CAMRADATA

Pension Conference

Investing in a Brave New World

27 April 2017

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Welcome to:

CAMRADATA's Pension Conference 2017

We are delighted you are able to join us today at our annual Pension Conference, this year titled 'Investing in a Brave New World'.

We are in an un-predictable...ever changing world.

Certainly, Defined Benefit pension schemes in the UK are entering a new era. For over twenty years employers have been closing schemes and more and more companies are now also closing to future accruals.

From an investment standpoint, we have endured the financial crisis in 2008 and many now state the future looks more positive…and that growth and interest rates are starting to rise.

The question is how do we prepare for unpredictability and change within pensions and investments?

Today we will learn about opportunities that pension schemes can consider in order to help meet their liabilities and generate return for the future; such as Multi Asset, Emerging Markets Debt, Diversified Growth Funds, Alternative Risk Premia and Multi Asset Credit. We will also hear about ESG and the increase in focus in these factors as more people look at investments which are "doing the right thing".

So let's find out what Investing in a Brave New World could feel like!

> "Certainly, Defined Benefit pension schemes in the UK are entering a new era"

Agenda

8.30 **Registration and tea/coffee**

8.50 **Introduction**
Amy Richardson, Associate Director, CAMRADATA

9.00 **Old Mutual Global Investors – Style Premia: The Democratisation of Alternative Beta**
Leif Cussens, Portfolio Manager, Multi-Asset

9.30 **PGIM – Emerging Markets Debt: As Exciting As You Want It To Be**
Tim Whyman, Principal, Emerging Markets Debt Portfolio Manager

10.00 **Forex Market Rigging - Panel Discussion**
Keith Butler, Partner, Strange & Butler LLP
Brian R. Strange, Partner, Strange & Butler LLP
Chaired by: Sean Thompson, Managing Director, CAMRADATA

10.30 **Break**

11.00 **LGT Vestra – TRUMP – Timing –Rally – Underlying Currencies – Markets – Perception**
Sanjay Rijhsinghani, Partner

11.30 **MacKay Shields – Why Investors Should Consider Multi-Asset Credit?**
Dan Roberts, Executive Managing Director, Head of the Global Fixed Income Group

12.00 **Amundi - How can big data help with ESG integration.**
Antoine Sorange, Head of ESG Analysis

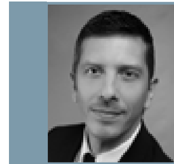
12.30 **Redington – Why we need to teach our children how to budget, save and invest?**
Robert Gardner, Co-founder

12.50 **Closing remarks**

13.00 **Lunch**

Speaker

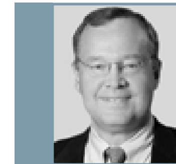
Bios



Antoine Sorange

Head of ESG Analysis

Antoine Sorange joined Amundi as a Quantitative Analyst in 2000 and subsequently joined the SRI Department as a Portfolio Manager in 2004. He notably managed global equity funds, based on both on a Best-in-Class approach and environmental themes such as Climate Change and Water. Antoine was appointed Head of ESG Analysis in October 2008. His team is composed of 17 analysts responsible for ESG research across Amundi Group. This team took top place in the SRI/ESG asset management category of the 2016 and 2015 editions of the "SRI & Sustainability" survey published by WebConvene Extel and the UKSIF. Antoine is a member of the French Asset Management Association (AFG) which contributed to the launching of a government-backed SRI label. Antoine holds a Master's degree in Fundamental Physics from the University of Paris XI and Imperial College London (2000) as well as a Master in Finance from the University of Paris VI (Pierre and Marie Curie University).



Dan Roberts

Executive Managing Director, Head of the Global Fixed Income Group

Dan C. Roberts is an Executive Managing Director, Head of the Global Fixed Income Group and its Chief Investment Officer. His responsibilities include spearheading macro-economic research, managing portfolios and chairing GFI's Investment Policy Committee (IPC). Dan joined MacKay Shields in 2004 when the firm acquired the fixed income business of Pareto Partners, where he had served as Chief Investment Officer. Dan first began assembling his team in 1989, when he was appointed head of fixed income at UBS Asset Management. In 1997 the team joined Forstmann-Leff International and was subsequently purchased by Pareto Partners in 2000. Prior to UBS, Dan worked at Chase Manhattan Bank, initially as a Financial Economist before being named head of Global Interest Rate and Currency Swaps Trading.

Before joining the private sector, Dan served at The White House with the President's Council of Economic Advisors from 1981 to 1983, was the Chief of Staff of the U.S. Congress' Joint Economic Committee from 1984 to 1985 and was an economist at the U.S. Securities and Exchange Commission from 1977 to 1978.

Dan holds a BBA and a PhD from University of Iowa. He has been working in the investment industry since 1977.

Sanjay Rijhsinghani

Partner

Sanjay is a Partner at LGT Vestra, specialising in managing global investment mandates with multi asset class solutions, and has developed the capability to provide a personalised options trading facility for private clients. Previously he was at UBS WM (UK) Ltd where he managed institutional funds along with private client money and prior to this he was an Investment Director at Laing & Cruickshank, and manager of the OM BD technology fund at Brewin.

Leif Cussen

Portfolio Manager, Multi-Asset

Leif joined Old Mutual in 2005. He is the lead portfolio manager of the Old Mutual Style Premia Absolute Return Fund. Prior to joining the alternatives team he co-managed the Global Statistical Arbitrage Fund. Previously, Leif was a portfolio manager in the quantitative strategies group where he co-managed a range of systematic global equity market neutral and long-only funds. In this role he was involved in a number of key successful product launches including the Old Mutual Global Equity Absolute Return Fund, the team's first market neutral UCITS fund, and a European 130-30 fund. Leif has a BSc in computer science from Royal Holloway College, University of London, and is a CFA charterholder.

