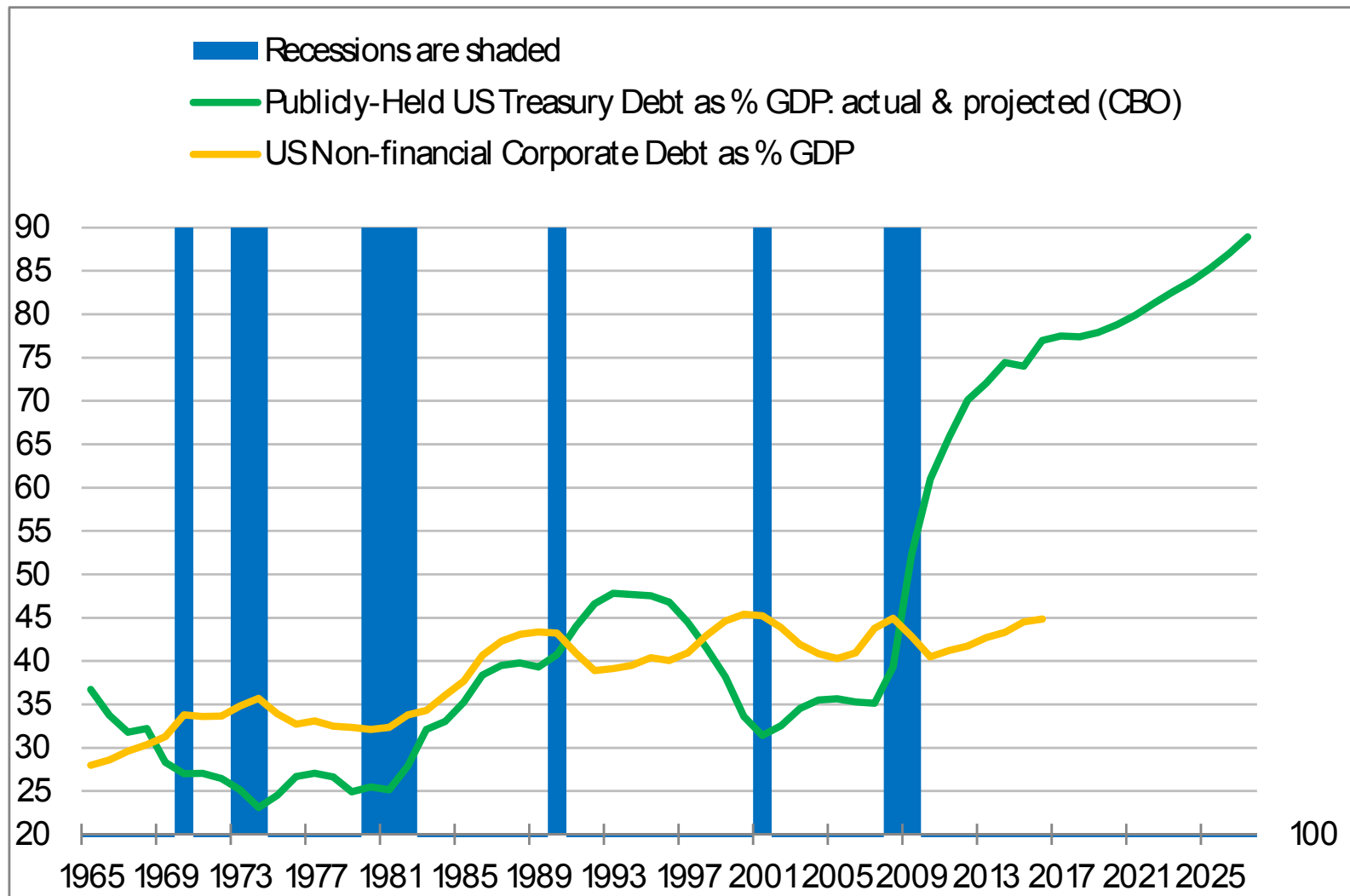


Cost of Capital: Equity Bubble Elevates Risk of a Jarring Correction

Don't Expect Much From Revenue-Neutral Fiscal Stimulus ... Despite 2009's More than \$800 Billion of Fiscal Stimulus That Approximated 9.8% of GDP, 2010's Real GDP Grew by Only 2.5%



Not Much of a "Crowding Out" Effect Despite How US Treasury Debt Soared from 2007's 35% to Recent 77% of GDP



Potential Impact of Proposed Corporate Tax Reform Across Broad Rating Groups

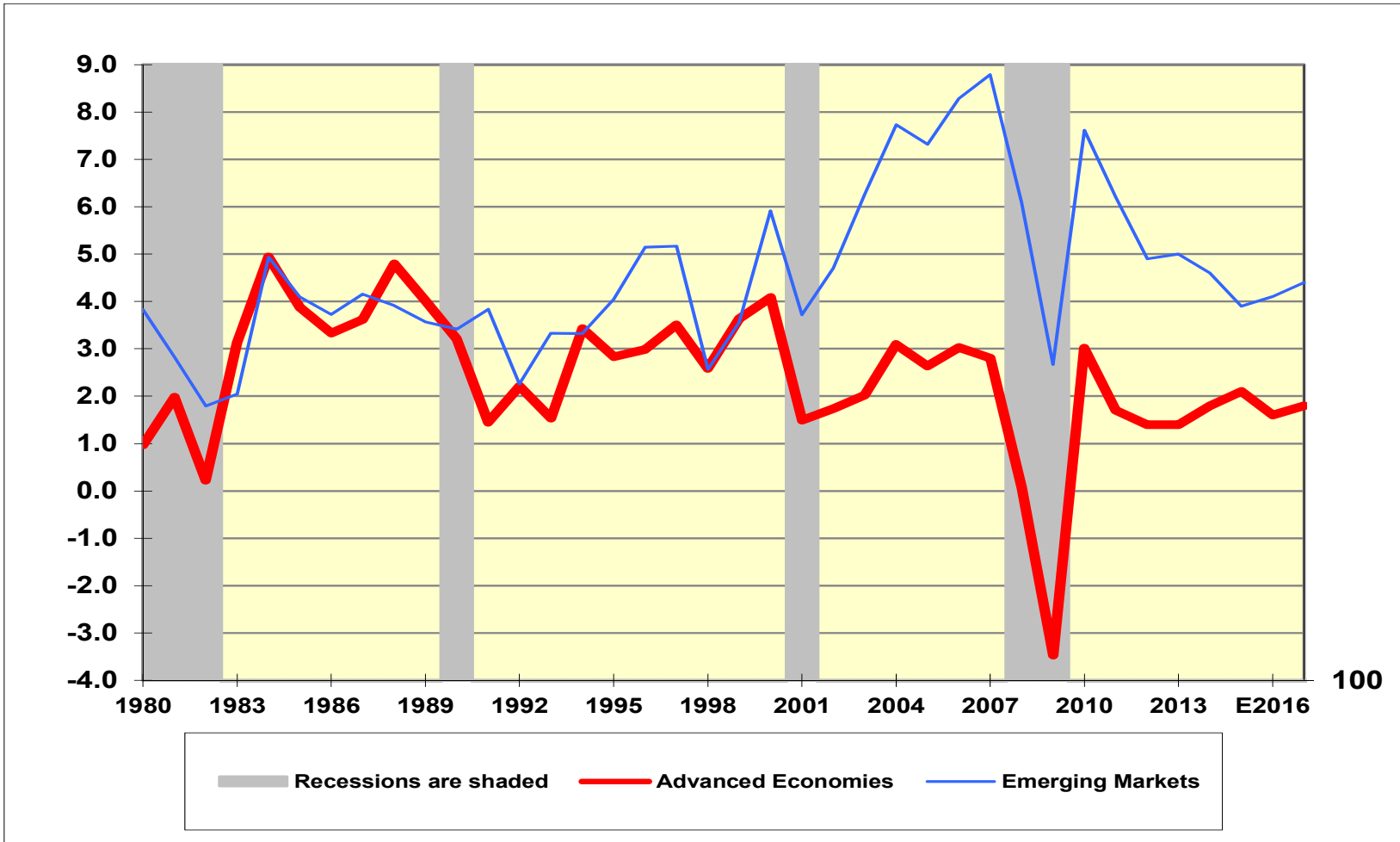
	Investment-Grade Issuers	Speculative-Grade Issuers (High Yield)
<i>number of companies sampled</i>	350	1,300
<i>Lowering Maximum Corporate Income Tax Rate from 35%:</i>		
Median Tax Rate	28%	6%
Percent of Companies Paying Tax	91%	76%
Taxes Incurred in 2015	\$240 billion	\$40 billion
<i>Eliminate Tax Deductibility of Interest Expense:</i>		
Median Interest Rate	4.10%	6.50%
Median Ratio of EBIT/Interest Expense	9.3x	1.3x
<i>Acceleration of Tax Deductibility of Capital Spending:</i>		
Median: Capital Spending as % of Revenue	4.2%	3.8%

Reasons for Today's Subpar Upturn

- Aging workforces and populations of most advanced economies.
- Global slack – supply exceeds demand.
- Loss of global competitiveness.
- Technological progress that does more to shrink payrolls than to create jobs.
- Lack of new product breakthroughs that create new industries and new jobs.

