

Passive Plus MPS

Quarterly report – Q4 2024
Annual report – 2024



Brewin
Dolphin

Introduction

The U.S. economy was a bright spot in 2024, with households continuing to spend and incomes rising. In contrast, China's economy was weak, with a decline in property prices and low consumer spending. The UK economy grew modestly, hampered by high government debt and households grappling with inflation. The global economy was marked by political change, with over 100 countries holding elections and many incumbent governments being dismissed.

In the UK, the new Labour government announced a budget that included tax increases and borrowing, which is expected to fuel inflation which could hamper economic growth. In mainland Europe, France and Germany experienced political instability, with early elections and changes in government.

The U.S. elections saw President-elect Donald Trump's victory and a surprise sweep for the Republicans in both legislative chambers (the U.S. Senate and House of Representatives), albeit with a narrow majority. This was cheered by the stock market, but bonds weakened towards the end of the year.

The Republican Congress is expected to cut taxes, but this might be challenging given the large federal budget deficit. The regulatory environment is expected to be lighter under a second Trump presidency, which could benefit U.S. financials.

The technology and communication services sectors performed well in 2024, driven by the increased investment in artificial intelligence (AI). Gold had a strong year, due to its limited supply and attractiveness as a store of value. Economists are sceptical that President-elect Trump's policies will increase economic growth, but the market is focusing on the easier regulatory environment that can be implemented without Congressional input.

Market overview Q4 2024

- The fourth quarter saw gold returning 5.8%, whilst globally, commercial property declined by 3.3%.
- Equity markets were mixed. North America stood out with a strong return of 9.8%. Japan also performed well, returning 2.8%. However, Developed Europe ex UK and Developed Asia ex Japan saw significant declines, slipping -3.7% and -1.8%, respectively. The UK and Emerging markets were also soft, with returns of -0.4% and -0.9%, respectively.
- Bonds fared poorly. Global Inflation Linked and UK Sovereign Bonds underperformed, returning -2.9% and -3.1%, respectively. Global Corporate Bonds and Global Sovereign Bonds also declined, but to a lesser extent, with returns of -1.5% and -1.8%, respectively.
- Cash delivered a positive return in the higher rate environment.

Passive Plus MPS performance

Passive Plus MPS performance												
	Q4	2024 YTD	1yr	2yr	3yr	4yr	5yr	2023	2022	2021	2020	2019
Cautious Portfolio	0.3	6.2	6.2	13.2	1.1	5.7	10.2	6.6	-10.8	4.5	4.2	10.0
Cautious Higher Equity Portfolio	0.8	7.6	7.6	15.7	3.7	11.2	15.0	7.5	-10.5	7.2	3.4	10.0
Income Portfolio	1.3	8.9	8.9	17.8	6.2	15.5	18.4	8.2	-9.9	8.7	2.5	12.2
Income Higher Equity Portfolio	2.0	10.5	10.5	20.8	9.9	22.2	24.5	9.3	-9.0	11.2	1.9	12.2
Balanced Portfolio	2.5	11.8	11.8	23.2	13.0	28.7	31.7	10.2	-8.3	13.8	2.4	15.0
Growth Portfolio	3.3	14.0	14.0	26.9	17.6	37.6	41.0	11.4	-7.4	17.1	2.4	18.4
Global Equity Portfolio	4.4	16.7	16.7	32.1	22.9	48.0	49.4	13.1	-6.9	20.4	0.9	21.7

All figures shown above are calculated to 31 December 2024.

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

Passive Plus MPS performance highlights Q4 2024



Asset allocation

What worked and why?

Portfolios benefitted from the overweight position to U.S. equities, which performed well in the hopes of lighter regulation under a new U.S. president. The underweight to European equities over a period of economic weakness was helpful. Gold also helped to drive portfolios higher.

What didn't work and why?

An overweight position to sovereign bonds was a detractor but much of the drag was offset by an underweight position to corporate bonds, which also declined.

Fund selection

What worked and why?

The SCOR Catbond fund, which provides insurance against earthquakes and wind events, had another strong quarter despite major storms in the U.S.

