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UBAM – POSITIVE IMPACT EQUITY

Quarterly Comment | Q4 2019

For Qualified Investors in Switzerland or Professional Investors or Eligible Counterparties as defined by the relevant laws.

Market Comment

- Q4 2019 contained its fair share of highlights (and lowlights) under the general Sustainability banner. Beginning with the lowlights, the weeks running up to Cop 25 had been filled with some expectation that the original 2015 Paris voluntary targets could be upgraded or enhanced. The ultimate lack of progress resulting from the Madrid summit produced reactions of frustration and in some areas condemnation, that world leaders appeared more focused on the value of outstanding carbon credits and the share of historic emissions rather than burying hatchet and committing to a shared path of travel forwards. When the latest United Nations Environment Programme report published in November calculated a requirement for the globe to cut emissions by 7.6% per annum every year to achieve the 1.5-degree Paris Accord target, it seems unhelpful in the extreme for countries to continue to focus on the historical share of emissions. As we know climate change cannot be solved at the national level. Global emissions are already 4% higher than in 2015 when the agreement was signed. The frustration is that if just China, India and the US could come on board with a shared global carbon pricing scheme together, this would represent over 50% of the globe's emissions. Putting a brave face on it, we should acknowledge that in the past there has been a trend for successive rounds of Cop talks to vacillate from inconclusive to constructive, and hope is already building that Cop 26 in Glasgow later in the year will prove more successful.

- Our television screens and newspaper front pages were dominated over Christmas by the tragic images of Australian bushfires. This natural disaster illustrates the complexity of the globe's predicament; its causation being partly a lack of satisfactory land management in recent years but equally fanned by record average temperatures in the country. A parallel can be drawn with the worst flooding in Venice for 50 years in November occurring as it did the same week that the council for the Veneto region rejected a number of amendments designed to tackle climate change. In an ironic twist, the council chamber in Palazzo Ferro Fini itself flooded the evening of the vote. Vested interests, aversion to the cost of climate change mitigation and generational belief conflicts are in commonplace but the level of debate is structurally rising.

- As we alluded to earlier, there were high points to celebrate during Q4. Europe welcomed the new President of the EC with a decidedly more environmental agenda. One of Ursula von der Leyen's first major speeches was used to announce a European Green New Deal, with an emissions reduction target of 50-55% by 2030 and an offer of subsidies for those countries like Poland, Czech and Hungary that may struggle to meet this timeline. Nothing within European politics is straightforward, however, this proposal has to be acknowledged for what it is, world-leading. Perhaps as significant, we would also highlight the various high-level initiatives, for example the Task Force on Climate-related Disclosure and the European Taxonomy for sustainable activities aimed at driving business forward in its role of tackling and reporting on climate change and related sustainability issues.

All performance figures are given net of fees unless stated otherwise. Past performance is not a guide to current or future returns.
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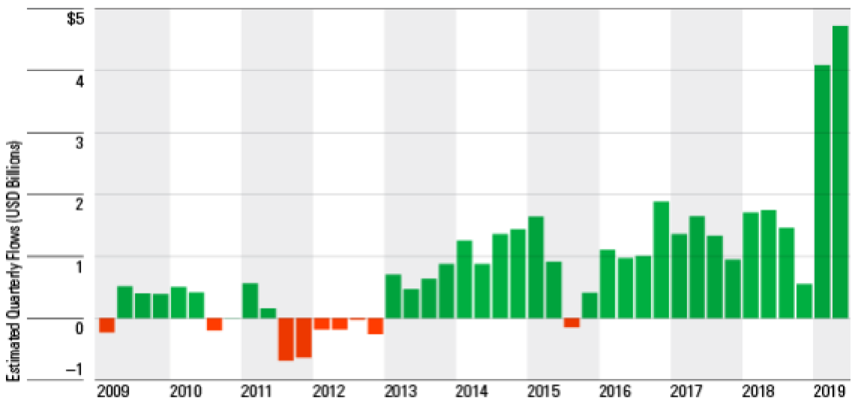
- Finally, one of the UBP Impact team attended the GIIN conference which took place in Amsterdam in October. The event has become the flagship event for the Impact world which now represents over $500bn of investible assets. The GIIN published one of the first collaboration measurement standardisation exercises seen in the financial market. The report was produced by convincing 11-member asset managers to share data on the impact of their investment in clean energy and social housing. The report boasting the delivery of clean energy to 2.8m new homes can be justifiably viewed as a first step in producing common standards of measurement for all 17 SDGs.

