PENGANA
CAPITAL GROUP

MONTHLY REPORT
SEPTEMBER 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.'

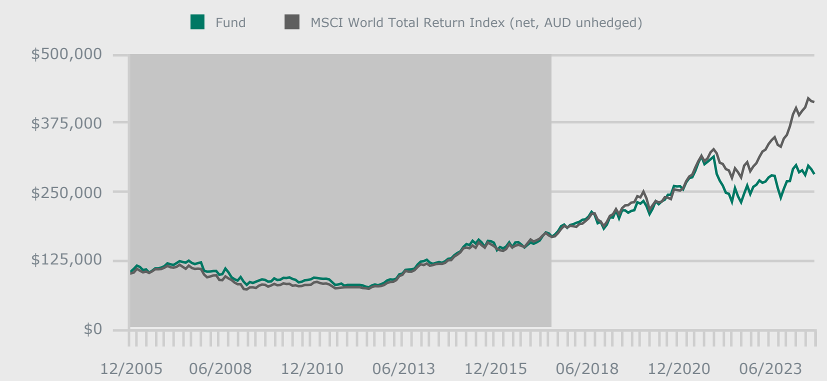
PERFORMANCE TABLE

NET PERFORMANCE FOR PERIODS ENDING 30 Sep 2024 [1]

	1 MTH	1 YEAR	3 YEARS P.A.	5 YEARS P.A.	SINCE INCEPTION P.A.
WHEB Sustainable Impact Fund	-3.1%	9.7%	-2.1%	5.6%	
Strategy (partial simulation – see below)					5.7%
MSCI World Total Return Index (net, AUD unhedged)	-0.4%	23.1%	10.6%	12.4%	7.9%

PERFORMANCE CHART

NET PERFORMANCE SINCE INCEPTION[2]



TOP HOLDINGS (ALPHABETICALLY)

Agilent Technologies Inc	Health Care
Autodesk Inc	Information Technology
Bureau Veritas SA	Industrials
Danaher Corp	Health Care
Ecolab Inc	Materials
Keyence Corp	Information Technology
Schneider Electric SE	Industrials
STERIS PLC	Health Care
Thermo Fisher Scientific Inc	Health Care
Xylem Inc/NY	Industrials

SECTOR BREAKDOWN

Consumer Discretionary	2.7%
Health Care	30.1%
Industrials	31.2%
Information Technology	23.3%
Materials	10.5%
Utilities	1.8%
Cash	0.3%

CAPITALISATION BREAKDOWN

2-10bn	18.8%
10-20bn	9.7%
>20bn	71.2%
Cash	0.3%

CUSTOM SECTOR BREAKDOWN

Health	25.9%
Resource Efficiency	26.2%
Sustainable Transport	7.9%
Environmental Services	8.4%
Water Management	14.1%
Safety	11.3%
Cleaner Energy	4.4%
Education	1.5%
Cash	0.3%

REGION BREAKDOWN

North America	46.2%
Europe ex-UK	35.1%
Japan	6.3%
UK	10.9%
Asia Pacific	1.2%
Cash	0.3%

NOT ALL CARBON OFFSETS ARE CREATED EQUAL

COMMENTARY

The MSCI World Index was down -0.4% in September amidst continued growth fears at the beginning of the month, although the US Federal Reserve's subsequent 0.5% interest rate cut helped markets recover some ground. Healthcare was one of the worst performing sectors, and the Fund's overweight to the sector led to relative underperformance.

Did you know that carbon offsetting projects sit on a wide spectrum from high-quality to low-quality? In this month's commentary, Katie Woodhouse evaluates carbon offsetting and discusses the potential pitfalls of low-quality carbon offsetting which can undermine its effectiveness.

Join Associate Fund Manager Claire Jervis for a webinar update, where she will discuss the Fund's current portfolio holdings, the factors influencing recent performance, and some of the market variables the investment team is considering moving forward. Register here.

Market Review

The strategy's benchmark MSCI World Index was down -0.4% in September. Continued growth fears sent markets off at the beginning of the month. After much anticipation, the Federal Reserve cut interest rates in the US by 0.5%, helping markets around the world to recover some ground. Market sentiment was also helped by China, which announced widespread monetary and fiscal stimulus measures to support economic growth at the end of the month.

On the other hand, European equity returns were muted. This was despite the European Central Bank delivering its second rate cut in September, taking interest rates to 3.5%. Economic data reinforced the sluggish nature of the eurozone recovery so far this year.

Utilities and Consumer Discretionary were the strongest sectors in the global market over the month while Energy & Healthcare were the laggards.

Fund Review

The fund returned -3.1% over the month. The Health theme was the largest detractor from returns, with negative contributions from several holdings. These included AstraZeneca, which struggled after the failure of two drug trials. AstraZeneca has an industry-leading pipeline and these drug trials are only a small part of it, but naturally the market was disappointed.

Diabetes and obesity specialist drugmaker Novo Nordisk also suffered a setback. Phase 2 data of small molecule weight loss drug monlunabant showed lower than anticipated weight loss and was seen as disappointing. This drug development is not part of Novo's market-leading GLP-1 obesity franchise, but the market is interested in Novo's ability to maintain its leadership position.

Resource Efficiency, on the other hand, contributed positively to returns. Trane, a world leader in air conditioning systems and services, continued to see strong demand for sustainable HVAC solutions, in particular from data centres. Autodesk, with leading products and services that drive resource efficiency in products and buildings, performed well after a strong endorsement from a leading broker.

