What lies beneath

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Important information

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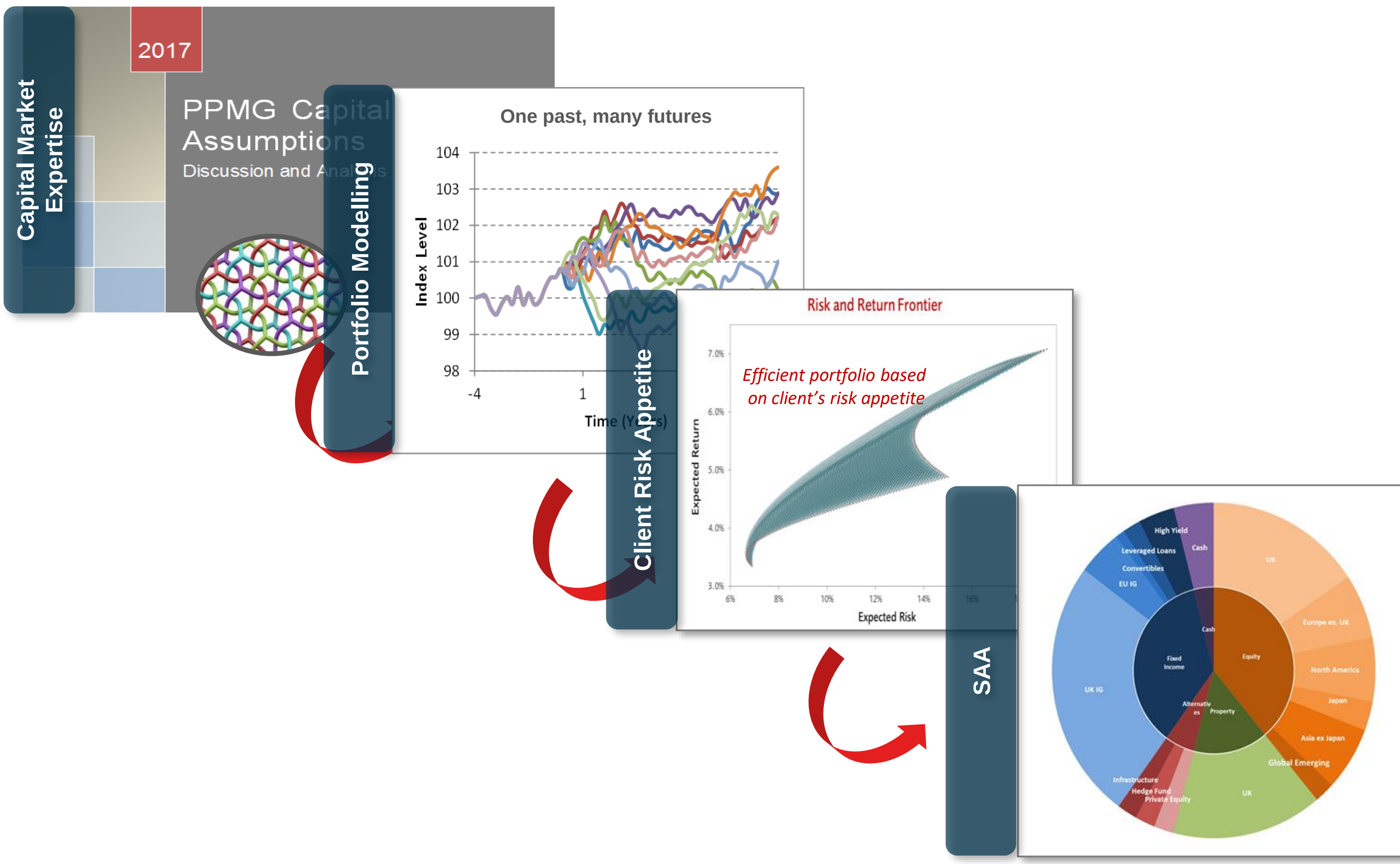
Our learning objectives for the session

1. Describe the relevance of key academic studies in today's multi-asset investment environment

2. Identify whether a multi-asset fund is truly diversified

3. Explain the role that alternative assets play in providing low correlation to traditional asset classes within a multi-asset fund

