

FOR PROFESSIONAL CLIENTS/
QUALIFIED INVESTORS/QUALIFIED CLIENTS ONLY

PORTFOLIO CONSTRUCTION

Navigating portfolio challenges

Dive into case studies and see how your peers are using indexing to maximise the efficiency of risk and fee budgets, reduce portfolio costs and focus on finding true alpha.

Capital at risk. The value of investments and the income from them can fall as well as rise and are not guaranteed. The investor may not get back the amount originally invested.

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01 Asset Manager

02 Asset Owner

03 Discretionary Portfolio Manager

Asset Manager

- 01 Re-thinking product choices**
- 02 Expressing short-term market views**
- 03 Building a defensive portfolio**
- 04 Managing allocations to alternatives**
- 05 Deciphering factor-driven returns**
- 06 Thinking sustainably**

01 Re-thinking product choices

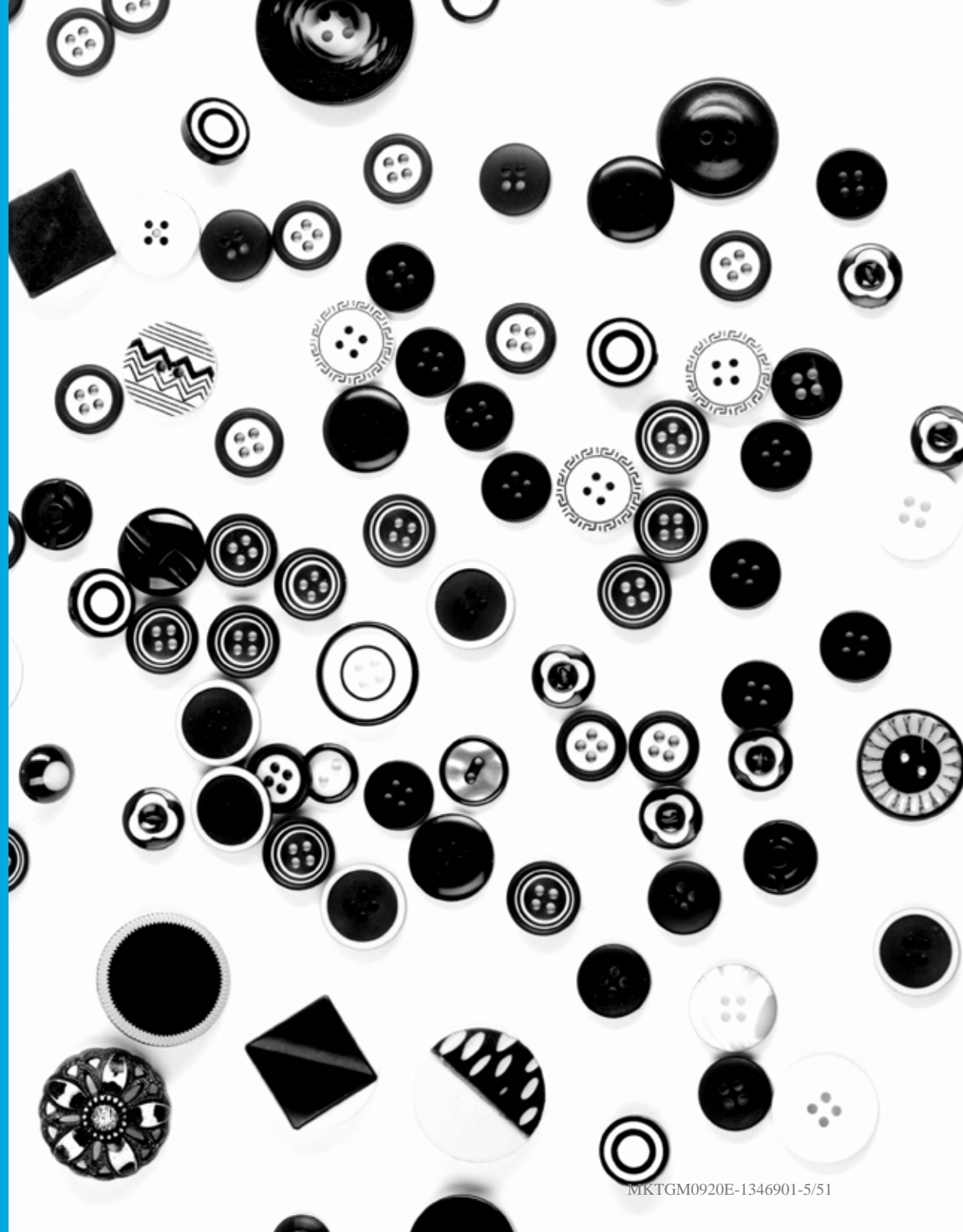
THE CHALLENGE

How can I decide which investment tools to use to implement my market views?

Portfolio managers are increasingly realising that 'active in x, passive in y' is too simplistic, while recognising the benefits of blending across investment tools to achieve stronger portfolio outcomes.

This means investors are re-thinking product choices to maximise the efficiency of their risk and fee budget allocation.

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01

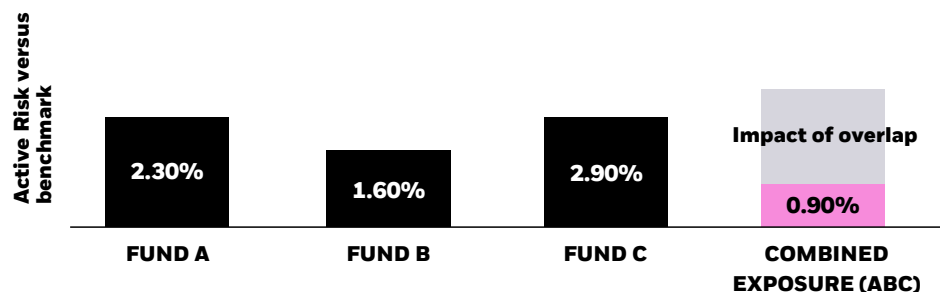
Re-thinking product choices

The action

Investors need to know what they are buying and how to identify the main drivers behind their portfolio risks and returns.

In this instance, while each of the below alpha-seeking managers had generated alpha, when combined their active bets had negated each other.

The portfolio was overdiversified, resulting in a large portion of risk being driven by broad market exposures, and therefore potentially replicable with an index solution.



Source: BlackRock, as at May 2020. For illustrative purpose only. Chart assesses ex-ante active risk of three active mutual funds with the same benchmark. Combined exposure (ABC) is an equal weighted combination of the three funds.

The outcome

Consolidation of the number of managers used to express the market view helped drive improved efficiencies.

By recognising different drivers of returns, the required benchmark expected return can be generated through low-cost indexing, with the remainder of the fee and risk budget allocated to selective alpha-seeking strategies that demonstrate 'true alpha'.

Why indexing?

Moving beyond an asset class siloed approach between 'active vs passive', and instead determining the optimal index and alpha split at a portfolio level, resulted in a greater allocation to indexing across exposures.

Taking a blended approach, while using indexing as an efficient way to express broad market views, can increase i.e. make less certain the portfolio information ratio, and can enable clients to maximise the efficiency of risk and fee budget allocations.

Risk: There can be no guarantee that the investment strategy can be successful and the value of investments may go down as well as up.

Case studies are for illustrative purposes only; they are not meant as a guarantee of any future results or experience, and should not be interpreted as advice or a recommendation.

