ISSUE 39 — FIRST QUARTER 2024

INVESTMENT INSIGHTS

THE MAGNIFICENT SEVEN

After driving markets higher over the past year, will the US tech superheroes ride to the rescue again in 2024?

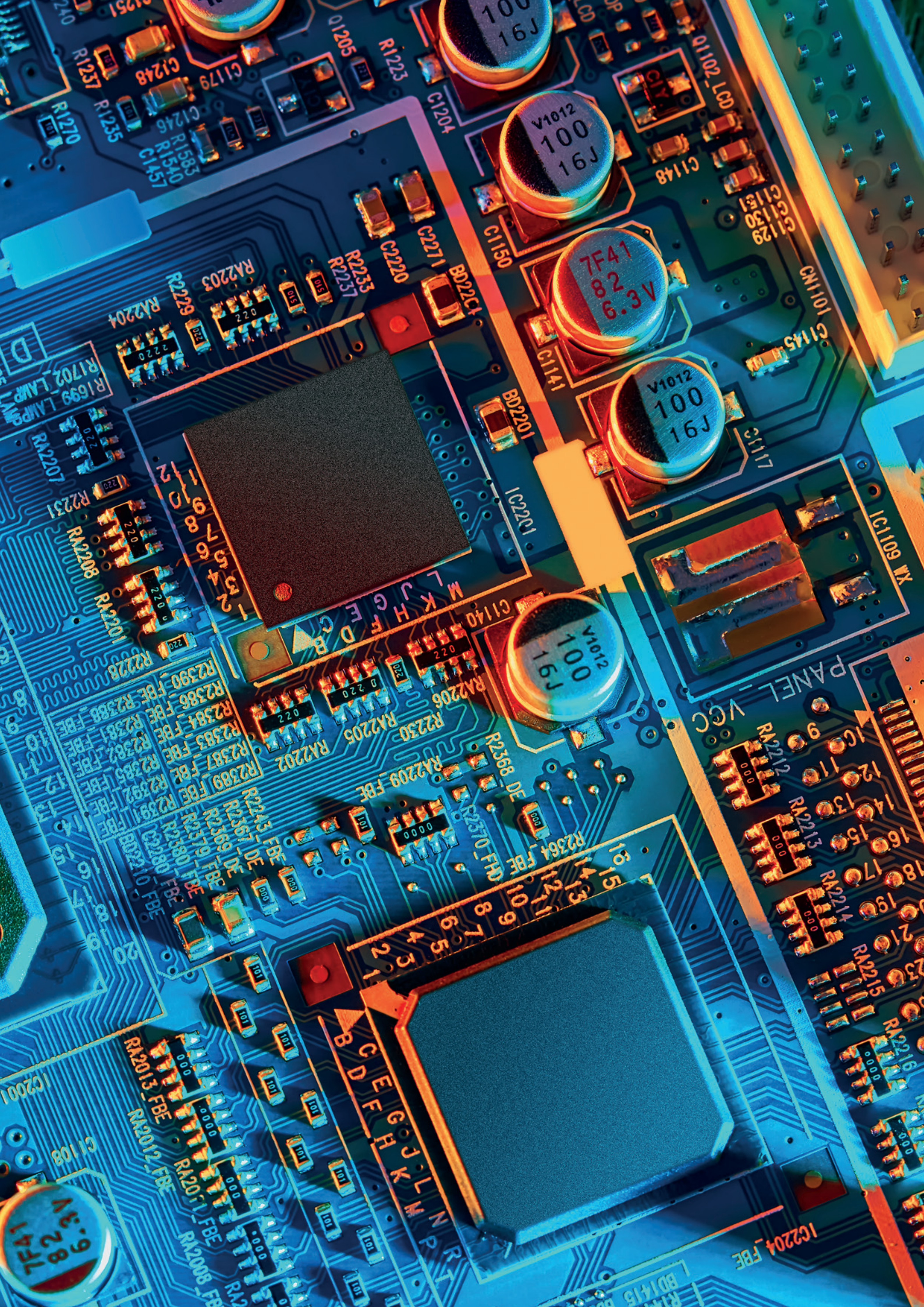
Higher for longer
Bonds should benefit from the new interest rate regime

Election fever
Markets could be unmoved by a busy year for voters

Return of the bull
Looking for opportunities when the economy recovers

Reflecting on renewables
The transition to clean power depends on energy market reforms

RATHBONES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FOREWORD

Investment Insights webinar with Q&A
Join our next webinar on Tuesday 16 January, from 12.00 to 12.30, to hear our latest thoughts on the investment outlook and opportunities. Visit https://registration.duuzra.com/form/investmentinsights16Jan24 to register.

Welcome to the latest issue of *Investment Insights*, and we hope it finds you well after the holidays. As we start the new year, we begin by looking at the tech companies known as the Magnificent Seven. Will these superheroes save the day again in 2024? Their stellar performance is partly a rebound from the precipitous declines of 2022. They've been able to continue growing while the wider market stutters, and we look at why the case for them to drive superior earnings growth long into the future remains compelling.

Our second article on page 6 explores interest rates. The financial press has been full of talk about them staying higher for longer. We agree rates are likely to remain higher over the next decade than they were during the 2010s. But how high, and for how long, and how could your investments be affected?

On page 8 our third article asks what impact the big elections in 2024 will have on financial markets. More than half of the world's population is set to go to the ballot box in 76 elections in 2024. We'll be keeping a close eye on two contests that could cause investor angst – the US election in November and the UK election, which must take place by the end of January 2025.

Our next article on page 10 looks at the opportunities that could arise for investors as the global economy recovers. We're maintaining a cautious investment stance as we enter a new year, but also beginning to prepare for this eventual recovery. We've identified five triggers that would encourage us to turn more positive, but only need two of them to happen.

