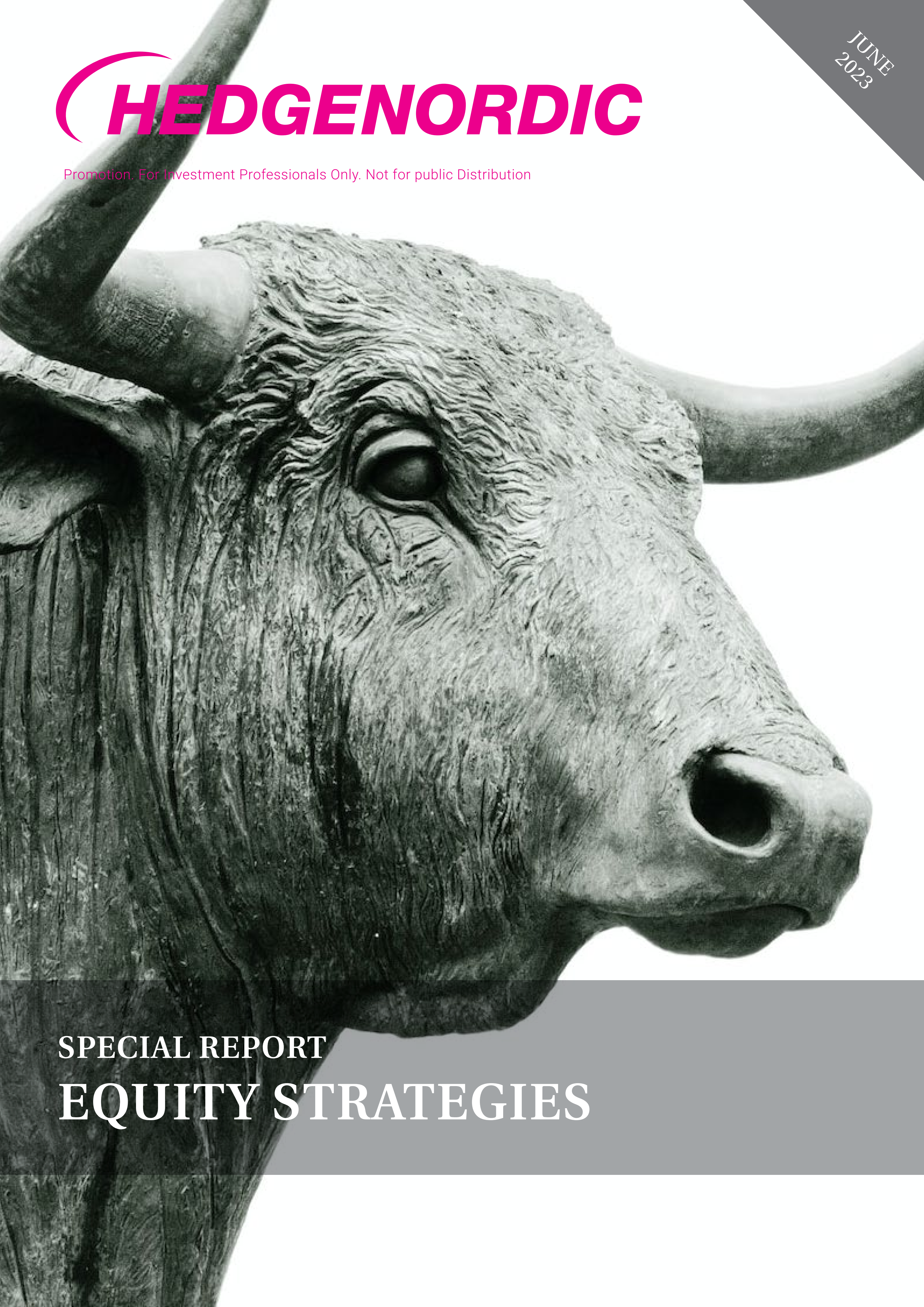
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SPECIAL REPORT
EQUITY STRATEGIES

HEDGENORDIC

Contents

INTRODUCTION

HedgeNordic is the leading media covering the Nordic alternative investment and hedge fund universe. The website brings daily news, research, analysis and background that is relevant to Nordic hedge fund professionals from the sell and buy side from all tiers.

HedgeNordic publishes monthly, quarterly and annual reports on recent developments in her core market as well as special, indepth reports on "hot topics".

HedgeNordic also calculates and publishes the Nordic Hedge Index (NHX) and is host to the Nordic Hedge Award and organizes round tables and seminars.

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Editor´s Note ...

A Captivating and Heterogeneous Marketplace

Stocks have delivered the highest return among major asset classes over extended periods of time. Equity investing, therefore, plays a significant role in investor portfolios, offering the potential for long-term capital appreciation and the opportunity to partake in the growth and ownership of companies. Within the realm of equity investing, a diverse array of strategies exists, each with distinct objectives, risk profiles, and investment methodologies.

The landscape of equity-focused investment management has evolved into a captivating and heterogeneous marketplace. Various dimensions come into play, such as directional versus non-directional approaches, active versus passive management, value versus growth orientations, public versus private markets, microcaps to large-caps, different geographic focuses and industries, and the list could go on.

In the universe of hedge funds and alternative investments, the opportunities become even more extensive. Managers can employ long and short positions, maintain concentrated portfolios, and utilize tools like leverage, options, or unlisted over-the-counter (OTC) instruments. There is a maze of opportunities to trade with equity instruments.

In this edition of HedgeNordic's special report on "Equity Strategies," HedgeNordic explores various approaches to equity investing employed by institutional investors and presents a wide range of equity strategies, spanning from passive to long-only active strategies and long/short equity approaches. The report aims to provide insights into the diverse landscape of equity investing and shed light on different investment strategies employed by market participants.

This publication kicks off with an article on "Demystifying Consensus," where Scott Rosen and Erin Gifford of Visible Alpha explain its software-as-a-service business model focused on sell-side equity research. Jan Petter Sissener recalls the early days of his directional long/short equity fund with downside protection, explains the fund's flexible mandate, looks back at its strong results from short selling in 2022, and describes his fundamental belief that "Cash Flow Never Lies."

Next, Head of Business Development Sukh Bachal talks about Neovest's "Modular Front Office Order and Execution Management Platform." In "Equities in the Runoff Phase of Pension Plan Management," Mattias Ledunger, the chief investment officer of Praktikertjänst, describes his and his team's approach to building an equity portfolio for a pension plan in runoff mode. Trond Tviberg and Mads Andreassen embarked on a new venture after resigning from Sector and launched Seior Healthcare Opportunities Fund, a low-net long/short equity fund specializing in the healthcare sector, to experience the "Stock Picker's Dream and Nightmare."

In "Unraveling the Truth about Market-Neutral Equity Strategies," Simon Røksund Johannessen from KLP and Jakob Nordestedt from Nordea discuss the role of equity market-neutral strategies in a portfolio, misconceptions, and manager selection hints. Joined by co-portfolio manager Henri Blomster, Ernst Grönblom then describes "Asilo's Path to Finding Tomorrow's Superstars." Precious metals specialist Eric Strand, who believes "Gold Stays Gold Forever," introduces AuAg's innovative ETF that offers investors a novel opportunity to gain exposure to gold through investments in "best-in-class" gold mining companies.

Tapio Koivu, Portfolio Manager at Veritas, goes on to explain "The Veritas Approach to Building a Well-Rounded Equities Portfolio," describing the pension fund's comprehensive range of strategies and investment styles to construct its equity allocation. Nicolas Rabener from Finominal then talks about "Trend Following in Equities," while Jonas Thuling from Erik Penser Bank explains "The Art of Tactical Investing" in equities. In an interview with the Swedish House of Finance, NYU's Sydney Ludvingson discusses drivers of equity value growth, the risks associated with high valuations and rising interest rates, and how policymakers and investors can mitigate those risks in "What Drives the Rise in Equity Value, Where Is It Headed?"

We hope you enjoy the read and who knows, maybe there is something new even for you old market goers.

Kamran Ghalitschi

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Demystifying Consensus Estimates

Comparing the Assumptions of Sell-Side Analysts

By Hamlin Lovell – HedgeNordic

Scott Rosen, Founder and Chief Research & Innovation Officer – Visible Alpha

Visible Alpha began in 2011 as a project backed by a consortium of banks who still support the firm. The company was carved out in 2015 and has now grown to over 800 employees globally. Demand for equity research actually increased after MiFID II unbundling required explicit payments for it. "Investors look at sell-side analysis and forecasts because no other source is as broad and deep for proving thoughtful and detailed analysis," says founder and Chief Research and Innovation Officer, Scott Rosen. But today's investors are increasingly demanding to see the rationale underlying the research.

When Rosen was a sell-side equity analyst in the 1990s, he found, "analysts had a huge information advantage in terms of access to information and could simply regurgitate it. Now, the environment has changed to a level playing field and investors are looking for insights to understand what is behind analyst views. But the difficulty of comparing analysts on very detailed issues created a granularity disconnect where it was hard to get consistent information about assumptions behind forecasts."

Visible Alpha's "deep consensus data" addresses this buy-side problem by demystifying models that were once perceived as "black boxes." The firm's platform is comprised of a library of historical and forecast data, including analysts' own estimates of geographic, segmental and product breakdowns (which may not be publicly disclosed by companies). "Visible Alpha builds consensus estimates from the bottom up, normalizing the data inputs, rather than just extracting and aggregating headline conclusions," says Erin Gifford, Marketing Director. The average number of line items feeding into a forecast is 161, but there could be as many as 1,000 for some companies. Visible Alpha is agnostic on accounting systems, but makes the data comparable — US GAAP and IAS are most often used in the raw estimates. "We aggregate what would otherwise be very disparate information," says Rosen.

The most intense users of the data tend to be fundamental equity long/short analysts feeding ideas into concentrated books at hedge funds. There are also a growing number of long only and quant clients. Some users are credit investors, but Visible Alpha does not currently capture models from fixed income analysts. "The market for fixed income research is much smaller and we would struggle to find enough names that have 3 analysts with enough granularity and similarity," points out Rosen.

USE CASES

The word "consensus" is misused by the media to imply an agreement distilled down to one definitive figure, when there are in fact multiple ways to define and measure the concept of "consensus" – and there can be differences between Bloomberg, Refinitiv and Visible Alpha consensus metrics. "It is a complete misnomer to imply agreement. If there was agreement, we would not need the market. In fact, there are a variety of forecasts and disagreements," explains Rosen.

"The consensus is just the mean summary statistic and arithmetic point of various numbers and this can be the least interesting part. Knowing the range of views can be more useful. Sometimes there is

Erin Gifford , Global Head of Marketing – Visible Alpha

"The environment has changed to a level playing field and investors are looking for insights to understand what is behind analyst views."

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"The difficulty of comparing analysts on very detailed issues created a granularity disconnect where it was hard to get consistent information about assumptions behind forecasts."

very tight agreement and sometimes a very broad spectrum of views." Clients can see the mean, mode, range and standard deviation of the estimates. Outliers are shown and could be excluded to create a different measure of consensus.

Data can be used for forecasting and also benchmarking opinions. "Consensus estimates can be a proxy for forecasting for those who do not have time to dig deep into the dynamics of the company. Alternatively, consensus estimates can be used to represent what the market believes and what is already reflected in current pricing. That can provide scope for expressing contrarian views on pricing, revenues, or other variables," says Rosen.

Investors might employ the data to find the fastest-growing companies in a sector that is doing well, such as AI. Or they could look for companies breaking out within an industry that is not doing well, such as traditional retail. The data could also feed into pairs trades for long/short or market-neutral strategies.

Visible Alpha produced an ad hoc report, "Shopping for Alpha," illustrating a possible investment application of picking winners and losers within sectors. It showed how two carefully selected metrics – comparable sales and operating margin growth – could have been used to predict relative share price performance within two highly leveraged industries: retail and restaurants. The metrics were chosen to enable apples–to-apples comparisons over time and between companies.

ACCURACY AND VALUATION

Visible Alpha's standard output equally weights the latest analyst models and does not attempt to rank individual analysts on accuracy of forecasts, though a client could, to some degree, create their own customized consensus subject to brokers entitling the client to their specific data.

