



# GIORNATA NAZIONALE DELLA PREVIDENZA

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# Agenda

- Global economic and market background
- Asset allocation trends
- Challenges facing pension funds
- Risk and uncertainty
- Thematic investing

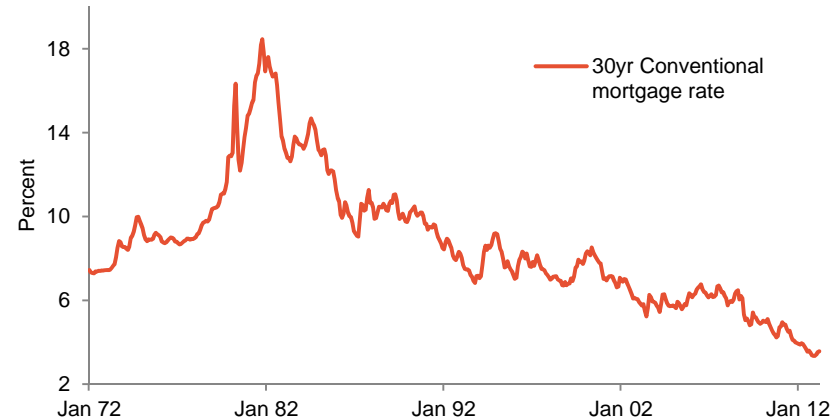
# Global economic and market background

# United States

## Strong evidence that US housing market bottomed in Q1 2012

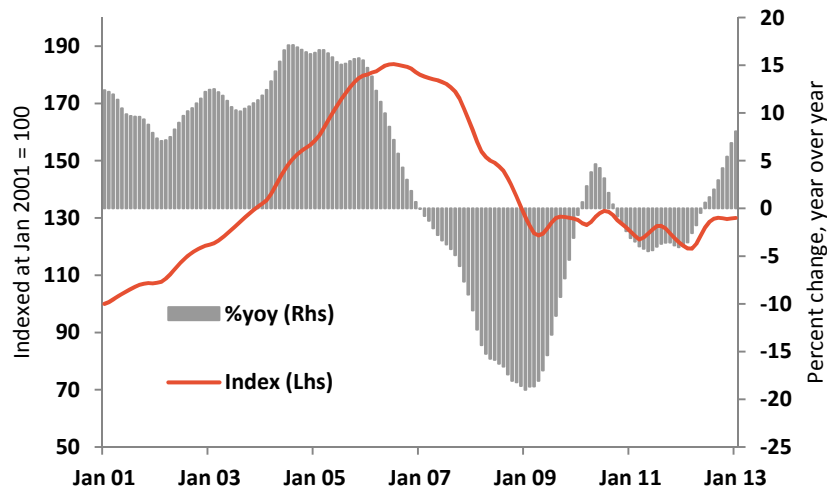
- House prices are following a sustainable upward trend.
- Near-record low mortgage rates have helped to sustain gross borrowing.
- Wider economic recovery is expected to reaffirm its improving trend over the coming quarters.

Near-record low mortgage rates have helped to sustain gross borrowings.



