SARASIN
& PARTNERS

Q4 2024
HOUSE REPORT

A MULTIPOLAR WORLD

Markets holding firm amid geopolitical shifts

- Semiconductors: Investing in an AI future
- Charity focus: Impact, sustainability and social investments
- Investing for a new generation of global citizens

This document is intended for retail investors. You should not act or rely on this document but should contact your professional adviser.

INTRODUCTION

STEPHEN ROTHWELL
EDITOR

Welcome to the latest edition of our House Report.

Into the final stretch of 2024, and it has so far been a year in which the news, when not focused on elections around the world, has been dominated, sadly, by conflict. While our thoughts first and foremost are of the humanitarian impact, it is surprising to note that markets have so far remained remarkably resilient in the face of events in the Middle East and Eastern Europe. However, wider shifts in global leadership, with the US and China jostling for position and influence, are likely to play a big part in recalibrating both the risks and opportunities in financial markets.

We discuss some of these influences in two articles this month. Firstly, Guy Monson focuses on the disconnect between the markets and geopolitical events in his lead article, 'Defying Crisis'. Equities, bonds, and commodities all delivered unexpectedly strong returns in the third quarter of the year - how long can this continue with such a challenging backdrop? The real focus points for investors, he finds, have been the remarkable 'soft landing' of the US economy, lower inflation globally and, most recently, a long-awaited Chinese stimulus package.

Sarasin's Chief Economist, Subitha Subramaniam, looks more broadly at an increasingly rivalrous global economy, with an emphasis on protectionism. Escalating US-China rivalry has huge implications across many industries and assets, from defence, cyber and security spending to the strength of the dollar - still seen as the world's 'reserve currency'.

No matter your physical geography, technology has brought us all closer together. In his article, analyst Kwai San Wong looks at one of the most crucial and ubiquitous components of the modern world, the semiconductor. From phones, to cars, appliances, industrial equipment, and especially recent rapid advances in AI, we've seen exceptional demand for ever more advanced chips, and giants like Nvidia have profited to take their place among the world's largest companies. But how robust is the investment case from here, and is a bubble emerging in tech stocks?

Also in this edition, Nick Wood and Harveer Mata explore the needs and preferences of the next generation of investors, in terms of global reach, awareness of the social and environmental impacts of their choices, as well as philanthropic goals.

Our article from Charities Partner, Oliver Bates, looks at the ramifications of new legislation covering Sustainability Disclosure Requirements (SDR) and how we, as an industry, define the concept of impact investing. Evolution in this space is both welcome, but also challenging.

We hope you enjoy reading our team's insights and, as ever, we welcome your feedback and suggestions. Please get in touch at housereport@sarasin.co.uk.

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GUY MONSON
CHIEF MARKET STRATEGIST
& SENIOR PARTNER

View from the
Chief Market Strategist

DEFYING CRISIS

Key points

- The third quarter of 2024 was positive for global markets, despite ongoing geopolitical concerns.
- An upward revision to US Q2 GDP revealed stronger-than-expected growth in disposable income and a higher savings ratio – could the economy be re-accelerating rather than slowing?
- Despite the enormity of today's geopolitical challenges, we believe investors should maintain a pro-equity stance across portfolios.
- While US financial dominance persists for now, the geopolitical landscape is shifting toward a multipolar world, a theme that will increasingly influence global investment over time.

Can global markets continue to thrive amid today's growing geopolitical turmoil?

Despite a formidable list of geopolitical concerns, asset markets were surprisingly resilient in the third quarter. Global bonds, equities, and commodities all posted positive returns, while equity volatility ended the month near the quarter's lows. True, the so-called 'Magnificent Seven' – Apple, Microsoft, Alphabet, Amazon, Nvidia, Meta, and Tesla – and other technology stocks plunged sharply in August, but they recovered most of their losses by the end of September. Encouragingly, market leadership broadened, with utilities, real estate, and other interest-rate-sensitive sectors leading the rally.

How can investors reconcile this seemingly benign market backdrop with the most divisive US election in a generation, and devastating wars in Ukraine and the Middle East that are likely still escalating? Indeed, aside from a modest rise in oil prices in the first week of October, spurred by Iran's massive rocket barrage, markets appear to want to overlook these geopolitical dangers once again. How much longer can this disconnect persist?

Investors are choosing economics over politics

Far from weakening in the face of global challenges, recent data suggests that the US economy is simply refusing to slow down. A scorching September jobs report followed strong readings from the Institute for Supply Management (ISM), which showed the US services sector expanding at its fastest pace since February 2003. The reading of 54.9 (with any figure above 50 indicating expansion) markedly exceeded expectations[1]. Moreover, upward revisions to US Q2 GDP revealed both stronger-than-expected growth in disposable income and a higher savings ratio. Some commentators are beginning to ask whether the US economy, far from slowing, might in fact be re-accelerating.

Globally, the counterweight to the US's economic momentum has been the deflationary forces stemming from China's deepening real estate crisis. Earlier this month, Chinese authorities finally acknowledged the risks and responded by loosening policy on three fronts: cutting interest rates and bank lending ratios, issuing loans to support stock buybacks, and promising fiscal stimulus – though the details of the latter remain unclear.

We estimate that this fiscal programme could amount to around 1.5% of GDP. While significant, it is a far cry from the 27% of GDP stimulus China unleashed in the two years following the global financial crisis in 2008[2]. Nonetheless, the mere recognition by the Chinese government of the need for stimulus remains a powerful tailwind for global growth.

Inflation: mostly surprising on the downside

Amid improving global growth, inflation continues to retreat. In the US, the core PCE deflator, the Federal Reserve's preferred gauge, showed prices rising at 2.7% in the year to August, down from a peak of 5.6% in early 2022[3]. In Europe, headline inflation is falling particularly sharply – French headline CPI stands at just 1.5%, while Germany's rate has slowed to 1.6%. Risks remain, of course: service sector inflation is proving sticky in Europe, while housing costs in the US remain elevated. But overall, the trend suggests a steady return towards central bank targets.

