



## **The View from Institutional Investors**

Tuesday, May 3, 2011; 2:30 PM – 3:45 PM

### **Moderator:**

Alexander Friedman, Chief Investment Officer, UBS Wealth Management

### **Speakers:**

Janet Cowell, Treasurer, State of North Carolina

Joseph Dear, Chief Investment Officer, California Public Employees' Retirement System (CalPERS)

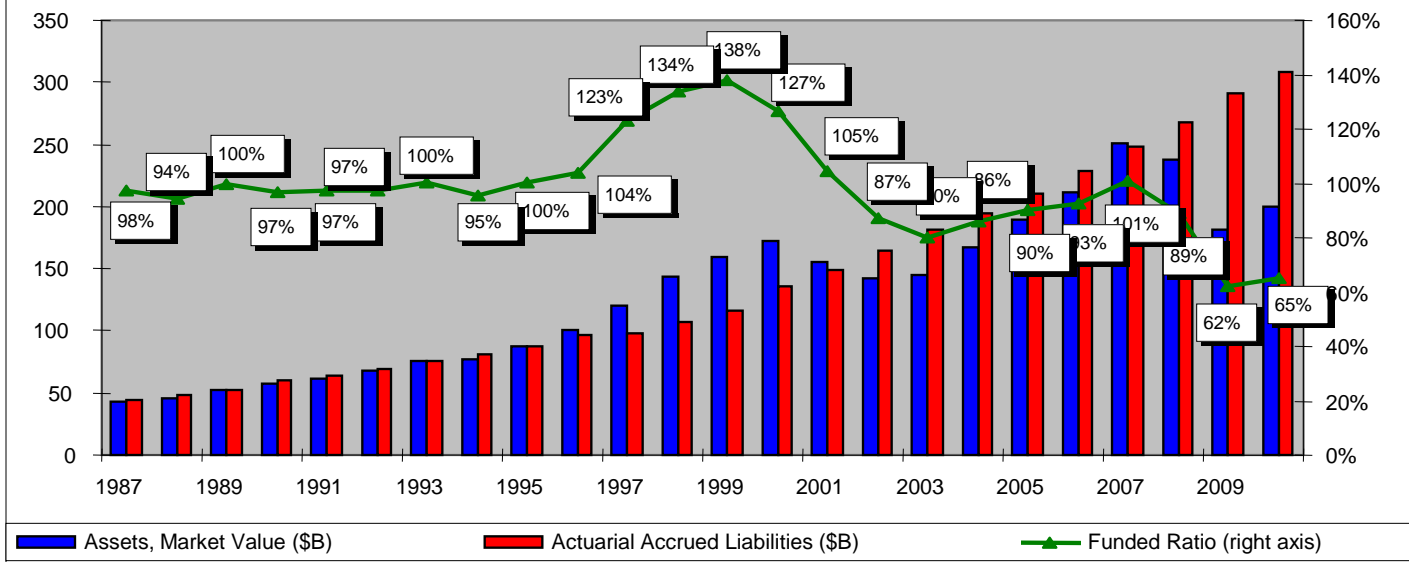
Andy Dillon, Treasurer, State of Michigan

Hazel McNeillage, Head of Funds Management, Queensland Investment Corp.



# **Slides from Joseph Dear Chief Investment Officer, CalPERS**

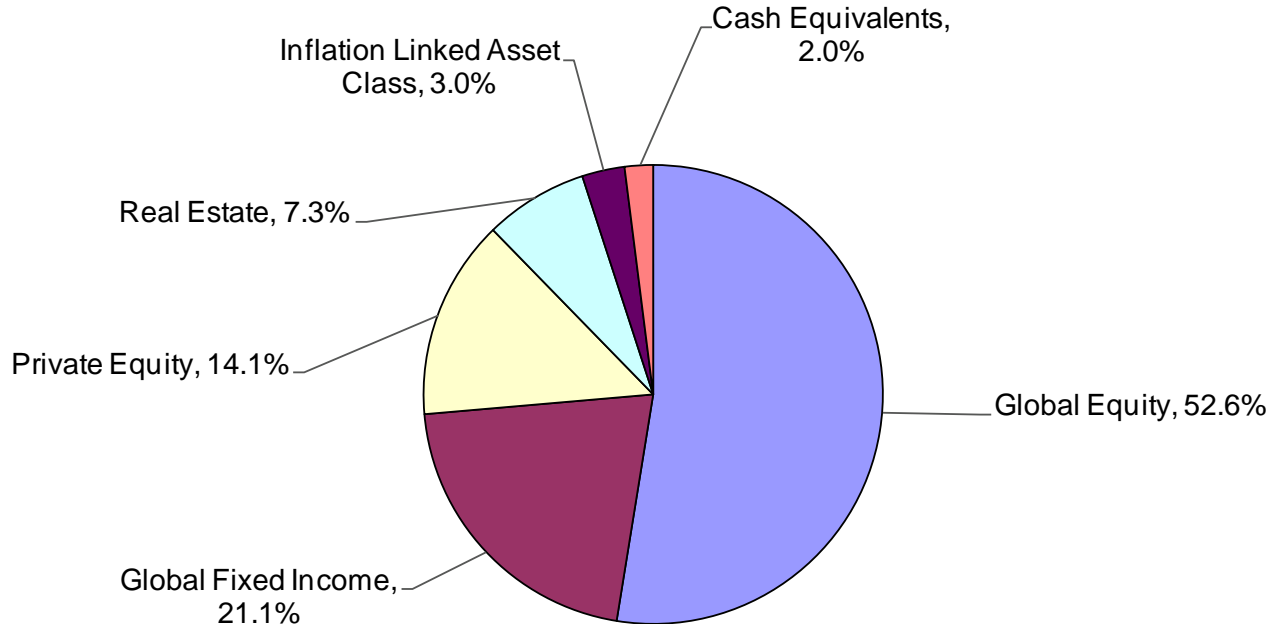
**CalPERS Funded Ratio**  
**Assets and Actuarial Accrued Liabilities, fy 1987-2010**



## Actual Asset Allocation as of December 31, 2010

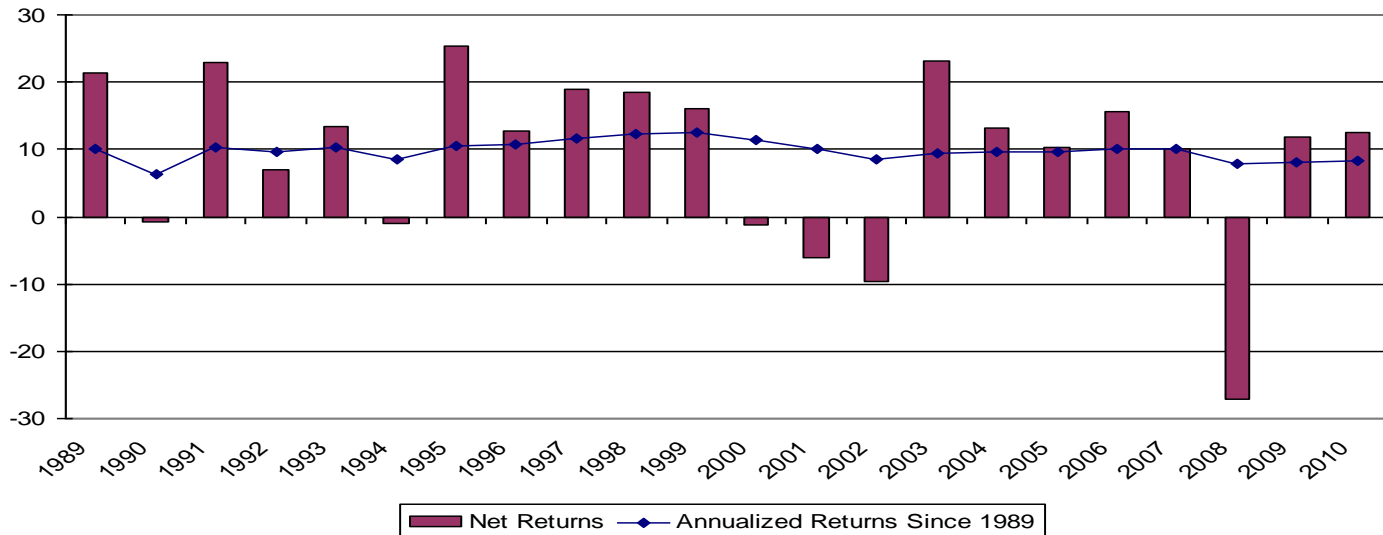


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### Total Fund - Historical Net Returns Calendar Year End

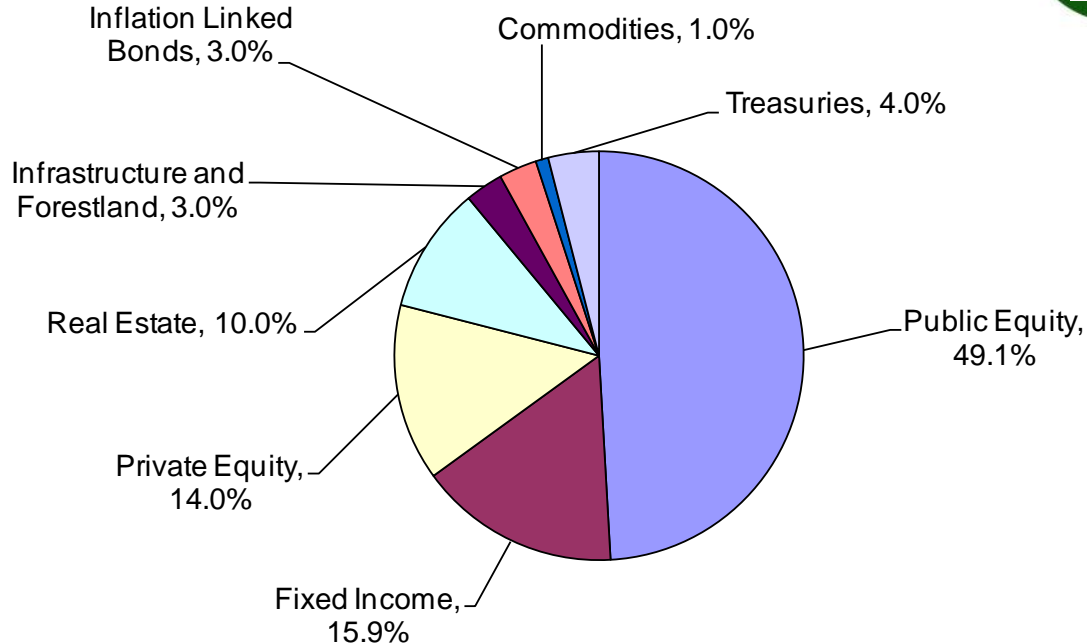


## Target Asset Allocation

Approved December 13, 2010



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**Slides from Andy Dillon  
Treasurer, State of Michigan**

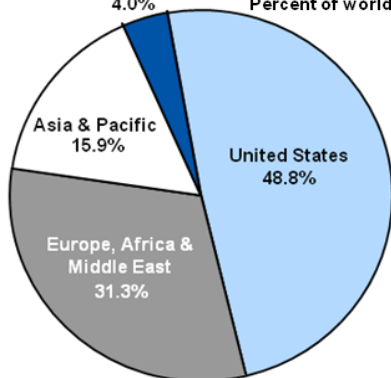
# World equity markets – share and growth

