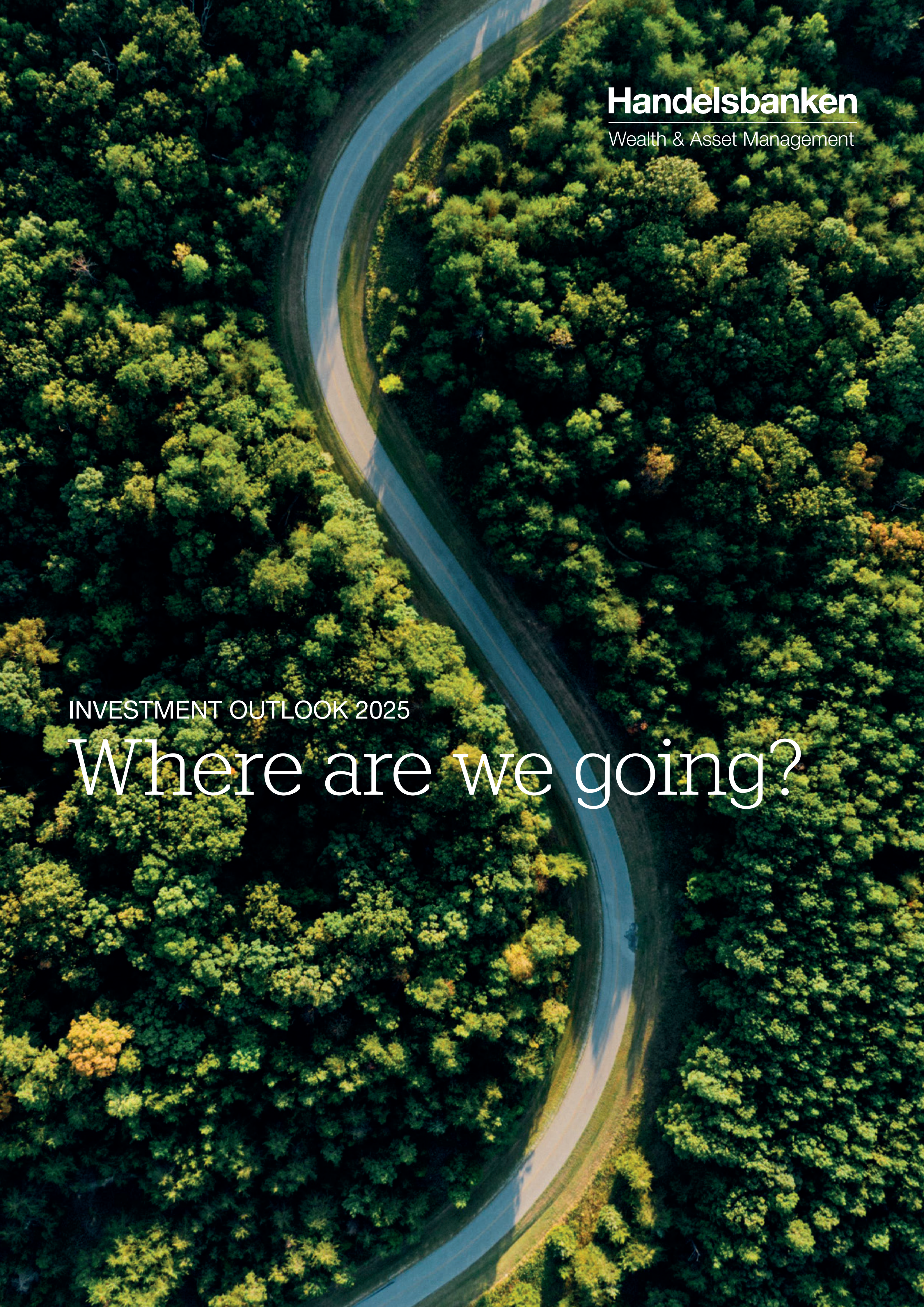


Handelsbanken
Wealth & Asset Management

INVESTMENT OUTLOOK 2025

Where are we going?

Contents

Welcome to the latest edition of our *Investment Outlook*

As we write, we're very pleased to say that our investment strategies have enjoyed an upbeat 2024. Is the economic resilience which appears to have developed in 2024 – particularly in the US – here to stay? In our first article, *In search of equilibrium*, we take a walk through our views on the global economy. We're mindful of potential banana skins for growth, inflation and interest rates, but also alert to the potential opportunities for investors.

Meanwhile, the reality of a second Trump presidency looms over 2025. In our second article, *When America sneezes…*, we chart Trump's return to power, and the true depth of his extraordinary victory. Perhaps more importantly for our readers, we consider the potential impact of Trump's views and policies on global trade, the world economy, and financial markets.

On home shores, politics have also been making a splash. In this edition of our *Investment Outlook*, a special short article on the UK Budget – *A word on UK finances and growth* – takes a closer look at the achievability of the new government's spending plan, and its likely economic impact.

In the later pages of this edition, we take a deeper dive into our investment strategies. *Translating our world views into your investments* outlines the important questions we need to ask ourselves when making decisions on how to invest your capital. We also give examples of the blend of asset types we use to serve different purposes, from capitalising on exciting opportunities to defending against market turbulence.