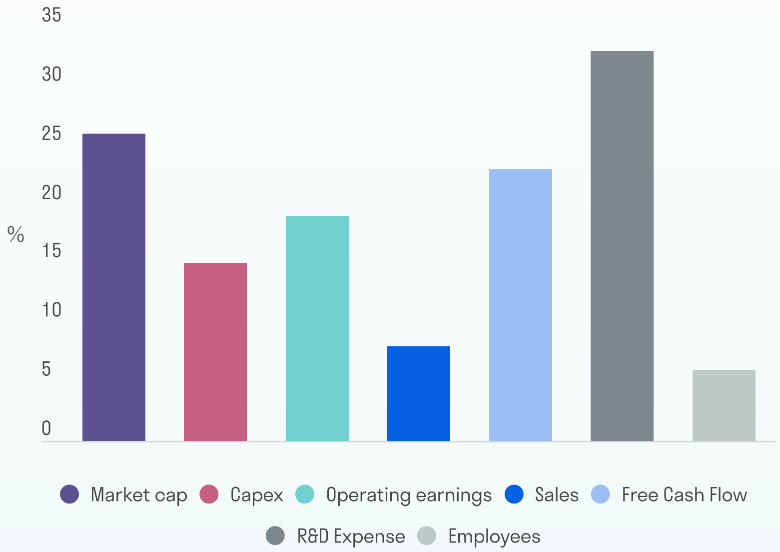
This easing of inflation is providing central banks with greater room to manoeuvre. In the past three months, market expectations for US interest rates at the end of 2025 have fallen from 3.9% to 2.9%[4]. With this backdrop, investors are probably right to believe that if growth does stumble central bankers will effectively 'have their backs'.

Magnificent earnings from the 'Magnificent Seven'

A third pillar of market resilience has been the robust earnings and cash flows generated by AI-linked technology giants, particularly the 'Magnificent Seven (MAG7).' In late July, concerns about the sustainability of these firms' massive capital spending on AI triggered a sell-off. An index of MAG7 stocks tumbled 17% from its peak in August, following an impressive 37% gain earlier in the year, while US equity volatility nearly quadrupled.

Yet, just six weeks later, these same stocks had clawed back roughly three-quarters of their losses, and volatility had eased. The rebound was driven by the realisation that, despite their towering valuations – MAG7 stocks now account for 28% of the S&P 500's capitalisation – these companies deliver profits, cash flow, and R&D spending in nearly equal measure. Unlike the dot-com bubble of 1999-2002, today's AI-linked stocks are underpinned by robust earnings and extraordinary cash flow.

CHART 1 THE MAGNIFICENT SEVEN % SHARE OF THE S&P 500 ON SELECT METRICS AS OF AUGUST 2024



SOURCE: EMPIRICAL RESEARCH PARTNERS ANALYSIS

Learning to live in a multipolar world

So yes, while global markets remain well supported by a likely soft-landing and and strong corporate earnings, they still face a bewildering list of geopolitical challenges. Many of these arise, at least in part, from a shift toward a multipolar world and away from the US dominated model that has managed global conflicts over the last three decades. As my colleague, Dr. Subitha Subramaniam, argues in the next article, today's geopolitical landscape is undergoing a profound transformation – US hegemony, which followed the Cold War, is giving way to a more fragmented multipolar world.

In this new world, the US cannot so easily control the global political narrative in the way we have grown to expect. The Biden administration, for example, has struggled to influence the war in the Middle East and, despite massive military aid, cannot decisively change the situation on the ground in Ukraine. Concerns are growing, too, that the US may struggle, in a future conflict, to deter a Chinese move to annex Taiwan. New alliances are forming and military capabilities are growing outside of NATO, while a strong group of non-aligned nations is forming.

The US will remain a financial superpower for a while yet

While the geopolitical world is increasingly multipolar, the financial world remains, for the moment, largely unipolar. US equities, for example, account for 63% of the MSCI All Country World Index[5], compared to the US's share of global GDP, which sits at around 26%[6]. In technology, US companies today comprise an extraordinary 90%[7] of the MSCI World IT Index. Only two non-US companies – ASML and SAP – make the top 10, and the largest of these is little more than a quarter the market capitalisation of Apple.

DEFYING CRISIS

Guy Monson, Chief Market Strategist and Senior Partner

> Despite the enormity of today's geopolitical challenges, we believe investors should maintain a pro-equity stance across portfolios.

The US dollar, too, remains dominant. According to the Bank for International Settlements' 2024 FX survey, the dollar was on one side of 88% of all currency trades[8]. So yes, we see the move toward a multipolar world as offering extraordinary investment opportunities but, for the present, it is US that still determines the direction of global financial markets.

Looked at from this perspective it is easier to understand why investors are comparatively sanguine today. They see a US soft landing, a low risk of recession, inflation rates that are falling and corporate earnings that are climbing, with dovish central bankers ready to step in as needed.

Oil and elections

However, two factors in particular, have historically had the power to derail US markets. The first is oil. In past Middle Eastern conflicts, energy prices were the primary transmission mechanism to the West. Today, crude prices (Brent) have risen by around 8% since the Iranian missile attack, but still remain broadly flat for the year. Why? The US has been the world's largest oil producer since 2018, mitigating supply concerns. Moreover, OPEC still sits on 3-4 million barrels per day of spare capacity, about 6% of global consumption. Even if Iran were to disrupt traffic through the Strait of Hormuz, supply appears secure for now.

The second challenge is, of course, the US election, with polls in swing states too close to call. A Trump victory would likely bring a tax-cutting, pro-business agenda but also significant uncertainty around trade and tariffs – though US assets would probably outperform. A Harris win would continue Biden's high-spending, green-energy-focused approach, with a more globally oriented policy outlook. In either case, government spending would support the US economy. Yet neither candidate has addressed the ballooning budget deficit and, for now, foreign investors remain willing to fund it.

