NATIXIS
GLOBAL ASSET MANAGEMENT

Global Portfolio Barometer
Review of 2015

Research and insights from the Portfolio Research & Consulting Group at Natixis Global Asset Management

Natixis Global Asset Management's annual *Global Portfolio Barometer* offers insights into model portfolios and asset allocation decisions from across the world. The report reviews a global sample of 855 "moderate risk" or "balanced" portfolios in seven different locations: Singapore, France, Italy, Spain, Latin America, the UK and the USA. The data covers portfolios seen in the six months from July-December 2015.

All statistics in this report are based on simulated returns for current model portfolios over the twelve months ending December 2015. These statistics are therefore representative, rather than actual historical figures.

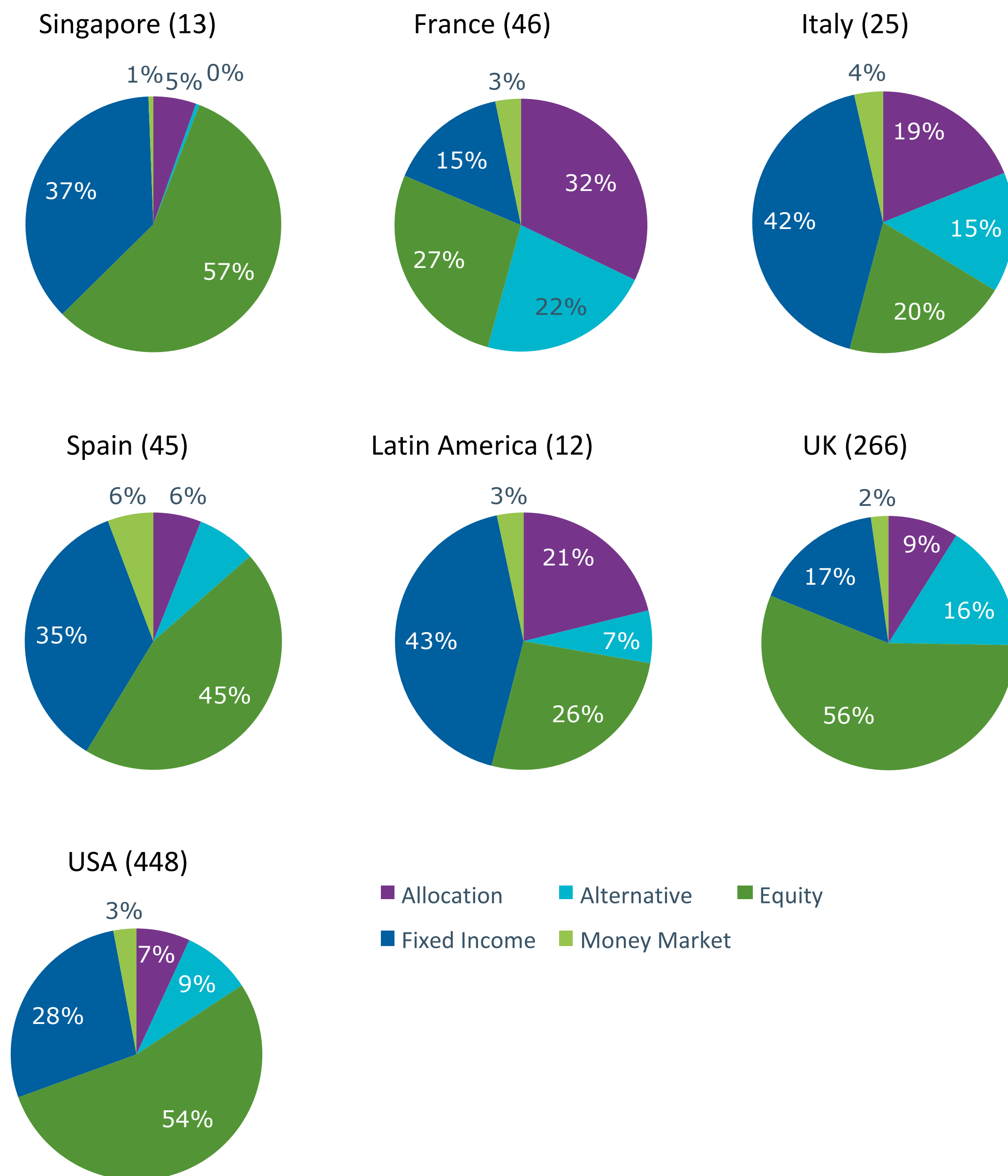
Key Findings

Asset allocation trends

- **Significant differences exist in the average asset allocation of a "balanced portfolio" across all countries**
- **As a result, investors with similar risk tolerances get very different portfolios depending on where they live**
- **In years of disparate asset class performance, such as 2015, the experience for investors across the globe can be expected to vary significantly**
- **The winners in 2015 appear to have been French investors, due to large holdings of outperforming European equities and preference for risk-managed products**
