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Schroder ISF* Global Climate Change Equity

Fund Managers: Simon Webber, Isabella Hervey-Bathurst | Fund update: December 2024

Performance overview

- Global equities were mixed in December. US shares fell, while eurozone and Japanese shares gained.
- The fund posted a negative return and underperformed the MSCI All Country World index over the month.

Drivers of fund performance

- Stock selection was negative, particularly in information technology, materials, and consumer discretionary. Our overweight allocation to industrials also detracted. Conversely, selection in communication services and consumer staples added value in the month.
- By region, the UK, Continental Europe, emerging markets, and North America detracted, while allocations to Japan and Pacific ex Japan added value in December.
- US energy company **NextEra Energy** underperformed in December as investors banked profits amid utility sector jitters following the US presidential election. However, the company continues to perform well, with third-quarter earnings per share exceeding analyst expectations. The company's growth continues to be driven by rising electricity demand, particularly from data centres, and a strong construction pipeline.
- **Nvent Electric, Top Build,** and **Weyerhaeuser** were among the biggest individual detractors in December. Allocations to **Owens Corning, Vestas Wind Systems,** and **Norsk Hydro** also detracted in the month.
- **Alphabet** outperformed in December, despite an antitrust case hanging over the company and intensifying competition in artificial intelligence (AI), as the company unveiled a new chip that it said was a breakthrough in quantum computing.
- **Amazon, BMW,** and **Sekisui Chemical** were among the biggest individual contributors in December. Allocations to **Hitachi**, **Siemens** and **Kroger** also added value in the month.

Portfolio activity:

- We initiated a new position in **Core & Main**, a U.S. distributor of water, sewer and fire protection products, in December. We believe it can grow above the broader water infrastructure and construction market growth due to its competitive advantages (scale and breadth of offering) and by expanding into adjacent areas such as storm drainage. While M&A is the key driver of the growth gap, Core & Main will also see margin expansion as it reaps the benefits of scale.
- We initiated a new position in **Comfort Systems** in December. The company, which provides HVAC installation and facilities management services to commercial and industrial end markets, is set to continue to benefit from the positive backdrop for US non-residential construction, particularly in manufacturing and AI capex. The growth gap is driven by both organic growth and M&A.
- We sold our position in **Owens Corning** in December. Although the company has delivered exceptionally well, we do not believe this level of profitability is sustainable given the industry capacity additions planned.
- We sold our position in **Top Build** in December. We have yet to see good momentum in new housing starts, so we plan to revisit the stock when we have a more positive view on house building.

Outlook/positioning

Financing costs are coming down, creating a tailwind for green investment: Global interest rates, which spiked in response to inflationary pressures, have stabilised, with some central banks starting to announce reductions. Lower borrowing costs provide a much-needed boost for capital-intensive green projects, making investments in renewables, energy storage, and other climate technologies more attractive. Potentially inflationary policies under a new Trump Administration pose a risk factor to this and raise the prospect of a persistently higher US yield curve.

Recovery potential in key end markets, following cyclical weakness: While markets such as EVs, heat pumps, and residential solar have experienced recent

*Schroder International Selection Fund is referred to as Schroder ISF throughout softness, driven by consumer demand slowdowns, and in some cases inventory cycles and policy changes, the medium-term outlook remains bright. As macroeconomic conditions improve and inventory clears, we expect a rebound in these sectors.

Long-term foundations for climate investment remain strong: Despite short-term challenges, global climate policy frameworks such as the EU Green Deal, along with widespread corporate commitments on climate, continue to support efforts to decarbonise global economies. Additionally, renewable energy remains very competitive with other energy sources, and EV prices are declining as the industry scales.

Valuations are attractive, pain has been taken: Valuations across many climate-related assets are at attractive levels after a period of prolonged weakness for the theme. However, investor sentiment towards the sector is subdued, presenting an opportunity for long term investors to buy into industry-leading companies at compelling entry points. Several end markets within the climate theme have now digested a significant amount of 'capital cycle' pain, resulting in significant market cap destruction and a handful of bankruptcies. Our focus remains on companies with the strongest business models, technology, and balance sheets.

US climate policy at risk: A Republican sweep of the Presidency and US Congress is likely to result in significant changes to US climate policy. Whilst it is far from inevitable that the Inflation Reduction Act will be repealed given thin majorities in Congress and competing policy priorities, certain elements are likely to be reduced or removed. Medium term, there will be less opportunity for an aggressive energy transition and climate investment in the US in the next 4 years. This is disappointing but the rest of the world will not stand still.

More broadly, the likely policy changes following the US election do not change the equation that the long-term outlook for the transition to a low carbon economy is robust. We believe that we are at or close to the bottom of a sentiment and valuation cycle for climate change investing despite a huge opportunity for growth and transformation ahead of us. The US election may represent the clearing event necessary to mark the eventual trough.

Past performance does not predict future returns. The value of investments and the income from them may go down as well as up and investors may not get back the amount originally invested.

Calendar year performance (%)

	Fund	Benchmark***
2024	4.3	17.5
2023	12.3	22.2
2022	-24.4	-18.4
2021	11.2	19.3
2020	51.7	15.9
2019	25.5	27.7
2018	-10.8	-8.7
2017	30.5	22.4
2016	2.7	7.5
2015	2.0	-0.9

Source : Schroders, net of fees, NAV to NAV with net income reinvested. C Acc share class, as at 31 December 2024. ***MSCI All Country World - Net Return. The Fund does not have a target benchmark. The Fund's performance should be compared against the MSCI All Country World (Net TR) index. The comparator benchmark is only included for performance comparison purposes and does not have any bearing on how the Investment Manager invests the Fund's assets. The Fund's investment universe is expected to overlap materially with the components of the comparator benchmark.

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– **Counterparty Risk**: The fund may have contractual agreements with counterparties. If a counterparty is unable to fulfil their obligations, the sum that they owe to the fund may be lost in part or in whole.

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- **IBOR Risk**: The transition of the financial markets away from the use of interbank offered rates (IBORs) to alternative reference rates may impact the valuation of certain holdings and disrupt liquidity in certain instruments. This may impact the investment performance of the fund.
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