Investment implications

In conclusion, despite the enormity of today's geopolitical challenges, we believe investors should maintain a pro-equity stance across portfolios. Within this, we advocate maintaining steady exposures to technology and AI-linked investments, where current valuations are still underpinned by strong industry fundamentals and growth prospects. US election risks remain and we are particularly mindful of the policy implications of a 'clean sweep' for either party (when the President's party wins control of both the House and Senate). Where appropriate, deploying portfolio insurance on a portion of equity positions seems prudent.

In our bond holdings, we remain modestly underweight, favouring corporate issuers. Here, inflows are supported by the substantial surplus accruing to UK pension funds. Within alternatives, our preferred asset remains gold. This is both as a hedge against rising budget deficits and as a beneficiary of increased purchases by Asian and emerging-market central banks, which are keen to reduce direct exposure to the dollar.

We continue to view the UK as something of a political, safe haven. Yes, we need to wait for the Autumn Budget on 30 October to assess whether Chancellor Reeves's growth agenda remains intact which, if confirmed, would warrant increasing allocations to sterling.

In summary, investors are likely to focus on the US and global economies over politics for a while longer. Together this supports a pro-equity stance despite a geopolitical backdrop of turmoil and the obvious human suffering. However, in the longer term, we are entering a multipolar world where US dominance can no longer be assumed – this shift will increasingly shape investment flows and is set to become a powerful investment theme in the months and years ahead.

[1] https://www.ismworld.org/supply-management-news-and-reports/reports/ism-report-on-business/services/september/

[2] https://www.economist.com/finance-and-economics/2024/09/27/at-last-china-pulls-the-trigger-on-a-bold-stimulus-package

[3] https://www.bea.gov/news/2024/personal-income-and-outlays-august-2024

[4] https://www.reuters.com/markets/rates-bonds/fed-rate-cuts-will-not-be-deep-market-expects-says-blackrock-2024-09-16/

[5] https://www.msci.com/research-and-insights/visualizing-investment-data/acwi-imi-complete-geographic-breakdown

[6] https://www.visualcapitalist.com/ranked-the-top-6-economies-by-share-of-global-gdp-1980-2024/

[7] https://www.msci.com/www/index-factsheets/msci-world-information/09375822

[8] https://blogs.lse.ac.uk/internationaldevelopment/2024/02/29/long-read-the-beginning-of-the-end-for-the-us-dollars-global-dominance/

SUBITHA SUBRAMANIAM
CHIEF ECONOMIST

Economist outlook

MAPPING A MULTIPOLAR WORLD

The geopolitical landscape is undergoing a profound transformation. US hegemony, which followed the end of the Cold War, is giving way to an unbalanced multipolar world.

China's rapid economic and military rise is creating a new 'pole', while other emerging nations are charting their own independent courses. The implications of this power shift are far-reaching and will impact financial markets.

From Cold War to US hegemony

The Cold War era (1947-1991) was dominated by two superpowers, the US and the Soviet Union, which maintained distinct but separate spheres of influence. This bipolar world order was surprisingly stable as the threat of a nuclear conflict between the two superpowers kept war at bay. With the collapse of the Soviet Union in 1991, the world gradually transitioned to a unipolar power structure within which the US emerged as the dominant force in markets, finance, technology, and military affairs.

As the sole hegemon, the US has been a leading architect of a rules-based system of global governance administered through multilateral institutions like the UN, NATO, WTO and the IMF. These institutions are embedded within both the western cultural values of democracy and human rights, and economic values such as co-operation and open markets. This became the platform for an increasingly efficient and interconnected global economy that raised living standards across the world. US allies benefited from a 'peace dividend' as fears around major conflicts ebbed; the US in turn reaped a 'power dividend', expressed most obviously through the dominance of the US dollar and the US financial system in international capital flows.

Over the past two decades, China has strategically capitalised on open trading markets to propel itself to the forefront of economic and military power, and is keen to gain a correspondingly bigger say in global governance. At the same time, there is a growing consensus within the US that the rules-based international order has contributed to negative domestic impacts like deindustrialisation and growing inequality, and should be reformed.

Key points

- After three decades of relative stability in the geopolitical landscape, China is driving the transition away from the unipolar system dominated by the US.
- The rise of protectionism and the potential for conflict are recalibrating both the risks and opportunities in financial markets.
- Despite the challenges, there are opportunities in sectors such as defence, technology, strategic resources, and domestically focused companies.

Continued

MAPPING A MULTIPOLAR WORLD

Subitha Subramaniam, Chief Economist

The multipolar world takes shape

As China, India and other emerging markets continue to grow, the global power balance is drifting away from the US. China's tacit support for Russia's war in Ukraine, its belligerence in the South China Sea, and the One Belt One Road initiative, are all efforts to chip away at US dominance and challenge its status as a sole hegemon.

At the same time, growing emerging powers, such as India, Turkey, Brazil, Vietnam, Saudi Arabia, and the UAE, are resisting calls to align with either the emergent Chinese pole or the incumbent US pole. Instead, they are pursuing their own national interests and forming flexible alliances depending on the issue at hand. As a result, the global power structure is likely to be much more decentralised than during the Cold War era: we expect two opposing poles accompanied by a multitude of alliances leading to a more complex, dispersed geopolitical structure.

Friction, flashpoints...

China has assembled a loose coalition of mostly authoritarian allies – Iran, Russia and North Korea – which are seeking to subvert US dominance. Hostile rhetoric and tit-for-tat sanctions reveal hardening positions. At the current trajectory, the likelihood of a confrontation, with Taiwan emerging as a potential flashpoint, is increasing. An end game where China establishes indirect control over Taiwan, with the US potentially backing down to avoid direct conflict, has gone from unthinkable to plausible.

