Sustainable Managed Portfolio Service

Quarterly report – Q4 2023
Annual report – 2023

Introduction

Welcome to this expanded edition of our Sustainable Managed Portfolio Service (MPS) investment review. In this report, we cover information and events that influenced performance, not only in the fourth quarter of 2023, but across the entire year.

The stock market finished 2023 by continuing to provide strong returns to courageous investors. In a year in which cash was assumed by many to be king, stocks were the best performing major asset class, easily outstripping the returns available from the highest yielding bank accounts.

As for bonds, they had a torrid start to the year but finished very strongly indeed. Whereas commodity prices were generally weak but for a special year for gold, which continued its impressive performance across 2023.

All in all, this was a far kinder year for investors than 2022, where most investments struggled against the sharp increase in inflation which led central banks to raise interest rates far faster than they had expected.

So, what enabled investments to prevail over the last few months? A lot comes back to interest rates, with the threat that higher rates might persuade investors to take the road less travelled of lower but more stable returns. However, 2023 exposed the risks of that strategy; investors flocked to bonds to lock in the relatively high yields on offer in anticipation that interest rates will be cut during 2024.

2023 saw inflation trend downwards and its continuation along that path was a major theme of the final quarter, particularly in the UK. Over the course of the year, agricultural and energy commodities declined by around 10% each, with energy proving to be particularly weak during the final quarter of 2023.

The UK's energy price cap, together with the government's support, sheltered households from the most severe rises as experienced in European gas markets. However, it did mean prices rose sharply in October 2022 and therefore contributed to the seemingly outlandish inflation rate reported in the UK. As the one-year anniversary of those increases passed, UK inflation has declined more significantly.

The decline in inflation, particularly the element relating to high commodity or transit costs, is of course reassuring. But while consumers can hope to benefit from lower price increases, reduced inflation also raises the possibility that recession will be avoided.

And while the performance of the stock market seemed to disproportionately reflect the performance of seven individual companies - a source of concern for some - as 2023 closed out, a much broader stock market rally was underway.

The big picture in Q4 2023

- The quarter sadly started with another major conflict, with Hamas' surprise attack triggering a full military retaliation from Israel. We remain concerned about the risk of the conflict expanding further, as the wider political instability issues of the Middle East region are entwined in the power struggles of this war.

- Australian company directors who fail to consider nature-related risks could be found liable for breaching their duty of care and diligence according to a new legal opinion. An example of nature-related risk is the European Union's decision to require companies not to import beef produced on land that has been deforested.

- The UK government increased the guaranteed starting price of electricity for the latest UK offshore wind auctions by 66% after a previous auction failed to attract any bids. Energy companies have been reluctant to take on new projects as steep inflationary cost increases have made the previous level economically unfeasible.

- At the end of November, we welcomed the publication of the Financial Conduct Authority (FCA)'s Sustainability Disclosure Requirements (SDR) and labelling regime. Whilst the product labels and disclosures do not yet apply to wealth managers like us, the regulation will make clear which investment products can be labelled with the name 'sustainability', in an attempt to reduce instances of greenwashing, which can be disadvantageous to clients. A selection of labels has been made available for UK investment products that fulfil and can evidence certain criteria. We will be participating in the consultation process regarding how this applies to portfolios, always keeping the interests of our clients front of mind.

- Finally, the turn of the year marks the moment that the 2021 agreement on the global minimum corporate tax rate of 15% comes into effect, which would increase taxes on companies based in low-tax jurisdictions. Under the rules, large companies would pay more taxes in countries where they have customers and less in countries where they have headquarters, employees, and operations. Although without the US and China as signatories, this is mostly a European-encompassing treaty.

Market overview Q4 2023

- Asset class performance in Q4 2023 was marked by a series of significant events, but despite the challenges, markets showed resilience and ended the quarter on a positive note.
- A reduction in interest rate expectations triggered a rally in invested assets and provided relief to real estate stocks in particular, which saw a robust return of 12.6%. North American equities also did well and returned 7%. Despite volatility in Chinese stocks due to potential strict regulations on the gaming industry, the emerging market equities still managed to return 5.4%.
- Bonds also performed strongly in response to the increasing likelihood of interest rate cuts in 2024 and returned between 5% and 8%.
- Gold also rallied strongly, giving a return of 6.3%, indicating its role as a safe haven during times of uncertainty.
- The US experienced political turmoil with the ousting of Kevin McCarthy as the speaker of the House of Representatives, causing a paralysis in the legislative process.
- Chinese economic activity exceeded expectations but remained weak, with Beijing implementing selective measures to address the housing downturn.
- December saw a rise in US personal spending data, indicating a robust consumer market supported by excess savings, a resilient job market, and falling gasoline prices. This led to the S&P 500 nearing record highs. However, Chinese stocks experienced volatility due to potential strict regulations on the gaming industry.
- The Bank of Japan's decision to maintain negative interest rates kept traders on their toes, with potential implications for global markets. Despite this, the impact was more on its currency rather than global bond yields, suggesting that the removal of low interest rates in Japan may not hinder a rally in global bonds in 2024.

Sustainable MPS highlights Q4 2023

Asset Allocation

What worked and why?

The overweight to UK Sovereign Bonds and the overweight to Cash have been positive contributors.

What didn't work and why?

The underweight to property was a mild contributor to underperformance.

Fund Selection

What worked and why?

Brown Advisory US Sustainable Growth was the most significant contributor to returns in Q4. Liontrust Sustainable Future US Growth fund also contributed positively to returns.

What didn't work and why?

Schroders Global Cities was the most significant detractor this quarter, underperforming the strong rebound in property. Evenlode Global Income was also a modest detractor from returns in Q4.

Sustainable MPS Portfolio changes Q4 2023

Asset Allocation

There were no changes to the strategic asset allocations this quarter.

In October, the Asset Allocation Committee took advantage of the higher rate environment by increasing UK gilts and Inflation-linked bonds by 0.5% each, funding this addition from absolute return and cash.

In December, the Committee decided to modestly increase exposure to equities by 0.5%, paying for that upgrade by reducing absolute return. The Committee also boosted the US weighting by 0.5% at the expense of each of the other geographical regions as the US market is most exposed to the upside of an 'AI boom', but also should be the most defensive market in a cyclical recession.

Fund Selection

In October, the L&G All Stocks Gilt Index and L&G Global Inflation Linked Bond Fund were increased whilst the allocation to BNY Mellon Sustainable Global Dynamic Bond and Blackrock ICS Sterling Liquidity were reduced.

In November, we introduced a new fund into the portfolios; Schroder Global Sustainable Value, which was funded from reductions to Brown Advisory US Sustainable Growth, TB Evenlode Income and CT Responsible Global Equity.

December saw a modest reduction in BNY Mellon Sustainable Global Dynamic Bond, with the allocation to Brown Advisory US Sustainable Growth increasing in line with Asset Allocation Committee guidance.