Multi-asset portfolio strategy design



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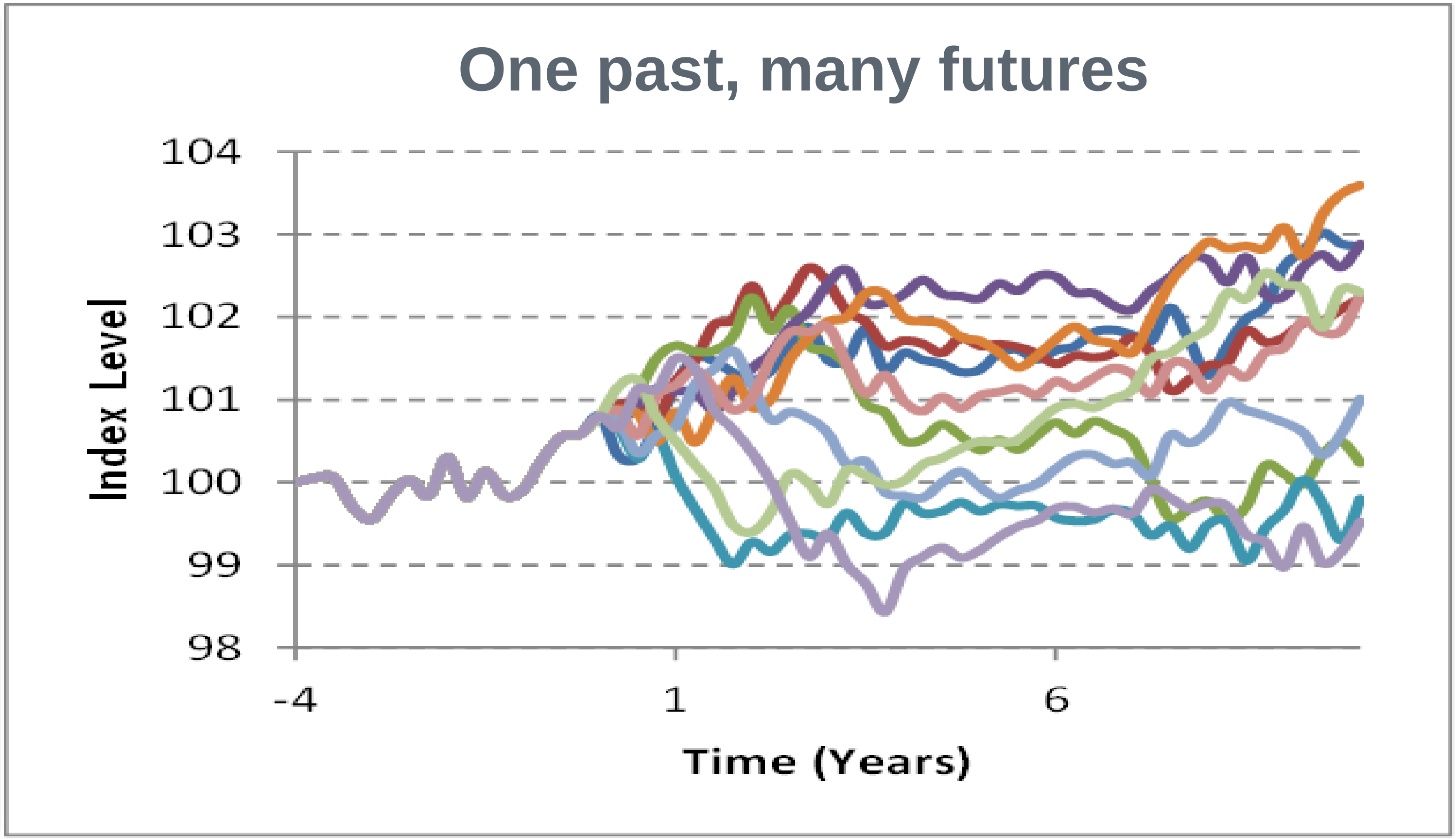
One past, many futures

Portfolio Modelling



Knowledge of capital markets across different scenarios and time

Source: Hypothetical example purely for illustrative purposes only.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INVESTMENT INSIGHTS

2017 Long-Term Capital Market Assumptions

21st Annual Edition | Executive summary

Time-tested projections to build stronger portfolios

IN BRIEF

This executive summary gives readers a broad overview of our 2017 Long-Term Capital Market Assumptions (LTCMAs); it also provides a context for how some of the structural factors affecting economies today are likely to drive asset returns over a 10- to 15-year investment horizon. The key takeaways from this year's LTCMAs:

- Growth remains under pressure as aging populations and below-average productivity take real economic growth down by 25 basis points (bps) in developed markets and 50bps in emerging markets; the result is lower equilibrium interest rates at all points in the yield curve.
- Policy normalization will take much longer than previously thought. In combination with lower equilibrium interest rates, this leaves returns on long-duration government bonds roughly in line with cash and implies that after several years of quantitative easing (QE), duration premia have finally collapsed to zero.
- Lower rates translate to elevated equity risk premia, even though growth has weighed on expected returns; credit is the bright spot in fixed income markets, but it is real assets that hold up best in a world of challenged growth and lackluster returns.
- Expected returns for a simple balanced 60/40 stock-bond portfolio are down by around 75bps and reinforce our view that static balanced allocation has run out of road; investors seeking to boost returns will have to increasingly consider alternative assets, new avenues of diversification and, above all, an active approach to asset allocation.