A gradual retreat by the US from its role as a global policeman is likely to make the geopolitical environment much more uncertain and insecure. Progress on nuclear non-proliferation has started to reverse and technologies, such as AI and cheap missile and drone swarms, are injecting huge uncertainty into outcomes of potential conflicts.

...lead to fragmentation

In an increasingly rivalrous global economy, countries are adopting protectionist measures to bolster their strategic advantage. Motivations include safeguarding critical supply chains, shielding domestic industries from foreign competition and addressing trade imbalances. Since 2012, advanced economies have led the way by increasing their use of trade barriers and industrial policy tools.

Over the next decade, we expect the globalised marketplace for goods and services to fragment further as tariffs, subsidies, import licensing requirements, anti-dumping duties, and trade sanctions, all aimed at protecting domestic industries and reducing reliance on foreign supply chains, become more common place.

> In an increasingly rivalrous global economy, countries are adopting protectionist measures to bolster their strategic advantage.

As global power shifts away from the US, the integrated global financial system it supported is also likely to splinter. Financial integration under US hegemony has been accompanied by 'dollar dominance' where the currency's role in global payments and settlements (circa 80%) is substantially larger than its share of Global GDP (circa 25%) and US Treasuries have become the de facto global 'safe asset'.

Escalating US-China rivalry is making investors wary of cross-border operations. Many financial institutions have begun to scale back operations in jurisdictions that could one day be exposed to sanctions from western governments. Global banks and investment firms, which had poured hundreds of billions into China over the past decade, have been scaling back future investment plans. Chinese companies are revisiting US listing plans over fears of heightened scrutiny from both the China Securities Regulatory Commission (CSRC) and the Public Company Accounting Oversight Board (PCAOB) in the US.

Market implications

The shift away from a US-centric globalised system, coupled with the rise of protectionism and the potential for conflict, is recalibrating both the risks and opportunities in financial markets. We believe there are three main risks to be considered:

- First, US reluctance to provide iron clad defence guarantees for global security, alongside the growing impatience of the China-led alliance with the status quo, increases the risk of global conflict.
- Second, the growing use of tariffs and industrial policies alongside bigger defence budgets will raise inflation, increase volatility, and worsen fiscal sustainability; this is likely to result in upward pressure on bond yields.
- Third, rising tension between the incumbent US pole and the emergent Chinese pole is likely to fracture global capital markets. Capital controls and sanctions are likely to become more pervasive, leading to a gradual erosion of dollar dominance.

These changes are also driving a range of investment opportunities:

- Defence, cyber, and security spending will experience a sustained increase, benefiting earnings and valuations for companies operating in these industries. Heightened uncertainty also supports the inclusion of tail risk protection within investment strategies.
- Strategic autonomy is becoming a higher priority across the world, with positive implications for investments in 'strategic resources' such as metals, agricultural products, and elements critical for industrial production.
- Similarly, the political imperative for shorter supply chains and stronger 'national champions' can have a range of positive impacts for domestically focused companies. This includes subsidies, more permissive regulation, and toleration of oligopolistic behaviour – with potential beneficiaries ranging from large US tech platforms to European utilities.
- Finally, a lessening of dollar dominance could be hastened by moves to use sovereign wealth funds to diversify government reserves, favouring 'trophy' assets and dollar alternatives, such as gold, and potentially even bitcoin.

Conclusion

In this new era of multipolarity, it is crucial that investors anticipate and adapt to the shifting tides of geopolitics, effectively managing the inherent risks and capitalising on the opportunities associated with a more complex and volatile landscape.

KWAI SAN WONG
ANALYST – GLOBAL EQUITIES

Thematic View

SEMICONDUCTORS: INVESTING IN AN AI FUTURE

Key points

- Semiconductors are essential components of many everyday tech devices, and the sector has experienced significant growth in recent years.
- The biggest driver of this growth has been the rise of AI and its need for power-hungry GPUs.
- This growth is challenging sustainability targets, and the industry needs to find better long-term solutions.
- Sarasin invests in a number of key semiconductor foundries, though we are keeping a close eye on the stocks amid concerns of a 'bubble' in prices.

Semiconductors may not be the first things that come to mind when we think of our tech devices, but they are critical to our modern technologies and are present everywhere. In short, they are the fundamental components - used to convert and amplify electronic signals - that make the chips which power our digital economy today.

Semiconductors are found in our everyday devices, from smartphones, to computers, appliances, cars, planes, and industrial equipment. Every day, we create products that have more and more semiconductor content. It's no surprise that global semiconductor sales have been growing at 5-7% annually in the past 20 years[1] – they are big business and investors are keen to gain exposure.

Nvidia and the rise of AI

The semiconductor industry has dominated the investment headlines in 2024, and much of the focus has been on one stock in particular, Nvidia. From its formative years in creating graphics cards for gaming and multimedia, the company has grown tremendously to hit a multi-trillion dollar market capitalisation. Today its graphics processing units (GPUs) are used extensively to power the development of artificial intelligence (AI).

As my colleague, Colm Harney, outlined in his article 'AI: The new industrial revolution' in the last House Report (Q3 2024), the pace of AI development has surpassed even the most optimistic predictions since the launch of ChatGPT in late 2022. This was a key event in kick-starting a new investment cycle involving big technology companies which currently rely on Nvidia's chips to build AI models. Nvidia and its suppliers have benefited significantly from this trend - the PHLX Semiconductor index (SOX) has climbed around 25% year-to-date (to 30 September), beating the 20% performance from the S&P 500 in the same period.

The semiconductor industry is known for its pronounced cyclicality; the high-tech foundries needed for production are very expensive and time-consuming to build, but once established can produce huge volumes of computer chips around the clock. This high ratio of upfront to operating costs means that relatively small swings in demand, due to the ebbs and flows of the economic cycle, are often amplified into huge swings in profitability for the semiconductor industry. Understandably, the growth of AI has sparked a record-breaking uplift in profits for the industry leader, Nvidia.