A reversal from bullish to bearish analyst sentiment (or vice versa) can be of most interest to institutional investors. It is important, however, to distinguish between the stronger and weaker skillsets of the typical sell-side analyst. "The primary role of analysts is understanding the mechanics of a business and how a company weathers change in a competitive landscape, over long-term forecasts of 1- 2, or even 10- 20 years. They are less good at working out what the market is willing to pay, because valuations depend on macro-market psychology. Big US brokers may give risk assessments but do not give so many short-term trading recommendations," says Rosen.

There can also be a perennially optimistic bullish bias in estimates, though accuracy checks occur every quarter when results are released.

UPDATES AND CORPORATE EVENTS

Analyst models need to be updated after key events such as earnings releases to keep their place in Visible Alpha consensus estimates. Earnings are the biggest reason for updating estimates, but analysts do update models in the interim throughout each quarter. A mix of machine learning and teams of sector specialists at Visible Alpha manage the updating process.

Corporate events can be another reason for updates. The Visible Alpha broker universe does not include specialist event-driven houses, who broke to merger arbitrage and other event funds and do not cover companies on a ongoing basis. However, "regular sell-side research around merger events may add another version of the future with proforma estimates if a takeover is completed," says Rosen.

COMPANY AND BROKER COVERAGE

At least three analysts need to be covering a stock for Visible Alpha to include it. Coverage is currently around 6,500 companies globally, which are mainly large-and mid-cap names. Coverage of small and micro caps is being expanded as Visible Alpha develops relationships with more brokers.

Most of the 180-strong Visible Alpha broker universe is listed on their website, and has been growing in Asia after the firm opened an APAC office in Hong Kong in 2019. It does not include specialist short-selling research houses, such as Hindenburg, because their published research tends to be more opportunistic and ephemeral in nature. "We like to see longevity of coverage, with some analysts having followed a stock for 20 or more years," says Rosen.

The list of brokers does include some independent research providers (IRPs), including some bank and broker units that have been reclassified as such post MiFID II.

A multitude of public companies citing Visible Alpha data, as well as buy-side users encouraging the sell side to contribute, are helpful in increasing contribution and coverage. One incentive is that sell-side contributors get free access to consensus data, and brokers can also receive some remuneration for their efforts.

Visible Alpha's business model is primarily Software As A Service (SAAS) subscriptions based on a range of metrics, including the number of users. "All clients essentially access the same data, with the exception of permissioned access to individual broker content. The client base also includes some smaller firms and even others that are pre-launch," says Gifford.

Most clients use the web app, though there are also Excel add-ins and an API cloud model. Visible Alpha is not currently integrated with Chat GPT.


Jan Petter Sissener, CEO – Sissener AS

Cash Flow Never Lies

By Eugeniu Guzun – HedgeNordic

"We use a top-down approach to determine the overall exposure at a given point, which we combine with a bottom-up valuation approach to select our long and short positions."

Upon approaching his own retirement age, Jan Petter Sissener recognized the importance of designing an investment solution that could deliver consistent returns across different market conditions. Acknowledging the shared needs of his clients, Sissener took the initiative in 2012 to establish Sissener Canopus, a directional long/short equity fund with downside protection.

"Our clients were not concerned about beating the index. They were looking for absolute returns and were willing to sacrifice some upside for downside protection," JP Sissener recalls the early days of Sissener Canopus. "I myself reached a stage in life where I no longer had the luxury of time to recover from financial losses," adds Sissener, who launched the long/short equity fund as he was approaching the age of 60.

FLEXIBLE MANDATE

The fund operates with a flexible mandate and can be net long, market neutral, or net short depending on Sissener's and his team's market outlook. "We use a top-down approach to determine the overall exposure at a given point, which we combine with a bottom-up valuation approach to select our long and short positions," explains JP Sissener. "From a top-down macro perspective, we spend a lot of time analyzing the market consensus on where we are headed," he elaborates. "Consensus is not always right, and taking a contrarian view can pay off, although it can be painful at times." This emphasizes the importance of having an accurate view of the current market conditions.

In the long run, maintaining exposure to equities has proven to be a rewarding investment strategy. "The world and companies are creating value every day, so investing in the stock market and individual stocks is a winners' game," argues JP Sissener. However, investing in equities carries risks, including the potential for capital loss during market downturns. An active manager needs the necessary tools to respond to these events to avoid drawdowns.

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When markets face events that could impact financial markets, such as a pandemic, an inflation shock, or a war, "liquidating the portfolio or parts of the portfolio to reduce exposure might take you days or weeks," according to JP Sissener. In the early days of the pandemic, Sissener Canopus swiftly decreased its net long exposure from 70 percent in February to negative exposure in March. "We have the toolbox to reduce net exposure straight away," says JP Sissener.

Sissener Canopus has maintained an average net market exposure of about 60 percent since launching in April 2012, with the exposure adjusted using index hedges based on the team's market outlook. The fund also maintains a small portfolio of short positions on single companies, capitalizing on an additional source of alpha. "Shorting individual companies is very difficult in itself, particularly when aiming to reduce overall risk," explains JP Sissener. "We only short with the intention of generating an absolute positive return on the short position. You want to avoid systematic risk when reducing the net exposure, and systematic risk is better managed using index hedges."

2022 – THE YEAR OF SHORT SELLING

As a directional long/short equity fund, Sissener Canopus primarily derives its returns from long positions, while variable hedges and single stock shorts play a complementary role. For Sissener Canopus, 2022 proved to be the best year for short selling, accounting for a good portion of the fund's 8.2 percent return in the difficult market conditions of 2022. The reported 8.2 percent return is also isolated from the depreciation of the Norwegian krona. Sissener Canopus has implemented currency hedging across different share classes, aiming to minimize the potential adverse effects of currency volatility on investment performance.

The short-selling book alone contributed 7.9 percent gross to the fund's return in 2022, followed by a 5.5 percent contribution from the portfolio of index hedges, which more than offset the 2.9 percent negative contribution from the long portfolio. "We had some really successful shorts last year, such as our short position in SBB," recalls Philippe Sissener, JP Sissener's son, who is responsible for managing Sissener's corporate bond fund launched in 2019. Sissener shorted struggling real estate group SBB at around 60 SEK a share and covered around SEK 5.50 apiece. "We still believed SSB was going to go bankrupt, but didn't want to risk a short squeeze," says JP Sissener.

> "Cash flow statements cannot be manipulated and our philosophy of 'cash flow never lies' very often leads us to overlook stocks that don't have any earnings or generate cash flows."

The Swedish real estate sector was the best source of short-selling ideas for the team at Sissener Canopus in 2022. The credit team at Sissener, primarily responsible for analyzing the bonds for Sissener Corporate Bond Fund, arrived at the conclusion that Swedish real estate companies would struggle to service their debt amid rising interest rates and lower rental yields on buildings. There is great synergy between the credit and equity teams at Sissener. "We are one team and one goal," emphasizes JP Sissener. "We have people with equity and credit backgrounds working together as one team on both fronts," elaborates Philippe Sissener.

CASH FLOW NEVER LIES

At the heart of the Norwegian asset manager's investment philosophy is the fundamental belief that "cash flows never lie." This guiding principle shapes their investment approach across both Sissener Canopus and Sissener Corporate Bond Fund. "Our approach is highly focused on cash flow generation," says JP Sissener. "Cash flow statements cannot be manipulated and our philosophy of 'cash flow never lies' very often leads us to overlook stocks that don't have any earnings or generate cash flows."

This principle has also influenced the asset manager's sector exposure, resulting in increased exposure in sectors such as energy, finance, and technology. "Energy stocks are very cash flow generative," says JP Sissener. For example, shares in French multinational energy and petroleum company Total at a free cash flow yield of 16 percent, providing great downside protection, according to the founder of Sissener. "Even at lower share prices, these stocks would continue to generate high returns for shareholders."

In contrast to some investors who may hesitate to invest in energy stocks due to environmental, social, and governance (ESG) considerations, JP Sissener views investing in oil-related companies as an integral part of an ESG-compliant and conscientious agenda. "Some investors strongly believe that this industry is not ESG compliant, but we think it is," says JP Sissener. "Firstly, major oil companies will be first to invest more into green energy. Secondly, from a security standpoint, we will be dependent on oil and gas much longer than European politicians believe, so we need to avoid dependence on Russia, Saudi Arabia, Iran, and other others."

Within the fund's portfolio, approximately half of the 40 percent exposure to the energy sector is derived from investments in oil and gas companies. The remaining portion of the energy exposure is diversified across various segments, including investments in electricity and hydropower producers, uranium miners, sub-suppliers to the wind and solar sector, as well as sub-suppliers to the oil industry who are actively expanding their presence in the offshore wind sector. By investing across these different segments, Sissener Canopus aims to capture opportunities arising from the broader energy landscape, encompassing both traditional and renewable sources.

With a current net exposure of 46 percent, the team at Sissener Canopus maintains a cautious stance on financial markets, anticipating a decline in earnings across the board. "Equity markets may appear cheap if you assume that earnings will remain stable at current levels. We are waiting for earnings to fall," states JP Sissener. For Sissener Canopus to adopt a more bullish stance and increase its net exposure, JP Sissener needs "to see that we are wrong in our expectations of earnings going down."

Neovest: Modular Front Office Order and Execution Management Platform

Swift and flexible solutions for execution and trading

By Hamlin Lovell – HedgeNordic

"Neovest is a global, multi-broker electronic order and execution management platform that specialises in equities, futures, options and FX markets."

"Neovest is a global, multi-broker execution management system that allows clients to communicate their orders to over 340 equities, futures, options and FX market brokers. Neovest consists of one integrated ecosystem that will allow you to trade the assets you want, when you want - all from a single screen," says Sukh Bachal, Neovest's Head of Business Development. Neovest (which simply merges the words new and invest to create a better trading experience for clients) was acquired by JP Morgan in 2005, but operates independently with broker neutrality. Neovest maintains client relationships spanning 30 years and has skilled and knowledgeable staff who provide excellent client support.

Neovest is used by hedge fund managers as well as family offices and proprietary traders – approximately 75% of Neovest's 600 clients are fund managers, with assets under management running

Sukh Bachal, Head of Business Development – Neovest

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> "Neovest consists of one integrated ecosystem that will allow you to trade the assets you want, when you want, through more than 340 brokers - all from a single screen."

the gamut from USD 75 million to over USD 100 billion. In common with the hedge fund industry in general, Neovest's client base is US centric, but is also growing globally--in particular in Europe, Asia and the Middle East. The Neovest Nordic region users include banks, asset managers, and pension funds in the region. However, given the Neovest platform is most suitable to hedge funds, Neovest are keen to expand in the Nordic region - the second largest European market for hedge funds.

MARKET COVERAGE

Neovest's broker FIX network allows clients the connectivity through their brokers to more than 70 equities exchanges globally, including all in the Nordic region, which includes Stockholm's First North Growth Market. More broadly, Neovest connects to over 340 brokers globally and is open to onboarding others. "If clients want to access a particular exchange, our nimble technology allows us to very quickly add brokers who have access to the exchange," says Vivek Nandha, a member of Neovest's EMEA Business Development Team.

Neovest's customer base manages strategies including long/short equity, systematic macro, managed futures and CTAs, sometimes all in one firm within a multi-strategy fund. Neovest customers generally send orders in listed equities, listed derivatives - futures and options - and some OTC FX orders to its brokers. While Neovest provides high speed data processing, it does not operate in the low latency HFT space where technology tends to be proprietary and co-located.

OPEN ARCHITECTURE

"We are very transparent in our capabilities to ensure we are the best fit for our clients so we can provide the best service we can. Neovest considers itself an Order and Execution Management System (OEMS), with more of an emphasis on the EMS", explains Bachal. Neovest is mainly focused on the front office with some compliance applications: "the Neovest system is flexible enough to integrate with both third party vendor systems and clients' proprietary systems. Neovest uses both FIX and REST APIs for integration and data feeds" explains Bachal.