Speaker

Bios

Tim Whyman

Principal, Emerging Markets Debt Portfolio Manager

Tim Whyman is a Principal and an Emerging Markets Debt Portfolio Manager for PGIM Fixed Income, based in London. Mr. Whyman is a sector specialist for PGIM Fixed Income's Emerging Markets Debt portfolio management team with responsibility for Eastern Europe and local rates strategies. Mr. Whyman has more than 15 years of experience in portfolio management. Prior to joining the Firm in 2011, he was an emerging markets fixed income specialist with Nomura. Earlier, he was a portfolio manager for Finisterre Capital LLP, an emerging markets hedge fund, and co-managed emerging markets portfolios at Rogge Global Partners. Mr. Whyman received a B.Sc. Honors in (MORSE) Mathematics, Operational Research, Statistics, and Economics from the University of Warwick.

Robert Gardner

Co-founder

Rob's dream is to transform people's financial future from hoping for the best to knowing what to do. He believes we can achieve this by focusing on education and collaboration, which is why he wrote the childrens book "Save Your Acorns" and co -founded Redington, Mallowstreet and RedStart.

In 2006 Rob co-founded Redington because he felt there was a better way to solve the pensions crisis. Redington is now a leading independent investment consultancy. Its goal is to make 100 million people financially secure, by empowering individuals, trustees and companies to make better decisions.

Rob also co-founded mallowstreet, an online community for the pensions industry. Which works to solve the pensions and savings crisis through education and collaboration.

Rob's passion is to help future generations save more for a better financial future. Which is why in 2012 he launched RedStart a financial literacy programme. RedStart aims to plant the seed for the financial well-being of young people. In 2016 he wrote the children's book "Save Your Acorns" to help 4 to 6 year olds learn about saving, investing and sharing.

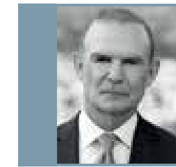
Rob also chairs the Children's Savings Policy Council for the Tax Incentivised Savings Association (TISA). To ensure all children in the UK can live the financial life they aspire to. By equiping them with the attitude, skills and resources to achieve their personal and financial goals. Rob is also a trustee of The FairLife Foundation, which helps people save and invest money for their future.

Keith Butler

Partner

STRANGE & BUTLER LLP

An experienced antitrust lawyer, Keith's practice focuses on affirmative recoveries for large corporate clients harmed by anti-competitive conduct. Keith began his career at Latham & Watkins, and has since recovered hundreds of millions of dollars for clients in financial services and other matters. Keith is active in the antitrust and competition law community, and has been published widely; his antitrust writings have appeared in Law 360, Global Competition Review, and Competition Policy International, among others.



Brian R. Strange

Partner

STRANGE & BUTLER LLP

An experienced and respected complex business trial lawyer. He was designated one of Southern California Super Lawyers from 2010 to 2015. Brian has decades of complex litigation experience, and has recovered hundreds of millions of dollars for clients during his illustrious career. Brian is admitted to practice before the United States Supreme Court, all courts in the State of California, and numerous federal courts throughout the US.

Speaker

Bios

Sean Thompson

Managing Director

With over 25 years' experience in London's financial services, including investment consultancy, asset management and insurance, Sean brings wide industry knowledge to CAMRADATA. He was previously Managing Director at Meridian Performance Services and has also worked for companies such as AllianceBernstein and City Capital Counselling UK.

Amy Richardson

Associate Director

Amy Richardson has worked in Investment Services for over 18 years with Pension Funds, Asset Managers and Consultants. Amy is currently responsible for Pension Funds and some key Asset Manager relationships at CAMRADATA. Prior to working at CAMRADATA, Amy specialised in Performance, Risk and Analytical services at BNY Mellon and started her career at Russell Investments, where she provided technical analysis to support the research of multiple universes of asset managers. Amy holds a BSc (Hons) degree from the University of Portsmouth, has the IMC and has passed the first level of the CIPM.

Why multi-asset investing?

The world of multi-asset investing since the financial crisis of 2008 has changed significantly. Investment managers have moved away from the almost binary choice of equities and bonds to a much more "multi-dimensional and much expanded opportunity set[1]" in order to provide the required returns for their investors and within their "risk budget".

Arguably the biggest challenge for all investors, and in particular pension scheme trustees looking forward, is how to manage their scheme investments with "risk assets" looking increasingly expensive. Value is becoming harder to find. The primary reason for this outcome has been the huge amount of liquidity released by the world's central banks in the form of "Quantative Easing" (QE). It is worth reminding ourselves that since 2008 and the advent of the financial crisis, it is estimated that some $13 trillion has been created by central banks to buy government and corporate bonds. To put this into context, this is equivalent to 70% of the annual economic output of the US. We have also seen renewed QE post-Brexit in the UK and the European Central Bank has extended its bond-buying programme until December 2017.

Simply, what we have witnessed since 2008, has been a huge manipulation of markets causing price dislocation with negative yields making the determination of a "risk-free rate" almost obsolete. To provide some further context, since the Bank of England introduced QE the FTSE All-Share has risen by 148.81%[2] and inflation, as measured by CPI, over the same period has increased by 18.4%[3] .

We are in uncharted waters and, as the Greek philosopher Heraclitus observed, "water in the river was never the same twice" which has never been more true for financial markets. It is important for trustees to be mindful of the fact that "for some asset classes past performance is not only a poor guide to future returns but maybe almost impossible to repeat"[4]. Making assumptions about future market conditions based on historic data can lead to false and erroneous conclusions and, although we cannot dismiss the lessons from history, "we do need to be careful how we use them (sic)"[5].