02

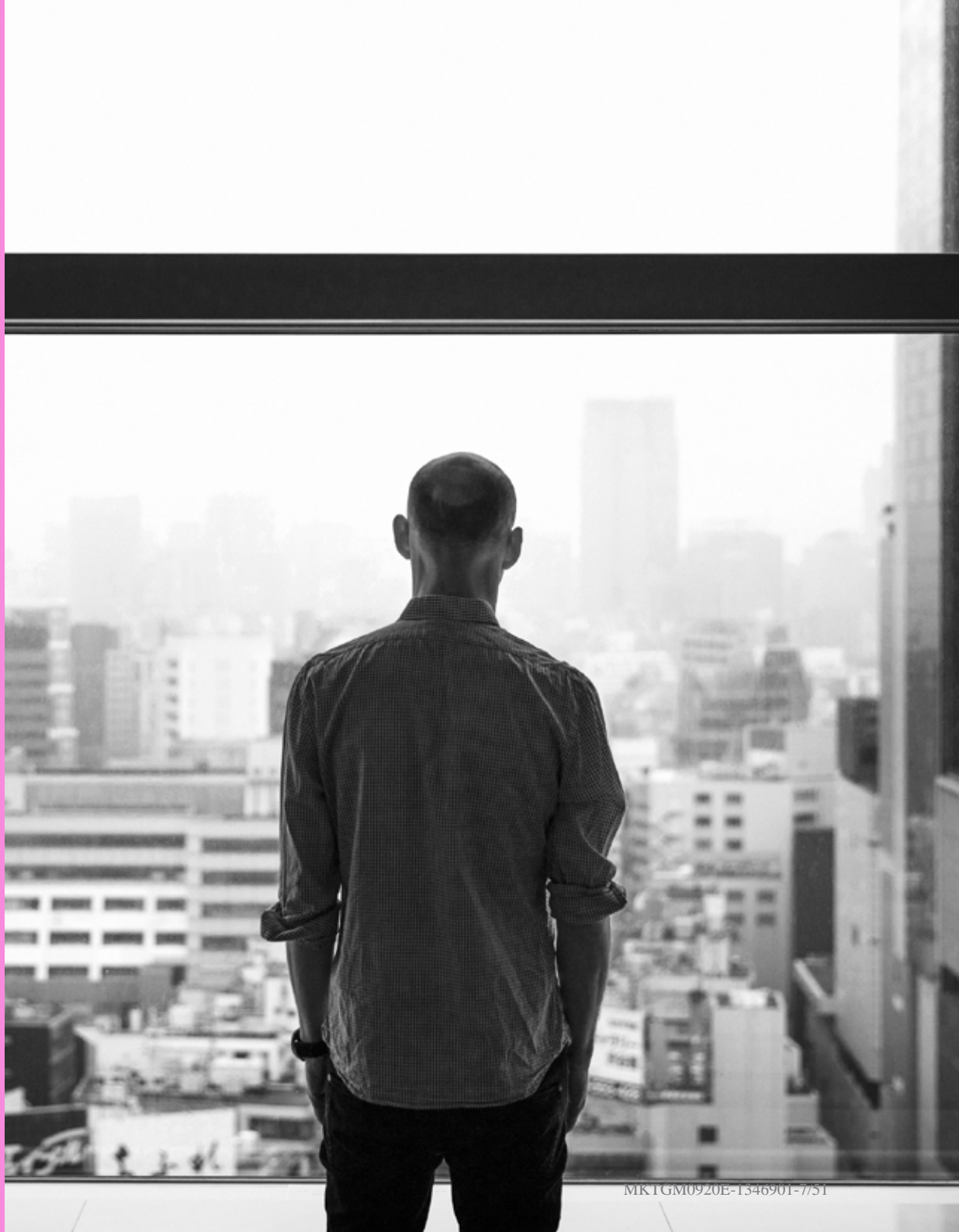
Expressing short-term market views

THE CHALLENGE

How can I manage my portfolio to express short-term market views?

Expressing differentiated views across countries, sectors, factors, durations or credit qualities is often a key value proposition among portfolio managers, in an attempt to differentiate from both the benchmark and their peers.

In heightened market volatility, the importance of tactical portfolio overlays is ever more in focus, as investors attempt to harness short-term gains as well as limit potential drawdowns.

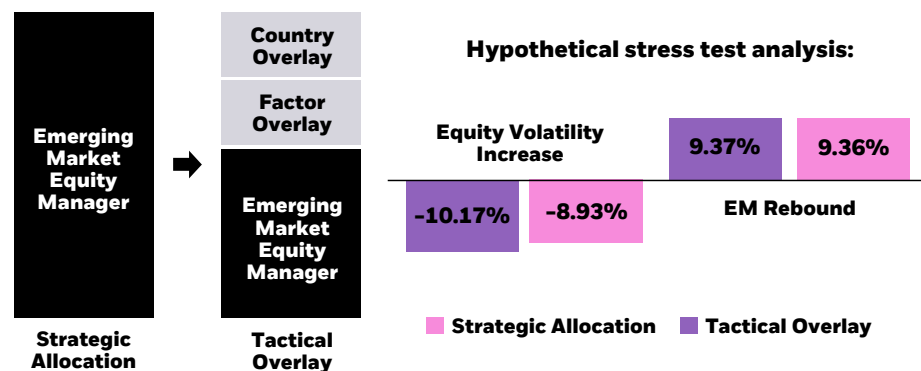


02

Expressing short-term market views

The action

Stress testing can help to identify ways to improve portfolio outcomes. BlackRock's range of scenarios, based on simulations of possible outcomes of macro and geopolitical events, can help managers to conceptualise resultant economic, market and portfolio alpha impacts.



Source: BlackRock, as at May 2020. For illustrative purpose only.

Equity Volatility Increase represented by a move in the VIX index by 16.5%. EM Rebound based on MSCI Emerging Markets Index up 10%. Index returns are for illustrative purposes only. Index performance returns do not reflect any management fees, transaction costs or expenses. Indices are unmanaged, and one cannot invest directly in an index.

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The outcome

The client re-evaluated the instruments that they were using to express differentiated, tactical views. The incorporation of ETFs into their portfolio construction process enabled them to become more nimble with their tactical asset allocation views.

Why indexing?

The liquidity of the ETF market, helping to minimise costs of accessing these exposures, led the client to increasingly utilise these tools to dynamically tilt the portfolio in accordance with market events.

03

Building a defensive portfolio

THE CHALLENGE

How can I build
a more defensive
portfolio without
too much cash?

Whether it is to finance derivatives, to de-risk, or simply while waiting for the right investment opportunity, cash is commonly held across portfolios.

When liquidity is not required on a T+0 basis, holding cash can result in an unnecessary drag on performance.

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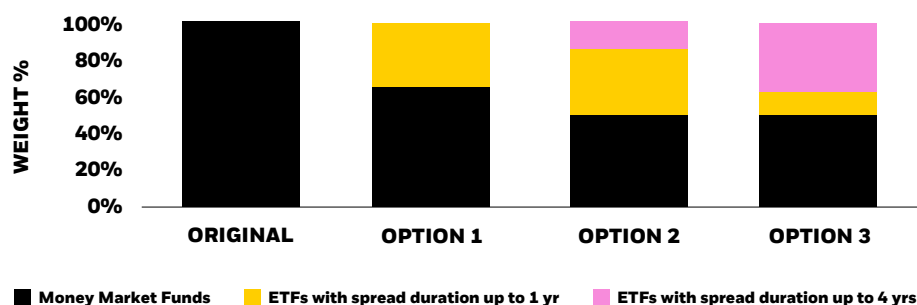
03

Building a defensive portfolio

The action

With the ability to take on slightly more credit and/or duration risk, blending across investment tools and looking beyond money market funds can help to bring portfolios closer to their yield requirements.

Cash and equivalents allocations:



	ORIGINAL	OPTION 1	OPTION 2	OPTION 3
YIELD	-0.48%	-0.21%	0.03%	0.09%
CREDIT QUALITY	A+	A+	A-	A-
SPREAD DURATION	0.1	0.3	0.9	1.3

Source: BlackRock, as at 30 June 2020. Currency = EUR. Currency = GBP. Spread duration in 0.1, 0.3, 0.9 and 1.3 years. For illustrative purpose only.

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The outcome

The growth in the liquidity of the ETF market provided assurance that the client would be able to quickly execute large trade orders when required, without paying a large spread or risking not being able to liquidate.

Why indexing?

The client invested some money in short-duration fixed income ETFs, to help increase net yield without significantly changing their overall risk or liquidity profile.