In our final article on page 12 we reflect on a torrid year for clean energy stocks in 2023, which were hammered by rising interest rates and surging costs of funding new projects. The world's ability to meet its net zero commitments will depend heavily on the proliferation of renewable energy infrastructure over the coming decades and beyond.

We hope you enjoy this issue and look forward to updating you in the coming months. We always welcome your questions about what's happening in the world today and how it affects your investments. If you'd like to find out more, please visit rathbones.com or contact your investment manager.

Liz Savage and Ed Smith
Co-chief investment officers

WILL THE TECH SUPERHEROES RIDE TO THE RESCUE AGAIN IN 2024?

"Dashing superheroes rescue distressed equity investors from the perils of rising interest rates" could be the headline for this year's lopsided stock market action. Dubbed the Magnificent Seven, a small group of companies – comprising Apple, Microsoft, Alphabet, Amazon, Nvidia, Meta and Tesla – have contributed more than half of the gain in the S&P 500 so far in 2023 (figure 1).

At the time of writing, their market capitalisation (the combined value of their outstanding shares) commanded 29% of the US market. Excluding these names, the remaining S&P 493 was up only 9%, struggling with sharp interest rate rises, cost inflation and weakening economies. Will the Magnificent Seven be able to maintain their superhero status and global domination?

This elite group shares a common thread – they embody the seemingly unstoppable rise of the technology sector, although a less charitable view might put Tesla with the traditional carmakers rather than whizzy software developers. Terms like FAANG (Facebook, Amazon, Apple, Nvidia and Google), Fang+, MAFANG, and MAMAAs have been coined over the past few years to encapsulate the influence these tech titans have on stock market returns.

Performance in context

Although this concentration was extreme in 2023, it needs to be viewed in context. In many ways, the Magnificent Seven's stellar performance is a rebound from the precipitous declines of 2022, when they were collectively down 40%. They accounted for almost as much of the S&P 500's decline last year as they did the gains in 2023 (figure 2 on page 5).

The Magnificent Seven haven't been the only protagonists in the tech sector's success story this year. Oracle, Adobe, Booking Holdings, and even UK-listed Sage have also delivered impressive returns, symbolising the broader ascendancy of the sector. While tech stocks command 40% of the US market and 27% of world indices, the pivotal question for investors is not what is driving the Magnificent Seven, but what explains the success of the tech sector in general?

No doubt some of the gains this year have been fuelled by hype around the potential for generative AI (exemplified by ChatGPT and other so-called large language models) to transform businesses and create lucrative new revenue streams.* We think the more important driver has been the recovery from oversold conditions in 2022. These outperforming tech companies, to varying degrees, have been able to continue growing while the wider market stutters – and the case for them to drive superior earnings growth long into the future remains compelling.

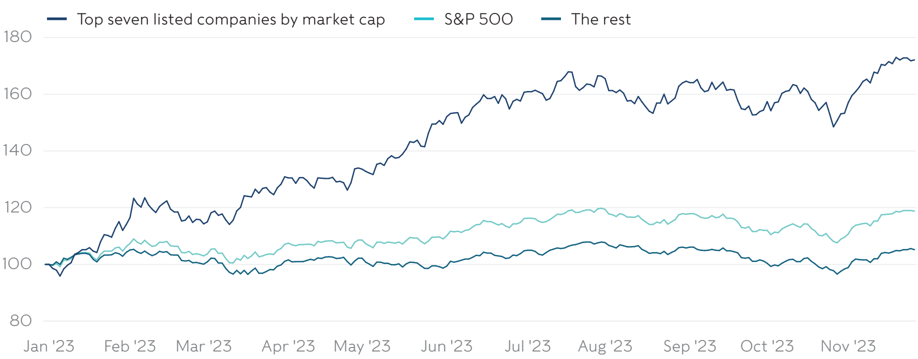
However, the sheer size of the Magnificent Seven demands special consideration. Apple and Microsoft boast market valuations greater than the entire UK stock market, making a view on these companies unavoidable for investors. To evaluate the sustainability of their performance, investors should eschew reliance on charts of share price performance and focus instead on business fundamentals and current valuations – the most reliable predictors of long-term equity returns in our view. Let's delve into each member of the Magnificent Seven.

Take a bite

Apple's revenues and operating profits have both fallen this year by 1% as demand was pulled forward during the pandemic when consumers in lockdown used excess savings to upgrade their iPhones. Given such soggy sales growth, it seems surprising that the shares have risen 52% this year, and are priced at 28 times expected 2024 earnings per share, a 25% premium to their five-year average. Apple's dominance in smartphones continues to increase, especially in emerging markets, and we expect it will return to 10%-plus profit growth next year. If Apple can deliver that growth, the shares are not expensive.

Microsoft trades at an even higher valuation of 30 times expected 2024 earnings, which is towards the higher end of its past range. Its partnership with OPENAI, despite the

Figure 1: Riding ahead
While the Magnificent Seven stocks (Apple, Microsoft, Alphabet, Amazon, Nvidia, Meta and Tesla) have performed strongly this year, the rest of the market has been relatively flat.
January 2023 = 100
Source: Refinitiv, Rathbones.



management turmoil over the past weeks, positions it as frontrunner in the race to develop generative AI services. One area we have a keen eye on is its cash generation, which is deteriorating across all the cloud providers. Yet with operating profits expected to grow 17% a year between 2024 and 2027, the shares still look attractive compared to other software stocks.

Meta trades on 20 times next year's forecasted earnings. This is a slight premium to the overall S&P 500 index, which has a price-to-earnings multiple (PE) of 19. Given Meta remains the preeminent force in social media, and its profit growth is expected to be significantly higher than the market average, it should be able to deliver market-beating returns.