Neovest works with many other providers, including some in the Nordics. Neovest specialises in advanced technology that is a critical aspect for Buy Side Front Office teams. Neovest expertise complements the capabilities of other OMS platforms including Limina and Copenhagen headquartered FinTech Athena Systems, which is part of United FinTech, resulting in a seamlessly integrated Multi-Asset OEMS experience that covers the entire trade order lifecycle. Bachal is very open to other partnerships with established and newer systems. For instance, Neovest can integrate its services with multiple providers to assist clients with regulatory and clearing reporting.

SCALED FOR CLIENT NEEDS!

Thus, the Neovest model is open architecture and modular. In some cases, clients simply use Neovest for trading - or even just for its user-friendly User Interface (UI). "Some firms tell us we just want your screens like a tableau to visualise data. They can plug in their own proprietary technology, bolting on their own systems above and below," says Bachal.

Clients need not be highly technical developers, coders or programmers to configure the system. They do however need to be prepared to define their own parameters and restrictions, regarding brokers, markets, position sizes and so on, which may be needed in areas such as UCITS counterparty or diversification constraints.

"Integrating an enterprise software system does not have to take months." says Bachal. Neovest boasts on-boarding times as short as one month, which removes what is the biggest obstacle to switching systems, according to FIX surveys.

Neovest can be used to transmit orders for high touch, voice execution, and is also a versatile platform for electronic and algorithmic trading. Neovest does not offer execution algorithms, but it can allow clients to easily send their orders to algorithms provided by banks, brokers and specialist execution brokers and algorithm experts such as quantitative brokers.

Similarly, Neovest has strategic partnerships with other specialists to populate functionality such as the short-able stocks feature. Based on client feedback, Neovest has partnered with providers to gather data on short-able stocks and importantly also where to locate security borrows: "The data generally comes from real time API feeds though data for hard to borrow stocks can take longer," reveals Bachal.

ESG

It is becoming increasingly common for ESG critics to seek underlying information on service providers' ESG policies. Neovest has 100% of their power needs sourced from renewable sources. "ESG is of paramount importance to Neovest and an attribute considered in our business decisions," reveals Bachal.

Additionally, Neovest is a founding and active member of Sustainable Trading, a non-profit organisation fostering best ESG practices for financial trading. The network brings firms together to devise practical solutions to industry specific ESG issues as well as providing a mechanism for self-assessment and benchmarking. Its members include asset managers, banks and broker dealers, exchanges and trading platforms and also technology and service providers.

To learn more about Neovest and explore how their sustainable trading solutions can benefit your business, visit Neovest.com

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Equities in the Runoff Phase of Pension Plan Management

By Eugeniu Guzun – HedgeNordic

> "We have an in-house model that supports our decisions on whether to deviate from the guideline exposure of 25 percent equities."

As the Chief Investment Officer of Praktikertjänst, Mattias Ledunger is entrusted with managing a pension trust that oversees the retirement funds of Praktikertjänst. The provider of private health and dental care employs a diverse range of professionals in the Swedish healthcare industry. This mainly includes doctors and dentists but also dental technicians and hygienists, physiotherapists, nurses, midwives, chiropractors, psychologists, and therapists all over Sweden.

The main pension plan, with SEK 8.7 billion under management, is no longer accepting new members and provisions, leading to reduced risk-taking requirements for managing the pension scheme. "One of the peculiarities of this pension fund is its relatively short duration and the pension fund is actually in runoff mode. It is a defined benefit plan, but no more pensions are earned under this plan," explains Ledunger. "The duration is approximately eleven years, which is quite a bit lower than the average pension fund."

Given the reduced risk-taking requirements, the pension fund has implemented guidelines mandating an allocation of 75 percent to bonds and 25 percent to equities with some wiggle room of plus or minus


Mattias Ledunger, CIO – Praktikertjänst Pension Trust

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20 percent. Despite these guidelines, the effective management of the equity portion holds significant importance in determining the prospects of pension recipients.

The Pension Trust rarely reaches the extremes of either minus or plus 20 percent from the target equity allocation. "We have an in-house model that supports our decisions on whether to deviate from the guideline exposure of 25 percent equities," explains Ledunger. The model takes into account the relative performance and momentum of asset classes, among other things. However, during the early stages of the pandemic, the fund significantly reduced its equity exposure and was slow to build up the exposure after that, which had a negative impact on performance. Ledunger recalls, "We were surprised by the speed and intensity of central bank interventions and the subsequent market recovery."

180 STOCKS WITH LONG/SHORT OVERLAY

To construct their equity portfolio, Ledunger and his team have chosen a benchmark consisting of 180 names, including 150 from the STOXX Global 150 Index and an additional 30 from the OMX Stockholm 30. "Our objective is to replicate that benchmark, so the number of stocks in our portfolio will broadly be in that ballpark," explains Ledunger. The portfolio primarily includes international mega caps and Swedish large caps.

The choice of benchmark emphasizes international diversification across industries, currencies, and regions while allowing for exposure to idiosyncratic or company-specific risks. Ledunger says, "We wanted something that was international, broad, diversified in terms of industries, currencies, and regions, but also possible to replicate." The portfolio is managed in-house through direct investments, using a long/short approach to adjust the weights of the 180 benchmark stocks.

"We will run an overlay of long and short positions on top of the replicated benchmark to overweight or underweight certain positions," explains Ledunger. "There will be names, especially Swedish ones, that can have a significant weight in the benchmark," says Ledunger. "We tend to take somewhere between one and two percentage points up or down to overweight or underweight certain stocks." His investment team will not run this long/short overlay to each individual position, however. "On top of the 180 long positions in each individual company, we will run an additional ten to 15 long and short positions to adjust the weights in the portfolio."

SAME PEOPLE FOR ASSET ALLOCATION AND SECURITY SELECTION

The investment team of four professionals, including Ledunger, analyzes and looks for investment cases to adjust the weights in the 180-name portfolio. While each team member has a slightly different investment style, the overall approach tends to be value-driven, with a focus on avoiding value traps. "The investment style is going to be colored by the individual. Most of us, however, tend to be a little value-driven," explains Ledunger. "We are old enough to be aware of our limitations in investing, so we really try to screen hard in order to stay out of value traps."

The team conducts thorough evaluations and relies on third-party research to document their decisions. "The decision-making process involves in-depth evaluation, and we look for triggers to support our choices," says Ledunger. "We don't want to have something that can be undervalued for a very long time, or forever."

The investment team not only manages individual positions within the portfolio but also focuses on top-down allocation, macroeconomic conditions, and strategy. "The team tends to always put a lot of effort into the top-down allocation, macro environment, and strategy," says Ledunger. "This process often involves decisions on asset allocation, duration decisions, how the curve will develop, and credit conditions in general," he elaborates. "But then we are also the same people who then take on different positions. The trick is to be disciplined and only take the risks that we can manage with the people we have."

VIEWS ON THE ECONOMY

Ledunger acknowledges the importance of the economic outlook in predicting equity market movements. To predict where equity markets might be heading, "you are going to have to start with the economy," begins Ledunger. He suggests that a recession seems likely due to various factors such as rising rates, banking crises, debt ceiling issues, contracting credit conditions, high market valuations, and geopolitical tensions. "Everything is in place for recession, but it has not really happened yet. There is a pretty fair chance that we are going to see a recession. And if we do, we are going to see earnings contract."

> "The signals that flash red could potentially, for the first time, not lead to a recession. This is uncharted territory."

In the current uncertain environment characterized by war, high inflation, and debt ceiling concerns, Ledunger maintains a slight short exposure in the S&P 500, resulting in an equity exposure of 23 percent. The fund also implements a "risk-reversal" options overlay as a precaution against potential market downturns. "We would rather be flat at delta one with an exposure of 25 percent, but then put that option overlay on for a little protection." When earnings turn down, Mr. Market is always panicking and selling, according to Ledunger.

Ledunger also acknowledges the possibility of avoiding a recession or experiencing a mild one, considering the substantial stimulus injected into the economy and markets by central banks and governments worldwide over the past decade, peaking around the Covid pandemic. "Trying to find how we are wrong, I would have to be open to a scenario where the lingering effects of these measures, such as the substantial injection of cash into the hands of consumers and businesses, could sustain strong consumption and robust employment through the industrial supply readjustment that normally spells recession," says Ledunger. "The signals that flash red could potentially, for the first time, not lead to a recession," he emphasizes. "This is uncharted territory."

Even so, chances are that markets are going to experience a landing. "Even if it is just a soft landing, earnings are going to come down," he argues. Given his view of the stock market being overvalued, Ledunger and his team have taken protective measures and are prepared to increase their selling activities. On the depth of any drawdown, however, he adds a caveat. "There is a risk that the recession and drawdown will be truncated because you can't underestimate the possibility of central banks becoming hyperactive again, despite their claims to the contrary. A lot of people are counting on the Fed put."

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From left to right: Mads Andreassen, Founding Partner and CEO, Trond Tviberg, Founding Partner and CIO – Seior Capital Partners

Healthcare: A Stock Picker's Dream and Nightmare

By Eugeniu Guzun – HedgeNordic

> "We wanted flexibility, which fits well with this sector, so we opted for running a quasi-directional long/short equity fund with a net exposure between zero and 50 percent."
>
> Trond Tviberg

Trond Tviberg, one of the founding investment managers of Sector Asset Management's healthcare-focused Gamma arm, embarked on a new venture after resigning from Sector in February 2021. Seeking a fresh challenge, Tviberg received an exciting proposition from Mads Andreassen, a former portfolio manager from the same Gamma team, to launch a new healthcare fund. Since September of last year, the duo has successfully managed Seior Healthcare Opportunities Fund, a low-net long/short equity fund specializing in the healthcare sector.

Reflecting on his then-surprising decision to leave Sector in February 2021, Tviberg recalls, "I needed a new challenge, a new start." Seven months later, Andreassen, who had also left Sector in 2018 after being part of the same portfolio management team, approached Tviberg with an idea to launch a new healthcare fund. "Mads was the driving force behind the idea," Tviberg affirms. Together with Are Søberg, the Chief Operating Officer at Seior and a member of the old team at Sector Gamma, the trio constituted 60 percent of the original team. Sector Gamma continues to run a market-neutral fund and a long-only fund specializing in healthcare.

The newly formed team began their project with a fundamental question: "What type of healthcare fund would we want to invest in?" The team decided against a market-neutral as conventional indicators of neutrality, such as beta, do not adequately capture systematic-like risk factors such as style exposures. Market-neutral strategies struggle to maintain neutrality across all phases of a market cycle and returns can suffer if certain styles fall out of favor.

"We also decided that long-only was not an option either, as there was no downside protection," explains Tviberg. "We wanted flexibility, which fits well with this sector, so we opted for running a quasi-directional long/short equity fund with a net exposure between zero and 50 percent," he continues. "There is a lot of dispersion within this idiosyncratic risk-dominated sector, which means it can be a stock picker's dream or nightmare." The healthcare sector lends itself well to a long/short equity strategy and the Seior team leverages their experience managing both long-only and market-neutral funds in the healthcare sector

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to inform and improve their approach. "We took forward what worked and enhanced or solved what we thought were challenges," says Tviberg.

CONCENTRATION, AND VALUATION FOCUS

Drawing from their experience running healthcare-focused funds at Sector, the team aimed to increase focus and concentration in the portfolio. From a universe of 400 healthcare companies globally, filtered by market cap above $1 billion and $5 million in daily liquidity, Seior Healthcare Opportunities Fund tends to maintain a portfolio with 20 to 40 long positions and 10 to 25 short positions.

The Seior team places a strong emphasis on valuation, constantly seeking undervalued stocks for the long portfolio and overvalued stocks for the short side. "Everything starts from valuation," emphasizes Tviberg. Research indicates that, as a rule of thumb, 80 percent of a healthcare company's intrinsic value comes from existing product lines and 20 percent from the product pipeline. "We look for companies that have pipelines with negative implied value. We don't take scientific or binary bets on a product in development. We make financial or product bets versus pipeline bets, considering the cyclical nature stemming from a product's lifecycle."

EARNINGS REVISION MODEL

Mads Andreassen has also developed an earnings revision model that assists the team in making more accurate assessments of a company's valuation and expected direction. "We aggregate different valuation models to identify potential alpha," says Tviberg. "The earnings revision model and the measure of implied volatility of the underlying stocks play an important role in the portfolio construction process. We may place larger bets on larger, less volatile companies," explains Tviberg.

