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A senior portfolio manager at Morgan Stanley's $665 billion investment-management business shares his playbook as stocks run higher in 2020 — and 3 non-COVID threats that will occupy his attention in 2021

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- **Andrew Slimmon of Morgan Stanley Investment Management says three forces that have supported the recent surge in stocks could become headwinds in 2021.**

- **Slimmon told Business Insider about what he's doing in his portfolios, including positions in cyclical and Asian stocks.**

- **Slimmon's US Core Fund has outperformed 91% of its peers in 2020, and bets on Big Tech and hard-hit stocks have helped. But for 2021, he intends to play more defense.**

MORGAN STANLEY INVESTMENT MANAGEMENT

Andrew Slimmon is a senior portfolio manager at Morgan Stanley Investment Management.

The stock market has given investors a lot to be thankful for in November, including double-digit moves and all-time highs for major indexes.

But that can't last forever, and the time to plan for more difficult days is now. Andrew Slimmon, who advises on Morgan Stanley Investment Management's long-equity strategies and manages its US Core Portfolio, is turning his attention to those future challenges.

"I suspect as we get closer to the end of the year, we probably will bring down the amount of risk," he told Business Insider in an exclusive interview. "For all the things that are pushing the market higher now, I think that's going to move from a tailwind to a headwind at some point next year."

Slimmon has done well this year at getting ahead of where the market is going to go. He's spent much of the year betting on economically sensitive recovery stocks, and the Core Fund has outperformed 91% of large-cap blended funds in 2020 as of November 23, according to Morningstar data.

"This past summer we bought the casinos, we bought the theaters, we bought gym stocks and obviously, certainly financials, and the credit card companies, and all those stocks are on the move big time right now," he said.

Slimmon is emphasizing stocks that were strong performers before the pandemic sell-off and haven't received much love from the market even though their businesses are recovering. He's also investing in Asian stocks.

"They're just very, very cheap relative to their growth rates and relative to their counterparts in the United States," he said. "With the dollar depreciating and Asian currencies appreciating, it means that money is flowing back to Asia and that will lead, in our opinion, to a valuation closure between Asian tech, Asian growth stocks, and US growth stocks."

3 market threats on Slimmon's radar

Those views for 2021 are built around three major market threats Slimmon is concerned about. The first is **inflation**, as he says the economy will continue to heal next year – and as that recovery continues, the Federal Reserve will start to move away from the rhetoric investors have found so encouraging this year.

While the Fed has made clear it doesn't plan to raise interest rates for years, the difference in approach will cause long-term bond yields to increase.

"Once we get through COVID, I think you're going to start to hear the Fed get less accommodative, at least in their verbiage," Slimmon said. "It could be problematic for some of the tech stocks that are trading at very, very high, very, very high multiples."

He says that could cause weaker returns and more volatility, as it did when the Federal Reserve altered its highly accommodative stance in 2010 when the Global Financial Crisis was fading into the rear view. Slimmon says those problems could kick in if the yield on the 10-year Treasury note rises to about 1.25%.

He added that political uncertainty about the upcoming Senate elections in Georgia could contribute to that turbulence.

"There's clearly a rotation going on, and people are chasing the rotation because we're way too overweight in growth stocks," he said. "The equal-weighted S&P should outperform the cap weighted, because the cap weight is so heavily in the mega-cap tech stocks that are really lagging here."

The second problem is that **sentiment** among investors is becoming very bullish, and that's usually a sign that a rally is in its late stages.

"All this cash has been sitting on the sidelines is only now coming in, and I think that will continue to next year," he said. "Managers are being forced to buy the market. And ultimately that's going to run out of steam at some point next year."

One of the most important parts of the recent rally, especially before the recent developments in the vaccine effort, was the fact that corporate **earnings** have been much better than experts expected given all the challenges the economy is facing. But Slimmon says Wall Street's expectations will adjust.

"Earnings have come in better than what people expected, and the markets respond to the second derivative," he said, referring to the rate at which they're changing. "I suspect that you're going to see a lot of estimates go up for next year on anticipation that we'll get through COVID, and that therefore the bar will be tougher for companies to beat."