Investec Asset Management

Jason Borbora-Sheen – Generating defensive returns in uncertain markets

- This has been the largest and longest bull run. Should we conclude that it must finish? It is not our base case. But even if that's the case, investors still need a defensive product at certain points in time
- If we look at the flash crashes across various assets that have occurred since this expansion began, there has been a lot less intermediation by banks as their ability to take risk has been constrained. This has created a tendency to crowd in and crowd out of investments
- This means there are issues in markets and investors need some form of defence as a ballast in the portfolio, even if they believe the market expansion can continue
- During those moments of crisis, it can be quite difficult to trade. High yield bonds have been a liquid asset class, but today only 0.5% of the market trades on a daily basis
- We're late cycle. Investors are unlikely to be rewarded as well as they were early in the cycle
- What could be useful in that context? Income. When we look at asset class performance over the last 20 years, even in low yielding asset classes, the contribution from income to total returns is over 50%
- If the risk of recession is increasing, having a reliance on capital growth may not be the best idea
- Defensive return is not just about missing the downside. There has been a lot of focus on low correlation and low downside capture, with little focus on upside capture. We are using income for that
- Returns generated from income are more stable than those based on share price appreciation
- We have a relative volatility target. We are not in control of market volatility. The danger is that investors need to buy risky assets when volatility falls (when they're rallying) and vice versa. We can move with the environment
- We focus on individual security selection and hedge the portfolio to reduce downside risk
- Defensiveness in this environment could be about hedging both your bond exposure and equities exposure in order to reduce overall exposure to risk
- We catch about 40% of the upside of rising markets, but only around 16% of the downside