SMPS performance

SMPS PERFORMANCE (%)					
	Q4	2023	1yr	2yr	2022
Income Portfolio	6.0	7.5	7.5	-5.1	-11.7
Income Higher Equity Portfolio	6.1	8.3	8.3	-4.4	-11.7
Balanced Portfolio	6.3	8.5	8.5	-3.9	-11.5
Growth Portfolio	6.5	9.4	9.4	-3.3	-11.6
Global Equity Portfolio	6.6	10.7	10.7	-2.3	-11.7

All figures shown above are calculated to 31 December 2023.

Inception Date of 26/04/2021 (Please note: we can only publish performance data for two years due to the inception date as shown)

Performance Calculation: All income is reinvested. Performance is shown inclusive of underlying fund charges but gross of RBC Brewin Dolphin's investment management charge. Deduction of this charge will have the result of reducing the illustrated performance. Neither simulated nor actual past performance are reliable indicators of future performance.

Funds in focus Q4 2023

Schroders Global Sustainable Value

The fund is managed by the Schroder Value Team, which is possibly the most stable and enduring value team in the UK. Whilst the track record of the fund is relatively short, the team's UK, European and Global Recovery strategies have all outperformed, demonstrating the effectiveness of the team and process.

The Schroder Sustainable Global Value strategy marries their long-standing value philosophy with only investing in ESG leaders. The team define an ESG leader as a business that: a) has a positive societal benefit, and b) is best-in-class relative to peers in its approach to sustainability.

The exclusionary policy of the fund should give it a wide SRI audience as it complies with all of our own exclusionary criteria but goes further to include no significant exposure to alcohol and fossil fuels, which are common red lines for SRI investors. Furthermore, Schroders is a clear leader in ESG integration and engagement. Schroders is one of the first asset managers with research tools that can put a financial value on the on the environmental and social impacts of a company, both positive and negative.

The fund is multi-cap with exposure from mega to small caps. Overall, the fund has a mid-cap portfolio market capitalisation of around £12bn. It only invests in the cheapest 20% of the market and in ESG leaders, meaning there are clear guard rails against style drift, either in terms of value or sustainability.

The value style has underperformed since 2007, however, valuation is receiving greater attention with inflation now running at higher levels and ultra easy monetary policy coming to an end in as many years. The benefits of having value stocks in portfolios surprised most investors in 2022 and as the "magnificent seven" drive market returns in 2023, this presents a renewed opportunity to build a position.

Anna Haugaard
Senior Analyst

Robeco Global Credits & SDG Global Credits

One of the mainstays of our fixed income allocation is the Robeco SDG Global Credits fund, which has very strong ESG and investment credentials. The credit team is comprised of 37 professionals who are supported by the 36-person strong dedicated SRI team. All team members are extensively trained on sustainable investing through in-house programmes that include:

- Quarterly knowledge-sharing sessions that share best practices and learning from each other. In each session, different investment teams present ESG integration cases, the SDG research framework, academic research, market intelligence, and the results from the firm engagement efforts.

- Ad-hoc sessions on topics such as the Sustainable Development Goals (SDG), contents of publications on sustainability, developments at the PRI, sustainability data gathering, and sustainability themes and investing.

All processes are evidence-based and have been optimised to identify and quantify ESG and financial risks comprehensively and accurately. The team also developed and continues to refine processes to analyse SDG contributions and assess Green bonds. Robeco also developed in-house Country Sustainability Ranking to assess government bonds from an ESG perspective. The ranking is based on their RobecoSAM ESG database. The ranking is updated twice a year and functions as an early-warning system that helps to identify both the threats and the opportunities in a country before they are reflected in spreads or ratings. The strategy also adopted the Climate Change framework and will actively seek to construct portfolio with reduced carbon emissions (at least 20% lower than the broader index).

Shakhista Mukhamedova
Head of Fixed Income and Alternatives

Update on our SDG alignment scores

In our last annual report, we wrote about significant movements in the alignment scores for the UN SDG (United Nations Sustainable Development Goal) that occurred in Q4 2022, as calculated by MSCI. These were significant downgrades as MSCI assessed that human rights supply chain issues in China's Xinjiang region affected a significant number of underlying investments. This updated assessment produced a notable change in SDG alignment at a portfolio level. Following this we undertook two pieces of work:

1. An engagement with MSCI to better understand what drove this specific change in assessment and its approach to controversies more broadly
2. An engagement with fund managers on several of the companies held that had parts of their supply chain within the Xinjiang region in China

Both engagements have been fruitful. Our discussions with MSCI revealed that several other investment firms had noted the change in stance, so MSCI undertook a collective client consultation around its UN SDG rating methodology, focusing particularly on controversy scoring. This resulted in a change to its methodology, which now better acknowledges the differences between companies that are directly involved in human rights abuses, and those that are indirectly involved through their supply chain.

Of course, this does not help us progress towards reducing the real-world impact of the underlying issue, which is sadly very real. This is where the engagement with fund managers on the underlying companies comes in, to agitate for progress towards a solution. This is covered in our annual stewardship report, which we encourage you to read for further details of our discussions with fund managers.

As was the case last year, the change in portfolio UN SDG alignment scores does not represent a change in the investment selection approach at RBC Brewin Dolphin. It also serves as a useful reminder as to why third-party ESG ratings do not form part of our investment assessment – we rely on our own criteria as well as face-to-face interviews to form our view on how well-integrated ESG factors are into a fund manager's research process. Our fund analysts also examine each manager's investment portfolio periodically to better understand portfolio alignment and identify holdings that may benefit from deeper engagement and stewardship activities.

We anticipate future fluctuations in the various sustainability-related metrics we report in our factsheets, as the new UK Sustainability Disclosure Requirements (SDR) regulation will come into force over the next few years. This, combined with various taxonomy requirements, will bring significantly more data to ratings providers, likely leading to further re-appraisals of companies in the investable universe. We hope that standards expected of companies continue to be raised and will continue to monitor developments.

Tom Buffham
Portfolio Analyst

ESG reporting for SMPS Income
(as at 31 December 2023)

MSCI ESG Ratings

ESG Quality Score 7.0

Carbon Intensity

Carbon Intensity measures a portfolio's exposure to carbon intensive businesses and is a recommended metric for assessing carbon risk by the Task Force on Climate Related Financial Disclosures (TCFD). It is calculated as a weighted average of each portfolio company's total Scope 1(1) and Scope 2(2) carbon emissions divided by their annual sales, with a lower score representing less (better) Carbon Intensity.

Comparisons of Carbon Intensity figures should be made with caution, as generally companies in the sectors with the highest carbon emissions (such as utilities) also have the highest potential for reducing their carbon emissions. We believe it is important to encourage these reductions in carbon emissions where they have the potential for highest impact.

