



NEPC, LLC

YOU DEMAND MORE. *So do we.*<sup>SM</sup>

# NEPC 2017 Market Outlook

## Themes, Actions, and Opportunities

January 30, 2017

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## Speakers



- **Mike Manning, CFA, CAIA**
  - Managing Partner



- **Christopher Levell, ASA, CFA, CAIA**
  - Partner, Client Strategy Research



- **Phillip R. Nelson, CFA**
  - Director of Asset Allocation



- **Kristi Hanson, CFA**
  - Director of Taxable Research

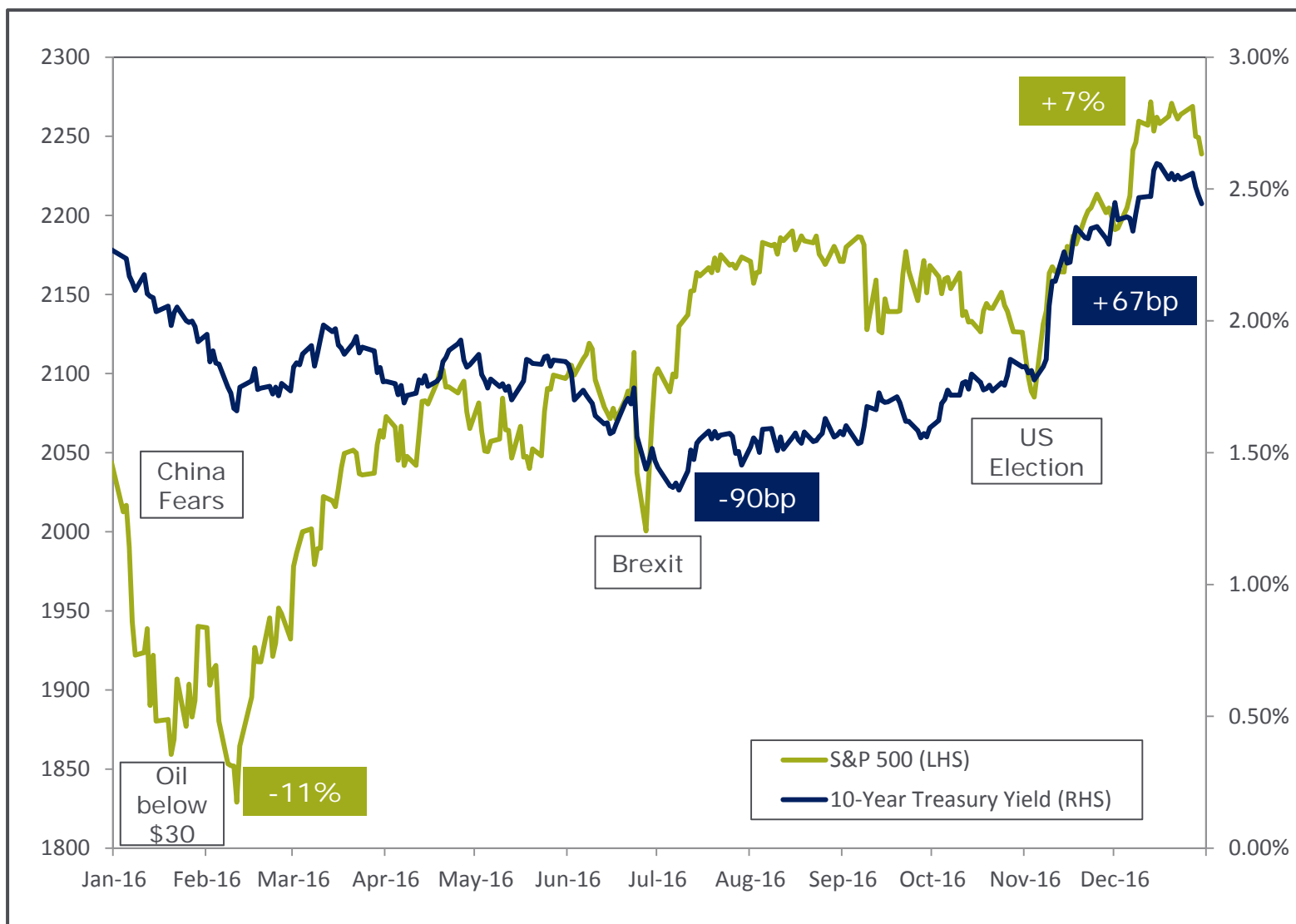
## Agenda

- **2016 Review**
- **NEPC Update**
- **Market Outlook**
- **Private Wealth**
- **Your Questions**