While the "name" turnover is not very high, the team frequently trades around positions based on valuation levels and insights from the earnings revision model. "We are data-driven, process-oriented, but we are not running a quant strategy," emphasizes Andreassen. Ultimately, the portfolio managers have the final say in the portfolio composition and net market exposure.

> "We are data-driven, process-oriented, but we are not running a quant strategy."
>
> Mads Andreassen

The team's approach to short selling is also driven by valuation. "We employ a similar approach for both longs and shorts. But we are more prudent on the short side," says Andreassen. "We don't need to squeeze the last 10 percent out of a short bet. We may enter shorts slightly late and exit early." The fund's net exposure is primarily determined by bottom-up stock selection and guided by insights provided by the earnings revision model regarding the sector's future earnings.

SUSTAINABILITY ENGAGEMENT

The healthcare sector gives investors the opportunity to support goal three of the UN's Sustainable Development Goals: "Ensure healthy lives and promote well-being for all at all ages." While the healthcare industry contributes to extended life expectancies, prosperity, and economic process, it also poses challenges for ESG investors due to issues such as drug pricing, affordability, lobbying practices, anti-competitive behavior, animal testing, or questionable clinical trials. This might be a tough pill to swallow for socially responsible fund managers and investors. The Seior team has found a way to integrate sustainability into its investment process.

"Sustainability is an integral part of the evaluation process," starts Andreassen. Seior Healthcare Opportunities Fund is classified as an Article 8 fund but does not shy away from investing in companies with low ESG scores. "Our approach involves actively engaging with companies regarding sustainability," emphasizes Andreassen. "When we identify points of concern, we set up calls or meetings to engage with management teams. If management acknowledges the issues, is transparent about them, and is working to address them, we can still invest."

HEALTHCARE AS AN EXPOSURE

Investing in the healthcare sector offers attractive opportunities due to steady demand, long-term growth prospects driven by demographic trends, continuous innovation, and technological advancements. "Healthcare is expected to grow at a higher rate of growth than the broader economy due to a number of structural trends such as demographics, lifestyle changes, innovation, and others. It also provides access to innovative companies at attractive valuations," explains Tviberg.

Additionally, investing in healthcare also provides indirect exposure to emerging markets as many healthcare companies sell their products to these markets. "Investing in this sector offers a way to get exposure to emerging markets through large, safe companies," elaborates Tviberg. However, investing in the healthcare sector also comes with risks, such as regulatory changes, clinical trial failures, pricing pressures, and competitive dynamics. "There are also headwinds, including political uncertainty in the U.S., and price pressure. It is an opportune time to invest in the healthcare sector when there is a combination of economic and political uncertainty."

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Unraveling the Truth about Market-Neutral Equity Strategies

By Eugeniu Guzun – HedgeNordic

Simon Røksund Johannessen, Portfolio Manager – KLP

"The primary benefits of market-neutral strategies are that they can reduce portfolio volatility and offer a source of returns uncorrelated with the rest of the market."

Simon Røksund Johannessen

In the dynamic world of investing, where volatility and uncertainty are ever-present, the quest for strategies that can deliver consistent returns while mitigating market risk remain a top priority for investors. Among the approaches that have emerged, market-neutral equity strategies have gained recognition for their ability to navigate turbulent markets and potentially enhance portfolio performance.

The performance of market-neutral equity funds in difficult market conditions is worth noting. In 2022, the ten market-neutral equity funds included in the Nordic Hedge Index achieved an average gain of 1.6 percent, while broader equity markets experienced double-digit declines. And yet, the performance of a broader market "is not a relevant comparison for a market-neutral strategy," argues Jakob Nordestedt, who runs a market-neutral strategy under the umbrella of Nordea Asset Management. "If investors would evaluate us like this, they would think I am doing something poorly when the market goes up and that I am a genius when the market goes down."

Instead, market-neutral equity managers should be judged by their ability to generate uncorrelated returns through their stock picking skills. "If a market neutral portfolio is run in a correct way, with zero market correlation, its performance will only be determined by the stock picking skills of your portfolio manager," considers Nordestedt. The true value of a well-designed market-neutral strategy lies in its ability to provide an uncorrelated return stream and "act as a risk-balancing tool against undesirable market movements."

Simon Røksund Johannessen, a portfolio manager overseeing an energy-focused market-neutral equity fund at Norwegian pension provider KLP, shares Nordestedt's viewpoint. "Market-neutral equity strategies are designed to deliver returns that are independent of the direction of the overall market," highlights Johannessen. These strategies eliminate the need for the broader market to move in a particular direction to generate returns. "The primary benefits of market-neutral strategies are that they can reduce portfolio volatility and offer a source of returns uncorrelated with the rest of the market."

Johannessen also emphasizes the importance of considering market-neutral strategies as a means of reducing systematic market risk in a portfolio. However, he underscores that the strategy must generate alpha, which is achieved through isolating stock-specific risk and focusing on individual opportunities rather than broad market exposure. "Of course, the strategy needs to generate alpha," emphasizes the portfolio manager of KLP Alfa Global Energi. Nordestedt concurs, stating that "all our returns are and should be coming from alpha generation."

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Jakob Nordestedt, Portfolio Manager – Nordea Asset Management

Nordestedt further explains that "the return of a market-neutral strategy should always be viewed as the risk-free interest rate plus the return of the active portfolio." He highlights the need for a market-neutral strategy to have zero impact from economic factors. "We take this very seriously and run the book with a net exposure of 0 at all times," says Nordestedt. "In addition, we implement a style factor hedge in order to be neutral to any economic factor, market rotations or whatever may be out there." The goal, at the end of the day, is to generate returns solely from alpha sources rather than beta exposure.

MISCONCEPTIONS

Despite the appeal of equity market-neutral strategies, several misconceptions surround them, often leading to confusion and skepticism among investors. "The most common misconception among investors must be that there should be some sort of market correlation," argues Jakob Nordestedt. He has sought to solve this misconception by building a fund that is truly market neutral. "If a market neutral fund is structured correctly, it will have no correlation at all to the market."

Another misconception, according to Johannessen, is that equity market-neutral strategies offer risk-free or guaranteed returns. "Market-neutral strategies are not risk-free. Investors need to understand these risks when considering market-neutral strategies," explains the portfolio manager of KLP Alfa Global Energi. The market-neutral fund specializing in the energy sector has enjoyed exceptional performance in recent years, atypical for a market-neutral fund. KLP Alfa Global Energi generated an annualized return of 15.3 percent in the three years ending April 2023 to reach a three-year Sharpe ratio of 1.9. While such performance is "unexpected and not normal," this feat is not unachievable going forward.

HOW TO CHOOSE A MARKET-NEUTRAL STRATEGY

Based on his experience as a market-neutral investor, Johannessen puts forward a three-step rule to analyzing and selecting a market-neutral strategy. "First, understand the strategy and what kind of unique alpha the fund manager provides," starts Johannessen. "Second, consider the track record of the manager and under what market conditions his strategy has worked," he continues. "Third, get a good understanding of what kind of risk has been used to generate the returns in the manager's portfolio."

Nordestedt offers a similar suggestion but emphasizes the importance of focusing on the "process" during due diligence. "Having done this for some time, I would do deep due diligence but only focus on one thing: process," starts Nordestedt. "One of the most important things is to understand the stock picking process and how it can be repeated over and over again. This is much more complicated than most would believe," he emphasizes. The second process that needs to be understood is the portfolio construction and risk framework, according to Nordestedt. "This is more important than the stock picking as this is where you are facing much more systematic risk than a bad case in a stock," highlights Nordestedt. He believes that the funds excelling in both of these processes will be the long-term winners.

Equity market-neutral strategies are a type of hedge fund strategy that allows investors to actively position their portfolios while limiting exposure to market risk. While there is no prescribed approach or strict definition for these strategies, they tend to be inherently defensive in nature. Market-neutral strategies may underperform broad market indices during bullish periods but can offer valuable downside protection during market downturns, and dampen volatility when added to a broader portfolio. Thoroughly evaluating the strategy's unique alpha, track record, risk framework, and investment process will be crucial in identifying strategies that can generate consistent returns while effectively managing market risk.

> "If a market neutral portfolio is run in a correct way, with zero market correlation, its performance will only be determined by the stock picking skills of your portfolio manager."
>
> Jakob Nordestedt

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Ernst Grönblom, Portfolio Manager – Asilo Asset Management

Henri Blomster, Portfolio Manager – Asilo Asset Management

Asilo's Path to Finding Tomorrow's Superstars

By Eugeniu Guzun – HedgeNordic

In contrast to benchmark-hugging managers, a truly active equity manager combines independent thinking, strong conviction, and a long-term perspective to generate superior investment results for clients. Ernst Grönblom has spent over a decade exemplifying the art of true active equity investing through his high-conviction strategy aimed at finding the superstar companies of tomorrow.

His previous fund (HCP Focus) ranked among the world's top ten equity long-only hedge funds in 14 quarters out of the 18 quarters over the period of 1Q 2016 through 2Q 2020 based on three-year annualized returns. No other fund in this category managed to join the top ten quarterly leaderboard compiled by BarclayHedge this many times during the period.

"At the risk of sounding arrogant, the way we approach active management is how most equity managers should operate," believes Grönblom. "Due to fear of career risk, many managers construct over-diversified closet-index portfolios. Our way involves running high-conviction, concentrated portfolios. It's not our job to be maximally diversified. If clients want more diversification, they can easily achieve it by increasing the number of funds in their portfolios. I believe this should be the norm." Otherwise, there are cost-effective passive instruments such as ETFs available that can provide the same market exposure as benchmark-tracking managers.

Joined by co-portfolio manager Henri Blomster and a broader team behind the scenes, Grönblom continues to run his decade-long investment strategy under his own independent fund boutique, Asilo Asset Management, since the beginning of 2023. The equity fund Asilo Argo continues to hold a concentrated portfolio of 12 current or potential future superstar companies where the market still underestimates their competitive advantage and potential.

IDIOSYNCRATIC STRATEGY AND PHILOSOPHY

High concentration is one of the main pillars of Asilo Argo's investment philosophy. "A concentrated portfolio allows us more time per position or buying decision, enabling us more time and space to explore different angles to an investment case," explains Blomster. "A concentrated portfolio gives us enough time to validate our view of the big picture and identify the aspects that are misunderstood by the market." So, what exactly are these superstar companies?

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"Superstar companies are a special type of companies that have distinct characteristics compared to most others," begins Grönblom. "If everything goes as planned and expected, these are companies that can deliver returns of several hundreds or thousands of percentages." Grönblom and Blomster aim to identify the tiny fraction of all listed companies that create the bulk of broader market returns, a discovery documented by Professor of Finance Hendrik Bessembinder. "We have a firm belief that most market participants grossly underestimate the extent of this phenomenon and erroneously assume that returns are more or less normally distributed even over longer periods," considers Grönblom. "This is a weakness we seek to exploit."

Recent research highlights the increasing relevance of innovation-related intangibles as drivers of economic growth in recent years and decades. This environment has facilitated the emergence of superstar firms such as Google, Apple, Facebook, Amazon, and Microsoft, which dominate their markets in terms of sales, profits, and returns. Grönblom and his investors have been among the beneficiaries of this winner-takes-all market, having made early investments in Amazon, PayPal, and Facebook, to name a few.

A SLOW-TRAVELING IDEA

Grönblom believes that the concept of "slow-traveling ideas" proposed by Jack Traynor explains why market participants systematically underestimate the potential of superstar companies. Slow-traveling ideas refer to ideas or trends that take time to gain widespread acceptance and recognition. One of Grönblom's long-held slow-traveling ideas revolves around network effects or demand-side economies of scale, which played a crucial role in capitalizing on the significant value creation of Amazon and Facebook. The Asilo team finds demand-side economies of scale intriguing for several reasons.

"First of all, network effects have a significant impact on the strategic positioning of a select few firms that enjoy truly sustainable network effects, creating and fortifying their economic moats," states Grönblom. Second of all, with network effects being a slow-traveling idea, many market participants still vastly underestimate the power of network effects. "Surprisingly often, you can find many cases where the market underestimates the power of network effects and thus underprices the security," says Grönblom.

