BPM Berlin Portfolio Management

Published as a guest column contribution (2. April 2019) for

DAS KNOW-HOW-MAGAZIN ZUR KAPITALANLAGE

INVESTMENT

This article appeared in German on **02/04/2019** at:
https://www.dasinvestment.com/vermoegensverwalter-uwe-guenther-mit-der-richtigen-strategie-erfolgreich-in-den-gesunden-abschwung

The Right Strategy Going into a Healthy Downturn

"The crucial question on the financial markets currently is: have the known risks already been fully evaluated or not?", Uwe Günther says. The founder and managing director of BPM - Berlin Portfolio Management is designing a suitable strategy for securities portfolios.

Despite the most varied assessments, views and deductions, many players on the capitals markets currently all seem to be able to agree on the lowest common denominator:

- The global economy is in the mature stage of its current cycle. Among other things, this is indicated by the interest rate developments in the USA. US 10-year sovereign bonds no longer yield more than three-month treasuries. And stock market cycles mostly pre-empt economic cycles. Global debt has also reached new levels. Its sustainability is directly determined by a robust global economy.

- If we consider historical comparisons, numerous indicators are pointing to a scenario typical for phases prior to the start of a recession. Interest rate developments, labour market data, the dynamics of company profits, cargo rates as well as mood indicators and individual trade data can all give reason for concern.

- The extent of large international conflicts, tensions, concerns, challenges in politics, the economy, nature and society has reached a level which is historically rarely seen. At the same time, the chances of the situation improving are slim.

- Free pricing on the securities markets is hampered by massive interference from the central banks and by government intervention. The interest rate has now mostly lost its function of steering of investments and risk assessment. After roughly two and a half years, yields on ten-year government bonds are again in the red. Thus there are faulty allocations of capital.

- Technical analysts hardly have anything to cheer about. In the last months worrying structures have been forming in many leading indices. At the same time, last year international central banks bought more physical gold than at any time in the last 50 years.

Two Basic Ways of Thinking and Acting

Based on these assessments, two basic ways of thinking and acting can be observed:

One: *"This is all familiar and included in the price of securities.*
So even partial solutions to problems - e.g., an amicable trade agreement between the USA and China - can invigorate markets considerably. The current uncertainty and lack of enthusiasm offer opportunities. Low interest rates are still the motor for share price gains."

Or two: *"Global problems have not been adequately calculated into the price of securities. States and central banks are also preventing this, so as not to let the unproductive debt mountain and the illusion of prosperity collapse, and with it consumption and social tranquillity. The low interest rates anticipate weak*
growth rates in the years to come."

The second way of thinking clearly poses the greater challenge for structuring a portfolio. Because, if this assessment is accurate, countless securities accounts with a balanced structure belonging to investors with a mid-level risk tolerance would be in drastic need of modification. Here are a few suggestions based on a funds-based securities account:

Classic Shares: Reduction of the equity proportion to around 20 percent. The focus here should be on solutions with proven success in falling markets, with strong track record and market quality, low level of debt and active management.

Alternative Shares: Increase of up to 20 percent of the total portfolio. Substantial potential for diversification and yield is recommended here. Excellent times should lie ahead for flexible management and premium strategies from proven experts.

Traditional Bonds: Up to 30 percent of the total quota. Quality titles from corporates – and, yes, – government bonds from some big players are THE choice Today. Weak corporate, so called high-yield or junk bonds are “out”. After overweighting, the bonds of emerging markets are currently to be weighted neutrally.

Alternative Bonds: In future the portfolio will only bear a proportion of up to 15 percent here. Investors will strike it lucky on the market with top level providers. Whoever identifies the fund managers who know how to play all the tricks and performance drivers like a master will still be one of the winners.

Precious Metals: Around 10 percent in gold - understood as a currency item and diversifier - and if necessary a small amount of silver are still a must. This item can be supplemented by a precious metal mining fund of up to 5 percent, according to appetite for risks. Investing in small to medium-sized mining companies and exploration professionals in politically stable regions is clearly to be preferred here.

Raw Materials: Although probably still too early, the relatively extreme valuations vis-a-vis the wider stock market is already tempting in the direction of opening an initial roll-optimised position of up to five percent of the account.

Classic and Alternative Multi-Assets: Around 25 percent can be entrusted to active managers here. These should be able to show proven experience in capitalising various sources of income and have excellent daily risk management or risk overlay. One-size-fits-all is out.

Conclusion: The goal of this kind of asset allocation is to convert the potentially upcoming, very healthy economic corrections into absolutely positive performance. This is the only thing that counts. Investors should still remain on their guard against propaganda like: "With a long-term view to investing you can weather any slump." As so often in history, the investor's psychology, costs, taxes, withdrawals, inflation, unexpected events and potentially even his/her own age can stand in the way. Preventing strategic losses remains the most important guarantee of good performance.

All the best and good luck in all your present and future endeavours!

Uwe Guenther and the BPM Team

Uwe Guenther is founder and Managing Director of BPM - Berlin Portfolio Management GmbH, Berlin, Germany.