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Investors scouring financial markets for new ideas

First-ever Nordic Investment Managers Forum a resounding success

In a first-ever event, five leading Scandinavian asset managers gathered for a public discussion of key market trends and investment themes with a select group of professional investors. The premier Nordic Investment Managers Forum in Luxembourg held at the historic Neumünster Abbey was attended by more than 60 professional investors. It addressed current issues and new ideas, ranging from changing portfolio structures, technological innovation and the negative interest rates in Euroland to developments and opportunities in Eastern Europe.

"There has been much talk about a big rotation from fixed income into equities but our analysis of global financial market data has revealed that while a rotation is under way, it's moving in a different direction than many analysts had expected. Instead of stocks, holdings of low-yielding government bonds are being replaced with other fixed income instruments as reflected by the trends we have all observed in high yield, emerging market debt, total return strategies and so on. There is even a considerable amount of cash in many investors' portfolios because of their aversion to risk. So we have not yet witnessed a significant rotation from bonds into stocks." Those words by Angus Foote, Head of Citywire's Global Editorial Team marked the opening of the conference. He went on to note that many fund managers were methodically analyzing the allocation of portfolio assets given the implications on future returns: "Asset allocation will separate the winners from the losers during the next leg of the cycle so it's important to seek and share new ideas, debate their merits and find new ways of generating alpha for investment portfolios."

The first Nordic Investment Managers Forum in Luxembourg was an insightful and interesting platform for new and exciting ideas. Danske Invest, Sparinvest, East Capital, Origo and DNB Asset Management each sent one portfolio manager to the Forum to present their views and ideas.

Global outlook

Kim Asger Olsen, a fund manager and the Managing Partner of Origo, spoke about global developments. He gave a self-critical portrayal of economists, likening them to entertainers whose job is to keep people from falling asleep before the real show starts: "Economics is technically a science but 95% of economic forecasts 12 months out are wrong. Forecasts are more reliable when they refer to the next three months or over a 15 year period. With a 12 to 18 month time frame there are just too many unpredictable disruptive factors." Olsen also mentioned Citibank's Global Economic Surprise Index. The roughly 500 economists it tracks are often surprised by actual developments, they are often overly optimistic and not even the average forecast turns out to be correct most of the time.

One trend was sure however: "A major realignment is now under way in forex markets. The euro had been overvalued for a long time and now that it's weakening it should give Europe's economy some support." Olsen pointed out that Europe's GDP was not yet back to where it was in 2007, whereas the USA is now in its fifth year of expansion. Europe's banking system in his opinion is dysfunctional and many are still struggling with the non-performing loans on their books that should have been written off years ago. The US, by comparison, chose more constructive policies, by being more resolute in tidying up bank balance sheets, cutting back less on government spending and by pursuing a more expansive monetary policy. Olsen therefore expects big moves ahead for the US and European currencies. In his opinion, the ensuing market movements will not make the tedious job of allocating between asset classes any easier in the coming 12 months. Sadly for investment professionals, whereas macroeconomics always wins in the long term, it usually does not help much in the short term, especially when the major economies are on different tracks. This calls for a more flexible approach to asset allocation, taking into consideration market dynamics and market risks, and a heightened readiness to react in a situation where the global economy is about to switch gears.

Absolute Return: Taking advantage of structural change

Structural changes are constantly happening around us and according to Danske Capital's portfolio manager Jens Wiberg Larsson "creative destruction is increasingly shaping the economy in Europe". These changes include the globalization of production and purchasing, demographic change that is affecting savings and consumption patterns, the spread of social networks and the global exchange of know-how and technological developments. There are many signs that structural change is accelerating, creating new business opportunities as well as destroying or breaking down old businesses. His advice to investors was to create a portfolio that will adapt to this.

"We believe that our investment approach best captures the impact of structural changes on stock prices," says Larsson. "We identify various investment strategies and invest in companies that are expected to win or lose from the structural changes we see around us." Co-manager Klaus Röpke says that "two interesting strategies where we see a lot of changes are Big Data and Wireless World." Big Data provides advanced hardware and software that different industries can use to process more data in less time. Transferred to the oil industry, this means for example that seismological studies can be used to give companies searching for oil valuable, reliable data at less cost. The use of modern information technology improves oil discovery rates while the oil companies reduce their costs and increase their profits. Larsson concludes: "Going forward we want to continue to create alpha from the significant technological changes that we are observing and that will have an impact on Western economies in the coming years." Looking at the sectors bets, IT is by far the largest single sector with a 43.6% weighting, followed by the financial sector with 21.6% as of end of August 2014.

