WELLS FARGO
INVESTMENT INSTITUTE

Global Investment Strategy

Global Fixed Income Strategy: Monthly Guidance

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Monthly Guidance on Global Fixed Income Investments

» *While U.S. Treasury yields have risen in recent months, yields remain relatively low on a historical basis.*

» *We recommend that individuals position duration below their individually-selected benchmarks.*

» *We recommend that investors maintain fixed-income exposure at targeted allocations and remain broadly and globally diversified.*

» *We continue to recommend raising average credit quality in fixed-income portfolios.*

» *The new tax law may result in increased demand for municipals in the near term, and reduced supply.*

Monthly Fixed Income Guidance: April 2018

In our Monthly Fixed Income Guidance report for April 2018, we share our tactical (six to 18 month) guidance for fixed-income classes and sectors. Wells Fargo Investment Institute (WFII) has moved to a five-tier level of investment strategy guidance from the previous three tiers of guidance. The current guidance levels are reflected below (and on the following pages).

	WFII Guidance						
	Most Unfavorable				Most Favorable	YTD	1 Year
U.S. Taxable Investment Grade Fixed Income		■				-1.5%	1.2%
U.S. Short Term Taxable Fixed Income				■		-0.2%	0.2%
U.S. Intermediate Term Taxable Fixed Income			■			-1.2%	0.6%
U.S. Long Term Taxable Fixed Income	■					-3.6%	5.0%
High Yield Taxable Fixed Income		■				-0.9%	3.8%
Developed Market Ex-U.S. Fixed Income (Unhedged)		■				4.5%	12.6%
Emerging Market Fixed Income (U.S. Dollar)			■			-1.8%	3.3%
Municipal				■		-1.1%	2.7%

	WFII Guidance						
	Most Unfavorable				Most Favorable	YTD	1 Year
Government Securities		■				-1.1%	0.4%
Treasury Securities			■			-1.2%	0.4%
Agencies		■				-0.5%	0.8%
Inflation-Linked Fixed Income			■			-0.8%	0.9%
Investment-Grade Credit				■		-2.1%	2.6%
Investment-Grade Corporate				■		-2.3%	2.7%
Preferred Stock				■		-0.6%	3.1%
Securitized			■			-1.2%	0.8%
Residential Mortgage-Backed Securities (MBS)			■			-1.2%	0.8%
Commercial Mortgage-Backed Securities		■				NA	NA
Asset-Backed Securities		■				NA	NA

WFII Guidance Legend:

Most Favorable **Favorable** **Neutral**

Unfavorable **Most Unfavorable**

Source: Bloomberg, March 31, 2018. **Past performance is no guarantee of future results**. See end of report for important risk information, index definitions, and WFII guidance definitions. Inflation-Linked Fixed Income equates to Treasury Inflation-Protected Securities. WFII = Wells Fargo Investment Institute. Asset classes in blue are tactical recommendations, and specific tactical allocation models can be found in the most recent Asset Allocation Strategy Report. Asset classes in gold represent sector guidance and do not have specific allocations within tactical asset allocation models.

Investment and Insurance Products: ▶NOT FDIC Insured ▶NO Bank Guarantee ▶MAY Lose Value

Tactical Guidance

U.S. Taxable Investment-Grade Fixed Income	Unfavorable

The U.S. economic outlook has improved since the Tax Cuts and Jobs Act was signed into law, and it continues to be generally supportive of investment grade (IG) fixed income—while putting some upward pressure on yields. We believe that investors' taxable total-return expectations should be tempered, given the increase in fixed-income volatility over the past several months. We believe that price risk should be muted by a Federal Reserve (Fed) interest-rate policy that is tightening at a measured pace, modest inflation expectations, and low global interest rates overall.

U.S. Short-Term Taxable Fixed Income	Favorable

Short-term rates have risen over the past several months, flattening the yield curve and providing an increasingly attractive interest-rate profile for short-term securities. Investing in short-term, fixed-income securities offers a lower risk profile than that of longer duration fixed-income instruments, helping to mitigate potential risk of unexpected interest-rate increases stemming from an unanticipated rise in inflation. Additionally, recent comments by Fed Chair Jerome Powell that the Fed will continue to increase rates at a measured pace signals attractive roll-down opportunities on the short end of the yield curve.

