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Casey Quirk

A Tailored Approach:
Positioning to Outcome-Oriented Global Investors
February 2014

More than 200 asset consultants, institutional investors and intermediaries worldwide responded to this year's survey.

Respondents highlighted five key themes in asset allocation and buying behavior:

1. Further implementation of outcome-oriented investing, as investors continue to accelerate their divergence in asset allocations and buying behaviors. This reflects the long-term desire of asset owners worldwide to design policy allocations around specific objectives, which differ from investor to investor.
2. A broad concern with a rising interest rate environment across buyer channels, especially pensions, as a primary theme guiding portfolio changes.
3. A continued realignment of fixed income, with 48% of all participants expecting to restructure their fixed income portfolios in 2014. Corporate plans, in particular, continue to adopt LDI and rate-concerned investors delink their portfolios from interest rate sensitive strategies.
4. Surging appetite for real assets as investors continue to diversify alternatives portfolios. Real assets represent the largest category of new search activity consultants expect in 2014, representing 14% of forecasted new search activity, versus 6% in 2013.
5. Increased competition amongst managers, in particular for traditional mandates, as net flows subside and replacement search activity becomes the norm. Domestic equity, EAFE equity, and domestic fixed income will see the collective proportion of expected search activity from manager replacement increase to 58%, from 45% in 2013.

Successful asset managers will adapt to changing demand drivers by:

- Segmenting clients in order to properly position products against desired outcomes
- Developing compelling thought leadership that addresses concerns of target buyers
- Implementing data-driven, forward-looking product development processes
- Designing new strategic engagement models for consultative sales and service

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Casey, Quirk & Associates is a management consulting firm focused solely on advising investment management firms worldwide. Our partners and associates help our clients develop broad business growth strategies, improve investment/product appeal and growth prospects, evaluate new market and product opportunities, and enhance incentive alignment structures. Our unparalleled industry knowledge and experience, detailed proprietary data, and global network of relationships make Casey Quirk the leading advisor to the owners and senior executives of investment management firms in the world.

eVestment provides a flexible suite of easy-to-use, cloud-based solutions to help global investors and their consultants select investment managers, enable asset managers to successfully market their funds worldwide and assist clients to identify and capitalize on global investment trends. With the largest, most comprehensive global database of traditional and alternative strategies, delivered through leading-edge technology and backed by fantastic client service, eVestment helps its clients be more strategic, efficient and informed. The company was founded in 2000 and is headquartered in Atlanta, Georgia with global offices in New York, Toronto, London, Sydney and Hong Kong.

Demographics

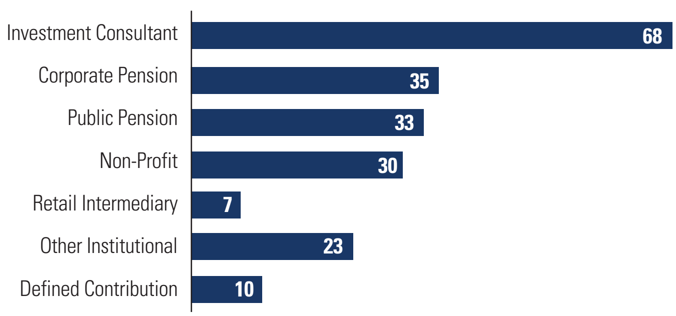
In the past, Casey Quirk and eVestment have conducted an annual Consultant Search Forecast, of which this would have been the eighth installment. This year's survey significantly expands the pool of respondents by gathering information from more professional buyers of investment services worldwide:

- More than 65 investment consultants, representing some $3.7 trillion in assets under advisement, participated in this year's survey.
- For the first time, more than 135 institutional investors of all types, accounting for $1.6 trillion in assets under management, also responded to the survey.
- Manager selection groups of large retail intermediaries also participated for the first time.
- Nearly 40% of this year's respondents reside outside the United States.

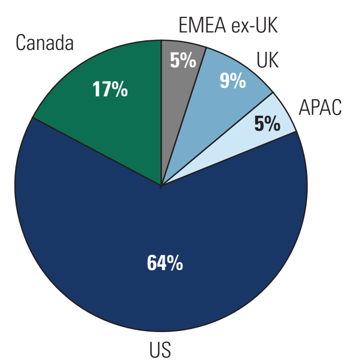
Exhibit 1

Demographics of Survey Respondents, 2014

Count of Respondents
By Organization Type



Count of Respondents
By Geography



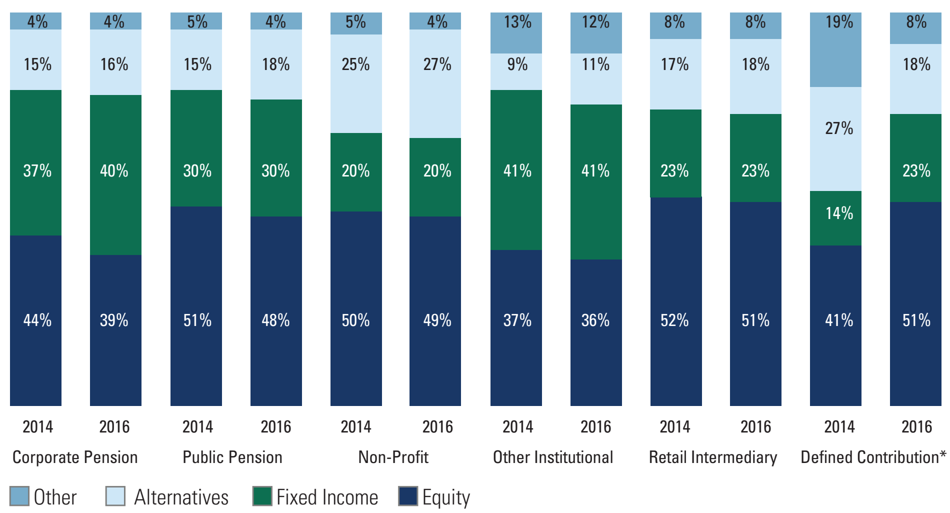
Note: Other Institutional category includes outsourcing/OCIO, and Taft-Hartley/multi-employer plans
Source: 2014 Casey Quirk / eVestment Global Investor Study