Navigating new challenges

Google parent Alphabet trades on a similarly pedestrian PE multiple of 20, reflecting concerns about its maturing advertising business and potential disruption to its search business by ChatGPT. However, we think Alphabet has sufficiently deep pockets and expertise to navigate through whatever challenges and opportunities AI presents and view the valuation as compelling for a business that controls the gateway to the internet.

Ecommerce giant Amazon is trading on a much richer multiple of 41. While cheap compared with where it's traded in the past, it looks expensive against its tech brethren. Investors are betting that significant margin expansion in its ecommerce business will drive 30% annual profit growth in the years ahead, and foresee a decade of robust revenue growth ahead for its data centre division, AWS, as enterprise IT spend shifts into the cloud. This one admittedly requires more of a visionary outlook from investors to justify the valuation.

Given that Nvidia's shares are up 240% since the start of the year, you may be surprised to learn that its PE is a mere 25. Sales of the firm's GPU chips to data centres for AI applications have blown away analyst forecasts, and it appears to have a lock on the chips AI applications need. However, the company is not without risks. Major customers like Amazon and Alphabet are developing their own chips and demand for AI chips could drop just as quickly as it climbed if large commercial applications for generative AI fail to materialise. For now, given Nvidia's quasi-monopoly and enviable profit margins, it's one we are following with growing interest.

Tesla is the most expensively valued of the Magnificent Seven, trading at 67 times 2024 profit estimates. The carmarker faces challenges with falling profits and ambitious growth expectations. Its valuation hinges on realising autonomous driving software's potential and achieving substantial scale. Scepticism is warranted, but its colourful CEO Elon Musk has proven doubters wrong many times in the past.

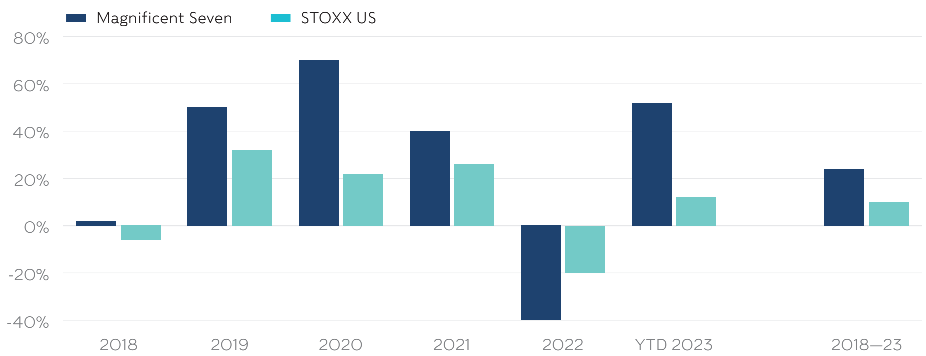
A regulatory caution

One note of caution is that big tech is in the cross-hairs of regulators – Nvidia in the form of chip export bans to China, Apple for the fees it charges on the app store, Alphabet for paying to be the default search option on the iPhone and Meta for its acquisition of Instagram in 2012. Negative developments on these fronts could erode the value of these businesses.

While four of the Magnificent Seven face regulatory risks, investors can still harbour a healthy appetite for these stocks. The broader question, however, extends beyond this group to whether the wider tech sector, with its colossal weight in indices, can continue outperforming. We believe conditions favouring technology companies will persist, including high returns on capital and structurally advantageous business models, and they will remain an important driver of equity returns. It doesn't have to be limited to the Magnificent Seven, but we expect more sequels from this band of superheroes.

All figures in this article are as of 1 December 2023.
* You can read more about generative AI in the previous two issues of Investment Insights, which are available online at ww.rathbones.com/insight/investment-insights

Figure 2: Annual returns since 2018
The Magnificent Seven have outperformed the broader US stock market in all but one of the past six years.
Source: Refinitiv, Rathbones.



BONDS SHOULD BENEFIT FROM THE NEW INTEREST RATE REGIME

The financial press has been full of talk about interest rates staying 'higher for longer' recently. However, this snappy phrase can obscure as much as it illuminates. Higher than what? How much higher, and for how much longer? The exact answers to these questions matter a lot for investors.

We agree that interest rates are likely to be higher over the next decade than they were during the 2010s. We set out our own view of why in the previous issue of *Investment Insights*. In short, we think several of the factors that pushed down inflation and interest rates in recent decades have now either faded or even shifted into reverse. They include globalisation, fiscal austerity and the need to rebuild household finances after the global financial crisis.

Consequently, we think advanced economies are in for greater inflation volatility and a higher average level of interest rates over the coming decade. Yet this is not a controversial view. After all, over the centuries of data the 2010s stand out as an anomaly – the lowest rates on record.

Precision matters
However, precision is important. Markets may be right that rates will stay higher than they did in the 2010s, but wrong about by how much. At present, market pricing suggests central banks will keep interest rates at current levels until mid-2024, and then cut them only gradually.

The Bank of England (BoE), for example, is only expected to take interest rates from 5.25% now to 4.00% by the end of 2025. As figure 3 shows, that would be a particularly gradual pace of cuts by historical standards, even though inflation has fallen quite quickly compared with previous cycles.

We think the risks are skewed towards the BoE cutting interest rates sooner, or to a greater extent, than that. After all, there are clear signs of higher rates affecting the economy. Inflation has fallen a long way (from a peak of 11.1% late last year to 4.6% in October) and there is convincing evidence that it will continue to ease in the next few months, particularly for food and other goods. Additionally, we've seen economic growth flatline in the third quarter of this year, while business surveys continue to paint a gloomy picture.

Wage growth is still strong, which means there is a risk of services sector inflation remaining higher. But a range of indicators suggest competition between firms for employees has eased, and the most up-to-date measures of wage growth are slowing too. These trends will probably continue as higher interest rates continue to be passed on to households and businesses.