U.S. Intermediate-Term Taxable Fixed Income	Neutral

We expect the Fed to maintain a measured pace of interest-rate hikes through 2018. With the recent increase in bond yields, the attractiveness of intermediate-maturity bonds has improved somewhat. We believe that investors should maintain some exposure to intermediate maturities within fixed-income allocations—to capitalize upon the term premiums.

U.S. Long-Term Taxable Fixed Income	Most Unfavorable

Increasing market uncertainty around the scope of further interest-rate increases, the potential for higher inflation, ambiguity around fiscal trade policy, and infrastructure spending all present this asset class with a wide range of potential outcomes. As a result, our most unfavorable weighting reflects our increasing concern over rising yield risks for long-term securities going forward.

Duration	Unfavorable

Duration positioning is critical for fixed-income investors. As noted, duration measures a bond's price sensitivity to interest-rate changes. Bonds with shorter duration tend to be less sensitive to changes in interest rates (assuming a parallel shift in the yield curve). Bond-market volatility recently has risen but remains low by historical standards. In an environment of shrinking monetary accommodation and increased fiscal spending, we believe that higher interest-rate volatility may provide opportunities to adjust duration to capitalize upon any dislocation. As such, we currently recommend that investors reduce duration to a level below their individually-selected benchmarks.

Portfolio Positioning

Structure

We believe that modest, but higher, global inflation and a gradual global recovery should help to keep interest rates relatively low. As we expected, rates have increased modestly, resulting in yields that are slightly more compelling on maturities across the yield curve than was previously the case. We recommend that investors consider utilizing multiple positions along the yield curve in the current environment. We believe that roll-down opportunities are most attractive on the short end of the yield curve.

Credit Quality

Credit spreads are near the tightest (lowest) they have been in a decade, and they no longer offer a compelling value proposition. Given our expectation for slow and steady U.S. economic growth, we believe that current spread levels can be maintained. However, we have witnessed some slippage in credit fundamentals, and we believe that investors should be particularly careful about security selection—we reiterate our emphasis on credit analysis with a focus on higher-quality issues (over those of lower quality). Recent weakness in IG spreads has caused lower-quality issues to underperform higher-quality securities, but current levels still only provide minimal compensation compared to historical levels.

Government Securities — Unfavorable

Uncertainties surrounding potential fiscal stimulus, funding of the recently passed tax cuts, and the Fed's balance-sheet reduction introduce the potential for increased volatility in this sector. We recommend that investors hold government security allocations for diversification, liquidity, and situations where investors chose to de-risk portfolios. Government securities may offer a hedge in the event of unexpected international events or an economic slowdown and are generally the beneficiary of risk-off events in the market.

Treasury Securities — Neutral

Yields on U.S. Treasury securities currently remain attractive versus those in developed sovereign bond markets abroad, but they could come under pressure as the Treasury's funding needs increase in 2018, especially on the short end of the yield curve. Treasury securities appear fairly valued relative to their risk and continue to offer an attractive liquidity profile.

Agencies — Unfavorable

We believe that yields in the agency sector will remain highly correlated with Treasury yields. Yet, agency securities currently offer very little spread for the added perceived risk, particularly when viewed on a historical basis. This limits the overall appeal of agency securities at this time, given the higher liquidity of Treasury issues and very little, if any, yield pickup to be gained in agency bonds at current levels.

Inflation-Linked Fixed Income — Neutral

Investors' inflation expectations, as measured by the breakeven rate for 10-year Treasury Inflation-Protected Securities (TIPS), recently have reached the current Consumer Price Index (CPI) level (after having been below that inflation measure for most of 2017). We currently see TIPS as fully valued; however, breakeven rates that are in line with (or below) the CPI may continue to offer an attractive hedge against unexpected inflation over the medium to long term. While TIPS generally have outperformed nominal Treasury securities recently, higher breakeven rates and some seasonal quirks in official inflation data make them somewhat less attractive today than they were in the recent past.

Investment-Grade Credit — Favorable

High-quality IG credit can allow fixed-income portfolios to generate excess yield through spread premium (also known as "carry") that is meant to compensate investors for perceived issuer credit risk. We believe that high-grade corporate debt offers investors better carry and liquidity per unit of risk than can be found in many other credit offerings in the fixed-income markets, such as high yield or securitized investments. While the sector appears to be fully valued, we believe that a bias toward higher quality in the current market will continue to offer valuable excess yield.