Professor of Physics Albert A. Bartlett argued that the greatest shortcoming of the human mind is our inability to intuitively understand exponential growth. Grönblom applies this conclusion to investing, stating, "Humans are not mentally primed to intuitively grasp exponential growth or compounding growth." He further explains, "20 years ago, it was very hard for people to comprehend the potential size of a company like Amazon because it was difficult to intuitively accept the enormous numbers the company would eventually reach. I am not saying that all companies will achieve exponential growth, and only a few will sustain it for a prolonged period of time, but certain companies have that potential."

"And what our job, to a significant degree, through studying history, economic theory, and market psychology, is to identify the characteristics that enable us to pinpoint the tiny minority of companies with the potential for prolonged exponential growth," emphasizes Grönblom. Superstar companies share several common characteristics compared to their peers. Alongside capturing a greater share of income and outperforming peers, superstars exhibit relatively higher levels of digitization, greater labor skill and innovation intensity; and more intangible assets. "We study economic history to identify the characteristics that set these companies apart from the average or norm."

SECTOR DIVERSIFICATION AND THE IMPORTANCE OF VALUATION

Although the information technology (IT) sector commonly houses companies with network effects, Asilo Argo maintains a well-diversified portfolio ranging across various sectors, including healthcare, hospitality, transportation, consumer discretionary, and energy, among others. Network effects can be found across most sectors. "Having a diversified portfolio across different sectors was not a conscious decision, but it offers significant benefits because certain industries such as hospitality may exhibit a different cyclicality compared to sectors like semiconductors," Blomster explains.

Existing or potential superstar companies targeted by Asilo Argo often trade at seemingly high valuations, or rather, high traditional valuation multiples. Nevertheless, Grönblom and his team attempt to buy these superstar companies at a substantial discount to their estimated intrinsic values. "We build a comprehensive valuation model where we look at the valuation level and ask ourselves if it's reasonable or achievable," says Blomster. "Valuation is a crucial part of the process, but it typically comes after the security analysis and qualitative analysis." Longer term, however, being accurate on the direction of the business is more important than the current detailed valuation. According to Keynes, "It is better to be approximately right than precisely wrong." This very much applies when hunting for superstars.

> "A concentrated portfolio gives us enough time to validate our view of the big picture and identify the aspects that are misunderstood by the market."
>
> Henri Blomster

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Eric Strand, Founder and Portfolio Manager – AuAg Funds

Gold Stays Gold, Forever

By Eugeniu Guzun – HedgeNordic

Gold has delivered an annual return of about 7.7 percent in U.S. dollar terms since August 15, 1971, the day U.S. President Richard Nixon removed the U.S. dollar from the gold standard. Eric Strand, a precious metals specialist who manages the fund boutique AuAg Funds, offers a different perspective on this development. At an annual rate of 7.7 percent, "the U.S. dollar has experienced a cumulative devaluation of 97 percent relative to gold since the historic date of August 15, 1971." Strand considers gold as the unchanging benchmark and measures the development of fiat currencies in relation to gold.

Despite gold's proven effectiveness as a hedge against the erosion of purchasing power over the past 50 years, Nordic institutional investors have broadly refrained from including this precious metal in their portfolios. "It is very strange that institutional investors overlook gold when, based on return tables, the metal exhibits a very stable return profile. Since 2000, it has had only three negative years compared to eight for the broader equity market," wonders Strand. He emphasizes gold's stability, attractive returns, low correlation, high liquidity, and absence of counterparty risk.

"The U.S. dollar has experienced a cumulative devaluation of 97 percent relative to gold since the historic date of August 15, 1971."

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"Investing in gold miners is a leveraged bet on gold because their production costs remain relatively static while their revenue rises and falls with the price of gold."

By incorporating exposure to metals such as gold, institutional investors can enhance their allocation to alternative investments and benefit from a distinct return stream that is relatively uncorrelated with other asset classes. AuAg Funds, a fund management boutique with a focus on precious metals and green tech elements, has introduced an innovative investment product – an exchange-traded fund (ETF) that invests in a select group of ESG-friendly gold mining companies. This ETF aims to provide both larger institutional investors and smaller investors with a leveraged play on the price of gold, without relying on financial leverage. "Investing in gold miners is a leveraged bet on gold because their production costs remain relatively static while their revenue rises and falls with the price of gold," says Strand.

This means a miner's profits increase faster than the price of gold. To illustrate the operational leverage of gold miners, Strand offers an example: "Suppose the price of gold is $2.000 and a miner's mining costs amount to $1.500. In this case, the miner would generate a net profit of $500." He continues, "Now, if the price of gold increases by ten percent to $2.200, the miner's net profit would rise to $700 given the static production costs." This increase in net profits from $500 to $700 implies a 40 percent gain for a ten percent increase in the price of gold.

AUAG'S INNOVATIVE ETF SOLUTION

Investor demand for exchange-traded funds (ETFs) has been steadily increasing and is expected to continue due to their appealing features, including low cost, simplicity, transparency, and liquidity. Recognizing this growing demand, Strand decided to design and launch an ETF that offers Nordic and European investors a novel opportunity to gain exposure to gold through investments in gold miners. "With major players such as iShares and VanEck in this space, we wanted to offer something better," explains Strand.

The AuAg ESG Gold Mining UCITS ETF (Ticker: ESGO) developed by Strand has three distinct features: non-market-cap weightings, less portfolio concentration risk than a market-weighted index, and a best-in-class sustainability-aligned portfolio. The ETF also boasts a competitive annual cost of 60 basis points, which is lower than that of traditional funds. The ETF currently trades on the London Stock Exchange, Deutsche Börse Xetra, Borsa Italiana in Milano, Euronext in Paris, and Zürich.

The initial step in creating the ETF involved developing an index with the German index provider Solactive. Strand's first decision was to avoid the traditional market capitalization-weighted structure employed by most ETFs. "While a market-cap-weighted ETF is generally beneficial, in relatively smaller sectors such as gold mining, a market-cap-weighted structure would result in two or three large companies accounting for 35 percent of the ETF's exposure," explains Strand. Aside from this concentrated risk, mega-cap companies within the sector may deliver smaller returns in a bull market compared to large and mid-cap gold mining companies. By design, the AuAg ESG Gold Mining UCITS ETF maintains a higher exposure to mid-sized mining companies compared to a market-cap-weighted ETF.

To address these concerns, the UCITS-structured ETF has 25 companies equal-weighted at four percent, resulting in more allocation towards mid-cap miners. This relatively concentrated portfolio is designed to offer diversified exposure to gold miners without diluting the exposure through excessive diversification, or diworsification. "We prefer concentrated portfolios because, as active managers, we can closely monitor all our investments within a concentrated portfolio," explains Strand. "Having 25 companies in a portfolio is sufficient for achieving diversification, demonstrating our strong belief in this select group of companies."

Another important reason behind the relatively concentrated portfolio is Strand's emphasis on investing in the "best-in-class" gold mining companies from a sustainability perspective. "We select the top 25 best-in-class miners based on their ESG risk scores using data provided by Sustainalytics," explains Strand. "Our portfolio is rebalanced quarterly to invest in the 25 best-in-class companies, favoring the adopters and excluding the laggards," he elaborates. "This approach not only aligns with sustainability goals but also incentivizes positive change within the mining industry. Inclusion in our ETF may not be their largest focus, but we view this as a mechanism to promote change and continuous improvement in ESG scores among mining companies."

Classified as an Article 8 fund under the SFDR, the AuAg ESG Gold Mining UCITS ETF also ranks in the 79th percentile within the global universe of approximately 34,000 funds in coverage, according to the MSCI ESG Fund Ratings. These ratings are designed to measure the Environmental, Social, and Governance (ESG) characteristics of a fund's underlying holdings.

THE BENEFITS OF GOLD AS A COMMODITY AND AS AN INVESTMENT

Strand sees gold as having two distinct narratives: one as a commodity with essential uses in various technologies, and another as an uncorrelated investment that protects against purchasing power erosion. "Gold has two different stories," starts Strand. "Due to its unique physical properties, around ten percent of all mined gold goes to industrial and technological applications serving a crucial role in various sectors such as computing, telecommunications, automotive, aerospace, medicine, and beyond," he elaborates. Gold's usage in technology contributes to its demand and adds a layer of fundamental support to its market dynamics. "Gold and precious metals are enablers for a lot of solutions."

On the monetary side, gold is recognized as an investment that protects against the loss of purchasing power and economic uncertainties. "Gold serves as a hedge against monetary inflation. Its price reflects the unabated amount of debt creation and money printing," explains Strand. "Short-term, price inflation may come from many different sources. But longer term, price inflation is a result of monetary inflation."

Strand argues that instead of enduring a severe recession, central banks opt to stimulate economies and financial systems at the first indications of economic difficulties. "That would mean monetary inflation again because nobody wants to go through a hard recession anymore. A recession may be a good thing to force inefficient businesses to restructure or exit the market, but nobody wants to experience that. No politicians normally survive it, so it's not going to happen. Incentives are there for more monetary inflation and that will be good for gold and gold fund

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The Veritas Approach to Building a Well-Rounded Equities Portfolio

By Eugeniu Guzun – HedgeNordic

Pension funds play a vital role in safeguarding the financial futures of millions of individuals. Equities serve as the cornerstone of institutional portfolios due to their significant potential for long-term growth, ability to hedge against inflation, capacity for diversification, and potential for income generation. Veritas, a Finnish pension fund responsible for managing €4.3 billion in assets, employs a comprehensive range of strategies and investment styles to construct its equity allocation, guided by its solvency framework.

The pension fund's investment team adopts a diverse set of approaches, carefully weighing active versus passive management, external versus internal management, and systematic versus discretionary strategies. This multifaceted approach allows Veritas to optimize its equity allocation in a manner that aligns with its solvency objectives. "The amount of risk that we can bear in the portfolio comes directly from the solvency framework that we need to follow as a pension company," explains Tapio Koivu, Portfolio Manager at Veritas. "Equities are typically the biggest risk contributor in the portfolio, and the solvency framework defines how much equity risk we can have."

"It is not just about getting the equity weight right; it is also quite important to decide where you want to be in the equity market."


Tapio Koivu, Portfolio Manager – Veritas

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While the solvency framework provides the big picture for asset allocation, there is room for fine-tuning based on the team's allocation views and assessment of the attractiveness of different asset classes. "The solvency framework defines the absolute upper limit for the equity allocation, but we have more room to be active below that upper limit to try to adjust the equity allocation appropriately based on our views," says Koivu. "It is not just about getting the equity weight right; it is also quite important to decide where you want to be in the equity market," he continues. "In recent years, there have been significant variations in equity returns among different regions, sectors, factors, and more. At times, choosing the right equities exposure becomes more important than determining the equity weight."

INTERNAL MANAGEMENT: DISCRETIONARY VERSUS SYSTEMATIC

As of the end of the first quarter of 2023, Veritas Pension Insurance had 31.6 percent or €1.35 billion of its investment portfolio allocated to listed equities. A sizable portion of this equity portfolio is managed in-house, primarily focusing on local Finnish equities and select European stocks. For investments outside Finland, Veritas utilizes external vehicles, including passive exchange-traded funds (ETFs) and actively-managed funds.

"It's fair to say that we have certain home bias, especially when comparing our portfolio to a global benchmark," begins Koivu. "Domestic equities are not less risky than global equities, but there are other benefits to investing in them." One of the main reasons for managing a sizable portfolio of Finnish equities in-house is the ability to engage in discussions with company management to promote its own ESG agenda. "We can easily follow up with Finnish companies, share our own views and suggestions if appropriate. In that sense, overweighting the home market is justified."

From a risk management perspective, Veritas recognizes the importance of building a well-diversified equity portfolio across regions. "But there's no one simple formula for deciding the exact right amount of exposure to local or global equities,"

> "The decision between active or passive management is based on our belief in the value creation potential of active management in specific markets."

acknowledges Koivu. Despite the relatively small universe of Finnish listed companies, the investment team at Veritas conducts thorough stock picking to build its portfolio of Finnish stocks. "We conduct traditional bottom-up stock picking. The universe is relatively small, so we know most companies quite well after following and analyzing them for a long time," explains Koivu. "Even though we engage in pure stock picking, we need to pay attention to specific features of the market to maintain appropriate sector weightings, for instance."

