Karen Ward: «Investors Place Too Much Weight on Politics»
Wednesday, 20 March 2024 09:26

Political considerations should not have a decisive say in an investment strategy, Karen Ward, chief investment strategist of J.P. Morgan Asset Management says in an interview with finews.com. Furthermore, she explains why Europe could surprise investors this year.

Karen Ward, how do you expect interest rates to evolve?

Central banks are quite confident that the 2 percent inflation rate is in sight for the summer. Consequently, they will start to cut interest rates moderately then. However, we will have considerably higher interest rates in comparison to before the pandemic.

Interestingly, we've learned over the past few years that our economies can cope well with higher interest rates. Particularly the US economy has been fascinating. In Europe, I attribute
the weakness in growth to the magnitude of the cost shock, the energy crisis, and the weakness in global trade and not necessarily the higher interest rates.

**What lessons can be learned from this?**

We've learned two things about resilience. On the one hand, as I mentioned especially the USA was very fascinating in its resilience. Thus, the US household and corporate sectors are in pretty good shape.

«Zero interest rates are not good for asset prices because they represent an ill economy»

On the other hand, even though in our industry we are all preoccupied with central banks and monetary policy, resilience also comes from fiscal policy. Fiscal policy is more potent in driving growth and finally, governments everywhere are spending again. This will be particularly interesting for Europe.

**What implications will the interest rate cuts have on both stocks and bonds?**

Let me start by talking about a statement that I particularly disagree with: «Zero interest rates were really good for asset prices». Zero interest rates were great for the S&P and tech, and growth stocks, but it wasn’t good for European stocks, bond returns, or emerging market stocks. Generally, zero interest rates are not good for asset prices because they represent an ill economy.

«Opportunities often stem from parts of the market where the expectations are low»

Hence, having slightly higher interest rates makes me more optimistic about medium-term stock prices. Furthermore, bonds can fulfill their original function again, which is to give a nice and steady income. In conclusion, I don’t think it will be significant for bond and stock prices and we are in a reasonably good spot for diversified portfolios.
Financial stocks had a successful year on the stock exchange in 2023. How will this develop in the upcoming year, and would you invest?

Firstly, I would invest. Secondly, the broad market is pricing for a benign economic scenario: growth is resilient and lower inflation and lower interest rates are expected. The market is rallied due to this. Therefore, investors could encounter some volatility this year. However, volatility is inevitable. Investors waiting for a clearly good situation will be waiting their whole life.

Where do you see opportunities in the market?

Opportunities often stem from parts of the market where the expectations are low. Currently, expectations around European stocks are low. However, what Europe has been through is simply a horrific cost shock. I think this year we will be surprised by Europe’s recovery and investors will pivot towards these stocks.

The commercial real estate market in various countries is going through a difficult period. How do you perceive real estate as an asset class, particularly when considering these current circumstances?

Commercial real estate was a key risk and remains a risk, however much less than in the previous year. Commercial real estate was hit by both a cyclical and a structural problem. On the one hand, structurally the office space was not necessarily required anymore.

On the other hand, interest rates on office blocks were much higher. However, many companies are increasingly seeing the benefits of working in the office again and interest rates are expected to be cut. Thus, this tends to not be a rapidly evolving systemic problem. Over the medium term, real estate remains a critical building block for a diversified portfolio, also because it’s an asset class that does well in a moderately higher inflation environment.

In your opinion, what are some thematic investing topics that are overcrowded?

I wouldn’t say AI is overcrowded, but I believe we must be mindful especially considering former «tech miracles». We tend to overestimate how much technology will impact the whole economic productivity. One must be very careful and an expert in picking the winner of the technology sector. Personally, I would not buy the S&P passively today because it is very vulnerable to single-stock disappointment.

And which thematic investing topics are undercrowded?
The green transition is certainly undercrowded, partly due to political retraction and partly also due to consumer pushback. However, I believe the global economy requires a transition to renewable sources of energy.

«The biggest challenge often turns out to be the best investment theme»

The execution of this global transition poses as one of the most comprehensive challenges. But the biggest challenge often turns out to be the best investment theme. Therefore, in my opinion, renewable energy is more compelling as a justified mega trend in comparison to AI. But I think I am lonely in that view.

What do you consider when setting up an investment strategy particularly taking into account current political events?

A common mistake of investors is to place too much weight on politics. Politicians say a lot to be eye-catching, but the actual policy or outcome could be completely different to what they proposed in the beginning. Therefore, it would be a mistake to shift a portfolio allocation due to political outcomes. Let’s not forget that a lot can change between now and the US elections on the 5th of November.

What is the biggest risk that could leave a lasting impact on the investment strategy?

Markets were shaped by inflation the past three years, and it’s expected to be behind us now. The key risk for stocks and bonds is if this expectation turns out to be false.

Karen Ward is a managing director and has been the Chief Market Strategist EMEA at J.P. Morgan Asset Management since 2017. Beforehand she was Chair of the Council of Economic Advisers for the Chancellor of the Exchequer. Furthermore, for many years she worked at the British bank HSBC in the area of Global Banking and Markets, most previously as the Chief European Economist. She started her career at Bank of England, where she supported the Monetary Policy Committee. She obtained her bachelor’s degree in economics at the University of Surrey and her master’s with distinction in economics at University College London.