Investment Grade Corporate — Favorable

Some caution is warranted in this sector—as credit fundamentals on corporate bonds have declined over the past several years. Leverage and interest-coverage ratios have steadily deteriorated since 2013, and these trends have the potential to push credit spreads to wider (higher) levels. However, in our opinion, these holdings continue to offer attractive carry potential in a market segment that we believe offers better liquidity than other sectors. Emphasis on sound credit analysis, with a focus on higher-quality issuers and sectors, is recommended. The recent tax law changes have resulted in a reduction of debt issuance by companies looking to finance capital expenditures and share buybacks. This trend should provide some relief to the increasing leverage narrative. We believe that corporate bonds on the short end of the yield curve (1-3 years) are attractive after recent spread widening pressure (due mostly to large corporations demanding less short-term paper as a result of new cash repatriation laws).

Preferred Stock	Favorable

The preferred sector does present some opportunities to purchase higher coupons, but this must be weighed against the interest-rate risk inherent in long maturity or perpetual preferred securities. We remain concerned that longer-term investors may be faced with higher interest rates that could decrease the value of certain preferred securities; those securities that have low coupons are most at risk in a rising-rate environment. We believe that the preferred market can maintain valuations should interest rates rise modestly from current levels. Should we enter a period in which the markets become risk averse, we would expect preferred securities to fall in value.

Securitized	Neutral

Yield is an important component of an investor's sector selection, and the securitized sector offers investors income opportunities that cannot be found in other highly-rated, fixed-income securities.[1] This sector can provide diversification to a fixed-income portfolio and generally has less correlation to other sectors.

Residential Mortgage-Backed Securities	Neutral

Residential mortgage-backed securities (MBS) could be favored by the market due to their (historically) strong liquidity and low-credit-risk profile. We favor a barbell structure with modest discounts and premiums (versus more current coupon issuance). Extension risk is always a concern during periods of rising rates. Also, the Fed's continued balance-sheet reduction of MBS is set to increase in the months ahead and could lead to some market dislocation.

Commercial Mortgage-Backed Securities	Unfavorable

Credit research is critical for investors purchasing commercial MBS. We are specifically concerned with retail-focused commercial MBS issuers. Given weakness in the retail space, we recommend that investors favor other segments of the market, such as the office and hospitality sectors. Commercial MBS represent less than 2% of the Bloomberg Barclays Aggregate Index. They can be especially illiquid, and investors should weigh their benchmark allocation and illiquidity factor when considering purchases of these securities.

Asset-Backed Securities	Unfavorable

This sector has been a steady outperformer for an extended period of time; however, it represents approximately 0.50% of the Bloomberg Barclays Aggregate Index. Although we believe that this sector currently is fully valued, and we don't expect much spread tightening from here, we do believe that asset-backed securities can provide investors with reasonably attractive yields, important sector diversification, and relative stability. Fundamentals remain strong as consumers have significantly reduced their leverage in recent years. We particularly favor AAA-rated credit card and auto issues. With rising delinquencies, we urge investors to avoid sub-prime auto paper (where aggressive borrowing and delinquencies resemble late-cycle behavior), along with the private student-loan sector

[1] Fixed-income securities whose interest and principal payments are backed by cash flows from a pool (or portfolio) of other securities are securitized fixed-income assets. Examples include mortgage-backed securities and asset-backed securities.

due to policy uncertainty and emerging litigation risks). Investors that are considering auto paper for purchase should fully understand the collateral and payment position of these investments.

Municipal	Favorable

Despite a 0.4% March gain, Municipals have been challenged by rising yields year to date (along with other domestic classes)—as rates rose in the face of tax reform and fiscal-spending-fueled economic growth. Nevertheless, new issuance has fallen by approximately one-third YTD from 2017 levels (which has been supportive). This resulted from record supply late last year, fueled by tax reform. Additionally, the new tax law eliminates municipalities' ability to advance refund debt (existing bonds retain their tax-exempt status). Tax season often fuels market weakness, but we believe that municipals will strengthen in coming quarters as reduced supply and a large June reinvestment offers support. This could create an opportunity for outperformance as municipals become even more scarce—while the tax law's cap on state and local tax deductions fuels rising demand. We have an unfavorable position on duration, given our rising-rate forecast. We expect Fed rate increases to continue, which would exert upward pressure on rates that would run counter to the effects of reduced supply. We view any weakness as a buying opportunity. We also favor a quality bias and a more defensive bond structure. We also favor higher quality essential service revenue securities today.

