Handelsbanken
Wealth & Asset Management

Investment Outlook 2023

Contents

Welcome to our Investment Outlook

Suffice to say that 2022 has been a memorable year, though many of us would ideally choose to forget its more tempestuous chapters.

Amid a cacophony of surprises and unwelcome guests, inflation has narrowly stolen the show. Much of the year has been characterised by central banks scrambling to control mounting pricing pressures, and we leave 2022 with interest rates far higher than where we began. We are global investors, meaning that the most important central bank for us to watch is not the Bank of England, but the US Federal Reserve Bank (the Fed), which has led the way with interest rate rises. In our first article – *The war on inflation: a fair fight, or a losing battle?* – we consider the response of central bankers to credibility issues, inflation, and the growth conundrum.

There's no doubt whatsoever that 2022 presented many extreme challenges, from cost of living crises to all out military warfare, and financial markets have not been spared. Our second article – *Few places to hide in 2022… but 2023 could be different* – revisits a volatile year for investors, and considers what the future could hold.

Amid such turbulent markets, bond prices have been especially hard hit. Arguably the most uninteresting area of mainstream markets for quite some time, 2022 changed the game for bonds. Our third article – *How bond markets escaped the naughty step* – takes a closer look at the changing dynamics at work for bonds, and outlines their newly promising status in an investment strategy of different asset types.

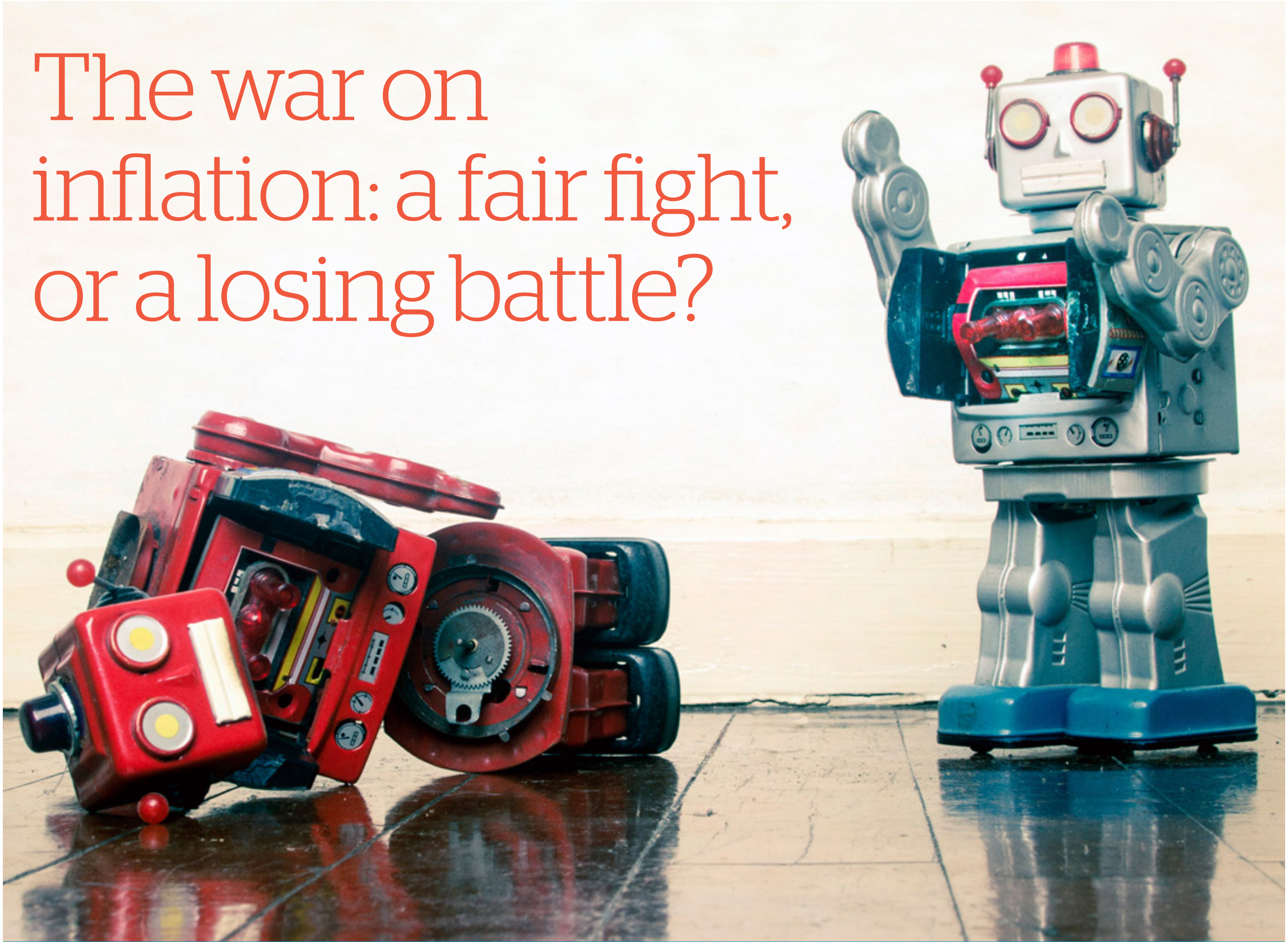
High conviction investment decisions, and diversity among the assets in which we invest, is fundamentally important to us. In our fourth article – *Is China turning a corner?* – we take a look at just one of the areas at work in our investment strategies: Chinese financial assets. Revisiting China's storied past, and charting its journey to a modern-day superpower, we explore the economic outlook for an ambitious authoritarian state, and the investment potential of a volatile area of financial markets.

