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 **HSBC** Asset Management

**Interview with  
Jean-Charles Bertrand  
of HSBC Asset Management**

**Frank J. Fabozzi, Editor**

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### Jean-Charles Bertrand

Jean-Charles Bertrand is Global CIO, Multi-Asset at HSBC Asset Management. The previous positions held by Jean-Charles included CIO and Managing Director of Sinopia Asset Management, which was the quantitative specialist of HSBC Asset Management. Jean-Charles joined us in 1994 and has been in the financial industry for 30 years. He graduated from the Ecole Supérieure des Sciences Economiques et Commerciales (France) and holds a post graduate degree in Applied Probability from the Paris VI University (France). Jean-Charles is a lecturer and an Affiliate Professor at HEC, a premier business school in France, and also a lecturer at Université Paris-Dauphine.



# Interview with Jean-Charles Bertrand of HSBC Asset Management

Frank J. Fabozzi, Editor

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**Frank J. Fabozzi:** How do you define your investment philosophy for managing multi-asset portfolios?

**Jean-Charles Bertrand:** At the core of our investment philosophy is the belief that long-term performance is anchored in a robust investment framework backed by extensive academic research and practitioner experience. There are two essential features that can yield robust and repeatable excess returns for multi-asset portfolios: breadth and cost-efficient flexibility. A robust multi-asset strategy cannot only rely on a few big macro directional bets across asset classes (bonds vs equity) but should also be based on a high number of active asset allocation decisions within asset classes (country/sector/style/rating...). This breadth enables us to build robust multi-asset solutions by diversifying sources of return. Additionally, we believe in the strategic use of liquid instruments, particularly liquid derivatives, when our clients are permitted to use them. This flexibility allows us to be active and responsive in adjusting allocations while managing real-life constraints, such as transaction costs.

To articulate our investment philosophy more clearly, let me frame it in terms of investment beliefs, a common practice within our industry. I hope that they are not only beliefs but are also close to scientific facts! Our investment beliefs include the notion that markets are “efficiently inefficient,” as elegantly phrased by Lasse Pedersen. Alpha opportunities exist because investors have biases and artificial constraints that create excess volatility and mispricings. Over time, these mispricings correct, allowing us to capture them through relevant investment models and metrics efficiently. Thus, while alpha opportunities exist, the challenge lies in identifying where these opportunities arise and determining when to align with market trends.

We also believe that diversification is key to resilient portfolios. Although this is largely a conventional belief for multi-asset portfolios, we consider our approach distinctive. We define diversification in terms of broad asset class inclusion and at a very granular level within asset classes. Diversification of signals is also key. As an example, we usually use a combination of carry/value/momentum indicators which are very complementary to take asset allocation decisions within asset classes.

Finally, discipline is essential for consistent long-term returns. A systematic approach to identifying opportunities across global markets is crucial for diversification to yield its full benefits. We rely on a robust quantitative framework to minimize behavioral biases. This systematic approach provides a clearer lens through which we can apply discretionary judgment. Discipline is also at the core of our portfolio construction approach: we use hierarchical mean-variance optimization for strategic asset allocation (SAA) and risk-budgeting for tactical asset allocation (TAA).

This comprehensive approach fosters a consistent investment process that gives us confidence that we can deliver stable risk-adjusted performance over the long term and across different market cycles and environments.



**Fabozzi:** What are the key components of your asset allocation strategy?

**Bertrand:** Our asset allocation strategy is structured around three fundamental stages: SAA, TAA, and implementation and monitoring. Let me focus on the first two stages (e.g., asset allocation strategy).

The first stage involves constructing an SAA, beginning with a reference portfolio that includes only two asset classes: equities and government bonds. This initial framework reflects the investor's risk tolerance, after which we build a more diversified SAA by expanding the investment universe and integrating unconditional (equilibrium) and conditional long-term expected returns (capital markets assumptions). Asset allocation construction is based on a 2-stage hierarchical optimization to avoid mixing highly correlated asset classes. At the sub-asset class level, we typically favor market capitalization splits, adjusted for liquidity and other qualitative factors or client preferences.

In the second stage, we implement TAA decisions using a predominantly quantitative framework. We have developed a set of systematic signals to identify market opportunities. These signals leverage patterns in market returns—such as momentum, carry, and value—while also considering the broader market environment, including macroeconomic factors and risk/sentiment assessments.