*Total market capitalization (in US Dollars) of domestic companies listed on member exchanges of the World Federation of Exchanges*



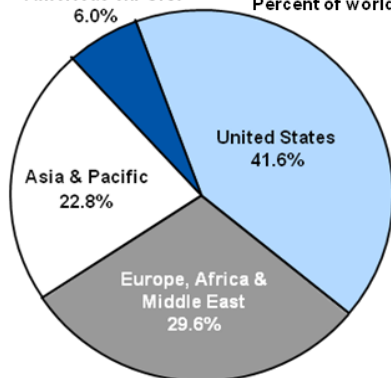
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**2000**  
Americas ex. U.S. 4.0%  
Percent of world



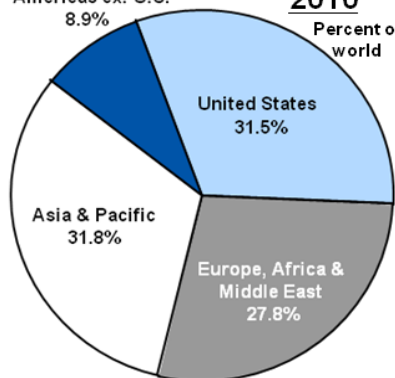
**2000 - 2005**

**2005**  
Americas ex. U.S. 6.0%  
Percent of world



**2005 - 2010**

**2010**  
Americas ex. U.S. 8.9%  
Percent of world



**2000 - 2010**

**5 Year (Compound Annual Growth Rate)**

**5 Year (Compound Annual Growth Rate)**

**10 Year (Compound Annual Growth Rate)**

<b>World Markets</b>	<b>5.72%</b>
<b>Americas</b>	<b>3.54%</b>
United States	2.39%
Americas ex. U.S.	14.65%
<b>Europe, Africa &amp; Middle East</b>	<b>4.56%</b>
<b>Asia &amp; Pacific</b>	<b>13.62%</b>

<b>World Markets</b>	<b>6.06%</b>
<b>Americas</b>	<b>2.65%</b>
United States	0.33%
Americas ex. U.S.	14.76%
<b>Europe, Africa &amp; Middle East</b>	<b>4.74%</b>
<b>Asia &amp; Pacific</b>	<b>13.37%</b>

<b>World Markets</b>	<b>5.89%</b>
<b>Americas</b>	<b>3.09%</b>
United States	1.35%
Americas ex. U.S.	14.70%
<b>Europe, Africa &amp; Middle East</b>	<b>4.65%</b>
<b>Asia &amp; Pacific</b>	<b>13.49%</b>



# World economies – share and growth

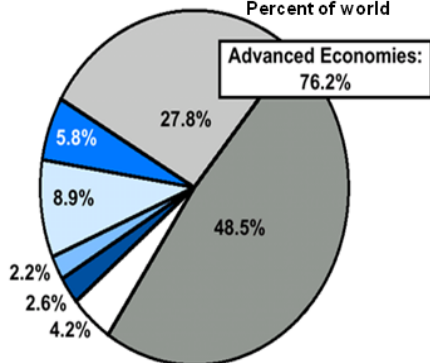
Year-end GDP, current prices, in US Dollars, Source: IMF



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2000

Percent of world



Legend

Advanced Economies

United States  
Advanced Economies ex. U.S.

Emerging and Developing Economies

Africa and Middle East  
Central and Eastern Europe  
Commonwealth of Independent States\*  
Developing Asia  
Latin America and the Caribbean



World

Advanced Economies

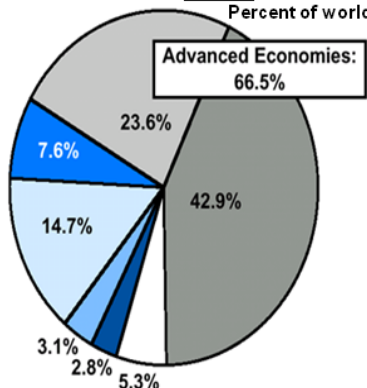
United States  
Advanced Economies ex U.S.

Emerging and Developing Economies

Africa and Middle East  
Central and Eastern Europe  
Commonwealth of Independent States\*  
Developing Asia  
Latin America and the Caribbean

2005

Percent of world



Compound annual growth rate

2005-2010

2010-2015

2005-2015

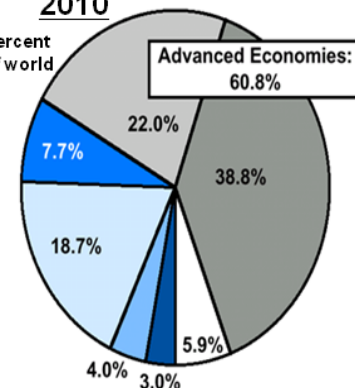
World 6.36%  
Advanced Economies 3.49%  
United States 2.96%  
Advanced Economies ex U.S. 3.79%  
Emerging and Developing Economies 13.94%  
Africa and Middle East 11.34%  
Central and Eastern Europe 7.93%  
Commonwealth of Independent States\* 14.18%  
Developing Asia 17.55%  
Latin America and the Caribbean 12.06%

World 5.75%  
Advanced Economies 3.87%  
United States 4.28%  
Advanced Economies ex U.S. 3.65%  
Emerging and Developing Economies 9.14%  
Africa and Middle East 8.12%  
Central and Eastern Europe 7.04%  
Commonwealth of Independent States\* 10.91%  
Developing Asia 10.94%  
Latin America and the Caribbean 6.00%

World 6.06%  
Advanced Economies 3.68%  
United States 3.62%  
Advanced Economies ex U.S. 3.72%  
Emerging and Developing Economies 11.51%  
Africa and Middle East 9.72%  
Central and Eastern Europe 7.48%  
Commonwealth of Independent States\* 12.53%  
Developing Asia 14.20%  
Latin America and the Caribbean 8.99%

2010

Percent of world



## **Additional Slides**

# Strong financial recovery in U.S.

*Particularly in much of 2009 and early 2010*



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Note: Data are as of April 19, 2011.

Source: Bloomberg.

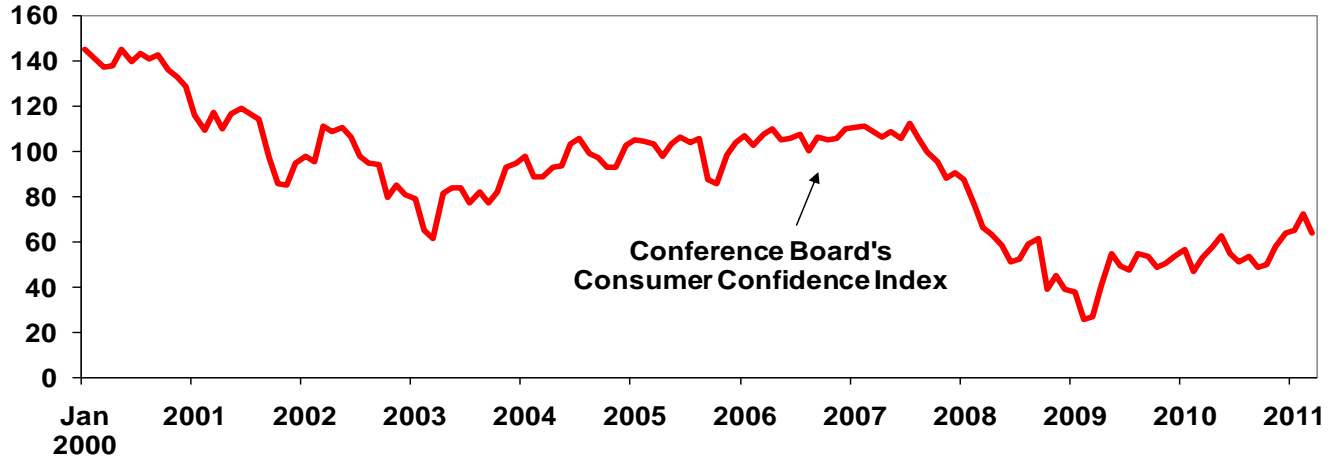
# U.S. consumer confidence improves slowly



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*Confidence improves slowly U.S. Consumer Confidence Index*

Index (1985=100)

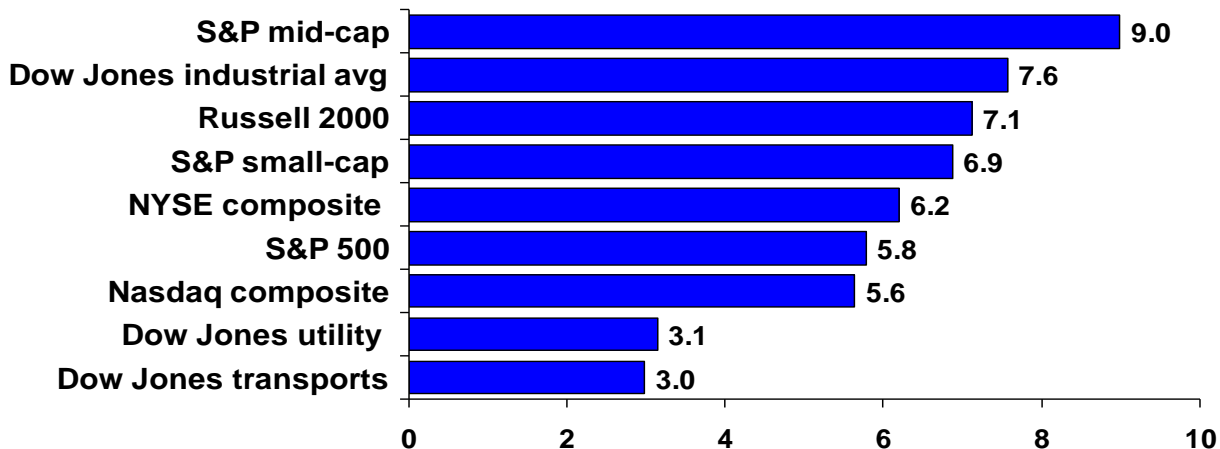


Source: Bloomberg.



