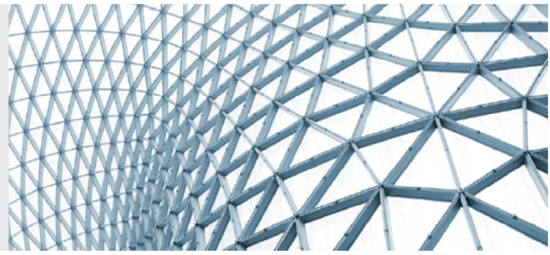
The HUB

NEWS AND VIEWS FOR INSTITUTIONAL INVESTORS



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Successful solutions require meaningful data

The complimentary of interesting investment ideas and robust data cannot be overstated, as Ossiam's experience in Italy clearly demonstrates.

Key Takeaways:

- The rising importance of Environmental, Social and Governance (ESG) investing has increased the need for custom strategies that align with the ethics, values and policies of any given institution
- The more specific the requirements of an investor become, the more the concept of a 'one size fits all' product gets called into question. The paradigm must shift from an 'off-the-shelf' product which acts as a proof of concept to a customized and scaled up solution to suit a specific investor's needs.
- With evolving regulatory frameworks and changing market dynamics, the importance of selecting a partner that understands nuance, exhibits flexibility and can proactively identify shifts in market backdrop rather than being beholden to them, cannot be understated.

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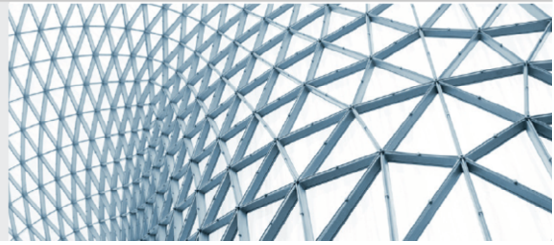
Can you explain the concept of a 'solutions provider' and explain how that differs to the traditional approach to products and services?

Carmine De Franco: When you buy a fund, and this is especially true when you buy an ETF, you are buying an investment strategy that is bundled into a product that exists, has a track record and an associated AUM. Now, while this has many advantages, the reality is that you are buying something that other investors in your peer group are also buying. Many investors, and especially institutional investors have quite specific constraints, their own views, their own capabilities their own asset allocation. As such, most of the time they need something that is tailor made to their needs.

What's more, the rising importance of Environmental, Social and Governance (ESG) investing has increased the need for custom strategies that align with the ethics, values and policies of any given institution. Some investors might prefer an exclusionary approach, others might prefer an approach favouring engagement. The more specific the requirements of an investor become, the more the concept of a 'one size fits all' product gets called into question.

The paradigm must shift from an 'off-the-shelf' product which acts as a proof of concept to a customized and scaled up solution to suit a specific investor's needs.

This is something that is part of our DNA at Ossiam. We are an asset manager focused on analysing, interpreting and testing data in the quest to develop investment ideas that will offer investors meaningful risk adjusted returns over the long term. The complimentary of interesting investment ideas and robust data cannot be overstated. Good ideas without good data or vice versa, will get you nowhere.



As such, when a client comes to us with an investment need and an associated set of constraints, we can work with them to translate that into an actionable investment strategy based on robust and material data. But it doesn't stop there. As a quantitative specialist, we are also able to identify whether such an investment strategy might result in unintended consequences and if so, work with the client to mitigate these. And in some instances, we even work with clients adjust and refine the investment needs or constraints when an appropriate solution just doesn't seem viable.

Creating tailored solutions often requires access to a variety of data, how do you go about selecting the right sources and providers?

Carmine De Franco: There's no unique checklist to verify the quality and materiality of data. Instead we've developed a flexible procedure based on our many years of experience, with a long list of potential aspects to explore and test. The data we use for designing and building customized solutions is the same data that we use in our publicly available ETFs i.e. it's both visible and transparent.

We typically, and this has been true historically for us, use an open-architecture infrastructure. We know that various data providers have differing areas of expertise, differing capabilities and differing strengths. It's rare that you find a data provider that is good at everything. This means that we buy and we license large amounts of data.

Take ESG data as an example. We have an overall ESG data provider, we tap into carbon data from another provider, we access Sustainable Development Goal (SDG) information from a third provider and we also leverage Biodiversity data from a fourth. Diversifying our data providers also means we are not overly reliant or dependable on a single model. If the same model is responsible for a wide variety of different data, you become highly dependent on that model. Any adverse impact, for whatever reason, will end up impacting all the underlying data.

Another thing that we do a lot is to thoroughly test the data used in a customized solution under a variety of conditions to ensure that everything that we put forward has been through a robust process internally. So if the data is flawed or if the data is meaningless, we recognize it before we embark on developing a solution.

What if a client wanted to make use of their own data or a preferred provider?

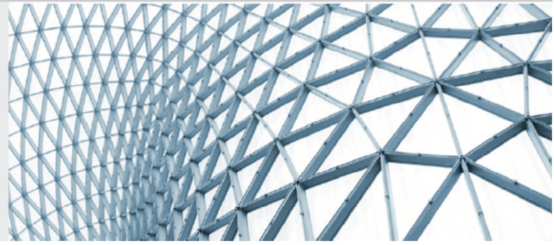
Carmine De Franco: Typically, there wouldn't be an issue using a client's preferred data provider or even a client's proprietary data set as long as it stands up to scrutiny. For example, many investors may have internal analytics or data sets that they would like to leverage. Companies around the world are waking up to the fact that they can start to monetize their data. If you can anonymise it, then you can sell it. As for institutional investors, they could potentially exploit all the data they produce in terms of asset allocation, investment themes and proprietary analytics . We can then help them exploit this internal data by developing a robust framework and test it to ensure it works under changing market conditions.