Drivers of Asset Owner Behavior

Increasingly, asset allocations of asset owners are diverging, reflecting different policy objectives among the various categories of professional buyers. While most investors plan to decrease equity commitments in favor of fixed income exposure during the next three years, the degree of change varies. More importantly, asset owners have starkly different views about continuing to raise their exposure to alternative investments.

Exhibit 2

Asset Allocation by Investor Type 2014 vs. 2016



Note: Other includes cash and ETF
** Defined Contribution plans consist primarily of Australian Superannuation funds.*
Source: 2014 Casey Quirk / eVestment Global Investor Study

Different goals appear to motivate each category of institutional investor:

- **Corporate pension** schemes, realizing improved funding ratios after a heady bull market in 2013, expect to accelerate de-risking as they aim to immunize liabilities once and for all.
- **Public pension** plans, still more poorly funded than many of their corporate counterparts, continue to focus on appreciation, raising alternatives exposures.
- **Non-profit schemes** such as endowments and foundations worry about meeting target returns while producing the necessary cash flow for operations. As a result, they exhibit the highest exposures to alternatives across all surveyed investor types, although their allocation profiles are expected to remain relatively constant through 2016.
- **Gatekeepers at retail intermediaries** also report that they expect more static portfolio allocations over the next three years, although they anticipate further reductions in cash positions built by cautious investors. Additionally, they expect the rising age of their investor base to favor more fixed income strategies.

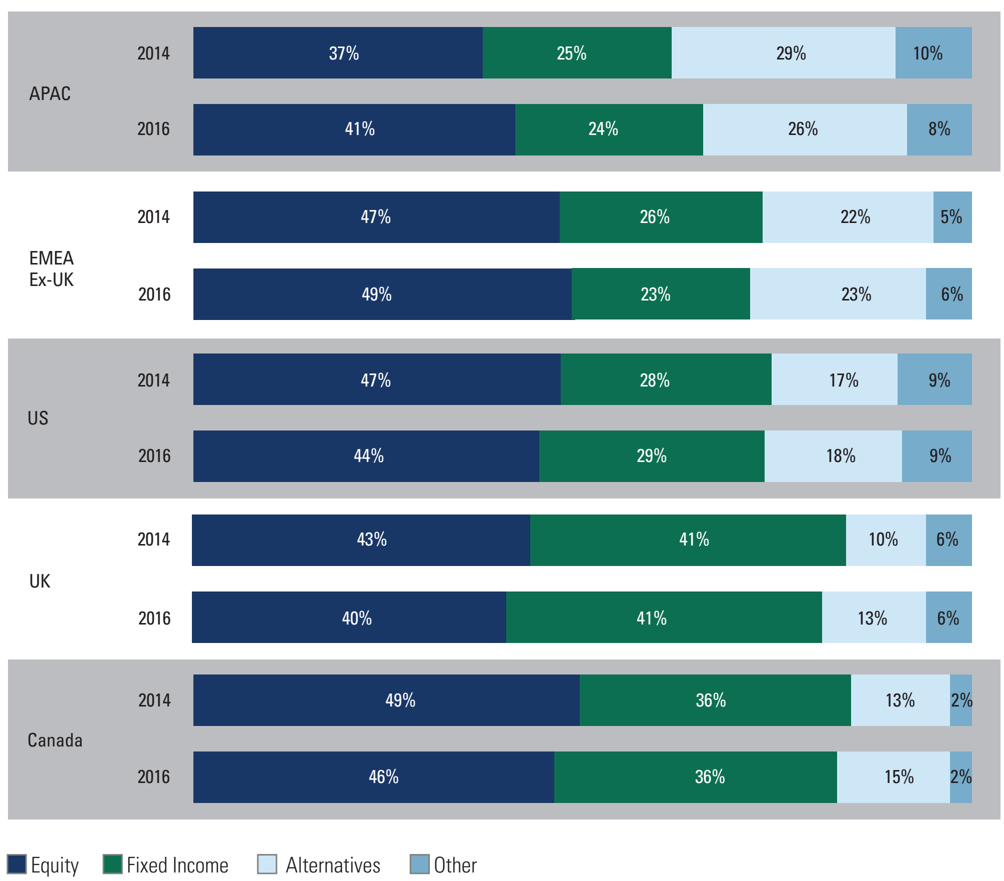
Asset allocation understandably differs by investor domicile as well, depending on historic equity exposure. Viewed through a geographic lens, a number of changes are apparent between now and 2016:

- **Australian respondents** report they expect to sell property—likely at a cyclical peak Down Under—in favor of equity investing. Australia's newly enhanced Superannuation Guarantee, which mandates substantial investments in retirement savings, will help drive this shift.
- **Institutional investors in Europe**, laggards in the implementation of alternative strategies, anticipate increasing their reliance on alternative investments and non-traditional strategies.
- **Asian institutions**, many of which have moved aggressively into alternatives in recent years, are shifting allocations from cash and alternatives and toward equity.

