Citywire Selector
01-LUG-2019
da pag. 14
foglio 1 / 4
www.datastampa.it
Tiratura: 0 - Diffusione: 0 - Lettori: 0: da enti certificatori o autocertificati
Superficie: 337 %

COVER STORY

A new frontier in alternatives

Fideuram CIO **Renato Zaffuto** has spearheaded ground-breaking forays into the real assets market and brought his clients along for the ride. He talks to Chris Sloley about his next pioneering moves

Renato Zaffuto knows all about change. During his 26 years in the markets he has worked in Milan, Amsterdam, London and Dublin, to name but a few, absorbing and responding to the various market cultures en route.

It was with one eye on further changes ahead that Zaffuto, in his capacity as CIO at Fideuram Investimenti, helped conceive the idea of Fideuram Alternative Investment's 'Mercati Privati Globali' project.

With this development, the giant Italian group took its first steps into the increasingly attractive realm of private markets. Zaffuto, who has influence over €85 billion in assets and responsibility for 35 people, says: 'When it came to developing the team covering private markets, we first looked at what we could add to our fund of funds by investing in different strategies across private debt, equity, real estate and infrastructure.

'At its heart, this is a strategic shift in asset allocation for our clients but it's designed with the express aim of preparing them for the new environment and increasing their exposure to these types of alternative strategies in our search for new sources of return and global diversification,' he says.

This builds on work they had previously done in partnership with private equity giant The Partners Group and US firm Neuberger Berman. It also means investors can tailor their weightings across these four areas as they see fit.

Speaking at the time of the November 2018 launch, Davide Elli, CIO for multi-manager and alternative investments, who reports to Zaffuto, said: 'There is a demand for new sources of returns, and this needs to be coupled with a longer-term focus. If you have a product with a 10-year view, then you need to ensure clients are aware and aligned with that.'


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Zaffuto echoes those points. 'It was about moving forward,' he says. 'Clearly this market is at a point where bond yields are at a historical low and there are rich valuations in equities. We need the tools to adjust and change our exposure to bonds. We have some in equities but we will be looking to increase exposure to alternative areas.'

CONVINCING THE CLIENTS

There may be appetite and capacity for a company to enter these new areas, but ensuring clients are adequately prepared for a world where capital is drawn down over much longer periods can be challenging. Zaffuto realises this is an important issue to address.

'We've been explaining the concept of diversification for many years and why, after 10 years of unconventional central bank action through QE and the compression of term and credit risk premia, and the changing shape of fixed income, we now need to move more types of strategies towards alternatives.'

This links back to a familiar stumbling block, Zaffuto says, which is liquidity. However, with market dynamics as they are, he says the case for adopting more illiquid thinking has strengthened. 'I think Illiquidity is a price worth paying in the case of private markets or new-style risk premia, which can invest in unlisted areas, for example.

'We have taken the time to educate our financial adviser networks on the need to increase exposure to these alternatives, steering away, in some places, from traditional balanced portfolios.

'We explained why the so-called "efficient frontier" has broken down decade after decade, both in terms of tail risk and volatility. This is why investors have experienced a drop-off in expected returns, even after the cost of portfolio management is taken into account. We needed to improve the diversification and this is one way to go about it,' he says.

RECALIBRATING ALLOCATION

At an asset allocation level, Zaffuto realises he cannot operate completely independent of the 'traditional' world. His biggest calls over Q1 2019 included increasing exposure to global emerging market equities and adding to German bets at the expense of the US.

Global emerging market equities remain his keenest area of interest and his portfolios are overweight here, while being underweight stocks with sensitivity to the global rates environment. He has also gradually reduced his major contrarian call, which was a significant allocation to tech.

Reverting to more offbeat thinking, Zaffuto has gradually shifted the company into alternative territory. The average fund now has 20% exposure to alternatives, which is largely focused on the Alternative Ucits market. Zaffuto speculates that the average balanced fund could be roughly one-quarter in alternative assets in the not-too-distant future.