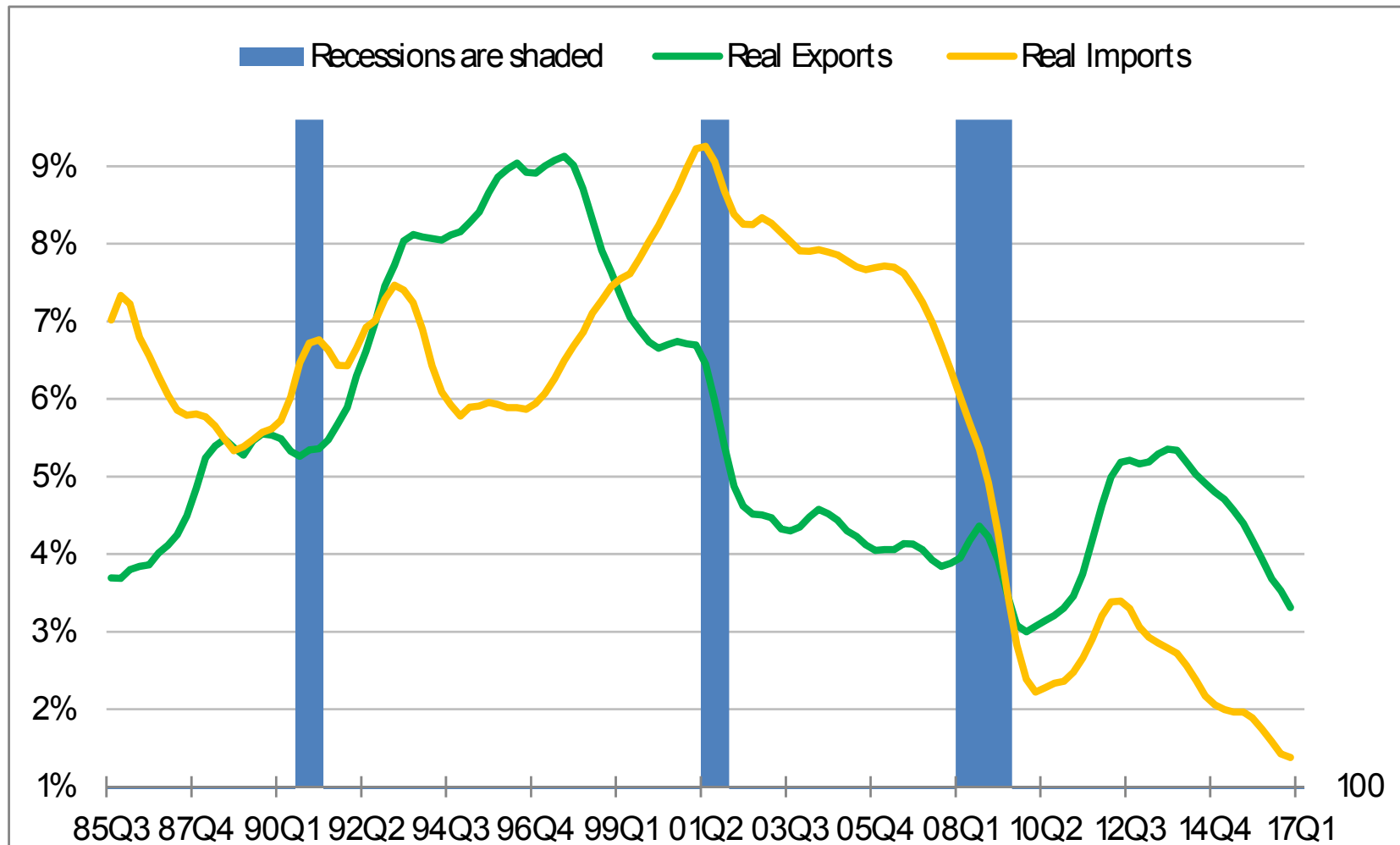
Comparing Moving 5-Year Average Annual Economic Growth Rates of 2007 and 2016 Shows Drops from (i) 2.7% to 1.7% for Advanced Economies and from (ii) 7.7% to 4.4% for Emerging Markets

yy % change of economic activity, source: IMF, Moody's Capital Markets



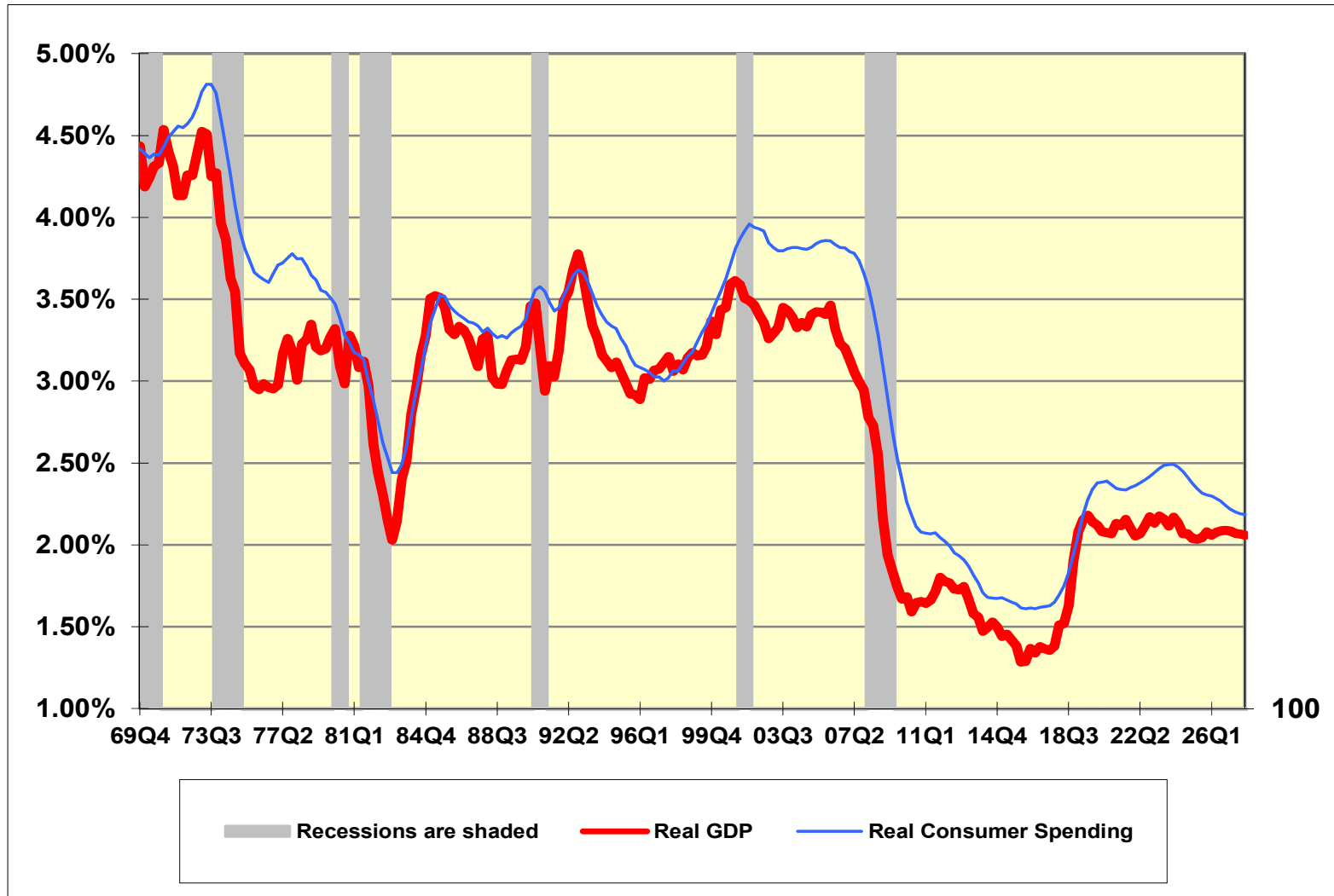
World Suffers from Deceleration by Long-Term Average Annual Growth of US' Real Imports from 2001's Record 9.5% to Recent 1.6%