# 2016 Review



## 2016: A Rollercoaster of Geopolitical Events



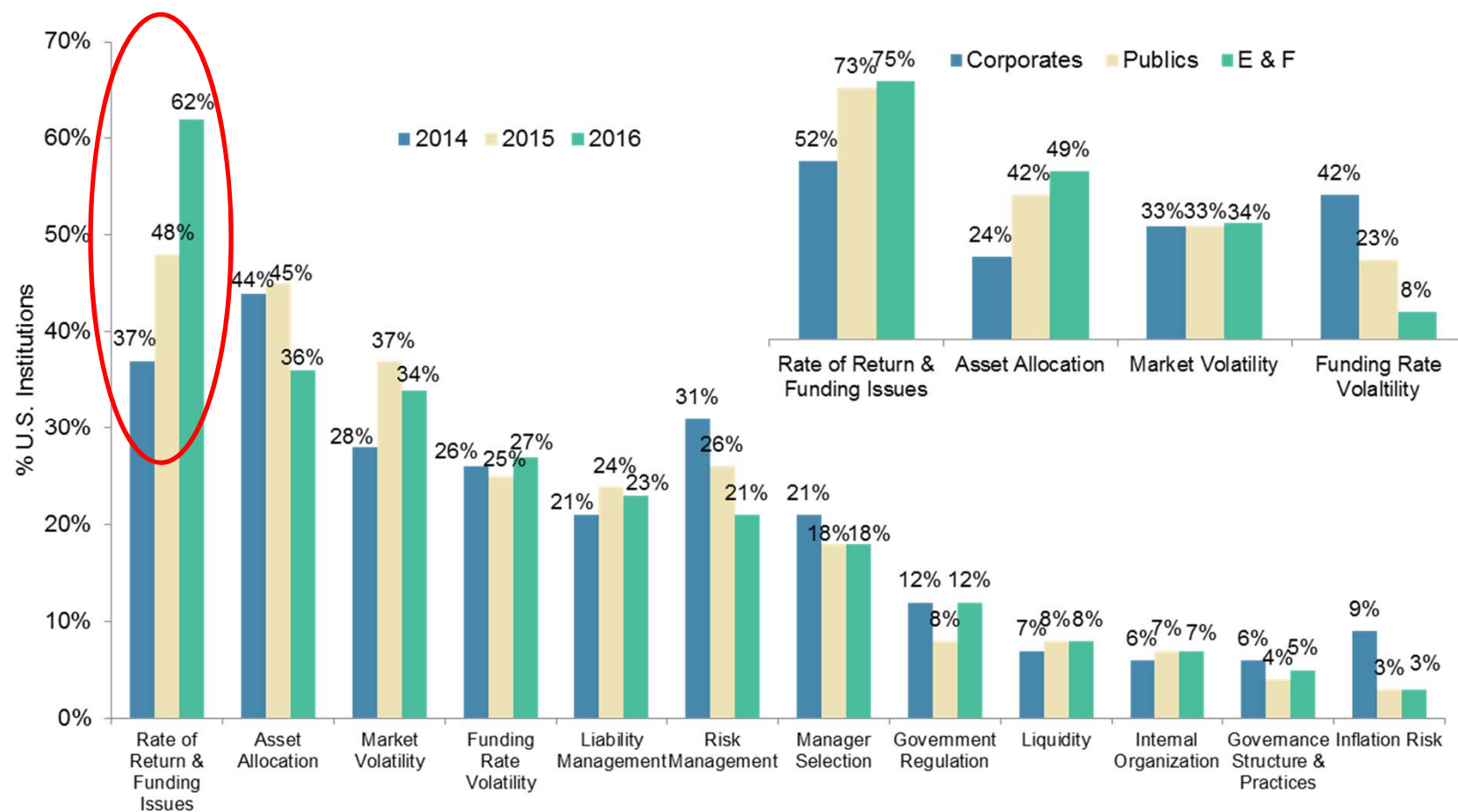
Source: Bloomberg, NEPC

## 2016: A Strong Year for Risk Assets



*\*Private Equity and NCREIF Real Estate lagged one quarter  
Source: NEPC, Barclays, S&P, Bloomberg, JPM, Russell, MSCI, HFRI, InvestorForce*

# Greenwich Associates: Key Challenges for Institutional Investors



Source: Greenwich Associates 2016 U.S. Institutional Investors Study

# NEPC Update

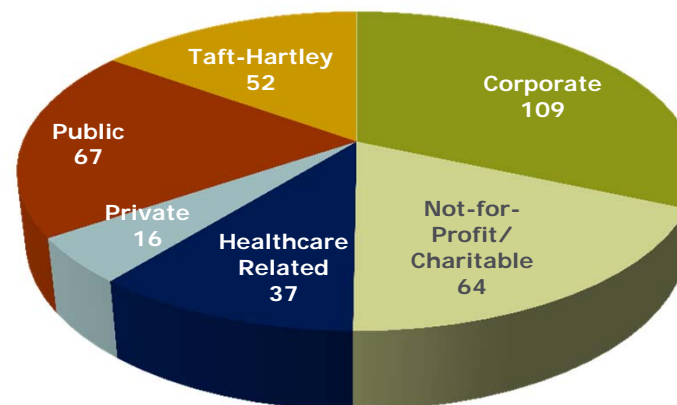


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## Our Goal is to be the Consultant of Choice

- **Independent, employee-owned consulting firm**
  - 256 employees in 8 regional offices
  - Employee-owned with 36 partners
  - 345 institutional clients and \$928 billion assets under advisement<sup>1</sup>
- **100% of revenue from advisory and discretionary consulting services**
- **Institutional scale with outstanding client service**
  - Practice groups within NEPC deliver expertise by client type



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## **"Great People + Right Resources = Happy Clients"**

### **Great People**

- **New Partners – Mike Sullivan, Kristi Hanson, Karen Harding**
- **New Principals – Phillip Nelson, Brian Roberts, Mike Valchine**
- **Increased learning and development**

### **Right Resources**

- **Low client-to-consultant ratio**
- **Significant research infrastructure**
- **Improved technology**

