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OCTOBER 2015 **TIMELY THINKING**

Is the sky really falling?

Eaton Vance Richard Bernstein (A) **EARAX**
All Asset Strategy Fund (I) **EIRAX**

Eaton Vance Richard Bernstein (A) **ERBAX**
Equity Strategy Fund (I) **ERBIX**

Eaton Vance Richard Bernstein (A) **ERMAX**
Market Opportunities Fund (I) **ERMIX**

In perhaps a massive understatement, volatility in the global financial markets picked up during the third quarter. Equity, fixed-income and commodity markets all around the world were disrupted to varying degrees. Of course, the renewed volatility unsettled investors, and bears roared loudly, while bulls pulled in their horns. To paraphrase Clement Clarke Moore, visions of 2008 danced in their heads.

The key question for investors is whether the secular bull market remains intact or whether a bear market and recession are looming. We think the secular bull market remains intact. Fear continues to overwhelm greed in most segments of the financial markets.



At Eaton Vance, we value independent thinking. In our experience, clients benefit from a range of distinctive, strongly argued perspectives. That's why we encourage our independent investment teams and strategists to share their views on pressing issues—even when they run counter to conventional wisdom or the opinions of other investment managers. **Timely Thinking. Timeless Values.**

Waiting for an entry point?

For the past year or more, many investors suggested that fundamentals were improving, but that the equity market was overvalued at current levels and investors should use pullbacks in the market as entry points to invest. Investors have gotten their pullback, but it doesn't look as though they are using the opportunity to buy equities. Rather, it appears that investors were too scared to invest as the stock market rose and are too scared to invest as the stock market corrects. One might say that one is waiting for the market to bottom; however, history suggests that the stock market bottoms at the point of maximum fear and not at a perceived point of maximum opportunity.

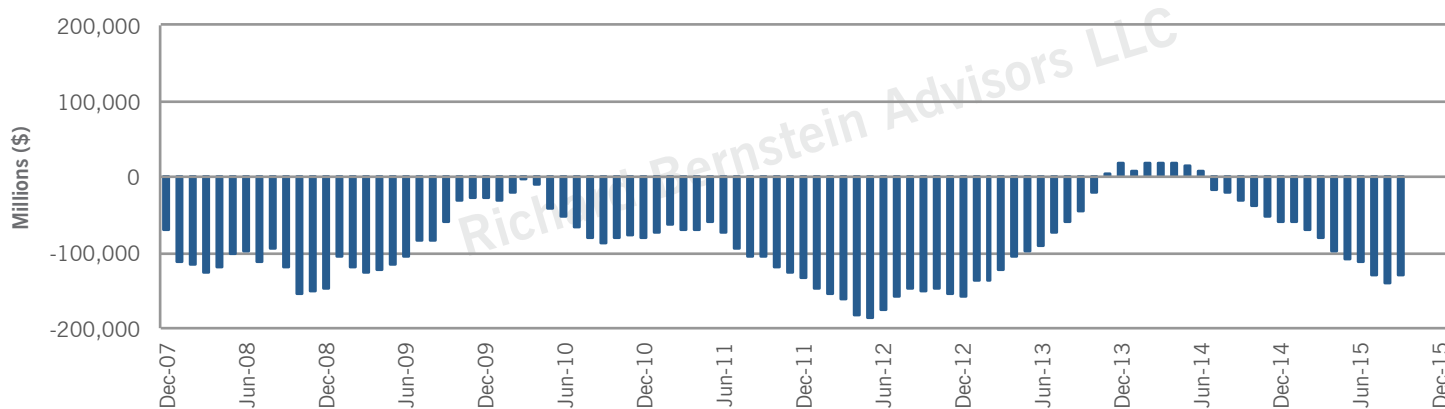
Whether one looks at ETF flows, mutual fund flows, Wall Street strategist-recommended asset allocations, institutional portfolio allocations or hedge fund positioning, the simple fact remains that investors are generally scared of equities (Exhibit A).

Why volatility now?