Our final article, *Making your investments work harder*, illustrates some of the latest developments in sustainable investing, and provides some highlights from our most recent Sustainable Impact Report. Designed to demonstrate how we put capital to work sustainably in our sustainable multi asset funds, the report showcases a range of our investments and their tangible, real-world impact. It also provides independent ratings and analysis for our own funds, across a range of sustainability criteria.

We look forward to your feedback, and wish you a peaceful and prosperous 2023.

Graham Bishop Chief Investment Officer

The war on inflation: a fair fight, or a losing battle?



Central banks across developed economies have faced a vivid credibility issue in 2022: control inflation, or face a widespread loss of faith. How much longer will the fight go on, and are they winning?

The US central bank is leading the charge, with the UK hot on its heels

Like the US economy, the US central bank – the Federal Reserve Bank (Fed) – sets the tone for its developed world peers. Over the course of 2022, US interest rates have gone from 0.25% to 4.5%, at the time of writing (mid- December).

The Fed is now on a clearly marked path, and one which has been well-signalled. In August, Fed Chair Jerome Powell made a forceful speech outlining the Fed's total focus on bringing down inflation by slowing economic activity. In doing so, he acknowledged that efforts to control inflation (most notably by raising interest rates) would cause short-term pain to households and businesses, but declared that "a failure to restore price stability would mean far greater pain."

This rhetoric has been likened to an infamous speech made by Mario Draghi (then President of the European Central Bank) a decade earlier. In the summer of 2012, Draghi said that he would do "whatever it takes" to save the euro area. For Powell and inflation, it's not so much a case of 'whatever it takes' as 'whatever it costs'. And what it costs, it seems, will be some US economic growth.

On home shores, the Bank of England has been on a similar path. The Bank's policymakers have been forced to choose between raising rates to bring inflation under control (and doing so in a deteriorating economic environment) and supporting struggling consumers. To date they have prioritised the former, taking interest rates to 3.5%, at the time of writing.

Interest rates have shot up in 2022

Benchmark central bank rates in the US, UK and Europe

US	UK	Europe
31/12/21	31/12/21	30/12/21
0.25%	**0.10%**	**-0.50%**
31/12/22	31/12/22	31/12/22
4.50%	**3.50%**	**2.00%**

Source: Bloomberg

How high will interest rates go?

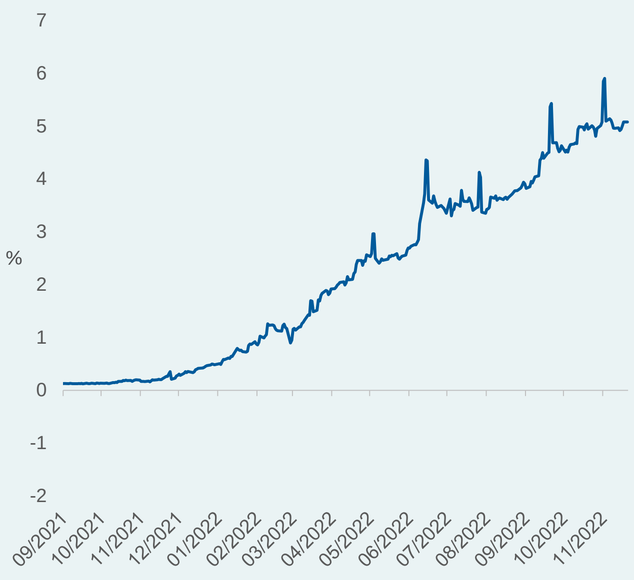
Until relatively recently, financial markets had anticipated a pause in interest rate hikes from the Fed early next year, and possibly even a rate cut during the first half of 2023. This is no longer the case. While headline US inflation has shown signs of peaking and core inflation (which excludes items with volatile prices like energy and food) came in lower than expected in October, the more persistent component of inflation like wages and shelter (rental costs) are still rising. Inflation may be turning in the right direction, but the war is not over yet.

Markets now expect the Fed to continue raising rates until they reach around 5% in the first half of 2023. In the UK, market expectations for the Bank are to reach a peak of around 4.5%, once again in the first half of 2023.

Ultimately the question of how high interest rates will go and how long they rest there will be determined by the path of inflation over the next twelve months. It's the world worst kept secret that inflation will fall from its 2022 highs, but the important questions are how quickly it will fall and where it will settle.

2022 saw investor expectations for the future of US interest rates increase rapidly

Market predictions over time for the benchmark US 'Fed Funds' rate by May 2023



Source: Bloomberg

What will happen to inflation?

Only time will tell how effective central bank aggression will be in bringing demand and supply back into balance in the global economy (without causing too much pain). Commodity prices will also be dictated by ever-present geopolitics. That's the short-term conundrum. In the medium term, we believe the developed world will have to adapt to a higher inflation regime than we have grown used to over the past 20 years, with inflation likely between 2% and 4%.

The deflationary forces of globalisation (particularly since 2002 when China joined the World Trade Organisation) and plentiful supply of cheap energy are fading. A trend of diversifying away from China-based supply chains has accelerated in a post-COVID-19 world, and while the journey to cleaner energy will be hugely beneficial in the longer term, it will be inflationary in the short term as the required infrastructure is built.

