Getting the best return in the smoothest possible way

Q&A with Parit Jakhria, Director of Long Term Investment Strategy, M&G plc

What are your responsibilities? (0:00 - 0:42)

So I'm responsible for helping set the strategic asset allocation for all of Prudential UK funds under management. That would include about £110 billion of With-Profits funds, £30 billion of Unit-Linked funds and £40 billion of annuities; totalling £280 billion across the board. In addition to that, I provide capital markets and economics expertise to the group, which might be used in various business planning processes modelling financials etc.

What is your process and philosophy? (0:43 – 02:19)

In order to get them the outcome in the smallest possible way we have a number of stages to think about in our processes.

Stage one, we spend a lot of time thinking about the global economic cycle. We think about the different asset classes and geographies. And we spend kind of long and hard thinking about what all of these asset classes and geographies will get. Not only now but across different time periods the will utility of those asset classes as well as the interrelationships across different scenarios.

Secondly, we fundamentally believe that whilst there is only one past there's many potential futures and we spend a lot of time thinking about different possible futures. An example would be the different trade scenarios across the global trade. The different flavours of Brexit, Eurozone disintegration, the different ways of the technology can change the world and the way at which the world is moving from west to east in terms of economic strength, different monetary policy scenarios, how interest rates are evolving amongst others. And we want to get the portfolio robust not only in the scenario which is most expected by us, but also in pretty good shape across a whole range of other scenarios, which are unexpected. And that has been testimony to returns going back; that comes up with the strategic asset allocation in the end.

What examples of scenario analysis are driving asset allocations? (02:24 – 03:14)

In terms of examples of some of the scenario analysis driving our allocation. Back in 2012,a lot of our modelling showed that our portfolios had an extremely high dependency on the UK economy and we elected to sell out of a large slice of UK equities and reinvest in a diversified basket of global equities, focusing primarily on the Asian emerging market regions. That was a really good investment as it turned out. That was not because we were worried about Brexit or we particularly thought Brexit was going to happen. It's simply in a range of economic scenarios we looked at the cost benefit of having such a large portfolio concentrated in UK domiciled assets wasn't appealing and hence we took that decision.

Any recent examples? (03:15 – 04:38)

Some more recent examples would be over the last 12 months we've been thinking particularly hard in terms of the global economic cycle. Even where we are now, we are 12 years on from the global economic cycle. The first sign of turbulence we felt was in the first quarter of 2018. And looking at where the asset prices were re-elected in August 2018, to take a large amount of risk off the table, that turned out to be a great decision in hindsight. And in fact so much so that by the time the capital markets had reacted across October, November, December in the year we-elected in the first two weeks of January to put a fair amount of risk back on the table. That turned out to be a great decision as well as central banks did a U-turn and provided extremely easy monetary policy. However by the time of May, we felt that the world was one year on and it was much more difficult for us to see future risk adjusted returns. So we elected to take the risk off the table again and that's where we stand so de-risked our portfolios and we are waiting to see how the global economic cycle unfolds.

What worries you at the moment? (04:40 – 06:15)

In terms of worries, I think there's maybe three main areas we spend a lot of time thinking about.

Firstly we think about the global economic cycle where we are in the economic cycle and how much resilience different economies have to potential economic shocks.

Secondly, we worry about longer term trade and the evolution of global economies. It looks increasingly like whilst there might be stabilisation of globalisation on the surface, underneath the surface there is going to be increasing balkanization or regionalization of trade and that means diversification across geographies is becoming even more important and we stand very well placed.

Thirdly, we are in a world of lower and lower yield across all assets, and that that makes our asset allocation and achieving and an Expected Growth Rate a lot more challenging. We have spent a lot of time thinking about the fixed income in particular and we have diversified away from low yielding diversified market fixed income to a basket of global and emerging market fixed income. We've also gone into private credit, so some examples would be a private credit opportunities fund in 2016 a private high yield fund in 2017, going into African debt in 2018 and in 2019 we're seeking to complete our exposure to global emerging market debt and expand our private credit opportunities.

What does this mean for our customers? (06:17 – 07:26)

There's about 4.6 million customers in the wider With-Profits funds and we spend most of our time thinking about not only how to get them the best value, the best return for the money they've put into a fund, but also thinking about how to get them the return in the smoothest possible way.

In terms of what it means for the customers, as I said right at the start, we strive not only to get the highest possible return for a given level of customers risk appetite; we try and do it in the smoothest way possible and that is evidenced in our outcome. So, if you look over the last 20 years across our peer group, we get an extra 100 basis points per annum for each of the last 20 years for the same amount of money put, compared to our peer groups. Or to put a different way, if you're taking rolling five year returns and take the returns from the Second World War onwards, there is only one five year period in which we had given back negative returns to the customers.

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