



INVESTOR INSIGHTS SERIES

# SMART MONEY NEVER SLEEPS

Evolution, innovation, adaptation and  
institutional investment strategy



## EXECUTIVE SUMMARY

Driven to meet the critical objective of balancing long-term liabilities with short-term performance goals, institutional investors have been the market's innovators for decades. Now, as they look to reconcile these all-too-often competing needs in an era of high volatility, low interest rates and growing regulatory pressure, these representatives of the so-called smart money are upping their efforts to keep assets on track.

In this, the fourth global survey of institutional investors conducted by the Durable Portfolio Construction® Research Center, we find that institutions will need to leverage skills built over decades of practice in order to respond to growing market challenges:

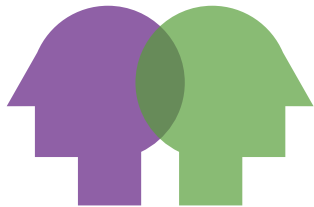
- Investment strategy is evolving, seeking to produce better risk-adjusted returns, address low yields and manage growing volatility, when 64% are reporting that alpha<sup>1</sup> is harder to come by.
- Institutions continue to invest in risk management to address highly correlated markets, with two-thirds of institutional investors planning to increase allocations to non-correlated asset classes in 2016.
- Decision makers are also focused on adapting to an increasingly complex business environment with nearly half (48%) saying the rapid pace of change can make it difficult to stay abreast of new investment strategies.

Through it all, institutions remain focused on achieving the highest risk-adjusted returns while managing their number one risk concern: volatility. There will be no rest for the weary as they pursue success.

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<sup>1</sup> Alpha is a measure of the difference between a portfolio's actual returns and its expected performance, given its level of systematic market risk.

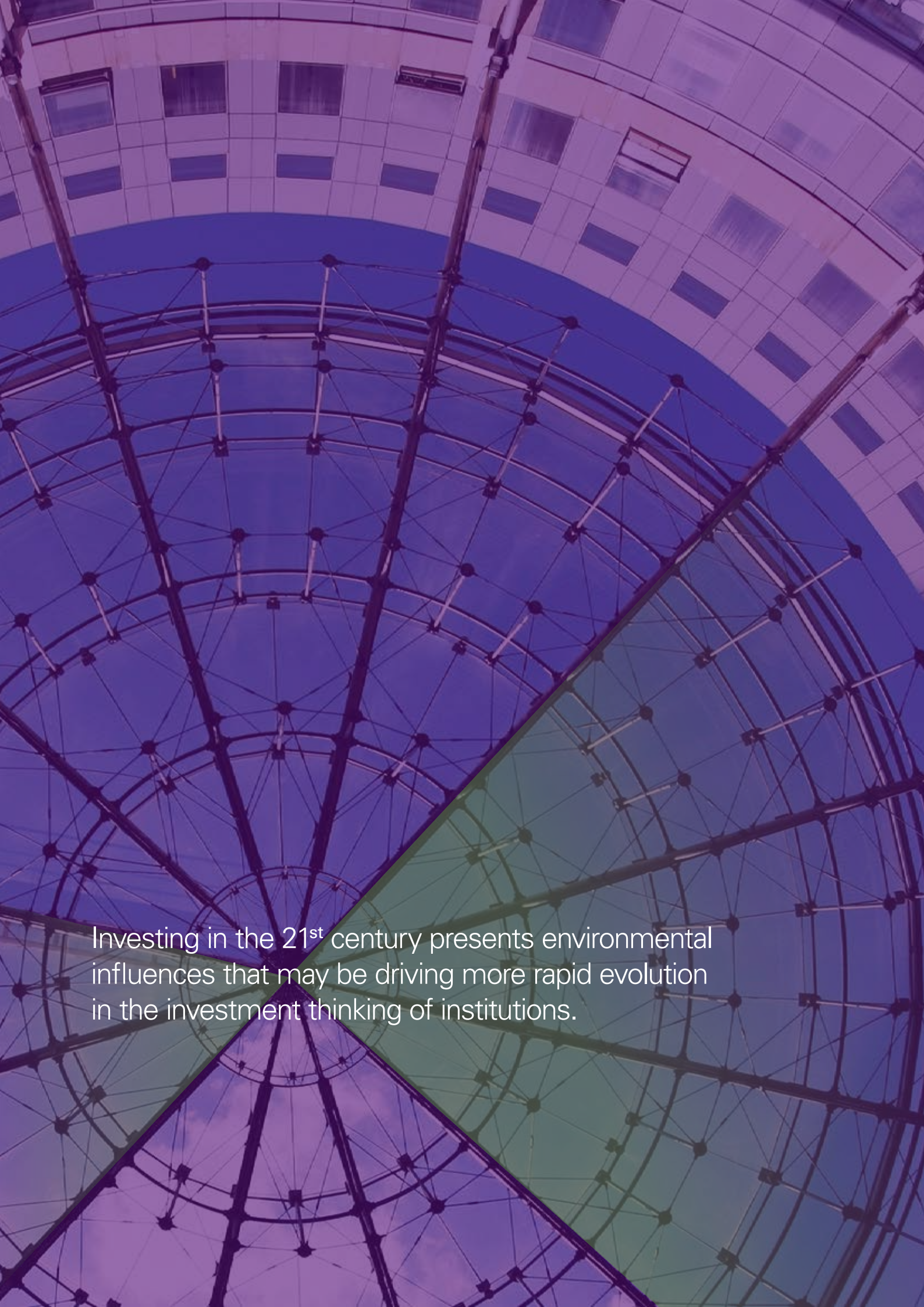




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Investing in the 21<sup>st</sup> century presents environmental influences that may be driving more rapid evolution in the investment thinking of institutions.

# Smart money never sleeps



Long considered the smart money in the market, institutional investors have set the standard for investment selection, risk management and portfolio construction over the course of decades. As those responsible for assets measuring in the billions and trillions of dollars, and liabilities that play out over 20, 30, and 40 years or more, they are ultimately long-term investors and they have made measured strategic changes designed to get them to their goals.

But investing in the 21<sup>st</sup> century presents environmental influences that may be driving more rapid evolution in the investment thinking of institutions. In this, our fourth annual global survey of institutional investors, we find that even as institutions look to meet financial obligations spanning multiple decades, many are forced to adapt quickly and efficiently to better position themselves for short-term performance.

## Long-term goals remain a constant

When asked their top investment goals in the next 12 months, the answers provided by 660 institutional decision makers would not seem out of place at any point in the past 30 years.



### PRIMARY INVESTMENT OBJECTIVES FOR INSTITUTIONS IN 2016

Achieve highest risk-adjusted annualized return	46%
Effectively manage volatility	42%
Generate stable income	36%
Grow capital	35%
Preserve capital	32%
Fund plan liabilities	25%

But environmental factors at work in modern markets significantly alter how institutions will rise to these challenges. As investment professionals, they have had to adapt in a relatively short time frame and integrate new strategies, new tools and new capabilities.

“ In the end, institutional investors are at a critical point in the evolution of investment strategy – one in which the need to meet long-term goals is often in direct competition with the need to meet short-term performance pressures.

