Q4 2023

# UBAM – BIODIVERSITY RESTORATION

Quarterly Comment

For Professional Investors in Switzerland or Professional Investors as defined by the relevant laws.
Fund classification under Sustainable Financial Disclosure Regulation (SFDR): Article 9

## *Market Comment*

- The fourth quarter of 2023 delivered a "Santa rally" for investors, fueled by rate cut expectations following the Fed's pivot towards a more dovish stance. Equity markets rallied across the board and the MSCI ACWI* returned 11.0% in USD terms in Q4 to double its total return for the year to 22.2%.
- Overall, 2023, was a year that defied expectations, with inflation roaring and the Fed enacting the fastest rate hike cycle in 40 years. Nonetheless, after a rise in yields from May to October 2023, bonds rallied until the end of the year when US 10-year bond yield declined to 3.88%, exactly where it started the year, after touching 5% in October. Over the last months of the year, the Fed changed its tone and economic indicators remained fairly encouraging, boosting hopes of a soft landing in 2024 for the US economy. On the back of this, equities accelerated in the last two months of the year.
- For the quarter in terms of style, the end of 'higher for longer' rates fears boosted growth stocks, with the MSCI ACWI Growth Index* returning 12.7% over the period. The MSCI ACWI Value Index* also delivered a very respectable 9.2% but naturally lagged the growing excitement of the market. Similarly, Small cap stocks outperformed Large cap stock for the for the first time this year, helping broaden the rally that had been dominated by "the magnificent seven". In terms of sectors, Technology, Real Estate, Financials and Healthcare outperformed, while Energy, Staples and Communication Services lagged.
- Across regions, Developed markets generally outperformed Emerging Markets. The US, using the S&P 500 Index* as a proxy closed 11.6% up, returning 25.7% for the year, while the MSCI Europe Index* closed the quarter up 11.3%, but was up 19.7% in 2023. Finally, the MSCI EM Index* was up 7.9% and up 9.8% for the year. Latin America was particularly strong for the quarter and the year but China remained a negative outlier, as it continued to ease policy in hopes of reaccelerating from its growth slump. Finally, the Topix Index* in Japan rose 8.2% in the fourth quarter, concluding its best annual result in a decade with its 18.9% return.
- This year's COP28 in Dubai drew over 100'000 attendees, almost double the size of COP21 in Paris. Encouragingly, the narrative on the link between nature and climate has become stronger since COP27, and this was cemented by a dedicated nature day for the first time at COP28. A joint statement on "climate, nature and planet" (signed by 15 nations including the UK and the US) called for countries to meet the Paris Agreement targets along with the Global Biodiversity Framework ambitions. This is great progress in terms of how capital will be allocated to solutions. Moreover, while the record-setting global public-private sector participation offered a signal of hope, the backdrop of oil refineries served a stark reminder of COP's dual nature as a symbol of climate progress and delay. There was no convincing increase in the level of urgency or ambition at collective level, but we can hope that keeping the 1.5°C target will lead to stricter targets for the next round of climate goals (i.e. the so-called "nationally determined contributions").

** net total return index, in USD*

*Sources: UBP, Bloomberg Finance LP.*

All performance figures are given net of fees. Past performance is not a guide to current or future returns. See full disclaimer at the end of the document.



*Performance Review*

- For the quarter as a whole, UBAM Biodiversity Restoration returned 10.63%, compared with the MSCI ACWI Index return of 11.03%. However, this does not reflect the main feature of Q4 2023: the market turnaround which occurred at the end of October. After that point, and helped by completely new sector and style dynamics, there was some relief for the portfolio's relative returns going into the final months of the year. Indeed after still difficult performance in October, relative performance of the fund improved significantly in November and December: UBAM Biodiversity Restoration +17.01% vs the MSCI ACWI Index +14.48% over the two month period.