Tech sector on the advance

Risks and rewards in the tech sector were the focus of the presentation given by Anders Tandberg-Johansen, DNB´s Head of Global Technology Equities and portfolio manager of the DNB Technology and DNB TMT Absolute Return funds. He presented six mega trends to show where and how money would be made in the new digital era. One was the Internet. Internet access will eventually be universal but today only 40% of the world's population can go online. The global spread of the Internet will spawn many business opportunities such as games, casinos, advertisement, money transaction services and taxi companies, all of which are destined for rapid growth with strong tailwind from mobile devices. More change will come to the media landscape in 2015. As Tandberg-Johansen pointed out: "Children already spend more time online than they do watching television; the most widely viewed channel in Norway today is YouTube."

He warned about dangerously high valuations in the Internet and cloud computing sector though. These investments initially generated profits for many players but then tumbled deep into negative territory. "Most of these stocks have not recovered from their losses," says Tandberg-Johansen. Nevertheless, his portfolio's performance shows that tech stocks are an interesting place to be: Many of the positions he has taken have delivered double-digit returns. Industry titans such as Google and Apple offer solid fundamentals and good growth momentum and their big difference to the high-flyers is not necessarily on growth but rather their much lower valuation levels. "Google is well positioned in all of the mega trends," says Tandberg-Johansen. The overall outlook for the sector is positive because infrastructure deficits must still be tackled and promising business opportunities lie ahead, for example in the healthcare sector or in retailing.

Arguments for Eastern European markets

Aivaras Abromavicius, a partner and member of the portfolio team at East Capital, spoke on the theme "Eastern Europe from a broader perspective". Abromavicius emphasized East Capital's broad coverage of the Eastern European investment region with its Eastern European fund, which covers 20 countries as opposed to the 6 countries in the MSCI Eastern Europe index. Focusing on the Russia-Ukraine situation with a very local touch, being himself based in Kiev, Abromavicius also explained how this year's events have affected the market: investors have shunned consumer companies and the weak ruble is benefiting exporters, hence a very difficult market situation. But he also gave a rather positive outlook for the Russian market, which East Capital still sees as very interesting long term due to low valuations, high dividend yields and growing companies. The philosophy of East Capital is to have a long term bet on the development of the local consumer and he confirmed that East Capital intends to continue with this focus despite short term market reactions. “The average earnings growth of the 12 consumer companies that we have in Russia is at 18% for 2014 and 25% for 2015.”

Abromavicius also mentioned that the frontier exposure of the fund added significant alpha last year and drew attention to investment opportunities in the Baltics and the Balkans and their favorable economic outlook. As an example, Lithuania’s GDP per capita has gained an impressive 55% during the country’s 10 years of EU membership, despite the financial crisis in 2009, and East Capital believes growth will continue across the Baltics.

“As for the Balkan markets, we believe that some of them may continue to outperform as they are still down by between 56% and 87% from the peak in 2008, despite the positive performance of between 7% and 49% already seen in 2013”. East Capital also has a high active part in their portfolios and likes off index exposure to private companies that offer better corporate governance, better diversification and higher growth.

The value bond strategy

With European savers’ returns threatened by negative interest rates, there has been heightened interest in finding attractive returns from low risk investment vehicles. Henrik Lind Grønbæk, Managing Director at Sparinvest S.A., spoke about Sparinvest’s solution – a short duration, fixed maturity high yield bond strategy which it has brought to market in recent years in the form of a series of funds. These funds have a common approach of seeking to lock in high yields from mispriced corporate bonds issued by quality companies with strong assets and low indebtedness.

Grønbæk explained how Sparinvest’s ‘Value Bonds’ strategy has, over the past 9 years, historically proven very successful in terms of achieving lower than average default levels within portfolios. In a fixed maturity fund it is default avoidance that permits the uninterrupted collection of coupons until maturity whilst the short duration provides some protection against interest rate movements. The latest fund in the series, Sparinvest High Yield Value Bonds 2018, aims to pay investors an average annual return of 5% (before fees) until it reaches maturity in December 2018.

“Sparinvest is on a mission to keep investors supplied with vehicles offering attractively high fixed-income returns at a time when they are very hard to come by,” said Grønbæk. “High yield pickings are getting thinner and thinner on the ground, but we still find attractive bonds by looking for value off index. By buying now, and if interest rates and default rates remain low, we can spend the next four year simply collecting the coupons.”*

Presentation documents can be viewed at www.nimf.lu. If you would like more information please contact the following persons:

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** Projected returns are indicated before charges and based on current yield levels taking the historic default and recovery rates experienced by running the strategy.*

Past performance is no guarantee for future performance.