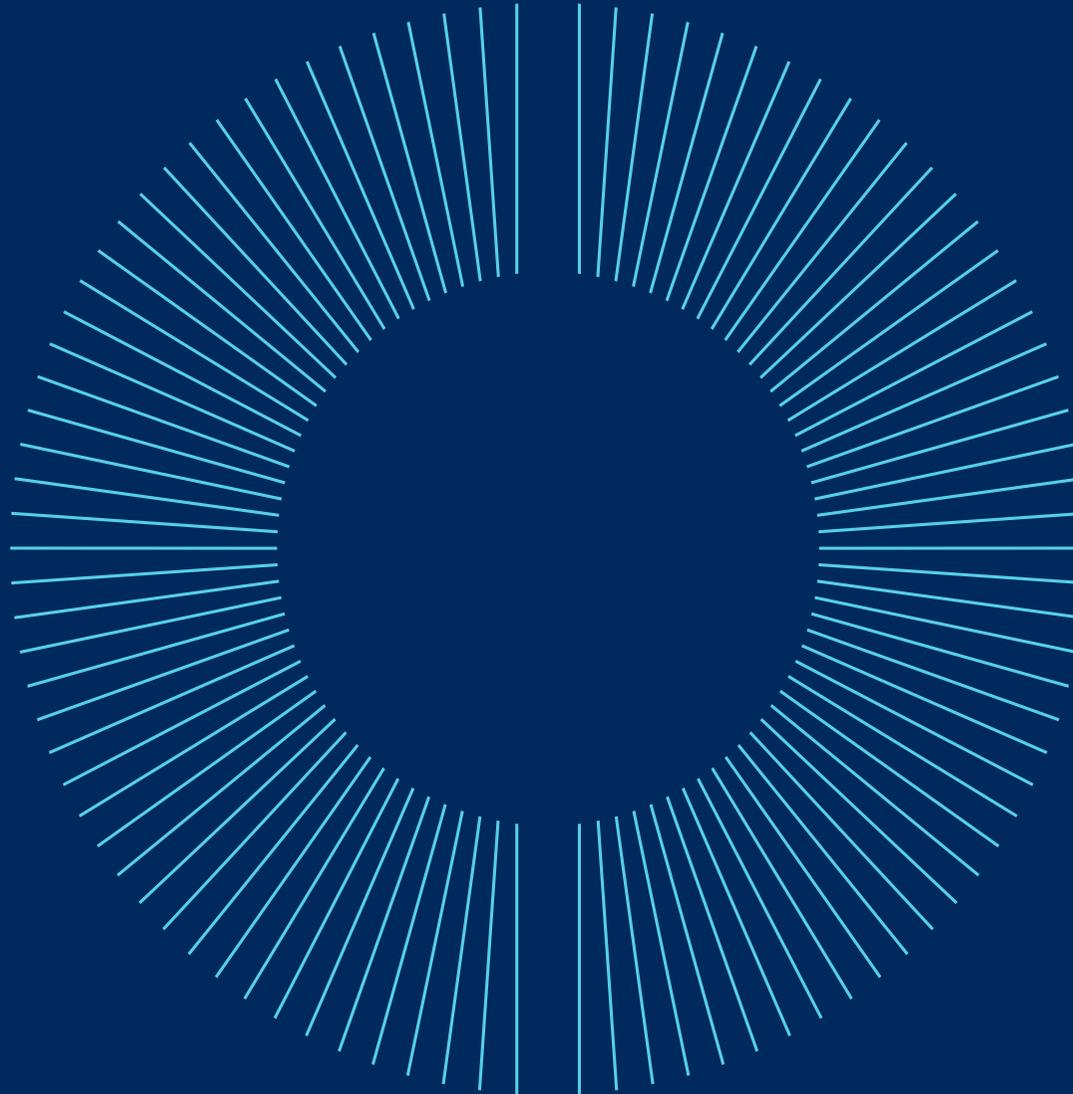


Schroders

Institutional Investor Study 2019

Geopolitics and investor
expectations



Marketing material for professional
investors and advisers only

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Executive summary

Schroders' third annual Institutional Investor Study

This Study analyses the investment perspectives of 650 institutional investors, collectively responsible for \$25.4 trillion in assets and from 20 locations across the world. The Study provides a snapshot of some of the world's largest investors' key areas of focus and concern including the macroeconomic and geopolitical climate, return expectations, asset allocation and attitudes to private assets and sustainable investing.



650

institutional
respondents



20

different
locations



\$25.4tn

assets
under management

Geopolitical turbulence and the threat of a global economic slowdown are seen as the most important influences on a portfolio's investment performance for the next 12 months. Since our inaugural Study in 2017, we have seen investors become more concerned about how world events are affecting growth (32% in 2017 vs. 52% in 2019). This is also evidenced by a steady decline in investors believing that stronger economic growth will shape portfolio performance (40% in 2017 vs. 34% in 2019).

Although geopolitical risks are a major concern, **annual return expectations have remained steady**, with North American investors still bullish in contrast to their European counterparts. Investors in Asia-Pacific are the most optimistic this year with 13% forecasting average annual returns above 10% for the next five years.

However, the most important **investment objective for investors for the next 12 months is meeting income and yield requirements (66%)**. Capital preservation and generating high risk-adjusted returns rank second and third, illustrating how institutions are looking to more defensive assets to de-risk portfolios during heightened geopolitical uncertainty.

The need for innovative, customised solutions and a broader tool kit has become increasingly important for institutional investors. **71% have indicated they are now comfortable adopting new financial instruments or asset classes** – demonstrating that investors are open to more specialist and targeted solutions tailored to their specific needs and goals.

Institutions also think their needs cannot just be met through pooled or commingled products or strategies. **53% say there is a greater need for customised or bespoke solutions because off-the-shelf funds are failing to meet their organisation's financial objectives.**