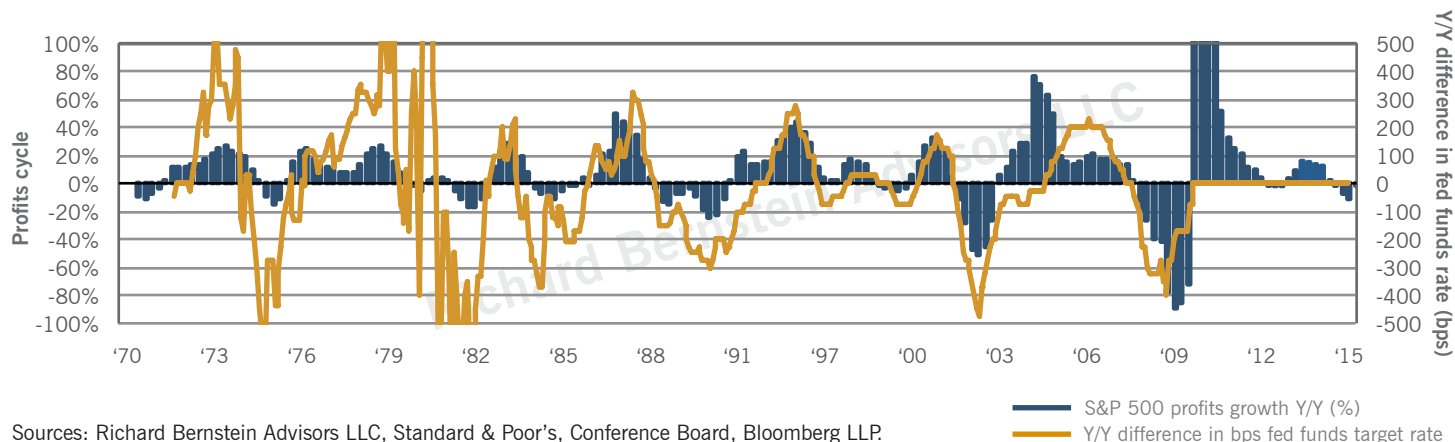
We pointed out last month that perhaps the main reason for the markets' volatility is the odd combination of the Fed hiking interest rates when the profits cycle was decelerating. Exhibit B shows the historical positive correlation between changes in the fed funds rate and the profits cycle. Historically, profits were revving up when the Fed would start increasing rates, and the positive of accelerating earnings would overwhelm the incremental negative of the Fed raising interest rates. However, this cycle appears uniquely different in that the Fed is "threatening" to raise interest rates when the U.S. is in a profits recession. Rather than a traditional offsetting relationship at this early point of the tightening cycle, the near-term interest-rate outlook and the near-term profits outlook are both negative.

Exhibit A Domestic equity rolling 12-month net mutual fund flows.

December 2007 - September 2015



Sources: Richard Bernstein Advisors, ICI.

Exhibit B Year-on-year difference in the fed funds rate and the S&P 500 profits cycle.**Is the secular bull market intact?**

Our proprietary research suggests that the profits cycle is likely to trough either in the third or fourth quarter depending on the level of write-offs toward year-end (Exhibit C). That would imply that the relationship between fed funds and the profits cycle might return to a more normal one and, if that is the case, we think the equity market can continue advancing as it would during a mid/late-cycle environment.

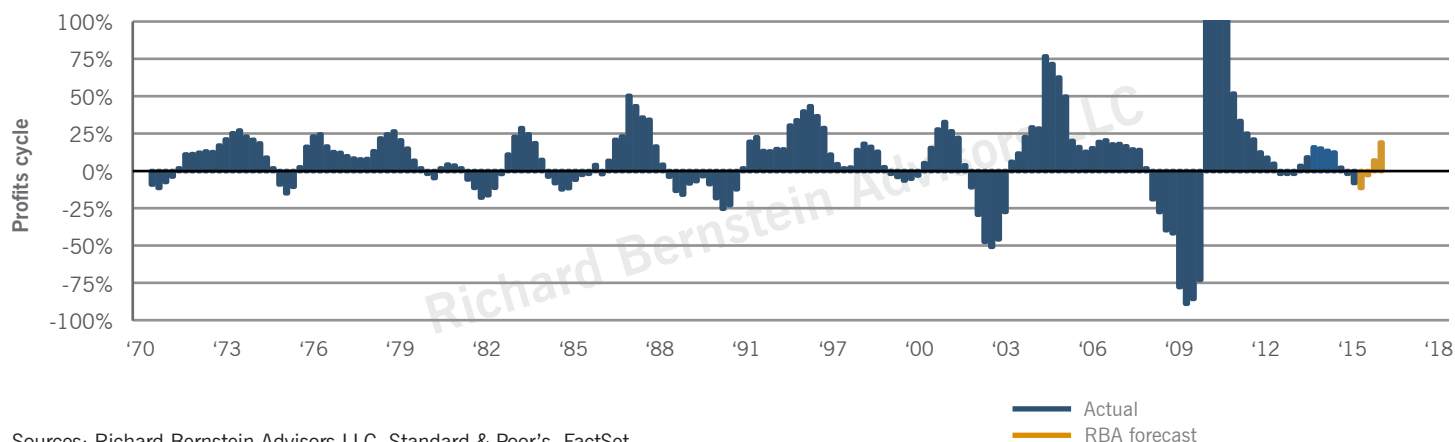
Is the sky really falling?