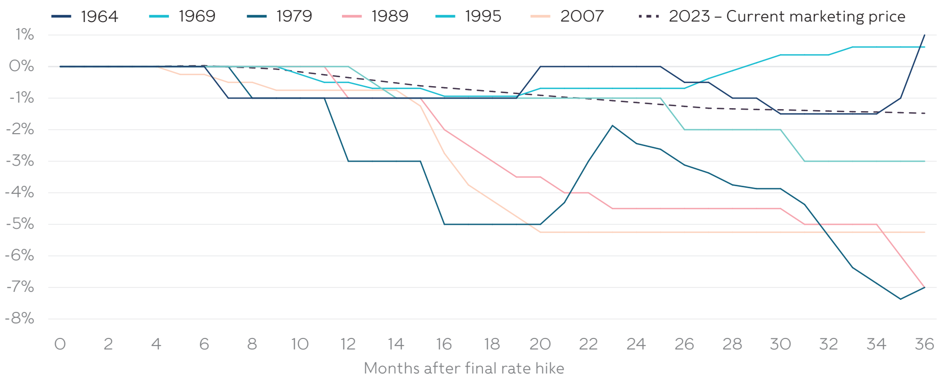
That view is still consistent with the post-pandemic regime being one of higher interest rates than the 2010s. Even if UK rates were cut twice as far as is currently discounted in financial markets over the next couple of years (to around 2.75%), that would still leave them a long way above the 0.10–0.75% range they occupied between 2009 and 2021.

Investment opportunities
We believe this presents opportunities in fixed income. Specifically, UK government bonds (gilts) look attractive, and they are likely to make up a larger share of our portfolios over the coming quarters as a result. If the Bank of England cuts interest rates sooner or by more than most expect, then gilts should rally.

Longer-dated gilts (those maturing further in the future), which tend to be more sensitive to changes in interest rates, are likely to benefit most. History suggests they perform better than shorter-dated bonds in the months around the Bank of England starting to cut interest rates.

On top of that, yields are starting from a higher, and therefore more attractive, point than they have for some time. For example, a gilt with a maturity of 10 years offered a yield below 1% between 2019 and 2021. Today it offers north of 4%. This gives us a greater margin for error. Even if interest rates come down more slowly than we expect, we may still achieve a moderate return from the yield alone.

Figure 3: Bank of England interest rate cutting cycles
This chart shows changes in the Bank of England's base rate in the three years following the final rate hike, alongside market expectations for rates over the next three years.
Source: Refinitiv, Rathbones.



MARKETS COULD BE UNMOVED BY A BUSY YEAR FOR VOTERS

More than half of the world's population is set to go to the ballot box in 76 elections in 2024, which will make it the biggest election year in history according to *The Economist*. We'll be keeping a close eye on two contests that may cause investors angst – the US Presidential election in November and UK election, which must take place by the end of January 2025.

Election analysis is often clouded by partisanship and emotion. As investors, we aim to take a dispassionate view by focusing on the fundamentals that matter most to markets. We can take some comfort from history, which shows elections don't tend to have a lasting impact on markets.

Governments on both sides of the Atlantic are in a tough spot, with the opposition ahead in the polls. In the UK, the Conservative Party has a mountain to climb to remain in power. Public opinion can change, and polls can misstate support – but usually only by so much. As figure 4 shows, we've never seen a swing in polls large enough to close the current gap between the two parties. A party ahead by over 10 points in the polls a year out from election day has never gone on to lose.

Too close to call

In the US, the race appears much closer than in the UK. Trump is out in front for the Republican nomination, while there is only negligible opposition to President Biden as the Democratic candidate. Things are therefore shaping up for a 2020 rematch, barring dramatic developments in the four criminal cases currently proceeding against Trump. The early polls pitting Trump against Biden show the former edging ahead. Key swing-state polls also have Biden trailing Trump.

People often have preconceived ideas of what different election results mean for markets. For example, plenty of commentary ahead of Trump's 2016 win suggested markets might react badly given his divisiveness, unpredictability and stances on various social issues. However, no such meltdown materialised, with markets ultimately caring more about the prospect of corporate tax cuts and looser fiscal policy (figure 5 on page 9).

Looking further back, it's hard to detect consistent patterns from past elections that stand up to statistical scrutiny. Our analysis suggests they rarely change market trends, which are typically determined by factors outside a government's control (like changes in the global economy or interest rates). In other words, we shouldn't lose sight of the bigger picture.

Political parties evolve, so looking to past cycles is limited. It makes more sense to assess each election on its own merits, comparing party plans on the key issues that matter to investors. We'll have much more to say as elections approach and we learn more about policy plans, but a few things stand out already.

Economic similarities

One surprising observation is the degree of similarity between the opposing parties on key economic issues. In the UK, the next election will offer voters a narrower choice than the 2019 contest. The Brexit issue has now largely been settled and, under Keir Starmer, the Labour Party has abandoned his predecessor's economic radicalism, declaring itself 'proudly pro-business'.

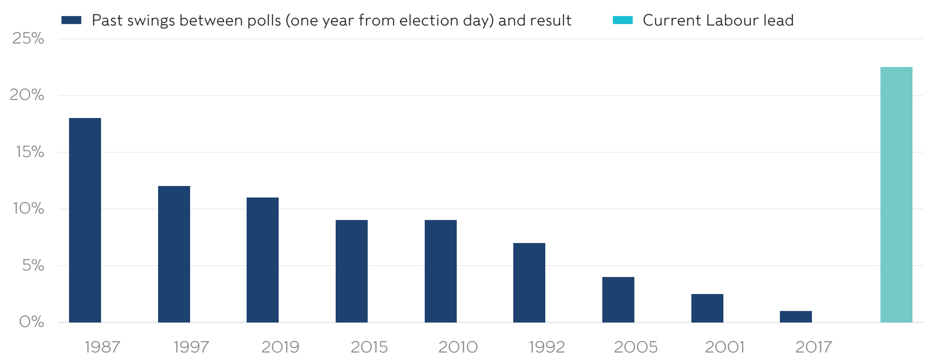
Most importantly for the near-term economic outlook, both parties have reiterated their commitment to strict fiscal rules following last year's 'mini budget' fiasco. That will limit their scope to make dramatic changes on taxation or spending (the Conservatives place more emphasis on lowering taxes, and Labour on activist industrial policy to support growth). The two parties are on common ground in other areas too – both have virtually identical targets to increase housebuilding.

