# Global Sustainable Outcomes update: Q3 2023

## Global equities | December 2023

**Pauline Grange**
Portfolio Manager,
Global Equities

Observing global markets this year has been a bit like watching Groundhog Day, in which Bill Murray's character repeats the same day over and over. We are stuck in a bit of a market loop where investors grow optimistic that inflation is peaking, which feeds into lower interest rate expectations, which supports a stronger consumer, which fuels inflation, which raises rate expectations, which slows the consumer, which feeds slowing inflation which … you get the picture.

A 29% jump in oil prices in Q3, combined with hawkish commentary from the US Federal Reserve around further rate hikes, pushed the US 10-year bond yield close to 5% – a level not seen since before the global financial crisis. Higher interest rates and oil prices create a tough backdrop for sustainable strategies, with the Columbia Threadneedle Sustainable Outcomes Global Equity (SOGE) strategy no different, falling 6.5% versus the MSCI ACWI's 3.3% over the quarter.

However, as interest rates rise, global financial and economic risks also rise. This raises concerns of "Black Swan" financial events – negative events that are difficult/impossible to predict[1] – like the one seen earlier this year which triggered the collapse of Silicon Valley Bank.

### Reality bites for renewables

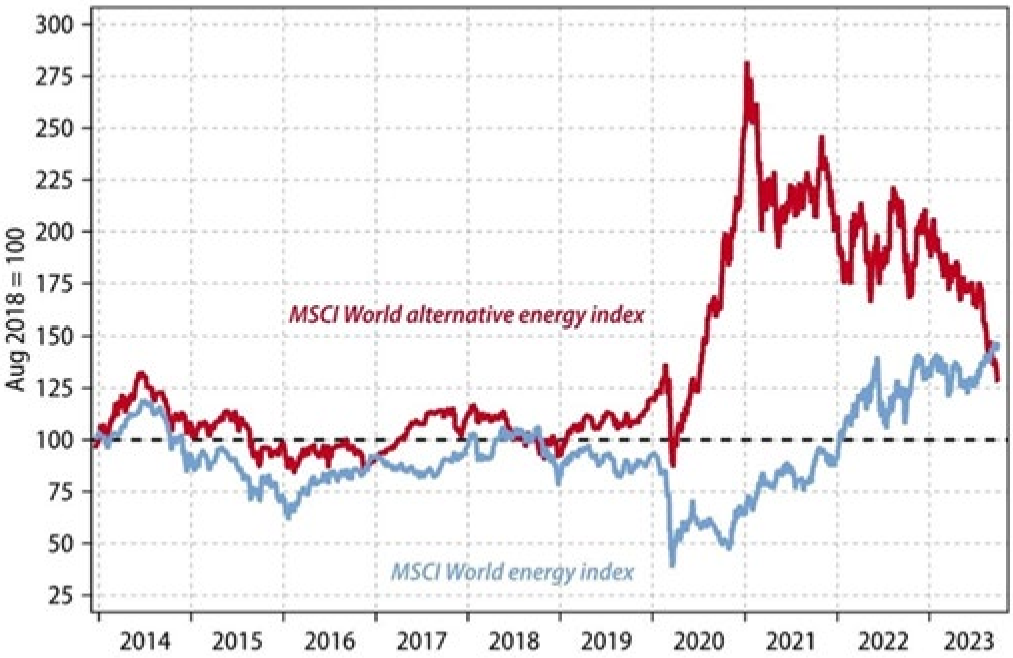
Sadly, it was the renewable sector that faced such an event in Q3. The latest surge in financing costs over the quarter triggered a spate of warnings across the sector, including from two of our investments, Orsted and Nextera[2], and wind turbine manufacturer Siemens Gamesa.

[1] Corporate Finance Institute, What is a Black Swan Event?

[2] Mention of specific companies is not a recommendation

The renewables sector has experienced a brutal de-rating since 2021 as rising interest rates weighed on high valuations and the cost of financing. The Q3 fall in renewables and rally in oil stocks erased all the outperformance of alternative energy relative to fossil fuels since 2018.

Figure 1: alternative energy performance versus the world energy index




Source: Gavekal Research/Macrobond, October 2023

Other factors have also been at play. Equipment costs have spiked in recent years due to higher commodity inflation and supply chain bottlenecks hindered by government targets to reduce reliance on cheap Chinese supply. Long permitting times and a growing backlog of renewables waiting to connect to power grids have also created headwinds to industry growth. In a recent report, the International Energy Agency (IEA) noted that more than 3,000 gigawatts (GW) of renewable power globally is waiting for connection to national grids, hindering current projects and putting new ones at risk[3].

