Handelsbanken
Wealth & Asset Management

INVESTMENT OUTLOOK 2024

Answering the big questions

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Welcome to our Investment Outlook 2024

Investors have endured a strange few years, as the global economy and financial markets attempt to adapt to a post-pandemic world, the highest inflation seen in decades, and a spate of interest rate increases from the world's leading central banks. Little surprise, then, that our customers have been brimming with questions about what will come next.

We're lucky to have a frank and open relationship with our customers, and throughout 2023 we've been fielding their queries on financial markets, the global and UK economy, and the decisions we've made in managing our own investment strategies. In this special Investment Outlook, we've compiled an assortment of the questions we've been asked throughout the year.

In our first section – *Ask us about… the economic picture* – we take a look at what's next for the economy in 2024. When will we see the recession we've long been predicting, and when will interest rates start to fall again? We discuss why the experience of inflation has been different in the UK, and what the British public should expect next for high street prices.

In our second chapter – *Ask us about… events on the global horizon* – we've cast our eyes around the globe, as we know that some customers are wondering how world events could impact financial markets in the new year. From a looming US presidential election to an inevitable assortment of (as yet unknown) geopolitical surprises, how are our investment strategies prepared to face the financial market consequences of real-world affairs in 2024? We outline the diverse range of assets and specialist protection instruments at work in our strategies, aimed at weathering any storms.

But with high interest rates offering compelling returns on cash savings, is it worth investing in financial markets at all? We've been asked this many times in 2023, and you'll have to turn to the third chapter – *Ask us about… financial markets* – to hear our answer. In this section, we also discuss the market's winners and losers, make the case for sustainable investing, and outline why we still think government bonds are the place to be.

Finally, we answer the trickiest questions of all in our fourth chapter – *Ask us about… our investment decisions*. Do we still have faith in a global 'multi asset' approach? How will we make money from bonds? Will sustainable assets and income investing continue to face challenges in 2024? We make the case for keeping the faith in our diverse, long-term strategies, tell you about the changes we've made in 2023, and what we hope this means for 2024.

As ever, we're keen to hear your feedback, you can contact us at **marketing.hwam@handelsbanken.co.uk**

We wish you a peaceful and happy 2024.

Graham Bishop Chief Investment Officer

Ask us about... **the economic picture**

Q Where is the recession you've been predicting all year?

When we talk about recession occurring in the global economy, we're generally referring to a tangible slowdown in growth in the world's most important economy: the US. Throughout history, whenever the US central bank (the Federal Reserve, or 'Fed') raises interest rates, something in the US economy breaks, and it's normally growth. Since early 2022, the Fed has raised interest rates 11 times in an effort to slow economic activity and force high inflation downwards. In doing so, the Fed has moved the top of its target interest rate range from 0.5% at the beginning of 2022 to 5.5% at the time of writing.

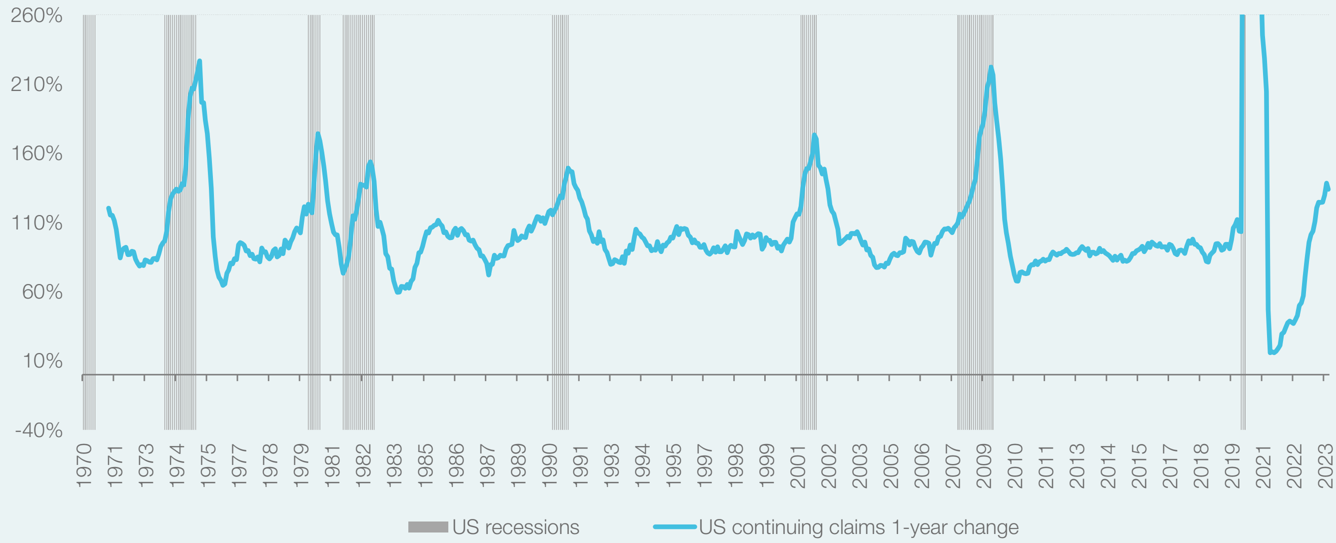
We've been predicting an economic downturn for much of 2023, and our best guess has always been late 2023/early 2024. While predicting the course of the US economy is never easy, it doesn't feel like rocket science (given this dramatic interest rate backdrop) to say that there will ultimately be a price to pay in terms of economic growth. Indeed, the Fed has been quite clear that it is willing to sacrifice future economic growth in the war on inflation.

We do not anticipate (nor have we ever anticipated) an especially severe recession like those witnessed in the global financial crisis (2008) or the COVID-19 crisis (2020). Nevertheless, we do expect a period of economic slowdown in the near future. Indeed, we are already seeing signs of cracks emerging, whether this is through banks becoming more discerning about lending to consumers and corporates, beginnings of weakness in US employment market data, and insolvencies and bankruptcies picking up on both sides of the pond. We expect these nascent cracks to become more apparent over the coming months.

> "We do expect a period of economic slowdown in the near future. Indeed, we are already seeing signs of cracks emerging in the global economy."
>
> **Graham Bishop** Chief Investment Officer

The annual change in long-term US unemployment is reaching levels consistent with periods of recession

1-year change in US continuing jobless claims, with periods of recession shown in grey



Source: Bloomberg, National Bureau of Economic Research

Q Why have interest rates risen so much, and where will they settle?

The COVID-19 era created the perfect storm for inflation, as the result of a potent cocktail of factors from extraordinary levels of government spending, pent-up consumer demand and a build-up of household savings.

