The Difficulty of Sticking to Your Guns

Stockholm (HedgeNordic) – Hindsight is always 20/20 but it is harder to look ahead with the same certainty. A safe bet is perhaps to say that the next decade will be different from the previous even if some people are always adamant that plus ça change.

One of those that argues that while every decade has its charms, a lot of things can change in 10 years, particularly when it comes to economic and investment environment is **Torbjörn Hamnmark, head of strategic asset allocation at AP3**, one of the Swedish national buffer funds. At least keeping an open mind about would be prudent, he suggested.

“The next decade will be determined by different fundamental drivers compared to the decade since the global financial crises, be it Modern Monetary Therory (MMT) or a different political landscape,” he said.

The dent left by the crisis over a decade ago was enormous not least because of the subsequent quantitative easing (QE) programmes adopted by central banks around the globe. “Market forces were basically put out of play and were not allowed to function in their natural rhythm because of extreme monetary policy,” he said.

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This disrespect for the economic machine has left a lot of stones in this well-oiled machinery such as tradewars and continued extreme monetary policy. “It is not these policies, as a result of politicising the central banks that have improved the lives of the average person in the past decades. It is globalisation and digitalisation that has enabled this economic boom,” he said.

This environment that some have called the ‘new normal’ with QE and historically low interest rates has in particular had an impact on global macro managers, trying to navigate these waters and questioning whether or not these are permanent or temporary changes.

To many global macro strategies encapsulate the essence of hedge funds because of the raft of instruments they utilise in trading global markets combined with their ability to use leverage and go long and short. This is also the hedge fund sector that often hits the news, for good or bad and where careers are made and ruined. Of course this is a superficial look and global macro managers are no more homogenous than any other strategy and the dispersion in the field is not only noticeable from their returns but also the varied investment philosophies adopted.

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“Macro managers are fundamentally dependent on the fact that the market makes mistakes. This natural market mechanism has not been allowed to play out for the past decade or more. Even if you were the smartest global macro manager in the 10 years prior to the crisis, it would not have worked as long as the central banks refused to let the market move in a natural way”, Hamnmark said.

One of the reasons for adhering to the extreme monetary policies, according to Hamnmark, is the obsession among central banks, such as the European Central Bank, with hitting their inflation targets ‘no matter what it takes’ despite having a 20-year low unemployment level, he noted.

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This has not made it for an easy environment to be a global macro managers, he said. “Low interest rates and difficult trends to predict or follow combined with the fact that you are stuck with your choices is a hard place to be. It is quite difficult to stick to your guns and models and at the same time keeping an open mind in a changing world,” he said.

Hamnmark said AP3 is less dependent on external macro hedge funds than 10 years ago. Poor performance and high fees lead to a reduced exposure and more selfreliance. Another change that AP3 is making is leaving factor exposure behind and focusing instead of asset classes, he noted. “The market is quant driven with fewer people and more machines. This leads to better decisions and a more efficient market. You have to accept this development. You have to have a clear allocation, which is a very important part of the information flow,” he said.

A decade ago AP3 moved into factor investing or risk buckets where the entire portfolio was viewed through risk factors and factor risks, thereby dividing the portfolio into risk classes instead of asset classes. AP3 is now stepping away from this to a degree, partly because of the difficulty of building a diversified portfolio which could be a challenge for the future even if it is not today, Hamnmark said.

Having built diversified portfolios around risk premia through very specific risk premia exposures is taking AP3 back to the classical asset class, at least when you are looking at the portfolio as a whole. AP3 with assets of SEK393.7 billion as at year-end 2019, had its second best year ever in 2019, returning 17.6%. The strategy seems to be working as 2019 was not just a fluke as the fund has returned 7.4% on average over 10 years and 8.5% over 5 years.

Looking ahead Hamnmark cannot see the concerns for trade-wars diminishing. “China will get more powerful in the 20s with continued growth and a population of 1.4 billion potential consumers. US will be increasingly under pressure. And for the rest of the countries? You pick a side,” Hamnmark said.

Despite Brexit and regular disgruntlement among the citizens of the European Union, he sees the EU as the dark horse in the superpower game with surveys continuously showing that the majority are pro-EU among the member states, he added.

Hamnmark said that as central banks fiscal stimulus packages play out their role, other drivers than monetary policy will take over which will be beneficial for macro managers for instance. “MMT use of fiscal policy would have a different effect on the bond markets than monetary policies have,” he concluded. It is anyone’s guess what the future holds but keeping an open mind about changes is probably sound advice, even for macro managers.

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> *He has been with AP3 since 2010 as Senior Strategist with responsibility for portfolio*

construction. Since October 2014 he is Head of Asset Allocation. Torbjörn is also a member of the investment committees for Mistra (The Swedish Foundation for Strategic Environmental Research) and WWF Sweden.

He has an MBA in Finance and International Business and an Executive MBA in Leading Innovation, both from the Stockholm School of Economics. Before joining AP3 he was Head of Fixed Income at DnBNOR Asset Management in Stockholm for ten years. Hamnmark started his career in 1989 as an options specialist with Arbitech. His options career continued with Citibank in Frankfurt and London, where he was based 1995-1998.

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