- Starting with October, notable areas of underperformance included the Consumer Staples, Materials, and Information Technology sectors. The fund remains impacted by its inability to invest behind large cap technology companies which created a significant negative allocation effect for the latter, but this is mainly a function of stock selection for the first two – namely Hellofresh (-27% MTD), Darling Ingredients (-15% MTD), Klabin (-9% MTD), and Re:Newcell (-83% MTD although exited before that). Meal-kit provider Hellofresh profit warned only 3 weeks after reporting 3Q23 results due to growing temporary issues: slower ramp up of its new facility, full capacity, and lower new customers. Oil recycler Darling saw continued pressures in the renewable diesel space and lower activity in its food and feed segments. Timber and paper producer Klabin faced higher for longer costs which weren't sufficient to offset volume improvements, and textile recycler Re:Newcell became pressured by a slower than expected ramp-up which revealed greater funding needs.

- This more than offset strong performance of several Industrial names: Wate Management's more defensive profile attracted cautious investors which drove performance (+8% MTD), water play Xylem (+3% MTD) published an excellent set of results beating consensus and raising guidance on the back of strong activity levels, and Lindsay (+6% MTD) rebounded strongly after benefitting from continuously supportive famer income levels.

- The second half of the quarter showed much stronger and homogenous performance: less, if any, sectors contributing negatively, and positive selection effect across the board. Notable areas of strength were Industrials (Advanced Drainage Systems, GEA Group), Materials (Sims Metal, West Fraser), Consumer Staples (Sprouts Farmers Market), and Real Estate (Berkeley and Gecina). Water management player ADS (+32% over 2M) published results ahead of expectations thanks to more resilient residential construction, GEA Group (+17% over 2M) showed good operational momentum and resilience in several end markets, recycler Sims (+25% over 2M) and timber company West Fraser (+22% over 2M) performed despite persistently weak market conditions thanks to improving commodity prices and a more optimistic medium-term view, and food retailer Sprouts (+15% over 2M) benefitted from a successful restructuring and repositioning in recent years which allowed it to combat inflation and the risk of lower consumer spending.

- Although minimal, weakness at the end of the year came mainly from more defensive or value sectors missing out from the full growth rebound – namely Veolia, Ahold Delhaize, and agriculture names Agco and Deere.


*Portfolio activity:*

- Reflective of the change in narrative which occurred during the quarter, the managers traded more actively in Q4. Five new names were added to the portfolio to benefit from opportunities in new geographies / underweight sectors:

- Autodesk (Restore, Enablers of Change and IMAP of 16): The company provides software for the architecture, engineering, and construction industries to help improve the way projects are designed, built, and operated. This results in lower energy consumption in buildings, allows customers to tackle embodied carbon of building materials, and reduces their construction waste streams. The team took advantage of improving fundamentals after a year of transition and a still discounted valuation.

- Daiseki (Protect, Planet Compatible Utilities and IMAP of 13): Industrial waste management company focused on the Japanese market. Thanks to its superior waste sorting process, the company is able to recycle as much as 90% of input waste which limits the subsequent need for incineration. This also reduces the underweight to Japan.

- Sumitomo Forestry (Protect, Sustainable Management of Natural Resources and IMAP of 12): Forestry and housebuilding company focused on Japan and the US. Sumitomo was one of the first private companies to develop a long term forestry management plan which it still operates with and has proactively become a leading supplier of net zero energy houses. This also reduces the underweight to Japan.

- L'Occitane International (Protect, Sustainable Management of Natural Resources and IMAP of 16): The company is a global manufacturer and retailer of natural cosmetics and well-being products but with an overarching mission to regenerate nature. The company focuses on planet-friendly ingredients and has strong incorporation of biodiversity friendly practices.

- Swire Properties (Protect, Green Cities and Urban Spaces and IMAP of 15): Real estate company with exposure to commercial, retail, and residential properties. Swire focuses on reducing energy consumption of existing buildings and enables better urban planning.