### Modern market forces drive efficient evolution

In the eight years following the Global Financial Crisis, investment markets have been marked by four factors which influence institutional decision making: accommodative monetary policy and ultra-low interest rates, low growth rates, market volatility, and tightening regulatory standards. As a result, institutions have had to evolve quickly and take new market realities into consideration in their investment management decisions.

We see these environmental factors driving change across three dimensions of the investment process:

- **Evolution in investment strategy:** In their quest to meet long-term liabilities institutional managers have made gradual changes to investment selection in order to seek more stable returns and more consistent income.
- **Innovation in risk management:** While core investment risks such as interest rates and volatility are ever present, institutions are forced to look more closely at the root causes of risk and seek alternative strategies<sup>2</sup> to help generate better risk-adjusted returns.
- **Adaptation to a changing business environment:** Beyond market forces, institutions have a range of business considerations that influence investment decisions. Their decision to outsource management to gain expertise, decisions to manage fees with passive investments and making investments that reflect core organizational values all come into play in portfolio decisions.

In the end, institutional investors are at a critical point in the evolution of investment strategy – one in which the need to meet long-term goals is often in direct competition with the need to meet short-term performance pressures and in many cases, liquidity requirements. As they have for decades, institutional managers appear to be taking these factors in stride and making the adjustments needed to succeed.

<sup>2</sup> An alternative is an investment that is not one of the three traditional asset types (stocks, bonds and cash). Alternative investments include hedge funds, managed futures, real estate, commodities and derivatives contracts. Alternative investments involve specific risks that may be greater than those associated with traditional investments, and there is no assurance that any investment will meet its performance objectives or that losses will be avoided.



## 2015 Global Survey of Institutional Investors

### ABOUT THE SURVEY

Natixis Global Asset Management commissioned CoreData Research to conduct a global study of institutional investors, with the aim of gaining insight as to how they are managing investments and meeting various challenges in today's world.



196  
Corporate  
Pension Plans



140  
Public or Government  
Pension Plans



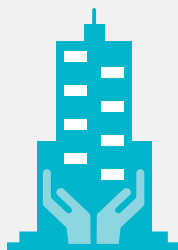
131  
Endowments/  
Foundations



100  
Insurance  
Companies



69  
Sovereign  
Wealth Funds



13  
Other Institutions\*



11  
Central Banks

660  
Total survey  
respondents

### PROJECT BACKGROUND AND METHODOLOGY

2015 marks the fourth year in which Natixis Global Asset Management has conducted its Global Institutional Investor Survey.

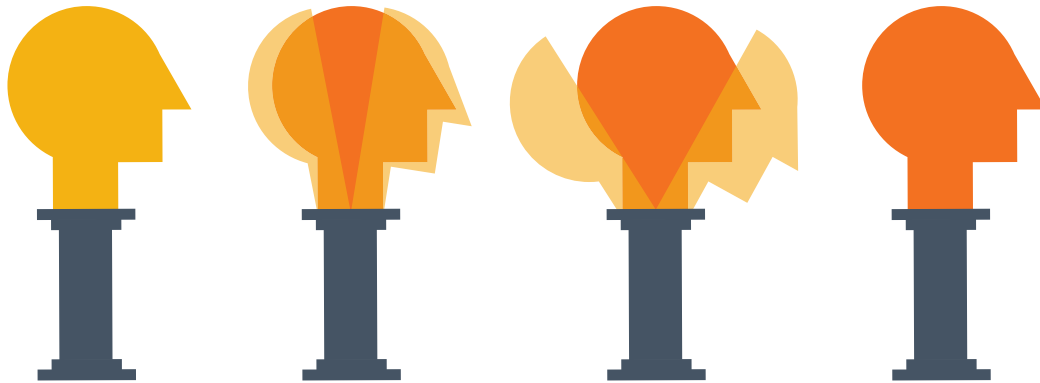
The 2015 Institutional Investor Survey was based on fieldwork conducted in 29 countries in October 2015 through an online quantitative survey of approximately 40 questions and was hosted by CoreData Research. The sample consists of 660 decision makers working in institutional investments.

\* Public Charity, Private Foundation, Social Welfare Organization, Labor Organization, Agricultural or Horticultural Organization, Business League, Trade Organization



Accommodative monetary policy has kept interest rates artificially low for seven years, making it increasingly difficult for institutional investors to pursue yield from traditional sources.

# Strategy evolving to meet modern market challenges



Call it the New Normal or the New Mediocre, post-crisis markets have underwhelmed many investors. Entering 2016, institutional decision makers say they are most worried about low yields and their ability to generate returns. The response has been a rapid evolution in strategy focused on capitalizing where markets present more attractive return opportunities.

## Yields continue to challenge institutions

Accommodative monetary policy has kept interest rates artificially low for seven years, making it increasingly difficult for institutional investors to pursue yield from traditional sources. Even though the Federal Reserve Bank was the first central bank to take action on increasing rates in December 2015, the move was limited to just 25 basis points. The Fed’s long-term policy calls for long slow escalation, prolonging the pain for investors.

In this environment it is not surprising that interest rates are the top issue for institutions, with 84% of those surveyed saying they are concerned about yields. However, our data indicates that institutions have come to grips with the idea that low rates will be with us for the foreseeable future, with the number of those who report they are “very concerned” about the issue dropping from almost two-thirds (65%) in 2013 to just over one-third (37%) in 2015.

Our respondents do not see a substantial change in the state of fixed-income markets over the short term. Bonds figure greatly among their picks for worst-performing asset classes in the next 12 months. Institutions rank emerging market fixed-income, global fixed-income and domestic fixed-income between commodities,<sup>3</sup> their number-one pick, and natural resources, their number-five pick for the laggards of 2016.



## RESPONDING TO RATE INCREASES

Institutions are ready to deploy a wide range of tools to better manage the impact of a rate increase

Shorten bond durations	65%
Reduce fixed-income exposure	49%
Increase use of alternatives	47%
Integrate absolute return strategies	32%
Diversify geographically	30%

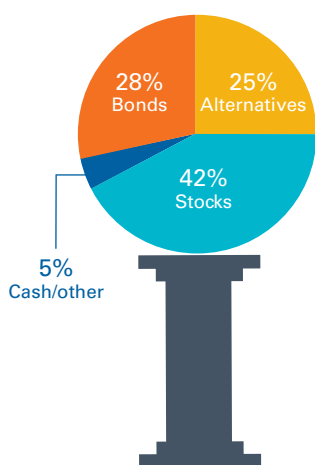
<sup>3</sup> Commodity trading involves substantial risk of loss.

In some cases we see that institutions are turning to fixed-income alternatives to help circumvent the interest rate roadblock. In our recent survey of the insurance market, where managers are particularly sensitive to income concerns, we found strong sentiment toward increasing allocations to real estate and infrastructure, both of which could potentially provide a stable source of long-term income.<sup>4</sup>

### Mediocre equity returns still better than bonds

Inconsistent market performance also weighs on the minds of institutions, with 82% of respondents saying they are concerned about return generation. Despite bright spots in select markets around the globe, real growth has been slow for a number of years, P/E ratios<sup>5</sup> have grown slowly and returns have been a case of feast or famine. But looking into 2016, institutions still place their faith in equities.