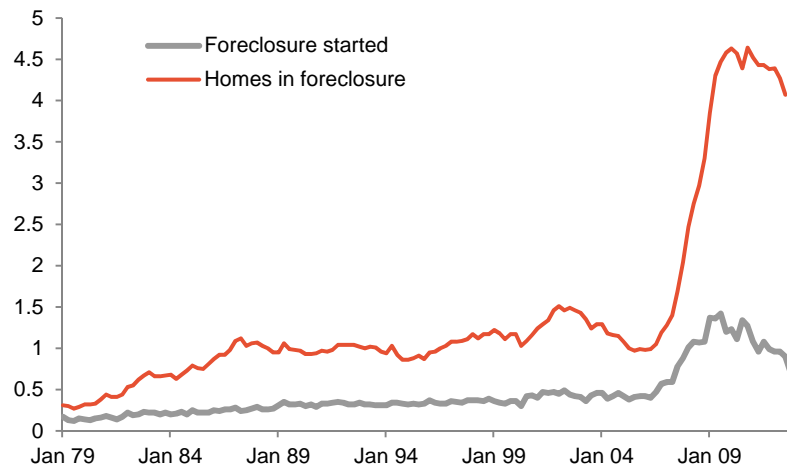
Source: Bloomberg LLP

### US house prices – Case-Shiller index



Source: Bloomberg LLP, Towers Watson

### US foreclosures have declined since peaking in 2009



Source: Bloomberg LLP

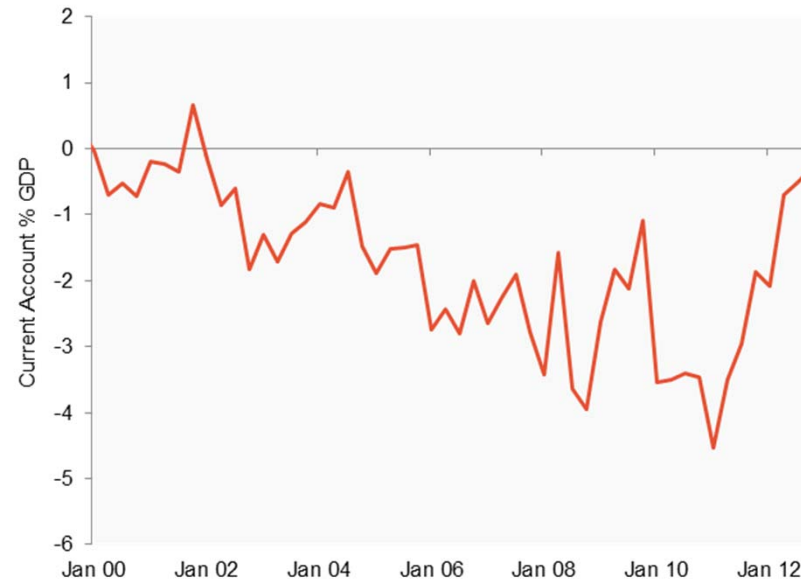
# Euro area: On a more sustainable debt path

## Funding gaps in the periphery have closed in the last six months

Spain's current account deficit has been cut to zero, primarily through a significant reduction in demand and imports