However, it is offshore wind that has been particularly hard hit. The world's biggest offshore wind developer, Orsted, was forced to cancel two US offshore projects and take about $4 billion in impairment charges rather than sustain heavy losses. The company won these projects during the period of ultra-low interest rates in 2020 and 2021, since when development and financing costs have surged. With pricing fixed at low levels and costs not hedged, Orsted subsequently faced a severe revenue-cost mismatch. This mismatch is also putting Orsted's expansion of the UK offshore wind development, Hornsea 3, at risk. Fortunately we exited our position in Orsted earlier in the quarter on concerns around the more structural pressures facing offshore wind development.

[3] International Energy Agency, Lack of ambition and attention risks making electricity grids the weak link in clean energy transitions, October 2023

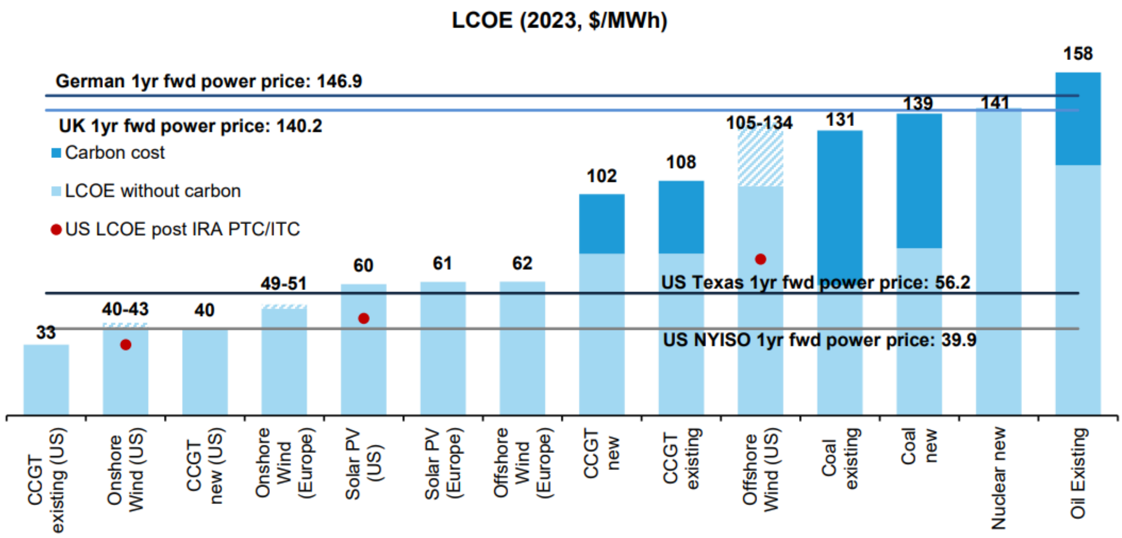
Given such headwinds, are government decarbonisation targets now at risk or is this merely a bump in the clean energy transition road?

Recent geopolitical turmoil in oil producing regions like Russia and the Middle East and the subsequent rise in costs have only increased the urgency of diversifying energy sources away from fossil fuels – especially for the 80% of the world who are net importers of oil and gas. Furthermore, with 2023 set to be the hottest year on record, governments globally are coming under increasing pressure to decarbonise their economies.

Another fund holding, NextEra, an operator of a regulated utility in Florida and a leading developer of US onshore wind and solar energy, dropped over the quarter after its yield company subsidiary, NextEra Energy partners (NEP), halved its dividend growth outlook citing the impact of higher interest rates. We retained our investment given our more positive outlook for US onshore wind and solar growth and returns. This was supported by subsequent meetings with Nextera's CEO, John Ketchum, and CFO, Terry Crews.

Unlike Orsted, NextEra has been able to renegotiate its renewables contracts in 2022 to offset higher costs. This is supported by data from LevelTen Energy, which indicates an approximate 85% increase in US PPA (power purchase agreement) prices for onshore wind and solar contracts compared with 2020. Despite these price increases, NextEra noted continued strong demand for renewables as onshore wind and solar remain the lowest cost source of new-build utility scale power in the US (including tax credits under the Inflation Reduction Act.

Figure 2: Renewable LCOE (levelised cost of energy) is below fossil fuels, especially in Europe




Source: BNEF, IRENA, Bloomberg, Bernstein analysis and estimates, as 2023. Note, ranges reflect 2023 LCOE as well as LCOE of a later year, if higher

NextEra subsequently reported strong results in Q3 which showed sustained strength both in renewable growth and returns. Its renewables backlog increased to a record 3.2GW adding to the company's total backlog of 21GW, while price increases mean expected returns on this backlog have increased to mid-teens for solar and more than 20% for onshore wind and storage. The company also noted an improving supply chain with the cost of solar modules dropping by about 40% over the past 12 months.