#### THE AVERAGE INSTITUTIONAL PORTFOLIO TODAY



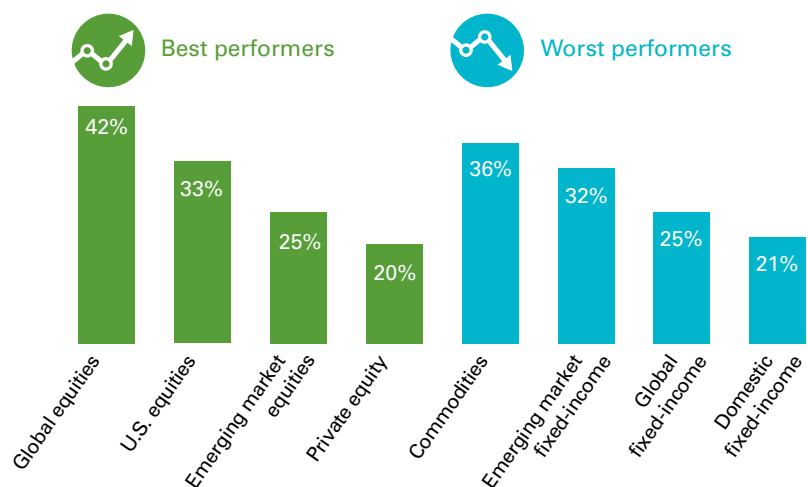
Institutions tell us they will emphasize equities for the next 12 months. When asked for their projections on the top-performing asset classes for 2016, our respondents put global equities at the top of the list followed by U.S. equities, emerging market equities and private equities. These predictions track closely to those we received from respondents in our 2014 survey.<sup>6</sup> (Note: respondents were asked to pick up to three from a list of 15 for their top performers. Ranking represents frequency of responses.)

“The institutional outlook for equities may not just be optimism for stocks so much as a commentary on the state of the bond markets,” says Natixis Global Asset Management chief market strategist David Lafferty. “Interest rates are low globally and negative in a third of European bond markets. These investors would rather tie themselves to corporate growth in stock than to sovereign stagnation in bonds.”

This dilemma is highlighted by institutional concerns over producing sufficient investment returns. When asked about their challenges, 72% are worried that they will not be able to fund long-term liabilities. Their confidence in successfully fulfilling this critical goal may also be diminished by their frustrations with market returns in recent years. Almost two-thirds (64%) of those we spoke with say alpha is becoming harder to obtain as markets become more efficient.

#### OUTLOOK ON THE BEST- AND WORST-PERFORMING ASSET CLASSES

Institutions see equities as the best performers for 2016



Investing involves risk, including the risk of loss. Investment risk exists with equity, fixed-income, and alternative investments. There is no assurance that any investment will meet its performance objectives or that losses will be avoided.

<sup>4</sup> Natixis Global Asset Management, Insurance Industry Survey conducted by CoreData Research, July 2015. Survey included 200 decision makers, 40 respondents from each respective country/region: U.S., U.K. & Ireland, France, Germany and the Nordics.

<sup>5</sup> Price to earnings ratio (P/E) compares a company's current share price to its per-share earnings.

<sup>6</sup> Natixis Global Asset Management, Global Survey of Institutional Investors conducted by CoreData Research, December 2014. Survey included 642 institutional investors in 27 countries.

## BIGGEST RISKS TO INVESTMENT PERFORMANCE

Institutions identify top choice of possible risk in 2016

Nonprofits & insurance companies



Market volatility

Sovereign wealth funds



Geopolitical risk

Corporate pension plans



Economic growth rate

Public or government pension



Monetary policy

## Risks abound

If institutions are to deliver on their primary investment objective of achieving the highest possible risk-adjusted return, they will need to address their second objective: effectively managing volatility. Given that they are looking for equities to be the top performers, they are entering 2016 with eyes wide open to the possible risks.

More than four in ten of our respondents (42%) view market volatility as a major threat to investment performance in 2016. After a year in which we saw 72 days with a 1% or more movement in the S&P 500, it should be no surprise that this weighs on the minds of investors. But volatility is not the only force that could derail plans as slow economic growth (40%), monetary policy (39%), and geopolitical risk (37%) round out institutions' top risk concerns.

## Sources of volatility reminders of recent events

With recent terror attacks in Paris, Beirut, San Bernardino, and Mali, the Syrian refugee crisis, and a polarized start to the U.S. presidential election cycle, it's no surprise that geopolitical events weigh in as the top cause of volatility (54%). But institutions see beyond the headlines. After witnessing volatile reactions to the failure of China's disparate efforts at financial stimulus, the health of markets there is also a concern for half (49%) of those we surveyed.

## Allocations follow market projections



Even though almost every institution invests with a long-term outlook, they still need to generate returns today. Among those we spoke with, 64% say short-term performance goals are prioritized over long-term liability matching objectives. This struggle is directly reflected in the allocation plans for the year ahead.

