

Understanding Asset Allocation of Family Offices

Rakesh Udyawar
Head- Investment Advisory Group
Edelweiss Private Wealth

Why Asset Allocation is Important

- Reduces dependency on any single asset class
- Risk management through diversification
- Optimization of risk-adjusted returns
- Alignment with investment horizon
- Liquidity management
- Any additional requirements/ goals



Is there any all-encompassing solution??

Conventional Approach – Too Standardised

- Identification of 3 risk profiles
- Strategic allocations as per thumb rules
- Model portfolios for each of the risk profiles
- Risk profile questionnaire/ IPS
- Portfolio creation



Need of the hour



Building Blocks for Customised Approach

- **Financial Goals of YOUR Family Office**

- Managing expenses
- Incubating business ventures
- Philanthropic activities
- Esoteric possessions
- Capital preservation and growth for long term



- **Risk Identification and Mitigation**

- Psyche for risk appetite – stereotype vs unconventional
- Identify the extremes – asymmetrical payoffs
- Bird's eye view for potential risks



Financial Goals

Risk Mitigation

Managing Expenses

Non-Discretionary Expenses



Utilities



Insurance



Education

Discretionary Expenses



Exotic holidays



Luxury cars



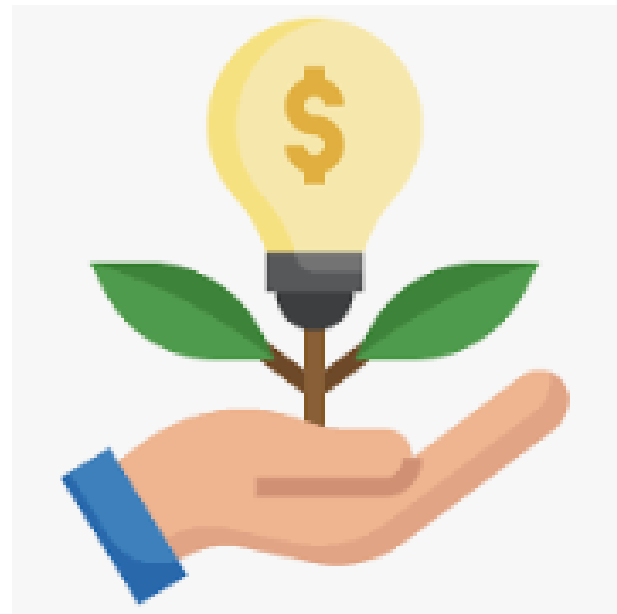
Lavish events

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Incubating Business Ventures

- Family owned = emotional attachment
- Identify source of funding and outer limit of investment
- Tentative cashflow calendar
- Business plans/ projections



Philanthropic Activities

- Own entity or third party?
- Nature of entity – public charitable trust/ private trust/ others
- Frequency and periodicity of donations
- Immediate requirements vis-à-vis future provisions
- Future vision



Esoteric Possessions



- Is it discretionary spending or balance sheet item?
- Periodical valuation is necessary
- Risk weighting and mitigation



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Financial Goals

Risk Mitigation

Fixed Income = Lower Risk (?)

IL&FS crisis: For NBFCs, India's 'Lehman moment' has meant reset of future

DHFL crisis puts over 100,000 fixed deposit holders at risk

Business Headlines : Is your Mutual Fund at a risk of defaulting due to the Zee Group crisis