For the past 18 months or so, central banks across the developed world have been waging war on the ensuing high inflation through sharp, frequent interest rate hikes. However, changes to interest rates impact the real-world economy with a lag of around 18 months, meaning that the true effect of the first round of interest rate hikes (in early 2022) are only just beginning to truly hit home.

Central banks know that they have taken a gamble with these rate hikes, and (as we noted above) have chosen to prioritise fighting inflation at the likely expense of future economic growth. Nevertheless, with economic cracks now beginning to show, we are inclined to agree with signals from bond markets, where bond yields and prices indicate that investors believe interest rates are now peaking in the developed world.

Importantly, though, we don't think that interest rates will begin to fall sharply in the immediate future. Indeed, we believe that rates are likely to stay at elevated levels while central banks take time to check the effectiveness of what they've done so far. We don't see interest rate cuts happening until the latter part of 2024, but we do see them happening.

Q Why has UK inflation been so stubborn, and is this set to change?

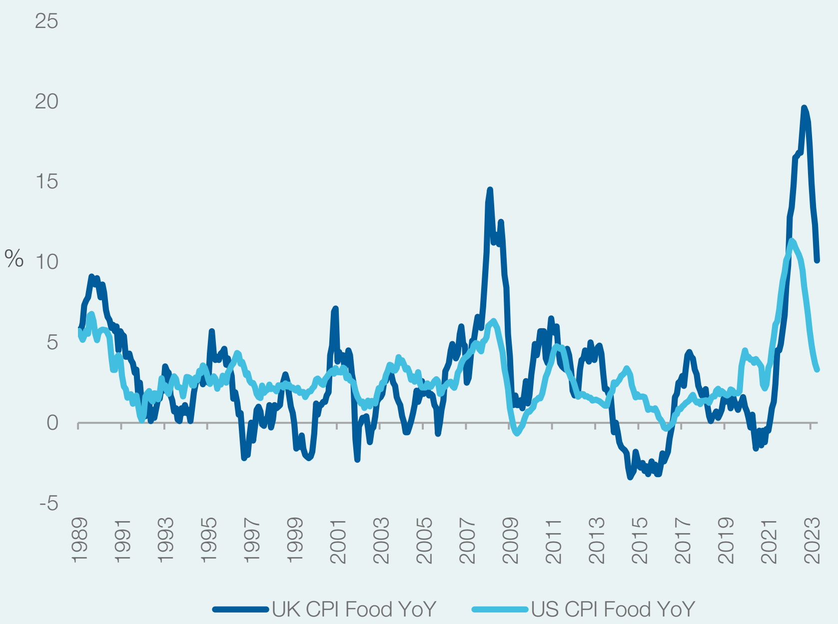
The UK has struggled with stubbornly elevated inflation versus the US, for example, due to a combination of factors, some of which unfortunately relate to Brexit. When the UK left the EU, it lost access to a pool of cheap labour (especially in industries like construction), creating a different set of inflationary wage pressures in the UK versus other developed economies like the US. What's more, the UK economy is heavily skewed towards the services sector, and this has also contributed to higher inflation given that lack of access to cheap labour mentioned above. Red tape around supply chains for goods going through Europe into the UK has also contributed to higher costs, particularly food, which has played a significant role in stubbornly higher UK inflation. Global food production costs peaked towards the end of 2022, With food prices starting to fall soon after in the US. In the UK we are only now beginning to see a similar scenario playing out.

Nevertheless, the UK inflation picture is beginning to change. UK inflation fell sharply in the one-year period up to October 2023, dropping to 4.6%. As a reminder, this fall in inflation does not mean that prices are falling, it simply means that the rate at which prices are rising has slowed. Cheaper energy prices (versus the same period last year) have been credited with this drop in UK inflation, but UK food costs have also finally begun to fall. Food production costs peaked in October, and lower costs should continue to feed through into high street prices in due course.

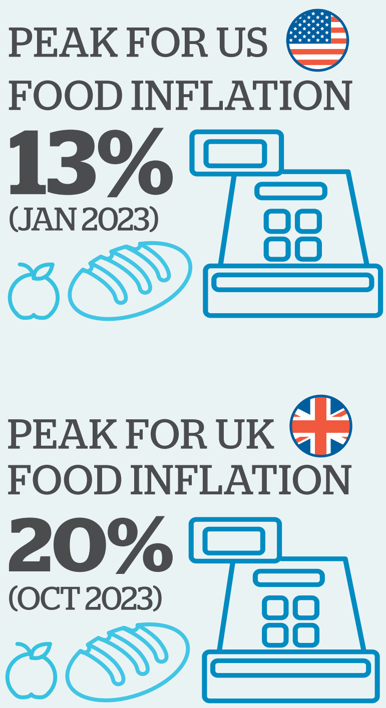
The US remains ahead of the UK on the journey to lower inflation, but we believe that the UK will follow a similar path from here. Asset prices in financial markets – perhaps a little overoptimistically in the US at least – suggest that investors believe aggressive interest rate cuts are on the horizon, but to reiterate, we think it's unlikely that rates will fall materially from here in the near term. However, we do expect them to fall to some degree over the course of next year, and more so in the UK than the US, as the UK economy looks comparatively weaker. Central banks will want to ensure that the war on inflation is truly won before cutting rates, and we anticipate a growing number of key central bankers making public remarks to temper the market's expectations for interest rate cuts in early 2024.

Price rises for food have finally begun to fall in the UK

Food inflation (measured by the Consumer Price Index) in the UK



Source: Bloomberg



Ask us about... events on the global horizon

Q Will the US election impact financial markets in 2024?

US elections are never boring, and 2024's is set to be no exception. As we write, the leading Republican candidate is former president Donald Trump, who is currently fighting four indictments and 91 charges against him. At this juncture, we have no idea whether he will even be available to take part in a cross-country election campaign in 2024, let alone win one.