# 2011: U.S. stock market is off to a good start

2011 YTD gains for key U.S. stock indexes (%)  
(as of 04/20/2011)

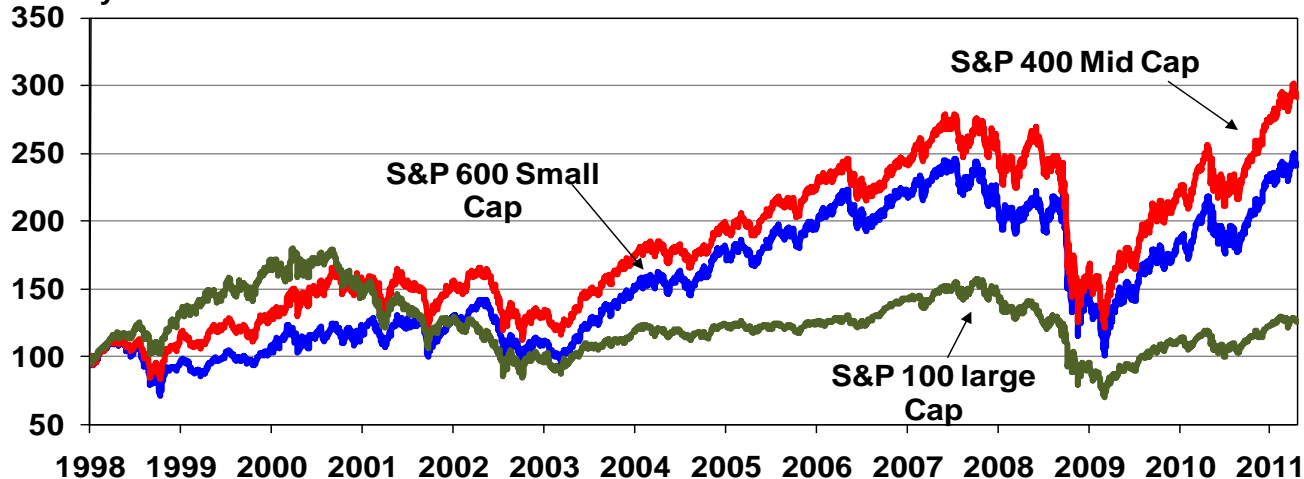


# The U.S. small- and mid-cap stocks outperform



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January 1998 = 100



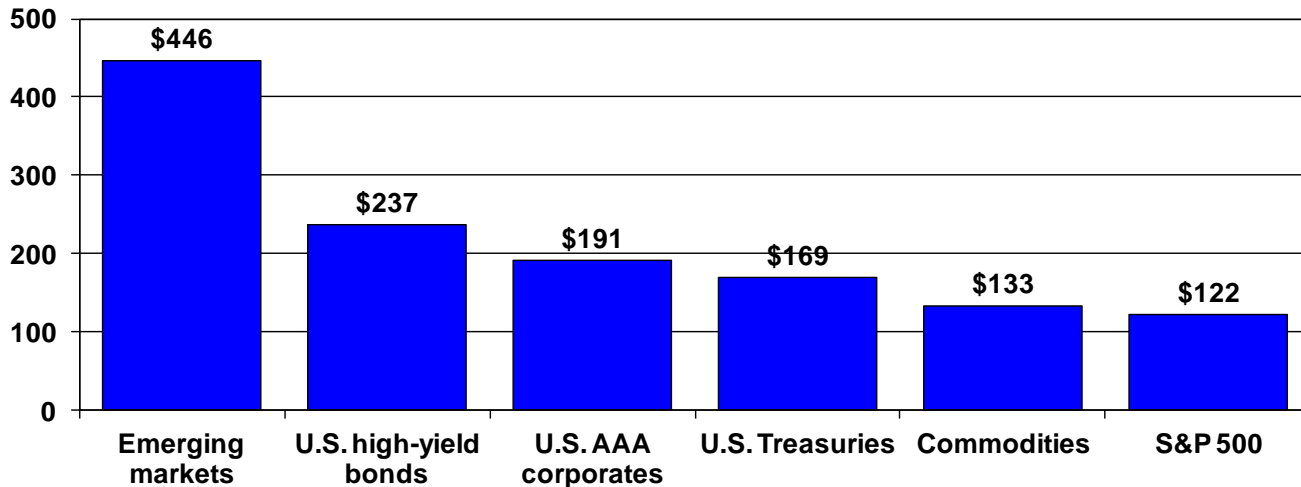
Note: Data are as of April 19, 2011.

Source: Bloomberg.



# Investment returns for selected asset classes

As of March 2011, a \$100 investment made in December 2000 gives you:



Sources: Bloomberg, Milken Institute.

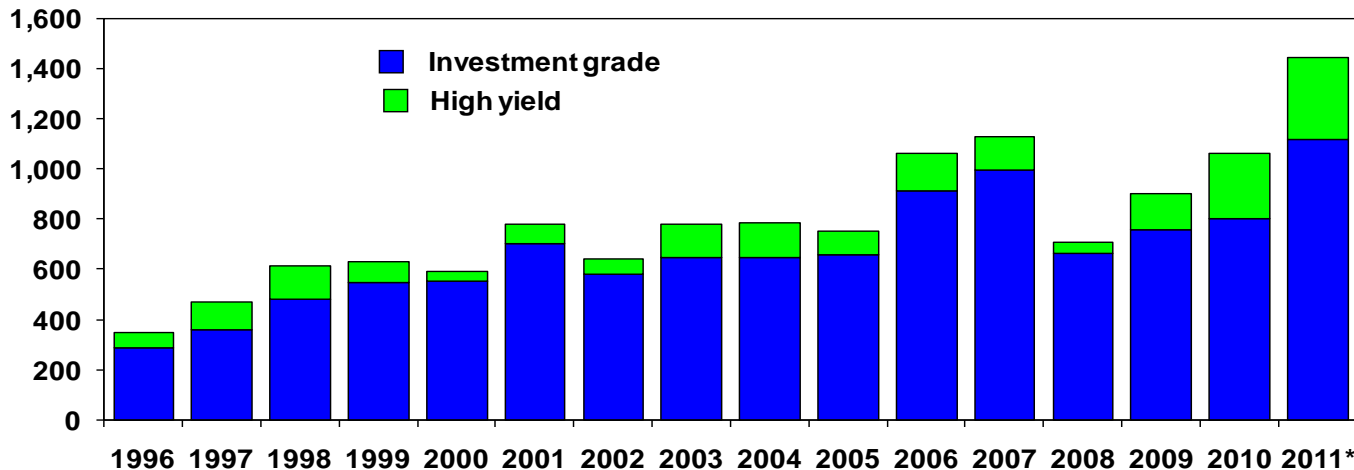
# A record issuance of high-yield bonds in 2010-11



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## United States

Total issuance (US\$ billions)



\* Year to date, annualized.

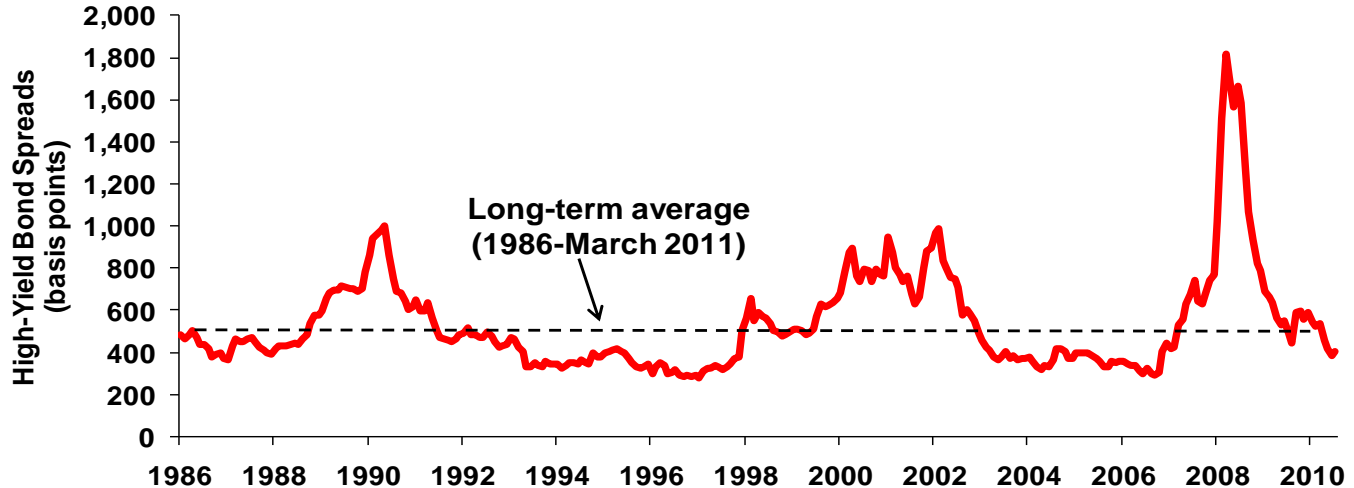
Source: Securities Industry and Financial Markets Association .



# U.S. high-yield bond spread over Treasury is at its historical average



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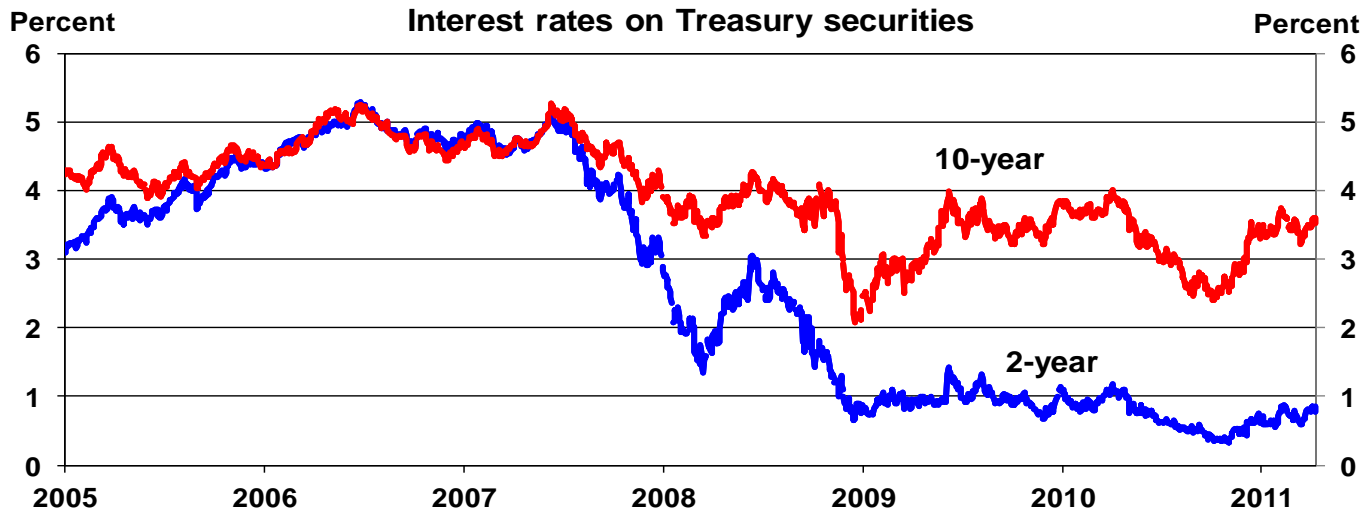


Note: Spread is the difference between the U.S. high-yield Merrill Lynch Master II index and 10-Year treasury bond  
Source: Bloomberg.

# U.S. Treasury yields remained low by historical standards



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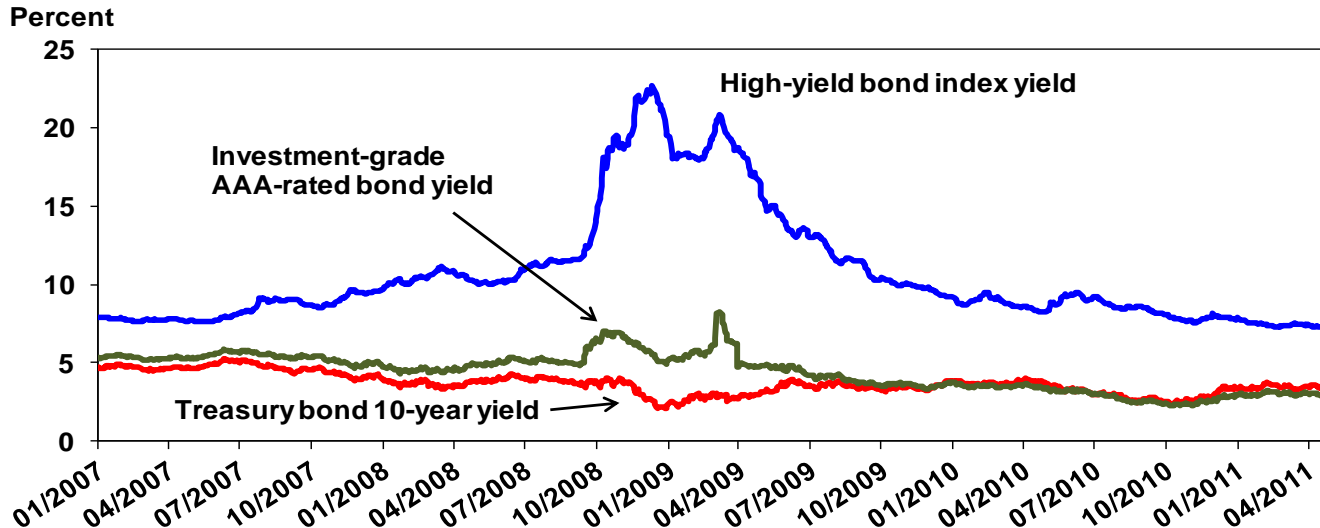
Source: Federal Reserve.

