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THE FIXED INCOMEVIEW

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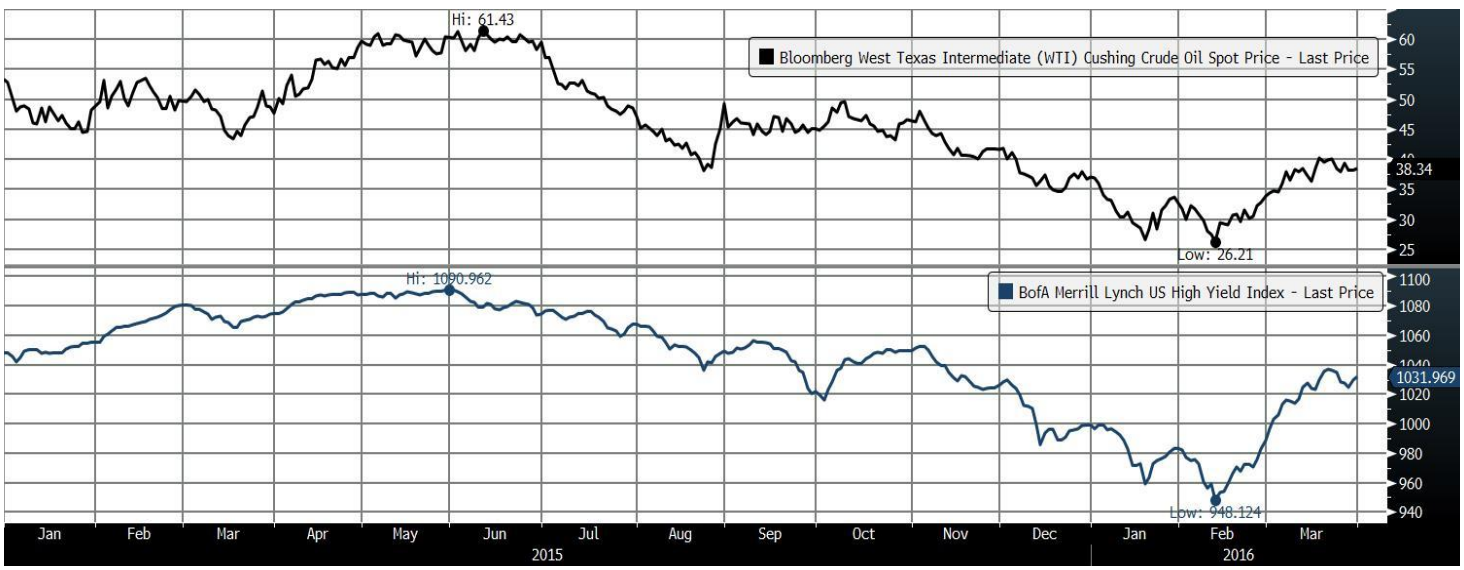
Q1 2016 - Risk Assets Finally Bounce on Oil Rally

Riskier fixed income assets had been in a prolonged downtrend since the end of May 2015, before finally bottoming on February 11, 2016. The Bank of America Merrill Lynch US High Yield Index had a cumulative loss of about 13% over that time frame, while the S&P 500 was also down about 12%. The high yield sell-off coincided with a 57% drop in oil prices from over $61/barrel in mid-June 2015 to a low of around $26/bbl on February 11, 2016. Oil prices have since bounced 46% off that low to $38/bbl at quarter-end, and risk assets have followed. The high yield bond market has become more correlated to oil prices since prices first began to collapse in mid-2014 after hitting $106/bbl, given that the energy sector had grown over the years to comprise about 15% of most major high yield indices. In addition, the markets have come to view oil prices as a proxy for global growth. Higher quality fixed income assets, including investment grade corporate bonds and US Treasuries also performed well in the first quarter, as interest rates fell sharply.

