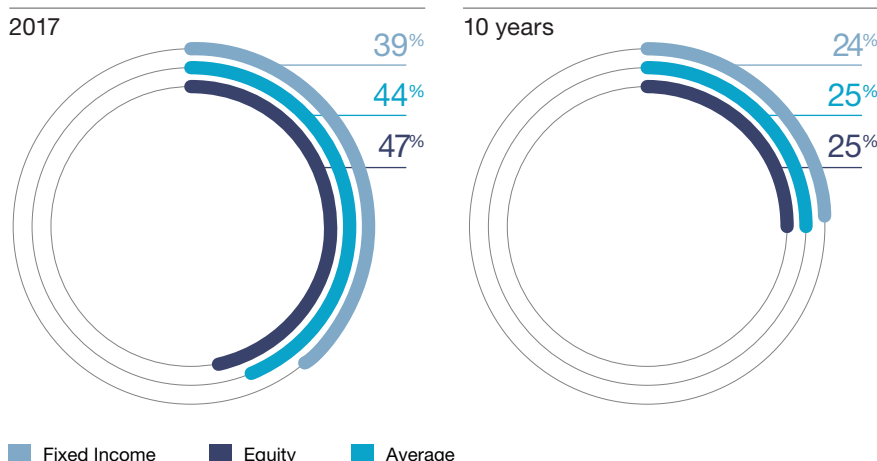
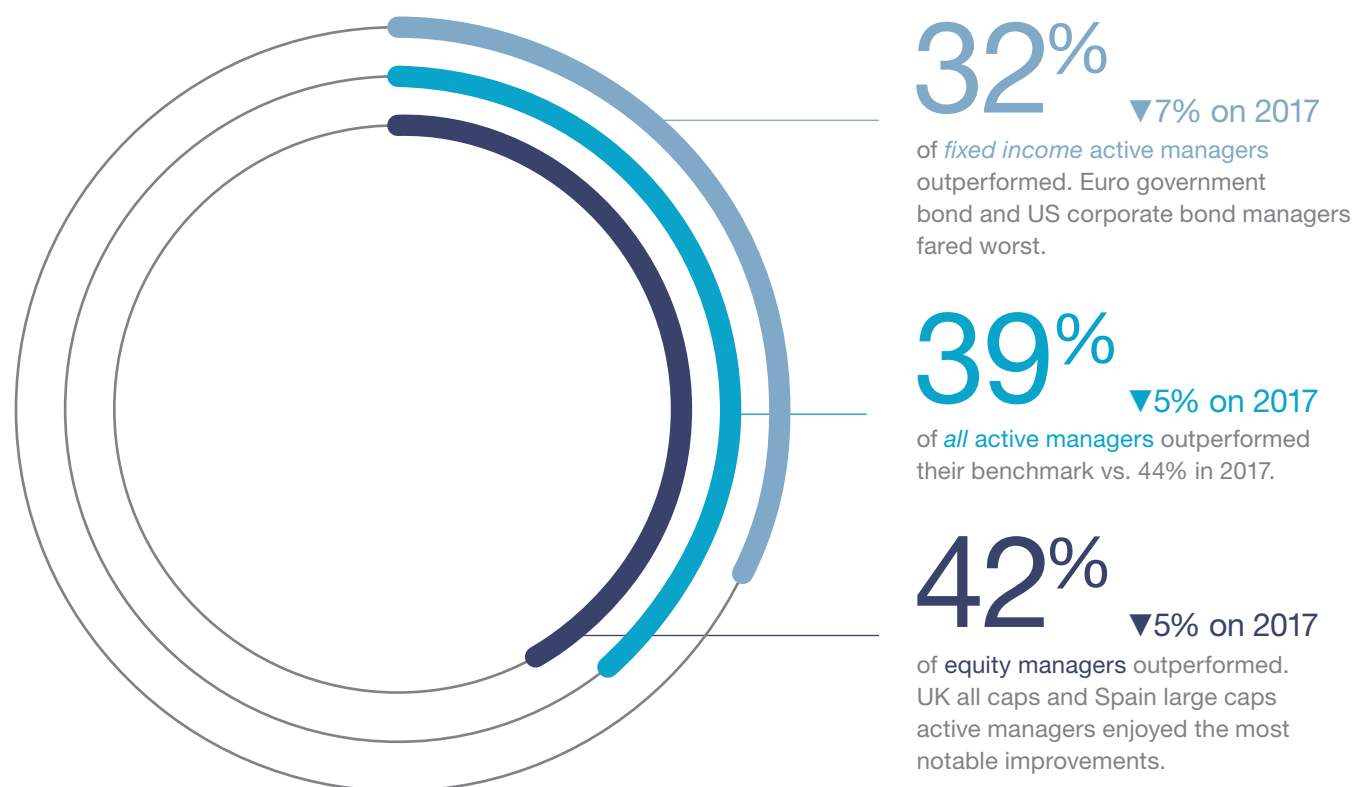