Central banks have told us their plan of attack

This year, central banks have been on a journey of higher interest rates in a pattern unseen since the 1980s. Policymakers in most developed economies are following a similar roadmap: not only increasing interest rates, but also removing support in other forms (e.g. bond purchase programmes are being reduced or allowed to expire without replacement).

Central banks know the economic pain this will cause in the near term, but are wholly fixated on bringing down inflation. Much of the heavy lifting in terms of rate rises has been done in 2022, but with a bit more likely to come in the first half of 2023. Whether rates are paused, cut or hiked again from that point will be determined, as mentioned above, by the economic data and inflation over the next 12 months. We will be keeping a particularly keen eye on increases to the unemployment rate as central banks pursue their goal of bringing demand and supply back into a healthier balance.

> "So far, we think that bond markets – which are notoriously sensitive to interest rate changes – are pricing in central bank action more aggressively than stock markets, resulting in a very challenging period of performance for bond prices."
>
> **David Absolon** Investment Director

What does all this mean for our investment strategies?

While past performance is never a reliable guide to future results, financial markets typically react very quickly to perceived danger. Little surprise, then, that in 2022 we witnessed extended spells of turbulence in both bond and stock markets, as investors attempted to digest rapid signals from the world's leading central banks.

So far, we think that bond markets – which are notoriously sensitive to interest rate changes – are pricing in central bank action more aggressively than stock markets, resulting in a very challenging period of performance for bond prices. However, when asset prices fall, there is potential for long-term value to emerge, particularly in an asset class (like bonds) which has appeared to offer poor value for an extended period of time.

As a result, we see selective opportunities in government bonds and corporate debt, as well as more niche 'alternative' areas of debt markets. In keeping with this, we have dialled back some of our exposure to higher risk asset types like shares which we believe have further adjustments to make in this new world of higher central bank rates. Our strategies are also likely to be carrying a higher proportion of cash than usual, which should help our managers to remain as flexible as possible as the market picture evolves.

Few places to hide in 2022... but 2023 could be different

2022 has been quite a year. Financial markets have been exceptionally volatile, and for investors, there've been very few places to hide. What's more, the usual port in a storm – government bonds – have been at the very epicentre of the turbulence.

The statistics paint a stark reality. Around the midpoint of 2022, it had been the worst year for US government bond prices since 1788, and the worst first half of a year for US share prices since 1932 (one of the Great Depression years).

Over the course of the year, over 90% of global financial assets have failed to deliver a positive 'real' return (i.e. positive financial gains once inflation is taken into account). The last time that happened was 2018. The time before that was 1927.

Interest rates and inflation have hogged the limelight

Inflation has been higher and more persistent than central banks and markets had predicted, meaning that interest rate rises in 2022 have been materially more significant than forecast.

One example that highlights the latter point perfectly is the trajectory of rate expectations for US interest rates this year. Towards the end of last year, yields (interest payments) in the bond market implied that we would see US interest rates finish 0.25% higher in 2022 than at the end of 2021. At that point, US interest rates were set at a range of 0-0.25%. At the time of writing (mid-December), that range is 4.25-4.5%, having squeezed in one more at the US central bank's December's meeting.

That represents an historically large resetting of expectations. Given the importance of interest rates (and their impact on economic activity) to financial markets, it's little surprise that we've seen such material adjustments and volatility in asset prices over the course of the year.

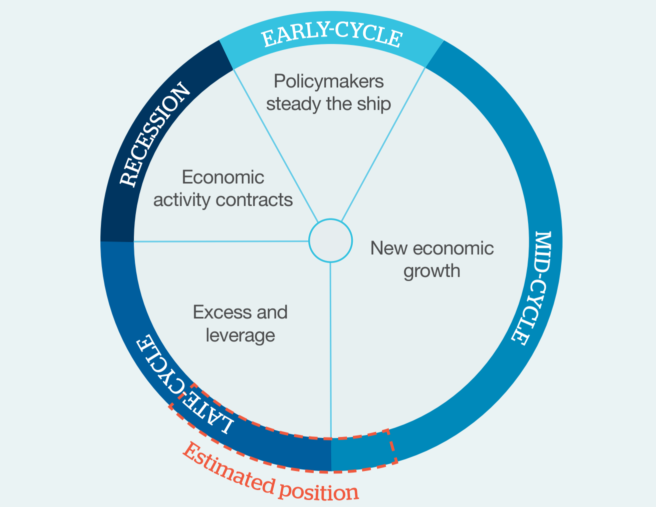
What does all this mean for the global economy?

The current economic cycle (the economy's perpetual fluctuations between growth and downtown) appears to be evolving exceptionally quickly. This cycle has been turbocharged by its unusual starting pistol (the COVID-19 pandemic – effectively a natural disaster, rather than a market event) as well as considerable economic support from governments and central banks in its early stages. As a result, we have moved through its phases at breakneck pace.

It can be difficult to pinpoint exactly where we are today, but our position in the economic cycle matters in terms of our outlook for the economy and financial markets. With this in mind, we draw on a multitude of economic and market data to determine our most likely current position. These indicators are highly varied, and typically deliver a wide spread of readings, leaving much open to interpretation. However, by late 2022, we believe that these indicators had shifted on aggregate, pointing to a later point in the economic cycle. By our best estimate, we now find ourselves much closer to the cycle's end than its beginning.