HIGH YIELD MARKET

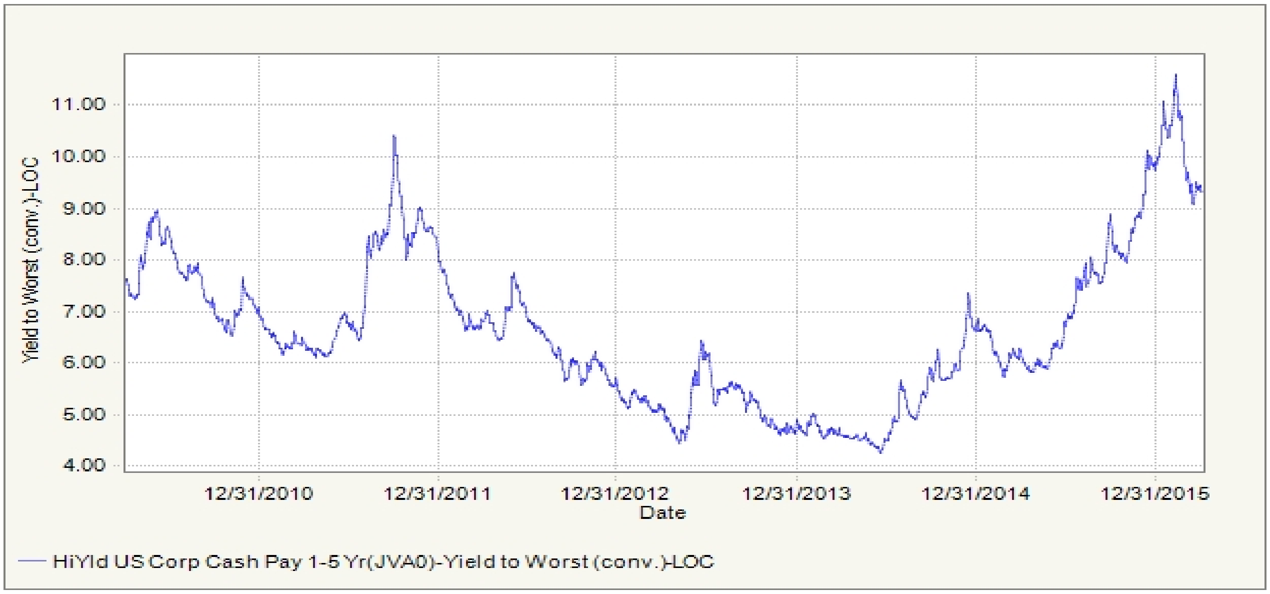
As oil goes, so goes the high yield market. The charts below show the correlation between oil prices and the high yield index value since the end of 2013. The high yield market hit a high just slightly before oil's one year high of $61.43 on June 10, 2015, and they both hit their lows on February 11, 2016. The high yield market rallied almost 9% from its low through March 31, 2016, while the high yield energy sector was up almost 27%.



Source: Bloomberg, Bank of America Merrill Lynch. Data through March 31, 2016. The BofA Merrill Lynch US High Yield Index tracks the performance of US dollar denominated below investment grade corporate debt publicly issued in the US domestic market. Bloomberg West Texas Intermediate (WTI) Cushing Crude Oil Spot Price uses benchmark WTI crude at Cushing, OK; and other US crude oil grades trade on a price spread differential to WTI, Cushing. Prices are on a free-board basis. It is not possible to invest directly in an index. Please see the end of this article for important disclosure information.

High yield reached very attractive valuation, in our view. As high yield prices fell, yields on the Bank of America Merrill Lynch 5-10 Year US Corporate Index rose to a six year high (see chart below). Its yield peaked at 11.60% on February 11, 2016 despite falling Treasury yields, as risk premiums expanded to 1,070 basis points (bps). Risk premiums have historically risen above 1,000 only during recessions when defaults rise sharply. According to JP Morgan's data, the high yield default rate was 3.2% at the end of the first quarter, up from 3.0% a year ago, but still below its long-term average of around 3.6%. The default rate for the high yield market, excluding the energy/metals/mining sectors, is currently only 0.4% compared to about 10%

for the energy sector and 22% for the metals/mining sector. JPM expects the overall default rate to increase to 6% by year-end, but only 2% ex-commodities. Given its extreme valuation, RiverFront's 2016 strategic asset allocation process continued to favor the sector and slightly increased its recommended exposure to short-term high yield bonds in our shorter time horizon portfolios. The high yield weightings in our longer-term portfolios did not increase, because equity valuations had also gotten more attractive after their sell-off.