10-year average annualized growth rates



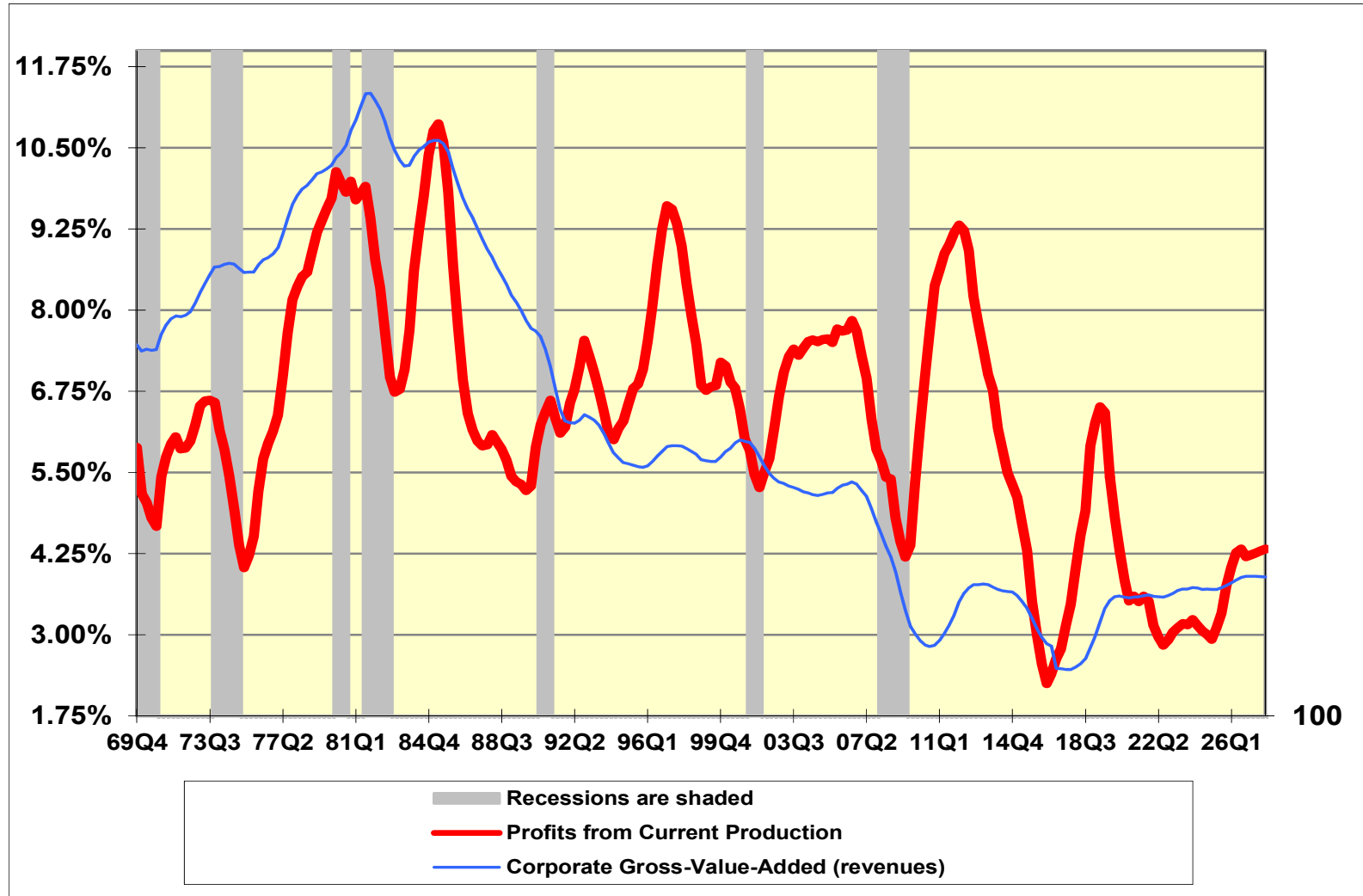
US Economy and Real Consumer Spending Are Expected To Grow By Roughly 2% Annually, on average, Through 2027

10-year average annual growth rates, actual & predicted by Blue Chip Consensus



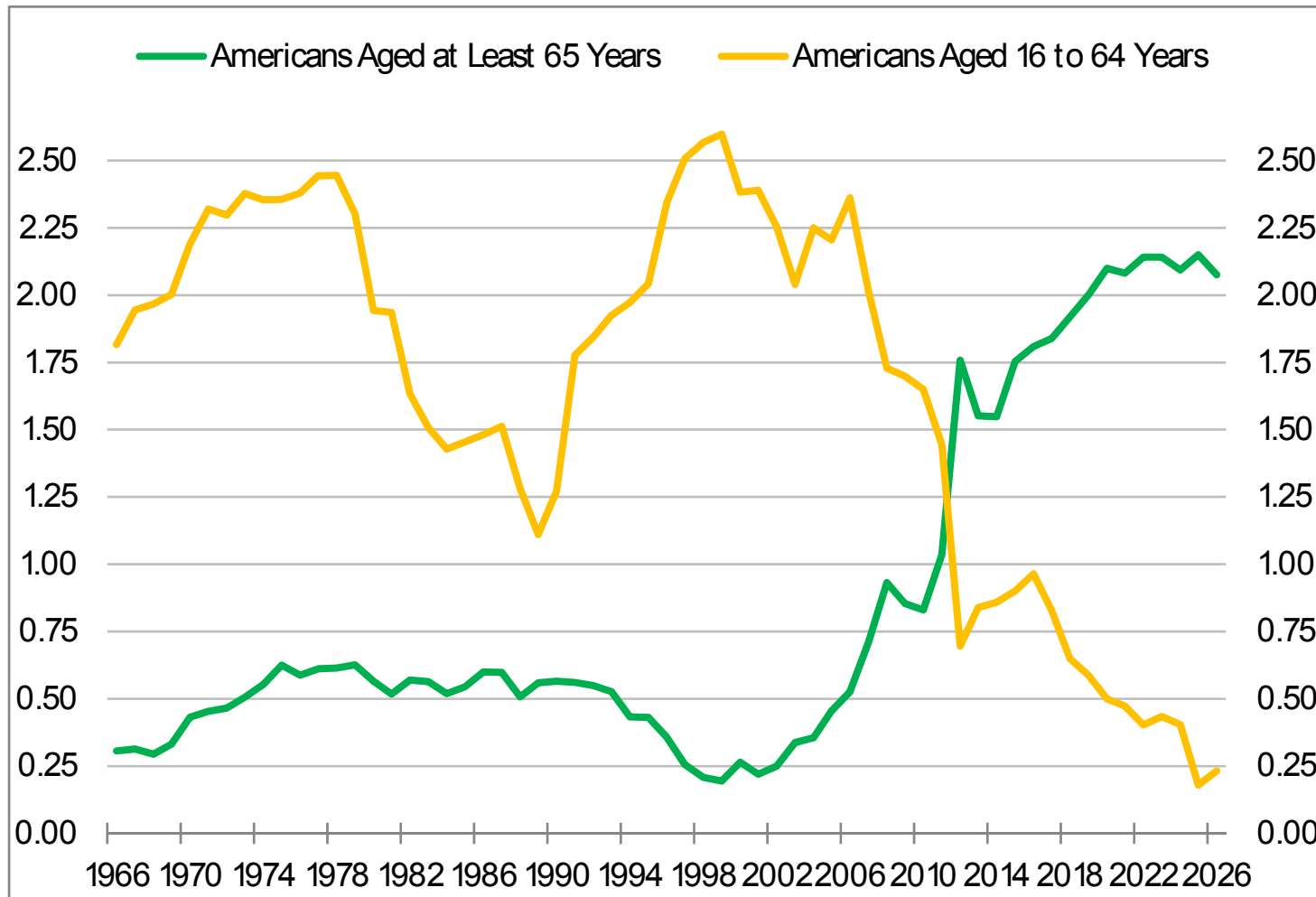
Modest Long-Term Outlooks for Both Corporate Gross-Value-Added (revenue proxy) and Profits from Current Production

10-yr average annualized growth rates, actual & predicted



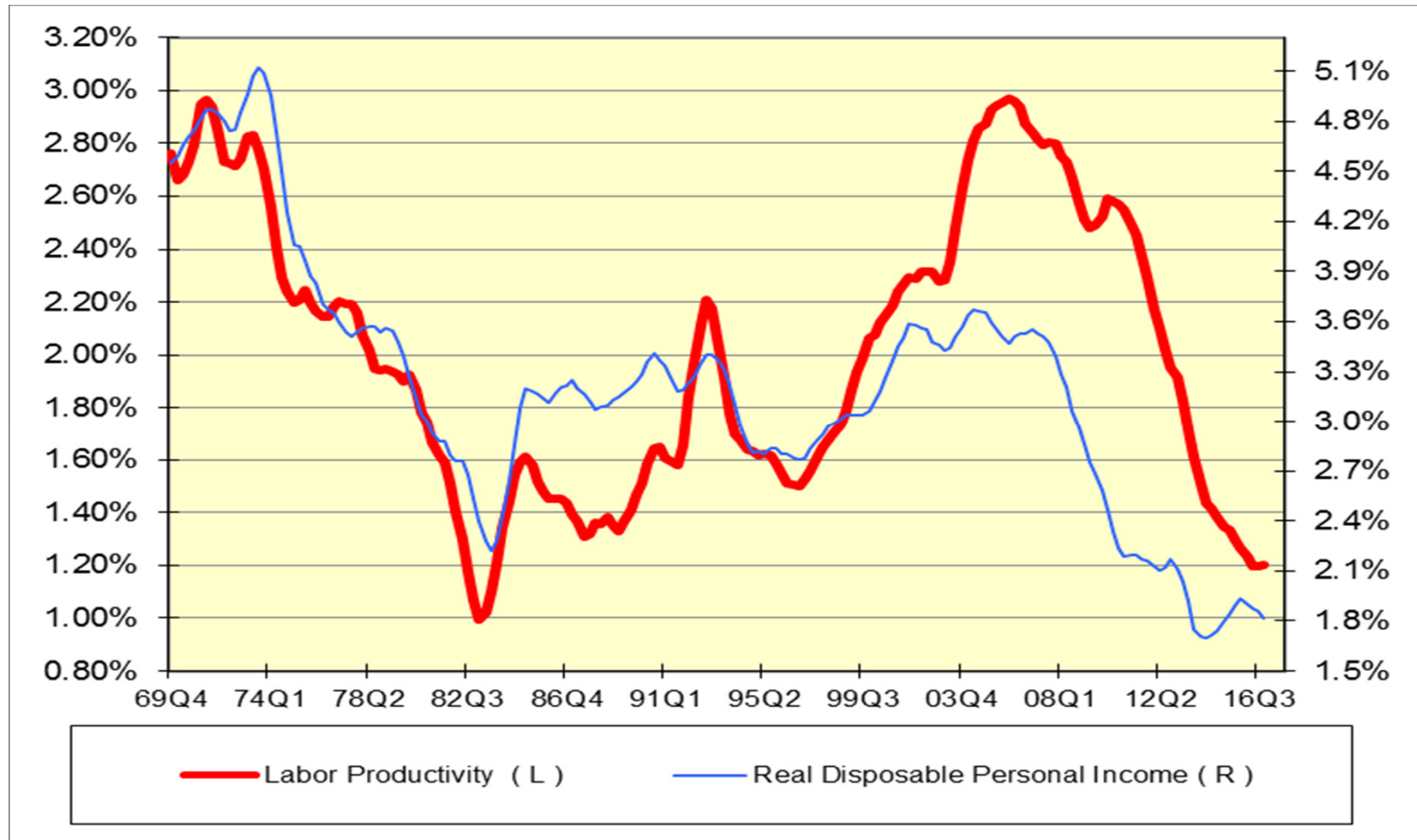
Profound Shift in Age Distribution of US Population May Influence Financial Markets for Years to Come