# Market Outlook



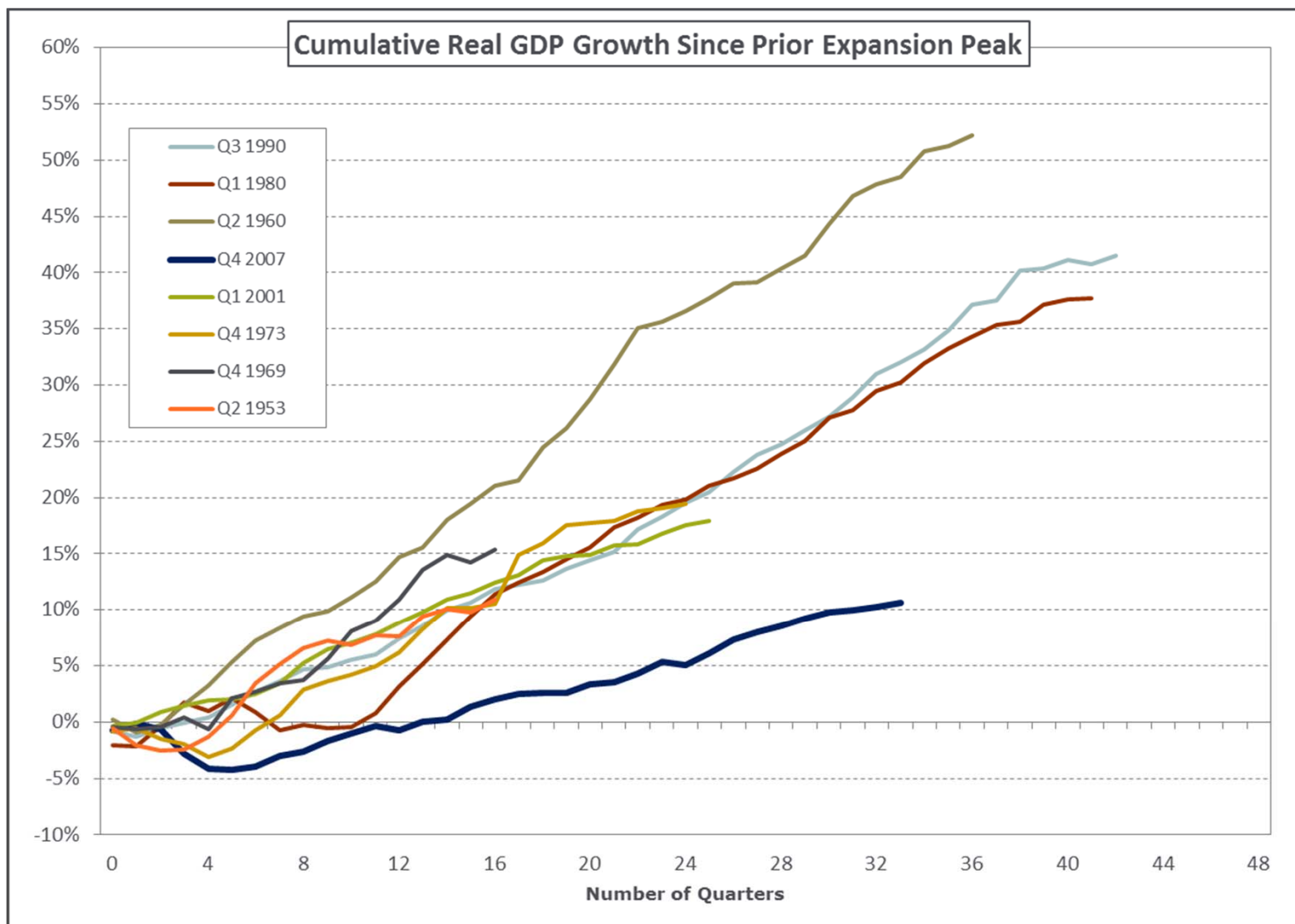
**Extended US Economic Cycle**

**Federal Reserve Gradualism**

**China Transitions**

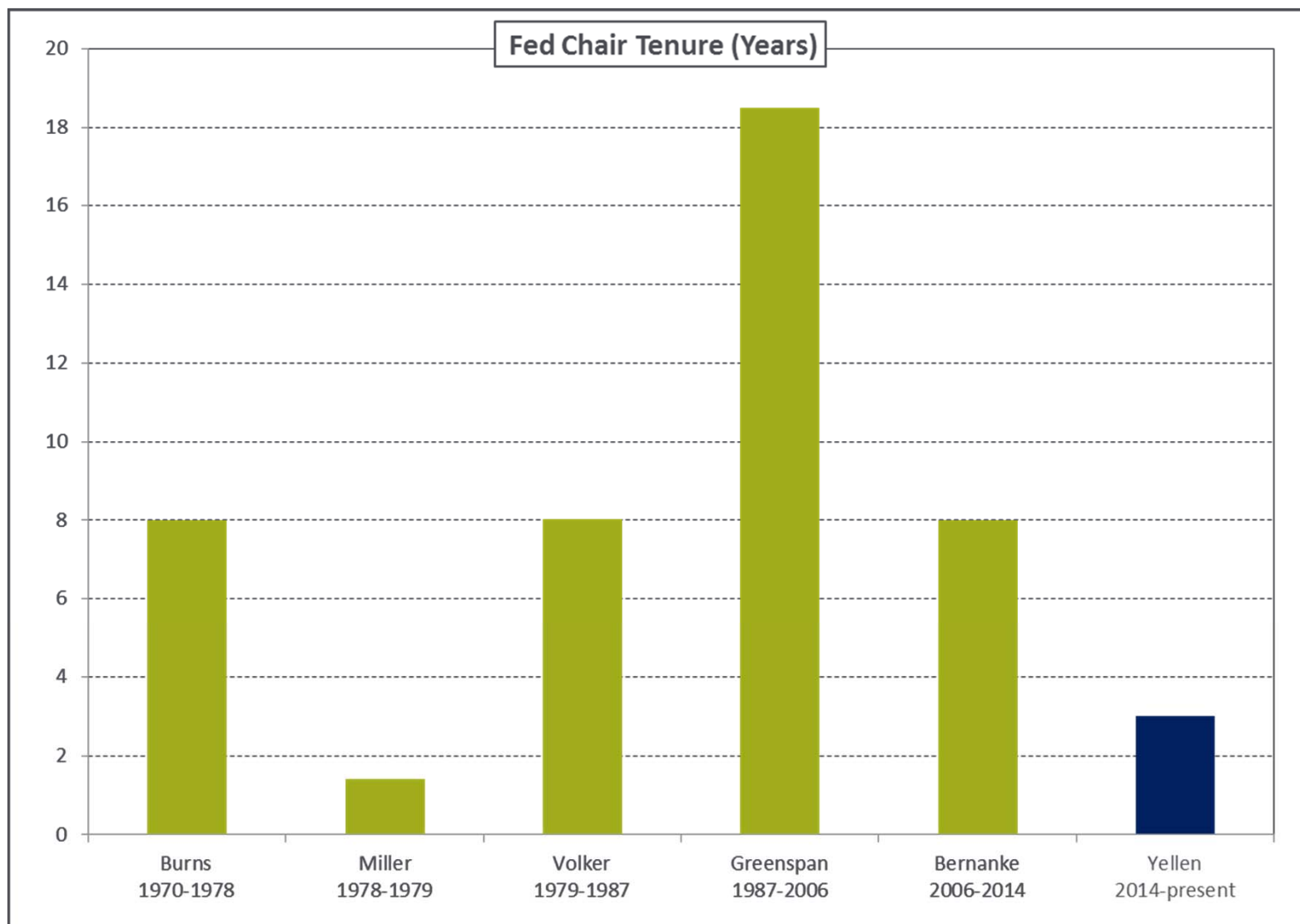
**Globalization Backlash**

## Economic Cycles Don't Die of Old Age – Opportunity for a Prolonged US Economic Expansion



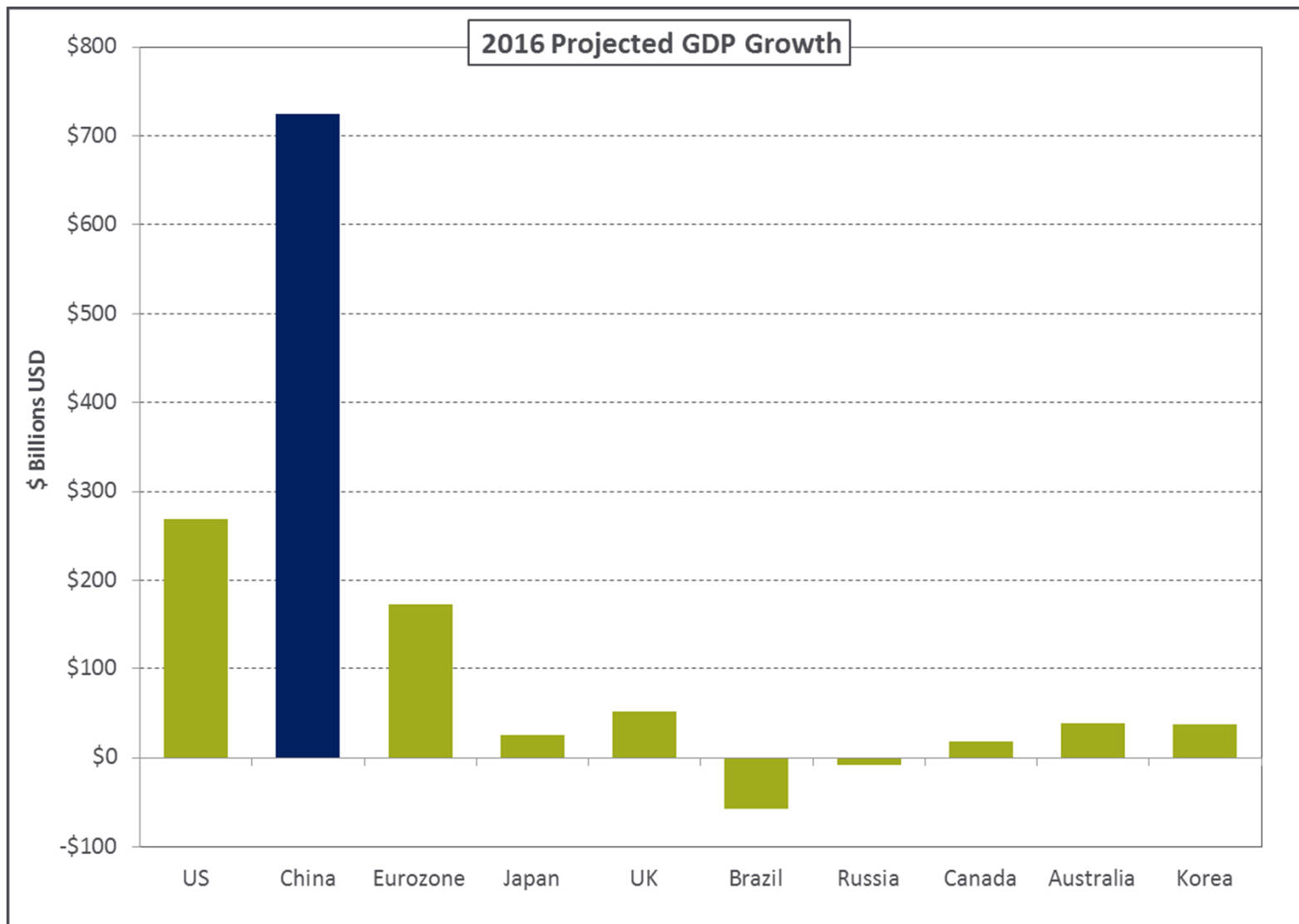