04

Managing allocations to alternatives

THE CHALLENGE

How can I manage my alternatives allocation within my portfolio?

Investments in private markets are becoming an increasingly core component of asset allocations for investors. With this comes the need to manage cash more efficiently to prevent cash drag on performance, as asset managers deal with capital calls, expiring vintages, or due diligence before an investment is made.

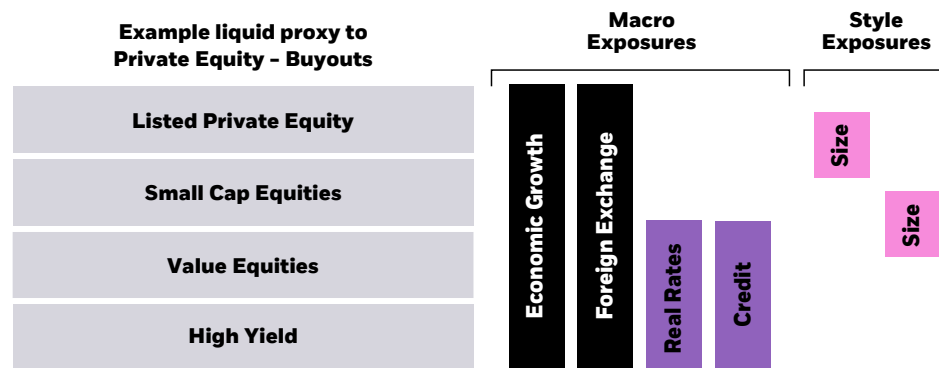


04

Managing allocations to alternatives

The action

ETFs could act as an interim vehicle for holding cash, while allowing investors to gain access to the broad economic exposures of the asset class before the capital calls are made.



Source: BlackRock, as at May 2020. For illustrative purpose only.

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The outcome

While risk-return profiles and the idiosyncratic nature of private markets differ from public markets, macroeconomic and style exposures driving these investments may be more similar.

By using ETFs as an interim vehicle for their private market investments, the client could gain earlier access to the targeted exposure, with a beta of 0.93.*

***Source:** BlackRock, Morningstar, Cambridge Associates. Beta measured against the Cambridge Associates Global Buyout Index, calculated using quarterly returns from 31/12/2009 - 31/12/2019.

Risk: There can be no guarantee that the investment strategy can be successful and the value of investments may go down as well as up.

Why indexing?

The liquidity of the ETF market enabled ETFs to be used as tactical investments solutions, to help manage cash flows and allow the portfolio to remain more closely aligned to its strategic asset allocation.

05

Deciphering factor-driven returns

THE CHALLENGE

How can I avoid paying too much for factor-driven returns?

It is important to differentiate between active returns and alpha returns. Active return, or excess return above a benchmark, is not just driven by alpha (security selection and factor timing of the manager) but also by factor exposures.

What you see is not what you get, and it is important to understand the sources of returns to ensure that the high fees are associated with 'pure alpha' that cannot be replicated with a low-cost solution.



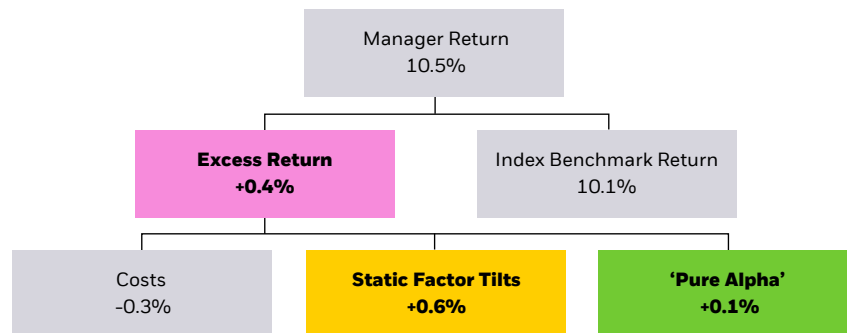
05

Deciphering factor-driven returns

The action

Through decomposing the drivers of returns, we identified that a large portion of the excess returns generated by some alpha-seeking managers could be tied to static exposures from factors, and not from 'pure alpha'.

Example of manager return decomposition



Source: BlackRock, as at May 2020. For illustrative purpose only.

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The outcome

The client opted to reduce reliance on some alpha-seeking managers, and instead take control of their own tactical views by using indexing to intentionally target specific factor and market exposures.

Why indexing?

Recognising that the outperformance was frequently tied to static factor tilts, the client realised that they were potentially overpaying for returns.

By taking a more balanced allocation across index, factors and alpha, the client was able to maximise the efficiency of their risk and fee budget.

Risk: There can be no guarantee that the investment strategy can be successful and the value of investments may go down as well as up.

THE CHALLENGE

How can I adapt my portfolio to fulfil sustainability objectives?

In recent years, environmental, social and governance (ESG) risks and opportunities have become an increasingly important component in the investment decision-making framework for fund managers.

As more and more studies of ESG integration emerge, an increasing number of fund managers are starting to believe that:

- 1) ESG integration can increase the prospect of stable long-term value**
- 2) Sustainability factors can materially influence the risk-return profile of their investments.**

Source: PLSA Made Simple Guide: Environmental, Social and Corporate Governance (ESG), March 2019

BlackRock research shows that sustainable assets could outperform non-sustainable ones in upcoming years, while also being relatively more immune to long-term risks such as climate events.



06

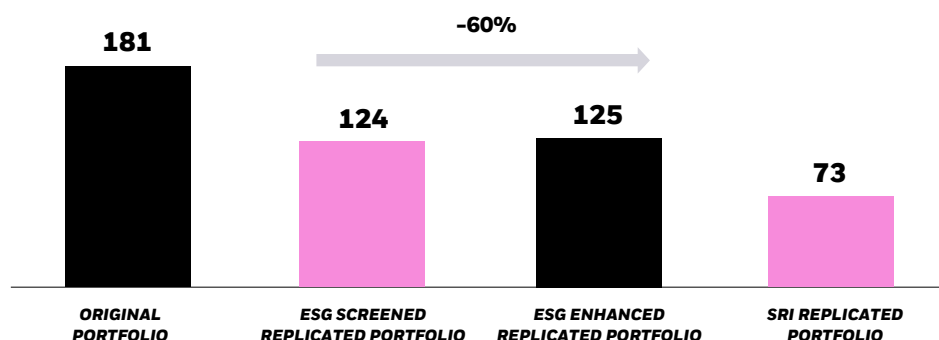
Thinking sustainably

The action

Embedding sustainability ratings and increasingly, capital market assumptions for sustainable assets into the portfolio design phase is an important third dimension to add to the current primary risk and return objective of building portfolios.

The proliferation of index building blocks featuring different ESG criteria is empowering investors to start implementing sustainable decisions into their investment process, and providing them with the opportunity to transform their whole portfolio, beyond the current tactical adoption of products at the fringes.

Carbon Emissions Intensity (Metric tonnes CO2/Sales)



***Source:** BlackRock, MSCI ESG Research as at May 2020. For illustrative purpose only.

Index returns are for illustrative purposes only. Index performance returns do not reflect any management fees, transaction costs or expenses. Indices are unmanaged, and one cannot invest directly in an index.

The outcome

In this example, transitioning the portfolio's strategic asset allocation to sustainable benchmarks of equivalent exposures resulted in a 60% reduction of carbon emissions, which is equivalent to 23 cars driven each year.*

Overall portfolio risk also decreased, which could have been partly driven by the increased exposure to companies that are adopting stronger working practices, and therefore exhibiting greater quality factor characteristics.

Why indexing?

The rules-based approach to defining the universe and standards for ESG characteristics within indexing enables investors to incorporate sustainability criteria in a transparent and low-cost manner while remaining aligned to their broader regional and sector investment views.

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Risk: This information should not be relied upon as research, investment advice, or a recommendation regarding any products, strategies, or any security in particular. This is for illustrative and informational purposes and is subject to change. It has not been approved by any regulatory authority or securities regulator.

