

Sustainable Investment

Q4 2023



Liontrust GF Sustainable Future Multi-Asset Global Fund



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The Fund returned 9.0% over the quarter, versus 5.9% from the comparator benchmark, a blend of 50% MSCI World, 35% Markit iBoxx EUR Overall and 15% ESTER*.

The future of sustainable investment has been questioned by a number of different parties recently. Yet, in contrast, we are more excited about the prospects for the sustainable themes and stocks we invest in than we have been for many years.

We believe interest rates are at peak levels and should fall towards the central banks' targets by mid to late 2024. The current higher interest rate environment will likely lead to lower economic growth, and we believe there will be cuts in interest rates earlier than the market expects.

Given this view and the fact that interest rate rises were the primary catalyst for the sell-off in the long duration growth equities in which we invest, we should expect that the valuation multiples applied to growth equities should stabilise in conjunction with the peak in interest rates/yields. This would remove a significant structural headwind from returns.

Indeed, the final quarter of 2023 delivered strong performance for investors, with positive returns across most major asset classes as a number of softer inflation prints in the US, Europe and UK eased investor worry regarding the length of time that interest rates would remain at elevated levels.

We are confident about the outlook for our sustainable investment strategies and believe they will build on their long-term positive track record as we back those businesses which are growing profitability while delivering solutions to critical environmental and social problems.

Those businesses which are providing these solutions will potentially access vast growth opportunities. In many cases, the speed and scale of this growth is likely to be underestimated in the valuation of their shares.

This is where the opportunity lies – finding great companies and helping to solve challenges we face as a society and world, whose prospects are undervalued by the market.

The Fund's fixed income allocation delivered strong performance driven by the significant moves lower in government bond yields and credit spreads in the fourth quarter. The catalyst was softer inflation releases in US and Europe, before the Federal Reserve (Fed) signalled that it was moving to a less hawkish stance, ushering in a sharp rally across financial markets. The speed and severity of these moves surpassed even the large moves seen earlier in the quarter, as markets lurched to pricing multiple rate cuts in 2024 and beyond.

In terms of stock attribution, after poorly received Q2 results in August, a more reassuring Q3 update from **Adyen** sparked a relief rally that recouped some of the lost ground. The company disclosed 22% year-on-year growth in net revenue to €414m and set a medium term growth target of low- to high-twenties revenue growth through to 2026. Adyen operates a global payments platform which services businesses globally. It provides a very important service for a small fee, thereby playing an important role in making transacting online safer and easier. The company is a core part of our *Enhancing digital security* theme.

Another notable performer was **TopBuild**, which we purchased over the quarter. Held under our *Improving the efficiency of energy use* theme, TopBuild is the largest installer and distributor of insulation products and related building materials in the US. It provides all the products and installation services for single family and multi-homes and also distributes products for other installers of home insulation. Highlights for the company over the period were a robust Q3 earnings release in October and a ratings upgrade in December.

American Tower also performed strongly following the release of an encouraging Q3 earnings release. Exposed to our *Connecting people* theme, US-based American Tower owns, operates and develops wireless communications and broadcast towers worldwide, renting its portfolio of over 220,000 communications sites to mobile network operators and space and connectivity in its newly acquired US data centres to a wide client base. American Tower announced that it expects total property revenue in 2023 of between \$10.895 billion to \$10.985 billion - up \$60 million from its previous range. In addition, the company raised its operating profit guidance for 2023 by 6.1%, quoting a range between \$7.01 billion to \$7.09 billion.

Among the detractors, while **Paylocity's** 25% year-on-year revenue growth in the quarter to 30 September satisfied investors, its forecast for 19% growth next quarter was seen as underwhelming. Paylocity is a cloud-based payroll and human capital management software provider. We hold the stock under the *Increasing financial resilience* theme. Human Capital Management (HCM) is key to the strength and resilience of small and medium sized companies, and has assumed further importance in ensuring workforce engagement in hybrid work environment.