A combination of QE and almost near-zero interest rates could be likened to the financial system taking a dose of morphine administered at regular intervals by central banks to numb the pain of the financial crisis of 2008. It has the effect of making the patient almost forget its illness. As markets rise, the question is whether investors have been lulled into a potentially dangerous and fatal false sense of security? Let's look at, for example, the VIX (CBOE Volatility Index) which is sometimes referred to as the "fear index". The VIX seeks to measure the implied volatility of the market and is "therefore a reflection of investors' perception of future volatility or market-risk"[6]. This year so far, the VIX has averaged at 12 which is a little below the longer term average and indicates perhaps that investors are sanguine about the levels of "risk". Is this a prudent reaction to market risk or a worrying complacency?

> "Making assumptions about future market conditions based on historic data can lead to false and erroneous conclusions"

So how can multi-asset investing protect trustees of pension schemes in a world where "risk" is being manipulated and where "financial repression" has been the policy of central banks since 2008? On top of this is an increased sense of political instability around the world that could "spook" investors into a quick and rapid change in sentiment. The result being that equity markets and "risk-assets" generally become vulnerable to "a sell-off" with an ensuing increase and spike in volatility.

1 Talib Sheikh: Morningstar Perspectives
2 Source Bloomberg. Total Return 5th March 2009 – 12th April 2017.
3 Source Hargreaves Lansdown, Lipper IM as at 4th March. Quoted in the Money Observer April 2017.
4 Jonathan Marriott "Did the ancient Greeks know a thing" Jersey Business Briefing. November 2014
5 Jonathan Marriott " Did the ancient Greeks know a thing". Jersey Business Briefing. January 2014.
6 Neil William Investment Director LGT Vestra US "Understanding Risk". April 2017

Clearly, an essential tenet of multi-asset investing is to adopt a carefully constructed top-down and appropriately diversified, actively-managed portfolio which has exposure to a blended range of different asset classes and strategies. The portfolio would be designed to mitigate and manage "volatility" over an "investment cycle" and provide a sustainable level of targeted return linked to the requirements of the pension scheme. If we accept the premise that a portfolio will invest (depending on market conditions) in a combination of "risk assets" such as equities and strategies that we can broadly categorise as "stores of value", then an experienced multi-asset manager can blend these differing approaches to meet a scheme's performance target through varied market conditions.

> "At LGT Vestra LLP we have extensive expertise and experience in managing a broad range of multi-asset portfolios for trustees of pension schemes"

Broadly, in periods where "risk-assets" are considered "good value", for example 2012/13, an overweight position in equities, specific skill-based and sector specific strategies could be an appropriate allocation for a scheme. In more challenging market conditions, a greater weighting towards asset classes and managers that are recognised "stores of value" and offer capital protection, would be the right approach. By definition, successful multi-asset portfolios have to be "forward-looking", requiring a convictional approach with a clear focus in terms of an investment philosophy that underpins and informs the ongoing management of the portfolio combined with a high quality research capability.

At LGT Vestra LLP we have extensive expertise and experience in managing a broad range of multi-asset portfolios for trustees of pension schemes. Each portfolio is bespoke to the scheme in question and tailored to meet the specific requirements of the scheme trustees. LGT Vestra is one of the few global wealth management firms in private ownership. Founded in 2008, we are a UK-based partnership between LGT, wholly owned by the Princely Family of Liechtenstein, and the executive partners of LGT Vestra. Our private ownership ensures a long-term outlook and financial stability, which together with a shared vision, creates the essence of our business.

If you would like any further information about our multi-asset investment capability and how this approach can be effectively deployed by trustees for pension scheme assets then please contact Tony Allan, Partner and Head of Business Development at tony.allan@lgtvestra.com

Written by

David Lane,
Partner / Business Development Technical Director
LGT Vestra

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A fresh approach

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Tony Allan, Head of Business Development
+44 (0)20 3207 8003
tony.allan@lgtvestra.com
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A Leader in Income-Oriented Investing

MacKay Shields is a fixed income investment manager specializing in income-oriented investment strategies.

As of March 31, 2017, we manage over $90 billion in assets with expertise in credit intensive research and asset allocation strategies, global credit and capital preservation.

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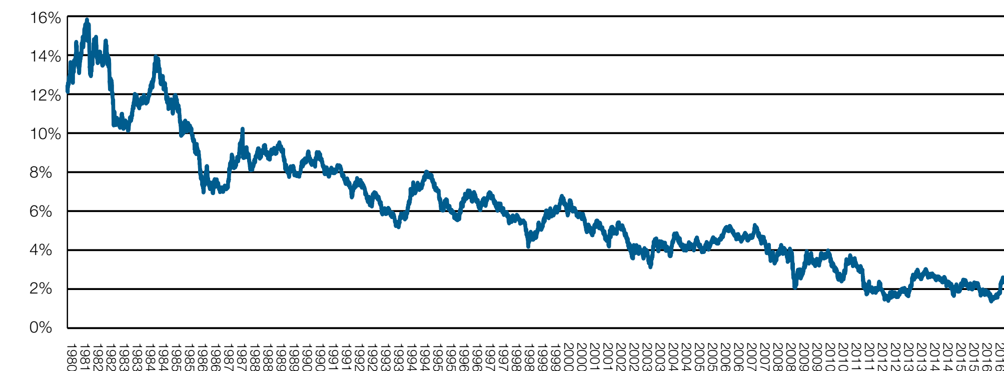
Unconstrained Fixed Income:

Why Now?

