

Interview with lead portfolio manager Joakim Ahlberg

Nordea 1 – North American Stars Equity Fund

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Please note that the conference call occurred on the 25th of November 2020. All market commentary and information refers to the period before then.

Key takeaways

- As bottom-up investors, the result of the US election is only a minor consideration for us. However, the Joe Biden victory might lead to sector dispersion, while once again increasing the importance of sustainability in the US.
- The investment process of the fund is modelled on the successful approach taken by the Nordea Global Stars Equity Strategy, splitting the portfolio between moat and expectation gap companies.
- North American companies have become more open towards ESG themes and engagements in recent years.
- As a flexible core portfolio, underpinned by a sound risk framework, this strategy offers an attractive alternative to North American funds with a core or growth bias.

Firstly, what is your reaction to Joe Biden's election victory earlier this month?

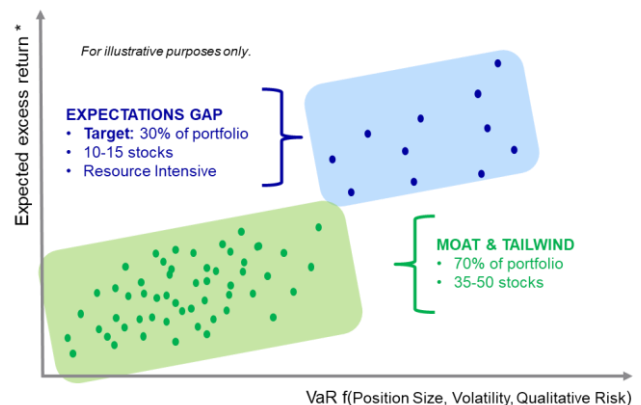
We predominantly look at the economic/business cycle, which we believe always trumps the political cycle – pardon the pun. This may be truer than ever right now, as the base case is the global economy will see a significant recovery next year, as we emerge from the pandemic. As for the election, if the Senate remains with the Republicans, it may be the best of both worlds for markets, as it will be harder to implement tax hikes on corporates. In the US, an important factor right now is fiscal spending. Infrastructure spending will be different under the new Biden government, with more allocated to greener areas. This will provide a positive tailwind for the renewables stocks we are currently invested in.

Will a 'greener' government have any impact on ESG thinking for US companies?

ESG has been underway in the US for some time, even before Trump was elected, but it could accelerate further. There have been large amounts of money flowing into ESG strategies over the past three years, and managements now face significant pressures from shareholders to improve reporting in this area. It is becoming easier to obtain the information we require, as the companies know that investors – including ourselves at Nordea – will vote with their feet. In any event, there is no shortage of positive ESG names to invest in today. For example, in the regulated utilities space, Xcel Energy is retiring coal-based plants and replacing assets with wind and solar. Ecolab is another example, which provides clean water and energy waste solutions.

What is the stock selection process behind the North American Stars Equity strategy?

Firstly, we follow the same process as the established Global Stars strategy we also run. We are active managers and look for two types of stocks. In the first bucket are what we call our 'moat and tailwind' stocks, which constitute about 70% of the portfolio. The easily distinguishable moats (sustainable competitive advantages) and tailwinds for these stocks provide attractive long-term returns on a risk adjusted basis. The remaining 30% of the portfolio is in what we call the 'expectations gap' bucket, which are stocks where we have a materially different view versus the market. This is often more research intensive, requiring months of due diligence before taking a position. However, this effort can deliver very attractive upside.

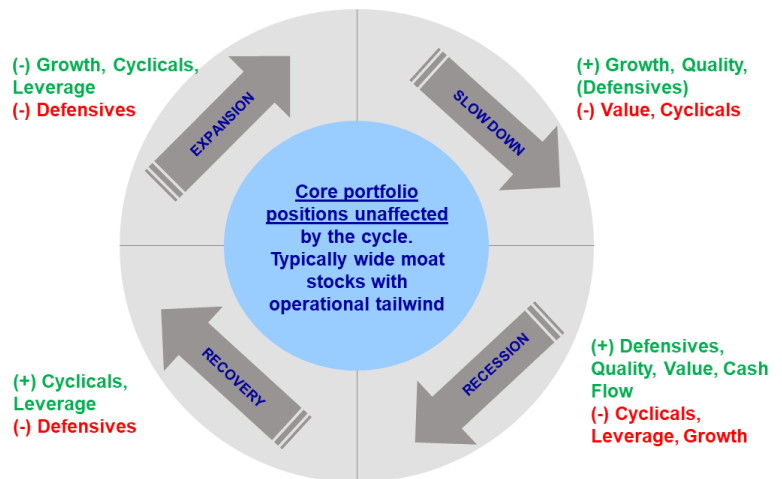


The North American Stars Equity strategy was transitioned into Nordea's STARS franchise about two years ago. How did you manage this process?

Global Stars had about a 65% weighting to the US when we took this North American strategy in-house, so our portfolio managers and analysts knew the companies very well and had followed each one for many years. While we had the core of the portfolio covered, it was quite research intensive initially to populate the remainder of the portfolio. Nevertheless, it was a smooth transition because of the synergies with Global Stars.

You mentioned the importance of the understanding the business cycle. Can you elaborate on why this is?

While we are bottom-up investors, co-portfolio manager Johan Swahn and I have a combined 35 years of experience covering cyclical stocks. We were both analysts, covering areas like industrials and energy, so we feel we have a good handle on where we are in the business cycle. While we gradually adjust the positions of the portfolio in terms of where we are in the cycle, we do not take directional bets on the market – it is all bottom-up. For example, through this bottom-up lens, our overweight in the Financials sector is 2.4% today, while it was a similar underweight level about 18-24 months ago. We made this gradual transition because we now see significant upside in our banking positions, as opposed to the limited upside in the recent past. The same is true with industrials today.



There is always talk about the merits of growth and value. How do you balance the portfolio's position between the two styles?

We are agnostic. Using the Financials sector as an example, as just mentioned, we see a lot of upside in this space after the pandemic-induced recession. After banks were sold down significantly, we took advantage and increased our weighting. Of course, banks are referred to as value stocks. This means we have increased our value position, but it occurred naturally, as a result of bottom-up stock selection.

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