In 2025, consensus is expecting Nvidia to earn $160bn from sales to the datacentre market, which is almost 10 times higher than in 2022[2]. This spectacular growth has made it more challenging for investors to forecast the next inflection point in the industry, and so every quarterly result is now closely watched by investors.

We at Sarasin hold a number of semiconductor companies in our portfolios, such as Nvidia, Broadcom, Taiwan Semiconductor Manufacturing Company (TSMC) and ASML, which fit within our key forward-looking theme of Digitalisation.

While individual investment cases differ, a commonality among all of them is the idea that AI will spark the next cycle of investment in semiconductors, particularly as tech companies need to build the hardware before they can make more progress on applications. This trend was the same in the previous technological cycle (e.g. personal computers, internet, mobile and cloud computing).

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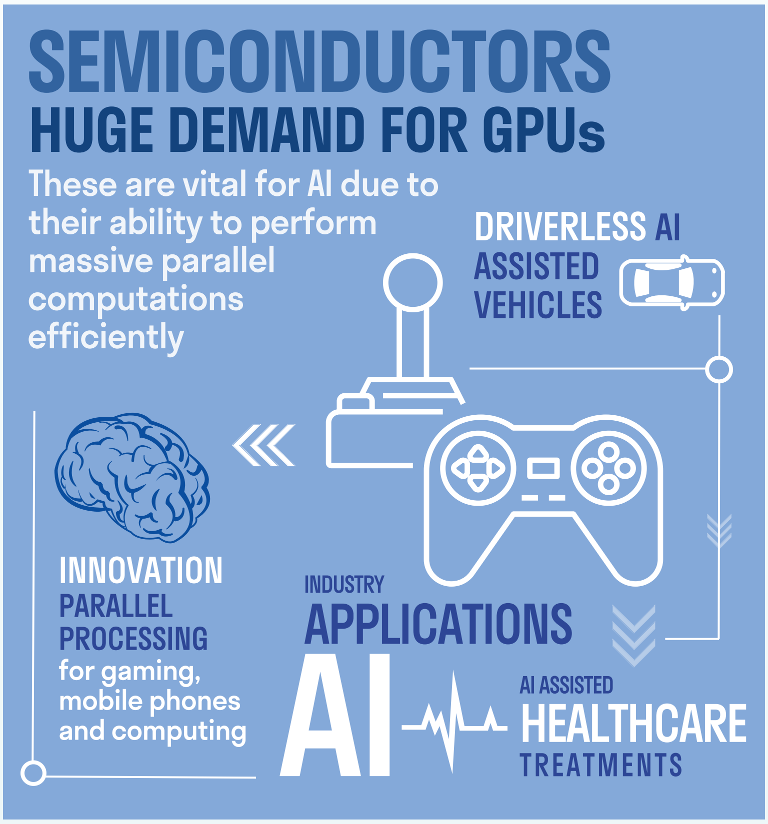


How are semiconductor companies embracing sustainability?

GPUs are power hungry, and so a huge drain on energy resources. In order to provide more computing power for AI training and inferencing, Nvidia has increased the power consumption with each new generation of its products. This, in turn, has meant significant incremental demand for power generation from the datacentres which house these GPUs.

While the semiconductor industry has a long track record of making chips with more efficiency with each new generation, the sheer amount of power needed by these AI datacentres is definitely something it needs to find a sustainable long-term solution for. This is a key area of concern for the biggest users of semiconductors. For example, Microsoft recently signed a 20-year deal with Constellation Energy to re-open previously decommissioned nuclear reactors at Three Mile Island to supply power to its AI datacentres[3]. Apple meanwhile has shared details of new reusable datacentre air filters; the company has a stated aim of being 100% carbon neutral across its products and supply chain by 2030[4].

Continued

SEMICONDUCTORS: A KEY ROUTE TO INVESTING IN AN AI FUTURE

Kwai San Wong, Analyst – Global Equities

What are the risks of investing in an AI future?

Despite the rapid progress in AI development in the past two years, we have still not seen a clear path for all related companies to turn into profitable businesses. Return on investment is front of mind of every investor.

While we have seen promising use cases for AI in areas such as customer service agents and code generation, helping software developers to be more productive, the question remains whether the scale of investment can be justified.

The market will certainly watch the launch of upcoming models such as GPT-5, Llama 4 and Gemini 2 closely, and analyse how much more capable they can be. If these new models fail to deliver an increase in abilities commensurate with the outlay on development and operational costs, then sentiment towards AI investments could cool. However, if the 'scaling laws' hold and these models meet expectations, we expect AI to unleash the next era of computing, with transformative effects on society and the global economy.

We have kept a close eye on the recent volatility in the share prices of semiconductor companies, and concerns about a potential 'bubble' in all things related to AI. However, as it stands today, we are happy to hold a basket of stocks that we see as long-term investments that remain well placed to profit from ongoing technological progress.

The future for semiconductors

Semiconductors are becoming more and more vital to our modern technologies. We expect semiconductors' importance to increase in the future and we will continue to attempt to identify the right investments in the sector for our clients.

We remain cautiously optimistic about developments in AI, though we are keeping a close eye on the profitability of related companies, and valuations within the wider tech sector.

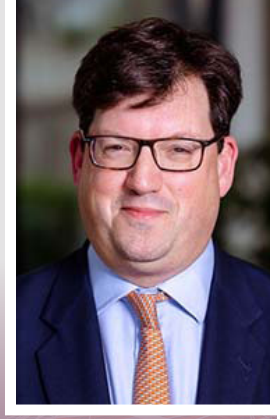
[1] https://www.wsts.org/61/market-statistics

[2] https://visiblealpha.com/blog/nvidia-nvda-earnings-preview-fiscal-q2-2025/

[3] https://energycentral.com/c/ec/microsoft-inks-20-year-power-purchase-agreement-constellation-reopen-tmi-1

[4] https://www.apple.com/environment/pdf/Apple_Environmental_Progress_Report_2024.pdf

A NEW GENERATION OF GLOBAL CITIZENS



NICK WOOD
PARTNER AT SARASIN & PARTNERS AND DIRECTOR AT SARASIN ASSET MANAGEMENT*

HARVEER MATA
SENIOR INVESTMENT MANAGER AT SARASIN & PARTNERS

Over the past 20 years, advances in technology and communications have created an interconnected world. This progress, combined with shifting societal trends has made it easier for investors to access opportunities across the globe, fundamentally changing investment behaviours.