# Credit spreads have returned to low levels

*United States*



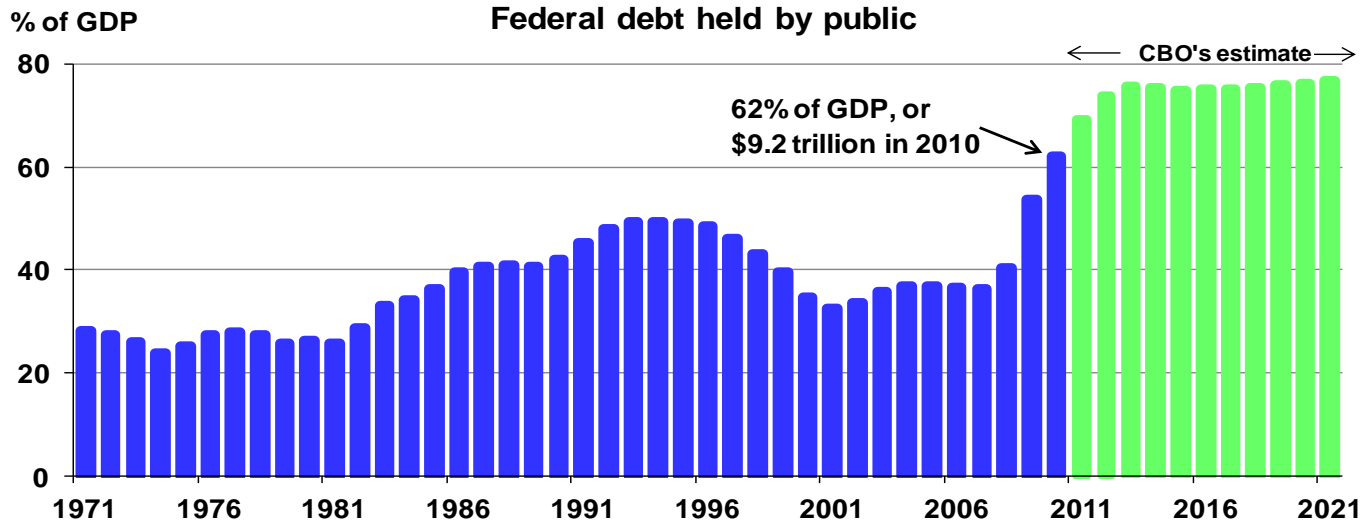
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# U.S. national debt will be close to 80% of GDP in the next decade



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Source: Congressional Budget Office (CBO).

# Are rate-of-return assumptions too high?

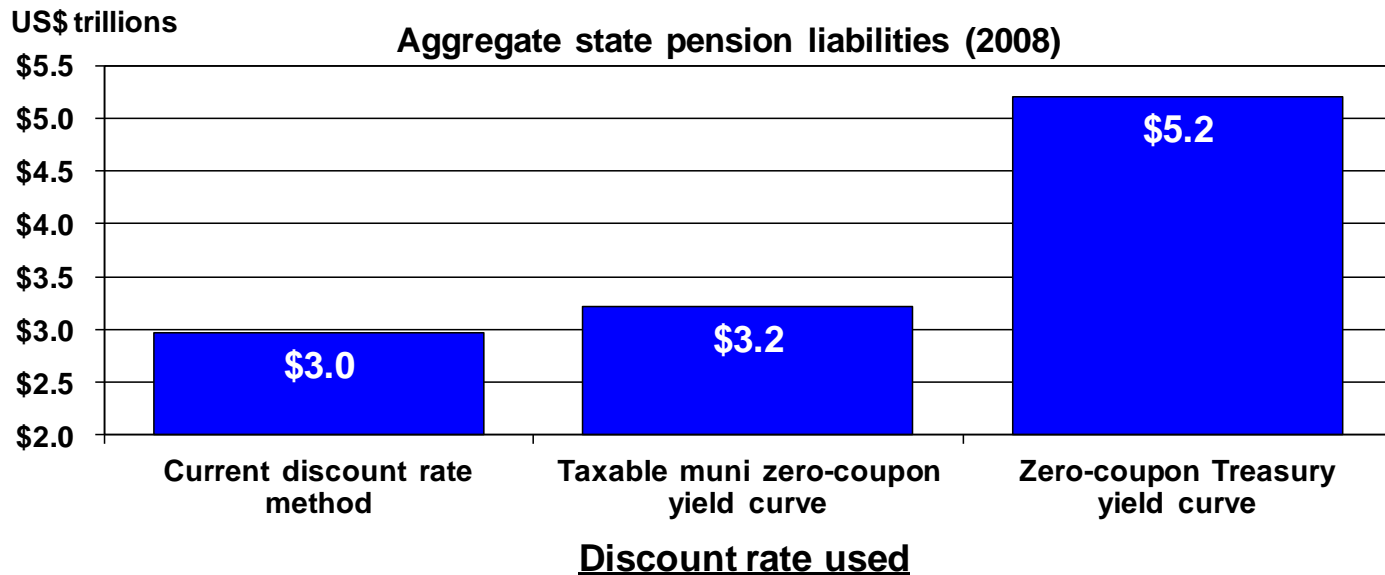
*Hurdle rates of the largest public pension funds in each state*



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Assumed rate of return	# of states with rate	States
7.25%	2	NC, SC
7.50%	7	GA, IN, IA, KY, TN, VA, WV
7.75%	7	CA, FL, ID, ME, MD, SD, UT
7.80%	1	WI
8.00%	22	AL, AZ, AR, DE, HI, KS, MI, MS, MO, MT, NE, NV, NM, NY, ND, OH, OK, OR, PA, TX, WA, WY
8.25%	6	AK, LA, MA, NJ, RI, VT
8.50%	5	CO, CT, IL, MN, NH

# Already-promised state pension liabilities rise significantly with lower return assumptions

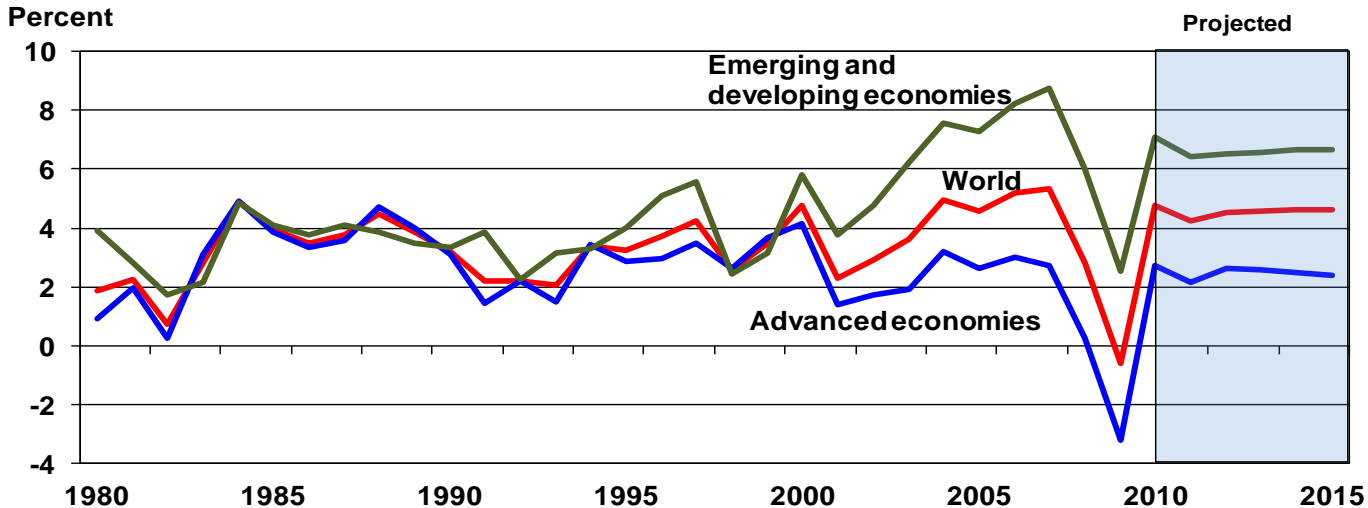


# World economic recovery



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*Real GDP growth rates, 1980-2015*



# World output forecasts

*Percent change from previous year*



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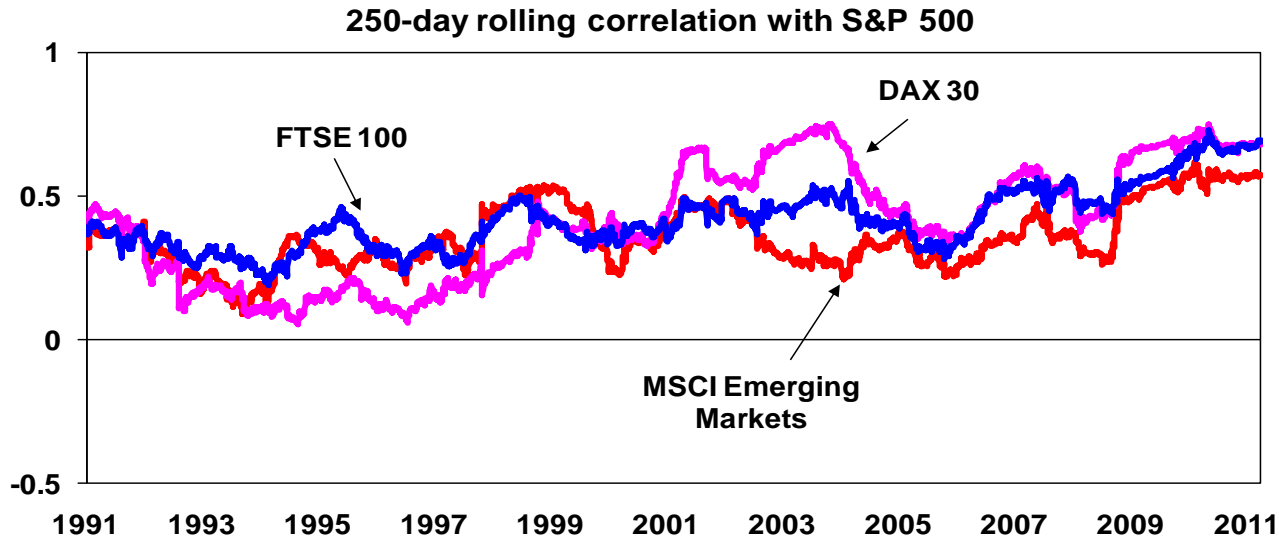
	2010	2011F	2012F
<b>World</b>	<b>5.0</b>	<b>4.4</b>	<b>4.5</b>
<b>Advanced economies</b>	<b>3.0</b>	<b>2.4</b>	<b>2.6</b>
United States	2.8	2.8	2.9
Japan	3.9	1.4	2.1
United Kingdom	1.3	1.7	2.3
Euro area	1.7	1.6	1.8
<b>Emerging and developing economies</b>	<b>7.3</b>	<b>6.5</b>	<b>6.5</b>
Brazil	7.5	4.5	4.1
China	10.3	9.6	9.5
India	10.4	8.2	7.8
Russia	4.0	4.8	4.5

Source: World Economic Outlook, International Monetary Fund, April 2011.





