NORDSIP
NORDIC SUSTAINABLE INVESTMENTS

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ARTICLE 9 FUND REVIEW

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content

ARTICLE 9 FUND REVIEW

Second Quarter 2024

Credit: NordSIP

Compared to their peers investing in public markets, managers of private assets are notably more optimistic, particularly in sectors like agriculture, financial inclusion, and emerging markets, where they see strong opportunities for growth.

Aline Reichenberg Gustafsson, CFA

THE EDITOR'S WORD

In this edition of NordSIP's Article 9 Fund Review, we dive into the key trends shaping sustainable investments during the first half of 2024.

As the Article 9 fund universe continues to evolve in response to regulatory developments and shifting manager priorities, it is clear that sustainable investing is a long-term endeavor. Yet, in an industry where short-term market dynamics dominate, it remains crucial to regularly check in with asset managers to understand how their strategies and focuses are adapting.

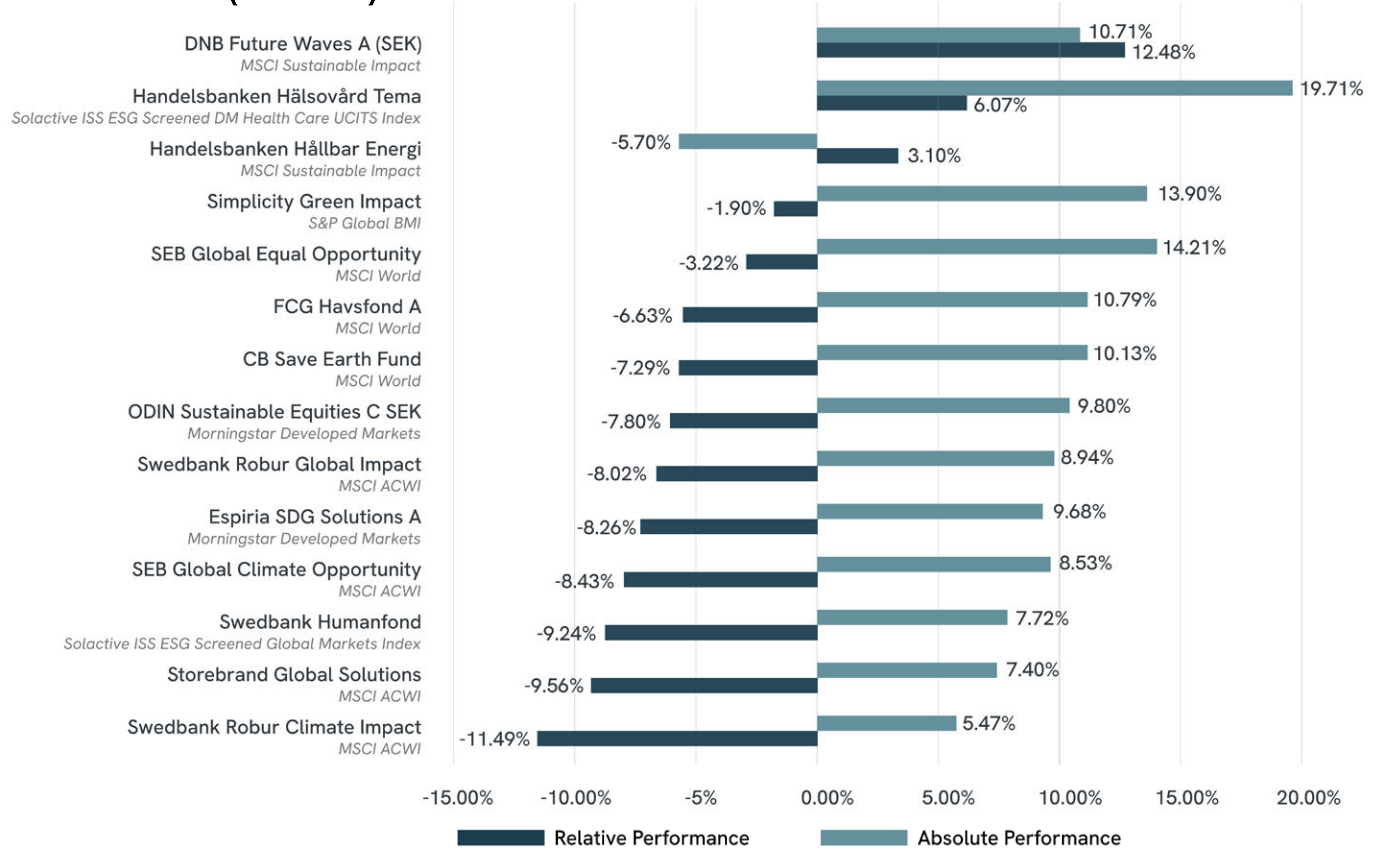
This review covers 53 global actively-managed Article 9 funds, encompassing 14 Nordic-based equity funds, 11 fixed-income funds, and 28 international funds, split between public and private asset strategies[1]. The report highlights the ongoing influence of a "higher for longer" interest rate environment, which provided support to long-duration bond funds but placed significant pressure on renewable energy stocks due to their capital-intensive nature. Nevertheless, despite recent headwinds, there is growing optimism about the future of renewables.

Artificial intelligence (AI) and healthcare remained the dominant themes driving market performance during the period, with bullish sentiment in these sectors boosting returns for many funds but also benchmarks. Fund managers across the board expressed caution regarding future macroeconomic developments, with most public asset funds maintaining a neutral outlook. However, managers of private assets are notably more optimistic, particularly in sectors like agriculture, financial inclusion, and emerging markets, where they see strong opportunities for growth.

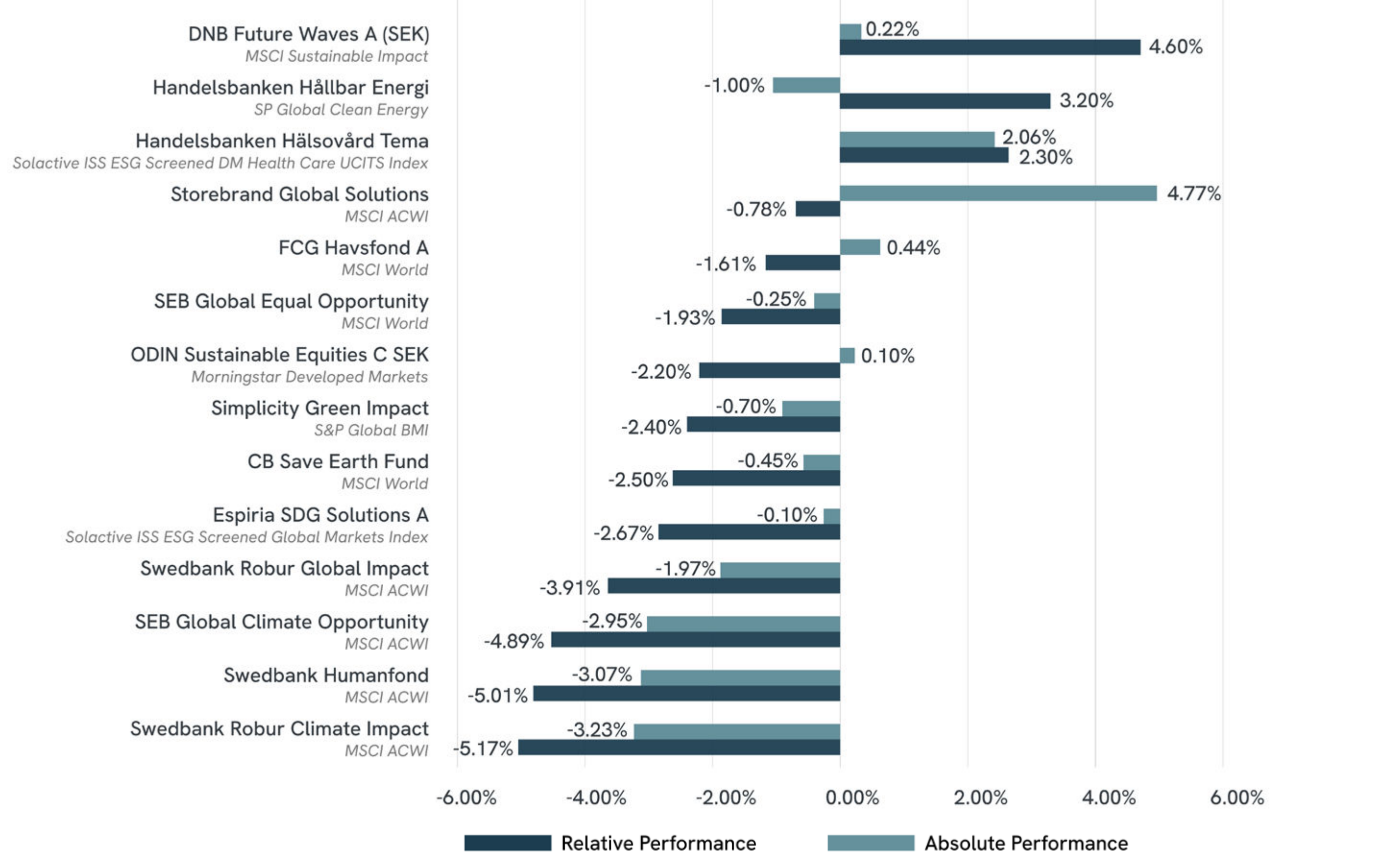
As we move forward, it will be fascinating to observe how Article 9 funds continue to balance long-term sustainability goals with the immediate challenges of today's market. This edition provides valuable insights for investors committed to navigating the evolving world of sustainable finance.

1 international managers included are NordSIP partners

Relative Performance of Selected Nordic Actively Managed Global Equity SFDR Article 9 Funds (1H 2024)



Relative Performance of Selected Nordic Actively Managed Global Equity SFDR Article 9 Funds (2Q 2024)



Source: Fund manager data

NORDIC MANAGERS

Equity Funds

Will AI Rescue Renewable Energy Stocks?

Filipe Albuquerque

During the first half of 2024, the MSCI ACWI, the MSCI World an the S&P 500 grew by 16.96%, 17.42% and 15.29%, respectively. On a quarterly basis, the same indices grew by 1.94%, 1.68% and 12.9% during the second quarter of 2024.

To better understand how these and other trends affected the performance of funds classified as Article 9 ("Dark Green") under the EU's Sustainable Finance Disclosures Regulation (SFDR), NordSIP reached out to 14 global funds actively managed by Nordic-based managers.

On average Nordic-based actively managed Article 9 SFDR funds underperformed their benchmarks over the first half of the year. The relative performance of these funds in the second quarter was also negative. According to Nordic asset managers, the dominating trends for the first half of 2024 were the slower-than-expected pace of interest rate cuts, inflation concerns, geopolitical tensions and the continued popularity of AI and IT stocks.

Going forward, asset managers remain optimistic based on expectations of an accommodating monetary policy environment, but worry about elections in the USA and geopolitical tensions with China.

Finding Appropriate Benchmarks

Benchmarking remains a consistent issue in sustainable fund performance analysis with asset managers noting that general market benchmarks such as the MSCI World or the MSCI ACWI do not offer ideal comparisons for the performance of their funds. "There is no applicable performance benchmark for the fund," Oskar Schyberg, portfolio manager of the FCG Havsfond argues. "The MSCI World Index is used solely to establish a risk level, not as a performance benchmark. This index does not account for ocean benefits or ESG factors and is not aligned with the fund's sustainability objectives. Morningstar has informed us that the fund category will change from "Global Large-Cap Blend Equity" to "Sector Equity Ecology" at the end of August, with the new category becoming effective on August 30, 2024," Schyberg explains.

To address these concerns, some asset managers have sought to find more focused benchmarks. This edition of the report marks the addition of the SP Global Clean energy, the Solactive ISS ESG Screened Developed Market Health Care UCITS index and the MSCI Sustainable Impact, a change that highlights the increased sophistication of the market.

