Seeking to Generate Income in a Low-Yield Environment

On the Holmes and Rahe Stress Scale used by psychologists to determine stress levels, retirement is rated as the 10th most stressful event, even though retirement ideally represents the reward for a lifetime of labor. Undoubtedly, no small part of that stress is linked to the pressing need for retirees to replace the income they once earned during their working years with investment-related income they require during retirement.

Given most families — even those approaching retirement — have little or no retirement savings, it is easy to understand why many Americans have legitimate worries that they will outlive their retirement savings. The current economic environment and uncertain financial market returns are not doing anything to help alleviate those worries.

Risks

Yields
Unconventional monetary policy over the past eight years has driven fixed income yields to historically low levels. This has created a large challenge for investors who rely on this asset class for income.

Returns
Traditional fixed income investments may now carry more risk and less reward. Investors searching for higher yields or income may be tempted to take on more risk than they are accustomed to.

Purchasing Power
Inflation impacts all investors and investments, although it can have a greater effect on fixed income investors who might have less flexibility in their investment approach or objectives.

Opportunities

Active Management
Consider both equity and fixed income strategies that balance the growth of both principal and income while preserving capital, and do not solely focus on the highest-yielding, higher-risk assets.

Diversification
By identifying which risks can cause the most damage to a portfolio, investors can look to develop the proper investment allocation to specifically target these risks and help mitigate the risk of drawdowns, i.e., sharp market reversals.

Think Outside the Style Box
In the current environment, Municipal bonds can potentially offer higher returns with lower risk relative to other fixed income assets, such as U.S. investment grade corporate bonds and U.S. Treasuries.
# Investment Considerations

## Active Management
Despite the challenging environment, investment opportunities still exist in financial markets. Active managers who specialize in fundamental research and have the ability to invest across sectors, regions and asset classes to identify growth and income, can potentially find the highest-quality opportunities while side-stepping lower-quality, higher-risk investments.

## Diversification
Consider both equity and fixed income strategies that balance the growth of both principal and income while preserving capital, and do not solely focus on the highest-yielding, higher-risk assets.

Alternative, multi-asset strategies that focus on asset allocation flexibility and capital preservation can help protect portfolios against extended volatility associated with a shift in central bank monetary policy.

Of course, asset allocation and diversification cannot assure a profit or protect against loss.

## Think Outside the Style Box
By identifying which risks can cause the most damage to a portfolio, investors can develop the proper investment allocation to specifically target these risks and help protect against drawdowns; i.e., sharp market reversals.

In the current environment, Municipal bonds can potentially offer higher returns with lower risk relative to other fixed income assets, such as U.S. investment grade corporate bonds and U.S. Treasuries.

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# Helping Meet Investor Challenges
Dreyfus is committed to help investors navigate complex global financial markets by aligning challenges presented by a changing investment environment with opportunities identified through a better understanding of risk. With a confluence of opposing forces at play, we help to identify opportunities which can improve investment outcomes in different market cycles.
1 | Yields

Traditional Fixed Income Investments Have Become a Less Reliable Source of Income

CHART 1

- Unconventional monetary policy from central banks globally over the past eight years has driven fixed income yields to historically low levels, and even into negative territory in many regions.
- For investors holding large allocations to fixed income investments, such as retirees, falling yields can have a significant impact on their current income and spending power just when they need it most.

Sources: BNY Mellon using Bloomberg Barclays Global Aggregate Index data, as of October 19, 2016. Past performance is no guarantee of future results.

CHART 2

- Beyond government bonds, the universe of negative-yielding assets — primarily government bonds in Europe and Japan but also a mounting number of higher-rated corporate bonds — continues to grow.
- As of September 30, 2016, over 90% of the bonds in the Bloomberg Barclays Global Aggregate Index yield 3% or less with a quarter of the index offering a negative yield.

2 | Returns
Tread Lightly When Considering Risk and Chasing Yield

CHART 3
• In addition to delivering lower yields, most traditional fixed income investments are now also carrying a higher degree of risk. Global bonds now carry on average a higher level of duration risk, a measure of bond prices’ sensitivity to a change in interest rates, relative to their yield, suggesting that the risk/return profile has turned more unfavorable.
• While interest rate risk seems far off given the current economic environment, it remains a risk that needs to be accounted for in portfolios. Investors need to be very selective when investing in this segment of the market to ensure they are being properly compensated for the risk they are taking.