Environmental policy is one area of divergence. Though Labour's 2021 Green Prosperity Plan has been scaled back due to fiscal constraints, Shadow Chancellor Rachel Reeves has ambitions to "ramp up" spending on green projects, which contrasts with the Conservatives' plans. Rishi Sunak announced a softening of the government's net zero policy, including delaying the ban on new diesel and petrol vehicles to 2035, and enhanced scrutiny on the costs of proposed environmental measures. (Read more about these issues on page 12.)

Figure 4: On course for victory

This chart shows the swing in past elections (from polls one year out from election date to election day result) compared with Labour's current lead in polls.

Source: PollBase, YouGov. Rathbones.



In the US, there is also a surprising degree of alignment on key economic policy issues. Biden has picked up the baton in Trump's trade war with China, for example, continuing the shift towards protectionism. We've also seen bipartisan support for various aspects of Biden's industrial policy, which focuses on domestic production, such as US semiconductor research and manufacturing, and for tougher antitrust policies.

Cutting corporate taxes was a flagship economic policy (and one that was welcomed by markets) during Trump's term as president. But there's no indication that he plans to do so again if he's re-elected, viewing the issue as settled. This time around, higher inflation and interest rates probably limit the scope of any President to loosen fiscal policy as Trump's tax reform did without an adverse market reaction.

Environmental differences

Otherwise, as in the UK, there's a stark difference between the two sides on the environment. The future of Biden's Inflation Reduction Act (IRA), which includes $369 billion in incentives for energy and climate programmes, looks uncertain. Trump, announced plans to cut a significant proportion of the IRA spending and increase investment in fossil fuels. During his term, Trump also focused on loosening environmental regulations, and withdrew from the Paris Agreement. Biden reversed this decision soon after taking office.

Banking regulation is another important area of contrast. In 2018, Trump introduced a major rollback of banking regulation, which reduced the oversight of small and midsize banks (including those such as Silicon Valley Bank and Signature Bank, which collapsed earlier this year). This is now being reversed under Biden following the turmoil we saw in March.

There are two further areas in which a Trump presidency could have consequences for markets. One is foreign policy, and specifically the issue of support for Ukraine. Trump has previously taken a softer line on Russia and complained about the cost of military aid to Ukraine. Many Republican congressmen and most Republican voters also believe the US is providing too much support. Developments in the conflict can affect global markets but it's hard to determine the impact of reduced US support. (You can read more about our views on geopolitical risks in our recent report *Peace of mind in a dangerous world*, which is available online at www.rathbones.com/peace-mind-dangerous-world.)

The other unpredictable area is the health of the domestic political system, following Trump's attempts to undermine the 2020 election. We don't know what changes he would make if he were to win again. Yet history suggests we should be careful of jumping to the conclusion that they would be a headwind for markets. They have a habit of looking through dramatic political events. As figure 5 shows , even the attacks on the Capitol in January 2021 failed to disrupt the pre-existing rally in US equities, which was fuelled by optimism about vaccines allowing the economy to bounce back from the pandemic.

Changing fortunes

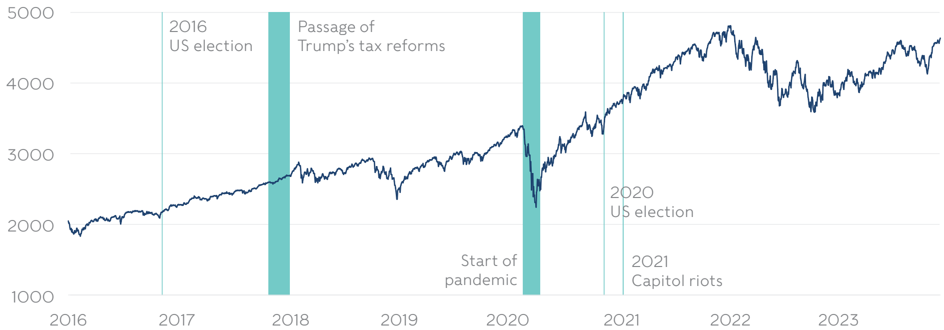
Changes in the fortunes of election candidates may be most visible within markets, specifically at the sectoral level. The starkest difference between incumbents and challengers on both sides of the Atlantic is probably on environmental policy, with the regulation of medium and small banks another schism in the US. We continue to monitor these and other policy areas and will be publishing a full report on the US and UK elections as greater details of candidates' positions emerges.

A key takeaway for investors is to avoid focusing on elections and remember the broader context. Neither election offers a choice between starkly different economic models, and the economic and market outlook for both will continue to be influenced by factors beyond either government's control. These include the ongoing weakness in the global economy and previous changes in interest rates which are still feeding through (both reasons why we're generally positioned cautiously). History suggests markets look through even the most dramatic political events, provided their direct economic implications are limited.

Figure 5: S&P 500 Index

Financial markets have tended to shrug off dramatic political events in the past and there's no reasons to doubt they will continue to do so in the year ahead.

Source: Refinitiv, Rathbones.