"APAC investors haven't embraced LDI"

Exhibit 3

Asset Allocation by Investor Domicile 2016 vs. 2014



Source: 2014 Casey Quirk / eVestment Global Investor Study

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Investor Concerns

Adapting portfolios for a rising rate environment and meeting target returns—two issues that are probably co-dependent—rank among the highest-level concerns of respondents.

Exhibit 4

Primary Concerns by Investor Type (Percent of Total Respondents)

	Rising Interest Rates	Government/Political Risk/Regulation	Meeting Target Returns	Market Correction/Recession	Risk Management/Volatility
Corporate Pension	48%	33%	21%	30%	18%
Public Pension	69%	24%	28%	41%	31%
Investment Consultant	58%	52%	44%	27%	31%
Non-Profit	40%	37%	37%	23%	27%
Other Institutional	48%	43%	30%	35%	17%
Defined Contribution	57%	39%	48%	35%	26%

Source: 2014 Casey Quirk / eVestment Global Investor Study

Again, attitudes differed by investor type:

- **Public pensions**, particularly those in North America and the United Kingdom, are the most concerned about interest rates, given their decision to implement liability-driven strategies.
- **Non-profits**, heavily focused on meeting annual spending needs, and public pensions, under a media spotlight for poor funding ratios, are the groups most concerned about volatility.
- **Investment consultants** cite increased regulation as a primary concern—a fear that fails to scare their clients, most of whom are less concerned about government interference.

Asset owners' anticipated changes in investment policy reflect these worries:

- **Pensions and retail intermediary gatekeepers**—with the most to lose from rising rates—are particularly focused on restructuring their fixed income portfolios during the next three years.

- **U.S. investors** are attracted to next-generation debt strategies, positioned to generate income, agnostic of interest rate movements.

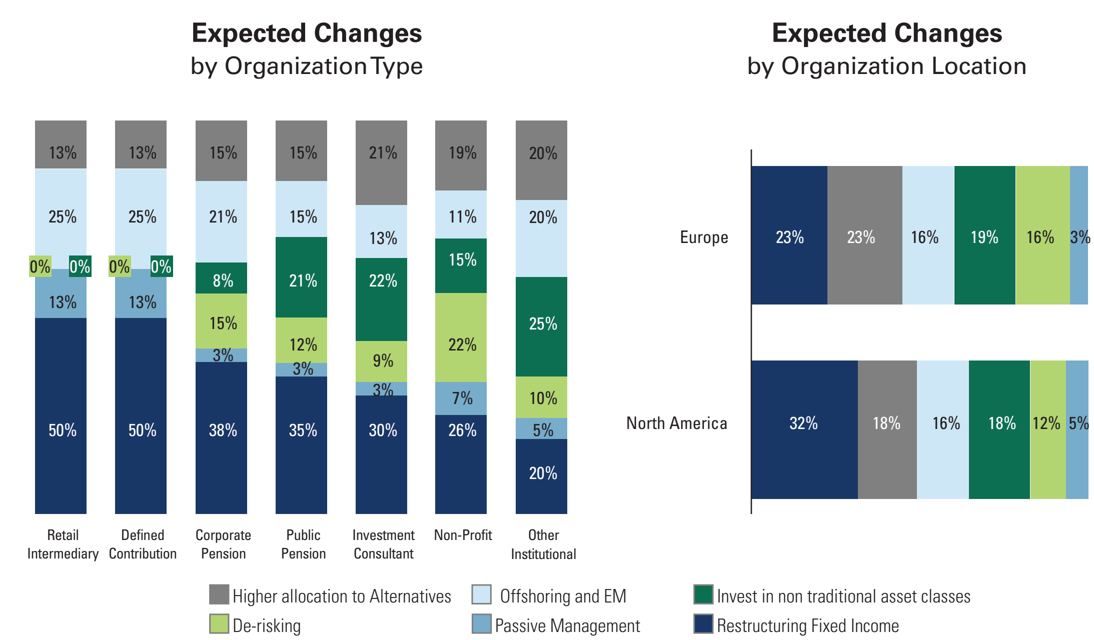
> ***"Domestic fixed income has a mix of strategic and tactical factors at play."***

- **European investors**, conversely, are more focused on raising their exposure to alternative and non-traditional asset classes.

- While **non-profits**, overall, expect little change in their asset allocation, they cite de-risking as a primary portfolio strategy for the next three years. This highlights the lack of homogeneity even within a buyer segment: many non-profits indicate they feel over-allocated to risk asset and illiquid stakes, while others are raising their allocation to drive total returns.