actual & predicted annual change in millions of people; source: US Bureau of the Census, Moody's Analytics



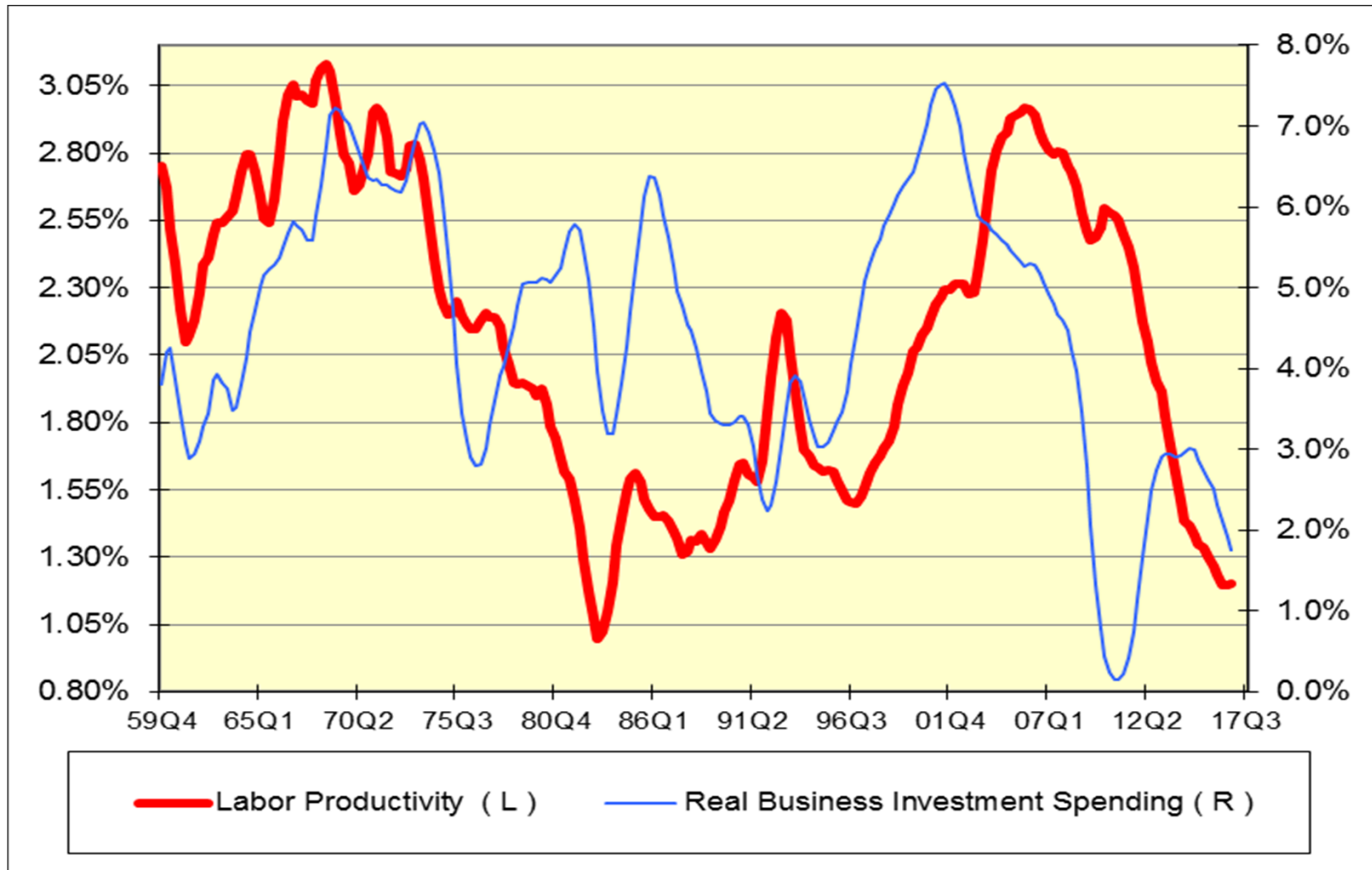
Prolonged Deceleration by Labor Productivity Slows Real Disposable Personal Income

10-year average annualized growth rates in %

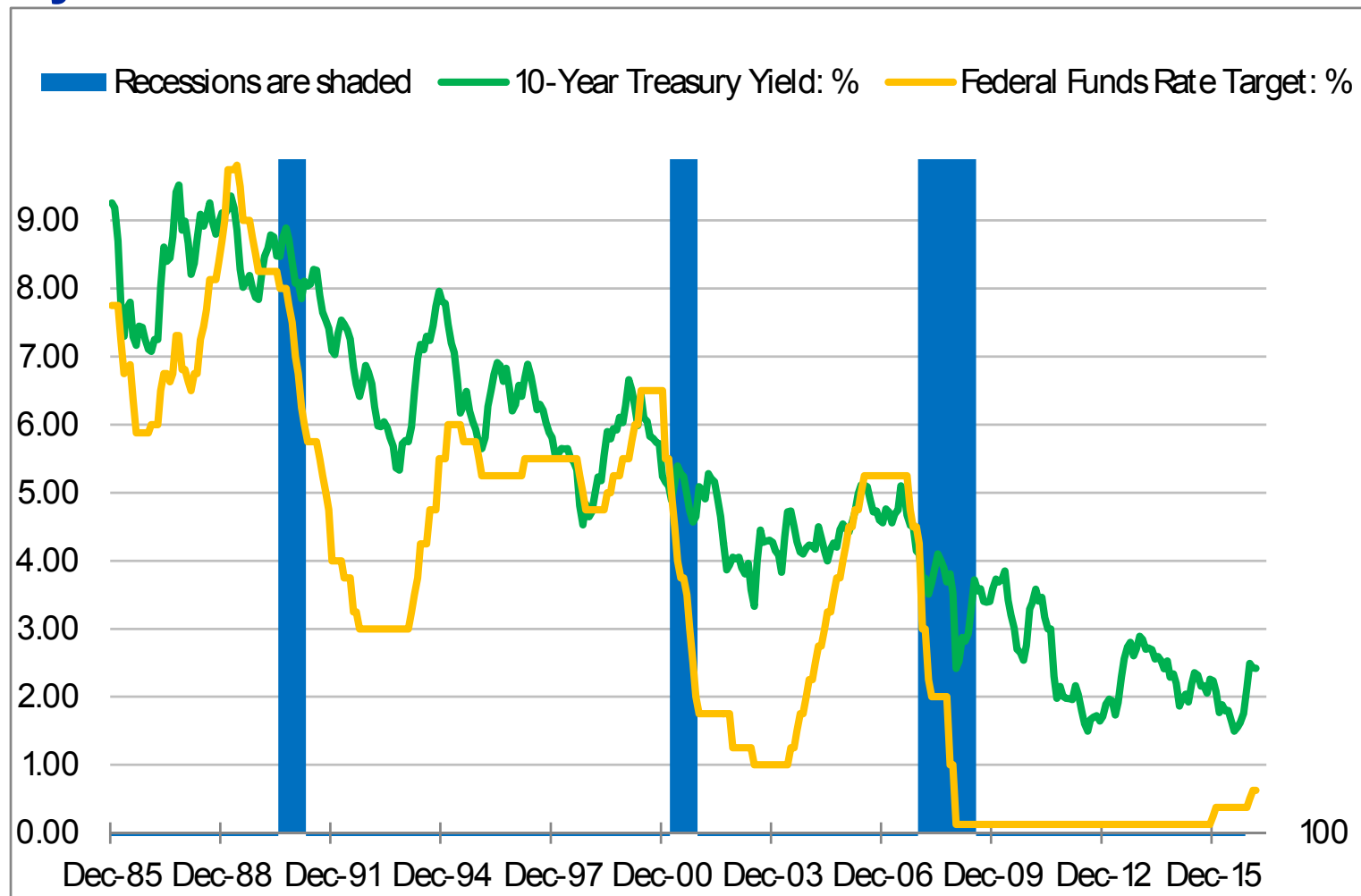


Prolonged Subpar Pace for Real Business Investment Spending Only Partly Explains Latest Slump by Labor Productivity