The change in the benchmark has a particularly noticeable positive effect on the performance of the Handelsbanken Hållbar Energi Fund, vis-à-vis the start of 2024. "While the long term ambition remains to outperform general stock markets we have have changed the funds benchmark to S&P Global Clean Energy (TR) to better illustrate the shorter term performance of the fund versus its segment," Patric Lindqvist, portfolio manager of the Handelsbanken Hållbar Energi Fund explains.

Buoyant Growth Despite No Cuts

The first half of 2024 was marked by a progressive adjustment of expectations by investors who ended 2023 expecting a large number of interest rate cut. While global interest rates are still expected to fall, the pace of this adjustments has been revised downwards. Nevertheless, equity markets continued to grow, with the S&P 500 enjoying its best first quarter in five years.

"2024 began with high expectations for falling inflation and rapid and substantial cuts in central bank policy rates. However, the market's forecast for the number of rate cuts turned out to be overly optimistic. In the United States, none of the five rate cuts expected at the beginning of the year were realized during the first half of 2024. Despite this, the global stock market performed very well in the first six months of the year. During this period, several index record highs followed one another. Not only did stocks performed strongly, but commodities such as copper and gold did also see significant price increases," says Johanna Ingemarson, portfolio manager of the Simplicity Green Impact fund.

"Expectations for rate cuts have come down during the quarter as inflation data was stronger than anticipated. The march consumer price index (CPI) in US presented during month came in at 3.5 percent which was higher than the market had expected and once again lowered hopes for rate cuts in the near term. We have noted however that the renewable sector as a whole does not react as negatively as previously. Although some of the most interest rate sensitive names in the portfolio were negatively impacted like Sunrun Inc which has a large exposure to the residential solar sector. There continues to be a lot of private equity interest in the renewable energy space, with several deals being announced in May – adding to the sentiment that there is more value in this segment than is being represented in the stock market," Philip Ripman, portfolio manager of the Storebrand Global Solutions fund, says.

"In Q2, the market shifted focus to become more macro-oriented. Strong inflation numbers led to changes in the anticipated FED monetary policy resulting in a repricing of interest rate risk. This was negative for interest rate sensitive business as the market now expect fewer rate cuts in this year. Companies in the buildings space was re-priced but also companies with large investments as the cost of capital affected project financing. If the performance of sustainable investments in Q1 was broader, Q2 was more challenging due to larger dispersion among companies," Tom Santamaria Olsson, portfolio manager of the SEB Global Climate Opportunity and the SEB Global Equal Opportunity funds, agrees.

Mikkel Tobias Nyholt-Smedseng, portfolio manager of the DNB Future Waves A (SEK) fund notes that the market was in more of a risk off mood while, Marcus Grimfors, portfolio manager of the CB Save Earth Fund, noted that "the market slowed down and the dispersion in Mag 7 increased."

AI and Healthcare Remain King

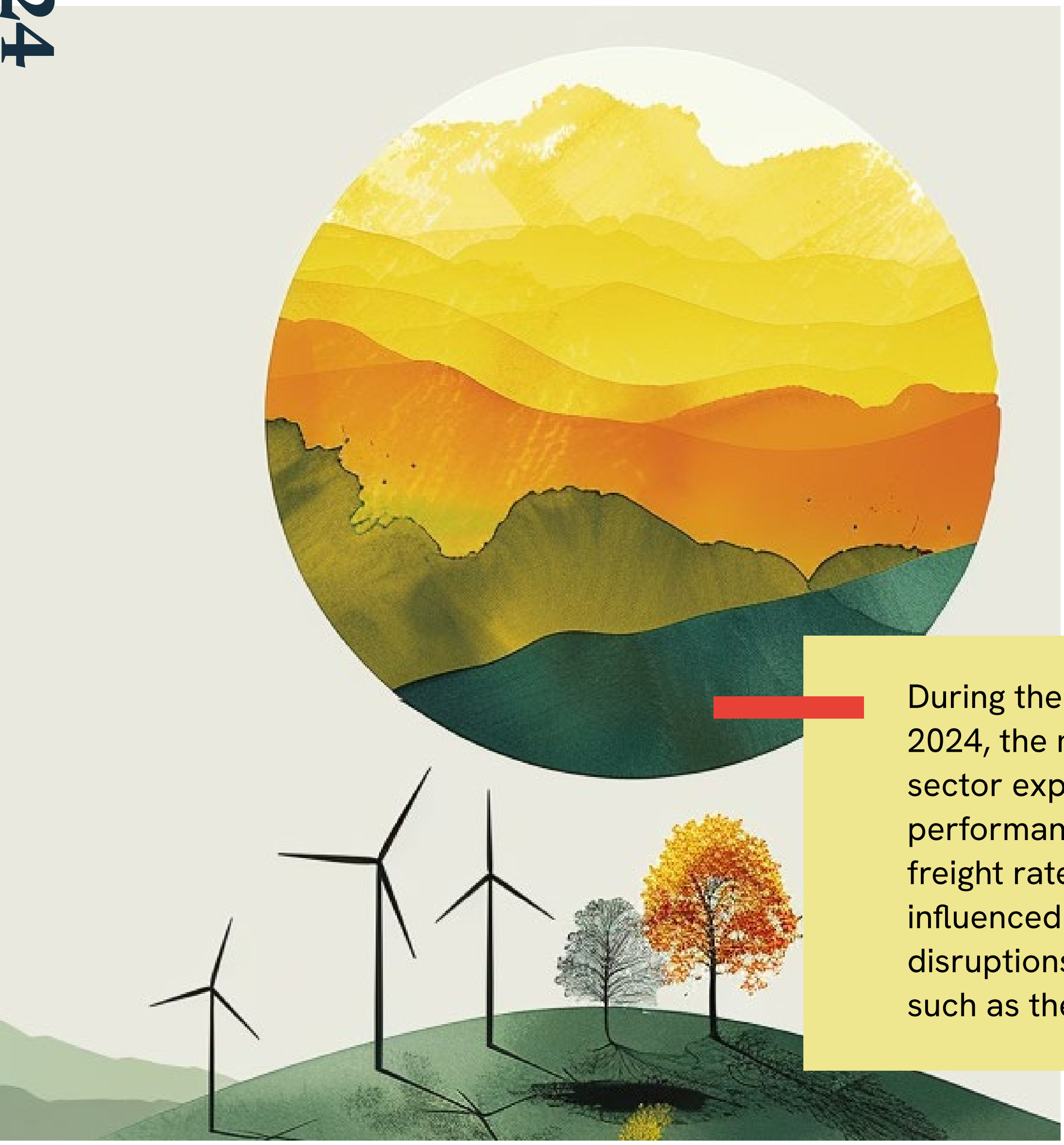
Notwithstanding the increased dispersion among the top 7 tech stocks (Alphabet, Amazon, Apple, Meta Platforms, Microsoft, NVIDIA, and Tesla), AI and IT remained the most popular themes during the first half of 2024.

"In the United States, the Technology and Communication Services sectors benefited from sustained enthusiasm for AI, continuing their strong performance into the second quarter. The Materials and Industrials sectors faced challenges primarily due to weakening demand and economic uncertainty. Meanwhile, Havsfonden's investments in Clean Energy Technology delivered substantial returns during this period. In Europe, the Information Technology sector continued to perform well, while the Consumer Discretionary sector faced ongoing challenges. The combination of political uncertainty particularly in France and diminished expectations for substantial interest rate cuts led to European equities remaining mostly stagnant throughout the quarter," FCG Havsfond's Schyberg explains.

The dominating trends for the first half of 2024 were the slower-than-expected pace of interest rate cuts, inflation concerns, geopolitical tensions and the continued popularity of AI and IT stocks.

Simpicity's Ingemarson also highlights the importance of AI stocks for her fund's performance. "Simplicity Green Impact had a return of 13.9% during the first half of 2024. Nvidia was the fund's best-performing holding during this period, with an increase of over 160%. The company has been the big winner in the development of artificial intelligence through its advanced chips. In general, a large proportion of the fund's major holdings performed very well during the first six months of 2024 and made a significant contribution to the fund, such as Microsoft, Sprouts Farmers Market, Nextracker, and First Solar. As a fund theme, investments in "energy-efficient technology" had the best performance, while the "sustainable infrastructure" theme was disadvantaged by negative developments in individual holdings," Ingemarson explains.

"The main performance driver during the first half of the year was energy efficiency where holdings such as Nvidia and Wiwynn had a strong tailwind from AI related investments," explains Johan Eriksson, portfolio manager of the Swedbank Robur Climate Impact, the Swedbank Robur Global Impact and the Swedbank Humanfond funds.



During the second quarter of 2024, the maritime transport sector experienced strong performance driven by rising freight rates, which were influenced by geopolitical disruptions in key shipping routes, such as the Red Sea.

SEB's Santamaria Olsson argues that several dynamics were at play in driving his funds' underperformance. "The main cause for the performance of the SEB Global Climate Opportunity funds is idiosyncratic, coming from stock specific events, country and style factor exposures contributed negatively but was balanced by positive contributions from sector exposures. Companies like Apple and Microsoft that the fund does not own had a strong Q2, which had a material impact on the performance. On a thematic point of view companies involved in solar and wind affected the performance negatively, whilst companies involved in hydro contributed," Santamaria Olsson explains.

"The drivers of the Q2 performance for the SEB Global Equal Opportunity fund were more balanced between multiple sources, the funds sector exposures its exposure to financials was a drag, companies with diverse organisations had positive impact but most of the underperformance is due to the strong Q2 performance of the magnificent 7, Apple, Microsoft and Tesla as the top three," Santamaria Olsson adds.

"The positive drivers were very much the same as in Q1; exposure to big tech, with names such as Microsoft, TSMC and Oracle, pharmaceuticals and exposure to the obesity theme with Novo Nordisk and Amgen, also the recovery in poor performers and turnaround stories such as Alstom and Organon. Schneider Electric and BYD are examples of large quality names that contributed to the performance of the fund," Peter van Berlekom, CIO and Portfolio Manager at Espiria says.

The healthcare theme continued to deliver strong returns driven by diabetes drugs that focus on weight loss. "Obesity and diabetes, the main theme for the 1st quarter, continued to deliver during the 2nd quarter. Eli Lilly, Novo Nordisk, and Zealand Pharma were the top contributors to performance of the fund," Gisela Gardelius, assistant portfolio manager at Handelsbanken argues.

Overall, there appears to have some consistency between the fist and the second quarters of the year. "The themes in Q2 didn't differ materially from those in Q1, large cap outperformed, market leaders outperformed, mixed performance in mature sectors such as Staples," Espiria's van Berlekom noted.

Will AI Rescue Renewables?

An interesting hypothesis emerged from the feedback of the asset managers surveyed, one of whom argued that the continued success of the AI theme might even spillover into the struggling renewable energy sector. "An area that was in focus during the quarter was how the rapidly expanding application of AI will mean a strong expansion of data centers with high capacity, which in itself means a materially increasing need for energy," Handelsbanken's Lindqvist says.

"This has put an additional focus on strengthening electricity grids and infrastructure and expanding energy capacity from cheap energy sources that can be built quickly, e.g. solar and wind power. The fund has about ten investments that particularly benefit from this trend and has also expanded these positions slightly during the quarter," Lindqvist adds.

Other Drivers of Positive Performance

Shipping was a positive contributor to the FCG Havsfond's performance. "During the second quarter of 2024, the maritime transport sector experienced strong performance driven by rising freight rates, which were influenced by geopolitical disruptions in key shipping routes, such as the Red Sea. Additionally, increased container demand, and operational efficiencies implemented by companies like Maersk contributed to the sector's robust results. This significantly boosted the performance of Havsfonden's investments in sustainable marine transportation, leading to particularly successful outcomes during this period," says FCG Havsfond's Schyberg.

Mikkel Tobias Nyholt-Smedseng, portfolio manager of the DNB Future Waves A (SEK) fund, highlighted the positive contributions of companies from the recycling, water and IT sectors to his portfolio's performance. Tomra (a Norwegian manufacturer of collection and sorting products for the food, recycling and mining industries), Core & Main (a U.S. distributor of water, sewer and fire protection products), Napatec (a Danish IT hardware company), stood out according to Nyholt-Smedseng.