The environmental, social and governance ("ESG") considerations discussed herein may affect an investment team's decision to invest in certain companies or industries from time to time. Results may differ from portfolios that do not apply similar ESG considerations to their investment process.

HOW CAN WE HELP?

We know that every investor has different portfolio needs. From technology, bespoke portfolio analysis to full outsourcing, explore the ways BlackRock could help you.

Explore portfolio solutions >

Source: BlackRock, May 2020.

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Asset Owner

- 07 Cash flow management**
- 08 Managing portfolio costs**
- 09 Thinking sustainably**
- 10 Adapting to a lower-yield environment**
- 11 Index your bonds**
- 12 Scheme asset reallocation**
- 13 Transitioning from high yield to high income**
- 14 Alternative investing**

07

Cash flow management

THE CHALLENGE

How can I improve portfolio liquidity and cash flow management?

In a lower for longer environment, with considerably lower yields compared to the historical average, pension funds and insurers are increasingly becoming cash flow negative. The ability to meet liabilities is being challenged.



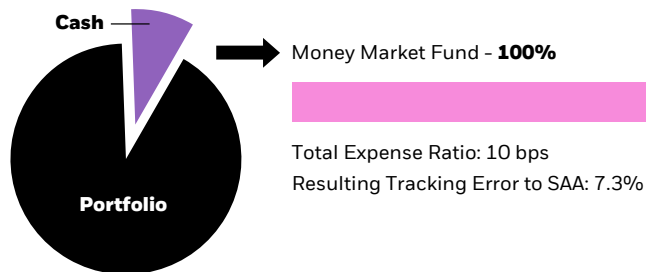
07

Cash flow management

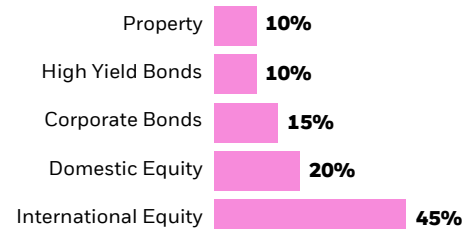
The action

Liquid beta sleeves, constructed using ETF building blocks, help investors avoid holding excess cash, and enable them to stay invested and closer to their strategic asset allocation (SAA) without compromising on liquidity.

Option 1 - Money market fund



Option 2 - 5 ETFs designed to replicate the SAA below



Total Expense Ratio: 16 bps - Resulting Tracking Error to SAA: 1.1%

Source: BlackRock, as at May 2020. For illustrative purpose only.

The outcome

The client replaced a portion of their cash with a combination of ETFs, which were designed to closely replicate their strategic asset allocation (SAA).

By keeping the portfolio in line with the SAA, the portfolio was able to reduce cash drag.

Why indexing?

Understanding that not all liquidity was needed on a T+0 basis, the client was able to take on additional risk to help reduce the funding gap.

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Risk: Diversification and asset allocation may not fully protect you from market risk.

08

Managing portfolio costs

THE CHALLENGE

How can I most efficiently lower the costs of my portfolio?

Regulatory pressures and continuing low yields have increased pressure on pension funds and insurers alike to manage fees and build cost-efficient solutions.



08

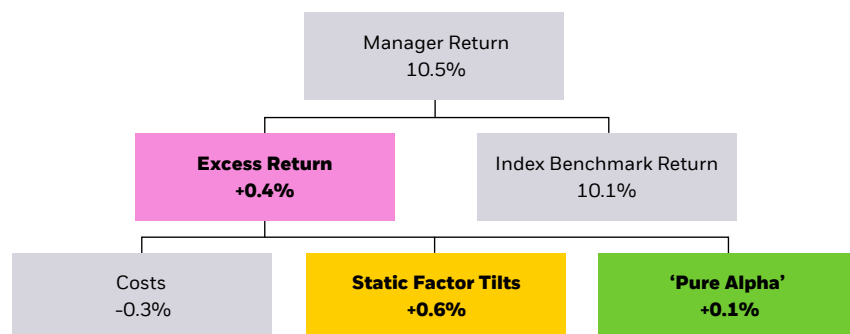
Managing portfolio costs

The action

BlackRock could help by assessing portfolio efficiency and identifying the main drivers of risk and returns.

Identifying where returns are largely driven from broad market exposures and static exposures to factors can help to ascertain where similar outcomes may be potentially replicable more cost-effectively through an index solution.

In this example, while the alpha-seeking manager generated excess returns, much of this was attributed to static factor tilts.



Source: BlackRock, as at May 2020. For illustrative purpose only.

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Risk: There can be no guarantee that the investment strategy can be successful and the value of investments may go down as well as up.

The outcome

The client opted to reduce reliance on alpha-seeking managers, instead intentionally targeting specific factors and index exposures through low-cost index solutions.

Why indexing?

Recognising that the manager outperformance was tied to static factor tilts, the client realised that they were potentially overpaying for returns.

By taking a more balanced allocation across index, factors and alpha-seeking managers, the client was able to maximise the efficiency of their risk and fee budgets.

THE CHALLENGE

How can I adapt my portfolio to fulfil sustainability objectives?

Sustainable investing has come to the fore, with heightened pressure from regulators to ensure that pension funds and insurers incorporate sustainability into investment decision-making.

Pension funds and insurers increasingly need to show that they can not only meet their liabilities, but also that they are making a positive contribution to society.



09 Thinking sustainably

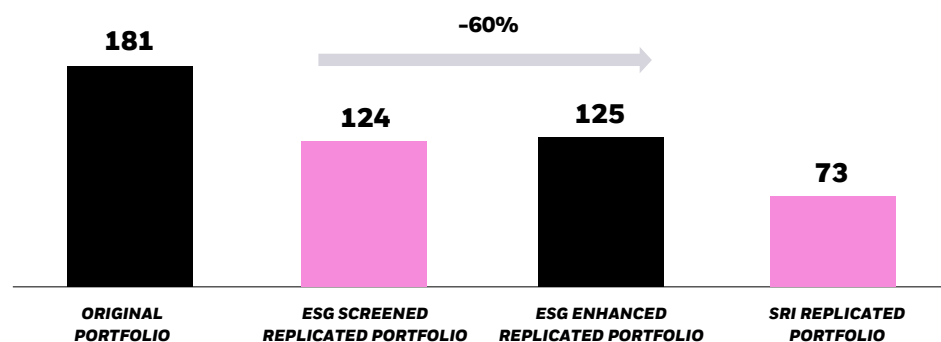
The action

It has become important to embed sustainability ratings and capital market assumptions for sustainable assets as a third dimension to add to the existing primary risk and return objectives.

The proliferation of index building blocks featuring different ESG criteria is empowering investors to start implementing sustainable decisions into their investment process, whilst keeping aligned to their strategic asset allocation and investment goals.

BlackRock is helping investors transition to sustainable investments by both decomposing ESG portfolio scores and building portfolios which are positioned to capture Sustainable opportunities.

Carbon Emissions Intensity (Metric tonnes CO2/Sales)



Source: BlackRock, MSCI ESG Research as at May 2020. For illustrative purpose only.

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The outcome

In this example, transitioning the portfolio strategic asset allocation to sustainable benchmarks of equivalent exposures resulted in a 60% reduction of carbon emissions, which is equivalent to 23 cars driven each year.

Overall portfolio risk also decreased which could have been partly driven by the increased exposure to companies which are adopting stronger working practices, and therefore exhibiting greater quality factor characteristics.

Why indexing?

Notably, different sustainable approaches above are associated with different levels of tracking error. The 'Enhanced' range, for example, seeks both a relatively low level of tracking error as well as a better sustainable profile such as higher ESG score and lower carbon emissions.

The rules-based approach to defining the universe and standards for ESG characteristics within indexing enables investors to incorporate sustainability criteria in a clear, concise and low-cost manner whilst remaining aligned to their investment policy benchmarks.

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10

Adapting to a lower-yield environment

THE CHALLENGE

How can I enhance my portfolio yield to meet cash flow requirements?