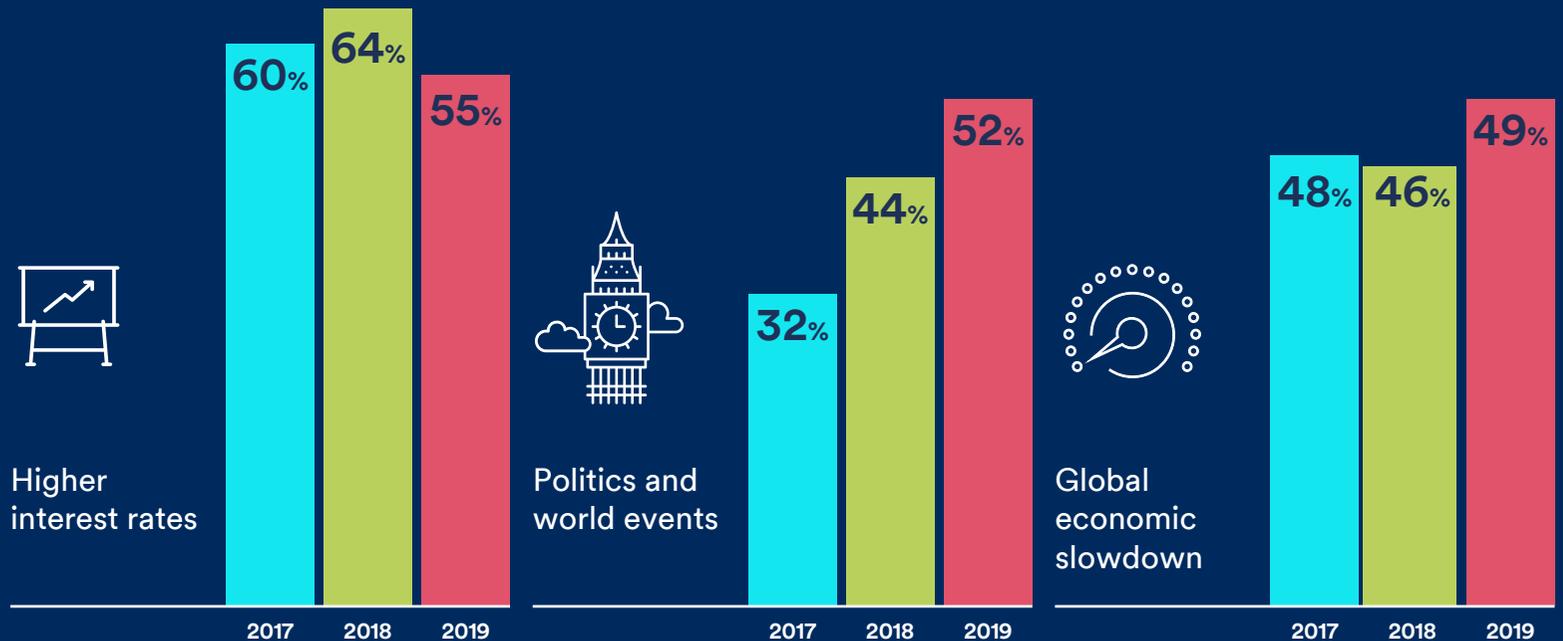
Portfolio performance

Geopolitical concerns dominate the investment landscape

Since our inaugural study in 2017, we have seen investors become more concerned about the effects of politics and world events on their portfolio performance. Geopolitical risk worries have increased from 32% in 2017 and 44% in 2018 to 52% in 2019. This is likely to reflect the ongoing uncertainty surrounding global events like the US-China trade war and Brexit.

In addition, a global economic slowdown (49% vs. 46% in 2018) is expected to have a high influence on portfolios and is considered the most concerning factor overall (37% vs. 27% in 2018).

In contrast, factors previously thought to be particularly influential – such as higher interest rates, monetary policy tapering, regulation, oil prices and the risk of cyber attacks – have all steadily decreased in importance.



Continued overleaf

What influence do you expect the following to have on your portfolio's investment performance in the next 12 months?

Portfolio performance

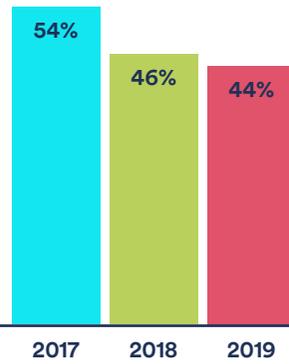
Geopolitical concerns dominate the investment landscape (continued)



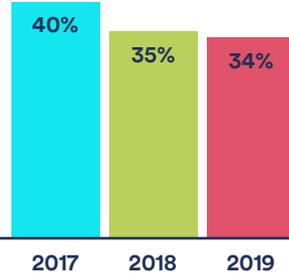
Emerging market risk



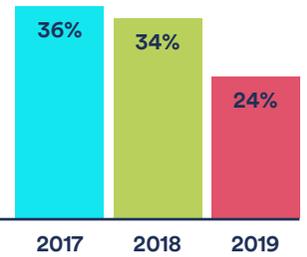
Tapering of monetary policy



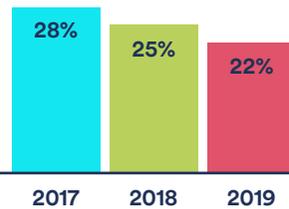
Strong economic growth



Regulation



Currency risk



Oil prices



Cyber attacks

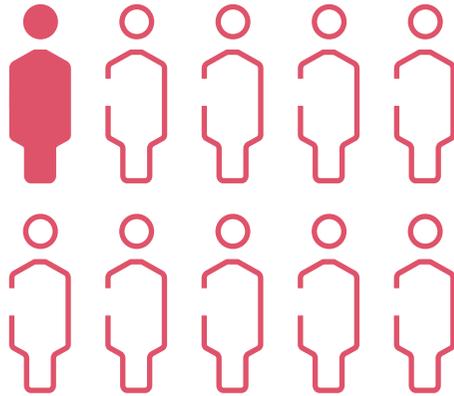


What influence do you expect the following to have on your portfolio's investment performance in the next 12 months?

Return expectations

Optimistic return expectations despite an uncertain landscape

Against this uncertain landscape, annual total return expectations over the next five years – and confidence in achieving them – have however remained relatively stable and optimistic in some regions.

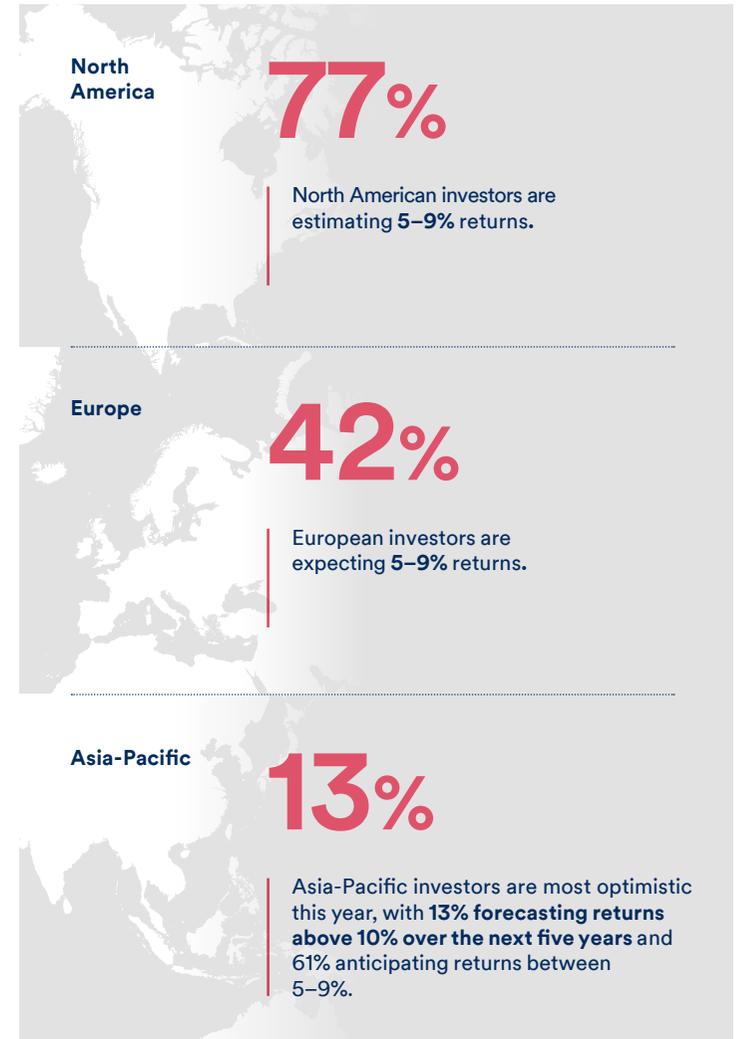


10%

Consistent with last year, **one in 10 global institutional investors** expects annual total returns above 10% over the next five years.

Similar proportions to last year also project returns between 5–9% (57% vs. 60% in 2018) and between 1–4% (28% vs. 26% in 2018).

Total return expectations across the continents are substantially different; the gap between optimistic North American investors and more cautious European investors are notably wide.