LOOKING FOR OPPORTUNITIES WHEN THE ECONOMY RECOVERS

We're maintaining a cautious investment stance as we enter a new year, but as we see recovery more clearly approaching we can begin to prepare for it. In recent publications we've identified five triggers that would encourage us to turn more positive, while also noting any two may be sufficient.

Of those potential triggers, an end to US interest rate increases seems likely to have happened and we believe a trough in leading global economic indicators is likely to happen soon. None of the others, having to do with attractive valuations, realistic estimates for company earnings and clear signs that investors have thrown in the towel, are close to fulfilment.

The US has made significant progress in bringing down inflation. There's also evidence that more disinflation is on the way, the labour market is loosening and the economy is likely to slow. Therefore, it seems likely that the US Federal Reserve has finished raising rates.

The US economy appears resilient and our global leading economic indicator (figure 6) has stabilised. Yet we're not confident it has bottomed out. The latest business surveys point to the eurozone and UK economies contracting, while China's housing market remains in a deep downturn with only limited policy support. There are also several reasons to expect the recent strength of the US economy to fade.

Preparing for a recovery

While we wait for a more definitive recovery to signal the ascendency of the 'bulls' over the 'bears', what can we do to prepare for the time when this second condition is met, and we turn more positive? Some parts of the global markets that would tend to do well in an economic rebound are looking cheap. They include smaller companies, sectors that are more dependent on broad economic strength and economically sensitive regions like developing markets.

Valuations of smaller company shares in particular are generally low compared with the past. However, we don't think this alone is a good reason to add more of them to portfolios — they could well get cheaper, given the continued risks to the economic outlook. Valuations alone have been a poor tool for timing entry points in the past. We still favour defensive stocks and sectors over the more cyclical, or economically sensitive, ones.

On a regional basis, Europe and developing markets have been the most cyclical, and have tended to be subject to larger moves up or down than the overall market (the technical description is 'high beta'). Relative to global equities, developing markets haven't done well for over 10 years, but there's value there now and some interesting long-term themes which may not be getting enough attention, such as the greening of emerging markets, the globalisation of services and the bifurcation of the trade in goods between US and Chinese axes. Japan and the US are two relatively defensive and low beta markets, and they've been among the best-performing regions over the past year.

We're working to identify specific investments in the more cyclical areas that we would consider attractively valued when leading indicators of the global economy bottom out. We're also looking at how we might increase our overall equity positioning, at the same time as we realign it towards more cyclical sectors, smaller stocks and more economically sensitive regions.

Looking for the rebound

Special situations funds could well be part of that mix too. They look for beaten down stocks with good catalysts for a rebound, and can perform particularly well when the global economy enters a recovery phase. This is the only part of the business cycle where stocks with weak recent profits, or low profits relative to their cost of debt, tend to outperform. Allocating to companies with management teams that are likely to turn things around after tough few years can benefit portfolios at this point in the cycle more than others.

Within bond markets, the higher returns now on offer from lower-quality high yield debt back may provide compelling risk-adjusted returns once we're a little further through the cycle of defaults that's only just beginning. They delivered better risk-adjusted returns than equities in the 2010s, the 2000s, the 1990s. We don't have good data for the 70s and 80s but lower-yielding investment grade bonds had better risk-adjusted returns than equities during those decades too. That's a lot of different monetary and economic regimes through which these types of bonds have been a useful addition to multi-asset portfolios.

We only need two of our five triggers to be met to turn more positive. We'll be keeping a close eye on that second one in particular in the months ahead, ready with our wish list of attractively valued assets that stand to benefit the most as the global economy recovers from what has been a difficult period.

THE TRANSITION TO CLEAN POWER DEPENDS ON ENERGY MARKET REFORMS

Over two years ago the cost of renewable power generation fell below the cheapest fossil fuel option. In the past year the International Energy Agency (IEA) estimated record-breaking new renewable electricity generation installations in 2023 and 2024. Yet renewable energy stocks endured another torrid year in 2023 – hammered by rising interest rates and surging costs of funding new projects. That's spurred our Stewardship team to use Rathbones' influence as a leading UK investor to prioritise working with the British government on energy market reform.

At the time of writing, the S&P Global Clean Energy Industry Index has fallen 28.4% since the start of 2023. By contrast, the S&P Global Mining & Energy Index has been flat over the same period (figure 6). Because renewable energy companies typically agree long-term contracts and fix the price at which they will sell energy before proceeding to develop projects, they have been hit especially hard as the Bank of England and other major central banks hiked interest rates. In the UK, it was reported that project costs for offshore wind developers rose 40% this year, with supply-chain challenges and uncertainty over grid connectivity compounding an already tough macroeconomic situation.

Committed to net zero

In October 2021, Rathbones publicly committed to achieving net zero carbon emissions across our operations and investment portfolios by 2050. Our ability to meet this commitment will depend heavily on the proliferation of renewable energy infrastructure, globally, over the coming decades and beyond. Given the challenges facing the clean energy industry, local policy environments will need to be as supportive of the deployment of renewable energy infrastructure as possible if industry is going to be able to attract the capital it needs to grow at the pace required to reduce net carbon emissions to zero.

China has thrown its weight behind policy measures intended to secure its position as the global supply-chain leader in clean technology. Earlier this year, following in the footsteps of the US Inflation Reduction Act – which included subsidies of $369bn for US green infrastructure projects – the European Commission announced updates to its European Green Deal, with the rollout of the Green Deal Industrial Plan. Meanwhile, in the absence of a similar policy response, the UK has fallen from fourth to seventh in terms of its attractiveness to clean tech investors.

With this in mind, we've made energy market reform a priority area for our stewardship activities in 2024. Rathbones was a signatory to a letter from a broad mix of investors, companies, industry groups and academics addressed to the Department of Energy Security and Net Zero, written in anticipation of the long-awaited Energy Bill becoming an act of parliament in October 2023. The letter praised the government for its decision to hand Ofgem – the UK's regulator for gas and electricity markets – a statutory net zero mandate as part of the Act.

