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Capital Market Projections 2017

Author: Jim Van Heuit

Each year, Callan develops long-term capital market projections, detailing expected return, standard deviation, and correlations for major asset classes. These projections are the cornerstone for strategic planning.
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From co-authors James Van Heuit and John Pirone, CFA, CAIA, of Callan's Capital Markets Research group:

Over the next 10 years, we forecast **annual GDP growth** of 2% to 2.5% for the U.S., 1.5% to 2% for non-U.S. developed markets, and 4% to 5% for emerging markets.

The real GDP expectation for the U.S. is higher than the average growth since the Global Financial Crisis but lower than that experienced over the last 50 years. Several factors will play into how much GDP actually grows over that time period.

A strong labor market, pro-business policies from the incoming administration (such as lower taxes or increased infrastructure spending), and increased exports to foreign countries with improving economies would push GDP growth higher. But interest rate hikes, limits to fiscal stimulus imposed by the federal deficit, a strong dollar, and restrictive trade policies that limit the attractiveness of U.S. exports would hinder growth.

For broad **U.S. equity**, we project an annualized return of 6.85% with a standard deviation (or risk) of 18.25%, for **non-U.S. equity** a return of 7.00% (risk: 21.00%), and for **U.S. fixed income** a return of 3.00% (risk: 3.75%).

All equity forecasts are developed by building off of this fundamental relationship:
Equity Return = Income Return + Capital Appreciation

While the short-term relationship is weak, over the long term earnings tend to follow economic growth. In the absence of this linkage profits would become an extraordinarily large or small part of the economy. The connection is more robust in developed economies than in emerging markets, where profit growth can substantially lag economic growth.

Our fixed income forecasts are created by deconstructing fixed income returns into subcomponents and incorporating a forecast for the evolution of the term structure over time. Fixed income return can be broken down into the following terms:
Fixed Income Return = Yield + Capital Gains + Roll Return

These figures represent our best thinking for long-term expectations and establish a mid-point within a wider range of potential outcomes. Multiple elements of the capital markets influence the projections: returns relative to inflation, equity valuations, risk premiums, GDP growth, and many other factors. These projections incorporate advanced quantitative modeling as well as qualitative feedback and the economic expertise of Callan's consulting professionals.

The capital market projections were produced by Callan's Capital Markets Research group, our specialized team of economists, mathematicians, and actuaries dedicated to research in the field of strategic planning, including asset allocation and manager structure, as well as the development of economic tools and statistical models.