Outlook

In the short-term, we see a divergence in the operating environments of the sectors in which we invest. Some, like electric vehicles, remain more challenged as they adjust to weaker short-term demand. Others are seeing more promising signs. In the Health theme, for example, we see the inventory destocking process coming to an end as orders show signs of improvement. Finally, there are also several sectors where we are seeing strong positive momentum, such as electrification and environmental consulting.

We are also seeing significant political shifts. In Europe, significant gains for right-wing parties have increased concerns about the future of sustainability initiatives. However, there are reasons for optimism as the results of the UK and French elections suggested that voters haven't yet given up on climate action. Importantly, all eyes will be on the US election in November.

As in previous quarters, the long-term structural opportunities are being complicated by short-term macro concerns. With declining interest rates, the trend should benefit smaller, growth-oriented impact stocks, although the exact timing remains uncertain.

Not all carbon offsets are created equal

By Katie Woodhouse

As the world grapples with climate change, reducing greenhouse gas emissions (GHG) is at the forefront of global conversations. Carbon offsets have emerged as one tool to help tackle this problem. They offer a way for individuals and businesses to balance out their emissions by investing in projects that reduce or capture GHGs elsewhere.

Put simply, carbon offsets let you make up for your emissions by funding projects that remove or reduce an equivalent amount of carbon dioxide (CO_2) from the atmosphere. So, for example, if you take a flight that can't be avoided, you could buy carbon offsets that support reforestation or renewable energy projects to "cancel out" the GHGs associated with your flight.

However, there's a catch – not all carbon offsets are created equal. If we want to make a real difference, we need high-quality carbon offsets that deliver genuine, long-term benefits for the climate that are only used for residual emissions that remain after all feasible direct emission reduction actions have been taken.

The problem with low-quality carbon offsets

While carbon offsets can play an important role in providing flexibility and reducing the cost of a GHG reduction programme, the reality is that most offsets don't live up to this promise. Low-quality carbon offsets can do more harm than good, for several reasons:

1. **Lack of additionality:** This is when a project would have happened anyway without the funding from carbon offsets. If the offset doesn't lead to extra emission reductions, then the extra capital is wasted.
2. **Permanence issues:** Some projects, like tree planting, sound great, but what if those trees are cut down or destroyed later? The carbon they captured gets released back into the atmosphere, removing the initial benefit. This risk is all too evident in many areas of the world. In California this summer, 45,000 acres of trees that had been allocated for conservation and sold as carbon credits were destroyed in wildfires.
3. **Weak monitoring:** Without strong oversight, it's hard to know if the projects are doing what they claim. Poor-quality offsets often lack the proper checks to make sure emissions are really being reduced. For example, an FT investigation found that a Shell-operated carbon capture project in Alberta registered

carbon credits equivalent to double the amount of GHGs that were actually being captured by the facility.

Carbon offset best practice

A current debate in the industry revolves around when and how much a company should offset its emissions. The Science Based Targets initiative (SBTi) has traditionally taken a strict view on offsets, requiring companies to meet emission reduction targets primarily through direct reductions in their operations and supply chains. Offsets have been permitted only for residual, unavoidable emissions. And even here they have been limited to 10% of base-year emissions.

However, the SBTi recently announced an intention to revise its Corporate Net-Zero standard to enable an increased use of carbon offsets by companies to meet their goals. This prompted an immediate backlash from both SBTi employees and signatories concerned with greenwashing. In response, the SBTi clarified that no immediate changes to the standard had been made.

At WHEB, we believe that a reliance on offsets without a strong commitment to reducing emissions can delay meaningful climate action. We encourage all of our portfolio companies to research credible offsetting providers and to use offsets as a last resort, rather than a tool to postpone the more difficult task of reducing emissions. For example, we recently engaged with Arcadis, an environmental consultancy firm held in our strategy. Arcadis currently offsets all scope 1 and 2 emissions, and its management has confirmed that they will be "ramping up" efforts to directly reduce emissions to meet a 90% reduction target by 2035, with the remaining 10% of emissions covered by carbon offset projects.

Our Offsetting Partners

WHEB's approach to offsetting our operational emissions, is based on a review we conducted in 2023 to identify high-quality projects and providers that we could partner with on a long-term basis. In the end we chose two providers to offset our residual emissions.

Make it Wild: Make it Wild is a family-run business that purchases degraded agricultural land across North Yorkshire in the UK to regenerate natural woodland and create wetland habitats. As credits are sold, new trees are planted, photographed and mapped by drone and allocated to each buyer. The amount of carbon sequestered is based on research from the University of Leeds and the drone mapping process prevents double-counting.

Wilder Carbon: Wilder Carbon is a not-for-profit organisation that provides high-integrity, nature-based carbon offsets to buyers who are demonstrably reducing their own emissions. Wilder Carbon conducted due diligence on us as a potential purchaser of offsets. The process ensures that Wilder Carbon only work with organisations that align with the Wilder Carbon principles. The projects available on the Wilder Carbon platform all deliver multiple benefits such as locking up carbon and regenerating biodiversity as well as benefiting local people and communities, for example through flood prevention. The projects are externally validated to ensure the projects meet the Wilder Carbon Standards as well as their carbon and biodiversity uplift targets.

As more companies look to carbon offsets to meet their climate goals, we encourage buyers to focus on quality over quantity. Offset buyers should have access to detailed information about the projects they're supporting. Whilst no carbon credit is perfect, knowing how emissions reductions are calculated, verified, and monitored is key to making sure the offsets used are effective.

FEATURES

APIR CODE	HHA0007AU
REDEMPTION PRICE	A$ 1.5478
FEES *	Management Fee: 1.35%
MINIMUM INITIAL INVESTMENT	$10,000
FUM AT MONTH END	A$ 239.42m
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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