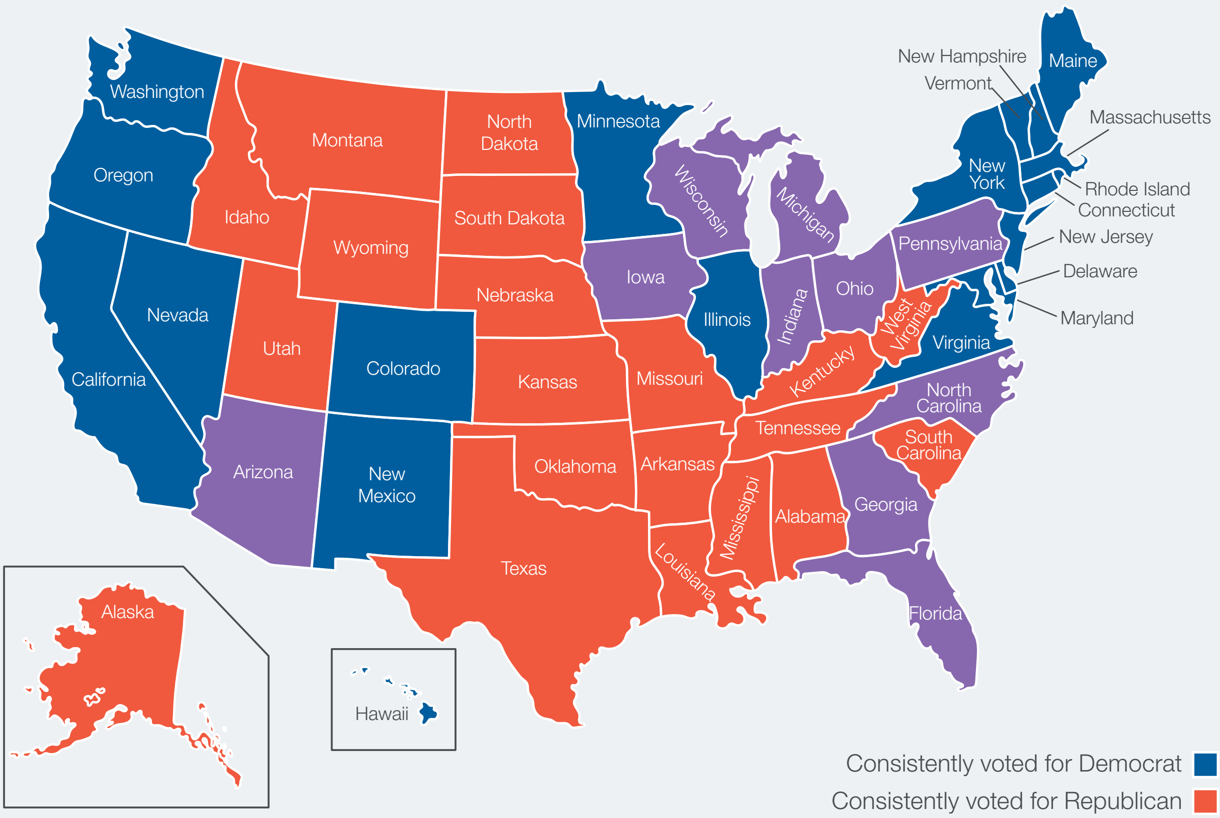
Nevertheless, Trump is currently ahead of incumbent President Biden in the opinion polls. Indeed, despite overseeing an economy with very strong employment levels and an economy that currently looks in stubbornly good shape, Biden's approval rating is close to record lows for any US president. Even so, history is on Biden's side: in over 100 years, no incumbent president has lost an election if the US economy has avoided recession in the two years running up to their second term election.

On a state-by-state basis, the US is currently roughly evenly split between Democrat and Republican supporters. It's likely that – as in previous elections – a relatively small number of voters in a limited number of swing states will decide the results of the 2024 election. This also suggests that no matter who lives in the White House in 2024, they will find it very challenging to secure meaningful majorities in either the Senate (upper house) or the House of Representatives (lower house) of US Congress. This will make it very challenging to make sweeping changes to government spending policies. For financial markets, which price stability and certainty, this could look like good news. With markets beginning to worry more and more about the cost of financing the debt burden of a very large US deficit, prudence in government expenditure (or indeed government inactivity) may not be such a bad thing after all.

> "No matter who lives in the White House in 2024, they will find it very challenging to secure a meaningful political majority. This will make it very difficult to make sweeping changes to government spending policies."
>
> **David Absolon** Investment Director

A relatively small number of states will decide the US presidential election

How US states voted in the 2008, 2012, 2016 and 2020 presidential elections



Source: Strategas

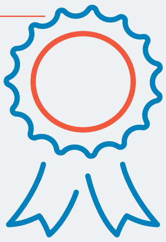
Presidential re-election campaigns live or die by the state of the economy

Re-election bids by US presidents

NO RECESSION TWO YEARS BEFORE RE-ELECTION

- Barack Obama
- George W. Bush
- Bill Clinton
- Ronald Reagan
- Richard Nixon
- Lyndon B. Johnson
- Dwight D. Eisenhower
- Harry Truman
- Franklin D. Roosevelt
- Franklin D. Roosevelt
- Franklin D. Roosevelt
- Woodrow Wilson

RE-ELECTED



RECESSION TWO YEARS BEFORE RE-ELECTION

- Donald Trump
- George H. W. Bush
- Jimmy Carter
- Gerald Ford
- Herbert Hoover
- William Howard Taft

NOT RE-ELECTED

Source: Strategas

Q How are we protecting portfolios from geopolitical events?

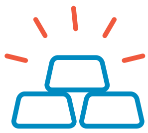
By their very nature, geopolitical events are unpredictable and very difficult to analyse, making it challenging to factor them into investment decision making. Historically, geopolitical events have often created good long-term buying opportunities for investors, but in the near term they can create significant volatility and unsettle nerves.

We believe that a multi asset approach can help weather the market storms caused by geopolitical events, as our investment strategies are much more diversified than a single asset type approach (such as a fund focused solely on shares). No investment outcomes can ever be guaranteed, but by investing across a range of asset types and geographies, we aim to participate in financial markets when the skies are blue, but defend when the skies turn grey.

We believe that a blend of diversifying assets in a wider investment strategy is the optimal approach to managing unpredictable events like geopolitical risk. Below, we outline some of the specific areas we see as ‘diversifiers’ within our multi asset investment strategies:

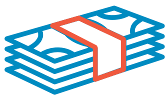
Government bonds

During the move away from ultra-low interest rates in 2022 and 2023, a major traditional area of the market – government bonds – has now regained a lot of its potency as a diversifier in the event of geopolitical events. Bond yields have risen from around 0% to around 5%, meaning that bond prices (which always move in the opposite direction to yields) have fallen, and now have much greater potential to rally in the event of any geopolitical volatility.



Gold

Gold is a constant feature in our multi asset investment strategies, as we do believe it has diversification properties, particularly during periods of volatility. The long-term relationship between the gold price and real interest rates has remained strong, but in times of geopolitical crises, the demand for safety has consistently supported gold.