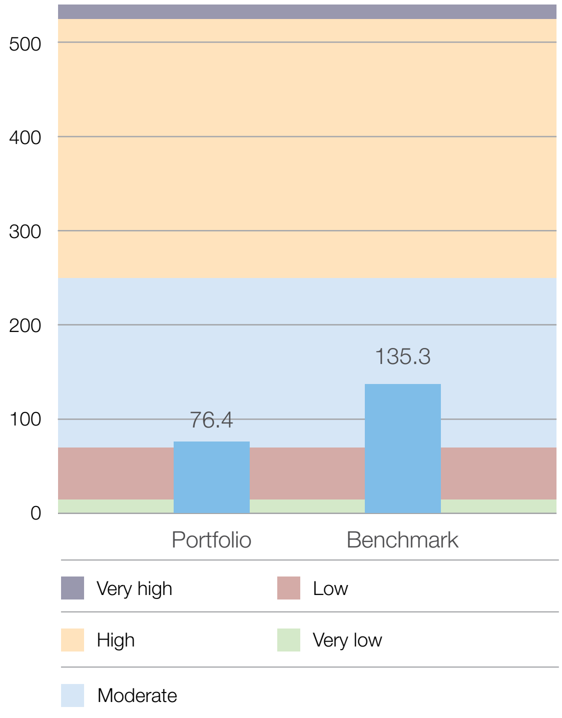
References:

(1) Scope 1: All direct GHG emissions from sources owned or controlled by the company (e.g. emissions from combustion in owned boilers, furnaces).

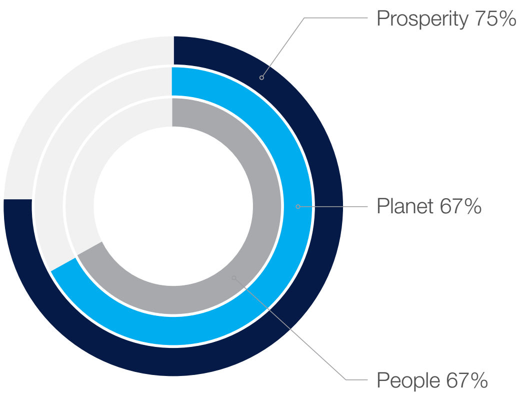
(2) Scope 2: Indirect GHG emissions that occur from the generation of purchased electricity, steam or heat consumed by the company.

Benchmark for comparison: 45% Global equity, 55% Global aggregate bonds

Carbon Intensity vs Benchmark (TCO2e / $m sales)



SDG Alignment



The UN SDG Alignment provides a framework for considering a broad set of 17 sustainability issues. Although not intended for investment purposes, it provides a useful context for measuring a portfolio's alignment with these goals.

We select 12 of these SDGs and place them into three sustainability themes: People, Planet, and Prosperity, with each sustainability theme consisting of four SDG goals. We use fund alignment data from MSCI to measure the alignment of the portfolio to each of our three sustainability themes. To calculate this, we take a weighted average of each fund's alignment to each of the three sustainability themes.

For instance, if Fund A is a 10% holding in the portfolio, and within the People theme is aligned with both "Zero Hunger" and "Gender Equality" but not the other two SDGs, then the fund will contribute 5% to the overall score of the People theme: 2.5% through Gender Equality and 2.5% through "Zero Hunger".

ESG reporting for SMPS Income Higher Equity
(as at 31 December 2023)

MSCI ESG Ratings

ESG Quality Score 7.2

Carbon Intensity

Carbon Intensity measures a portfolio's exposure to carbon intensive businesses and is a recommended metric for assessing carbon risk by the Task Force on Climate Related Financial Disclosures (TCFD). It is calculated as a weighted average of each portfolio company's total Scope 1(1) and Scope 2(2) carbon emissions divided by their annual sales, with a lower score representing less (better) Carbon Intensity.

Comparisons of Carbon Intensity figures should be made with caution, as generally companies in the sectors with the highest carbon emissions (such as utilities) also have the highest potential for reducing their carbon emissions. We believe it is important to encourage these reductions in carbon emissions where they have the potential for highest impact.

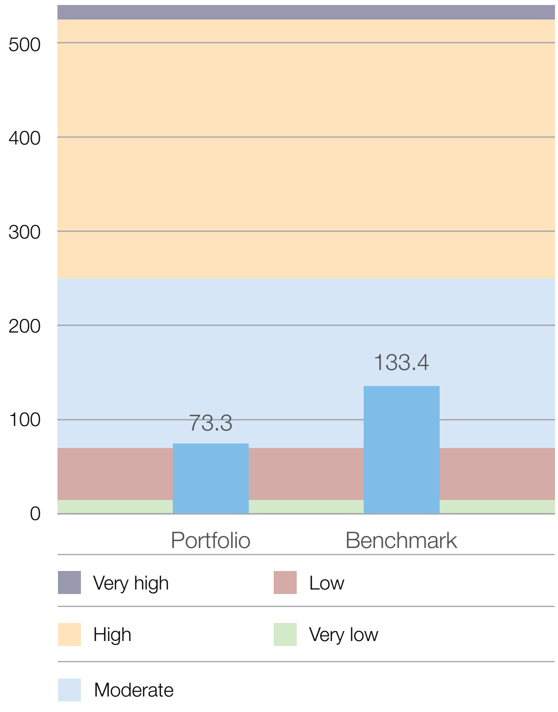
References:

(1) Scope 1: All direct GHG emissions from sources owned or controlled by the company (e.g. emissions from combustion in owned boilers, furnaces).

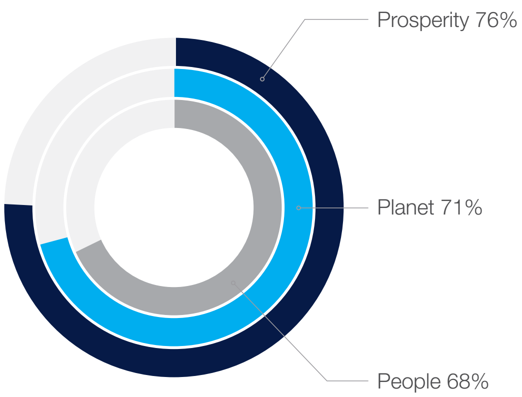
(2) Scope 2: Indirect GHG emissions that occur from the generation of purchased electricity, steam or heat consumed by the company.

Benchmark for comparison: 55% Global equity, 45% Global aggregate bonds

Carbon Intensity vs Benchmark (TCO2e / $m sales)



SDG Alignment



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For instance, if Fund A is a 10% holding in the portfolio, and within the People theme is aligned with both "Zero Hunger" and "Gender Equality" but not the other two SDGs, then the fund will contribute 5% to the overall score of the People theme: 2.5% through Gender Equality and 2.5% through "Zero Hunger".

