



Perspectives on blending active and index products

## Quality portfolio construction – underpinned by a defensible philosophy

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The foundation of quality portfolio construction is

- a clearly articulated, **robust, contemporary and defensible portfolio construction philosophy**
- that has a consistent, efficiently and effectively implemented **policy and process, and**
- that is most likely to **meet investors' objectives.**

# Modern Portfolio Construction

## ■ New Face of Modern Portfolio Construction

**Portfolio  
Manager  
Styles**

**Asset Allocation Style**

**Active**

**Passive**

**Investment  
Selection  
Style**

**Active**

**Passive**

<b>Manager-Based Tactical Asset Allocation (active, active)</b>	<b>Manager-Based Strategic Asset Allocation (passive, active)</b>
<b>Index-Based Tactical Asset Allocation (active, passive)</b>	<b>Index-Based Strategic Asset Allocation (passive, passive)</b>

# Modern Portfolio Construction

## ■ New Face of Modern Portfolio Construction

Sources of Alpha

Asset Allocation Style

Active

Passive

Investment Selection Style

Active

“Double” alpha

Manager Search-&-Selection Alpha

Passive

Portfolio Management Alpha

There Is No Alpha!

All styles still participate in Beta

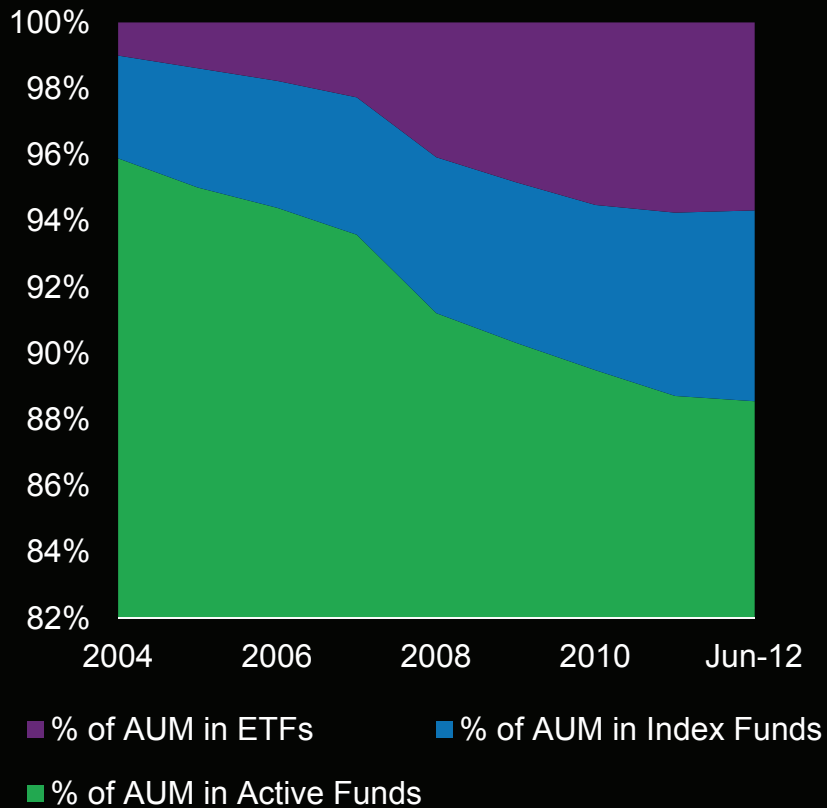


Perspectives on blending active and index products

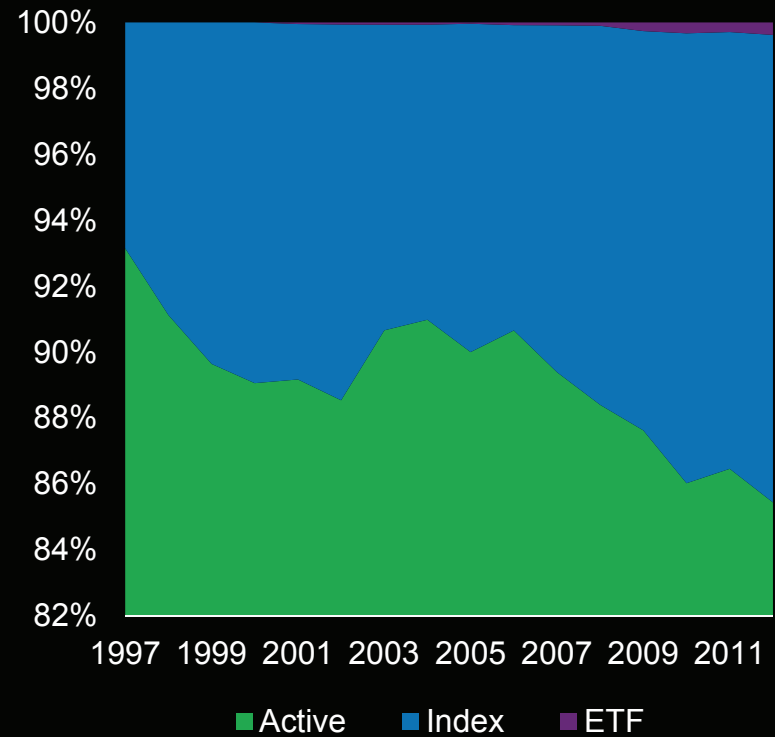
**Mark Oliver**  
Managing Director  
BlackRock

# Changing shape of usage of indexing

European AUM split by active and passive



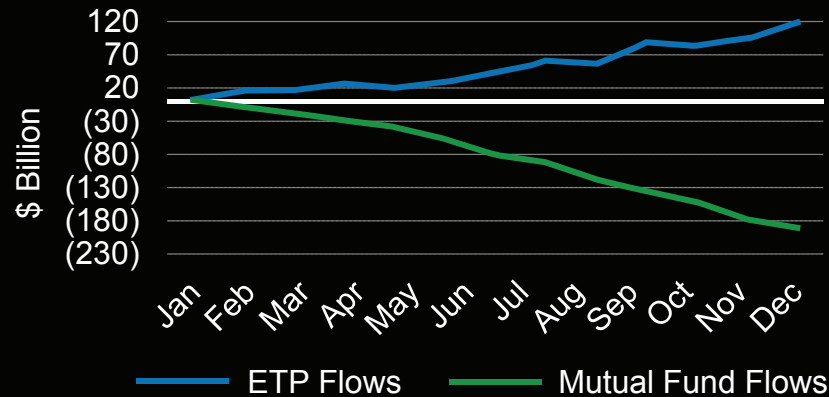
Australian AUM split by active and passive



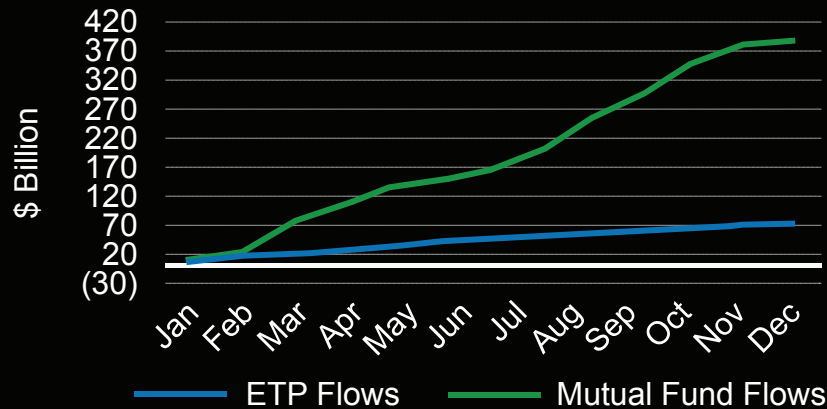
Source: BlackRock, Simfund, Rainmaker Please note, the European data is for European domiciled funds but excludes AUM in Cayman Islands, British Virgin Islands and Bermuda domiciled funds.