We are closer to the end of this economic cycle than the beginning

The global economic cycle, showing our estimated current position



Source: Handelsbanken Wealth & Asset Management

> "It's likely that growth will continue to slow in 2023, but this stuttering period of growth is unlikely to persist for long enough to cause a deep contraction in economic activity."

Graham Bishop Chief Investment Officer

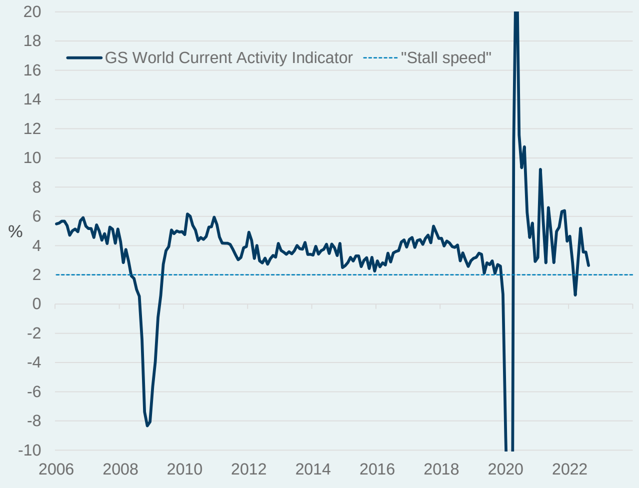
The trajectory of inflation and interest rates will continue to dictate the path for the global economy and markets over the course of 2023. Take a look at another of the articles in this *Investment Outlook – The war on inflation: a fair fight, or a losing battle?* – to find out more about central bank efforts to bring demand and balance back into a healthier balance.

While history is often an unreliable guide, it does tell us that achieving this without causing a technical recession (defined in the UK as two consecutive quarters of negative economic growth) is very much an art, not a science. It's increasingly apparent that some regions of the world are already in recession, even if this is yet to show up in economic growth data.

Nevertheless, we do not believe that the conditions are in place for a deep and prolonged contraction like the most recent two recessions (2008-09 and 2020). This is because the imbalances that normally precede a deep recession do not appear to be evident. Labour markets are strong and the housing market is slowing (two common imbalances that can foreshadow recession), but the level of financial excess seen from 2005-08 is absent, and the banking system is in good shape.

Economic growth is slowing, and will continue to slow in 2023

Global economic growth tracker



Source: Bloomberg

Given this set of dynamics, it's likely that growth will continue to slow in 2023, but this stuttering period of growth is unlikely to persist for long enough to cause a deep contraction in economic activity.

Is poor economic news a good thing for markets?

In 2022, markets did what they always do: move ahead of reality and price the future, not the present or past. In 2023, in the wake of this extreme volatility and repricing, we believe that attractive investment opportunities will continue to present themselves.

Our hunch is that the pattern between 2022 and 2023 may look quite similar to that of 2018 and 2019. In 2018, global growth was deemed strong enough for the US central bank to start to raise interest rates and begin the process of reducing its balance sheet (bloated by assets bought during/following the 2008-09 recession). The rate rises that followed were negligible compared to those witnessed in 2022, but were taken poorly by investors, who had grown used to ultra-low rates and central bank support.

Economic growth subsequently slowed quite materially in 2019, leading the US central bank not only to back off from further planned rate increases, but actually to unwind most of what they had already done. Markets reacted very positively to this, and 2019 was a very strong year for most asset types. While history never repeats itself, it sometimes rhymes. Could this happen in 2023?

The current inflation backdrop is very different to 2018-19, and central banks are extremely unlikely to unwind their 2022 actions. However, given that economic growth is likely to deteriorate, at some point in 2023 central banks will at the very last need to ease off the accelerator.

Over the course of 2022, we think bond markets have incrementally begun to price a more realistic backdrop. In stock markets, near-term weakness could persist as investors awake to the reality that corporate earnings may not be as resilient as forecast. To find out more about what our view on the financial market outlook means for our investment strategies, take a look at our next article: *How bond markets escaped the naughty step*.

How bond markets escaped the naughty step

2022 has been a tumultuous year of adjustment for financial markets. Investors have been abruptly weaned off the post-2008 era of low inflation and ultra-accommodative central bank policies, featuring record-low interest rates and central bank bond-buying. All asset types have been impacted, but – we would argue – none more so than bonds. What's changed, and what does it mean for investors?

