The World According to MSCI – Emerging Trends in Portfolio Advisory

Andrew Tong, Executive Director & Head of Greater China Consulting at MSCI, gave the audience at the Hubbis Investment Solutions Forum valuable insights into portfolio advisory trends for investors taking exposure to the global financial markets.

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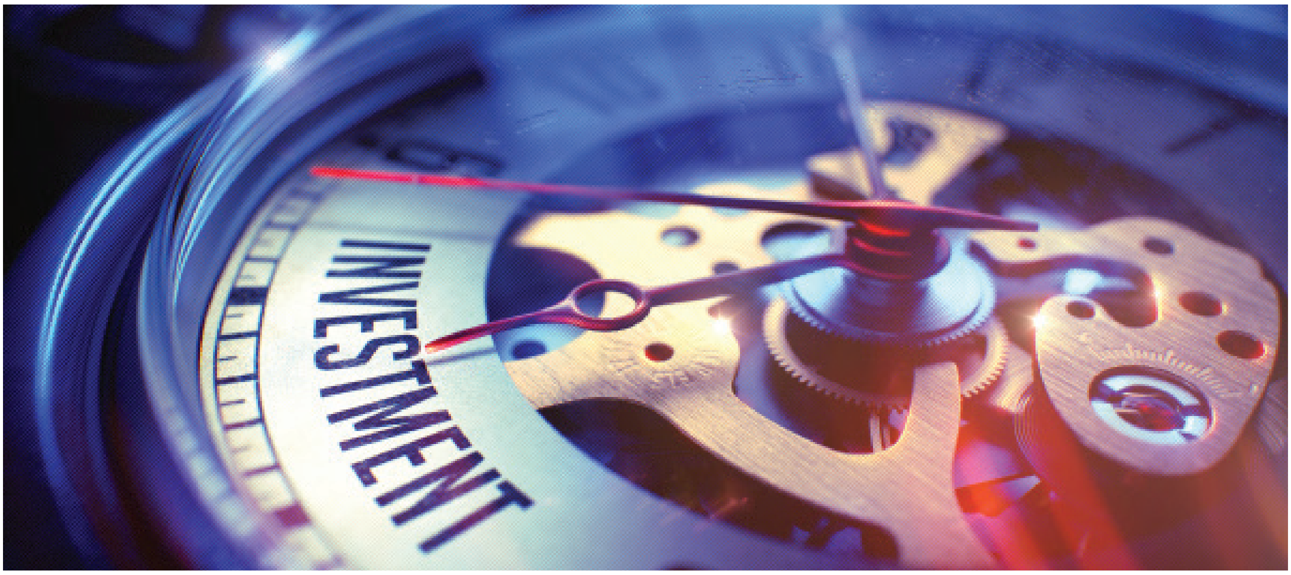
Executive summary

Many of Asia's high-net-worth individuals and their wealth management advisers will be very familiar with MSCI's index offerings. The firm has more than USD13 trillion of assets benchmarked and there are hundreds of thousands of indices that are generated daily and used by asset managers, asset owners, banks and of course the global wealth management industry.

In order to support the entire product creation and management cycle, MSCI has also developed a full range of portfolio analytics and ESG solutions as presented by Andrew Tong, Executive Director & Head of Greater China Consulting at MSCI, at the Hubbis Investment Solutions Forum.

He explained that MSCI also offers significant resources in analytics and ESG research to help clients in the areas of portfolio construction, risk management and ESG research with the overall goal of trying to help wealth advisory clients and their end high-net-worth (HNW) clients achieve better risk adjusted performance of their portfolios.

ANDREW TONG
MSCI



FOR MORE THAN 40 YEARS, MSCI's research-based indexes and analytics have helped the world's leading investors build and manage their portfolios. "Clients," Tong explained, "rely on our offerings for deeper insights into the drivers of performance and risk in their portfolios, broad asset class coverage and innovative research. Our line of products and services includes indexes, analytical models, data, real estate benchmarks and ESG research. We serve 99 of the top 100 largest global money managers."

