Investment Insight
Lessons from 2023

Morningstar Investment Management EMEA

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For Financial Advisers to use with their clients

Each year reminds us what's important for investors, here are three insights from 2023.

The first is the increased importance of managing risk well. Handling uncertainty, behavioural biases and fundamental economic shifts, are essential if investors want to stay on track to achieve their financial goals. This has become more important because of the dramatic rise in interest rates and the breakdown of global stability. It's much easier for companies and investors to make money when they can borrow at no cost, usually fuelling much higher levels of speculation than usual or rewarding investors for following long standing themes. All prior episodes suggest a rougher ride is in store as we all adjust to much higher cost of debt by cutting back on spending, selling assets or renegotiating with lenders. Thinking about a wide range of scenarios and accessing diversifying assets that are fairly priced all help to deal with risk.

This leads me onto our second insight from 2023: the importance of deep global research. There was a time when you could get by with a small talented team based in London but the today the world is too complex and the number of markets too large. Greater specialisation is required. Making sense of what is happening today, let alone the future, has become both more challenging and rewarding. We are fortunate to have large, regionally based research teams as well as access to methodologies and research within Morningstar covering single companies, proprietary risk modelling, credit ratings, private markets and sustainability. Paramount is the modelling of future cashflows and assessing fair value to avoid overpaying for in-vogue investments or falling into value traps where things get a lot worse than you expected. Deep research led to our identification and allocation to profitable vintages of opportunities for our clients over the years, with Emerging Market Debt notable in 2023.
The third insight is the value of taking a long-term perspective, as this is more closely aligned to investors' time horizons for accumulating wealth during a working lifetime and drawing down on assets in retirement. Many great investment opportunities also require patience to profit from. This was the case with oil and gas companies which took 2 years to transition from pariah status when we acquired them in 2020 to messiah status by 2022 as oil prices rebounded. Emerging market bonds had a similar journey while healthcare stocks were very out of favour in 2018/19 rebounding in 2020 and 2021. In 2023 it's been Infrastructure related companies that have fallen out of favour, triggering us to add exposure recently.

Interestingly cash has also gone from being loathed to being loved today for its security and the higher level of return. This makes sense for funding short term needs but not for building wealth or deriving an income in retirement. Over the longer term, returns are much less likely to beat inflation vs equities and bonds. Cash also scores poorly as a diversifier vs government bonds, in times of crisis and returns turn out to be less stable over time because interest rates fluctuate. A long-term investing perspective is key for staying the course and improving the odds of achieving financial goals.

Unless stated otherwise, all data sources are from Morningstar Direct as at 31/10/2023.

Disclosures