Why have customized solutions risen in popularity amongst Italian institutions in recent years?

Marco Avonto: Italy is one of the largest institutional markets in Europe. It is a market dominated by large pension funds, many of which began their operations less than 25 years ago as a result of Italy's pension reforms. In this relatively short space of time they have grown quite significantly. There are many asset managers therefore targeting the Italian institutional market.

What is extremely important is differentiation. It is not just a case of providing the best performance, but also providing the best client service. This goes beyond hygiene factors such as access to fund managers and customized reporting. Instead, clients are looking for trusted partners that understand their specific business, their specific objectives and the specific obstacles or constraints that lie in the way of achieving them. These partners then however need to have the relevant expertise and innovative capacity to develop tailored solutions that work around the obstacle and constraints to help them meet their objectives.

On paper this sounds straightforward, but in reality it's anything but. Institutions are faced with an ever-changing environment.



Whether it's evolving regulatory frameworks such as Solvency II or SFDR, changing market dynamics such as low or negative yielding rates or emerging trends such as ESG investing and disclosure, the importance of selecting a partner that understands nuance, exhibits flexibility and can proactively identify shifts in market backdrop rather than being beholden to them, cannot be understated.

What are some of the specific challenges that asset owners face today and how can their trusted partners help them overcome these?

Marco Avonto: ESG is clearly a huge overarching topic that is here to stay. Most investors started talking and thinking about ESG many years ago and now they're at the implementation stage. In a sense, there is a beauty to the diversity in which ESG has become adopted. Some investors adopt one kind of approach, others another. This further underlies the importance of selecting a trusted and consultative partner.

The other theme that is emerging and is related the current market climate is the validity of historic and traditional asset allocations. This goes beyond just equity versus bond allocations. Investors are increasingly thinking about their exposure at a much more granular level and thinking about which underlying factors and geographies they want exposure to and asking whether they are too biased towards certain areas of the markets.

It is worth bearing in mind that Italian investors have often had large exposures to domestic equity markets and government bonds, which in turn can create unintended risks and biases in portfolios.

How is the availability of data and tools used for analysis impacting the relationship between asset managers and asset owners?

Carmine De Franco: For us, it has been always our natural environment. Our investors know exactly what we do because we are a systematic asset manager. Even if we are increasingly developing active ETFs, our approach is a systematic one based on objective quantitative choices. Increasingly clients really want to dig into their investments and understand what has or hasn't worked and most importantly why?

A question clients are starting to ask more often is "What do you expect in the next six months?". Historically, what they were interested in was a market view. Now however, they're not looking for a market view but instead they want to understand how we expect our strategy will evolve. Where might it go in terms of allocation, in terms of sector exposure or in terms of degrees of risk.

Investors are getting much more precise and they want to know a lot detail more about their investments. And this is a good thing for the entire industry and a welcome change from our perspective.

Marco Avonto: Increasing interest in delving into the data is certainly a trend that we are witnessing with our Italian clients. Importantly however, it directly relates to the earlier point about selecting the right data. If the solution has been built on robust meaningful data and tested under a variety of market conditions, then conversations about the strategy and how might evolve ex-post can be hugely helpful for consultants and investment committees who are responsible for overseeing the interaction of entire portfolios comprised of various strategies and solutions. However this becomes more challenging if the quality of the data is lacking or the process is less systematic and more intuitive.

It is also not simply a question of asking the same five questions or trying to rely on the same five metrics across the board. Instead you must ensure that you are seeking meaningful insight that is directly related to the strategy before then considering what this might mean for a portfolio as a whole. This is no mean feat and is why many institutional investors still lean on consultants for their expertise in this area.

With ESG investing being such a hot topic among investors globally, as trusted partners and solutions providers how do you ensure investor expectations are aligned with investment reality?

Carmine De Franco: It's always a little bit frustrating to so many contradicting stories on the performance of ESG.

Last year there were news headlines, almost daily, extolling the outperformance of 'ESG' during the pandemic. Then in the first half of 2021 the strong performance of the energy and industrial sectors meant that all of a sudden, the same ESG companies and funds that had outperformed during the pandemic were underperforming. It reminds me of the debate surrounding factor investing and specifically the debate between value and growth. When a factor stops working, even for a relatively short period of time people start to challenge it.

My hope is that ESG investing doesn't become conflated with factor investing. Even if one year you might underperform because you don't have exposure to oil companies and oil is booming, that's fine, it's not the end of the world. If you are genuinely investing in sustainability, it shouldn't be an issue. Our clients do understand that, and as such they don't complain.

Marco Avonto: Even if there might be short-term performance opportunities in oil or coal, most people agree that ultimately these will not be sustainable. Of course, we will likely zigzag a little bit, taking two steps forward, one step backward. But ultimate direction of travel looks clear. If you asked me this question 10 years ago, I would have been more inclined to say that people were overly concerned with the relative performance of ESG strategies with respect to traditional ones. Now clients are more interested in the true impact of their investments, rather than the relative performance per se.

My perception is that increasingly investors really care and want to have an impact through their investments. And even those who may initially have adopted ESG investing for reputational reasons, are increasingly finding themselves swept up in the trend.

Carmine De Franco: A small group of investors trying to create change alone will face an uphill struggle, but as more and more investors adopt ESG investing, the higher the likelihood of creating real and lasting change.

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