RESPONSIBLE AND SUSTAINABLE GLOBAL EQUITY FUND

COMMENTARY FOR QUARTER TO END MARCH 2021

PERFORMANCE

	3 Months	6 Months	1 Year	3 Years	5 Years	10 Years
Fund Performance (B Class)	6.31%	17.62%	43.62%	32.09%	75.98%	111.68%
FTSE World TR GBP	4.09%	13.04%	39.93%	46.12%	99.16%	200.46%
IA Global	3.25%	13.16%	40.58%	43.22%	90.11%	153.83%
Sector Quartile	1	1	2	3	3	4

Source: Morningstar. Figures compared on a Bid to Bid basis with Net Income Reinvested.

REVIEW

Global equities, as measured as by the FTSE World Index, rallied 4.1% in the first quarter of 2021 (on a total return basis in sterling terms), buoyed by optimism around reflation, COVID-19 vaccines and hopes that the combination of reopening, further fiscal stimulus and pent-up demand would propel global growth higher. The single most important factor during the quarter was early evidence that COVID-19 vaccines were having the desired effect on the pandemic, with over 37% of American and 58% of British adults now having received at least one dose of vaccine and the number of people being hospitalised with COVID much lower than at the start of the year. These developments have opened the door to the possibility of a sustainable reopening once the virus was under control. Consequently, financial markets began transitioning from a liquidity to a growth-driven regime, which came with higher volatility and new leadership from a sector and regional perspective. Overall, developed market equity bourses broadly outperformed their counterparts in emerging markets, while global value indices outperformed their growth peers by more than 10%.

The US equity market delivered robust absolute returns and outperformed the broader global equity market over the course of the first quarter. The S&P 500 Index delivered a total return of 6.2% (in US dollar terms), while the Nasdaq Composite Index fell by 2.8% (in US dollar terms), as equity investors rotated away from Defensive, Quality and Growth winners of the previous few years, and towards more reflationary Cyclical and Value names that are expected to benefit from an improving growth and inflationary environment.

Following Joe Biden's US Presidential victory in November, domestic politics took more of a back seat during the first quarter. The Democrats won both Georgia runoff races at the beginning of January to take control of the Senate, before President Biden was inaugurated later that month. Biden made it clear that one of his priorities when taking office surrounded fiscal policy, and in March the US president signed a further $1.9 billion stimulus package into law (worth 9% of GDP). Alongside this, the US president has pledged to introduce a $2 trillion infrastructure package, focused on accelerating the fight against climate change by hastening the shift to new, cleaner energy sources.

In continental Europe, equity markets gained 7.1% (in Euro terms), however adjusting for the weakness in the Euro, these gains were reduced to 1.8% for sterling based investors. Investor attention remained on the COVID-19 pandemic, fuelled by a chaotic vaccine rollout across the bloc, rising COVID infection rates and new lockdown policies. Concerns over these developments were offset by hopes of the global economic recovery alongside regional forward-looking economic data-points that exceeded consensus expectations. The region's equity market bias towards economically sensitive areas of the investment universe (notably Energy and Financials) also supported quarterly performance.

The UK equity market, as measured by the FTSE All-Share Index, delivered a total return of 5.2% over the quarter, as rapid vaccine rollouts gave confidence that a mid-year reopening could unlock consumer and corporate demand in the second half of the year. A number of business surveys demonstrated notable improvements, providing support for economically-sensitive areas of the domestic equity market such as the Materials and Energy sectors. UK banks also performed strongly and a sharp increase in bond yields as the global economic outlook improved.

edentree
investment management

Equity markets in Asia Pacific (excluding Japan) delivered positive returns over the quarter but underperformed the broader global equity market, as continued optimism of an economic recovery was marginally offset by a strengthening US dollar and higher US Treasury yields. At a national level, the leading markets were Taiwan, where strong performance from I.T. names supported gains, and Singapore, where banks under-pinned domestic equity market returns.

Finally, in Japan, the equity market delivered a total return of 7.8% (in Japanese yen terms) over the quarter, however the weakness in domestic currency (which fell 5.3% on a trade-weighted basis over the three-month period) erased the positive returns for sterling-based investors. The equity market was supported by improving corporate fundamentals, as highlighted by a strong set of quarterly financial results, consistent weakness in the value of the yen relative to the US dollar improving the value of domestic exports and expectations of a global economic recovery. Additionally, there is an increasing likelihood of the Tokyo Olympics being held in 2021, however, the Japanese government confirmed that international spectators will not be allowed to attend.