# Cumulative net flows in 2012: Global ETPs and Mutual Funds

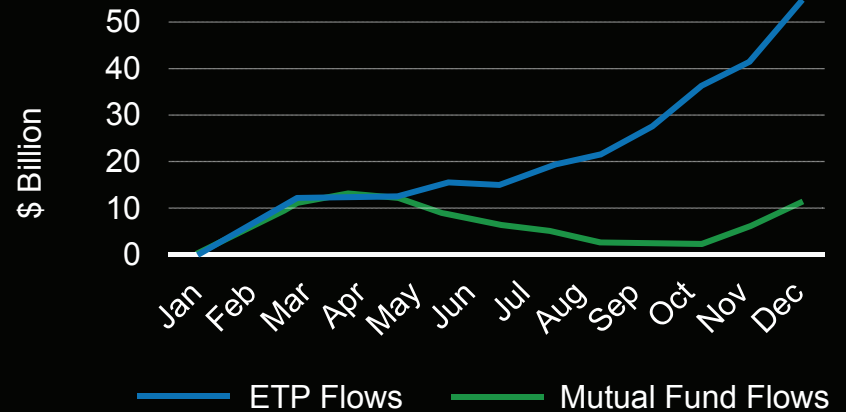
## Developed Markets Equity



## Fixed Income



## Emerging Markets Equity

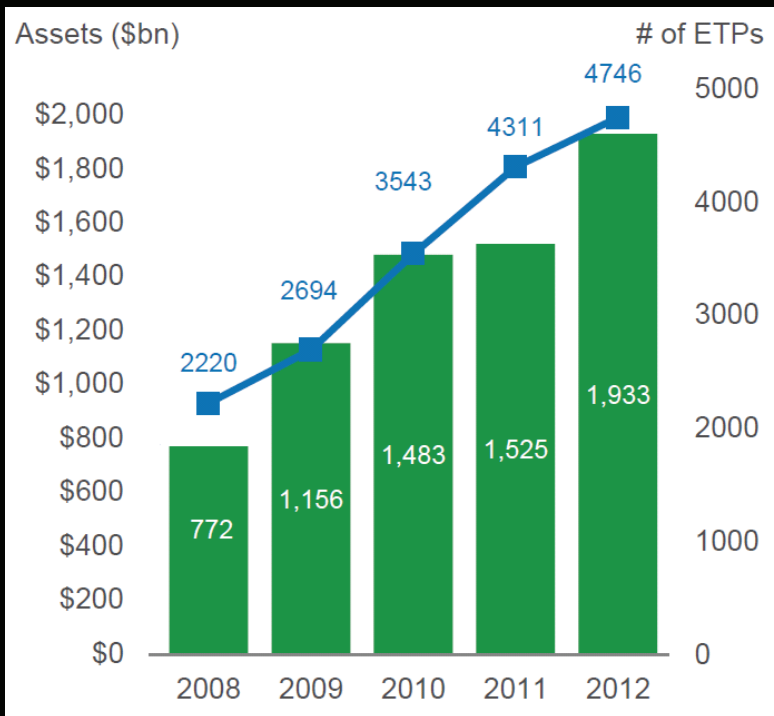


Source: BlackRock Investment Institute – ETF Research, Bloomberg. Data as at end of 2012.

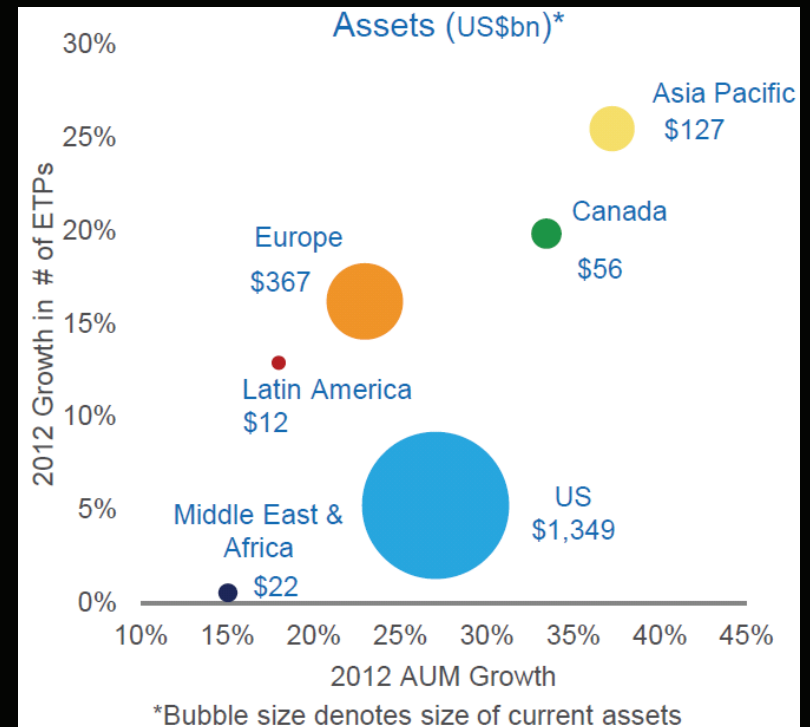
# Global growth of exchange traded funds