Investors today find themselves in an unusual quandary. Historically, they have thought of fixed income investments as a relative safe haven to offset more volatile and risky investments in other parts of their portfolios, including equities. The risk of capital loss in bond portfolios was generally viewed as limited. That premise no longer holds. After decades of falling interest rates and the past several years of unprecedented global monetary intervention, investors in conventional bond strategies are becoming increasingly concerned about risk of loss as interest rates potentially renormalize. They are reviewing the role of traditional fixed income and are seeking alternatives that better avoid uncompensated risk. We believe that unconstrained fixed income strategies are a potential answer to these concerns. Unconstrained approaches are able to allocate capital and adjust their risk exposures dynamically, across the fixed income spectrum, with fewer constraints.

Historical US 10-Year Treasury Yield



Through 07/04/2017, Source: Bloomberg, MacKay Shields

The Investment Landscape Has Changed

The risk-return trade off offered by duration-sensitive assets has changed. The most obvious aspect is the scarcity of yield has made things increasingly difficult for income investors. More fundamentally, the whole concept of high grade bonds as “safe haven” assets is being called into question.

In the past, investors have been well compensated for taking interest-rate risk through both income and capital appreciation. For 30 years, institutional investors were commonly advised to have between 20 and 40% of their portfolio in bonds because of their negative correlation to equities and ability to provide ballast in times of stock market upheaval. And, historically, Treasuries and other high quality sovereign bonds have been an effective safe haven.

However, Treasuries’ usefulness as a diversifier rests on their potential to appreciate and, given today’s low level of yields, that potential is now more limited, irrespective of whether risk aversion increases. It’s not safe to assume that the periods of strong negative correlation with equities we’ve seen in the past will be repeated in the future.

One way to think about the risk/return tradeoff is breakeven levels: how much of an increase in interest rates can a bond investor absorb before incurring a loss? For example, in 1999, rates rose dramatically and bond prices fell by more than 7%, but coupon income was high enough to absorb most of that, and the total return on the Barclays US Aggregate fell by just -0.83%. Today, that layer of insulation is awfully thin. At the end of March 2017 the average yield on the index was only 2.6%—less than half of what it was at the start of 1999. At those levels, yields would only need to rise 0.43% before the Barclays Aggregate would start to suffer a loss.

> “The risk of capital loss in bond portfolios was generally viewed as limited”

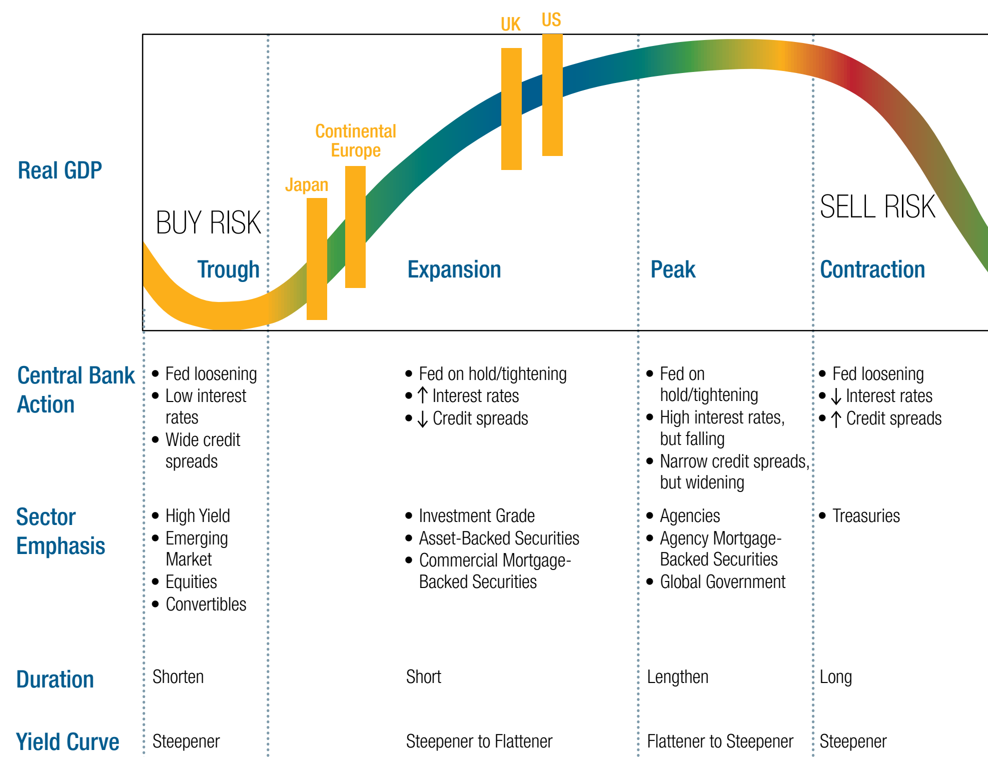
A Different Landscape Calls for a Different Approach

Concern about rising rates and a desire to manage downside risk are fueling investors' interest in unconstrained bond strategies. As the name suggests, unconstrained is a "go anywhere" approach that gives managers the flexibility to allocate capital more efficiently, taking the risks that offer the best compensation at different stages in the economic cycle. They are able to invest in a broad global opportunity set spanning sectors such as emerging markets and high yield corporates as well as investment grade securities. They are not tied to a traditional benchmark so they can choose how much interest-rate exposure they take. To varying degrees, they typically also use hedging instruments and short positions to manage risk.

History has shown that no single fixed income sector performs well in every environment, so increased flexibility and a dynamic approach can enhance returns. For example, if the economy is moving into an expansion phase, credit-risk driven securities such as high-yield corporate bonds have historically tended to outperform Treasuries. Conversely, if the economy is heading into a slump or risk appetite is falling, managers might choose to reduce their credit exposure and take on more duration. The 2008/09 financial crisis is a good example: Duration assets outperformed credit during the crisis, then credit sharply outperformed Treasuries in the recovery.