CHART 4
• Investors need to be mindful that adding to higher-risk investments usually brings with it higher volatility and higher probabilities of larger drawdowns — something fixed income investors may not be able to tolerate.
• Portfolios that balance the need for income with both capital preservation and risk-adjusted returns should offer investors the potential to enhance income opportunities. In the current environment, investors may want to consider fixed income investments such as U.S. Municipal Bond strategies that have exhibited higher returns with less risk than some other fixed income asset classes in the past three years.

Sources: BNY Mellon using Bloomberg Barclays Global Aggregate Index as of October 1, 2016. Past performance is no guarantee of future results.
### 3 | Purchasing Power

**Additional Headwinds Facing Income Seekers**

**CHART 5**

- While inflation expectations are currently low, and typically only slightly increase the costs of goods and services from year to year, they still represent a challenge for investment planning, especially when looking out into the future.
- In certain time periods such as the 1970s and 1980s, inflation was much higher, averaging 7.25% in the 1970s and 5.82% in the 1980s.

**CHART 5**

**CURRENT INFLATION EXPECTATIONS...**
**BENIGN NOW BUT WORTH WATCHING CLOSELY**

Inflation Expectations

Sources: BNY Mellon and the Federal Reserve Bank of St. Louis; inflation expectations measured by the 5-Year, 5-Year Forward Inflation Expectation Rate, as of November 4, 2016.

**CHART 6**

- Taxes are another consideration investors need to consider when planning their current and future investment objectives.
- Looking at the current U.S. Treasury maturity structure, when inflation and taxes are taken into consideration, you would need to buy 7, 10, or 30 year bonds in order to get a positive real return given today’s inflation rate. If you factor in taxes (25% rate), only 30- year bonds would deliver a positive return.

**CHART 6**

**DON’T FORGET THE TAX MAN**

Sources: BNY Mellon and Bloomberg, as of October 20, 2016. Real Yield assumes CPI inflation rate of 1.5%, as reported on September 30, 2016, and a tax rate of 25%. **Past performance is no guarantee of future results.**
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**RISKS**

All investments involve risk, including risk of principal loss. Equities are subject to market, market sector, market liquidity, issuer, and investment style risks to varying degrees. Bonds are subject to interest rate, credit, liquidity, call and market risks, to varying degrees. Generally, all other factors being equal, bond prices are inversely related to interest-rate changes and rate increases can cause price declines. Investing in foreign denominated and/or domiciled securities involves special risks, including changes in currency exchange rates, political, economic, and social instability, limited company information, differing auditing and legal standards, and less market liquidity. These risks generally are greater with emerging market countries. Income from municipal securities may be subject to state and local taxes for out-of-state residents. Capital gains, if any, are taxable.

**INDEX DEFINITIONS**

The BAML High Yield Master Index II is a market capitalization-weighted index of all domestic and Yankee High-Yield Bonds. Issues included in the index have maturities of at least one year and have a credit rating lower than BBB-Baa3, but are not in default. Bloomberg Barclays Global Aggregate Index represents the U.S. investment grade fixed rate bond market, with index components for government and corporate securities, mortgage pass-through securities and asset-backed securities. Bloomberg Barclays U.S. Aggregate Bond Index represents the U.S. investment grade fixed rate bond market, with index components for government and corporate securities, mortgage pass-through securities and asset-backed securities. Indexes are unmanaged and one cannot invest in an index. The Bloomberg Barclays U.S. Corporate Bond Index is a rules-based market-value weighted index engineered to measure the investment grade, fixed-rate, taxable, corporate bond market. The Bloomberg Barclays U.S. Municipal Index tracks the performance of the U.S. municipal securities. The Bloomberg Barclays U.S. Treasury Index measures U.S. dollar-denominated, fixed-rate, nominal debt issued by the U.S. Treasury. S&P 500 is one of the most commonly used benchmarks for the overall U.S. stock market, and is an index that tracks the performance of the largest 500 U.S. companies. S&P 500 Dividend Aristocrats® measure the performance S&P 500 companies that have increased dividends every year for the last 25 consecutive years. The Index treats each constituent as a distinct investment opportunity without regard to its size by equally weighting each company. It is not possible to invest directly in an unmanaged index.

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