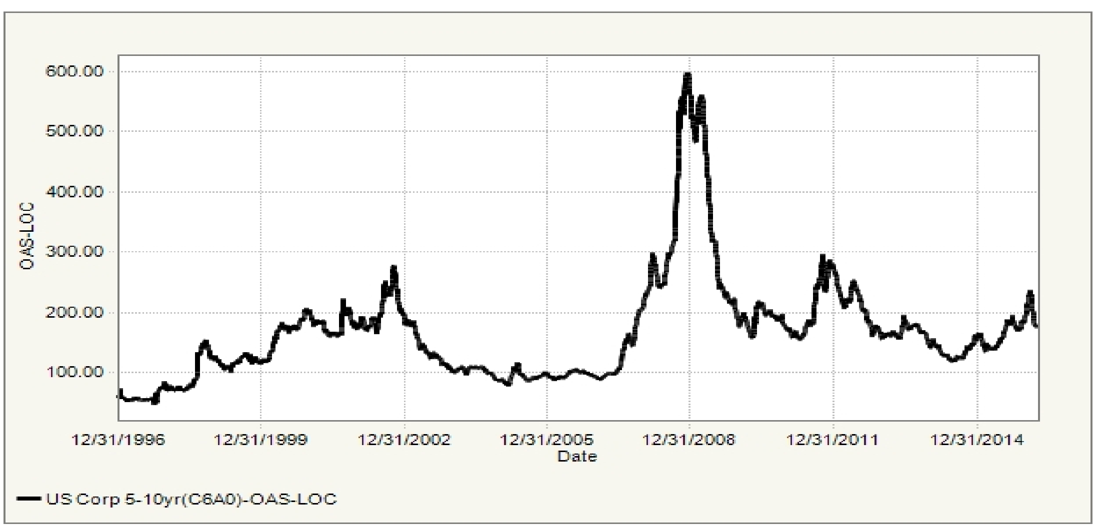


Source: Bank of America Merrill Lynch. The BofA Merrill Lynch 1-5 Year US Cash Pay High Yield Index is a subset of The BofA Merrill Lynch US Cash Pay High Yield Index including all securities with a remaining term to final maturity less than 5 years. It is not possible to invest directly in an index. See the end of this article for important disclosure information.