While quantitative signals are invaluable, they cannot capture all investment considerations, particularly in areas where data is qualitative or historical data is limited. Therefore, we incorporate a discretionary overlay within our portfolios, analyzing political developments, technical data, and insights from asset class specialists. The overall views generated from these analyses are formalized during our investment committee meetings, where we synthesize the various inputs. Finally, we size nominal active positions within portfolios through a risk budgeting approach. Risk budgets are defined based on the strength of current opportunities and confidence in alpha drivers measured by their information coefficients.

**Fabozzi:** What tools or models are most effective for analyzing asset correlations and diversification benefits?

**Bertrand:** Analyzing the price dependence structure of assets through correlations can serve as an effective starting point. We employ a hierarchical clustering approach based on correlation distances to classify asset classes into clusters. This method allows us to identify groups of asset classes that exhibit similar performance patterns, enabling us to focus on the correlations between these clusters rather than getting lost in numerous individual correlations.

However, understanding the economic rationale behind asset correlations is essential. We adopt a factor-based approach at the macro level to identify key factors that explain the returns of multi-asset portfolios. Our proprietary model identifies four primary investable factors: growth, duration, inflation, and defensiveness. Investable factors are defined as combinations of market variables such as equity returns, credit spreads, breakeven inflation, and commodities. They also serve as reasonable proxies for macroeconomic variables like GDP growth and inflation and market uncertainty indicators such as the VIX. We estimate asset classes' sensitivities to these factors, allowing us to measure asset classes' correlations based on exposure to these four factors and construct portfolios targeting specific factor exposures.

Yet, it is vital to go beyond mere correlation! Correlation measures only linear dependence between assets, which can be misleading during market crises when everything is correlated, particularly with equity markets. We evaluate correlation breakdowns by calculating conditional correlations based on negative equity returns to address this. We have developed a complete set of quantitative metrics to assess asset classes' defensive properties, including convexity, reactivity, and reliability. Additionally, we employ heuristic approaches that involve worst-case, or scenario



analyses based on simulations of historical crises. This helps to identify concentration and hidden risks and explore if the current asset allocation is robust to future shocks.

Regarding tools, we utilize a combination of proprietary systems, such as HSBC Analytics, our front office Portfolio Management System, alongside industry solutions. Developing our internal tools enables us to implement our factor-based and portfolio construction approaches more effectively.

**Fabozzi:** How do you approach the liquidity management challenge across multiple asset classes?

**Bertrand:** This is indeed a challenging yet crucial question. In my experience, investors often hold strong beliefs about illiquidity premia but may not focus enough on properly integrating liquidity considerations in portfolio construction.

When tackling the liquidity issue, it is vital to distinguish between liquid assets and less liquid assets, such as private markets. As regards liquid assets, liquidity management is mainly limited to monitoring them at the security level using third-party market impact liquidity models.

Regarding illiquid assets, it is essential to incorporate liquidity considerations directly into the portfolio construction process, as assets are no longer perfectly substitutable. As an example, private assets introduce complexities due to limited data availability, infrequent valuations, and difficulties in portfolio rebalancing and market timing. Said in another way, illiquid assets can provide illiquidity premia but there are also some opportunity costs! Our approach integrates these practical investment challenges with portfolio theory by making several adjustments to incorporate liquidity considerations into our expected returns and risk estimates. We utilize a framework introduced in a 2013 article published in this journal, "Liquidity and Portfolio Choice: A Unified Approach, co-authored by Will Kinlaw, Mark Kritzman, and David Turkington, to address multiple dimensions of liquidity, treating it as a shadow asset or liability within the portfolio. This framework quantifies the expected return and risk associated with liquidity. For risk estimation, we adjust the time series of private assets by identifying a related liquid benchmark and applying a de-smoothing technique to remove autocorrelation. This process helps provide a more accurate representation of the risk characteristics of these assets.

**Fabozzi:** What role do macroeconomic factors play in your investment decision-making process?

**Bertrand:** Rather than very actively forecasting economic variables such as growth or inflation and translating these directly into asset class views, we recognize the inherent uncertainty in both macroeconomic indicators and market responses. This uncertainty makes maintaining a strong forecasting edge in this area challenging.

Nonetheless, the economic environment is fully integrated into our decision-making process in several ways. Our Global Investment Strategy team is responsible for defining macroeconomic scenarios and providing monthly updates that include detailed analyses. Long-term economic scenarios are also inputs to our capital market assumptions, which drive our Value signals. These macroeconomic scenarios are extensively discussed in our *Quarterly Strategic Forum* across our global investment platform.

