Taking a tactical approach to a new investment era

Investors across the Asia Pacific region are becoming more selective in their asset choices, with long-term capital growth, diversification and sustainability playing key roles in where, why and how they allocate in 2021, according to an exclusive survey by AsianInvestor and S&P Dow Jones Indices (S&P DJI).

S&P Dow Jones Indices
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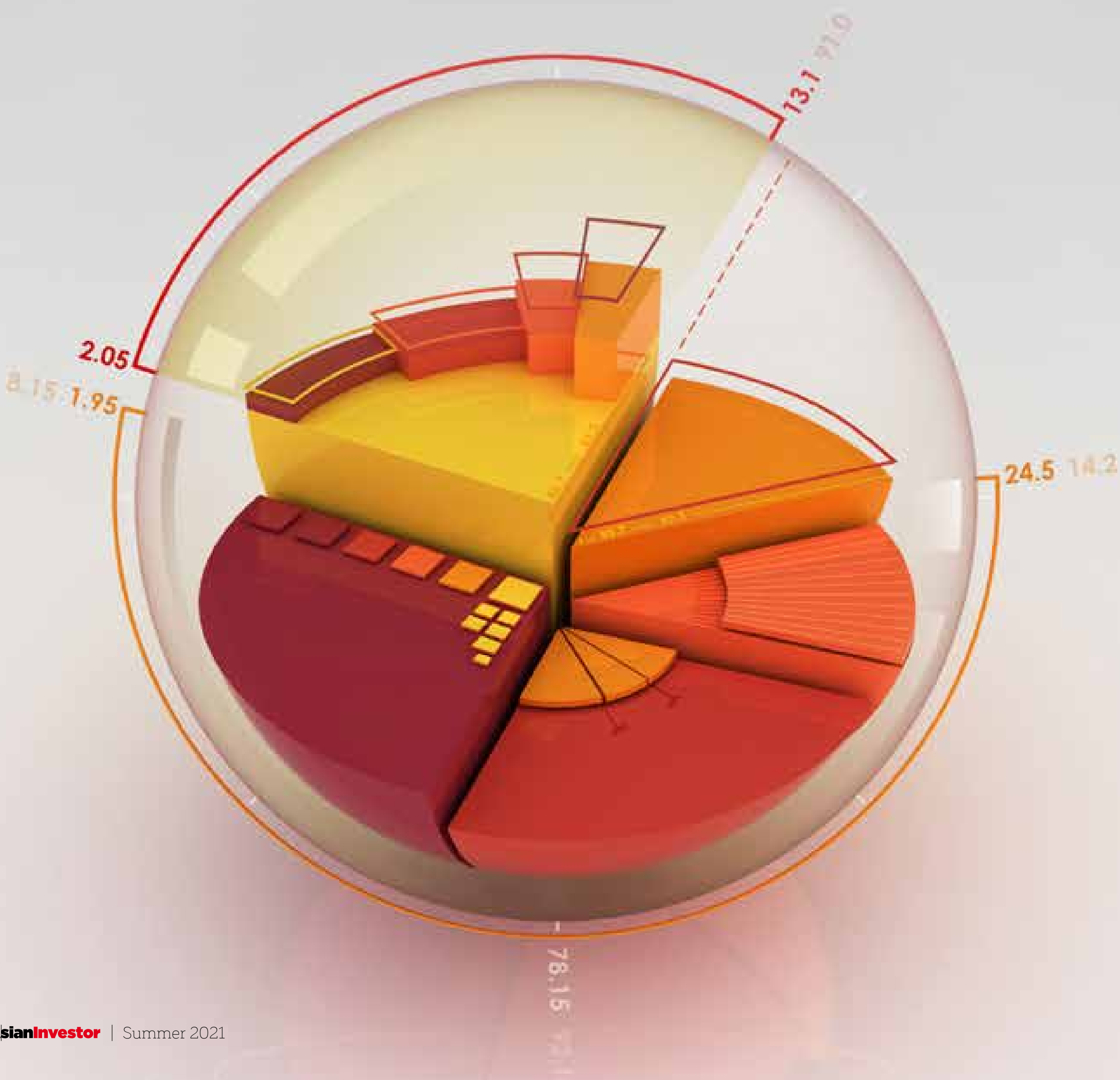
AsianInvestor



The seemingly never-ending rollercoaster for economies and markets has sharpened the focus of the region's leading asset owners on the need for long-term capital growth and portfolio diversification.

To achieve these two goals this year, there appears to be a preference among investors for listed securities in Asia and private market assets in North America. At the same time, the influence of technology as well as environmental, social and governance (ESG) factors is stronger than ever, both in terms of target assets and the investment process.

This is all based on the views of 105 senior investment executives from sovereign wealth funds, government entities, insurance companies, public and private pension funds, endowments, private banks and other asset owners across the Asia Pacific region.