# Global stock markets are highly correlated



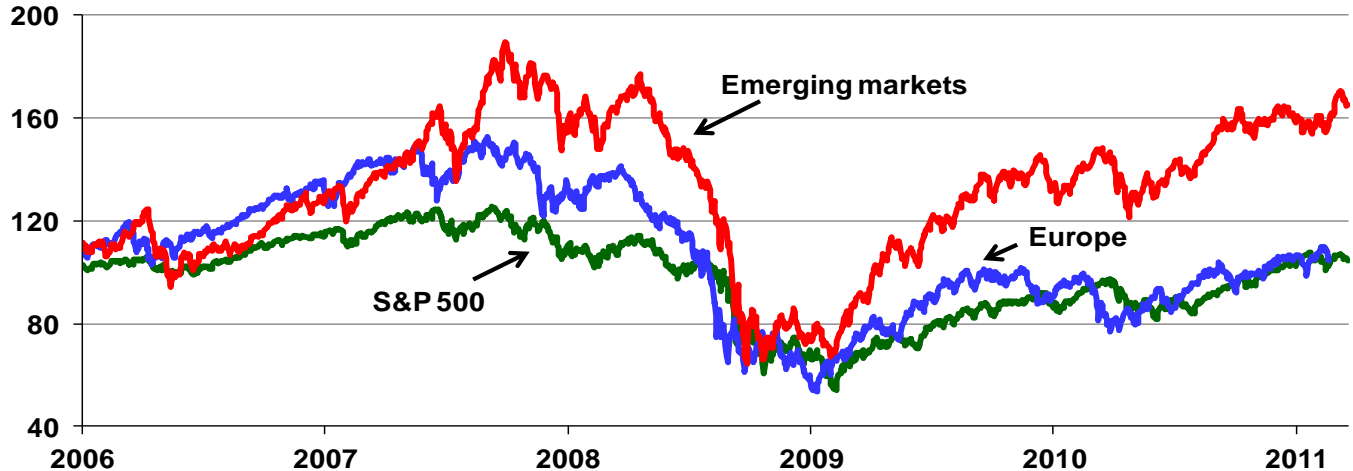
Positive & highly  
correlated

# Stock prices around the world gained strongly, but remained below their pre-crisis peaks



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January 2006 = 100



Note: Data are as of April 20, 2011.

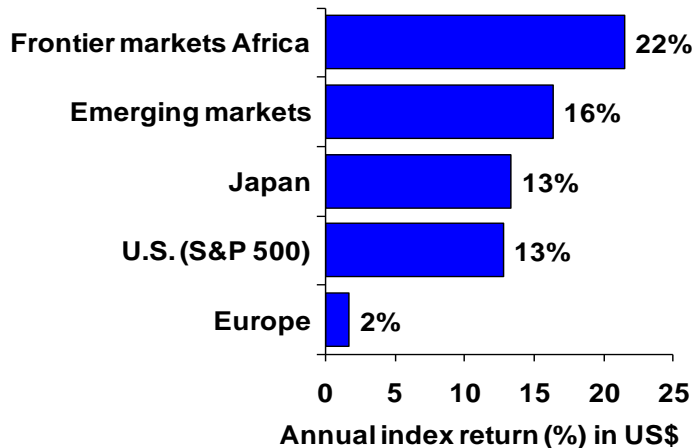
Source: Bloomberg.

# Will 2011 be another strong year for global stock markets?

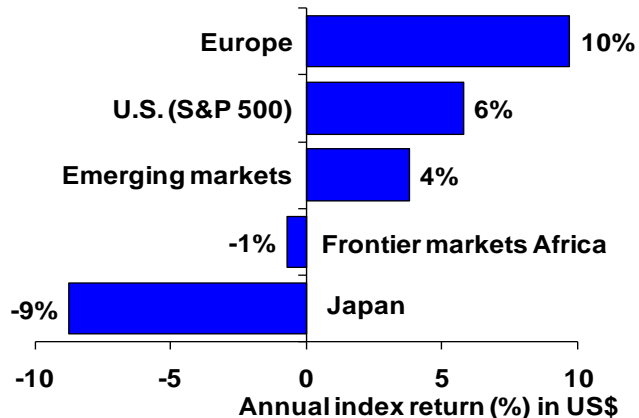


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2010



YTD (as of 4/20/2011)



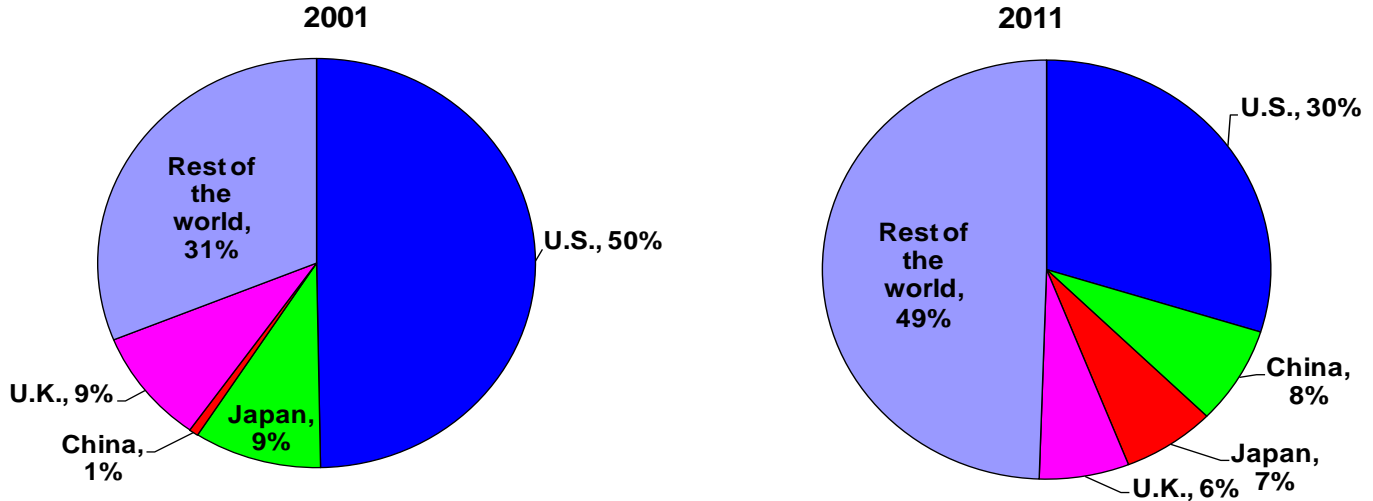
Note: the regional equity indices are based on the MSCI equity indices.  
Source: Bloomberg.

# U.S. stock market's share is shrinking

*Share of the world's market capitalization*



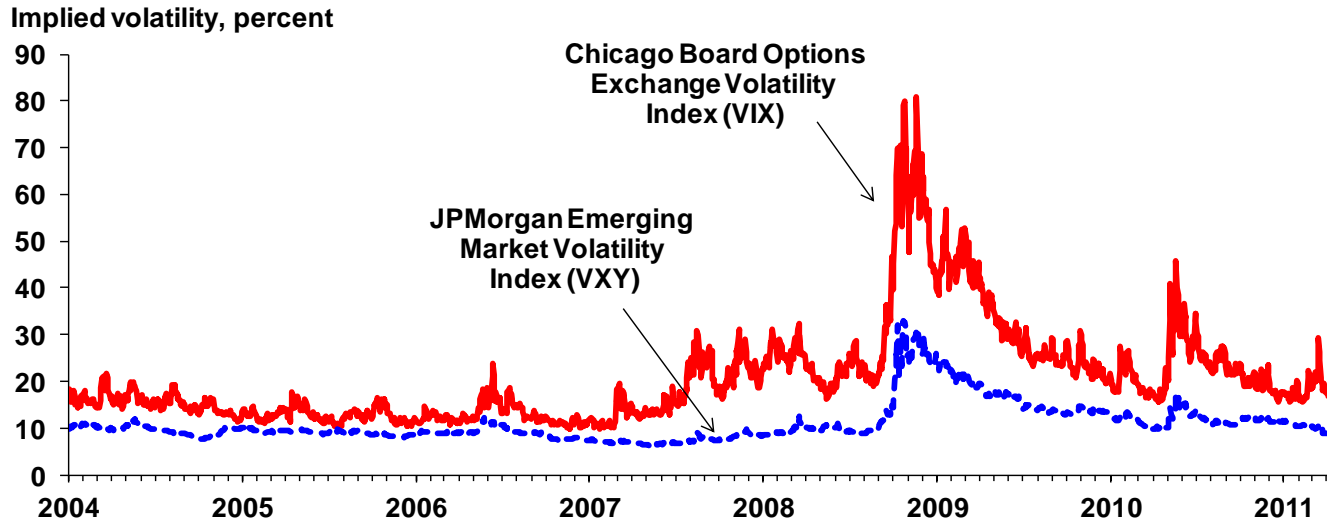
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Note: The 2011 data are as of April 18, 2011.  
Source: Bloomberg.



# Implied volatility: U.S. vs. emerging markets



Source: Bloomberg.

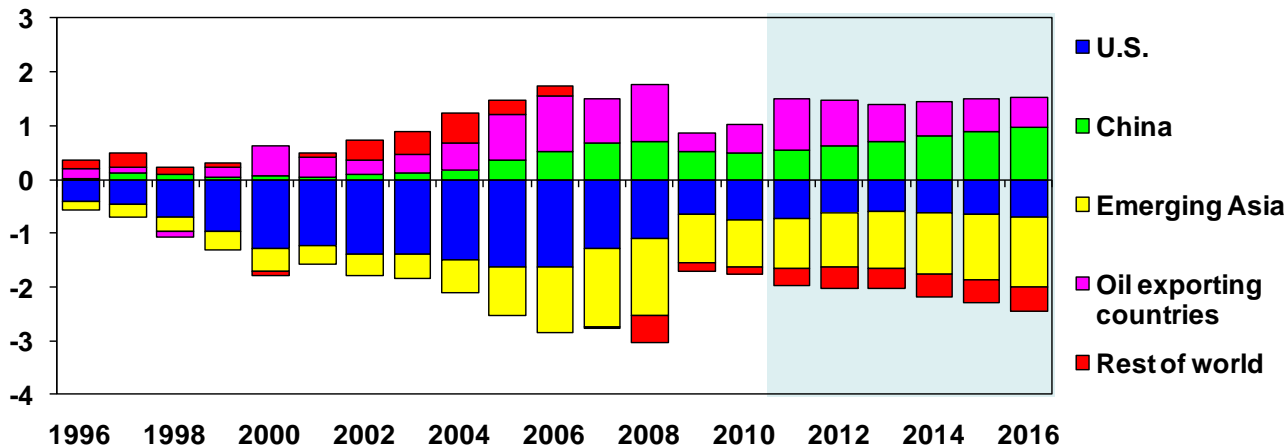
# Global imbalances on the rise again

*Projections after 2010*



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Percent of world GDP



Sources: International Monetary Fund, Milken Institute.

