

FIRST STATE CIO ROUNDTABLE



Setting the stage

Objective-based investing

Growing pains

Opinion poll

Driving forces: fixed income and multi asset

Highlights from First State's recent Singapore CIO roundtable

By Nazneen Halim



On June 8, First State Investments (First State) and *Asia Asset Management (AAM)* jointly hosted an intimate roundtable in the Lion City, which was attended by top directors and fund managers from Singapore-based institutions and family offices. The theme was *Driving Forces: Fixed Income and Multi-Asset*, and it aimed to explore multi-asset investing and dispel the many myths surrounding the sector, particularly in the Asian context.

Setting the stage

Following the opening remarks by Tan Lee Hock, publisher and founder of *AAM*, Paul Griffiths, chief investment officer of fixed income and multi-asset solutions at First State, provided context to the discussion with an overview of the mar-

ket and the backdrop in which the multi-asset universe is currently operating.

According to Mr. Griffiths, there is still no clear overarching theme in the multi-asset investment space, other than turbulence and turnover. He said that in terms of "good news", it seems as though the only reasonable pattern is that of markets moving from one latest good investment to the next. In terms of returns, he said that it is still relatively low, similar to volatility – which seems rather ironic considering all the external factors influencing the global economy at present – adding more pressure to active managers.

Among the reasons for the dip in volatility, said Mr. Griffiths, are: "Quantitative Easing, which has provided the world with a huge amount of liquidity; and the popularity of passive investing, which

has dampened turbulence even in the face of potential triggers such as rising interest rates, or geopolitical events such as Brexit, North Korea, and Donald Trump."

He added that from a historical point of view, the correlation of asset classes is not consistent, and that this presents an opportunity for the nimble investor: "When bond markets and equity markets are highly correlated, where do you invest your money? The solution is to be dynamic. Make sure you invest in a way that diversifies risk. It is never as simple as a static, balanced-type approach."

In terms of Asian fixed income, Mr. Griffiths believes that movement in US Treasuries and geopolitics in general will have an impact on the market, but there will be a lower level of correlation. "The market is seeing a transformation



Griffiths
Investment Officer, Fixed Income and Multi-Asset Solutions
State Investments

terms of breadth and depth, and we need to be dynamic to take advantage of the ability to switch between asset classes. This needs to be done in a systematic and structured way, and that's what our multi-asset solutions team at First State are doing. We do it in a way that doesn't use static or quasi-static underlying allocations to asset classes, but rather a combination of a long-term judgement of asset allocation with a short-term dynamic overlay to take advantage of different opportunity sets." Taking a long-view approach, Mr. Griffiths said that compared to the last few years, the next few years will be very much impacted by the current quantitative easing measures, and it will continue to be a huge factor in bond markets. "The opportunity set in fixed income as a whole is quite limited and because of the very low yields, we need to find interesting and unique stories in fixed income and switch between asset classes. However, if there's anything I

can anticipate, it is that we (the market) will get shock that we're not anticipating in the next few years. Therefore, we need to be dynamic in asset allocation and portfolio construction."

Objective-based investing

Epcó van der Lende, head of multi-asset solutions at First State, then took the stage with a presentation entitled *Multi-Asset, A Means to An End*. The premise of Mr. van der Lende's presentation centred around objective-based investing, and how to leverage on multi-asset investments for risk management.

"What is all the hype about multi-asset investing in today's market?" he asked. "To begin with, multi-asset investing has a very natural risk element to it that favours that approach over a single asset class gamble. For us as an investment manager, there is tremendous opportunity for us to leverage on that. Multi-asset investing is more than diversification and risk management – it is essentially

something that we all know. Every portfolio and private asset you have – be it a savings account, real estate, etc., even pension funds at a holistic level has a multi-asset portfolio."

Distilling multi-asset investing into a simple philosophy of achieving one's objective, Mr. van der Lende explained that elements such as risk and tolerance of risk should be linked to one's investment objectives. "So even though you can see that, for example, the winners of today could be the losers of tomorrow and vice versa, the underlying objective does not change – but the appropriate mix does. Therefore, flexibility is key when managing a pool of assets with a singular objective in mind."

"Asset allocation, on a strategic level can often times be static and not appropriate or relevant to the world in which we are living in. Thus, investors need to become more conscious of objective-based investing – i.e. this is what I want, and how do I achieve that? And in this



Epco van der Lende
Head of Multi-Asset Solutions
First State Investments



Lauren Prendiville
Head of Distribution, Southeast Asia
First State Investments

efficient in your active management you need volatility," he added.

Of course, as nothing is very straightforward, Mr. van der Lende reminded the audience that economic realities and markets are constantly changing even though investment objectives might remain constant. "So, if you invest in multiple asset classes, how do you pick the right ones, and how do you get to the objectives in case the markets are not working in your favour? Having a mix can help you diversify and manage your risk and allow you to be on an optimal track at all times, but you need an additional source of return which comes in the form of active management," he explained, adding that investors need to have a more systematic approach.

"Multi-asset investing is becoming more active and you need alpha, but not all players are picking up on that. Using the metaphor of a sailboat, you as the investor are in a sailboat and want to get to the island – which is your investment objective. So, the first thing you do

is set the rudder so you're generally in the right direction. This is strategic asset allocation. And you need to be tactically changing course so you don't just drift – i.e. you need to actively manage your portfolio."