Informed Investor: Manager Monitor Q1 2018

# Q1 2018: Difficult start of the year for active managers

By Marlène Hassine Konqui, Head of ETF Research and Kristo Durbaku, ETF Research Analyst

Slight decline in performance in Q1 2018



## Q1 summary

- Difficult conditions for active managers
- More volatility leading to higher correlations, made the job harder for equity active managers
- Fixed income managers continued to find the environment challenging

Source: Morningstar and Bloomberg data from 31/12/2007 to 29/03/2018.  
The figures relating to past performances refer to past periods and are not a reliable indicator for future results. This also applies to historical market data.

## Manager Monitor

## Highlights


 39%
**1. Active manager performance declines**

39% of active managers outperformed their benchmark in Q1 2018 – a slight drop from last year's 44%. 42% of equity managers outperformed vs. the 47% we saw in 2017, while 32% of fixed income active managers outperformed (vs. 39% in 2017). Long-term results still suggest only 1 in 4 active managers outperforms over 10 years.


 42%
**2. Equity active fund performance weakens**

Over the quarter, equity managers failed to come to terms with the more volatile environment and increasing correlations. The main weaknesses were found in biggest, more efficient markets like the World, Japan, US and Eurozone. Interestingly, performance also tailed off in some less efficient markets like US and European small-caps and Italy. In contrast, we saw the biggest improvement in the UK all-cap universe where 75% outperformed in Q1 2018 (see our special focus on p5).


 32%
**3. Fixed income managers still find the environment challenging**

32% of fixed income active managers outperformed their benchmark in Q1 2018 vs. the 39% we saw last year. Credit managers were again largely to blame, with only 18% of euro and 19% of US corporate bond managers outperforming. Global bond managers again enjoyed the best results with 74% of them finishing ahead vs. the 67% that beat the benchmark in 2017. Euro inflation-linked bonds are the only area of real improvement – with 29% outdoing their index vs. 9% in 2017.


 -€47bn
**4. Fixed income active fund flows decline sharply**

Overall, European domiciled active fund flows declined by 46% in Q1. This is mainly explained by a decline of 82% for fixed income funds to €10.7bn, which could in part be explained by the very poor results we've seen. In contrast, we saw a significant increase in passive equities flows. On the active side, equities flows have continued to increase (from €23bn in Q4 2017 to €33bn in Q1 2018) despite the declining results.

**Blending active and passive management in Q1**

- ▶ In fixed income, the less favorable credit spread environment caused issues – most obviously among investment-grade credit where passive clearly won out
- ▶ When it comes to equities, US, emerging markets, World and Japan managers clearly struggled. Favoring passive products in these areas may have made more sense
- ▶ However, in the European universe more than half of active managers outperformed, mainly driven by the good performance of UK managers. Selecting the best managers in this area would have been positive for portfolio construction

Source: Morningstar and Bloomberg data from 31/12/2007 to 29/03/2018.

