AS AT 29.02.2024

Market Review

Market expectations for monetary policy changed significantly in February as it became clear that easing would start later than thought. Compared to the levels seen at the end of 2023, two 25bp policy rate cuts by the US Federal Reserve (Fed) have largely been taken off the table.

Market movements were hesitant during the month as forward-looking scenarios yo-yoed in response to conflicting economic indicators. In its latest outlook, the OECD said 'recent economic indicators point to continued moderate global growth' but that 'it is too soon to confirm whether the inflationary episode that began in 2021 is over'.

In the US, the implied probability of a first rate cut by the US Federal Reserve (Fed) in May 2023 fell abruptly from around 90% in January 2024 to 60% after the employment report and then to 30% after the inflation figures. It ended the month of January 2024 at around 20%. Gross Domestic Product (GDP) growth remained solid while services inflation in January 2024 was stickier than expected. Private consumption fell in real terms, as did consumer confidence.

In the eurozone, the ECB's wage indicator show pay increases still high in absolute terms but no longer accelerating. Core eurozone inflation continued to slow, although services inflation, still at 4.0%, remains too high for the central bank. Flash purchasing managers' surveys (PMI) for February in the core eurozone economies were better than expected, except in Germany, where the contraction in manufacturing accelerated sharply.

In China, the prime minister calls for 'pragmatic and forceful' action to boost confidence in the economy. The growth target will be set in March at the National People's Congress. The People's Bank of China (PBoC) does not expect the economy to slip into deflation, but anticipates that inflation will remain moderate enough to allow further easing.

Across other emerging markets, the resilient GDP growth seen at the end of 2023 has so far continued into 2024. Inflation, while still above target in many countries, continues to slow, giving central banks room to hold or ease interest rates.

Several global equities indices set new all-time highs in February, with investors plumping for a fairly positive view on global growth and side-lining concerns about stubborn (especially services) inflation. The MSCI AC World index in EUR terms gained +4.69% ending the month at a record high.

European stock markets also beat their previous records to reach symbolic thresholds (8000 points for the CAC 40, for example). The EuroSTOXX 50 gained 4.9% on the month and the MSCI EMU rose by 3.2% (in euro terms).

Fund Performance & Portfolio Activity

Fund Performance

Source: BNP Paribas Asset Management as at 29 February 2024. **Past performance is not indicative of current or future performance.** The above views represent our judgement as at the date of this report and may be subject to change without notice. Any economic and market trends/forecasts are not a guide to future performance of the fund. The funds/securities mentioned above are for illustration only and shall not constitute any investment advice. Calendar year performance: 2023: -25.77%, 2022: -35.22%, 2021: -16.85%, 2020: 188.38%, 2019: 2.55%

The energy transition theme has been under pressure since the start of the year of 2024, once again driven by macroeconomic concerns on the future interest rate trajectory. Since the end of last year, market expectations have swung massively from pricing in aggressive rate cuts in 2024, to a view that Fed cuts will remain unrealised in the short term. The Fed is navigating this extreme change in expectations and is trying to manage this by not having interest rates "front-running" Central Bank cuts. This has negatively impacted the energy transition theme year-to-date. We firmly believe that the sell-off in the theme is mainly profit-taking and not an indication of fundamentals.

The BNP Paribas Energy Transition fund detracted by –6.21% in February (Classic, Capitalisation share class, net of fees, NAV-to-NAV with dividends reinvested, in EUR) underperforming the MSCI ACWI (EUR) by -10.90%. The majority of this underperformance was driven by underpeformance of the theme versus the broad equity market (as explained above). From a sub-industrial perspective, our stock selection detracted from performance of the fund versus the MSCI ACWI while sub-industry allocation made a positive contribution. From a regional point of view, our stock selection within North America underperformed.