- ▶ Total assets have increased by 27% from 2011 to \$1.9 trillion in 2012, reaching \$2 trillion in early 2013
- ▶ 195 Providers worldwide – 84% of assets with top 10 providers, top 3 account for 9 of the top 10 ETPs by AUM
- ▶ Continued expansion of product choice and granularity

## Global ETP assets & number of ETPs



## Asset growth rates & new products



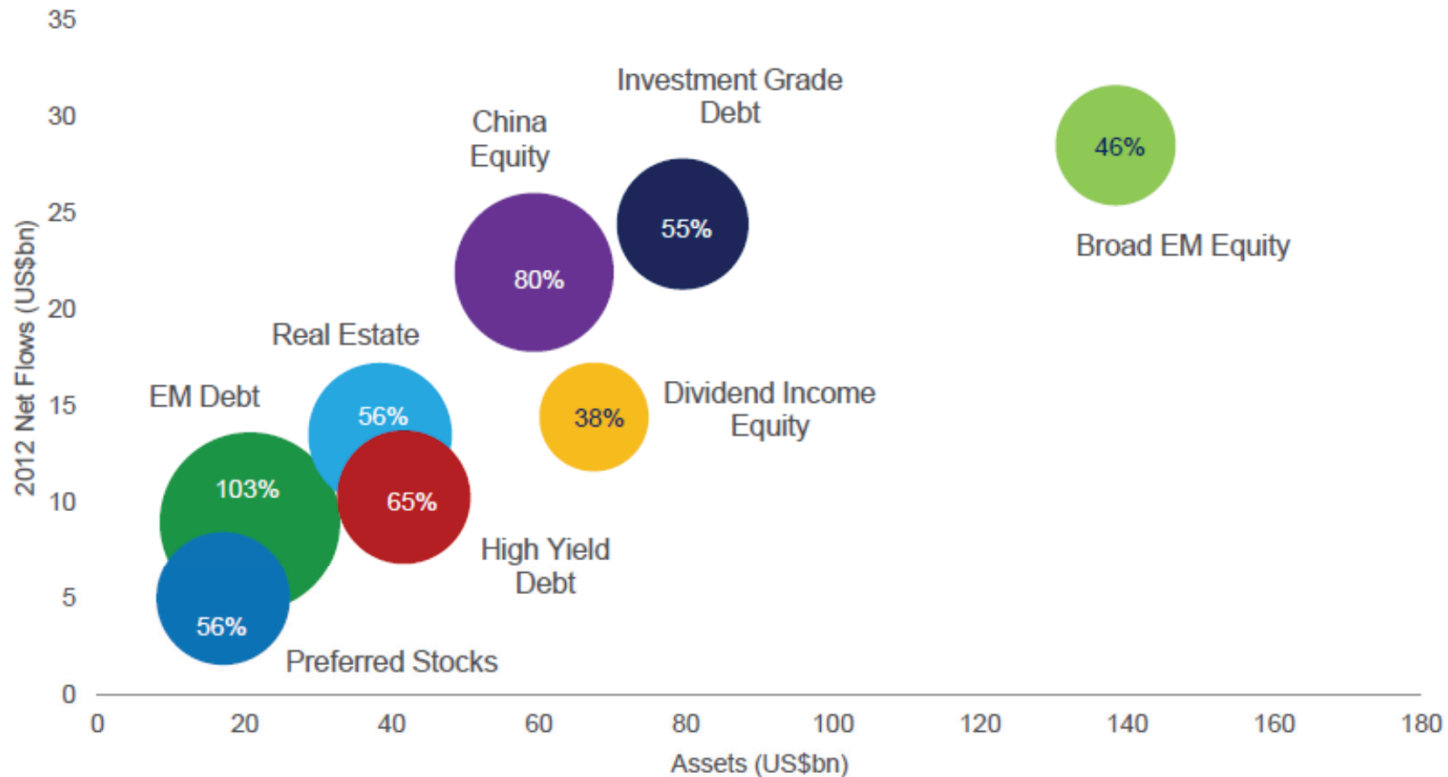
Source: BlackRock as of December 2012



# Rapid growth across a diverse range of exposures

## Exposures with High Asset Growth Rates in 2012<sup>1</sup>

For Exposure categories with Assets > \$15bn and growth rates >35%



Bubble size denotes growth rate in assets from year end 2011 to year end 2012

# Catalysts – what's driving this change?

Current  
investment  
markets

Client-driven

Growth in index  
product range

What is driving these **changes**  
in **investment approach?**

Costs

Regulation

Performance of  
Active Funds

Business  
opportunity

## Blending – Some insights

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# Our approach

## We interviewed:

- ▶ **35** Multi-asset, Advisory and Discretionary institutions across EMEA
- ▶ Investors with predominantly **active**, **blended** or **passive** portfolios
- ▶ Our respondents manage **~€2.5 Trillion\***
- ▶ **5** of the **top 10** Global Private Banks\*\*



\*Source: BlackRock, as of year end 2011

\*\*Source: Scorpio Partnership Private Banking Benchmark 2012

# Three identities emerge

## Actively Active

- ▶ Currently focused on using active management to generate alpha and not actively blending
- ▶ Indexing, where it is used, is only for cash management or as a last choice if other alternatives are unavailable

## Embracing Blending

- ▶ Adopting indexing for tactical or short-term exposures, or
- ▶ Moving towards a more comprehensive approach to blending

## Agnostic Allocators

- ▶ Agnostic process for blending and the use of indexing
- ▶ Primary focus on asset allocation to deliver alpha – implementation choice often a secondary consideration

Which identity  
would you most  
associate  
yourself and your  
firm with today?