## % of Active Funds outperforming the Benchmark and their performance difference

Universe	Q1 2018		2017		10Y	
	% of funds outperforming the benchmark	Performance difference	% of funds outperforming the benchmark	Performance difference	% of funds outperforming the benchmark	Annualised performance difference
Europe Large Caps	58%	0.1%	45%	0%	36%	-1%
Eurozone Large Caps	49%	-0.2%	55%	0%	41%	-1%
Europe Small Caps	56%	0.1%	72%	1%	10%	-2%
Germany Large Caps	57%	-0.5%	61%	2%	14%	-1%
France Large Caps	28%	-0.2%	38%	-1%	13%	-1%
UK All Caps	75%	0.5%	30%	-2%	26%	-1%
Italy Large Caps	0%	-1.9%	81%	2%		
Spain Large Caps	70%	2.4%	32%	1%	38%	0%
Switzerland Large Caps	47%	-0.1%	37%	-1%	23%	-2%
US Large Caps	19%	-1.1%	32%	-1%	11%	-1%
US Small Caps	42%	-1.1%	57%	2%	50%	-1%
Japan All Caps	33%	0.1%	49%	0%	23%	-1%
World Large Caps	35%	-0.7%	54%	1%	11%	-2%
Emerging Markets Large Caps	30%	-1.0%	42%	0%	24%	0%
China Large Caps	37%	0.8%	24%	-2%	37%	1%
Euro Govies	18%	-0.3%	20%	0%	16%	-1%
Euro Corporate	24%	-0.2%	52%	1%	26%	-1%
Euro High Yield	22%	-0.2%	16%	-1%	0%	-3%
Euro Inflation Linked	29%	-0.2%	6%	-1%	82%	0%
US Corporate	19%	-0.1%	57%	-2%	0%	-3%
US High Yield	26%	-0.4%	56%	-1%	0%	-2%
Global Bobnds - EUR HDG	74%	0.2%	67%	1%	50%	0%
Emerging Debt	43%	0.1%	41%	0%	15%	-2%
<b>Average Equity</b>	<b>42%</b>	<b>-0.2%</b>	<b>47%</b>	<b>0.1%</b>	<b>25%</b>	<b>-1.0%</b>
<b>Average Fixed Income</b>	<b>32%</b>	<b>-0.1%</b>	<b>39%</b>	<b>-0.3%</b>	<b>24%</b>	<b>-1.5%</b>
<b>Average</b>	<b>39%</b>	<b>-0.2%</b>	<b>44%</b>	<b>0.0%</b>	<b>25%</b>	<b>-1.2%</b>

Source: Morningstar and Bloomberg data from 31/12/2007 to 29/03/2018.

## Special focus on fund performance

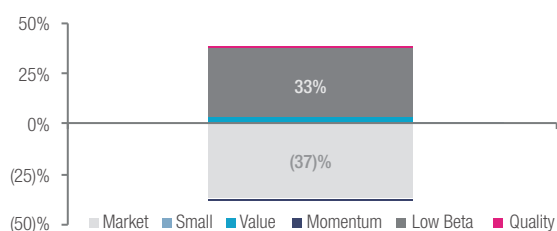
# Factor analysis

Developed by Lyxor's quantitative research team, our new tool has enabled us to analyse active fund risk factor\* biases for each quarter and each universe (left hand side graphs).

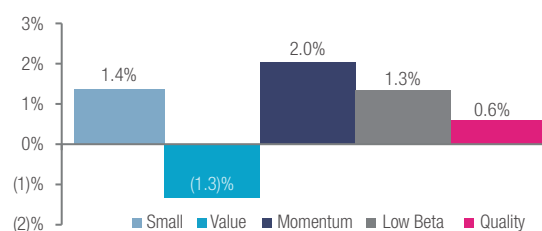
This helps us explain active fund performance when it is allied to risk factor performance vs relevant benchmarks. See the results in the graphs below.

