Emotions and your money

5 potentially costly mistakes and how to avoid them
Agenda

1. Understanding Emotions
2. Emotions and Investing—5 potentially costly mistakes and how to avoid them
3. Managing Emotions—the keys to staying calm in a turbulent market
Many psychologists believe that people are “hard-wired” to make irrational, emotional decisions.
It’s known as a **Psychological Bias**.

A tendency for the human brain to respond emotionally and make errors in judgment when faced with uncertainty.

One of the most common biases is **Loss Aversion**, a psychological trait that makes losses seem twice as painful as the pleasure of gains.
Let’s put this bias to the test

Which investment would you choose in each of the following scenarios?

If you had $1,000 to invest, would you select:

- **Investment A**
  Offers a sure gain of $500

- OR

- **Investment B**
  Offers a 50% chance of either gaining $1,000 or gaining nothing
If you had $2,000 to invest, would you select:

- **Investment A**
  Offers a sure *loss* of $500

- OR

- **Investment B**
  Offers a 50% chance of either *losing* $1,000 or *losing* nothing
Surprising results

If you’re like most people, you chose:

- **Investment A**
  Offers a sure gain of $500

  84% chose this answer

  OR

- **Investment B**
  Offers a 50% chance of either gaining $1,000 or gaining nothing

- **Investment A**
  Offers a sure loss of $500

  OR

- **Investment B**
  Offers a 50% chance of either losing $1,000 or losing nothing

  69% chose this answer, even though it’s the riskier choice
Surprising results

Why did most people make this choice? Because *Loss Aversion* causes you to take on more risk to avoid a sure loss!
Psychological biases combined with the emotions of investing can lead to costly mistakes

Greatest opportunity for gain
Fear and panic cause many equity investors to sell at the bottom of a bear market. However, this point in the equity market cycle actually provides investors with the highest growth potential over time.

Greatest risk of loss
The old adage says “buy low and sell high,” but many investors do just the opposite. Motivated by excitement and overconfidence, they often buy at the top of a bull market, just in time to see their investments decline.
"The more emotional the event is, the less sensible people are."

~ Dr. Daniel Kahneman
One of the fathers of behavioral finance and the 2002 Nobel Prize winner for Economics
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1. Impatience

- **Investment Trap:**
  Trading more frequently to try to quickly enhance returns

- **Unintended Consequence:**
  Potential for higher trading costs, more taxes and lower returns

- **How to Avoid the Trap:**
  Build and follow an investment plan that can help you stay invested
Many investors don’t have the patience to stay invested

How long do you think most equity fund investors have remained in their investment over the last 20 years?

Only 3.6 years!

Source: 2018 Quantitative Analysis of Investment Behavior, DALBAR.
Moving in and out of the market can lead to lower returns.

Investor behavior contributed to a performance gap of 6.0% per year over 30 years!

Source: 2018 Quantitative Analysis of Investment Behavior, DALBAR. This study utilizes data from the Investment Company Institute and Standard & Poor’s to compare investor behavior with the returns of the overall equity market. The Average Equity Fund Investor represents the aggregate action of all investors in equity mutual funds. Investor returns are determined using the change in total equity fund assets after excluding sales, redemptions and exchanges. This method of calculation captures realized and unrealized capital gains, dividends, interest, trading costs, sales charges, fees, expenses and any other costs. The S&P 500 Index is an unmanaged index of large-cap U.S. stocks that is considered to be representative of the U.S. equity market.
Following a plan can help control emotions

- Stay focused on strategy, not emotions
- Don’t get distracted by the short-term movement of the market
- Remain on track with your long-term goals
2. Overconfidence

- **Investment Trap:**
  Relying on “hot” investments to help boost your portfolio’s performance

- **Unintended Consequence:**
  Lower performance and increased risk of loss

- **How to Avoid the Trap:**
  Diversify and select investments based on research, not emotions or hot tips

Note: Diversification does not ensure a profit or protect against market loss.
Momentum can turn at any time

*Follow the crowd and you may end up buying at the top of the market, right before a significant decline!*