Exhibit 5

Expected Portfolio Strategy Changes by Investor Type and Domicile, 2014



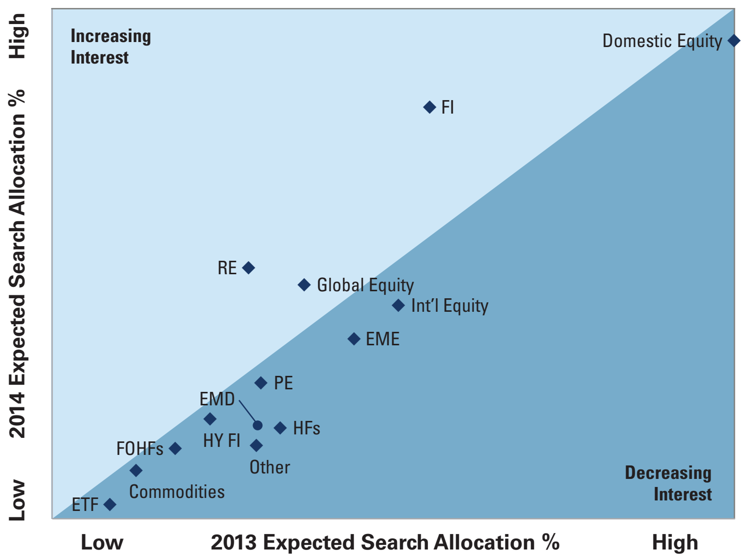
Source: 2014 Casey Quirk / eVestment Global Investor Study

Consultants' Viewpoint

Respondents' concerns over the potential for rising interest rates and higher volatility are reflected in their expected demand for investment products and services over the next one to three years. Our product opportunity map compares the search activity consultants expect for the upcoming year relative to their forecasts from last year. For many asset classes, demand levels appear to remain somewhat consistent in 2014—reflecting that many elements of strategic policy allocation have finally stabilized following the global financial crisis of 2008 through 2009.

Exhibit 6

Expected Consultant Search Activity, 2014 vs. 2013



Source: 2014 Casey Quirk / eVestment Global Investor Study

Consultants expect search activity to rise primarily within three asset classes:

- **Real assets, real estate and infrastructure** will see the greatest spikes in search search activity, as institutional investors of all types seek long-dated, unlisted investments that also generate strong recurrent cash flow, well-designed for liability immunization and inflation protection.

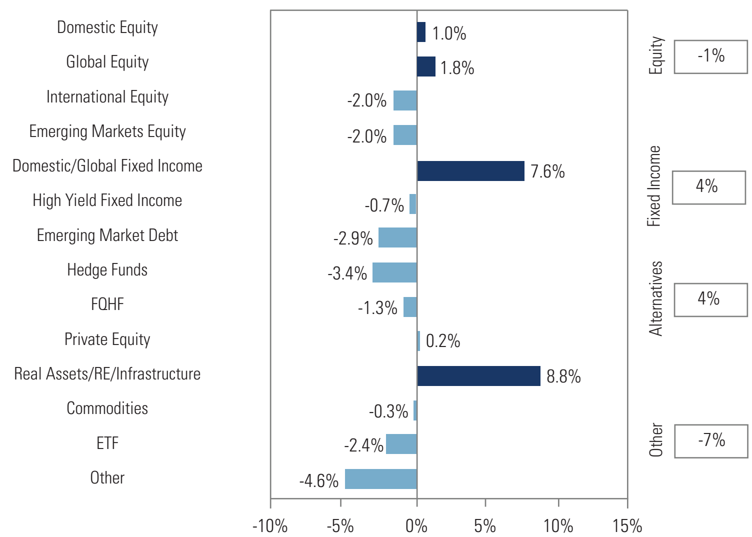
"The real asset story is synonymous with the theme of finding uncorrelated income."

- **Domestic and global fixed income** allocations will be redesigned by professional buyers to protect themselves from the fallout of rising interest rates.

- **Global equities** will benefit from the long-term trend away from home-biased portfolios—and even from domestic equity mandates more broadly. Consultants continue to increasingly favor the flexibility of global, relative to domestic-EAFE, equity mandates.

Exhibit 7

Expected Nominal Change in New Search Activity by Asset Class, 2014



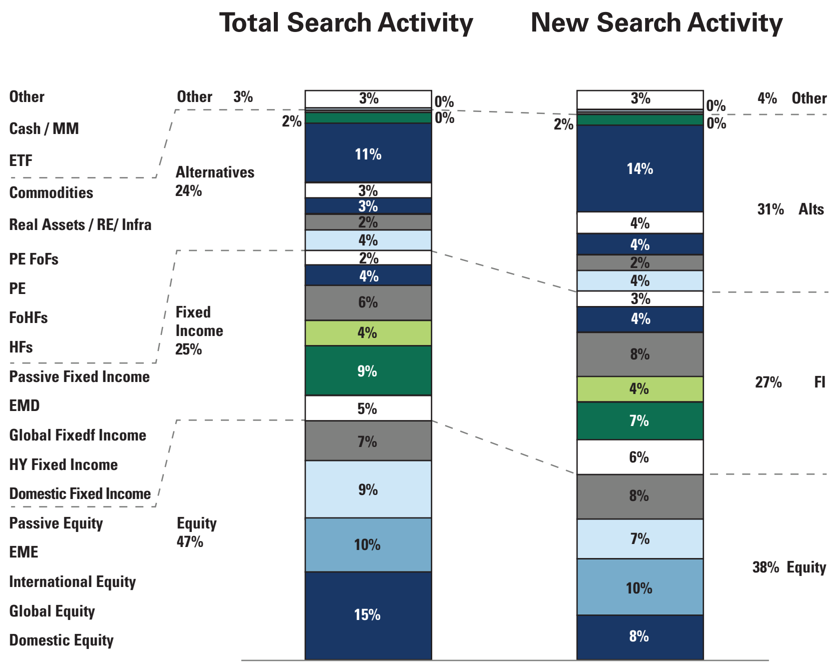
Source: 2014 Casey Quirk / eVestment Global Investor Study

