Foreword

It is a pleasure for me to present this book devoted to the investment management policy of institutional investors, which a group of friends and colleagues have written with great dedication and expertise, providing a methodical and in-depth perspective of a multifaceted topic that is in continuous evolution.

The book is composed of four parts. The first one analyses the different types of institutional investors, institutions which, with different objectives, professionally manage portfolios of financial and real assets on behalf of a wide variety of individuals. The development factors and benefits for the financial system generated by institutional investors are identified, and a comparison is made at the international level. The first part goes on with an in-depth analysis of the economic, technical and regulatory characteristics of the different types of investment funds, assuming the perspective of a European Union investor. Management strategies, restrictions to investment policies, public documentation and charges of investment funds are explored. This section also analyses other types of asset management products which have a high rate of substitutability with investment funds and represent their natural competitors.

The second part of the book identifies and investigates the stages of the investment portfolio management, dividing the investment process into the following stages: the identification of the objectives and the constraints of the investment policy, the formalisation of the investment strategy, the implementation of the financial strategy, the periodic rebalancing of the portfolio and the assessment of results and risk control. Given the importance of strategic asset allocation in explaining the *ex post* performance of any type of investment portfolio, this section provides an in-depth analysis of asset allocation methods, illustrating the different theoretical and operational solutions available to institutional investors. This section focuses on the concepts and applications of traditional approaches to asset allocation, based on mean-variance optimisation, but also deepens the new risk-based approaches for asset allocation, which eliminate estimation risks associated with the traditional approaches. Finally, the second part concludes with a presentation of the methods and instruments for portfolio selection available to institutional investors for a more aware identification of the "optimal portfolio", taking into consideration management objectives and constraints.

The third part describes performance assessment, its breakdown and risk control. The first step in performance assessment is the calculation of return, with the identification of the most appropriate measure among the different methods of calculation available. Performance evaluation requires then the identification of the risk of an investment portfolio, in its different forms of absolute, asymmetric and relative risk, and the calculation of the related risk-adjusted performance measures, which will enable to assess the efficiency of the asset manager with respect to the benchmark, the competitors and the *ex ante* risk limits. When comparing the performance of competitors, it is essential that homogenous peer groups be created, made up of portfolios with the same management approach. To this end, the most common operational solution is to create a peer group based on the investment style, by using a deductive approach founded on the so-called returns-based style analysis. This section provides alternative methods and utilisation rationales of style analysis. In the case of non-indexed portfolios, an in-depth *ex post* performance assessment also requires the evaluation of the asset manager in terms of the ability to realise effective stock picking and market timing activities. For this purpose, this section presents the most appropriate performance attribution model aimed to shed light on those management choices that generated the gap between the overall result of the portfolio and the benchmark, breaking down relative performance into its determinants and attributing it to the various factors that contributed to its generation.

Finally, the fourth part deals with the subject of diversification towards alternative asset classes, identifying the common characteristics and their possible role within the framework of investment management policies. This section analyses hedge funds, identifying their operational characteristics, management strategies, the regulatory framework and the specific performance assessment techniques. The distribution of the hedge funds returns highlights some statistical anomalies that compromise the validity of normality assumption, which is a necessary condition for the application of classic performance measures. The section continues with a complete and exhaustive analysis of the other types of alternative investments: private equity, real estate, commodities and currency overlay techniques. A common characteristic of these alternative asset classes is to have returns that are often uncorrelated with those of traditional asset classes, although the direction and intensity of the correlation varies greatly over time and according to the specific category of alternative investment.

I believe it is worthwhile to highlight three strengths that enrich this work and make it an easy reading and of interest to a wide audience: First, an abundance of up-to-date data and numerical and graphic illustrative tables. This is a very important aspect that facilitates the understanding of even the most complex concepts. Second, the ability to analyse frontier themes in relation to investment management, without underrating the fundamental concepts that lie at the basis of the most advanced research. This feature makes the book of value and of service to experts, who are interested in cutting-edge models and techniques, and also to those who are less experienced on the subject. Lastly, there is the meticulous work done by the editors, who, thanks to the logical coherence and sequence of the subjects, have succeeded in the difficult task of making a book written by different qualified authors comparable to a manual written by a single author.

To conclude, in its thorough and precise analysis of all these subjects, the book edited by Ignazio Basile and Pierpaolo Ferrari is a useful and effective tool for tackling the topic of the investment management policy of institutional investors.

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