RBI Takes Control Of Bad Loan-Burdened Yes Bank: Timeline

आज का ज्ञान

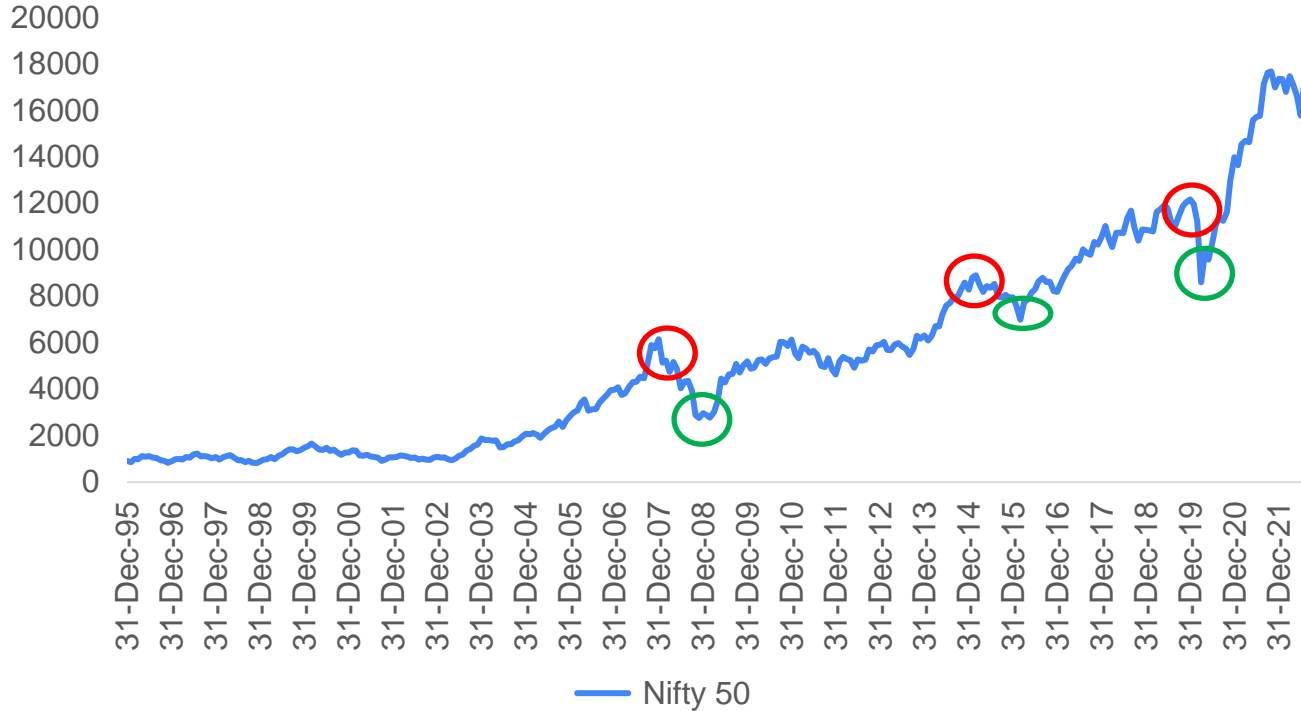
मतलब की दुनिया में कौन
किसी का होता है
धोखा वही देता है जिस पर
भरोसा होता है ।

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Opportunity in Crisis – Asymmetrical Payoffs

Mr. Market



आइसीसी के कार्यक्रम में पीएम कोरेना को आत्मनिर्भर भारत के लिए टर्निंग प्वाइंट बनाना है

आपदा को अवसर में बदलना है मोदी

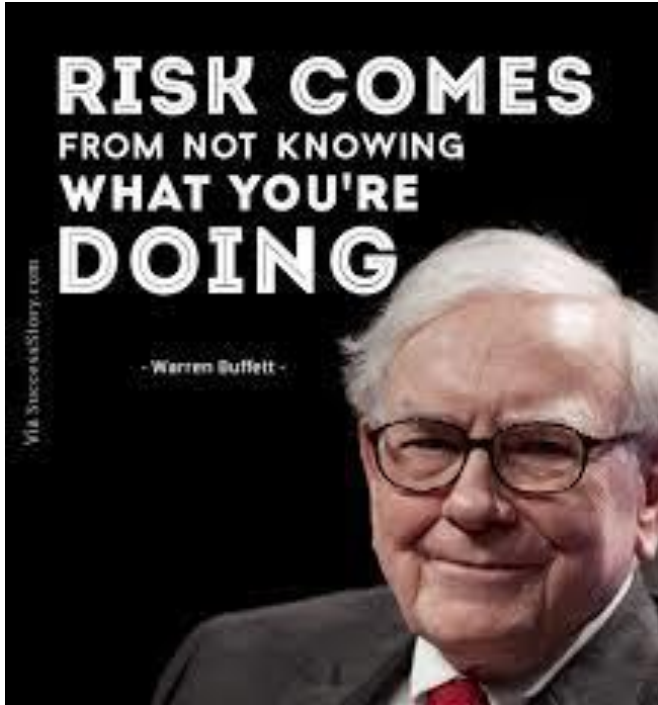
कोरेना संकट से निकलना है आत्मनिर्भर अभियान

विश्वो - 4 मार्च को देश को पीएम मोदी के नेतृत्व में आत्मनिर्भर भारत का आशीर्वाद देते हुए संबोधित करेंगे। उन्होंने कहा कि कोरोना संकट को हमें अवसर के रूप में देखना होगा। आत्मनिर्भर भारत का आशीर्वाद देते हुए उन्होंने कहा कि कोरोना संकट से हमें अवसर के रूप में देखना होगा।

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Ultimate Definition of Risk



Period...