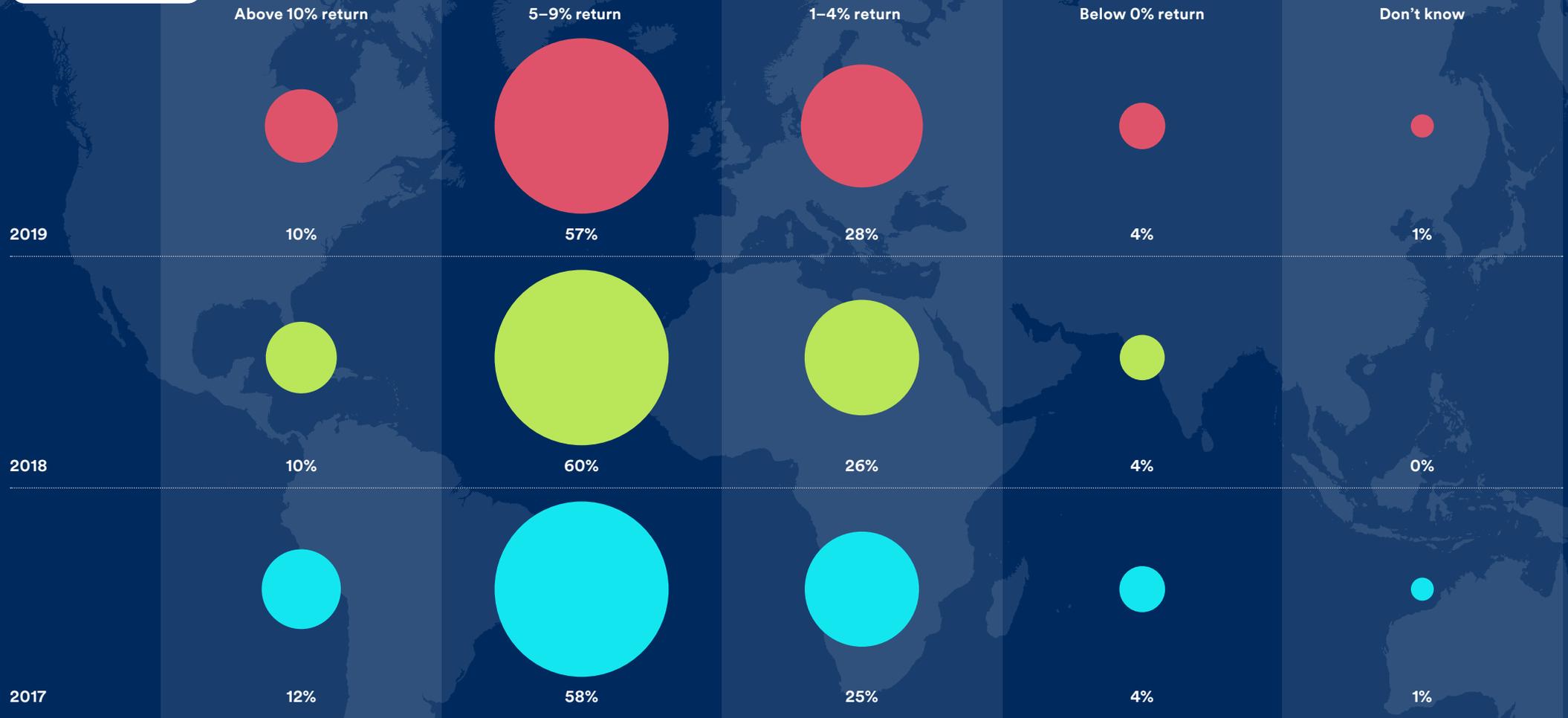
Continued overleaf

Please estimate your average annual total return expectations for your organisation's portfolio over the next five years?

Annual total return expectations

Optimistic return expectations despite an uncertain landscape (continued)

Global

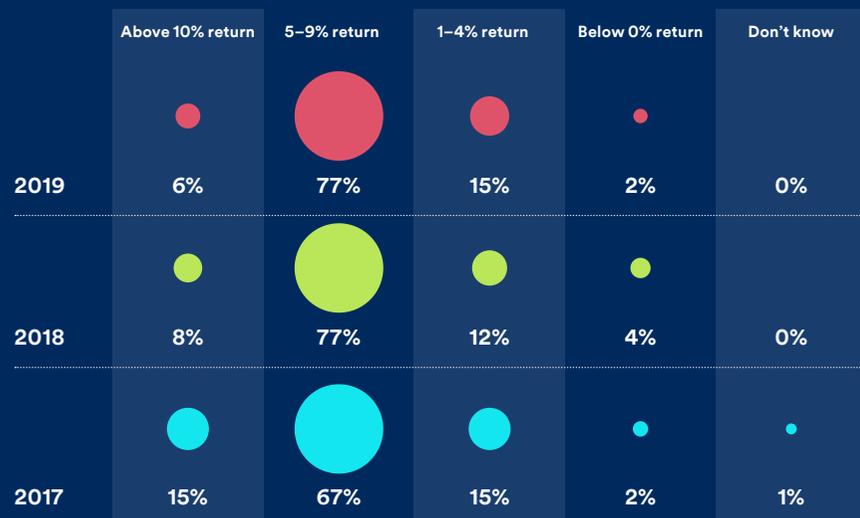


Please estimate your average annual total return expectations for your organisation's portfolio over the next five years?

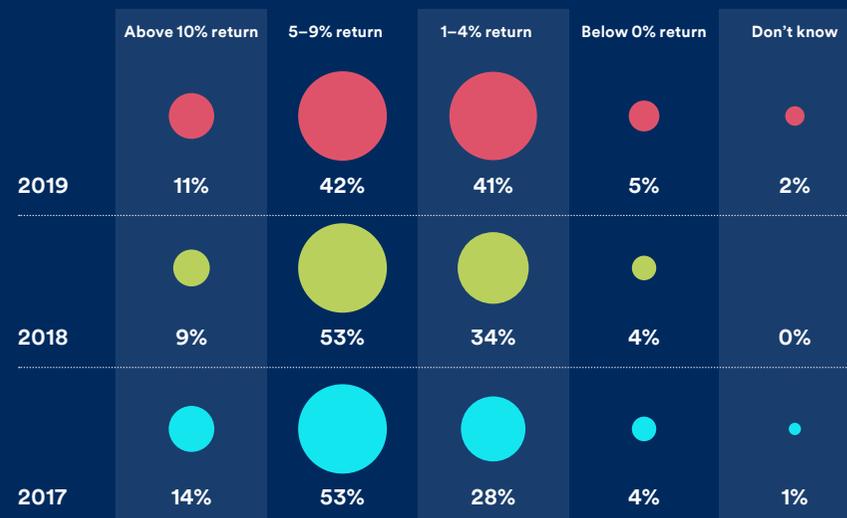
Annual total return expectations

Optimistic return expectations despite an uncertain landscape (continued)