Largest contributors

ALBEMARLE CORP (+20.6%, +76bp) Albemarle is a global leader in the production of lithium, with afully integrated supply chain from mines through to lithium hydroxide and carbonate, and asset diversity across both regions and brine/spodumene. Lithium prices are showing signs of bottoming out after a rebound in February with supply exiting the market and EV demand recovering post Chinese New Year. Current lithium prices are significantly below reinvestment costs and we would expect delays in new projects and high-cost supplier exiting the market to drive price inflection.

NEXTRACKER LLC (+21.6%, +39bp) NEXTracker is the leading manufacturer of solar tracker systems globally. Positive performance this month due to strong earnings and outlook as the company increases guidance for the third time this year, showing robust demand in the utility solar market

BYD CO LTD (+10.8%, +18bp) BYD is a leading EV manufacturer in China with a broad product portfolio and differentiated LFP Blade Battery technologies, support by a vertically integrated model with in house battery and semi conductor production. The stock benefitted from more positive sentiment in China driven by signals that the government is putting in place measures to support the stock market and new product launches from the company.

ARCADIUM LITHIUM PLC (+9.2%, +14bp) Arcadium was formed by the merger of Alkem and Livent in 2024. Similarly to Albemarle, Arcadium benefits from a rebound in lithium price seen in February with supply exiting the market and EV demand recovering post Chinese New Year.

CONTEMPORARY AMPEREX TECHNOLOGY CO LTD (+8.1%, +12bp) CATL is a leading global battery manufacturer with industry leading scale and technological development The stock benefittedfrom more positive sentiment in China driven by signals that the government is putting in place measures to support the stock market and signs of restocking cycle in the EV supply chain post Chinese New Year.

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Largest detractors

SUNNOVA ENERGY INTERNATIONAL INC (-30.6%, -284bp) Sunnova is a leading provider of residential rooftop solar, battery storage and energy solutions in the US, helping customers to finance energy services at home through loans and leases, as well as offering maintenance and service contracts. Sunnova reported solid Q4 2023 earnings and reiterated FY24 guidance of customer additions of 185,000-195,000, up 32% at the midpoint, and noted that 90% of targeted 2024 revenue is already locked in. We believe the market reacted overly negatively on the announcement that the company plans to put in place a $100m at the market offering (ATM) in the coming weeks that was already mentioned 2 quarters ago. The company does not intend to utilise the ATM between now and its next earnings call, and previously mentioned its purpose is for opportunistic acquisitions/ customer growth, or international expansion.

FLUENCE ENERGY INC (-22.6%, -146bp) Fluence is a leading global provider of large-scale battery storage system, services and software that optimise renewable and energy storage assets. Its share price in February was negatively affected by a short seller report We have since spoken to the management team of Fluence to clarify the points that were raised in the short report and believe there were a number of inaccurate facts. For example, the short seller report mistakenly stated that the ongoing lawsuits with Siemens Energy at $2mn (which is immaterial given the size of Fluence and ordinary course of business) is the reason that Siemens AG is selling down its stake in Fluence, but in fact, Siemens Energy and Siemens AG are two different parties. In addition, although it is true that AES is becoming a smaller part of Fluence revenue mix, it is because Fluence is growing its business with other customers, and on an absolute basis, AES increased their business with Fluence by 52% in 2023.

SUNRUN INC (-17.1%, -142bp) Sunrun reported a Q4 result and FY24 guidance in line with expectations on solar installation The fundamentals of the business are improving with California bouncing back strongly. Sunrun has seen sales growth +40% quarter on quarter (qoq) outpacing growth in the rest of country and a significant increase in storage attachment rate. However we sold down our position as rate cut expectations have now been pushed out given the strong US economy which is putting downward pressure on the residential solar names that are very sensitive to rate expectations. As a result, we are reducing risks in the residential solar space, with a view to revisit the space once we are closer to the rate cutting cycle.

Key Portfolio Activity

Over the month, we introduced to our portfolio British-based SSE PLC, Danish-based ORSTED A/Sand Canadian-based CAMECO CORPORATION.