10-year average annualized growth rates

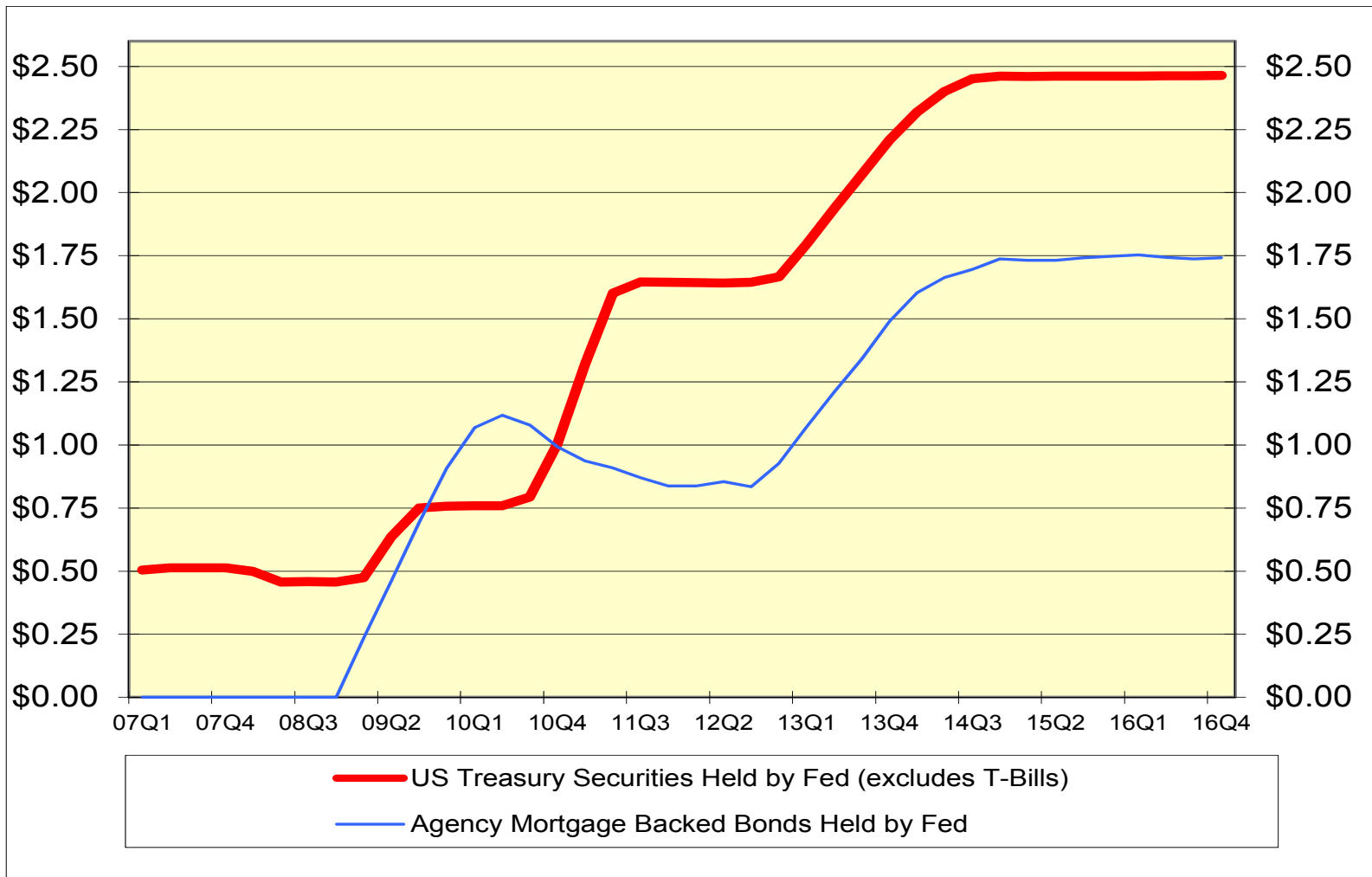


Fed Policy Seems Unlikely to Risk an Inverted Yield Curve ... Last Three Recessions Averaged a Five Percentage Point Drop by Fed Funds



Federal Reserve Holds 20% of Outstanding US Treasury Notes & Bonds and 17% of Home Mortgage Debt