Italy's external position has experienced similar improvement

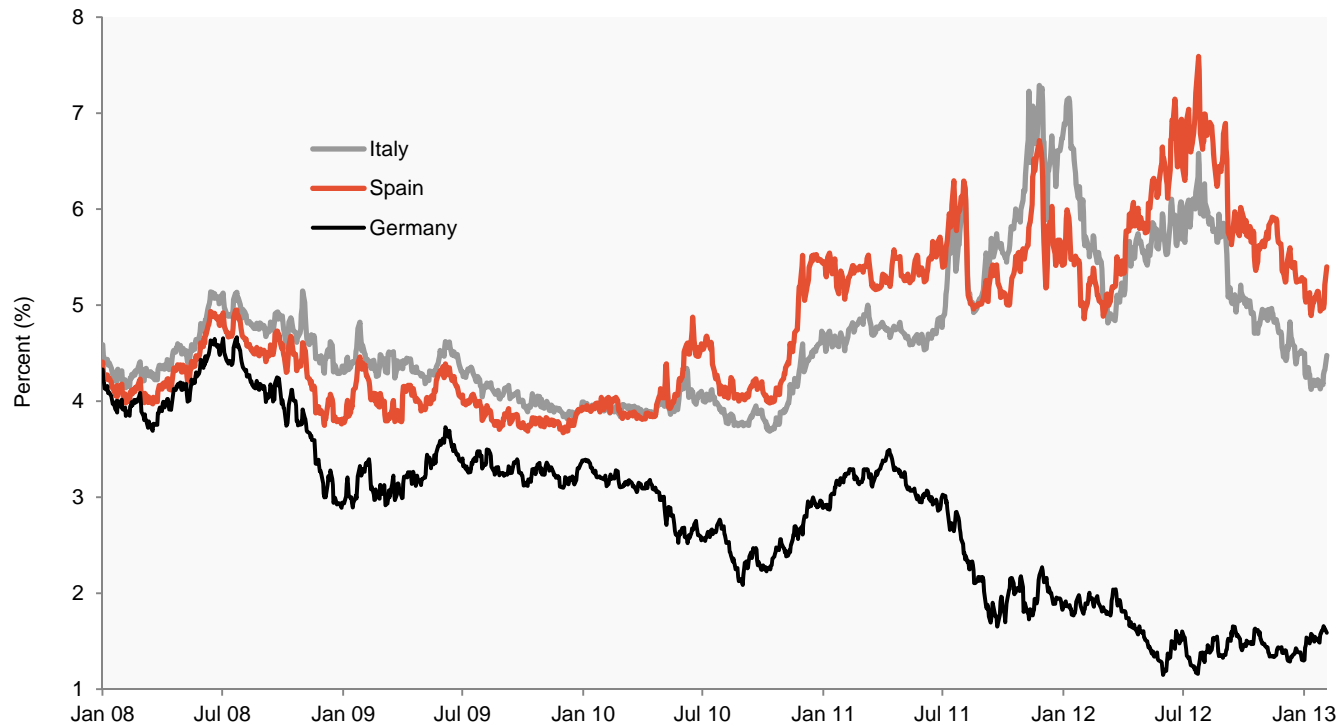


Sources: Bloomberg LP, Datastream, Towers Watson

# Euro area

Spanish and Italian debt dynamics are manageable – economic conditions will remain depressed

10-year bond yields in Italy and Spain remain too high relative to weak underlying economic conditions



Source: Bloomberg LP, Datastream, Towers Watson

# Government Bonds

Bond yields fall back below start-of year levels

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## An unchanged outlook

- Official rates are expected to be close to zero until 2015. Central bank purchases of long bonds have also depressed yields of longer maturity bonds.
  - The unwinding of such policy could result in significant bond losses over a 3-4 year horizon.
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US 10yr nominal yields fell sharply in late March/early April.



Source: Federal Reserve

# Equities

We remain positive

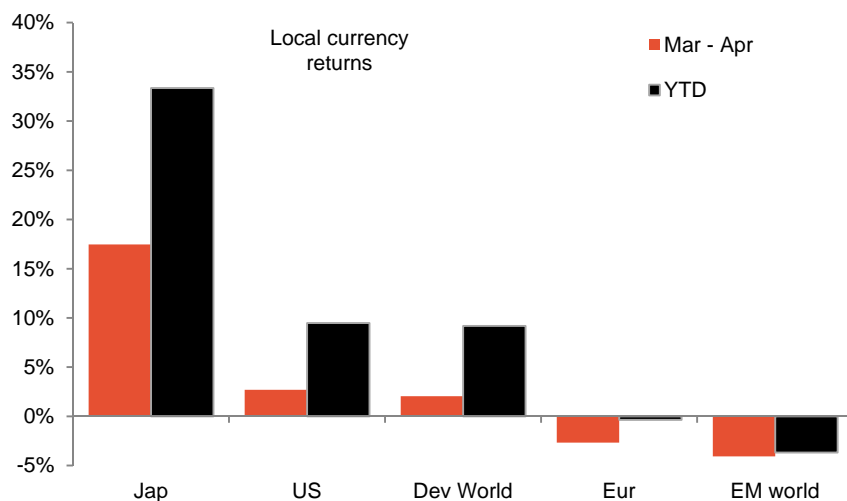
**Developed market performance strong year-to-date, emerging markets lag**

- Accommodative monetary policy in conjunction with improving economic data has continued to support equity prices year-to-date.

**Markets remain moderately attractive**

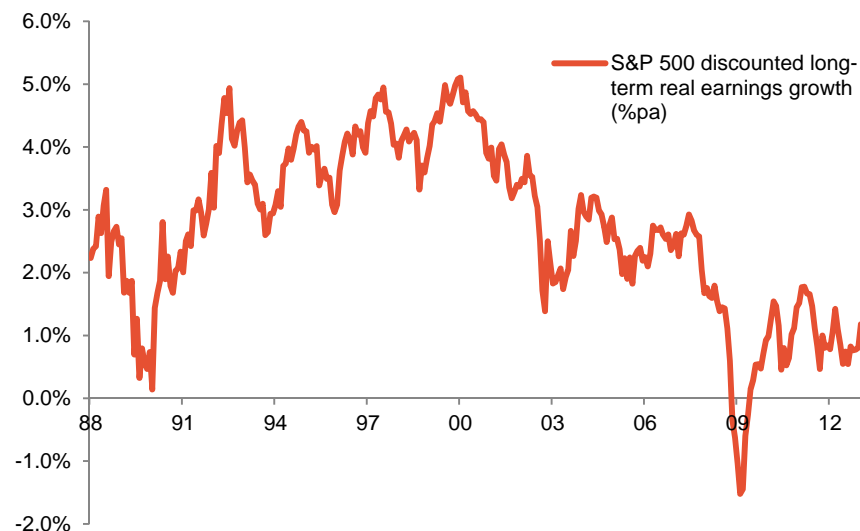
- Markets continue to price-in mediocre expectations for earnings - we think equities are reasonably attractively valued over the medium term.