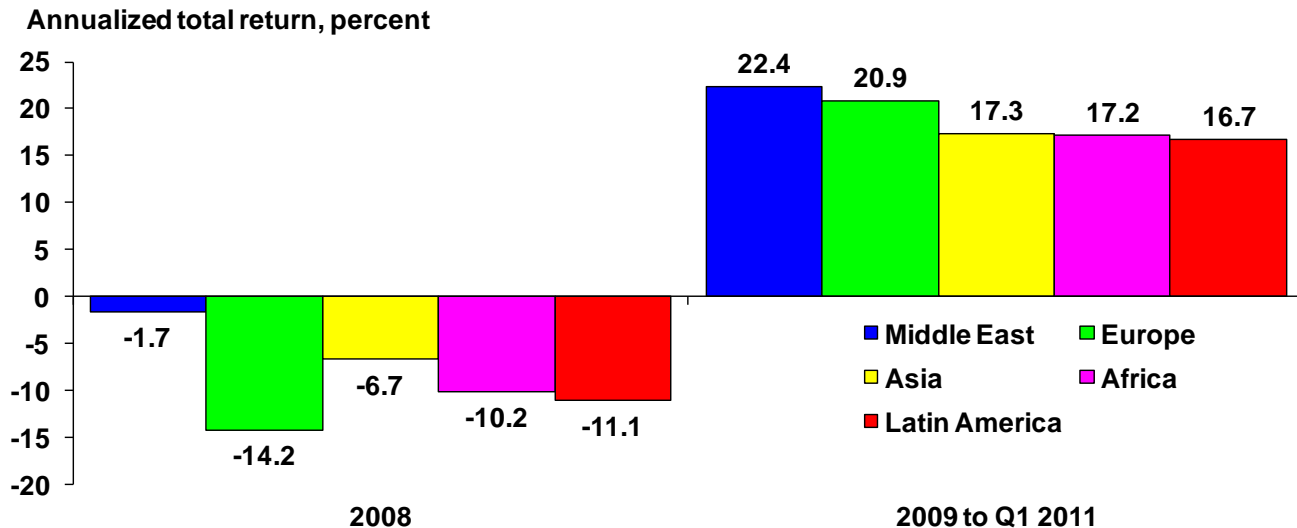
Note: Discrepancies are not plotted.

# Performance of emerging bond markets

*Total return of JPMorgan EMBI Global indexes*



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Sources: DataStream, Milken Institute.



# The persistence of sovereign defaults

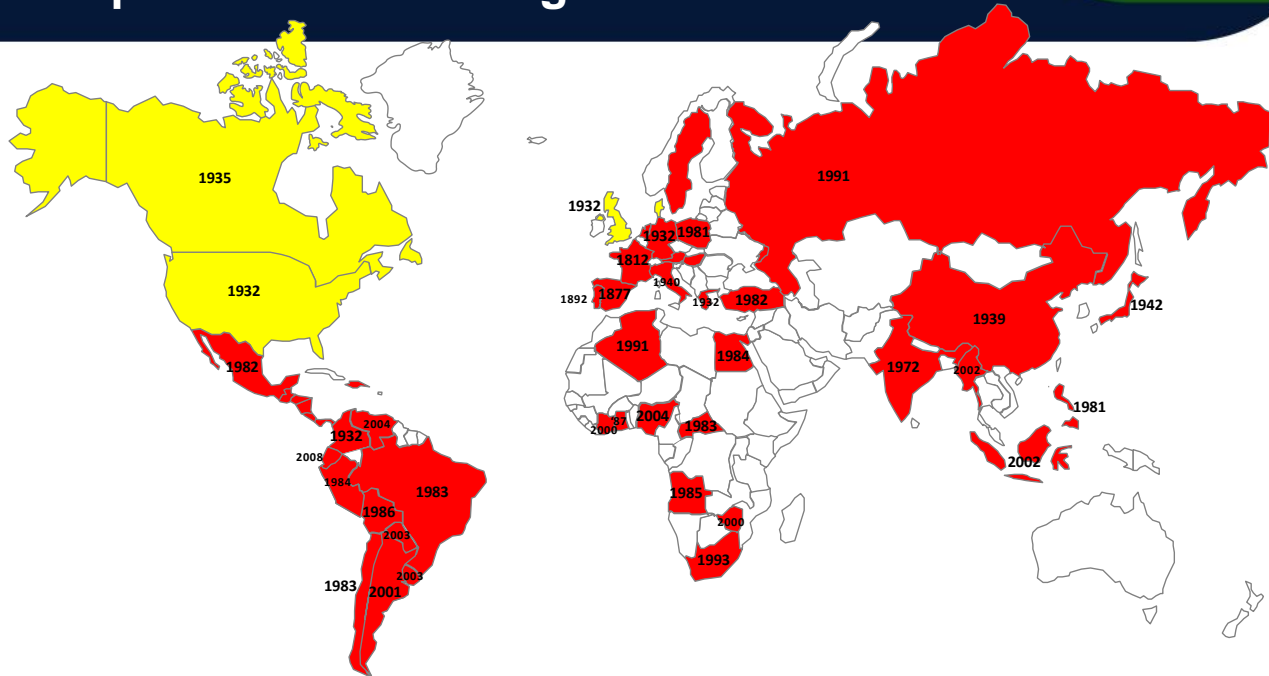
## Sovereign defaults in selected countries, 1824 to 2008

Argentina	Ecuador	Paraguay	Uruguay	Venezuela
<ul style="list-style-type: none"><li>• 1830</li><li>• 1890</li><li>• 1915</li><li>• 1930s</li><li>• 1982</li><li>• 2001</li></ul>	<ul style="list-style-type: none"><li>• 1832</li><li>• 1868</li><li>• 1911</li><li>• 1914</li><li>• 1931</li><li>• 1982</li><li>• 1999</li><li>• 2008</li></ul>	<ul style="list-style-type: none"><li>• 1827</li><li>• 1874</li><li>• 1892</li><li>• 1920</li><li>• 1932</li><li>• 1986</li><li>• 2003</li></ul>	<ul style="list-style-type: none"><li>• 1876</li><li>• 1891</li><li>• 1915</li><li>• 1933</li><li>• 1983</li><li>• 2003</li></ul>	<ul style="list-style-type: none"><li>• 1832</li><li>• 1878</li><li>• 1892</li><li>• 1898</li><li>• 1932</li><li>• 1998</li></ul>

Sources: Sturzenegger and Zettelmayer (2006), Moody's, Milken Institute.



# A map for world sovereign default



# Sovereign debt most likely to default in five years

*As of Q1 2011*



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Rank	Country	Five-year cumulative probability of default (%)
1	Greece	57.7
2	Venezuela	51.8
3	Ireland	43.0
4	Portugal	40.1
5	Argentina	34.7

Rank	Country	Five-year cumulative probability of default (%)
6	Ukraine	27.7
7	Dubai	24.7
8	Lebanon	21.9
9	Iraq	21.1
10	Egypt	21.1

Source: CMA Global Sovereign Credit Risk Report.

Note: Ranked by five-year cumulative probability of default.

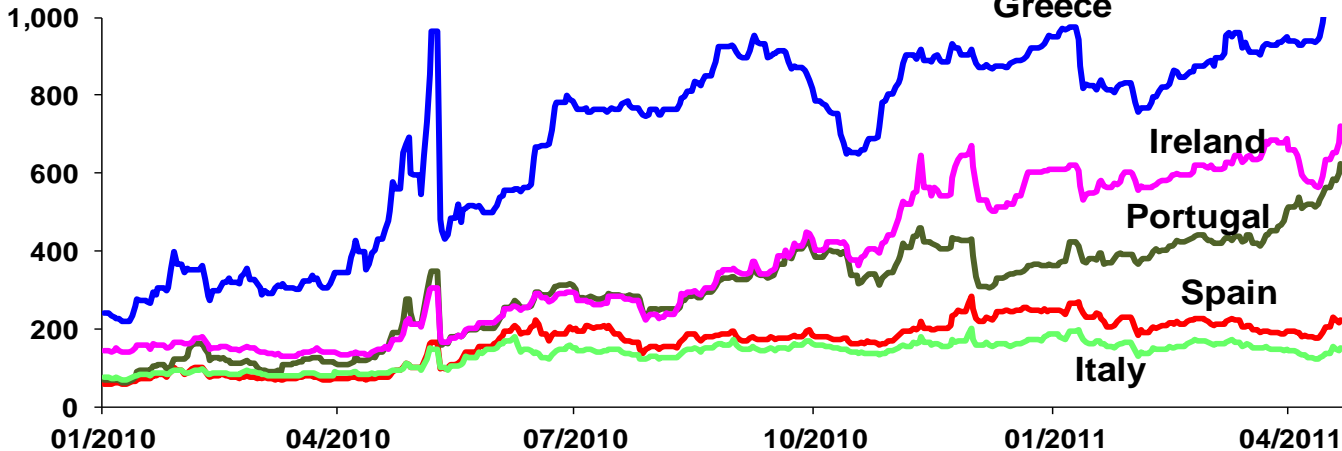
# European sovereign debt crisis

*Widening spreads over German government bond*



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10-year gov't bond spreads over  
German gov't bond (basis points)



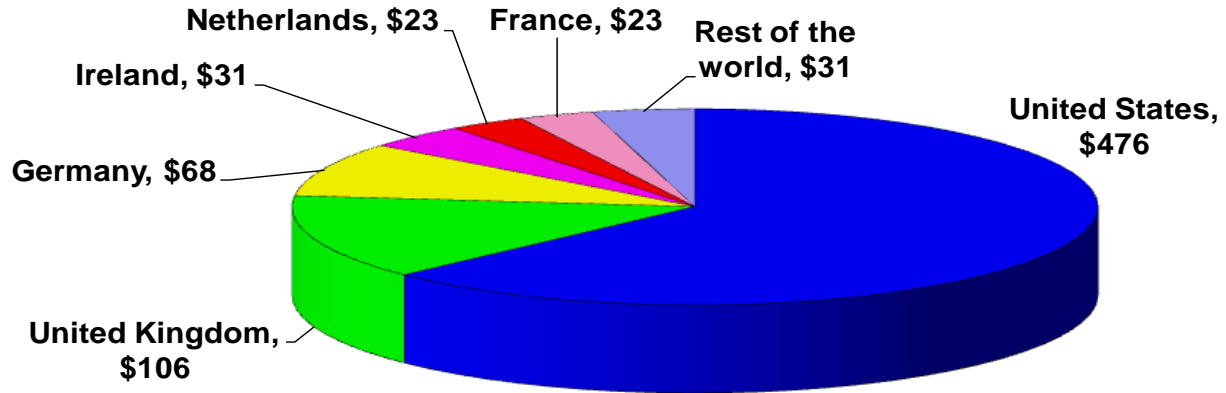
# Total financial bailouts by country



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## *Government capital investments in financial firms*