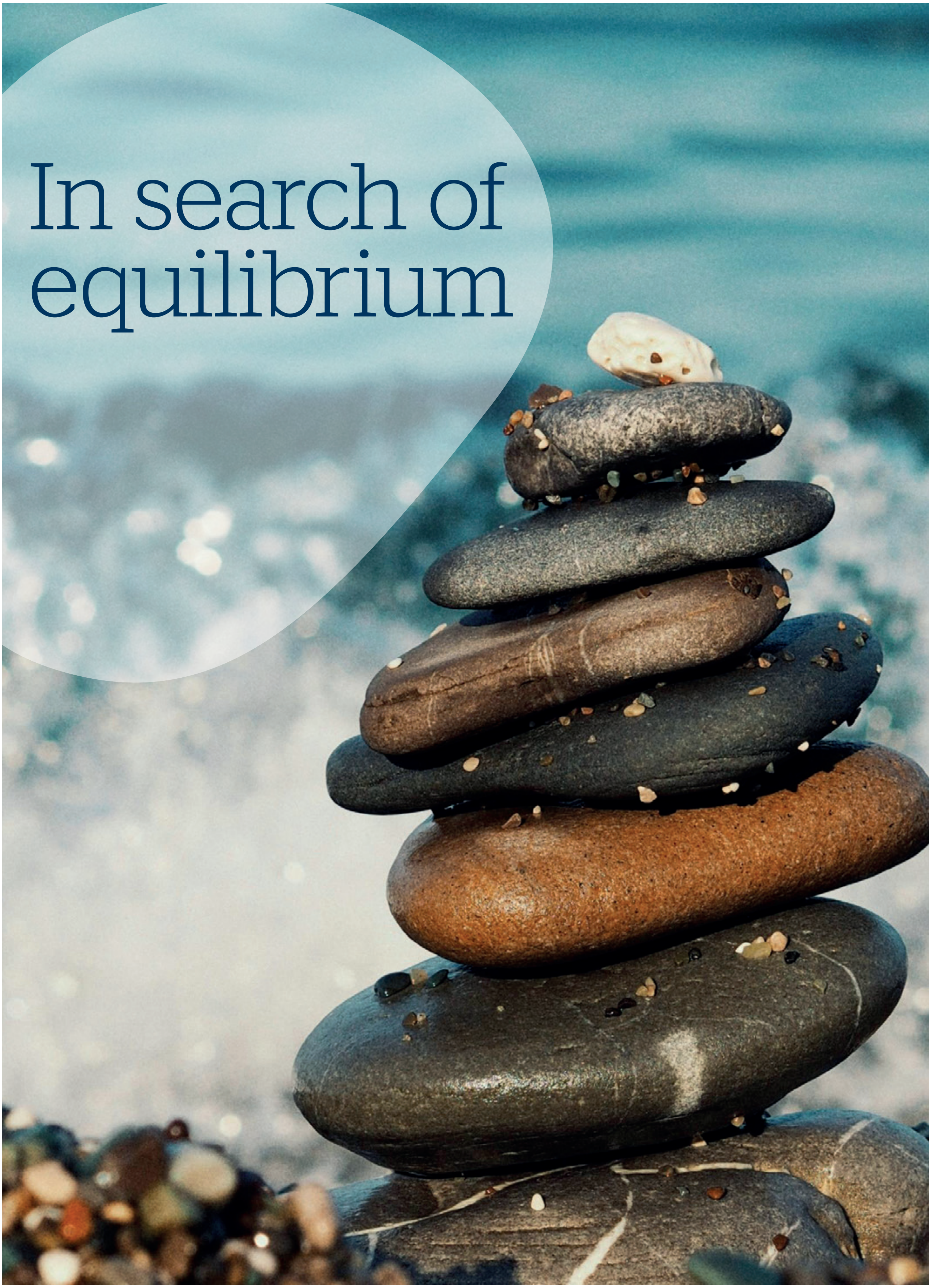
Finally, we recap the recent changes to our multi asset funds, which came into effect on 1 December 2024, and remind you of our long-term, global approach to investing, which has not changed. *From ideas to outcomes: mapping how we invest your money* is a journey through our investment process, from building up our central framework for investing, to populating our investment strategies with the assets we think offer the best chance of delivering returns to you over the long term. This article also features a special focus on 'passive' investing: the diverse and cost-effective financial products which have exploded in availability and popularity over the past two decades.

As always, we're keen to hear your feedback on this edition of our *Investment Outlook*. You can contact us with any thoughts or queries at marketing.hwam@handelsbanken.co.uk.

We wish you a safe and happy 2025, and look forward to keeping in touch.

Graham Bishop Chief Investment Officer

In search of equilibrium



The sharp rise in interest rates since the COVID-19 crisis has, against all odds, been insufficient to derail the global economy. Though some economies have experienced technical recessions over the last year or two, the long-feared 'cliff edge' simply didn't happen. This appears to speak volumes about the resilience of the global economy.

In fact, as 2024 unfolded there even appeared to be some green shoots appearing. Whether it was a bounce back in some consumer and business confidence indicators, or lenders' willingness to lend, the outlook appeared rosier. This opened up the possibility of shifting into the early phase of the business cycle, a good place to be. Is economic resilience here to stay?

Chief among the reasons for this economic resilience, particularly in the US, has been the ongoing boost provided by government economic support packages in recent history. As we look into 2025, President-elect Trump will surely maintain prior tax cuts, thus not causing a tax shock to the US consumer. So-called 'excess savings' (extra savings built up during the COVID-19 era) have also created a financial buffer for US consumers. Simply put, the effects of the myriad stimulus measures deployed during the pandemic have been greater than previously forecast, supporting economic health and consumer confidence for longer.

Watch out for bends in the road

As things stand today, the global economy continues to be subject to the lagged impact of central bank interest rates, but seems to be managing. Of course, there are still potential banana skins to deal with. At Handelsbanken Wealth & Asset Management, the Investment Team frequently frets about economic boosts turning into economic drags.

For example, limited headroom for government finances in the US may mean the President-elect tempers his tax cutting agenda, for fear of a stateside version of 2022's Truss/Kwarteng debacle in the UK. In addition, those excess US savings may have been underestimated in the recent past, but they can't last forever.

In fact, there are a great many shocks that can derail the status quo. Tariff increases, tensions in the Middle East broadening out to oil-producing nations, or government spending recklessness could all be harmful.

But what about the potential for positive surprises? Sensible government support measures, investment in artificial intelligence (AI) technologies spilling over into the wider economy, or moderate levels of borrowing for investment are all positives that could manifest themselves over the coming months.

Has the global economy found its way?