"We also saw contributions from Owens Corning, a company involved in insulation materials. Other areas with positive performance contribution were health care related investments within basic needs and water related investments within natural resources," says Swedbank Robur's Eriksson.

According to Alexander Løes Nilsson, portfolio manager of the ODIN Sustainable Equities fund, Prysmian, Tetra Tech, and Edwards Lifesciences were the main positive contributors to the fund. "In 2024, we have purchased Diasorin, SolarEdge, ResMed, Ariston, Andritz, and A.O. Smith. Diasorin sells diagnostic products and services in immunology, molecular diagnostics, and licensed technologies. SolarEdge manufactures components for the solar energy industry. ResMed offers products and solutions to patients suffering from sleep-related breathing disorders, such as sleep apnea, chronic obstructive pulmonary disease (COPD), and other respiratory failures. Ariston is a manufacturer of several brands of heating and hot water systems, known for their energy-efficient and renewable products. Andritz is a global leader in the supply of plants, equipment, automation solutions, and services for a variety of industries, including hydropower, pulp and paper production, metalworking, and environmental and green energy sectors. AO Smith is a leading manufacturer and distributor of water heaters and boilers in North America. So far in 2024, we have divested from Microsoft, CAF, Xylem, Tracsis, Verisk, and NIBE," ODIN's Nilsson adds.

Renewable Energy Continues to Struggle

Consistent with what was reported for the first quarter of 2024, the renewable energy sector remained a consistent drag for the portfolios of sustainable asset managers.

"All environmental sectors the fund invests in (renewable energy, cleantech and water) were down in Q2 (in SEK). Water was the most stable and was down less than the others, while renewable energy was down more than 5%. ABB, Alfa Laval and Badger Meter were the individual investments that contributed the most during Q2. Franklin Electric, IDEX and Watts Water were the largest individual detractors. At quarter-end the fund had no exposure to the renewable energy sector," CB Fonder's Grimfors explains.

"The fund performance is slightly behind the index so far this year what is since large parts of the market have been driven by the technology and IT sectors, where we are underweight. Companies related to renewable energy have also struggled in 2024. The companies that have contributed to lower returns are SolarEdge, EDPR, and Ariston," Alexander Løes Nilsson, portfolio manager of the ODIN Sustainable Equities fund, explains.

"The Real Estate and Consumer Discretionary sectors encountered significant challenges, primarily due to the depreciation of the yen. Additionally, Havsfonden reported a downturn in its Sustainable Seafood segment, further affecting the fund's overall performance in the region," Schyberg adds.

"Renewables, unfortunately, had a rough first half of the year with most of the holdings in negative territory. An exception though was First Solar with meaningful positive contribution partly driven by US trade policy updates," Johan Eriksson, portfolio manager of the Swedbank Robur Climate Impact, the Swedbank Robur Global Impact and the Swedbank Humanfond funds. DNB's Nyholt-Smedseng also pointed towards the fund's holding of Vestas stock, a Danish installer, and servicer of wind turbines

Patric Lindqvist, portfolio manager of the Handelsbanken Hållbar Energi Fund, has a more indepth view of the sustainable energy sector. "The reports from the companies in the fund during the quarter were generally better than they have been in recent quarters and the average report outcome was perceived as better than expected. Several segments contributed strongly to the development, above all companies that contribute with efficiency in industry and wind power companies, while the segment for solar energy had weaker development," Handelsbanken Hållbar Energi Fund's Lindqvist explains.

"The strongest development was Enovix, a pioneer in the field of batteries in terms of energy density, which has started to scale up its battery production and which announced that it has concluded agreements with a couple of large customers. Cadeler, which installs offshore wind turbines, and TSMC, a world leader in the development of semiconductors, also contributed strongly," Lindqvist adds.

"The worst contributor was Array, which makes solar trackers for solar power parks, which despite a strong report had a volatile price development based on concerns that projects will be postponed. The salmon company Bakkafrost and the electricity system developer Shoals, with a focus mainly on large solar parks, also had weaker development," Lindqvist continues.

"The development during the second quarter was slightly up, which was slightly weaker than the world index but better if you look at a selection with similar funds or similar indexes," Lindqvist says.

However, renewable energy was not the only sector that struggled. "Consumer Discretionary struggled as consumers were absent. Chinese stocks and those with a strong renewable focus showed weak development," Espiria's van Berlekom explains.

Managers Remain Optimistic for the Future

Looking ahead, given the general trends in the market, portfolio managers expect the performance of their funds to improve.

"Interest rates are set to come down during the second half of the year – and expectations have already ramped up. We remain positive to the themes in the portfolio – and through diversification of themes, Equal Opportunities has managed to offset some negative developments

> One of the deciding factors will be the US presidential election, especially regarding renewables. A Harris win will give renewables a tailwind whereas if Trump wins the challenging year for renewables may well continue. Other sustainable areas are more uncertain and harder to predict for the rest of the year.

connected to the greener sid. Deployment of renewable energy still has positive momentum – and the energy landscape through digitalization and electrification will require more energy in the future e," Storebrand's Ripman argues.

"Our view is largely the same as last quarter. Given the increased dispersion in Mag 7 and a less narrow market, the opportunities for sustainable investments should probably increase relative to the MSCI World Net index," CB Fonder's Grimfors says.

"We remain positive towards the fund's sustainable investment themes – including the energy transition, circular economy, sustainable infrastructure, and sustainable water investment themes," Johanna Ingemarson, portfolio manager of the Simpicity Green Impact fund agrees.

On the energy front, Patric Lindqvist, portfolio manager of the Handelsbanken Hållbar Energi Fund is also optimistic. "Lower interest rates, gradual transition of political ambitions into firm regulations and low valuations make for a good startingpoint for the second half of 2024. The fund is to date (23/9) up 4,7% against the benchmark up 3,6%," he explains.

Meanwhile, there is no reason to believe that the excitement about healthcare will fade. "We remain positive on the sector. Several interesting readouts from clinical studies are due during the 2H of the year. We are positive on the sector and especially see a significant future potential within oncology and obesity/diabetes. We also see potential in smaller companies in the sector in earlier stages of clinical development within areas where there is a large unmet medical need and potential for medical progress," Gisela Gardelius, for the Handelsbanken

Hälsovård Tema Fund says.

"We take a bottom-up view of the markets in this respect, but our most likely scenario is in line with the broader market. The question mark remains for younger and less proven business models (and companies)," says Espiria's van Berlekom

(Geo-)Political Risks Ahead?

The one consistent worry on investors minds appears to be the outcome of the US election in November and the continued commercial tensions between the USA/EU and China.

"Elections have become an x-factor and a source of volatility in terms of uncertainty connected to regulatory packages, and geo-political concerns remain elevated when discussing value chains and US-China-EU relations," Storebrand's Ripman warns.

"The long-term demand and need for sustainable investments are still our base case but for the remaining of the year we are still positive on an absolute basis. Once the anticipated macro data starts softening and the monetary policy from central banks will be softer, we expect a rebound from sustainable investments. There is one big black swan on the horizon the US election in November that will have consequences for certain industries. We believe that the overall commitment of US companies to fight climate change is too strong and will not be affected by the election. However, due to uncertainty in what policies the potential new president will focus on will dampen the risk appetite and when presented will impact specific companies some companies more than others. So increased volatility of sustainable investments I the near term is a most likely," SEB Santamaria Olsson explains.

"We think one of the deciding factors will be the US presidential election, especially regarding renewables. A Harris win will give renewables a tailwind whereas if Trump wins the challenging year for renewables may well continue. Other sustainable areas are more uncertain and harder to predict for the rest of the year," Swedbank Robur's Eriksson concludes.