Traditionally safe-haven currencies

Historically, the Japanese yen and the US dollar are seen as ‘safe haven’ hideouts during periods of stress. While the past can be an unreliable guide to future performance, we believe that having some exposure to these currencies will aid us during bouts of volatility or geopolitical stress.

Specialist protection instruments

Our multi asset strategies also hold a specialist protection strategy designed to protect against sudden and extreme market falls, such as in response to a geopolitical event. This ‘tail risk hedging’ works a bit like an insurance premium that pays out only if certain stars align. Unlike our other diversifiers, our tail risk hedging instrument is extremely specific: it can be a very valuable diversifier in times of stress, but the exact conditions must be met for it to show its full potency.

Ask us about...
financial markets

Q What's the point in investing, versus enjoying high interest rates on cash or short-dated government bonds?

Holding cash savings or short-dated UK government bonds to maturity guarantees you a return (assuming your bank/the UK government does not default). However, we believe there is increasingly limited potential for financial returns through these routes.

Interest rates on cash and bond yields appear to be close to peaking, meaning that we are likely close to the peak in returns for cash/short-dated government bonds as a standalone investment tactic. The risk of reinvesting cash or the proceeds of maturing, short-dated bonds is therefore very high: in the foreseeable future, the 'rate of reinvestment' will be going down, not up, alongside interest rates and government bond yields.

When returns on cash savings peak, and bond yields fall, bond prices rise. Therefore, we believe that a blend of short, medium and long-dated government bonds, plus positions in corporate bonds, provides a much more attractive opportunity than cash or short-dated bonds alone.

This is how we are shaping our multi asset investment strategies for the future, particularly our low-risk Defensive strategy, which now holds around 75% of its assets in bonds (as at November 2023). Over time, as this lower bond yield/higher bond price narrative plays out, we foresee that this will also be supportive for the price of shares and 'alternative assets'. So, once again, we feel strongly that a global, multi asset approach is the right place to be.

A challenging few years for a huge range of asset types

Real returns (after accounting for inflation) by asset type: positive returns in green, negative returns in red

Rank	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023 YTD
1	MSCI North Am	MSCI Japan	Oil	MSCI EM	Gold	UK Property	Silver	Oil	Commodities	MSCI North Am
2	UK Linkers	MSCI Eur x-UK	Silver	UK Property	Global Gov't	Oil	Gold	UK Property	Oil	MSCI World
3	UK Property	MSCI North Am	MSCI North Am	MSCI Eur x-UK	MSCI North Am	MSCI North Am	HF Equity LS	Commodities	HF CTAs	MSCI Eur x-UK
4	HF CTAs	MSCI World	Commodities	MSCI Pac x-JP	UK Gilts	MSCI World	MSCI North Am	MSCI North Am	Silver	US Lev Loan
5	UK Gilts	UK Property	MSCI EM	MSCI Japan	UK Linkers	MSCI Eur x-UK	MSCI EM	MSCI World	Gold	MSCI Japan
6	UK Corp	Global Gov't	MSCI World	MSCI World	HF RV	MSCI UK	MSCI World	MSCI UK	HF Macro	US HY
7	MSCI World	EM Gov't	Gold	HF Equity LS	UK Corp	MSCI Japan	MSCI Japan	MSCI Eur x-UK	MSCI UK	Gold
8	Global Gov't	UK Corp	MSCI Pac x-JP	MSCI UK	US Lev Loan	MSCI EM	UK Linkers	HF Event Driven	MSCI Pac x-JP	UK Property
9	EM Gov't	UK Gilts	UK Linkers	MSCI North Am	MSCI World	MSCI Pac x-JP	HF FoFs	HF Equity LS	HF RV	EM Gov't
10	US Corp	HF CTAs	MSCI Japan	EM Gov't	Silver	Gold	HF Event Driven	HF Macro	US Lev Loan	UK Corp
11	Gold	HF FoFs	MSCI Eur x-UK	HF FoFs	HF Event Driven	US Corp	UK Gilts	HF RV	HF Event Driven	MSCI UK
12	MSCI Pac x-JP	HF RV	MSCI UK	HF Event Driven	US Corp	Silver	UK Corp	HF FoFs	MSCI Japan	US Corp
13	HF Macro	US Corp	US HY	US HY	US HY	US HY	US Corp	HF CTAs	HF FoFs	HF RV
14	MSCI EM	HF Equity LS	UK Corp	US Corp	MSCI Pac x-JP	HF Equity LS	MSCI Eur x-UK	MSCI Pac x-JP	MSCI Eur x-UK	Global Gov't
15	HF RV	HF Macro	US Lev Loan	UK Corp	HF FoFs	EM Gov't	HF Macro	US HY	MSCI World	HF Event Driven
16	HF FoFs	UK Linkers	UK Gilts	HF RV	HF Macro	UK Corp	Global Gov't	UK Linkers	MSCI North Am	HF Equity LS
17	US HY	MSCI UK	HF Event Driven	Gold	Commodities	US Lev Loan	US HY	US Lev Loan	MSCI EM	HF FoFs
18	MSCI Japan	US Lev Loan	EM Gov't	Oil	EM Gov't	UK Gilts	EM Gov't	MSCI Japan	HF Equity LS	MSCI EM
19	HF Equity LS	MSCI Pac x-JP	HF RV	US Lev Loan	MSCI Japan	HF FoFs	MSCI Pac x-JP	US Corp	Global Gov't	Silver
20	HF Event Driven	HF Event Driven	US Corp	UK Linkers	HF CTAs	UK Linkers	HF RV	MSCI EM	US HY	HF Macro
21	US Lev Loan	US HY	HF Equity LS	UK Gilts	HF Equity LS	HF Event Driven	HF CTAs	Global Gov't	US Corp	UK Gilts
22	MSCI UK	Gold	Global Gov't	HF CTAs	MSCI UK	HF RV	US Lev Loan	EM Gov't	UK Corp	HF CTAs
23	MSCI Eur x-UK	Silver	HF Macro	HF Macro	MSCI EM	Global Gov't	Commodities	UK Corp	EM Gov't	MSCI Pac x-JP
24	Commodities	MSCI EM	HF FoFs	Global Gov't	MSCI Eur x-UK	HF Macro	MSCI UK	Gold	UK Gilts	UK Linkers
25	Silver	Commodities	HF CTAs	Silver	UK Property	HF CTAs	UK Property	UK Gilts	UK Linkers	Commodities
26	Oil	Oil	UK Property	Commodities	Oil	Commodities	Oil	Silver	UK Property	Oil