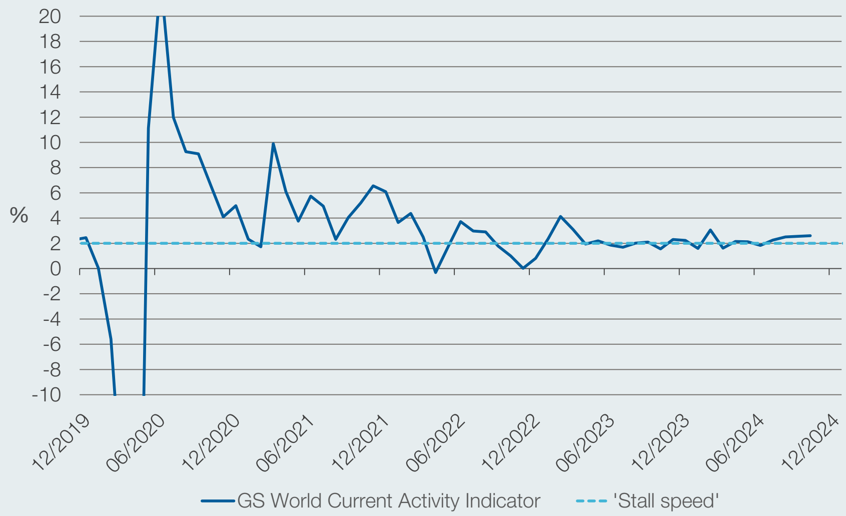
The view of many market participants is that the global economy has achieved a soft landing. By this, they mean a gentle return to equilibrium (between economic expansion and contraction), with minor disruption, rather than major booms and busts.

We have some sympathy with this view. The volatility of global economic growth has been falling over the past year, and growth is now generally hovering just above 2%, or what we describe as 'stall speed'. Though modest, and masking a great deal of country variations, it could be a lot worse. Calmer economic growth at a global level is surely one of the reasons behind a gently upbeat market tone in 2024.

Another positive feature of 2024 was the reduction in inflation. Somewhat driven by lower energy prices (although these have recently risen since the 'price cap' was removed), there has also been a certain normalcy returning to pricing behaviours. Fears about 'second round effects', when an initial inflation shock becomes engrained and self-reinforcing, thankfully have not materialised. (As a reminder, this does not mean that price levels have fallen, just that the rate of price increases has eased off.) The full impact of higher price levels may have not yet been felt, but falling inflation is a good start. For financial markets, the fact that inflation data (of which there is plenty) is also coming in below expectations is another positive factor.

Economic growth looks calmer, hovering just above 'stall speed'

GS World Current Activity Indicator



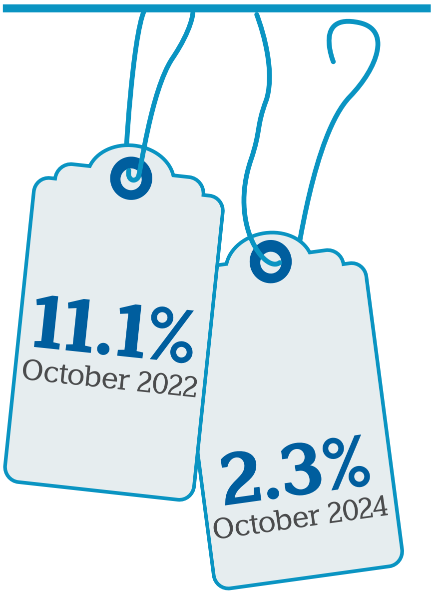
Source: Macrobond, Goldman Sachs

What are central banks looking out for?

Lower inflation is the main reason for central banks reducing interest rates throughout 2024. Interest rates have been coming down around the world, but there is further to go.

Besides inflation, the other key economic variable for central bank decision making is the labour market. A spate of data-related issues have plagued labour market statistics in the US, raising questions over the usefulness of these figures, and leading to close scrutiny. However, it certainly appears that growth in demand for labour in the US is declining by approximately 1% each year, whereas the growth in the supply of labour is still marginally positive. These numbers frequently disconnect, but demand being lower than supply doesn't normally bode well from an economic point of view.

It may be that the labour market situation unfolds so slowly that other issues overtake it. If not, though, then we would become more worried about the outlook for unemployment, consumption, and wider economic activity.



Some **normalcy** returns to **pricing pressures**

Annual inflation: UK Consumer Prices Index

Source: Office for National Statistics

What does this mean for markets?

Financial markets are taking the combination of relative calmness in economic growth, lower inflation and falling interest rates as a good thing. This is why 2024 was materially better for financial returns from most types of asset classes than 2022-2023. It can take markets time to absorb changes, and digestion phases are always unpleasant, but it appears this one is behind us.

The global economy moves in periodic stages in a cycle of expansion and contraction, and in many ways, the current and prospective situation resembles a 'late cycle' type of environment. This is typically not a bad phase for riskier asset types like shares. But complacency is dangerous.

What does this mean for your investments?

Our view of the inflation outlook supports the interest rate cuts being made by most central banks. A shock to economic growth is not impossible, which is reflected in our bond positioning. We've recently slightly lowered our overall allocation to bond markets, and we prefer UK to US debt, as a result of the factors being accounted for in the yields of these bonds. With credit spreads (differences in bond yields) currently quite narrow, we prefer higher quality 'investment grade' bonds to higher yielding, lower quality bonds.

When it comes to stock markets, we are mindful of the lagged impact of past central bank interest rate cuts (which can take many months to appear in the real economy), as well as potential Trump tariffs and geopolitical escalation. These threats are live at a time when global economic growth is stable but anaemic. We therefore have an 'overweight' stance when it comes to shares, meaning that our overall stock market holdings are slightly higher than our long-term average positions.