- **US and Latin American investors in our study experienced lower returns due primarily to high exposure to underperforming US and emerging market equities**

Based on hundreds of portfolios analysed in 2015 by Natixis's Portfolio Research & Consulting Group across the globe, this report highlights the key differences that we found between countries in typical asset allocation models and seeks to explain the key drivers in performance differentials.

Chart 1 – Average allocations across global portfolios – moderate risk



It is not surprising that different countries have a variety of styles of investing and favour certain asset classes over others, but the pie charts above highlight just how different the asset allocation experience is for investors in moderate risk model portfolios the world over.

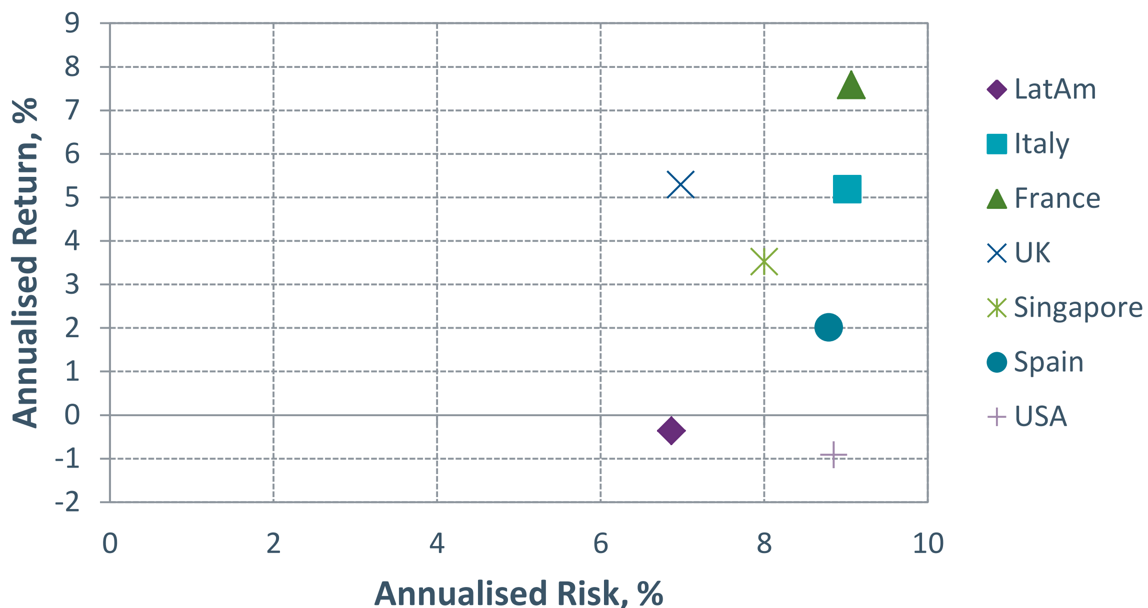
The classic 60% equities, 40% fixed income model remains largely intact in countries such as the US, UK and Singapore. The main deviation from the traditional model in the US and the UK is that fixed income allocations are increasingly being replaced by alternative and asset allocation funds. While this may make sense for investors worried about holding duration risk in their portfolio in a low interest rate environment, it alters the risk and correlation dynamics in their portfolios by replacing a traditionally negatively correlated asset class (government bonds) with historically less volatile but more correlated assets such as “balanced funds” and “absolute return funds”.

