PENGANA
CAPITAL GROUP

MONTHLY REPORT
SEPTEMBER 2023

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.'

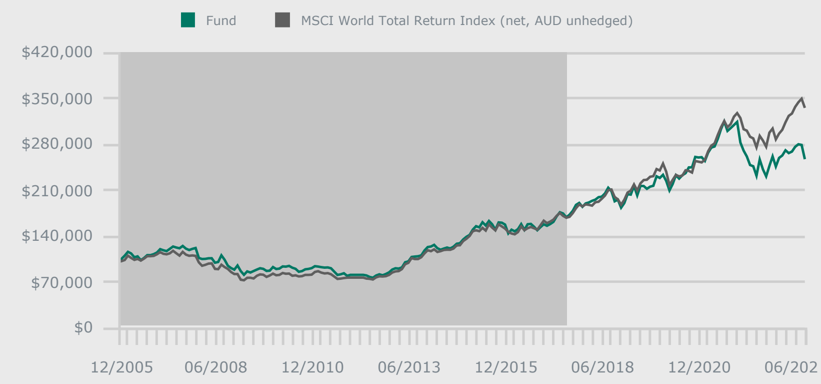
PERFORMANCE TABLE

NET PERFORMANCE FOR PERIODS ENDING 30 Sep 2023[1]

	1 MTH	1 YEAR	3 YEARS P.A.	5 YEARS P.A.	SINCE INCEPTION P.A.
WHEB Sustainable Impact Fund	-7.8%	11.3%	1.7%	4.3%	
Strategy (partial simulation – see below)					5.5%
MSCI World Total Return Index (net, AUD unhedged)	-4.0%	21.5%	11.9%	9.7%	7.1%

PERFORMANCE CHART

NET PERFORMANCE SINCE INCEPTION[2]



TOP HOLDINGS (ALPHABETICALLY)

ANSYS Inc	Information Technology
Autodesk Inc	Information Technology
CSL Ltd	Health Care
Danaher Corp	Health Care
ICON PLC	Health Care
Linde PLC	Materials
MSA Safety Inc	Industrials
STERIS PLC	Health Care
Thermo Fisher Scientific Inc	Health Care
Trane Technologies PLC	Industrials

SECTOR BREAKDOWN

Consumer Discretionary	3.5%
Consumer Staples	1.8%
Health Care	29.2%
Industrials	27.6%
Information Technology	27.2%
Materials	9.8%
Cash	1%

CAPITALISATION BREAKDOWN

2-10bn	31.3%
10-20bn	9.3%
>20bn	58.4%
Cash	1%

CUSTOM SECTOR BREAKDOWN

Health	25.5%
Resource Efficiency	29.7%
Sustainable Transport	9.3%
Environmental Services	11.2%
Water Management	6.6%
Safety	6.6%
Cleaner Energy	5%
Wellbeing	3.4%
Education	1.7%
Cash	1%

REGION BREAKDOWN

North America	67.7%
Europe ex-UK	14.9%
Japan	7.7%
UK	6.4%
Asia Pacific	2.4%
Cash	1%

A WALK DOWN WATER STREET – HIGHLIGHTS FROM OUR RECENT US RESEARCH TRIP

COMMENTARY

In this month's commentary, Claire Jervis shares some highlights from her recent US research trip including Xylem's 'Reservoir Center for Water Solutions' which aims to speed up progress in finding solutions to the world's water challenges. Claire also attended the the Jefferies' IT Hardware and Semiconductor summit in Chicago which showcased potential opportunities in the lidar space with these sensors emerging as a 'new frontier' for the electric vehicle industry.

We are delighted for WHEB to have won the ESG Clarity Award for 'Best ESG Fund House (Active)' in recognition of their commitment to sustainable investing with the judging panel commenting that "in addition to WHEB's track record as an active impact investor in the UK, there is arguably further evidence in its submission of making continued efforts to drive forward positive change in the sustainable investing market."

We are pleased to include a special feature written by Seb Beloe and Charlie Crossley, an Investment Engagement Manager at Friends Provident Foundation. "Unleashing the potential of impact measurement in listed equities: The crucial role for asset managers" presents a compelling case for impact investing in listed equities.

