MONTHLY REPORT
APRIL 2024

PENGANA WHEB SUSTAINABLE IMPACT FUND

DESCRIPTION

The Pengana WHEB Sustainable Impact Fund invests in companies with activities providing solutions to sustainability challenges. WHEB have identified critical environmental and social challenges facing the global population over coming decades including a growing and ageing population, increasing resource scarcity, urbanisation and globalisation. The Fund invests in companies providing solutions to these sustainability challenges via nine sustainable investment themes – five of these are environmental (cleaner energy, environmental services, resource efficiency, sustainable transport and water management) and four are social (education, health, safety and well-being). WHEB's mission is 'to advance sustainability and create prosperity through positive impact investments.'

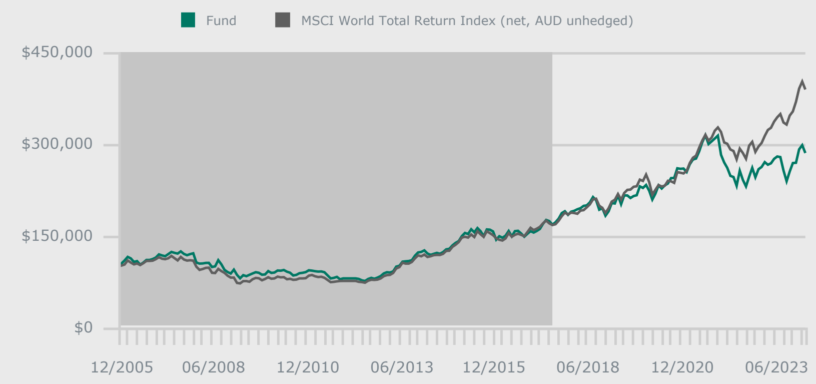
PERFORMANCE TABLE

NET PERFORMANCE FOR PERIODS ENDING 30 Apr 2024[1]

	1 MTH	1 YEAR	3 YEARS P.A.	5 YEARS P.A.	SINCE INCEPTION P.A.
WHEB Sustainable Impact Fund	-4.3%	7.2%	1.3%	5.7%	
Strategy (partial simulation – see below)					5.9%
MSCI World Total Return Index (net, AUD unhedged)	-3.2%	20.4%	11.9%	12.2%	7.7%

PERFORMANCE CHART

NET PERFORMANCE SINCE INCEPTION[2]



TOP HOLDINGS (ALPHABETICALLY)

Agilent Technologies Inc	Health Care
CSL Ltd	Health Care
Danaher Corp	Health Care
Ecolab Inc	Materials
ICON PLC	Health Care
Keyence Corp	Information Technology
Linde PLC	Materials
Schneider Electric SE	Industrials
Thermo Fisher Scientific Inc	Health Care
Xylem Inc/NY	Industrials

SECTOR BREAKDOWN

Consumer Discretionary	3%
Health Care	33%
Industrials	28.9%
Information Technology	23%
Materials	11.4%
Cash	0.7%

CAPITALISATION BREAKDOWN

2-10bn	21.2%
10-20bn	12%
>20bn	66%
Cash	0.7%

CUSTOM SECTOR BREAKDOWN

Health	29.9%
Resource Efficiency	25.3%
Sustainable Transport	7.1%
Environmental Services	9.8%
Water Management	11%
Safety	8.6%
Cleaner Energy	4.4%
Wellbeing	1.5%
Education	1.8%
Cash	0.7%

REGION BREAKDOWN

North America	43.2%
Europe ex-UK	34.7%
Japan	6.3%
UK	9.7%
Asia Pacific	5.3%
Cash	0.7%

NAVIGATING POLICY UNCERTAINTY IN SUSTAINABLE INVESTING – WHY STOCK SELECTION MATTERS

COMMENTARY

Global equities endured a challenging month, with persistent inflation and some economic strength fuelling market fears that central banks will not ease monetary policy as quickly as previously hoped. This economic resilience and the danger of an escalation in the Middle East boosted energy prices, which when coupled with lower interest rate sensitivity supported the outperformance of value over growth companies as well as non-sustainable over sustainable companies.

In this month's commentary, Victoria MacClean delves into the complex mix of issues including climate policy, trade policy and regional protectionism, and the demand environment. With these factors pointing in different directions in terms of whether they are "good" or "bad" for sustainability, Victoria looks at how they are influencing our near- and longer-term thinking.

Market Review

April was a challenging month for global equity markets. The MSCI World Index was down -3.2%.

Persistent inflation, and some economic strength, fuelled market fears that central banks will not ease monetary policy as quickly as previously hoped. That economic resilience and the danger of an escalation in the Middle East boosted commodities prices. A combination of rising energy prices and lower interest rate sensitivity also supported value stocks, which outperformed their growth counterparts.