In contrast to the in-house approach for Finnish equities, Veritas relies on a more quantitative process to invest in the broader European market due to the market's size and the team's capacity. "Direct investments in European stocks are mostly driven by a quantitative process rather than a qualitatively-driven fundamental analysis in Finland," according to Koivu.

EXTERNAL MANAGEMENT: ACTIVE VERSUS PASSIVE

Veritas aims to establish a robust and diversified structure for its equities portfolio by combining in-house investments, outsourcing certain investment activities, and leveraging various investment instruments. This strategy allows Veritas to achieve optimal diversification and benefit from the expertise of both internal and external investment professionals, ensuring a well-rounded equities portfolio. "The decision on whether to internally manage or use external actively-managed funds or passive ETFs depends on several factors, including costs," begins Koivu. "In some areas, it is cost-efficient to manage investments in-house, but that requires the necessary capabilities."

Investing in emerging markets, the US, and other markets presents different challenges. "In emerging markets, we need to find specialists who understand those markets, dive deep into them, and have the necessary resources to cover them," says Koivu. "As a relatively small organization, we cannot handle everything ourselves. When it comes to investing in global markets, the most significant and challenging decision revolves around allocation, ensuring that we are allocated to the right places."

For exposure to US equities, Veritas primarily relies on low-cost passive ETFs. Koivu notes the struggles of many active managers to outperform benchmarks in the US market due to its efficiency and market structure dominated by a few large companies. "The decision between active or passive management is based on our belief in the value creation potential of active management in specific markets."

Veritas also uses an active approach to selecting the right exposure even when using ETFs. "When investing in ETFs, we don't merely invest in the S&P 500, EuroStoxx 600, or MSCI Europe. Even though it's passive, we actively select different passive instruments to achieve the desired exposure," explains Koivu. "We can also use factor-based ETFs that differ significantly from the market benchmark. In summary, we have the tools to adjust our portfolio as markets change. Different periods and market environments require different solutions, and we strive to be flexible investors with the readiness to change."

Veritas takes a regional approach when building and assessing its equities portfolio. Within each region, the pension fund employs various approaches to build equity exposure, whether through in-house investments or external management via funds or ETFs. "Our job is to find managers who do a good job in their own universe or area. It is then up to us to select the right mixture of different managers, passive instruments, and individual equities to ensure that the overall portfolio reflects our own view and thinking."

Trend Following in Equities

By Nicolas Rabener, CAIA – Finominal


Nicolas Rabener, Founder and CEO – Finominal

Imagine a world where economic growth is anaemic. Governments and central banks do everything to stimulate growth, but their powers have weakened over time to the extent that even the most extreme fiscal and monetary policies have only a short-lived impact.

Although such a scenario sounds utterly depressing, it is difficult not to see that we are on its trajectory. Economic growth is a function of productivity and the working-age population. Despite all the technological innovation, productivity has not increased in most developed countries over the last decade. And demographics are poor across developed and emerging markets, e.g. China is expected to lose 400 million people over the next 80 years.

HOW DO YOU INVEST IN SUCH A WORLD?

Real estate, aside from nursing homes, will be unattractive given large vacancies. Governments won't be able to repay debt as their taxable populations are shrinking and they have to deal with exploding healthcare and pension costs. The demand for commodities will be reduced as there is less construction and industrial activity happening. Traditional diversification will fail to provide the desired benefits as they all represent bets on positive economic growth.

HOW ABOUT EQUITIES, OR EQUITY PROXIES LIKE PRIVATE EQUITY OR VENTURE CAPITAL?

Well, corporations will still aim to generate a profit for their shareholders, although this will be more difficult when economic growth is low or negative. Stocks might simply go as investors do not like the alternatives, but an elderly population does also not like to take too much risk. The long-term outlook for equities is unclear.

Instead of the traditional buy-and-hold approach to stocks, investors may consider applying a trend-following strategy to equities, which we explore in this article.

TREND FOLLOWING IN EQUITIES

Trend following funds, which are also known as CTAs or managed futures funds, have had a comeback recently given strong performance in 2022.

The basic strategy is to buy asset classes that are trending upwards, and short ones that are performing poorly. The resulting portfolio is typically diversified across all asset classes and frequently changes its positions.

We will focus on the US stock market and apply four simple trend-following strategies. Each portfolio is rebalanced monthly and performance is evaluated with a one-day delay so that implementation is

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realistic. Trading costs are ignored, but the portfolios do not change frequently within one year. Long-term long-short trend following: Long equities if the 12-month performance is positive, short equities otherwise

Long-term long-only trend following: Long equities if the 12-month performance is positive, hold cash otherwise

Short-term long-short trend following: Long equities if the 1-month performance is positive, short equities otherwise

Short-term long-only trend following: Long equities if the 1-month performance is positive, hold cash otherwise

We observe that none of the four trend-following strategies outperformed the US stock market in the period between 1927 and 2023. However, long-term long-only almost achieved the same return, while short-term long-short performed worst.

Pursuing trend following in equities can be challenged as bull markets tend to be long and bear markets short, which makes it difficult to exploit trends with the same model assumptions.

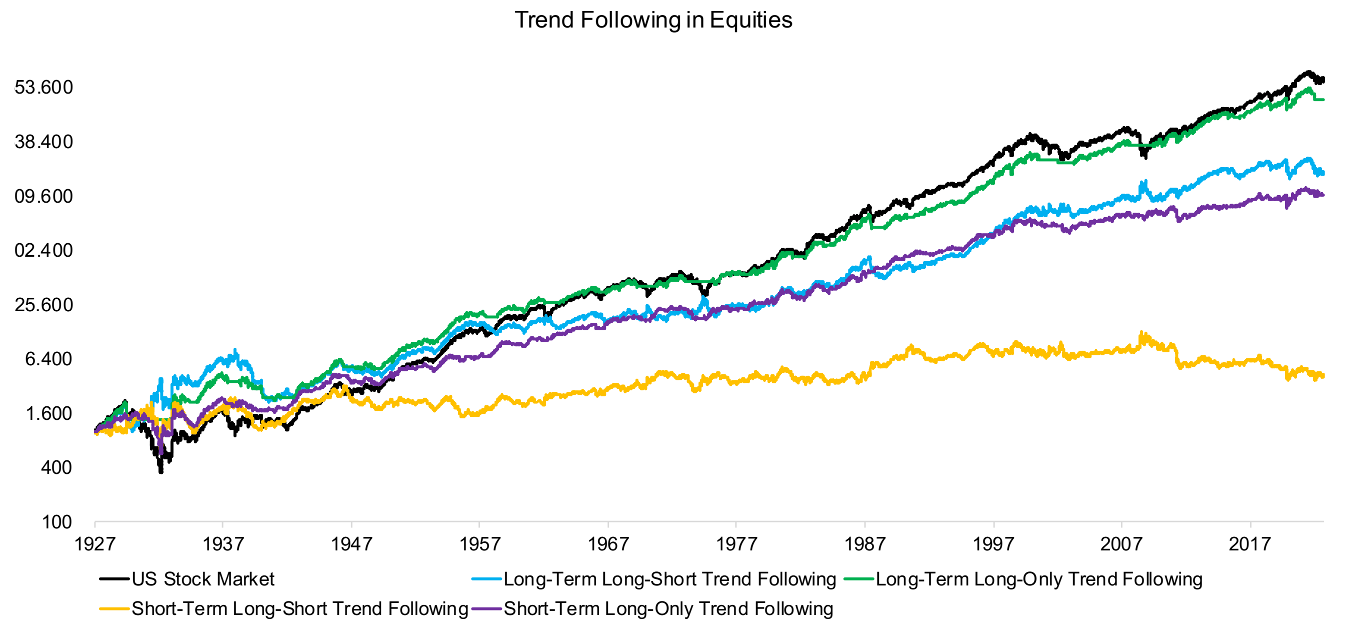
In contrast, other asset classes like commodities feature bull and bear markets that are more similar in duration. Stated differently, stock market returns are negatively skewed, which perhaps makes them sub-optimal for applying trend-following strategies.

The analysis highlights that long-term trend following in equities generated higher returns than short-term trend following, which broadly reflects the approach of the CTA industry. Although there are some CTAs that focus on short-term trends, even intra-day time frames, most use lookbacks of up to a year for evaluating the performance of asset classes.

SHARPE RATIOS

Analysing the Sharpe ratios of the four trend-following strategies highlights that the long-only ones generated attractive risk-adjusted returns. Although we have ignored transaction costs, which decrease returns, we have also ignored reinvesting cash into interest-bearing bonds, which would have increased returns.

The relatively high Sharpe ratio of the long-term long-only trend-following strategy can be explained by this broadly participating in the major bull markets



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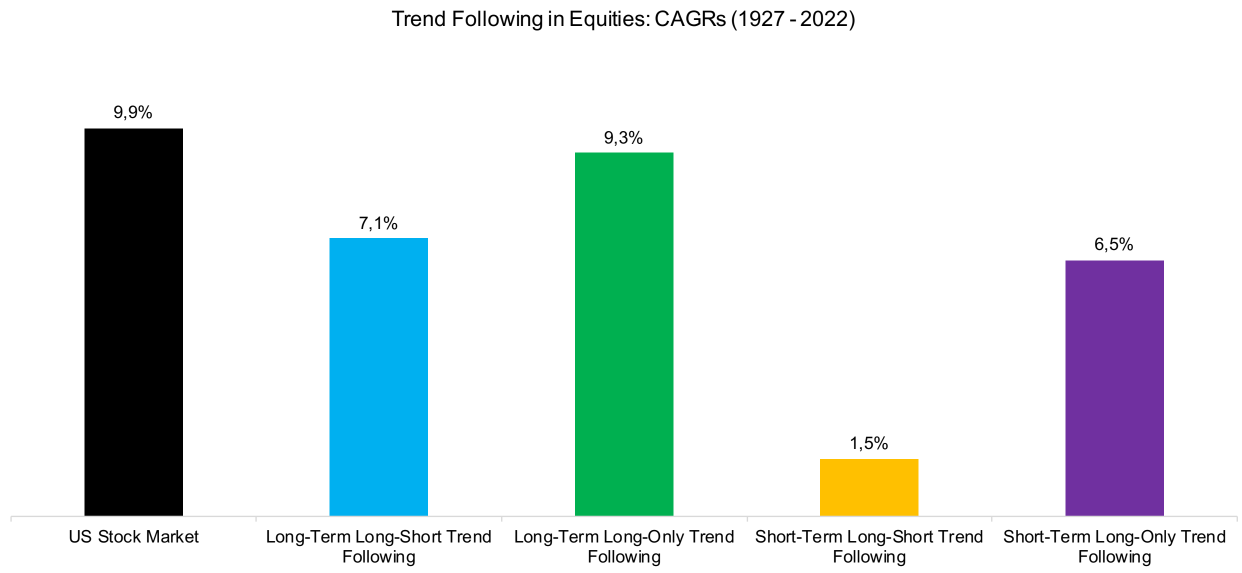

