A MOVE TOWARDS TACTICAL ASSET ALLOCATION IN INDIA

ACCORDING TO PANELISTS AT THE HUBBIS INDIAN PRIVATE BANKING FORUM 2014 IN MUMBAI IN LATE AUGUST, PRIVATE BANKS IN INDIA ARE INCREASINGLY ADVISING ON DYNAMIC PORTFOLIOS, WITH FUNDS IMPLEMENTING TACTICAL ASSET ALLOCATION.

Pankaj Sharma
DSP BlackRock

"There are enough studies that show a few days out of the market could materially alter an investor's long-term returns"

The common advice to retail investors is that they shouldn't try to time equity markets by deciding when to enter and exit. While this is true on a very short-term basis, there may be value in looking at a more medium-term "dynamic" asset allocation approach, which can provide better results than a long-term buy-and-hold strategy.

There are now asset allocation funds available in the Indian market which make the equity/defensive assets call based on valuations.

High net worth (HNW) investors around the world use these sorts of funds, so Indian HNW clients may also want to consider this. They can also get more customised advice through private banks with good global networks and robust processes.

This was the conclusion of the panel discussion on asset allocation at the Hubbis Indian Private Banking Forum 2014, held in Mumbai in late August.

DYNAMIC VERSUS TACTICAL

Hansi Mehrotra, the moderator for the session, set the scene by sharing her experience in advising private banks across the Asia Pacific region on setting asset allocation processes.

She said that even institutional investors such as pension funds have had to adapt their views on a "set and forget" approach to strategic asset allocation and implement more medium-term dynamic asset allocation processes.

The panel discussed the difference in the nomenclature between tactical and dynamic. While tactical asset allocation means taking tilts away from neutral allocation based on very short-term market fluctuations, these are difficult to implement due to delays in getting client approvals and also costs. It's also hard to predict short-term market fluctuations, added speakers.

However, dynamic asset allocation is based on more medium-term views, looking out 12 to 24 months. This is a better time frame to see valuation mispricings, said the panel.

Vishal Kapoor, regional head - wealth management, South Asia at Standard Chartered Bank, said investors can add

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Prateek Pant

RBS Private Banking

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value by making dynamic calls on a cyclical basis compared with a long-term term hold approach.

"When making dynamic call recommendations, it's not upsetting your portfolio, it's about going underweight or overweight on certain assets because you have stronger views on some assets and lesser views on others," explain Kapoor. "It's about where we see a greater opportunity over one to three years that is different from a long-term buy-and-hold approach."

He also emphasised that global banks focus on risk adjusted returns.

Prateek Pant, executive director- products & services at RBS Private Banking in India, added that the firm had worked with a research platform to set up an institutional processes including focusing on value-add from dynamic asset allocation.

He said the process had been vindicated since it was set up in 2008.

"When we do tactical allocation, we look at relative valuations or the attractiveness of the asset pairs, the most common being debt versus equity, long-term GSec versus short-term, cash versus gold, etc," said Pant.

He agreed with Mehrotra's suggestion that any asset allocation process should also look at underlying drivers of returns of asset classes rather than just at historical quantitative relationships.

Mehrotra also said that some global private banks have asymmetrical ranges around the neutral asset allocation, allowing portfolios to get out of an asset class completely but not go too much overweight in case the call was wrong.

Pant and Kapoor explained that their clients are comfortable with smaller ranges and they would execute any drastic calls, such as liquidating, themselves.

Both also confirmed that their medium-term dynamic process had added value, outperforming their longer-term strategic asset allocation benchmarks.

OBJECTIVE-BASED PORTFOLIOS

Mehrotra also presented a behavioural framework based on a paper titled "Beyond Markowitz". That suggests dividing clients' wealth into three risk buckets – no downside risk, market risk and aspirational risk.

Pant and Kapoor agreed that clients intuitively follow the risk-bucket approach, in that they ask for advice on a long-term strategic portfolio, but also sometimes they just want ideas for their opportunistic bucket.

"As far as we can, we try to understand the clients' requirements and objectives, and work with them on creating opportunistic portfolios, where the client is willing to take risk, or into more strategic portfolios for long-term wealth," said Pant.

Kapoor echoed this view: "Basically the client requirements and objectives will decide the investment framework."

ROLE OF ASSET ALLOCATION FUNDS

The panel also discussed the role of asset management companies (AMCs) in India in terms of providing asset allocation services.

AMCs are well placed to help investors with dynamic and tactical asset allocation, not only due to their expertise but also the ease of implementation.

Pankaj Sharma, executive vice president and head business development & risk Management at DSP BlackRock, cited the example of clients who have to invest overseas to hedge against the liability of their children's education. Such investors should invest overseas but don't have the expertise, hence may choose to invest through a fund that takes care of asset allocation across overseas equities and debt.

DSP BlackRock has recently launched a feeder fund into the BlackRock Global Allocation Fund, which has a 60/40

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neutral allocation to equities/debt but with a "go anywhere" strategy.

Interestingly, inflows have not just been from retail investors but also from private banks and institutional clients – perhaps proving that funds not only have the ease of execution (that private banks and institutions could match) but also expertise which is harder to find.

Even on the domestic front, while there are funds in India with static asset allocation which re-balance back to strategic asset allocation, such as the Axis Triple Advantage Fund, there are also funds that tilt based on their views on valuations.

DSP BlackRock's Sharma pointed out that there are enough studies that show a few days out of the market could materially alter an investor's long-term returns.

Hence, it makes sense to have a dynamic asset allocation approach.

Karan Datta, chief business officer of Axis Asset Management, pointed out that asset allocation funds will gain prevalence because "investors have shifted from relative returns to absolute returns".

Karan Datta

Axis Asset Management

"Investors have shifted from relative returns to absolute returns"

"Lower risk doesn't always necessarily lead to lower returns."

His view was that investors are interested in the outcome, which has to be better than fixed term deposits. Datta also pointed out that "lower risk doesn't always necessarily lead to lower returns". Datta added that investors around the world are getting reminded that asset allocation can use diversification to lower returns without compromising returns.For example, Axis' joint venture partner, Schroders, has experienced increased flows into asset allocation products worldwide.

Vishal Kapoor

Standard Chartered

"Investors want simplicity in their portfolios"

Datta said that if the asset management industry creates products with clear objectives and guidelines, then advisers and investors are likely to implement through funds.

Kapoor agreed that private bankers might support asset allocation funds because investors want simplicity in their portfolios, so are happy to replace 50 sector funds with three to four well-designed and good-performing funds. Hence asset allocation funds have a role to play.

Pant agreed, saying such recommendations depend on private banks knowing their clients well; some clients can handle seeing volatility for whom balanced funds would work well. ■

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