Given the unprecedented disjoint in the market between "green growth" and other growth sectors, we have continued to enhance overall diversification by reducing the maximum position size in the portfolio and increasing our number of holdings, while maintaining our pure play approach. We have also shifted the portfolio into more defensive utilities such as SSE and Orsted given the more attractive risk-reward for these stocks after the YTD sell-off of this sector.

As part of this shift in portfolio strategy we sold SUNRUN INC (as mentioned in the previous section) and NEXTRACKER LLC. We also sold GREEN PLAINS INC, a biofuels company, as part of our strategy to reduce exposure to sub themes that in our view are most sensitive to US election risk.

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Fund Outlook

Interest rates are still close to 20-year highs and we believe the headwinds since 2021 are likely to turn into significant tailwinds for the energy transition theme given its cyclical exposure to growth and interest rates. We are now building conviction that we are close to the bottom of the cycle with numerous catalysts underpinning this view. From a macro perspective, looser monetary conditions should ease pressure on earnings. From a bottom-up standpoint, energy transition companies are trading at a significant discount both relative to the history of the sector and to the broad equity market.

Despite short term volatility, we firmly believe that the YTD sell-off in the theme is mainly profit-taking and not an indication of fundamentals.

The downside risks to our outlook are that interest rates may stay higher for longer, keeping pressure on valuations and earnings in the short term and there could be further delays in US Treasury guidance on tax credits related to the Inflation Reduction Act. We will continue to monitor these risks and adapt our exposure to these cyclical risk factors.

It is also worth considering the energy transition implications of the 2024 US presidential election. A second Biden term could see additional efforts to ramp up climate action. In contrast, a Republican presidency would likely see some attempted pull-back on climate action, slowing, but not reversing, climate adaptation. Any negative impact on climate policies from a Republican win would likely affect electric vehicles, biofuels and batteries only as climate policies favour Republican states, creates jobs and factories - and votes.

There is no doubt that climate policy is not high on the Trump agenda, however, there are a number of misperceptions about US climate policy, who benefits and what Trump really can do in regard to overturning or changing the Inflation reduction Act (IRA). We believe that the market underappreciates how difficult it is to undo legislation like this. For the Republicans to be able to change or repeal the IRA, they must not only control the White House but also both chambers of Congress. Absent this, it seems unrealistic that much will change from what the IRA look like today. Whilst a Republican president could repeal some Environmental Protection Agency (EPA) regulations targeting vehicle and power plant emissions, there will be no authority to change or repeal existing tax credits.

In the case where Republicans do win the White House And both chambers, we expect some legislated changes to the IRA which is very different from a full repeal.

Controversially, we do in fact see some positive outcomes on environmental policy from unified Republican government in accelerating permitting timelines. This would unfortunately bring meaningful benefits to fossil fuels, but equally to clean energy and electric transmission projects.

Lastly, from a longer-term perspective, we believe the structural tailwinds underpinning the strategy remain as strong as ever. These include:

- Government commitments and intergovernmental treaties
- Trillion of dollars of funding needed for the energy transition to reach net zero by 2050
- Governments' motivation to develop domestic, nationally secure and inflation-decoupled supply chains
- Continued cost decline in renewable energy technologies making them increasingly competitive with

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fossil-based solutions

It is worth noting that, regardless of any secular theme one considers, including Al and Internet, investors have always early on

1) Underestimated the speed and magnitude of adoption of emerging technologies.

   The implication is that investors are typically late in getting into the theme and miss out on the most material performance from the emerging theme, think Artificial Intelligence (Al) for example that has really only emerged as "mainstream" investable theme 6 months ago.

2) Been too focused on the short term (on both earnings and macro-economic cyclicality) and not appreciated the long-term secular growth opportunity

   Both Al and Internet companies had very volatile revenue and earnings growth as theme emerged - as most emerging technologies have per definition - which saw most investors screening these companies out from their investment universe. In addition, cyclicality often shakes investors out at the bottom - only to get in when most of the returns have been made in the team (this is what happened in late 2020).

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