Voya Global Perspectives

Markets. Insights. Opportunities.®

Douglas Coté, CFA
Chief Market Strategist

Karyn Cavanaugh, CFA
Senior Market Strategist

Executive Summary

- Central banks likely will continue backstopping unexpected risks and normalizing rates cautiously
- The U.S. and global economies are muddling along without apparent growth catalysts but few observable risks
- Market leadership has shifted from the U.S. toward riskier asset classes
- Investors should prudently stay broadly globally diversified to spread out risks and increase opportunities

Shift to Riskier Assets — not just EM

Index	Sep 2016	Q316	2016 YTD
Equity			
S&P 500	0.0	3.9	7.8
S&P Midcap	-0.6	4.1	12.4
S&P Smallcap	0.6	7.2	13.9
Global REITs	-0.9	1.5	11.0
EAFE	1.3	6.5	2.2
Emerging Mkts	1.3	9.2	16.4
Average	0.3	5.4	10.6
Fixed Income			
Corporate	-0.2	1.4	9.2
U.S. Treasury 20+	-1.7	-0.3	15.5
Global Aggregate	0.6	0.8	9.8
High Yield	0.7	5.6	15.1
Average	-0.2	1.9	12.4
Overall Average	**0.1**	**4.0**	**11.3**

Data as of 09/30/2015

Source: FactSet, FTSE NAREIT, Voya Investment Management

Perpetual Monetary Stimulus Keeps Global Risks at Bay

The world's central banks have been exceedingly cautious, acting as if markets cannot stand on their own two feet eight years after the Financial Crisis. Whenever a bout of volatility erupts, even entirely normal volatility, the world's central banks step in with more of the same — monetary stimulus. If central banks were the only answer, inflation and economic growth would be robust and self-sustaining — but it is not. Let's look at it. In the third quarter, fear of Brexit fallout drove the Bank of England to extraordinary lengths to stimulate the British economy. It worked remarkably well, and markets recovered within a week. Then, Bank of Japan confused the market by bringing out an unusual scheme that seems a lot like price controls — "targeting its sovereign yields." Lastly, the U.S. Federal Reserve punted on raising rates even though arguably it satisfied its dual mandate on inflation and unemployment. Today's net result is continued low yields, low growth, rising asset prices and suspicious investors.

This is not 2008, and even with recent concerns over European banks, the global banking system is sound. But growth continues to muddle along even in the resilient United States. What is the likelihood the next administration will improve growth prospects?

Without getting too political, we have two presidential candidates that in their own way believe that more government spending is at least partially the answer, and that global trade hurts the middle class. No matter which candidate is elected, progress on economic growth seems ephemeral. Without organic economic growth the world's central banks will remain in the precarious position of managing markets. Against this backdrop, investors should expect more of the same but prepare for the unexpected. A broadly diversified portfolio will mitigate, to revive a phrase from Donald Rumsfeld, "the unknown and unknowable" while improving the probability of reduced risk and increased return.

Q3 Market Review: A Litany of Surprises

True to form it was the summer of surprise. The biggest surprise came from emerging markets. Out of favor for several years, emerging market (EM) valuations became exceedingly attractive. A Fed on hold and a slightly weaker/stable dollar have taken the heat off EM currencies, allowing most to appreciate against the dollar in 2016. In addition, commodity prices rebounded from first quarter lows, helping many of the emerging commodity-producing nations. Emerging markets were up more than 10% in the quarter, nearly triple U.S. large cap stocks, sending returns to over 16% year to date.

Another surprise was the lack of negative market impact as the result of Brexit. In fact, most global markets moved up, posting strong gains in July before tapering off in August and September. A stellar quarter for MSCI EAFE's developed market stocks reversed losses of the previous two quarters, bringing the index into the positive column for the year. Large U.S. equities continued to grind higher though shifting in favor toward growth over value stocks. Technology dominated the quarter, surging over 12% and contributing nearly two-thirds of the S&P 500's overall return. The financial sector scored gains second only to high-flying technology issues but financials are still negative for the year as banks continue to struggle with ultra-low rates. Interest sensitive global REITS enjoyed another positive quarter despite

worries over potential Fed action. U.S. small-cap stocks nearly doubled their large-cap brethren for an astounding +7% return and were likewise dominated by technology. Investors were more willing to venture out on the risk spectrum knowing global central banks are exceedingly accommodative.