- Elsewhere in the portfolio, we added to existing positions in several companies including energy efficient industrial equipment manufacturer Trane, and real estate developers Berkeley and Gecina. We made full exists of three holding on the fund:

- Trimble: Position was fully exited following announcement of joint venture with Agco as the portfolio could now have access to Trimble geolocation technology by only holding the former, which is a higher conviction position.

- Re:Newcell: Position in the textile recycler was exited as it came under pressure of a slower than expected ramp-up which revealed greater funding needs, therefore pushing operational milestones several years out.

- Danimer Scientific: The position in the plastic alternative producer had to be divested as the stock drifted below $150m market capitalisation levels, triggering prospectus rules.

  In addition we trimmed our holdings in companies which saw strong relative returns in order to control their weightings and reduce potential concentration in the top holdings of the portfolio. This included all environmental consultants Stantec, Tetra Tech and Arcadis, but also food retailer Sprouts Farmers Market, and environmental service company Clean Harbors.

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*ESG Monitoring*

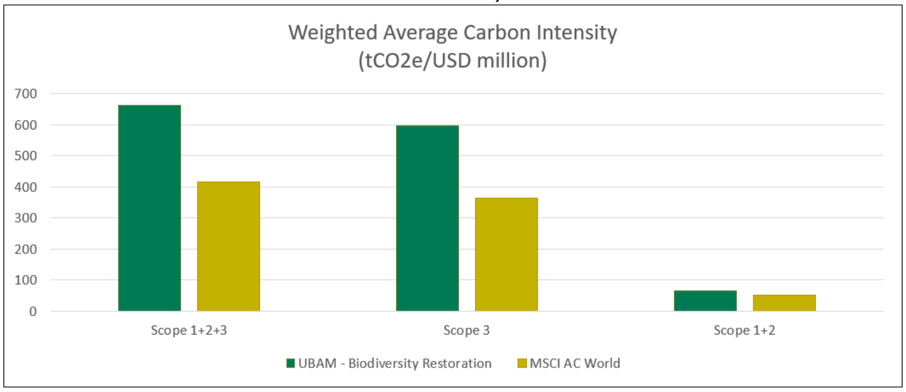
➢ **Human rights and Social**

(Disclosure: Fund 91.8% / Index: 100%)
**and Social** (Disclosure: Fund 91.8% / Index: 100%)

| | UN Global Compact | | | Human Rights Compliance | | |
|---|---|---|---|---|---|---|
| | Pass | Watchlist | Fail | Pass | Watchlist | Fail |
| UBAM - BRF | 45 | 0 | 0 | 45 | 0 | 0 |
| MSCI AC World | 2782 | 119 | 18 | 2773 | 128 | 18 |
| UBAM - BRF | 100% | 0% | 0% | 100% | 0% | 0% |
| MSCI AC World | 95% | 4% | 1% | 95% | 4% | 1% |

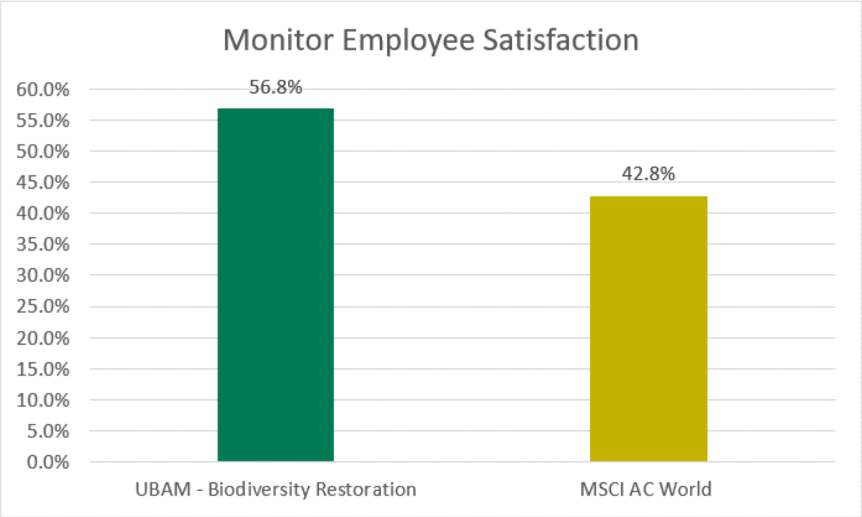
| | Labour Compliance - Core | | | Labor Compliance - Broad | | |
|---|---|---|---|---|---|---|
| | Pass | Watchlist | Fail | Pass | Watchlist | Fail |
| UBAM - BRF | 45 | 0 | 0 | 45 | 0 | 0 |
| MSCI AC World | 2865 | 41 | 13 | 2830 | 75 | 14 |
| UBAM - BRF | 100% | 0% | 0% | 100% | 0% | 0% |
| MSCI AC World | 98% | 1% | 0% | 97% | 3% | 0% |