J.P.Morgan
Asset Management

"***Expected returns*** for a simple balanced 60/40 stock-bond portfolio are ***down*** by around 75bps and reinforce our view that static balanced allocation has run out of road; investors ***seeking to boost*** returns will have to increasingly consider ***alternative assets***, new avenues of ***diversification*** and, above all, an ***active approach to asset allocation***"

Source: J.P.Morgan, October 2016

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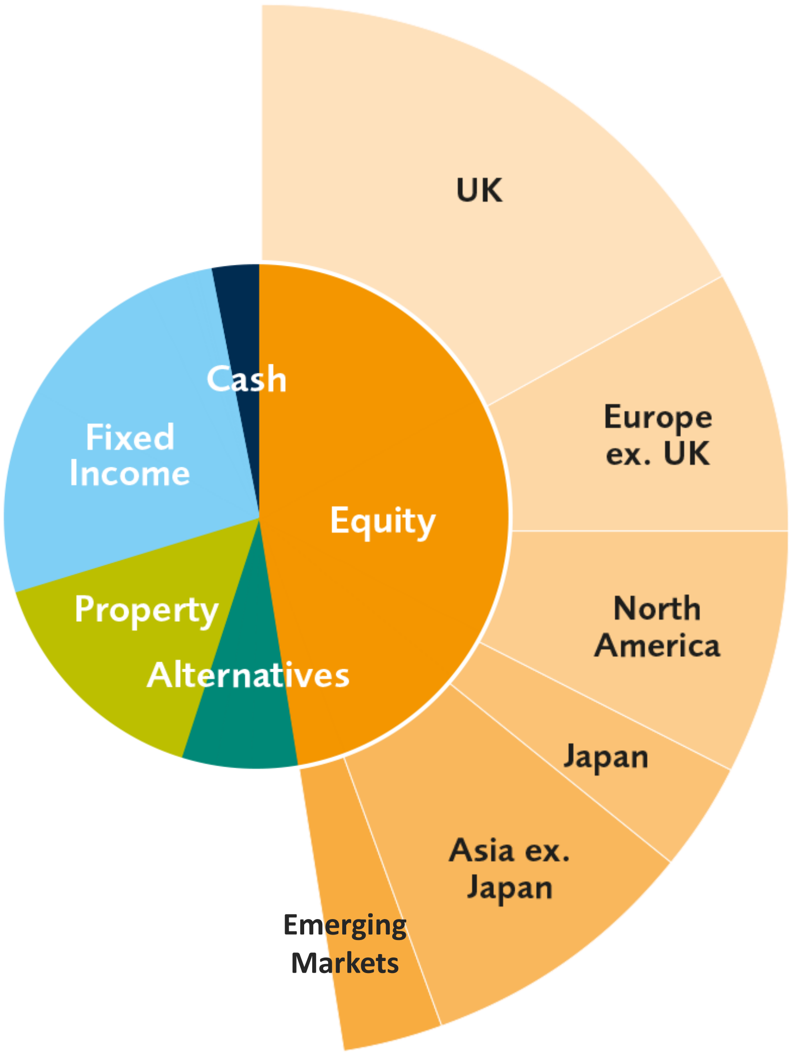
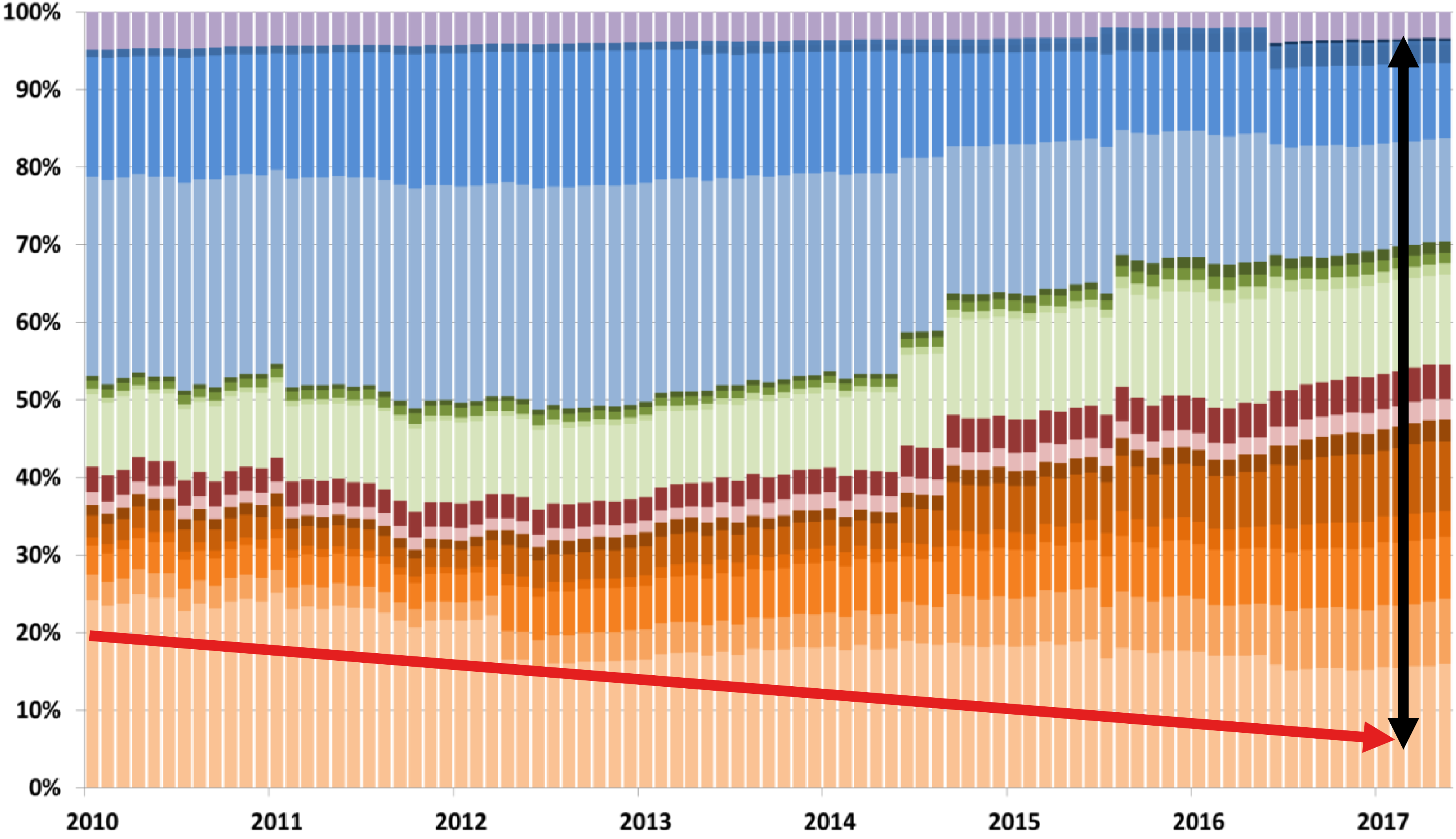
Example diversification and strategic asset allocation