ESG reporting for SMPS Balanced
(as at 31 December 2023)

MSCI ESG Ratings

ESG Quality Score 7.3

MSCI ESG RATINGS AA

CCC | B | BB | BBB | A | AA | AAA

Carbon Intensity

Carbon Intensity measures a portfolio's exposure to carbon intensive businesses and is a recommended metric for assessing carbon risk by the Task Force on Climate Related Financial Disclosures (TCFD). It is calculated as a weighted average of each portfolio company's total Scope 1(1) and Scope 2(2) carbon emissions divided by their annual sales, with a lower score representing less (better) Carbon Intensity.

Comparisons of Carbon Intensity figures should be made with caution, as generally companies in the sectors with the highest carbon emissions (such as utilities) also have the highest potential for reducing their carbon emissions. We believe it is important to encourage these reductions in carbon emissions where they have the potential for highest impact.

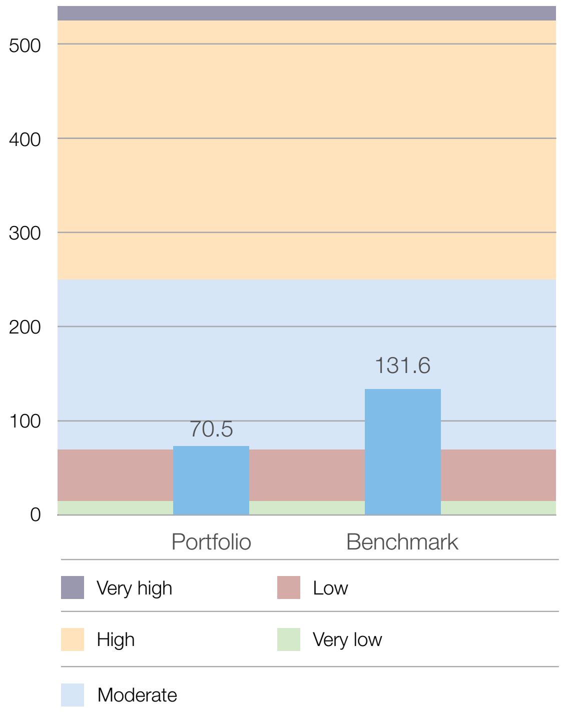
References:

(1) Scope 1: All direct GHG emissions from sources owned or controlled by the company (e.g. emissions from combustion in owned boilers, furnaces).

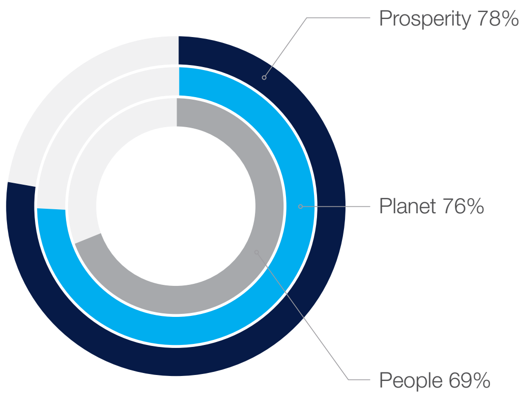
(2) Scope 2: Indirect GHG emissions that occur from the generation of purchased electricity, steam or heat consumed by the company.

Benchmark for comparison: 70% Global equity, 30% Global aggregate bonds

Carbon Intensity vs Benchmark (TCO2e / $m sales)



SDG Alignment



The UN SDG Alignment provides a framework for considering a broad set of 17 sustainability issues. Although not intended for investment purposes, it provides a useful context for measuring a portfolio's alignment with these goals.

We select 12 of these SDGs and place them into three sustainability themes: People, Planet, and Prosperity, with each sustainability theme consisting of four SDG goals. We use fund alignment data from MSCI to measure the alignment of the portfolio to each of our three sustainability themes. To calculate this, we take a weighted average of each fund's alignment to each of the three sustainability themes.

For instance, if Fund A is a 10% holding in the portfolio, and within the People theme is aligned with both "Zero Hunger" and "Gender Equality" but not the other two SDGs, then the fund will contribute 5% to the overall score of the People theme: 2.5% through Gender Equality and 2.5% through "Zero Hunger".

Prosperity

Planet

People

ESG reporting for SMPS Growth

(as at 31 December 2023)

MSCI ESG Ratings

ESG Quality Score 7.5

MSCI ESG RATINGS: AA (CCC | B | BB | BBB | A | AA | AAA)

Carbon Intensity

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Comparisons of Carbon Intensity figures should be made with caution, as generally companies in the sectors with the highest carbon emissions (such as utilities) also have the highest potential for reducing their carbon emissions. We believe it is important to encourage these reductions in carbon emissions where they have the potential for highest impact.

References:

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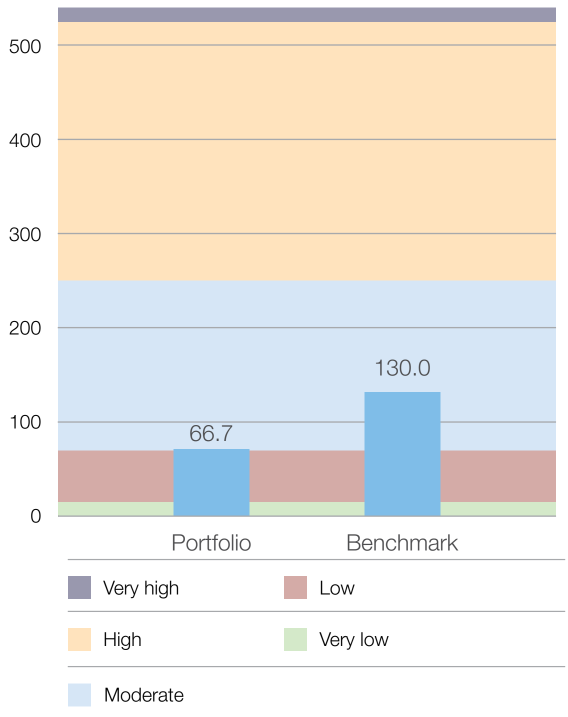
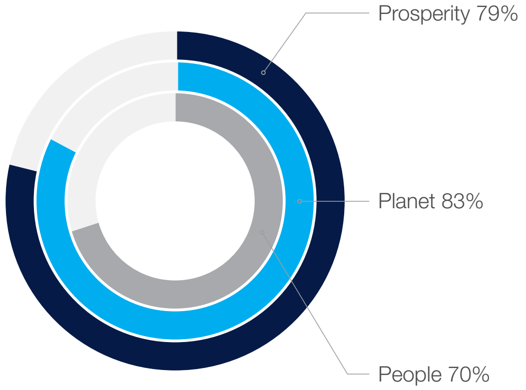
(2) Scope 2: Indirect GHG emissions that occur from the generation of purchased electricity, steam or heat consumed by the company.

Benchmark for comparison: 85% Global equity, 15% Global aggregate bonds

Carbon Intensity vs Benchmark (TCO2e / $m sales)



SDG Alignment



The UN SDG Alignment provides a framework for considering a broad set of 17 sustainability issues. Although not intended for investment purposes, it provides a useful context for measuring a portfolio's alignment with these goals.