NORDIC MANAGERS

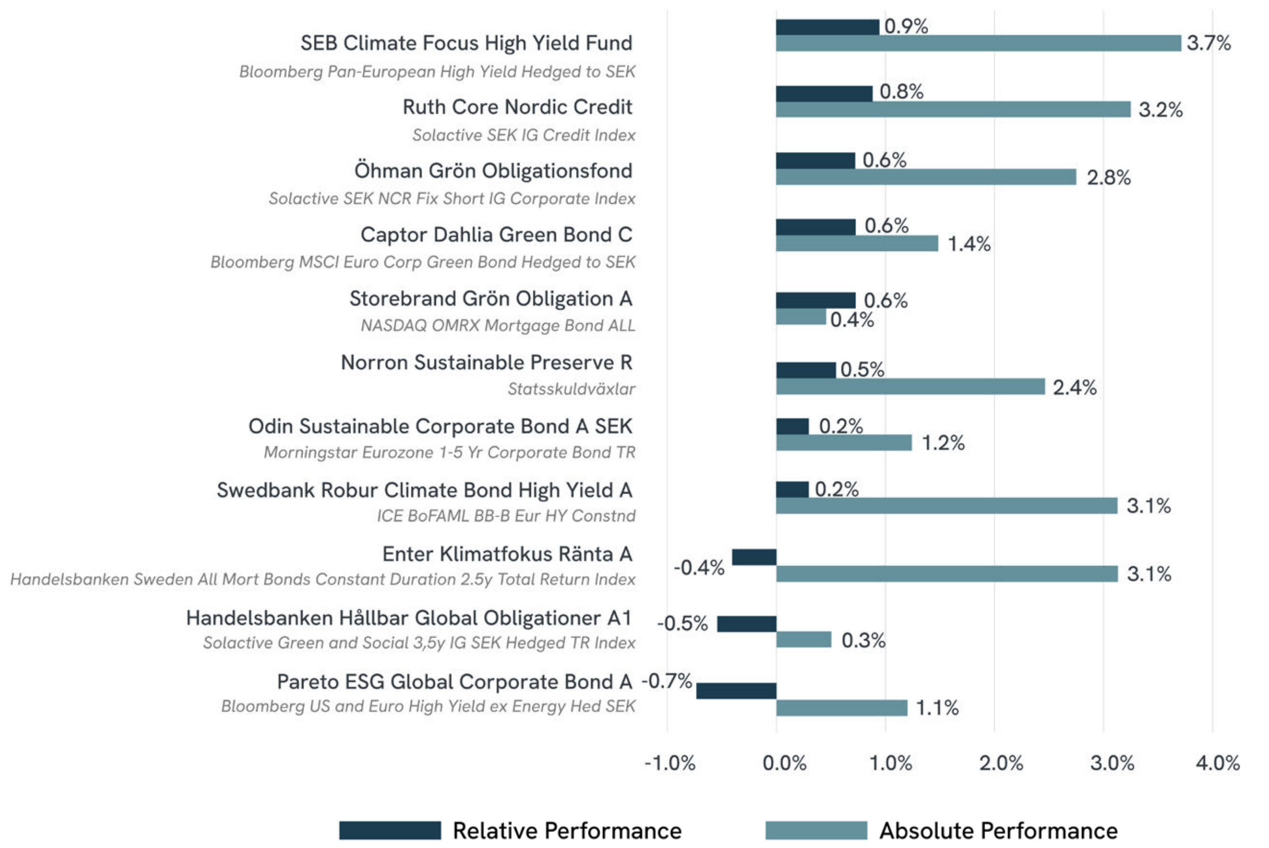
Fixed Income Funds

Rate Cuts Nudge Nordic Fixed Income Performance Up

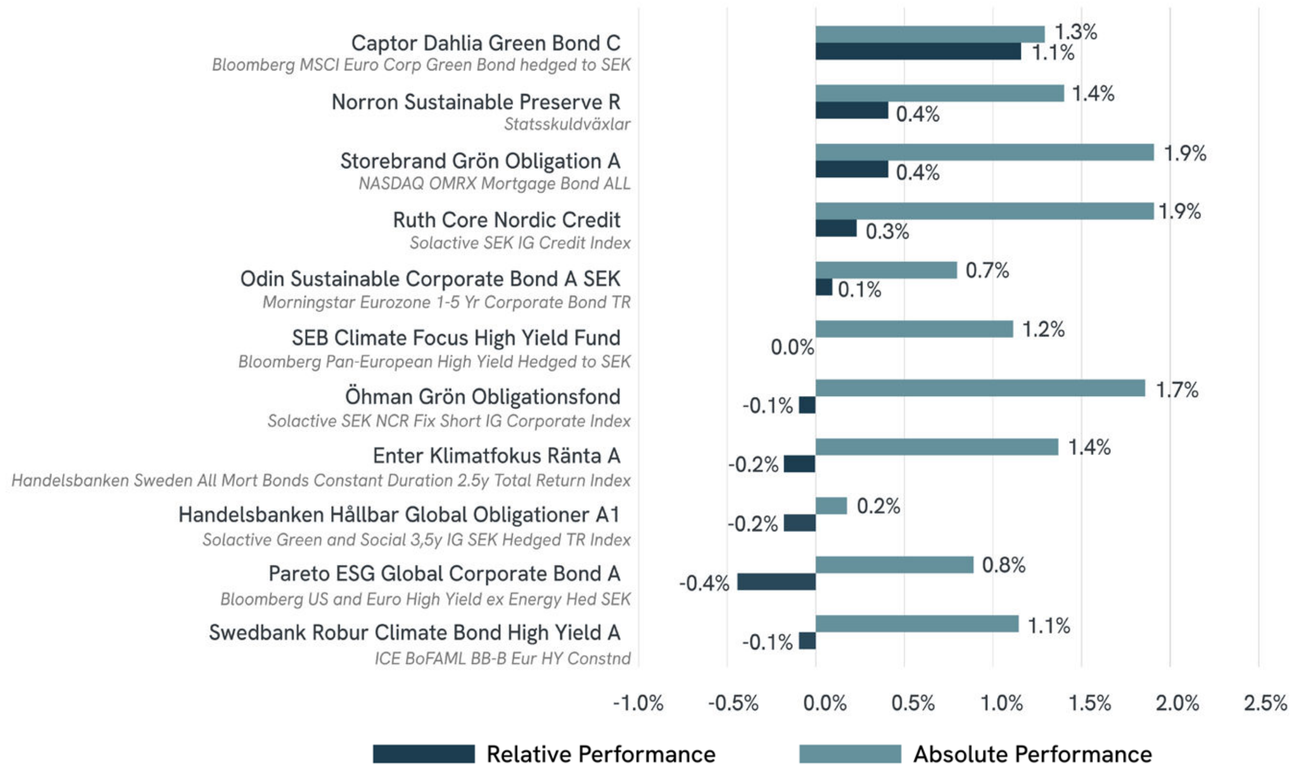
Filipe Albuquerque

Although, the US Federal Reserve, the Bank of England and Norges Bank continued to resist market pressure to cut interest rates during the second quarter of 2024, Sweden's Riksbanken (on May 15th), Danmark's Nationalbank (on June 6th) and the ECB (on June 12th) all lowered their policy rates, from 4% to 3.75%, from 3.6% to 3.35%, and from 4.5% to 4.25%, respectively.

Performance of Selected Nordic-based Art9 SFDR Fixed Income Funds (1H 2024)



Performance of Selected Nordic-based Art9 SFDR Fixed Income Funds (2Q 2024)



Source: Fund manager data. Benchmarks used for relative performance figures listed under fund names

The first half of the year also saw SEK and NOK on a downwards path until on April 30th they reached troughs of €0.085 and €0.0843, respectively. Thereafter, they returned to an upwards path, peaking on June 18th and June 21st at €0.0892 and €0.0886, respectively[1]. During the first half of the year SEK lost 1.9% vis-à-vis the EUR. NOK lost 1.8% in the same period.

To better understand how these dynamics played out and how these developments affected sustainable investors during the first quarter of 2024, NordSIP reached out to the portfolio managers of 11 actively managed Nordic-based fixed-income funds classified as Article 9 (dark green) under the EU's Sustainable Finance Disclosures Regulation (SFDR), available to retail investors in Sweden[2]. Overall, performance was positive but not as buoyant as in the second half of 2023. This is consistent with the materialisation of fewer interest rate cuts than asset managers had originally expected. However, it appears that most of the improved performance took place during the second quarter of the year which saw much higher performances than during the preceding quarter.

Nevertheless, the dominant drivers of performance mentioned by fund managers were similar to those mentioned in the first quarter of 2024. Duration and real estate stand out as the most prominent sources of success for the funds surveyed.

Central Banks Finally Cut Rates

The main development that asset managers highlighted as defining fixed income markets during the during the first half of 2024 was the decision of major central banks to cut their interest rates in the second quarter.

"Interest rate cuts are still the main focus in the market. The start of the year saw a reversal of the previous quarters sharp interest rate drop. This can attributed to the uncertainty about timing and the extent of interest rate cuts from mainly the Fed. From mid-April interest rate yields started shifting lower again as interest rate cuts appeared to be getting closer. The Swedish Riksbank was first out cutting rates by 25 basis points in May, followed by the ECB in June," Charlotte Lind, portfolio manager of the SEB Climate Focus High Yield Fund, explains.

[1] The Danish Crown (DKK) is pegged to the euro, which makes its evolution relatively irrelevant from an analytical perspective.
[2] The selected asset managers include Nordic, European as well as Global strategies, with different durations and risk preferences, which will inevitably be reflected in the funds performances. The benchmarks for the different funds also vary and are either the official or unofficial benchmarks that the fund managers shared with NordSIP as reference. The choice of the benchmarks will inevitably have an impact on the relative performance of the funds. The figures illustrate the multitude of performances available depending on the funds' specific strategic preferences and choices.

"Both the Riksbank and ECB delivered their first rate cut during the second quarter. The credit market remained strong with good risk appetite and high activity in the primary market," Julia Stålbro, portfolio manager of the Öhman Grön Obligationsfond, agrees.

"June was characterized by declines in long-term interest rates. The U.S. 10-year Treasury yield fell by 10 basis points to end the month at 4.4 percent, while the German equivalent fell by 16 basis points to end at 2.5 percent. The economic Citi Surprise Index, which measures how macroeconomic indicators come in compared to expectations, shows that the market was negatively surprised. This put downward pressure on interest rate expectations," the asset management team of the ODIN Sustainable Corporate Bond argues.

"However, so far this year, the 10-year yield has risen by 0.5 percentage points in both Germany and the USA. Inflation in the USA and the eurozone has fallen significantly from its peak but remains above the 2 percent target, and it has taken longer to bring down policy rates than the market anticipated at the beginning of the year. The market is pricing in one to two more rate cuts in the eurozone during the fall, while about two cuts are priced in for the USA," the Odin team adds.

"We saw much lower interest levels during the summer and for the rest of the year which will be positive for our longer duration strategy in the fund together with good Investment grade companies," Sebastian Uddén, portfolio manager of the Norron Sustainable Preserve fund, says.

The asset managers highlighted four drivers of performance: Real estate, duration, Nordic exposure and security selection.

Real Estate Leads the Way

According to Cecilia Dahlstedt Myrgård, portfolio manager of the Captor Dahlia Green Bond fund, it is possible to see the impact of monetary policy decisions on the real estate market. "In the Swedish credit market, the main theme has continued to be that real estate companies' credit spreads have continued to converge. This is due to upcoming interest rate cuts, which will provide cheaper financing for the property companies and then better key figures. After market interest rates during Q1 were corrected upwards, they have come down again during Q2. mainly due to lower inflation figures," Myrgård notes.

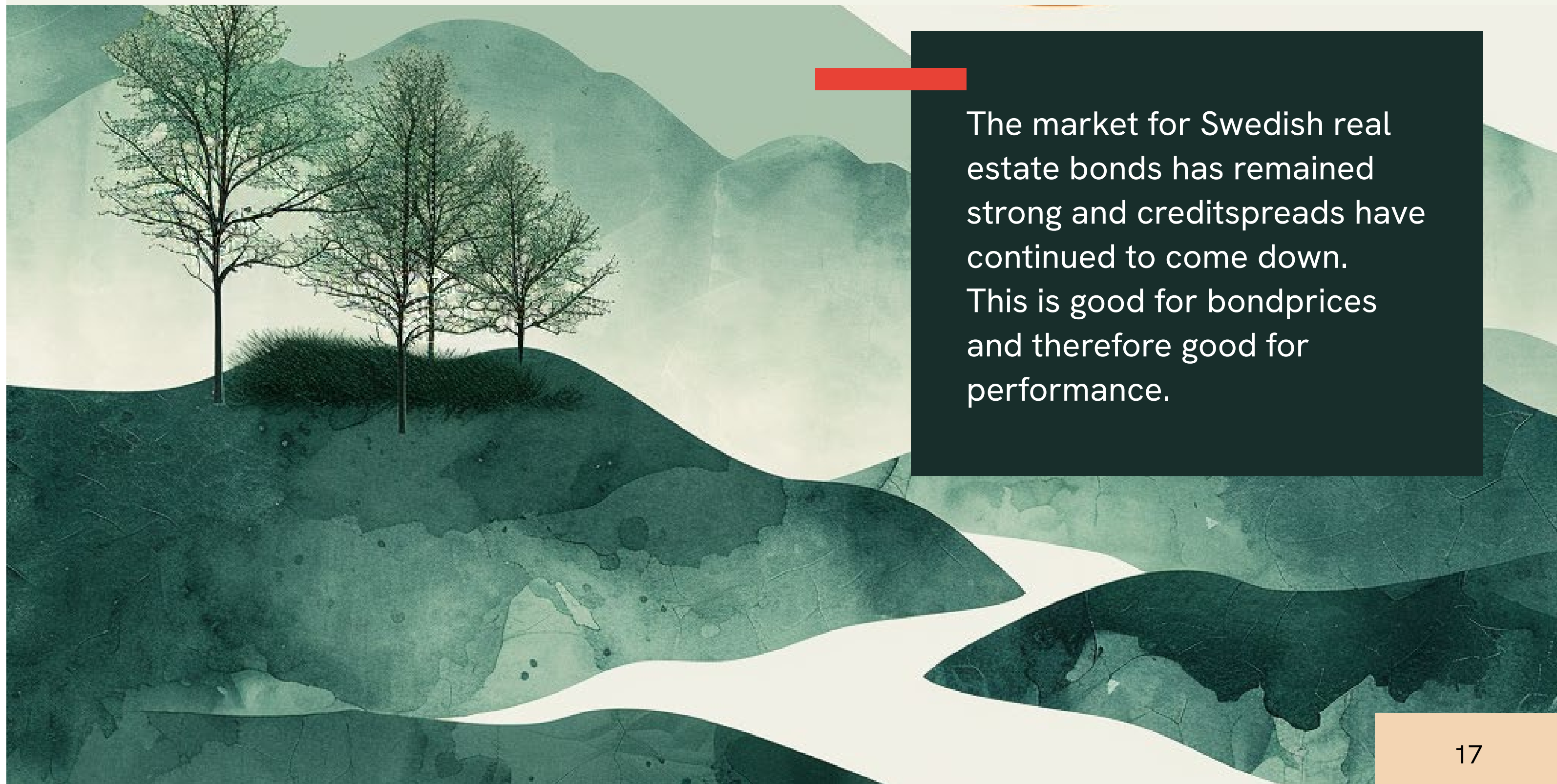
"The market for Swedish real estate bonds has remained strong and creditspreads have continued to come down. This is good for bondprices and therefore good for performance. Dahlia green bond fund holds a lot of such bonds while our benchmark does not. That is the main reason why we have outperformed the index during this period," Myrgård adds.

Gustaf Tegell, portfolio manager of the Enter Klimatfokus Ränta fund agreed that real estate market had performed well, noting that "real estate and financials led the way" during this period, while SEB's Lind agrees, noting that "our Swedish real estate bonds outperformed the most."