Portfolio Positioning

Duration	Unfavorable

We have moved to an unfavorable duration position, given our higher interest-rate forecast (along with the short-term market pressures on municipals). We see near-term pressure in municipals as a longer term buying opportunity, given the expectation of reduced municipal supply in 2018. Unfortunately, municipals have had negative performance year to date (-1.1%) despite supply being 31% below last year's levels (due to rising interest rates). It should be noted that, in general, municipal-bond benchmark indices are slightly longer in duration than overall fixed-income benchmark indices.

Structure

Longer-term, premium-coupon callable bonds often offer higher yields relative to duration and can provide an income "cushion" to help offset rising rates. We favor premium coupon structure; intermediate, lower-coupon bonds are trading near or through their de minimis limits. (Once a bond falls below the de minimis threshold, liquidity and market price can be affected—as the buyer now has to pay capital gains on the bond's accretion.) Callable bonds can benefit those who are concerned about rising rates, but balance is needed, as too many short-callable securities in a portfolio also can pose a risk to stable income flows. (Short-callable securities also have been offering less compelling spreads recently.) We believe that caution is warranted relative to longer-maturity, lower-coupon bonds that may underperform and provide less liquidity during rising-rate cycles.

Curve Positioning

We now favor the shorter part of the yield curve for municipals (and other domestic classes). Short-dated paper has been in abundance, and there has been less demand globally stemming from government funding needs (and lower corporate demand for short-dated debt). We believe that this could offer investors the advantage of higher short-term yields (combined with the historically lower volatility of shorter-duration assets). In March, two year municipal securities hit a nine-year high. They now trade at higher ratios versus Treasury securities, making them even more attractive.

Credit Quality

We continue to recommend a focus mainly on single-A-rated and higher-credit-quality issues today. Some stable, BBB-rated credit issues (in strong sectors, such as essential service revenue credits), may be appropriate for certain investors with a higher risk tolerance (that can look at the lower portion of the IG space). Shorter maturities may be a compelling maturity area for such lower-quality credits today.

We prefer to emphasize the underlying credit, particularly as bond insurers come under greater scrutiny by the rating agencies. A sound bond insurance wrapper can provide further credit support; however, it may become more difficult to diversify insurance providers in portfolios, due to the increasingly limited number of high quality insurers.[2]

Revenue (Essential Service)	Favorable

Although economic growth remains muted, we believe that fundamentals are stable-to-improving in essential-service sectors, given their lower leverage and relatively consistent operating margins, and their lower vulnerability to broader budgetary concerns. We believe that essential-service revenue bonds generally are better equipped (than other types of municipal bonds) to deal with extreme market events, should they occur. Like general obligation bonds (below), some revenue sectors such as health care and education may have greater exposure to broad matters of political policy than traditional essential-service revenue bonds. Fixed-income market participants are watching developments in Puerto Rico's bankruptcy case as it pertains to special revenue bonds.

General Obligation (State and Local)	Neutral

We believe that state and local general-obligation (GO) holdings offer both opportunity and sources of concern. Generally speaking, we favor state (over local) GO issues, but we would caution that there is a wide degree in credit discrepancy in those categories. There are unique cases that should be closely watched going forward, particularly where unfunded pension liabilities are an issue. Additionally, we are closely monitoring possible nearer-term policy impacts on both GO and revenue debt arising from the new tax legislation. Tax policy changes carry potential impacts on state and local revenues and expenses. Federal treatment of state and local taxes, reduced federal support of programs and projects that are shared with states and localities, any changes in health care support, and other potential downstream effects all could impact various municipal issuers.

Taxable Municipal	Favorable

We have seen stronger demand for taxable municipal debt recently. We believe that this warrants a favorable recommendation. We prefer shorter-term taxable municipals as we believe that they offer a combination of improved credit characteristics with attractive yield potential versus their taxable counterparts.

Pre-Refunded	Most Favorable

Pre-refunded securities currently are fairly priced relative to non-refunded municipals, with yields 1-2 basis points better than AAA-rated securities, but 3-8 basis points more expensive than AA-rated securities. The larger issue is that tax reform is ending the pre-refunding of outstanding municipal issues. This will leave a shrinking pool of pre-refunded bonds in the marketplace. Under these circumstances, existing pre-refunded bonds likely will be in high demand while they remain outstanding.