Source: St. Louis Federal Reserve

## Federal Reserve Policy is Not a Certain Path



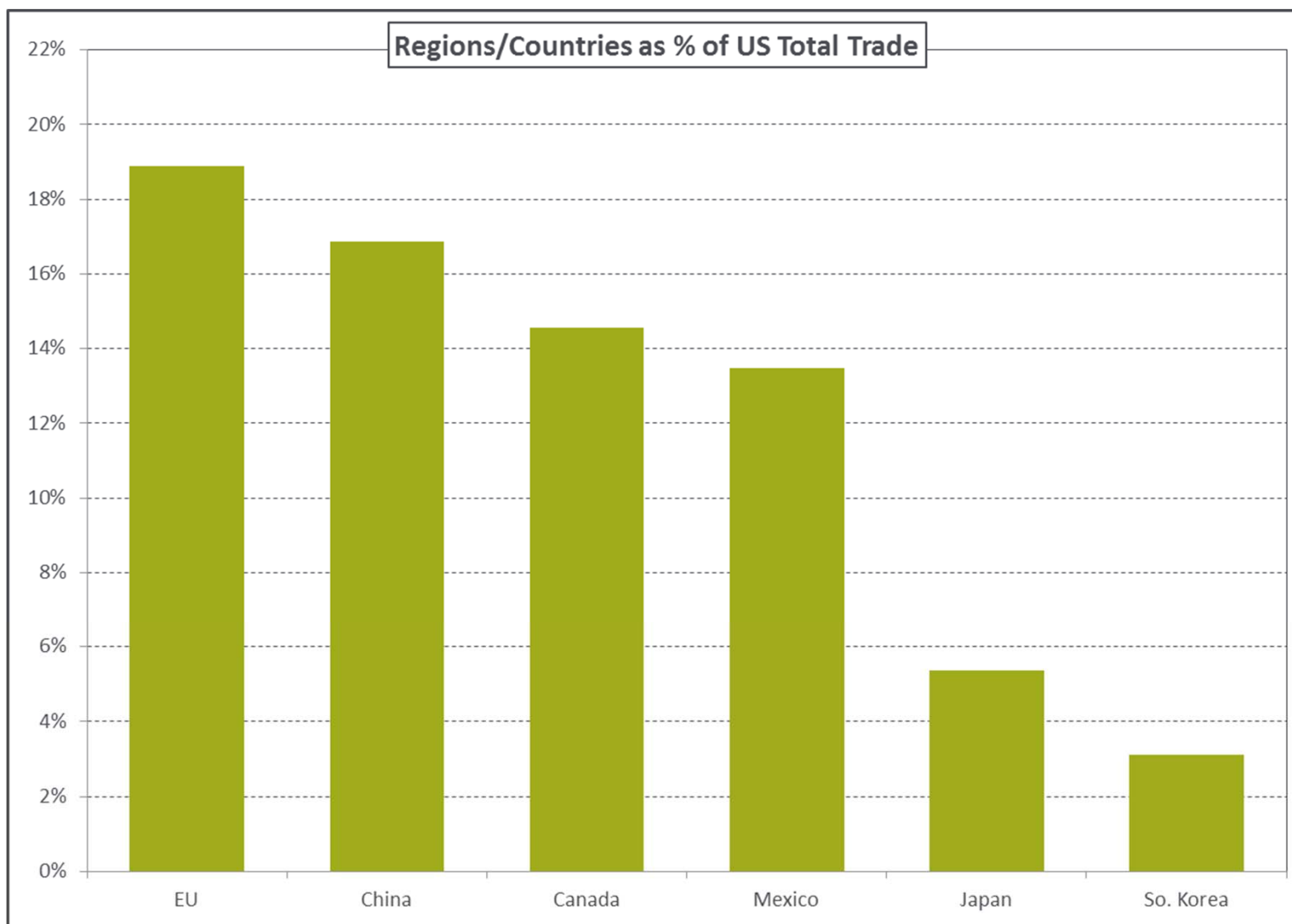
Source: Federal Reserve

## Why China Matters



Source: IMF, Bloomberg

## A Strong US Pivot Away from Global Trade is a Tail-Risk for the Global Economy



Source: IMF, Bloomberg



**Trim US Equity Gains**

**Overweight Non-US Developed