Large caps, the S&P 500 Index in particular, have been dominant over the last five years but at this point lag most other asset classes for the quarter and year. As a result, 2016 has seen a globally diversified portfolio of stocks and bonds once again besting the S&P 500 with less risk.

Yet another surprise — as equities rallied so did bonds. It was another strong quarter for bonds across the board as yields moved lower. High yield bonds led the way, although spreads remained in the historically normal range. Nevertheless, long U.S. Treasuries remain the best performer year to date. The currency stability that helped emerging markets also helped global fixed income performance. Investors, convinced that bond yields could not go any lower, continue to be vexed. Low global growth and the search for yield will keep the pressure on bond yields here and abroad. Notwithstanding the Fed's desire to increase rates, it is quite apparent that rates are stuck in the mud for a while.

U.S. Corporate Q2 Reported Earnings

There is positive news. Despite negative second quarter earnings growth that fully reported in September, the outlook is more sanguine. It is rare to see an earnings bear market without an accompanying recession. Investors have every right to be jittery. How can a market move to new record highs without accompanying fundamental growth? Quite simply, the market is looking forward. Negative earnings growth likely has troughed. Second quarter earnings growth was less negative than first quarter, and Q3 probably will be even better than Q2 — we may even see a return to the positive growth track after five quarters of negative growth. Sales are the precursor to earnings. Sales growth improved dramatically in Q2 from negative to essentially flat, and revenues look definitively positive for the third quarter. Finally, U.S. equity markets are relatively cheap compared to alternative investments, some of which offer negative yields.

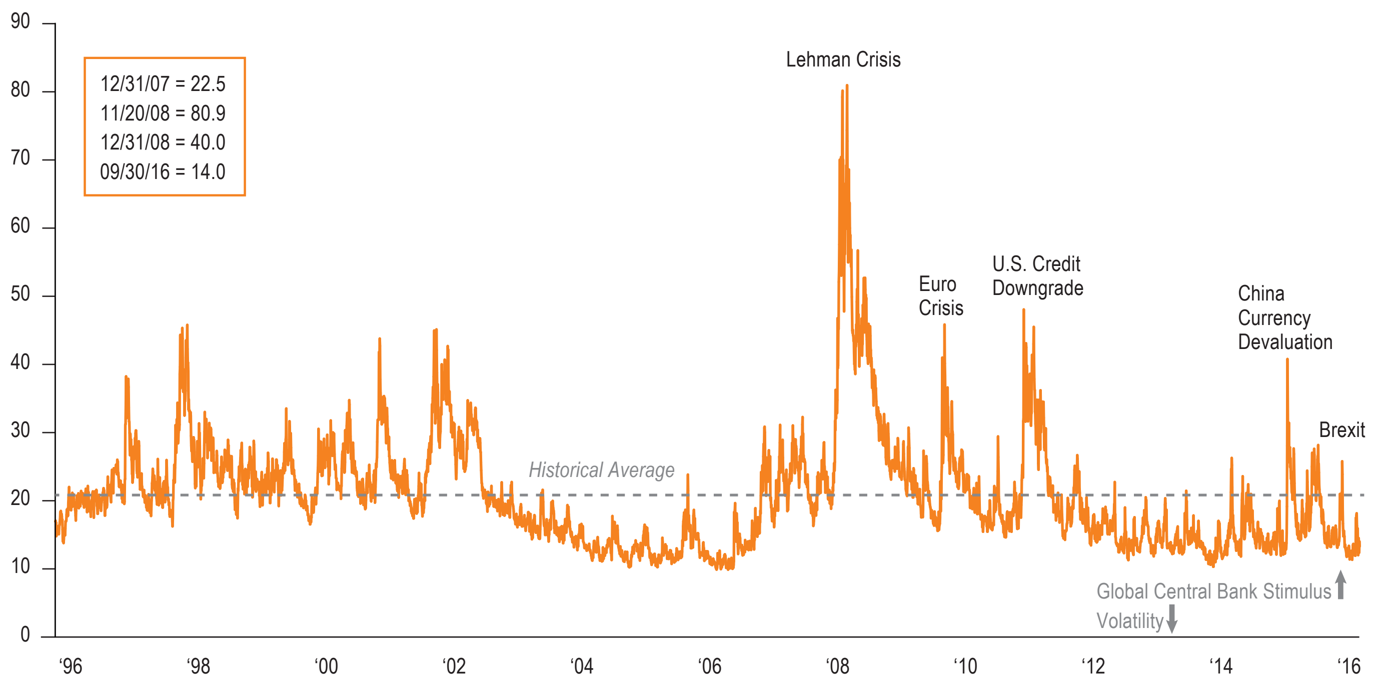
S&P 500 EPS Growth Negative for Five Consecutive Quarters as of 2Q 2016