Using Duration and Carry to Leverage Rate Cuts

As monetary policy rates fall, there is a tendency for the yields on long-term to fall faster than those of short-term[3]. Several asset managers reported being able to exploit this dynamic for their returns. "Short rate duration during the first quarter and higher during the second quarter was a positive contribution compared to index," Henrik Rosencrantz, portfolio manager of the Ruth Core Nordic

[3] The price of bonds moves inversely to their yields. When yields fall, the price of bonds increases, and vice versa.



The market for Swedish real estate bonds has remained strong and creditspreads have continued to come down. This is good for bondprices and therefore good for performance.

> We see an increased interest in issuing green and sustainable bonds from sectors other than real estate and municipalities.

Credit Fund explains. Johan Hedengren, portfolio manager of the Storebrand Grön Obligation, also notes that "rates moving lower" and the funds' exposure to "long covered and credit bonds" were important themes and drivers of performance.

"Good risk appetite in the credit market has continued to benefit the fund's positioning, both in absolute terms and relative to its benchmark. The fund added duration during the first quarter of the year, which contributed positively to the fund's absolute performance as interest rates ended the period lower. Relative its benchmark, the long duration position was somewhat neutral due to curve positioning," Öhman's Stålbro adds.

However, duration was not a boon to every asset manager, with both Pareto's Lindgren and SEB's Lind acknowledging a negative effect on their funds' performance. "The slightly shorter duration than our index made a small negative contribution against the benchmark but all in all we are happy with our performance in the first half of the year," SEB's Lind says.

According to Pareto's Lindgren, coupon payments were the main drivers of performance. "Good cash return was the main driver of our performance. In other words, the higher coupons we now get from the bonds we hold were the biggest positive contribution to the fund's performance," Lindgren says.

Nordic Outperformance and Security Selection

Lastly, asset managers also highlighted the stability of Nordic market and the contributions of their investment choices.

"The Nordic market outperformed the European High Yield market during the first half of the year so our tilt towards the Nordics, which was 43% of the portfolio at the end Q2, generated better returns compared to our benchmark. We have a strong focus on security selection towards environmentally sustainable companies and projects which also contributed positively, both in absolute return and risk adjusted return," SEB's Lind argues.

"During the period, the Nordic credit market has seen lower credit premiums for both Investment Grade and High Yield, which is largely driven by more positive market sentiment and demand for corporate bonds being greater than supply," Öhman's Stålbro adds.

"Investments in Four Green Bonds and One Regular Bond in June ODIN Sustainable Corporate Bond invested in four green bonds and one regular bond in June," the ODIN team explains.

"Two of the green bonds are issued by the grid companies Stedin and Redeia, which develop and operate the electricity grid in the Netherlands and Spain, respectively. The fund also invested in a green bond issued by the Norwegian fertilizer and chemical company Yara. Fertilizers are necessary to meet the food needs of the growing world population, and Yara has developed a mineral fertilizer with significantly lower greenhouse gas emissions compared to other types of fertilizers," the ODIN team continues.

"The fund also invested in a regular bond from the Swedish telecommunications company Tele2. This is the fund's second position in the company, which is a leader in several sustainability factors within the telecom industry. The company has set ambitious goals in circularity and presents comprehensive and transparent sustainability reporting," the ODIN team says.

Sustainable Markets Going Forward

Nordic managers of Article 9 SFDR fixed-income funds are generally positive about the performance of sustainable investments going forward.

"We believe that sustainable markets will perform better in a lower interest levels environment," Norron's Uddén says. Pareto's Lindgren agrees, noting that "Sustainable investing will continue to perform well in H2 2024, in our view," before adding that "the high carry in the fund and anticipated lower market rates will contribute positively to the fund's performance." Ruth's Rosencrantz also agrees, noting that "our outlook for the second half of 2024 is for rates to remain stable since rate cuts are already priced in. We do expect sustainable markets to perform better than 2023."

Some investors prefer to qualify these positive expectations. "The fundamentals for investment grade credits looks solid. However there are signs of pockets with overbought securities so caution is warranted," Enter's Tegell warns.

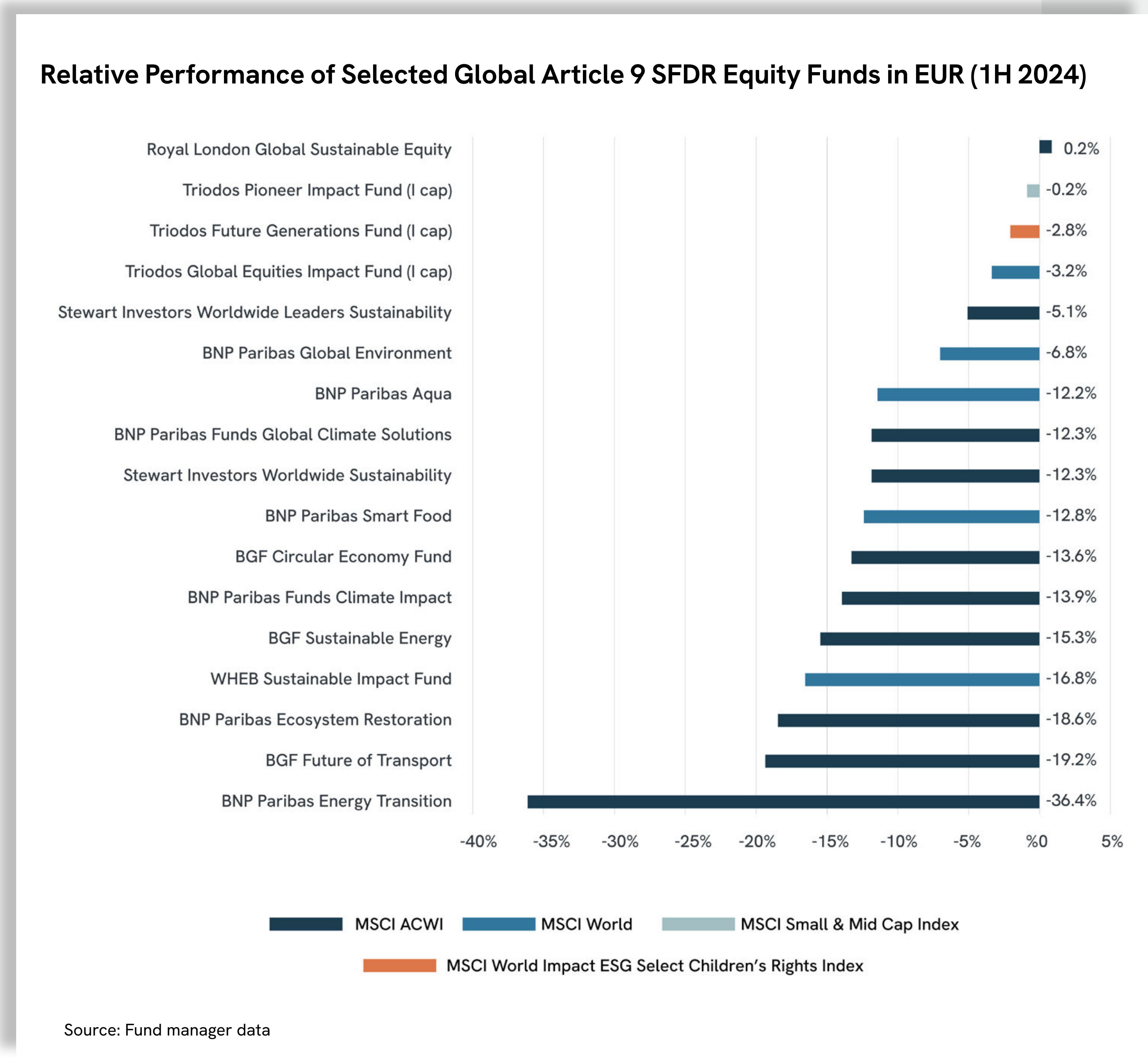
Öhman's Stålbro shares this optimism but is more cautious in the long term. "Credit spreads have tightened significantly over the last 12 months and there is now less room for continued tightening. In the short term we expect credit spreads to remain at low levels but are somewhat cautious in the long term due to uncertainty about the pace of interest rate cuts, weaker economic outlook, and geopolitical tensions abroad," Stålbro says.

"The economy is ticking along with steady growth and falling inflation which paves the way for interest rate cuts. This will benefit our high yield companies as the maturity wall approaches and they need to refinance their bonds at a higher interest rate. At the same time, the markets have shown that they are susceptible to shocks, as we saw in the beginning of August , and as spreads are at tight levels we remain somewhat cautious and security selection becomes more important. Our portfolio of environmentally sustainable companies, together with the green bonds, where the use of proceeds are earmarked towards green projects, provide a good sector diversification and have consistently delivered steady returns in the fixed income market. We believe this positive trend will continue into the year-end and beyond," SEB's Lind adds.

"Interest rate cuts are now fully priced in the market rates and we believe that they have been priced in too much. Furthermore, credit spreads have traded down to levels where we were before the covid epidemic. Credit spreads are trading very low now and running out of room to tighten further. Because of this we cannot expect the same performance for credit funds as we have seen in 2023 and H1 2024. We see an increased interest in issuing green and sustainable bonds from sectors other than real estate and municipalities. This is something we welcome and think is very positive," Captor's Myrgård concludes.

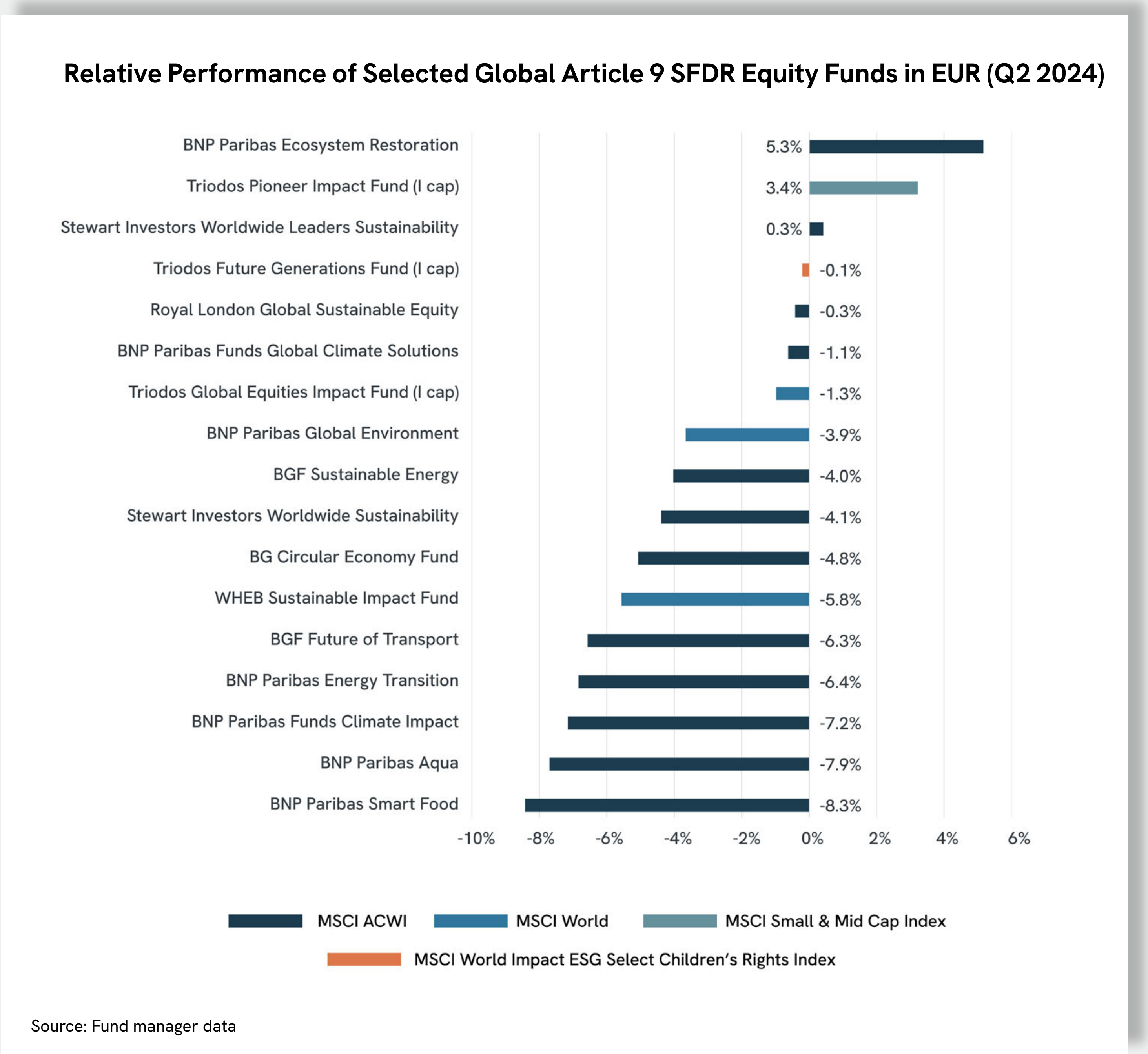
INTERNATIONAL PARTNERS

Public Market Funds



Renewable Optimism Amidst Economic Change

Filipe Albuquerque



According to the US Bureau of Economic Analysis, GDP grew at an annual rate of 3% during the second quarter of 2024, following 1.6% growth in the preceding quarter. Second quarter GDP growth was considerably less buoyant in the EU, according to Eurostat, which put the figures at 0.8% , up from 0.7% in the first quarter of the year. During the first half of the year the US Dollar gained 3.07% vis-à-vis the Euro.