Portfolio Construction for Capital Preservation and Growth

- Selection of asset classes – lower correlation
- Strategic long term allocation for each asset class
- Tactical calls – Overweight or underweight
- Sub-asset class level decisions
 - a) Equity – market cap categories
 - b) Debt – Accrual or duration
 - c) International equities – Developed or emerging
- Asset allocation alpha



Uncorrelated Asset Classes – Reduced Varcovar Risk

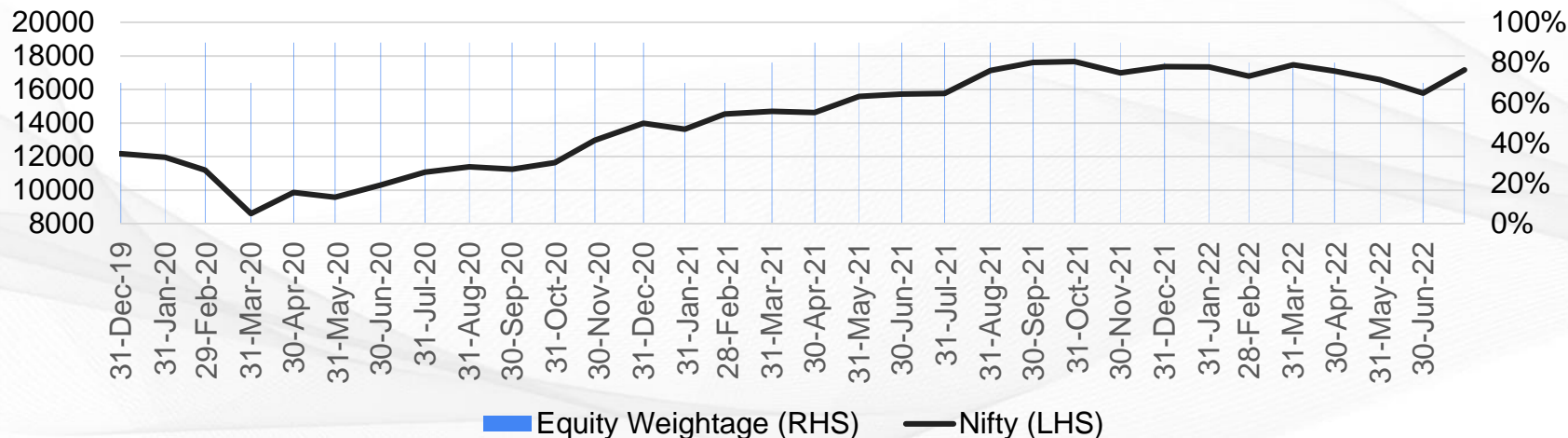
Financial Year	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
Equity-Large Cap*	8%	88%	19%	27%	-32%	53%	10%	-8%	14%	14%	24%	-3%	20%	16%	11%	-15%	50%
Equity-Midcap*	27%	82%	4%	35%	-44%	112%	3%	-8%	6%	14%	46%	5%	39%	13%	-13%	-22%	81%
Equity-Small Cap*	67%	102%	14%	30%	-56%	108%	2%	-8%	-5%	24%	40%	-4%	44%	15%	-22%	-36%	112%
Debt*	3%	4%	5%	9%	11%	5%	5%	9%	9%	8%	10%	9%	9%	6%	8%	10%	8%
Gold*	10%	55%	-5%	27%	26%	16%	32%	27%	-10%	-1%	-4%	14%	-5%	8%	2%	42%	3%

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Quant Model for Equity Tactical Calls