Volatility is always unsettling for investors. However, one has to assess whether the volatility is forecasting an end to the profits, economic and market cycles or whether the volatility is a correction within the context of a longer bull market.

Our corporate motto is “Uncertainty = Opportunity®” and our portfolios are positioned accordingly.

Exhibit C The S&P 500 profits cycle.

Year-on-year percent change in trailing reported EPS



Index Definitions

The following descriptions, while believed to be accurate, are in some cases abbreviated versions of more detailed or comprehensive definitions available from the sponsors or originators of the respective indexes. Anyone interested in such further details is free to consult each such sponsor's or originator's website.

The past performance of an index is not a guarantee of future results.

Each index reflects an unmanaged universe of securities without any deduction for advisory fees or other expenses that would reduce actual returns, as well as the reinvestment of all income and dividends. An actual investment in the securities included in the index would require an investor to incur transaction costs, which would lower the performance results. **Indexes are not actively managed and investors cannot invest directly in the indexes.**

S&P 500: Standard & Poor's (S&P) 500 Index. The S&P 500 Index is an unmanaged, capitalization-weighted index designed to measure the performance of the broad U.S. economy through changes in the aggregate market value of 500 stocks representing all major industries.

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Richard Bernstein Advisors LLC serves as subadvisor to three Eaton Vance mutual funds.

Richard Bernstein is chief executive officer of Richard Bernstein Advisors LLC, a registered investment advisor.

For more information on Richard Bernstein Funds, visit eatonvance.com/Bernstein.

About Risk

Equity investing is subject to stock market volatility. Smaller companies are generally subject to greater price fluctuations, limited liquidity, higher transaction costs and higher investment risk than larger, established companies. Investments in foreign instruments or currencies can involve greater risk and volatility than U.S. investments because of adverse market, economic, political, regulatory, geopolitical or other conditions. In emerging or frontier countries, these risks may be more significant. Smaller companies are generally subject to greater price fluctuations, limited liquidity, higher transaction costs and higher investment risk than larger, established companies. Investing involves risks including possible loss of principal.

Investing is an inherently risky activity, and investors must always be prepared to potentially lose some or all of an investment's value. Past performance is, of course, no guarantee of future results.

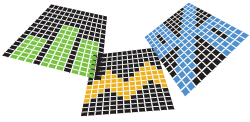
The value of commodities investments will generally be affected by overall market movements and factors specific to a particular industry or commodity, including weather, embargoes, tariffs, or health, political, international and regulatory developments. Derivative instruments can be used to take both long and short positions, be highly volatile, result in economic leverage (which can magnify losses), and involve risks in addition to the risks of the underlying instrument on which the derivative is based, such as counterparty, correlation and liquidity risk. If a counterparty is unable to honor its commitments, the value of investments may decline and/or the investments could experience delays in the return of collateral or other assets held by the counterparty. An imbalance in supply and demand in the income market may result in valuation uncertainties and greater volatility, less liquidity, widening credit spreads and a lack of price transparency in the market. As interest rates rise, the value of certain income investments is likely to decline. Securities with longer durations tend to be more sensitive to interest rate changes than securities with shorter durations. A portfolio with negative duration generally incurs a loss when interest rates and yields fall.

Unless otherwise stated, index returns do not reflect the effect of any applicable sales charges, commissions, expenses, taxes or leverage, as applicable. It is not possible to invest directly in an index. Historical performance of the index illustrates market trends and does not represent the past or future performance of any fund.

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