## US

Graph 1: US active funds factors over/under weights vs. benchmark

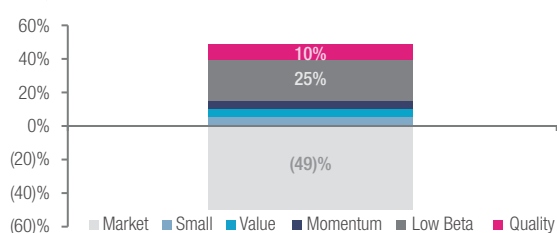


Graph 2: Factors out/underperformance vs. benchmark

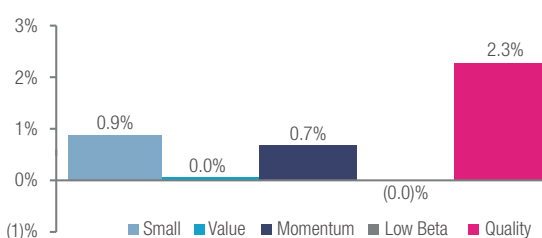


## Europe

Graph 3: Euro active funds factors over/under weights vs. benchmark

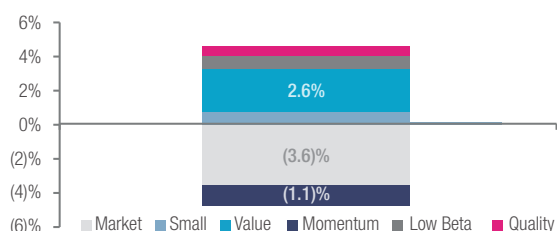


Graph 4: Factors out/underperformance vs. benchmark

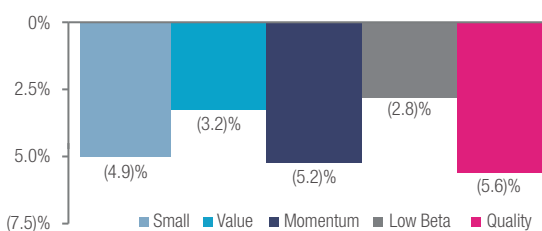


## Japan

Graph 5: Japan active funds factors over/under weights vs. benchmark

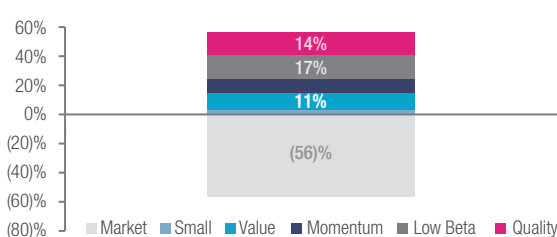


Graph 6: Factors out/underperformance vs. benchmark

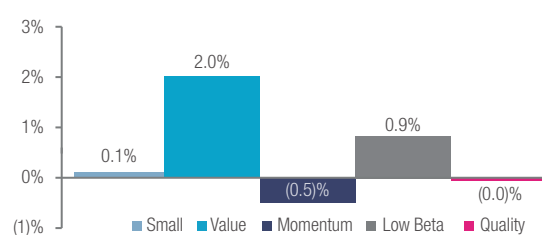


## EM Equity

Graph 7: EM Equity active funds factors over/under weights vs. benchmark



Graph 8: Factors out/underperformance vs. benchmark



Source: Lyxor and Morningstar data from 31/12/2017 to 29/03/2018.

\*Weighted average results using the MSCI SMALL CAPS INDEX and the following four Risk Factors from J.P. Morgan Equity Risk Primia indices: MOMENTUM FACTOR Long Only Index, LOW BETA FACTOR Long Only Index, VALUE FACTOR Long Only Index and QUALITY FACTOR Long Only Index.

## Special focus on fund performance

# Tough times, wherever you look

## Equities

In Q1 2018, 42% of equity active managers outperformed their benchmark – a decline of 5% on 2017 results. The main weaknesses were found in biggest, more efficient markets like the World, Japan, US and Eurozone. Interestingly, performance also tailed off in some less efficient markets like US and European small-caps and Italy. The more volatile environment with increasing correlations following February

market corrections made the job of active managers harder. In contrast, we saw the biggest improvement in the UK all-cap universe where 75% outperformed in Q1 2018. Managers in this area benefited from their slight overweight to outperforming small-cap stocks and the re-rating of non-UK exposures as sterling strengthened.