Tackling climate change

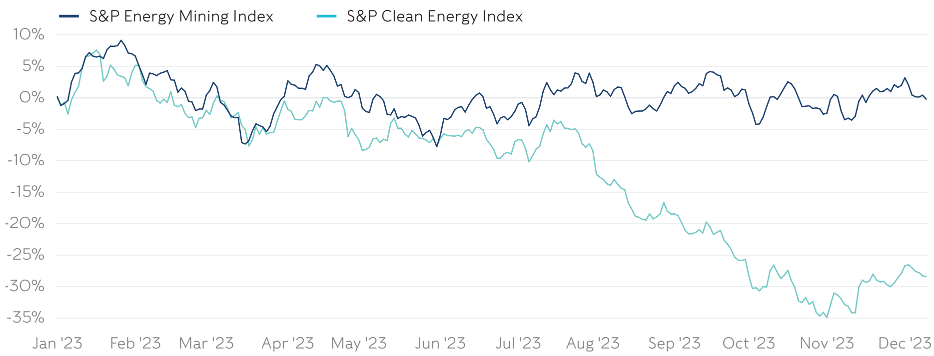
It also urged the government to move quickly to ensure that Ofgem is equipped with the resources and technical expertise required to deliver on this new mandate.

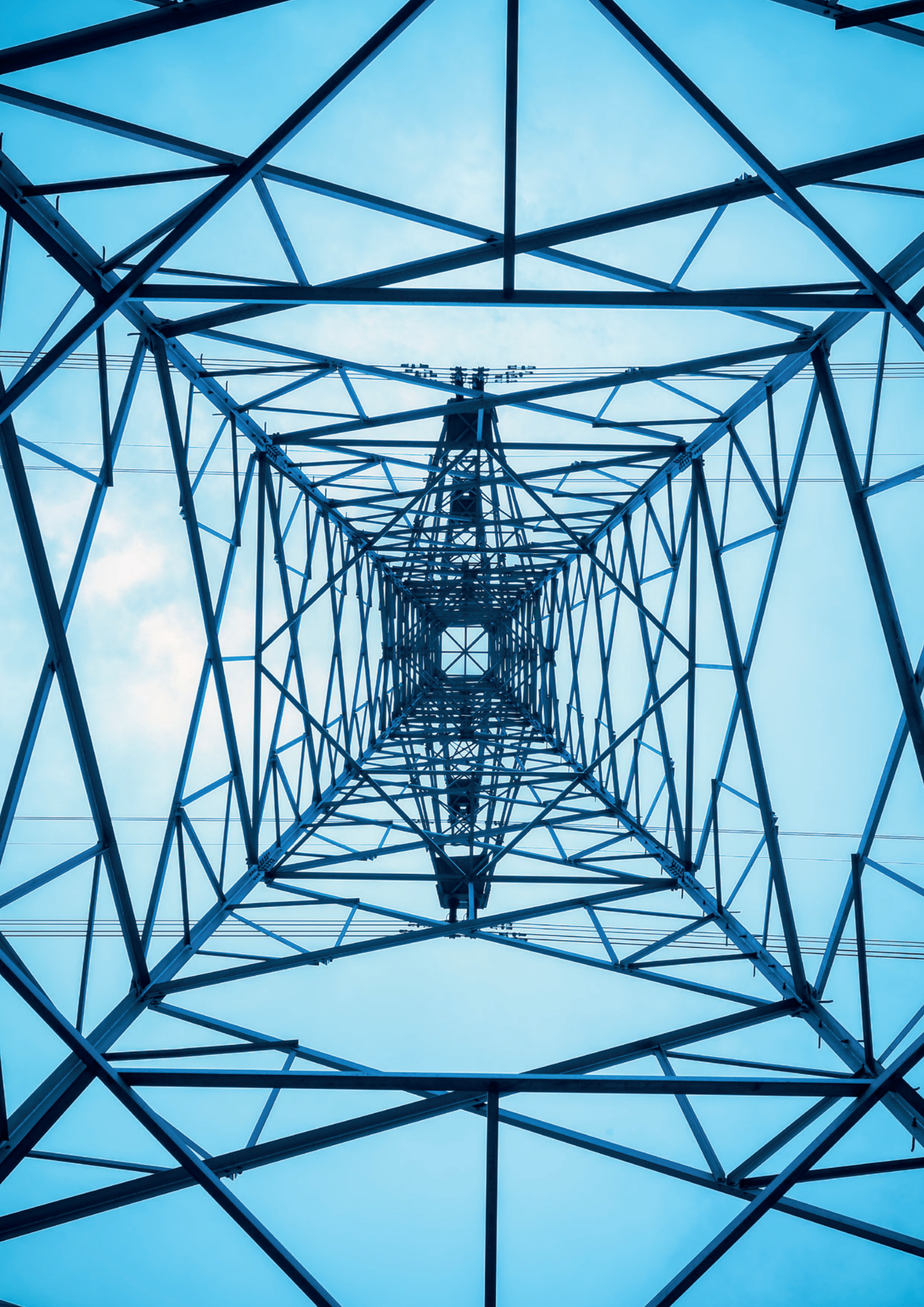
As we move into 2024, we expect that what have so far been broad discussions around the UK government's direction of travel on net zero will become more focussed and specific. In Chancellor Jeremy Hunt's most recent Autumn Statement welcome measures were introduced to give the electricity system operator (ESO) powers to address grid connectivity backlogs. However, a number of proposed reforms around locational electricity pricing and the decoupling of renewables pricing from gas in the wholesale electricity market, to name but a few, still need to be tackled.