Bond markets were uninspiring in the run up to 2022

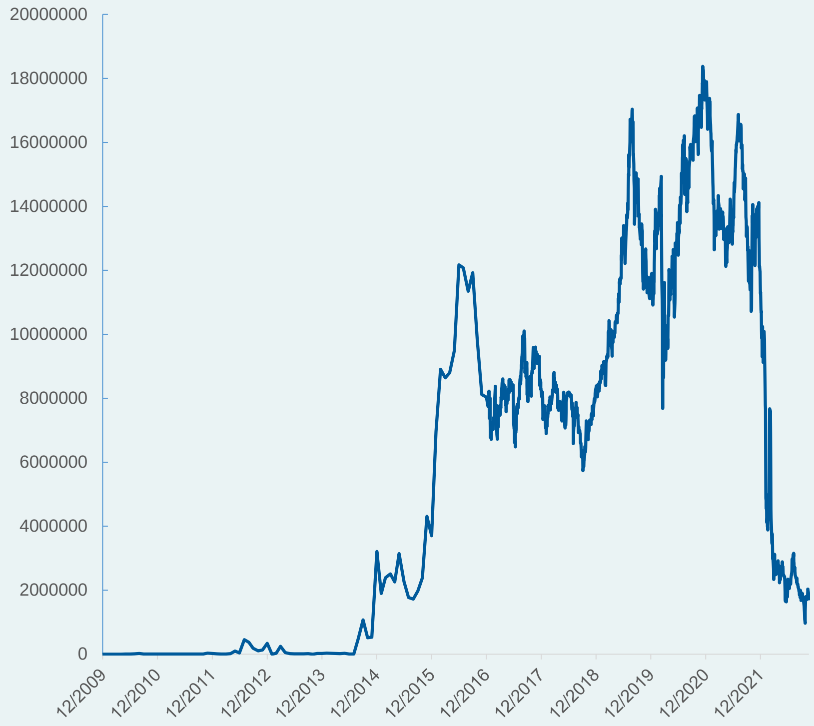
As a reminder, bonds are effectively IOU notes, most commonly issued by governments and companies. These issuers pay regular coupons to their bond holders, and the amount paid out in coupons each year as a percentage of the bond's price is referred to as its 'yield'. When a bond's price rises, its yield falls, and vice versa.

One of the consequences of the post-2008 regime was extremely low – and even negative – bond yields. In fact, we came close to $18trn of negative-yielding debt (bonds) at the height of the pandemic, meaning that investors were effectively paying to lend out their own capital (if they held these bonds to their maturity date). At the same time, 'duration' – the sensitivity of bonds to changes in interest rates – rose materially. This means that 'interest rate risk' for bonds was heightened.

> "One of the consequences of the post-2008 regime was extremely low – and even negative – bond yields. In fact, we came close to $18trn of negative-yielding debt (bonds) at the height of the pandemic, meaning that investors were effectively paying to lend out their own capital (if they held these bonds to their maturity date)."
>
> **David Absolon** Investment Director

The phenomenon of negative-yielding bonds has faded away in 2022

Global total of negative-yielding debt ($)



Source: Bloomberg

Meanwhile, taking a wider view, the correlation between bonds and shares went from negative to positive. This means that instead of behaving differently/inversely to one another (the ideal scenario in maintaining a diversified set of investments), bonds and shares began behaving in a similar fashion, as central bank actions drove the performance of both types of assets.

These factors meant that the diversification benefits of bonds as part of a mixed selection of investments, as well as their risk-versus-reward incentives, had deteriorated materially. Accordingly, we (and most of our peers) allocated relatively more capital towards other asset types. Stock markets looked much more interesting. Indeed, this period of time gave birth to an acronym – TINA (There Is No Alternative) – referring to the appeal of buying shares rather than super-expensive bonds, which were left sitting on the naughty step.

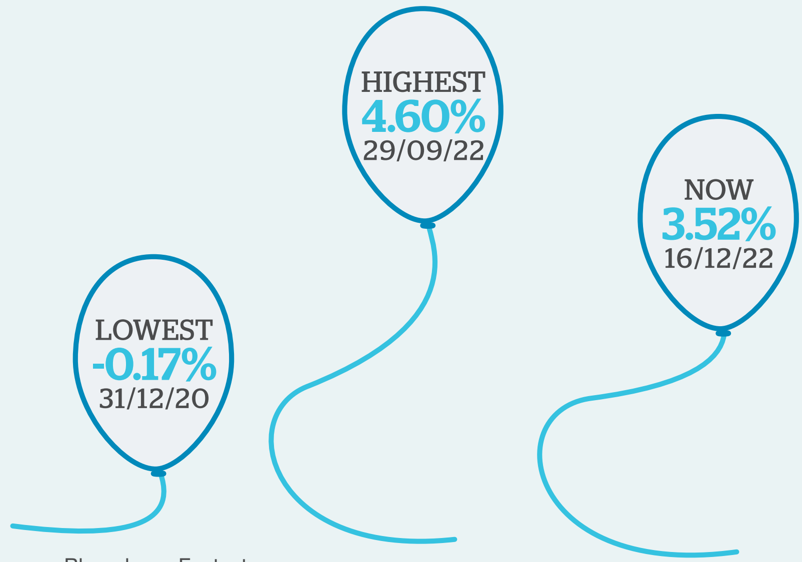
Everything changed for bond markets in one tempestuous year

Financial markets have been through huge readjustments in 2022, with many major asset types 'repricing' accordingly. We would argue that – of all the asset types repricing during this period – bonds have been the most notable. As such, for the first time in many years, valuations in more areas of bond markets look much more attractive on a risk-versus-reward basis for long-term investors.

For example, at the height of the COVID-19 pandemic, the yield-to-maturity (the rate of return if a bond is held until its redemption date) on 2-year UK government bonds was negative: -0.17%. This meant that investors holding these bonds to maturity were paying to lend their capital to the UK government over that period. At the time of writing, the yield-to-maturity on 2-year UK government bonds is now 3.52%. At one point during the brief Truss government, it reached 4.60% – a level not seen since October 2008. A positive yield-to-maturity with negligible interest rate risk seemed a pipedream only two years ago, but is now a reality.