There are other countries where the core holding in a balanced portfolio remains fixed income – Italy, Spain & Latin America. We have seen a steady shift over the last 2 year, where investors from these countries have cut their fixed income exposures from over 50% to around 40%, yet it still remains a material holding. We have also seen a shift in the way investors in these countries invest in fixed income, with an increasing shift away from holding many individual bonds to outsourcing this selection and management to specialist bond funds.

French asset allocation is notably different from both of these styles. Investors in France benefit from being able to invest in a high interest paying cash-like product called *Fonds En Euros* that sets a "risk free" benchmark for all other asset classes to beat[1]. As a result, in these low interest times, this makes up a significant portion of a French investors' "risk reducing" allocation. They, along with LatAm and Italian investors, also favour utilising allocation or "patrimonial" funds in significant size. These funds, which include a combination of asset classes, have characteristics similar to the overall moderate portfolios themselves, and do not always offer the diversification benefits expected. They form nearly one third of French portfolios, a far greater proportion than elsewhere.

Within the both the Equity and Fixed income buckets there is also a significant "home country bias" to asset allocation. For instance, in the UK and France, approximately 50% of equity exposure is domestic or in the local region. This is less prevalent in Latin America and Singapore, where the domestic markets are far smaller and investors have a more international outlook, almost by necessity. In these markets, local market exposure is below 20%..

<u>Section 2 – Disparate asset allocation leads to variable performance</u>



[1] This is in many ways similar to "with profits" funds in the UK, whereby the underlying pool of assets is invested in risky assets, but returns to investors are smoothed.
2. Past performance is not indicative of future results.

These disparate asset allocations have led to very different performances over 2015. The best performing region in our sample for 2015 was France, with average 2015 returns of 7.6%, and the worst was the US with -0.9%. Italian (+5.2%) and UK(+5.3%) portfolios also had a solid year, followed by Singapore(+3.5%) and Spain (+2.0%). Along with , US, LatAM investors also struggled, with returns stifled by poor performance across the markets, including equities, US Government bonds and corporate credit. Italian investors, whilst generally happy with their solid performance, may also rue their asset allocation decisions. As Chart 3 below shows, the Italian equity market performed strongly in 2015 but, because of their low exposure to it, most Italian investors did not reap a material benefit.

In fixed income, France and Italy noticeably outperformed, and the UK and Latin America noticeably underperformed. There are several reasons for this. First, Italy and France had high allocations to European fixed income managers, which performed well for them, and particularly so in France where manager selection played a big role. Investors in those markets also hedged less of their fixed income currency exposures than other regions, which benefitted them as the USD rose by 11% against the EUR. This means that European investors investing in USD assets saw an additional 11% return compared to their US and Latin American/LatAm counterparts. Latin American investors suffered from high allocations to US and emerging market fixed income, which performed poorly. In the UK, global and European/Sterling fixed income managers (the lion's share of allocations) underperformed.

Why the big difference between France and LatAm?

French portfolios were heavily invested in European equities, which did very well, and had little exposure to US or EM equities, which did poorly. On the other hand, Latin American portfolios were almost the opposite. Allocation funds were another significant driver, with both sets of investors having substantial asset allocation fund exposure (32% and 21%, respectively). However in 2015 EUR allocation funds outperformed their USD competition by around 10%, partly due to the aforementioned gain of the USD against the EUR. This will have the greatest impact on equity allocations, which are usually not hedged, and the least impact on fixed income, which is usually hedged.

Where does the US stand?