Commodities – an index representing commodity market prices

EM Gov't – bonds issued by governments in developing economies

Global Gov't – bonds issued by governments around the world

Gold – an index representing the price of gold

HF CTAs – Commodity Trading Advisor hedge fund (invest in financial market trends)

HF Equity LS – hedge funds that bet for/against specific assets

HF Event Driven – hedge funds which bet on specific corporate actions (like mergers)

HF FoFs – a hedge fund which invests in other funds (typically hedge funds)

HF Macro – macro hedge funds (invest based on economic or political views)

HF RV – relative value hedge funds (invest in temporary differences in asset prices)

MSCI EM – an index representing stock markets in developing economies

MSCI Eur x-UK – an index representing mainland European stock markets

MSCI Japan – an index representing Japanese stock markets

MSCI North Am – an index representing North American stock markets

MSCI Pac x-JP – an index representing Pacific region stock markets

MSCI UK – an index representing the UK stock market

MSCI World – an index representing global stock markets

Oil – an index representing the price of oil

Silver – an index representing the price of silver

UK Corp – corporate debt issued in the UK

UK Gilts – bonds issued by the UK government

UK Linkers – inflation-linked UK government bonds

UK Property – an index representing the UK property market

US Corp – corporate debt issued in the US

US HY – high yielding (usually higher risk) corporate debt issued in the US

US Lev Loan – loans given to already indebted US companies/individuals

Source: Handelsbanken Wealth & Asset Management, as at November 2023

Q Who have been the market winners and losers in 2023, and who will be next?

It's been a tough period for global, multi asset investors over the past few years. 2022 and 2018 were two of the three worst years (in a 96 year window) for the number of asset types producing a positive 'real' financial return (i.e. a positive return after accounting for inflation). For context, the worst year was 1929, in the Great Depression! 2023 has also seen a lot of negative returns from a range of asset types, reinforcing this challenging period for investors.

How have different asset types fared?

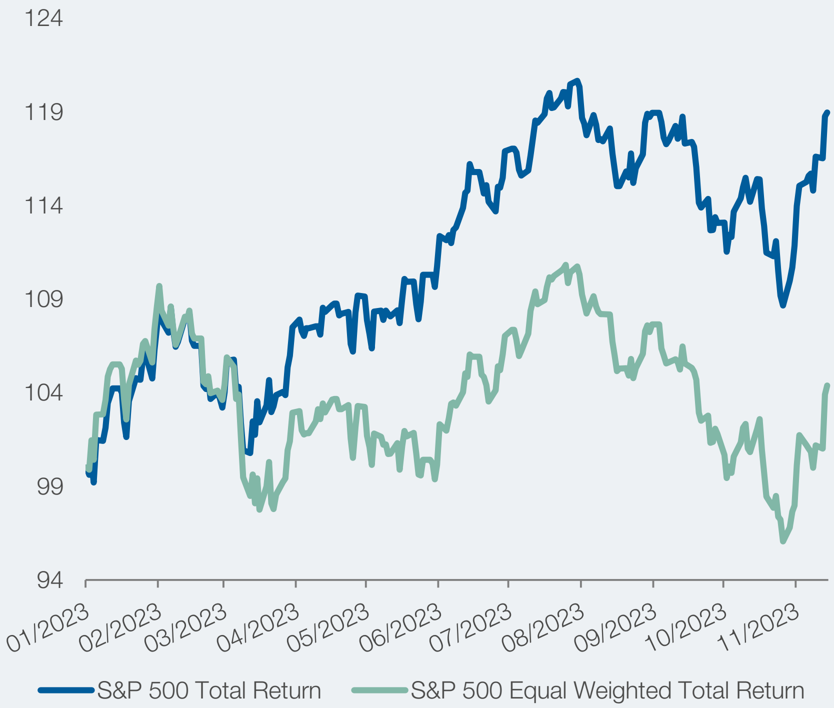
Stock markets led by a narrow group of companies

Winners for the year have largely been concentrated in a few select areas, primarily shares, where the overwhelming majority of returns have come from just a few businesses in the US – the 'Magnificent Seven', i.e. the seven largest technology companies in the S&P 500 Index (a representative basket of the 500 largest US-listed companies). Because of the market size of the Magnificent Seven companies, their shares account for almost a third of the S&P 500, and can skew its performance. As we write, the S&P 500 Index has risen by 19% in 2023. However, if all shares in the index were represented equally (or 'equally weighted'), it would have delivered only a slightly positive return for 2023.

> "Commercial property has been hit by its inherent sensitivity to interest rate expectations, while among hedge funds, managers of strategies which benefit from higher market volatility have been largely disappointed."
>
> **Robert White** Investment Manager

Stock market returns have been very concentrated

S&P 500 Index versus S&P 500 equally weighted



Source: Bloomberg

Bonds at the eye of the storm

Until very recently, bond markets have continued to be at the eye of the storm for financial markets, buffeted by stubbornly high inflation and central banks determined to control pricing pressures by raising interest rates. This has meant that most areas of bond markets have struggled this year, particularly government bonds – a traditional 'safe haven' asset.

A mixed bag for commodities

Despite various conflicts and other geopolitical issues, oil is perhaps surprisingly down for the year. Meanwhile, gold (often seen as a place to hide) has made some progress, though not as much as some might have hoped.

A challenging environment for 'alternative' assets

It's also been a struggle in the alternatives sector (beyond traditional stock and bond markets). Commercial property has been hit by its inherent sensitivity to interest rate expectations, while among hedge funds, managers of strategies which benefit from higher market volatility have been largely disappointed – despite all the challenges facing markets, volatility has remained relatively low versus historical standards.

So, aside from a concentrated area of stock markets, it's been a real struggle for global assets this year. We never rely solely on history as a guide, but we do know that periods of struggle are more often than not followed by fertile periods for investors. With the 2024 starting point for asset valuations now lower, we believe that their potential for future returns is now higher.

Q Is investing sustainably really still worth it?

Our short answer is 'yes'. This has been a challenging period for financial markets, with sharply higher inflation and interest rates disproportionately affecting sustainable asset prices, as sustainable investing tends to lean towards smaller, growth-oriented businesses (more impacted by a rising interest rate environment). However, this near-term environment does not change our high conviction in sustainable investing as a long-term approach to putting our customers' capital to work. We currently see attractive areas for sustainable investing across the full breadth of financial markets, from green government bonds and renewable energy to biopharmaceutical research and clean water funds.

Importantly, we continue to believe that sustainable investing can provide a cost effective and diverse way to invest, and over the past few years we've been encouraged to see the financial services industry waking up to high levels of demand for sustainable investments. This means that more and more investment options are coming to the market, across the full spectrum of asset and sub-asset types, and a broader set of structures/approaches.