Source: Hypothetical example purely for illustrative purposes only.

Example active strategic asset allocation



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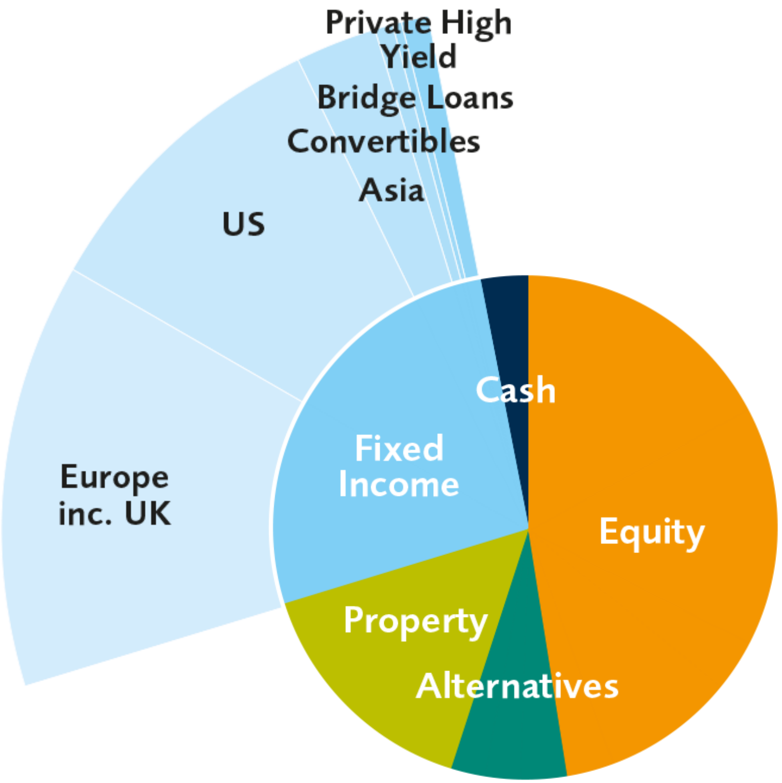
Example diversification and strategic asset allocation