At the multi-asset level, directional decisions—specifically asset allocation—are guided by a multi-signal approach that combines value, momentum, risk/sentiment, macroeconomic factors, and discretionary considerations. The direct impact of changes in the economic environment is reflected in our macro input, which incorporates eight indicators selected based on academic literature, historical performance, and cross-correlations. These signals ensure a balanced representation of economic growth, monetary policy, inflation, and credit conditions. The outputs from these macro factors are then contextualized within the framework of the strategy team's macro scenarios.



**Fabozzi:** How do you incorporate alternative investments into your multi-asset portfolios?

**Bertrand:** Let me start by saying that I have always been mindful of the differing perspectives between academics and practitioners regarding alternative assets. While alternative investments, whether liquid alternatives or private assets, have gained significant popularity among asset owners and managers—often referred to as the Yale model—academics tend to express some reservations. They argue that not all alternative investments are genuinely “alternative” and caution that their superior returns may be overstated when accounting for fees, survivorship biases, and factor exposures.

I believe alternative investments can play a crucial role in multi-asset portfolios, provided they are thoroughly analyzed. Their diversification properties must be assessed to classify them into two categories: diversifying alternatives and return-enhancing alternatives. Diversifying alternatives are uncorrelated with existing portfolio holdings. Good examples of diversifying liquid alternatives are trend-following strategies, long-short risk premia strategies, gold, and selective commodities. On the other hand, return-enhancing alternatives are related to existing portfolio holdings but can improve returns or reduce risk. They typically achieve this by adding a liquidity premium, as seen in private equity or direct real estate, or a complexity premium found in selective corners of credit markets, such as asset-backed securities.

In principle, most return-enhancing alternatives can be incorporated into the portfolio process similarly to conventional assets. As long as we have reliable estimates for their prospective returns and can accurately represent their risk characteristics—such as de-smoothing price data to estimate actual volatility and accounting for illiquidity—they are suitable candidates for classical optimization processes like mean-variance optimization. Conversely, diversifying alternatives requires a distinct approach. Given that they typically offer sustainable risk premiums unrelated to equity, credit, or duration, we aim to maximize their inclusion within strategic allocations while adhering to a defined risk budget. Additionally, we consider substituting conventional assets with diversifying alternatives where appropriate; for instance, gold may be an effective substitute for government bonds due to its defensive properties.

Thus far, our focus has primarily been on liquid alternatives, mainly for liquidity and regulatory reasons. However, we have recently begun integrating less liquid asset classes, such as private equity and infrastructure, in a semi-liquid format (like evergreen funds) for long-term investors. It is important to emphasize that active management, particularly manager selection, is critical for private assets, as “we cannot buy the market since no investable index exists,” as noted by David Swensen in his 2009 book *Pioneering Portfolio Management*. While Yale’s experience demonstrates that some investors can achieve significant success in this area, it is not systematic and requires superior fund selection skills.

**Fabozzi:** What strategies do you employ to hedge against significant market downturns?

**Bertrand:** In an asset allocation framework, protecting against downside risk can be approached in at least two distinct ways: active asset allocation and well-diversified allocation.

Active asset allocation involves tactical adjustments—specifically, reducing exposure to richly priced assets or taking long volatility positions. Historically, these tactics have proven more effective in weathering potential drawdowns than static strategies. For instance, we initiated long volatility exposure during the summer of last year and successfully monetized those positions. However, timing these moves is, of course, very challenging.



This is why it should be complemented by a well-diversified asset allocation that remains resilient during market downturns. Traditionally, government bonds have been a key component of equity hedging strategies; however, the dynamics shifted in 2022, suggesting that bonds should not be the sole option for hedging against significant market downturns. Our approach involves implementing exposure to defensive strategies that can mitigate risk over a defined investment horizon. We believe combining strategies with explicit downside protection—such as long put options and Cboe VIX exposure—with safe-haven assets (like gold or currencies such as the Swiss franc, Japanese yen, or US dollar) presents a compelling strategy. Explicit downside protection strategies provide strong reliability and consistency of protection, albeit at a cost during normal market conditions. At the same time, safe-haven assets offer attractive convexity, performing well in stable times but less reliable during stress periods. Another complementary strategy to hedge against bearish equity markets is incorporating trend-following strategies, which have demonstrated strong convexity properties.