\$ trillions

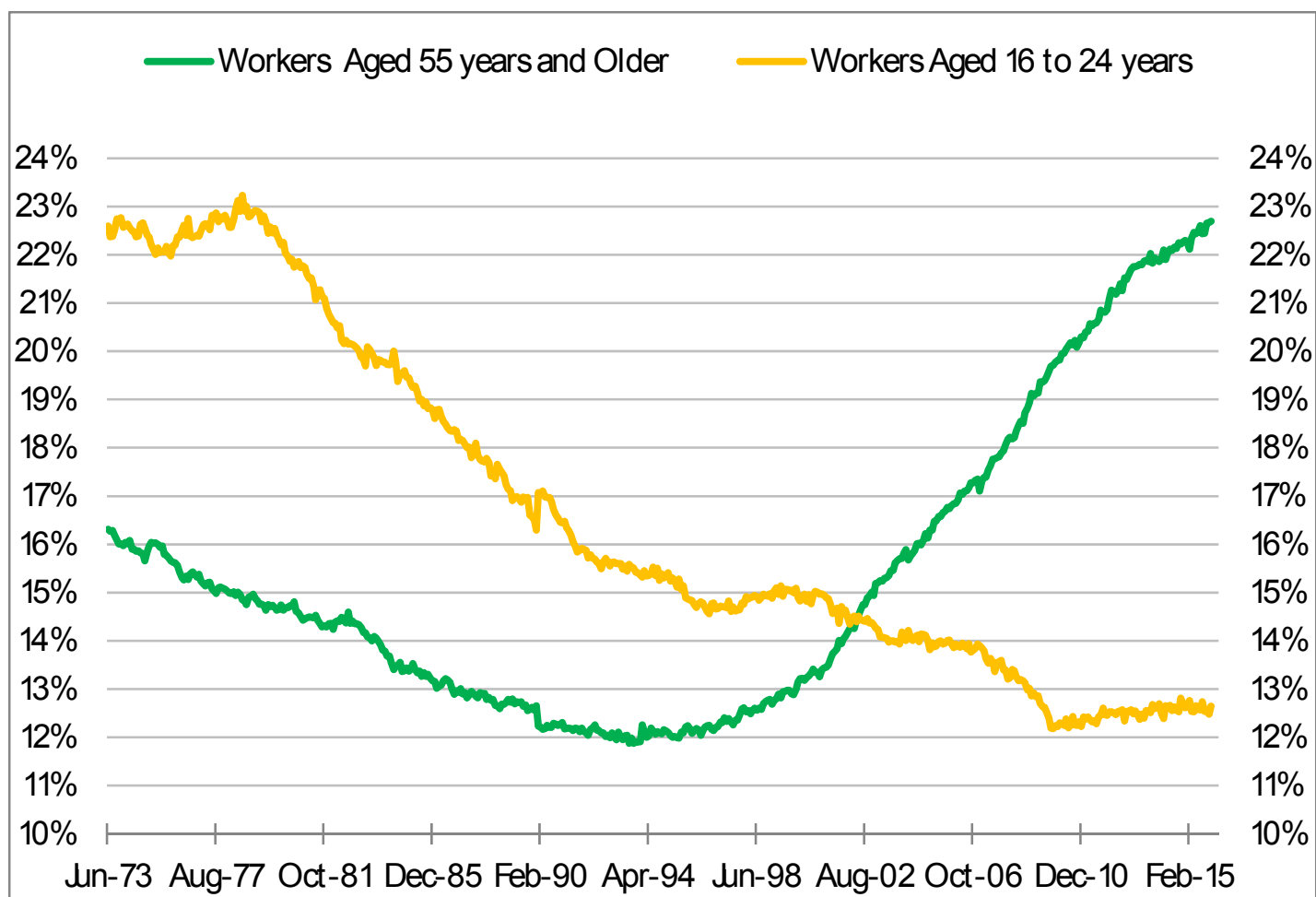


Price Inflation Lacks Breadth

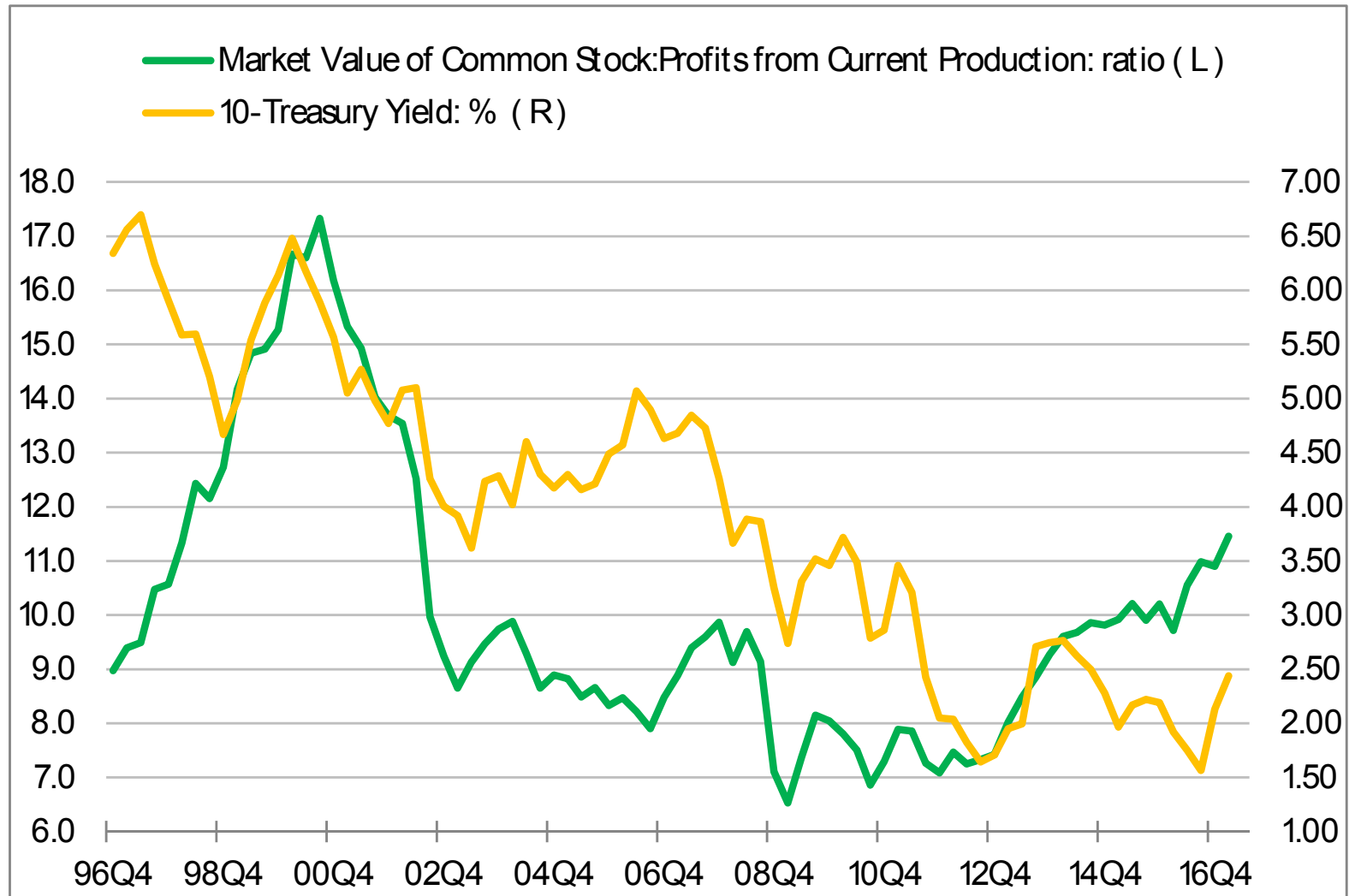
1. March's annual rate of inflation was **2.4%** for the **CPI**.
2. March's **2.0%** annual rate of **core CPI** inflation (excludes food & energy) was skewed higher by core consumer service inflation of **2.9%**. Core consumer goods showed price deflation of **-0.6%**.
3. **Core CPI** inflation slowed to **1.0%** after excluding a **3.5%** annual jump by shelter costs that supply 42% of core CPI.
4. February's **PCE price index** (the Fed's preferred inflation metric) rose by **2.1%** yearly.
5. February's **1.7%** rate of **core PCE price index** inflation included **-2.4%** price deflation for consumer durable goods.
6. PCE price index for consumer services grew 2.4% annually.

Age Distribution of Employment Goes From Being Inflation-Prone in the 1970s to Disinflationary Today

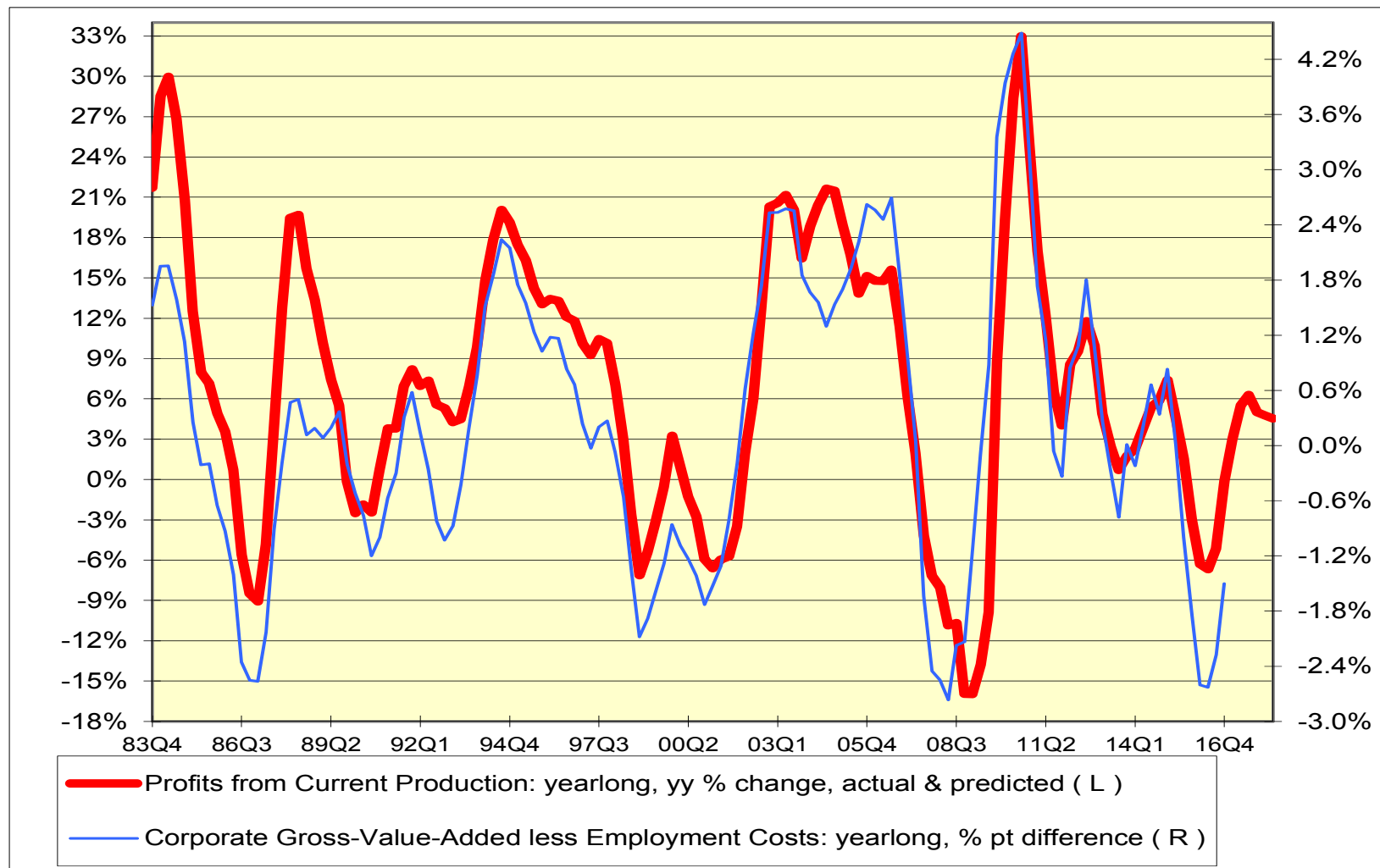
age cohort as % of household survey employment