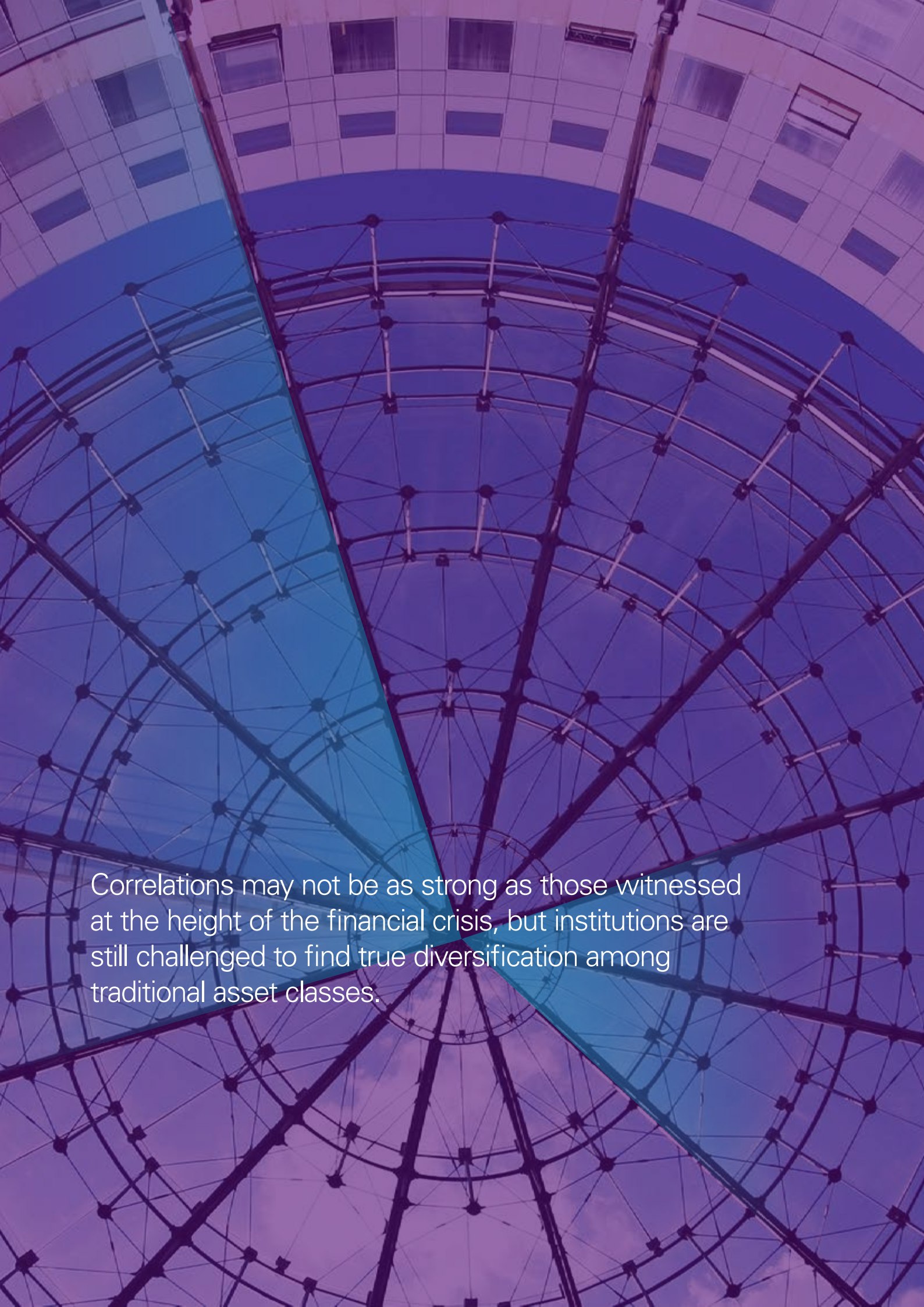
Based on our respondents, the average institutional portfolio allocation includes 42% stocks, 28% bonds, 25% alternative investments, and 5% to cash and other instruments. Current market forces will call for a number of changes in 2016 with 50% saying they will up allocations in private equity, 48% will increase equities, 46% will increase investments in private debt, 41% hedge funds and 34% real assets. Most significant on positions to be trimmed are the 42% who will reduce bond holdings.

## Making moves around the edges

These plans for re-allocation may reflect the frustrations institutions have with today's market constraints. Three-quarters of those surveyed say it is difficult to take tactical advantage of market movements. It appears that these challenges are driving greater innovation in the areas of alternative investments and risk management.

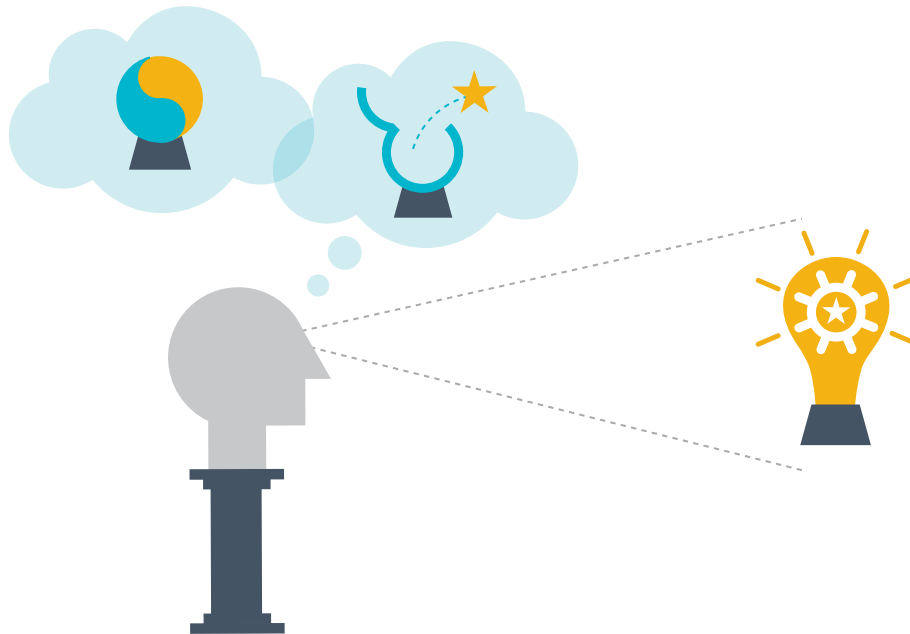
## ALLOCATION CHANGES FOR 2016

Asset Class		
	Increase	Decrease
Equities	48%	14%
Fixed-income	6%	42%
Private equity	50%	12%
Private debt	46%	7%
Hedge funds	41%	14%



Correlations may not be as strong as those witnessed at the height of the financial crisis, but institutions are still challenged to find true diversification among traditional asset classes.

# Risk, returns and liquidity needs drive investment innovation



With slow growth and structural volatility making for inconsistent equity markets and artificially low rates making bond markets a challenge, institutional decision makers are being resourceful in their pursuit of better risk-adjusted returns. This line of thinking is driving innovation in the application of alternative investments, in the development of more sophisticated risk management strategies, and in the adoption of liability matching strategies.

Alternatives are nothing new to institutional investors. Direct ownership of real estate, fine art, farmland and a wide range of hard assets have all been part of the picture for decades. Institutions have also embraced private equity, hedge funds and other strategies to enhance diversification and returns. But alternatives are taking on new prominence within institutional plans as the drive for non-correlated returns heats up.

## An alternative route around high correlations

Correlations may not be as strong as those witnessed at the height of the financial crisis, but institutions are still challenged to find true diversification among traditional asset classes. More than half of those we spoke with (54%) said that high correlations make it difficult to obtain distinctive sources of return using just traditional asset classes.



### WHY INSTITUTIONS IMPLEMENT ALTERNATIVE INVESTMENTS

Diversification	64%
Alpha generation	50%
Risk mitigation	49%
Access to new investment opportunities	37%
High risk-adjusted returns	32%

## MANAGING LIABILITIES

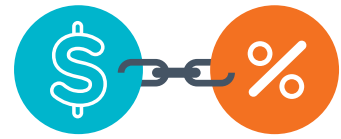
Tools institutions implement in their LDI strategy



50%  
use nominal  
bonds



47%  
cite hedging  
strategies



45%  
implement inflation-  
linked bonds

The answer for many is found in alternative investments. Two-thirds of respondents believe that increasing allocations to non-correlated asset classes is an effective risk mitigation tactic, and virtually the same number say they use alternatives to help diversify portfolios. But their views on alternatives are not limited to the risk side of the equation.

Spotty market performance in recent years has made it difficult to consistently generate the annual returns needed to meet long-term funding goals. We see that many institutions are turning to alternative investments here as well. Half (50%) say alternatives can help them generate alpha. Almost the same number (49%) also say it is essential to invest in alternatives in order to outperform the broader markets.