The yields paid on bonds look increasingly attractive

Yields on 2-year UK government bonds at key points over the past 2 years



Source: Bloomberg, Factset

As a reminder, as bond yields rise, bond prices – which move in the opposite direction – have fallen. This means that bonds are now cheaper, and paying out more to their holders. This re-rating in valuation has taken place not only for government bonds, but also to corporate bonds and debt issued in developing economies. The yield-to-maturity in high yielding global debt (higher risk than government bonds, and therefore offering higher compensation to investors) dropped to a low of around 5% in 2021, but reached around 9.5% in the summer of 2022. While history is not always a reliable guide, future returns from the high yield area of global bond markets look compelling at these levels.

What does this mean for bonds today? Put simply, given how bonds have repriced over the course of 2022, the asset class is well and truly off the naughty step. We've now said goodbye to the world of TINA, and have entered the world of TARA: There Are Reasonable Alternatives. We believe that bonds have very much emerged as one of those alternatives.

What does this mean for the assets within our investment strategies?

Bonds

- Bonds now have a more material role in our strategies once more
- We have moved from an underweight to an overweight position in bonds versus our long-term average during the course of 2022, albeit with a focus on shorter-dated bonds
- Government bonds now have yields which should truly help to diversify our investment strategies in future volatile times
- Corporate bonds and developing economy debt can compete with stock markets among the assets we hold with the intention of driving financial returns

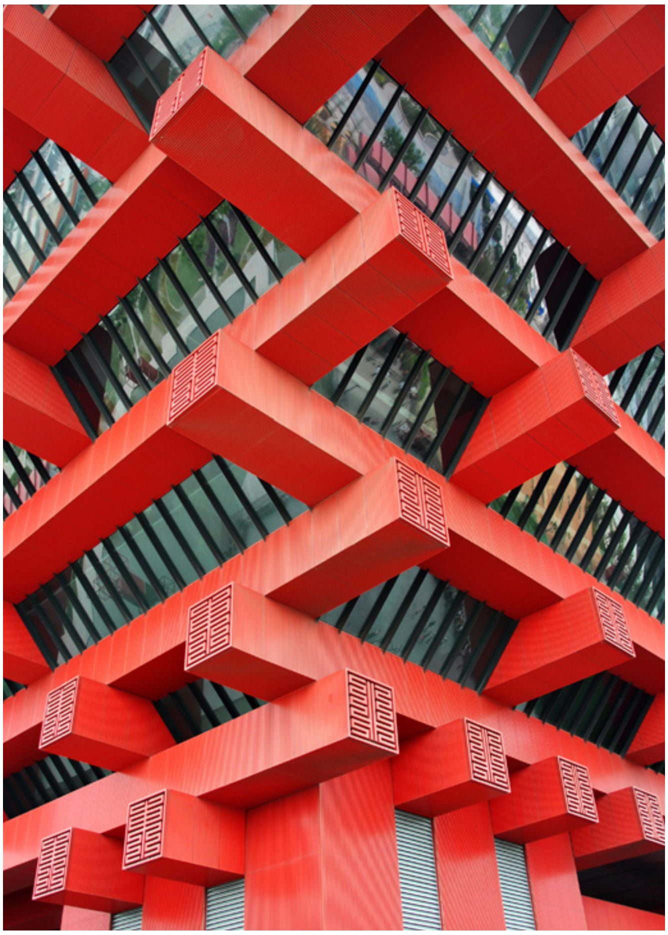
Shares

- At this juncture, 'TINA' is no longer relevant, as the relative value of shares versus bonds is a much less compelling argument than it once was
- Shares continue to play a key role in our investment strategies (particularly our higher risk strategies), but we have reduced our overall positions in stock markets
- We continue to see areas of value in small and mid-size companies, as well as certain areas of the technology sector and developing economies

Alternatives

- As well as shares, alternative asset types (outside of traditional bond and stock markets) were a major beneficiary of the 'TINA' era, and we have previously increased our positions here at the expense of bonds, largely being rewarded for that move both in terms of asset diversification and financial returns
- Given our view on bonds today, while we still want to have alternative asset types in our portfolio, we have dialled down some of the positions that benefited from the low interest rate and inflation backdrop
- Specialist strategies designed to protect against sharp market falls, as well as music royalties and selective hedge funds currently remain our preferred investments in this space

Is China turning a corner?



Since Chairman Mao proclaimed the People's Republic of China in 1949, the nation has been on a journey to reclaiming its role as a dominant force on the world stage. In the COVID-19 era, China has faced stark new challenges, emerging as both the starting point of the virus as well as the strictest enforcer of related population controls. Against this complex backdrop, Chinese financial assets have been on a wild ride in recent history. But are things beginning to change?

The return of the prodigal superpower

As one of history's great superpowers, China accounted for around a third of the global economy as late as 1820. However, its position on the world stage faded rapidly in the industrial age, with its dominance superseded by newly industrialised Western powers. Following a century or so in a comparatively meagre position, China's modern trajectory to becoming the world's manufacturing hub and its second largest economy has been rapid, if not without difficulties.

Over the past few decades, China has played a pivotal role in the 'globalisation' of supply chains around the world. Thanks to its capacity for cheap, large-scale manufacturing, China emerged as a key exporter, earning the nickname 'the world's factory floor'. Meanwhile, Chinese financial markets, which were initially very slow to open up to outside investors, have now ballooned to make up a significant portion of the assets available to global investors in developing economies.