But there are signs of discipline returning to the offshore wind market, with developers seeking higher prices at auction and regulators showing willingness to increase them. For example, a UK offshore wind auction in September attracted zero bidders as the government failed to increase prices sufficiently to cover higher costs. However, the UK government indicated it is preparing to offer significantly higher subsidies in subsequent offshore wind auctions.

The updated Net Zero Roadmap published in Q3 by the IEA set out a refreshed pathway to net zero by 2050 . It highlighted that even after the acceleration in global deployment across clean energy technologies in recent years, renewable capacity still needs to triple by 2030 if targets are to be met. Although a further rise in interest rates could continue to pose challenges, supportive government policies like the US IRA will be a mitigating factor to financing headwinds. With renewable developers increasingly prioritising returns, and continuing robust demand for renewables, we could just be finished with this bump in the energy transition.

## Q3 2023 CTSOGE strategy new company purchases[4]

| Company | Sustainable category | Investment case |
|---|---|---|
| **Humana**<br><br>**Mission:** “Helping people live healthy and happy” | **Leader**<br>**MSCI A**<br><br>Health, Wellbeing & Food Security<br><br>3 GOOD HEALTH AND WELL-BEING | Humana generates 95% of sales from its US health insurance operations, which support access to medical care for Humana plan members. Its focus on Medicare Advantage, Medicare (for people 65 or older) and Medicaid (for people on limited income) aligns its commercial incentives with positive health outcomes for its members. 4% of sales are from CenterWell, the company’s value-based care operations. Strong product innovation and increased access to healthcare through Medicare and Medicaid demonstrate clear sustainable intentionality. Humana’s service quality assurance outperforms its peers, with 4.9 million members in 4-star or higher plans. They also enjoy a strong competitive position with 50% share in Medicare lives and share gains in both Medicare and Medicaid. |
| **Dexcom**<br><br>**Mission:** “Empowering people to take control of health” | **Leader**<br>**MSCI A**<br><br>Health, Wellbeing & Food Security<br><br>3 GOOD HEALTH AND WELL-BEING | Healthcare sustainability is core to Dexcom management’s ambitions. As a leader in continuous glucose monitoring (CGM) solutions, Dexcom is helping patients suffering from chronic diabetes to better manage the disease. The company demonstrates sustainable intentionality by innovating in the field of glucose monitoring, introducing a convenient and more accurate alternative for finger pricks. The growth outlook for the CGM market is strong, driven by continued rates of device penetration for both type 1 and 2 devices. Within this market, Dexcom is a share gainer supported by its international growth and product innovation. Despite concerns to the contrary, CGMs are a powerful tool for GLP-1s patients whilst helping to inform doctor dosing of this. |

[4] Mention of specific companies is not a recommendation

# Threadneedle Global Equity Sustainable Outcomes Composite

## GIPS Report: Columbia Threadneedle Investments EMEA APAC

Reporting Currency: USD

### Statement of Performance Results

| Calendar Year | Gross-of-fees Return (%) | Net-of-fees Return (%) | Index Return (%) | Composite 3-Yr St Dev (%) | Index 3-Yr St Dev (%) | Internal Dispersion (%) | Number of Portfolios | Total Composite Assets (mil.) | Total Firm Assets (bil.) |
|---|---|---|---|---|---|---|---|---|---|
| 2022 | -22.56 | -23.07 | -17.96 | 20.18 | 19.86 | N.A. | ≤ 5 | 139.1 | 114.9 |
| 2021 | 19.21 | 18.45 | 19.04 | 14.52 | 16.83 | N.A. | ≤ 5 | 177.7 | 161.3 |
| 2020 | 28.12 | 27.30 | 16.82 | N.A. | N.A. | N.A. | ≤ 5 | 1.5 | 149.8 |
| 2019 | 33.17 | 32.32 | 27.30 | N.A. | N.A. | N.A. | ≤ 5 | 1.2 | 140.5 |

### Annualized Trailing Performance as of December 31, 2022

| Period | Gross-of-fees Return (%) | Net-of-fees Return (%) | Index Return (%) |
|---|---|---|---|
| 1 Year | -22.56 | -23.07 | -17.96 |
| Inception | 12.03 | 11.31 | 9.78 |

Inception Date: December 31, 2018

1. Columbia Threadneedle Investments EMEA APAC 'the Firm' claims compliance with the Global Investment Performance Standards (GIPS®) and has prepared and presented this report in compliance with the GIPS Standards. Columbia Threadneedle Investments EMEA APAC has been independently verified by Ernst & Young LLP for the periods 1st January 2000 to 31st December 2022. The verification reports are available upon request. A firm that claims compliance with the GIPS standards must establish policies and procedures for complying with all the applicable requirements of the GIPS standards. Verification provides assurance on whether the firm's policies and procedures related to composite and pooled fund maintenance, as well as the calculation, presentation, and distribution of performance, have been designed in compliance with the GIPS standards and have been implemented on a firm-wide basis. Verification does not provide assurance on the accuracy of any specific performance report. GIPS® is a registered trademark of CFA Institute. CFA Institute does not endorse or promote this organization, nor does it warrant the accuracy or quality of the content contained herein.