<table>
<thead>
<tr>
<th>Year</th>
<th>Net Investments ($ billions)</th>
<th>Equity Returns (%)</th>
</tr>
</thead>
<tbody>
<tr>
<td>2006</td>
<td>472</td>
<td>15.81%</td>
</tr>
<tr>
<td>2007</td>
<td>879</td>
<td>5.49%</td>
</tr>
<tr>
<td>2008</td>
<td>426</td>
<td>-37.00%</td>
</tr>
<tr>
<td>2009</td>
<td>-146</td>
<td>26.47%</td>
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<tr>
<td>2010</td>
<td>-281</td>
<td>15.06%</td>
</tr>
<tr>
<td>2011</td>
<td>-96</td>
<td>2.11%</td>
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<tr>
<td>2012</td>
<td>200</td>
<td>16.00%</td>
</tr>
<tr>
<td>2013</td>
<td>177</td>
<td>32.39%</td>
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<tr>
<td>2014</td>
<td>104</td>
<td>13.69%</td>
</tr>
<tr>
<td>2015</td>
<td>-100</td>
<td>1.38%</td>
</tr>
<tr>
<td>2016</td>
<td>-227</td>
<td>11.96%</td>
</tr>
<tr>
<td>2017</td>
<td>174</td>
<td>21.83%</td>
</tr>
</tbody>
</table>

For example, from 2006-2017, the best year in terms of new money invested into the financial markets was followed by the worst year in terms of investment returns!

What a difference a year makes—
Last year’s winner may be this year’s loser!

<table>
<thead>
<tr>
<th>BEST Performing Asset Class</th>
<th>WORST Performing Asset Class</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Emerging Markets Stocks, 2012</strong></td>
<td><strong>Emerging Markets Stocks, 2013</strong></td>
</tr>
<tr>
<td>+18.22%</td>
<td>-2.60%</td>
</tr>
<tr>
<td><strong>Emerging Markets Stocks, 2007</strong></td>
<td><strong>Emerging Markets Stocks, 2008</strong></td>
</tr>
<tr>
<td>+39.38%</td>
<td>-53.33%</td>
</tr>
</tbody>
</table>

Source: Callan Associates, 2018. Emerging Markets stocks are represented by the MSCI Emerging Markets Index. Asset class rankings are based on nine indices representing different asset classes from cash to emerging market stocks. Investments in non-US stocks are subject to additional risks including political and social instability, differing securities regulations and accounting standards and limited public information.
Diversification can help you generate more consistent returns in any market

Annual returns for select asset classes (1998-2017)

PAST PERFORMANCE IS NOT A GUARANTEE OF FUTURE RESULTS. The historical performance data for each index is provided to illustrate market trends. Indices are unmanaged and do not represent the performance of any specific fund or investment product. You cannot invest directly in the indices. Indices do not include expenses, fees, or sales charges that are typically associated with investments and would lower performance results. Equity investments are subject to market risk. Stocks with lower market capitalization generally involve greater risks. An investment in foreign securities may be subject to different and additional risks associated with, but not limited to: foreign currencies, securities regulation, investment disclosure, commissions, accounting, taxes, political or social instability, war, or expropriation. Bonds and bond funds are subject to interest rate risks. If held to maturity, bonds can provide a fixed rate of return and a fixed principal value, while bond funds will fluctuate in value and may be worth more or less than your original investment when redeemed. High yield bonds are subject to greater price swings than higher-rated bonds and payment of interest and principal is not assured. Source: Wilshire Compass, 2018.
3. Fear

- **Investment Trap:**
  Waiting too long to get back into the equity market

- **Unintended Consequence:**
  Inability to capitalize fully on a potential market rebound

- **How to Avoid the Trap:**
  Consider easing back into equities with an automatic investing strategy like dollar cost averaging (DCA)
Fear may result in lost income

Bull markets have historically been front-loaded. Miss the first year of a rebound and you could lose out on NEARLY HALF of the average bull market’s total gains!