They shared these insights as part of a survey by *AsianInvestor*, in collaboration with S&P DJI, conducted between March and April 2021, covering Hong Kong, Taiwan, Australia, South Korea, Japan, Singapore, Thailand, Malaysia, Indonesia, the Philippines and India.

Broadly, the consensus tallies with the relatively robust and fast recovery that S&P DJI sees as a driving theme for Asia, certainly compared with other parts of the world.

"This has been supported by government stimulus, accommodative monetary policy and large-scale investments. The recovery has been the key influence on rates, equity markets and valuations across the spectrum of asset classes," said Tianyin Cheng, senior director, strategy indices at S&P DJI.

KEY TAKEAWAYS FROM THE SURVEY

- Respondents believe public equities will see the greatest increase in exposure (in percentage terms) in portfolios in 2021.
- Around a quarter of respondents believe ESG as an investment theme will offer the highest risk-adjusted returns in 2021.
- Incorporating ESG factors via additional data and analytical tools is the most appealing way for investors to enhance returns as they emerge from Covid-19.
- Respondents said there is either a "high" possibility (13%) they will use more passive strategies in the next six to 12 months, or a "medium" chance (45%) they will do so.
- The biggest portfolio risk for respondents is rising rates and inflation (36%), followed by uncertainty over liquidity (21%).
- Conducting virtual due diligence is still the preferred approach this year when outsourcing to external managers, at 45%, with just over a quarter (27%) of respondents confirming they have no intention to add any new external managers.

SUSTAINABILITY COUNTS

Against this backdrop, positioning for transition continues to dominate allocation decisions for many investors.

This reflects the importance of themes of tactical exposure for many respondents in 2021 – being more prominent than geographical diversity or taking a sector focus. And when investing in themes, respondents believe the highest risk-adjusted returns this year will come from ESG (26%), closely followed by transformative tech (21%) and healthcare and biotech (20%).

In line with the commitment to sustainability, respondents ranked the process of incorporating ESG factors via additional data and analytical tools as their preferred route to enhanced returns in a post-pandemic landscape.

"We have witnessed the focus on climate change for the last few years, but it is now at a turning point," explained Cheng. "It is now about action rather than just talk, with investment money supporting the transition to a low-carbon economy."

At the same time, implementing technology and better systems such as artificial intelligence and big data solutions is also high on the priority list for investors, as is their intention to more closely scrutinise the performance of external active managers. These approaches are expected to be much more effective than traditional ones, like taking on more risk by going down the credit curve or hiring more investment staff.

> **"Positioning for transition continues to dominate allocation decisions for many investors**

FOCUSED EXPOSURE

To implement their thematic view, as well as make tactical tilts in today's challenging investment landscape in general, survey respondents pinpointed public equities as by far the most desirable asset class to which they plan to add more exposure in 2021. Listed debt was number two on the list.

However, private markets remain of interest to certain investors in their hunt for yield, with respondents opting for greater exposure to private equity (especially), but also private debt and real estate.

"We see increasing allocations to replacements for listed fixed income," added Cheng, referencing real assets and the alternatives space. "There are other options too," she added. "Liquid alternatives are scalable and tend to have little correlation with traditional asset classes. These are very systematic, so are suitable for indexing to create a low cost, effective way for investors to get access to some alternative strategies."

To obtain this exposure, the preference among respondents is via an internally managed approach (36%), followed by a separate account (23%) and ETFs or index-linked solutions (19%).

As part of the muted interest in passive investing, the next six to 12 months is likely to see some growth, according to respondents; 13% said there is a "high" chance of adding more passive strategies, with another 45% calling it a "medium" chance.

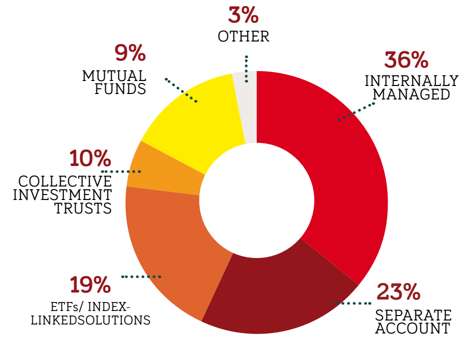
The relatively staunch focus on active investing reflects the broader trend in Asia. By comparison, in the US and Europe,

ASSET ALLOCATION

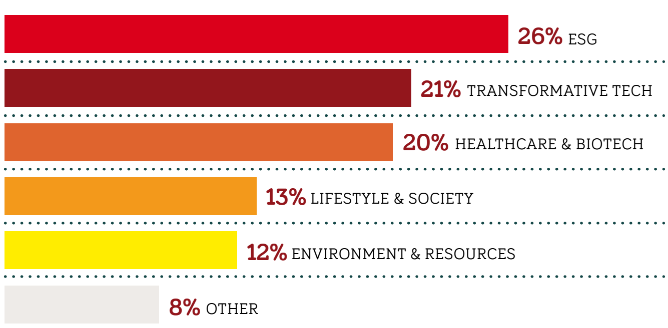
TO WHICH OF THESE ASSET CLASSES WILL YOU INCREASE EXPOSURE BY THE LARGEST % IN YOUR PORTFOLIO IN 2021?