What didn't work and why?

Schroder Global Cities struggled over the quarter as the possibility of inflation remaining higher dampened interest in the commercial property sector.

The value of investments can fall and you may get back less than you invested.

Passive Plus MPS portfolio changes Q4 2024

Asset allocation

The Asset Allocation Committee increased the exposure to Asia ex Japan in October, funded by a reduction in our UK equity allocation, and further reduced our corporate bond allocation in favour of sovereign bonds. We also increased the allocation to gold, funded by a reduction in cash.

Following the U.S. presidential election in November, we reduced our European equity allocation by 2% and increased our U.S. equity allocation by 2%, given the potential negative impacts of trade tariffs on European economies.

Fund selection

In October, we increased the gold allocation and reduced corporate bond strategies, investing the proceeds in sovereign bonds. We also increased the allocation to the Fidelity Index Emerging Markets fund, which has exposure to China and surrounding regions. In November, we reflected the Asset Allocation Committee's guidance by reducing our allocation to Vanguard Developed Europe ex UK and increasing our allocation to Fidelity Index US, which provides broad market exposure to U.S.-listed equities.

Passive Plus MPS

Annual report – 2024



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Passive Plus MPS annual market overview 2024

- Generally, 2024 was a good year for investors with gold and U.S. equities the standout performers, rising 27.3% and 26.3% respectively. Other asset classes also put in respectable performances, with commercial property and absolute return rising 4.2% and 4.7%, respectively.
- Bonds were more mixed. Global Corporate Bonds performed well with a return of 3.6%, whilst UK Sovereign Bonds fell -3.4%.
- As noted above, North America was the standout equity market, followed by Japan at 10.1% and the UK at 9.5%. Developed Asia ex Japan returned 11.8%, while Developed Europe ex UK saw a relatively modest return of 2.2%. Emerging markets, however, experienced a decline of -5.3% as the Chinese economy languished.
- Cash delivered positive returns in the higher interest rate environment.

Passive Plus MPS performance highlights 2024



Asset allocation

What worked and why?

Overweight positions to U.S. equities and gold were positive in a year when they were the star performers, rising over 25%. An underweight to absolute return was also beneficial during a year when this part of the benchmark made more modest gains.

Fund selection

What worked and why?

The SCOR Catastrophe Bond fund, which effectively receives premiums for taking on the risk of hurricane or earthquake property damage from insurance companies, within the MI Select Managers Alternative fund has had another strong year.



What didn't work and why?

An overweight position to sovereign bonds was a detractor but much of the drag was offset by an underweight position to corporate bonds.

What didn't work and why?

The Lumyna Commodity Alpha strategy fell -2.5% over 2024. December was a challenge as natural gas prices rallied due to a cold winter forecast coupled with production decreases, driving a tighter market for the commodity. Our approach with absolute return is to diversify across strategies and fortunately, other funds more than offset this weakness.

The value of investments can fall and you may get back less than you invested.

Passive Plus MPS portfolio changes 2024

Asset allocation change highlights

In Q1, the Asset Allocation Committee made several changes to our tactical guidance. In February, we increased the allocation to U.S. equity and global property by 0.5% each, funded by reductions in cash and Absolute Return. In March, we raised the allocation to non-U.S. equity regions to neutral, while maintaining a positive stance on U.S. equities, again funded by a reduction in Absolute Return exposure.

In Q2, we made further changes. In April, we increased the allocation to U.S. equity by a further 0.5% and reduced cash. We also took advantage of weakness in the gold price to move overweight, funded by a reduction in global index-linked bonds. Additionally, we moved overweight on UK equities due to the improved economic backdrop, funded by reducing the cash allocation.

In Q3, we advised for no tactical changes, maintaining our overweight position in sovereign bonds and underweight position in corporate bonds. We believed that the overweight position in sovereign bonds was appropriate ahead of the forthcoming interest rate cutting cycle, and that corporate bonds did not provide adequate compensation for the level of risk.

