5 preventative measures for non-profit fiduciaries to take in 2020

Russell Investments Research

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With simmering trade tensions, sputtering growth worldwide and a historically long, but slow, U.S. economic expansion, investors will have to brace themselves for a challenging investment environment in 2020. Change, adaptability and diversification are the key words. Here are steps you can take early in 2020 to position your investment program well for the rest of the year.

Incorporating downside protection strategies by investing in well-diversified multi-asset portfolios

The global macroeconomic and geopolitical outlook is dominated by uncertainty, suggesting that this late-cycle environment of low returns, sluggish growth, and high valuations may continue well into 2020. This presents a challenge for fiduciaries who are looking to generate attractive returns while preserving capital during periods of market volatility. Fiduciaries should consider taking a multi-asset approach, which can help provide downside protection as well as growth opportunities. Multi-asset investing affords exposure to a globally diverse mix of asset classes and investment styles that is dynamically managed at a holistic, total-portfolio level. This can bring increased access to the world's leading investment opportunities, greater transparency around risks and exposures, and enhanced diversification potential.

We believe that including an active approach in a dynamically managed multi-asset portfolio helps create a well-diversified portfolio and provides exposure to a wide variety of return sources. For more guidance on navigating market volatility, see our downside management toolkit.

Ensuring that your return expectations reflect the realities of current market conditions

You should be aware of the realities of the asset classes you own in your investment portfolio and understand any risk-reward trade-offs you will have to make, particularly in a low-return environment. For example, investors with a return target of 8% to 9%, who wish to limit their investments in alternative asset classes, are setting themselves up for high levels of equity risk in their portfolios. Fiduciaries should ensure alignment of their spending and return targets with their risk appetite. If you desire high returns, but are unable to tolerate higher risk either through market volatility or the illiquidity premium, you and your team should revisit your goals.

For more information on ways to help meet targeted returns within appropriate risk levels, read our paper on the low-return imperative.

Establishing your return requirements based on organizational goals

You should also be familiar with your return requirements, which will vary depending on the asset pool and your organization's goals. For example, fiduciaries of non-profit organizations need to determine how much endowment spending is permissible, based on economic conditions, their mission, and the desire for perpetuity. In contrast, fiduciaries of healthcare systems and hospitals, who have to manage multiple investment pools, need to consider various factors—for example, maintaining the funded status of their pension plan, or making sure that their operating pool is well positioned to fund capital projects and/or preserve the health of their days cash on hand and balance sheet metrics. Overall, institutional investors should stay on top of their broader organizational goals and ensure that their investment portfolio takes these goals into account.

To help fiduciaries narrow down their desired outcomes and ensure their investment programs can help deliver their goals, we have put together handbooks for non-profit and healthcare organizations, and for defined benefit and defined contribution plan sponsors.

Taking a holistic approach to ESG integration

There is little doubt that responsible investing is fertile ground for new investment opportunities. Responsible investing assets in the United States alone reached $12 trillion in 2018, representing close to a 40% jump from 2016.[1] There is widespread acceptance today of the correlation between environment, social, and governance (ESG) factors and an organization's economic value—as well as growing recognition that the integration of ESG factors does not necessarily mean sacrificing financial return. In fact, building an investment portfolio with a greater focus on ESG considerations has the potential to lead to superior risk-adjusted returns. To that end, fiduciaries should work with their providers on a unique and holistic approach to ESG integration that aligns with their financial objectives. Fiduciaries should understand how ESG factors are incorporated into their providers' offerings, as they are making high-level decisions at every stage of the investment process, from putting investments into place to monitoring and managing the portfolio on an ongoing basis. There are many different ways to incorporate ESG factors into a sound investment process, including:

- Ensuring that ESG assessments are part of the manager research process and evaluation criteria
- Making your voice heard through active ownership and shareholder engagement, such as proxy voting
- Participating in industry collaborations, such as the United Nations-backed Principles for Responsible Investment
- In certain cases, incorporating customized ESG strategies, such as impact investing, exclusion screens, and decarbonization

It is incumbent on fiduciaries to ensure they are doing the best they can to achieve their organization's goals—and to ensure that their providers are aligned with them. For further insights on the integration of ESG considerations in investment processes, check out our annual ESG survey of active managers.

Aligning your team on your investment beliefs and objectives

In an uncertain investing environment, you need to ensure your team is aligned on your investment beliefs and objectives now, before the markets take a turn for the worse. It can then only get harder to introduce a new idea, let alone implement a proposed change. This means setting robust due diligence practices, conducting frequent and effective investment committee meetings, clearly defining governance and delegation structures, and ensuring that investment policy statements and other key documents are up to date. The continual education of investment committee members is also critical to the success of your investment program; this can help keep committee members from misjudging the results of a particular strategy and, perhaps even more importantly, keep them focused on your broader investing objectives.

Read our piece on running effective investment committee meetings.

> As risks build, you and your team should prepare for the impending market correction now so that your investment program is better primed to weather the storm later. By taking these steps now, you and your team can both remain in control and nimbly adapt to change as needed.

[1] *Report on U.S. Sustainable, Responsible, and Impact Investing Trends*. U.S. SIF Foundation, the Forum for Sustainable and Responsible Investment. October 31, 2018

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For more information

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