In terms of portfolio activity, we initiated a position in **Edwards Lifesciences**, the developer and supplier of patient-focused medical innovations for heart disease and critical care monitoring under our *Enabling innovation in healthcare* theme. All of the company's products and services provide lifesaving results. As compared with open heart surgery, minimally invasive techniques (and percutaneous in the case of Edwards) are lower risk for the patient, as well as cheaper and timelier for both they and the healthcare system as a whole.

We also bought **Veralto** under our *Improving the management of water* theme. Veralto is a spin-out of Danaher's 'Environmental and Applied Solutions' segment, which focusses on providing tools and services to enable the testing and treatment of water, as well as the creation and key regulatory printing of consumer-packaged goods.

We sold our position in air conditioning and heating pump provider **Daikin**. We have previously flagged the military division of Daikin with our advisory committee, and have been satisfied it is both immaterial (at around 0.50% of sales) and a legacy business which continues to shrink. We discussed the production of white phosphorus, which is manufactured solely for artillery shells that produce smoke (i.e., not incendiary) and are used purely for training purpose. The advisory committee felt the risks in the current geo-political environment meant that there was a material chance that the production of white phosphorous may one day be used as a weapon. So whilst this did not constitute a breach of screen, they felt we needed to engage with Daikin to get them to divest its military division – something we have done on numerous occasions, without any success.

We also identified an emerging risk from the chemicals division in Daikin – the production of Polyfluorinated Substances (PFAS). These “forever chemicals” are an emerging risk to both food and water systems, and our process is tracking the issue through testing and detection companies.

We have come to the conclusion that these two risks are material to the Daikin investment case, and despite the positive environmental impact of the Daikin business, these risks weigh heavily on Daikin. We therefore decided to exit our position in the company.

We also sold e-signature software provider **DocuSign**, which was held under our *Delivering a circular materials economy* theme. While DocuSign continues to dominate the high-end of the e-signature market, the rest of the market is increasingly commoditised, and pricing well below what works for DocuSign. In our opinion, the company needs to accelerate core growth above 10% in the near-term and thus needs to carve out a new market and new products in the contract lifecycle management software (CLM) space. While this may work, we believe the chances they’ll dominate as in e-signature are lower than we require for investments in our process – we therefore exited our position in the company.

Discrete years' performance (%) to previous quarter-end:

	Dec-23
Liontrust GF Sustainable Future Multi Asset Global A5 Acc EUR	11.5%
50% MSCI World, 35% Markit iBoxx EUR Overall, 15% ESTER	12.7%

*Source: FE Analytics, as at 31.12.23, primary share class (A5), in euros, total return, net of fees and income & interest reinvested. 10 years of discrete data is not available due to the launch date of the fund.

For a comprehensive list of common financial words and terms, see our glossary at:

<https://www.liontrust.co.uk/benefits-of-investing/guide-financial-words-terms>

Key Risks

Past performance does not predict future returns. You may get back less than you originally invested. We recommend this fund is held long term (minimum period of 5 years). We recommend that you hold this fund as part of a diversified portfolio of investments.

All investments will be expected to conform to our social and environmental criteria.

Overseas investments may carry a higher currency risk. They are valued by reference to their local currency which may move up or down when compared to the currency of the Fund.

Bonds are affected by changes in interest rates and their value and the income they generate can rise or fall as a result.

The Fund may encounter liquidity constraints from time to time. The spread between the price you buy and sell shares will reflect the less liquid nature of the underlying holdings.

Outside of normal conditions, the Fund may hold higher levels of cash which may be deposited with several credit counterparties (e.g. international banks). A credit risk arises should one or more of these counterparties be unable to return the deposited cash.

Counterparty Risk: any derivative contract, including FX hedging, may be at risk if the counterparty fails.

The issue of units/shares in Liontrust Funds may be subject to an initial charge, which will have an impact on the realisable value of the investment, particularly in the short term. Investments should always be considered as long term.

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