Crossover Opportunities	Favorable

Short-term corporate yields have risen significantly relative to yields on municipal securities. Based on our measures, this represents a good crossover buying opportunities. Historical data (z-scores) suggests that corporate securities can be expected to outperform over the medium term.

High Yield Taxable Fixed Income	Unfavorable

Valuations, on a spread basis, are expensive in the high-yield debt class. Leverage has continued to increase. Given the increase in leverage, valuations and the laws of bond mathematics, the high-yield debt class is faced with an asymmetric risk profile. We recommend moving up in credit quality. Within the overall portfolio and even within the fixed-income asset group, we believe that better risk-adjusted return opportunities present themselves.

[2] **Bond insurance:** When an insurance company guarantees scheduled payments of interest and principal on a bond in the event of default by the issuer.

Bank Loans — Neutral

Bank loans are higher in the capital structure than traditional high-yield bonds and can help to diversify a high-yield allocation. As LIBOR (the London Interbank Offered Rate) continues to rise, along with the Fed's interest-rate targets, many bank loans now have risen to levels above their interest-rate floors, with the potential to provide a partial hedge against a rising-rate environment.

High Yield Tax-Exempt Fixed Income — Unfavorable

While the high-yield municipal market recently has outperformed the IG municipal market, we believe that this sector has benefited from investors seeking yield and "chasing" past performance. We don't believe that future prospects for this sector warrant the volatility risk that we expect this year. We hold an unfavorable view of this sector, which is consistent with our broader view on high yield issues. In a down market, investors tend to sell weaker credits first, often exacerbating price declines on those lower-credit-quality names.

Developed-Market Ex-U.S. Fixed Income — Unfavorable

We are unfavorable toward developed-market (DM) debt as many DM yields remain below Treasury yields. While yields are rising and fundamentals outside the U.S. appear to be improving (notably in the eurozone), the yield differential is still too wide to make DM bonds attractive. Additionally, it entails high foreign-exchange risk, which is insufficiently compensated by income or capital gain prospects (since the strategic index is unhedged in term of currency exposure). We look for continued euro gains versus the dollar to enhance returns over a one-year time horizon, but this expectation is subject to higher uncertainty—and it is in the context of continuing low coupons and anticipated capital losses as yields gradually normalize. Consequently, we believe that expected returns will remain low and expected volatility will remain high.

Regional

Despite recent credit upgrades, we believe that (from current tighter levels) any further narrowing in Spanish and Portuguese spreads will be harder won. We also believe that Italian spreads may remain somewhat wider than those of Italy's peers. Even if investors are currently prepared to ignore the threat of a populist government in Italy after general elections held on March 4, the country remains a weak link within the eurozone, economically and politically. Further, as the European Central Bank (ECB) has reduced its sovereign-debt buying program by half from January 2018, market anticipation of this program's eventual end may cause spreads to widen later in 2018—and spreads of countries with larger issuance needs (such as Italy) may become vulnerable again to any economic slowdown. For these reasons, we maintain a cautious view on eurozone sovereign spreads on a tactical timescale.

DM Eurozone Sovereigns (versus IG Corporates) — Unfavorable

Eurozone-denominated sovereign yields initially rose sharply with U.S. Treasury yields in early 2018, but since that time, they have declined somewhat. Although spreads of eurozone IG corporates over sovereigns are historically narrow, we believe that sovereign yields have been artificially depressed by ECB buying. We expect them to rise gradually as quantitative easing (QE) ends in 2018 or early 2019. This low absolute value (the largest sovereign markets within the benchmark index, the eurozone and Japan, still have yields close to zero or negative across much of the yield curve) offsets the better relative value from narrowing spreads. Further narrowing of corporate spreads below recent lows, a rise in risk-asset volatility, or a deterioration in the macro environment would encourage us to move to a neutral rating.

DM Eurozone Investment-Grade Corporates (Euro-Denominated) (versus Sovereigns)	Neutral

Although corporate yields (in this bond class) were initially slower to rise than sovereign yields early in 2018, corporate yields have not reversed their ascent even as government bond yields dipped lower recently. An increase in equity-market volatility and general market uncertainty is to blame, offsetting the still-positive credit backdrop. We lowered our favorable view on corporate spreads to neutral on the break below 100 basis points, and we maintain the neutral view for now—even though spreads have widened sharply (back) after failing to establish a level below 80 basis points. This mirrors our neutral sovereign rating above. Although corporate spreads remain historically tight, and may be vulnerable later as the ECB withdraws its asset-purchase support, for now, corporates are making up a larger part of the asset purchase program than they did in 2017. Consequently, we would not expect spreads to continue to widen sharply in the near term (unless the macro environment becomes less conducive to credit than we currently anticipate).