BEER* + Momentum Model

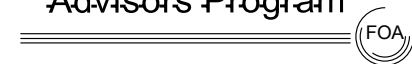


* BEER = Bond Equity Earnings Ratio

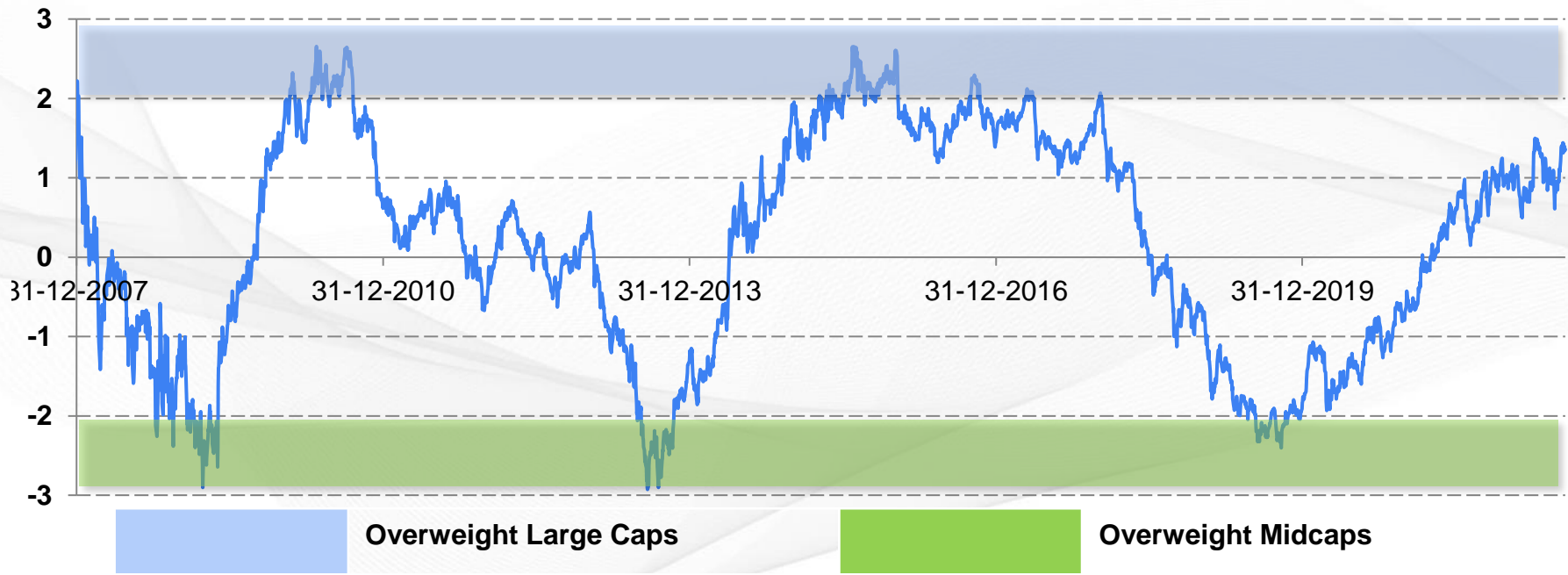
3 Years CAGR on daily Rolling basis since 2010

	Average	Median	Standard Deviation	Prob of negative returns
Nifty	10.46%	10.79%	5.17%	3.18%
Model	11.82%	12.61%	3.01%	0.88%

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Relative Valuation Indicator



Asset Allocation Alpha

Portfolio Alpha



Asset Allocation Alpha = (Portfolio Allocation – Benchmark Allocation) * Asset class returns

Overweight on Positive Returns

Parameters	Equity	Debt	Total
Benchmark Allocation	50%	50%	100%
Portfolio Allocation	60%	40%	100%
Returns	10%	2%	
Benchmark Performance	5.00%	1.00%	6.00%
Portfolio Performance	6.00%	0.80%	6.80%
Asset Allocation Alpha	1.00%	-0.20%	0.80%

Underweight on Negative Returns

Parameters	Equity	Debt	Total
Benchmark Allocation	50%	50%	100%
Portfolio Allocation	40%	60%	100%
Returns	-5%	2%	
Benchmark Performance	-2.50%	1.00%	-1.50%
Portfolio Performance	-2.00%	1.20%	-0.80%
Asset Allocation Alpha	0.50%	0.20%	0.70%

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Summary

- Conventional asset allocation approach is too standardised
- Every investor/ wealth manager should devise unique approach for asset allocation
- Tactical calls are necessary to generate asset allocation alpha

Thank You