- Finally, as if we need reminding, sustainable investing remains one of the bright spots in active fund management as the flows chart below shows.

US Sustainable Funds Estimated Flows: Quarterly



Source: Morningstar Direct, June 2019 – Includes ESG integration, Impact and Sustainable Sector funds as defined in sustainable funds U.S Landscape Report, 2018. Includes funds that have been liquidated; does not include funds of funds.

Performance Review

Investment Theme	Average Theme Q3 Performance	Average Theme FY19 Performance
Basic Needs	+10.38%	+26.06%
Health & Wellbeing	+12.85%	+38.21%
Inclusive & Fair Economies	+5.78%	+15.40%
Healthy Ecosystems	+2.14%	+14.74%
Sustainable Communities	+11.62%	+29.74%
Climate Stability	+11.26%	+19.17%

- You may recall that our Q3 performance review was somewhat subdued reporting as it did the NAV fall of 2.37% net of fees after a strong first two quarters for 2019. Three months on it is with some satisfaction that we are able to report a 10.21% rise in the NAV net of fees for Q4, a terrific return by any standards.

- For 2019 as a whole, the fund delivered a credible 27.52% return in euro terms. Readers familiar with listed equity funds in the impact sector will be aware that we are without a truly fitting benchmark given the novelty of this style of investing. Nevertheless, it is worth pointing out that our aspiration as investors is to generate returns over and above broad global stock market indices. To this end, the 26.51% returns generated in euro terms by the MSCI ACWI index and the 26.05% of the MSCI Europe have been comfortably beaten. We know that one swallow does not make a summer but we hope the result engenders confidence that a strategy that considers so much more than simple financial analysis and traditional stock selection tools does not need to sacrifice investment returns for these additional features.

- The most relevant way we would guide investors to assess the portfolio's returns is by impact theme as attached above. This is indeed the framework by which the Impact team categorises the UN SDGs and hunts for investment ideas that deliver them. Since inception we have monitored the performance of the fund constituents held within each them to give a sense for how these hugely diverse constituents are behaving. These themes represent the Impact world's version of industrial sectors. During Q4, we witnessed a real pick up in performance from Climate Stability and Basic Needs whilst both Sustainable Communities and Health and Wellbeing stocks simply continued their strong 2019 market leadership in the quarter.

- It is worth repeating, the UBAM Positive Impact fund is well diversified at the country level, with the largest country weight at only 15.4%. This is in contrast to typical benchmark plus funds which tend to follow more constrained risk-based country allocations and can leave them hostage to idiosyncratic currency and economic fluctuations. During Q4 the UK, Norway, Switzerland and the Netherlands generated the lion's share of the returns.

- At a GICS sector level, the opposite is true as regards diversification with only 7 sectors having any representation at all. By far the largest allocation (25.9%) remains in industrials, a rich hunting ground for enablers of change. Our second largest allocation, consumer discretionary (21.2%) also drove fund returns in the quarter.

- At the stock level, nearly all shares in the portfolio rose during the quarter. However, we should highlight Aquafil Spa, Loop Industries Inc, Christian Hansen A/S and ASA International Group PLC. In the case of Aquafil and ASA International, two of our smallest portfolio companies, the impact case (IMAPs of 15 and 18) is very strong. However, the companies suffer from a lack of profile in the market and need to communicate their corporate strategy more convincingly to win more supporters. The decline in Loop shares during Q4 is best explained by the huge rise in price (+81.8%) witnessed in Q3. The company is still at the commercial testing stage of its rPET process and is thus exposed to swings in market sentiment. Finally, in the case of Christian Hansen, we have been disappointed by the newsflow from the company in 2019 when management was forced to talk down prospects of medium-term organic growth prospects. The company's near term valuation multiple did not leave huge room for disappointment and when it came the shares were harshly derated.

