Desjardins Sustainable Cleantech Fund

(formerly Desjardins SocieTerra Cleantech Fund

QUARTERLY COMMENTARY AS OF MARCH 31, 2024

PORTFOLIO MANAGER:
Impax Asset Management

INCEPTION DATE:
June 14, 2016

CIFSC CATEGORY*:
Global Small/Mid Cap Equity

Contributors to relative performance

Within the portfolio, Q4 earnings season was largely positive. Companies tended either to beat expectations or report stable to improving guidance, both of which were well-received by the market. Stocks with US construction exposure continue to perform strongly.

- **Pentair** (water distribution & infrastructure, US) made the largest contribution to performance. The company delivered in-line expectations with positive guidance for the year ahead. This came despite a year-on-year decline in Pentair's high-margin Pool business, demonstrating the value of its diversified portfolio, particularly the recent acquisition of Manitowoc Ice. With additional potential tailwinds from further Pool inventory normalisation, Pentair remains a high-conviction holding.

- **AZEK** (recycled, recyclable products & biomaterials, US) boosted returns. The composite decking producer reported strong Q1 results and raised guidance. In a subsequent call, management pointed to the resilience of US consumers, increasing market share gains and the development of new products. While guidance is apparently conservative and the company is pointing to potential upside, the team has taken some profits given strong share price performance.

- **Advanced Drainage Systems** (water distribution & infrastructure, US) also contributed strongly to performance. Shares reacted positively after the water management and drainage specialist reported results that beat consensus and lifted full-year earnings guidance. Margins improved thanks to a combination of better pricing, more favourable sales mix and operational efficiencies. Looking forward, ADS guidance is underpinned by better-than-expected demand in its residential, infrastructure and agricultural end markets.

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Detractors from relative performance

Weakness was primarily concentrated in IPPs due to lower power prices and those holdings still experiencing inventory destocking.

- **EDPR** (renewable energy developers & IPPs, Portugal) had the largest negative impact on performance. In addition to changing market expectations around interest rates, a warm winter, ample gas supply and soft industrial demand mean European power prices are now 90% lower than the record highs seen after Russia’s invasion of Ukraine. Despite modest exposure to spot power prices, the dramatic fall has had a significant but temporary impact on earnings. Donald Trump’s vocal stance against the Inflation Reduction Act has also weakened sentiment around US pipeline projects. Nevertheless, operational performance remains robust, and there is little to shake our conviction in long-term structural demand for clean energy.

- **LEM** (industrial energy efficiency, Switzerland) also detracted from returns. The producer of specialist electrical components reported disappointing earnings and weak guidance due to uncertain end demand. In key areas like automotive and renewable energy, LEM is still facing a period of customer destocking, with additional pressure in automation from China’s economic slowdown. The company is also working hard to recover market share lost when supply chain issues constrained production. LEM’s focus on operational improvements is encouraging, but a meaningful rally in the shares will require a clear sign that destocking is coming to an end.

- **Nibe** (buildings energy efficiency, Sweden) similarly weakened overall performance. The home heating specialist reported numbers that were in-line with lowered expectations, with margins and sales growth both sequentially contracting. Nibe’s key heat pump business is struggling with excess inventory at distributors, muted European construction and uncertain fiscal support. The company has announced a cost saving programme, but management expect limited demand visibility and strong past performance to make for a challenging H1. Given robust longer-term conviction, the team continues to hold at these levels.

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Desjardins Wealth Management Investments

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Major changes to portfolio in the period

Added:

- **CATL** (advanced road vehicles & devices, China) a producer of batteries for electric vehicles (EVs) and static storage. The company is a global market share leader thanks to a history of technological innovation and competitive pricing. Future growth is expected to be underpinned by structural uptake of EVs, as well as continued market share gains, particularly in Europe. CATL also benefits from diversified exposure across battery chemistries, a market-leading cost structure and robust balance sheet. At the time of purchase, a temporary slowdown in the pace of EV sales growth weighed on the shares, creating an attractive entry point for the team.

Sold:

- **Indraprastha Gas** (cleaner energy, India) is a provider of natural gas for the Indian market, with a focus on transportation. Regulatory changes are increasingly pushing for electrification of the latter. While medium-term demand may prove resilient, this development represents a change in the investment thesis.

- **Dialight** (efficient lighting, UK) is a maker of energy efficient lighting for a range of industrial end markets. Poor operational performance has undermined the investment thesis, with the managers reallocating a subscale position to higher conviction opportunities.

*CIFSC refers to Canadian Investment Funds Standards Committee. The CIFSC has the mandate to standardize the classification of mutual funds in Canada. http://www.cifsc.org/.