At the same time, responsible investment and philanthropy have developed a wider appeal. So, what might be in store for the next 20 years as existing wealth is transferred to a new generation of investors, and fortunes are made in industries that are perhaps yet to exist? How can we ensure conversations with multi-generational and next generation clients focus on the right topics? We set out three ideas below:

Global citizens need global investments

The global mindset of this new generation of potential investors is underpinned by an increasingly dynamic education system. In 2023, it was estimated that more than one million international students were studying in the US[1], with many of these hailing from China and India. With the US proposing to ease the H1-B non-immigrant work visa for international graduates[2], we will likely see an increase in the next generation permanently relocating to the US after their studies. In the UK, the academic year of 2021/2022 recorded roughly 680,000 foreign students studying at UK higher education institutions, equivalent to 24% of all higher education students in the UK[3].

The next generation of high earners and entrepreneurs will inevitably have even more of a global outlook. While an investment manager's primary objective is to structure a portfolio to meet clients' changing investment requirements, they must also be mindful of inadvertent tax pitfalls affecting clients across the globe. For example, the tax considerations for US connected individuals and families are complex and necessitate specialist advice.

Key points

- A younger generation of investors are increasingly thinking on a more global scale, both in terms of how they invest and where they base themselves in the world.
- Many are more conscious of the social and environmental impact of their investments, and are seeking to align their portfolios with their values.
- Investment managers can also work with clients to meet their philanthropic goals.
- Family foundations and donor-advised funds (DAFs) are likely to have a bigger role to play in the years ahead.

A NEW GENERATION OF GLOBAL CITIZENS

Nick Wood, Partner at Sarasin & Partners and Director at Sarasin Asset Management;
Harveer Mata, Senior Investment Manager at Sarasin & Partners

More so than ever, investors are diversifying strategically across global markets with the aim of tapping into growth opportunities across equities, bonds, and alternative strategies. Encouraging investors to look beyond traditional geographical boundaries enables them to benefit from the potential returns generated by long-term thematic trends in the global economy. In particular, key themes such as those identified by Sarasin & Partners – Digitalisation, Automation, Evolving Consumption, Climate Change, and Ageing – will continue to reshape our economies. Investing in leading global companies which are beneficiaries of these trends is likely to present significant opportunities for the next generation of investors to grow their capital.

> Investment attitudes are evolving and in general, this generation appears passionate about how their investments are managed, and often looks through a different lens.

Evolving attitudes to responsible investing presents opportunities

Despite recent short-term challenges presented by geopolitical events, long-term capital invested by individuals and families increasingly prioritises responsible investment goals alongside performance objectives. It may be a cliché, but it's often true that these requirements are expressed by members of the younger generation.

At a fundamental level, scrutinising the environmental, social and governance characteristics of a potential investment makes good sense as a complement to detailed financial analysis. To state the obvious, poorly governed companies tend to make bad investments. There is much more nuance, however, to the subject of responsible investment and stewardship, and guiding families with diverse views requires expertise and experience.

Families and their advisers are having increasingly open discussions to understand and respect varying views. This can involve finding common ground and creating diversified portfolios that reflect the collective values and goals of the family, while also educating family members on the potential risks and rewards associated with investing from a responsible standpoint. A good investment manager can guide the conversation to help bridge generational gaps and align investment decisions with the family's long-term plans for wealth preservation. In certain cases, the flexibility to address specific ethical considerations in a bespoke investment strategy can unlock an opportunity to engage with the next generation of family members.

Philanthropic giving

Philanthropic giving has always been at the heart of many wealthy families' planning in the US, and is becoming more and more prevalent in the UK.

Family foundations and donor-advised funds (DAFs) are popular vehicles to facilitate philanthropic giving. These structures provide flexibility, tax benefits, and a strategic approach to long-term charitable giving. DAFs were first established in the US in the 1930s and their use has also become more common in the UK. Dual compliant US/UK charitable structures are also available to transatlantic families.

While family foundations offer control over the distribution of funds and the ability to create a lasting legacy, they come with administrative responsibilities and regulatory requirements that can be onerous. DAFs, on the other hand, provide a more straightforward approach with lower costs, while still offering tax advantages. They allow donors to recommend grants to their preferred charities, while the sponsoring organisation handles the administrative tasks.

Investment managers and their tax advisers can work closely with different generations of a family to determine the most suitable philanthropic structure. This involves assessing charitable and investment goals, levels of retained control, and associated costs.

Through a different lens

Inheritance and professional success will drive an unprecedented amount of wealth to a new generation. Investment attitudes are evolving and in general, this generation appears passionate about how their investments are managed, and often looks through a different lens. However, much of the research published about the Great Wealth Transfer points to the concern that families are not having the right conversations at the right time. If you require advice on any of the contents of this article, there are excellent advisers on these areas, and we would be delighted to help you find the right team.

If you would like to get in touch regarding the above, please talk to your usual Sarasin contact, or Nick or Harveer via the details below:

Nick Wood
Partner at Sarasin & Partners and
Director at Sarasin Asset Management*

T +44 (0) 20 7038 7086

E nick.wood@sarasin.co.uk

Harveer Mata
Senior Investment Manager
at Sarasin & Partners

T +44 (0) 20 7038 7262

E harveer.mata@sarasin.co.uk

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[1] https://monitor.icef.com/2023/01/us-foreign-enrolment-once-again-exceeds-one-million-students/

[2] https://economictimes.indiatimes.com/nri/study/us-to-relax-visa-processing-for-graduates-with-job-offers/articleshow/112159216.cms?from=mdr

[3] https://commonslibrary.parliament.uk/research-briefings/cbp-7976/

OLIVER BATES
PARTNER, CHARITIES

Charity Focus

IMPACT, SUSTAINABILITY & SOCIAL INVESTMENTS: WHAT DO THEY MEAN FOR CHARITY INVESTORS?