Market Equities**

**Emerging Market Equities Remain Attractive**

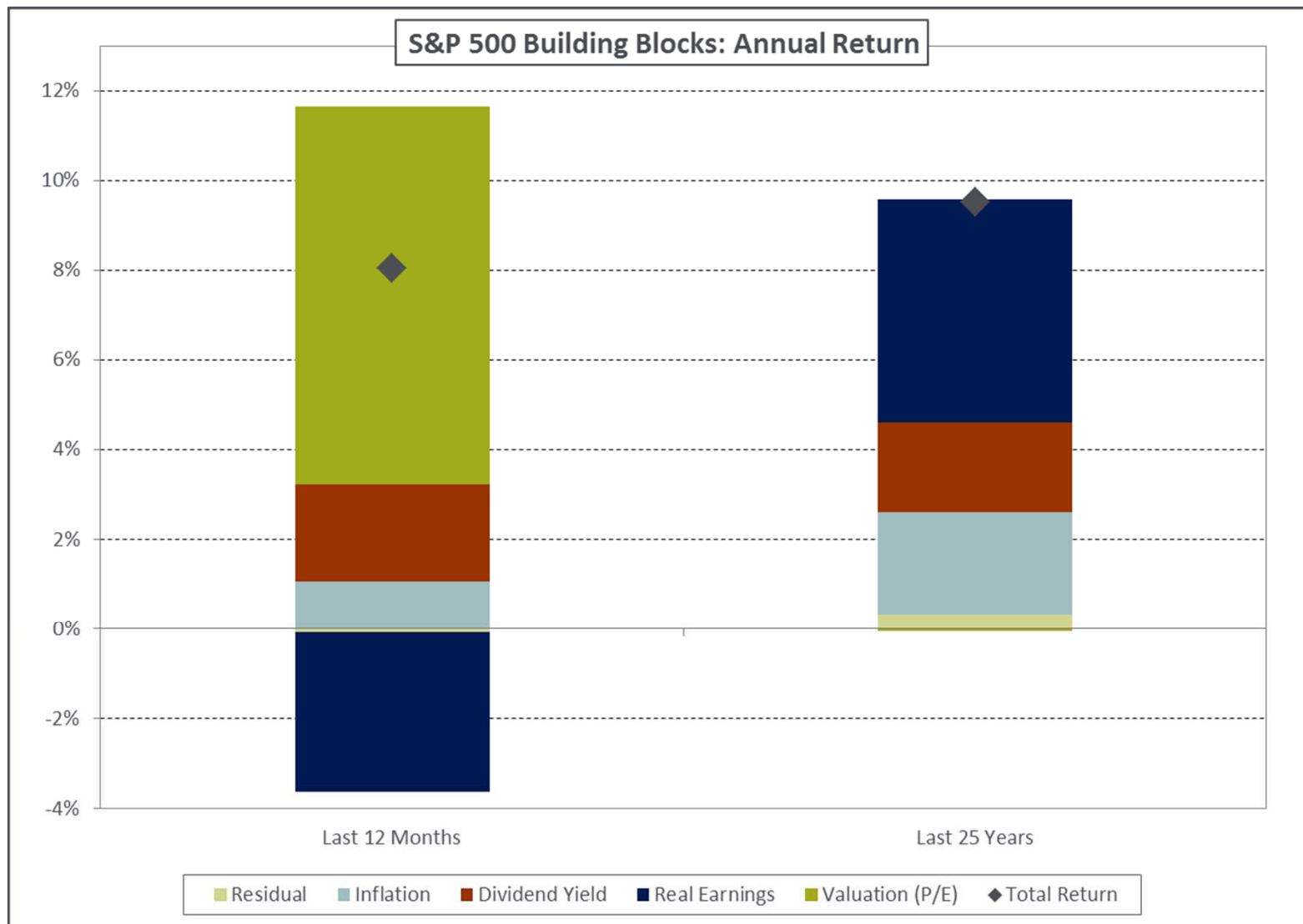
**Allocate to TIPS from Core Bonds**

**Reduce High Yield for Other Credit Strategies**

**Fund Emerging Local Debt from Risk Assets**

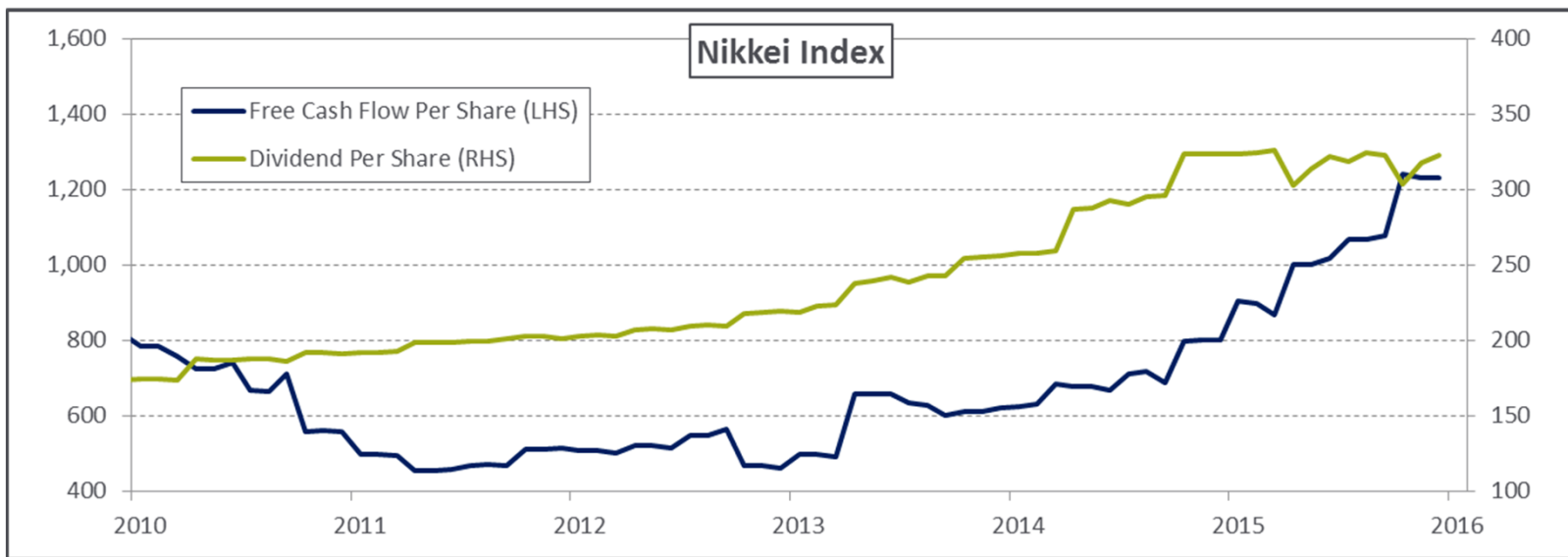
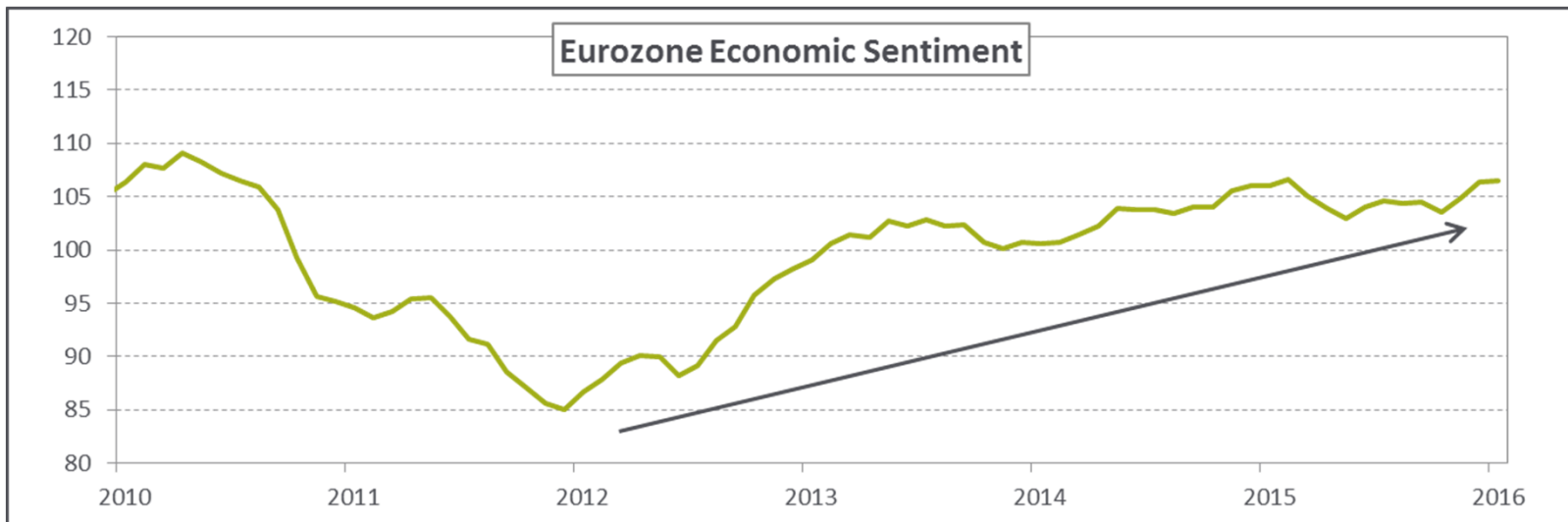
**Add Macro Hedge Fund Strategies**

