INVESTMENT INSIGHTS

Optimizing institutional portfolio opportunities with multi-asset strategies

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Outcome-oriented solutions offer significant potential to enhance risk-adjusted performance across both strong and weak market cycles. Invesco portfolio managers David Millar, head of multi-asset, and Scott Wolle, chief investment officer of global asset allocation, highlight the current trends driving interest in the segment and how these strategies can fit into an institutional portfolio.

|Pensions & Investments| Why are more investors considering multi-asset strategies?

|David Millar| Institutional investors continue to search for ways to capture greater return consistency and temper equity risk, especially in light of general-consensus expectations for higher market volatility and potentially lower returns moving ahead. While much of the cyclical macro data for major markets has generally supported risk assets over the recent past, there are increasing concerns around important structural factors that are likely to have a more dampening long-term effect. Issues including private-sector debt levels with higher servicing costs associated with rising interest rates — particularly in key markets such as China, where credit growth over the past several years has been highly supportive of global trade — point to longer-term pressures on global growth. This and other structural headwinds, combined with a backdrop of generally less easy monetary policy, can create greater challenges for traditional assets.

7% of U.S. institutional investors plan to significantly increase multi-asset exposure

|Scott Wolle| Multi-asset strategies offer a compelling choice in this type of climate by providing more levers and a broader opportunity set to enhance overall expected portfolio performance. These strategies allow investors to potentially reduce equity risk by including more absolute-return-oriented solutions that seek return across a broad mix of assets with below-equity-market-risk. The segment encompasses a wide range of strategies, from traditional 60/40 balanced portfolios to more customized, sophisticated solutions that seek to capture positive performance over full market cycles, with carefully managed volatility and low correlations compared to traditional asset classes.

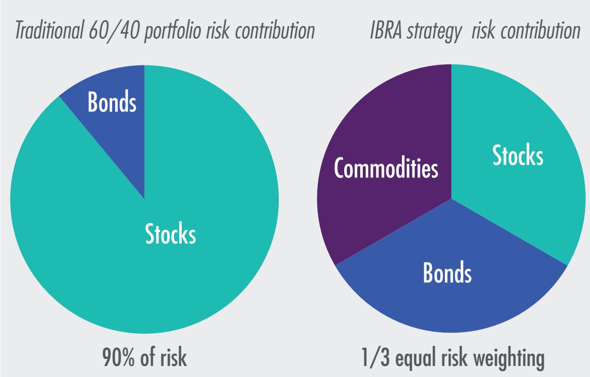
|P&I| How do multi-asset strategies pursue absolute returns?

|Wolle| The flexible nature of multi-asset investing offers a tremendous range of options to achieve these objectives, depending on the strategy and manager. For example, the Invesco Balanced-Risk Allocation strategy (IBRA) pursues a full-cycle target return of 6% above three-month U.S. Treasurys, with 8% volatility. The result is low to moderate correlation to traditional financial markets by focusing on economic diversification to optimize allocations across equity, fixed-income and commodity markets.

In a traditional balanced portfolio of 60% stocks and 40% fixed income, as much as 90% of portfolio risk can come from the equity allocation, which is not that balanced. While stocks do well in noninflationary growth environments, they can struggle during other phases of the economic cycle. The IBRA strategy includes long-duration government bonds to serve as a shock absorber during recessions or periods of crisis, and commodities help defend the portfolio during inflationary growth periods.

While economic diversification provides a solid foundation, the strategy is also more flexible than a traditional balanced portfolio. We take a more adaptive approach, recognizing that the phases of the economic cycle can be long, which allows us to increase exposure to assets during more favorable times and to reduce exposure during less favorable times. Systematically rebalancing these strategic and tactical allocations monthly has helped the strategy meet its long-term volatility targets. Since inception, the strategy has demonstrated low correlations of 0.7 and 0.3 to global equities and U.S. fixed income, respectively.