**Strong developed market performance YTD, emerging markets less so**



Source: Thomson, Towers Watson

**Discounted long-term real earnings growth in the US**



Source: Thomson, Towers Watson



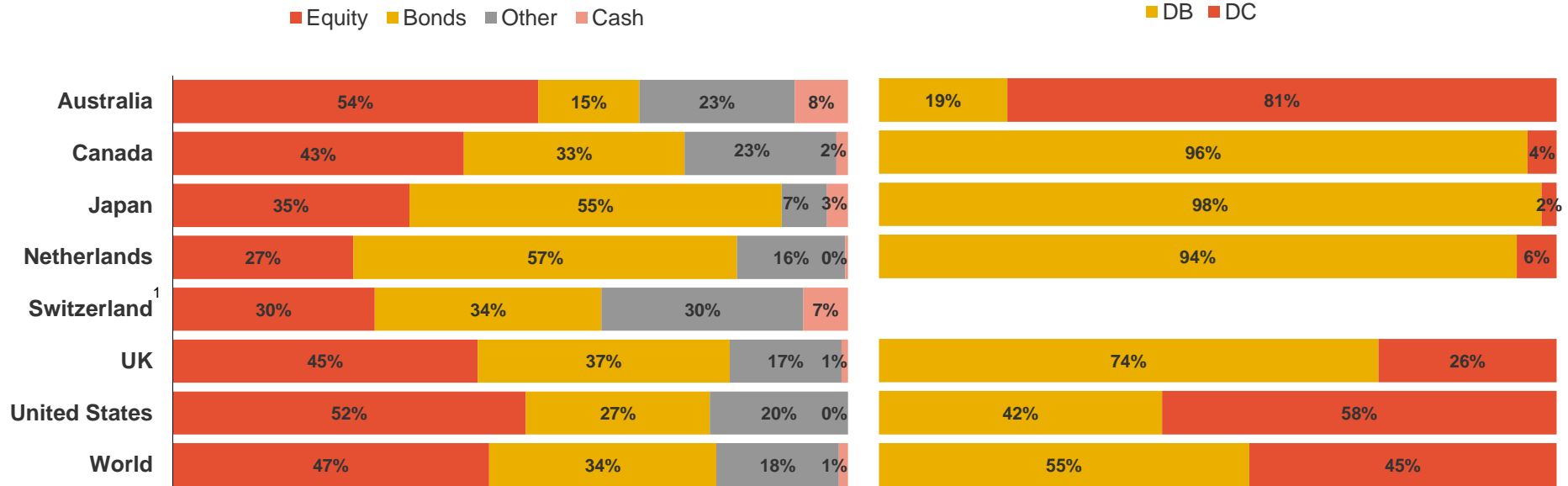
# Asset allocation trends

# Global Pension Assets Study 2013

## Key findings

### Asset allocation 2012

### DB/DC Split 2012

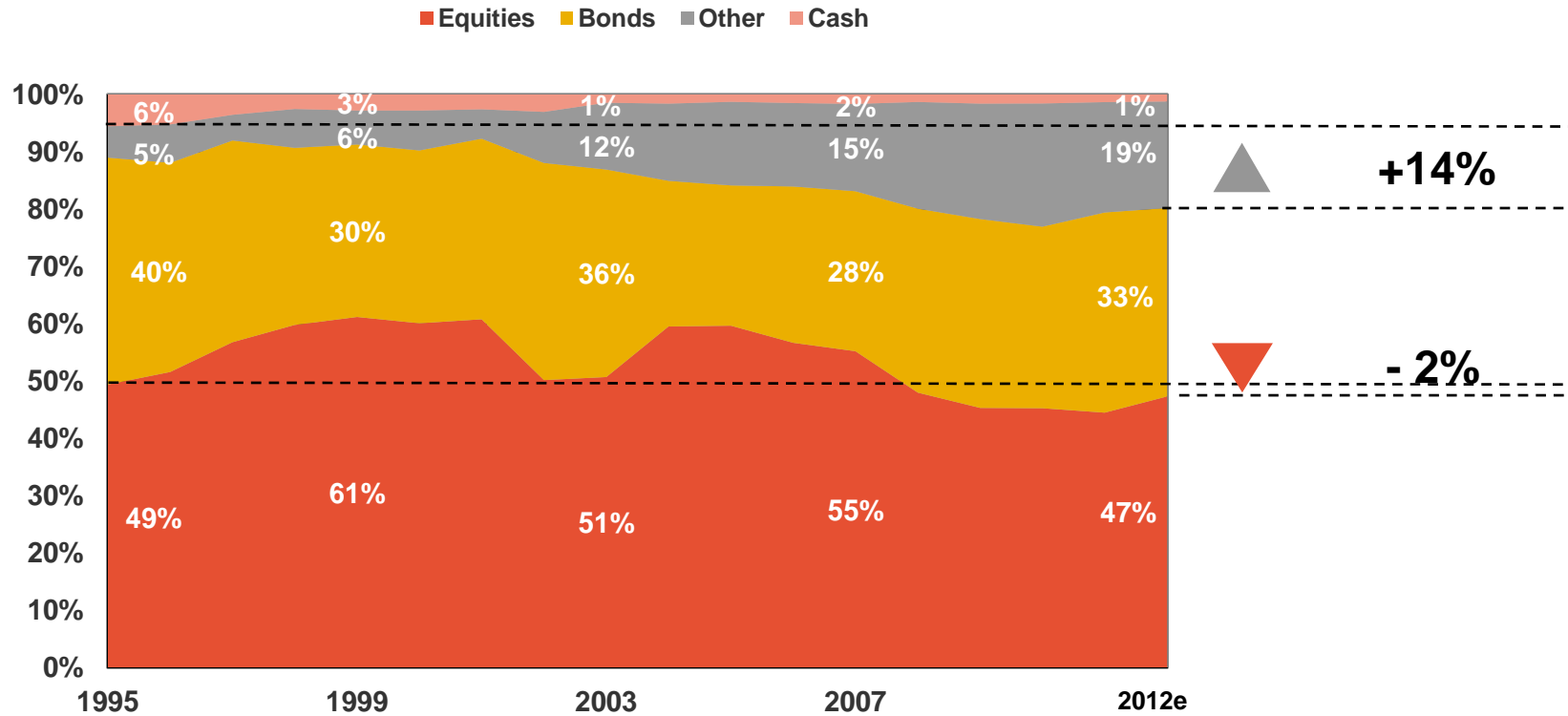


Source: Towers Watson and secondary sources

<sup>1</sup> DC assets in Switzerland are cash balance plans and are excluded from this analysis.

# Pension asset allocation

Aggregate P7 asset allocation from 1995 to 2012



Source: Towers Watson and secondary sources

# Challenges facing pension funds

## Issues facing pension funds

- Global assets now exceed \$30 trillion\*, up 80% in 10 years, but liabilities are about \$5 trillion more than this
- Pension fund strategy has moved more defensive and more diversified
  - *'40/40/20 is the new 60/40'*
- Strategy is now challenged by the credit risk of sovereign bonds
  - Doubts on the risk free safe place
  - A lack of appropriate hedging assets
  - LDI evolution hampered by low interest rate regime
- But most of all, funds need higher returns than seem likely under the new macro