Search activity in domestic equities and bonds, along with EAFE mandates, remains driven by manager turnover, rather than new allocations. Additionally, only a minority of searches for funds of hedge funds are for new mandates, underscoring the challenges facing funds of hedge fund firms as institutional investors of all types build experience and comfort in investing directly.

> ***"There is a reduction in allocations toward the Barclays Aggregate [index] and a movement toward long-duration."***

Exhibit 8

Expected Consultant Search Activity: Total Search Activity and New Search Activity, 2014

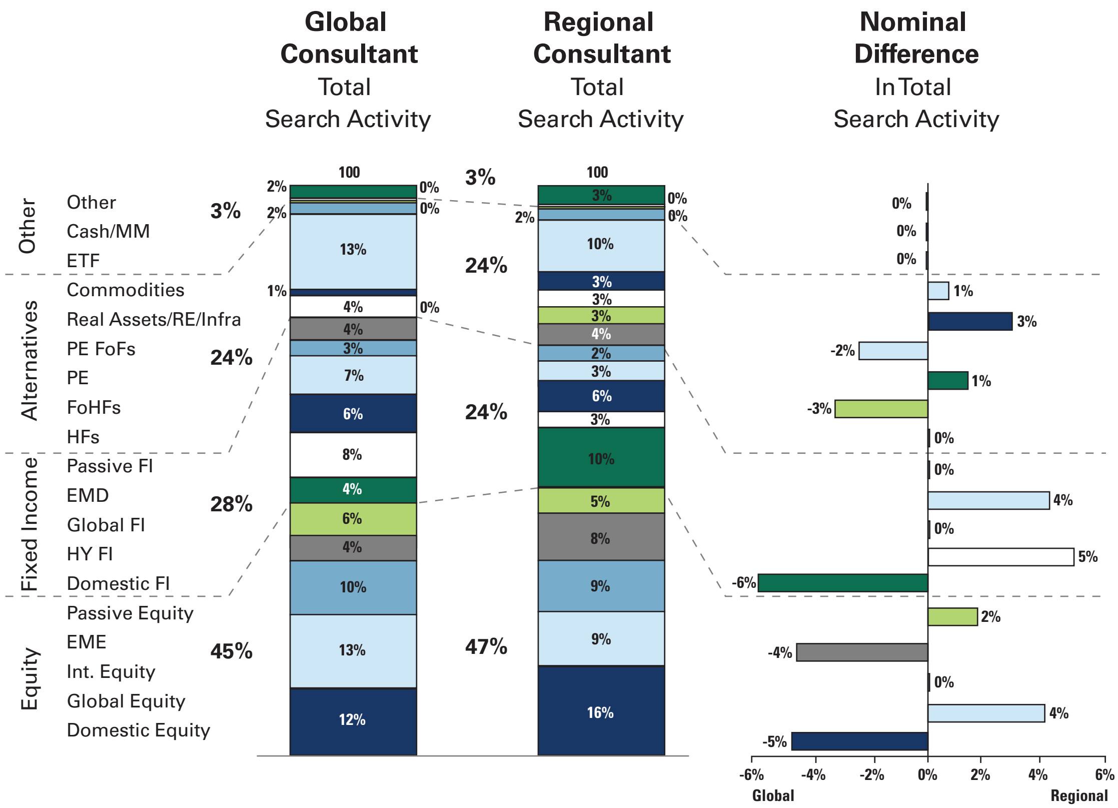


Source: 2014 Casey Quirk / eVestment Global Investor Study

This year's survey, for the first time, provides insight regarding the different expectations of large, global asset consultants and their smaller, regionally-focused competitors. Global consultants expect a higher proportion of their search activity to center on fixed income strategies, while regional consultants continue to focus on domestic and emerging market equity mandates. For the asset manager, segmentation strategies extend to the consultant marketplace by prioritizing on scale and underlying client demographics.