We intend to work with whichever political party is in power following the next general election in the UK to ensure that the policy environment is as conducive as possible to continued investment in the infrastructure and technologies needed to drive us towards net zero.

Figure 6: Falling behind

Clean energy stocks have underperformed the mining and energy sector substantially over the past year.
January 2023 = 0
Source: Refinitiv, Rathbones as of 15 December 2023





FINANCIAL MARKETS

With inflation easing, there were signs that major central banks have probably finished raising rates. The US Federal Reserve (Fed) held its benchmark interest rate steady, although left the door open for further rises amid evidence that the US economy remains strong. So far it has been more resilient than expected, with low unemployment boosting hopes of a 'soft landing' for the economy next year, rather than a recession.

High interest rates and soaring bond yields rattled market nerves at the beginning of the period, with long-term US government bond yields reaching levels not witnessed in 15 years or more. The surge in bond yields (meaning that prices fell) hit everything from real estate to equities.

Bouncing back

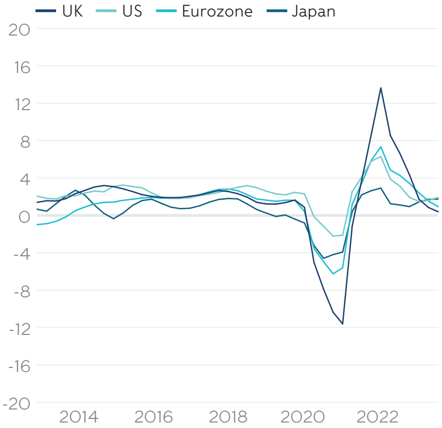
Equity and bond markets bounced back strongly in November, driven by weaker-than-expected job creation and the belief that the Fed has stopped raising interest rates. The Fed and the Bank of England both left interest rates unchanged in their December meetings, providing broad hints we have now reached the peak of the current rate hiking cycle.

Major stock market indexes like the S&P 500 and Nasdaq posted their best monthly gains in over three years in November. Gains were compounded on the news of lower-than-expected inflation. The market rally continued into December, with the S&P 500 hitting a high for the year.

Markets were largely unaffected by tragic events unfolding in the Middle East, although oil prices rose modestly amid ongoing concerns renewed geopolitical tensions could disrupt the region's oil supply. Despite the general advances in global stocks over the quarter, Asia-Pacific markets dipped amid mixed economic data from across the region.

GDP growth

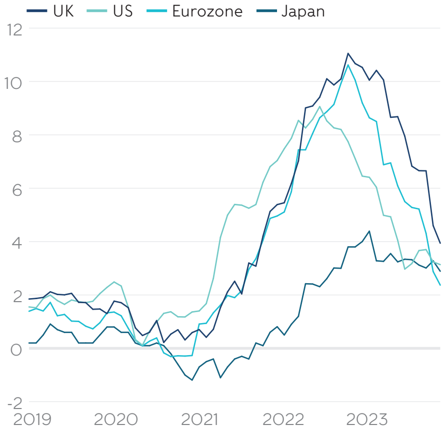
Annual change (%)



Source: Factset and Rathbones.

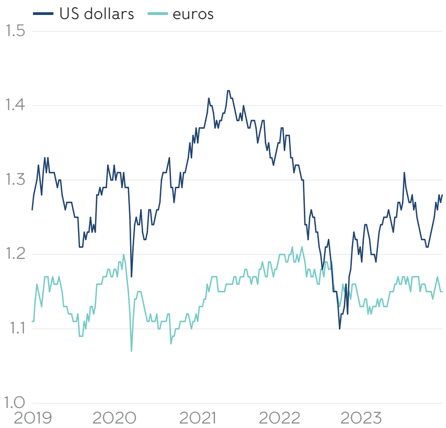
Inflation

Annual change (%)



Source: Factset and Rathbones.

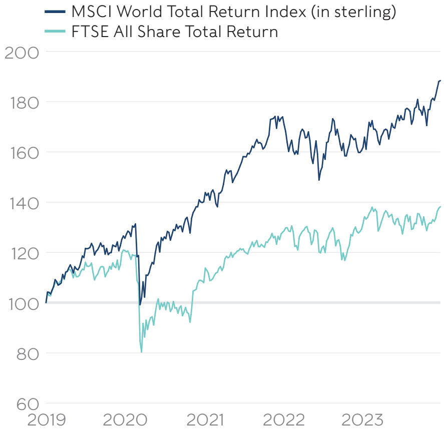
Sterling



Source: Factset and Rathbones.

Equities

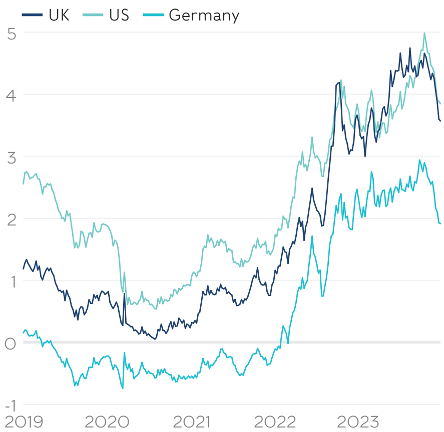
December 2018 = 100



Source: Factset and Rathbones.

Government bonds

10-year yields (%)



Source: Factset and Rathbones.

Gold

US dollars per troy ounce

Source: Factset and Rathbones.

Past performance is not a reliable indicator of future performance.

ADDITIONAL INFORMATION

Information valid at 31 December 2023, unless otherwise indicated. This document and the information within it does not constitute investment research or a research recommendation. The value of investments and the income generated by them can go down as well as up.

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Visit
rathbones.com

Email
enquiries@rathbones.com

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Greenbank
0117 930 3000
enquiries@greenbankinvestments.com
greenbankinvestments.com

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Rathbones Investment Management International
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