Allocation challenges in unpredictable times

At the end of last year Tell Media Group, in cooperation with **Blackrock** and **BNP Paribas Asset Managers**, gathered Swedish asset owners to discuss expectations going into 2024, some of the major surprises in markets and their views looking ahead to 2025.

By: **Niklas Tell** Photo: **Jennie Nyström**

The annual gathering of Swedish institutional investors to discuss asset allocation and the outlook for 2025, which was hosted in Stockholm in December, started with the investors sharing what they see as some of the key surprises over the past year.

CLAES AHREL: "I must of course highlight the strength of the equity market as the main surprise – especially the Nasdaq and the magnificent seven. I must also admit that I expected higher volatility during last year. Even if it increased during the second half, I think the VIX was around 15 on average and that's quite low considering what's going on in the world. I also expected higher energy prices. The price of Brent oil today is almost exactly where we started the year."

CECILIA THOMASSON BLOMQUIST: "I would also say that the strength of the equity market has been the big surprise, especially in the US, and the fact that concentrations continue to increase. I was also taken by surprise by the strong market reaction during the summer. That showed that it's quite fragile. Almost nothing happened and still you had this sell-off in the market. I also think it's interesting that equity markets continue to rise despite the fact that we now know that the Fed will not decrease rates as much as previously expected."

JON VALDELIN: "I agree with that. I was quite surprised about inflation falling without a resulting growth slowdown and typical recession signals did not pan out. Interest rates remain quite elevated and a high-for-longer scenario has become the new consensus while markets continue to perform strongly. The old playbook no longer applies."

DANIEL MORRIS: "If we go back to the beginning of the year, the consensus was that we were to have a recession. Why? Because of the inverted yield curve. However, the equity markets were telling us that a recession was not going to happen. The inverted yield curve only told us that eventually growth will slow, inflation falls and rates go down. I also think it's important to note that we had come through an unprecedented time of pandemic lockdowns, QE and massive fiscal stimulus. Now I think we're back to some sort of normalcy."

CECILIA THOMASSON BLOMQUIST: "I mentioned I was surprised about the equity market but I should add that going into 2024, I was bullish. I expected equities to perform, but not in the way they have done."

CLAES AHREL: "I agree – it was the same with us. When we realised what was going on, we took an active decision to add to our US equity exposure. We did that in January so that was of course a good call. However, when we reached July, we reduced that exposure and with hindsight we should of course have kept that exposure."

MARIE GIERTZ: "Within the equity exposures, the biggest change on our end has been that we have continued to divest from emerging markets. At least in the short run that's been a good call as we shifted the assets to global developed markets, which is a lot of US. Emerging markets have been a disappointment from a performance point of view for a very long time and it's something that we've discussed since I joined the firm. More recently, we've of course also seen the governance issues increase when Russia invaded Ukraine, so now it was also more of a strategic call, also from an ESG point of view."

NIKLAS TELL: CECILIA, YOU'VE ALSO MADE SOME CHANGES TO YOUR EMERGING MARKETS ALLOCATION.

CECILIA THOMASSON BLOMQUIST: "In the overall allocation, we were overweighted equities in the beginning of the year and we stayed overweighted until October/November. Then we thought we better consolidate and take some of the gains. When it comes to emerging markets, we had two mandates, where one was heavily overweighted China and another that was more neutral China. We didn't want to exit emerging markets completely as we think that's a very big call, but we did decide to eliminate the mandate with the overweight to China."

NIKLAS TELL: WAS THE MAIN REASON FOR DECREASING THE EXPOSURE TO EMERGING MARKETS PERFORMANCE OR WAS IT MORE ABOUT ESG AND GOVERNANCE?

CECILIA THOMASSON BLOMQUIST: "It was more of a governance issue. How protected are you when you invest in emerging markets? I did not expect what happened in Russia but it did and I think that's one of the reasons why these are called emerging markets."

CAROLINE LIINANKI: JON, WHAT ARE YOU HEARING FROM NORDIC INVESTORS WHEN IT COMES TO THE EMERGING MARKET EXPOSURES?

JON VALDELIN: "Nordic investors look at emerging markets through different lenses. Should I generalise, emerging markets has been a debated topic in 2024 and more so than in 2023. Some investors have exited, some have chosen a customised approach, while others see opportunities on the debt side. Later in 2024, we saw more investors adding emerging market exposures as part of their strategic asset allocation changes."

