Instis Foresee Increase in Asset Allocation Changes

Stockholm (HedgeNordic) – A new survey from Fidelity Global Institutional Investor has found that institutional investors will be making more asset allocation changes over the coming two years than in 2012 and 2014. The survey, which culled respondents from 933 institutions across 25 countries with USD 21 trillion in investable assets, examines the foremost preoccupations of institutional investors on a yearly basis.

According to the global survey, 72% of institutional investors expect to increase their allocation of illiquid alternatives across 2017-2018, with 64% expecting to raise allocation of domestic fixed income, and a further 55% and 42% expected to do the same for cash and liquid alternatives respectively. Institutional investors in some regions are holding out, however, such as in the U.S., where, for example, the number of respondents expected to increase allocations to domestic equities has risen only from 8 to 11%.

> "With 2017 just around the corner, the asset allocation outlook for global institutional investors appears to be driven largely by the local economic realities and political uncertainties in which they're operating," says Scott E Couto, president of Fidelity Institutional Asset Management. "The U.S. is likely to see its first rate hike in 12 months, which helps to explain why many in the country are hitting the pause button when it comes to changing their asset allocation."

However, "institutions are increasingly managing their portfolios in a more dynamic manner, which means they are making more investment decisions today than they have in the past. In addition, the expectations of lower return and higher market volatility are driving more institutions into less commonly used assets, such as illiquid investments," Mr Cuoto continues. "For these reasons, organizations may find value in re-examining their investment decision-making process as there may be opportunities to bring more structure and accommodate the increased number of decisions, freeing up time for other areas of portfolio management and governance."

The survey also found that the top concerns for institutional investors are: a low-return environment, market volatility, and capital markets. Investment concerns also vary according to the type of institution. For example, sovereign wealth funds, public sector pensions, insurance companies and foundations/endowments worry most about market volatility. By contrast, private sector pensions worry most about the low-return environment.

> "As the geopolitical and market environments evolve, institutional investors are increasingly expressing concern about how market returns and volatility will impact their portfolios," says Derek Young, vice chairman of Fidelity Institutional Asset Management and president of Fidelity Global Asset Allocation. "Expectations that strengthening economies would build enough momentum to support higher interest rates and diminished volatility have not borne out, particularly in emerging Asia and Europe."

96% of the institutional investors surveyed, however, still believe that the can generate alpha over their benchmarks to meet growth objectives, with a majority (56%) saying growth remains their primary investment objective. They remain confident of generating on average 2% alpha per year with targets of approximately 6% required return, with roughly half the excess return over the next three years coming from short-term decisions like tactical asset allocation and individual manager outperformance.

“Despite uncertainty in a number of markets around the world, institutional investors remain confident in their ability to generate investment returns, with a majority believing they enjoy a competitive advantage because of confidence in their staff or access to better managers,” Mr. Young says. “More importantly, these institutional investors understand that taking on more risk, including moving away from public markets, is just one of many ways that can help them achieve their return objectives. In taking this approach, we expect many institutions will benefit in evaluating not only what investments are made, but also how the investment decisions are implemented.”

46% of institutional investors in Europe and Asia have changed their investment approach in the last three years, by comparison to 11% in the Americas. Across institutional investors surveyed globally, the most common change was to add more inputs – both quantitative and qualitative – to the decision-making process.

Mr. Cuoto explains that institutional investors are reporting conflict in behavioral approaches due to the overwhelming amount of information available, which can have a considerable impact on how decisions regarding asset allocations are reached: “Institutional investors often assess quantitative factors such as performance when making investment recommendations, while also managing external dynamics such as the board, peers and industry news as their institutions move toward their decisions. Whether it’s qualitative or quantitative factors, institutional investors today face an information overload,” he says. “To keep up with the overwhelming amount of data, institutional investors should consider revisiting and evolving their investment process.”

> “A more disciplined investment process may help them achieve more efficient, effective and repeatable portfolio outcomes, particularly in a low-return environment characterized by more expected asset allocation changes and a greater global interest in alternative asset classes.”

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