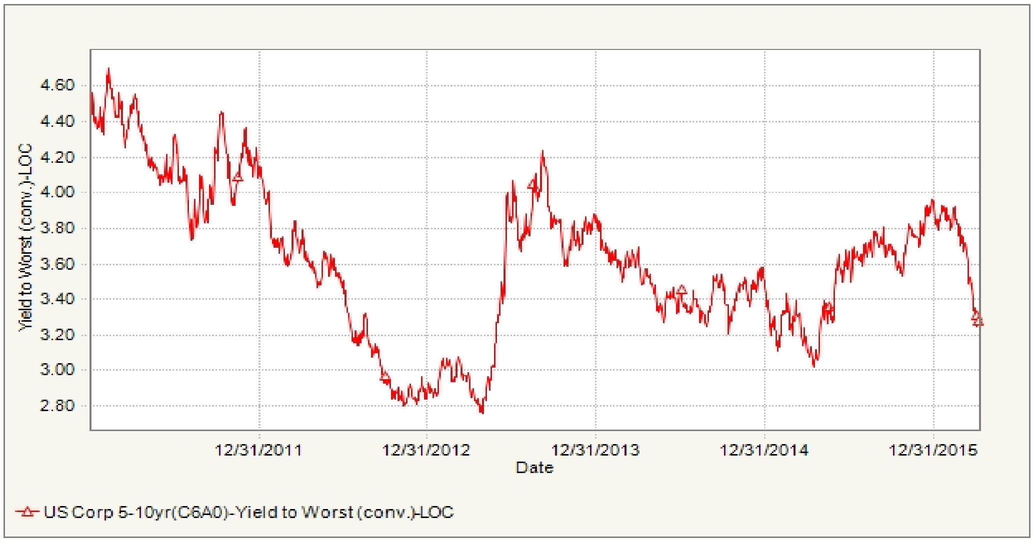
HIGH GRADE MARKET

Tailwind of falling rates. High grade corporate bonds and Treasuries both performed well in the first quarter, as interest rates fell sharply. The 10-year Treasury yield fell 0.50% during the quarter to close at 1.77%, after hitting 1.66% on February 11, 2016. In our view, Treasury yields fell due to concerns about global growth, a less aggressive rate hike cycle by the Fed, as well as continued quantitative easing measures and negative rates in Europe and Japan.

Valuations on intermediate corporate bonds hit attractive levels, in our view. Risk premiums on intermediate (5-10 year) investment grade corporate bonds had also increased sharply (similarly to high yield bonds) and hit a 3 year high of 237 bps on February 11, 2016. They have since tightened 60 bps to close the quarter at 177 bps. In addition, the yield on intermediate investment grade corporate bonds approached 4%, a level not hit since the end of 2013.



(See next page for source and disclosure information)



Source: Bank of America Merrill Lynch. The BofA Merrill Lynch 5-10 Year US Corporate Index is a subset of The BofA Merrill Lynch US Corporate Index including all securities with a remaining term to final maturity greater than or equal to 5 years and less than 10 years. It is not possible to invest directly in an index. See the end of this article for important disclosure information.

Taken together, these two factors led our 2016 strategic asset allocation process to reallocate the shorter term portfolios' investment grade corporate bond maturities from short-term (1-3 year) to intermediate-term (5-10 year).

FIRST-QUARTER REVIEW

The table below shows total returns for a broad cross sector of the fixed income market for the following time periods: 5/31/15-12/31/15 (risk market sell-off), 12/31/15-2/11/16 (the 2016 low point for risk assets), 2/11/16-3/31/16 (the rebound from the lows), and for the full quarter. The table also shows yields and risk premiums on 5/31/15, 12/31/15, 2/11/16, and 3/31/16, as well as quarter-end yields. During the first quarter all the major fixed income classes posted positive returns, with longer maturity bonds outperforming shorter-maturity bonds as Treasury yields fell sharply. High yield and emerging market bonds were able to post positive returns, despite a difficult start to the year.

	5/31/15-12/31/15	12/31/15-2/11/16	2/11/16-3/31/16	1Q16	5/31/2015	12/31/2015	2/11/2016	3/31/2016	
Oil $/bbl					$62.46	$39.98	$30.76	$38.34	
		Total Return (%)				**Yield**			
S&P 500	(1.80)	(10.27)	12.95	1.35					
2-year Treasury	(0.14)	0.91	(0.08)	0.82	0.61%	1.05%	0.65%	0.72%	
5-year Treasury	(0.19)	3.31	(0.36)	2.93	1.49%	1.76%	1.13%	1.21%	
10-year Treasury	(0.52)	5.95	(1.10)	4.78	2.12%	2.27%	1.66%	1.77%	
30-year Treasury	(1.88)	10.98	(1.84)	8.94	2.88%	3.02%	2.50%	2.61%	
		Total Return (%)				**Risk Premium (bps)**			**3/31/16 Yield**
Broad Bond Mkt	(0.43)	2.45	0.64	3.11					2.08%
5-10 Yr Corporates	(1.66)	1.06	3.05	4.15	145	185	237	177	3.34%
1-3 Yr Corporates	(0.10)	0.27	0.94	1.22	79	108	147	108	1.81%
High Yield[1]	(8.38)	(5.14)	8.84	3.25	452	695	887	705	8.39%
BB	(4.73)	(3.65)	7.64	3.71	307	424	582	428	5.69%
B	(9.15)	(5.56)	8.48	2.45	469	715	900	686	8.18%
CCC	(17.89)	(9.49)	14.71	3.83	930	1653	2066	1777	18.91%
HY Energy	(28.67)	(18.98)	26.59	2.56	651	1415	1984	1282	14.18%
S/T High Yield	(8.22)	(5.14)	7.68	2.15	516	835	1071	844	9.38%
Emerging Markets[2]	(2.23)	(0.63)	5.83	5.17	350	388	463	388	5.48%

Source: RiverFront Investment Group, Bank of America Merrill Lynch. Past performance is no guarantee of future results. See next page for index definitions.