Sector	Reported			Earnings Growth			Earnings Surprise		
	Actual	/	Total	Percent	Positive	Negative	Percent	Positive	Negative
Consumer Discretionary	86	/	86	11.7%	58	28	5%	61	16
Telecommunication Services	5	/	5	7.2%	2	2	2%	2	1
Health Care	56	/	56	5.6%	44	10	3%	47	3
Utilities	29	/	29	5.1%	17	9	3%	16	9
Consumer Staples	35	/	35	0.3%	20	15	3%	26	7
Information Technology	67	/	67	-0.6%	45	21	7%	56	4
Industrials	68	/	68	-3.7%	34	34	6%	49	14
Financials	90	/	90	-4.2%	52	38	3%	61	20
Materials	26	/	26	-8.8%	15	11	2%	15	9
Energy	38	/	38	-84.2%	4	27	-26%	25	10
S&P 500	500	/	500	-3.2%	291	195	4%	358	93

Source: FactSet. Note: Earnings growth is the percentage change in the cumulative share-weighted earnings per share from that of a year ago. Earnings surprise percent is the share-weighted average of the ratio of actual company earnings vs. the consensus estimates.

Since 2012, QE3 Volatility has been Muted

Equity Volatility (VIX)



Sources: Standard & Poor's, Chicago Board Option Exchange, FactSet. Data as of September 30, 2016.

Economic Update

Domestic

- On the economic home front, the data have been positive but patchy. The chance of a U.S. recession remains low, bolstered mainly by the household sector and consumer spending
- In Q3, the U.S. economy continued to add jobs. The 12-month average continues at over 200,000 jobs per month and unemployment remains low at 4.9%, keeping the consumer outlook strong
- Adding to consumer strength is the housing market, which continues to post price gains at double the core inflation rate. The latest Case-Shiller index reading was up 5%
- U.S. CPI and Core CPI made significant gains in August, driven by rising health care prices, but the Fed's preferred measure, PCE, remains below the target 2%

International

- Euro-area industrial production fell more than expected, dropping -1.1% month over month in July, hinting that the true effect of Brexit is beginning to be felt across Europe's industrial sector
- Japan introduced yet another stimulus package, but the yen's strength continues to hurt corporate profits and push down import prices, making it difficult to generate inflation; core CPI fell below 0% in September
- A third quarter surge in China's industrial production is encouraging and reinforces the theme of stabilization in the Chinese economy

Conclusion

The central banks have been — and likely will continue — backstopping unexpected risks and normalizing rates very cautiously. Meanwhile, U.S. and global economies are muddling along without an apparent catalyst to propel growth forward but also with few observable risks. Investors, though, should take note of the pronounced shift of market leadership away from the U.S. toward riskier global asset classes. This may or may not be a sign of things to come, but it is always prudent to stay broadly globally diversified to spread out risks and increase opportunities.

Diversification does not guarantee a profit or ensure against loss

This commentary has been prepared by Voya Investment Management for informational purposes. Nothing contained herein should be construed as (i) an offer to sell or solicitation of an offer to buy any security or (ii) a recommendation as to the advisability of investing in, purchasing or selling any security. Any opinions expressed herein reflect our judgment and are subject to change. Certain of the statements contained herein are statements of future expectations and other forward-looking statements that are based on management's current views and assumptions and involve known and unknown risks and uncertainties that could cause actual results, performance or events to differ materially from those expressed or implied in such statements. Actual results, performance or events may differ materially from those in such statements due to, without limitation, (1) general economic conditions, (2) performance of financial markets, (3) interest rate levels, (4) increasing levels of loan defaults (5) changes in laws and regulations and (6) changes in the policies of governments and/or regulatory authorities.

The opinions, views and information expressed in this commentary regarding holdings are subject to change without notice. The information provided regarding holdings is not a recommendation to buy or sell any security. Fund holdings are fluid and are subject to daily change based on market conditions and other factors.

Past performance is no guarantee of future results.

©2016 Voya Investments Distributor, LLC • 230 Park Ave, New York, NY 10169 • All rights reserved.

BBGP-COMMENTARY_1016 • 100516 • IM-1004-28016-1017 • **163081**

PLAN | INVEST | PROTECT

VOYA®

voyainvestments.com