**\*Source: Towers Watson 2012 Global Pension Asset Study**

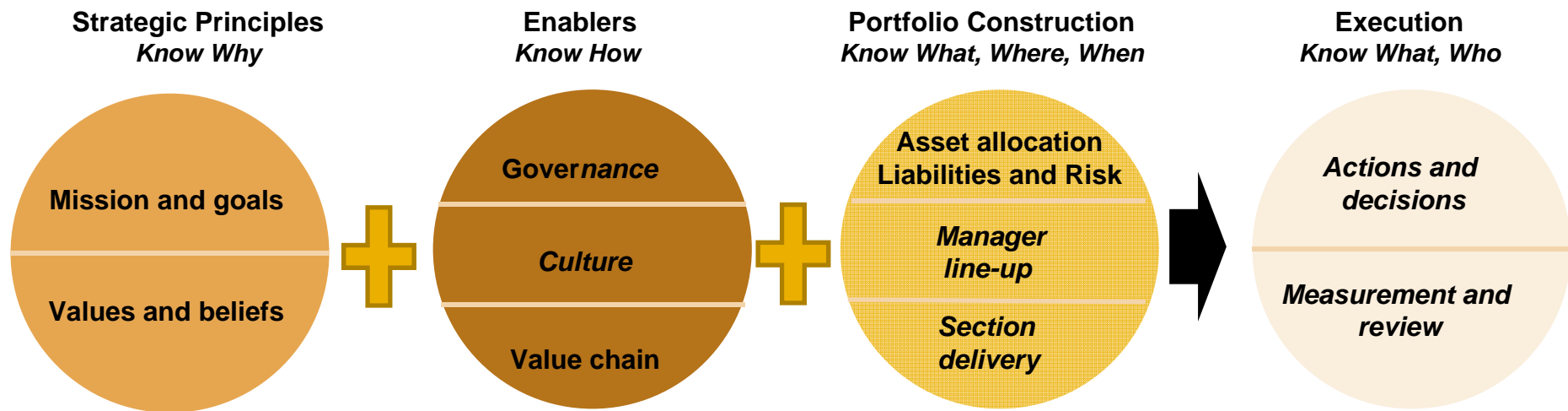
## **‘Thrifty Fifty’ - the 50 biggest and most influential long-term asset owners**

- **‘Thrifty’** = *‘wise economy in the management of money and other resources’*
- **‘Fifty’** = 50 funds all above or around \$50 billion and 50 professionals
- 33 pension funds, 14 sovereign wealth funds, 3 endowment/ foundations, totalling \$10.3 trillion
- 2012 report card:
  - Mission: Fiduciary responsibility and playing their part in wealth creation/ well-being
  - Governance: organisational effectiveness and transformational change
  - Private market integration: private markets made up to public market standards
  - Long termism: optimising sustainably to the long term, satisficing the short term

***Several reasons to study these funds’ next moves***

# Investment governance

- Organisational effectiveness concepts
- Effective Board and executive team roles
  - The product of Board and executive team should be more than the sum of parts
- Emphasis on strategic principles and enablers
- Value comes from optimising governance budget and risk budget