In Q4, we made several changes. We increased our exposure to Asia ex Japan, funded by a reduction in UK equity, and further reduced our corporate bond allocation in favour of sovereign bonds. We also increased our allocation to gold, funded by a reduction in cash. Following the U.S. presidential election, we reduced our European equity allocation by 2% and increased our U.S. equity allocation by 2%, given the potential negative impacts of trade tariffs on European economies.

Fund change highlights

In Q1, we made several changes to portfolios. In January, we reduced the allocation to overseas sovereign bonds and increased the allocation to UK gilts, reflecting our preference for domestic bonds. In February, we decreased the BlackRock Sterling Liquidity fund and increased Fidelity Index US, while also increasing Schroder Global Cities and reducing Absolute Return strategies in alternatives. We believe the bad news in global property is largely reflected in prices, making it a more attractive opportunity.

In Q2, we continued to refine portfolios. In May, we increased the allocation to the Fidelity US Index fund again, reflecting our preference for the U.S. equity market, and decreased the BlackRock ICS Sterling Liquidity fund to fund the position. In June, we increased the UK midcap exposure and the allocation to gold in the MI Select Managers Alternatives fund, while reducing cash and index-linked bonds.

In Q3, we added the One River Risk Responders strategy to the MI Select Managers Alternatives fund, which should provide diversification and protection in case of a sharp equity market sell-off. We also increased our allocation to infrastructure investment trusts, taking advantage of attractive discounts. These changes aimed to enhance the overall resilience and potential for growth in our portfolio.

In Q4, we made further adjustments. In October, we increased the gold allocation and reduced corporate bond strategies, investing the proceeds in sovereign bonds. We also increased the allocation to the Fidelity Index Emerging Markets fund, which has exposure to China and surrounding regions. In November, we reflected the Asset Allocation Committee's guidance by reducing our allocation to Vanguard Developed Europe ex UK and increasing our allocation to Fidelity Index US, which provides broad market exposure to U.S.-listed equities.

Information is provided only as an example and is not a recommendation to pursue a particular strategy.

Asset Allocation Committee investment outlook

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

Cash

Although cash continues to offer a decent yield, we are underweight. We see continued scope for equity market gains, and gold to move higher.

Bonds

Government bond yields tend to move in a directionally similar fashion as central bank rate expectations. In the U.S., the market is currently pricing in 85 basis points of Federal Reserve (the Fed) rate cuts by this time next year. In the UK, market implied expectations are for 78 basis points in cuts. Our base case is that both the U.S. and UK experience decent economic growth over the next year. Our expectation is that inflation continues to slowly subside, but that there will be an element of stickiness. As such, we doubt central banks will reduce rates by more than what's already priced in. The upshot is that in this scenario, government bond prices probably don't have much upside. Nevertheless, we remain overweight, offsetting this with an underweight position in corporate bonds, where spreads are very tight. This positioning provides a hedge to our equity overweight if economic growth disappoints.

Global Equities

We expect the global economy to continue to expand, which is consistent with corporate profits going up. We also believe there's the potential for artificial intelligence (AI) themes to drive both strong economy-wide productivity and solid profit gains among the pick and shovel plays. There's a lot of momentum behind the stock market, and we believe it makes sense to stay on the right side of the trend. However, it doesn't appear to be a great time to raise our exposure further. For one, there's limited room for cyclical economic growth. With most economies close to full employment and high labour force participation, there isn't much scope for workers on the sidelines to get a job, earn an income, and increase aggregate consumption. Meanwhile, equity sentiment is bullish, with the dominant market emotion being one of 'greed' rather than 'fear'. The implication is that a lot of good news is already in the price. Finally, U.S. equity valuations are unappealing. Valuations don't work as a good predictor of medium-term returns, but eventually, the medium-term becomes the long-term. As such, we maintain only a modest global equity overweight.

