



## **Think Wealth** CIO Exchange

### Portfolio construction amid AI innovation and policy uncertainty

By Willem Sels, Global Chief Investment Officer, HSBC Private Bank and Premier Wealth and Johanna Kyrklund, Group Chief Investment Officer, Schroders

#### **Willem Sels**

Thank you, Johanna, for sitting down with me for our first CIO Exchange.

And of course, the first topic we should address is the potential for further upside in AI in the US markets and so on. The way that we tend to think about it is by splitting the earnings side from the valuation multiples.

Now the valuation multiples are high but they've come down a bit over the last few weeks. And on the earnings side, we're actually quite optimistic that we will see, through that innovation, a lot of earnings growth and further upside for the US market.

Is that the way you think about it?

#### **Johanna Kyrklund**

Yes. We actually see evidence of earnings broadening out as well, so we are quite positive on earnings. And also, thinking about valuations, you know, at the end of last year we were comparing it to the internet bubble.

But when you think also about the price to earnings ratio relative to bond yields, compared to back then, the bond yield is at a much lower level, which helps to underpin equity valuations.

So from that perspective, we still think the valuations are sustainable. We then need to think about the AI risk. Firstly from a market standpoint, there is more differentiation at stock level. I think that's good news.

That shows a bit of froth being taken out of the market. We need to watch, whether that capital expenditure turns into return on investment. So very much a stock picker situation.

But then we also need to think about the impact of AI on the economy. And actually at the margin, it is cooling the labour market a little bit, which again, allows the Fed to lean dovish, which in turn underpins bond yields.

So as long as the bond yield is fine I think the equity valuations are also fine.

#### **Willem Sels**

So it seems we're still optimistic – both of us. But we need to look at, nevertheless, the concentration risk right. The US is a big share of global market indices. Technology is a big part of that.

The way that we handle that is by looking across and beyond AI to other sectors to be overweight on, as well as Asia, which we like as a region.

How do you manage concentration risk



### **Johanna Kyrklund**

Just in the last couple of months, we've been diversifying into international value stocks. So we're still overweight US, but we've diversified the overweight into international value.

The benefit of that, as you say, it provides geographical diversification but also diversifies a little bit away from the AI risk.

So we think style diversification is helpful.

### **Willem Sels**

And what about the US dollar? We saw a lot of weakness last year. Maybe a little bit less so now, but still weakness. I had the impression that people don't flee away from US assets just because of that, because we have all those opportunities there. But they want to hedge the FX exposure.

Is that what you see with institutional clients as well?

### **Johanna Kyrklund**

Yes, I would agree. For now, it's very much a question of managing your risk.

People recognise they have a very high weight to the dollar. And so a bit of diversification, but not fleeing the dollar. At the margin, we are still negative on the dollar because we think the Fed will lean dovish, while we see other central banks, in some cases actually starting to raise rates.

And this view also leads us to be positive on emerging market assets, both equities and debt.

### **Willem Sels**

Now geopolitics creates a lot of headlines. Some of it is noise and that we try to manage through portfolio diversification, multi-asset solutions, alternatives and so on, but there are some clear trends taking shape as well.

And one of them, which we like is, you know, countries wanting to be self-sufficient in terms of electricity, in terms of materials. And so those are two areas we like.

What are your thoughts on geopolitics?

### **Johanna Kyrklund**

Well, we do think commodities are a helpful diversifier because firstly, the transmission mechanism from geopolitical risk to markets is typically via commodities.

And secondly, because you're right, in an environment of geopolitical uncertainty what you typically see is countries looking to stockpile their commodity exposure.

So from that perspective we've been positive on gold for quite a while.

And we've also now expanded our overweight into commodities more broadly. I think it's a helpful position that hedges you against geopolitical risk.

But also the other reasons why we like it, because growth is still quite strong.

### **Willem Sels**

Do all of those headlines and all of the news make this investment environment particularly difficult for you?



### **Johanna Kyrklund**

I think it's easy to read the paper and say, "Oh my god! it's impossible. It's too uncertain."

But I think in the 30 years I've been doing this job, there's never been one day where it felt easy.

And I think, think about where we were before: zero yields, negative yields. That's not a good environment for investment, actually we've seen the return of yield which is quite positive.

So I think, look our job is to make decisions under uncertainty.

### **Willem Sels**

So a lot of volatility but a lot of opportunities as well, I couldn't agree more.

We really see a huge opportunity set and it's by building resilient portfolios that can weather that volatility and you can remain exposed to all of those opportunities.

Thank you so much for your thoughts.