- At the other end of the scale the breadth of themes represented by our strongest performers is noteworthy. Countryside Properties shares had remained directionless for much of 2019 as the threat of the general election influenced sentiment. However, as the clouds around UK stocks cleared in Q4, so the true weight of scepticism was revealed by the 44.6% return the shares generated over such a short period in time. Infrastructure orientated companies like Sika AG and Kingspan Group also generated strong returns as the threat of recessionary conditions in the world's major economies receded. Finally, Health and Wellbeing names, Thule Corp and Basicfit NV both shook off the declines of Q3 and produced strong runs into the end of the year.

Performance Activity

- Portfolio changes in Q4 was pretty muted. The most significant changes we made were in the reduction of our holdings in Countryside and Basicfit on the grounds of profit-taking and our holding in Aquafil to reflect the transition risk affecting the company as it invests to increase its renewable feedstock, in particular recycled carpets in the US. We believe that over time, these near term investments will pay dividends and increase the impact case for Aquafil, however, we have to concede that near term profitability is more challenging than we had originally expected.

- We increased our holdings in Arcadis, Corticeira Amorim SA, Croda International PLC and Laureate Education Inc during Q4.

Quarterly Thematic Focus: Sustainable Communities, Cement and Hoffman Green

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- Cement. Less noticeable than plastic waste in landfills yet equally present in human environments. It is the main component of concrete which is the most widely used man-made material in existence. Today it is responsible for over 8% of the world's carbon dioxide emissions, making it the 3rd biggest source of emissions behind the industries of transport and energy production.
- Due to a process which has not changed in nearly 200 years, manufacturing 1 tonne of cement currently emits 1 tonne of CO2 – an obviously worrying ratio which highlights the need for innovation.
- This brings us to this quarter's thematic focus: Hoffmann Green Cement. The French company is our latest addition to the fund and belongs to the Sustainable Communities theme as the first manufacturer of a green alternative to cement at industrial scale. After a series of meetings and on-site company visits, we took part in its initial public offering which allowed the company to secure funding for future manufacturing plants. Such early involvement reflects that although we are investors on listed markets, there are opportunities where we can supply new capital in the field of positive impact.
- Unlike other cement alternatives which can only apply to niche applications, Hoffmann has developed a technology and process which addresses all mainstream segments of the construction market but also more niche uses. Unlike traditional cement which requires limestone from quarries, the Hoffmann process uses the by-product of other industrial processes such as slag from steel production, sludge from clay bricks or gypsum from construction site rubble. This input is then combined with activators and other low cost, widely available raw materials. The resulting substance is of superior performance compared to traditional cement but with emissions that are 5 times lower.

- Such companies are ideal constituents of our Sustainable Communities theme. On one hand, market penetration is supported by the start of the carbon tax cycle as CO2 quotas become effective and traditional cement manufacturers are running out of previously free allocations. On the other hand, Hoffmann's cement greatly reduces carbon emissions while providing productivity gains and higher technical performance. Finally, the transition is smooth as customers do not need to alter their manufacturing process.
  As the company further industrialises its process and contributes to making our communities more responsible, we believe the next few years will be very exciting for Hoffmann.

Engagement activity during Q4 – Case Study: Kerry Group

- In the context of Impact Investing, collaboration between companies and investors is essential to achieve satisfactory impact measurement. This places engagement at the centre of our investment research method and subsequent holding monitoring process. Although straightforward for companies with single business lines and clear generation of positive impact, entities that include uniquely different revenue streams or that are experiencing the sustainability transition within their operating structure are faced with a much more difficult task. The first step is usually to identify what to measure, trying to find a balance between relevance and achievability from both a cost and technological feasibility point of view.

- This quarter, amongst others, we engaged with Kerry Group, who started as a small dairy company 40 years ago and now manufactures taste and nutrition ingredients for a range of industries. Today, the company serves a wide customer base with diverse product lines, and because their solutions become part of customer products, they have no control over end-product launches. This makes it difficult to measure impact at group level and also creates uncertainty as to whether a metric will exist hence be measurable over time.