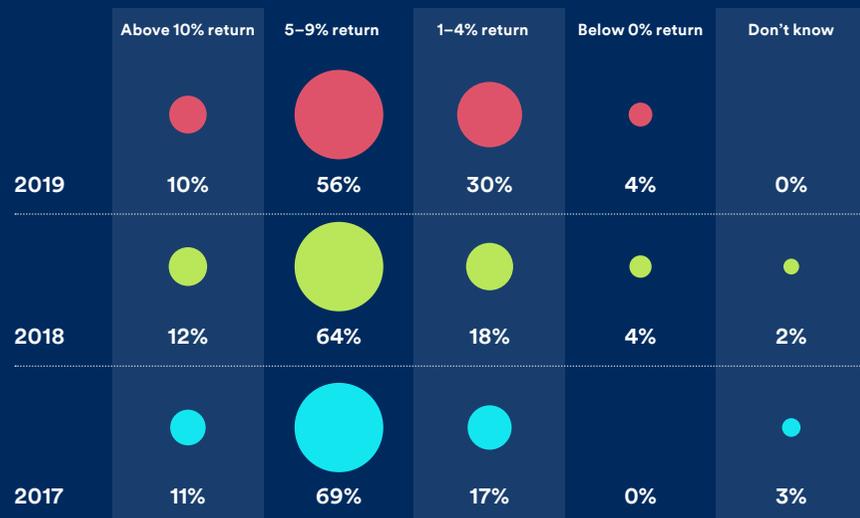
North America



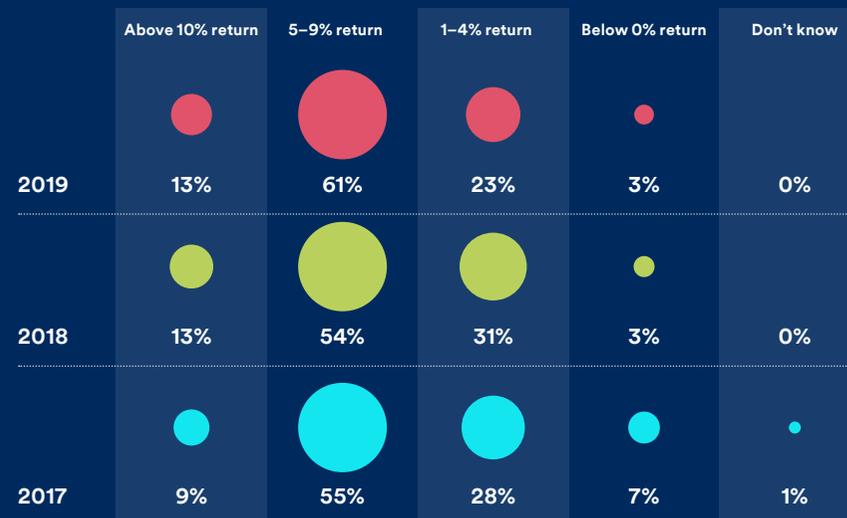
Europe



Latin America



Asia-Pacific



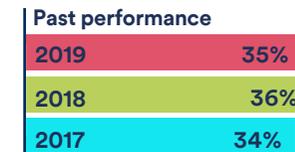
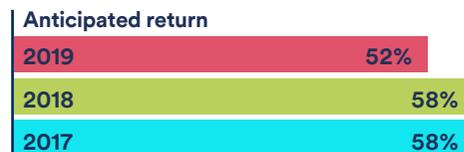
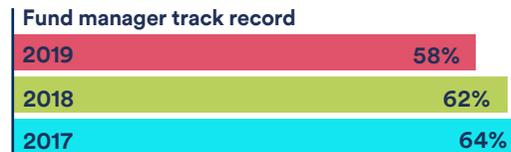
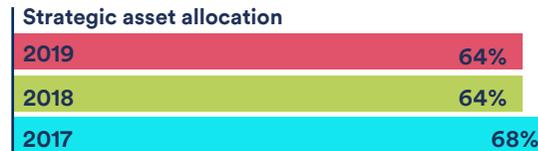
Staying strategic

Strategic asset allocation driving decision making

Although strategic asset allocation (64%) remains the primary factor influencing the decision-making of institutional investors, this has decreased in importance from 2017 (68%). Tactical asset allocation has seen a steady decrease over the last three years, with only 43% (compared to 53% in 2017) looking to make tactical tweaks to capitalise on short-term market movements.

This year, risk tolerance (54%) replaces anticipated return as the third most influential factor impacting decision-making, highlighting concerns over volatility and signs of slowing global growth. Institutions are now looking for solutions more aligned to risk profiles than desired returns, indicating an appetite for risk-managed, active investment strategies. Anticipated return (52% vs. 58% in 2018) has consequently decreased in importance as investors prioritise risk over return.

As with last year, fund manager track record (58%) is considered the second most influential decision-making factor. However, this has steadily declined in importance from 64% in 2017 and 62% in 2018.



How much influence do the following factors have on your investment decision making?

Staying strategic

Focus on long-term holding periods

The proportion of investors with a holding period of over three years has increased from 49% in 2017 to 52% in 2018 and 56% in 2019. This suggests investors are sticking to their investment principles amid market turbulence.



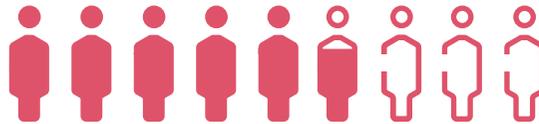
Investment goals

Generating income comes out on top

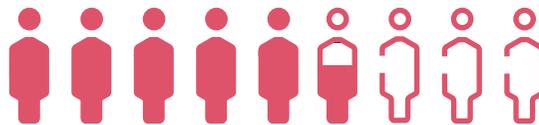
Despite the expectation for high returns in an uncertain climate, meeting income requirements (66%) has been identified as the most important investment objective for the next 12 months. Capital preservation (57%) and generating high risk-adjusted returns (55%) came in second and third.



66%
generating income

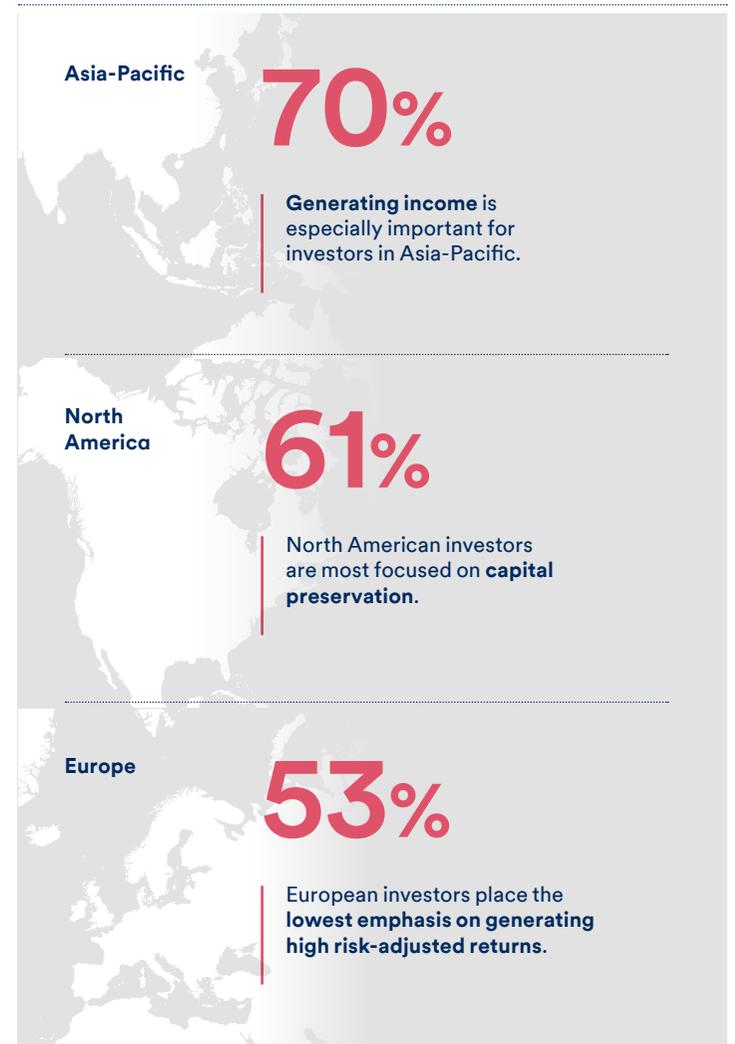


57%
capital preservation



55%
generating high risk-adjusted returns

How important are the following investment objectives for your organisation over the next 12 months?