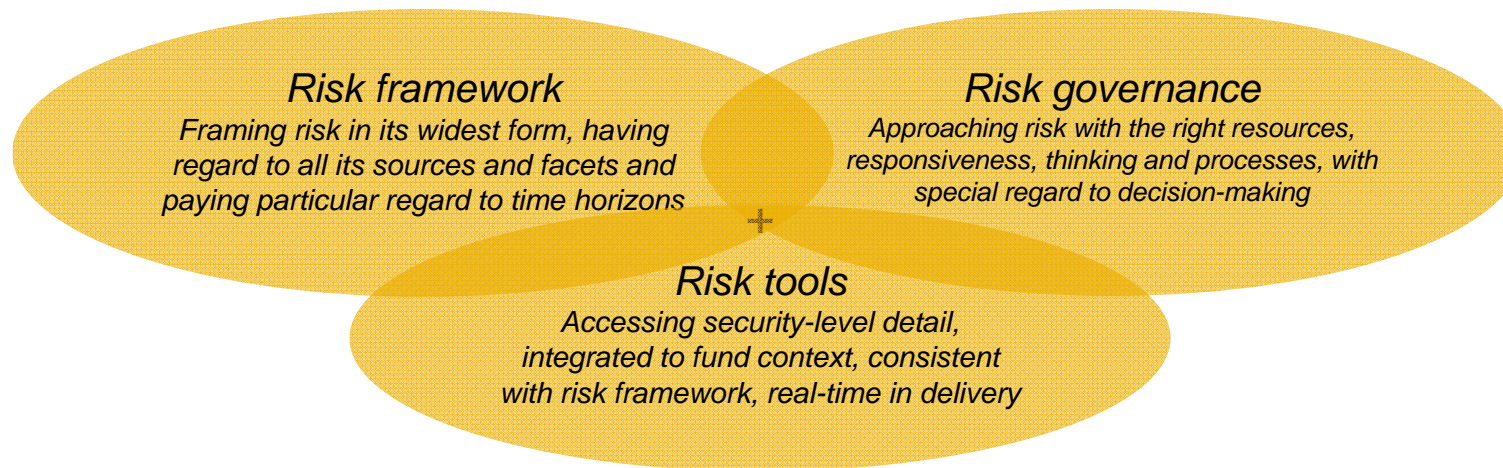


# Risk and uncertainty



## The big picture on 'risk'

- We tend to manage risk we can see and measure
  - a case of 'wrong type of snow'
- Risk is a considerable source of competitive edge for organisations
- While the tools and theory to manage risk are getting there, the problems are on the people and processes side
- Managing risk well involves combining *a strong risk framework* with *strong risk governance*, with the *effective risk tools* completing the list

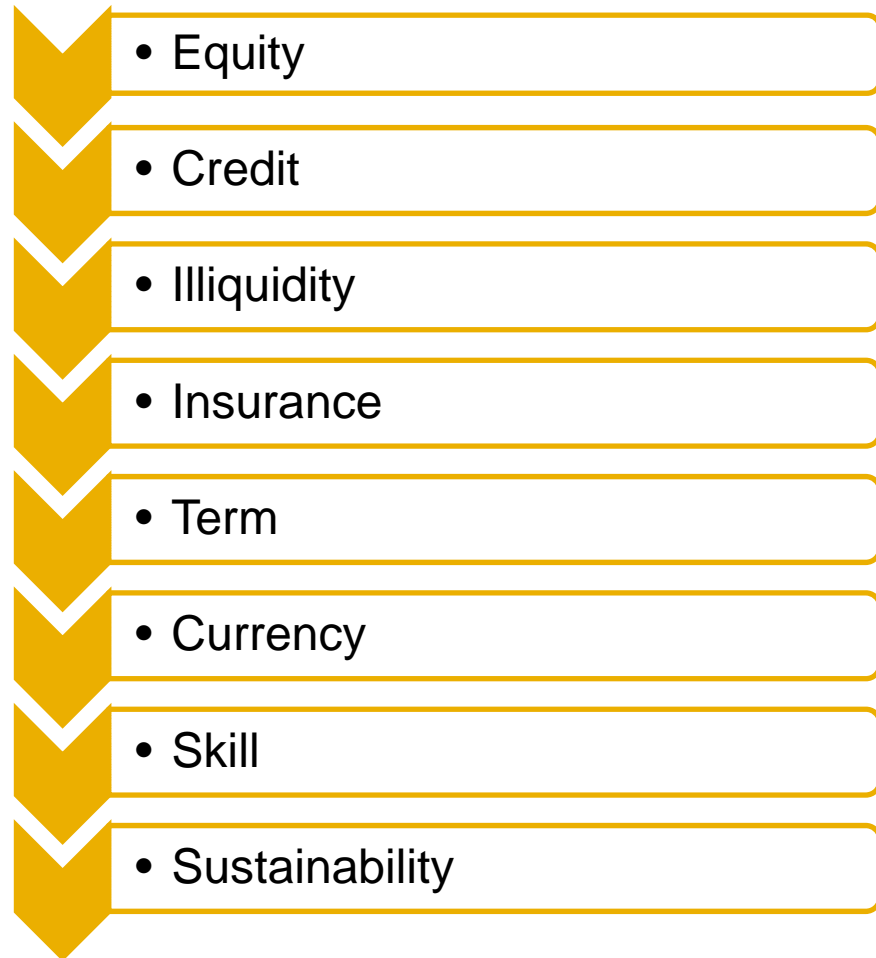


# Risk is multi-sourced



## Risk can be good as well as bad

- Funds with long-term missions need to take risk to create wealth and meet liabilities
  - Taking the right amount of the right types of risk
- Deliberate taking of risk is a major area of decision
  - Economically justifiable factors
  - Secular and temporal factors