- Combined with a lack of non-financial disclosure requirement, this could have been a sufficient reason for the company to report very little non-financial data – especially as a AA-rated entity on MSCI which scores amongst the best food products companies

- Despite its size (€19bn market capitalisation), the company has only had a handful of impact investor requests – but thanks to engagement to which we contributed with regular conference calls and emails exchanges, Kerry identified the growing traction of sustainable strategies and the corresponding need for new data disclosure. From the existing site specific initiatives and ESG targets, the company is now collaborating with industry bodies to establish the "agreed metrics". Alongside, the company is working internally to assess sustainability from a product perspective and the management team hopes to announce the new phase of the journey in this year's sustainability report.
- Reflective of the collaborative relationship that the process of engagement builds, the sustainability team provided us with a temporary indicator (tonnes of sugar reduction in customer products) and wishes to engage again with their draft plan early this year.

- Our relationship with Kerry Group reflects the long-term nature of the collaboration and that it is a journey for both investors and companies rather than one-off interactions with immediate results. We also think it is a telling example of the effect that investor engagement can have on stimulating the sustainability path of an entity, even the larger and more traditional ones.

- Elsewhere, the team was hugely busy communicating with our portfolio and watchlist stocks as well as getting to know new companies that we want to incorporate into our growing warehouse of impact stock ideas. Engagement is absolutely fundamental to impact investing in listed market and we do not expect the interaction to deliver immediate results. Our example of Intertek highlighted in Q3 shows how patience can be rewarded. A further example in Q4 of this collaboration involved an approach from a portfolio company with whom we have been deeply engaged for over 12 months. The company in question is reviewing what elements it should measure in terms of non-financial data and has employed one of the big four accountancy firms to advise them on this topic. The UBP Impact team was the first port of call for the company when it came to surveying investors on the right path forward. Despite being still modest in terms of AUMs, it is hugely encouraging to us that our team is considered as an authority in sustainability and impact.

Q4 Recommended Read, documentaries and podcasts

- **Read:** En finir avec le plastique: Pour un monde sans plastique à la maison comme à l'horizon – Will McCallum (leads the Ocean campaign at Greenpeace). We're seeking to add a little bit of internationality into our recommendations here! It's more of a guide than a novel but certainly informative.

- **Documentaries:**

  - Game-changers – interesting, confrontational and in parts controversial Netflix documentary.

  - Inside Bill's Brain – a more optimistic look at the world of Bill and Melinda Gates in 3 episode Netflix series which also covers the whole backstory of Microsoft's rise to dominance. A fascinating watch that cannot fail to leave you with a greater appreciation Microsoft founder.

- **Podcast:** Global Goalscast – hosted by Claudia Romo Edelman, founder of 'We Are All Human Foundation' and Edie Lush, social media interviewer. The podcast shares stories broadly in the theme of achieving a more sustainable world. Great guests including Greta Thunberg and Gillian Tett.

Outlook

- January 2020 feels like more than the start of a new year; it isn't entirely unrealistic to think of it as the start of a more optimistic decade, the time when finance got its house in order and become the enabler of change.

- We sit at a fascinating crossroads. As one recent survey in the UK showed, an overwhelming majority (81%) of mass affluent investors are interested in investing their money ethically, and yet nearly the same percentage (74%) are knowingly invested in stocks that conflict with these values. This is the opportunity for impact investors in listed markets can offer.

- Equally, there are encouraging signs that businesses are beginning to really focus on the challenge. In 2019 some very surprising companies including Heidelberg Cement AG, Thyssenkrupp AG, ArcelorMittal SA and Centrica PLC all published net zero emissions commitments. Yet, Climate Action produced a report stating only 9% of the 161 companies they reviewed had emissions plans in line with a 2-degree warming scenario. It is evident that business is making improvements, and some of these have already required painful choices. For example, Repsol's announcement of a commitment to a net zero target was accompanied by a near €5bn balance sheet write of assets including exploration investments. This is the stranded asset argument in motion.

- With a backdrop of modest global earnings growth once again in 2020, we would highlight to investors the potential following winds evident within the impact investment theme. Whether it is a need for companies to better demonstrate their sustainable commitments or a need to cut emissions or any other focus areas of the UN SDGs, we have positioned the UBAM Positive Impact Fund to contain the best enablers of these ambitions.

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