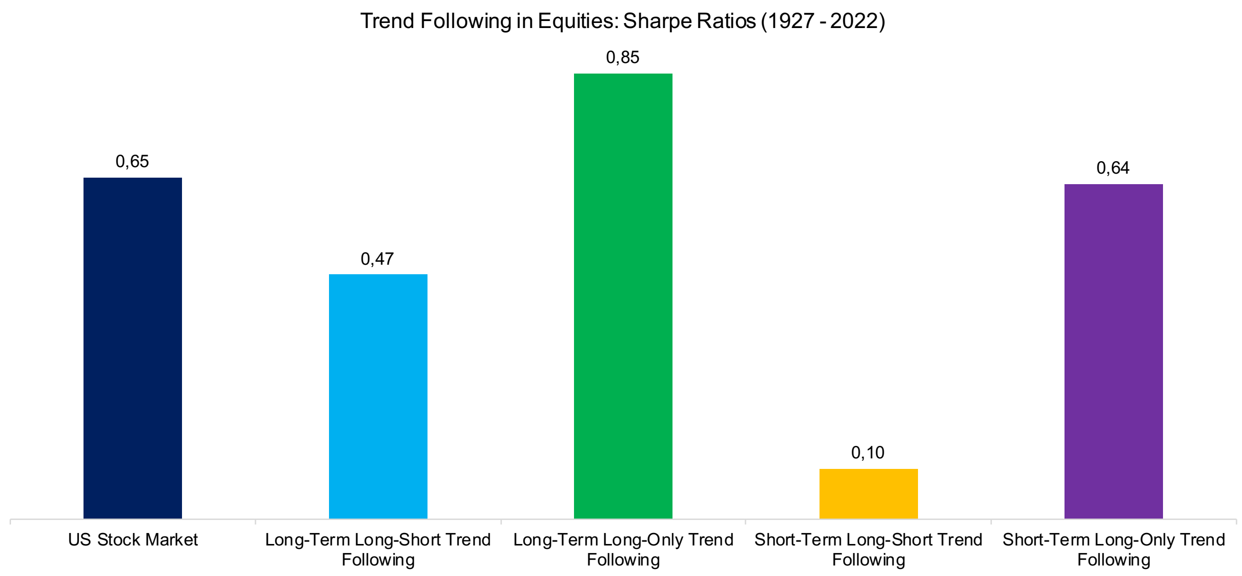

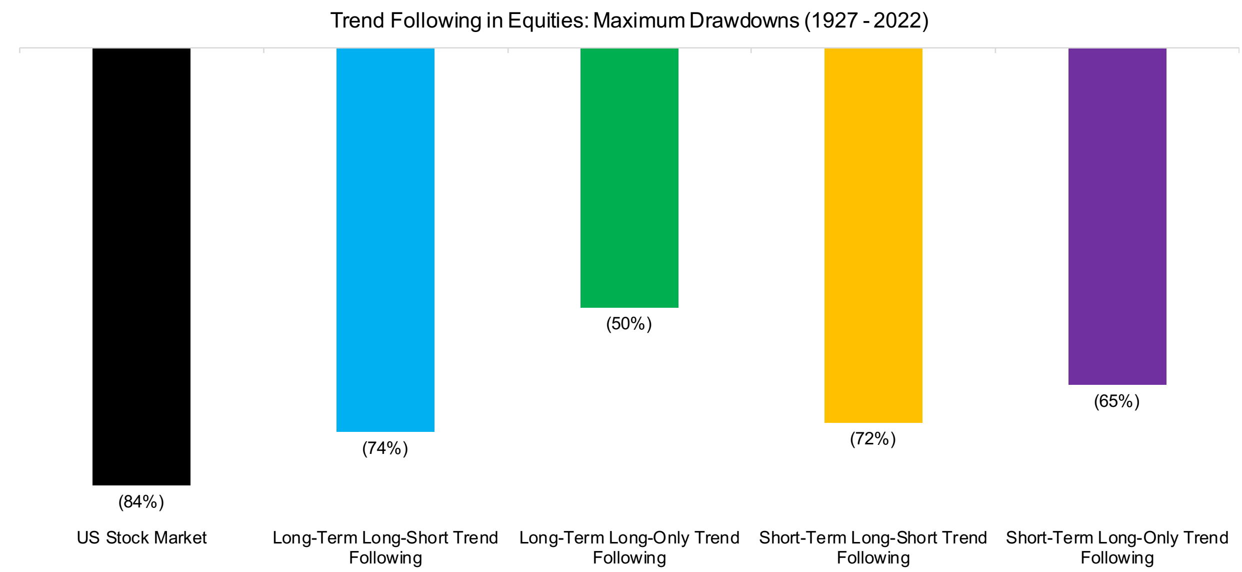

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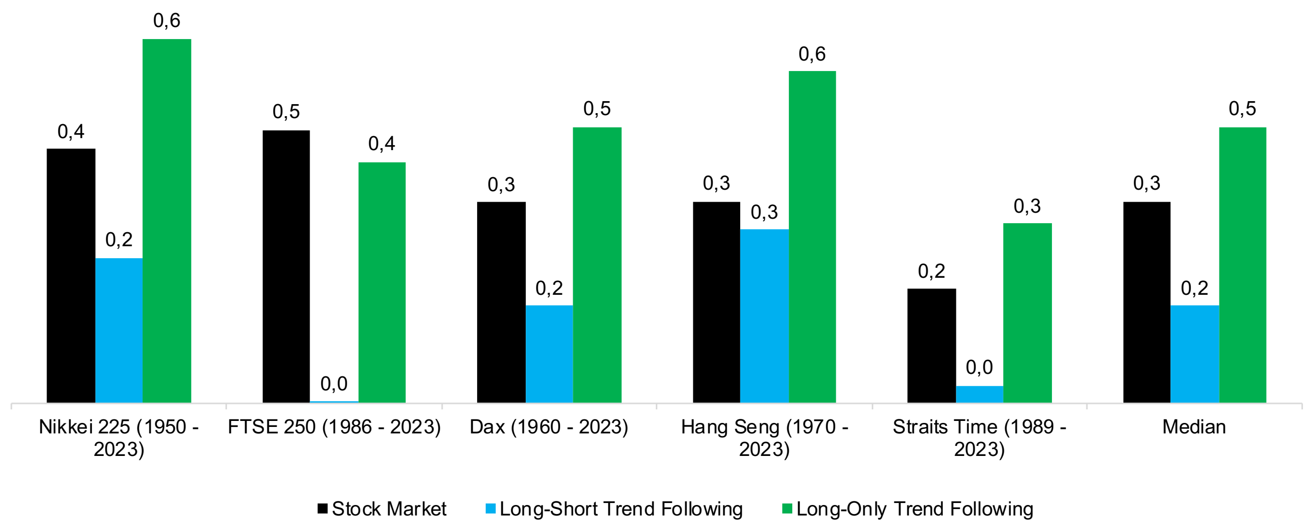
Trend Following Across Stock Markets: Sharpe Ratios



Source: Finominal

of the US stock market, but reducing the exposure to equities during bear markets. We observe that the maximum drawdown was below 50%, compared to 84% for the stock market in the period from 1927 to 2023.

It is worth highlighting that trend following does not protect against stock market crashes like in 1987 as it takes time for these strategies to switch from long to short or into cash. Investors need to consider tail risk or long volatility strategies for hedging stock market crashes.

INTERNATIONAL EVIDENCE

Finally, we evaluate the performance of the long-term trend following strategies across five European and Asian stock markets, where the starting point of the data ranges from 1950 to 1989.

We observe that long-short trend-following strategies generated significantly lower Sharpe ratios than long-only trend-following strategies, whose returns were even better than from buy-and-hold stock market exposure.

FURTHER THOUGHTS

Given the poor long-term outlook for investing, would trend following help?

Japan can be used as a case study as it is ahead of the rest of the world in terms of a declining population. Economic growth has been anemic and its stock market features a long bear market between 1989 and 2010. The results from this analysis do not highlight that long-short trend following was effective when applied to the Nikkei 225, although long-only trend following generated attractive risk-adjusted returns.

Long-only trend following in equities combined with long-short trend following in other asset classes may be an attractive combination. After all, there is a difference between betting on the decline of copper or a currency like the Japanese Yen versus betting against the ingenuity of highly incentivised CEOs and entrepreneurs.

Jonas Thulin, Head of Asset Management – Erik Penser Bank

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The Art of Tactical Investing

By Eugeniu Guzun – HedgeNordic

Managing an investment portfolio can involve a wide array of approaches and strategies. Erik Penser Bank, a Swedish private bank, distinguishes itself through its active approach to managing investment portfolios for its wealth management clients. The bank's Head of Asset Management, Jonas Thulin, believes in the importance of adapting allocations based on the prevailing market environment, allowing them to seize opportunities and effectively navigate through changing market conditions. Erik Penser Bank extends this active mindset to all investor portfolios, including their equity components.

"To put it simply, we quantify the macroeconomics to decide on our allocations," starts Thulin. The team at Erik Penser Bank has developed an econometric quantitative framework that analyzes a vast amount of high-frequency data on technical, fundamental, economic, liquidity, valuation indicators, and more, to better understand the current macro environment. "The framework uses artificial intelligence to analyze all the macro and financial stress data every single day," he explains. Thulin emphasizes that their concept of macro data includes a wide range of financial stress data beyond just GDP and industrial

"To put it simply, we quantify the macroeconomics to decide on our allocations."

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“A lot of old-school portfolio theories have been put to shame and the importance of tactical work has increased.”

data indicators. “For us, macro data includes a lot of financial stress data such as spreads, and liquidity pricing as well. All that is macro data to us, too.”

NO REASONS TO BE UNDERWEIGHT EQUITIES

Through a daily evaluation process, the econometric framework provides insights into asset class positioning, such as equities, for the next 12 months. “Statistically, our average holding period for an equity strategy is six months. We change the broader asset allocation once or twice a year, not more than that,” explains Thulin. In recent years, there have been few reasons to be underweight equities, even with the onset of the coronavirus pandemic. “We haven’t seen a reason for quite some time to be underweight equities,” emphasizes Thulin.

Even if investors have concerns about their equities exposure, there have not been any traditional alternatives, according to Thulin. “If your alternative is bonds, for example, being overweight equities would have been a better choice for the past three years,” he says. Thulin highlights that the allocation decision process takes into account alternatives to equities. “It is not an equity call by itself.”

The market environment of the past few years has underscored the importance of employing a tactical asset allocation approach. Thulin provides an example, “Let’s say you were overweight equities going into 2022 and all of a sudden we have this horrible war. Then we realize that rates will be equally as bad as equities in this environment due to continued rising inflation.” In such cases, simply shifting out of equities or adopting a neutral stance would not be sufficient. “We cannot just shift out of equities and pretend that we are doing a good job. We have to work smart tactically.”

Erik Penser Bank can use spreads by taking long positions in one sector and short positions in another and can use derivative overlays, covered calls, or volatility protection within its equity strategies. “We work tactically with the risk exposures.” Instead of making hasty decisions based on nervousness and shifting funds to bonds, Thulin believes that working tactically within the equity market has proven to be a better choice.

Thulin notes that the period from 2020 to 2023 has been unique in that the maximum drawdown in bonds and equities was equal. “But only equities had upside, he highlights. “If you started with $100 on January 1, 2020, knowing that we would experience a pandemic, lockdowns, subsequent waves, a war, and skyrocketing inflation, many people might have thought it would be better to be risk-neutral or even underweight equities,” says Thulin. However, up to the present date, that has been a completely wrong call. “This has been a very specific period that we have gone through. A lot of old-school portfolio theories have been put to shame and the importance of tactical work has increased.”

TRANSITION FROM FROM LOW GROWTH, HIGH INFLATION TO LOW GROWTH, NORMAL INFLATION

Erik Penser Bank’s econometric model identified a transition from a low growth, high inflation to an environment of low growth and normal inflation. This shift altered Thulin’s views on the trajectory of equity markets. “Up until last June, we had cash, short positions, volatility overlays, and a lot of dollar investments to minimize risks coming from our equities exposure,” explains Thulin. Realizing that a paradigm shift was approaching with the peak of inflation, Thulin and his team could anticipate where the pivot would happen.

“There are a lot of definitions of what the pivot from the Fed is. But if you look at the maximum momentum of aggressive hiking priced into the market, that was in October last year,” explains Thulin. “We could see that already during the summer and realized it was the time to shift out of those positions and increase the exposure to equities. And that’s what we did.”

Expecting lower interest rates due to the transition to a low-growth, normal inflation environment, Thulin and his team increased exposure to longer-duration equities – particularly in “growth” companies. These are expected to generate the bulk of their cash flows in the distant future. “We are strong believers in very narrow and specific tech industries such as artificial intelligence, cybersecurity, and semiconductors, among others,” says Thulin. This belief has led them to build select exposure to markets like India and South Corea. “We are also ridiculously overweight US tech for the time being.”

PROCESS

Erik Penser Bank’s active mindset starts by scanning over a million equity products every single day. “We start every day with a white paper, then survey the market and bring on board all the funds out there, including ETFs, ETNs, mutual funds, UCITS, non-UCITS, everything. Then we have the quantitative framework that identifies the best strategies for our mandates given by our customers.” They have specific requirements regarding volatility, Sortinos, returns, and more, resulting in a top list of strategies.

