MONTHLY REPORT
SEPTEMBER 2021

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.'

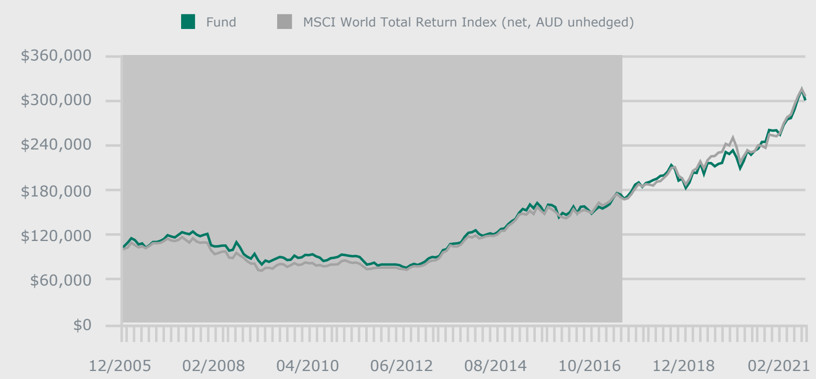
PERFORMANCE TABLE

NET PERFORMANCE FOR PERIODS ENDING 30 Sep 2021[1]

	1 MTH	1 YEAR	3 YEARS P.A.	5 YEARS P.A.	SINCE INCEPTION P.A.
WHEB Sustainable Impact Fund	-4.6%	22.8%	13.0%		
Strategy (partial simulation – see below)				14.3%	7.2%
MSCI World Total Return Index (net, AUD unhedged)	-3.0%	27.8%	13.2%	15.1%	7.3%

PERFORMANCE CHART

NET PERFORMANCE SINCE INCEPTION[2]



TOP HOLDINGS (ALPHABETICALLY)

A.O. Smith	Industrials
Agilent Technologies	Health Care
CSL	Health Care
Danaher	Health Care
Icon	Health Care
Koninklijke DSM	Materials
Linde	Materials
Orpea	Health Care
TE Connectivity	Information Technology
Thermo Fisher Scientific	Health Care

SECTOR BREAKDOWN

Consumer Discretionary	7.1%
Health Care	32%
Industrials	28.2%
Information Technology	18.8%
Materials	10.3%
Cash	3.6%

CAPITALISATION BREAKDOWN

1-2bn	2.8%
2-10bn	23.8%
10-20bn	17.8%
>20bn	52%
Cash	3.6%

CUSTOM SECTOR BREAKDOWN

Health	23.7%
Resource Efficiency	20.7%
Sustainable Transport	10.1%
Environmental Services	10.5%
Water Management	6.9%
Safety	6.8%
Cleaner Energy	4.5%
Wellbeing	10.3%
Education	2.9%
Cash	3.6%

REGION BREAKDOWN

North America	56.4%
Europe ex-UK	20.6%
Japan	8.8%
UK	5.5%
Emerging Markets - Europe, Middle East & Africa	2.2%
Asia Pacific	2.8%
Cash	3.6%

STATISTICAL DATA

VOLATILITY[3] 13.1%

NUMBER OF STOCKS 45

WE'VE BEEN WARNED – CLIMATE TRANSITION SUPPLY CHAINS RELY ON A SERIES OF WEAK LINKS

COMMENTARY

There was a sharp turn in market sentiment in September as investors responded to abruptly changing conditions. A significant rise in natural gas prices in Europe and global supply chain disruption drove fears of inflation. Power outages in China exacerbated the global supply chain turmoil. There were also concerns that a liquidity crisis for China Evergrande could cause ripple effects on emerging markets. Overall, the Fund returned -4.6% versus -3.0% for the MSCI World Index. While the Health and Cleaner Energy themes were relatively strong, the strategy saw underperformance from the Resource Efficiency and Wellbeing themes.

In this month's commentary, Claire Jervis discusses how this year's supply chain disruptions are much more than just a transitory pandemic-related phenomenon, being driven by extreme weather events, unprecedented (and growing) demand for climate transition technologies, and geopolitics.

We are thrilled that WHEB has won the Best Sustainable & ESG Fund Management Group of the Year (AUM under £20bn) category in Investment Week's 2021 Sustainable & ESG awards.

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In these volatile market conditions, WHEB's strategy turned from outperformance relative to our benchmark in the first half of the month to underperformance by the end of the month. Overall, the Fund returned -4.6% versus -3.0% for the MSCI World Index. While the Health and Cleaner Energy themes were relatively strong, the strategy saw underperformance from the Resource Efficiency and Wellbeing themes.

Our Health theme was once again the biggest positive contribution to performance in September, led by ICON. ICON is a clinical research organisation, helping pharmaceutical companies develop new therapies. Its services and technologies were particularly useful to facilitate remote clinical trials during the pandemic. Its share price has now more than recovered from the loss suffered when it announced the acquisition of its peer PRA Health Services in February this year. We believe the recent comments from management have boosted investor enthusiasm over the acquisition.

Our Cleaner Energy theme also performed well this month, driven by outperformance from First Solar. First Solar is the largest manufacturer of thin-film solar panels, with a long track record of good execution, and remains very cost-competitive through innovation. The company continues to gain from supportive decarbonising policies. First Solar is also benefitting as its competitors are struggling with a US ban on polysilicon produced in Xinjiang, China due to forced labour concerns.