To understand how international active asset managers with global mandates performed under these conditions, NordSIP reached out to our partner asset managers to hear about their performance during the first three months of 2024.

NordSIP surveyed the performance of 20 global actively managed funds classified as Article 9 under the Sustainable Finance Disclosures Regulation (SFDR):17 equity funds and 3 global fixed-income funds, from non-Nordic asset managers with whom NordSIP has an ongoing partnership. Article 9 funds not only invest in sustainable assets, but also have sustainable investment as their objective. They are also referred to as "dark green" funds.

Although the majority of sustainable equity funds continued to underperform general benchmarks not associated with sustainability, there was a clear improvement in relative performances in comparison to the first quarter of the year.

Most fixed income funds also performed better in the second quarter of 2024. Among international fund managers as elsewhere, we find that improved hopes of an accommodating monetary policy environment played a key role.

Although the AI and healthcare remained the dominant theme in the markets, there seem to be some positive developments in renewable energy. Although a turn-around in the sector is not yet the consensus, there is some evidence to suggest optimism is not unwarranted.

Monetary Policy and Inflation Rule Expectations

Monetary policy and market expectations of its future evolution based on inflation data drove equity markets during the first half of the year.

"The first half of 2024 saw global equity markets rise on the back of strong corporate earnings, improved economic conditions and favorable monetary policy. They recorded their best first quarter performance in five years, supported by hopes of a soft economic landing in the US and enthusiasm about Artificial Intelligence. Volatility also remained low during the period, as measured by the Volatility Index (VIX)," says Ted Franks Partner and Fund manager at WHEB said regarding the performance of the WHEB Sustainable Impact Fund.

"The 1st quarter was dominated by the big US Technology stocks ('The Magnificent 7'), including our investment Nvidia. This means that the market was driven by only a handful of stocks. In the second quarter this was less pronounced and the market was also supported by the performance of other sectors. There was also a bit of a rotation out of large caps into mid-and small caps," Triodos comments.

"The second quarter was a volatile period for equity markets as a result of changes in US inflation data, and the subsequent shift in market expectations around the pace and timing of interest rate cuts. From a thematic perspective, many of the themes seen in the first quarter of the year continued in the second quarter," George Crowdy, Fund Manager at Royal London Asset Management argues.

"Equities continued to advance in the second quarter, albeit at a slower pace than in the first quarter. Uncertainty over the timing of monetary policy easing and election outcomes in major developed and emerging economies drove sentiment during the quarter. Given this macro and geopolitical backdrop, it was a volatile quarter for equities, with a pullback in April, a rebound in May and more moderation in June," WHEB's Frank continues.

"Global stock markets showed positive growth overall in the second quarter. Initially markets fell in April due to persistently high US inflation, which lowered expectations of interest rate cuts. But in May, markets rose thanks to strong earnings reports and lower US inflation, which made investors less worried about an interest rate hike. The stock market continued rising in June, especially in the US, with the S&P 500 reaching a new high, driven by optimism around tech stocks. Even though the Federal Reserve changed its plan from three to one rate cuts by the end of the year, investors were not surprised, and the market maintained it's gains," Adam Robbins, Head of Business Development at Triodos Investment Management comments regarding the Triodos Pioneer Impact Fund.

"The dominant theme in the fixed-income market remained the US interest rate curve. In Q2, rates initially sold off but later rallied as US inflation moderated and employment data softened. This shift bolstered sectors such as real estate in credit markets, which outperformed as a result. Compared to Q1, which was marked by concerns over rate hikes and persistent inflation, Q2 saw a more favorable environment for risk assets as inflation data suggested the possibility of a softer monetary policy stance in the future,"Jeremy Sitruk, portfolio manager of the responsAbility Impact - Transition to Net Zero Fund

Ted Franks
WHEB

AI Rules and Heath Care Continue to Rule the Day

The first half of 2024 continued to be marked by the dominance of AI and large IT stocks. Given sustainable funds' tendency to not hold the stocks of the top 7 (tech) stocks and the preponderance of green energy stocks in their portfolio, it can be said that these two trends conspired to dampen relative performance.

"The strategy's benchmark, the MSCI World Index, had a strong start to the year, dominated by a few mega cap US stocks - highlighting the narrowness of the market rally. It was a more challenging time for sustainability themes, with comparatively few of the companies that we consider to deliver positive impact keeping up with the broader market. Cleaner Energy stocks particularly struggled, as concerns around overcapacity and higher interest rates grew," WHEB's Franks says.

"Key themes included digitalisation, which has been accelerated by AI, reindustrialisation trends, particularly in the US, and innovation in healthcare, particularly related to weight loss medicines," Royal London Asset Management's Crowdy argues.

"During the period, the fund made a positive return but lagged the benchmark significantly. The very strong performance of the "mega cap" technology stocks that are not qualified for WHEB's impact investment universe, was a meaningful headwind. Not owning just six non-impact stocks (Nvidia, Meta, Amazon, Microsoft, Alphabet and Broadcom) accounted for about half of the difference in performance between the fund and the index," WHEB's Franks continue

Although large AI and tech stocks are often excluded from Article 9 SFDR funds, on account of labour, privacy or governance controversies, a few managers were able to

George Crowdy
Royal London
Asset Management

benefit from the continued interest in these sectors.

"Performance was driven by a variety of holdings but with a particularly notable contribution from semiconductor holdings that enable or are exposed to AI. Over the period, the top performing holdings were NVIDIA and TSMC. The strategy also benefitted from gains in industrial holdings such as Wabtec, a leader in rail locomotives and rail technology and Schneider Electric, which is benefiting from growth in data centres and the broader electrification of society. The key headwind to relative fund performance came from not holding Apple, which performed strongly over the period. Our holding in Bank Rakyat, an Indonesian Bank focussed on micro lending, also detracted from performance following a slowdown in loan growth reflecting a more challenging credit environment," Royal London Asset Management's Crowdy added.

Royal London Asset Management was not the only asset manager to argue they were able to benefit from the AI craze. "The Artificial Intelligence (AI) theme definitely contributed to the performance of the funds. Our investment Nvidia reported strong quarterly results with a beat on sales, gross margins and earnings per share. In addition, the outlook remains strong with the company unveiling the Blackwell Superchip. The new Blackwell can run a generative AI model consuming around 25 times less cost and energy. These AI growth dynamics are also reflected in the results of semi (equipment) players. As such, the shares from companies like TSMC, KLA and BESI also contributed to the performance of our funds. But also a renewable company like First Solar performed well on this theme. The US solar panel manufacturer could be a beneficiary if the artificial intelligence-driven electricity demand ramps up. In addition, the strong performance of the Healthcare sector contributed to the performance, with Novo Nordisk doing very well. Another theme were M&As: in particular some of our mid-and small cap investments were approached for an acquisition, which underpins the attractive valuation of many small- and midcap companies. Examples were DS Smith (packaging company), Millicon (telecom), PowerSchool (education software) and Blackbaud (software)," Triodos commented in relation to the genera performance of its equity funds.

The healthcare sector continued to offer good returns on account of the continued popularity of anti-obesity drugs. "In Health, there were strong contributions across several stocks, including Novo-Nordisk, the pharma company. Wegovy, which is Novo's GLP-1 anti-obesity drug continued to report very strong prescription growth in the US. It also received regulatory approval for long-term weight management in China," WHEB's Franks continues.

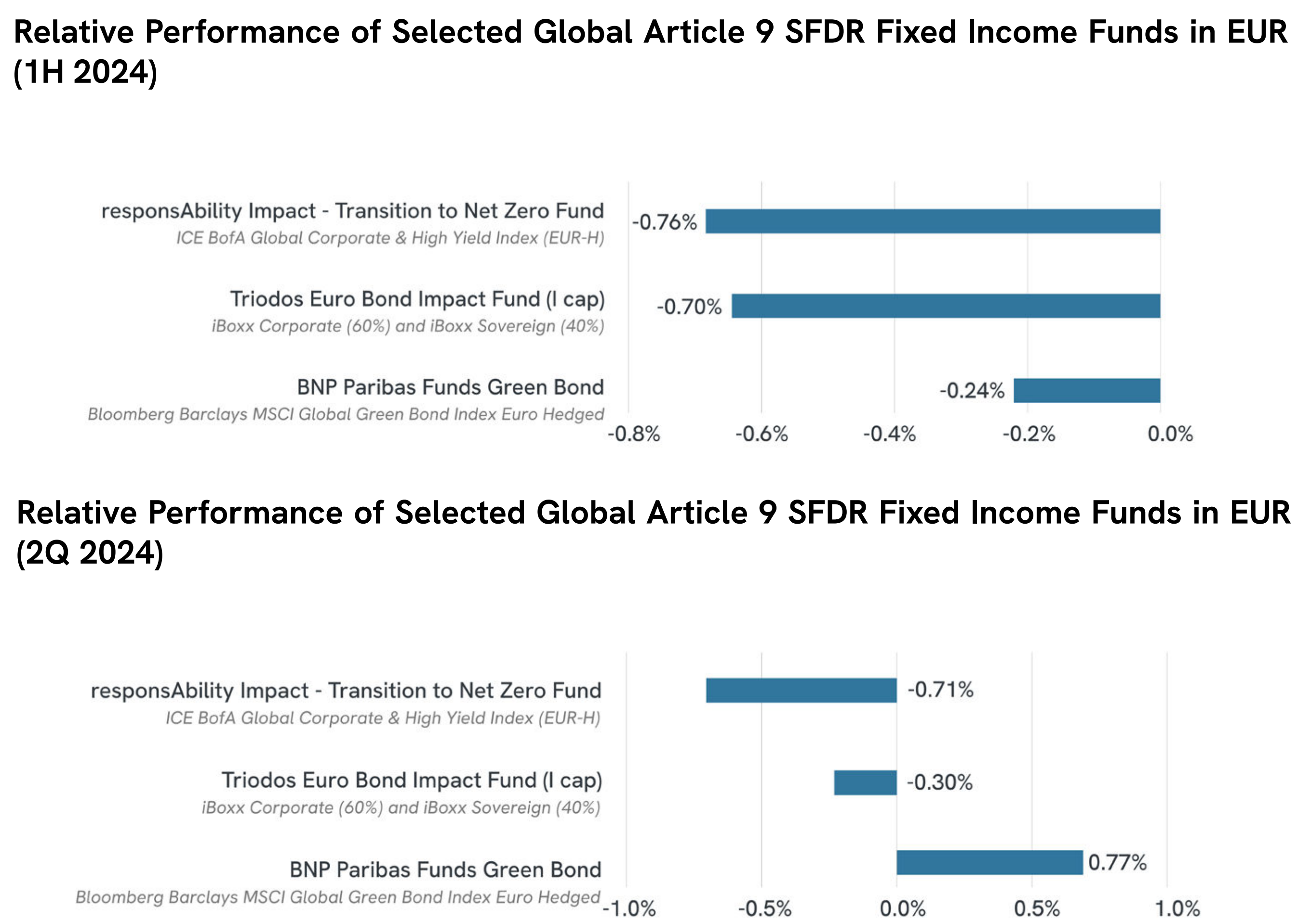
Mixed Performance in Renewables

Renewables, which have struggled since interest rates started to increase, appear to have experienced mixed performances during the first half of the year. While some managers pointed to stocks in this sectors as pushing performance downwards as is patent, others highlighted some positive contributions. The improvement of the performance of the BNP Paribas Energy Transition fund relative to the first quarter may be symptomatic of this shifts.