The team then compares this list with the existing portfolio exposure. “If the list is dominated by Nasdaq and tech today, we don’t have to do anything because we are already fully invested. We do also consider the macro perspective and evaluate if this exposure makes sense, and how the market has priced in future developments compared to where inflation is headed.”

Thulin points out that their investment decisions are not always complex but rather involve identifying trigger points and straightforward analysis. By accurately forecasting macro trends, they have made successful investments in areas like artificial intelligence, which have yielded solid returns. “It’s not rocket science all the time. It’s just a question of deriving the trigger points, which are quite fairly straightforward.”

What Drives the Rise in Equity Value, Where Is It Headed?

By the Swedish House of Finance

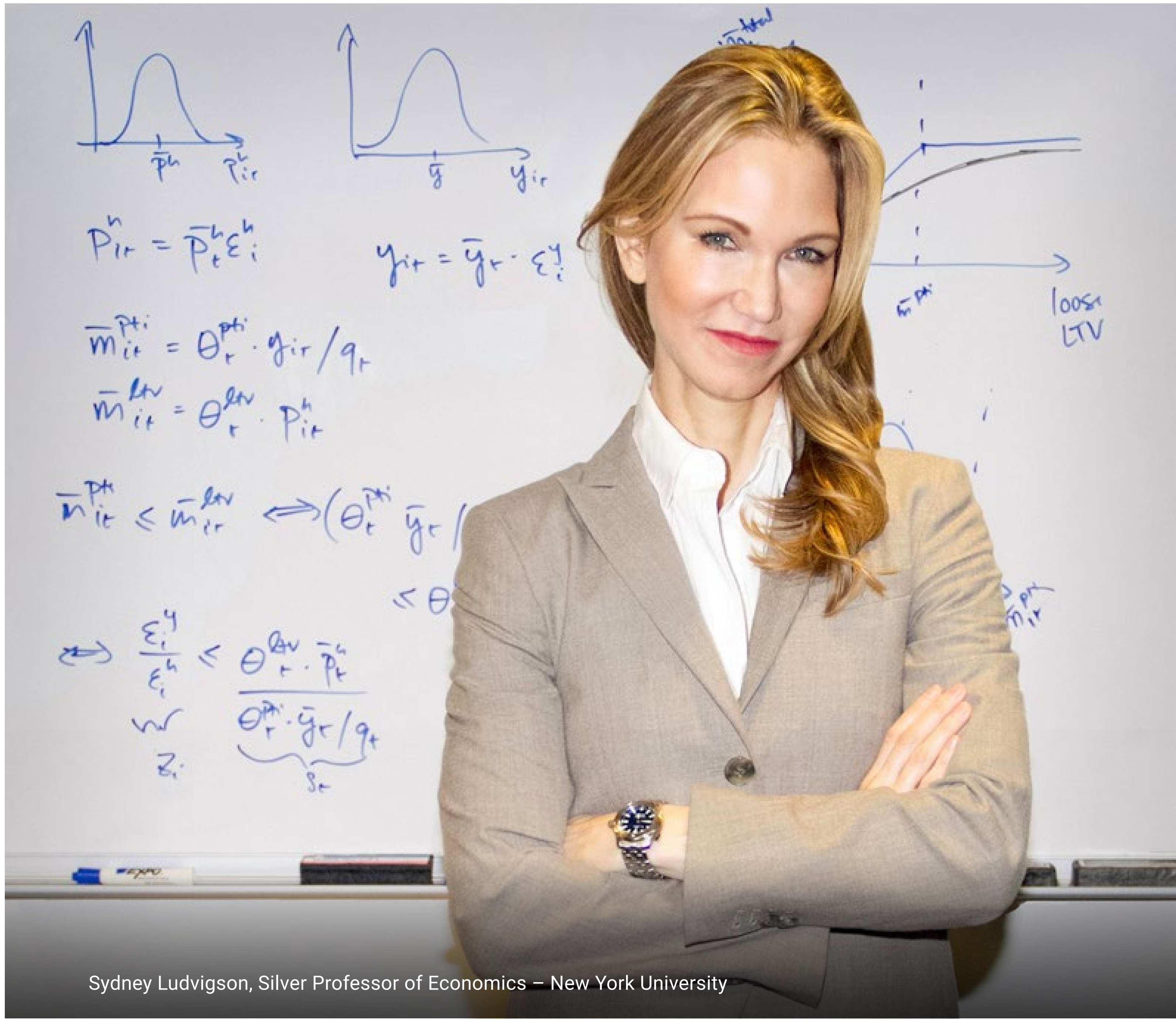
> "Valuations remain high by historical standards, even though markets declined about 20% last year."

By the Swedish House of Finance, Sweden's national research center in financial economics: NYU's Sydney Ludvingson discusses drivers of equity value growth, the risks associated with high valuations and rising interest rates, and how policymakers and investors can mitigate those risks.

WHAT ARE THE KEY FACTORS THAT HAVE SIGNIFICANTLY INFLUENCED THE RISE IN EQUITY VALUES SINCE THE POST-WAR ERA?

"It is useful to take note of two striking patterns in the data over the post-war period.

The first is equity cash flows, or the earnings and profits generated by a company that are distributed to its shareholders as a return on their ownership. These payouts represent measures of fundamental value to the stock market. According to textbook theories, the stock market and the broader economy should share a common trend, implying that the same factors that boost economic growth, are also the key to rising equity values over longer periods of time.



Sydney Ludvigson, Silver Professor of Economics – New York University

Yet if we look at the post-war period, economic growth averaged only 2.6% per annum in the 1989-2017 period compared to 3.9% in 1966-1988, while the real value of market equity of the U.S. corporate sector grew at an average rate of 7.5% per annum over the 1989-2017 period, compared to only 1.6% over 1966-1988. Why? Despite lower growth, the 1989-2017 period exhibited growth in after-tax corporate profits of 5.1% per annum, far outpacing the 1.8% profit growth of 1966-1988.

This implies that there was a markedly higher profit share of output in 1989-2017 compared to 1966-1988. Our estimates suggest that these shifts in the share of rewards going to equity holders alone explain around 45% of the increase in equity values over the past 30 years.

The second striking pattern in the data is related to discount rates, which refer to the rate at which future cashflows, such as earnings or payouts, are adjusted or discounted to their present value. Changes in interest rates influence the short-rate component of the discount rate, which in turn can impact equity values.

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We find that periods of accommodative monetary policy align with consistently high stock market valuations, while restrictive periods coincide with low valuations.

The 1978-2001 period was characterized by a restrictive monetary policy with low valuations. In 2006-2008, just before the Global Financial Crisis, also saw somewhat restrictive policy, but to a lesser extent. Most of the last 20 years and all of the last 15 years had accommodative regimes with high equity valuations."

WHAT ARE SOME OF THE RISKS ASSOCIATED WITH THE LEVEL OF EQUITY VALUES RIGHT NOW AND HOW CAN POLICYMAKERS AND INVESTORS MANAGE THESE RISKS?

"Valuations remain high by historical standards, even though markets declined about 20% last year.

This is because the run-up in equity values even in the last five years prior to these declines had been so rapid that stocks are still high relative to where they have been historically. Markets appear optimistic once more, rising at a healthy pace so far this year, even though they are still richly valued. As interest rates rise, there is a risk that markets will decline back toward more normal valuation levels."

HOW CAN POLICYMAKERS AND INVESTORS MANAGE THESE RISKS?

"Lower equity return premiums are associated with declines in the federal funds rate (FFR) due to policy regime change, while increases in the FFR from policy regime change are linked to higher equity return premiums. This relationship is found only for policy-driven changes rather than general movements in short rates.

This type of correlation can happen if markets/ investors have a form of 'fading memory' of past policy rules. Once investors have spent enough time in a particular policy regime, memory of past policy rules fades, and they come to view the existing policy stance as the new normal. Investors extrapolate too much from the observed continuity in the policy stance, so that the perceived persistence of policy regime shifts overstates their true persistence. Fading memory of past policy rules means that investors overreact to policy shifts and are always surprised by the inevitable transition out of the existing policy regime.

> "If investors believe these rate increases are likely to reverse soon, equity values may continue rising again."

The risk something like this would create for the Fed and other central banks currently is that markets/ investors may have a harder time buying into the idea that the accommodative policy regime they had become accustomed to over the last 15-20 years has been replaced by a truly restrictive policy stance.

This is despite the ten nominal rate increases recently which, given the persistently higher inflation, have not led to very high real rates especially at the short end of the term structure, at least not yet. Due to the recent history of prolonged accommodative policy, markets may continue to price in the expectation of a quick pivot to lower rates if an adverse shock occurs, even if inflation remains stubbornly well above the central bank's long-term objective of 2%. Markets may not fully believe the inflation-fighting resolve of central banks.

One could speculate that expectations of this form are partly why markets have risen healthily this year, despite the increased odds of a recession. To the extent that this creates additional inflationary pressure, which the Fed seems to worry about as a real possibility, this is not helpful to their objectives.

Managing these risks is likely going to involve persistent, clear communication, about the precise conditions under which investors should expect a rate cut and how central banks will credibly handle a conflict between the twin objectives embedded in their dual mandate, should those in fact become at odds with one another."

HOW HAVE POLICY MAKERS BEEN MANAGING THESE RISKS SO FAR?

"It is a tough line to walk, especially as central banks are also learning in real time.

You can see the efforts with communication by policymakers directed at markets. You can also see hints that markets are not very clear or convinced about how central banks will handle complications to their plans, such as a banking crisis, a default on U.S. debt, or a sharp downturn that creates stagflation.

Central banks could try to be even clearer on these aspects of their forecasts and plans, though this is admittedly challenging as it involves many contingencies and unknowns."

HOW WILL CHANGES IN INTEREST RATES AFFECT EQUITY VALUES IN THE YEARS AHEAD?

"Although short rates are on their way up now, which all else equal would tend to put downward pressure on stocks, it really depends on how persistent investors believe those rate changes will be.

If investors believe these rate increases are likely to reverse soon, equity values may continue rising again. If they believe the Fed and other central banks will persist in keeping them higher for longer, in the event that inflation remains stubbornly high, equity valuations could stay where they are or even decline again. Only time will tell."

Bio: Sydney Ludvigson is Julius Silver, Roslyn S. Silver, and Enid Silver Winslow Professor of Economics at New York University, and a Co-Director of the National Bureau of Economic Research Asset Pricing Program. Her research centers on the interplay between asset markets and macroeconomic activity, with applications to role of monetary policy in stock market fluctuations, the measurement and analysis of systematic and demonstrable errors in macroeconomic expectations by both professional forecasters households, the use of machine learning and AI algorithms to measure errors in human judgement, the pricing and risk premia of stock, bond, and housing markets, the role of heterogeneity and wealth inequality in housing and stock market valuations, and the dynamic causal effects of uncertainty for business cycle fluctuations.

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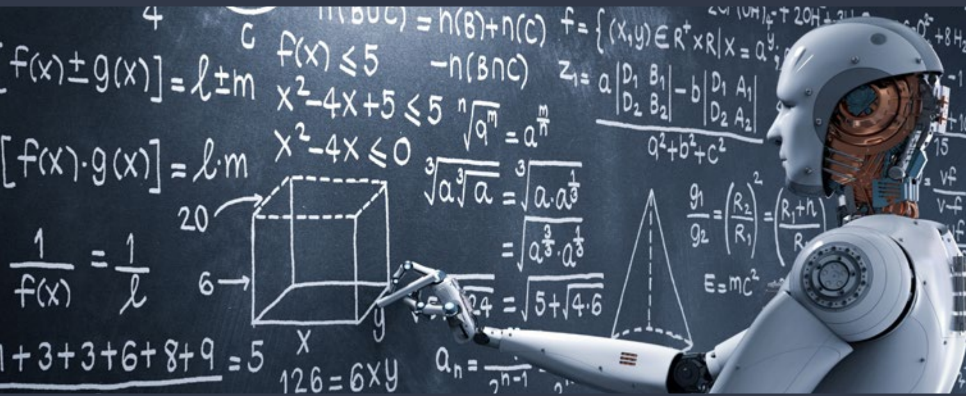

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