Emerging-Market Fixed Income	Neutral

Credit spreads on emerging-market (EM) bonds have tightened (declined) to levels below their long-term averages, driven by improving global growth and benign inflation. Valuations are not cheap, but are not yet excessively expensive. We remain neutral on this asset class, as we see positive and negative factors as balanced over the tactical horizon. Positive factors are an attractive yield around 6%, good fiscal fundamentals (relative to local-currency EM issuance and to U.S.-dollar-denominated corporates) and a still fairly benign global macro backdrop. Factors that we view as more negative include the potential for increases in underlying U.S. Treasury yields (EM sovereigns have relatively longer duration), and risks to the sovereign credit from domestic and international politics and trade—as the global policy environment becomes more unpredictable (which should limit further spread tightening from here).

EM U.S.-Dollar-Denominated Sovereigns (versus EM U.S.-Dollar-Denominated Corporates)	Favorable

EM sovereign spreads (for U.S.-dollar-denominated debt), at 300-350 basis points, are relatively tight, but they are not extreme in the post-2008 period. The rise in U.S. Treasury yields (the benchmark for sovereign spreads) hit EM dollar bond returns in early 2018, but we expect the impact of this factor to be reduced going forward as U.S. Treasury yield increases level off. EM sovereign credit metrics have improved considerably since the crisis in the 1990s. EM sovereigns have an aggregate government debt/gross domestic product (GDP) ratio of around 50 percent, less than half the ratio for developed markets. We modestly favor U.S.-dollar-denominated EM sovereigns over corporates, in part because they make up the strategic benchmark, and corporates are therefore an off-benchmark bet. Yet, this view also is because of better fiscal fundamentals and somewhat less extreme valuations on a spread basis. We do not rate sovereigns as most favorable because their longer duration may make them more vulnerable (than corporates) to an unanticipated rise in U.S. Treasury yields.

EM U.S.-Dollar-Denominated Corporates (versus EM U.S.-Dollar-Denominated Sovereigns)	Unfavorable

Over the medium-term, we continue to prefer EM U.S. dollar sovereigns to corporates. The large increase in corporate leverage over the past few years (especially in China) puts corporates more at risk of defaults than sovereigns if the global environment deteriorates and/or U.S. rates rise sharply. Aggregate non-financial corporate debt has risen by 30-40 percentage points (of GDP) in the past decade. Valuations (in terms of the spread over U.S. Treasury securities) are somewhat more stretched versus history than for they are for sovereigns (perhaps reflecting the lesser liquidity in corporates), with corporate index spreads below 300 basis points, close to the 2011 lows of approximately 250 basis points.

Risk Factors

Investments in fixed-income securities are subject to interest rate, credit, liquidity, prepayment, extension and other risks. Interest rates change over time due to market conditions and changes in government policies. Bonds with longer durations are generally more price sensitive and volatile than those with shorter durations. Because bond prices generally fall as interest rates rise, the current low interest rate environment can increase the bond's interest rate risk. 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 than investment grade securities. Liquidity risk is the risk that an investor may have difficulty selling a particular bond and thereby be forced to sell at a significant discount to market value. This risk is greater for thinly traded securities. If sold prior to maturity, all fixed income securities are subject to market risk and may be worth less than their original cost.

Bank loans are subject to interest rate and credit risk. They are generally below investment grade and are subject to defaults and downgrades. These loans have the potential to hedge exposure to interest rate risk but they also carry significant credit and call-risk. Call risk is the risk that the issuer will redeem the issue prior to maturity. This may result in reinvestment risk which means the proceeds will generally be reinvested in a less favorable environment. Bank loans are difficult to value, have long settlement times and are relatively illiquid. As a result, they could face liquidity challenges.

Exposure to the commodities markets may subject an investment to greater share price volatility than an investment in traditional equity or debt securities. 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. Products that invest in commodities may employ more complex strategies which may expose investors to additional risks.

U.S. government securities, including Treasury securities, are backed by the full faith and credit of the federal government as to payment of principal and interest if held to maturity. Although free from credit risk, they are subject to interest rate risk.