On the negative side, WHEB's Franks notes that "the largest detractor at a thematic level was Cleaner Energy. Wind turbine manufacturer Vestas' shares were weak as gains by political parties hostile to green energy spooked investors. There was also speculation that the number of new orders it received in the second quarter would miss expectations," WHEB's Franks adds.

On the other hand, Triodos' Robbins highlighted the positive contributions of solar to the performance of the Triodos Pioneer Impact Fund. "The success of the fund was mostly due to a strong performance in May when First Solar's stock rose by over 50%. This US solar panel company might benefit from increased electricity demand driven by artificial intelligence. Telecom company Millicom did well after its largest shareholder made an offer to buy the company. DS Smith is also being taken over by International Paper, showing that many small- and mid-cap companies are attractively valued," Triodos' Robbins said.

Jeremy Sitruk
responsAbility



Source: Fund manager data

Indeed, Triodos's outlook for this sector remains positive. "For the equity funds, we remain positive on the sustainable segments in the markets like Renewable Energy after a difficult 2023. In wind, we see already proof that things are changing in the right direction. New orders are signed at more favorable terms and, for example, the auction system (for offshore projects) is adjusted. This will result in better profitability for the players in this segment. Earnings momentum at Vestas and Nordex is showing improvement. In solar, visibility is low but we believe demand is around the bottom. Uncertainty about government subsidies (in countries like the Netherlands for example) did have a negative impact on demand. In California, the payback time is increased. However, if we look at the planned capacity expansions, there is still reasonable growth in front of us. A lot of investors have given up on companies in the solar segment and although we have not added extra exposure due to the lack of short term visibility, we still see long term opportunities," the asset managers at Triodos add.

The improvement of conditions was also felt in the fixed income sector, even if the underweight position of the responsAbility Impact - Transition to Net Zero Fund vis-à-vis this sector hurt the funds performance. "Over Q2, the fund's gross return was closely aligned with its benchmark, delivering 2.37% (USD-shareclass) versus 2.45%. Our sector allocation played a crucial role in this performance. We outperformed in the Healthcare, Telecom, and Real Estate sectors, while our underweight positions in Energy and Financial Services, due to our sustainability focus, led to underperformance in those areas. Notably, our cautious stance in High Yield detracted slightly, costing the portfolio 2 basis points. However, our longer-duration positioning, particularly in EUR-denominated credit, provided a significant positive contribution," responsAbility's Sitruk argues.

Water Management and Transport

Beyond these insights, Water Management, Sustainable transport and industrial engineering also stand out.

"On the other side of the ledger, the best performing themes were Water Management and Health. Within Water Management, both Xylem and Ecolab performed strongly. The US recently established the first national-level drinking water standard for PFAS. This will likely be positive for Xylem's growth as the company has a broad portfolio of high-quality water treatment solutions. Similarly, Ecolab's dual focus on high-quality business and environmental outcomes makes the company a preferred partner for companies looking to achieve their sustainability goals," WHEB's Franks says.

"Further negative contributions came from the Sustainable Transport theme due to positions including Aptiv, which specialises in the electrification of vehicles. The share price dropped following news that Volkswagen has invested US$ 5 billion in a joint venture with Rivian to access the electric vehicle company's software. We think this response is overdone as we do not believe this move substantially weakens Aptiv's competitive position," WHEB's Franks adds.

"At a stock level, the largest detractor overall was Spirax, the industrial engineering company, which has faced a challenging end-market environment across most of its segments. With broad end-market exposure, Spirax is exposed to industrial production levels generally, and these have been weak. In addition, the semiconductor and life sciences markets which have been successful for Spirax in recent years, experienced greater struggles. These are high margin businesses for the company and their underperformance has resulted in a margin decline for the group. While guidance for 2024 was taken positively it is significantly weighted to a recovery in the second half, and the uncertainty about whether that will come through has weighed on share price performance," WEB's Franks continues.

Cautious Optimism Going Forward

Fund managers seem optimistic about the way forward, although they warn against potential labour market pressures on inflation, sectoral divergences and a potential waning in political support for sustainability in the EU.

"Looking ahead, we expect headline inflation to continue falling slowly in the US, UK and Eurozone over the remainder of 2024. However higher wage inflation and continued geo-political risks mean this is far from certain," Triodos' Robbins says.

"Looking ahead, we anticipate companies leading in decarbonization within their respective sectors to outperform peers over the longer term. These companies are positioning themselves at the forefront of an inevitable transformation in business models driven by sustainability imperatives. In the next 12 months, we expect lower financing costs to support the lower-credit-quality spectrum, which has pushed valuations higher in the High Yield space. Consequently, we remain cautious in that segment, maintaining a conservative approach despite improving conditions. Overall, we believe the structural trends driving sustainable investments will continue to gain momentum, though market volatility may persist," responsAbility Sitruk adds.

"In the short-term, we see divergence in the operating environments of the sectors in which we invest. Some, like electric vehicles, remain more challenged as they adjust to weaker 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," WHEB's Franks says.

"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, including the UK and French elections which suggest 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. Although expectations of interest rate increases have been tempered, the direction of change should still favour smaller and more growth-oriented impact stocks even if the timing is uncertain," WHEB's Franks continues.

Looking ahead, we anticipate companies leading in decarbonization within their respective sectors to outperform peers over the longer term. These companies are positioning themselves at the forefront of an inevitable transformation in business models driven by sustainability imperatives.

INTERNATIONAL PARTNERS

Private Assets

Stability leads to higher private market returns in Q2

Filipe Albuquerque

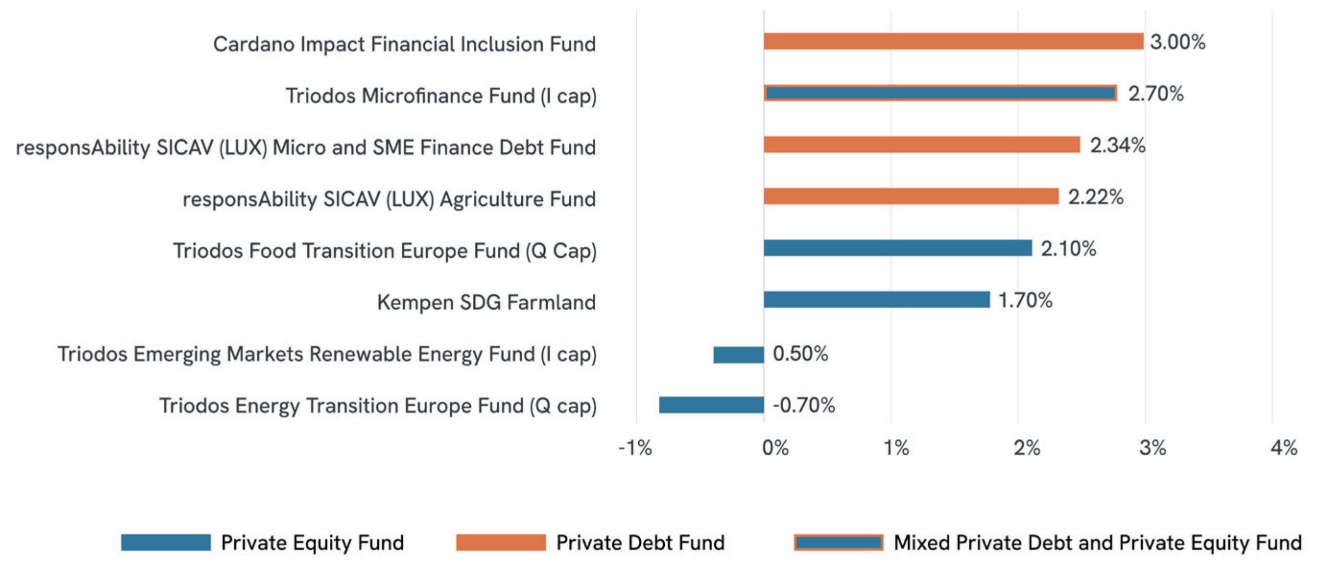
Although public markets are more liquid, sustainable private market investments are often taunted as providing investors with the opportunity to make a stronger and more material contribution to making the world more sustainable.

To better understand the performance of private debt and private equity markets during the first half of 2024, NordSIP approached a range of such Article 9 funds to hear about their experiences. Our survey covered eight private market funds. Three Article 9 private debt funds replied to our inquiries: the Cardano Impact Financial Inclusion Fund, the responsAbility SICAV (Lux) Agriculture Fund and the responsAbility SICAV (LUX) Micro and SME Finance Debt Fund. Their replies were complemented by feedback from the portfolio managers of four Article 9 SFDR private equity funds: the Kempen SDG Farmland Fund, the Triodos Energy Transition Europe Fund, the Triodos Food Transition Europe Fund and the Triodos Emerging Markets Renewable Energy Fund. Finally, we also received feedback from the Triodos Microfinance Fund, which invests in both private equity and private debt.

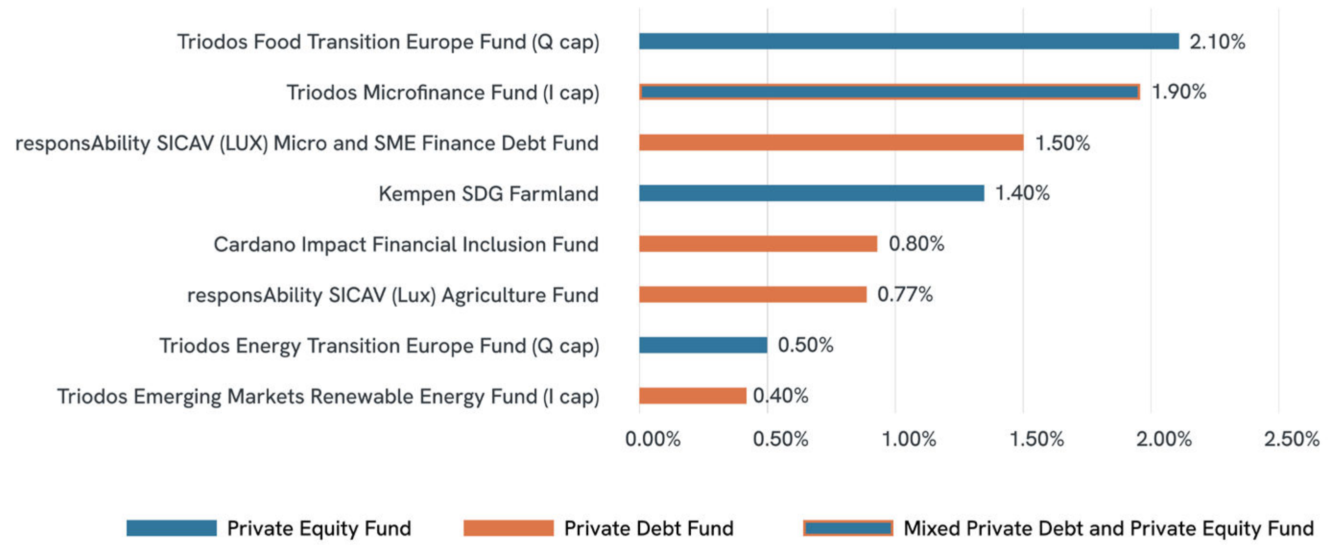
Consistent with the experience of asset managers from in public markets, it appears that green shoots of monetary policy easing during the second quarter of 2024 facilitated better returns for private market funds, more so than their private equity counterparts.