Recent market uncertainty and stretched valuations have caused many investors to opt to de-risk by increasing their cash allocation.

However, for long-term investors, who are better placed to weather short-term volatility and downside, the risk of holding excess levels of cash can mean losing out on meaningful performance.

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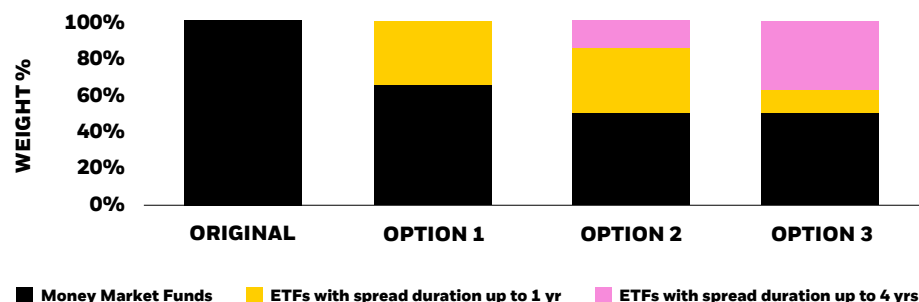
10

Adapting to a lower-yield environment

The action

BlackRock could help build customised solutions that manage portfolio risk while achieving a positive yield and avoiding cash drag.

Cash and equivalents allocations:



	ORIGINAL	OPTION 1	OPTION 2	OPTION 3
YIELD	-0.48%	-0.21%	0.03%	0.09%
CREDIT QUALITY	A+	A+	A-	A-
SPREAD DURATION	0.1	0.3	0.9	1.3

Source: BlackRock, as at May 2020. Currency = GBP. Spread duration in 0.1, 0.3, 0.9 and 1.3 years. For illustrative purpose only.

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The outcome

Blending across product types helped demonstrate that, by taking on slightly more credit and/or duration risk, different yield requirements can be met.

Why indexing?

Understanding that not all liquidity was needed on a T+0 basis, the client was able to invest some money in short-duration fixed income ETFs, which increased yield without significantly changing the liquidity profile and without significantly changing the risk profile of the portfolio.

11 Index your Bonds

THE CHALLENGE

How can I better manage the operational efficiency of a single line bond portfolio?

Many clients opt to allocate towards single bonds in attempt to be selective across duration, credit quality and yield. Yet, managing a number of bonds can lead to operational complexities, and also possible misalignment between the risks intended and that experienced if not monitored in a holistic approach.



11

Index your Bonds

The action

BlackRock first analysed the portfolio using Aladdin® risk factor models and found that the level of risk of the portfolio was significantly different to what the insurer expected, with the majority of the unintended risk coming from euro corporate bonds.

BlackRock ran a comprehensive liquidity and trading cost analysis to show to the client that the most liquid corporate bond ETFs offered trading cost advantages over their underlying bonds due to secondary market liquidity.

Risk: While proprietary technology platforms may help manage risk, risk cannot be eliminated.

Liquidity / trading cost analysis



For illustrative purposes only.

Source: BlackRock, Pre-Trade Tool, as at May 2020.

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Action characteristics

	Bond Port	Bond Port + Indexing
Ex-Ante Risk	2.4%	2.2%
Yield-to-maturity	1.1%	1.1%
Duration	3 years	2.9 years
# Holdings	200-300	100-150
Trading cost	25 bps	17 bps

For illustrative purposes only.

Source: BlackRock, Aladdin® as at 31/01/2020. While proprietary technology platforms may help manage risk, risk cannot be eliminated. Risk management cannot fully eliminate the risk of investment loss.

The outcome

By partially indexing the portfolio, the client was able to reduce the operational complexity of the portfolio and improve trading costs.

Why indexing?

The increased use of indexing could help decrease portfolio complexity, manage spread and rates risk through diversification as well as potentially decrease trading costs.

12

Scheme asset reallocation

THE CHALLENGE

How can I keep better control of my portfolio outcomes?

A complex portfolio does not always make the best portfolio.

In many cases, a portfolio with many different positions can result in a lack of understanding of portfolio risks and exposures, and consequently the potential to miss out on required return targets.

Knowing the main drivers of risk and return behind the portfolio is fundamental to ensuring that portfolios meet their investment objectives.



12 Scheme asset reallocation

The action

BlackRock performed a risk factor analysis on the client portfolio. The study showed that only 20% of the securities captured about 95% of the portfolio VaR (Value at Risk), meaning the portfolio contained redundant holdings.

Leveraging the BlackRock Investment Institute (BII) capital market assumptions (CMAs) to generate a forward-looking risk return estimate on the portfolio we identified that the client's strategic asset allocation was estimated to generate a 2.1% annual return over a 10-year basis, short of its 3.5% required return.

The outcome

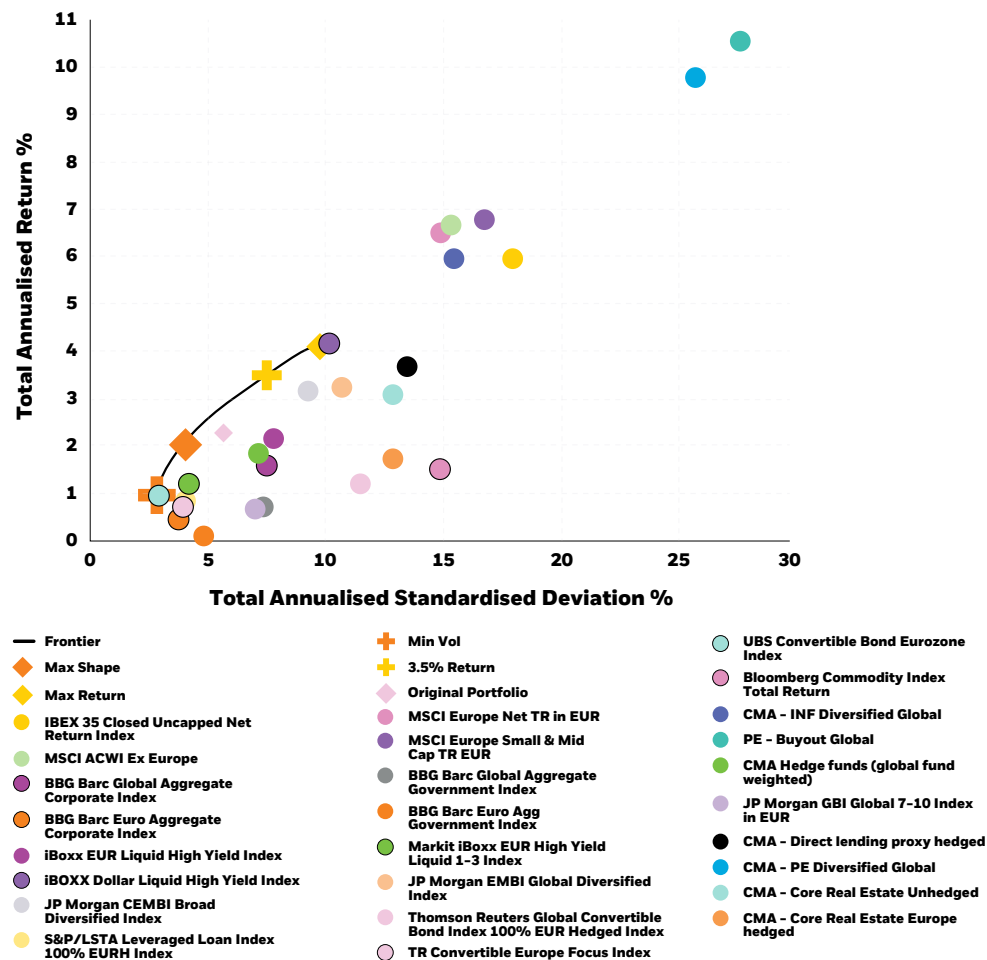
A mean variance optimisation was run using CMAs, which showed that a 3.5% return could be achieved by increasing the allocation to diversified infrastructure and convertibles which also had low correlation to the rest of the portfolio.