Exhibit 9

Expected Consultant Search Activity by Consultant Type, 2014



Source: 2014 Casey Quirk / eVestment Global Investor Study

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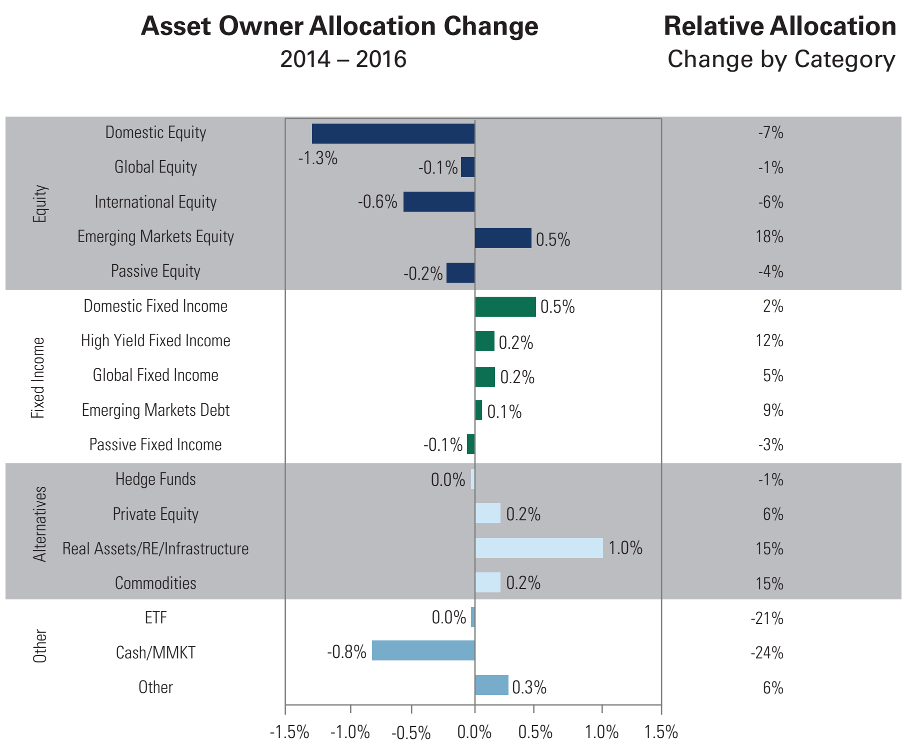
Longer-Term Trends: Asset Allocation in 2016

Asset owners responding to this year's survey report expected changes in allocation over a three-year timeframe. This longer view, coupled with the use of asset allocation shifts rather than the flows implied by 2014 expected consultant search activity, complicate any comparisons between the two data sets. In general, however, asset owners expect increased investments in fixed income and alternatives, mostly at the expense of benchmark-tracking domestic equities. Notably, in the aggregate, asset owners expect no substantial increase in their passive portfolio exposure.

Exhibit 10

Expected Investor Allocation Changes by Asset Class, 2014 – 2016

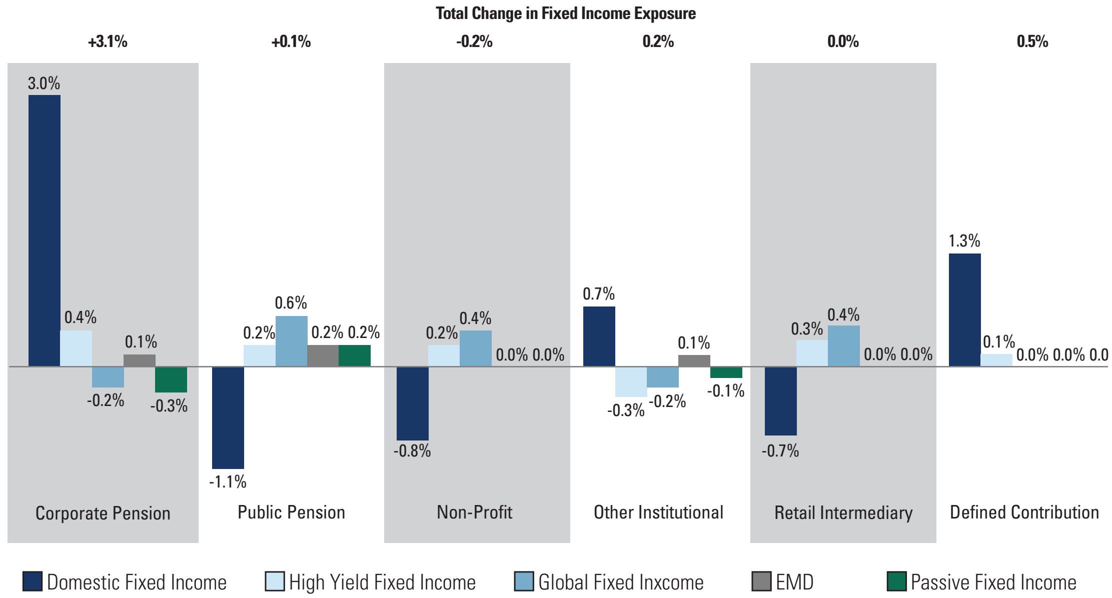


Sources: 2014 Casey Quirk / eVestment Global Investor Study

Consistency in institutional demand varies substantially by product. Most asset owners, regardless of their objectives or their location, plan to boost holdings in real assets and decrease exposure to domestic equities. But with other asset classes, respondents report diverging expectations, particularly regarding domestic fixed income, where opinion regarding future allocations is polarized relative to the organization's likelihood to implement an immunization strategy.