Key points

- SDR rules are aimed at improving transparency in the asset management sector, and eliminating greenwashing.
- However, so far a limited number of funds have been able to comply with the FCA's requirements.
- Investors must beware definitions around 'impact investing', which are not black and white.
- Evolution in impact investing is both promising and challenging and will become an increasingly relevant investment category.

We have written multiple articles over the years trying to make sense of the terminology and practices relating to ethical investing, stewardship, and everything ESG (environmental, social and governance).

This time our attention turns to the word 'impact', with many charities looking to align at least a part of their investments with their mission. At the same time, there are new rules on sustainability, with some products looking to be classified as 'sustainability impact' funds. This article sets out to determine where the terms are linked and, indeed, how they overlap.

SDR – Sustainability Disclosure Requirements and impact

New rules relating to sustainability in the UK are a welcome guard against 'greenwashing' or 'impact washing' while promoting fund transparency. The UK's Financial Conduct Authority (FCA) published its new legislation, SDR, in late November 2023[1]. The regulations aim to improve the transparency and accountability of companies regarding their sustainability and environmental practices. One such method across the asset management sector has been to standardise the terminology and disclosure of sustainability metrics to investors in funds. Sustainability claims must be fair, clear, and not misleading.

The UK is not alone in introducing such measures; the European Union introduced its Sustainable Finance Disclosure Regulation (SFDR) in 2021[2], while in the US the Securities and Exchange Commission (SEC) also has its own rules in place.

One of the four labels is 'Sustainability Impact,' which 'aims to achieve a pre-defined positive measurable impact in relation to an environmental and/or social outcome'. To date, however, there has been low appetite for the UK's SDR labels, with seemingly few funds approved (or even applying). This has led to the FCA recently extending its deadline by four months out to April 2025 to give firms more time to comply.

Some firms are choosing not to apply for the fund labels at all: Stewart Investors, arguably a pioneer of sustainable investing, will drop 'sustainability' and any related terms from its fund range, including the £6.5bn Asia Pacific Leaders Sustainability fund[3]. Its decision highlights the real challenge faced by the investment management industry, as well as the FCA in trying to demonstrate sustainability credentials, while tackling greenwashing. It is early days, but for investors, the end result could be a smaller pool of sustainable funds, which was clearly not the FCA's intention.

What does 'impact' mean to charities?

In recognition of charities looking to maximise their impact, and the FCA's SDR rules, the Charity Commission of England and Wales has clarified the approach to both responsible and social investments in revised guidance for trustees (CC14) in August 2023[4]. This Followed the conclusion of the much publicised 'Butler-Sloss' case in 2022[5] – which concerned the general power of investment and its relationship to charitable purposes. The guidance gives trustees even greater latitude in determining a responsible investment policy, as long as they consider if there is any material potential impact on financial returns.

So, is there a connection between the SDR's sustainability labels and CC14's social impact investments?

In short, yes. We are hearing from more of our charity clients how important it is to seek investments that might achieve a definitive positive contribution to either the environment and/or society, while also making a financial return. As a result, a fund with a 'Sustainability Impact' should be a win-win in this respect, but as ever, it is not straightforward as few funds will be able to align specifically with a charity's own mission and fulfil the true definition of a social investment for them. The Charity Commission provides two examples:

- A poverty relief charity, making some investments in affordable housing, affordable medicine, or in companies that pay workers a living wage, alongside the financial return that the trustees are aiming for from the investment. This helps to achieve a positive impact in support of the charity's purposes, while the charity's money is invested.
- A development charity making a loan to a small-scale farming business. This helps to achieve the charity's purposes directly through the investment by bringing benefits to the local population, as well as by providing a financial return from interest on, and repayment of, the loan.

A key participant in this sphere in the UK is Better Society Capital (formerly called Big Society Capital), which has defined impact investment as 'investments made with the intention to generate positive, measurable social and environmental impact alongside a financial return'[6].

Social impact investing is a specialist field, requiring investors to navigate challenges such as sourcing genuine, high-impact investments with limited financial history, monitoring their effects, and generating an attractive financial return in the process. There are a number of hurdles between agreeing to take part in impact investing, to then actually committing. For charity trustees, success in social impact investing largely depends on the skills of the board and the ability of key individuals to dedicate the necessary time and effort.

So, how might charities approach this?

1. Invest in a sustainable impact fund

There are an increasing number of impact investment funds, however selecting which to invest in is not without its challenges. Typically, the more impactful a fund is, the less liquid it is, and much greater due diligence is required from the outset. Though still limited within a small universe, these can be invested in just like any open-ended pooled fund.

The presumption that impact funds are distinctly different to traditional retail funds is brought into question if one takes a closer look into the detail. Some of the funds on offer to charity investors include statements such as investing in companies "…moving towards greater sustainability". However, when you look under the bonnet, the top-five investments of one such fund included: Nvidia, the semiconductor chip manufacturer; EssilorLuxottica, an eyewear company; and Elevance Health, a healthcare insurance company. None of these have obvious sustainability characteristics.

Those who would consider themselves more evangelical about impact investing may challenge how 'impactful' these funds really are. Investors clearly need to be mindful of what they are really investing in.

A key requirement of the SDR rules is to provide evidence of any sustainability claims. With many listed companies held in these funds also held widely in traditional investment portfolios, it is important for charity investors to understand the thought process behind how and why an investment manager considers them to be impactful investments.