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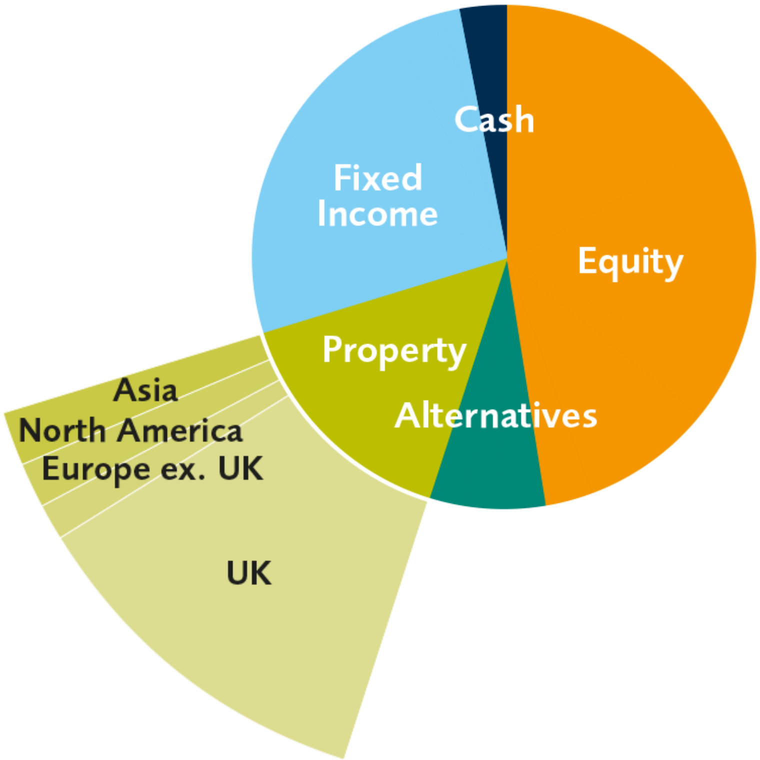
Example diversification and strategic asset allocation



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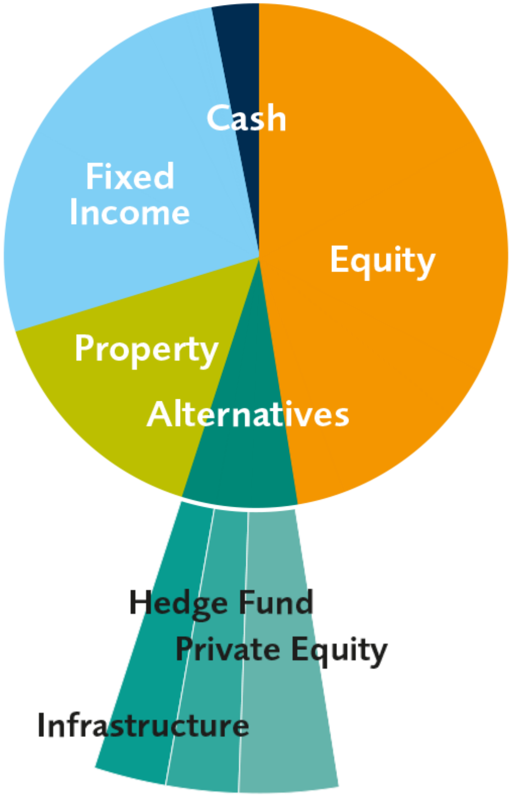
Example diversification and strategic asset allocation



Source: Hypothetical example purely for illustrative purposes only.

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Investment examples – Alternatives

Global opportunities	Low correlations	Illiquidity premia

- Differentiated return streams
- Diversification vs. traditional assets
- Generate excess returns

Alternative assets

Private Equity

- Mature, middle market-focused buyout primary funds
- Special situations & distressed strategies
- Venture capital
- Direct lending/leveraged loans

CALVIN CAPITAL

Date invested:	Sept 2007
Date exited:	Jan 2017
Equity ownership:	100%
Asset IRR	33.6%
Return on exit:	3.8x
Annual Cash yield:	14.5%

Source: Prudential Portfolio Management Group (PPMG)

Alternative assets

Hedge Funds & Other

- Investments with focus on alpha generation and low correlation to long-only portfolios
- Insurance linked securities
- Structured credit
- Bank loan portfolios

Private High Yield

- Whole loan portfolios

PHARO Management

- Emerging markets
- 12%-15% pa total return
- Long-term holding

Source: Prudential Portfolio Management Group (PPMG)

Alternative assets

Infrastructure (equity) & Real Assets

- **PPP assets** – core exposure to low risk projects with long-term government revenues (often index linked)
- **Renewables** – exposure to multiple technologies backed by long-term government incentives
- **Core/Core+** - regulated utilities, transport, communications and energy infrastructure
- **Greenfield** – post planning, pre-construction assets
- **Asset leasing** – aircraft leasing
- **Royalties** – Pharma and other royalty backed investments

Source: Prudential Portfolio Management Group (PPMG)

Alternative assets

Infrastructure (equity) & Real Assets

- **Greenfield**, initial investor long-term 12%-15% pa return
- **Private Finance Initiatives**, 6.5%-7% pa