He has worked with the company's fund selection team to ensure it takes on board his thinking and forecasts. 'Looking to the future, fund selectors are likely to place increasing emphasis on alpha-generation skills in the active space along with ensuring investors get value for money.

'In the assessment process it'll be more important to separate performance generation into beta and real alpha, so in the breakdown of fees we'll be able to pay a low charge for beta-like components of funds aligned with passive vehicles or ETFs, and a reasonable fee for the real alpha components.

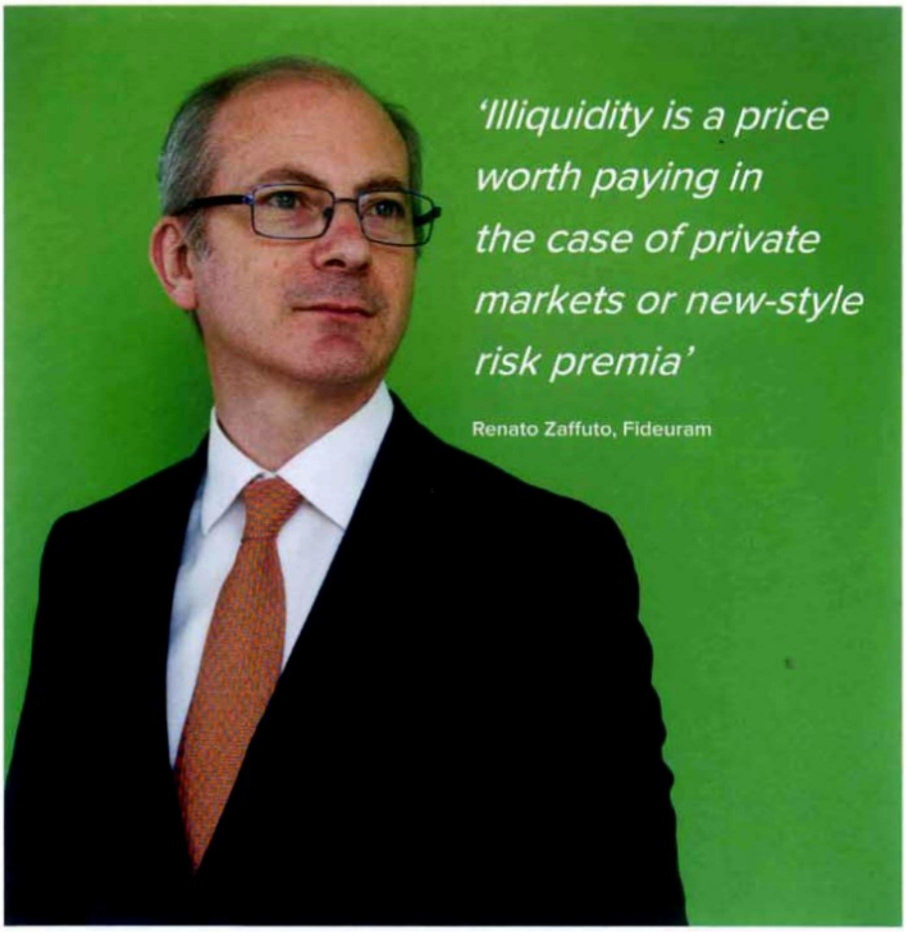
'On top of that we think that unconstrained, non-benchmark-driven and ESG-oriented investments will be favoured in the active fund selection process,' he says.

THE FUTURE IS DIGITAL

When discussing fund picks, Zaffuto name-checks the **Edmond de Rothschild Big Data** fund, overseen by **Jacques-Aurélien Marcireau**. Zaffuto says this is one of the few funds available with a 'pure play' approach to the Big Data market, which he expects to become increasingly important.

'We are now in the early stages of a radical transformation of the global economy. Following on from the industrial revolution, this is the digital revolution. It will change institutions, behaviours, lifestyles, attitudes and consumption models, across industries and geographies.