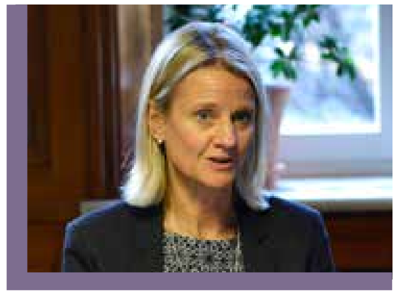
MARIE GIERTZ: "I also think it's important to highlight that we do have an indirect exposure to emerging markets through our global equity allocation. This is even more so when it comes to Swedish equities where companies are even more exposed to emerging markets. That's why it's still very important to continue to follow what's happening in these regions."

CLAES AHREL: "We haven't made any bigger changes. We've reduced our allocation a little bit but we do keep some exposure. We have of course also been disappointed by the performance, but we don't have that big exposure in the strategic portfolio anyway."

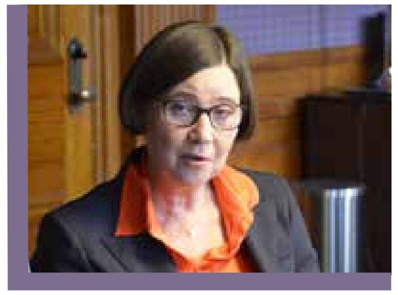
CAROLINE LIINANKI: DANIEL, WHAT ARE YOUR THOUGHTS ON EMERGING MARKETS AND WHAT KIND OF EXPECTATIONS SHOULD YOU HAVE GOING FORWARD? THERE HAS BEEN A LOT OF DISAPPOINTMENT WHEN IT COMES TO PERFORMANCE OVER THE YEARS.

PARTICIPANTS

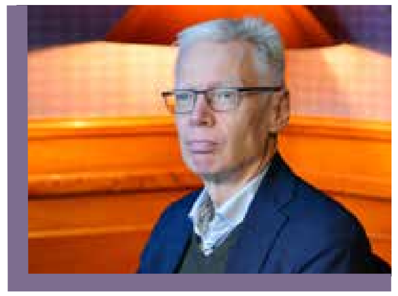
- **MARIE GIERTZ**
  Chief investment officer at the time of the discussion but CEO since February 1, Kåpan Tjänstepension
- **CECILIA THOMASSON BLOMQUIST**
  Chief investment officer, PP Pension
- **CLAES AHREL**
  Managing director, Telia Pension Fund
- **DANIEL MORRIS**
  Chief market strategist, BNP Paribas Asset Management
- **JON VALDELIN**
  Head of institutional Nordic region, Blackrock



MARIE GIERTZ
Chief investment officer of Kåpan Tjänstepension, the Swedish government employees pension fund, at the time of the discussion but CEO since the beginning of February. Before joining the pension fund in 2017, she worked as chief economist at Swedish Export Credit Corporation and prior to that as chief economist at Länsförsäkringar.



CECILIA THOMASSON BLOMQUIST
Chief investment officer of PP Pension, the pension fund for media employees. Before joining the pension fund in 2009, she spent more than 10 years at Swedish buffer fund AP1 where she was part of the executive management team. She started her career at NCC Treasury as a senior dealer in fixed income and FX.



CLAES AHREL
Managing director of Telia Pension Fund. Before joining the corporate pension fund in 2014, he spent seven years as a senior portfolio manager in the asset allocation team at AP4. He has also been chief strategist at Länsförsäkringar Asset Management.

DANIEL MORRIS: "We are currently neutral as you would to keep some exposure. If we go back to the investment case that was made some 20 years ago, it was all about the potential for emerging market catch up and learning from the mistakes of developed markets. Maybe that's worked from a GDP point of view, but that also just reminds us that we're not investing in GDP. Right now, we hope that India will give us the returns that we thought we were going to get out of China. However, in the near term, I agree that it looks like a challenging time with a strong dollar and higher yields. Also, tariffs are not going to help."

NIKLAS TELL: WHAT WOULD YOU SAY ARE SOME OF THE BIGGEST CHALLENGES THAT YOU'RE STRUGGLING WITH FROM AN INVESTMENT POINT OF VIEW?