Graph 1: Peer group vs. benchmark relative performance compared to the GBP/EUR exchange rate – UK all caps Equity



Source: Morningstar and Bloomberg data from 31/03/2017 to 29/03/2018.

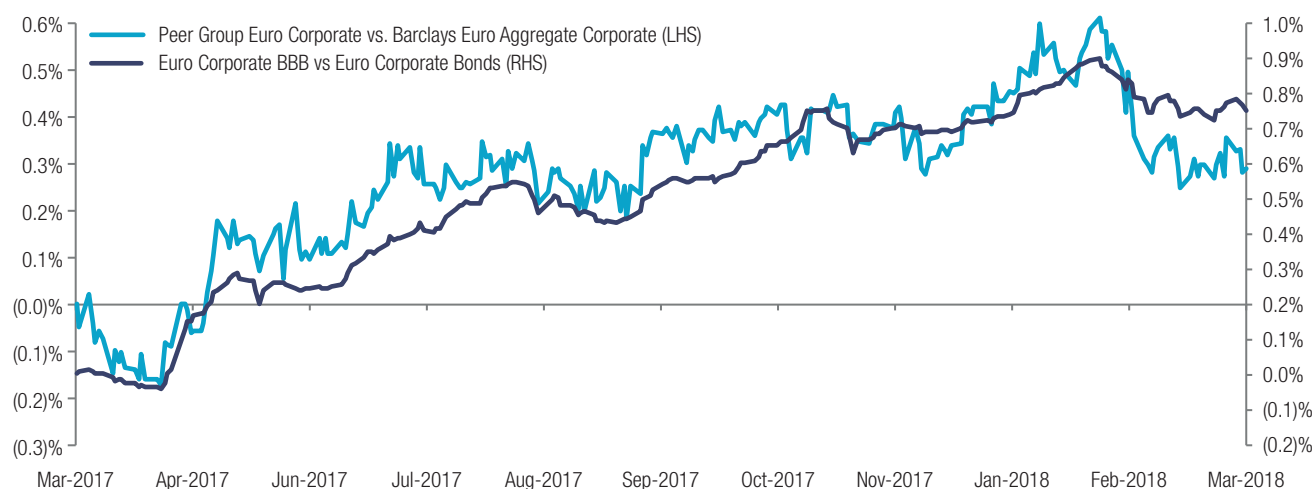
## Special focus on fund performance

### Fixed Income

Only 32% of fixed income managers outperformed vs. 39% in 2017 – driven largely by the performance of credit managers where we've seen some huge declines in just a few short months. In 2017, fixed income active managers slightly improved their performance in a rather difficult interest rate environment as rates remained rangy after an increasing at the beginning of the year. Those who did well on the global bonds as well as on credit areas were able to benefit from the positive trend of the credit market. The reversal on this trend on the credit market hurt credit active