# Trim US Equity Gains



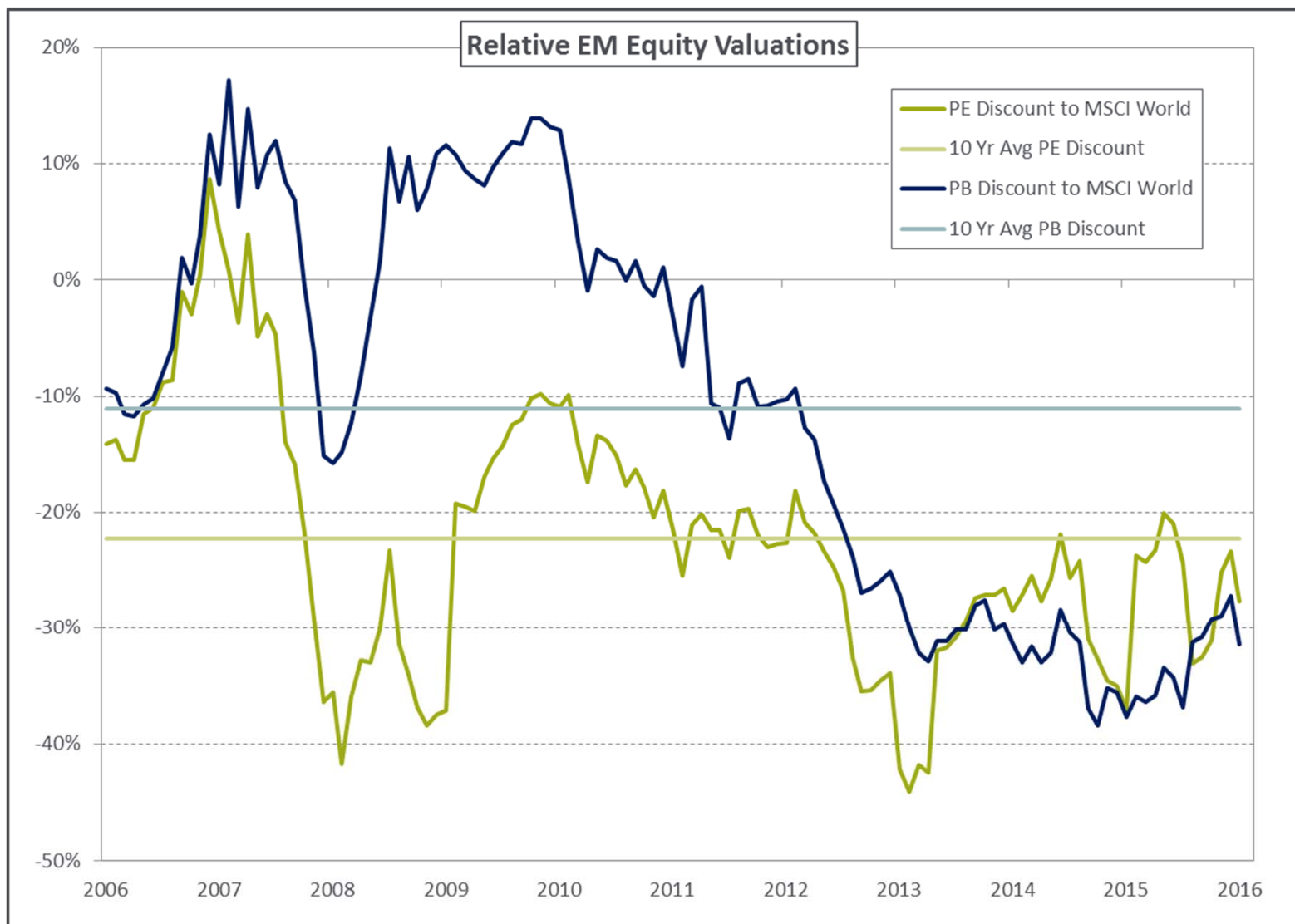
Source: Standard & Poors, Bloomberg, NEPC