MARIE GIERTZ: "For us, I would say real estate is the main challenge and especially the US office space – even if that's a small allocation for us. If you only look at the GDP figures and look at what's happening in the stock market in the US, it seems as if everything is great. But there are real challenges in the real estate market. Another thing that we talked a lot about in the beginning of the year was the challenges for regional banks but that seems to have been almost forgotten. So my hope for 2025 is a healthier real estate market – in the US but also here in Sweden and in Europe."

CECILIA THOMASSON BLOMQUIST: "I think the development of the magnificent seven and the concentration that creates in the US market is a challenge. We've reduced our US allocation, even if the development of course can continue for another year or another two years but suddenly it will not. Also, as a Swedish pension fund, I'm worrying about the yield because we need to have something in our portfolio without any risk and we need to have the decent return on that part. So this year has been good because we've had between 4 and 5 per cent on our fixed income portfolio. If that comes down and if we get negative real yields again, that will be a challenge."

CLAES AHREL: "I'm not too worried about the magnificent seven or the US in general. I'm actually more worried about Europe – it's doesn't look too bright. There are so many things going on in Europe right now and even if it's nothing new, it feels like it's going faster now. I hope that sooner or later it will all be discounted and at some point it will be time to invest in Europe again. Maybe it's too early right now but the time will hopefully come."

DANIEL MORRIS: "Do you think we need a crisis in order for Europe to change?"

CLAES AHREL: "Yes, I think so."

CAROLINE LIINANKI: HOW DO YOU NAVIGATE THAT?

CLAES AHREL: "If we're talking about inflation, I particularly like Swedish inflation-linked bonds. They are cheap and serve as a hedge. They are priced for a perfect world so I think it's a good trade if you can buy them and be long term and keep them. That's my call. We'll see if I'm right."

JON VALDELIN: "One of the challenges we see is navigating the mega forces of geopolitical fragmentation, demographics, AI, low-carbon transition and the future of finance as they are driving transformations of economies and societies. These are incredibly strong forces although at times they collide and that basically turns the old playbook upside down. At a moment of economic transformation, investors may need to rethink their approach to portfolios and the 60/40 model may need to be reassessed. We've seen some of those big trends in 2024 with for example the surprising capex of the hyper-scalers in AI that rallied the entire US market. Another trend is decarbonisation, spurring major innovation and infrastructure investments, which will impact societies, sectors and individual companies at large. It will require of investors to be more tactical and nimble."

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>
> *– Marie Giertz, Kåpan Tjänstepension*

DANIEL MORRIS: "I think the development of AI is one of the biggest uncertainties. We've seen the first wave that was all about the semiconductors and the next wave was the rest of the infrastructure with data centres and utilities. However, I think the biggest shift and impact will be the implementation in the non-tech parts of the economy. When we think about growth in developed economies, the primary constraint of growth is generally the labour market. You just don't have enough people to do all the jobs you need to do. With technology and AI, we can potentially solve that – especially for companies and industries where labour costs represent a high share of total costs. My guess would be that this will happen sooner and to a greater degree in the US simply because of the flexibility of the labour market."

JON VALDELIN: "I also think it's interesting to think about the longer term and consider demographic changes. The situation in countries such as Japan and South Korea are fairly acute from a demographics point of view and their productivity will shrink as the population shrinks. They will be very incentivised to increase AI adoption to uphold productivity levels. I think it's going to be interesting to see how countries embrace this and how this development potentially creates bigger divides among countries."

NIKLAS TELL: YOU MENTIONED EARLIER THAT INVESTOR NEED TO BE MORE ACTIVE AND NIMBLER. WHAT DOES THAT MEAN IN MORE PRACTICAL TERMS? IS IT ABOUT TACTICALLY REPOSITIONING THE PORTFOLIO THROUGHOUT THE YEAR?

JON VALDELIN: "Yes, investors are also thinking more in terms of themes rather than strict asset classes. As a firm, we're broadly risk-on and lean into US equities as the area of greatest opportunity because we think the AI theme will broaden to other sectors, drive earnings and justify valuations and you need to be tactical as this develops across different industries. We also note that many investors wish to maintain exposure to the very largest companies in the market-cap-weighted index. We also see investors becoming more granular in their implementations in fixed income by broadening their toolkit to also include targeted ETF exposures."