We currently prefer shares in developed (rather than developing) economies. We've also been deliberately neutral when it comes to the 'Magnificent 7' (Nvidia, Tesla, Apple, Microsoft, Alphabet, Amazon and Meta), but due to their prominence in the US stock market, a neutral stance means that they are represented accordingly in our investment strategies. We will continue that stance near term. The factors contributing to the underlying worth of these behemoths (their 'fundamentals') are better than equivalent technology stocks around the 'dotcom bubble' of the late 1990s. Nevertheless, things rarely move in straight lines, so we are alert to bumps in the road.

Overall we feel that our investment strategies are robust given our exposures to a wide variety of asset types. You can find out more about this in our article *Translating our world views into your investments*, later in this report.

“When it comes to stock markets, we are mindful of the lagged impact of past central bank interest rate cuts (which can take many months to appear in the real economy), as well as potential Trump tariffs and geopolitical escalation.”

Graham Bishop Chief Investment Officer

When America sneezes…

… the world catches a cold, or so the old adage goes. The US has the most influential economy and stock market in the world, meaning that whatever happens there can – and does – affect others around the globe. As we enter into a new Trump presidency, should international investors worry about the ripple effects of his second term in the White House?

Since 2022, a remarkable 35 noteworthy elections have been held around the world. In 70% of these elections, incumbents have either lost some of their seats, or lost the election entirely. There is a common thread running through these losses: inflation at multi-decade highs, and its impact on consumers. Whatever the complex root causes of this inflation, voters evidently believe that it's the incumbents who should pay the price.

In the UK, this has meant a swing towards the left of the political spectrum, with the Conservative Party evicted from Downing Street after 14 years, and Labour ushered in. In some European countries, incumbents have been swept aside in favour of right-wing candidates. In the US, Vice President Harris (officially the incumbent, having been elected on a joint ticket with President Biden) has also been rejected. But why did Harris lose out?

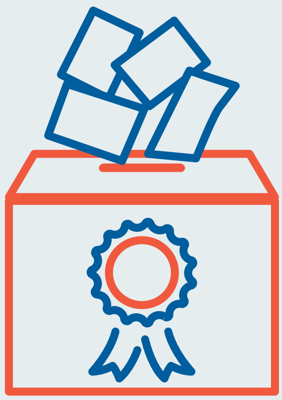
It wasn't the economy, stupid

The near-apocryphal line "it's the economy, stupid" is attributed to one of the campaign managers behind Bill Clinton's successful 1992 presidential bid. As a general (if slightly imperfect) rule of thumb, if you can keep the US economy in the green, you'll be re-elected to the White House next time. But for Harris, this wasn't enough.

On this side of the Atlantic Ocean, European nations like Germany and the UK suffered a technical recession (two consecutive quarters of negative economic growth) as a result of the global inflation storm. But the US economy held up remarkably well compared to its international peers. In particular, despite occasional signs of strain, US labour markets have held fairly steady, and US unemployment is currently at its lowest level since the 1960s.

But while the US economy has generally fared surprisingly well, people still felt worse off in the US thanks to higher inflation (three quarters of US voters said they believed inflation created hardship for them). What's more, beneath the headline of positive US economic growth, the US manufacturing sector was hit by recession. The states hurt the most by this – the Midwest – voted in their droves for Trump.

Since 2022, a remarkable **35** noteworthy **elections** have been **held** around the **world**



Trump didn't just win, he won big

The Harris versus Trump betting odds were always relatively tight, but – unlike in 2016 – Trump's victory was not a shock result. What did come as a surprise, though, was the sheer magnitude of his win.

What did Trump win?

- 51% of the popular vote – very unusual for a Republican candidate
- The highest number of electoral votes for a second (but not consecutive) term president since 1892
- 54% of voters without a college education
- 52% of white women voters
- 45% of the Latino vote (up from 13% in 2020), and much more of the African American vote than last time
- Not only the 'sunny states', but also the 'blue [Democrat] wall', rust-belt states like Pennsylvania, Michigan and Wisconsin

Trump's victory vindicated his strategy of 'economic nationalism' – appealing to the working class with promises of an industrial revival, and a general emphasis on the economy.

For some, this election was also a choice between strong rule (the fiery Trump) or rule by committee (the uninspiring and rather last-minute Democratic nominee, Harris). The result implies a vote for a leader who is – rightly or wrongly – unafraid to create change.

What will Trump do?

The world is a vastly different place to when Trump first took office in 2016. Back then, inflation was below its 2% target, interest rates were 0.5%, and the US national deficit was 40% lower than it is today. The cost of servicing (paying the interest on) that national debt was $400bn a year for President Trump 1.0; for President Trump 2.0, it will be more than $1 trillion.

But some things remain the same. An economic ideology of deregulation, international trade policy (via tariffs), and lower personal and corporate tax rates is set to be consistent with Trump's first presidency. The difference this time around is that his Republican Party has control of both the lower (House of Representatives) and upper (Senate) houses of Congress. In theory, he has a better chance of enacting his agenda without opposition.

Without opposition, any checks and balances on President Trump 2.0's behaviour could come from financial markets – specifically the bond market. If the cost of capital (i.e. the cost of issuing and servicing debt/bonds) rises too high, the economy and markets will suffer – this is not what Trump wants.

What does this mean for the economy?

Trump will be focused on economic growth, so it's reasonable to expect so-called US exceptionalism to continue. Tax cuts and lower regulation are very much on the table. The US economy does not need turbocharging, but that's exactly what Trump is planning to do.

Will this growth roll out to the rest of the world? It's hard to say. While a healthy US economy is broadly a good thing for the global economy, Trump's approach to trade (and tariffs) creates plenty of question marks. His upcoming return to the White House also comes with serious geopolitical risks, least not for Ukraine.

What does this mean for our market views?

Trump's second bite of the cherry doesn't drastically alter our global views, but his potential to influence US economic growth – and by extension inflation and interest rates – is meaningful. Below, we outline the areas where we see the biggest potential for impact:

Stock markets

- We expect 'US exceptionalism' to continue, with the US stock market still leading the way versus its global peers (despite cheaper share prices elsewhere).
- Tax cuts and deregulation will be welcomed with open arms by US companies, while export businesses outside the US are already holding their breath for tariffs. Expect these factors to continue to show up in share prices.
- Large businesses could buy back more of their shares from investors (as they did in Trump's first presidency).
- Smaller companies could face more risks, as the potential for inflation to rise again could lead to higher interest rates (and therefore higher bond yields/cost of capital) than would have been the case under Harris.
- If higher interest rates do emerge, economic growth and consumer demand could slow, presenting some risks to company earnings and therefore to share prices.