> "History has shown that no single fixed income sector performs well in every environment, so increased flexibility and a dynamic approach can enhance returns"

Some market participants argue that unconstrained investing is simply about replacing interest rate risk with credit risk. But the reality is much more nuanced. We'd argue that it's more a case of shifting away from uncompensated risk in favor of compensated risk. The landscape is a moving target: duration is of great concern in the current environment and investors are better compensated for credit risk. So today, many unconstrained portfolios hold more credit than duration (for example, we think high yield bonds currently continue to offer an attractive risk/return tradeoff.) But the opposite is likely to happen at some point down the road. A key objective of unconstrained managers is to correctly identify shifts in the landscape and adjust the portfolio accordingly, and flexible mandates allow them to do so.



	Trough	Expansion	Peak	Contraction
Central Bank Action	• Fed loosening • Low interest rates • Wide credit spreads	• Fed on hold/tightening • ↑ Interest rates • ↓ Credit spreads	• Fed on hold/tightening • High interest rates, but falling • Narrow credit spreads, but widening	• Fed loosening • ↓ Interest rates • ↑ Credit spreads
Sector Emphasis	• High Yield • Emerging Market • Equities • Convertibles	• Investment Grade • Asset-Backed Securities • Commercial Mortgage-Backed Securities	• Agencies • Agency Mortgage-Backed Securities • Global Government	• Treasuries
Duration	Shorten	Short	Lengthen	Long
Yield Curve	Steepener	Steepener to Flattener	Flattener to Steepener	Steepener

As of 1Q 2017

The Outlook for 2017 and Beyond

We believe there will be continued upward pressure on short-term US interest rates in 2017 as the Federal Reserve tightens monetary conditions and the new administration embarks on looser fiscal policies. The fundamental economic backdrop in the US has been durable; consumption is being supported by a healthy consumer enjoying wage gains from a tighter labor market, and an increase in wealth from a burgeoning housing market. President Trump's fiscal platform calls for an increase in spending, especially on infrastructure, and lower taxes for households and businesses. While tax cuts should be stimulative for the US economy in the short-to-medium term, some of the other proposals may not have the same impact, in our view. In particular, protectionist trade policies would likely curtail global growth and incite trade wars.

We do believe credit spreads could tighten modestly given our tempered outlook for corporate earnings and high levels of idiosyncratic risk. Valuations generally remain fair across the credit sectors but greater vigilance is required as we navigate the late stages of the current economic cycle.

Written by

Dan Roberts,
Executive Managing Director, Head of the Global Fixed Income,
MacKay Shields

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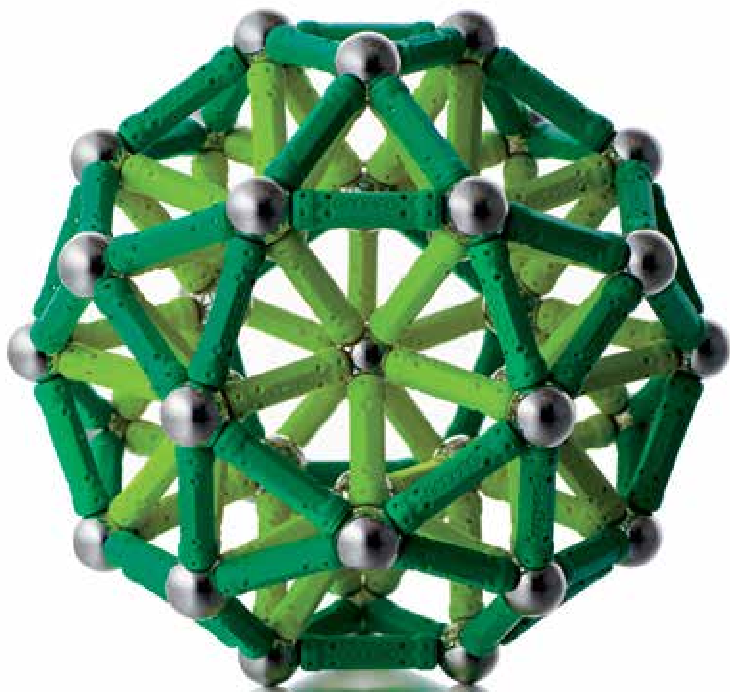
> "President Trump's fiscal platform calls for an increase in spending, especially on infrastructure, and lower taxes for households and businesses"

IT'S A COMPLEX FINANCIAL WORLD OUT THERE.

WE MAKE SENSE OF IT.



Old Mutual Global Investors is the London-based asset management arm of Old Mutual Wealth. With over £31.2bn* under management our reach covers key international markets including the UK, Europe, Asia and the Americas.

We don't believe in house style. Instead, our fund managers actively manage assets using their own expert judgement, giving them the freedom to seize opportunities in a fast changing market.

Today's complex, interconnected and increasingly globalised world requires fund managers to be more transparent and accountable than ever. But more importantly it calls for a simple, clear and sensible investment approach.

Please remember that past performance is not a guide to future performance. Investment involves risk. The value of investments and the income from them can go down as well as up and you may not get back the amount originally invested.

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Style Premia:

More than just Academia

Leif Cussen, manager of the Old Mutual Style Premia Absolute Return Fund, outlines four elements crucial to the selection of factors that can be harnessed to build systematic, liquid and well-diversified strategies.

Factor investing, whereby the fundamental and technical drivers of securities are used to create diversifying strategies, has in recent years become democratised: it is now accessible to investors beyond those willing and able to pay hedge funds 'two and twenty.'