**Fabozzi:** How do you evaluate the performance of your multi-asset portfolio?

**Bertrand:** Evaluating the performance of our multi-asset portfolios is a multifaceted process that reflects our clients' varying objectives.

Our primary focus for our traditional multi-asset long-only portfolios is to maximize investment returns relative to the client's risk budget, typically measured by Sharpe ratios. We also assess active performance against a reference benchmark, which is tailored to the investment universe and the client's risk appetite. For our institutional clients, the evaluation criteria shift slightly. Here, the objective is to maximize excess returns against their SAA or benchmark while adhering to a defined risk budget and specific investment constraints and the standard metric is the Information ratio.

As regards less directional multi-asset strategies such as absolute return (e.g., long/short, alternative risk premia) or risk-managed strategies (constant proportion portfolio insurance and option-based portfolio insurance strategies), performance evaluation encompasses additional objectives, such as achieving low correlation to traditional asset classes and controlling portfolio risk and drawdown, which can be set as primary objectives. Relevant risk-adjusted return metrics are the Sortino and Omega ratios.

In addition to these financial objectives, we incorporate sustainability metrics into our performance evaluation for our ESG multi-asset solutions, aiming for higher ESG scores and exposure to SDGs, lower carbon intensity compared to the multi-asset benchmark.

I would like to highlight two crucial considerations regarding time horizons and performance league tables. The industry often places excessive emphasis on short-term performance, which can be noisy and makes it challenging to distinguish skill from luck. As an anecdote, I usually show a chart displaying rolling one-year and three-year performances for Warren Buffett without revealing his identity. Many people remain unconvinced by the track record. This reveals something!

Additionally, while performance league tables are popular, they can be misleading. Fund categories are often too broad and fail to account for structural biases between funds. It is crucial to consider more granular categories and, ideally, conduct style analysis to identify these biases. Although this approach has gained traction over the years, it is still not as common as it should be, in my opinion.

**Fabozzi:** What are your biggest challenges in managing multi-asset portfolios today?

**Bertrand:** In my view, there are two longstanding yet more than ever relevant challenges in managing multi-asset portfolios. The first challenge is building truly diversified portfolios.



Actually, we observe that major economic factors, such as inflation, and geopolitical events, like trade wars increasingly influence markets. This interconnectedness can undermine traditional diversification strategies. To address this challenge, extending the investment universe to include alternative asset classes is beneficial, as previously discussed, but this must be done thoughtfully. Another approach is to focus on a combination of defensive liquid assets that are genuinely uncorrelated, such as safe-haven currencies and gold, alongside tail risk hedging strategies that provide negative correlation, like trend-following and options-based portfolio insurance. This multifaceted strategy aims to enhance resilience against market shocks.

The second significant challenge lies in the interaction between asset allocation and security selection decisions within multi-asset portfolios. A simplistic approach would be to rely solely on market exposure for fulfilment, but this would forfeit the alpha generated from security selection. Typically, in many multi-asset organizations, security selection is delegated to specialized equity and fixed-income portfolio managers through investments in single-asset class sleeves or funds. At the same time, asset allocation decisions are made by multi-asset portfolio managers. However, this approach can be suboptimal, as specialized teams may make tactical or structural decisions regarding country, sector, or style allocations that could offset or inadvertently increase the risks taken by multi-asset teams. This results in limited control over the active risk and performance of the total portfolio.

To mitigate this risk, we recommend implementing a framework that governs security selection decisions, providing clear guidelines to equity and fixed income portfolio managers, including maximum deviations and tracking error limits. Additionally, utilizing plain-vanilla derivatives, such as futures, to implement asset allocation decisions can be extremely helpful. This ensures a clear delineation of responsibilities and instruments between teams, allowing for better measurement of contributions from different teams. This structured approach facilitates improved oversight and alignment across our multi-asset portfolios.

**Fabozzi:** How has the integration of ESG criteria impacted your portfolio construction?

**Bertrand:** It is essential to manage clients' expectations regarding the impact of ESG considerations. Many investors assume that achieving superior performance (doing well) and sustainable investing (doing good) go hand in hand. While this can be true, the reality is often more nuanced, a distinction that is well understood in academic circles but not as prevalent in the industry. Consequently, we differentiate between our standard multi-asset solutions and our ESG Multi-Asset solutions.

All our multi-asset solutions incorporate ESG criteria at the security selection level, adhering to HSBC's minimum responsible investment requirements. This includes implementing exclusions and integrating ESG considerations into investment decision-making, particularly when they impact securities' financial performance. We also view stewardship, voting, and engagement as powerful tools for driving positive change and enhancing the value of the companies we invest in on behalf of our clients.