1. PUBLIC EQUITIES
2. LISTED DEBT
3. PRIVATE EQUITY
4. PRIVATE DEBT
5. REAL ESTATE
6. SHORT TERM ASSETS/ CASH
7. INFRASTRUCTURE
8. COMMODITIES

WHAT IS YOUR PREFERRED VEHICLE FOR YOUR PREFERRED EXPOSURE?



WHAT THEME DO YOU THINK WILL OFFER THE HIGHEST RISK-ADJUSTED RETURNS THIS YEAR?

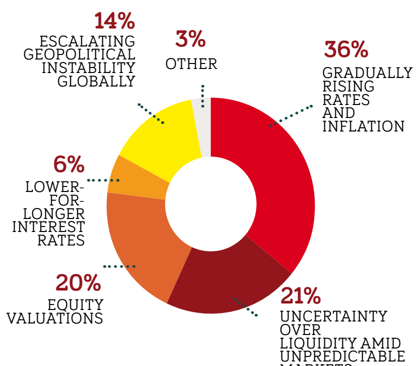


WHAT WILL HAVE THE GREATEST INFLUENCE ON YOUR ALLOCATION DECISION THIS YEAR?

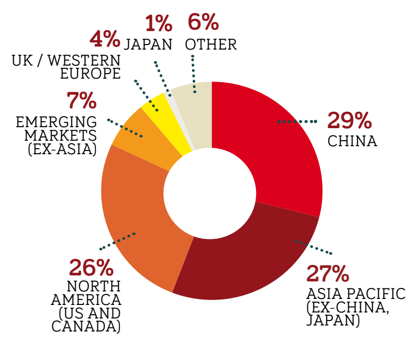
WHAT APPEALS TO YOU MOST FOR ENHANCING RETURNS AS WE EMERGE FROM COVID-19?

1. INCORPORATE ESG FACTORS VIA ADDITIONAL DATA/ ANALYTICAL TOOLS
2. IMPLEMENT TECHNOLOGY AND BETTER SYSTEMS (SUCH AS AI/BIG DATA SOLUTIONS)
3. MORE CLOSELY SRUTINISE ACTIVE MANAGER PERFORMANCE
4. TAKE MORE RISK (SUCH AS GOING DOWN THE CURVE, INVESTING IN FRONTIER MARKETS, ETC)
5. ADD MORE INTERNAL INVESTMENT RESOURCES
6. SEEK CO-INVESTMENTS WITH OTHER INVESTORS

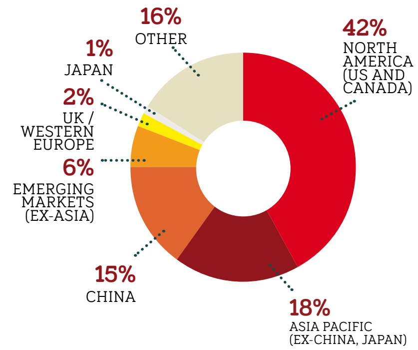
WHAT POSES THE BIGGEST PORTFOLIO RISK FOR YOU IN 2021?



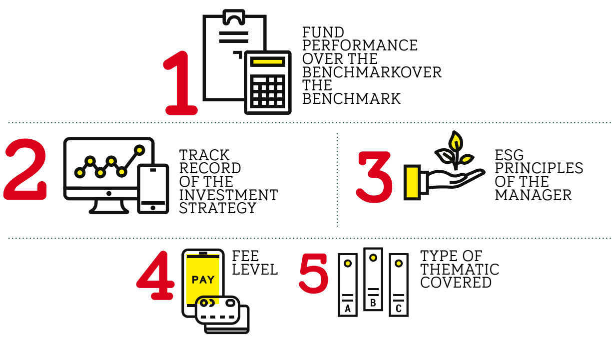
FOR LISTED SECURITIES, WHICH REGION IS MOST APPEALING IN TERMS OF OPPORTUNITES TO GENERATE RETURNS?



