Adapting to a changing asset management landscape

Passives may be gaining ground for now, but in the long term, active strategies should outperform, says Aberdeen Asset Management's Hugh Young, a veteran Singapore-based investor.

Annual inflows into passive funds might have surpassed flows into active ones – yet active management will remain key to generating long-term gains for investors.

That's the view of Hugh Young, veteran investor and managing director of Aberdeen Asset Management Asia.

According to Morningstar, active funds saw outflows of USD285 billion in 2016, while passive funds attracted inflows of USD429 billion. While more assets continue to be held in active strategies, the shift towards passive has been very noticeable in recent years.

One reason for the popularity of passives is that they are much cheaper than their active counterparts and have shown better performance.

However, the better performance is just a phase, according to Young. "When you manage equities actively, there will be some years of underperforming the benchmark. But over time, actively managed equities will outperform, especially as interest rates normalise."

In addition, disappointed by active returns, many investors have also been piling into exotic instruments that are less liquid and riskier as they hunt for higher yield. "Investors need to be cautious about backing such exotic instruments too heavily because while they may offer a one-off bounce in returns, they do not represent a long-term sustainable investment solution," notes Hugh.

CHANGING LANDSCAPE

Nevertheless, the current poor performance of actively-managed funds has put pressure on fees – one of the key reasons for the consolidation seen in the asset management industry.

HUGH YOUNG
Aberdeen Asset Management Asia

Indeed, in early March 2017, Aberdeen Asset Management and Standard Life Investments (SLI) disclosed that they were in late-stage discussions for an all-stock merger of the two Scottish fund houses. Under the terms of the deal, when completed, SLI is expected to own 66.7% of the combined entity, while Aberdeen will own the rest. The combined group will have more than USD800 billion in AUM.

The merger comes during a challenging time for Aberdeen globally, which has a high exposure to emerging markets and has suffered heavy outflows from its emerging market funds in the past two years.

On the plus side, the combined entity will benefit from Aberdeen's strong and well-respected presence in Asia. Young is optimistic that this will enhance the value of the SLI deal.

STRONG REGIONAL FOOTPRINT

Based in Singapore since 1992, Aberdeen Asset Management Asia is the main regional investment arm of the global fund house. In addition to Singapore, the group has offices in Hong Kong, Thailand, Malaysia, Australia, Japan, Taiwan, Indonesia, China and Korea.

Local markets have been an increasing focus for the firm. In 2016, for example, the Indonesian subsidiary launched its first-ever Islamic investments products. The goal, according to Aberdeen, is to be one of the top 10 fund managers by assets in the country by 2021.

Not many managers have set up shop in Indonesia. However, the decision to operate a local business was fairly straightforward for the group.

"On the equities side, there are potentially some great companies in Indonesia, and on the debt side, the market offers decent yields," says Young.

"We had already invested millions of dollars in investments in the country's financial markets, setting up a business was a natural progression. We believe there is immense growth potential but it won't happen overnight. It will take at least 5 to 10 years."

While Indonesia is a very young market and fund penetration remains very low, the Singapore-based investor believes that as the economy matures, fund adoption will increase.

"As wages rise and the country develops, we will definitely see improvement," he adds.

China is another long-term play for Aberdeen. Two years ago, it was among the first fund house to be granted a wholly foreign owned enterprise (WFOE) business license.

The group is spending a lot of time building its relationships in China, according to Young.

"China's asset management industry is very young and the potential is huge, but it's important to avoid short termism and focus on quality," he says

THE COMING OF BIONIC ADVICE

Aberdeen was also one of the first firms of its type to understand the impact of digital technology on the distribution landscape; it acquired Parmenion Capital Partners, one of the largest robo-advisory firms in the UK, in 2015.

According to recent media reports, the firm is keen to expand into Asia. Young believes that the merger with SLI could potentially accelerate those plans.

Aberdeen group CEO Martin Gilbert certainly has a clear view on the role of robo-advisory. In a blog post late last year, he noted: "Online platforms can take some of the manual labour out of the exercise of giving financial advice. But there are a great many people who want the comfort of having a well-qualified professional to guide where they can put their money. Technology presents a huge opportunity in this situation. It can give advisers more effective tools to give more efficient and better reasoned advice."

He added that the future of advice is one where the decisions of humans are augmented by technology, not replaced.

"In this sense, advice will be bionic, not exclusively robo." ■

Hunt for yield continues

In terms of investment appetite, there continues to be high demand for multi-asset products. The quest for better yield is never-ending.

"Investors are looking for LIBOR+4% targeted returns achieved through diversified portfolios," says Young.

One strategy which he says the group is keen to bring to Asia is based on property. "We are keen to make a push on Asian property as there are lots of opportunities around the region, especially in Japan and Australia."

He expects the fund to do well here, given the preference among local investors for property. Another fund that has also done well in the region is the USD108 million Aberdeen Global - Indian Bond Fund, launched in the last quarter of 2015.