We select 12 of these SDGs and place them into three sustainability themes: People, Planet, and Prosperity, with each sustainability theme consisting of four SDG goals. We use fund alignment data from MSCI to measure the alignment of the portfolio to each of our three sustainability themes. To calculate this, we take a weighted average of each fund's alignment to each of the three sustainability themes.

For instance, if Fund A is a 10% holding in the portfolio, and within the People theme is aligned with both "Zero Hunger" and "Gender Equality" but not the other two SDGs, then the fund will contribute 5% to the overall score of the People theme: 2.5% through Gender Equality and 2.5% through "Zero Hunger".

ESG reporting for SMPS Global Equity
(as at 31 December 2023)

MSCI ESG Ratings

ESG Quality Score 7.8

MSCI ESG RATINGS AA

CCC | B | BB | BBB | A | AA | AAA

Carbon Intensity

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References:

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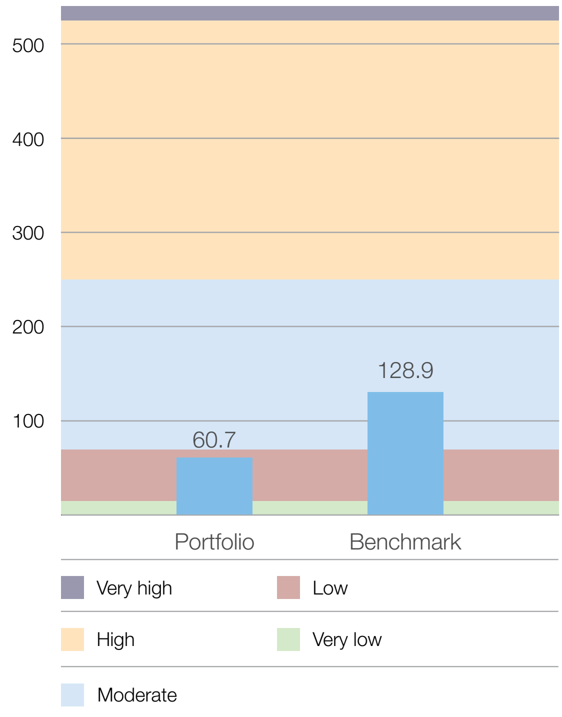
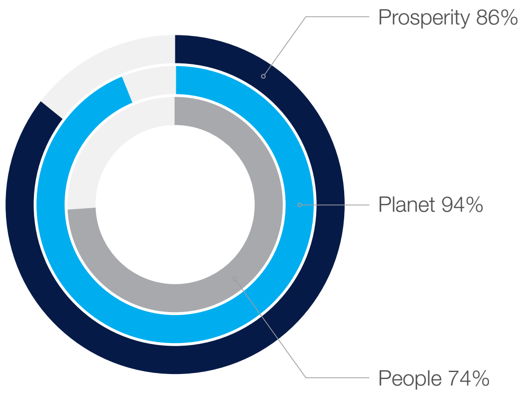
(2) Scope 2: Indirect GHG emissions that occur from the generation of purchased electricity, steam or heat consumed by the company.

Benchmark for comparison: 100% Global equity

Carbon Intensity vs Benchmark (TCO2e / $m sales)



SDG Alignment



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Prosperity | **Planet** | **People**

Sustainable Managed Portfolio Service

Annual report – 2023

Sustainability at RBC Brewin Dolphin

Sustainability is relevant to everything we do, from being a responsible business and corporate citizen to the way we invest. At RBC Brewin Dolphin, we think of sustainability in terms of three pillars:

Responsible investment	Stewardship	Responsible business
Ensuring that we offer clients the right responsible investment choices for them	Ensuring responsible ownership of the assets we hold for clients	Ensuring we are a company that seeks to have a positive impact on society

Looking forward to the year ahead, we are excited about our plans at RBC Brewin Dolphin and developments in the world of sustainable investment.

November 2023 saw the long-awaited announcement about the FCA's Sustainable Disclosure Requirements (SDR). Asset managers will be able to use the labels from July 2024, and we are looking forward to the clarity that these will bring to the market. We are expecting more details later in 2024 on how SDR and the labelling regime will directly apply to wealth management firms and managed portfolio services, and will then assess implications for our offerings. The anti-greenwashing rule, which focuses on misleading messaging and unsubstantiated claims relating to ESG and sustainability, is expected to apply from May 2024. We welcome this regulation, which we believe will create a level playing field.

A critical year for climate change

2024 will also be a critical year for climate change, and possibly the year that greenhouse gas (GHG) emissions start to decline. We are looking forward to seeing how national governments change rules and policies based the UAE Consensus, agreed at COP28 in Dubai in December 2023. Risks and opportunities related to climate change will remain a key consideration for our managers as part of their ESG integration processes.

Stewardship through partnership

From a stewardship perspective, we believe that partnering with other aligned investors is a powerful way of influencing companies, regulators, and policymakers on priority issues. By joining forces with other investors with the same objective, we can increase our chances of securing a positive outcome. Through our engagement partnership with Columbia Threadneedle reo©, and as members of Climate Action 100+ and Nature Action 100, we plan on continuing our collaborative engagement work in the climate and nature space.

Evolving our approach to responsible investment

We will also continue to evolve our approach to responsible investment over the next 12 months. We are planning on submitting a fourth application to continue as a signatory of the Financial Reporting Council's Stewardship Code and expect to receive our United Nations Principles for Responsible Investment (UN PRI) scores in early 2024. Lastly, we expect to see proposals from the UK Treasury on regulating ESG ratings agencies. We welcome this initiative, which we hope will lead to greater consistency and transparency from data providers.

In terms of our own operations, we will continue efforts to reduce our operational emissions, which are aligned with RBC's commitments to reduce GHG emissions by 70% by 2025, and to increase sourcing of electricity from renewable and non-emitting sources to 100% by 2025. In 2022, RBC's emissions were 58% less than in 2018, and 90% of our global electricity consumption came from renewable and non-emitting sources.

Tom Blathwayt
Head of Sustainability

Stewardship

Stewardship is a core part of our Sustainable MPS service. Our team selects funds that are industry leaders in integrating ESG factors into investment decisions and in stewardship. We believe fund managers that act as responsible owners, or good stewards, of our clients' assets can help maximise positive outcomes by encouraging better behaviour from investee companies.

We take the time to fully assess stewardship capabilities at the fund selection stage and on an ongoing basis actively monitor their stewardship work. One aspect of this approach is through controversy tracking. We continually scan news flow for controversies in the companies to which we are indirectly exposed. When these arise, we assess specific issues and, if significant enough, reach out to our fund managers that hold the company in question to understand how they are monitoring and engaging on these issues, and the effect on their investment decisions.