➢ **Environment**
(Public Disclosure: Fund 85% / Index: 93.5%, Coverage Including estimates: Fund 97.9% / Index 99.1%)

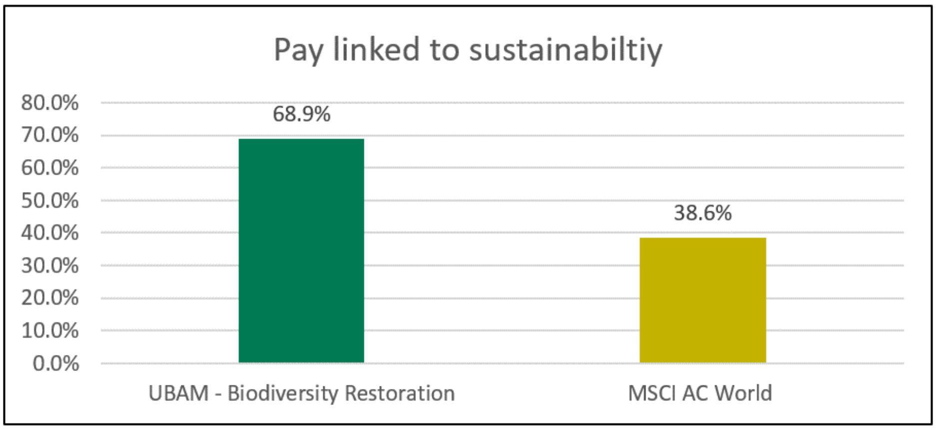



*The fund is at the same level as the benchmark on a scope 1&2 basis. If we include scope 3 emissions, the Weighted Average Carbon Intensity of the benchmark is lower than for the fund. This situation suggests a significant change from previous reporting, especially on the benchmark side, requiring further analysis from the portfolio managers. Scope 3 emissions are an important part of any analysis of GHG emissions, but they are also hard to estimate and a few outliers can lead to significantly different portfolio levels. There are also cases in which scope 1, 2 &3 emissions do not capture the full benefit of certain products. We will report on our conclusions in the next quarters.*


**Social** (Disclosure: Fund 89.8% / Index:100%)




- **Governance** (Disclosure: Fund 91.8% / Index: 99.9%)




*Sources: UBP, Based on MSCI ESG Research LLC and Urgentem*



*Outlook*

- Market sentiment was even more mercurial than normal over 2023, bouncing from recession worries at the start of the year, to resilient growth over the summer, to higher for longer in the autumn, and ending the year focused on future rate cuts.  Arguably, the strong run into year-end may have dragged some of 2024's expected equity return into 2023 as market consensus moved to price in a soft landing. The MSCI ACWI generated double digit returns despite negative earnings growth for most constituents as investors navigated an altering backdrop. Consequently, 2023 was largely driven by valuation expansion, while 2024 is supposedly going to be driven by better corporate earnings across the board. Investors' focus is now shifting from inflation concerns and towards softening economic growth. For 2024, consensus predicts 9-11% EPS growth - which is the traditional starting point. Nevertheless, risks are always present as financial conditions remain constrictive – higher interest rates have made borrowing more expensive, which has reduced spending and investment.