Bonds

- The inflation risk caused by tariffs on incoming international goods could lead to a return to higher interest rates, with knock-on effects for bond yields.
- This, alongside a potentially overstimulated US economy, makes us a little more wary of long-term US government bonds.

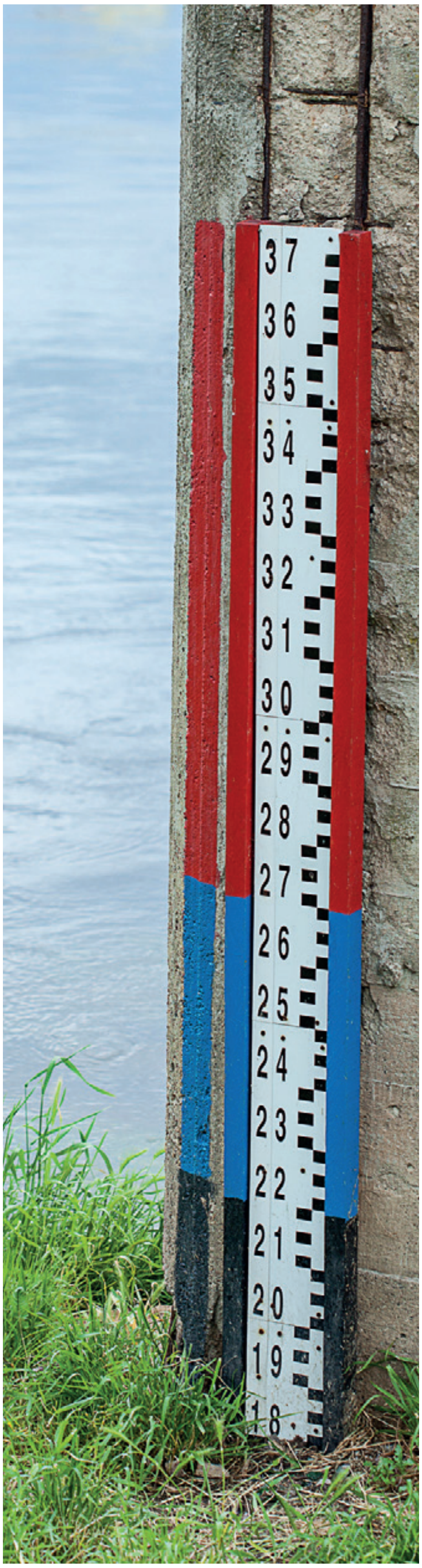
Gold

- The gold price tends to rise (although it's not entirely dependable) in times of heightened geopolitical risk, as we're likely to see under President Trump 2.0.
- However, this could be a volatile journey, given gold's typical sensitivity to interest rates.
- We think gold is a good place to park some capital, but are braced for a bumpy ride over the short-term.

"Will this growth roll out to the rest of the world? It's hard to say. While a healthy US economy is broadly a good thing for the global economy, Trump's approach to trade (and tariffs) creates plenty of question marks."

David Absolon Investment Director

A word on UK finances and growth



Pre-Budget leaks of a £22 billion 'black hole' in public finances ensured that Labour's first Autumn Budget for 14 years was met with considerable interest, even if many of its key points were already in the public domain.

Promoted as a 'Budget for growth', the Chancellor announced record increases in spending of £70 billion annually: two-thirds directed to public services, with the remainder on investment (including in roads and transport). Just over half of this additional expenditure will be funded by tax increases, with £28 billion coming from additional borrowing.

A two-part plan... but is it achievable?

To help balance the budget and reduce net financial liabilities, the Treasury has devised a two-part government finances framework comprising:

1. A stability framework, with the commitment to create a budget surplus by the end of this decade and subsequently on a three-year rolling basis.
2. An investment framework, targeting a reduction in debt-to-GDP by 2029/30. In addition, the Chancellor is broadening the government's definition of debt to include public sector net financial liabilities, which will include assets for the government to invest in, consequently providing more headroom for government finances. This should allow for record spending on public services and investment, while not breaking election pledges to raise the threshold on personal or corporation tax.

The independent oversight body, the Office for Budget Responsibility (OBR), noted in a follow-up assessment that the Chancellor can meet both her targets, but by "small margins". The Chancellor stated there would be no need for further tax increases or additional borrowing, but at a time when the UK economic growth outlook is already low and possibly subject (along with its peers) to a more strident trade policy in the US following Trump's election, some analysts are already downgrading growth prospects due to potential trade tensions.

The economic impact: the jury's out

The OBR believes the Budget will contribute to an annual rise in economic growth in 2024 from 0.8% to 1.1% and in 2025 from 1.8% to 2%. Others (including ourselves) are less sure. The increase in employers' National Insurance Contributions could easily make employers less keen to hire workers in an already weakening labour market. Meanwhile, rises in capital gains and carried interest taxes, as well as changes to the Non-UK Domiciled tax status could disincentivise investment when the returns profile is likely to be lower. Households juggling with the much higher price of goods in shops and heightened geopolitical tensions may also act to hold back household consumption.

Investor reaction to the Budget was relatively subdued – a victory of sorts for the incoming government, with memories of the 'Liz Truss' moment of two years ago still relatively fresh. However, the longer-term consequences may prove less benign.

> "The increase in employers' National Insurance Contributions could easily make employers less keen to hire workers in an already weakening labour market."

Scott Ingham Investment Director

Translating our world views into your investments

Throughout this Investment Outlook, we're outlining our 'house views' – detailing how we see the world and financial markets. But how does this translate into the assets we choose to invest in on behalf of our customers?