### Liquidity concerns

While our respondents find alternatives to be effective as portfolio tools, they do express reservations about a perceived lack of liquidity presented by the asset class. As they are subjected to greater regulatory pressure in the form of Dodd-Frank in the U.S. and Solvency II in Europe, institutions must focus on overall liquidity. For many, these requirements present investment constraints.

“ Two-thirds of respondents believe that allocations to non-correlated asset classes are an effective risk mitigation tactic.

Nearly seven in ten (68%) of those surveyed say it is a challenge to meet long-term liquidity needs while investing to meet growth objectives. Thanks to the requirements spelled out in Solvency II and Dodd-Frank, insurance companies feel this pressure more severely with almost eight in ten (79%) reporting this balance is a challenge.

These sentiments could also be tying the hands of institutional decision makers in terms of selecting alternative investments, as 65% believe illiquidity is a necessary part of alternative investments. Institutions are beginning to recognize that recent innovations in the industry may present a potential solution, with 53% of respondents saying that liquid alternatives are an effective tool for managing portfolio risk.

It would seem that as institutions strive to meet long-term liabilities, they are considering how innovations made in the liquid alternatives space might also be leveraged to help maintain liquidity while pursuing long-term growth. Our respondents also believe that the liabilities end of the equation is in need of similar innovations.



## Liability-driven investing

One of the core risks facing virtually any institution is its ability to fund future liabilities. Almost seven in ten (68%) say it's a challenge for them to manage liabilities linked to longevity. Even though we continue to see confidence among respondents in their ability to meet long-term liabilities, this does not mean there is confidence that all institutions will be successful.

Most of those surveyed (89%) say they are confident in their own ability to meet long-term liabilities, but nearly half (46%) also say that most organizations will fail in this critical objective.

Increased regulatory scrutiny may be raising the stakes for institutions in how they manage liabilities. Over the past three years we've seen a substantial increase in the number of institutions that say they are incorporating liability-driven investments (LDI) into their portfolio strategy, rising from 46% in 2013 to 60% in 2015.

When it comes to implementing these strategies, a majority of institutions are incorporating LDI as part of their overall portfolio strategy, with only 39% saying they manage liability assets separately. Almost three-quarters believe they have all the tools they need to appropriately manage liabilities, but that's not to say there isn't room to enhance the tool kit.

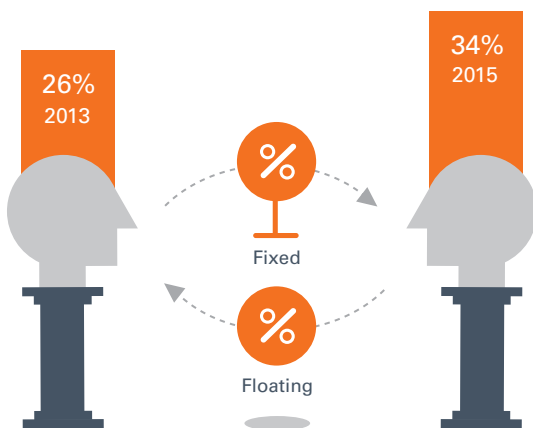
We find that 50% of those surveyed use nominal bonds in their LDI strategy. Another 47% cite hedging strategies, and 45% implement inflation-linked bonds. We also see that institutions are increasingly looking at interest rate swaps, with the number implementing these strategies rising from 26% in 2013 to 34% in 2015.

## Liabilities part of a greater focus on risk management

Longevity risk is just one in a wide array of risks presented by modern markets, and institutions continue to focus efforts on finding effective strategies for managing them. Even in setting up the basic strategies for examining risks, we see institutions digging in deeper. Many (78%) are finding that risk budgeting is an effective strategy.

Beyond managing risk, there are a number of forces at play in today's environment that will require institutions to adapt: building a strategy to meet new and increased regulation, efficient management of investment fees, and marrying corporate policy to return generation.

“Increased regulatory scrutiny may be raising the stakes for institutions in how they manage liabilities.”



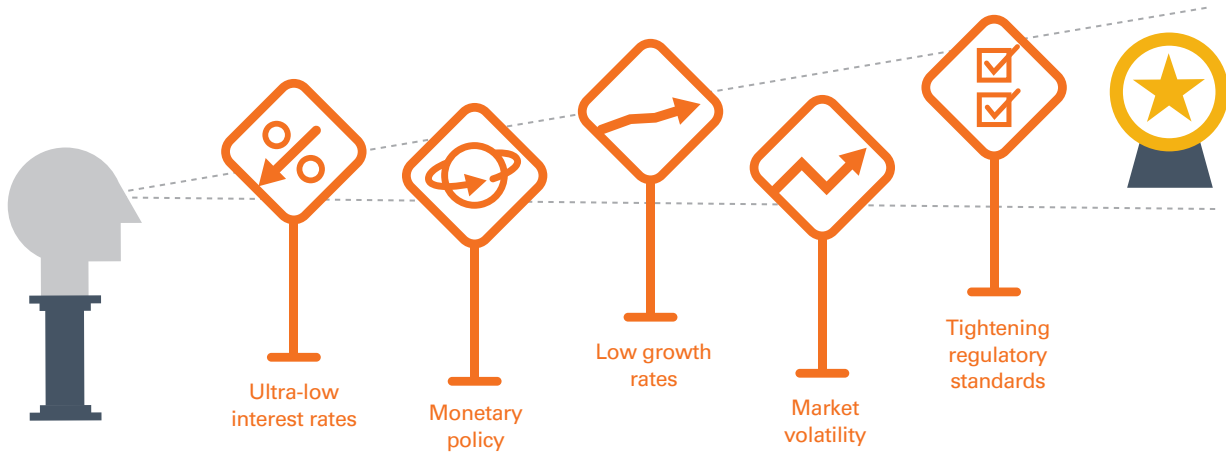
### INSTITUTIONS INCREASING USE OF SWAPS TO MANAGE LIABILITIES

Interest rate swaps are playing a prominent role in LDI strategy as institutions look to secure the cash flow needed to meet liabilities that can stretch out over decades. Swaps are derivatives that allow two parties to exchange a series of cash flows over time. Since their liability cash flow can resemble long-dated bonds, layering in these instruments often helps managers to more closely match assets and liabilities.



As much as institutional decision-makers believe the deployment of new asset classes and strategies is essential to meeting long-term investment goals, it also adds short-term complications.

# Adaptation and the response to new business realities



Above and beyond investment selection and portfolio construction, institutional investors must also address a wide range of management decisions that can influence results as much as their own asset class calls. From dealing with the added complexity of modern markets to containing investment costs to addressing organizational objectives through investment policy, these investment professionals have much to consider.