Our controversy tracking philosophy

Real-time analysis of ESG leadership

- ESG leadership is often assessed by a collection of factors, such as policies, reporting or committees. However, we believe that you only truly know how a company treats stakeholders when controversies emerge.
- We evaluate a fund's ESG integration predominantly by analysing its past investment actions. Monitoring their response to corporate controversies can build evidence or provide challenge to our conclusions.

Monitor funds' stewardship processes

- Our controversy tracking process allows us to monitor their activities as they are happening, as well as the initial due diligence we undertake with each fund.
- We will escalate matters within a fund house where we feel their engagement is not of a sufficient standard.

Throughout the year, our process highlighted 11 controversies that we felt warranted further engagement. In total, we made contact 86 times with fund managers to confirm their awareness of the issue, rationale for continuing to hold the company in question, engagement efforts and next steps. Through this process, not only do we encourage better outcomes for the underlying companies, but we also effectively monitor funds' ESG and stewardship processes. Should responses by unsatisfactory, we will not hesitate to escalate within the fund house.

Case study: Insulin drug prices

Many responsible investors consider access to medicine important. This subject, like many others that fall into the 's for social' of ESG, has likely been exacerbated by the Covid-19 pandemic and the increased attention vaccine makers received. With everyday costs, including medication, rising rapidly and trust in the pharmaceutical industry at historic lows, in the early part of the year the states of California and Kansas sued pharmaceutical companies for violating competition law to raise insulin prices.

The discovery of insulin won a Nobel prize 100 years ago, and synthetic insulin has been marketed since 1982. As an old drug with little new R&D investment required, lawmakers claim the 'skyrocketing' prices cannot be justified. With a complicated and expensive healthcare system and only a segment of the population benefiting from the Medicare price cap at $35 per month, up to 20% of diabetics in the US claim to ration their insulin to keep costs down.

We reached out to around 20 fund managers flagged as owning companies facing this legal action. Many of them have already engaged directly with the affected companies. The responses we received were detailed and considered, citing the complexity of the US healthcare system and diabetes-specific factors such as chronicity. Some noted that certain impacted companies are actually very active in insulin affordability programmes.

Most managers noted the lawsuit has so far provided no tangible evidence to suggest material financial or reputational risk to the companies and highlighted that insulin prices have in fact remained static over the past five years. This differing of opinion is due to the complex system of prices and rebates in the US.

In summary, we feel comfortable that fund managers are aware of the issues and have been engaging proactively with their investee companies. The lawsuit is still ongoing, with more states suing the companies and a potential settlement of $13.5m from one company being rejected.

Alongside our controversy tracking process, we have undertaken engagement campaigns with our fund managers on more systemic issues that we believe have the potential to pose a risk to our clients' assets, as well as the clear environmental and social risks. We wanted to understand how they view their holdings' exposure to forced labour allegations in Xinjiang, China, and non-alignment with the goals of the Paris Agreement.

Case study: Forced labour in supply chains

In 2023 we launched a programme of engagement with our fund managers based on allegations of forced labour of the ethnic minority Uyghur population in the Xinjiang region of China.

A number of large companies, both in the West and in Asia, were flagged by MSCI, a provider of ESG data, as being exposed to this issue. Considering the indirect exposure we have to these companies, we reached out to the relevant fund managers to understand their views on this important but complex situation.

While this work is ongoing, initial responses have highlighted challenges with oversight of supply chains and sensitivities around company disclosures. While there is indeed a fair level of complexity and opacity across certain supply chains, there is also an increased recognition of the material effect that supply chain issues can have on businesses and a heightened regulatory focus on companies' obligations to ensure that the right due diligence is applied.

The protection of human rights is one of our stewardship priorities at RBC Brewin Dolphin and we believe that management of supply chains plays a key part in addressing related risks, reputational risk being one of many. We therefore plan to continue our work on this important issue in the year ahead.

Case study: TPI

For the third year, we have engaged with our fund managers regarding their exposure to companies unaligned with the goals of the Paris Agreement, as flagged by the Transition Pathway Initiative. The Paris Agreement targets keeping global temperature rises to 1.5°c to avoid the worst effects of climate change. The TPI is a global, asset owner-led initiative which assesses companies' preparedness for the transition to a low carbon economy. Using this data, we reached out to 44 fund houses, covering 103 funds including some within Sustainable MPS, which hold approximately 96 companies showing as non-aligned.

We asked managers to comment on how they have assessed the attempts of these companies to reduce emissions and the financial implications of failing to comply with global pledges. We also wanted to understand any engagements that had been undertaken, including group initiatives and commitments. Furthermore, we wanted to see their assessment of company progress since our last TPI engagement and how the fund has used their votes to hold companies accountable. We are continuing to fully assess and grade the replies we have had, but our initial impressions are of thoughtful responses with clear processes to assess and engage on climate risks. We will be engaging further with any fund managers who we feel need to improve upon their processes with regards to managing climate related risks.

Kelly Eva
Stewardship

Sustainable MPS annual market overview 2023

- The stock market concluded 2023 on a high note, providing strong returns to investors. Despite the assumption that cash would reign supreme, stocks emerged as the best performing major asset class, surpassing the returns from the highest yielding bank accounts. North America lead the way with an impressive 18.8% return, followed by Developed Europe excluding UK at 14.4%, and Japan at 13.3%.
- Bonds, after a challenging start, ended the year strongly in anticipation of interest rate cuts in 2024, which led investors to flock to bonds to secure the relatively high yields on offer. UK Corporate Bonds had a particularly strong year, returning 9.7%, as did Global Corporate Bonds, returning 7.9%.
- The year was more favorable for investors compared to 2022, which saw most investments struggle due to a sharp increase in inflation.
- Inflation trended downwards in 2023, particularly in the UK, driven by a decrease in commodity prices, notably both oil and natural gas. Lower energy prices were beneficial for consumers and most businesses. Governments, recognising the impact of rapidly changing energy prices, implemented measures to mitigate their effects. We have seen a steady normalisation from the disruptions to supply chains that were a major source of inflation in 2022.
- The lack of demand from China, which continues to struggle economically, has helped the rest of the world on the path to inflationary salvation.
- The rapid decline in cost-driven inflation across 2023, coupled with sharp pay increases for lower income cohorts, means many consumers are now seeing their pay outpace price increases. This will enable them to spend or save more.
- The emergence of artificial intelligence (AI) was a positive catalyst for markets as investors antcipate it acting as a major growth driver for the global economy beyond 2023, with the potential to reduce inflationary pressure and enable companies to deliver their services more cheaply.
- The performance of alternatives was also positive, with gold returning 8% and Absolute Return at 4.8%. Gold continued its impressive performance throughout the year, despite generally weak commodity prices. Even property was positive despite challenges, returning 5.1%.
- Overall, 2023 was a more favorable year for investors compared to 2022, with invested assets providing positive returns.

Sustainable MPS highlights 2023

Asset Allocation

What worked and why?

