

DNB's Market-Neutral Upgrade

Stockholm (HedgeNordic) – “The ‘problem’ with all long-only equity portfolios is that no matter how good your portfolio manager is or what strategy you choose, the portfolio will suffer from the equity market cycles,” Ole Jakob Wold (*pictured*), Head of the Systematic Active Equity team at DNB Asset Management, writes in a blog post announcing the launch of a quant-based equity market-neutral strategy. “A low-risk portfolio will fall less in a bear market, but it will fall.”

DNB's Systematic Equity team led by Wold recently went live with a European equity market-neutral strategy, which is now one of the ingredients in multi-strategy, multi-asset absolute return fund **DNB Fund Multi Asset**. “On the last day of the month, we introduced a European quant-based market-neutral strategy in the fund,” writes the team running DNB Fund Multi Asset in a monthly update to investors. A team of three, consisting of Lena Öberg, Kim Stefan Anderson and Anette Hjertø, are responsible for portfolio construction at DNB Fund Multi Asset, which allocates across a number of strategies managed by different teams at DNB Asset Management.

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“This portfolio aims to generate strong, stable absolute returns with as low correlation as possible to equity markets,” Wold writes about the quant-based market-neutral strategy. “It's a portfolio that delivers outperformance that is not ‘contaminated’ with the market return.”

Risk Control - Paramount in Market-Neutral Strategies

“I am a quantitative portfolio manager, but contrary to what many would expect, I don't think quantitative managers are better at generating alpha than traditional managers, in general,” writes Wold, who joined DNB Asset Management in 2017 as a Portfolio Manager and Head of the asset manager's Systematic Active Equity team. “I do think quants are better at risk management. And risk management is a real challenge in constructing a market-neutral equity portfolio,” he emphasizes. Wold reckons that one can become a successful money manager without sophisticated risk control, but does not think “it is possible to make a true market-neutral equity portfolio without serious efforts to control risk.”

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The alpha and risk management models used to run the freshly-launched market-neutral strategy have been developed and tweaked over the course of more than 25 years. The strategy relies on around 60 company characteristics to identify the investor preferences that explain performance differences across periods. “We do this on monthly numbers to forecast what the preferences will be next month,” explains Wold. The market-neutral strategy goes long favourably-positioned companies and goes short companies that do not fit expected market preferences.

“To put it simply, we have an expected return for every listed company in the eligible investment universe,” which covers more than 40,000 companies. “That means that we have an updated expected return for all companies in the selection universe every month,” points out Wold. “That is a huge advantage when it comes to market-neutral portfolios.”

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DNB's Systematic Equity team has also developed and refined a risk management model to manage the now-running equity market-neutral strategy. "We do balance our portfolios money-wise. We control for beta (sensitivity to stock market) and differences in volatility-exposure," highlights Wold. "Markets tend to peak when volatility is low, and vice versa. So if your long- and short- portfolios have different volatility exposure, that would probably lead to correlation issues as well," he elaborates. "We also control for factor-exposures, company characteristics, that we have found can cause problems similar to beta- and volatility."

Picture by Stig B. Fiksdal. Picture courtesy of DNB.