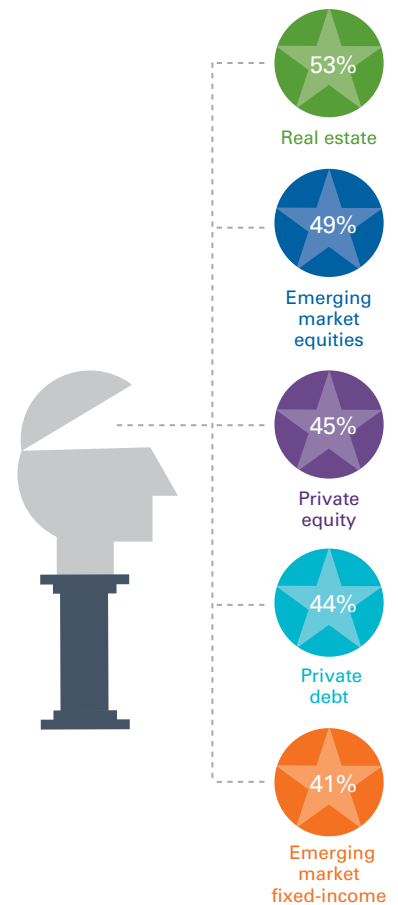
## Managing added complexity

As much as institutional decision-makers believe the deployment of new asset classes and strategies is essential to meeting long-term investment goals, it also adds short-term complications. Nearly half of those surveyed (48%) say the rapid pace of change and innovation can make it difficult to stay abreast of new investment strategies. On top of that, finding the right manager and monitoring performance increase the complexity, with 62% saying manager due diligence and selection is challenging.

As a result of these challenges, we are beginning to see a number of institutions rely on external resources for investment management. Today, about three-quarters of respondents say they manage their entire portfolio in-house. The remaining 25% say they turn to an outsourced CIO or fiduciary manager for at least part of their portfolio. On average they are turning to outside managers to run about 9.5% of total assets.

Why do these sophisticated managers look to outsource investment management responsibilities? Our respondents present a specific rationale for using outside managers. They cite access to specialist capabilities and expertise (49%) as a prime motivation, and say they can often achieve better returns with outside help (18%). Perhaps equally important is to gain the added help to manage the complexity of their portfolios.

## TOP ASSET CLASSES WHERE INSTITUTIONS OUTSOURCE MANAGEMENT



“ Institutional investors give the advantage to active investment for a much wider array of investment objectives than passive ones.

This last benefit is clearly demonstrated in the areas where institutions seek outside counsel. Most frequently they are looking to add expertise to research-intensive asset classes where building capabilities in their own staff could wind up being more expensive and less efficient.

Among their top choices for outsourced management are real estate (53%), emerging market equities (49%) and private equity (45%). Each of these asset classes requires unique expertise, and success depends on the ability to evaluate a broad investment universe in order to identify inefficiencies and real opportunity. Rather than building in-house teams, it makes the most sense to rent the specialist capabilities.

### Active and passive strategies plug into specific roles

While some institutions are willing to pay for outside expertise in less efficient parts of the markets, fees are coming under closer scrutiny in areas that are more efficient. This is where passive management appears to have found a foothold with institutions.

The debate of active versus passive has heated up in recent years as inconsistent market returns and lackluster performance has led many to call into question the value of active management over the short term. Just as we found in our 2015 Global Survey of Financial Advisors,<sup>7</sup> our institutional respondents tell us that it is more like a case of active *and* passive, rather than the winner-take-all title bout that many in the media and blogosphere make it out to be.

While institutional managers have historically focused on active strategies across their portfolio, expense management is leading them to test the waters with passive, index-based strategies. Three-quarters (75%) of those surveyed say they use passive strategies to manage at least part of their portfolio.



The vast majority (90%) say they turn to passive in order to minimize fees. Most frequently they report using passive investments to access efficient asset classes such as stocks. But all is not positive on the passive part of the equation and institutions are split, still making up their minds as to whether passive investments distort relative stock prices and risk/return tradeoffs.

### A clear preference for active management

Institutional investors give the advantage to active investment for a much wider array of investment objectives than passive ones. According to these decision makers, active strategies are more effective in generating alpha (87%) and gaining exposure to the non-correlated asset classes that have become important components in institutional strategies (77%).

Active also gets the nod for being better suited to take advantage of short-term market movements (71%) and ultimately generating the risk-adjusted returns that are a high priority for institutions. It is likely that these reasons are why two-thirds of institutional investors tell us that they believe that current macroeconomic factors favor active investments, and why nearly six in ten tell us they believe active strategies will outperform on a long-term basis.

#### INSTITUTIONS FAVOR ACTIVE FOR WIDER RANGE OF OBJECTIVES

Objective	 	
	Active	Passive
Minimizing fees		X
Taking advantage of short-term market movements	X	
Exposure to non-correlated asset classes	X	
Generating alpha	X	
Accessing emerging market opportunities	X	
Providing risk-adjusted returns	X	

<sup>7</sup> Natixis Global Asset Management, Global Survey of Financial Advisors conducted by CoreData Research, July 2015. Survey included 2,400 financial advisors in 14 countries and territories.

Innovation is catching up here as well, as managers begin to look at smart beta strategies that apply alternative indexing to achieve better diversification, volatility management or other objectives. They say these hybrid strategies often provide the best of both worlds. Just over half say smart beta is a valid and efficient approach to better returns and reduced costs.

## ESG becoming more than a screen

Investment policy is becoming an opportunity for institutions to express organizational values. In recent years investment teams have applied social screens with an eye toward managing assets to reflect an interest for elevating standards for environmental, social and corporate governance (ESG) issues.

As highly visible, large-scale investors with diverse constituents, many institutions see such screens as a tool to help insulate portfolios from headline risk. But in limiting ESG to a screening process, institutional investors may be missing out on a greater opportunity.

Among the 660 managers we spoke with, there is growing interest in ESG, but adoption has been slow. The vast majority (95%) say their organizations incorporate ESG criteria in their analysis and decision-making process. Some believe these screens can help mitigate risk and potentially enhance alpha, but they need more proof. In fact, 64% say they believe ESG measures are primarily a PR tool.

Motivations for incorporating ESG appear to be one-sided. Today, managers most frequently incorporate these strategies because they are mandated by their fund. Insurance companies in particular say it's a tool to help them manage headline risk more effectively. Half of those we surveyed say it helps them protect from asset losses as a result of lawsuits, social discord and environmental hazards.

## ESG as an investment strategy

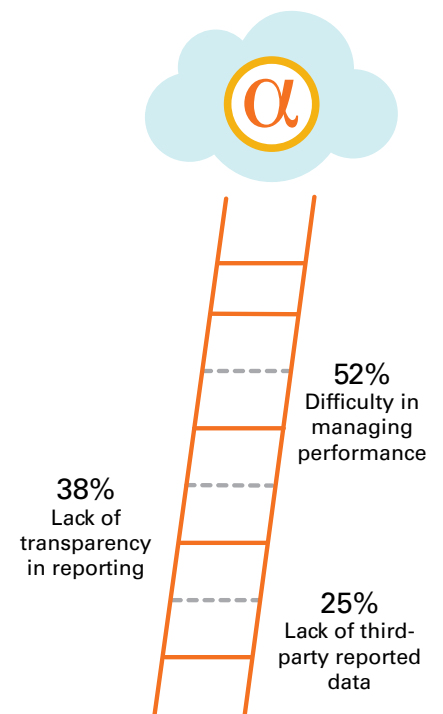
But many are also beginning to see that ESG may also provide direct investment benefits. Half (50%) of those surveyed say these strategies could also be a source of potential alpha, but there is much more to be learned as only 26% have found that incorporating ESG into investment decision-making has had a positive impact on investment performance.