Nevertheless, although the feedback NordSIP received acknowledges the importance of the more accommodating monetary policy environment, the effect of this factor on performance appears to be mediated by a range of other variables specific to impact investment.

Performance of Selected Article 9 SFDR International Private Market Funds in EUR (H1 2024)



Performance of Selected Article 9 SFDR International Private Market Funds in EUR (2Q 2024)



Source: Fund manager data

Monetary Policy Matters

Unsurprisingly, private debt fund asset managers are most keen to discuss the effect of monetary policy developments on their portfolio.

"In the second quarter, we observed a pick-up in our investment pipeline across several geographies, which was partly driven by typical seasonality. Additionally, clearer signals from the U.S. Federal Reserve regarding potential future rate cuts positively influenced market conditions, providing a more favorable environment for pricing and negotiation. This contrasts with the first quarter, where high interest rates remained a key theme, and our focus was on capturing income opportunities in emerging markets," says Jaskirat Chadha, portfolio manager of the responsAbility SICAV (LUX) Micro and SME Finance Debt Fund.

"The fund's strong performance during second quarter was driven by our ability to capitalize on attractive yields while maintaining an optimally invested portfolio. Higher income from our debt investments, combined with stable provisioning in line with historical averages, contributed to steady returns. We would particularly highlight the investments in regions like South Asia and Central Asia, where we saw robust opportunities in financial inclusion and SME lending, supporting micro and small businesses. Our investment in Seeds Fincap and Bank Arvand in Tajikistan are notable examples, reflecting our commitment to resilient financial institutions in emerging markets," responsAbility's Chadha adds.

"In the first half of 2024, emerging markets' economic growth has been better-than-expected and the latest news on inflation has been encouraging. Nevertheless, the uncertainty surrounding the timing of Federal Reserve (Fed) rate cuts has led to some currency volatility, as emerging markets remain overly sensitive to US inflation and Fed interest rate policy expectations because of the impact that these decisions will have on the US dollar," the portfolio managers of the Triodos Microfinance Fund note.

Elections, Debt Restructurings and Emissions Shortcomings

However, private debt markets are not exclusively driven by monetary policy dynamics. Other macro factors, such as elections and debt restructuring, also seemed to be on top of asset managers' mind.

"Several countries have been holding elections this year, including India, Mexico and South Africa. After losing their majority, the ruling parties in both India and South Africa will need to work with others. In Mexico, the landslide victory of the ruling party paves the way for institutional changes," the Triodos Microfinance Fund report explains. "Several leading emerging markets saw elections during the Q2 2024. Inflation has been still a topic. Overall, inflation dynamics are turning more divergent," Sinisa Vikuc, portfolio manager of the Cardano Impact Financial Inclusion Fund agrees.

"Inflation and 'Core inflation' is already at or below central bank targets in EM Asia but remains elevated in much of LatAm and EMEA EM. EM credit spreads have continued to retrace lower in the quarter," Cardano's Vikuc adds. Although Vikuc notes that his portfolio benefited from a lack of relevant credit events, other investors chose to highlight the recent restructurings.

"Positive news came from emerging markets involved in debt restructuring deals, like Pakistan and Sri Lanka. Sri Lanka reached a first step in a debt restructuring agreement with official creditors. Meanwhile in Kenya, protests have taken the upper hand after implementing tax reforms to meet fiscal targets required by the International Monetary Fund (IMF). IMF agreements remain a main source of financing for many emerging economies and are also seen as evidence that countries are taking the necessary steps for long-term stability under IMF surveillance," the portfolio managers of the Triodos Microfinance Fund comment.

Asset managers also highlighted reports from the World Bank and the International Energy Agency shedding a light on global shortcomings regarding emissions cutting.

"Emerging economies are securing investments for climate mitigation and adaptation; however, they are hindered by funding challenges," the asset managers of the Triodos Emerging Markets Renewable Energy fund say in the funds half year report. "The International Energy Agency (IEA) issued a report stating that the global clean energy plans fall short of 2030 targets agreed at United Nations (UN) climate talks last year. Affordable financing from multilateral organisations, including IMF and World Bank is helping but is not yet sufficient. The IEA estimates that the private sector will have to come up with 70% of the climate finance globally needed," Triodos adds regarding the Emerging Markets Renewable Energy fund.

Adam Kybird, portfolio manager of the (private equity) Triodos Food Transition Europe fund, also noted that "the World Bank's call for an 18-fold increase in investments to halve agrifood emissions underscores the need to tackle environmental impact of food production globally, as the sector is estimated to contribute one-third of global greenhouse gas emissions."

Agricultural Prices Stabilise

On a more micro level, the private equity managers of both the responsAbility SICAV (Lux) Agriculture (private debt) fund and of the Kempen SDG Farmland (private equity) fund highlight the normalisation of agricultural commodity prices.

Alice MacNeil
Kempen

"The main market themes during the second quarter have been similar to the first quarter, namely a continuation of the relative weakening of prices for various agricultural commodities compared to the previous year. Forecasts point to a downward trend in global commodity prices over remainder of the year. However, farmland prices have proven resilient in the face of challenges such as rising interest rates, the decline in commodity markets and concerns over the profitability of agriculture. On average, farmland prices remained largely unchanged this quarter. Whilst certain categories of land have lost value, high value farms remain attractive to competitors and retain their value," says Alice MacNeil, portfolio manager of the Kempen SDG Farmland Fund.

Suhasini Singh, portfolio manager of the responsAbility SICAV (Lux) Agriculture Fund agrees, "A notable theme in the second quarter was the normalization of cocoa prices, following heightened volatility in the first quarter. This trend coincided with broader disinflation across emerging markets, which provided a more stable environment for agriculture-focused financial institutions. Additionally, our investments in coffee-producing countries, such as Uganda, continued to deliver stable returns during this period," Singh explains.

"Operationally, the year is going well. The fruit is setting well in most of our permanent crops without any significant setbacks. The 2024 planting season in the northern hemisphere for row crops was interrupted by significant rainfall, which resulted in delayed sowing (outside the optimal time window), but since then the growing season has gone well. In the southern hemisphere, most of our row crop farmers were able to successfully grow a winter crop. The only exception was South Australia, where there has been no rain at all so far this year," Kempen's MacNeil adds. She highlights the performance of the farm Kempen owns in New South Wales (Australia), acquisitions in La Palma (Uruguay) Marskgaarden (Denmark) and the evaluation of opportunities in the US's Pacific Northwest's blueberry market and opportunities for growth in New Zealand's organic apple market.

"The Fund's performance in the second quarter of 2024 can be attributed to strong investments in South America, particularly in the coffee harvest in Peru, which yielded favorable results. The funds invested amounted to over USD 12 million across seven countries, with USD 8 million allocated to Latin America. This was driven by the coffee harvests in Peru, as well as additional investments in Bolivia and Nicaragua. These investments in resilient agricultural sectors were pivotal in delivering a quarterly return of +1.23% in USD and a year-to-date return of +3.15% in USD," responsAbility's Singh adds.

Food Inflation Slows Down in Europe

Given these agricultural dynamics, it is not surprising to find that food prices have also stabilised in Europe.

"There is welcome news on the food price front. After reaching a peak of 5.6% in February, food inflation has fallen significantly to 2.6% by May. This decline is particularly evident in unprocessed foods like fruits and vegetables, likely due to a comparison effect from high price increases in 2023. Stabilizing energy and commodity prices are the main drivers behind this positive trend," says Triodos' Kybird

"This offers much-needed relief for consumers, but it's important to note that food price inflation remains above pre-pandemic levels. While declining, it still sits higher than the long-term average of around 2.1% experienced before the pandemic," Kybird adds.

Jaskirat Chadha
responsAbility

"The fund delivered a positive result this quarter reflecting stronger performance for many of our key investments. This was welcome after a challenging period in the Private Equity and sustainable food space but also reflects the resilience of our portfolio and strategy," Kybird explains while pointing to the recent contributions of CrowdFarming, KoRo and Stadtsalat as sources of "strong revenue growth".

Heat Records impact Food and Energy Transition in Europe

The Triodos Energy Transition Europe fund and the Triodos Food Transition Europe fund focused on the impact of the war in Ukraine, regulation and climate change. "Since the end of 2021, we have seen continued unrest in the energy markets. After Russia's invasion of Ukraine, prices have risen rapidly. Prices have now fallen again but are still well above the level before the Russian invasion. Nevertheless, installed wind and solar capacity is at record hights and is the cheapest energy source which can run without the need of subsidies. The installed capacity is expected to double in the next 5 years following an exponential growth path," the asset manages of the the Triodos Energy Transition Europe fund, say in their half year report.

"Furthermore, the first half of 2024 witnessed no respite from the global heating crisis. Records continued to shatter for a 13th consecutive month, with June 2024 becoming the warmest ever documented. This relentless warming aligns with projections from the IPCC, which suggest a likelihood of exceeding the 1.5°C warming threshold by 2100," the asset managers of the Triodos Energy Transition Europe fund add.

Commenting on these continued heat records, Triodos's Kybird notes that "this is echoed by a recent study published in Nature Climate Change, which argues that current national plans to reduce carbon dioxide emissions fall short of what's needed to achieve the Paris Agreement goals."

Triodos' analysts note four recent and future developments on the regulatory. The asset managers of the Triodos Food Transition Europe Fund highlight the approval of the EU's Nature Restoration Law and note that the "Corporate Sustainability Due Diligence Directive (CSDDD) marks a significant step forward for the EU". Kybird highlights two regulatory developments to look forward from the EU: a post-2027 potential reduction in the environmental regulations of the EU's Common Agricultural Policy (CAP) and the conclusion of "the stalled comprehensive reform on pesticide use".

After reaching a peak of 5.6% in February, food inflation has fallen significantly to 2.6% by May. This decline is particularly evident in unprocessed foods like fruits and vegetables, likely due to a comparison effect from high price increases in 2023. Stabilizing energy and commodity prices are the main drivers behind this positive trend.

An Optimistic Outlook

Beyond these regulatory developments, the asset managers of private market funds share a distinctively optimistic tone about the future, based on the perceived popularity of natural capital and an accommodating monetary, economic and regulatory environment.

"As reported in Q1, there is a steady demand – especially from institutional investors - for investments in natural capital aimed at addressing and mitigating the pressing biodiversity and climate challenges we currently face – a recent study (bfinance) identifies more than 50 asset managers active in this sector (Natural Capital Report, 2024). Our expectation is that this demand will continue to grow, but that investors will become more discerning in their choice of asset classes as some fail to deliver on quality expectations," Kempen's MacNeil says.

"We remain optimistic about the outlook for the second half of 2024. The fund is positioned to continue benefiting from its attractive yields and anticipated stable provisioning levels. GDP growth in our key investment markets, particularly in emerging economies, is expected to remain strong. Additionally, with potential rate cuts in the U.S., we foresee increased capital flows to emerging markets, which should create a supportive environment for our investments. Overall, we expect sustainable markets to perform better in 2024 than in 2023, as financial inclusion and SME growth continue to gain momentum across our target regions," responsAbility's Chadha adds.

"We expect the second half of 2024 to perform better than 2023, as the Fund continues to benefit from strong commodity market yields, particularly in coffee and cocoa. Losses related to the pandemic and geopolitical disruptions have begun to normalize, which supports a positive outlook. Additionally, we anticipate a fully invested portfolio by the end of the third quarter, driven by financing opportunities across Vietnam, the UAE, and Turkey," responsAbility's Singh continues.

"With some exciting new investments on the near horizon and some positive moves in the policy / regulatory environment we are optimistic about the coming years," Triodos' Kybird concludes.

NORDSIP

NORDIC SUSTAINABLE INVESTMENTS

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