The US was the weakest performing region as valuations came under pressure from rising bond yields. UK equities were the best performing, supported by their high exposure to commodity and energy companies. Energy was the strongest sector in the global market, followed by Materials and Utilities, while Consumer Discretionary and Technology were the weakest.

Fund Review

The fund delivered negative performance over the month of -4.3%.

The Cleaner Energy theme detracted, including specific weakness in solar tracker maker Nextracker. Concerns about growth in the US solar market weighed on the stock. We think this is misplaced, not least because of the company's global footprint. The Safety theme further hurt performance with both Steris and MSA Safety making negative contributions, on no particular news.

On the other side of the ledger, Trane in the Resource Efficiency theme was the largest positive contributor. The company delivered another beat-and-raise quarterly results driven by strong demand for its highly efficient commercial heating and cooling systems in Americas. The growth was broad-based across market verticals including data centres, healthcare, and education.

At a thematic level, Water Management was the largest positive contributor, with holdings including Veralto performing well. Veralto reported positive results in the company's second quarter as a standalone company, after its spin out of another portfolio company, Danaher. Better than expected margin expansion resulted in a raise of their full year guidance.

Outlook

Following the fall in inflation, sentiment in global equities is more positive with markets expecting that the central bank tightening is nearing its end. This environment should be more supportive for the generally smaller and more growth-orientated impact stocks we invest in.

Meanwhile, several of our key sustainability markets have cyclical challenges to overcome, as well as repositioning around China's changing role in global manufacturing. We remain convinced that the companies we invest in retain the competitive edge to deliver the transition to a more sustainable economy.

Navigating policy uncertainty in sustainable investing – why stock selection matters

By Victoria MacClean

There have recently been negative sentiment towards electric vehicles (EVs), headwinds facing Clean Energy companies and a risk that Trump would try to repeal elements of the Inflation Reduction Act (IRA) in the US if he comes into power later this year.

Underneath the surface of those topics is a complex mix of issues including climate policy, trade policy and regional protectionism, and the demand environment. Some of these factors are pointing in different directions in terms of whether they are "good" or "bad" for sustainability and for companies in our portfolio.

In this article, we will look at those issues and how they are influencing our thinking, both in the near-term and over a longer time horizon. While the picture may be complicated, we believe that there is still significant support for the structural sustainability drivers that underpin our investments.

Climate policy

Over the past few years, we've seen the launch of several high-profile climate package policies. The US introduced the Inflation Reduction Act (IRA) and the Infrastructure Investment and Jobs Act (IIJA), Europe announced its Green Deal, and China formalised its "dual-carbon goals" with 2030 and 2060 emissions targets.

These packages support growth across multiple themes and sub-themes within the portfolio. As an example, the IRA and IIJA cover renewable energy, electric vehicles, hydrogen, water infrastructure, and buildings. Together they invest over $1 trillion to address climate needs.[1]

Last year, more solar panels were installed in China than the US installed in its entire history[2] and the government is likely to exceed its renewables installation and non-fossil energy targets.[3] China is also the world's largest EV market with sales expected to account for half of all car sales this year.[4] This compares to an expected penetration rate of around 11% in the US and 28% in Europe.

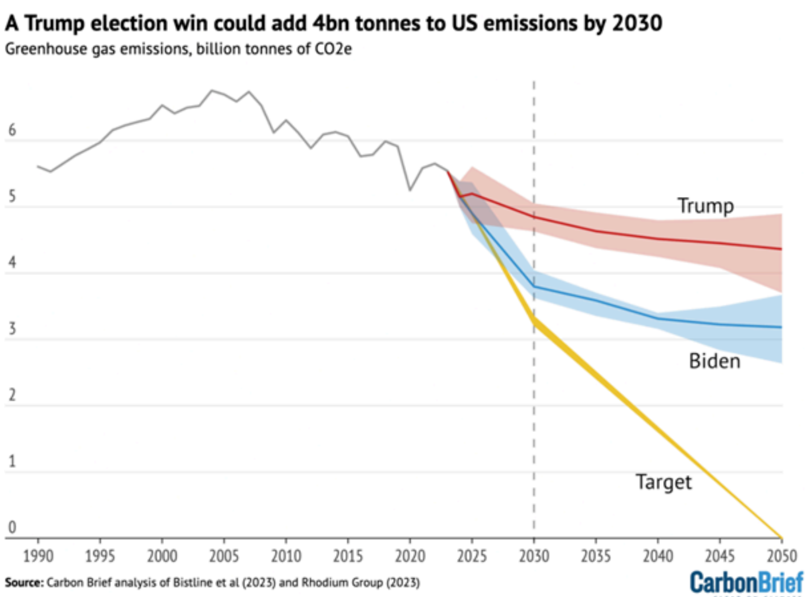
Against that backdrop, it may seem surprising that Clean Energy and Sustainable Transport returns have lagged within the portfolio, but we believe there are three reasons for this. First, the risk that policy may change. Second, protectionist trade policies around the world are complicating the impact of climate policies. Third, there is a question about which companies will be able to generate positive equity value from addressing climate change.