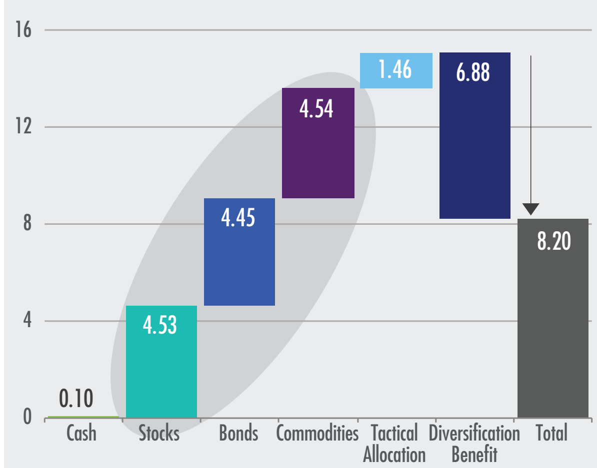
Portfolio risk exposure drives performance in different market environments resulting in a range of performance outcomes



INVESCO BALANCED-RISK ALLOCATION: Disciplined and dynamic risk allocation has helped deliver on volatility targets

Sept. 30, 2008 (inception)—Dec. 31, 2017

Risk Attribution (annualized %)



- Full-cycle target volatility: 8%
- Roughly 1/3 by asset class
- Tactical allocation risk consistent with target of 2%

Realized risk consistent with targeted risk by capturing significant diversification benefit.

|Millar| The Invesco Global Targeted Returns strategy (GTR) takes a different approach, breaking from traditional asset allocation models to pursue absolute returns through an idea-driven portfolio. The strategy seeks to deliver an annualized return of 5% above three-month U.S. Treasurys with less than half the volatility of global equities over rolling, three-year periods. The portfolio typically has between 20 to 30 investment ideas that the team has developed by searching globally across all assets, geographies, sectors and currencies for attractive investment opportunities that can provide the best blend of risk and return. These ideas are then applied

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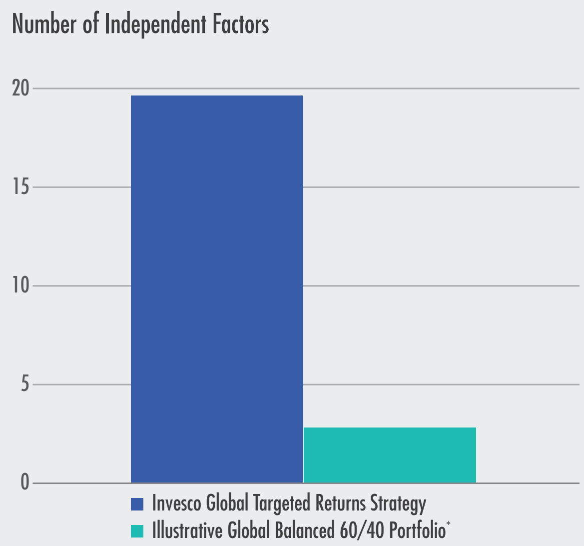
INVESCO GLOBAL TARGETED RETURNS: Broader opportunity set aimed at persistent diversification to deliver an independent return stream



*Comprise of 60% global equities (15% FTSE 100, 15% Eurostoxx 50, 30% S&P 500) and 40% global bonds (20% US Treasuries, 5% Global High Yield, 15% Global Corporate bond indices).

using what the team believes is the best implementation route from a variety of asset types and instruments that range from commodities to credit, equities, currencies, inflation, interest rates and volatility.

For example, one current idea is around equity dispersion. Correlations for individual stocks vs. their relative equity indexes have begun to fall, indicating greater return variance across securities and less reliance on the broad momentum-based returns that have tended to dominate equity markets since the 2008 economic crisis. Our research indicates that this trend should continue, and we implement this view through an options-based index that captures the volatility of a basket of constituents from the S&P 500 and Euro Stoxx 50 indexes that rise relative to the indexes themselves.

The team can also look across asset classes for ideas. In an emerging markets carry idea, for example, the team takes advantage of the carry available from two currencies, the Brazilian real and the Mexican peso vs. the U.S. dollar, and pairs them with a short position in the relative country equity indexes.