PERFORMANCE & ACTIVITY

The Edentree Responsible & Sustainable Global Fund rose 6.3% in Sterling terms, around 2.1% ahead of the FTSE World benchmark return of 4.1% and global peer group average of 3.2% quarter, finishing first quartile for the period.

The primary driver of outperformance was stock selection, with the fund's holdings outperforming in US, UK, Europe ex UK and Asia, although the fund's Japan holding marginally underperformed. Overall, regional attribution was slightly negative driven by the underweight allocation to the US, which at index level rose only c.4.6%, driven by sharp gains in US banking and energy stocks. A greater contribution came from the fund's US holdings which gained 7.1% due to their mid-cap sustainable and cyclical orientation – an example is sustainable flooring leader **Mohawk Industries** which gained over 35% on the quarter continuing to add to its Q4 recovery on the back of strong housing market and repair and modelling trends.

The fund's overweight allocation to the UK was positive with the region gaining 5.2%, while the fund's holdings gained 9.9% offsetting some lag experienced last year. The fund's overweight allocation to Europe (ex UK) was supported by the fund's holdings gaining 6.4%, outperforming the broader bourse return of 2.5%. In Asia (ex Japan) the fund's holdings modestly outperformed with a total return of 5.5%, versus the 4.2% total benchmark return led by Australian construction and buildings waste recycler **Bingo Industries** which gained 20%, following a highly conditional bid from an infrastructure consortium. The bid at $3.50 represents a 28% premium to prevailing undisturbed share price.

In terms of sector allocation, it was a similar trend to the fourth quarter of 2020 with the fund's overweight allocation to Industrials sector contributing positively with the sector rising 5.4%, reflecting continued demand for economically sensitive exposure as expectations of an economic recovery as lockdowns eased. The fund's industrial holdings performed particularly strongly rising 8.8%, again led by smart-irrigation leader Valmont Industries rising 35% on improving agriculture outlook as well as rising demand for the Valmont's renewable energy products. Financials were the strongest performing sector at index level gaining 10.9% with the fund's holdings outperforming gaining 14.8%. Dutch based digital banking leader ING was a key contributor gaining 31% recovering from a sharp COVID related retracement last year. Additionally, the fund's holding in IP Group was a strong performer gaining 25%, as its leading genomic sequencing asset Oxford Nanopore continued to demonstrate the value of its technology during the pandemic. The largest sector relative outperformance of 15% was within the basic materials sector, with the fund's holdings gaining 22.3% vs. the sector of 6%, driven largely by Borregaard, a world leader in bio-refinery and speciality chemicals from paper. A number of Borregaard's products are direct replacements for heavy carbon emitting oil-based products, which is seen as attractive amid commodity price volatility, in addition to contributing to the long-term transition to Net Zero. In terms of detractors, the energy sector continued to rebound strongly as expectations of rising industrial activity led Brent Crude to rise further from $52/barrel at year end to over $62/barrel. The zero weighting to energy was a modest detractor as the sector gained 17.0%. Having had an exceptional 2020, as a result of rapid digitalisation and stay at home trends, the technology sector experienced some profit taking, with higher growth names correcting as rising bond yields reflected improving economic sentiment. The fund's exposure to NXP Semiconductors was a particular positive gaining 26% on strong, early cycle, demand dynamics, although concerns are rising regarding acute supply shortages within the broader chip industry.

In terms of fund activity, we began the quarter by completing our exit from **Nintendo** which has been a strong performer since we initiated a holding in 3Q18, however we considered the valuation no longer proved attractive following an additional (stay-at-home) year of peak sales for the Switch console, rising competition, and continued execution uncertainties around their mobility strategy. We redeployed some funds within Japan, buying **Welbe**, which provides employment services for people with disabilities, as well as child development support services. Additionally, within Japan we added to emissions and environmental testing company **Horiba**. Additionally, we exited **SAP** due to execution and competition concerns, while we sold our residual holding in **Tesco** following the substantial capital return arising from the sale of the Asian business.