Continued

IMPACT, SUSTAINABILITY AND SOCIAL INVESTMENTS: WHAT DO THEY MEAN FOR CHARITY INVESTORS?

Oliver Bates
Partner, Charities

2. Invest to achieve demonstrable social impact

For investors wanting to achieve the greatest impact, much more comprehensive analysis is required to assess the capability of an investment manager to source, manage, and report on the social KPIs. It is likely that such an investment will be via an unlisted private market vehicle, and therefore this approach comes with the additional challenges of very little liquidity, as well as a plethora of legal forms.

While the financial returns from genuinely impactful investments may be below the wider market in the short term, the positive impact return can be very attractive, and provide some compensation. However, herein lies a second critical challenge: how does one set about measuring the impact an investment has had?

What about measuring impact?

For an investor wanting to understand how to approach impact measurement, the Global Impact Investing Network (GIIN) has provided the following summary[7]:

Investors' approaches to impact measurement will vary based on their objectives and capacities. Measurement choices usually reflect investor goals and investor intention. In general, best practices for impact investing include:

- Establishing and stating social and/or environmental objectives to relevant stakeholders.
- Setting performance metrics and targets related to these objectives using standardised metrics wherever possible.
- Monitoring and managing the performance of investees against these targets.
- Reporting on social and/or environmental performance to relevant stakeholders.

In summary, the evolving landscape of impact investing is both promising and challenging and impact investments will undoubtedly become an increasingly relevant category. The FCA Sustainability Disclosure Requirements (SDR) and the Charity Commission's updated guidance reflect a growing commitment to transparency and efficacy in sustainable investing.

As investors and trustees navigate this complex field, it is crucial to understand impact investments thoroughly. While the path to meaningful impact may be demanding, for those who are prepared to go the extra mile, the rewards will be worth it, in more ways than one.

If you are interested in discussing impact investment in more detail, please do get in touch:

Oliver Bates
Partner, Charities

T +44 (0) 20 7038 7193

E oliver.bates@sarasin.co.uk

1 https://www.fca.org.uk/publications/policy-statements/ps23-16-sustainability-disclosure-requirements-investment-labels

2 https://finance.ec.europa.eu/sustainable-finance/disclosures/sustainability-related-disclosure-financial-services-sector_en

3 https://citywire.com/wealth-manager/news/exclusive-fresh-sdr-blow-as-stewart-investors-rejects-fca-labels/a2450321

4 https://www.gov.uk/government/news/guidance-on-investments-refreshed-to-help-improve-clarity-and-boost-trustee-confidence

5 https://www.gov.uk/government/news/update-on-investment-guidance-following-butler-sloss-case

6 https://bettersocietycapital.com/our-approach/impact/

7 https://thegiin.org/publication/post/about-impact-investing/

WHAT WE ARE READING AND LISTENING TO

Here is a selection of what is on our reading and listening lists, helping our team understand some of the greatest drivers behind our complex world.

Books

Barbarians At The Gate, Bryan Burrough and John Helyar

This is about the leveraged buyout of RJR Nabisco during the 1980s, one of the largest and hotly contested corporate deals of the 20th Century.

Sam Jefferies, Head of Asset Management

More Thank You Know – Finding Financial Wisdom In Unconventional Places, Michael J Mauboussin

Investing success requires more than just financial knowledge. Human behaviour is often irrational, and investors frequently fall prey to biases like overconfidence, herd behaviour, and loss aversion. By understanding these tendencies, investors can recognise and avoid common mental traps. The book talks about skill and luck in investing success (highly skilled investors can have poor short-term results, while lucky investors can have good short-term results).

Nikki Martin, Senior Global Portfolio Manager – Global Equities

On The Edge, Nate Silver

The famed statistician applies the lessons he learned as a professional gambler to the world at large – drawing parallels between the poker rooms of Las Vegas, venture capitalists in Silicon Valley, crypto enthusiasts, astronauts, and art collectors. His central thesis, that the mindset of informed, deliberate risk-taking is gradually spreading throughout the global economy, certainly rings true in the world of investing.

Colm Harney, Investment Strategist and Portfolio Manager

Psychology Of Intelligence Analysis, Richards Heuer

Published by the CIA, the book discusses how the human mind struggles to cope with uncertainty and biases, and provides tools to help minimise cognitive limitations when analysing complex problems.

Tom Kight, Global Equity Analyst

Podcasts

All-In with Chamath Palihapitiya, Jason Calacanis, David Sacks & David Friedberg

The podcast is hosted by four venture capitalist friends that have forged their careers in technology and finance. The show covers a wide range of topics from economics, market trends, and business to technology, politics, and current affairs. Debate among the hosts is often heated, but usually well-informed and in good humour.

Tom Santa-Olalla, Senior Associate Partner

Flirting With Models

Corey Hoffstein, CIO of Newfound Research, interviews a range of guests from the world of quantitative investing. A great way to boost your understanding of a topic that continues to grow in importance and relevance.

Colm Harney, Investment Strategist and Portfolio Manager

Acquired

A series of deep-dives into the world's greatest companies and what has made them successful.

Tom Kight, Global Equity Analyst

EVENTS

Q4 2024

Visit our website, sarasinandpartners.com for more information.

How to register

To join any of our events or for more information, please visit our website, sarasinandpartners.com, or contact our events team at **events@sarasin.co.uk.**

Trustee Investment Training in conjunction with Charity Finance Group

Advanced Charity Investment Training

This training is free of charge and further details can be found on our website.

12 November 2024

Virtual session

Charity Funds Annual Review

14 November 2024

The Royal College of Physicians

SAVE THE DATE

Sarasin Spring Investment Seminars 2025

12 & 18 March 2025

The Royal Society of Medicine

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SARASIN & PARTNERS LLP

Juxon House
100 St. Paul's Churchyard
London EC4M 8BU

T +44 (0)20 7038 7000
sarasinandpartners.com

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00103_UK_11 October 2024 1:54 pm