Each idea is selected to deliver an independent, positive return to the portfolio over a two- to three-year time horizon and is sized based on its return potential and its assessed volatility under various economic scenarios, both in isolation and in relation to other ideas. Collectively, the team looks to derive a strong consistent hit ratio, with the majority of the ideas delivering incremental returns to the portfolio and no single idea or risk exposure dominating. This gives investors access to many diversified return streams, which historically has positively skewed monthly portfolio return distributions while avoiding extreme negative performance.

|P&I| How are institutional investors incorporating these types of strategies into their portfolios?

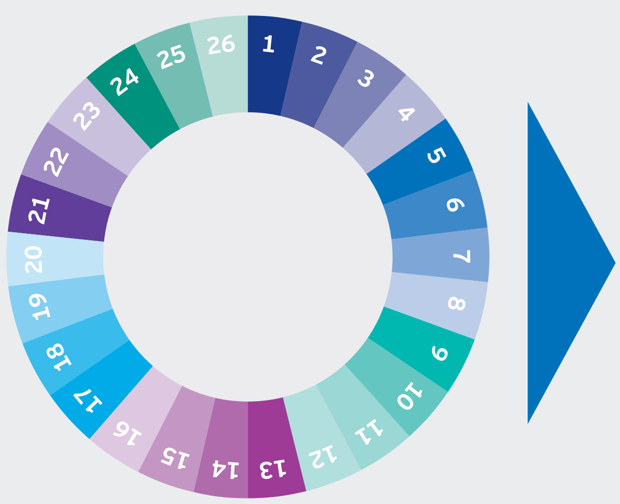
|Wolle| Investors are incorporating multi-asset strategies into their portfolios in a number of different ways. For IBRA, we see it often utilized as a more risk-efficient option for traditional 60/40 portfolio allocations, due to the high degree of added diversification and potential for a higher Sharpe ratio. Some have introduced an independent multi-asset sleeve, taking advantage of low correlation between different multi-asset strategies. Others place it within a liquid alternatives sleeve or as a hedge fund replacement or complement, given its excess return focus, low fees, daily liquidity, daily pricing and absence of lock-ups.

> "We expect multi-asset interest to remain strong. One of the most exciting areas of evolution is the increasing ability of managers to blend their flagship products to meet specific institutional investor needs."

|Millar| Invesco Global Targeted Returns is often placed within a global tactical asset allocation or opportunistic sleeve, or within the same liquid alternatives and hedge fund sleeves that Scott mentioned. One of the unique characteristics within the multi-asset space is that in addition to having lower correlations to traditional assets, these strategies also often exhibit lower correlations to one another, due to the relatively wide range of objectives and investment styles. As such, investor allocations can include complementary strategies to further optimize portfolio risk/reward exposures.

In the U.S., multi-asset-targeted return strategies are still a relatively newer allocation for many institutional investors, though they have experienced considerable growth. After years of strong equity performance and with fixed-income holdings facing increased pressures from tightening monetary policy, investors are naturally interested in strategies that are less dependent on broader markets and won't necessarily fall at the same time when traditional markets are weak. As more look to outcome-oriented strategies as an effective way to help build out their overall portfolios, we expect multi-asset interest to remain strong. One of the most exciting areas of evolution is the increasing ability of managers to blend their flagship products to meet specific institutional investor needs. ■

INVESCO GLOBAL TARGETED RETURNS: AT THE HEART OF EVERY SUCCESSFUL INVESTMENT IS A GREAT IDEA



26 ideas
Each idea is sized to deliver an estimated 25–50 bps contribution to return per annum

7 asset classes
No one asset class should constitute more than 50% of total risk

17 regions
Reduce risk of concentration to a particular country/region

Based on portfolio positions as of March 31, 2018 and subject to change. Past performance is not a guarantee of future results.

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Source: Invesco analysis. Data as of March 31, 2018, unless otherwise stated. All content provided by Invesco is for informational purposes only and is not an offer to buy or sell any financial instruments. Invesco Advisers Inc. is an investment adviser; it provides investment advisory services to individual and institutional clients and does not sell securities.

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