The underweight position to property and to bonds have been positive for excess performance.

What didn't work and why?

Given risk assets strong run, the overweight to Cash has represented a drag to excess performance.

Fund Selection

What worked and why?

With technology names capturing investor interest on the back of the potential of artifical intelligence (AI), it was the growth style managers that delivered the strongest performance in 2023. Liontrust Sustainable Future US Growth was the strongest contributor with Royal London Sustainable Leaders also positive over the year.

What didn't work and why?

After being the top contributor last year, Schroders Global Energy Transition fund was the most significant detractor in 2023 as renewable energy stocks found their margins under pressure due to rapidly rising cost inflation. NinetyOne Global Environment and Pictet Environmental Opportunities were also detractors for similar reasons, although to a lesser degree.

Sustainable MPS Portfolio changes 2023

Asset Allocation

Throughout the year, the Asset Allocation Committee took advantage of spikes in bond yields to add to bond exposure. In January, it increased the allocation to UK gilts and global inflation-linked bonds by 0.5% each, funded by a reduction in cash and absolute return. In March, the Committee maintained a small underweight to equities but neutralised regional tilts due to uncertainty in markets. In May, it increased the allocation to UK gilts and made small adjustments to the regional equity allocation. In July, an increase in fixed income was offset by a decrease in absolute return exposure. The Committee added 0.5% each to global sovereigns and inflation-linked bonds, and rotated 0.5% from global credit into UK credit. In October, it increased UK gilts and Inflation-linked bonds by 0.5% each, funded by absolute return and cash. As the likelihood of a soft-landing appeared to increase, in December, it increased exposure to equities by 0.5%, funded by reducing absolute return, and boosted the US weighting by 0.5%.

Fund Selection

Over Q1, the portfolio weightings in Brown Advisory US Sustainable Growth, Robeco Global Credits SDG Fund and the ASI Global Government Bond Tracker funds were all increased. These were funded through reductions in TB Evenlode Income, Royal London Sustainable Leaders, Royal London Ethical Bond and BNY Mellon Sustainable Global Dynamic Bond funds.

In Q2, we reduced exposure to BNY Mellon Sustainable Global Dynamic Bond, increasing portfolio exposure to Muzinich Global Tactical Credit and L&G All Stocks Gilt Index Trust.

Q3 saw the introduction of two new funds to the portfolios, Trium ESG Emissions Improvers and Liontrust Sustainable Future US Growth. The Trium fund and an increase in ASI Global Government Bond Tracker were funded by reducing the allocations from Muzinich Global Tactical Credit and BNY Mellon Sustainable Global Dynamic Bond. The Liontrust fund was a direct replacement for its 'sister' Liontrust Sustainable Future Global Growth and a reduction to Brown Advisory US Sustainable Growth. There was a tweak to the credit exposure within portfolios to Royal London Ethical Bond by reducing RobecoSAM Global SDG Credits.

Q4 also saw the addition of a new fund into the portfolios; Schroder Global Sustainable Value, which was funded from reductions to Brown Advisory US Sustainable Growth, TB Evenlode Income and CT Responsible Global Equity. The L&G All Stocks Gilt Index and L&G Global Inflation Linked Bond Fund were increased whilst the allocation to BNY Mellon Sustainable Global Dynamic Bond and Blackrock ICS Sterling Liquidity were reduced.

Inpactful companies

Many of the companies held within RBC Brewin Dolphin's Sustainable Model Portfolio Service are driving the transition towards a more sustainable economy. Our clients' investment in these companies indirectly supports them in their ongoing expansion. So, we have picked a few highlights to demonstrate some of the amazing things that are happening under the bonnet of the portfolios:

Alignment to supporting the Planet

Eaton – held by Pictet Global Environmental Opportunities

Eaton is an intelligent power management company that provides energy efficient products, technology and services to assist customers in managing electrical and mechanical power more reliably, safely, and sustainably. It operates across five business segments: Electrical Americas, Electrical Global, Aerospace, Vehicle, and E-Mobility. It has shown its commitment to providing cleaner technology solutions, particularly through its investments in research and development, which are targeted to reach $3bn by 2030. Much of this is being deployed towards developing products and technologies that are critical to managing the complexity of an accelerating energy transition.

Eaton is well positioned to take advantage of: (1) electrification, the energy transition and changing grid; and (2) the explosive rise of digitalisation, and the interconnectivity of products and systems. Eaton is responding to these trends by innovating solutions that transform the electrical power value chain, investing in electrical vehicle markets, increasing focus on electrification, and employing digital technologies for power management.

The company is using its "design for the environment" and "everything as a grid" approaches to reduce the overall impact of products and solutions across their lifecycle. Its long-term ambition is for 75% of its products to help with climate change mitigation or adaptation by 2050.

Cadence Design Systems - held by Brown Advisory US Sustainable Growth and Liontrust Sustainable Future US Growth

Cadence Design Systems offers software and tools that support the design and verification of increasingly complex semiconductor chips, printed circuit boards, and integrated systems. Its technologies enable the creation of electronic products that optimise energy usage by addressing all aspects of power management. Cadence's solutions help solve two key issues that arise as semi-conductor chips become smaller, more condensed, and more complex: wasted energy, which can lead to shorter battery life; and excess heat, which can lead to poor reliability and shorter product lifespans. The company's software and tools play a vital role in driving sustainability innovations in various end-market applications. For example, electronic design automation (EDA) technology is crucial in the design of the advanced chips that power electric vehicles.

Alignment to supporting people

Cochlear LTD – Stewart Asia Pacific Leaders Sustainability

Cochlear is the leader in implantable hearing solutions, connecting hundreds of thousands of people globally to a life full of hearing by providing a range of implants and sound processor upgrades. The company has a 60% global market share, which has been achieved through consistent investment in research and development to keep its devices at the forefront of technological innovation. It has built a portfolio of more than 1,700 patents.

Over the past 40 years, Cochlear has provided more than 750,000 implant devices to people who benefit from its implantable solutions. In 2023, the company developed its Responsible Supply Chain Action Plan that aims to drive continuous improvement across the supply chain, with a focus on human rights, labour practices, corporate governance, safety and well-being, and environmental sustainability.

Manpower Inc – held by Schroders Global Sustainable Value

Manpower is a US recruitment company connecting job seekers and employers with a focus on increasing access to employment. It provides career development programmes aimed at closing the gender skills gap and upskilling underserved populations. For example, Manpower has reskilled and provided language training to more than 20,000 refugees in the last five years. Using artificial intelligence (AI), it is working on improving the inclusiveness of hiring and removing human biases. As a staffing company, it is in possession of significant customer data but has strong data security processes in place to protect this. Manpower has low exposure to environmental risks but is committed to reaching net zero by 2045 or sooner, and was the first company in the industry to have validated science-based net zero targets.