Managers identify some of the key challenges to seeing more broad-based adoption of ESG: the difficulty in measuring performance (52%) and a lack of transparency in reporting (38%). With a growing number of managers offering specialist capabilities within this realm, these concerns will likely dissipate.

These specialists are looking at ESG through a new lens, investing in key trends such as green energy, in which businesses will benefit from increased societal focus on sustainability. This kind of impact investing may be the opening for more managers to incorporate ESG into institutional strategy. It may be one critical reason why more than four in ten (44%) of those surveyed say ESG will be a standard practice for most managers within five years.

### KEY CHALLENGES TO THE ADOPTION OF ESG

50% of respondents say ESG strategies could be a source of potential alpha, but identify challenges that need to be addressed

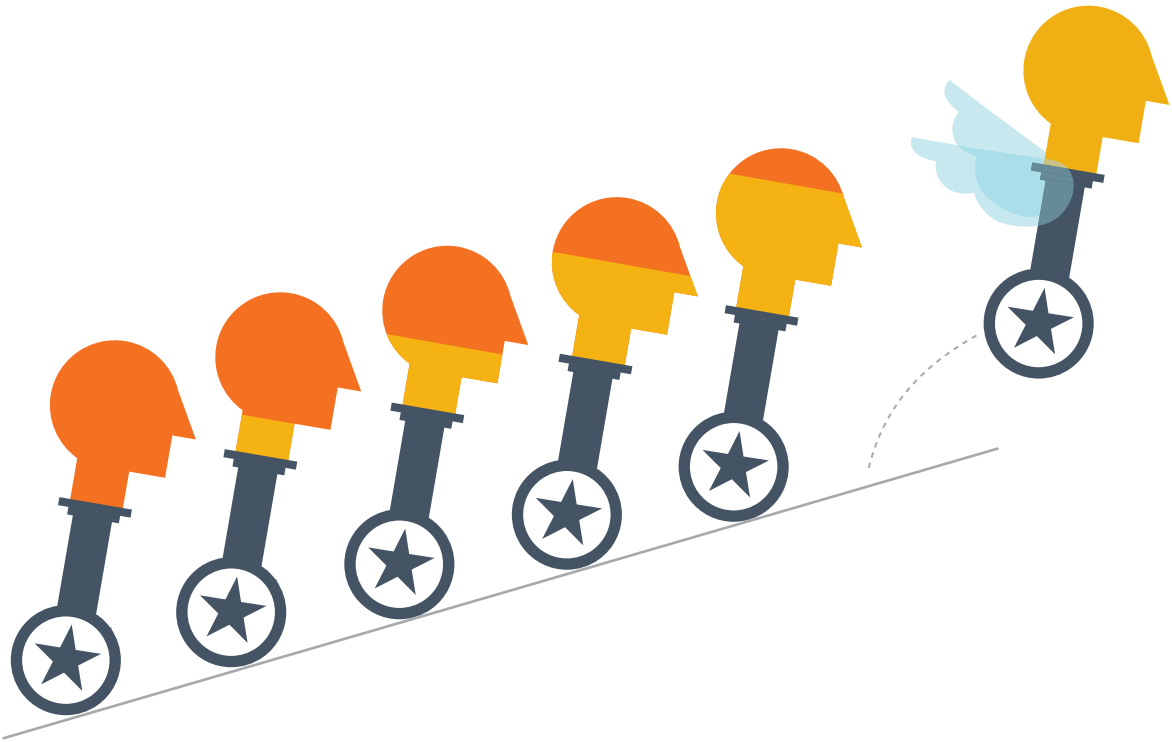




We anticipate that change will always be a constant but the rate of change will continue to increase, making it imperative for the smart money to stay alert.

## CONCLUSION

# No rest for the weary



Modern markets present a complex range of challenges and opportunities. Institutional investors have been adept at adapting strategy in response to changing market dynamics, new investment opportunity and business objectives. In the years ahead we anticipate that change will always be a constant but the rate of change will continue to increase, making it imperative for the smart money to stay alert.

### Markets continue to drive evolution of strategy

Institutional strategy has long had to balance two competing forces: the need to meet long-term obligations and the need to generate returns over the short term. Looking ahead, the pressures here are likely to increase. Accommodative monetary policy continues to keep interest rates low, which will continue to challenge managers' ability to generate stable income. Equity markets will continue to be marked by uncertainty and volatility.

As always, institutions will be challenged to make short-term tactical changes without detracting from their ability to meet long-term funding goals. This will be particularly difficult as risk and volatility are not wholly the result of just market factors. As events happen, it will be imperative to take market reactions into account in allocation decisions.

## Rapid innovation to meet organizational goals

Over the long term, we have seen institutions to be a wellspring for new investment ideas. Advances in technology and financial innovation are likely to expand the tool box.

Early adoption of alternatives has helped shape the development of new asset classes and investment vehicles. Acceptance of alternative investment strategies has traditionally flowed downstream, but now innovations made at the retail level, such as liquid alternatives, may actually find new utility in institutional portfolios. In particular, it would appear that institutional investors are looking at these strategies as a tool that can potentially provide a strategic solution for achieving diversification goals while still meeting liquidity requirements spelled out in new financial regulations worldwide.

In addition, we anticipate that there will be greater innovation with liability-driven investments as institutions look to address a wide range of market risks and the ever-present longevity risk presented by an aging population.

## Adapting to business challenges

Institutional managers have more to consider than just investment selection and asset allocation. With markets becoming more complex, institutions show that they are willing to look for outside expertise. While few would consider turning over management of the entire portfolio to an outsourced CIO, some are turning to outside help for managing parts of the portfolio. While this sort of move allows institutions to tap into new strategies and non-correlated asset classes without having to add to staff, it does create new challenges around manager oversight. This model may be particularly effective as institutions look to integrate research-intensive strategies such as ESG, infrastructure and private equity into the investment mix.

Costs are top of mind for institutions, and we see many deploying passive strategies in more efficient asset classes in order to reduce expenses. But active strategies still hold favor for generating alpha and pursuing better risk-adjusted returns overall.