Performance Commentary

Market Review

For the month overall, the MSCI World Index fell -4.0%. US equities sold off in September with the "Magnificent Seven" mega-cap tech stocks having a weaker month after their strong year.

In a key macroeconomic intervention, despite leaving interest rates unchanged, the US Federal Reserve Bank made it clear that, while inflationary pressures may be easing, interest rates are likely to remain higher for longer. At the same time, economic indicators continue to weaken.

Surging oil prices, due to lower global output also weighed on investors. Higher oil prices could prove problematic for central banks if headline inflation begins to reaccelerate.

Renewable energy stocks sold off sharply as the sector battled with negative sentiment linked to higher interest rates. Some companies in the industry have agreed long-term contracts, fixing the price at which they would sell energy before developing the projects. The surge in global inflation and rising interest rates have meant these projects have been hit by higher costs and the high levels of borrowing have become more expensive to service.

The sector's challenges were compounded by weakening regulatory support. The UK government decided to push back net-zero targets to 2035, including delaying the bans of petrol and diesel cars, and new gas boiler sales. Climate watchdogs and industry leaders warned Britain risked losing a lead on green technology.

In the global equity market, Energy (i.e., oil and gas) and Financials were the strongest sectors while Technology and Real Estate were the laggards. Small and mid-cap stocks underperformed large caps.

Fund Review

With no exposure to Energy and Financials (being sectors that do not solve sustainability challenges), as well as having a bias toward mid-cap stocks, the Fund delivered a negative relative return during the month.

Positively, the Education theme contributed positively due to the holding in Grand Canyon Education. Additional positive contributions came from JB Hunt (Sustainable Transport) and AstraZeneca (Health). The freight recession has appeared to come to an end, benefiting JB Hunt. While there was no significant news, AstraZeneca did have several incrementally positive data readouts in late-stage trials.

On the other side of the ledger, Smurfit Kappa within the Environmental Services theme was the largest detractor. The company announced a merger with US company WestRock to create the world's largest listed paper and packaging company, which was not received well by the market due to the premium paid. We would also have preferred a lower premium but see the strong business rationale for the deal, which we expect to create additional shareholder value over time.

Elsewhere in the portfolio, the sell-off in renewables further impacted US holdings SolarEdge and First Solar. The stocks struggled due to ongoing concerns about demand amid persistent high-interest rates, as well as negative sentiment due to the growth headwinds in US residential solar and the risk of increasing competition. However, we remain convinced of their prospects over the long-term, due in part to an expectation that First Solar will see strong demand for utility-scale solar (being one of the cheapest forms of energy and which is set to receive significant support from the US Inflation Reduction Act), as well as supportive demand for European commercial solar benefitting SolarEdge's inverter and power optimiser business, even as US residential demand slows.

Outlook

The outlook remains mixed. The US economy has remained remarkably resilient but there have been signs of weakness in Europe, and China has been suffering from weak domestic demand as well as slowing exports. Globally, export growth has been impacted by a slowdown in manufacturing industries, leading the World Trade Organisation to halve its full-year forecasts recently.

Labour markets have held up well as worker shortages have kept wages high and unemployment low. However, there are emerging risks to growth in the US including the recent auto strikes; rising oil prices; dwindling pandemic savings; the rising burden of auto loan repayments; and the resumption of student loan repayments after a three-year freeze.

Overall, there remain several headwinds to the economy in the near term. We continue to believe that the diversification and the quality of the portfolio should provide some resilience as set forth below.

- The portfolio has exposure to a range of end markets and industries. Economic shocks are unlikely to affect all companies to the same extent at the same time. For example, within the semiconductor space, Infineon has experienced resilient demand due to its exposure to EVs, in contrast with many peers who have seen a slowdown in growth. Other areas of the portfolio that are less exposed to the economic cycle generally include pharmaceutical companies like Genmab and AstraZeneca. Companies like Grand Canyon, an education provider, can even be counter-cyclical as people invest more in education when unemployment increases.
- Geographic diversification plays a similar role in providing resilience as companies in the portfolio have a range of geographic exposures. In the current environment, companies with higher China exposure are seeing more headwinds than those skewed towards the US. The performance of companies like Advanced Drainage Systems, Trane Technologies, and Steris, reflects their high US exposure and the relative strength of the US economy.
- The benefit of quality comes through in how companies navigate difficult periods. In general, portfolio

companies have done a good job of passing inflation on to customers through pricing, as well as managing their cost base. Strong balance sheets and cash generative business models also provide resilience at the operational level in a downturn. For example, **Spirax-Sarco's** growth is linked to the industrial cycle, but the company has an excellent track record of delivering growth well above the industry average and maintaining margins even during periods of slower growth, as we are seeing currently.