Why Indexing

By restructuring the portfolio to add greater use of indexing vehicles within public market exposures, the client was able to free up risk and fee budget to deploy to alternative sources of risk/return that can potentially help improve risk-adjusted returns in the long term.

Risk: Diversification and asset allocation may not fully protect you from market risk.

CMA Optimisation



For illustrative purposes only.

Source: BlackRock, as at May 2020. Time Period is May 2015 - May 2020

13

Transitioning from high yield to high income

THE CHALLENGE

How can I obtain additional income in my portfolio?

A change in market fundamentals, or economic regime, can often results in schemes needing to make substantial asset allocation changes to meet required income, risk or return targets.

Exploring dividend focused indexed products and diversifying sources of risk and income is one way that can help to achieve such objectives.



13

Transitioning from high yield to high income

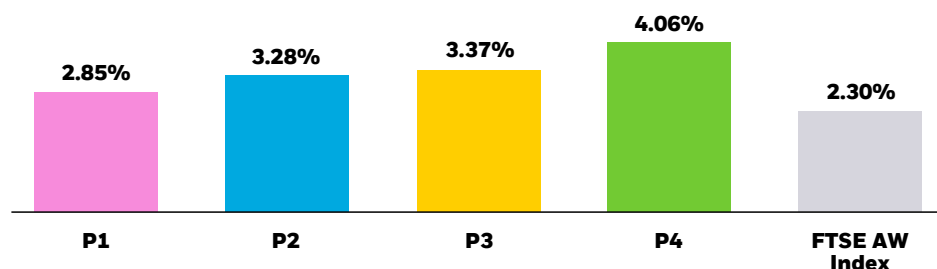
The action

Restructuring a strategic asset allocation requires a multi-dimensional approach, that moves beyond optimising for risk and return, but also considers other metrics such as ESG and income considerations.

BlackRock's approach to portfolio design, leveraging our risk management platform Aladdin, provides clients with the tools and support needed to ensure that portfolios meet investment objectives in the most efficient manner.

In this case, BlackRock was able to find an alternative equity solution, which enabled the client to transition out of high yield exposures and better manage their overall portfolio risk.

Dividend Yield

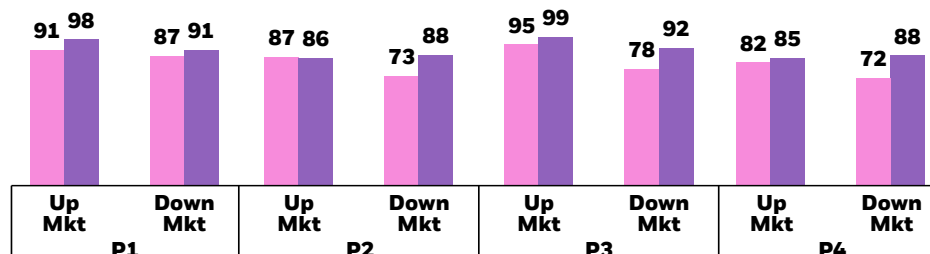


For illustrative purposes only.

Source: BlackRock, Aladdin as at May 2020.

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Up Market and Down Market Capture Ratio



For illustrative purposes only. **Source:** BlackRock, Aladdin as at May 2020. Time Period is May 2015 - May 2020. Calculated using FTSE All World Index as Benchmark.

The outcome

The solutions showed how the client could obtain up to a 77% increase in dividend yield with a 14% decrease in the 2-year historical standard deviation of the portfolio.

Why indexing?

The expansion of index building blocks, beyond their use to access broad market exposures, has acted as an additional toolkit for investors to make more granular investment decisions. In this case, a quality dividend ETF strategy provided a useful solution to help simultaneously manage risk and income needs.

14

Alternative investing

THE CHALLENGE

How can I reduce the effect of the J-curve of alternative investments in my portfolio?

Investments in private markets are becoming becoming an increasingly core component of asset allocations for investors. At the same time, pension funds and insurers need to balance the desire to harvest illiquidity premia with the need to retain sufficient liquidity to meet their liabilities.



14

Alternative investing

The action

As pensions look to increase their exposure to illiquid alternatives within their return portfolios, long ramp-up periods can result in investment outcomes being impacted as a result of waiting solely in cash.

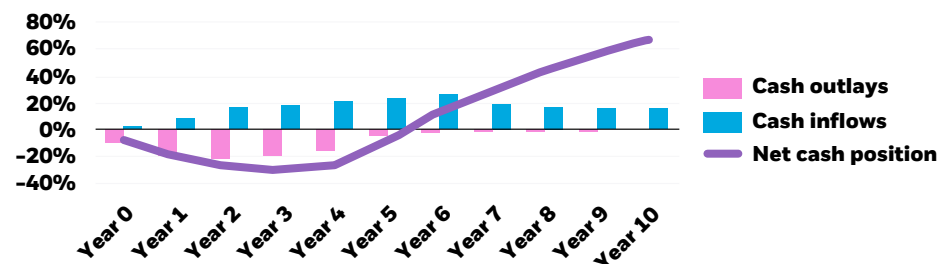
In many instances, we find that clients underutilise risk budgets as a result of this overallocation to cash, whilst awaiting capital commitments.

In this instance, BlackRock was able to create a liquid market complement to the private market portfolio, which allowed the client to be fully invested from year 0 to avoid double and reduce cash drag and mitigate J-curve effect.

BlackRock leveraged our risk management platform, Aladdin, to identify private market macro exposures that could be accessed through iShares ETFs such as economic growth, real rates, credit, inflation and emerging markets.

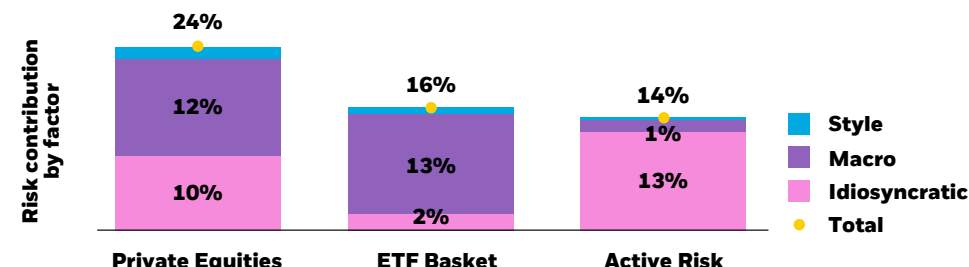
BlackRock created customised baskets of ETFs replicating the macro

The Curse of the J-Curve



For illustrative purposes only. **Source:** BlackRock, as at May 2020.

Example: Private Market Basket



For illustrative purposes only. **Source:** BlackRock, as at May 2020.

The outcome

While risk-return profiles and the idiosyncratic nature of private markets differ from public markets, macroeconomic and style exposures driving these investments may be more similar.

In this instance, the active risk of the ETF baskets demonstrated that the macro exposures in private markets could be replicated to high quality and therefore acted as a good interim vehicle for their private market investments.

Why indexing?

While alternative investments have idiosyncratic risks that cannot be replicated through indexing, certain macro risks such as economic growth or real rates can. Such indexed strategies can offer alternative-like exposure on a temporary basis. The liquidity of the ETF market also made ETFs valuable as tactical investments solutions to help manage cash flows in a more targeted manner while reducing the risk of a funding shortfall.

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HOW CAN WE HELP?

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Source: BlackRock, May 2020.