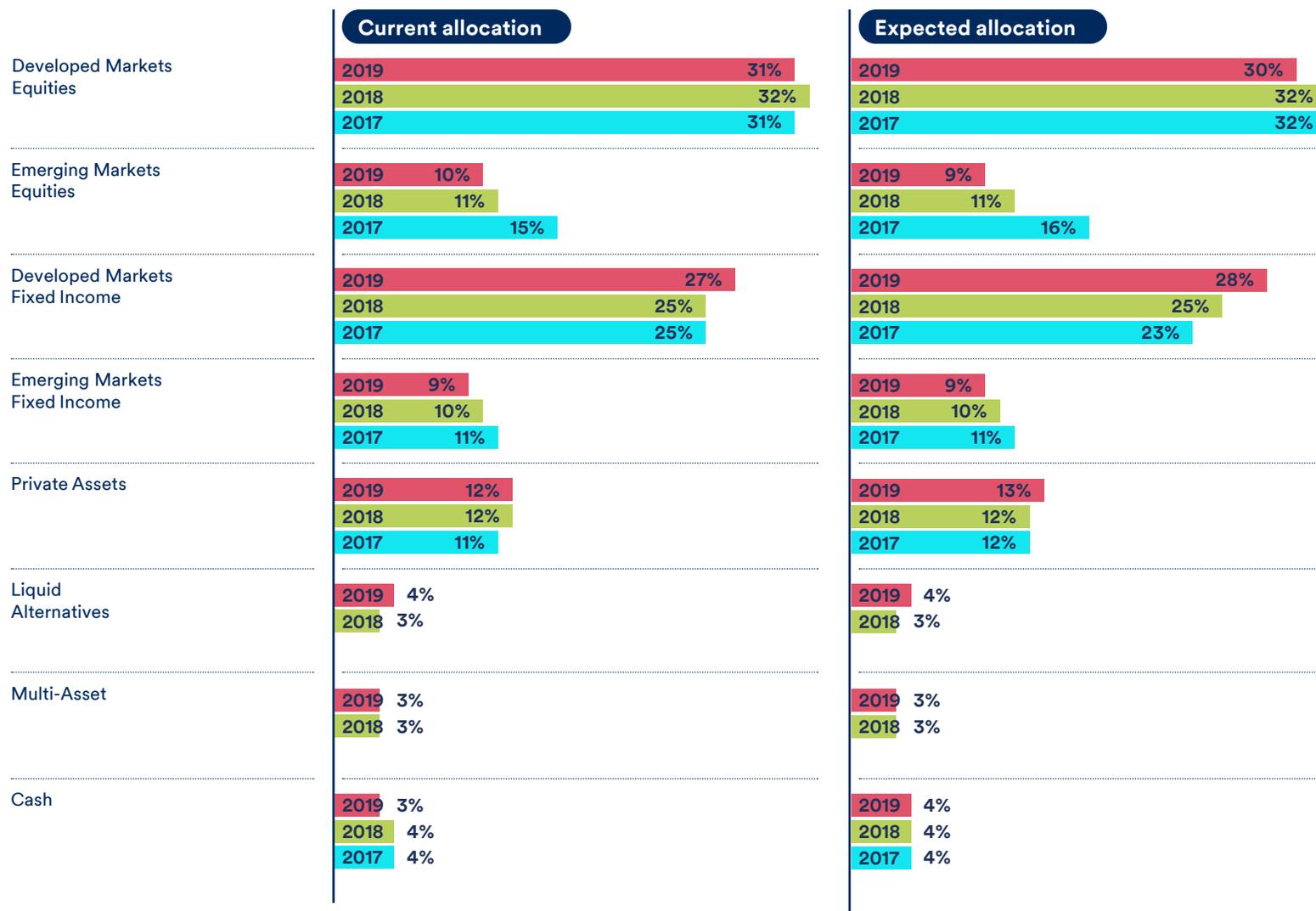
Investment goals

Increasing allocations to fixed income

The importance of income and yield is reflected in increasing allocations to fixed income. Institutional investors have increased their current allocations to developed market fixed income from 25% in 2017 and 2018 to 27% this year. Furthermore, they expect to increase allocations to 28% over the next 12 months from 23% in 2017.

Conversely, current allocations to developed market equities have decreased (31% vs. 32% in 2018) and are set to further decline to 30% over the next 12 months.

Elsewhere, defensively-minded investors are steering clear of emerging markets on the back of recent volatility. Current allocations to emerging market equities have lowered from 15% in 2017 to 10% in 2019, and this has also been seen in expected allocations for the next 12 months (16% in 2017 to 9% in 2019). This likely reflects heightened turbulence and currency volatility emanating from the escalating trade war between the US and China.



Approximately what percentage of your institution's portfolio is currently allocated to each of the following asset classes? And what allocation do you expect over the next 12 months?

Growing appetite for innovation

The quest for new, customised solutions

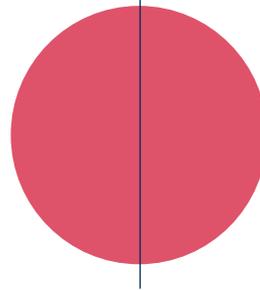
Institutional investors are reaching out for customised solutions and a broader tool kit to maintain meet their income requirements.

Seven in 10 (71% vs. 69% in 2018) say they are comfortable adopting new financial instruments or asset classes – indicating conventional approaches are perhaps not satisfying the demands of today’s institutional investors.

Institutions also think their needs cannot just be met through pooled or commingled products or strategies. 53% say there is greater need for customised or bespoke products.

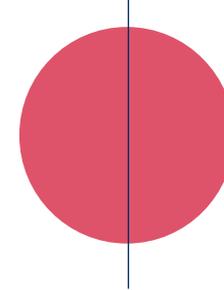
2019

71%



My organisation is comfortable with adopting new financial instruments or assets classes

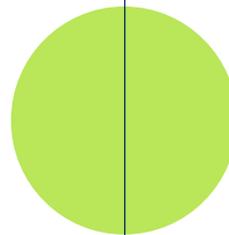
53%



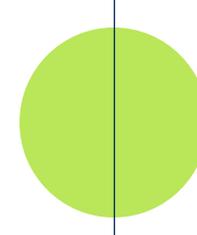
There is a greater need for customised or bespoke products since 'off the shelf' funds are not sufficient to meet my organisation's financial objectives

2018

69%



50%



How strongly do you agree or disagree with the following statements?
(% Strongly Agree + Agree)

Growing appetite for innovation

De-risking through LDI

This drive towards solutions is further evidenced by the global importance attached to Liability Driven Investment (LDI) i.e. a strategy that looks to purchase assets, such as bonds, to construct an investment strategy that closely matches the behaviour of future liabilities – often referred to as ‘LDI assets’ or ‘matching assets’.