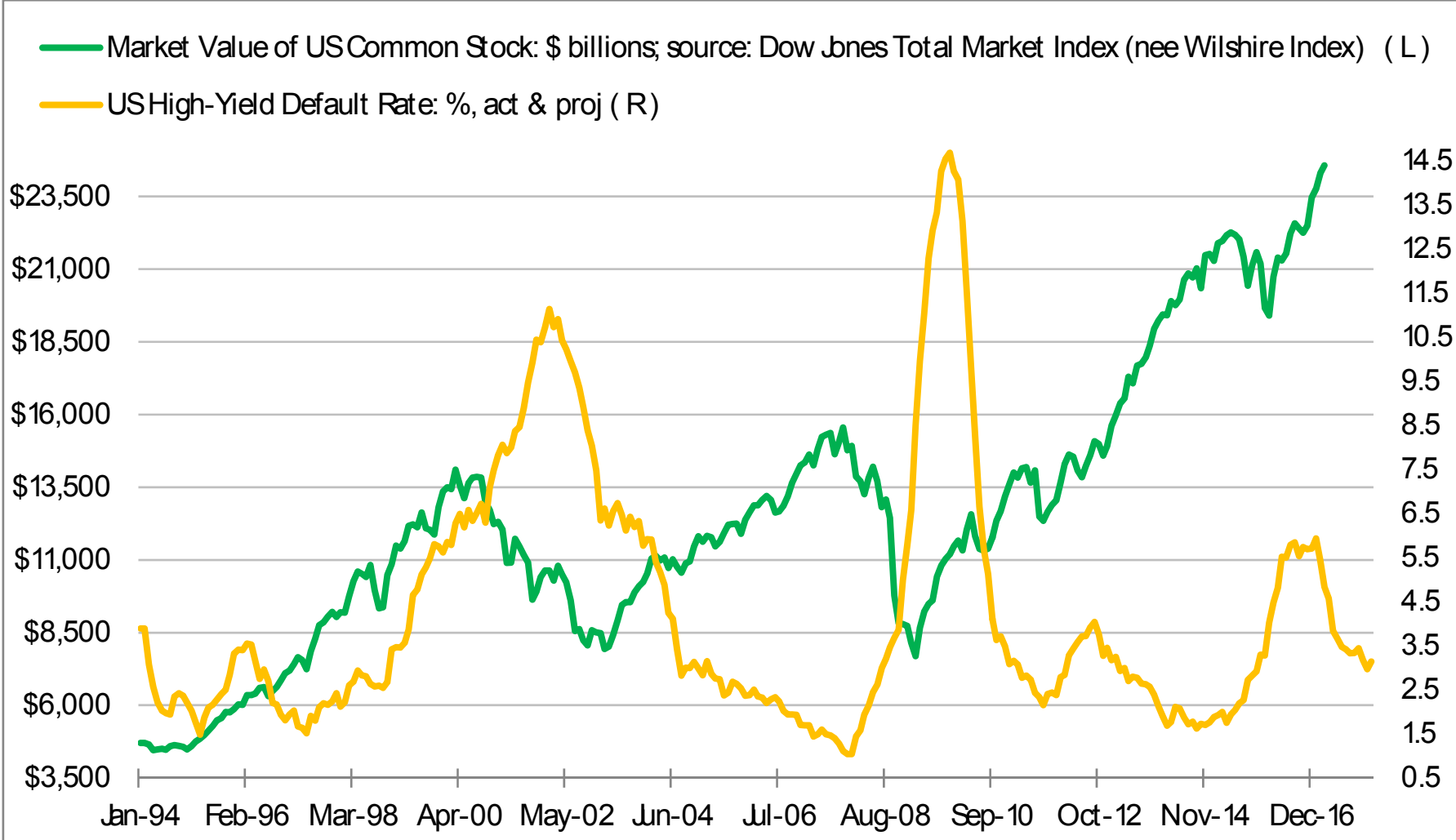
Inevitable Correction of an Overvalued Equity Market Will Drive Treasury Bond Yields Lower



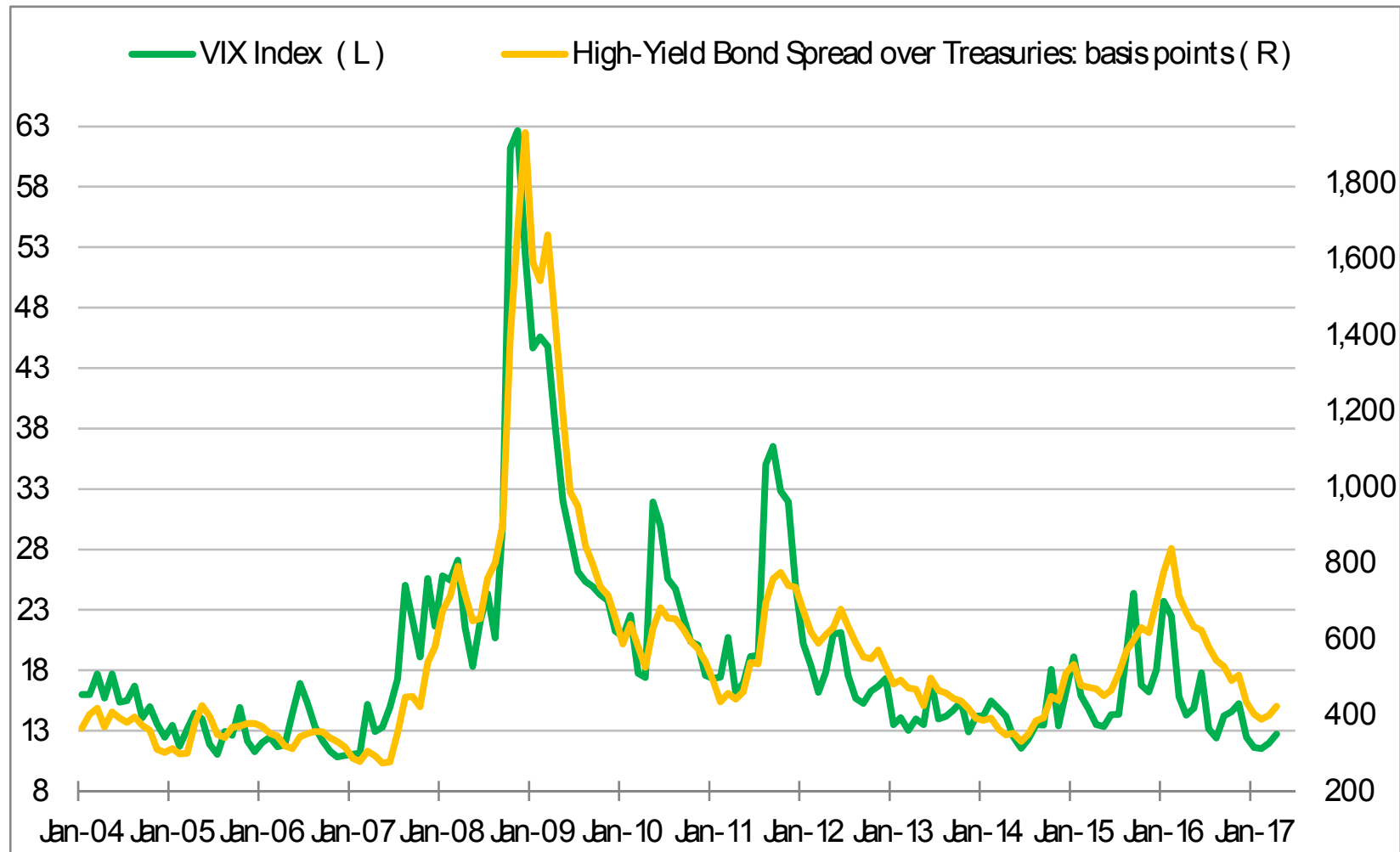
Assuming 4.5% Employment Costs Growth, Projected 5% Growth by 2017's Profits Implies Annual Increase of Corporate Gross-Value-Added Needs to Quicken from 2016's 2.9% to 4.4% for 2017 (correlation = 0.86)



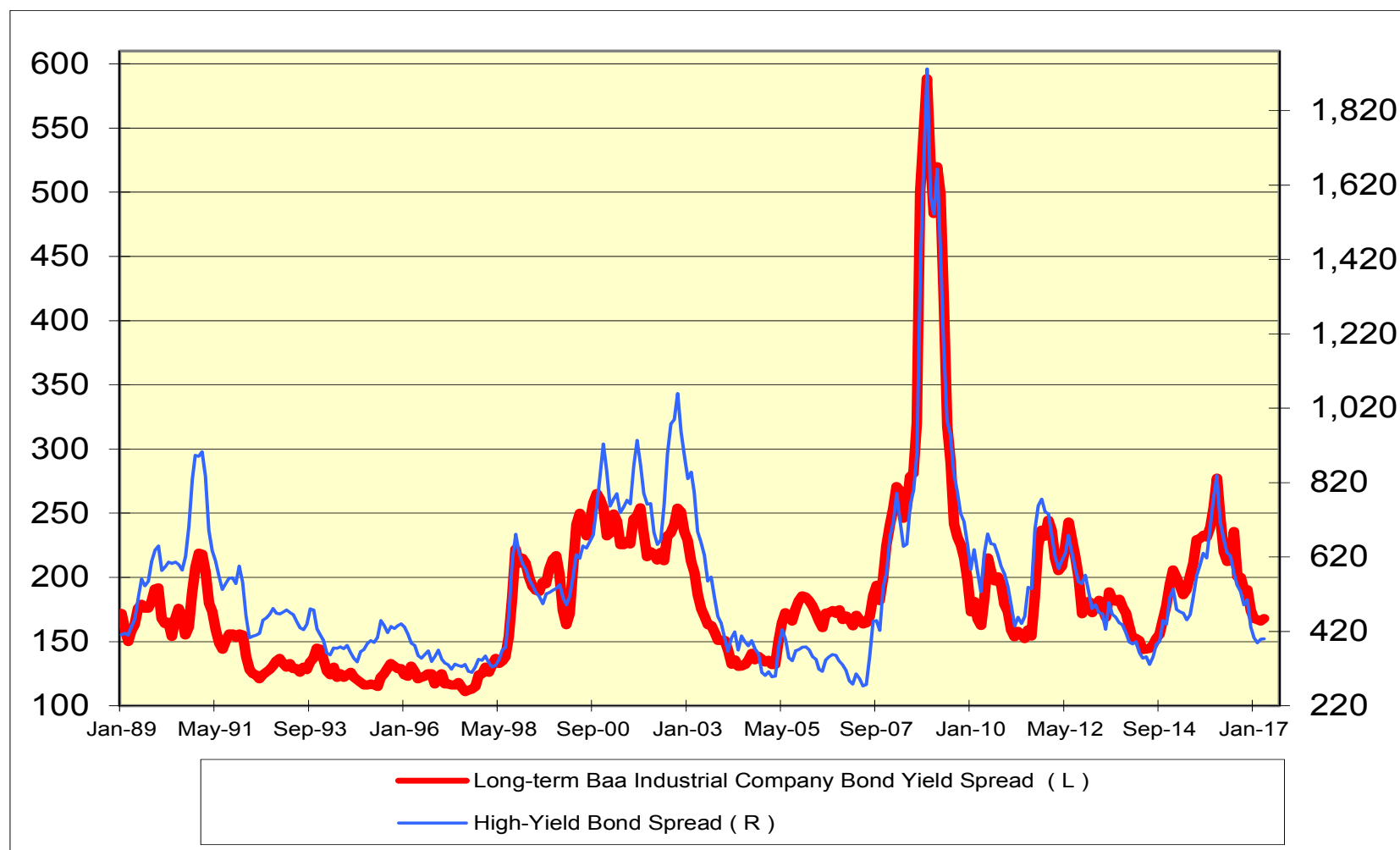
Since 1993, Higher Default Rate Followed Each Deeper than -10% Drop from Prior High by Market Value of Common Stock