Source: Prudential Portfolio Management Group (PPMG)

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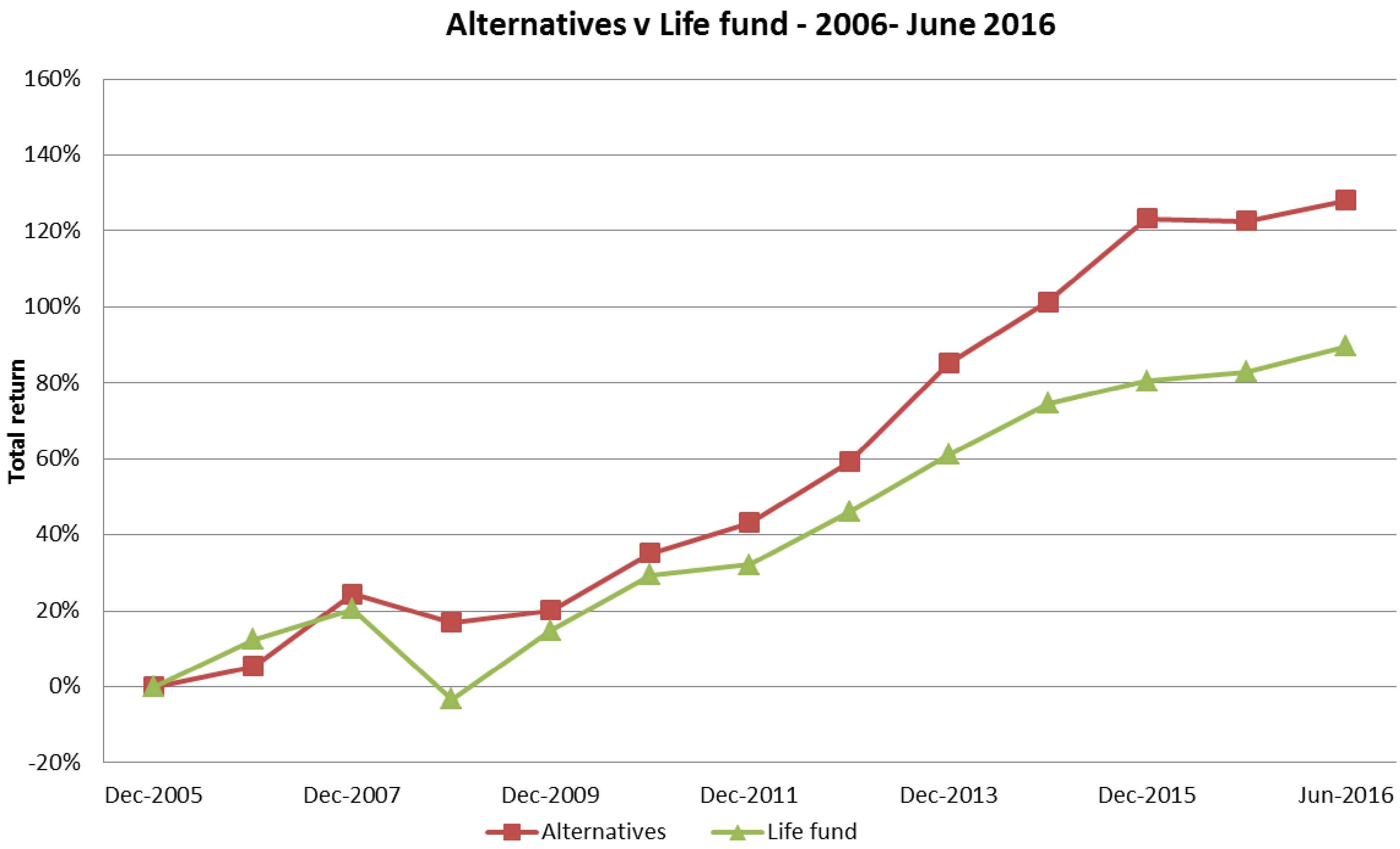
Capturing diversification benefits via alternatives



Source: Prudential Portfolio Management Group (PPMG)

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Portfolio examples - diversification benefits

	Volatility	Max Drawdown
75/25 Equity Bond Portfolio	7.95	-9.03
As above but 50:50 split on equities and bonds between UK and Overseas	7.60	-8.18
As above but reduce equity exposure by 10% and adding to Property	6.68	-6.76
As above but reduce equity exposure by a further 5% and add to Alternatives	6.40	-6.31

All figures from FE Analytics for period from 31 Jul 2012 to 31 Jul 2017. Initial 75/25 portfolio is UK Equities and UK Bonds only. UK Equities represented by FTSE All Share, Overseas Equities by MSCI World, UK Bonds by IBOXX UK Sterling Corporate All Maturities, Overseas Bonds by Barclays Global Aggregate, Property by FE UK Property Proxy and Alternatives by Investment Trust Hedge Fund Sector and Investment Trust Private Equity Sector.