Institutional investors are attaching more importance to LDI. About half of global investors (48%) say LDI is crucial to managing their investments – up from 40% in 2017 and 45% in 2018. Regionally, LDI plays the most important role for investors in Europe, where over half (51%) say it is crucial to managing investments. North American investors (49%) also attach a strong weight to LDI.

Nearly four in 10 investors (36%) say meeting cashflow requirements has become a concern over the past year, and one third (33%) of global investors say the pressure of meeting liabilities is making them take on more risk than they would have preferred.

How strongly do you agree or disagree with the following statements?
(Liability Driven Investment is crucial to managing our investments)



Risk management strategies

The dominance of diversification

Diversification across asset class and geographies, cited by 82% of institutional investors, is the preferred risk management strategy for the third consecutive year. The diversification desire is most pronounced among investors in North America (86%) and Europe (85%).

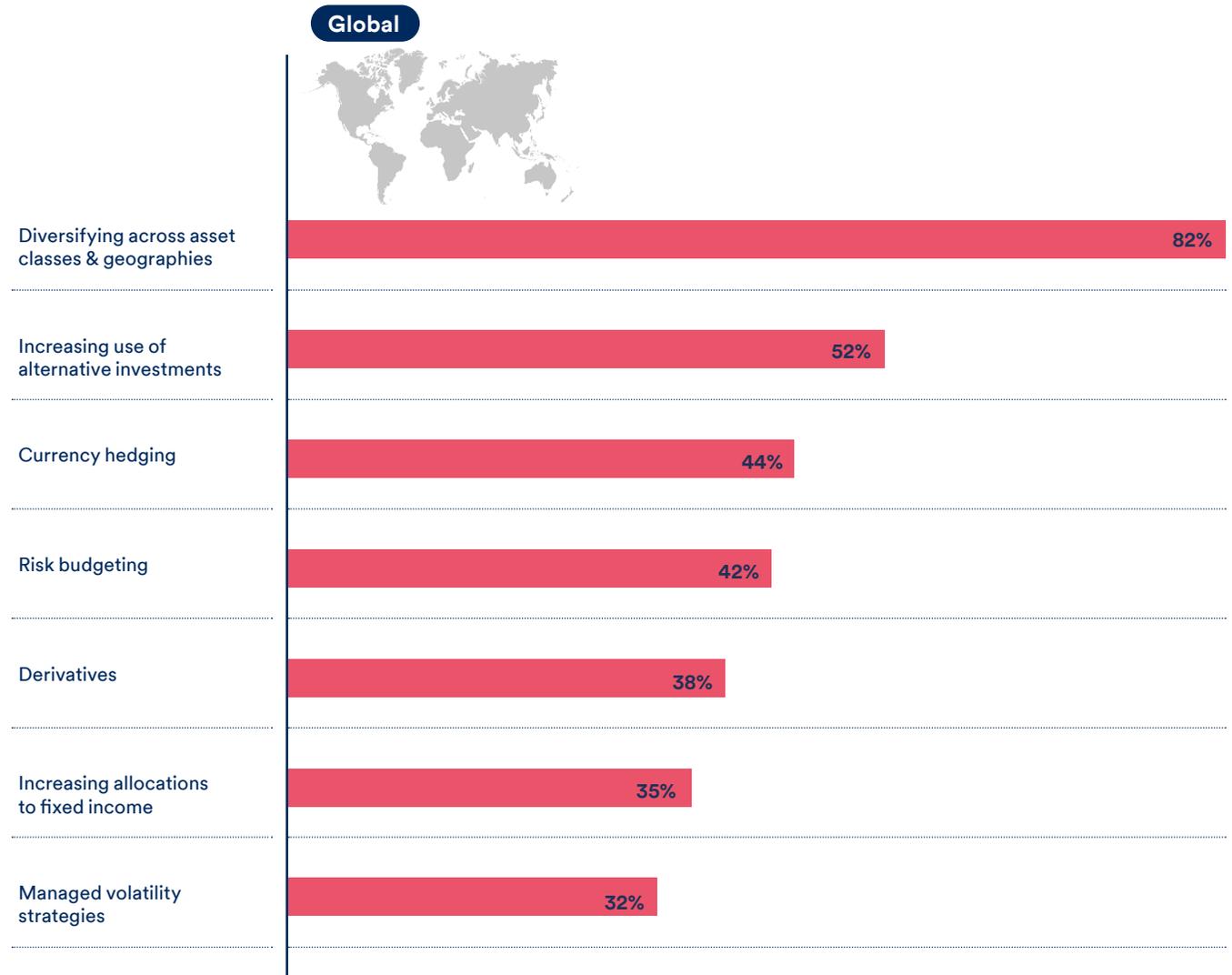
The need to achieve diversification is further underscored by the finding that more than half of investors (52%) are increasingly using alternative investments to manage risk within portfolios. Investors in North America (61%) are most likely to turn to alternatives to manage risk, in comparison to 20% of Latin American investors.

Currency hedging (44%) is the third most popular risk management strategy, followed by risk budgeting (42%) and derivatives (38%).

Increased allocations to fixed income is particularly important for Latin American investors (60%) for managing risk, in comparison to 27% in Europe and 35% in Asia-Pacific.

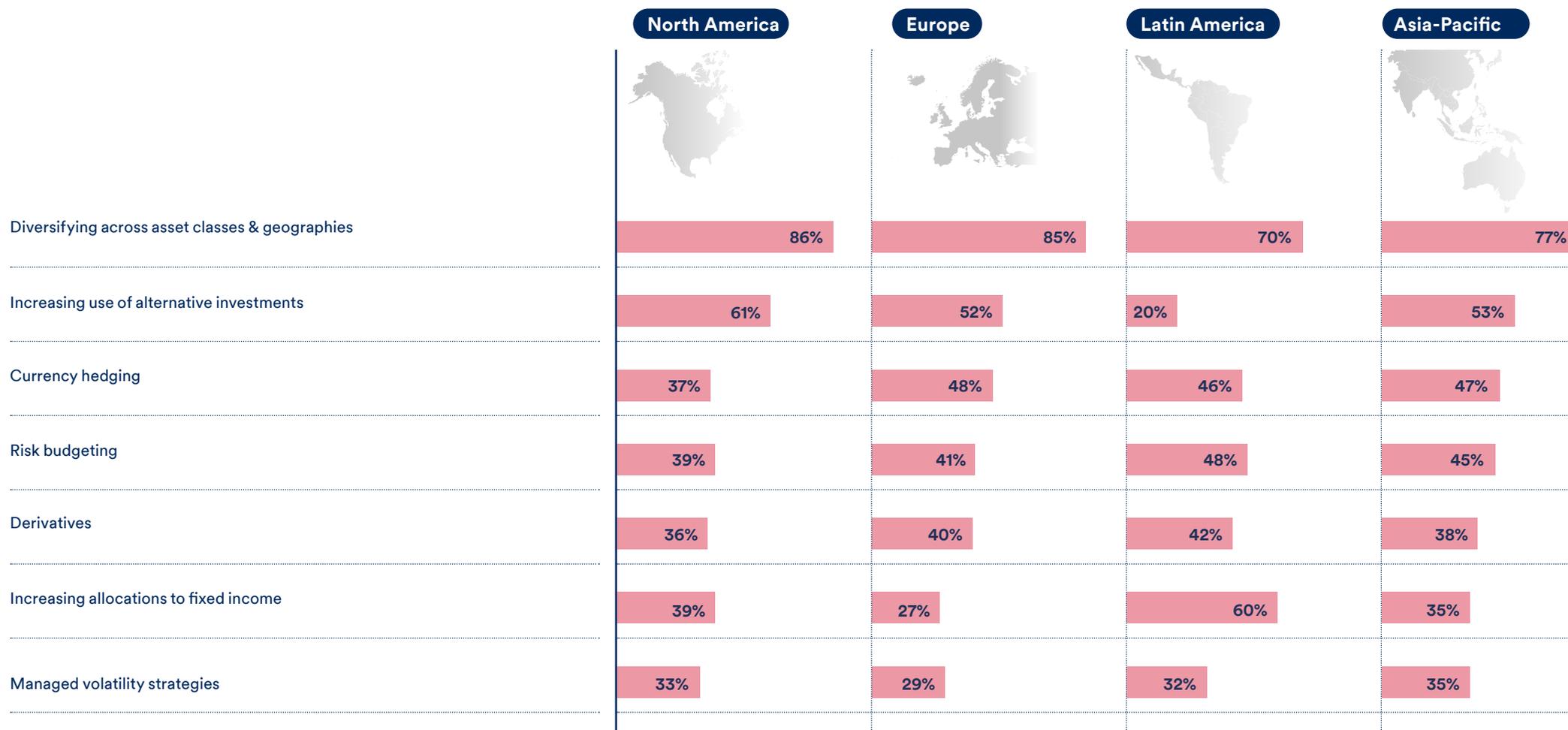
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Across all your investments, which of the following strategies do you use to manage risk within the portfolio?