Exhibit 11

Change in Fixed Income Allocation by Organization Type, 2014 – 2016



Sources: 2014 Casey Quirk / eVestment Global Investor Study

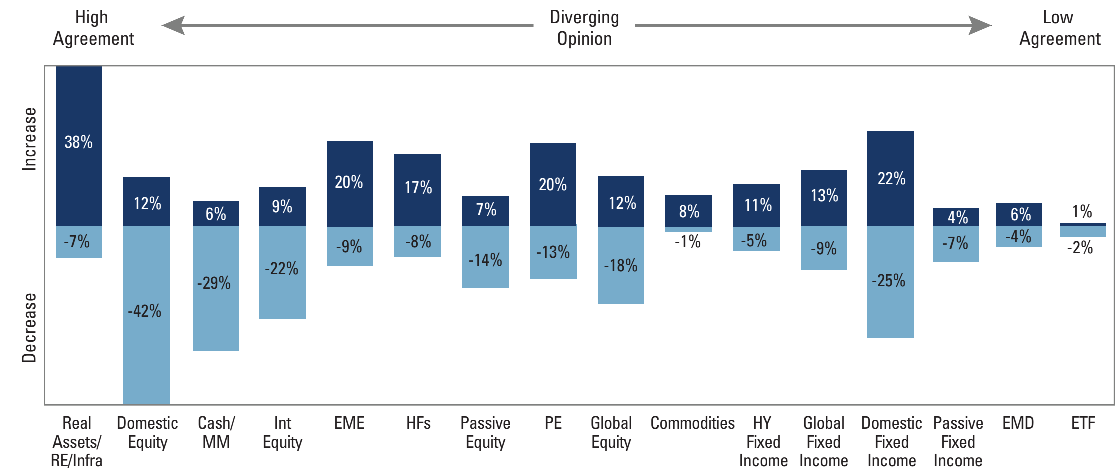
Private equity is another interesting asset class that is experiencing divergent opinion. While most investors continue to express interest in increasing their allocations to unlisted equity, the presence of a significant and diverging group of respondents indicates that the marketplace still has two key concerns:

"Investors are increasingly agnostic to product structure and more focused on opportunity."

- The impending quality of performance figures of funds from pre-crisis, record vintage years;
- The health of industry deal flow and implied ability to support expected asset class outperformance.

Exhibit 12

Range of Expected Investor Allocation Changes by Asset Class, 2014 – 2016



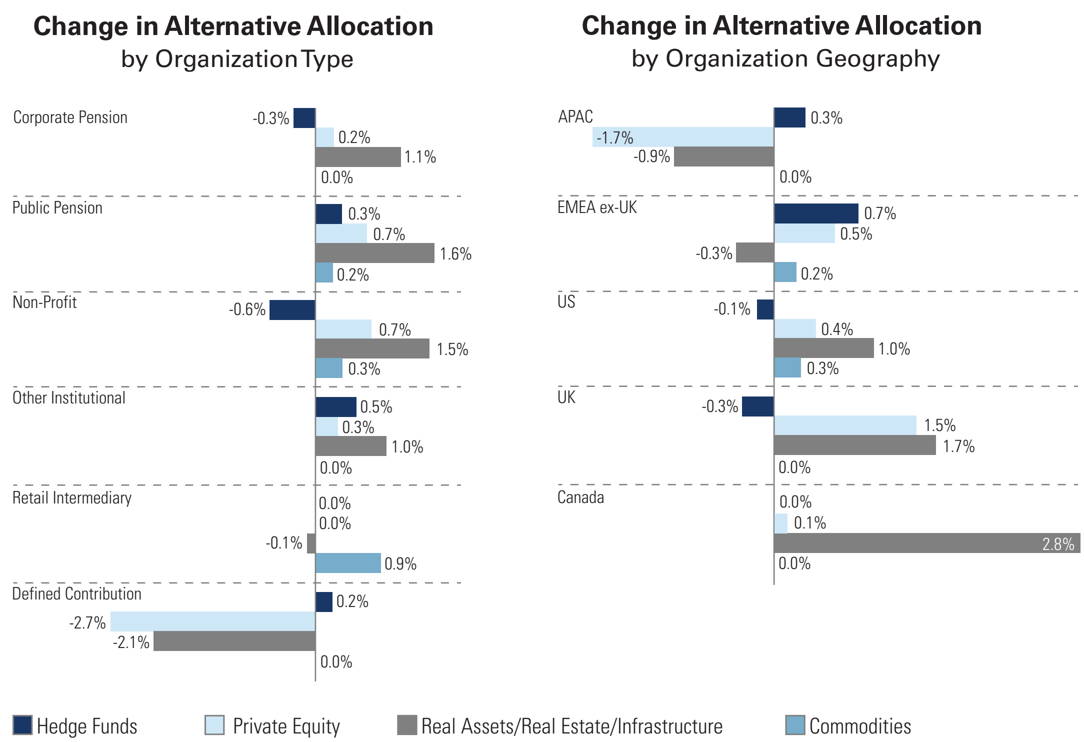
Note: Excludes institutions that expect no allocation change in the asset class.
Source: 2014 Casey Quirk / eVestment Global Investor Study

Asset owners, in the aggregate, report continued appetite for alternative investments, but demand is centering among investors of certain types and domiciles:

- Large corporate defined benefit pension plans, particularly those in the U.S., expect to allocate assets away from both liquid and illiquid alternatives during the next three years, partly to de-risk and partly to generate cash for paying retirees.
- For the remainder of institutional investors in the U.S., demand for alternative investments continues to diversify. Infrastructure and commodities, in particular, project to be big winners through 2016.
- Smaller U.S. pensions and non-profits, as well as European and Asian investors, meanwhile, expect large additional investments in hedge funds and private equity during the next three years.