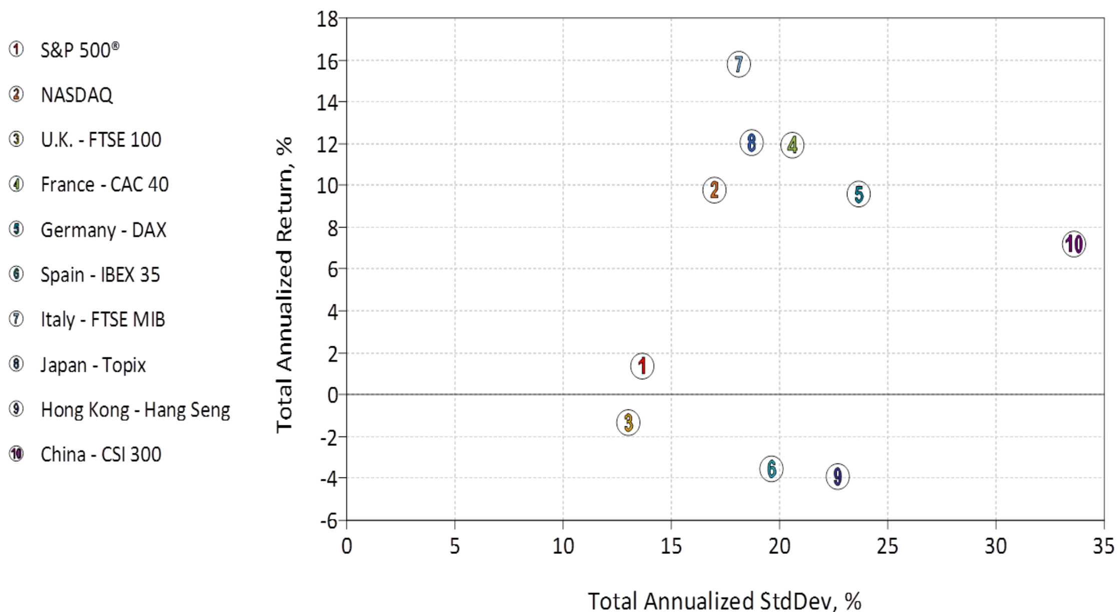
In the US, the best-performing portfolios outperformed the worst-performing portfolios by 6.0% in total return. The biggest driver of this dispersion was at the sub-allocation level in 2015. The winners were overweight US Large Cap relative to International and EM equities, but also had a larger overweight to Growth versus Value. Growth had a 9.5% advantage over Value in the US. Also, the best performing portfolios avoided poor performing sectors like Master Limited Partnerships (MLP's), which were down over 30% for the year. The last element we found that set portfolios apart was fund selection. The narrow nature of the market caused dispersion to rise well above normal in some areas, namely US large cap equity where the difference between the best and worst performing fund was 31%. This could perhaps be a harbinger of what's to come in the active vs passive arena.

Looking ahead, we see a few major themes developing that we will monitor in 2016. First the home country bias is as large as ever. US equities are now responsible for 69% of the

risk in investor portfolios. Second, plummeting energy prices drove investors out of credit and into the safety of curve products like Intermediate Term Bonds. Lastly we saw investors continue to embrace alternatives as allocations to the category hit all-time highs. In 2013, 17% of investors used three or more alternative products. At the end of 2015, that number had grown to 36%. Volatility has returned to markets in a meaningful way, and the increased allocation to alternatives could be a very helpful diversification tool in portfolios. We would like to see US investors embrace diversification in their equity allocations as well.

Lastly, a comparison between the portfolios yields a noticeable cohorting whereby the US, UK & Singapore comprise the pro-growth group with roughly 55% allocated to equity and a modest third or less to fixed income, contrasted with the more defensive Latin America and Italy, where almost half of portfolios are in fixed income and only a quarter or less in equity. France stood out with a portfolio on average structured quite a bit differently than the others with a 22% commitment to alternatives compared with a 12% average across the countries mentioned throughout as well as 32% in allocation funds compared with 7% for the US. These considerable differences driven by risk appetite, cultural precepts, and confidence in one's own investment acumen and opportunity set, led to appreciable differences in outcomes and will likely continue to in the future.