Risk management strategies

The dominance of diversification (continued)

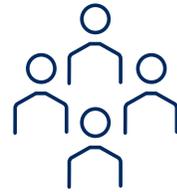


Across all your investments, which of the following strategies do you use to manage risk within the portfolio?

About the Study

Schroders commissioned CoreData to conduct the third Institutional Investor Study to analyse the world's largest investors' key areas of focus and concern including the macroeconomic and geopolitical climate, return expectations, asset allocation and attitudes to private assets and sustainable investing.

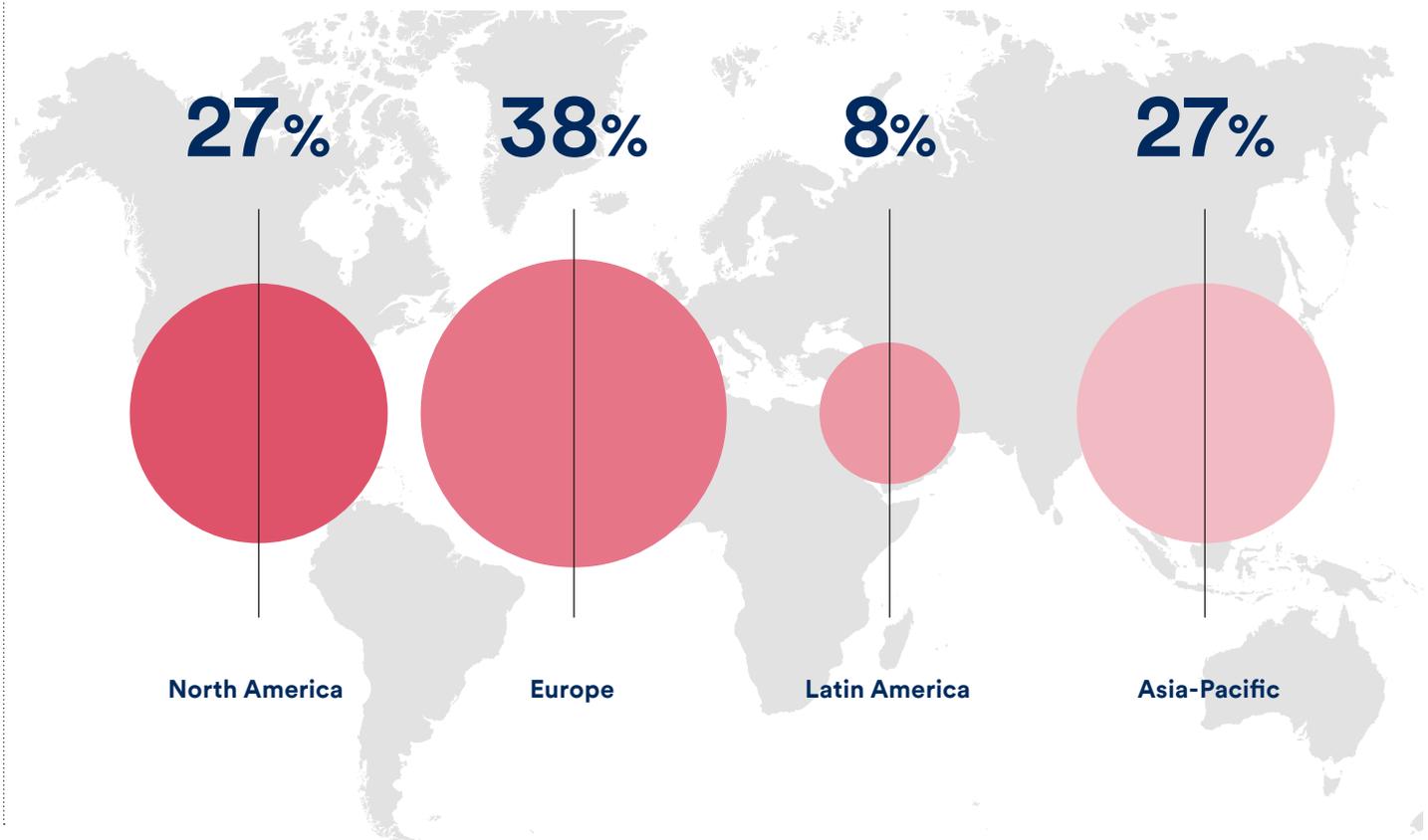
The respondent pool encompasses a spectrum of institutions, including pension funds, insurance companies, sovereign wealth funds, endowments and foundations managing \$25.4 trillion in assets. The research was carried out in May 2019. The 650 institutional respondents were split as follows: 175 in North America, 250 in Europe, 175 in Asia-Pacific and 50 in Latin America. Respondents were sourced from 20 different locations.