- There are a few additional features central to the investment thesis for the coming year. First, 2024 will be the biggest election year in history, with more than half the people on the planet living in countries that will hold nationwide elections in 2024. The US presidential election in November is the most significant event, however, global trade and diplomacy will be impacted much sooner given two major conflicts ongoing and the undercurrent of geo-political tensions. Next there is the question of nominal and real growth. Inflation rates have been coming down faster than consensus expected, and this has now created the possibility of meaningful rate cuts towards the third quarter of the year, with some forecasting this coming earlier. Europe is expected to lag the US in its rate pivot, however, there is a chance that the more sclerotic growth in Europe, impacted badly by Germany's export reliance particularly to China, means the ECB decides to move faster, depending on the inflation outturn. A strong US dollar peaking towards the beginning of the year, would be positive for emerging markets and small caps among others.

- During Q4, bond yields fell dramatically as investors played the pivot theme, however, since the start of 2024 some of that yield compression has been given back. This holds true with recent market volatility reacting to short term changes in news flow, in this instance Fed minutes suggesting that market had got too premature in its US rate cut expectations. Further bond market volatility is likely to influence equity markets rather than the other way around in 2024.

- On the sustainability front, among the standout positive developments in 2023 was a very high renewables growth rate (50% more renewable capacity in 2023 than in 2022*), numerous climate commitments at COP28, and multiple signs of technology advancement. Standout challenges in 2023 included geopolitical conflicts, high weather volatility that put strains on power grids (driving multiple countries to increase their reliance on fossil fuels temporarily) higher interest rates driving up decarbonization project costs and multiple missteps and challenges relating to companies' business models. On that last challenge, 2023 was a reminder that it is not enough to have a business model focused on enabling the sustainability transition; you must also be a high-quality business. Stocks that face risks of commoditisation, are cash flow constrained, and/or are exposed to significant execution risks will continue to struggle and a disciplined allocation remains critical.

*Sources: UBP, COP28, ****IEA***



*Appendix*

*Methodology*

- Global Compact Compliance

  This factor indicates whether the company is in compliance with the United Nations Global Compact principles. The possible values are Fail, Watch List, or Pass.
- Human Rights Compliance

  This factor indicates whether the company is in compliance with the United Nations Guiding Principles for Business and Human Rights. The possible values are Fail, Watch List, or Pass.
- Weighted Average Carbon Intensity

  This figure represents the company's Scope 1 + Scope 2+ Scope 3 greenhouse gas emissions normalized by sales in USD, which allows for comparison between companies of different sizes. This is a weighted average calculated using Urgentem data.
- Labor Compliance - Core

  This factor indicates whether the company is in compliance with the International Labour Organization’s fundamental principles. The possible values are Fail, Watch List, or Pass.
- Labor Compliance - Broad

  This factor indicates whether the company is in compliance with the International Labour Organization’s broader set of labor standards. The possible values are Fail, Watch List, or Pass.
- Monitors employee satisfaction

  Flagged as "Yes" if company monitors employee satisfaction.
- Pay Linked to Sustainability

  Has the company, if designated as having either a high environmental or social impact, failed to incorporate links to sustainability performance in its current incentive pay policies? Flagged if yes. This metric is based entirely on the company’s own reporting, and is strictly focused on the specific inclusion or not of such metrics in the determination of variable pay components and does not take into consideration their effectiveness. High Environmental Impact: If any of the following ESG Ratings Key Issues carry more than a 5% weight: Carbon Emissions, Water Stress, Toxic Emissions & Waste, Product Carbon Footprint, Raw Material Sourcing, Packaging Material & Waste, Electronic Waste, Biodiversity & Land Use, Energy Efficiency. High Social Impact: If any of the following ESG Ratings Key Issues carry more than a 5% weight: Labor Management, Health & Safety, Product Safety & Quality, Supply Chain Labor

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