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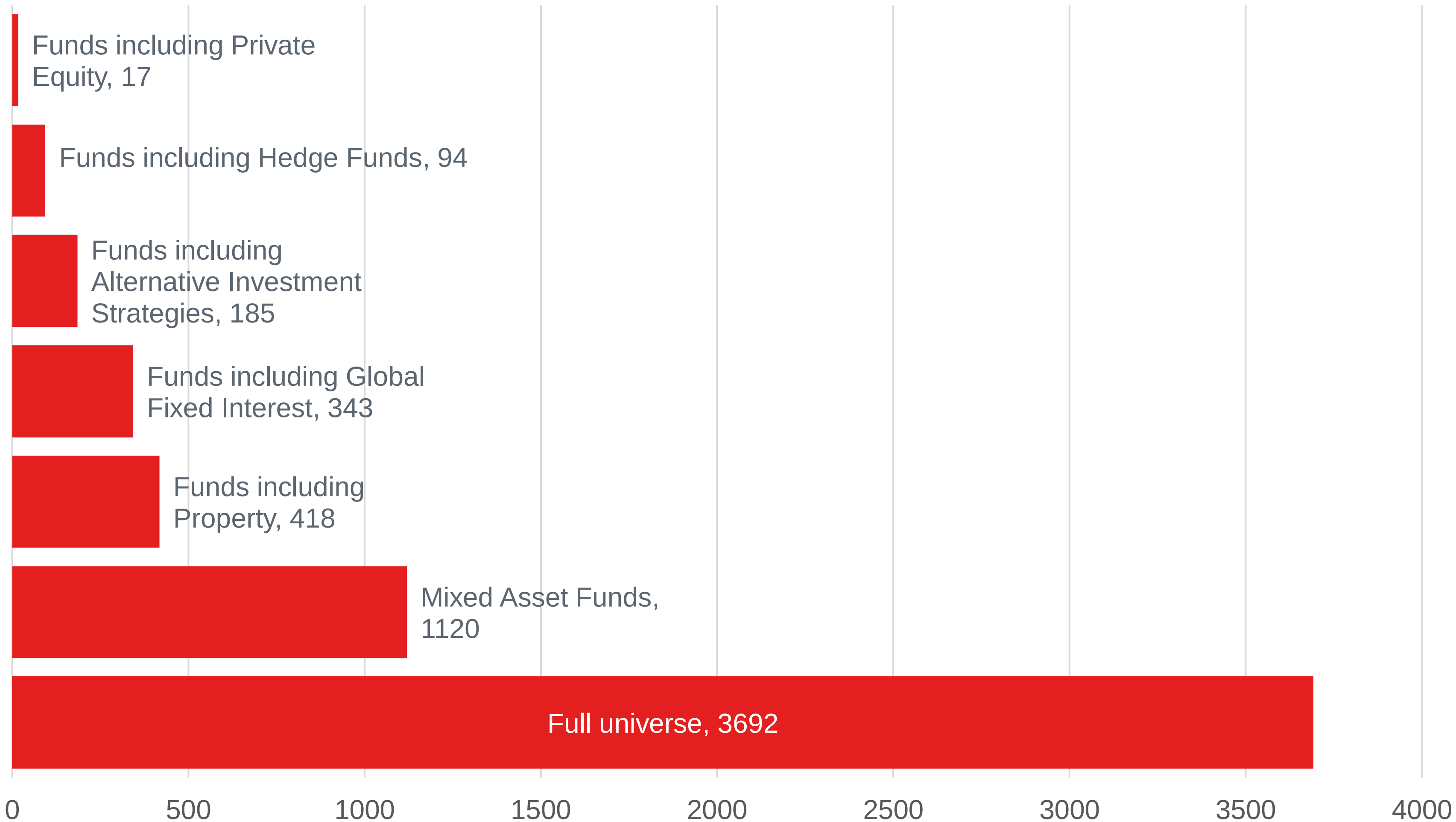
What lies beneath – a wide universe of choice?



Source: FE Analytics, 29th August 2017. Total number of funds represents Investment Association universe.