A. Actively Active



B. Embracing Blending



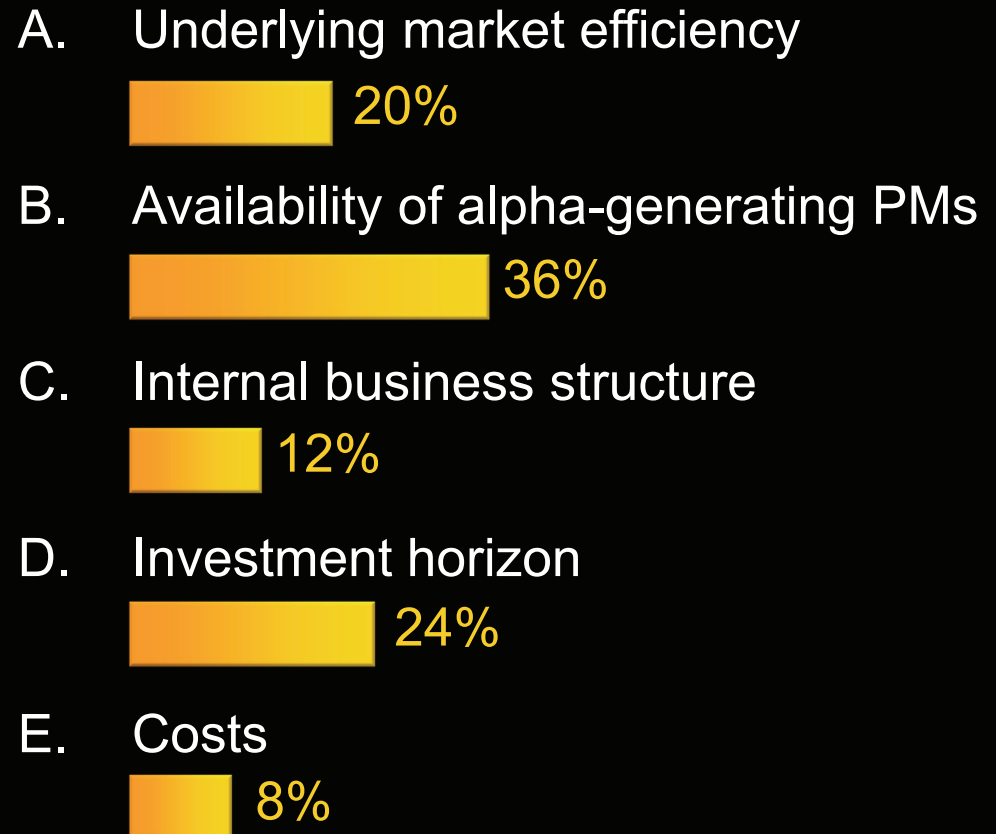
C. Agnostic Allocators



# Which catalyst has driven blending the most in your business / market?

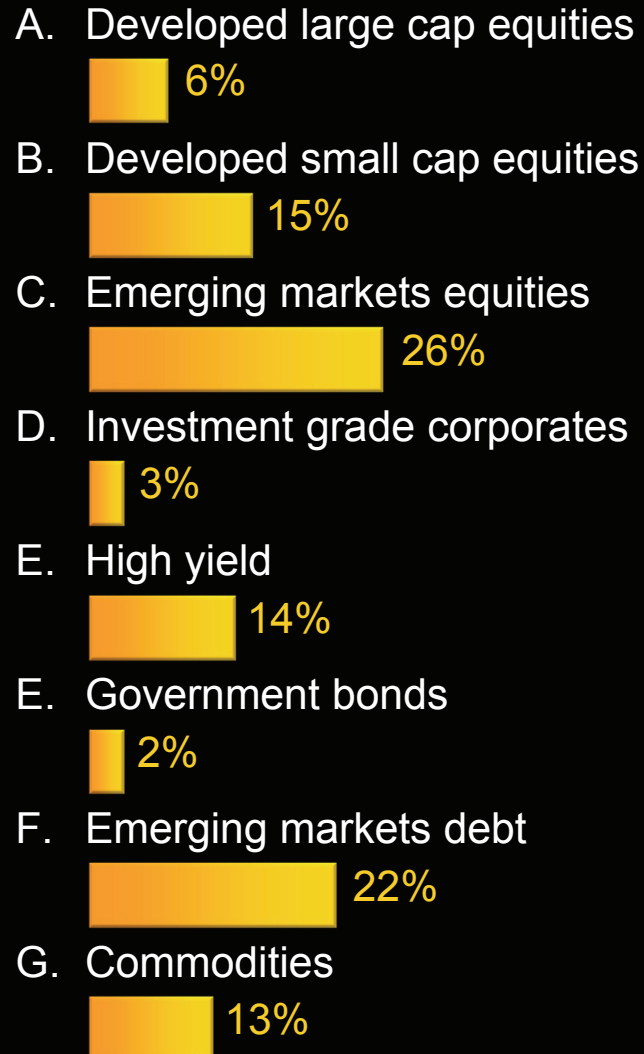


# What criterion would drive you to use indexing as opposed to active funds?





Which exposure would you see as being the most “inefficient” and therefore consider using active products for?



# There's no single answer

“ “

I think the fact that we've tried to go all the way down a very **technical** route and come all the way **back** down to what is more a **qualitative** approach has been a bit **surprising**.

” ”

# Investment philosophy and client base are key

It's not just a theoretical or academic discussion of what's best...

“ “

I've been a **fund selector** for so many years, and I have to **believe** that I can **add value** through selecting funds.

” ”

“ “

So, we really try to go from an **agnostic** standpoint, throw it all in the machine and purely from a quantitative perspective, as **emotion free** as physically possible, to say 'is it possible for a fund selector to **find value?**'

” ”

# Blending isn't easy

Selling a story

Communication

Availability and  
structure of  
indexing

Advisory  
Revenue Model

***Blending*** active and index  
strategies does not come without  
***challenges*** and ***obstacles***

Education

Changing a  
mind-set

Operational challenges  
of using ETFs

Having an in-house  
manager

Over the next  
2–3 years, do  
you expect  
greater use of  
blending in your  
business?

A. Yes



B. No



# The future



## Future of blending

We do think that in time, **blended** will be the range that we **sell the most** of. That combination of **value** for money, plus the active overlay, plus the active fund selection, that combination is the **sweet spot** of what everyone wants.



# Lifecycle Investing

Accumulation  
Decumulation