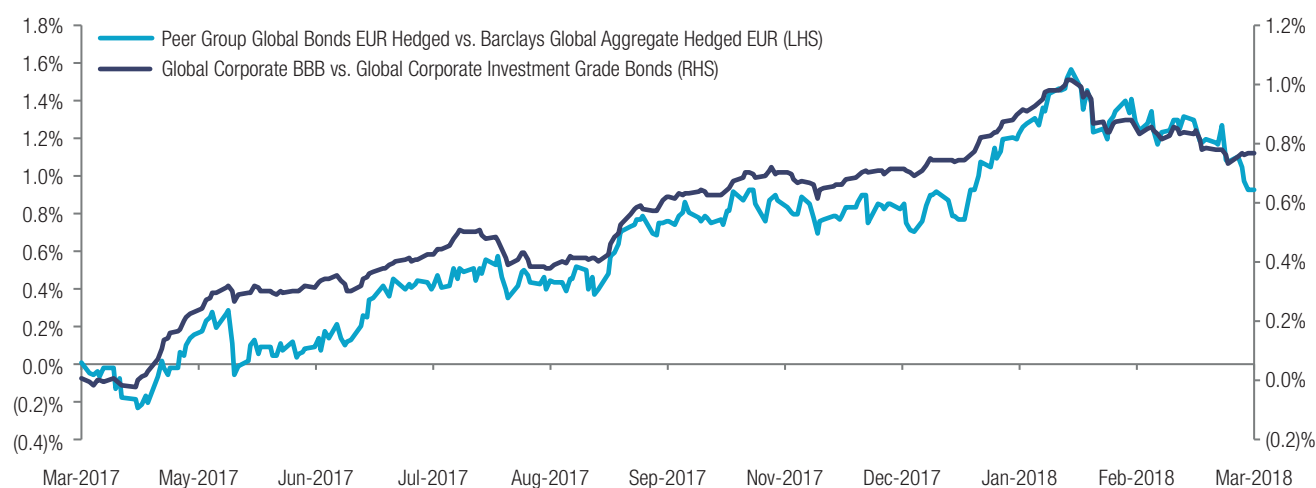
managers in Q1 2018. 19% of US corporate bond managers outperformed vs. 57% last year, meanwhile 24% of their euro counterparts outperformed (down from 52% in 2017). High yield bond performance was little better, with less than 1 in 4 US high yield bond managers outperforming. Global bond managers did best (again), as 74% outperformed – a modest gain on last year's 67%. Most benefited from increasing US interest rates and the positive trend for credit we saw at the very beginning of the year.

Graph 2a: Peer group vs benchmark relative performance compared to BBB yield spread – Euro Corporate



Source: Morningstar and Bloomberg data from 31/03/2017 to 29/03/2018.

Graph 2b: Peer group vs benchmark relative performance compared to BBB yield spread – Global Bonds EUR Hedged



Source: Morningstar and Bloomberg data from 31/03/2017 to 29/03/2018.

## Special focus on fund flows

# Is the money going to the right place?

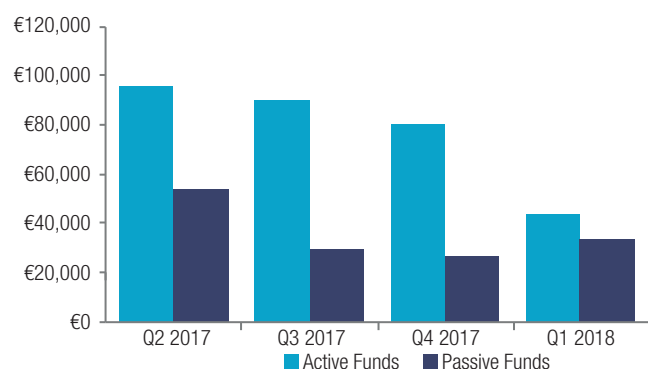
Overall fund flows slowed by 28% in Q1 2018 to €77bn. Active management suffered the bulk of the decrease with flows 46% below those of Q4 2017 at €43bn. On the other hand, ETF passive fund flows continued to increase up 27% at €34bn.

Flows were positive for active equities (up 43%) despite declining results, and were up by 60% for passive. The higher pace of passive management

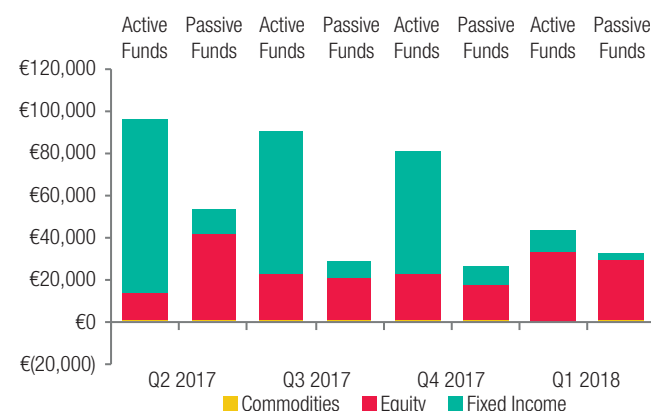
flow growth illustrates the greater confidence investors have in passive vehicles in many areas.