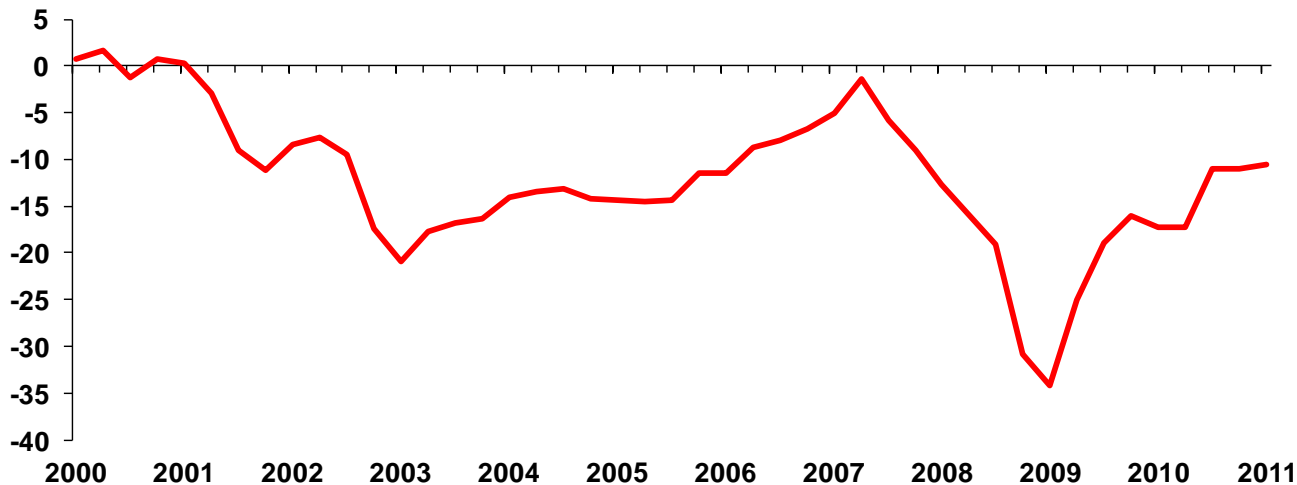
Total outstanding = \$757 billion  
Data as of April 20, 2011 (US\$ billions)





# Consumer confidence index: Eurozone

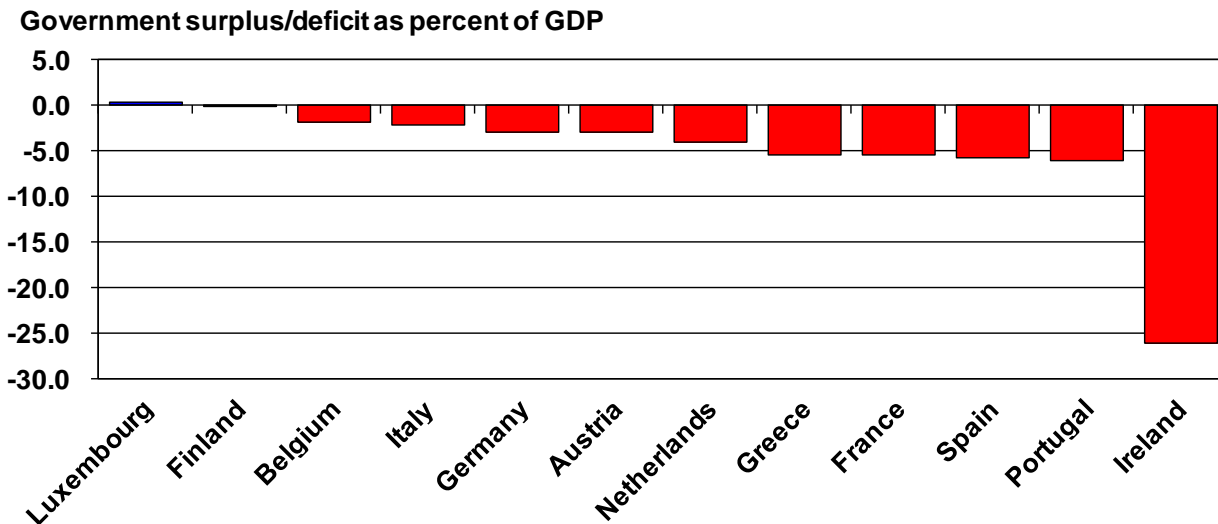
Consumer confidence index



Sources: Eurostat, Bloomberg.



# Fiscal deficit for selected Eurozone countries



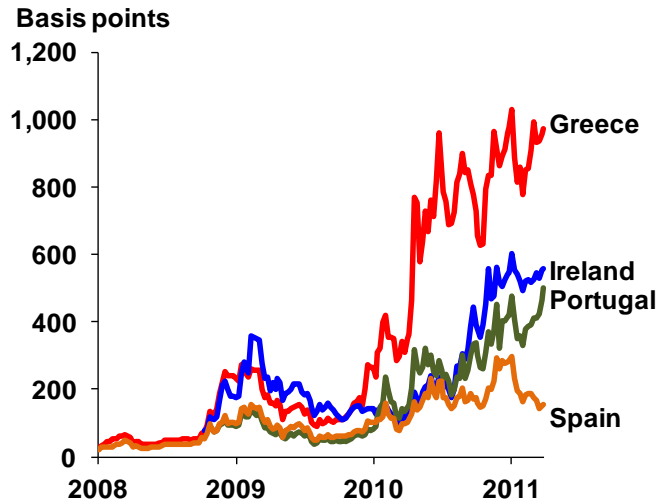
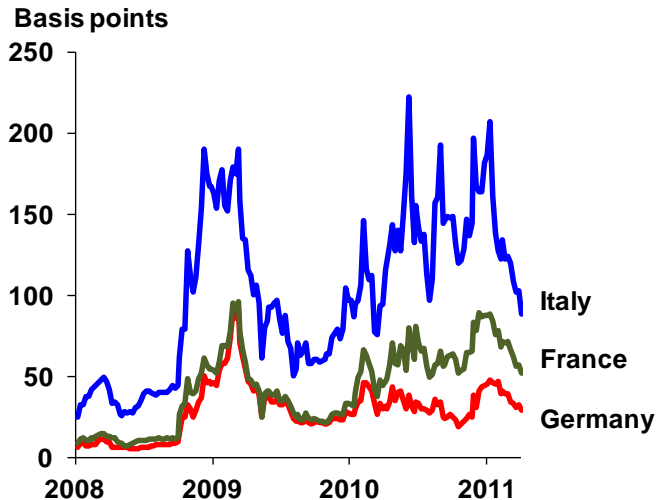
Source: OECD.

# Sovereign risks heightened after 2009

*Credit default swap spreads, five-year government bonds*



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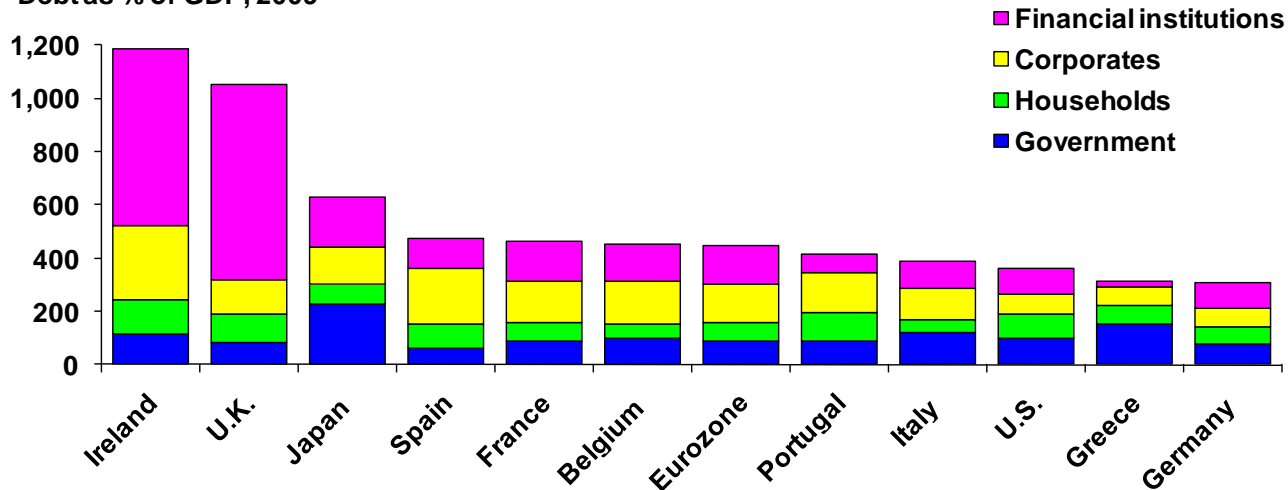


Source: DataStream.



# Debt-to-GDP ratios in selected countries

Debt as % of GDP, 2009



Source: International Monetary Fund.

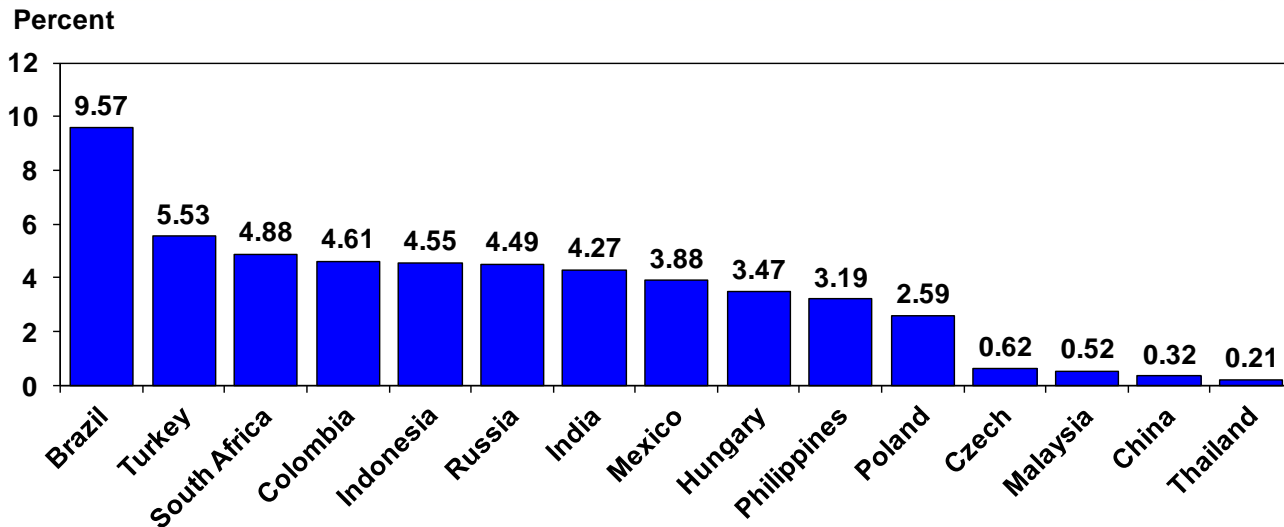


# Emerging market bond yield spreads

*As of April 8, 2011*

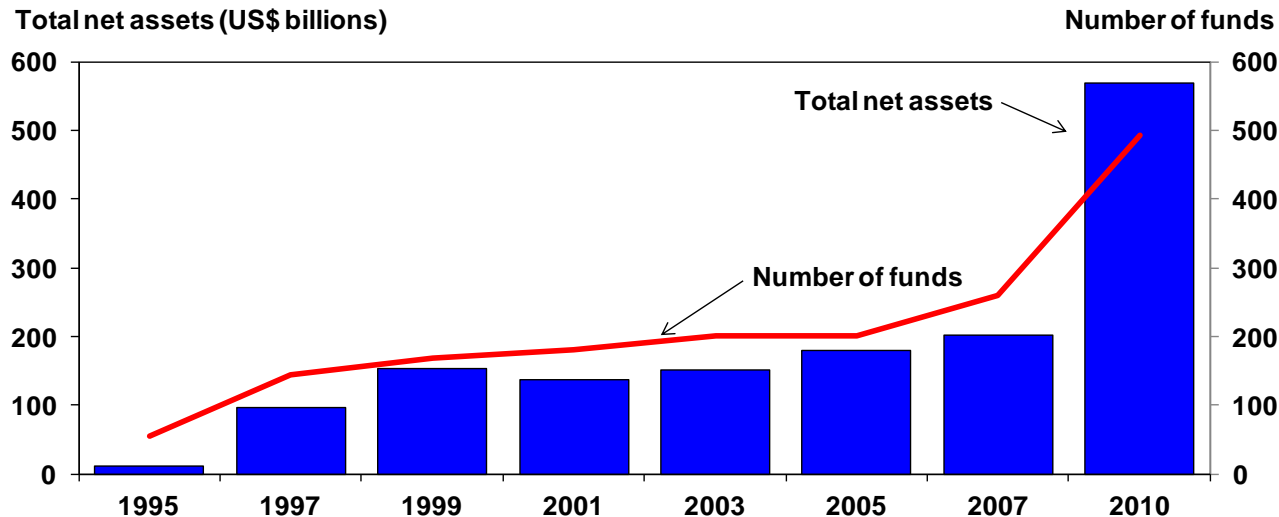


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# Growth of investment funds using ESG factors