Returns of the Dow Jones Industrial Average for every bull market since 1900

- Median first-year return: +41.8%
- Median total return: +85.7%

Note: Past performance is not a guarantee of future results. The Dow Jones Industrial Average is an index that consists of 30 of the largest and most widely held public companies in the U.S. Indices are unmanaged and cannot be invested in directly. Data sources: The Leuthold Group, from the following articles:
  - Thomas Franck, “On the Bull Market’s Ninth Birthday, Here’s How It Stacks Up Against History,” CNBC, March 8, 2018
Take the guesswork out of timing the market

*Dollar cost averaging (DCA) allows you to increase your exposure to the growth potential of equities, while potentially reducing the average cost of your investment.*

### LUMP SUM
$40 invested in one single purchase

<table>
<thead>
<tr>
<th>Investment Frequency</th>
<th>Amount Invested</th>
<th>Price Per Unit</th>
<th>Units Bought</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>$40</td>
<td>$10</td>
<td>4</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>$40</strong></td>
<td><strong>$10</strong></td>
<td><strong>4</strong></td>
</tr>
</tbody>
</table>

### DOLLAR COST AVERAGING
$10 invested on four separate occasions

<table>
<thead>
<tr>
<th>Investment Frequency</th>
<th>Amount Invested</th>
<th>Price Per Unit</th>
<th>Units Bought</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>$10</td>
<td>$10</td>
<td>1.00</td>
</tr>
<tr>
<td>2</td>
<td>$10</td>
<td>$12</td>
<td>0.83</td>
</tr>
<tr>
<td>3</td>
<td>$10</td>
<td>$8</td>
<td>1.25</td>
</tr>
<tr>
<td>4</td>
<td>$10</td>
<td>$5</td>
<td>2.00</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>$40</strong></td>
<td><strong>$7.87</strong></td>
<td><strong>5.08</strong></td>
</tr>
</tbody>
</table>

In this example, more units at lower cost equals greater potential for future growth!

NOTE: Dollar cost averaging does not guarantee a profit or protect against a loss in declining markets. Dollar cost averaging involves continuous investment in securities regardless of fluctuating price levels. Before starting such a program, you should consider your ability to make purchases through periods of fluctuating price levels. This hypothetical illustration is for illustrative purposes only. It is only intended to show how dollar cost averaging works, not to reflect the performance of an actual investment.
4. Panic

• **Investment Trap:**
  Selling equities in down markets and moving to cash for short-term safety

• **Unintended Consequence:**
  Potential shortfall in retirement income

• **How to Avoid the Trap:**
  Stay calm and use history as a guide to maintaining your long-term focus
The cost of selling stocks can be high

*Stocks have historically outperformed bonds and cash over time.*
*In fact, stocks generated at least $1.5 million more over the last 30 years!*

Hypothetical growth of $100,000 over 30 years, 12/31/87 – 12/31/17

- **Stocks**
  - $2,109,747
- **Bonds**
  - $636,511
- **Cash**
  - $266,052

*Note: Past performance is not a guarantee of future results.* Stocks are represented by the S&P 500 Index; bonds by the Barclays U.S. Aggregate Bond Index; and cash by the BofA Merrill Lynch US Treasury Bill 3-Month Index. Stocks are subject to significant price fluctuations and therefore an investor may have a gain or loss in principal when shares are sold. Government Bonds and Treasury Bills are subject to interest rate risk but are backed by the full faith and credit of the U.S. government if held to maturity. This example does not take into account taxes, fees or expenses; if shown, the results would be lower. Indices are unmanaged and cannot be invested in directly. Source: Wilshire Compass, 2018.
It can pay to stay invested in the market

The price of missing the best days of the equity market from 12/31/97 – 12/31/17

- If you were fully invested for the entire period: 7.2%
- If you missed the market’s 10 best days: 3.5%
- If you missed the market’s 20 best days: 1.15%
- If you missed the market’s 30 best days: -0.92%
- If you missed the market’s 40 best days: -2.8%