However, in very recent history, China has been irrevocably entangled with the COVID-19 pandemic. In late 2022, when most of the world had moved on to a more pragmatic phase of COVID-19 management, new outbreaks of the virus led China's authorities to reiterate its zero-tolerance policy, announcing new lockdowns in major cities. Financial markets reacted badly to ongoing evidence of China's uncompromising approach, predicting knock-on effects for economic activity, and the price of Chinese financial assets fell sharply.

Faced with yet another spate of severe lockdowns, a rare wave of protests broke out among Chinese citizens tired of this zero-tolerance approach to the virus. While the resulting crackdown from Chinese authorities was swift, these protests (perhaps combined with the financial market outcry) appear to have impacted the way COVID-19 will be managed in China in the future. According to changes already announced, lockdowns will now be more targeted and localised, and testing and quarantining rules will be relaxed. A fresh vaccination drive, focused especially on the elderly, is in the works. A recent study in the US has also suggested that the efficacy of the Chinese-developed vaccine could be better than had previously been reported, potentially offering rates of immunity comparable to Western-developed vaccines. All in all, this was welcome news for both the Chinese population and the global investment community.

An authoritarian state in a modern world

China is unusual among the world's largest economies for its authoritarian political regime, with the country ruled by leading members of the Chinese Communist Party. President Xi Jinping has been in power for around a decade, and an amendment to the state constitution means that there is no longer any term limit on his presidency.

In 2022, Xi reshuffled the Communist Party's leadership, replacing a number of senior figures with party members reported to be personally loyal to him. Financial markets appeared to react very badly to this news too, although investors may also have been responding to unfounded hopes that Xi's announcement would also contain news of COVID-19 easing (which ultimately came later). The price of Chinese financial assets fell quickly, and businesses with a substantial proportion of international shareholders (such as ecommerce giant Alibaba) were especially hard hit.

It's worth noting that Xi's newly appointed senior leaders may have more than merely their loyalty to recommend them: they could also be seen as experienced and competent hands. For example, Li Qiang – promoted to become Xi's de facto second-in-command – is at least partially responsible for the development of high-tech industries and financial and technological innovation in Shanghai's 'Special Economic Zone'. Li will reportedly lead a team of economists and administrators with significant international experience, who are committed to ongoing economic development and technological innovation. It may yet transpire that financial markets have more to gain from these new leaders than first anticipated.

What do developments in China mean for the global economy?

China may be entering a new phase of development on a number of fronts. The longer-term effects of President Xi's committee reshuffle remain to be seen, but fresh ideas from these new promotions, combined with an increasingly pragmatic approach to managing the COVID-19 pandemic, has the potential to improve the economic growth backdrop.

Indeed, China's rulers are committed to policies which will, at the very least, support economic stability into 2023. In November 2022, China's regulators expanded a financing programme aimed at supporting bond issuance in the property sector, as well as issuing a 16-point plan to support the sector. More meaningful policies are likely to be laid out at the Central Economic Work Conference (December 2022): an annual meeting which sets the national agenda for China's economy. Further economic stimulus is likely to be on the way.

For China's economy, and the value of Chinese assets, this should be good news. In the very near term, under more relaxed COVID-19 rules, we could see a slight impact to the economy as virus case numbers rise. But over the longer term, looser rules, and new senior committee members with a growth mandate to fulfil should lead economic activity to pick up.

When it comes to pricing pressures, domestic inflation is currently very low (around 2%), but fewer (or less extreme) lockdowns could allow inflation to rise higher. Similarly, a boost to China's economic activity could also create a boost for the global economy, which is in dire need of growth. However, it remains to be seen what this would mean for global inflation.

> "Chinese asset prices can be extremely volatile, as the past year has shown. But, bearing in mind these risks, and mindful that no outcomes are ever guaranteed, we continue to see real potential in selective areas of Chinese financial markets."
>
> **Jaisal Pastakia** Investment Director

Are Chinese financial assets a good bet?

Chinese asset prices have been penalised at various points in 2022, but at the time of writing, we are seeing welcome signs of recovery. Within our investment strategies, two areas could be especially helped by ongoing positive momentum. The first is a position in high-yielding Asian bonds, which so far has responded well to new policies introduced to support China's property sector. The second is our position in a fund focused on internet and ecommerce in developing economies. This set of investments has substantial exposure to businesses in China, which are set to benefit from the economy opening up.

Chinese asset prices can be extremely volatile, as the past year has shown. But, bearing in mind these risks, and mindful that no outcomes are ever guaranteed, we continue to see real potential in selective areas of Chinese financial markets. Against the right backdrop, 2023 could see China turn an interesting corner in terms of domestic policy change, economic growth, and financial market performance.

China's rapid evolution from sleeping giant to volatile superpower

1949
Chairman Mao proclaims the People's Republic of China

1958-61
A failed scheme of rapid industrialisation – the Great Leap Forward – leads to around 30 million deaths due to starvation

1966-71
China displaces Taiwan to join the UN

1985
China's first trade surplus (exporting more than it imports) with the US

1989
Protests in support of political reform end when the army kills hundreds in Tiananmen Square

2001
China joins the World Trade Organisation

2008
Beijing Olympic Games highlight China's entry to the world stage

2010
China becomes the world's second largest economy, displacing Japan

2012-13
Xi Jinping comes to power and unveils the Belt and Road Initiative, designed to grow China's global influence

2018
State constitution amended to remove term limits for the president, allowing Xi to retain power for life

2019
COVID-19 breaks out in Wuhan, sparking a devastating international health crisis and economic turmoil

2020
First sweeping lockdowns begin in China (January)

2022
President Xi reforms his committee of leaders

Anti-lockdown protests shock China's authorities, sowing the seeds of COVID-19 policy change

Making your investments work harder

2022 has been a volatile year for investors across the board, but the year has also played host to some important developments in sustainable investing. We recently produced our Sustainable Impact Report, which contains more detail on the evolution of sustainable investing, as well as a closer look at the specific investments at work in our sustainable strategies. Below, we discuss some of the themes highlighted in the report.