Tong explained that MSCI focuses on four areas of research, namely index, analytics, Environment, Social & Governance (ESG) research and real estate. "There are four things we are doing to support the advisory process," he reported. "These are looking at fund and portfolio robustness through a factor lens, market scenarios, structured products analysis and then, finally, impact and sustainability assessments."

Addressing the first of these - fund and portfolio assessment - Tong said that what the industry has seen for some years is the idea of looking at funds and putting them through 'Style Box', which he said was made popular by Morningstar.

Updating the style

The traditional style box, which was introduced 26 years ago, was a simple way to frame portfolio decisions along two dimensions, namely market capitalisation and style, in terms of value versus growth. "The style box transformed how investors built and evaluated portfolios," Tong elucidated. "It has served investors well but can be too limiting. While that has been used for years, we are increasingly hearing interest in 'factors' related to 'smart beta' from more financial institutions and end clients." Accordingly, MSCI has worked on and launched what it has called the MSCI Factor Box, which leverages the innovative MSCI FaCS hierarchy.

"In essence," Tong clarified, "FaCS, which stands for MSCI Factor Classification Standard, enables the measurement of a fund's exposure to value, low size, momentum, quality, yield, and low volatility, which are common style factors investors want to assess. With this MSCI is providing to the market the ability to look at any particular fund through a different prism - it is effectively an innovation on the traditional style box that is relevant to contemporary trends and practical to use."

Testing for stress levels

Tong then moved on to look at stress testing and scenario analysis. This means reviewing the potential impact of a particular market shock on a client's portfolio, gaining insight into the portfolio's robustness, and assessing possible behaviour across multiple scenarios.

He highlighted one particular possible scenario, namely a potential US-China trade war. "How do you translate that high-level concern into some specific forecast and assess the potential market impact?" Tong asked. "That is where it is important to have access to macroeconomic models and risk models where you translate the high-level scenario into possible GDP and inflation shocks resulting from trade-related impacts. And how does that impact the markets? With analytics, one can model moderate to extreme scenarios across multiple asset classes."

Tong moved on to broader scenario analysis. "This is all about checking the robustness of your clients' portfolios," he explained. "You can assess multiple scenarios and their potential impacts to your client's portfolio and check how rate hikes, policy events which can shock growth and inflation expectations, and so forth translate into different manifestations in the market. This helps portfolio analysis and rebalancing decisions."

Tong then highlighted MSCI's analytics that provide insights into structured products. "In this segment, MSCI can help clients and advisers understand the implicit exposures through to the underlying reference securities, bringing clarity to the overall composition of their portfolios."

This is an area, Tong elucidated, where MSCI is seeing tremendous growth for clients and partners. "There is always the challenge of better understanding about the characteristics of the structure that we are looking at," he explained. "What we are most interested in is understanding the exposures that we would have to underlying securities for assets, over time, and how we should use those kinds of insights in helping us with making hedging and other decisions."

ESG – striking a chord with Asia's younger HNWIs

Tong closed his talk with reference to impact and sustainability, which he described as one of the 'hottest topics' in the market currently. "Institutions and individuals, especially millennials, are highly focused on ESG nowadays and this is a trend we see expanding as the trend moves to mass market. Again, MSCI provides research and analytical tools for assessing the ESG risks of funds and portfolios, as well as develops investable ESG indices."

"Instead of looking at single assets and their characteristics of E, S, or G we want to be able to look at the entire portfolio," he explained further. "We want to look at the characteristics of funds available to investors in terms of the ESG characteristics and of course we would still like to look at individual assets in terms for these behaviours. It is complicated enough to look at ESG issues separately, so what you want to be able to do is offer a full bottom-up and top-down approach to see total cover risk, reputational risk and so on."

Tong summarised his talk as follows. "I will leave you with four key thoughts on research ideas to support your advisory process. The first is the MSCI Factor Box for analysing funds and unit trusts. Second is scenario analysis to enrich your conversations with clients. The third is delving more deeply into structured products used within portfolios, including their underlying exposures. Finally, building and understanding portfolios in the context of impact and sustainability." ■