1. High-yield securities (including junk bonds) are subject to greater risk of loss of principal and interest, including default risk, than higher-rated securities.

2. Investments in international and emerging markets securities include exposure to risks such as currency fluctuations, foreign taxes and regulations, and the potential for illiquid markets and political instability.

Index Definitions:

It is not possible to invest directly in an index.

- *Standard & Poor's (S&P) 500 Index measures the performance of 500 large cap stocks, which together represent about 75% of the total US equities market.*
- *Broad Bond Market is measured using the BofA Merrill Lynch US Corporate, Government & Mortgage Index, which tracks the performance of US dollar denominated investment grade debt publicly issued in the US domestic market, including US Treasuries, quasi-governments, corporates, covered bonds and residential mortgage pass-throughs.*
- *5-10 Year Corporates measured using the BofA Merrill Lynch 5-10 Year US Corporate Index (defined above)*
- *1-3 Year Corporates measured using the BofA Merrill Lynch 1-3 Year US Corporate Index, which is a subset of The BofA Merrill Lynch US Corporate Index including all securities with a remaining term to final maturity less than 3 years.*
- *High Yield measured using the BofA Merrill Lynch US High Yield Index (defined above)*
- *BB measured using the BofA Merrill Lynch BB US High Yield Index, which a subset of the BofA Merrill Lynch US High Yield Index including all securities rated BB1 through BB3, inclusive.*
- *B measured using the BofA Merrill Lynch Single-B US High Yield Index, which a subset of the BofA Merrill Lynch US High Yield Index including all securities rated B1 through B3, inclusive.*
- *CCC measured using the BofA Merrill Lynch CCC & Lower US High Yield Index, which a subset of the BofA Merrill Lynch US High Yield Index including all securities rated CCC1 or lower.*
- *High Yield Energy measured using the BofA Merrill Lynch US High Yield Energy Index is a subset of the BofA Merrill Lynch US High Yield Index including all securities of Energy issuers.*
- *Short-Term High Yield measured using the BofA Merrill Lynch 1-5 Year US Cash Pay High Yield Index (defined above).*
- *Emerging Markets measured using the BofA Merrill Lynch BBB & Lower Sovereign USD External Debt Index, which tracks the performance of US dollar-denominated emerging market and cross-over sovereign debt publicly issued in the eurobond or US domestic market.*

Important Disclosure Information:

Past performance is no guarantee of future results.

In a rising interest rate environment, the value of fixed-income securities generally declines.

High-yield securities are subject to greater risk of loss of principal and interest, including default risk, than higher-rated securities.

Investments in international and emerging markets securities include exposure to risks such as currency fluctuations, foreign taxes and regulations, and the potential for illiquid markets and political instability.

Yield to worst is calculated on all possible call dates. It is assumed that prepayment occurs if the bond has call or put provisions and the issuer can offer a lower coupon rate based on current market rates. If market rates are higher than the current yield of a bond, the yield to worst calculation will assume no prepayments are made, and yield to worst will equal the yield to maturity. The assumption is made that prevailing rates are static when making the calculation. The yield to worst will be the lowest of yield to maturity or yield to call (if the bond has prepayment provisions); yield to worst may be the same as yield to maturity but never higher.

Buying commodities allows for a source of diversification for those sophisticated persons who wish to add this asset class to their portfolios and who are prepared to assume the risks inherent in the commodities market. Any commodity purchase represents a transaction in a non-income-producing asset and is highly speculative. Therefore, commodities should not represent a significant portion of an individual's portfolio.

A basis point is a unit that is equal to 1/100th of 1%, and is used to denote the change in a financial instrument. The basis point is commonly used for calculating changes in interest rates, equity indexes and the yield of a fixed-income security. (bps = 1/100th of 1%)

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