He added: "Another metaphor is don't lie at anchor – if you lie at anchor, you're also sure that you won't get there because you don't move. Lying at anchor is essentially just buying cash, and you need to be active and take risk. If you're a relative manager, you could go passive. In an objective-based world that's not an option. And don't just follow another floating boat. A benchmark is essentially a floating sailboat. There's no objective behind a benchmark, so in essence, by combining the rudder, strategic asset allocation, with the sails – which is dynamic – in a systematic asset allocation process, you can reach your objectives. The investible universe is huge, and if you look at opportunity sets, one of the more interesting asset classes is Asian fixed income. There is a lot of

context, multi-asset investing is a means to an end. Translated into an absolute or real return objective, protecting real capital – any type of objective – asset allocation is a means to an end and to be



Jamie Grant
Head of Asian Fixed Income
First State Investments

return potential on the dynamic and strategic side to leverage that market," concluded Mr. van der Lende.

Growing pains

The final presentation before the Q&A session was by Jamie Grant, head of Asian fixed income at First State, in which he provided a breakdown of the opportunity that is investment grade Asian fixed income.

According to Mr. Grant, bank demand for Asian fixed income, and especially the flows into US dollar instruments remains healthy, providing positive support to the market.

Interestingly, Mr. Grant pointed out that investment in Asian fixed income should always be backed by quality credit analysis. "Recent years have seen an increase in defaults, particularly in China. Whilst overall default levels remain low, investors must be diligent and all investments should be backed by quality credit analysis," he said.

A lack of volatility in the market is also

a concern, and as of February 2015, Mr. Grant said that Asian fixed income had been on par with US fixed income. "The market is, however, maturing and the investors in Asian fixed income are now dominated by Asian investors, not foreign participants. We are based in Asia and know the market very well, and I can also say that volatility is also improving."

A final misconception, said Mr. Grant, is that the returns "just aren't there" in Asia. According to the JP Morgan benchmark, he said, there have only been two down years in Asia since 2005 and the markets have performed "very well". When asked about the prospect of green bonds in Asia, citing China and Singapore as examples of countries intent on becoming Asia's green bond hubs, Mr. Grant added that whilst it is still early days for environmental, social and governance (ESG) investing in Asia, it is relevant for investors, and relevant to green bonds also.

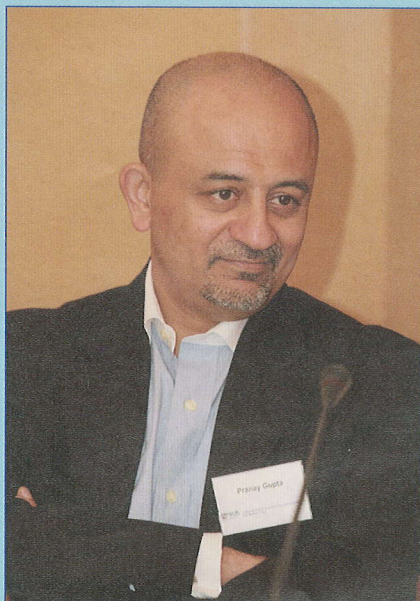
"Responsible investing is in our DNA and is an important part of our invest-

ment process, ESG is still not a big concern to many Asian investors. It is still a developing story here and most of the investments will still originate from Europe for now. It is growing in Asia, but from a very low base. First State however has a long track record of incorporating ESG as part of the credit assessment."

Opinion poll

The presentations were followed by a quick online polling session, which required participation from all attendees. The questions posed included: What are the biggest threats to longer-term returns? Some 53% of the audience replied "inflation".

This was followed by a question on "key reasons for investing in Asian fixed income", with 50% of the audience selecting "yield" as their main reason. Finally, 19% of the audience said that they currently invest in mixed-asset funds and mandates; with 31% stating that "risk diversification" was the most appealing reason for investing.



Pranay Gupta
 Research Consultant
 Centre for Asset Management Research and
 Investments (CAMRI), NUS Business School

The event ended with a Q&A session, with Mr. Griffiths, Mr. van der Lende, Mr. Grant, and Pranay Gupta, research consultant at the Centre for Asset Management Research and Investments (CAMRI) at NUS Business School, answering questions from the audience on everything multi-asset – from real estate to asset allocation, and stewardship codes. Mr. Gupta also shared his thoughts on the industry, providing a provocative view on what needs to change in the current landscape to enable it to achieve more meaningful growth.

“Ironically, in the investment world, 90% is spent on solving the 20% that doesn’t matter. We spend all our time hiring and firing managers to diversify alpha, but we don’t spend our time in diversifying the allocation decision,

which is responsible for 80% of the risk. Just as there are 20 ways of picking stocks, there are 20 ways of picking allocation. Ideally, what should happen is, [you should] take your allocation and break it into three-to-five pots: active, passive, alternative, etc.,” he said.

“Money is coming into multi-asset because the client sponsors have realised that the single asset allocation decisions inside their plan is going to hurt them at some point, and multi-asset absolute return is a way of diversifying that allocation decision by putting some money out of the traditional beta boxes into this box which aligns the interests of the asset manager with the overall return of the plan, and still has the same level of transparency and low fees. The problem is that the products are not keeping up,” Mr. Gupta concluded. ■

Up and Coming

August 2017

First State CIO Roundtable – Hong Kong

For more information, please contact:
 Veronica Chung – Email: veronica@asiaasset.com

Asia Asset Management