Flows in to fixed income fell very sharply however. Active fund flows fell by 82% to €11bn, while passive flows dropped by 46% to €4bn. This trend aligns with the poor performance results and an even more challenging outlook now the credit spread rally has reached its end.

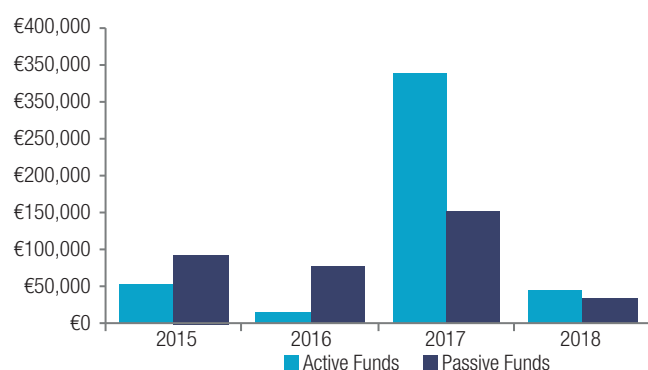
Quarterly Global Europe Active funds and Passive funds flows



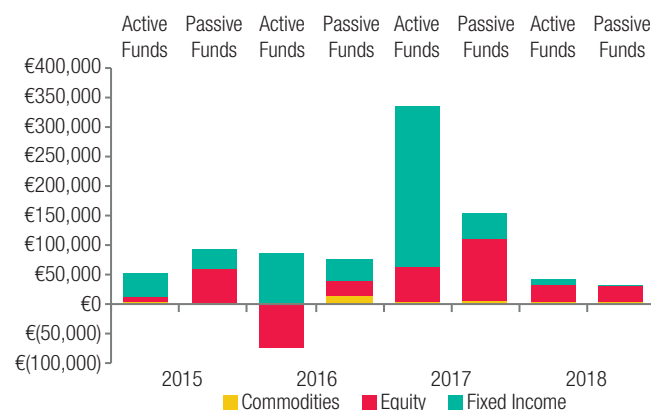
Quarterly Europe Active funds and Passive funds flows by category



Yearly Global Europe Active funds and Passive funds flows



Yearly Europe Active funds and Passive funds flows by category



Source: Lyxor and Morningstar data in EURbn from 01/01/2015 to 29/03/2018.

