AS AT 31.01.2024

Market Review

For much of January, hopes of a rapid cut in key rates from the US Federal Reserve supported risk-asset markets. But right at the end, Fed Chair Powell raised investor jitters by insisting that a first rate cut in March was definitely 'off the table'. The chances of a soft landing for the US economy increased, in our view, although the outlook is less rosy in other developed economies – especially Europe – and the path for China remains uncertain.

In the US, fourth quarter Gross Domestic Product (GDP) growth was stronger than expected, at 3.3% annualised, mainly on the back of strong consumption. Average GDP growth over the whole of 2023 was 2.5%. The Fed expects the normalisation of the labour market to continue and contribute to slower economic activity.

In the eurozone, the ECB again kept its key rates on hold. European Central Bank (ECB) Governing Council members remain concerned about inflation, particularly in view of the upcoming wage negotiations season. Eurozone GDP saw no growth in the fourth quarter – economic stagnation continues. The business climate, according to the IFO survey fell in January, confirming the difficulties in particular Germany's industrial sector.

Global equities see-sawed during January in line with rising and falling expectations over whether there might be a rapid cut in key rates by the Fed. While inflation data reassured, the strong growth momentum in the US weighed on investor sentiment and on equities. After sharp swings, the MSCI AC World index (in US dollar terms) ended the month up by only 0.5%.

Following the strong rebound at the end of 2023, the energy transition theme has had a tough start to 2024. Market expectations have swung massively from pricing in aggressive rate cuts in 2024, to a view that the Fed cuts by 25 bps in March 2024 will remain unrealised. 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.

Fund Performance & Portfolio Activity

Fund Performance

The BNP Paribas Energy Transition fund detracted by −16.93% in January (Classic, Capitalisation share class, net of fees, NAV-to-NAV with dividends reinvested, in EUR) underperforming the MSCI ACWI (EUR) by -19.22%. From a sub-industrial perspective, both stock selection and sub-industry allocation held back performance

At the fund level, our major holdings have performed largely in line with the energy transition theme. As active high conviction managers, we continue to dynamically manage the portfolio in terms of overall risk and our exposure to individual themes and holdings.

Source: BNP Paribas Asset Management as at 31 January 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%

Largest contributors

German-based SIEMENS ENERGY AG (+16.3% ; +59bp): Siemens Energy has a broad portfolio of products and services that contributes to energy transition, covering the full energy value chain from gas services, grid transmission to decarbonisation technologies including hydrogen electrolysers, and wind turbines following the acquisition of its remaining stake in Siemens Gamesa in 2022. The company released preliminary result on 24 January that is better than expectation with very strong growth in order intake particularly in grid technologies and the wind business showing signs of a stabilisation.

British-based CERES POWER HOLDINGS PLC (+32.7% ; +41bp): Ceres has a differentiated asset light business model through licensing its solid oxide fuel cell technology. Shares rallied after the announcement of a new licensing partner, Delta Electronics, for both solid oxide electrolysers and fuel cells.
Ceres already has strong partners including Bosch and Doosan Fuel Cell. Adding another global leader as a licensee provide validation to its technology, the end market, and the business model.

Indian-based STERLING AND WILSON RENEWABLE ENERGY LTD (+33.6% ; +22bp): Sterling and Wilson Renewable Energy is one of the largest solar Engineering, procurement and construction (EPC) and Operation and Maintenance (O&M) solutions provider globally. In January, the Company reported its Q3FY24 results, which were ahead of expectations. Revenues increased 43% YoY, while consolidated losses reduced significantly. Importantly, management announced very strong order inflows in the quarter, further strengthening the orderbook, which now stands at $1bn and provides strong revenue growth visibility. The stock also benefited from the launch of the Suryodaya Yojana scheme by the Indian Prime Minister, which is expected to further bolster the order book.

Largest detractors

American-based SUNNOVA ENERGY INTERNATIONAL INC (-29.8% ; -313bp): Sunnova is a leading provider of residential rooftop solar, battery storage and energy solutions in the US. It provides a number of financing options for customers including leases, power purchase agreement (PPA) and loans for their solar energy system, together with services contracts and other ancillary services. Sunnova was affected by broader macro environment/volatility in interest rate expectation and continued weak sentiment in residential solar particularly in California. However, we maintain our high conviction in Sunnova as we continue to see a number of tailwinds for the residential solar industry including higher utility prices, declining solar equipment costs, and IRA tax credits driving value proposition to install residential solar, together with valuation supported by underlying NCCV (net contracted customer cashflow).

American-based SUNRUN INC (-25.0% ; -179bp): Similarly to Sunnova, Sunrun performance was affected by broader macro environment in January, while we maintain our high conviction in the name due to tailwinds in the industry a mentioned above.

Canadian-based ARRAY TECHNOLOGIES INC (-19.9%; -125bp): Array is the second largest manufacturers of solar trackers for utility scale solar projects. The negative performance on Array in January can be attributed to concerns on project delays in utility scale solar sector. However, the company pipeline continues to be strong particularly in the US stimulated by the IRA and we maintain a positive view on utility solar industry.
At regional level, our stock selection within North America penalised the relative performance.

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Key Portfolio Activity

Over the month, we introduced to our portfolio French-based ENGIE SA. We sold American-based PLUG POWER INC.

Fund Outlook

We continue to believe that the macro-economic environment will provide more long-term tailwinds than headwinds which has to be balanced with uncertainty and sentiment around a potential re-election of Trump. We believe that the Electric Vehicles (EV) and biofuels sectors are most vulnerable to Trump and that the media is overplaying the actual power Trump and Republicans would have in case of a Presidential win.

We are slightly more cautious of areas where commoditization is happening and/or equipment prices where pockets of oversupply is likely to build. This includes electric vehicles, batteries, and inverters to name a few, but it is important to know that we might see a "winner-take-all" in these areas where exposure can be quite favourable.

One last point that we suspect is going to be on most investors' mind is a year where 49% of the world's population will head to the polls as at least 64% of countries are meant to hold national elections that are likely to drive policy and be quite consequential for years to come.

The most anticipated of those in 2024 is likely US election where it seems likely that it will be a run between a Democratic candidate and current president Biden and former president Republican Trump.

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. Here we see the main risks around new EV credits (45W and 25E) as well as making it harder to access the individual clean vehicle credit (30D).

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.

Needless to say, a divided government or a unified Democratic government would bring incremental or significant, respectively, benefits to US environmental policy and the companies most exposed to this geography.

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