Exhibit 13

Expected Changes in Allocations to Alternative Investments by Investor Type and Domicile, 2014 – 2016



Source: 2014 Casey Quirk / eVestment Global Investor Study

Implications for Asset Managers

Shifting demand characteristics among asset owners worldwide are creating tactical product-related opportunities for asset managers. But this year's survey findings also underscore five broad themes reshaping strategic asset allocation among investors globally, with repercussions for asset managers and the way they position their capabilities to clients:

1. **Outcome-oriented investing:** Continually diverging approaches to asset allocation among different types of investors underscores the fact that asset owners and intermediaries increasingly allocate their portfolios among outcomes, not benchmarks. This means an asset manager's products and services will increasingly play different roles in the portfolios of different investors. Recognizing the investor-specific positioning will improve the chances of winning a specific mandate and deepening a client relationship.

2. **Fixed income:** The end of tapering and the prospect of rising rates will be the most powerful short-term trend reshaping retail and institutional investor portfolios. Asset managers who can position their offers within the context of a shift from compartmentalized, benchmark-oriented fixed income assignments to a more dynamic, multi-sector approach to bond investing will benefit dramatically. Winning next-generation products will include multi-asset income portfolios, unconstrained bond mandates, global and emerging market strategies and volatility-managed products.

3. **Liability-driven strategies:** The survey findings clearly indicate that the conversations asset managers have with corporate pensions will differ dramatically than those they have with any other investor. As defined benefit plans move into their twilight phase, they will seek products that help them achieve specific objectives linked to de-risking, liquidity, and cash flow to retirees. Additionally, the competitive environment for these assignments will change, as insurers offer pension risk transfer arrangements. Asset managers will need to separately evaluate and service the opportunities they see in the defined benefit segment.

4. **Real assets:** Increasing allocations and search activity indicate that asset owners have growing demand for non-correlated investments, but seem dissatisfied with the current products—and, by extension, the real asset managers—on offer. This partly reflects that asset managers still sell real assets as illiquid yield generators, rather than developing and positioning real asset products that meet specific outcomes. This is particularly critical given that different asset owners use such products as a means to different ends; for example, corporate pensions use real assets for long-term yield, while non-profits seek alpha. Asset management firms must carefully think through the product and positioning strategies attached to their real asset strategies.

> ***"Size is a factor for real assets. Not every institution can take advantage of opportunities."***

5. **Globalization:** Globalizing portfolios and products is a secular trend well underway in the market. Asset managers, however, also need to explore globalizing their clientele. Alternative asset managers, in particular, must evaluate their ability to distribute their products in Europe and select parts of Asia, where appetite for hedge funds and private equity is now expanding more quickly than it is in the United States, where many investors already have sizeable allocations to alternative investments.

> ***"We're seeing globalization of the benchmark as institutions drop their home-country bias."***

All of these themes imply that positioning investment strategies differently—by asset owner and professional buyer segments—will help asset management firms grow their businesses more sustainably and profitably.

Exhibit 14

Positioning Strategies for Key Asset Classes by Investor Type

	Corporate Pension	Public Pension	Non-Profit	Other Institutional	Retail Intermediary	Defined Contribution
Equity	Growth to match pre-retirees in plan and dividend income	Growth to match pre-retirees in plan and dividend income	Growth to meet return requirements	Capital growth to improve funding ratio	Capital appreciation of retirement and other savings	Retirement accumulation
Fixed Income	Liability matching	Globalized opportunities	Short-term to meet operating requirements	Yield and current income	Income for retirement spending	Capital preservation and income
Alternatives	Liquidity premium for long-dated liabilities, risk management	Liquidity premium for long-dated liabilities, risk management	Meet return requirements and outpace inflation	Diversification and liquidity premium benefits	Volatility protection	Diversification

Source: 2014 Casey Quirk / eVestment Global Investor Study

Evolving investor demand not only shapes competitive positioning in the marketplace, but also the structure of asset management firms. This survey's findings underscore that asset managers seeking greater success in the global marketplace for institutional investment mandates must:

1. **Effectively segment the global institutional marketplace.** The increasingly different needs of various institutional investors will mean an asset manager's product set will not resonate uniformly with asset owners worldwide. As sales cycles increase in duration, segmenting clients by long-term revenue and profit potential will help focus expensive and constrained technical and sales resources on the best prospects.

2. **Develop thought leadership that credibly positions their products within an outcome-oriented context.** Asset managers able to lead broad discussions about investments, markets and portfolios—and translate those opinions into a conversation about how their investment products and strategies will help meet client needs in a rising rate environment—will stand out.

3. **Support data-driven product development processes that meet the increasing complexity of investor needs,** as asset owners measure managers by their ability to meet outcomes rather than beat benchmarks.

4. **Use a strategic engagement model with clients.** As relationships with professional buyers become more complex in an outcome-oriented environment, correctly staffing and structuring both sales and client service to support a consultative approach to institutional clients will become a critical competitive differentiator.

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About eVestment (www.evestment.com)
eVestment provides a flexible suite of easy-to-use, cloud-based solutions to help global investors and their consultants select investment managers, enable asset managers to successfully market their funds worldwide and assist clients to identify and capitalize on global investment trends. With the largest, most comprehensive global database of traditional and alternative strategies, delivered through leading-edge technology and backed by fantastic client service, eVestment helps its clients be more strategic, efficient and informed. The company was founded in 2000 and is headquartered in Atlanta, Georgia with global offices in New York, Toronto, London, Sydney and Hong Kong.

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