Source: Bloomberg and Wellington Management Company, 2018. This chart is for illustrative purposes only. It is based on the S&P 500 Index and is not intended to be indicative of the performance of any specific investment. Indices are unmanaged. An investment cannot be made directly in an index. Past performance is not a guarantee of future results.
History has been on your side

Since 1926, stocks have consistently provided long-term growth through wars, recessions, financial crises, natural disasters and more

Source: Wilshire Compass, 2018. Large company stocks are represented by the S&P 500 Index, an unmanaged index of large-cap stocks in the U.S. stock market. Stocks are often subject to significant price fluctuations and therefore an investor may have a gain or loss in principal when shares are sold. Higher volatility and greater risk may be associated with investing in stocks of small or emerging companies. This chart is for illustrative purposes only and is not representative of any specific investment. Performance for any specific investment is available from your investment representative. Past performance is not a guarantee of future results. Indices are unmanaged; you cannot invest directly in these indices.
5. Indecision

- **Investor Behavior:**
  Staying in cash to help protect your assets from market volatility

- **Unintended Consequence:**
  Loss of purchasing power over time

- **How to Avoid the Trap:**
  Review your asset allocation mix
Don’t let indecision reduce your returns

Cash alone is unlikely to generate the returns necessary to achieve your retirement goals

Real rate of return, 12/31/1925 – 12/31/2017

<table>
<thead>
<tr>
<th>Category</th>
<th>Before Taxes and Inflation</th>
<th>After Taxes and Inflation</th>
</tr>
</thead>
<tbody>
<tr>
<td>Stocks</td>
<td>10.2%</td>
<td>5.1%</td>
</tr>
<tr>
<td>Bonds</td>
<td>5.5%</td>
<td>0.6%</td>
</tr>
<tr>
<td>Cash</td>
<td>3.4%</td>
<td>-0.8%</td>
</tr>
</tbody>
</table>

Source: Morningstar, 2018. Stocks are represented by the S&P 500 Index; bonds by 20-Year U.S. Government Bonds; cash by 30-day U.S. Treasury Bills; and inflation by the Consumer Price Index. Stocks are often subject to significant price fluctuations and therefore an investor may have a gain or loss in principal when shares are sold. Government bonds and Treasury Bills are subject to interest rate risk but are backed by the full faith and credit of the U.S. government if held to maturity. The data assumes reinvestment of income and does not account for transaction costs. Federal income tax is calculated using the historical marginal and capital gains tax rates for a single taxpayer earning $120,000 in 2015 dollars every year. No state income taxes are included. Indices are unmanaged and cannot be invested in directly. Past performance is not a guarantee of future results.
Consider using the “3 Buckets” model to help determine the right asset allocation for you

- **Short Term Investment Bucket**
  - **Investment time horizon:** Less than 1 year
  - **Includes assets like CDs**
  - **Average annual return on investment:** 3.4%

- **Intermediate Term Investment Bucket**
  - **Investment time horizon:** 2-5 years
  - **Includes assets like bonds**
  - **Average annual return on investment:** 5.5%

- **Long Term Investment Bucket**
  - **Investment time horizon:** 6+ years
  - **Includes assets like stocks**
  - **Average annual return on investment:** 10.2%

NOTE: Performance is based on annualized of various investments from 12/31/1925-12/31/2017. Short term investments are represented by 30-day U.S. Treasury Bills; intermediate term investments by 20-Year U.S. Government Bonds; and long-term investments by the S&P 500 Index. Stocks are often subject to significant price fluctuations and therefore an investor may have a gain or loss in principal when shares are sold. Government bonds and Treasury Bills are subject to interest rate risk but are backed by the full faith and credit of the U.S. government if held to maturity. Individuals may not invest directly in an index. Past performance is not a guarantee of future results. Source: Morningstar, 2018.
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The keys to staying calm in a turbulent market

- **Knowledge**: Understand how your investments will react to different market conditions.

- **Strategy**: Build a broadly diversified portfolio that may help you generate more consistent returns. Develop an income plan that you won’t outlive.