650
institutional respondents



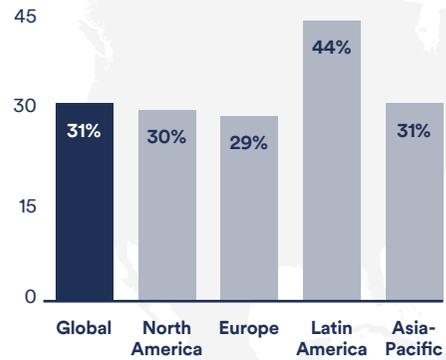
20
locations



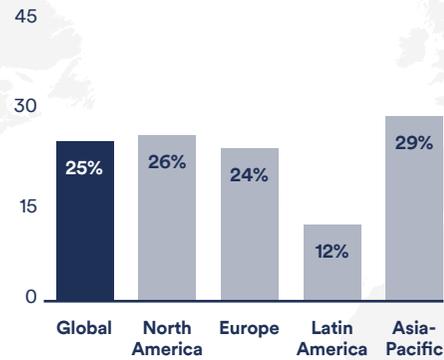
About the Study

Type of organisation

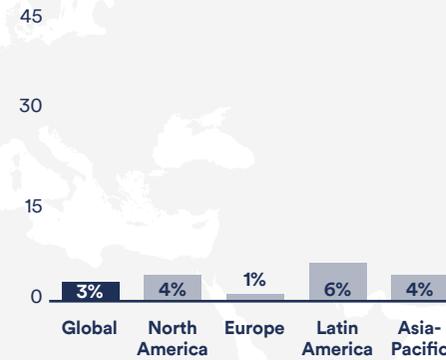
Corporate pension plan



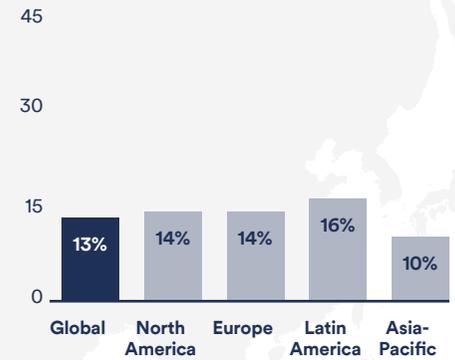
Public or government pension plan



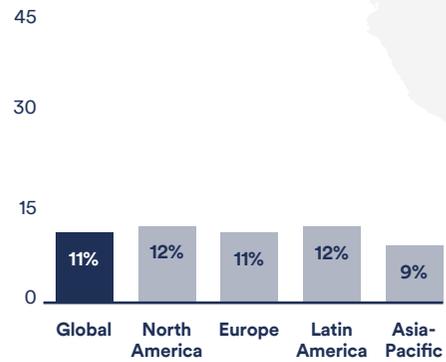
Sovereign wealth fund



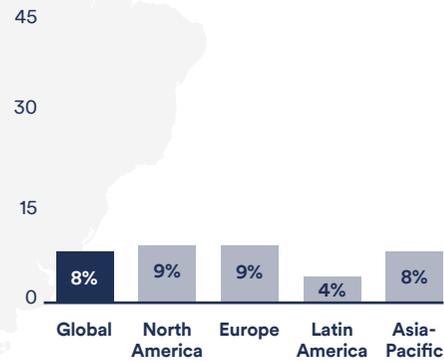
Life insurance company



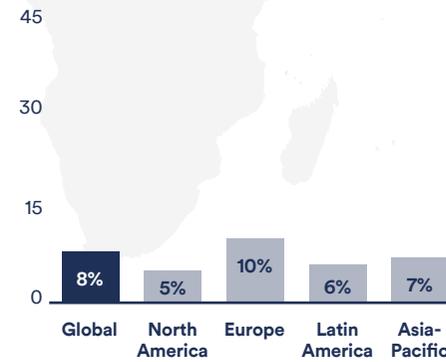
Non-Life insurance company



Endowment



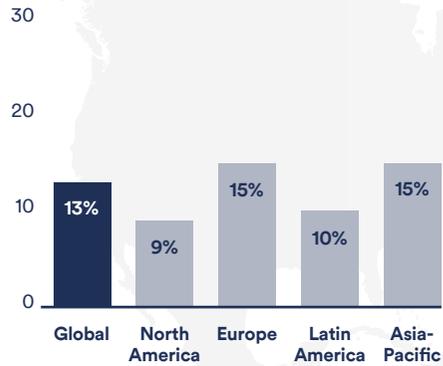
Foundation



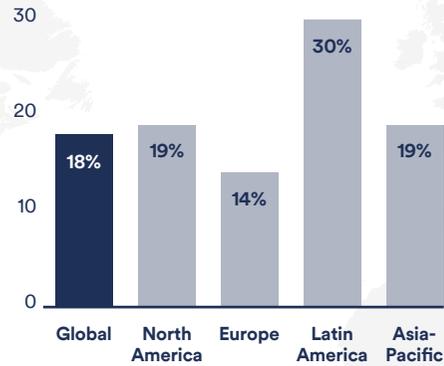
About the Study

Assets under management

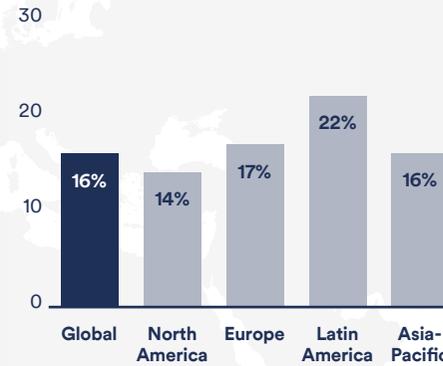
Less than \$1bn



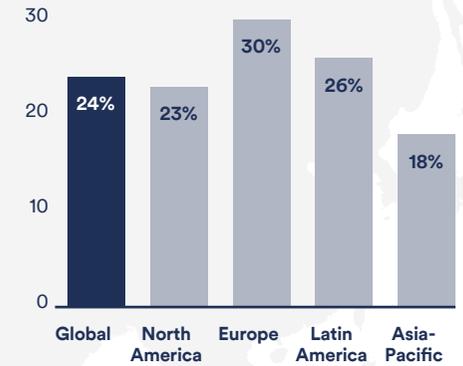
\$1bn to less than \$5bn



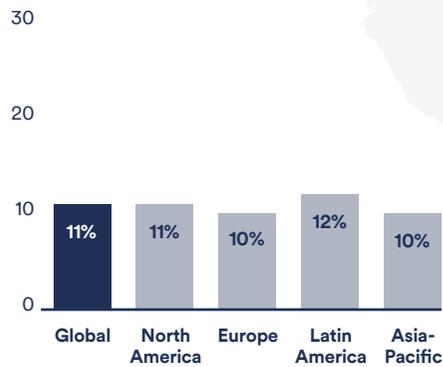
\$5bn to less than \$10bn



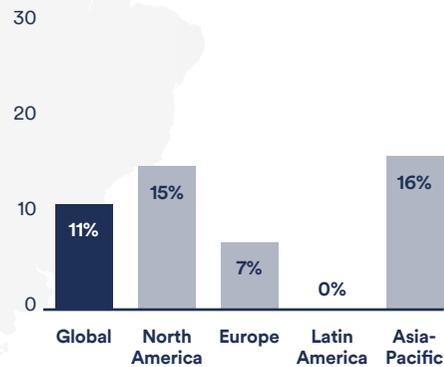
\$10bn to less than \$50bn



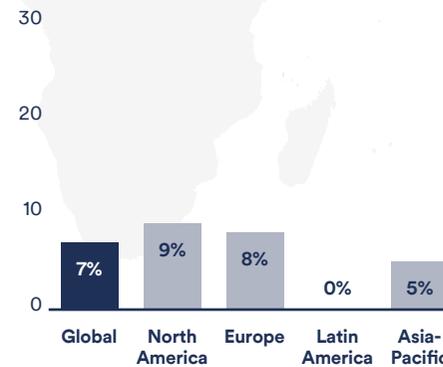
\$50bn to less than \$100bn



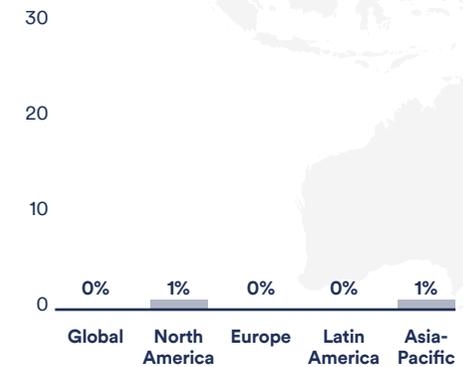
\$100bn to less than \$250bn



\$250bn to less than \$500bn



\$500bn to less than \$1tn



Schroders



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