*Investment funds incorporating ESG factors, 1995-2010*

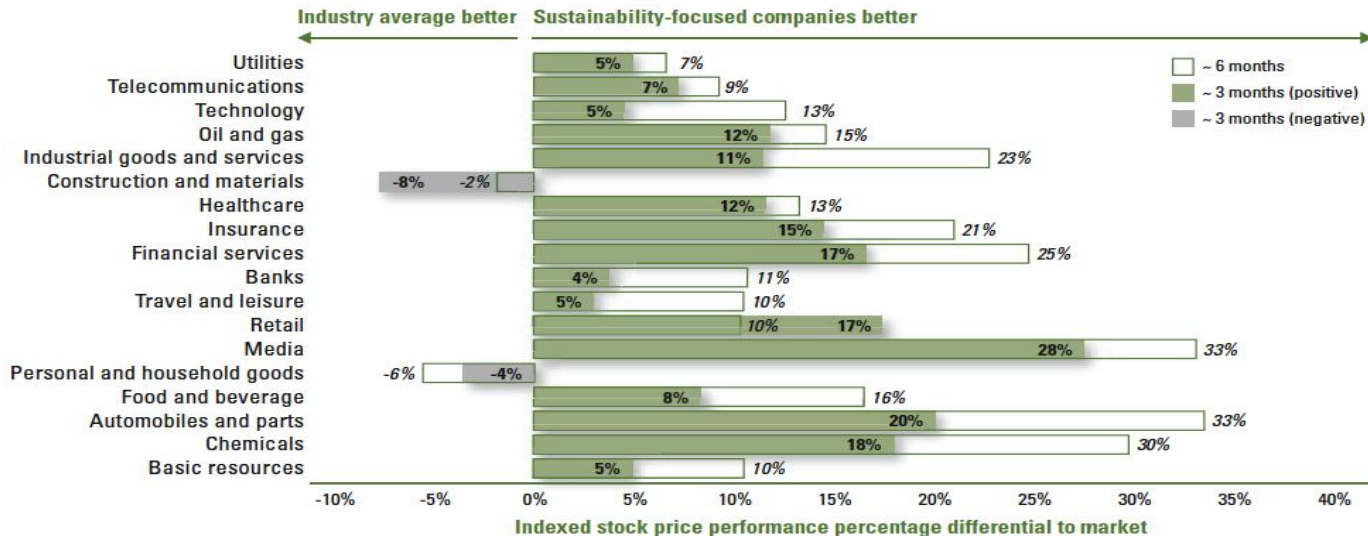


Note: ESG funds include mutual funds, annuity funds, closed-end funds, exchange-traded funds (ETFs), alternative investment funds and other pooled products, but exclude separate account vehicles.

Source: Social Investment Forum Foundation.

# Green Winners: Sustainable companies outperform peers

**FIGURE:** Sustainability-focused companies outperform peers



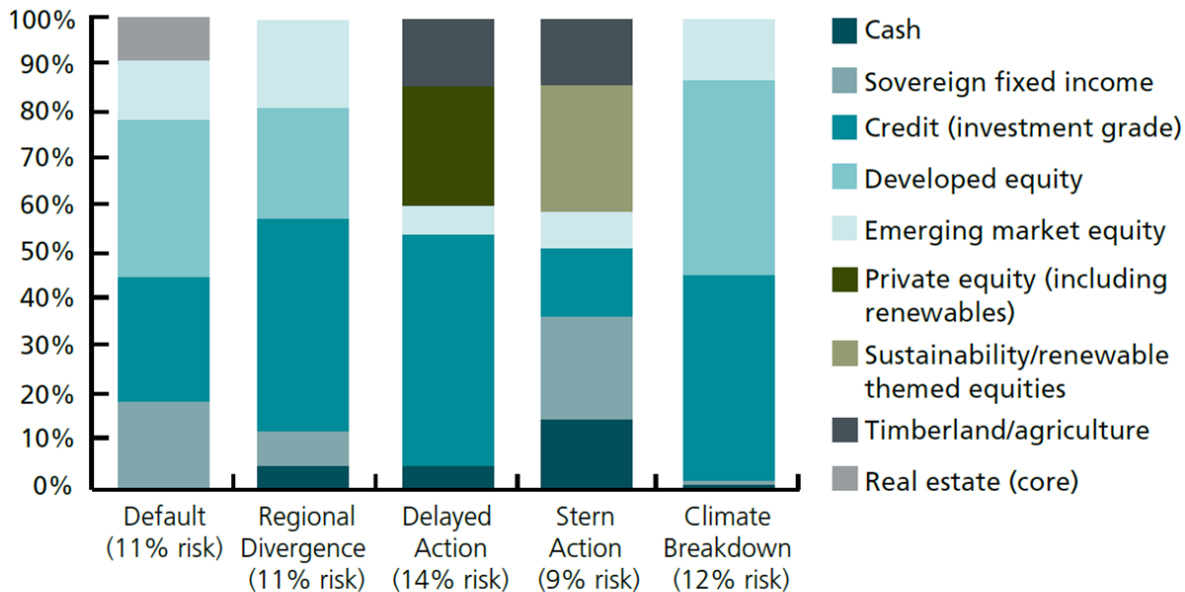
Note: Indexed stock prices at ~ 3 months = September 8, 2008 and ~ 6 months = May 19, 2008 to current date, November 24, 2008. Percentage performance differential calculated by taking the percentage point difference of averaged sustainability companies' indexed performance to the market indexed performance over the market indexed performance. Sustainability companies include DJSI World 80 2008/2009 + DJSI 2008 Supersector Leaders + Goldman Sachs SUSTAIN focus list for mature industries.

# Managing climate change risk across scenarios

*Portfolio to target 7% return*



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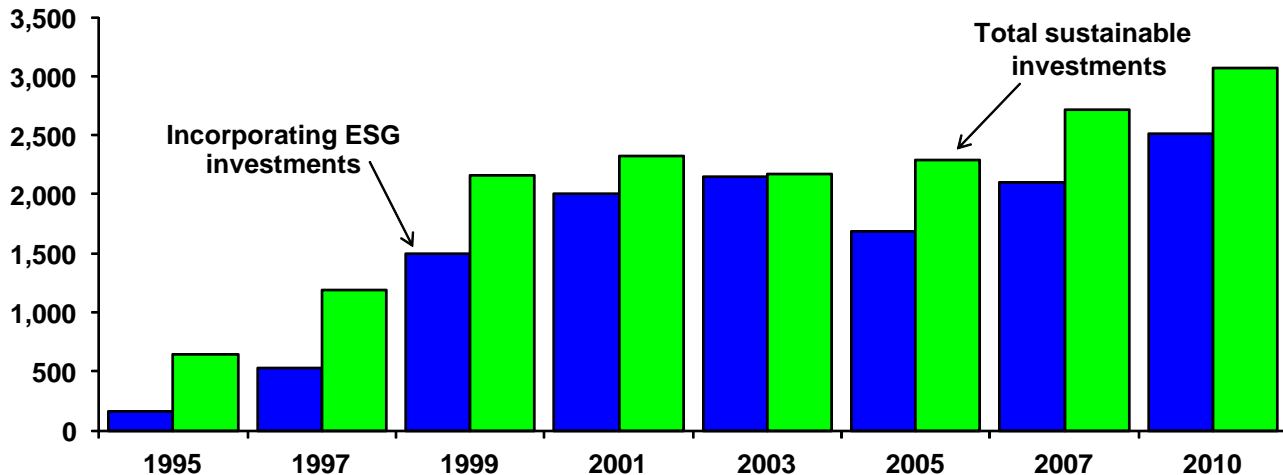
# ESG factors are increasing in U.S. investments



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*Sustainable investing, 1995-2010*

Sustainable investing (US\$ billions)



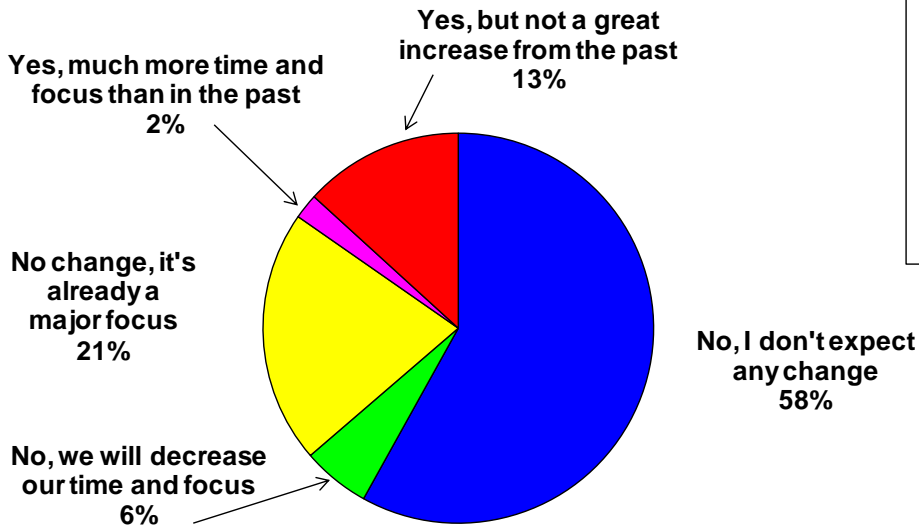
Note: Overlapping assets involved in some combination of ESG incorporation, filing shareholder resolutions or community investing are subtracted to avoid potential effects of double counting. Prior to 2010, assets subject to ESG incorporation were limited to socially and environmentally screened assets.

Source: Social Investment Forum Foundation.

# Directors are not responding to their environmental stewardship



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Please indicate if you would like your board to devote more time this year on the **sustainability/climate change** (% of total 1,104 surveyed directors)

Note: Surveyed companies are the top 2,000 publicly traded firms (by revenue) listed with the NYSE Euronext, the NYSE Amex, and the NASDAQ OMX Group stock exchanges.

Source: PwC, "Annual Corporate Directors Survey 2010" (formerly titled "What Directors Think").