PFA’s Multi-Factor Hedge Fund Strategy

Stockholm (HedgeNordic) – Investors are increasingly focusing on diversifying risk and return sources, stimulating the emergence and growth of factor-based investing. The asset management arm of Danish commercial pension fund PFA launched a multi-factor multi-asset hedge fund in the early part of this year to meet some of the increased demand for risk premia investing.

With €571 million in assets under management, the new hedge fund called Yggdrasil Multi-Asset Fund already manages more capital than PFA Asset Management’s second hedge fund Midgard Fixed Income Fund – a fixed-income vehicle that returned an average 13.3 percent per year since launching in September of 2009.

In an interview with HedgeNordic, Jesper Slemming *(pictured)*, chief investment officer of both Yggdrasil Multi-Asset Fund and Midgard Fixed Income Fund, explains how the new hedge fund invests, talks about the benefits of risk premia as additional sources of returns, and shares his thoughts on the future of risk premia-based investing.

Multi-Skilled Team Running Multi-Factor, Multi-Asset Strategy

Yggdrasil Multi-Asset Fund is a Luxembourg-domiciled multi-asset fund seeking opportunistic risk premia in liquid products and mature financial markets. The fund is currently harvesting six uncorrelated factor premia – volatility, tail risk, carry, curve, spread, and model trading – across a wide range of asset classes. Yet, “we continue to scan for additional factors to contribute to the return,” says Jesper Slemming.

More interestingly, however, different portfolio managers part of PFA Asset Management’s investment team are responsible for running individual single-risk-premia strategies. With each portfolio manager allocated a risk mandate, building a core portfolio of mandates constitutes an essential part of the fund’s strategy to achieve returns that are uncorrelated with a standard portfolio of assets. “The strategy is built to ensure that no single factor is dominant in risk consumption or return contribution to ensure a high aggregated portfolio return on low volatility,” explains Jesper Slemming.

“Both risk allocation and monitoring are done from the top-down, whereas the strategy implementation is done bottom-up at the level of the individual portfolio managers,” says Jesper Slemming about the key characteristics of the strategy. “PFA Asset Management’s philosophy is based on individual portfolio managers having decision-making capabilities, leading to minimum consensus and crowd behaviour for the overall positioning,” further adds Jesper Slemming. “This ensures a low internal correlation.” The team running the fund aims to ensure investment competencies are in-house, which means the fund does not invest in asset classes in which PFA Asset Management’s investment team has no outright expertise.

Whereas risk premia or factor premia are sources of systematic returns, “the fund is by no means restricted to fully systematic strategies,” explains the chief investment officer. “The individual portfolio managers implement chosen strategies as they deem optimal,” he adds. The capital deployed, however, “is monitored dynamically via risk budgeting to allow for the optimal expression of systematic as well as thematic views.”

Benefits of Risk Premia-Based Investing

Investment products capturing alternative drivers of returns are receiving increased interest from investors. Jesper Slemming corroborates this opinion. “The risk premia-based approach is definitely growing in importance and offers an added layer of sophisticated return contribution to a traditional portfolio of well-diversified assets, as well as offers a low-risk stand-alone investment,” says Jesper Slemming. In his view, “the ability to keep a dynamic and agile approach towards return contribution and risk management is of the utmost importance for all hedge funds and asset managers.”

Speaking of the benefits offered by Yggdrasil Multi-Asset Fund, in particular, Jesper Slemming says that “the fund is to be viewed as an addition and a top layer to a well-diversified multi-asset portfolio, where the return contribution is made in a relative value framework with low exposure to outright financial market movements. The strategies implemented have the advantage of adding risk premia return with a low correlation to equities, yields, and commodities.” “Low correlation and continuous active contribution from different factors are key to the strategy” employed by Yggdrasil Multi-Asset Fund. The fund seeks to extract return in any market environment, while simultaneously focusing on maintaining low aggregated risk levels using a “solid and well-tested risk monitoring framework.”

Yggdrasil Multi-Asset Fund returned 3.7 percent since launching in April of this year. The fund’s underlying strategies, however, had tested the waters before the launch. The strategies currently employed by the fund have been implemented at PFA since 2012 and generated a cumulative return of 51 percent, corresponding to an average annual return of more than eight percent.