Policy risk

We wrote about the growing trend of watered-down environmental policies in a previous blog.[5] Since then, we've seen the EU making concessions to farmers following protests,[6] the Scottish government scrapping its ambitious net-zero targets after a damning report by its independent advisers who warned that they were no longer credible,[7] and the US Environmental Protection Agency (EPA) watering down tailpipe emission limits to allow a slower adoption rate of EVs.[8]

Despite the headlines, things are nonetheless moving in the right direction. The International Energy Agency (IEA) predicts that demand for coal, oil and natural gas will peak this decade even without any new policies.[9] A study by Ember released in early May goes even further, anticipating that global power sector greenhouse gas emissions will peak as soon as 2024.[10] Once up and running, currently announced manufacturing capacity additions in solar and batteries would be enough to meet demand by 2030.[11] In April the G7 countries, which together account for 20% of global emissions, also reached a milestone agreement to phase out the unabated use of coal by 2035. This sends a clear message to the rest of the world.

It seems clear that the tide has turned. The issue now is one of speed not direction. The potential for repeal of the IRA under a Trump administration is a good example. Emissions would still decline but they would fall at a much lower rate than under Biden's policies. But both of those scenarios still fall short of what's needed.[12]



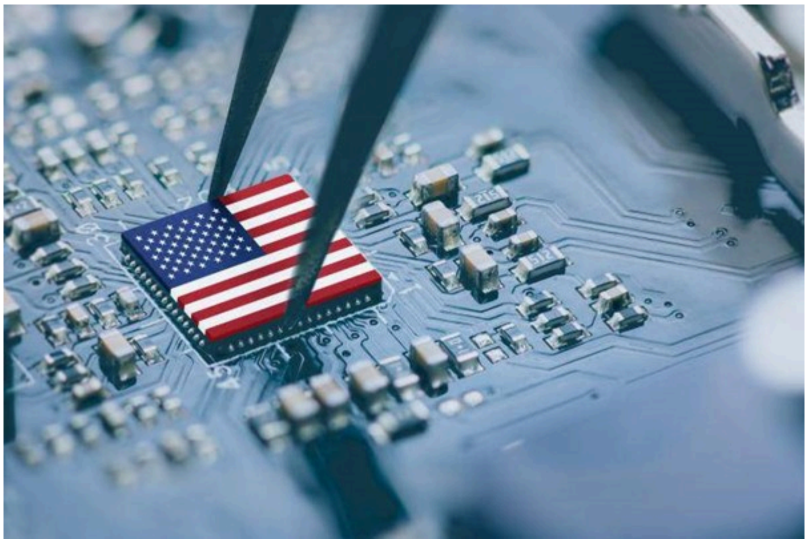
Green trade tensions

Policy support is uncertain and needs to improve. However, we see increasing positive momentum from companies setting their own climate and nature-based targets which drives demand for our investments. Trane Technologies and Schneider Electric are two examples in heating, ventilation, and air conditioning (HVAC) and electric components and software respectively which are benefiting from this in their results.

One complicating factor in the current environment is the way that climate policy is interacting with trade policy. For example, the US has introduced several measures to severely limit the import of Chinese solar panels. China on the other hand has excess supply because their weak economy is supressing demand. That excess can't go to the US and so Europe has to absorb a lot of it, resulting in pressure on pricing.[13]

The EV supply chain is another example of this complicated dynamic. EVs contain more semiconductor content than traditional vehicles so they are a great opportunity for semiconductor companies. However, there is a big push in China to grow the local value chain which means Chinese EV manufacturers are under pressure to use as much Chinese content as possible.

In Europe and the US there is also an increasing focus on creating a more regional supply chain. The US CHIPS Act and the EU Chips Act both have the aim of increasing supply chain resilience and protecting against Chinese technology advancements for security reasons. As a result, the US is projected to triple its manufacturing capacity by 2032, the fastest rate of growth globally.[14]



What does it mean for investment opportunities?

The answer is: it depends. There are a lot of moving parts to this complex landscape. That's why we think bottom-up analysis and a fundamentals-driven approach to investing is so important in the sustainability space.

One area of focus for us is technology innovation creating a defensible moat around the business. If a company has technology that others can't replicate this can help protect against some of the protectionist measures. Infineon is a good example – it's the number one player in Micro Controller Units (MCUs). While Chinese companies are catching up in some technologies, they are significantly behind in MCU technology with a very small market share. Infineon's head start and continued focus on product development stands the company in good stead to defend its position.