Treasury Inflation-Protected Securities (TIPS) are subject to interest rate risk, especially when real interest rates rise. This may cause the underlying value of the bond in the portfolio to fluctuate more than other fixed income securities.

Municipal bonds offer interest payments exempt from federal taxes, and potentially state and local income taxes. Municipal bonds are subject to credit risk and potentially the Alternative Minimum Tax (AMT). Quality varies widely depending on the specific issuer. Municipal securities are also subject to legislative and regulatory risk which is the risk that a change in the tax code could affect the value of taxable or tax-exempt interest income.

The yield, average life and the expected maturity of mortgage-related, commercial mortgage-backed securities and asset-backed securities are based on prepayment assumptions that may or may not be met. Changes in prepayments may significantly affect yield, average life and expected maturity.

There are special risks associated with investing in preferred securities. Preferred securities generally offer no voting rights with respect to the issuer. Preferred securities are generally subordinated to bonds or other debt instruments in an issuer's capital structure, subjecting them to a greater risk of non-payment than more senior securities. In addition, the issue may be callable which may negatively impact the return of the security. Preferred dividends are not guaranteed and are subject to deferral or elimination.

Investing in foreign securities presents certain risks not associated with domestic investments, such as currency fluctuation, political and economic instability, and different accounting standards. This may result in greater price volatility. These risks are heightened in emerging markets. In addition to the risks associated with investing in international and emerging markets, sovereign debt involves the risk that the issuing entity may not be able or willing to repay principal and/or interest when due in accordance with the terms of the debt agreement.

Sovereign debt is generally a riskier investment when it comes from a developing country and tends to be a less risky investment when it comes from a developed country. The stability of the issuing government is an important factor to consider, when assessing the risk of investing in sovereign debt, and sovereign credit ratings help investors weigh this risk.

Forecasts are not guaranteed and are subject to change.

WFII Guidance Definitions

Most favorable: WFII's highest conviction guidance that indicates a strong desire to overweight an asset class (or sector) within a portfolio. It also communicates that, over a tactical time frame, WFII views the asset class (or sector) as offering investors a very attractive risk/reward opportunity.

Favorable: Guidance that indicates a desire to overweight an asset class within a portfolio. It also communicates that, over a tactical time frame, WFII views the asset class (or sector) as providing investors with an attractive risk/reward opportunity.

Neutral: Guidance that indicates a desire to maintain an asset class near the long-term (strategic) allocation guidance within a portfolio. It also communicates that, over a tactical time frame, WFII views the asset class (or sector) as providing investors with an acceptable risk/reward opportunity.

Unfavorable: This WFII guidance level indicates a desire to underweight an asset class (or sector) within a portfolio. It also communicates that, over a tactical time frame, WFII does not view the asset class (or sector) as providing investors with an attractive risk/reward opportunity.

Most unfavorable: WFII's highest conviction guidance indicating a strong belief in underweighting an asset class within a portfolio. This also communicates that, over a tactical time frame, WFII views the asset class (or sector) as offering investors a very unattractive risk/reward opportunity.

Rating Definitions

AAA/Aaa rating: The highest quality debt, with minimal credit risk.
AA rating: High quality and subject to very low credit risk.
A rating: Upper-medium grade and subject to low credit risk.
BBB rating: Obligations are subject to moderate credit risk; considered medium-grade, and as such may possess certain speculative characteristics.

Index Definitions

An index is unmanaged and not available for direct investment.

Agencies:
Bloomberg Barclays U.S. Agency Index measures the performance of the agency sector of the U.S. government bond market and is comprised of investment-grade, native-currency U.S- dollar-denominated debentures issued by government and government-related agencies, including FNMA. The index includes both callable and non-callable agency securities that are publicly issued by U.S. government agencies, quasi-federal corporations, and corporate and foreign debt guaranteed by the U.S. government.

Developed-Market Ex-US Fixed Income (Unhedged):
JPMorgan GBI Global ex-U.S. Index (Unhedged) is an unmanaged market index that is representative of the total-return performance in U.S. dollars on an unhedged basis of major non-U.S. bond markets.

Emerging-Market Fixed Income (U.S. Dollar):
JP Morgan Emerging Markets Bond Index (EMBI Global) currently covers 27 emerging market countries. Included in the EMBI Global are U.S.-dollar-denominated Brady bonds, Eurobonds, traded loans, and local-market debt instruments issued by sovereign and quasi-sovereign entities.