Alternatives

Gold has corrected from overbought territory following the U.S. election. Looking ahead, there are both cyclical and structural factors supporting gold. These include the scope for real bond yields to continue to decline, and central banks diversifying their reserve holdings out of the U.S. dollar and other developed world currencies. Gold also acts as a good hedge against several risks. Turning to property, while fundamentals are challenging in the office space, the market cap weighting of this subsector is small. The backdrop is notably brighter in other REIT (Real Estate Investment Trust) subsectors. We maintain a neutral position.

→ UK Equities

UK relative performance should continue to be closely linked to value versus growth style performance, and there are reasons to believe the outlook for the latter remains brighter. However, some diversification into the value plays that the UK is so heavily weighted in makes sense at this stage, in our view. Although the domestic economic outlook is less important for UK equity relative performance given its high international exposure, it still matters. Indeed, there's a positive relationship between the performance of UK versus global gross domestic product and UK versus global equity performance. We suspect Labour will have some success in boosting economic growth. However, the pathway to success isn't guaranteed. The UK equity market trades on very undemanding valuation multiples.

↑ U.S. Equities

A key concern with regards to U.S. equity exposure relates to valuation. Equity valuation multiples and the valuation of the dollar both appear stretched. Nevertheless, we're more optimistic on U.S. equities than other regions. The secular outlook appears relatively bright for the technology stocks the U.S. is so heavily weighted in. The main upside risk for the global equity market over the next few years is if an 'AI boom' scenario unfolds. With the Fed now cutting rates, a weaker version of the second half of the 1990s is a possibility this cycle. Back then, excitement linked to the growth of the internet drove gains. This cycle, AI could be the driver. Following November's presidential election victory of Donald Trump, we've boosted our U.S. equity exposure. In a trade war, the country with the trade deficit stands to win most (or lose the least), and the U.S. runs trade deficits against many countries. Trump's trade policies give the U.S. a better chance of maintaining its growth advantage versus the rest of the world. Relatively strong growth could boost the U.S. dollar, providing support to U.S. equity relative performance in common currency terms. In the event of a global trade war, the U.S. might also benefit from its relatively defensive sector composition.

↓ Europe ex-UK Equities

We remain underweight Europe ex UK. The European Union (EU) will be in Trump's sights given its big trade surplus versus the U.S. The EU also has additional growth headwinds coming from its two biggest economies. In France, the new government has just collapsed, and political uncertainty is high. The next government will be confronted with the same fiscal reality and will likely be forced to take steps to reduce the deficit, which should weigh on growth. Germany continues to struggle, with its automobile companies under pressure from cheap Chinese electric vehicles. More broadly, its export sector is under pressure due to weak Chinese domestic demand.

↑ Japan

There's momentum behind shareholder-friendly reform in Japan, which could help drive a further expansion in relatively depressed price-to-book multiples. However, demographics amount to a major structural headwind for Japanese equity relative performance. Meanwhile, with the unemployment rate low and labour force participation high, Japan doesn't have much scope to put idle economic resources to work to drive cyclical growth. Despite low price-to-book multiples, Japan doesn't stand out as cheap, in our view. Indeed, it trades at a premium to the world ex U.S. market on 12-month forward price/earnings.

Asia ex-Japan Equities

The Chinese authorities appear to be taking the deflation risk more seriously. To successfully boost inflation, the authorities will try to stoke demand growth. The combination of higher inflation, stronger growth and declining real interest rates is a supportive backdrop for equities. The Chinese housing market remains weak, but the authorities are incentivised to drive an improvement as soon as possible. Given that over 90% of the Chinese population own their own home, they'd be risking a breakdown in social instability (who they're very keen to avoid) if house prices decline much further. China and Hong Kong equities appear oversold on a medium-term time horizon. We acknowledge that the change in tack by the authorities doesn't alter the fact that the structural headwinds leaning against China haven't gone away. However, there are structural bright spots in the Asia ex Japan equity index, including India and Taiwan.

Emerging Markets ex-Asia

Brazil, Saudi Arabia, South Africa, Mexico and the United Arab Emirates are the countries with the highest market cap weightings in the EM ex Asia equity index, making it very commodity exposed. We don't expect much upside to commodity prices in an environment where global growth is slowing. That said, EM ex Asia remains very cheaply valued.



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