Northern Trust | The Next 5 Years: What Investors Can Expect

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Every year, we undertake a comprehensive review of our five-year outlook, culminating in six key themes and asset class forecasts. While our themes have evolved to capture recent developments, our outlook for continued economic growth, controlled inflation, and accommodative monetary policy is expected to result in good, but not great returns across most asset classes.

Let's explore three of those themes here. Our first key theme is mild growth myopia. It is our expectation that subdued economic cycles and stronger financial systems will push out the next recession and limit its severity. Those analysts who focus just on the age of the expansion are missing the point that the slow pace of the recovery has actually extended its lifespan.

Our theme of stuckflation returns for its third year in a row. We think low and durable structural inflation has altered both monetary policymaking and investor behaviors. Our third theme is pass/fail monetarism. Central banks are missing a template for policy normalization, so it is difficult to grade their efforts.

But central bankers know they must not fail, which could happen if they raise interest rates, just to build dry powder for the next downturn. The end of the 30-year-plus bond bull market does not mean the start of a bear market, as we expect interest rates to stay low, driven by stuckflation.

We've bumped up our fixed-income returns this year, supported by higher starting yields, continued central bank accommodation, and steady credit spreads. We expect equity returns to be below historical averages, but higher than what would be suggested by current valuations.

We expect developed market equity returns in the mid-single digit range and emerging markets to deliver a healthy premium, due to stronger growth and cheaper valuations. We expect real assets to generate a return similar to global equities, but with diversification benefits.

We foresee an improving outlook for natural resources, as ongoing growth and better calibration between supply and demand will be supportive. Finally, we continue to recommend private equity and hedge funds to enhance risk-adjusted portfolio returns.

Opportunities have increased for private equity firms as companies are staying private longer, while in hedge fund investing, manager selection is proving paramount. So "What does this mean for investors?" All in all, our forecast call for a 5.2% return for a portfolio, invested 60% global equities and 40% in US bonds.

While this is low by historical standards, it is acceptable in a world of stuckflation, where US inflation is forecasted just under 2%. To get our full set of forecasts and insights across asset classes, "download our five-year outlook at CapitalMarketAssumptions.com."

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