What's more, despite a challenging period for investors, demand for sustainable investing has proven resilient. Even when investors have taken money away from other areas of the market, for example during turbulence caused by the war in Ukraine, capital has flowed into sustainable assets. Times may have been tough, but sustainable investors remain committed to investing in line with their principles whilst also seeking attractive long-term financial returns.

> "We currently see attractive areas for sustainable investing across the full breadth of financial markets, from green government bonds and renewable energy to biopharmaceutical research and clean water funds."
>
> **Nikki Howes** Investment Manager

AROUND **£100BN** FLOWED INTO SUSTAINABLE INVESTMENT FUNDS IN 2022

Approximate net figure, December 2022 currency conversion rate of approximately $1 to £0.83.

Source: Morgan Stanley Institute for Sustainable Investing

Q Why are you still pro-bonds when bond markets have performed so badly?

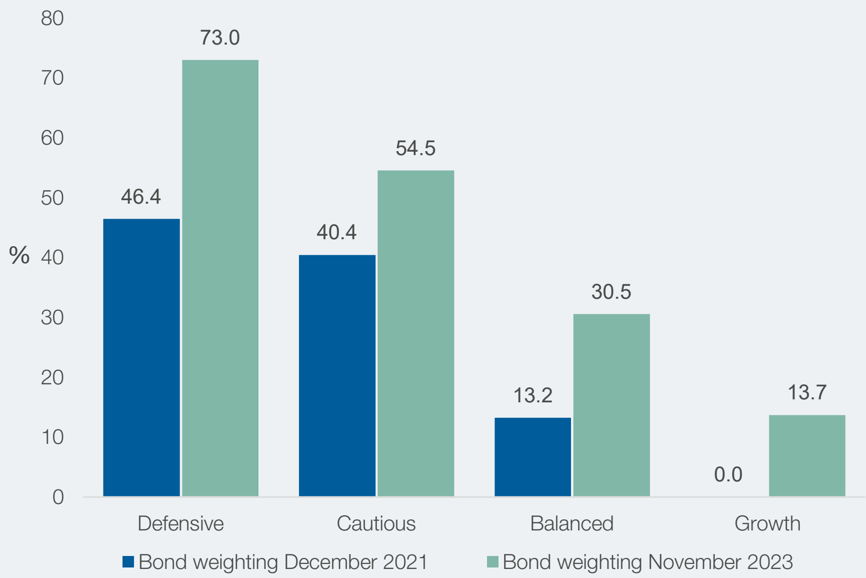
For most of the time since the 2008 financial crisis, bonds valuations have looked very poor. This was especially problematic for investors in lower risk investment solutions, where bonds are a major feature. More recently, bonds have performed poorly as bond yields were forced to adjust to higher interest rates. UK government bonds (including inflation-linked bonds) have seen more extreme falls during this period of adjustment than stock markets in the financial crisis.

Bond yields (which move in the opposite direction to bond prices) have risen a lot in 2022 and 2023. With bond yields high and bond prices low, the potential for future returns from bonds also look attractive. We believe bond yields are at, or close to their peak, and expect yields to fall over the next 12 months.

With hindsight, we arrived early to the party for bonds, but it remains an area of high conviction for the Investment Team. When bond yields fall, bond prices rise, and we believe that in certain areas of the bond market prices could be set to go up materially. As a result, we have been increasing not only the amount of bonds we hold in our strategies, but also the maturity of these bonds. The longer our bonds have to run, the bigger the potential move in price and financial return. No investment decision comes without risk, but if our views are correct, bonds should be a major driver of returns in our investment strategies over the next few years.

We've added significantly to our bond market positions

Changes to our bond allocation across our core multi asset strategies



Source: Handelsbanken Wealth & Asset Management

Ask us about... **our investment decisions**

Q Do you still think multi asset is the right way to invest?

The short answer is: absolutely. We know that it's been a very tough period for global multi asset investors over the last few years, particularly in recent times. Few types of assets have been entirely immune to the issues that arise with adjusting from interest rates at or close to zero to a more historically 'normalised' rate environment.

For a while, you might have heard market commentators insisting that there was no alternative to buying shares when it came to financial returns. However, we firmly believe that those days are over. Not only have strong positive returns in stock markets been limited to an extremely small number of major US businesses in recent history, but other asset classes that have been vulnerable to interest rates rises (like bonds) are now offering the potential for extremely compelling future returns to long-term investors. Similarly, commercial property and various alternative income strategies have performed poorly of late, but their market valuations are becoming more attractive when it comes to competing for attention in an investment strategy built of a range of asset types. We also subscribe to the view that certain areas of stock markets which have struggled (such as the shares of smaller companies) are now beginning to look appealing in terms of the balance of long-term risk and potential reward they offer to investors.

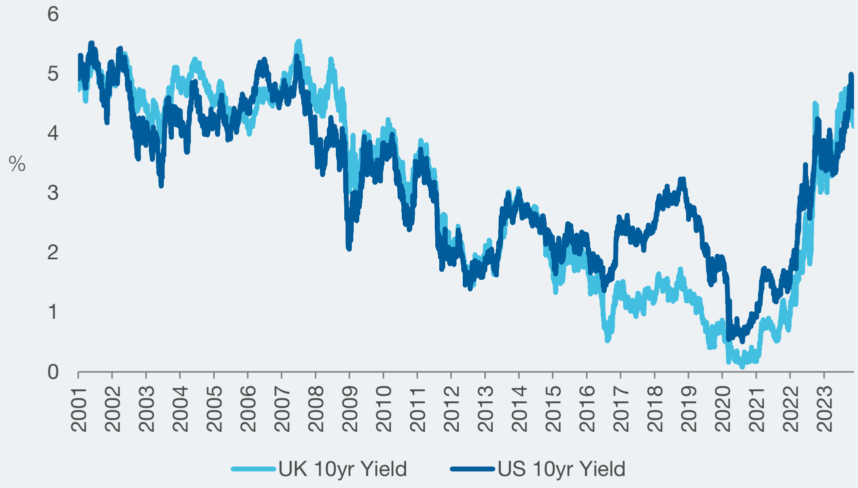
In summary, we believe we are now shifting from a world where the only assets in town were shares (and a very concentrated group of shares at that) to a backdrop which warrants a much more diversified and global approach to investing. Encouragingly for us, this plays very nicely to our long-standing investment proposition.

> "Other asset classes that have been vulnerable to interest rates rises (like bonds) are now offering the potential for compelling future returns to long-term investors."