NIKLAS TELL: HOW DO YOU BALANCE THE NEED FOR BEING MORE ACTIVE WHEN YOU AT THE SAME HAVE SEEN AN INCREASE IN THE ALLOCATION TOWARDS PRIVATE MARKETS, WHICH BY DEFINITION ARE LESS LIQUID AND DOESN'T LEND ITSELF TO TACTICAL SHIFTS?

DANIEL MORRIS
Chief market strategist and co-head of the investment insights centre at BNP Paribas Asset Management, which he joined in 2015. He has previously held roles at Bank of America Securities, Lombard Street Research, JPMorgan Asset Management and Nuveen.

JON VALDELIN
Managing director and head of institutional for the Nordic region at Blackrock. Before joining Blackrock in 2013, he was head of equity distribution for the Nordic region at BofA Merrill Lynch in London. He has also worked at Credit Suisse First Boston and Schroders.

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>
> *– Cecilia Thomasson Blomquist, PP Pension*

MARIE GIERTZ: "You need to stay with your private market investments for the long term in order to truly benefit, so you need to have a clear plan for your strategic allocation. That also means having enough room for the more volatile listed market investments. We looked at our allocation at the beginning of the year and saw that we were a bit overexposed to private equity, so we have been careful with new managers in that space while continuing to invest with our existing managers. Instead, we have shifted focus towards infrastructure and have made some new investments there."

CECILIA THOMASSON BLOMQUIST: "We have a large real estate portfolio and our exposure to private equity is more limited. I think the reason why private equity could be interesting and why we would be ok to lock up the capital for a longer period of time is that the companies can focus 100 per cent on the return on capital. Their CEOs don't need to spend the same amount of time on external engagements but can focus their energy on growing their companies."

CAROLINE LIINANKI: WHAT ARE YOUR THOUGHTS ON THIS, CLAES?

CLAES AHREL: "When it comes to AI, I think it's more positives than negatives, even if I'm aware of the negative things such as fake news. I hope, however, that the positive forces will be stronger in this case. With regards to private equity, that's an area that we have decided to avoid. Not because it's a bad investment, but because we're a small organisation and we don't have the resources that you need in order to do it in the right way."

NIKLAS TELL: WE HAVE TALKED ABOUT YOUR EXPECTATIONS GOING INTO 2024 AND THE SURPRISES BUT WHAT ABOUT 2025? DO YOU THINK WE WILL SEE MORE OF THE SAME OR ARE YOU EXPECTING SOMETHING DIFFERENT FOR THE NEW YEAR?

CLAES AHREL: "I think we will see more of the same. I would, for example, still expect higher volatility because of Trump and higher energy prices because of geopolitical uncertainties. My view could, of course, change by the time the magazine reaches its readers but right now that's my take."

DANIEL MORRIS: "Since the election, energy prices have fallen and the VIX has fallen. Do you think that will reverse?"

CLAES AHREL: "I'm humble but we did see the same development the last time Trump won – then volatility went down as well – but I still think that trend will reverse."

JON VALDELIN: "Elections are interesting because we had a lot of them around the world in 2024. If I generalise, it seems like the incumbent has been ousted driven by a vote for change. A clear mandate to change can in itself cause volatility like you're saying, Claes."

NIKLAS TELL: CECILIA, WHAT ARE YOUR EXPECTATIONS GOING INTO THE NEW YEAR?

ROUNDTABLE - ASSET ALLOCATION AND 2025 OUTLOOK

CECILIA THOMASSON BLOMQUIST: "I think one of the challenges is to have the courage to act and stay with your own analysis. In my case, that analysis is that the US market has been too strong and that it's grown too fast. The development could, of course, continue but you're paid to make decisions and believe in your own research."

NIKLAS TELL: IF I HEAR YOU CORRECTLY, YOU'RE LOOKING TO REDUCE YOUR EXPOSURE TO US EQUITIES?

CECILIA THOMASSON BLOMQUIST: "We have already reduced our exposure and I would like to reduce further in 2025. I hope I'm correct in my analysis but I think I need to follow my conviction. We should be aware of the fact that Trump has received a big mandate for change and there are high expectations for change. However, we don't know the outcome of these changes. It could be good or bad, so I think we need to be open-minded and not think of the US in terms of how it used to be because it will be different going forward."

CAROLINE LIINANKI: SO HOW DO YOU PREPARE FOR THAT KIND OF ENVIRONMENT?