Government Securities:
Bloomberg Barclays U.S. Government Bond Index is comprised of the U.S. Treasury and U.S. Agency Indices. The index includes U.S. dollar-denominated, fixed-rate, nominal U.S. Treasury securities and U.S. agency debentures (securities issued by U.S.-government-owned or government-sponsored entities, and debt explicitly guaranteed by the U.S. government). The U.S. Government Index is a component of the U.S. Government/Credit and U.S. Aggregate Indices.

High Yield Taxable Fixed Income:
Bloomberg Barclays U.S. Corporate High-Yield Index covers the universe of fixed rate, non-investment-grade debt.

Intermediate Term Taxable Fixed Income:
Bloomberg Barclays U.S. Aggregate 5-7 Year Bond Index is unmanaged and is composed of the Bloomberg Barclays U.S. Government/Credit Index and the Bloomberg Barclays U.S. Mortgage- Backed Securities Index, and includes Treasury issues, agency issues, corporate bond issues, and mortgage-backed securities with maturities of 5-7 years.

Investment-Grade Corporate Bonds:
Bloomberg Barclays U.S. Corporate Index includes publicly-issued U.S. corporate and Yankee debentures and secured notes that meet specified maturity, liquidity, and quality requirements.

Investment Grade Credit:
Bloomberg Barclays U.S. Credit Index measures the investment grade, U.S.-dollar-denominated, fixed-rate, taxable corporate and government-related bond markets. It is comprised of the U.S. Corporate Index and a non-corporate component that includes foreign agencies, sovereigns, supra-nationals and local authorities.

Long Term Taxable Fixed Income:
Bloomberg Barclays U.S. Aggregate 10+ Year Bond Index is unmanaged and is composed of the Bloomberg Barclays U.S. Government/Credit Index and the Bloomberg Barclays U.S. Mortgage-Backed Securities Index, and includes Treasury issues, agency issues, corporate bond issues, and mortgage-backed securities with maturities of 10 years or more.

Mortgage-Backed Securities:
Bloomberg Barclays U.S. Mortgage Backed Securities (MBS) Index includes mortgage-backed pass-through securities of Ginnie Mae (GNMA), Fannie Mae (FNMA), and Freddie Mac (FHLMC). The MBS Index is formed by grouping the universe of more than 600,000 individual fixed rate MBS pools into approximately 3,500 generic aggregates.

Municipal Bonds:
Bloomberg Barclays U.S. Municipal Index represents municipal bonds with a minimum credit rating of at least Baa, an outstanding par value of at least $3 million and a remaining maturity of at least one year. The index excludes taxable municipal bonds, bonds with floating rates, derivatives and certificates of participation.

Preferred Stock:
S&P U.S. Preferred Stock Index is an unmanaged index consisting of U.S.-listed preferred stocks.

Securitized:
Bloomberg Barclays U.S. Mortgage-Backed Securities (MBS) Index tracks agency mortgage backed pass-through securities (both fixed-rate and hybrid ARM) guaranteed by Ginnie Mae (GNMA), Fannie Mae (FNMA), and Freddie Mac (FHLMC). The index is constructed by grouping individual TBA-deliverable MBS pools into aggregates or generics based on program, coupon and vintage.

Short Term Taxable Fixed Income:
Bloomberg Barclays U.S. Aggregate 1-3 Year Bond Index is unmanaged and is composed of the Bloomberg Barclays U.S. Government/Credit Index and the Bloomberg Barclays U.S. Mortgage-Backed Securities Index, and includes Treasury issues, agency issues, corporate bond issues, and mortgage-backed securities with maturities of 1-3 years.

Treasury Inflation-Protected Securities (TIPS):
Bloomberg Barclays U.S. TIPS Index consists of Inflation-Protection securities issued by the U.S. Treasury.

Treasury Securities:
Bloomberg Barclays U.S. Treasury Index includes public obligations of the U.S. Treasury with a remaining maturity of one year or more.

U.S. Taxable Investment Grade Fixed Income:
Bloomberg Barclays U.S. Aggregate Bond Index is an index composed of the Government Bond Index, the Asset-Backed Securities Index and the Mortgage-Backed Securities Index and includes U.S. Treasury issues, agency issues, corporate bond issues and mortgage-backed issues.

General Disclosures

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