A global shake up

With around half the globe heading to the ballots in what is set to be the biggest election year in history, how will global equities markets, and managers, fare in 2024, asks Sandra Haurant

Summary

- Global equities have long been a mainstay of pensions' portfolios, traditionally providing a relatively reliable source of growth.
- With half the world heading to the polls in 2024, including with the US presidential elections, political turbulence is certain to affect global equity markets.
- Conflict, crisis and tensions around the world mean managers must be alert and ready to react to shifts in the markets, seeking to avoid cycles and negative correlations where they can.
- The sheer scope offered by the global equities market, with its span of geographies and sectors, offers managers the chance to benefit from the opportunities that present themselves around the world; the emphasis, against a backdrop of global uncertainty, is on a shift towards sustainable choices.

Global equities are "the traditional return driver of a pension scheme's growth portfolio", says Cardano senior investment strategist, Ross Barr. "As earnings grow over time in line with inflation, they are an important driver of the asset return of a pension scheme."

But defined benefit (DB) and defined contribution (DC) pensions have different requirements from their portfolios, and over time the traditional shape of pension investment has adjusted to suit different needs.

"As DB pensions mature, the volatility and drawdown risk associated with equities has led schemes to diversify into various public and private assets," says Barr. "However, many pension schemes still require a role for equity returns and the continued strong performance of global equities means exposure to this asset class – but at a lower rate of volatility – remains desirable for pension schemes."

For DC, meanwhile, the need for growth remains as strong as ever, with global public equities in pensions portfolios important both now and in the future, and the emphasis shifting towards durability and sustainability. As Barr says: "UK pension schemes increasingly desire exposure to sustainable equities in their global equity portfolios."

Shifting sands

Multiple elections are due to take place across the globe, and in the coming months, the political landscapes of countries at every point of the compass could change significantly.

"While unelected central bankers have dominated the headlines going on two years now, clearly, at the start of 2024, this is now switching to the 'elected officials' side of things, given the sheer volume of elections coming down the pike this year," says GQG global investment strategist, Josh Snyder.

"While the former focus isn't terribly surprising, given the increase in interest rates from zero or below zero during the past two years, and now the focus on how many rate cuts may occur going forward, the election focus, in our view, offers up a bit more ambiguity," he adds.

After all, polarised populations in multiple democracies mean that a lot of the upcoming elections are far from a done deal – and if there's one thing markets are not keen on, it's uncertainty.

The US presidential election is, of course, the one to watch, says Barr, not just because of the way in which the US equity markets themselves may respond, but also because of the nation's wider international weight.

"Our expectation is that whoever wins will likely have to deal with a split congress," Barr says. "In the past, this has suited equity markets, as policy is deemed not to interfere too much with earnings growth. Regardless of who takes the presidency – small caps may outperform due to post-election optimism."

When it comes to wider impact on global markets, Barr says: "The US election is also unlikely to change the supportive nature of fiscal policy on the US economy – which in turn is supportive for regional markets tied to the US economic cycle, such as Europe, Japan and emerging markets (EM). EM and China may suffer longer-term from an increased focus on trade tariffs."

At home, the widely anticipated UK general election might not have such an impact on global equity markets, but that doesn't mean it won't be significant. Potential shifts in the relationship with the EU, in particular, could have an important impact in the longer term, Barr says.

Conflict and crisis

Beyond the ballot box, conflict and tragedy around the world are an ongoing source of concern.

"Global equities offer inflation-hedging properties, more attractive valuations and allow for international diversification, hence reducing reliance on any single country's monetary policy. However, the benefits of global equities must be balanced against increased risks, notably political risk," Tobam head of fixed income, Axel Cabrol, says. "Since 2022, geopolitical risks have surged to the forefront, exacerbated by events such as Russia's invasion of Ukraine and escalating conflicts in the Middle East, alongside growing tensions between the US and China, leading to decreased trade and a more regionally structured global trade system."

Geopolitical factors necessarily influence long-term returns, says Cabrol. "The Russian market debacle is on everyone's mind, and it is hard to ignore the underwhelming, close to zero, China long-term performance, despite the most impressive GDP development in history."

Tobam, Cabrol says, believes there is "an opportunity to capitalise on the global equity premium while mitigating unrewarded geopolitical risks stemming from authoritarian regimes". This means minimising "authoritarian exposure in both equities and fixed income portfolios", which, says Cabrol, enhances long-term return and risk profiles.

For Ninety One portfolio manager, Stephanie Niven, the priority is to seek strength in "sustainable drivers of structural growth, able to deliver growth through macro volatility". She adds: "Global equity strategies have a wealth of opportunities to invest in first class businesses with acyclical revenue streams, particularly those companies with durable competitive advantages able to deliver sustainable returns."

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It's a wide world

One of the clear benefits of a space as vast and varied as global equities is the almost endless choice it offers, spanning, as it does, geographical regions and industry sectors; with that comes the potential opportunity to reduce correlation with areas that are struggling.

"We see a wealth of opportunities across a range of businesses with sustainable drivers of structural growth from decarbonisation, financial inclusion, and health impact, to climate adaptation, digital inclusion, and access to education," says Niven.

"These businesses, particularly when combined with a strong management team and a multi-stakeholder approach, offer pension investors acyclical growth opportunities, delivering healthy cash flows and returns through a period of heightened macro volatility."

And, says Barr, varied strategies can bring additional room for manoeuvre: "At Cardano, we use derivatives to give flexibility to the global equity and multi-asset portfolios," he says. "Equity futures mean we can gain, or minimise, exposure to different global equity markets quickly in response to changing macro conditions. We also use option strategies to protect against downside or upside risks to our global equity positioning, helping to minimise equity drawdown risks in our portfolios."

"We continue to view the breadth of the global equity opportunity set quite strong, assuming one knows where to look. This does not mean we always get everything right, because we certainly do not, but it does mean that active management should indeed be that: Active," says Snyder.

"Our view is that regardless of election outcomes, opportunities across sectors such as information technology, given strong strides in AI, or energy, given government policy and a relative tight supply backdrop moving forward, are worth a look," Synder adds.

In geographical terms, Snyder prefers India, with its "positive policy backdrop," to China, where "policy whiplash and large debt" reduce clarity around future earnings growth.

Still, with such scope available to fund managers, it's important to know how best to navigate this broad and diverse world, says Niven.

"Increasingly it has become essential that global equity strategies offer the active role in portfolios that investors and allocators are looking for. Global equity strategies need to provide differentiated alpha streams that come from high conviction, high active share approaches," she says.

"Global equity approaches need to articulate the nature of their investment edge, with expectations increasing for portfolio managers with regards to explaining the way in which the portfolio intends to deliver alpha relative to the market."

Written by Sandra Haurant, a freelance journalist