Yet these generic factors – which we call 'style premia,' given they also refer to different investment styles – have proliferated in recent years.

In this piece, we describe our process for selecting from hundreds of potential candidates the style premia factors that can be harnessed to build systematic, liquid strategies – at the same time as being generally uncorrelated to each other and to major asset classes.

Rigorous research

A basis in academic research is our starting point. Intuitively most investors could probably name a number of different factors that generate returns across different asset classes, but in order to create a robust, systematic strategy, we utilise the wealth of research conducted into these approaches over the last few decades.

As such, when examining a factor, we are looking for peer-reviewed research. But a foundation of academic research is not enough to give us confidence in persistent returns going forward. Indeed, a recent paper found over 300 factors with peer-reviewed, published research[1].

Just because one can brandish an academic paper about a factor does not mean it should be included in a portfolio. Given the risk of data-mining we would not necessarily expect all of these factors to deliver persistent returns over the coming years.

> "Just because one can brandish an academic paper about a factor does not mean it should be included in a portfolio"

Intuition

Next, for any factor, we ask the question: why are we being paid for taking on this exposure?

Typically, for us to seek to use a factor, there is typically at least one of three distinct answers to this question. The first is the 'risk premia' argument: by taking on a particular set of exposures, we are taking a risk – for which the market is compensating us.

The second is that there is a structural inefficiency in the marketplace, which we expect to persist and of which we can take advantage in order to generate returns for our investors. The third reason: there are behavioural biases that we expect to persist in the future, which will also enable us to generate returns.

These answers, or a combination of them, give us some comfort that the factors we are examining are not simply the result of a data-mining model or signal.

Persistence and pervasiveness

Still, having a good story that is backed up by research is still not enough, which is why we look for persistence and pervasiveness in a factor.

We seek persistence in returns over an extended period of time. This does not mean that factors will have only ever gone up: some will certainly have periods of not insignificant drawdowns. But we do look for factors that have delivered persistent positive returns.

1 Harvey, Campbell R. and Liu, Yan and Zhu, Heqing, …and the Cross-Section of Expected Returns, SSRN, 2013

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Pervasiveness – and effectiveness – across regions and asset classes is also crucial. If it makes sense that a factor should have efficacy in the US, Europe and Japan – but it fails to deliver positive returns in Europe, this would start ringing alarm bells. The cause for this inconsistency might be explained, as an example, by differing micro-structure of each market; however, because we take a conservative approach, we favour those factors that perform well across regions.

Similarly, intuition may suggest that a factor that works in equities should also be applicable to fixed income, FX and commodities. Again, if a factor fails to work across a number of asset classes, this also raises questions

> "We seek to harness transparent, generic factors that enable us to give clearer insights into what is driving portfolio returns"

Transparency

Selecting style premia is not simply about picking those factors that, once harnessed, enable us to 'look under the hood' of a portfolio and examine the underlying code. We seek to harness transparent, generic factors that enable us to give clearer insights into what is driving portfolio returns.

One of the attractions of generic style premia factors to many investors is the insight it can give them into what is driving portfolio returns. Style premia strategies typically take a more generic approach to factor implementation. This more transparent approach can lead to a better understanding among investors over what is driving portfolio returns and whether a product is behaving as would be expected.

This increasingly popular generic approach has the added benefit of leading to the commoditisation of many factor-based products, which has improved accessibility to these types of strategy.

Four factors

Once all these elements have been taken into account, we are left with a small-yet-robust group of factors from which we can build a well-diversified portfolio. In the Old Mutual Style Premia Absolute Return Fund, these are value, the idea that relatively cheap assets tend to outperform those that appear to be expensive; quality, the idea that high-quality, low-risk assets tend to deliver higher returns on a risk-adjusted basis; carry, the idea that relatively higher-yielding assets tend to generate higher returns; and momentum, the idea that performance trends tend to continue.

Crowding risk

Of course, building a well-diversified portfolio requires more than simply choosing effective style premia. Once these principles have been applied to factor selection, we look at the risks that accompany the implementation of the strategy.

As this type of systematic investing has grown in popularity, so too has the perceived risk of crowding, whereby investors huddle around the same positions, creating problems when the market environment shifts and there is a 'rush to the exit.' The purposefully generic nature of the style-premia approach could even compound the risks posed by crowding, namely lower returns and higher chances of significant drawdowns.

As a result of this, it is important for investors who deploy style premia to consider how their portfolios might fare in the event the market suffers risk-off episodes. Strategies aimed at mitigating the downside – such as statistical arbitrage, which we deploy – could be particularly useful under such scenarios.

While style premia present an exciting and low-cost opportunity to capture what had once been within the purview of hedge funds alone, they clearly pose risks, too. This is why we seek to adhere to these four simple principles in factor selection – and have strategies in place for the event that market volatility spikes.

Written by

Leif Cussen,
Portfolio Manager, Style Premia (cf Multi-Asset)
Old Mutual Global Investors

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A Sweet Spot for Emerging Markets Debt

Q2 2017 Outlook

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- Emerging markets debt is expected to perform well in Q2 given attractive valuations and the improved outlook for global economic growth.
- Many EM central banks have more room to maneuver given that the U.S. Federal Reserve's future rate hikes are largely priced into the yield curve.
- EM local currency bonds may 'catch-up' with the recent strength in EMFX. With positive inflows and supportive technicals, EM local rates are expected to outperform.
- Both EM hard and local currency debt offer value on a name-by-name basis.

