Systematic investing: advancing the debate beyond Factors, beyond Equities ... and into Fixed Income
Founded 1999
In Frankfurt, Germany

Over 120 clients
made up of pension Funds, Public Funds, Foundations and Sovereign Wealth Funds

More than EUR 25 billion
in assets

Shareholders are Partners and Union Asset Management Holding AG

More than 100 employees

London branch opened in August 2014

Data as of 31 December 2015
Successful investment management was once about the search for information, but:

- The investment universe is expanding
- The quantity of information is increasing
- The level of competition is increasing

Managing successful investment strategies is now about the systematic processing of information, in a risk-controlled framework.
1. Factor Investing has become a popular term when it comes to managing Equities. Is “crowding” a concern for you in this context?
2. Can Factor Investing also be applied to Fixed Income?
3. Is quantitative asset management likely to grow in importance compared to traditional asset management?
Crowding risk of outperforming strategies increases as the popularity of equity factor investing grows.

DR VOLKER FLÖGEL
Director, Head of Equity Research
Quant investing is systematic factor investing, also in Fixed Income.

DR HARALD HENKE
Associate Director, Head of Fixed Income Research
Generating asset returns which can fund the Scheme sponsor's defined benefit pension promises in today's low return world is a major challenge. Factor investing can help us in doing so because it addresses and exploits systematically all relevant drivers of return in a risk-controlled manner.

NIGEL STAPLETON
MA(Cantab), FCWA
SYSTEMATIC INVESTING – ADVANCING THE DEBATE

... BEYOND FACTORS
... BEYOND EQUITIES
The returns of equity factor portfolios are well-documented

Performance of ‘pure’ long/short factor portfolios

- USA, Dec 1931- Nov 2015, log scale!
- ‘Bet against Beta’ has highest return (total beta=0 ⇒ shorting + leverage)

Source: Andrea Frazzini www.econ.yale.edu/~af227/data_library.htm
AuM of outperforming strategies grow strongly

- Keyword search on “low vol”, “managed vol” etc.
- Strong growth, but AuM in mutual funds are still low
- Estimates for institutional money (not shown in Morningstar) are much higher

Source: Morningstar mutual fund database for equity funds, as of Dec. 2015.
Search for keywords in fund name, excluding funds without low risk objective.
High demand challenges capacity – Case study emerging markets

How long does it take to invest a large portfolio?

- Build up $80 bn in low-risk smart beta (2% of market cap)
- Participate in 20% of average daily volume
- Compare standard, equal-weighted, risk-weighted and MinVol index
- A significant portion of the (more concentrated) MinVol index is illiquid

Source: MSCI and Datastream. Portfolios as of 29/05/2015. Trading volume 3 mth average, Market data from 14/06/2015
Crowding in Low Risk strategies increases, but the effect can be reduced through active management...

The active low risk strategy (MinRisk) is less exposed to crowded stocks

The passive low risk strategy (MinVol) is constructed without alphas and penalty for crowding

Source: MSCI and Datastream.
The result is a strategy with less crowding and similar returns

- The penalty on crowding does not impair performance
- The return of a passive MinVol portfolio (without alpha signal) is lower than the return of the MinRisk portfolio

Source: MSCI and Datastream.
... AND INTO FIXED INCOME

DR HARALD HENKE
Associate Director,
Head of Fixed Income Research
We switched our investment in global corporate bonds to a passive investment strategy. We noticed that our corporate bond managers were almost solely loading on carry and made decent returns during the bull market. When the crisis [of 2008/09] hit, they lost 10% or more.

(A large global asset owner)
Market cap determines issuer spreads – globally
Popular equity factors are highly correlated to spreads
Stock options vs. bonds – the case of Lehman Brothers

Implied volatility derived from Lehman Brothers options signalled danger ahead well in advance of Lehman corporate bond spreads.
Corporate bond spreads and returns are predictable using economic factors

A factor-based model can consistently yield alpha over the course of a credit cycle.

Performance of a multi factor corporate bond model
Biographies

Dr Volker Flögel, CFA, Director, has worked at Quoniam Asset Management since March 2006 and leads the Equities Research team. After being awarded a degree in business administration from Ludwig-Maximilian University (LMU) in Munich, he went on to obtain his doctorate in 2006 at the European Business School in Oestrich-Winkel, specialising in the microstructure of capital markets. At the same time, he worked as a consultant for alpha portfolio advisors GmbH in Bad Soden, Germany. The focus of his consulting work was on measuring the transaction costs of institutional investors and selecting managers. Dr Volker Flögel has been a CFA charterholder since 2010.

Dr Harald Henke, Associate Director, has been with Quoniam Asset Management since November 2006. As leader of the Credit Strategies team, he is responsible for the credit models and their update/enhancement. Dr Henke studied economics at Frankfurt am Main’s Goethe-University. He completed his doctorate on empirical market microstructure analysis, with a particular focus on capital markets in emerging countries, at European University Viadrina in Frankfurt an der Oder.

Nigel Stapleton, MA(Cantab), FCWA
Nigel is Chair of Trustees for two large UK Defined Benefit Pension Scheme; the Mine-workers Pension Scheme (AUM £10.5b) and the National Grid UK Pension Scheme (AUM £17B) His functional background is in finance in which he undertook a number of roles with Unilever during the first 18 years of his business career, latterly as Vice President Finance of the Holding company for their US and Canadian businesses. At Reed Elsevier – the professional and business publisher – he served as CFO from 1993 and subsequently as its Co Chairman. He has held a varied portfolio of Non Executive roles since 2002, including with the London Stock Exchange (to 2010); the UK Postal Regulator where he was Chair from 2004 to 2010 and Samruk Kazyna (the Sovereign Wealth Fund of Kazakhstan) until 2015.
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