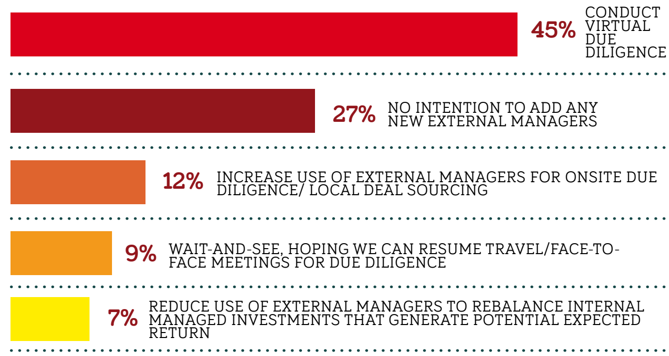
FOR PRIVATE MARKET ASSETS, WHICH REGION IS MOST APPEALING IN TERMS OF OPPORTUNITIES TO GENERATE RETURNS?



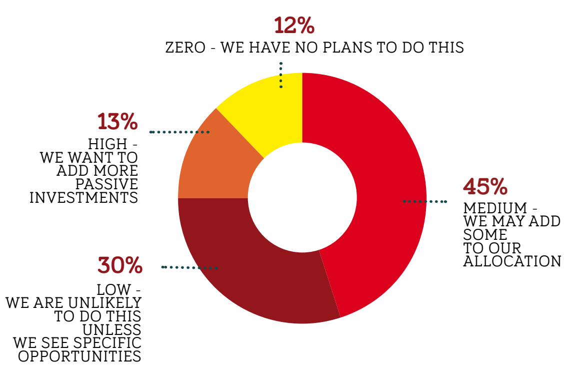
WHICH OF THE FOLLOWING IS NOW YOUR MAIN FOCUS WHEN ASSESSING DIFFERENT FUNDS?



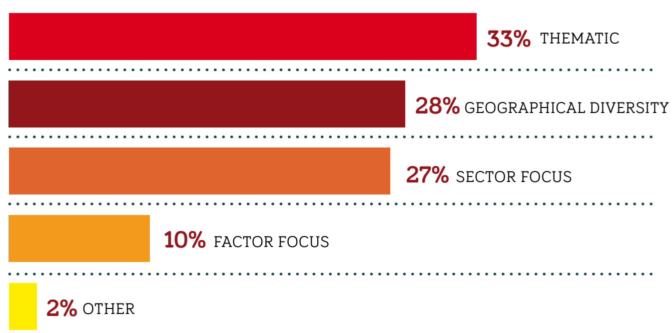
WHAT IS YOUR PREFERRED APPROACH THIS YEAR WHEN OUTSOURCING TO EXTERNAL MANAGERS?



HOW LIKELY ARE YOU TO USE MORE PASSIVE VEHICLES/ STRATEGIES IN THE NEXT 6 TO 12 MONTHS?



WHICH OF THE FOLLOWING IS MORE IMPORTANT TO YOU FOR TACTICAL ALLOCATION IN 2021?



Cheng said there have been considerable inflows into passive products. “This highlights the need for further education on passive investing in Asia, across most types of institutions.”

Investors also see their ideal mix of listed and private assets as most likely to protect their portfolios from their biggest portfolio risk in 2021: gradually rising rates and inflation, according to 36% of respondents.

At the same time, 21% of respondents said they fear uncertainty over liquidity amid unpredictable markets, with equity valuations weighing on the minds of another 20%.

By geography, Asia Pacific seems to be the destination of choice for listed securities. In terms of opportunities to generate returns, the majority of respondents said China is most appealing this year, at 29%, with the rest of Asia Pacific (ex-Japan) a close second, at 27%. However, around a quarter of investors (26%) are also eyeing the US and Canadian markets.

“In general, we are seeing a shift in power from a geopolitical perspective,” added Cheng. “China is getting a lot more attention as investors look to economies which they believe will deliver growth.”

North America is a clear favourite, though, when it comes to generate returns from private market assets; 46% of respondents said they will look at the US and Canada. Asia Pacific and the emerging markets, meanwhile, are also of some interest.

CONSIDERED SELECTIONS

Regardless of asset class, vehicle or geography, the new investment reality has led the majority of investors in the survey to consider long-term capital growth as the main source of their allocation decisions this year, as well as the objective of portfolio diversification.

The rationale is, it seems, that this approach will help them achieve other goals such as cash yield or income, inflation protection and uncorrelated returns.

In outsourcing to third-party funds as part of their strategy, however, the disruption in the wake of Covid-19 hasn’t altered their inclination towards fund performance over the benchmark when assessing different funds; this is followed by the track record of the investment strategy. Notably, survey respondents identified the ESG principles of the manager as the third most important factor in their due diligence.

Yet roughly a quarter (27%) of investors don’t plan to add any new external managers for the rest of the year anyway. Those respondents who do said they will continue to prefer virtual due diligence when looking to outsource.

Ultimately, investors are trying to adapt their outlook and expectations to ensure their portfolios are positioned to manage risks and capture new opportunities that arise, added Cheng. “These investors may tend to approach external providers for information and support where it can help them make better and more informed decisions.”

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