CECILIA THOMASSON BLOMQUIST: "You need to prepare to be calm, logical and you need to listen to yourself."

CLAES AHREL: "We keep some dry powder because if we get the volatility, I would like to be able to use that to make adjustments. We don't normally do the short-term trading, but when things happen, it's good to have dry powder in order to capture those moves."

MARIE GIERTZ: "I would say that I'm fairly optimistic when it comes to 2025 but I agree with what's been said already that we should probably be more worried about Europe than the US. I hope things will change for the better but if it doesn't, we will continue to say that European equities are cheap, but they will be cheap for a reason. I would also like to see improved performance in the private asset space."

JON VALDELIN: "One very important aspect to keep in mind is that a lot of governments have large deficits while increasing spending on security. This gives rise to interesting opportunities within private market investments, especially within infrastructure. There's a need to upgrade infrastructure in general in addition to financing the energy transition and allowing for advancements in AI. I think we need public-to-private partnerships to a greater extent, with the use of blended finance vehicles, where government entities come in as catalytic investors complementing private capital."

NIKLAS TELL: CONTINUING THE SUSTAINABILITY TRACK. HOW DO YOU VIEW TRANSITION INVESTING? IS IT MORE OK TODAY TO BE AN INVESTOR IN HIGH EMITTING SECTORS OR COMPANIES, BECAUSE YOU HAVE A STRONG BELIEF OR PROOF THAT THEY ARE TRANSITIONING? OR ARE YOU STILL MORE IN THE CAMP OF AVOIDING 'BAD' COMPANIES?

MARIE GIERTZ: "I think we're not the first mover but we are following the development. At the beginning, you had these low hanging fruit and an easy way to reduce your carbon footprint was by simply introducing an ESG index and exclude the worst sectors. In order to truly do transition investing, you need internal expertise in order to know if company A or company B is truly transitioning. We're starting to walk that path right now as things are improving fast. We have better access to data and companies are also improving their metrics and are committing to these targets."

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>
> *– Claes Ahrel, Telia Pension Fund*

CLAES AHREL: "I agree that you should exclude sectors if it's about chemical weapons or something where you can't be a good guy. Just get rid of it. But I don't like when you exclude energy companies because they're in a business you don't like. I prefer the transition strategy."

CECILIA THOMASSON BLOMQUIST: "We're investing through funds and we've decided that the majority of the funds should be Article 8. We do have some special mandates that are more transition focused but they have unfortunately been lagging both in 2023 and 2024 so you can't put your entire portfolio into that type of strategy."

NIKLAS TELL: WHAT ARE SOME OF THE FACTORS ARGUING FOR AND AGAINST 2025 BECOMING A GOOD INVESTMENT YEAR?

CLAES AHREL: "On the negative side, we of course have political uncertainty, which could postpone investments. I also see inflation risks caused by tariffs and of course the development in China and Europe that could change a lot. On the positive side, which we have already covered, we see a strong momentum in many areas. Corporate earnings in the US looks ok and US households have locked-in low interest rates. We've hopefully also discounted a lot of the bad news, which could be a positive surprise for Europe, for example."

DANIEL MORRIS: "I'm worried that Trump could be too successful – that you get too much growth and that inflation rises again. What would it mean if the Fed then hiked rates again? The probability is low but it's not zero."

CECILIA THOMASSON BLOMQUIST: "I agree that inflation coming back is the biggest risk. Both in the US, but also in Europe due to energy prices."

MARIE GIERTZ: "I'm less worried about inflation. My main concern is Europe and the energy dependence."

CAROLINE LIINANKI: DO YOU NEED TO THINK A BIT MORE ABOUT INFLATION PROTECTION AND WHAT'S THE BEST WAY OF GETTING THAT?

CLAES AHREL: "I see it as a risk and not the main scenario. As I said earlier, we buy Swedish index-linked bonds as a way of protecting ourselves."

CECILIA THOMASSON BLOMQUIST: "I would say real estate and equities are a hedge up until a certain level. Inflation is very real for a pension fund because your balance sheet is impacted by the high inflation."

JON VALDELIN: "I think infrastructure, with long-term contractual revenues, is an interesting inflation hedge, while benefitting from long-term investment trends such as the energy transition, advancements in AI and the need to upgrade existing aging infrastructure."