Link to the Video

Finding value for private clients in 2023

HARMEN OVERDIJK
Leo Wealth

"Fixed income is more attractive than it used to be before last year's selloff, but we are not overly bullish on a fixed income. We don't believe that bond yields can go down much from current levels."

Where do you think the value lies in 2023?

This year is going to be a very different year than last year. We think in a way this year is going to be like a mirror image of 2022. We don't think we are going to see a recession in the US and we don't think we're going to recession globally. We do believe inflation will cool down quite a bit, especially in the first half of this year. We believe central banks will pause the current hawkish monetary policy. We don't believe they will cut rates anytime soon. That they will only do if they're really sure inflation is under control, which it won't be for quite some time. Or if we see a recession, which we don't believe will happen anytime soon, at least not in the next 12 to 18 months.

That's a bit different than the rest of the world currently looks at the market. So that means that we are a lot more positive on risk assets this year than we were last year and we think that even though we had a bit of a rebound in the last couple of months, that we have a lot more to be gained in risk assets this year.

How are you positioning client portfolios?

In our portfolios, as we are more positive on non-equity markets, we think that valuations have come down more than enough, and more than earnings will come down. We're actually quite bullish on equity markets for this year, which means we have a slight overweight into equities. We have a slight overweight into growth. We have an overweight into Asia, both China and Japanese equities. We think we'll see a growth acceleration in Asia, mostly driven by the Chinese economy rebound. This will be a lot stronger than a lot of people expect at the moment. Fixed income is more attractive than it used to be before last year's selloff, but we are not overly bullish on a fixed income. We don't believe that bond yields can go down much from current levels.

If inflation surprises to the upside later in the year, which is a potential risk, bond yields could actually rise. Again, we don't expect central banks to cut interest rates this year, so we don't see bond yields coming down. So, within fixed income, we focus a bit more on credit. Both high yields and private credit, as attractive, but we'd rather focus on other risk assets. Within the risk asset space, we also like commodities. We think that commodities will rebound this year based on stronger economic growth, but it's also going to be a combination of higher demands and tighter supply in the commodity space. So

GET IN TOUCH
View Harmen Overdijk LinkedIn's Profile
Find out more about Leo Wealth

we definitely think you need to have an allocation to the commodity space, both metals and energy.

If we look out a little bit further for portfolio strategy, there are definitely risks in the market. Obviously, the war in Ukraine could escalate. There is unrest in the Middle East or skirmishes between Iran, Turkey, and Azerbaijan. Some sort of escalation in the Middle East could have an impact on oil prices. At the same time, another risk is that the economy's holding up very well this year and the employment markets holding up very well is that we could see a re-acceleration of inflation later this year, and with that, potentially more hawkish monetary policy or at least hawkish language from central banks towards the end of the year. The risk is the debt eventually will lead to a recession.

We think the risk of a recession is much higher in 2024 than in 2023. That also means the market could and most likely will remain quite volatile. If we look at portfolio strategy a bit longer term, we start to like adding alternative investments like hedge funds and private credit to the portfolio. Hedge funds, especially had a pretty poor performance record over the last 15 years, while equity markets rallied. But if you look back in the late 90s, early 2000s, we had an economy and a monetary policy that is in a way quite comparable to today's environment. Hedge funds performed really well. So, from a longer-term portfolio strategy, few. We start recommending clients again to add more non-correlated hedge funds to the portfolio strategy mix.

Are there any other risks?

The risk this year is obviously geopolitical, but the geopolitical risk is always very hard to predict, if not impossible to predict because of what could go wrong, which could actually go better than expected. The Ukraine war could escalate but could also turn out that we might find some sort of solution this year, which would obviously be positive. Economic risks are obvious. And that's a big question mark, can the global economy, can the US and the European economy, withstand the higher interest rates? Obviously, we're at a very aggressive rate hiking cycle from basically 0% to almost 5% in the US. So far the economy, and that's our view, can deal with it.

The question mark is, what is the level where it really starts to hurt? And that is a risk no one knows. And there was always a time lack of monetary policy having an effect on the real economy, which typically takes 12 to 18 months. So it's possible that we see some of the effects only later this year. And perhaps interest rates are already too high and we will see some real pain in the market. Another risk is obviously the employment market. Right now, employment is strong. We had surprisingly high new job gains in the US in January. Unemployment rates are at record lows, like 40-year lows, mostly in the US but also in Europe the market is very tight.

The risk is obvious once the economy starts softening, more companies start to lay off people. So far, almost all the layoffs have been concentrated in the tech sector, and that we don't see as a risk to the economy because all these people that get laid off by Google, Spotify, and Twitter, can easily find a new jobs, relatively quickly. For example, the car industry sees it as a positive that they can finally hire software developers that otherwise would stay at Google. The real risk is obviously once other sectors need to lay off people and might like to see a soft landing where the unemployment rate goes up a little bit. But unfortunately, it does not really work like that. Once the unemployment rate seriously starts to go up, it tends to go a lot further than everyone would like, and then you effectively have a recession. So that's the real risk in the coming years. We just don't think it's going to happen in the next 12 to 18 months.

Where do digital assets fit into your thinking at the moment?

The digital asset space obviously had a bit of a rough year last year. The key reason is lower liquidity and less appetite for risk-taking. So cryptocurrencies especially weren't the uncorrelated asset class that everyone told it was. It was a high-alpha play on the tech sector. So Bitcoin and other cryptocurrencies deflated in line with the high-growth tech companies and obviously, that led to a lot of issues in the industry, which is an unregulated industry, and still is, to large extent. And there were the same excesses in the crypto space, as happened in the global financial crisis in the investment banking space. Basically too much leverage, and not enough risk control. And then if all these companies lend to each other, if one or two go under, a whole chain of them goes under.

What was for us a positive thing, the fact that FTX, which was a large player, went bankrupt in November, it didn't have a real impact on the price of Bitcoin and Ethereum. So we believe blockchain technology is still going to have a great future. It's going to change the way the capital markets work. We still don't know who is going to be the long-term winners, but we always said that by investing in this space, you want to have some exposure, but we prefer to stay with the big players, in this case, Bitcoin, and Ethereum, and we remain positive. We think clients should have this year still some exposure to Bitcoin, and Ethereum in their portfolio. ■