When we populate our investment strategies with specific holdings, like government bonds or positions in stock markets, we're balancing a whole host of potential options. Beyond simply deciding which broad asset types – bonds, shares, or 'alternative' assets – to invest in, we must be very specific about the areas of financial markets we're targeting.

Plenty to think about...

Let's say you're thinking of investing in the US stock market. Will you choose large companies, or smaller businesses? Their share prices will react very differently to changes in the political and economic landscape.

Will you go for a growth-oriented company, which reinvests its earnings back into the business, or an income-payer, which pays out its earnings to shareholders? Reinvestment creates better potential for growth (and future higher share prices), but you won't be paid while you wait. Meanwhile, shareholder dividends are money in your pocket, and suggest good corporate financial health, but the business is not necessarily prioritising future growth.

Do you want to target any specific sectors – perhaps technology, or energy, or healthcare? How are these industries likely to respond to the new Trump presidency, and the coming economic environment?

Before you can even come close to investing, you probably need to think about many other factors – from the share's market valuation to your confidence in the manager of the investment you're considering.

These are just a few of the considerations that come into play when we're thinking about how to invest. What's more, these examples refer to just one market (the US), just one type of asset (shares), and just a couple of factors (company size and growth/income potential).

What do we look for in our investment choices?

Building a portfolio made up of a range of different assets means making sure everything works together. In our strategies, you'll find assets that are designed to perform when the market's risk appetite is high, as well as assets that are more likely to shine in defensive environments.

Let's take a look at some examples…

Big hitters: go carefully, but don't miss out

In the summer of 2024, our Mid-Year Investment Outlook took a closer look at the so-called 'Magnificent Seven' – a collection of ultra-large US businesses dominating stock market performance: ecommerce titan Amazon, electric vehicle manufacturer Tesla, communications powerhouses Meta (Facebook) and Alphabet (Google), and technology giants Microsoft, Apple and Nvidia. At the time of writing, these seven businesses have accounted for around 44% of returns in the US stock market in 2024.

The Magnificent Seven are prominent in our investment strategies as a result of our US stock market and technology sector positions. Their performance has been bolstered by the market response to news of their strong company earnings. Compare this to the rest of the market, where earnings have been stagnant for the last two years.

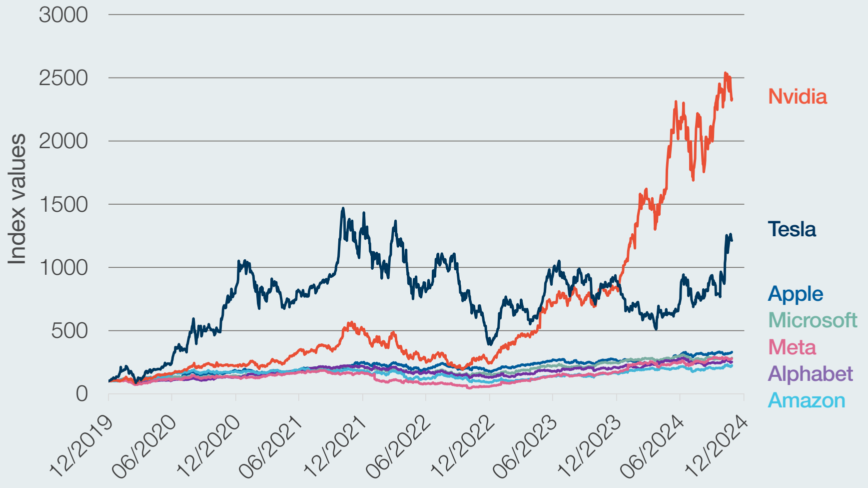
The Magnificent Seven companies are at the forefront of technological advances, and adapting to shifts in consumer behaviour, specialising in sectors such as artificial intelligence, electric vehicles, cloud computing and digital services. These are businesses with a consistent record in developing new products and services that drive consumer demand and business growth. All have had strong financial health, enabling them to continue to invest in research and development.

Will their appeal amongst investors continue? With global economic growth perhaps on the brink of easing off, investors could look to the behemoths of the US stock market for stability and reassurance. Historically, when economic growth moderates, investors have preferred to be in areas where they can still see growth coming through.

But history is a very unreliable guide, and the share prices of these businesses – in particular Nvidia – have risen astronomically in recent history. Can this go on indefinitely? Share prices among the Magnificent Seven have been very volatile at times. Without the benefit of hindsight, it's not been a journey for the faint of heart. As ever, we believe balance is necessary.

The 'Magnificent Seven'… but Tesla and Nvidia stand out

Performance of the leading stocks on the US stock market



Source: Macrobond. Rebase 31/12/2019=100.

On the defensive: looking for cover

Our investment strategies also contain assets designed to play a defensive role. As you might expect, this includes areas like government bonds, which we added to in the wake of the COVID-19 crisis, particularly in the UK. We reduced our bond positions slightly in late 2024, but are being paid to wait (via coupon/interest payments) on those bonds that we've chosen to hold.

Returning to our stock market positions, our holdings in certain sectors can also make our investment strategies more defensive. We've been invested in areas like insurance and healthcare, which have demonstrated some attractive defensive properties.

The insurance sector has been a beneficiary of rising bond yields, and very good insurance underwriting standards have also contributed to good growth. Our global healthcare investments also have defensive properties, thanks to strong company finances, cash-generative business models, and subsequent mergers and acquisitions in the sector, as well as innovation in pharmaceutical drugs.

As with all investments, we need to keep a close eye on thematic investments like insurance and healthcare, to ensure that their share price valuations remain reasonable relative to our expectations. We also need to ensure that all positions in our investment strategies continue to align with our outlook for economic growth, central bank decisions on interest rates, and the outlook for inflation.

Getting creative: beyond bonds and shares

The investment universe beyond traditional bond and stock markets is huge, ranging from basic commodities to complex investment products.