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Discretionary Portfolio Manager

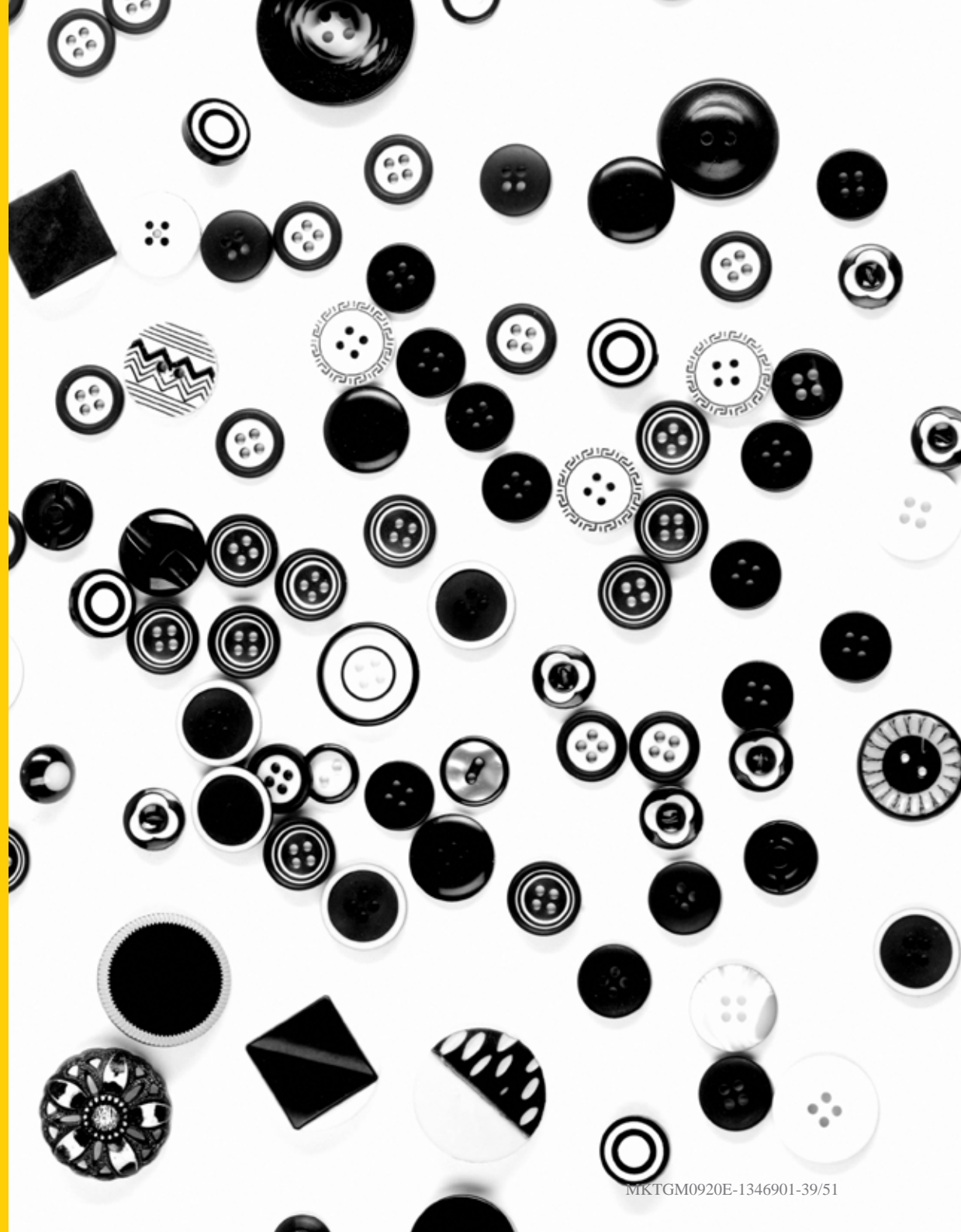
- 15 Managing portfolio costs**
- 16 Expressing short-term market views**
- 17 Building a defensive portfolio**
- 18 Thinking sustainably**
- 19 Deciphering factor-driven returns**

15 Managing portfolio costs

THE CHALLENGE

How can I most efficiently reduce the costs in my portfolio to deliver stronger outcomes?

In an environment of regulatory change and continuing low-yields, wealth managers are increasingly re-thinking their product choices to maximise the efficiency of their fee budget allocation.



15

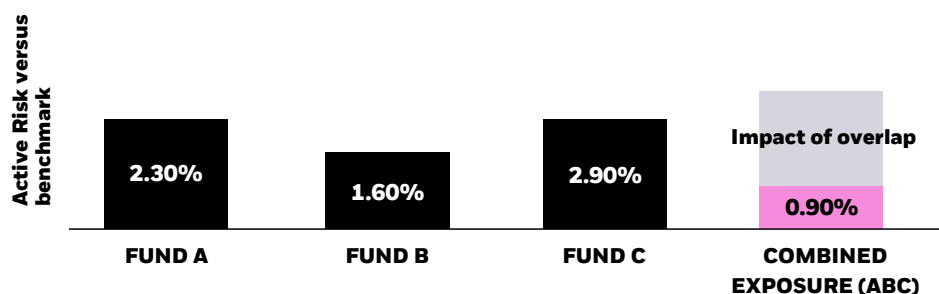
Managing portfolio costs

The action

In order to assess value-for-money within the portfolio, BlackRock analysed the portfolio to determine the main drivers of risk and return.

We found that a large portion of portfolio risk was driven by broad market exposures, and therefore potentially replicable with a low-cost index solution.

Looking deeper into the analysis, on an individual fund basis, alpha opportunities existed but when combined their active bets had negated each other. This resulted in a portfolio which looked much more similar to an index.



Source: BlackRock, as at May 2020. For illustrative purpose only. Chart assesses ex-ante active risk of three active mutual funds with the same benchmark. Combined exposure (ABC) is an equal weighted combination of the three funds.

The outcome

Since the return was largely driven by broad market exposures, the client opted to implement their strategic asset allocation through index strategies.

An indexed core of the portfolio, complemented by a select group of high octane alpha-seeking managers helped increase net return and reduce portfolio costs.

Why indexing?

Indexing is an efficient tool for expressing broad market views.

Due to the more selective investment approach, more time could be dedicated to research per manager leading to increased quality of alpha-seeking managers.

Case studies are for illustrative purposes only; they are not meant as a guarantee of any future results or experience, and should not be interpreted as advice or a recommendation.

Risk: There can be no guarantee that the investment strategy can be successful and the value of investments may go down as well as up.

16

Expressing short-term market views

THE CHALLENGE

How can I manage my portfolio to express short-term market views?

Recent market volatility has prompted portfolio managers to want to express a more differentiated view across potential countries, sectors and factors.

Making tactical portfolio overlays can potentially help to harness short-term gains as well as provide added protection in different market environments.



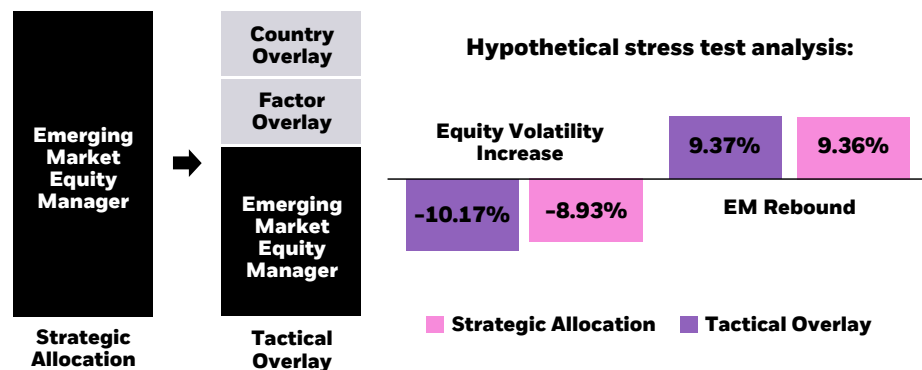
16

Expressing short-term market views

The action

BlackRock can partner with clients to perform stress-testing analysis and assess how the portfolio might perform under different scenarios.

We showcased that, through the use of a tactical overlay using ETFs, the client was able to construct a portfolio that was protected in the instance of a market volatility increase, but remained invested to harness gains in the event of an emerging markets rally.