The weakest performance this month was from the Resource Efficiency theme. This was mainly due to AO Smith and Lennox.

AO Smith is a world-leading manufacturer of water heating equipment and water treatment solutions. Its products help improve building energy efficiency. Lennox designs and manufactures products for heating, ventilation, air conditioning and refrigeration. The company has established a particular focus on higher efficiency equipment. There was no company-specific news which explained their underperformance this month. Both companies are exposed to the US housing market, which has experienced both labour and materials constraints recently. Similar to other industrial companies, both also face inflationary pressure, although we believe they have reasonable pricing power and should not be too troubled by it.

Our Wellbeing theme also performed poorly in September. This was mainly due to LHC, one of the largest home care group and hospice operators in the USA. Efficient home care has great potential in reducing substantially the cost burden created from lengthy hospital stays. Its share price continued to be weak this month after the company reduced the organic growth outlook for its hospice business in August. Hospice is a relatively small part of LHC, and we believe the challenges in the hospice market are temporary. We remain bullish over the long-term prospect of its home care business, supported by several structural drivers.

September marked the largest decline in global stock markets (using our benchmark as a proxy) since March 2020. Stock markets have been somewhat shielded from economic volatility so far this year by quantitative easing. Now that central banks are considering scaling back quantitative easing, and raising interest rates in view of rising inflation, equity markets may exhibit higher volatility in the near term. We continue to keep a close eye on how global economies juggle between supply chain disruption, inflation, rising interest rates and reduced market liquidity.

We've been warned – climate transition supply chains rely on a series of weak links

Whether you've tried to fuel up your car recently, were warned by a friend to buy your Christmas presents in August, or are currently waiting over a month for the new iPhone 13, you'll know that global supply chains are facing severe disruption.

Many news outlets and politicians have been quick to blame the easy target and reassure us that this is just a temporary glitch. They're not entirely wrong – COVID-19 has led to significant labour shortages which have shut down manufacturing plants across the world and taken swathes of truckers off the roads. But truthfully, the reasons behind this year's supply chain disruption are complex and manifold. They include extreme weather events; unprecedented (and growing) demand for climate transition technologies; and the creeping gloom of Sino-Western geopolitics… and they're not going away.

In February, severe winter storms caused massive electricity failures in Texas. Texas is the centre of semiconductor manufacturing in the US, with more facilities than any other state. These clever little chips power most of the world's transition technologies, including electric vehicles, renewable energy, and energy-efficient home appliances.

The Texas Freeze led to significant lost production for semiconductor manufacturers like Infineon, in our portfolio, and the echoes are still reverberating through supply chains today.

In a world where extreme weather events are becoming uncomfortably common, physical asset risk from climate change needs to climb up corporate and investor agendas.

We met with Infineon this month to discuss their asset risk mitigation strategies. We were reassured to learn that they had audited their organisation for physical climate risk and had hired a third party to oversee the process. Disclosure could be better though, and we are concerned that Infineon may be underestimating its risk. This will remain an ongoing topic of engagement with Infineon and throughout our portfolio.

On the other side of the equation, demand for climate transition technologies is running hot. Electric vehicles have doubled their share of global car sales in the last 12 months. Solar and wind capacity additions are running about 50% higher than pre-pandemic levels, and will need to continue a rapid growth trajectory if we are to meet the Paris goals. This means significantly higher volumes of semiconductors and raw materials being channelled towards transition technologies.

Silver isn't often mentioned as a critical raw material, yet solar panel manufacturers guzzle up 10% of global silver production and are estimated to need seven times more by 2035. The differentiated manufacturing process employed by **First Solar**, the photovoltaic module manufacturer in our portfolio, thankfully doesn't use silver. First Solar isn't immune to potential capacity constraints from other materials, however, like copper, aluminium, and steel.

Steel is of particular concern since it is practically ubiquitous within climate transition technologies. Nearly 50% of global steel production happens in China. The Chinese steel industry is aiming to peak its greenhouse gas emissions by 2025. With steel decarbonisation technologies still nascent, China is having to cap domestic production to meet its target. For a country growing as fast as China, this can only mean one thing: hoarding steel.

China has already revived taxes on steel exports to keep more supply at home. The CEO of **Lennox**, a HVAC manufacturer in our portfolio, recently lamented that steel costs four times more than it did 18 months ago, and blamed 'the oligopoly that is the steel industry for keeping supply down'. Steel importers need to make a decision – absorb the higher prices, find alternatives, or seriously ramp up domestic steel production (and, with it, steel decarbonisation technologies).

We shouldn't believe anyone who claims that this year's supply chain disruption is just a transitory phenomenon resulting from COVID. We have been given a clear warning signal for what's to come if we don't manage physical asset risks from climate change and reshape global supply chains to meet the immense demand for transition technologies. Some jurisdictions, including the US, seem to be waking up – the Biden administration has established a Supply Chain Disruptions Task Force which seeks to secure crucial materials supplies.

FEATURES

APIR CODE	HHA0007AU
REDEMPTION PRICE	A$ 1.6496
FEES *	Management Fee: 1.35%
MINIMUM INITIAL INVESTMENT	$10,000
FUM AT MONTH END	A$ 223.09m
FUND INCEPTION DATE	31 October 2007

FUND MANAGERS

Ted Franks
Partner, Fund Manager

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. 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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