2. The 'Firm' is defined as all portfolios managed by Columbia Threadneedle Investments EMEA APAC (prior to 1 January 2021, the firm was known as Threadneedle Asset Management) which includes Threadneedle Asset Management Limited, (TAML), Threadneedle International Limited, (TINTL), Threadneedle Investments Singapore (Pte.) Limited, (TIS), and Threadneedle Management Luxembourg S.A. (TMLSA), excluding directly invested property portfolios. The firm definition was expanded in 2015 to include portfolios managed by then newly established affiliates of Threadneedle Asset Management in Singapore. TAML & TINTL are authorised and regulated in the UK by the Financial Conduct Authority (FCA). TINTL is also registered as an investment adviser with the U.S. Securities and Exchange Commission and as a Commodities Trading Advisor with the U.S. Commodity Futures Trading Commission. TIS is regulated in Singapore by the Monetary Authority of Singapore. TMLSA is authorised and regulated in Luxembourg by the Commission de Surveillance du Secteur Financier (CSSF). On 1 July 2020, Threadneedle Asset Management Malaysia Sdn. Bhd (TAMM) was removed from the firm. Columbia Threadneedle Investments is the global brand name of the Columbia and Threadneedle group of companies. Beginning 30 March 2015, the Columbia and Threadneedle group of companies, which includes multiple separate and distinct GIPS-compliant firms, began using the global offering brand Columbia Threadneedle Investments.

3. A concentrated global equity strategy with a focus on high quality companies that seeks to deliver both positive sustainable outcomes, in accordance with the UN Sustainable Development Goals (SDGs), and superior financial returns. Derivatives are not allowed. The composite was created November 30, 2018.

4. The gross-of-fees returns are time-weighted rates of return with cash flows at the end of the day. Returns reflect the reinvestment of dividends and other earnings and are net of commissions and other transaction costs. Returns are calculated net of non-reclaimable withholding taxes on dividends, interest, and capital gains and are shown before management and custodian fees but after the deduction of trading expenses. Composite returns are calculated by using underlying portfolio beginning of period weights and monthly returns. Periodic returns are geometrically linked to produce longer period returns. Net of fee returns are calculated by deducting the representative fee from the monthly gross return. Prior to 30th Sept 2022 the gross returns were calculated using daily authorised global close valuations with cash flows at start of the day, and were shown before management and custodian fees but after the deduction of trading expenses. Returns were gross of withholding tax. Policies for valuing investments, calculating performance, and preparing GIPS Reports, as well as the list of composite descriptions, list of pooled fund descriptions for limited distribution pooled funds, and the list of broad distribution pooled funds are available upon request.

5. The dispersion of annual returns is measured by the equal weighted standard deviation of portfolio returns represented within the composite for the full year. Dispersion is only shown in instances where there are six or more portfolios throughout the entire reporting period. The Standard Deviation will not be presented unless there is 36 months of monthly return data available.

6. The three year annualised ex-post standard deviation measures the variability of the gross-of-fees composite and benchmark returns over the preceding 36 month period.

7. The following fee schedule represents the current representative fee schedule for institutional clients seeking investment management services in the designated strategy: 0.65% on the first £50m; 0.6% on the next £100m; 0.55% on the next £350m; 0.5% thereafter. Gross of fee performance information does not reflect the deduction of management fees. The following statement demonstrates, with a hypothetical example, the compound effect fees have on investment return: If a portfolio's annual rate of return is 10% for 5 years and the annual management fee is 65 basis points, the gross total 5-year return would be 61.1% and the 5-year return net of fees would be 55.9%.

8. The benchmark for this strategy is the MSCI AC World Index. The MSCI AC World Index is designed to provide a broad measure of equity-market performance throughout the world and is comprised of stocks from 23 developed countries and 24 emerging markets Index returns reflect the reinvestment of dividends and other earnings and are not covered by the report of the independent verifiers.

9. Past performance is no guarantee of future results and there is the possibility of loss of value. There can be no assurance that an investment objective will be met or that return expectations will be achieved. Care should be used when comparing these results to those published by other investment advisers, other investment vehicles and unmanaged indices due to possible differences in calculation methods.

10. The percentage of non-fee-paying assets in the composite as of the end of 2020 and 2019 were 100% and 100% respectively. By the end of 2021 it was 0%.

11. Prior to 31st March 2022 the composite was known as Threadneedle Global Sustainable Equity Composite. This was a name change only.

**Important Information**

**For use by professional clients and/or equivalent investor types in your jurisdiction (not to be used with or passed on to retail clients). For marketing purposes.**