- **Perspective**: Work with a trusted financial professional who has the expertise, experience and third-party objectivity to guide you through difficult times.
Understanding your investments

Focus on three areas:

- Volatility and income
- Key benefits
- Potential pitfalls

Remember, the more volatile your investment, the greater the range of emotions you may feel and the more likely it may be that you’ll make costly emotional mistakes.
Volatility and Income

Monthly returns of the S&P 500 Index
(12/31/2007-12/31/2017)

Key Benefits
- Growth potential
- Diversification opportunities
- Possibility of dividend income

Potential Pitfalls
- No protection against market uncertainty
- No income guarantees

*When you invest in equities, your emotions and income may go up or down with the market.*
Bonds

Volatility and Income

Key Benefits
- Fixed rate
- Government bonds backed by the U.S. government
- Certain types of bonds offer tax advantages

Potential Pitfalls
- No potential for market growth
- No lifetime income options

Bonds tend to be less volatile than stocks, so your emotions and income may not fluctuate as much.
Cash

**Volatility and Income**

Monthly returns of 91-day Treasury Bills (12/31/2007-12/31/2017)

-20 -15 -10 -5 0 5 10 15 20


*Treasury Bills and other cash investments can help you stay calm, but they offer little income and no potential for market growth.*

**Key Benefits**

- Fixed rate
- Returns guaranteed by the FDIC (CDs) or the U.S. government (T-bills)
- Good for short-term investing

**Potential Pitfalls**

- No potential for market growth
- No lifetime income options
Key Benefits

- Growth potential
- Diversification
- Tax deferral
- Lifetime income options
- Income guarantees
- Death benefit

Potential Pitfalls

- Higher cost
- Optional income benefit subject to additional fees, restrictions and limitations

Annuities will fluctuate with the market, but they can guarantee income growth for a certain number of years, even if your contract value drops to zero!

Note: This illustration is not to scale and is intended to show how a variable annuity with an optional income protection feature can work. It illustrates the potential for an increased income payment in the first 12 contract years, regardless of how the market performs.
Build a broadly diversified portfolio
and comprehensive financial plan that address critical needs and
goals, while helping to reduce emotional risk

In addition to stocks, bonds, cash and annuities, consider:
• **Mutual funds** for diversification, professional money management and growth potential
• **IRAs, 401(k)s and other retirement plans** to help you accumulate assets and generate retirement income
• **Life insurance** to provide for your loved ones
• **Long term care** to help meet rising nursing home costs

Note: Mutual funds are subject to investment risk, including the possible loss of principal. Please read the prospectus for risks, fees, and additional information before investing.
Create a withdrawal strategy that can help ensure your income lasts for life

### 30-year Retirement

<table>
<thead>
<tr>
<th>Initial Withdrawal Amount</th>
<th>Stock/Bond* Mix</th>
<th>20/80</th>
<th>40/60</th>
<th>60/40</th>
<th>80/20</th>
<th>100/0</th>
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</thead>
<tbody>
<tr>
<td>3%</td>
<td></td>
<td></td>
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<tr>
<td>98%</td>
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<td>96%</td>
<td>93%</td>
<td>90%</td>
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<tr>
<td>4%</td>
<td></td>
<td></td>
<td></td>
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<td></td>
</tr>
<tr>
<td>74%</td>
<td>80%</td>
<td>80%</td>
<td>79%</td>
<td>77%</td>
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<tr>
<td>5%</td>
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<tr>
<td>28%</td>
<td>46%</td>
<td>56%</td>
<td>60%</td>
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<tr>
<td>5%</td>
<td>19%</td>
<td>32%</td>
<td>40%</td>
<td>44%</td>
<td></td>
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</tr>
</tbody>
</table>

*A 4% initial withdrawal amount may no longer be safe*

Assuming 4% annual withdrawals from a portfolio of 60% stocks and 40% bonds, there’s a 20% chance that your income will fail to last a 30-year retirement.