Alignment to supporting prosperity

Wise PLC – held by Liontrust Future UK Growth

Wise PLC is a money transfer business whose mission is to bring transparency and fairness into moving money around the world securely. This covers pricing of products and sharing the economies of scale. Its mission is to bring foreign exchange costs down to zero. A resilient financial system helps to support all in society. Liontrust looks for businesses that dramatically improve access to financial services and reduce the costs for all. 1.7 billion people remain unbanked in the world. Traditionally, foreign exchange has been very costly for individuals, especially those remitting small amounts regularly; Wise offers a significantly better rate, lower fees, and very simple app-based approach alongside security. Offering better rates is not just about having more to spend on your holiday. For migrant labour, the typical 6% charge to remit earnings has a very real impact on household spending. Wise can reduce this by an average 60%.

Swiss Re – held in RobecoSAM Global SDG Credits

Swiss Re AG offers reinsurance, insurance, and insurance-linked financial market products – including automobile, liability, accident, engineering, marine, aviation, life, and health insurance. The company also manages fixed-income and equity investments for itself and other insurance companies. It contributes to a sustainable economy through the reduction of risk and the mitigation of financial impact for the policy holder, thereby producing a safety net for people and businesses in times of catastrophe. It also contributes to a sustainable economy through the adoption of more responsible investment policies. Robeco believe this business is proactive in understanding and managing climate risks

Tom Buffham
Portfolio Analyst

Asset Allocation Committee investment outlook

These views are implemented across our portfolios but there may be deviations where asset classes or suitable investments are unavailable or excluded.

Cash

We remain overweight. Cash currently offers an attractive return and acts as dry powder that can be deployed when conditions for the riskier asset classes improve.

Bonds

With central banks now looking ahead to rate cuts, we maintain an overweight to government bonds. We remain underweight corporate bonds. Credit spreads are not sufficiently large to compensate for global economic growth risks, in our view.

Global Equities

Supportive of the global equity market is the resilience the economy has exhibited. Indeed, the probability of a US soft landing appears to have risen. Meanwhile, there is the potential for AI-related themes to push equity prices higher. The main headwinds are sentiment and positioning (on balance already bullish), the current stage of the economic cycle (late), US valuation metrics (high), and the returns available on competing assets such as cash (high). Weighing everything up, holding a tactical equity exposure broadly in line with one's strategic benchmark appears sensible.

Alternatives

Gold broke out to a new all-time high in USD terms late last year thanks to a weak dollar, strong central bank buying (particularly from China), and the recent decline in real bond yields. However, on a longer-term basis, the gold price appears stretched considering how much real bond yields have risen over the last couple years. In addition, after declining so violently, real yields probably don't have a lot further to fall, at least for now. Finally, sentiment toward gold had improved in recent months and is now clearly bullish, which should make further gains more difficult. Against this backdrop, we retain a neutral position. We remain underweight property. It is often the case that one corner of the economy and/or markets "breaks" in response to central bank rate hikes, and commercial real estate seems like a prime candidate to experience pain in this cycle. Fundamentals are particularly challenging in the office space, but those are offset by stronger fundamentals in other subsectors, such as datacentres.

UK Equities

The UK market is undeniably cheap and unloved. With that in mind, it might not need a lot of good fundamental news to outperform. However, the most important determinant of UK equity relative performance is global sector and style performance. Given its high weightings in value-oriented sectors like energy and financials, and low weightings in growth sectors such as tech, the UK equity market benefits strongly during periods when global value stocks outperform. The bad news is that the outlook for value appears uninspiring. The composition of the UK market also probably makes it a good hedge against an inflation problem. Cyclically, inflation pressures have moderated. The pound would be vulnerable to a decline if markets go back into risk off mode, and the odds of that happening seem elevated. A decline in the pound would create a headwind for UK equity relative performance in common currency terms.

US Equities

There are several concerns regarding the US relative performance outlook, with the big risk relating to valuation (including the valuation of the dollar). Notwithstanding the risks, we are more optimistic on US equities than other regions, for two main reasons. The first relates to the secular outlook, which appears relatively bright for the tech stocks the US is heavily weighted in. The main upside risk for the global equity market over the next few years is if an "AI boom" scenario unfolds. With the Federal Reserve now on hold and likely to begin cutting rates next year, a weaker version of the cycle that played out during the second half of the 1990s is a possibility today. Back then, excitement linked to the growth of the internet drove gains. This cycle, AI-related investment could be the driver. The US has much greater exposure to the "pick and shovel" plays positioned to benefit from an AI spending boom than any other region. The second reason for favouring the US relates to the cyclical outlook. Even though the odds of a soft landing have gone up, economic growth risks are still significantly higher than in any given year. The US is the most defensive of our six regions, which is an attractive characteristic at a time when growth risks remain elevated.

Europe ex-UK Equities

If we can predict where the relative performance of global tech and and continental European FX are going, we stand a good chance of predicting whether Europe ex-UK Equities will outperform. We are cautiously optimistic on the secular outlook for the global tech sector, which bodes poorly for Europe ex-UK as it has low weightings in this sector. With regards to continental European FX, over the longer term, there appears to be room for appreciation, which would support regional equity relative performance in common currency terms. The euro is cheaply valued, and existential risks have declined. However, over the medium term, FX direction will likely be more influenced by risk appetite. The euro is a risk-on currency, and odds of markets moving into a risk-off phase remain elevated.

Japan Equities

Shareholder-friendly reform momentum is building in Japan, which could help spark an expansion in relatively depressed price-to-book multiples. However, demographics amount to a major structural headwind to Japanese equity relative performance. Cyclically, Japan does not have much scope to put idle economic resources to work. Despite low price-to-book multiples, Japan does not stand out as obviously cheap vs the world ex US market, in our view.

Asia ex-Japan Equities

The Chinese authorities have continued to implement policies that negatively impact the profit outlook of its megacap companies, with new online gaming restrictions the latest high-profile measure announced. Meanwhile, incoming Chinese economic data continues to disappoint. Property remains a key area of weakness. House prices continue to contract, and residential floor space sold remains deep in negative territory on a y/y basis. Nevertheless, it is still not a bad bet that GDP in China and Asia ex Japan more widely outpaces that of the rest of the world this year. In addition, more investors have "thrown in the towel" on China. Despite this attractive combination of decent relative growth prospects and depressed investor sentiment, we are not optimistic with regards to Asia ex-Japan relative performance. China is becoming steadly less shareholder friendly. Geopolitics is likely to remain a headwind. High indebtedness and challenging demographics should act as longer-run economic headwinds in China.

Emerging markets ex-Asia Equities

EM ex Asia is undisputedly cheap, but there does not appear to be a catalyst on the horizon to unlock that value. Brazil, Saudi Arabia, South Africa, Mexico, and the UAE are the countries with the highest market cap weightings in the EM ex Asia equity index, making it very commodity exposed. We do not expect much upside to commodity prices in an environment where global growth is slowing and China refrains from large scale stimulus.

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