## Overweight Non-US Developed Market Equities



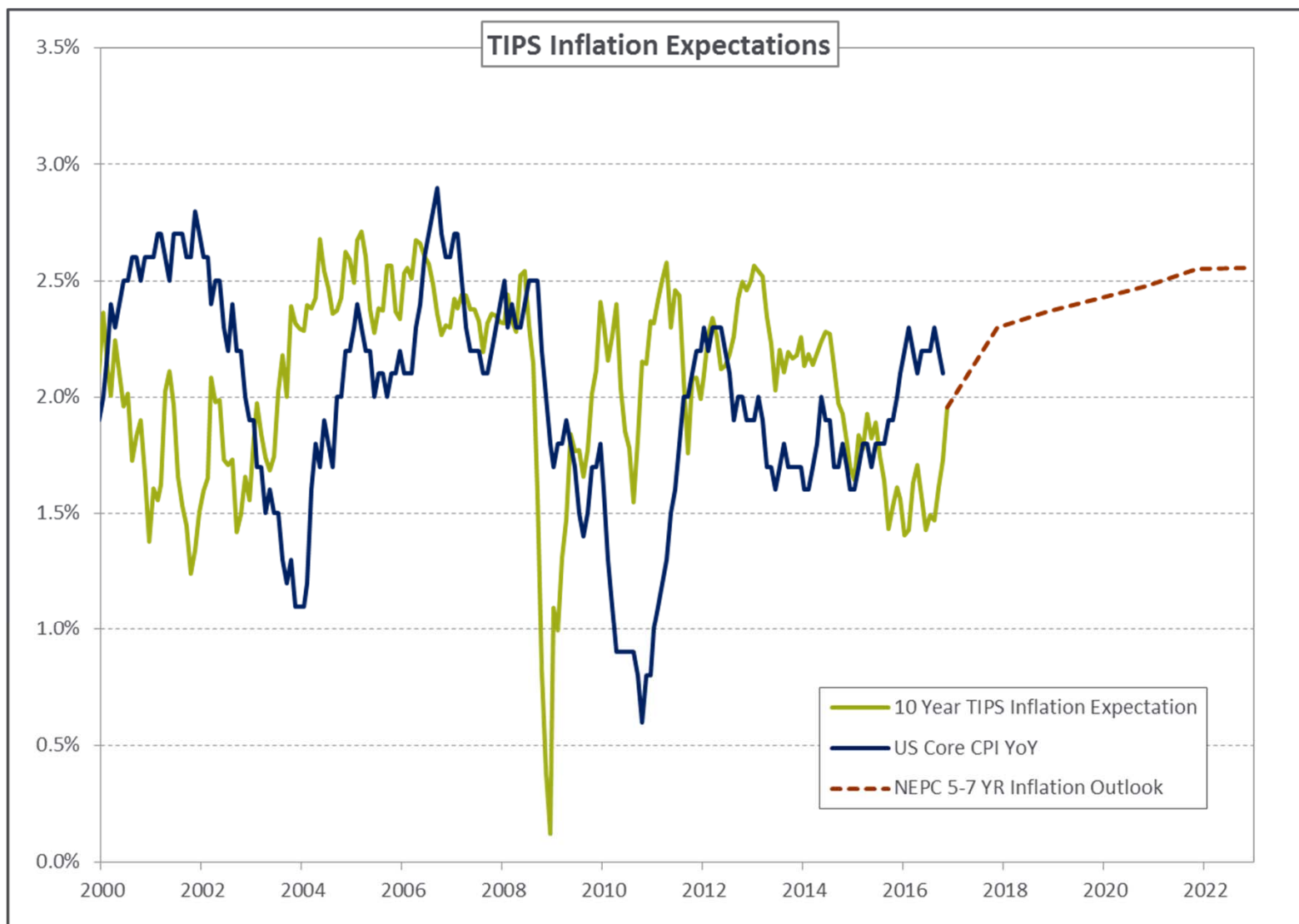
Source: Bloomberg

## Emerging Market Equities Remain Attractive



Source: MSCI, Bloomberg

# Allocate to TIPS from Core Bonds



Source: Bureau of Labor Statistics, Bloomberg, NEPC

## Themes for 2017 Asset Class Assumptions

5-7 Year Return Expectations			
Asset Class	2016	2017	2017-2016
Cash	1.50%	1.75%	0.25%
Core Bonds	2.46%	2.65%	0.19%
TIPS	2.50%	3.00%	0.50%
Long Treasuries	2.25%	1.75%	-0.50%
Municipal Bonds	2.25%	2.25%	-
High-Yield Bonds	5.25%	4.75%	-0.50%
Bank Loans	5.50%	5.25%	-0.25%
Global Bonds	1.00%	1.00%	-
EMD Local Currency	6.50%	6.75%	0.25%
US Large Cap Equity	6.00%	5.75%	-0.25%
Non-US Developed Equities	7.25%	7.25%	-
Emerging Int'l Equities	9.75%	9.50%	-0.25%
Commodities	4.50%	4.75%	0.25%

### Return outlook for risk assets is marginally lower relative to last year

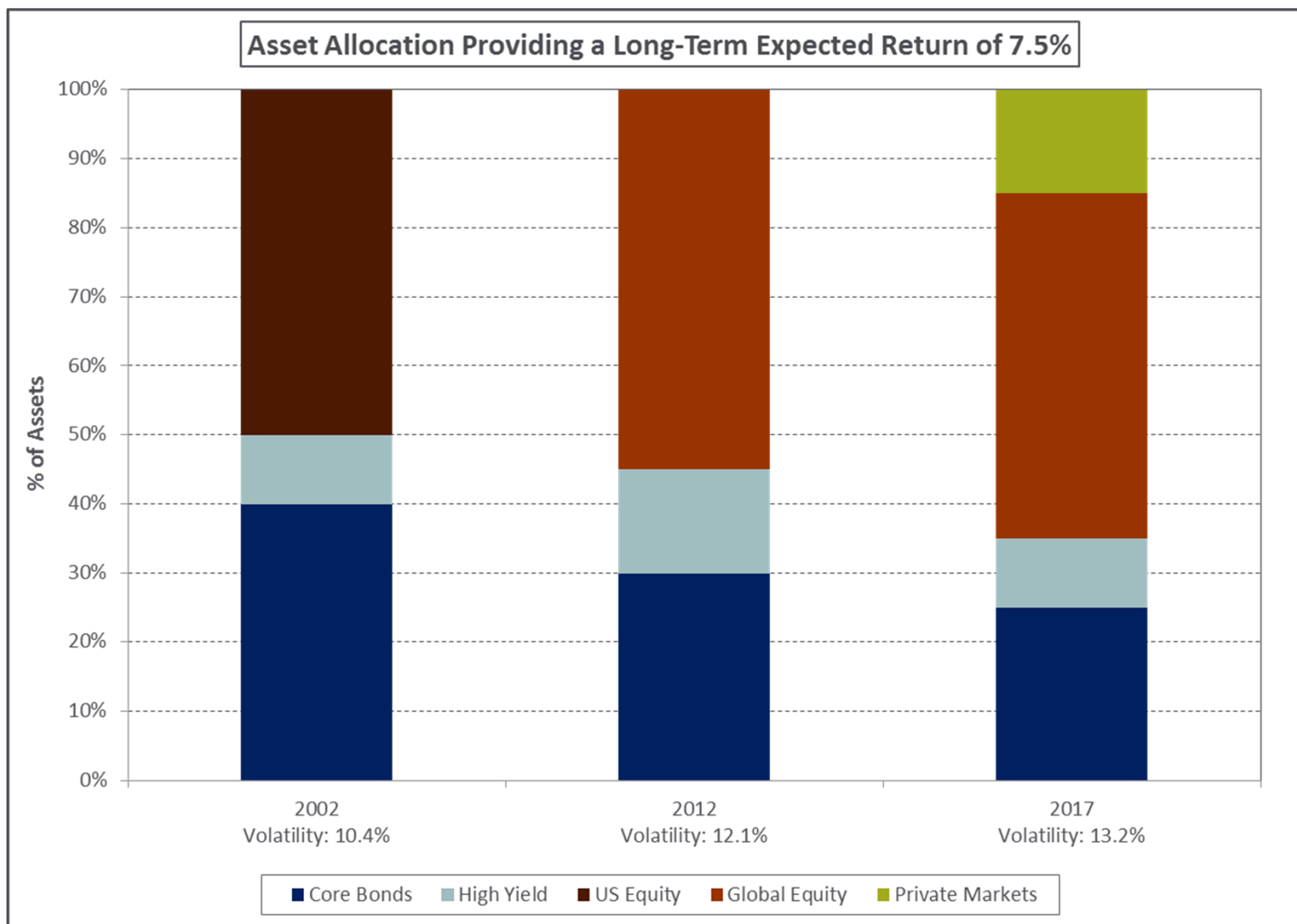
Our inflation outlook for US CPI has increased from 2.25% to 2.5% over 5-7 years