For our ESG Multi-Asset solutions, we offer a range of investment options with sustainability targets embedded in their objectives. We are committed to innovation in this area and have developed approaches to integrate ESG considerations at the macro-level (top-down) and not only at the security level (bottom-up), either through risk and return estimates or the utility function. This includes using proprietary long-term ESG and climate-aware expected returns. Additionally, we have built climate-aware long-term risk estimates by examining the exposure of volatilities and correlations to macro variables such as GDP growth and inflation, as well as the use of climate scenarios. More recently, we have developed a methodology to measure cross asset climate betas and build multi-asset portfolios considering climate risk exposure.



**Fabozzi:** How do you stay informed about new investment opportunities and innovations in asset management?

**Bertrand:** I firmly believe that many strategies and tools employed by practitioners today are built upon the foundation of academic research. Similarly, some of the most impactful innovations arise from the practical applications of this research. This is why I prioritize maintaining strong connections with the academic community.

On a personal level, I serve as an affiliate professor at HEC Paris, which keeps me engaged with the academic world. Additionally, we collaborate closely with academic consultants such as Guillaume Coqueret, our co-author of recently published research papers including one in this special issue, who offers valuable insights into emerging trends and methodologies that can enhance our investment processes.

Beyond my personal involvement, I strive to cultivate a culture of learning within our multi-asset team. This includes encouraging the reading of leading academic and practitioner journals, which are essential resources for understanding the latest research findings and their implications for asset management. I also promote participation in internal research meetings and seminars, where portfolio managers can share insights and discuss innovative ideas. Furthermore, I highly encourage attending academic and practitioner conferences, as these events provide opportunities to network with industry leaders and gain exposure to new concepts and strategies. I also advocate for our portfolio managers to pursue recognized certifications, such as the CFA or CFA ESG investing. This commitment to professional development not only enhances their knowledge but also strengthens the team's overall expertise.

**Fabozzi:** What trends or shifts are you observing in the multi-asset investing landscape?

**Bertrand:** I would mention three significant trends reshaping the multi-asset investing landscape: moving away from 60/40 portfolios, artificial intelligence (AI) application to portfolio construction and the development of better retirement solutions.

Firstly, there is a noticeable shift away from the traditional 60/40 portfolio model, a change underscored by the market movements of 2022 and the search for true diversifiers. It is crucial to approach this transition carefully, conducting thorough assessments of diversification properties. Investors may sometimes overemphasize artificial diversification among certain asset classes or alternative strategies, particularly when faced with stale pricing (i.e., assets not marked to market).

Secondly, the application of AI and machine learning is becoming increasingly relevant in multi-asset investing. Historically, machine learning has focused on return prediction and large-scale problems like security selection, with limited application in portfolio optimization. While robo-advisors have enhanced customer knowledge and personalization, their impact on portfolio management approaches has been more modest. However, recent research is paving the way for more effective integration of parameter estimation and portfolio construction in a single stage. Additionally, emerging reinforcement learning approaches are enabling us to tackle multi-period decision-making problems more effectively. This evolution in technology and methodology holds great promise for enhancing multi-asset solutions.

Lastly, there is an urgent need to develop better retirement solutions. I believe the industry tends to recycle classic lifestyle balanced portfolios into retirement solutions. Target date funds based on age-based allocation (glidepaths) are not often well designed and significantly diverge from economic theory. For example, these funds typically employ deterministic allocations and consider cash or traditional fixed-income benchmarks as safe assets. Moreover, they tend to focus on maximizing wealth at retirement without adequately addressing the retirement income needs of investors. However, as rightly pointed out by Robert Merton in his 2014 *Harvard Business*

Review article, “The Crisis in Retirement Planning”, the relevant risk is retirement income uncertainty, not portfolio value.

To tackle these challenges, the industry must develop a “Retirement 2.0” offering that enhances target date funds by incorporating dynamic allocations based on market opportunities and defining a true safe asset, such as a deferred inflation-indexed annuity. A paradigm change from collective age-based investing to personalized goal-based investing is also necessary. This should evolve into a “Retirement 3.0” model, paving the way to new, individualized retirement solutions that customize each investor’s asset allocation based on his/her personalized retirement objectives, expected savings plan, and risk objective. While this is “a tough engineering problem” as noted by Robert Merton, developments in this direction should be a key priority for all asset managers.