Winning with defence

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■ In defensive investing, low-volatility strategies provide portfolio stability and resilience amid market uncertainty

■ Asia and EMs' attractive valuations look compelling, positioning them well to attract capital

"ATTACK wins you games, defence wins you titles." – Sir Alex Ferguson.

With Premier League clubs playing their pre-season fixtures across Asia recently, the importance of an effective defence could be seen in full play.

Whatever a football team's formation, every successful strategy includes defenders.

Defenders provide stability, shielding against turbulence and unexpected threats and ensuring the team remains effective under pressure.

In much the same way, a defensive investment allocation, such as in a systematic low-volatility strategy, acts as the anchor of a portfolio, offering resilience across a wide range of market conditions.

A messy pitch

We have gone past half-time, and global equity markets have navigated a turbulent eight months of the year, characterised by alternating risk-on and risk-off sentiment.

The period was shaped by tariff uncertainties and subsequent deals/extensions, policy developments such as the "One Big Beautiful Bill Act", geopolitical tensions in the Middle East, and a better-than-expected US corporate earnings season.

More recently, signs of cracks in the US labour market and President Donald Trump's tariff announcements caused the S&P 500 to fall 1.6% on Aug 1, the most negative since May 2025.

Uncertainty remains a central theme in global markets.

Uncertainty persists around policy direction, the outcome of trade tariffs and the trajectory of economic growth.

While US corporate earnings have been strong, data suggests that this uncertainty is now filtering through to corporate earnings.

Since the beginning of April, "uncertain", "uncertainty" and "uncertainties" have appeared about 3,100 times in corporate earnings calls, conference presentations and related events, according to transcript analysis compiled by *Bloomberg*.

This marks the highest quarterly count in over two decades, surpassing even the peaks of the Global Financial Crisis in 2008 and the Covid-19 pandemic in 2020.

Clearly, the level of uncertainty continues to rise.

Against this backdrop, Asian and emerging market (EM) equities have outperformed the US and developed market equities.

With the Dollar Index down 9% year-to-date, a trend that is historically supportive of EM assets and expected to continue, Asia and EMs' attractive valuations look compelling.

This positions them well to attract capital seeking diversification from US-centric portfolios.

Playing active defence

Amid the volatility, Asian markets are becoming increasingly concentrated, with the effective number of stocks in Asia Pacific ex-Japan now well below their long-term average.

The "effective number of stocks" helps us to understand how diversified a market index is.

It is calculated as the inverse of the Herfindahl-Hirschman Index (HHI), a commonly used measure of concentration.

The higher the HHI, the lower the effective number, the more concentrated the market index.

Taiwan, in particular, stands out with just three effective stocks.

This growing concentration highlights the pressing need for diversification and reinforces the value of active management in Asia.

As such, for investors with existing exposures in Asian equities or looking to increase their allocations, a systematic low-volatility strategy appears well suited for volatile times such as these.

Rather than chasing short-term fads which could lead to over-concentration in portfolios, a systematic low-volatility strategy is based on a long-term investment thesis which is grounded on the statistical average of sound investment principles, specifically, the low-volatility anomaly.

This anomaly, coupled with refinements introduced by practitioners, suggests that stocks with lower price fluctuations, attractive dividend yields, and multi-factor alpha characteristics tend to deliver superior risk-adjusted returns over time.

Data of over more than 24 years supports this – the rolling 12-month returns of an Asian-focused low-volatility strategy, proxied by the MSCI AC Asia Pacific ex-Japan Minimum Volatility Index, have consistently outperformed the broader market during periods of market stress, as well as during periods of modest or steady gains.

This performance holds across diverse market scenarios, from declines of minus 20% to gains of plus 20%.

Notably, the low-volatility style has a greater than 50% probability of outperforming the broader market when the market's returns range between plus 10% and plus 20%, demonstrating the strategy's robustness even in moderately bullish environments.

Scoring with stability

While year-to-date equity market rallies have been narrow, and skewed towards high-growth, high-volatility stocks, the recent market sell-off in early August and the potential for a period of range-bound trading highlights the enduring importance of defensive allocations in investor portfolios.

Just as defenders in football teams are key in securing victories, low-volatility strategies play a vital role in helping portfolios weather market turbulence by mitigating downside and delivering consistent returns over time.