### Risk assets outside the US remain the most attractive total return opportunity for public markets

Declines in US equity and high yield reflect valuation shifts over the last 12 months

### 30 year return assumptions are largely unchanged and reflect subdued capital market assumptions relative to the long-term history

## Evaluate the Feasibility of Long-Term Objectives



Source: 30 Year NEPC Capital Market Assumptions

### **We anticipate inflation will shift marginally higher in the coming years**

A prolonged US economic expansion can support a continued rally for US risk assets

### **Fed must balance the path of future interest rate increases with the disruptive effects of a strong dollar on global markets**

### **Asset returns offer less support for investors to achieve objectives**

Expected returns greater than 7.5% (5% real) will be a high hurdle for diversified investors to realize

### **A mature private markets portfolio is a key contributor to meeting long-term portfolio objectives**

Building a self-sustaining private markets allocation is a long process but provides meaningful wealth creation

### **Ensure portfolio structuring supports investment objectives**

Focus on high conviction alpha strategies or those that truly drive diversification

### **Core market beta exposures can be sourced in a low cost manner**

Market inertia towards passive is unlikely to moderate in the coming years



# Private Wealth



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- **Combine best practices from rigorous research processes with the flexibility inherent in Private Wealth portfolios**
- **Capitalize on broad market trends identified by the Investment Strategy group**
- **Leverage opportunities for broad client base, where appropriate**
- **Current Initiatives**

Tax Driven Strategies

Direct Investments

Discovery Platform

- **Tax uncertainty could cause volatility in certain asset classes in the short term**
  - Buying, selling and arbitrage opportunities
- **Determine strategy as tax policy becomes more clear**
- **Potential opportunities may include**
  - Refreshing portfolios to take advantage of lower taxes on gain realizations
  - Changes in the municipal market if Private-Public Partnerships gain momentum
  - Potential for more domestic M&A if companies are incentivized to repatriate offshore cash holdings
- **Detailed work on tax characteristics of hedge funds underway**

## Direct Investment Framework

- **Framework for identifying direct investment or co-investment partners**
  - Identifying and evaluating entities involved in direct investments
  - Determining alignment of interest and risk tolerances with those of our clients
- **Private direct investments and co-investments provide an interesting opportunity**
  - Long-term investments
  - Higher return potential (as well as higher risk)

### Survey: Enhancing Performance with Direct Investments

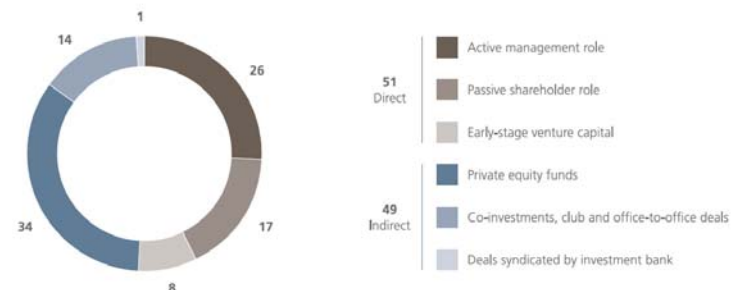
#### Do you currently engage in direct investing?



Source: Family Office Exchange  
FOX Trends and Insights, January 18, 2017

### Private Equity Allocations

Fig 2.1. Private equity allocations  
% of portfolio share, private equity holdings only



Source: UBS/Campden Research  
The Global Family Office Report 2016

- **What is the Discovery Platform?**
  - Distinct framework for manager due diligence
  - Allows NEPC to more quickly identify unique opportunities
  - Appropriate for certain clients willing to take additional risks
- **What types of strategies would be included on the Discovery Platform?**
  - Unique, emerging, or minimal coverage ideas
  - Higher returning strategies
  - Higher potential operational or investment risks



## Your Questions

While we answer your questions, we encourage you to read about our other upcoming events and NEPC Conference Presentations:

**NEPC's 22nd Annual Investment Conference:** Save the date! The conference will be held at the InterContinental hotel in Boston on May 9-10, 2017. Stay tuned for additional details in the coming months.

**Lenia Ascenso**, Director of Discretionary Services, will be speaking at the Annual ICIO Outsourcing Solutions Conference for Institutional Investors, Consultants and Money Managers on February 23, 2017 in Stamford, CT.

**Scott Perry**, CAIA, Partner, will be speaking at the Responsible Investment Forum on a panel "Impactful Ways to Approach ESG as an Asset Owner" on March 7-8, 2017 in New York.

**Kristine Pelletier**, Senior Consultant, will be speaking at the Opal Annual Impact Investment Forum on the panel "Breaking Down ESG Strategies and SRI Strategies" on April 23-25, 2017 in Boca Raton, Florida.

**\*\*To see more updates and NEPC publications, please visit the Insights section of our website: <http://www.nepc.com/research/>**



- **Past performance is no guarantee of future results.**
- **Information on market indices was provided by sources external to NEPC. While NEPC has exercised reasonable professional care in preparing this report, we cannot guarantee the accuracy of all source information contained within.**
- **The goal of this report is to provide a basis for substantiating asset allocation recommendations.**
- **All investments carry some level of risk. Diversification and other asset allocation techniques do not ensure profit or protect against losses.**
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