# Universe description

Universes	Benchmark	Selection Criteria	Nb of Funds	AUM (M€)
Europe Large Caps	MSCI Europe Net Return EUR Index	Morningstar Category Europe Equity Large Cap	805	166,369,604,772
Eurozone Large Caps	EURO STOXX 50 Net Return EUR	Morningstar Category Eurozone Equity Large Cap	354	16,375,327,871
Europe Small Caps	MSCI Europe Small Cap Net TR EUR	Morningstar Category Europe Equity Small Cap	80	7,003,164,709
Germany Large Caps	Deutsche Boerse AG German Stock Index DAX	Morningstar Category Germany Large Cap Equity	72	16,272,359,869
France Large Caps	CAC 40 Total Return Index	Morningstar Category France Large Cap Equity	154	15,545,325,591
Uk All Caps	FTSE UK Series FTSE All Share TR	Morningstar Category UK All Cap Equity	235	85,044,670,487
Italy Large Caps	FTSE MIB Net Total Return Index	Morningstar Category Italy Large Cap Equity	30	3,169,973,284
Spain Large Caps	IBEX 35 Net Return Index	Morningstar Category Spain Large Cap Equity	121	7,876,913,447
Switzerland Large Caps	Swiss Exchange Swiss Performance Index	Morningstar Category Switzerland Large Cap Equity	138	42,675,082,893
Us Large Caps	MSCI USA Net Total Return USD Index	Morningstar Category US Large Cap Equity	617	144,700,812,705
Us Small Caps	Russell 2000 Total Return Index	Morningstar Category US Small Cap Equity	71	7,383,799,148
Japan All Caps	Topix Total Return Index JPY	Morningstar Category Japan Equity	540	73,433,614,508
World Large Caps	MSCI World Net Total Return USD Index	Morningstar Category Global Equity Large Cap	1,252	262,166,106,042
Emerging Markets Large Caps	MSCI Emerging Net Total Return USD Index	Morningstar Category Emerging Markets Equity	628	230,613,790,180
China Large Caps	MSCI China Net Total Return USD Index	Morningstar Category China Equity	80	21,455,188,457
Euro Govies	FTSE MTS Eurozone Government Bond IG Index (Ex-CNO Etrix)	Morningstar Category EUR Governments Bonds	135	26,494,006,353
Euro Corporate	Bloomberg Barclays Euro Aggregate Corporate Total Return Index Value Unhedged EU	Morningstar Category EUR Corporate Bonds	192	76,104,531,875
Euro High Yield	ICE BofAML Euro High Yield Index	Morningstar Category EUR High Yield Bonds	72	15,797,679,215
Euro Inflation Linked	Bloomberg Barclays Euro Govt Inflation-Linked Bond All Maturities Total Return I	Morningstar Category EUR Inflation-Linked Bonds	33	4,734,566,464
Us Corporate	Bloomberg Barclays US Corporate Total Return Value Unhedged USD	Morningstar Category US Corporate Bonds	44	14,541,142,472
Us High Yield	Bloomberg Barclays US Corporate High Yield Total Return Index Value Unhedged USD	Morningstar Category US High Yield Bonds	53	35,154,701,707
Global Bonds - Eur Hdg	Bloomberg Barclays Global-Aggregate Total Return Index Value Hedged EUR	Morningstar Category Global Bonds EUR Hdg & Global Flexible Bonds EUR Hdg	56	35,800,936,921
Emerging Debt	JP Morgan GBI-EM Global Diversified Composite Unhedged EUR	Morningstar Category Global Emerging Markets Bond - Local Currency	108	58,470,583,684
<b>Total</b>			<b>5,870</b>	<b>1,367,183,882,654</b>

Source: Morningstar data in EUR as of 31/12/2017.

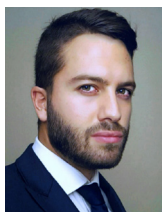
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Read the full 2017 analysis  
on active and passive  
performance

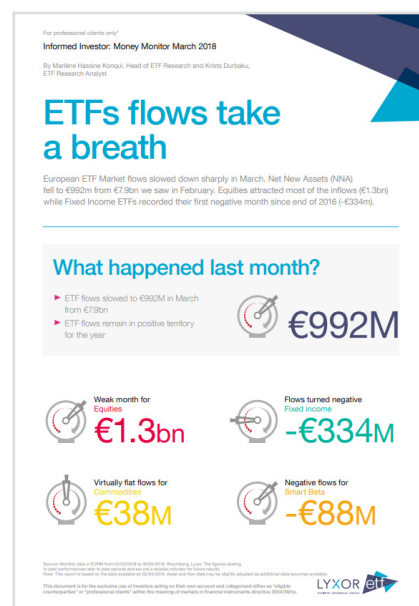
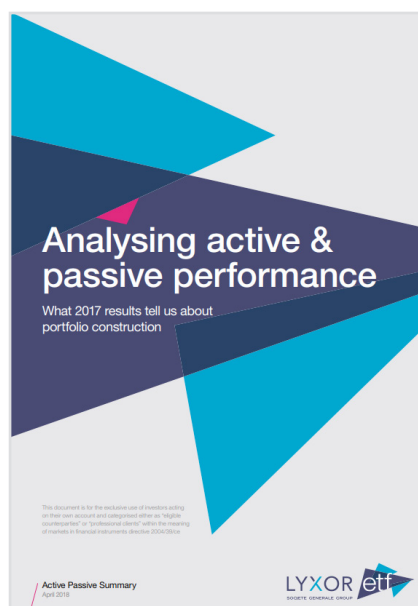
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