Chart 3: Global equities: significant performance differentials



Source: Morningstar

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Methodology

All figures, unless otherwise stated, are derived from detailed analysis conducted by the Portfolio Research & Consulting Group of 855 moderate risk model portfolios across seven different locations worldwide: Singapore (13 portfolios), France (46), Italy (25), Spain (45), Latin America (12), the UK (266) and the USA (448). The data covers the 12 months from January to December 2015.

About the Portfolio Research & Consulting Group
The Portfolio Research & Consulting Group provides a free and bespoke service to advisers to help build more durable portfolios for their clients. The group uses advanced analytical capabilities derived from sophisticated, institutional grade software to help improve the way advisers create and manage their portfolios. More information is available at www.durableportfolios.com.

James Beaumont, International Head of Portfolio Research & Consulting Group for Natixis Global Asset Management

In this UK based position, James Beaumont has responsibility for analytical services the portfolio research and consulting team offers to clients across Europe, MENA and Asia.

He oversees a team of 6 Consultants and 6 Analysts, all experienced and highly qualified professionals that provide detailed portfolio analysis to help advisers improve the way they create and manage client portfolios. James Beaumont's team is independent and focuses its analysis on risk exposures to improve diversification with a goal of achieving better returns with lower overall volatility.

James Beaumont was previously at Standard Life Investments, where he was a Senior Investment Analyst in SLI's Fund Solutions team. Prior to that, he held roles as a Fund of Hedge Funds Portfolio Manager at Thames River Capital LLP and as a Partner and Senior Analyst at Eden Rock Capital Management.

Marina Gross, Executive Vice President, Portfolio Research & Consulting Group for Natixis Global Asset Management

Marina Gross joined the firm in 2003 and is Executive Vice President of the Portfolio Research and Consulting Group. She and her group are responsible for a full range of portfolio construction-related analyses. She conducts extensive research on asset allocation tools, techniques, methodologies and protocol fostering unique ways to approach portfolio design. She provides highly customized analytics and consultation to clients designed to inform, validate and advance their decision-making around asset allocation.

Ms. Gross has over 17 years of investment industry experience and was previously at Merrill Lynch in Fundamental Equity Research followed by Equity Capital Markets. She received her BSBA from Boston University.

Matthew Riley, Head of Research, Portfolio Research & Consulting Group for Natixis Global Asset Management

Matthew has over 17 years' experience in the investment management industry, and previously specialised as a risk consultant at Falcon Money Management where he was responsible for risk management, investment process and analytic reporting. Matthew also worked as an Investment Director at Aida Capital, the Fund of Hedge Funds arm of Standard Life Investments where he created portfolio construction, statistical analysis and risk management tools.

Prior to that he spent five years at Union Bancaire Privée where he managed fund of hedge fund portfolios for institutional and high net worth clients. He has a master's degree in Chemical Engineering from Pembroke College, Cambridge University.

About Natixis Global Asset Management, S.A.

Natixis Global Asset Management, S.A. is a multi-affiliate organization that offers a single point of access to more than 20 specialized investment firms in the Americas, Europe and Asia. The firm ranks among the world's largest asset managers.[1] Through its Durable Portfolio Construction® philosophy, the company is dedicated to providing innovative ideas on asset allocation and risk management that can help institutions, advisors and individuals address a range of modern market challenges. Natixis Global Asset Management, S.A brings together the expertise of multiple specialized investment managers based in Europe, the United States and Asia to offer a wide spectrum of equity, fixed-income and alternative investment strategies.

Visit ngam.natixis.com for more information.

[1] Cerulli Quantitative Update: Global Markets 2014 ranked Natixis Global Asset Management, S.A. as the 17th largest asset manager in the world based on assets under management as of December 31, 2014.

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