

NEW Consulting Room - Nordic investors' interest in alternatives renewed

By Jan Willers | Published: 01 February 2012

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Nordic investors are looking for more customised products and transparency from alternatives investment managers as interest in the asset class begins to pick up once again, says Jan Willers.

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Although 2011 represented another tough year for alternative investments there are some signs of recovery. There is an increasing, though varied, interest among Nordic investors for some of the various asset classes within alternatives. Investors expect more customised products and more transparency from their investment managers.

Investors indicate the highest interest in private equity, real estate and infrastructure, whereas interest in commodities and forestry is relatively limited. Interest in hedge funds and fund of funds structures continues to be very low.

Last year the share of alternatives decreased from 13 per cent to 12 per cent, which to some extent reflects changes in the value of derivatives. The interest in alternative assets is also affected by capital requirements in relation to the EU's Solvency II directive.

An increasing number of investors expect to maintain an allocation to alternatives in 2012. Finnish investors have the highest allocation in the Nordic region. For example, the Finnish insurer Varma has close to 30 per cent of its total portfolio in alternatives including real estate.

Norwegian investors in general have low allocations to alternatives, restricted to a maximum of 10 per cent by regulators. Swedish investors have made a modest increase in allocation to alternatives whereas the share of alternatives in Denmark has decreased.

Private equity

Private equity is still recognised as an interesting asset class and quite a few Nordic investors stress its attractiveness. The challenges at the moment are liquidity, risk and solvency, which for many investors will dampen the interest for large new commitments to this asset class. In this environment, some investors consider exposing themselves to the overall themes through listed and more liquid securities.

Hedge funds

There is a slight decrease in interest in hedge funds, especially funds of hedge funds. Generally speaking, investors have a stronger preference for single funds if they choose to invest. The interest shown by investors is based in part on the focus on absolute management. Equally, some investors stated that hedge funds are important in creating a diversified portfolio and a number of Danish and Finnish institutional investors indicate that they will be looking for hedge fund managers in the coming period.

We find that the structure of demand for hedge funds is changing and proximity and knowledge are important factors, favouring local providers. An interesting question is whether hedge funds are seeing competition from traditional asset managers – ie investors that do not wish to pay the 2 per cent plus 20 per cent fees and, therefore, look for the same management in more traditional structures supplied by long-only managers or investment banks.

Commodities

Commodities are attracting little interest although it appears that commodities have entered institutional portfolios seemingly on a more strategic basis. Thus, a number of investors use commodities as diversifiers and protection against inflation.

Forestry

Although interest in forestry has increased considerably in Sweden, the number of new expected mandates is still rather low. For some Nordic investors forestry is considered a green investment and this could possibly contribute to increased interest in this asset class going forward.

Infrastructure

Infrastructure remains interesting for many investors seeking inflation protection and predictable long-term cash flows. Investments in alternatives among Danish investors may be further encouraged given the link to the economic, social and governance (ESG) profile the Danish government wishes to promote. By agreeing to sign off on contractual agreements to buy windmill energy for a prolonged period of

time the Danish government aims to ensure that investment in environmentally-friendly alternative assets are less risky. Likewise public-private partnerships attract some attention and some Danish investors have shown interest in such agreements.

Real estate

Direct investment dominates real estate investments and the majority of investors so far invest locally. However, going forward investors are interested in a greater internationalisation of investments in real estate and an increased exposure to fund structures. Real estate investments can be affected by ESG interests as there is increasing demand for green/environmentally-friendly property not least from public organisations. The increasing interest in real estate is reflected in the expectations to future mandates and a number of the Nordic investors expect new mandates on real estate.

Investment in real estate internationally remains somewhat unfamiliar to some investors and therefore requires greater assistance from the managers.

Investors are looking for greater expertise from their alternative investment managers and signs that managers are attuned to the country specific requirements when investing in alternatives. Due to the size of the internal organisations, a number of investors find it difficult to allocate adequate resources to the management of alternatives knowing that performance depends critically on the resources invested. Liquidity and exit strategy are also factors that are considered relevant and, likewise, transparency is key to investors.

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