Throughout Much of 2016, VIX Index Correctly Hinted of a Thinner High-Yield Bond Spread ... Recent VIX Index Favors a 470 bp Midpoint for High-Yield Spread Versus Actual 415 bp (*correlation = 0.90*)

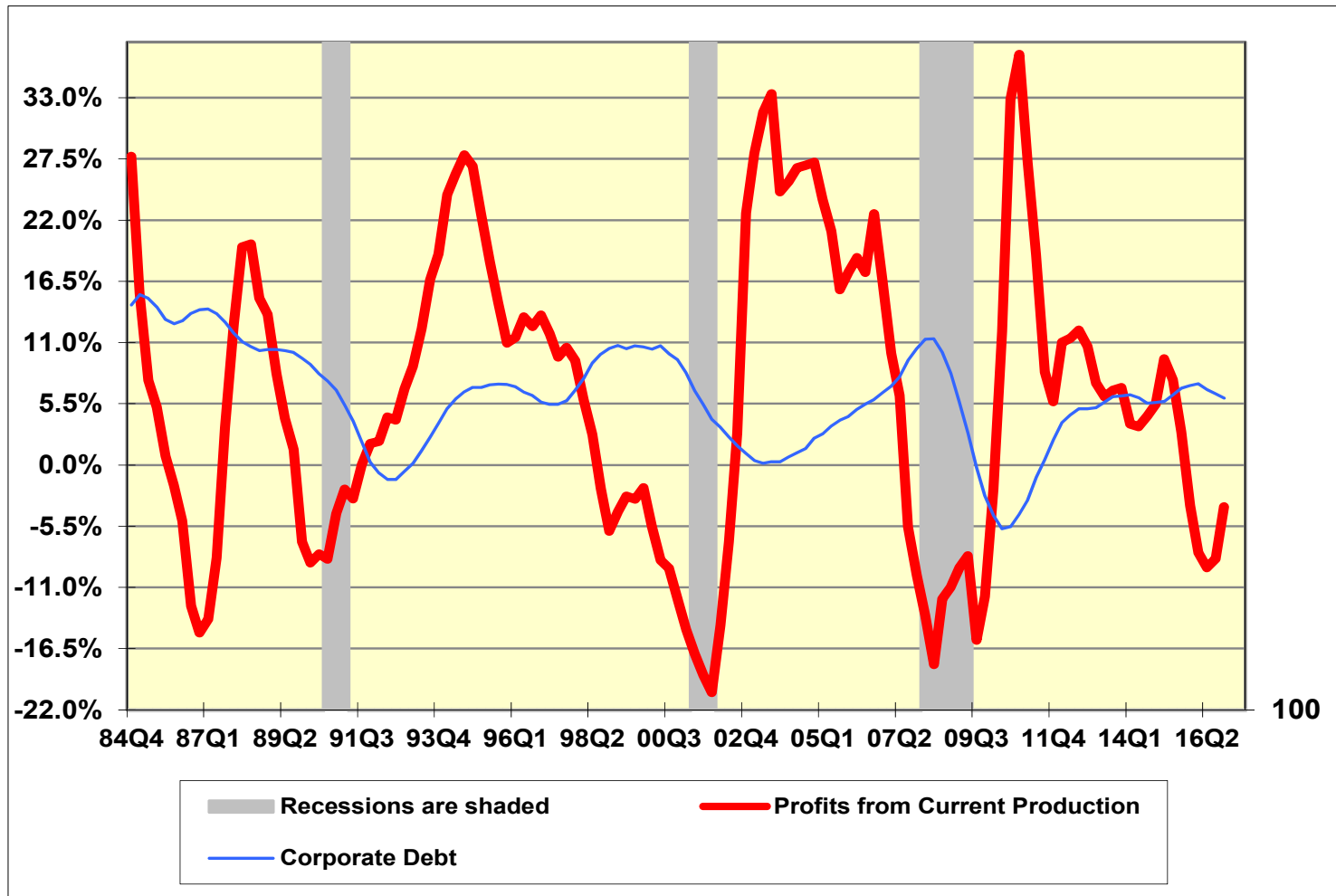


Strong Correlation of 0.91 Between High-Yield and Long-Term Baa Bond Yield Spreads ... Recent Baa Spread of 168 bp Statistically Implies a Nearly 500 bp Midpoint for High-Yield Spread *in basis points*

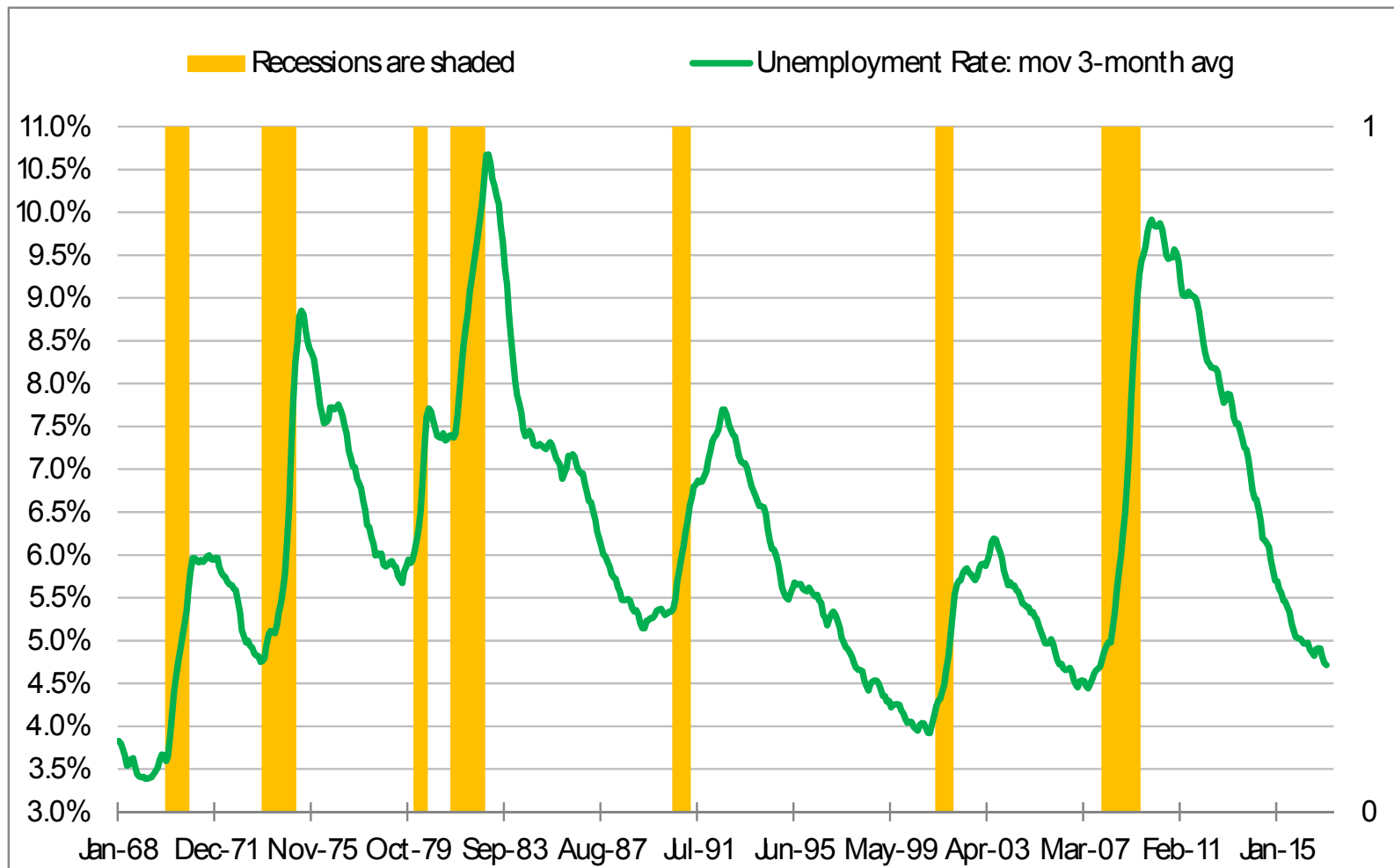


Markets Sense Profits Will Again Outrun Corporate Debt

yy % changes of yearlong averages for US nonfinancial corporations



Recession May Be Present When Unemployment Rate's Moving Three-Month Average Turns Higher Amid a Mature Economic Recovery



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