David Absolon Investment Director

Bonds are offering fresh potential for attractive long-term returns

Yields (%) on 10-year US and UK government bonds



Source: Bloomberg

Q What have we done/changed in our investment strategies?

The interest rate environment has changed dramatically over the past 12-18 months. Mindful of this change, and the economic implications it brings, over a similar timeframe we have made material changes to the mix and proportions of the assets held in our investment strategies.

In keeping with our view that real value has emerged in bond markets, we have been significantly increasing our bond market positions, at the expense of our holdings in stock markets and 'alternative' (i.e. beyond traditional stock and bond markets) income-yielding assets. As a result our portfolios look more traditional, more liquid (easier to quickly buy/sell the assets we hold), and more diversified than they have for many years. In a world where bond yields have risen to such attractive levels, we don't feel that we need too much complexity in our investment strategies in terms of the assets we hold specifically to drive financial returns, or the assets we use to diversify risk.

Some key changes:

More invested in:

- Developed market government bonds and good quality corporate debt
- Bonds which are more sensitive to changes in interest rates
- Passive (index-tracking) bond market, stock market and global property instruments

Less invested in:

- Emerging market bonds and shares
- Illiquid (difficult to buy and sell quickly) private assets
- Alternative assets (i.e. investments beyond traditional bond and stock markets)

These changes have been designed to make our market positions simpler, cheaper, and ready for the future. Importantly, our strategies are still expressing our highest conviction views in all areas of the market.

Q How do you intend to make money from bonds?

We expect future returns from investing in bonds to come from a combination of income (through the 'interest' paid on bonds) and capital return (a rise in the price of the bonds we hold).

The yields on our short-dated government bond positions, if we hold these bonds to maturity, should provide a key area of future returns. We have also increased our longer-dated bond holdings, giving our investment strategies greater sensitivity to potentially falling bond yields in the future. Unlike the shorter dated bonds, it's unlikely we will hold these bonds until their redemption dates, given the amount of time left before they mature. However, we do not need to wait for this redemption date for these bonds to increase in value: when bond yields do start to fall, the price of these bonds should increase, and we can choose whether or not to hold onto them or sell them at these higher valuation levels, depending on our view of the world at that time. We also see selective opportunities in high quality corporate debt.

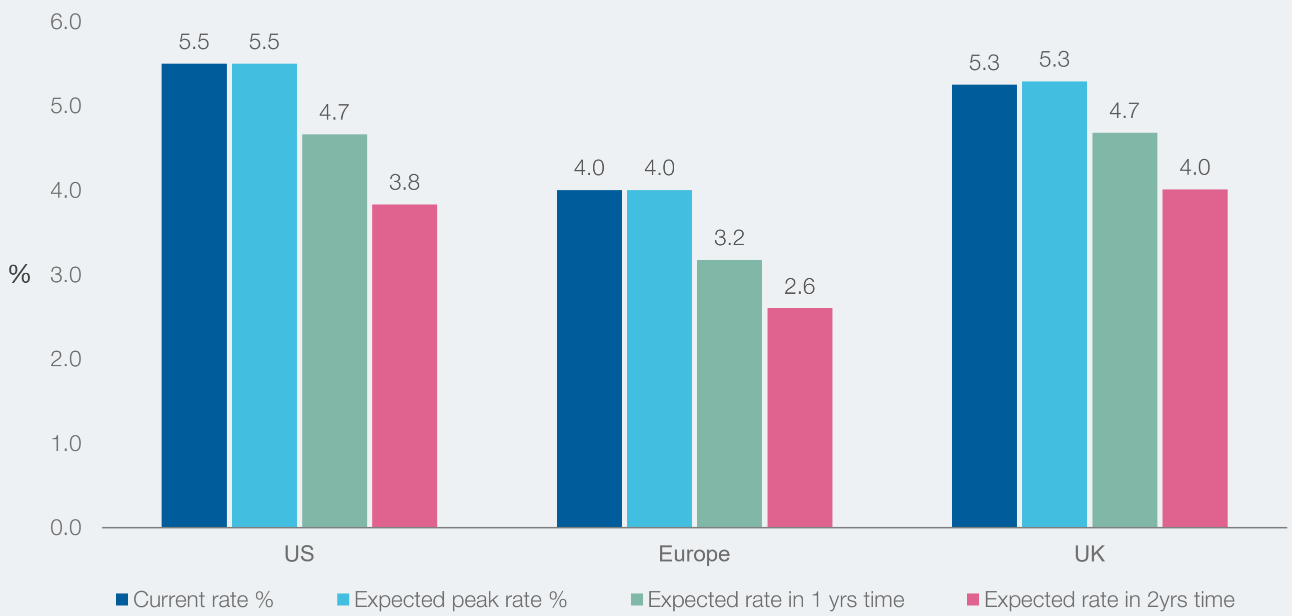
In our view, bonds will be a major driver of financial returns for all of our investment strategies over the next few years, but particularly for our lower risk strategies which hold a greater proportion of bonds.

"In our view, bonds will be a major driver of financial returns for all of our investment strategies over the next few years, but particularly for our lower risk strategies which hold a greater proportion of bonds."

Scott Ingham Investment Director

Markets expect interest rates to fall from here, meaning returns from cash have peaked but bond investors can lock in higher yields

Financial market expectations for interest rates in the US, Europe and UK



Source: Bloomberg

Q Will the performance of sustainable assets continue to lag behind mainstream financial markets in 2024?

Firstly we would say that sustainable investing is increasingly mainstream investing, as more and more investors choose to put their money to work sustainably.