When inflation eases and interest rates stabilise, we believe company fundamentals will begin to drive share price returns to a greater extent. When that happens, we believe the portfolio will benefit due to its structural overweight to growth and quality which we see as positive fundamental drivers over the medium- to long-term.

A walk down Water Street – highlights from our recent US research trip

By Claire Jervis

America is one of the most innovative countries in the world. It is also the wealthiest, contributing nearly 30% of the world's spending on research and development[1]. It is no surprise, then, that American companies feature prominently in our impact investment universe.

In September, I took the opportunity to visit Chicago and Washington D.C. to meet with some of these American sustainability leaders. I met with 14 companies in all – some we own, many we don't. It was a great opportunity to catch up with businesses we've known for years on their home turf, while scouting for new opportunities.

A particular highlight was my visit to Xylem's global headquarters, in Washington D.C. Xylem is America's champion for improving global access to clean water. Their solutions help customers use water more efficiently, detect leaks, and prevent polluted water from entering communities. We've been investors since 2014 and remain hugely supportive of their work.

Located on Water Street, overlooking the Potomac River, Xylem's 'Reservoir Center for Water Solutions' is something quite special. Xylem shares their HQ with 33 leading organisations in the water industry. The collaborative workspace is home to non-profits such as Water for People and EarthEcho, as well as policy organisations like the US Water Alliance and the Aspen Institute. Its purpose is to bring together the greatest minds from across the water sector, to speed up progress in finding solutions to the world's water challenges.

During my visit, I had the opportunity to pick the brain of Austin Alexander, Xylem's VP for Sustainability and Social Impact. We had a wide-ranging conversation covering Xylem's water-saving technologies, their own plans to reach Net Zero emissions, and the diversity of Xylem's leadership team. I was also able to discuss business fundamentals with Mike Travers, of the investor relations team. I came away feeling assured that Xylem is a clear impact and sustainability leader which deserves its space in our portfolio.

During my time in the States, I also joined Jefferies' IT Hardware and Semiconductor summit in Chicago. This summit gave me the opportunity to meet with loads of companies operating in this sector, to uncover hidden gems and emerging trends.

I was particularly intrigued by my meetings with two companies operating in the lidar space. Lidar sensors are emerging as a 'new frontier' for the electric vehicle industry. They are used to detect and respond to objects around the car, to enhance the safety of passengers and other road users. One company I met with thinks their sensors can reduce the rate of road traffic accidents by up to 60% compared to today's average[2].

These sensors are technically challenging to design and manufacture, and they are also expensive. This is why we don't see them much on cars today, and why we won't be investing immediately. But this complexity also creates an opportunity for the company, or companies, that can rise to the challenge. We will be watching this space with interest over the next few years.

The opportunity to meet company management teams in-person is often extremely valuable. While video calls are certainly very productive, they can't replicate the immersive experience of a sector conference or company visit.

1 https://ncses.nsf.gov/pubs/nsb20221/u-s-and-global-research-and-development#:~:text=R20has%20declined.-,Global26D,global26D%20(Figure%2012).

2 This lidar company's website provides a great demo – keep scrolling! https://www.innovusion.com/

FEATURES

APIR CODE	HHA0007AU
REDEMPTION PRICE	A$ 1.4109
FEES *	Management Fee: 1.35%
MINIMUM INITIAL INVESTMENT	$10,000
FUM AT MONTH END	A$ 252.79m
FUND INCEPTION DATE	31 October 2007

FUND MANAGERS

Ted Franks
Partner, Head of Investment

Seb Beloe
Partner, Head of Research

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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