Additionally, we trimmed a number of strong performers that had grown materially in terms of position size and valuation no longer supported as significant a risk position. For example, since the end of 1Q20, the strong economic recovery led **Valmont Industries**, **Borregaard** and **Mohawk Industries** to outperform the FTSE World benchmark by 64%, 77% and 87% respectively in GBP terms. Additionally, we reduced our exposure to **Nokia** following rapid share price spike led by exuberant US retail investor base.

OUTLOOK

The short-term outlook for markets remains dominated by two interlinked factors –the extent of additional fiscal and monetary stimulus, and the success of COVID-19 vaccination rollout. In terms of the outlook for fiscal stimulus, at the end of the first quarter, President Biden announced the American Jobs Plan, a $2.3 trillion climate-focussed infrastructure bill that is likely to be spread over the next eight years. The Plan is ambitious, focussing on building greener and more resilient infrastructure, and in doing so creating millions of jobs. The Plan reflects the President's goals for zero-carbon electricity by 2035 and net zero emissions by 2050, with specific goals of deploying 30GW of offshore wind by 2030, building two million affordable and sustainable homes and spending $111billion on modernising water infrastructure. The bill is likely to face significant challenges on the road to enactment, not least around the need for funding that could come in the form of higher tax rates within both the corporate and high net worth segments.

With regards to monetary stimulus, despite rising inflation expectations and a steepening yield curve, central banks remain keen to downplay the risks of inflation overshooting, signalling a continuation of exceptionally loose monetary policy. Despite a repeated willingness to refrain from tapering in the short-term, we would question the Fed's continued ability to micro-manage the bond market's reaction to inflationary spike. The limited early signals on withdrawing this level of monetary stimulus appears to be linked to the success and penetration of vaccine roll-out, which is inherently linked to the probability of a persistent easing of lockdown and broadening of the economic recovery. As the demand-side recovers, recurring bottlenecks and supply chain imbalances could provoke an inflationary bout.

One example are the rising concerns around an acute global supply shortage in semiconductor chips appears significant, with lead times for some components reported to be between 39 and 52 weeks, leading to excessive security of supply premiums. Given the implications for national security, employment and wider economy, further federal investment to ensure long-term security of supply looks essential. These supply and demand imbalances are a function of COVID induced supply chain disruption, with inventory levels depleted and demand profiles ahead of forecast ordering, the conditions are there for potential price inflation. While historically a lagging indicator, inflation has yet to spike materially on this dynamic, the outlook for gross margins is likely to feature in this and next quarter's earnings season. Taking the US semi-conductor sector as an early-cycle indicator, the consensus forecast gross margin appreciation is more likely to accrue to those with strong pricing power, while those reliant on scarce components could face significant disruption in production.

As for the pandemic, we continue to expect the path to recovery to be bumpy. While developed countries like the US have accelerated their rollout plans, less developed countries particularly Brazil and India continue to face increase accelerating outbreaks of COVID-19. Short-term vaccine protectionism and nationalism has not been conducive to better geopolitical sentiment, at best it is likely to hamper a co-ordinated global economic recovery.

We continue to retain the view that the environment for sustainable investing has never been more supportive. From a stimulus perspective, most major economies have witnessed governments enacting legislation to channel stimulus funds into sustainable projects to address often upgraded carbon emissions targets. Clearly there remains significant work to do to meet the long-term goals set out in the Paris Agreement and it appears that the broader population are increasingly aware that action is required.

In late January, The UN Development Programme revealed the results of their People's Climate Vote survey. The Peoples' Climate Vote is the largest survey of public opinion on climate change ever conducted, with over 1.2 million respondents, spanning 50 countries. It found that 64% of people felt climate change was an emergency, and 59% of those believed the world should urgently do everything necessary in response. Based on this indicative support from the electorate, we would consider long-term government policy and targeted stimulus towards addressing climate change will persist. In this context, we see a greater focus on mechanisms to incentivise and accelerate investment, of which one may come in the form of a higher carbon price, or carbon tax. As significant incremental capital is channelled towards sustainable challenges, we remain acutely aware that we must retain a healthy valuation discipline while recognising the scarcity context.