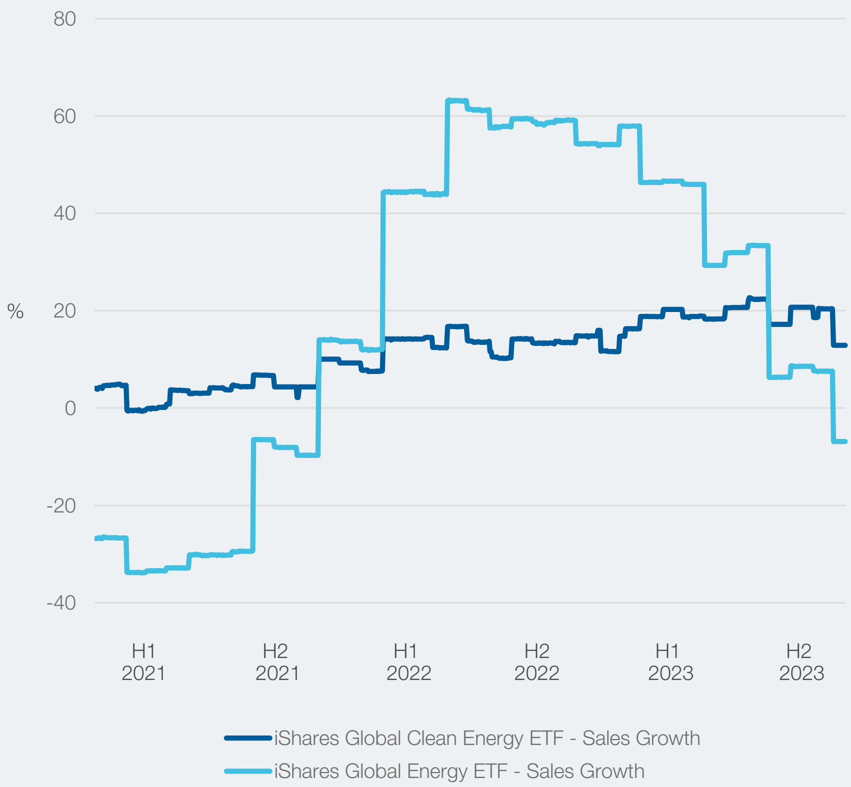
However, there's no denying that it's been a challenging couple of years for sustainable assets. Perhaps the biggest factor weighing on sustainable investment strategies (including our own sustainable range) in recent history has been the strength of traditional energy (fossil fuel) companies versus the sustainable energy industry. In 2019 and 2020, sustainable energy had an exceptional run, while traditional energy markets struggled. This tailed off in the following years, with a complete reversal when the oil price gained momentum following the conflict in Ukraine. This led to a large jump in revenue growth for traditional energy companies.

Sustainable investment strategies (again, including our own) have also been more at the mercy of interest rate rises, due to the uneven impact that the higher cost of money/debt refinancing has had on different areas of the market. Alternative assets, shares in growth-focused businesses, and shares in smaller businesses in general have been much more affected by a higher interest rate environment, and this very much includes the renewable energy sector. Naturally, this has disproportionately impacted sustainable investments.

Nevertheless, we do see causes for optimism for sustainable assets from here. Indeed, we believe that we're already seeing signs that a lot of these trends are reversing. At the time of writing, as the chart shows, clean energy and renewables sales are once again growing faster than the incumbent oil companies. Asset valuations now look exceptionally attractive in these areas, especially if we see interest rates beginning to fall in the coming years. It's worth noting that many of these are high yielding assets too (offering periodic payouts to shareholders/investors), meaning that sustainable investors are being paid to wait for this opportunity to play out.

Growth in clean energy sales is outstripping the wider energy sector

Clean energy sales growth versus global energy sales growth



Source: Factset

Q Will the challenges for income investing continue into 2024?

The past year has indeed been a challenging year for income investing. Firstly, as we've mentioned elsewhere, stock market performance in 2023 has been led by a very small number of large US businesses, which do not pay dividends to shareholders. Meanwhile, our income funds tend to look to the UK, Europe and developing economies in order to find shares offering compelling dividend payouts. This has inevitably led to fishing for dividends in a pool of companies whose share prices have not delivered especially stellar performance.

Secondly, higher income investments are often related to the property sector, and property markets have had a difficult 2023. Thirdly, bonds – another traditionally good source of income – have had a rocky year too. Taken together, this has created an extremely cramped space for finding income without compromising on the market value of assets held.

When it comes to the outlook for income investing, in keeping with our views on the outlook for the global economy, we would be surprised to see such narrow stock market leadership continue in a period of economic slowdown. A levelling off of stock market performance would be better news for income investors. For our own income funds, we also see increasingly attractive valuations in selective areas of property markets and various alternative income strategies. We've long been proud of the smooth journey of income payments we've been able to offer our customers, and while no one can predict the future, we expect the stable nature of our income distributions to customers to continue.

“When it comes to the outlook for income investing, in keeping with our views on the outlook for the global economy, we would be surprised to see such narrow stock market leadership continue in a period of economic slowdown.”

Jaisal Pastakia Investment Director

Investment team

Graham Bishop
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Investment Director

Nikki Howes
Investment Manager

Robert White
Investment Manager

Andrew Bovell
Investment Performance
& Risk Manager

Caroline Von Celsing
Investment Associate

Awards

2023 MoneyAge Awards
Winner: Wealth Management Firm of the Year

2023 WealthBriefing European Awards
Winner: Marketing & PR Campaign

The Asset Management Awards 2022
Winner: Multi Asset Manager of the Year award

2022 WealthBriefing European Awards
Winner: Specialist Wealth Manager with assets under management between £2-5 Billion

2022 PAM 50 Most Influential
Tracey Davidson, Chair of Handelsbanken Wealth & Asset Management

2022 PAM Top 40 Under 40
Jaisal Pastakia, Investment Director

2022 Citywire Thirty Under Thirty
Nikki Howes, Investment Manager

2021 WealthBriefing European Awards
Winner: High Net Worth Team

Commended: Tax Team

Commended: Marketing or PR campaign

To find out more please get in touch:

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Assessing the performance of our investment strategies

Our 'target return' performance benchmarks

Most of our investment strategies aim to deliver financial returns at levels linked to the rate of UK inflation (measured by the Consumer Price Index, or CPI). Over any given five-year period, these strategies target returns which are a pre-defined level above the rate of inflation. Our CPI-linked goals are known as the strategies' target return benchmarks, and are designed to help customers evaluate the strategies' performance in a real-world context. These targeted returns range from CPI+1% for our lowest risk (Defensive) strategies up to CPI+4% for our higher risk (Growth) strategies. Our highest risk (Adventurous) strategy is the exception, as it does not use a CPI-linked goal. Instead, this strategy aims to beat the returns offered by the global stock market (represented by the MSCI All Country World Index).

If the strategies deliver total financial returns to investors (after all costs and charges have been taken) equivalent to the total return of their target return benchmarks, we consider the strategies to have achieved their targets.

Our financial market performance benchmarks

The performance of our investment strategies can also be compared to representative indices for two of the main asset types in which most of the strategies invest. These indices are 'MSCI United Kingdom (£) – net total return' (representing the performance of UK shares) and 'BoA Merrill Lynch UK Gilts' (representing the performance of conventional UK government bonds). These indices are known as the strategies' comparator benchmarks, and are designed to help clients evaluate the strategies' performance in a financial market context.

It is important to note that financial returns are not assured: there is no guarantee that the strategies' performance objectives will be met, or that a positive return will be delivered over any time period. When you invest, your capital is at risk.