Financial regulators are coming for greenwashing

One of the (very fair) criticisms levelled against sustainable investing in recent years is that the terminology and labelling of investment products is inconsistently applied, and poorly regulated. Companies, bonds and funds can all be labelled as green, 'ESG' (environmental, social, governance), sustainable, responsible, or ethical, with little or no formal delineation between these terms, and without the need to adhere to any strict rules as a result of their labelling. Not only does this lead to investor confusion (as it is challenging to understand and compare investment products), it has also created the potential for 'greenwashing'.

What is greenwashing?

Greenwashing is a form of deception, where marketing, advertising or PR coverage falsely indicates or exaggerates a company/product's environmental or socially responsible credentials. This could be achieved by the use of misleading labels and language (such as including the word 'green' in a fund's name), or through visual messaging (such as the use of imagery focused on the natural world).

As we speak, new regulation is emerging around the world, designed to tackle these grey areas, put a halt to misleading labelling, and improve investor understanding of sustainable investment products. Regulators in the UK, the EU and the US are all cracking down on vague, misleading or false labelling, aiming to provide greater clarity to investors when it comes to the sustainable credentials of the products in which they invest.

We welcome this clarity, and the greater confidence it should bring to the industry. 'Green bonds', which are issued to finance sustainable projects, are critical for many companies and governments in funding the move to a more sustainable future, so it's important that they can be easily identified.

A record **$517.4bn green bonds** were **issued** in **2021**, **up 74%** (from $297bn) in **2020**

Source: Climate Bonds Initiative

Responsible investing is about more than renewable energy

Quite understandably, renewable energy has long been the poster child for sustainable investing. But while it is critically important to fund the transition to a cleaner future, sustainable investing covers a much broader remit, from reducing social inequality and improving Boardroom diversity, to finding the medical solutions to our gravest health problems. Indeed, the latest report from the IPCC (Intergovernmental Panel on Climate Change) discusses the need for a 'just' transition to renewable energy – one which decarbonises the economy in a fair way, ensuring no one gets left behind.

of the **world population lives** in **countries emitting less** than **3 tonnes CO_2 per person annually**, but a **substantial share** of these people **lack** access to **modern energy** services.*

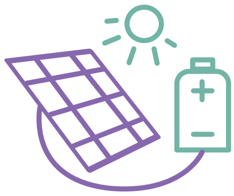
Source: IPCC, 2019 figures. *Defined as access to clean, reliable and affordable energy services for cooking, heating, lighting, communications, and productive use.

Bringing social responsibility into the heart of sustainable investing also means rethinking the way we've classified investments in the past. This is less about greenwashing, and more about taking a wider-reaching approach. For example, any investment in the transition to cleaner energy would historically have been viewed as a sustainable investment. Today, sustainable investing is a more holistic undertaking.

With this in mind, a wind farm operator is not automatically given a free pass because it ticks the 'E' box in 'ESG' – what about that company's governance, its Board diversity, its industrial accident rate, and its impact on the local community?

> "Bringing social responsibility into the heart of sustainable investing also means rethinking the way we've classified investments in the past. This is less about greenwashing, and more about taking a wider-reaching approach."

Ben Matthews Investment Director



To meet **'net zero'** commitments, **battery storage capacity** must **expand** by **44 times** by **2030**

Source: International Energy Agency

Investors are continuing to wake up to the knowledge that we can address social issues by putting our money where our principles lie. To take another simple example, at a time when the cost of living is rising, finding affordable housing is becoming increasingly challenging for vulnerable people. By investing in social housing, investors can choose to fund safe, specialist shelter for those who need it, while also seeking a return on their capital.

Source: National Housing Federation

8.5 million people in **England** have some form of **unmet housing need**.

Overcrowding is the **largest housing problem** nationally, **affecting** nearly **3.7 million** people.

Why do we produce an annual impact report?

When people choose to invest their money sustainably, they have a right to see how it has been put to work to create a genuine positive impact. Our Sustainable Impact Report is designed to demonstrate how – and where – our sustainable funds do this.

By outlining some of the features of our sustainable funds in detail, the report highlights how individual investments are able to make a real difference. It also uses independent analysis to rate our funds across a range of sustainability criteria. Our aim is to be accountable and transparent, while bringing sustainable investing to life for our customers.

Click here to read our Sustainable Impact Report.

Investment team

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Investment Director

Scott Ingham
Investment Director

Charu Lahiri
Investment Director

Ben Matthews
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Jaisal Pastakia
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Investment Manager

Nathan Henry
Investment Associate

Caroline Von Celsing
Investment Associate

Awards

The Asset Management Awards 2022

Winner: Multi Asset Manager of the Year award

2022 Wealth Briefing 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 Wealth Briefing 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.