> "Building a portfolio made up of different assets means making sure everything works together… when the market's risk appetite is high, and in more defensive environments."

Jaisal Pastakia Investment Director

Here are just three examples at work in some of our investment strategies:

Puts: allowing investors to hedge their bets

- Financial securities which can be bought and sold in the marketplace, and give the holder the right (but not the obligation) to sell certain assets at a pre-specified price
- Enable investors to 'hedge their bets' – investing in the stock market, but protecting against large market falls
- The value of 'puts' can rise and fall. Purchased for an upfront cost (which is the only outlay) allowing good visibility of maximum financial loss

Gold: an historical store of value

- Traded for over six millennia, gold is a traditional investor 'safe haven' in times of political or market turbulence
- Does not provide an income stream (through earnings/dividends), but remains one of the world's oldest stores of value
- Despite its reputation, gold doesn't always do well in times of strife, but the gold price has certainly risen strongly throughout 2024

Tail risk protection: protecting in the worst of times

- Another insurance-like product, which pays out in times of high market stress
- A highly specialist strategy, which (as professional investors) we are able to access on behalf of our customers
- Protects against dramatic market falls only, not against smaller bouts of volatility

Gold: a port in a storm for worried investors

Price ($) for one troy ounce of gold

Source: Macrobond, Bloomberg

The road ahead…

We keep a close eye on the global economic cycle and the investment landscape, and make sure our investment strategies are positioned (and – when appropriate – repositioned) accordingly.

Things can change very quickly, with the market mood shifting at lightning speed. It can be tricky to resist the urge to chase after every exciting opportunity that comes along, but our advice is generally to think long-term and invest with conviction.

Timing is also essential: spotting a forthcoming crisis or opportunity is laudable, but anticipating the sequencing and pacing of market and economic events is notoriously difficult. There is a balance to be struck between opportunism and caution.

It sounds obvious, but our approach to choosing investments is all about trying to give our strategies the best chance of performing well, in exchange for taking on a given level of carefully managed risk.

From ideas to outcomes: mapping how we invest your money

As we write, we're very happy to say that our investment strategies have enjoyed an upbeat 2024, so far. The way ahead for the global economy (and financial markets) is far from clear, but we feel optimistic about how we've positioned our investment strategies for the future.

As we head into 2025, it seems like the perfect time to revisit some of the recent changes we've made to our funds, and to recap our approach to investing, which hasn't changed.

What have we changed?

We recently made some changes to our multi asset funds. This included removing their previous inflation-based target benchmarks, in effect from 1 December 2024.

This change reflects the limitations of using inflation as a performance target. Inflation is measured using the Consumer Price Index, which is not an investible benchmark. This means that it does not contain investments that can be purchased in the market, or easily replicated by investors. As a result, it is not an ideal reference for assessing the performance (over different timeframes) of the investments we hold in our multi asset funds.

What prompted this change?

The limitations of using inflation-linked targets were highlighted during 2022 and 2023, when inflation rose sharply, reaching multi-decade highs in response to a potent cocktail of factors, least not supply and demand distortions caused by the COVID-19 crisis. Very few assets were able to keep pace with inflation and provide investors with a 'real' return (i.e. positive financial returns after accounting for inflation). In more recent history, this disparity between inflation and asset performance has levelled off, with pricing pressures stabilising – albeit at higher levels than those we'd grown used to before the pandemic crisis. Nevertheless, recent history has highlighted the shortcomings of using an inflation-linked target for our funds, leading us to review this.

We are now introducing market-linked 'composite' comparator benchmarks to help our customers compare fund performance with the performance of real financial assets. In future, our funds' performance will be compared against these composite benchmarks. These changes should provide our customers with a more accurate way to understand how our investments are performing.

If you're a Handelsbanken Wealth & Asset Management customer who'd like to know more about this, or have any other queries about our funds, you can contact your Client Director or our **Client Support Team** clientsupport.hwam@handelsbanken.co.uk.

Is our approach to investing changing?

While we may be moving on from our former inflation-linked target benchmarks, the way we approach investing is not changing.

Nevertheless, we're always looking for ways to manage our customers' investments more cost-effectively, with a keen eye on the balance between risks and potential financial rewards. With this in mind, we think this is a good time to recap our wider approach…

There are four key components to our approach:

1. Building a central framework

First, we build (and regularly review) our central position, which we call our Strategic Asset Allocation. This is a way of building frameworks for our investment funds, built of a mix of the types of assets available to us. You can think of it like a central – or 'neutral' – version of an investment portfolio, which we can use as a reference point for managing our customers' money, and for monitoring the risks taken on by investing.

Indeed, this central framework provides us with a good way of considering and comparing the levels of risk at work across our different investment funds. 'Neutral' positioning for our higher-risk funds naturally includes a greater proportion of riskier asset types, like shares, while 'neutral' positioning for our lower risk funds means allocating a greater portion of investments to typically lower-risk assets like developed world government bonds.

2. Reacting to (and preparing for) change

Second, we make considered choices to deviate from these central positions, responding to events and expectations in the economic, geopolitical and financial market environment. We call this our Tactical Asset Allocation.

For example, our expectations for changes to interest rates could cause us to allocate more (or less) of our customers' capital to government bond markets. Alternatively, our expectations for growth in the very largest US companies (the so-called 'Magnificent Seven') could influence how much exposure we think our funds should have to the technology sector (where many of this leading group are situated) or to the US stock market (which these businesses dominate).

When we invest more in a given type of asset than our central – or 'neutral' – position, we are 'overweight' this asset type. If we invest less, we are 'underweight'. By making overweight and underweight decisions, we are expressing our highest conviction views about investments. We regularly revisit these views, and move between overweight, underweight, and neutral in keeping with our latest thinking.

3. Selecting investment assets accordingly

Thirdly, with these views and our central framework in mind, we choose the specific assets which will populate our investment funds. This is known as 'security selection'.

In recent years, this has evolved more than any other area of our process, as we move to simplify the assets we hold on our customers' behalf, and keep costs low. A huge influence on this change has been the explosion in 'passive' investment options over the past two decades. You can read more about passive investing on the next page.