Through March 2017, top-performing sovereign EM debt issuers were primarily lower-rated credits that posted double-digit returns, such as idiosyncratic Belize (+61.32% on restructuring), Mongolia (+12.68% on an IMF program), Iraq (+8.21%), Dominican Republic (+7.74%), select African commodity names that were up between 6-7%, and Brazil (+6.22%). Even Turkey was up (+5.31%) on supportive technicals and valuation, despite a deteriorating policy backdrop and a credit rating downgrade.

In addition, the credit rating outlooks for Russia and Argentina were upgraded to positive and, for Brazil, to stable. EM corporates were mixed during the quarter, although many credits performed well. Relative to EM sovereigns and quasi-sovereigns, however, we believe EM corporates appear to be fully valued.

	Total Return (%) Q1	Spread/ Yield Change (bps) Q1	OAS (bps)/Yield % 3/31/17
EM Hard Currency	3.87	-31	310
EM Local (hedged)	2.08	-24	6.55%
EMFX	5.18	-90	3.73%
EM Corporates	2.97	-20	295

Source: JP Morgan as of 31 March 2017. Past performance is not a guarantee or reliable indicator of results. An investment cannot be made directly in an index. Data is for the following JP Morgan emerging markets debt indices, respectively: JPM EM Bond Global Diversified, JPM Government Bond-EM Global Diversified, JPM EM Local Markets Plus, and JPM Corporate EM Bond-Broad Diversified.

> "The credit rating outlooks for Russia and Argentina were upgraded to positive and, for Brazil, to stable"

The strong quarterly performance in EMFX reflected the outperformance of higher-yielding currencies versus the USD on the reach for yield and a more optimistic EM economic growth outlook.

Historically, a widening growth differential between developed markets and emerging markets has historically proven to be a supportive tailwind for EMFX, as observed in the following chart. Particularly solid EMFX returns included the Mexican peso (+10.98%), Russian ruble (+9.16%), and Brazilian real (+5.09%).

Laggards included lower-yielding Asian FX, in part reflecting global trade uncertainty and a weaker Chinese currency, while the Turkish lira fell (-1.21%).

Overall, we expect current, positive trends to continue in EMFX with a range-bound USD and accelerating EM growth. The next trade is likely in Central and Eastern European FX, a region which has recently lagged.

An improved outlook for the euro makes us more likely to fund EMFX positions versus the USD instead of the euro.

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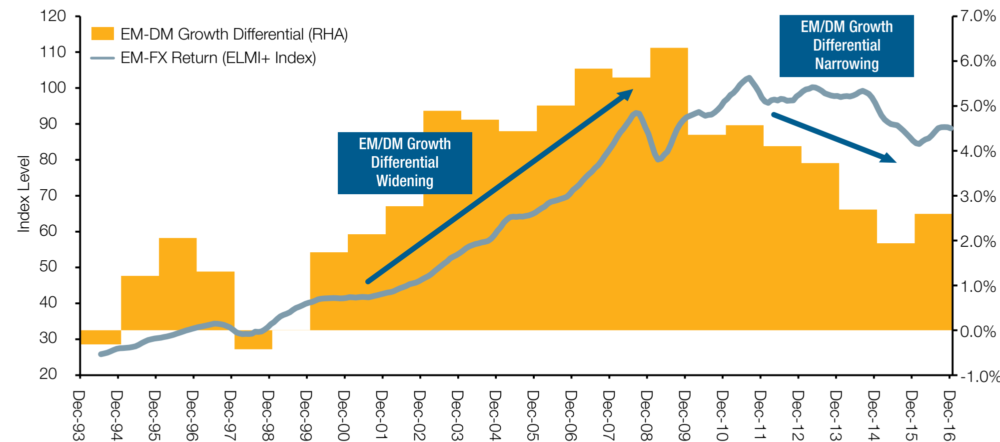
Emerging Markets/Developed Markets Growth Differential Compared to Emerging Markets FX



Source: IMF, J.P. Morgan, and PGIM Fixed Income. As of 31/12/2016.

> "A number of central banks are cutting rates, including Brazil, Chile, Colombia, and Russia"

EM hedged local bonds have lagged due to the move higher in U.S. Treasury yields, making them increasingly attractive from an overall yield perspective. Brazil was the top performer again, returning (+4.57%) as its central bank continued to cut rates. Peru, Indonesia, and the Philippines also performed well, each up more than (+4.0%) for the quarter. The outlook for EM inflation remains relatively benign.

A number of central banks are cutting rates, including Brazil, Chile, Colombia, and Russia. There are adequate premiums over policy rates in markets where the policy rate is going up. In Mexico, the central bank is hiking, and local bonds have been improving with the local bond yield curve flattening. We believe the somewhat improved outlook in Mexico makes its bond market attractive. Rates have lagged the currency and should do well over the next year. Given overall yield levels and the outlook for EMFX, we expect EM local rates will do well in Q2, notwithstanding additional Fed rate hikes. EM technicals have been impressive so far in 2017. There has been over $119 billion of new, gross issuance with most supply readily absorbed. And, the second quarter presents significant cash flow that is expected to be reinvested into the asset class amid generally strong interest in the sector.

Risks on the horizon include uncertainty surrounding U.S. trade policies, China, and commodities, which could negatively impact global growth expectations. Even with China's focus on FX reserves and its currency, financial stability and growth are paramount for its leadership. All indications are that going into the Party Congress later this year, China's economic growth should be in the 6.7% range, which should support EM assets.

While U.S. trade policy is a wildcard, the business-friendly cabinet is unlikely to initiate a trade war where the U.S. stands to lose significantly. Regarding the politics of populism, the momentum may be fading, though we are watching the French elections closely. Even on the back of lower oil prices and the Fed's rate hike in March, we are encouraged at how well EM debt has traded so far in 2017 as we appear to be in a "sweet spot" for the asset class.