'Furthermore, over the next five years we'll see a process of monetary policy normalisation, as well as an adjustment or a second phase of globalisation. A huge pool of new consumers from emerging countries, such as China, India, Indonesia



> *'The so-called "efficient frontier" has broken down decade after decade, both in terms of tail risk and volatility. This is why investors have experienced a drop-off in expected returns'*
>
> Renato Zaffuto, Fideuram

and Brazil will get into marketplace. It'll have a huge impact.'

With that in mind, Zaffuto says Fideuram is watching three important trends. These include digital changes in aiding a sustainable environment, which will affect energy, commodities and materials. He is also looking at digital impacts from automation and disruptive tech in manufacturing cycles. Another focus is global standardised consumer needs and preferences driven by new generations of investors.

INNOVATION IN ACTION

Along with the selection unit, Zaffuto says a CIO's role has to evolve with the times. This goes beyond Mercati Privati Globali and into other areas as well. Over the past few years, he has modernised the company's traditional balanced fund with less emphasis on traditional bonds along with a move into new territory. One of these key areas, he says, is alternative risk premia.

'In the alternative investing space we created a new suite of Ucits funds investing in alternative risk premia two years ago. We set up a fund management team based in London to create a new platform to select all of the risk premia-based strategies out there. We have funds investing in carry, value, momentum and quality across asset classes such as rates, credit, equity, commodities and currencies. Our approach was to set up an open platform analysing and selecting all rules-based systematic strategies provided through indices by main investment banks.

'We are very committed to this space,' he says. 'We are experiencing genuine interest from some institutional investors such as sovereign wealth funds in Asia, as they want to increase exposure or change exposure to commodities. This is another step, as we are moving away from traditional long-only to alternative risk-premia-based exposure to commodities, for instance.'

Zaffuto is convinced that the market can only respond to differing client demands if the industry acts together. He points to a conference he is attending in September – featuring the likes of MSCI and Goldman Sachs – which aims to improve institutional understanding of private markets.

But, he is not stopping there. When we speak, Zaffuto is busy preparing for a conference the following week where Fideuram will launch a series of new funds based on factor-investment-led ETFs. This is the result of an ongoing collaboration with BlackRock, which is keen to make its mark on alternatives.

'We see this as a new frontier in asset allocation when it comes to factor investing. We want to improve the drivers and the forms of return, as well as the sources of diversification we can offer private clients, but that requires a more granular approach.'

POWER TO THE PEOPLE

The growth of the 'convenience economy' means people want to be able to get what they want as soon as they want it. Fideuram sought to get ahead of this trend with another project part-developed by Zaffuto within its discretionary portfolio manager service.

The project, called Fogli, allowed investors to choose from 45 different areas which are split into four sections – single securities, bonds and equities, mixed assets and a host of thematic portfolios. 'Fogli is a new discretionary portfolio management service. We have had inflows of €2.2 billion since we launched it last year, so it is a big success in Italy,' Zaffuto says.

'We designed this product for a traditional face-to-face approach between financial adviser and client, as well as for a new digital experience. It is a valuable and innovative tool for advisory under MiFID II.

'In terms of the future application, if we think about it as a digital platform, our financial advisers can combine and mix different asset classes and strategies to construct personalised portfolios matching client risk profiles. It is like creating your favourite playlist by downloading tracks from Spotify. In a similar way, the financial adviser can support their client by selecting the Fogli as different building blocks to build a personalised portfolio.'

While many companies are getting their heads around real assets, Zaffuto is pushing on into the digital world.

'This new investment service consists of more than 40 single Fogli or portfolio building blocks divided into four sections as single asset classes in bonds and equities, multi asset, style and thematic-based investment strategies. If we can combine an improved digital experience with access to different yet integrated investment themes, then that is a strong value proposition.

'This could include third-party mutual funds, ETFs and securities, as we can feasibly construct different portfolios based on these varied investment opportunities. In terms of fixed income today, it makes sense to have more exposure to ETFs, and equities have different areas of development. This is how we see data and digitalisation changing the industry as we move forward.'