Another consideration is end-market exposure. In Clean Energy, First Solar is US-focused and a clear beneficiary of the shift to more US manufacturing. Many of our environmental themes also have diverse industry exposures, including exposure to commercial customers where the economic case is more compelling and less sensitive to interest rates.

In Sustainable Transport we have no direct original equipment manufacturer (OEM) exposure. We believe our holdings should benefit regardless of which car brands are the winners and the geographic mix of growth. Aptiv is a good example. It's a tier one supplier of electrical components and software which has been announcing increasing design wins with Chinese OEMs as those companies take share in the global market.

There will be winners and losers in the transition. We think the companies that can capture the opportunities in the shift to a green economy will be well placed to outperform over the coming years.

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[1] https://www.brookings.edu/articles/why-workforce-development-is-crucial-to-new-infrastructure-and-clean-energy-investments/

[2] https://www.vox.com/climate/24139383/climate-change-peak-greenhouse-gas-emissions-action

[3] https://www.carbonbrief.org/guest-post-why-china-is-set-to-significantly-overachieve-its-2030-climate-goals

[4] https://www.ft.com/content/5b8a02ab-2d0d-4459-85fb-4ae500de494f

[5] https://www.whebgroup.com/our-thoughts/environmental-policies-vs-economic-realities-unravelling-the-conundrum-amid-a-cost-of-living-crisis

[6] https://www.politico.eu/article/france-tractors-farmer-protests-gabriel-attal-emmanuel-macron/

[7] https://www.politico.eu/article/scottish-government-abandons-flagship-climate-goal-mari-mcallan-says/

[8] https://www.reuters.com/business/autos-transportation/biden-administration-relax-ev-rule-tailpipe-emissions-ny-times-2024-02-18/

[9] https://iea.blob.core.windows.net/assets/ac433d3a-3f9e-482e-b8bf-17653b1c4024/NetZeroRoadmap-2023Update-ExecutiveSummary.pdf

[10] https://ember-climate.org/insights/research/global-electricity-review-2024/#about

[11] https://iea.blob.core.windows.net/assets/ac433d3a-3f9e-482e-b8bf-17653b1c4024/

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[12] https://www.vox.com/climate/24139383/climate-change-peak-greenhouse-gas-emissions-action

[13] https://www.ft.com/content/2ea6bf6d-04e9-453b-a35f-cd6431cfc7bf

[14] https://www.semiconductors.org/america-projected-to-triple-semiconductor-manufacturing-capacity-by-2032-the-largest-rate-of-growth-in-the-world

FEATURES

APIR CODE	HHA0007AU
REDEMPTION PRICE	A$ 1.567
FEES *	Management Fee: 1.35%
MINIMUM INITIAL INVESTMENT	$10,000
FUM AT MONTH END	A$ 264.51m
FUND INCEPTION DATE	31 October 2007

FUND MANAGERS

Ted Franks
Partner, Head of Investment

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1. From August 2017, performance figures are those of the Pengana WHEB Sustainable Impact Fund's class A units (net of fees and including reinvestment of distributions). The strategy's AUD performance between January 2006 and July 2017 has been simulated by Pengana from the monthly net GBP returns of the Henderson Industries of the Future Fund (from 1 January 2006 to 31 December 2011) and the FP WHEB Sustainability Fund (from 30 April 2012 to 31 July 2017). This was done by: 1) converting the GBP denominated net returns to AUD using FactSet's month-end FX rates (London 4PM); 2) adding back the relevant fund's monthly ongoing charge figure; then 3) deducting the Pengana WHEB Sustainable Impact Fund's management fee of 1.35% p.a. The WHEB Listed Equity strategy did not operate between 1 January 2012 and 29 April 2012 – during this period returns are zeroed. The Henderson Industries of the Future Fund's and the FP WHEB Sustainability Fund's GBP net track record data is historical. No allowance has been made for buy/sell spreads. Please refer to the PDS for information regarding risks. Past performance is not a reliable indicator of future performance. The value of the investment can go up or down.
2. The Fund incepted on 31 October 2007 as the Hunter Hall Global Deep Green Trust. The Fund was relaunched on 1 August 2017 as the Pengana WHEB Sustainable Impact Fund employing the WHEB Listed Equity strategy. This strategy was first employed on 1 January 2006 by the Henderson Industries of the Future Fund and currently by the FP WHEB Sustainability Fund.
3. Annualised standard deviation since inception.
4. Relative to MSCI World Total Return Index (net, AUD unhedged)

* For further information regarding fees please see the PDS available on our website.

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