Source: PGIM Fixed Income and JPMorgan. The information contained herein represents views and opinions of the author as of 31 Mar ch 2017 and is for informational purposes only. The information does not constitute investment advice and should not be used as the basis for an investment decision. Past performance is not a guarantee or a reliable indicator of future results. An investment cannot be made into an index. This material is presented only to persons who are professional clients or eligible counterparties. 2017-1929.

Written by

David Bessey, Managing Director,
Head of Emerging Markets Debt Team,
PGIM Fixed Income

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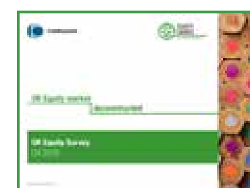
Emerging Markets Debt

Equities

UK Equities



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Amundi's approach to water risk analysis

When evaluating companies' exposure to the environmental component of ESG risk, great emphasis is placed on the consideration of greenhouse gas emissions. However, we know that water risk can often be significant, as evidenced by the $14 billion in water-related financial impacts reported by companies disclosing to CDP (formerly, Carbon Disclosure Project) in 2016. To better evaluate how portfolio companies might be impacted by worsening water security, we have developed a proprietary methodology to assess the extent to which companies are exposed.

According to a study by the Water Resources Group, the gap between supply and demand of water will reach 40% by 2030, taking into account demographic growth and assuming no advances are made in terms of efficiency. Companies that operate within sectors that are particularly water intensive, including Utilities, Mining, Beverages, and Oil and Gas, are increasingly exposed to a range of reputational, operational and regulatory water-related risks.

Our methodology uses information from public databases and company statements, including CDP data, to support analysis methods that have been developed internally.

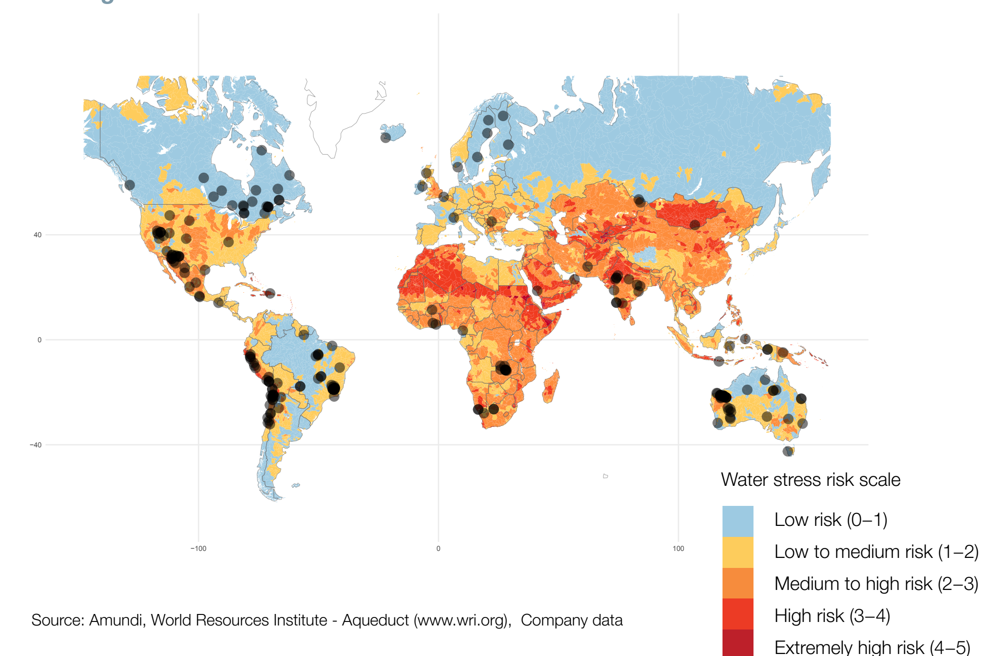
Take the mining sector, where significant quantities of water are required during both the extraction process and for mineral processing. Increased resource depletion and frequency of extreme weather events are leading to growing uncertainty around future resource availability. To analyze companies' exposure to this risk, we have developed an innovative analysis model that combines:

- Data from the World Resources Institute that examines the probability of extreme events (floods, drought), rainfall variability, and the level of competition between users, within river basins around the world; and
- GPS data for all the mining sites of the companies that we analyze.

Using this data, we map water risk, site by site and company by company, as shown in the map below:

> "According to a study by the Water Resources Group, the gap between supply and demand of water will reach 40% by 2030"

Mining sites and water stress



Source: Amundi, World Resources Institute - Aqueduct (www.wri.org), Company data

Amundi
ASSET MANAGEMENT

Once the risk has been identified at site level, we analyze company policies and performance against our water criteria. We are paying particular attention to raw data such as water withdrawal data and we use CDP data to make the comparison easier. For example, to analyze the performance, we compare key metrics for each company such as water intensity of conventional water (conventional water in megaliters/year divided by turnover), the proportion of alternative water, the proportion of recycled water, we analyze the trend in recycled water mix and the trend in alternative water mix. For companies identified as not taking appropriate actions to address water risks, Amundi will either enter into a phase of dialogue or downgrade the company, which can ultimately lead to divestment.

Our water analysis methodology, which we have also applied to the utility sector, palm oil production and non-conventional hydrocarbons, demonstrates our ability to develop robust and innovative analysis tools to determine companies' exposure to ESG risks. This ultimately enables us to better understand and, if necessary, challenge their practices for managing these risks efficiently.

> "Once the risk has been identified at site level, we analyze company policies and performance against our water criteria"

Written by

Antoine Sorange,
Head of ESG Analysis
Amundi Asset Management

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CAMRADATA

CAMRADATA
5th Floor, 80 Leadenhall Street,
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