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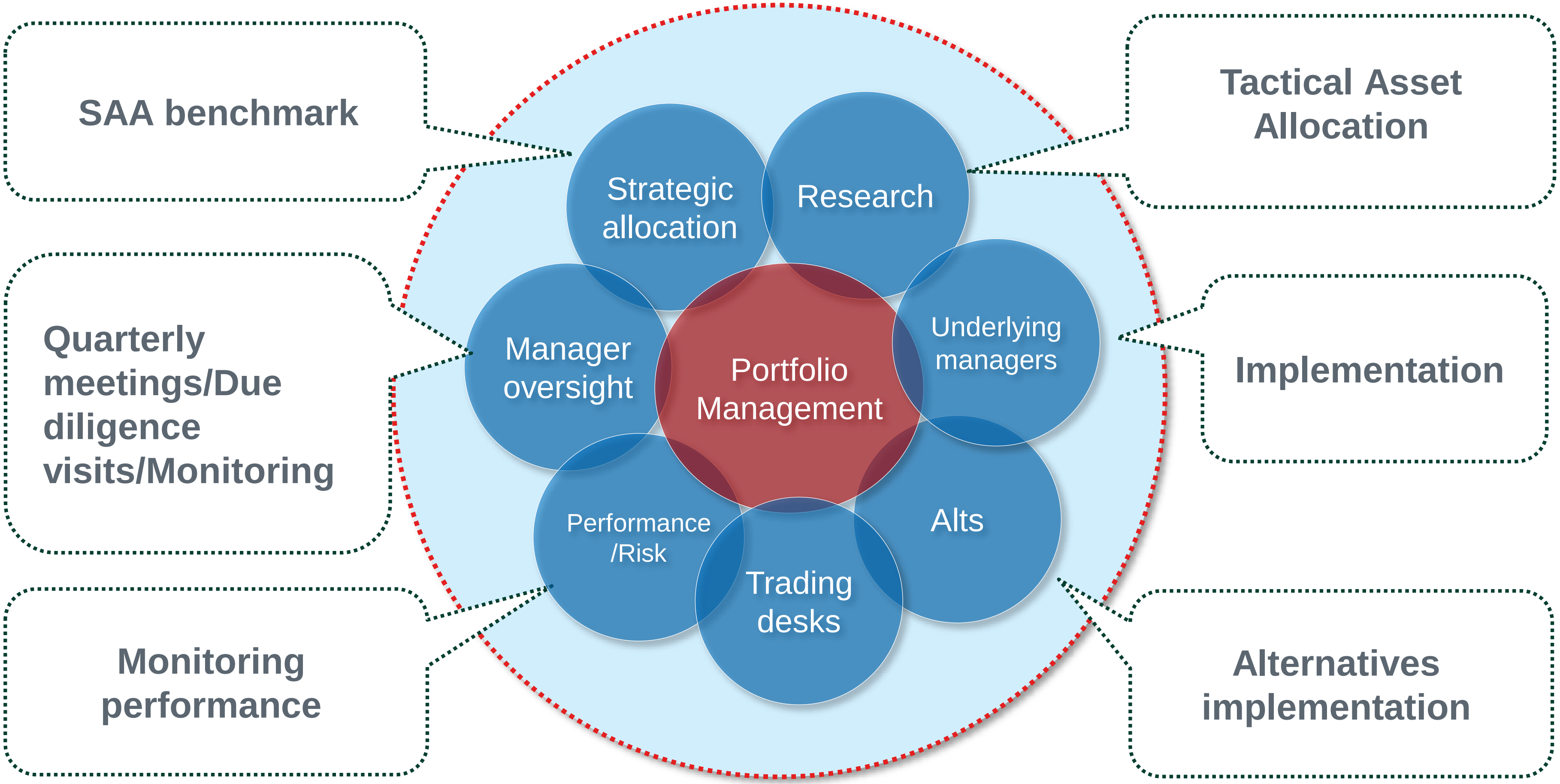
What lies beneath – what expertise is required

A collaborative effort between specialist teams



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Prudential Portfolio Management Group skill set

PruFunds	Risk Managed PruFunds	Dynamic Portfolios	Dynamic Focused
Unique smoothing process and strength inherent within one of the largest With-Profit funds in the UK	Unique smoothing process adopted from proven PruFunds	A choice of five risk managed portfolios each investing in independently selected and recommended funds	A choice of five risk managed portfolios, active internal management and passive equity exposure
		60-100 Portfolio – DT 6	60-100 Portfolio – DT 6
	RMPF 40-80 – DT 5	40-80 Portfolio – DT 5	40-80 Portfolio – DT 5
PruFund Growth – DT 4	RMPF 20-55 – DT 4	20-55 Portfolio – DT 5	20-55 Portfolio – DT 4
	RMPF 10-40 – DT 4	10-40 Portfolio – DT 4	10-40 Portfolio – DT 4
PruFund Cautious – DT 3	RMPF 0 -30 – DT 3	0-30 Portfolio – DT 4	0-30 Portfolio – DT 3

Source: Prudential. Distribution Technology (DT) risk ratings are as at 31 Mar 2017

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Dynamic Focused 20–55 Portfolio

Source: FE Analytics. Past performance is not a reliable indicator of future performance.
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Thank you for your time

If you would like to give us feedback directly or request information not covered elsewhere please e mail us at

speakernotes@prudential.co.uk