Source: BlackRock, as at May 2020. For illustrative purpose only. Equity Volatility Increase represented by a move in the VIX index by 16.5%. EM Rebound based on MSCI Emerging Markets Index up 10%.

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Index returns are for illustrative purposes only. Index performance returns do not reflect any management fees, transaction costs or expenses. Indices are unmanaged, and one cannot invest directly in an index.

The outcome

The client re-evaluated the instruments that they were using to capture different sources of return. The incorporation of ETFs in their portfolio construction process enabled them to become more nimble with their tactical asset allocation views.

Why indexing?

The liquidity of the ETF market, helping to minimise costs of accessing these exposures, led the client to increasingly utilise these tools to dynamically tilt the portfolio in accordance with market events.

17

Building a defensive portfolio

THE CHALLENGE

How can I build a more defensive portfolio without too much cash?

Recent geopolitical uncertainty and market volatility have caused many wealth managers to decide to de-risk their clients' portfolios by increasing their cash allocation, resulting in a cash drag.



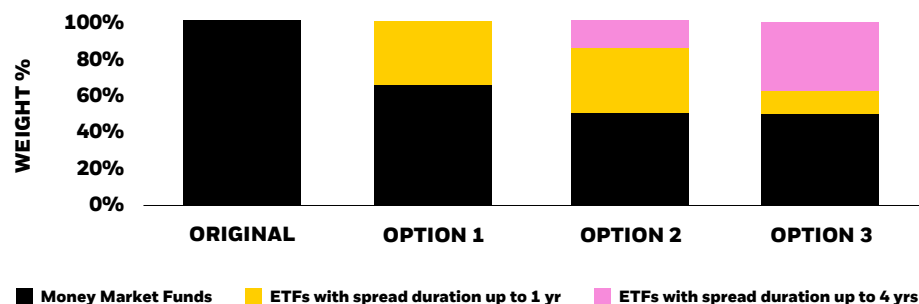
17

Building a defensive portfolio

The action

BlackRock could help build customised solutions to manage portfolio risk while achieving a positive yield and avoiding cash drag.

Cash and equivalents allocations:



	ORIGINAL	OPTION 1	OPTION 2	OPTION 3
YIELD	-0.48%	-0.21%	0.03%	0.09%
CREDIT QUALITY	A+	A+	A-	A-
SPREAD DURATION	0.1	0.3	0.9	1.3

Source: BlackRock, as at May 2020. Currency = GBP. Spread duration in 0.1, 0.3, 0.9 and 1.3 years. For illustrative purpose only.

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The outcome

Blending across product types helped demonstrate that, by taking on slightly more credit and/or duration risk, different yield requirements can be met whilst still providing a degree of portfolio protection.

Why indexing?

Understanding that not all liquidity was needed on a T+0 basis, the client was able to invest some money in short-duration fixed income ETFs, which increased yield without significantly changing the liquidity profile.

THE CHALLENGE

Will incorporating ESG into my investment processes impact my performance?

Investors are increasingly demanding that their investments align with their own values and make a positive contribution to society. This is bringing sustainable investments to the forefront of portfolio construction and establishing sustainability as the new normal in many client portfolios.

Sustainable investing has moved from the peripheral to the core of wealth management investment propositions. This 'new normal' is not only about the ability to prove that you can generate excess returns above benchmark, but also about demonstrating a valid sustainable proposition if managers are to compete effectively for future investments.



18

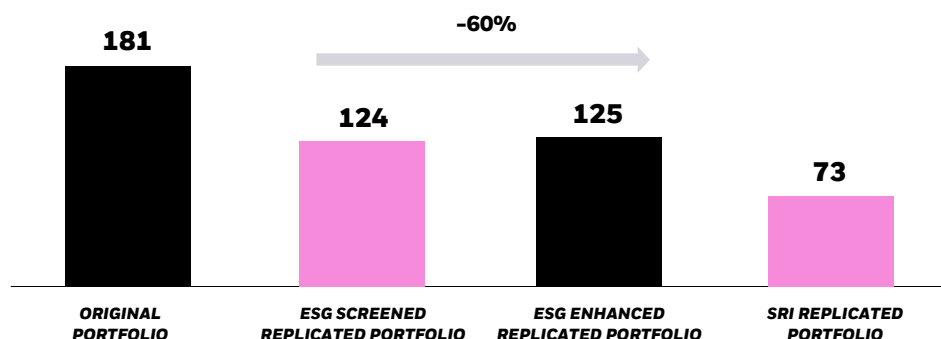
Thinking sustainably

The action

Increased clarity around sustainable performance return drivers, an expanded product set and longer track records are empowering investors to start implementing sustainable decisions into their investment process, while keeping aligned to their strategic asset allocation and investment goals.

Many wealth managers are partnering with BlackRock to gain a better understanding of the ESG metrics on their portfolio, and to redesign portfolios where the incorporation of 'values' does not necessarily mean giving up value.

Carbon Emissions Intensity (Metric tonnes CO2/Sales)



Source: BlackRock, MSCI ESG Research as at May 2020. For illustrative purpose only.

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The outcome

In this example, transitioning from market-cap weighted exposures to sustainable benchmarks of equivalent exposures resulted in a 60% reduction of carbon emissions, which is equivalent to 23 cars driven each year.

Overall portfolio risk also decreased, which could have been partly driven by the increased exposure to companies that are adopting stronger working practices, and therefore exhibiting greater quality factor characteristics.

Why indexing?

The rules-based approach to defining the universe and standards for ESG characteristics within indexing enables investors to incorporate sustainability criteria in a transparent and low-cost manner while remaining aligned to their broader regional and sector investment views.

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The environmental, social and governance ("ESG") considerations discussed herein may affect an investment team's decision to invest in certain companies or industries from time to time. Results may differ from portfolios that do not apply similar ESG considerations to their investment process.

THE CHALLENGE

How can I avoid paying too much for factor-driven returns?

The evolution of factor investing has prompted wealth managers to look closer at the factor exposures within client portfolios for tilts or biases.

These exposures could be intended or accidental as a by-product of fund and security selection. By reviewing the underlying factor exposures, investors can be more aware of what is driving returns and create a more efficient portfolio.



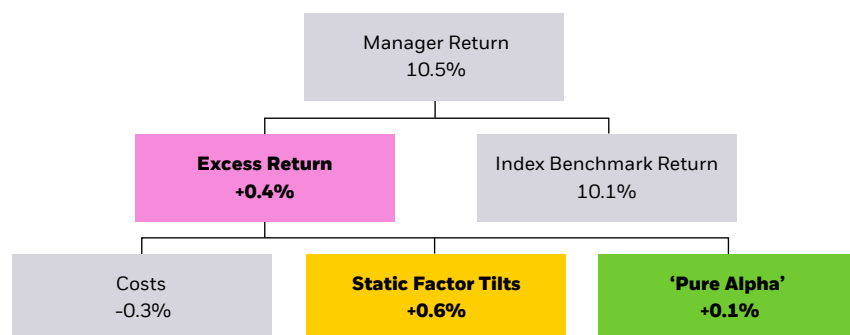
19

Deciphering factor-driven returns

The action

BlackRock can help with decomposing drivers of returns.

In this case, we identified, by breaking down the excess return of some of the client's existing alpha-seeking managers, a large portion of returns generated could be attributed to static exposures from factors, and not from 'pure alpha'.



Source: BlackRock, as at May 2020. For illustrative purpose only.

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The outcome

The client opted to reduce reliance on alpha-seeking managers, instead intentionally targeting specific factors and index exposures through low-cost solutions.

Why indexing?

Recognising that this alpha-seeking manager's outperformance was tied to static factor tilts, the client realised that they were potentially overpaying for returns.

By taking a more balanced allocation across index, factors and alpha, the client was able to maximise the efficiency of their risk and fee budget.

HOW CAN WE HELP?

We know that every investor has different portfolio needs. From technology, bespoke portfolio analysis to full outsourcing, explore the ways BlackRock could help you.

Explore portfolio solutions >

Source: BlackRock, May 2020.

iShares by BlackRock



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