*The following allocations include short-term bonds: 60/40 is 60% stocks, 30% bonds, and 10% short-term bonds; 40/60 is 40% stocks, 40% bonds, and 20% short-term bonds; and 20/80 is 20% stocks, 50% bonds, and 30% short-term bonds.

Source: T. Rowe Price, 2017, based on Monte Carlo Analysis and a 30-year retirement. The initial withdrawal amount is increased 3% annually for inflation. Monte Carlo Analysis is hypothetical in nature, does not reflect actual investment results, and is not a guarantee of future results. It is based on a number of assumptions. There can be no assurance that the results shown will be achieved or sustained. Results may vary, and such results may be better or worse than the simulated scenario. Underlying long-term expected annual returns for the asset classes are not based on historical returns. Rather, they represent assumptions that take into account, among other things, historical returns. They also include T. Rowe Price estimates for reinvested dividends and capital gains. These assumptions, as well as an assumed degree of fluctuation of returns around these long-term rates, are used to generate random monthly returns for each asset class over specified time periods. The monthly returns are then used to generate thousands of scenarios, representing a spectrum of possible return outcomes for the modeled asset classes. Success rates are based on these scenarios.
Consider a variable or index annuity with a living benefit rider for more guaranteed income for life

By allocating a portion of your retirement assets to an annuity with a living benefit rider, you can guarantee lifetime withdrawals of 2-7% per year depending on the product and rider you select.* Fees, restrictions and other limitations apply.

*Withdrawal amounts are calculated as a stated percentage (generally 2% to 7%, though rates above 5% are typically available only if withdrawals begin at age 70 or later) of a shadow account, known variously as the benefit base, income base or income account. Source: 2018 IRI Fact Book, Insured Retirement Institute.
Gain a new perspective on retirement income planning

Checklist for finding the right financial professional

- Knowledge
- Experience
- Responsiveness
- Availability
- Trust
A good financial professional can help you navigate the ups and downs of investing.
Let’s work together to create a customized accumulation and income strategy that can help smooth out your emotions in today’s uncertain market!
Variable annuities and mutual funds are sold by prospectus only. Please read the prospectus carefully before investing. The prospectus contains the investment objectives, risks, fees, charges, expenses and other information regarding the fund or the contract and underlying funds, which should be considered carefully before investing.

Annuities are issued by American General Life Insurance Company (AGL), Houston, TX, except in New York, where they are issued by The United States Life Insurance Company in the City of New York (US Life). Variable annuities are distributed by AIG Capital Services, Inc. (ACS), Member FINRA, 21650 Oxnard Street, Suite 750, Woodland Hills, CA 91367-4997, 1-800-445-7862. AIG Funds are advised by SunAmerica Asset Management, LLC (SAAMCo) and distributed by AIG Capital Services, Inc., Member FINRA., Haborside 5, 185 Hudson Street, Suite 3300, Jersey City, NJ 07311, 800-858-8850. AGL, US Life, SAAMCo and ACS are members of American International Group, Inc. (AIG).

Annuities are long-term products designed for retirement. Early withdrawals may be subject to withdrawal charges. Withdrawals of taxable amounts are subject to ordinary income tax and, if taken prior to age 59½, an additional 10% federal tax may apply. Tax-qualified plans, such as IRAs and 401(k)s are tax-deferred (and subject to required minimum distributions) regardless of whether or not they are funded with an annuity. Products and features may vary by state and may not be available in all states.

Index annuities are not a direct investment in the stock market. They are long-term insurance products with guarantees backed by the claims-paying ability of the issuing insurance company. They provide the potential for interest to be credited based in part on the performance of the specified index, without the risk of loss of premium due to market downturns or fluctuations. Index annuities may not be suitable or appropriate for all individuals.

An investment in a variable annuity involves investment risk, including possible loss of principal. The contract, when redeemed, may be worth more or less than the total amount invested. The purchase of a variable annuity is not required for and is not a term of the provision of any banking service or activity.

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Not FDIC or NCUA/NCUSIF Insured
May Lose Value  No Bank or Credit Union Guarantee  Not a Deposit  Not Insured by Any Federal Government Agency