There are also other ways for us to keep costs down, without compromising on our convictions. For example, we can buy individual government bonds directly, which not only allows us to express our views more accurately, but also keeps costs low – we don't need to pay a third-party manager, and our trading costs are efficient.

4. Continuously managing risks

Finally, and running throughout our investment process, we actively manage the risk levels at work in our investment funds. It's worth noting that absolutely no investment (including just holding your wealth in cash) comes without some form of risk. However, we can certainly seek to manage, understand and monitor the levels of risk we take on, and we place risk controls at every stage of our process.

Our central positioning (Strategic Asset Allocation) allows us to ensure we have taken on the right level of risk in each of our different investment funds, relative to one another and to the wider market. Our deliberate deviations from these positions (our Tactical Asset Allocation) are balanced to ensure that any additional risk-taking remains reflective of our highest conviction views. Our selection of specific assets to populate our funds (security selection) includes challenges from opposing viewpoints, close monitoring of performance, and regular points of review within our experienced investment team.

Spotlight on 'passive' investing

What are passive investments?

Passive investments are designed to track, or mirror, the performance of a given financial market, area of the market, or set of financial instruments. By investing passively, an investor can experience the performance of a market, or theme, or set of assets, without directly holding these assets outright.

Are passive investments cheap?

Passive investments are often cheaper than 'active' investments, which rely on manager skill to select which assets the managers believe have the best potential to perform. 'Passives' cut down on their costs by not relying on third party manager skill, and – since buying a passive investment strategy is not the same as owning the underlying assets – they do not incur the same type of transaction costs through buying and selling assets. In this way, passive investments can allow asset managers (like us) to access the markets, themes and ideas we like, at a lower cost.

What are ETFs?

You might have heard the term 'ETF' (exchange traded fund) or seen it written in your investment reports. ETFs are an extremely popular form of passive investing. They are a 21st century phenomenon, with the first ETFs launching in the early years of the new millennium. Since then, their popularity has skyrocketed. Since infancy, they've been very popular with large institutional investors (like pension funds), who have valued their low-cost approach and their potential for wide-reaching diversification.

> "Passive investments require careful selection, with strong due diligence, an understanding of the risks involved, and – if you're investing in more than one passive instrument – awareness of the level of diversification/duplication at work in the products you're using."

Graham Bishop Chief Investment Officer

Number of **ETFs** globally

2003: 276

2023: 10,319

Source: Statista

Are all passives the same?

The term 'passives' covers an enormous range of investment products. These include:

- **Index passives:** track the performance of a financial market index. This could be an index which represents the global stock market, such as the MSCI World Index, or a regional stock market, such as the FTSE100 in the UK or EURO STOXX 50 in the euro zone. It could also be an index tracking the performance of an area of bond markets, such as corporate debt in developing economies.
- **Thematic passives:** track the market performance of assets which fall into a specific group or theme, such as sustainable infrastructure.
- **Sector passives:** track the market performance of assets within a certain industry or sector, such as insurance, healthcare or information technology.

Investing in passives which target specific segments of financial markets can offer a comparatively cheap way for investors to express their convictions and preferences in these areas.

However, despite their seemingly unbiased nature, passive investments require careful selection, with strong due diligence, an understanding of the risks involved, and – if you're investing in more than one passive instrument – awareness of the level of diversification/duplication at work in the products you're using. It also helps if you have the scale and status to negotiate cost-effective fees with the providers of passive products.

Are passive investments risky?

No investments are risk-free, and 'passives' are no exception. Different passive investments are exposed to very different levels and types of risks, but it's especially worth highlighting how volatile the performance of ETFs can be. For example, if an ETF tracks the US stock market by mimicking the performance of the S&P 500 Index, its own performance will move up and down in line with that index. So if the S&P 500 Index falls by 50%, the ETF will fall by 50% too. Of course, the opposite is also true: when the S&P 500 performs very positively, so will the ETF which tracks it. It's important to be aware of this potential for volatility – and its impact on your investment journey over time – when opting for a passive investment product.

Does my investment with you contain passive investments?

Our approach to investing very much includes passive investments. The explosion of ETFs over the past two decades has created a huge pool of available and relatively low-cost investment options. When it comes to populating our multi asset investment funds, we will only opt for an 'actively-managed' product (reliant on manager skill) over a passive product if we believe it brings something genuinely worthwhile to the wider fund. We want to keep costs low, so the bar to entry for active products is now set high. This is particularly relevant for our fixed income (bond market) positions, where ETFs have transformed the way we can access certain areas, such as bonds in developing economies.

Investment team

Graham Bishop
Chief Investment Officer

David Absolon
Investment Director

Scott Ingham
Investment Director

Ben Matthews
Investment Director

Jaisal Pastakia
Investment Director

Tom Griffin
Investment Manager

Nikki Howes
Investment Manager

Robert White
Investment Manager

Andrew Bovell
Investment Performance
& Risk Manager

Caroline Von Celsing
Investment Associate

Awards

2024 PAM NextGen Leader

Emma Savory, Associate Client Director – Private Office Team Leader

2023 MoneyAge Awards

Winner: Wealth Management Firm of the Year

2023 WealthBriefing European Awards

Winner: Marketing & PR Campaign

2022 WealthBriefing European Awards

Winner: Specialist Wealth Manager with assets under management between £2-5 Billion

The Asset Management Awards 2022

Winner: Multi Asset Manager of the Year award

2022 PAM Top 40 Under 40

Jaisal Pastakia, Investment Director

2022 Citywire Thirty Under Thirty

Nikki Howes, Investment Manager

To find out more please get in touch:

marketing.hwam@handelsbanken.co.uk

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- Understand more about the language and terminology used in the financial services industry and our own publications through our Glossary of Terms: https://wealthandasset.handelsbanken.co.uk/glossary-of-terms/

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wealthandasset.handelsbanken.co.uk