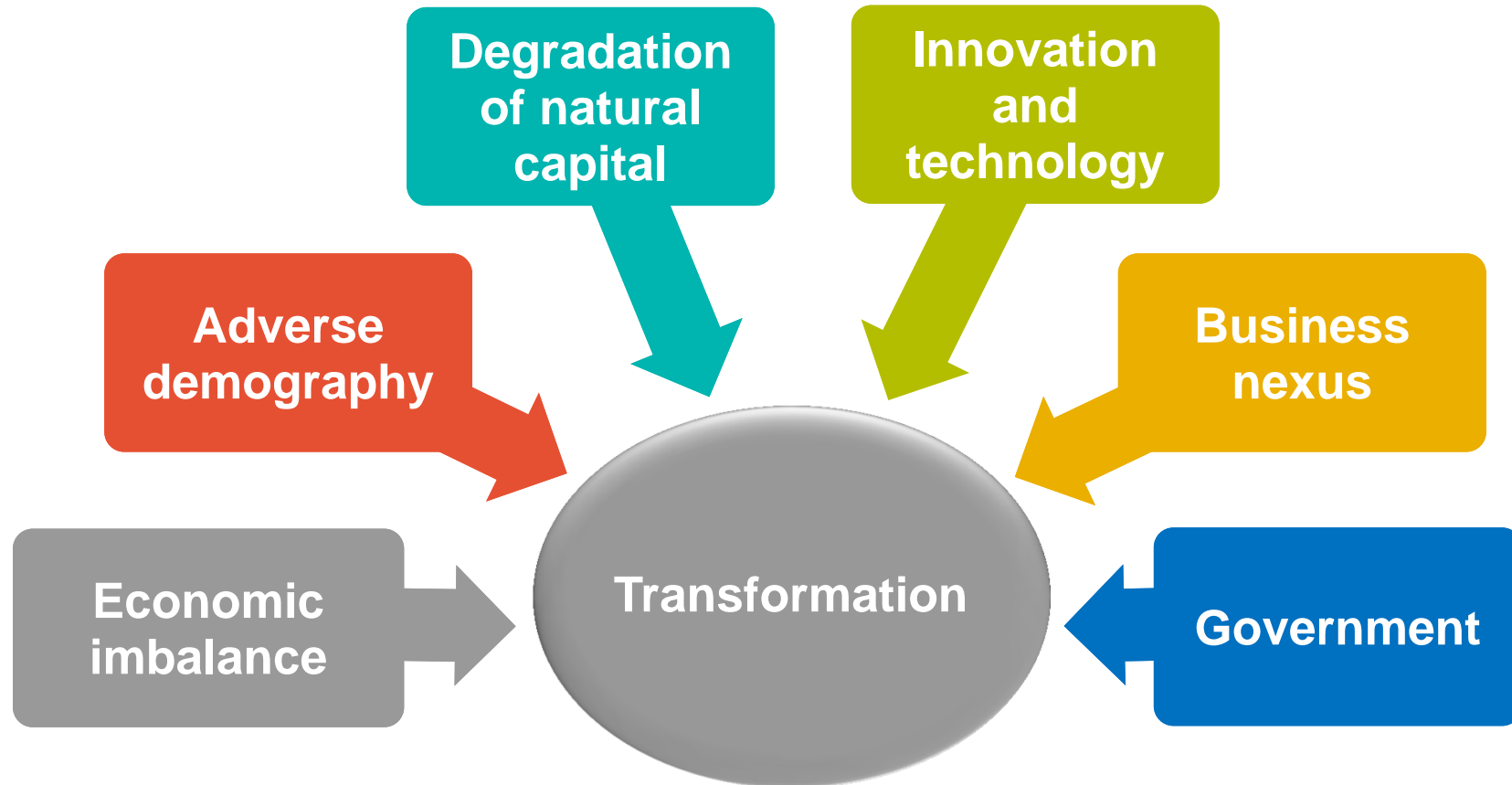
# Ultimately, risk is about not surviving the journey

- Risk is not volatility
- Risk is permanent impairment to mission
- Need better risk framework
- Need better risk governance
- Need better tools



# Thematic investing

## Position yourself for transformative change



Thematic approach helps us to **understand, and anticipate structural changes**  
Our themes are ones we expect to be important over the next decade and beyond

# TW's thematic framework (1)



# TW's thematic framework (2)





# TW's thematic framework (3)



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