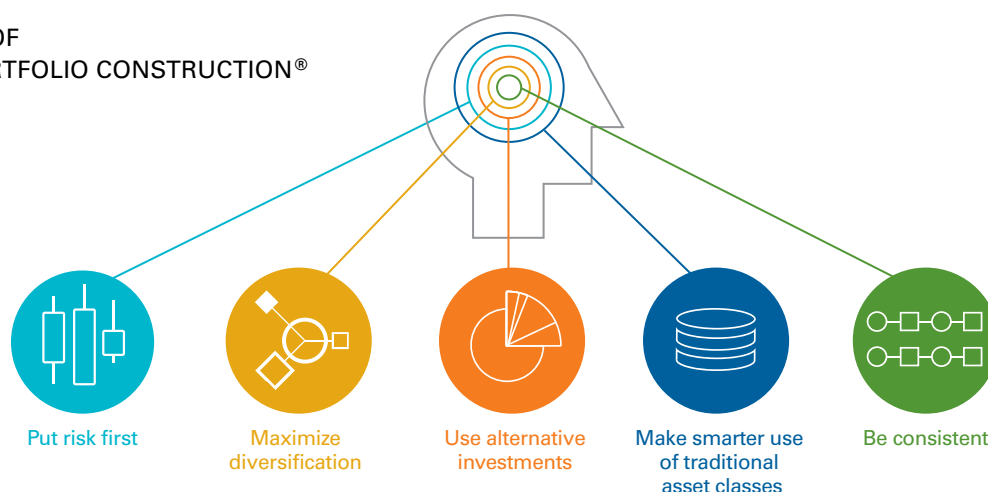
## Moving toward a more durable strategy

While the themes of evolution, innovation and adaptation all imply the need for steady meaningful change, the end goal is one that does not change. We know that institutions are focused on meeting long-term liabilities and producing better risk-adjusted returns. Each adjustment in strategy is made with the intended goal of producing a more durable portfolio. Institutional investors are masters at the art of continual learning, and the process of integrating small changes over long periods of time is intended to ensure their assets will be sustained for decades or longer.

“ While the themes of evolution, innovation and adaptation all imply the need for steady meaningful change, the end goal is one that does not change.



## FIVE TENETS OF DURABLE PORTFOLIO CONSTRUCTION®



### Toward more durable portfolios

In markets across the globe we have seen investors of all types challenged to meet the competing priorities of generating returns through short-term market cycles and funding long-term financial liabilities. In our view, meeting these modern market challenges demands a more consistent investment framework.

We believe **Durable Portfolio Construction®** can make a difference to individuals, advisors and institutions as they look to build portfolios that can help address risk concerns while also pursuing long-term asset growth. Our tenets for Durable Portfolio Construction include:

**Put risk first** – Use risk parameters as the main input for asset allocation to manage volatility. Durable Portfolio Construction targets a consistent range of risk rather than a potential range of returns. The result is added predictability and, ultimately, durability in the portfolio.

**Maximize diversification** – Consider the broadest possible range of asset classes and investment strategies – long and short exposures to global equities, global fixed-income, commodities and currencies – with a goal of managing volatility in the overall portfolio.

**Use alternatives** – Alternatives may be an effective means of diversification. They also may lower correlations, temper volatility and offer new sources of return. For example, alternative strategies well suited to a durable portfolio include long or short exposures to commodities, currencies or real estate for new sources of return, or hedging to help reduce risk.

**Make smarter use of traditional asset classes** – Seek new, efficient ways to capitalize on the long-term potential of stocks and bonds. Smarter use of equities includes techniques and strategies that have the potential to enhance long-term returns or reduce short-term risk. Smarter use of fixed-income may include inflation-aware bond strategies and multisector bond funds.

**Be consistent** – Maintain a consistent portfolio construction process to focus on the big picture and withstand short-term market changes. Choosing and using a rational, repeatable construction process is the hallmark of a durable portfolio – and perhaps the most important principle of Durable Portfolio Construction.

Durable Portfolio Construction® does not guarantee a profit or protect against a loss.



## PROGRAM OVERVIEW

### About the Durable Portfolio Construction Research Center

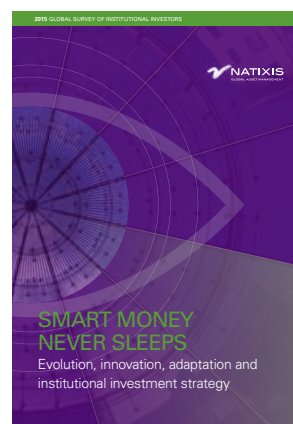
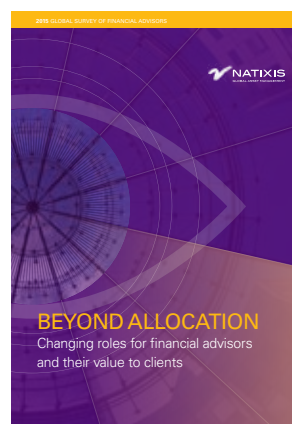
Investing can be complicated: Event risk is greater and more frequent. Volatility is persistent despite market gains. And investment products are more complex. These factors and others weigh on the psyche of investors and shape their attitudes and perceptions, which ultimately influence their investment decisions. Through the Durable Portfolio Construction Research Center, Natixis Global Asset Management conducts research with investors around the globe to gain an understanding of their feelings about risk, their attitudes toward the markets, and their perceptions of investing.

### Research agenda

Our annual research program offers insights into the perceptions and motivations of individuals, institutions and financial advisors around the globe and looks at financial, economic and public policy factors that shape retirement globally with:

- **Global Survey of Individual Investors** – reaches out to 7,000 investors in 17 countries.
- **Global Survey of Financial Advisors** – reaches out to 2,400 advisors in 14 countries and territories.
- **Global Survey of Institutional Investors** – reaches out to over 600 institutional investors in 29 countries.
- **Natixis Global Retirement Index** – provides insight into the environment for retirees in 150 countries based on 20 economic, regulatory and health factors.

The end result is a comprehensive look into the minds of investors – and the challenges they face as they pursue long-term investment goals.



### About the surveys referenced in this paper

**2014 Global Survey of Institutional Investors** – Natixis Global Asset Management commissioned CoreData Research to conduct a global study of institutional investors, with the aim of gaining insight as to how they are managing investments and meeting various challenges in today's world.

Interviews were conducted throughout October and November 2014. Globally, the study involved 642 decision-makers working in institutional investment who collectively manage \$31 trillion in assets in 27 countries.

**2015 Global Survey of Financial Advisors** – Natixis Global Asset Management commissioned CoreData Research to conduct an international study of financial advisors, with the aim of better understanding the contemporary attitudes and needs of this key collective of individuals to the financial services industry.

Data was gathered over a five-week period spanning June and July 2015. Globally, the study involved 2,400 financial advisors in 14 countries and territories.

**2015 Insurance Industry Survey** – Natixis Global Asset Management commissioned CoreData Research to conduct a study of key decision-makers in the insurance industry, to provide insight into how they plan on facing the challenges of increased regulatory pressures, investment constraints, and the difficulties of managing the portfolio construction process.

The survey was conducted and hosted by CoreData Research in July 2015. The sample consists of 200 decision makers working in the insurance industry – 40 respondents from each respective country/region (U.S., U.K. & Ireland, France, Germany and the Nordics).

### Helping to build more durable portfolios

Natixis Global Asset Management is committed to helping advisors build better portfolios that stand up to the challenges of modern markets. To learn more about our **Durable Portfolio Construction**<sup>®</sup> philosophy, visit [durableportfolios.com](http://durableportfolios.com).

This communication is for information only. Analyses of the survey referenced herein are as of January 26, 2016. There can be no assurance that developments will transpire as may be forecasted in this material. This material may not be redistributed, published, or reproduced, in whole or in part.

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