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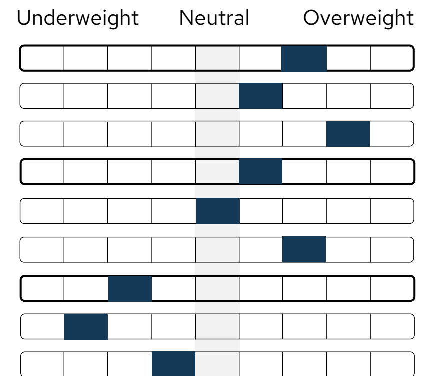
Market view

High yield: Continued overweight, with a focus on the Nordic region

Equities: Expensive relative to bonds

Interest rates: Short-term rates should go down and long-term rates up

Megatrends: Finance, Infrastructure, Sustainability, and AI



"Don't fight the Fed"!

We see good conditions for risk-taking in high-yield bonds and parts of the stock market. The Riksbank, as the second central bank in the western world, has lowered interest rates. This was the first time in eight years. The ECB is likely to follow in June, and the Federal Reserve in September. The recovery has already started and will gain more momentum now that the interest rate cuts are materializing. Global economic signals are stronger and more broadly anchored again. Both purchasing managers and households are positive, resulting in rising consumption and housing prices.

High yield

The world economy never entered a severe recession in 2022-2023. This has meant that the rate of defaults barely rose above the historical average and is now declining. Looking ahead, interest rate cuts will now make life a bit easier for more indebted companies. High-yield bonds are also attractive compared to stocks, especially in the Nordic region where the risk premium in the high-yield market (credit spread) is favorable compared to the risk in the stock market (volatility).

Equities

The stock market benefits when growth picks up but struggles when interest rates rise. The stock market has already had large gains and looks historically expensive compared to bonds.

For example, the earnings yield (profit divided by stock price) on the S&P500 is lower than the 10-year U.S. Treasury yield. Smaller companies are more attractively priced and will get additional support from declining liquidity premiums.

Interest rates

Interest rate cuts will lead to lower short-term rates and higher long-term rates. This means that the inverted yield curve we have today will revert to a positive slope. It also means that it is too early to buy duration; long bonds will fall in price when interest rates rise. Interest rates will also be kept up by central banks now being massive net sellers of bonds.

Megatrends

Finance: Benefits from normalization of debt markets

Infrastructure: Large investments are necessary

Sustainability: A temporary setback in a long trend

AI: Will revolutionize some industries more than others

Finance

A sector that has lagged significantly since the credit crisis of 2008 and has undergone a rigorous phase in the 2010s. Requirements for higher capital adequacy ratios, lower lending risk, and a decade of zero interest rates have depressed valuations. Now we are entering a fantastic environment for the sector with higher interest rates and a normalization of the yield curve. Additionally, we are entering a phase of higher growth and lower credit risks.

Infrastructure

Decades of underinvestment in infrastructure have really caught up. To meet challenges such as a sustainable energy system, developing domestic metal and mineral extraction, NATO membership, and the need for efficient logistics solutions, society faces very large investment needs. Companies focused on infrastructure are in a megatrend.

Sustainability

Our society faces enormous challenges. We need to fix the climate while preserving biodiversity and recycling resources. Green investments have performed poorly recently, but we believe this is only a temporary setback. Investors are ready with substantial capital to invest in new technologies and solutions on the path to a sustainable society.

AI

AI is not just about some software manufacturers in California. It is a megatrend that will reshape how we work in the future. We are only at the beginning of this change, and it will create significant productivity improvements. Assessing which companies and sectors are winners and losers in this shift is crucial for good portfolio returns.

Macro Indicator (ViGMa)

ViGMa reflects expectations of overall economic activity and is based on information from multiple sources. ViGMa combines data from a broad range of macroeconomic indicators and pricing in both bond and commodity markets. The indicator provides important support for assessments of the economic situation and the environment for returns and risks in the markets.

The credit clock is at three

The credit clock or credit/equity cycle is a powerful model that identifies how corporate behavior affects the development of the credit and equity markets in different phases of the business cycle. When markets fall, the credit clock is at nine. The next phase is when companies start taking measures to ensure their survival. This is positive for the credit market but negative for the equity market (e.g., new issues, suspended dividends, etc.). We argue that the clock is now at three, a phase where both the credit and equity markets perform well because the economy has started to pick up.

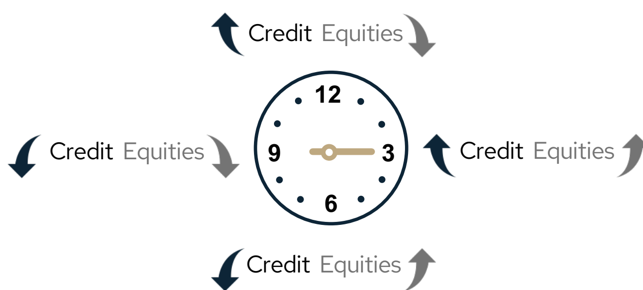


Figure: Credit clock (credit/equity cycle)

Product & business proposal

Our sister company, Vinga Wealth Management, develops business proposals to reflect the current market view. They often consist of a mix of long-term investments to benefit from megatrends and short-term opportunistic investments. The common goal is to add value and focus to the portfolio. Vinga's market view and business proposals are updated quarterly.

If you would like to receive a business proposal, contact our wealth advisors at Vinga Wealth Management.

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