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FUND MANAGER QUARTERLY REPORT

Fund Manager First Quarter Report – March 2025.

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Over the Hump

The quarter ended with market turmoil as "liberation day" approached, with markets continuing their fall into the new quarter. Market gains were wiped out for 2025, and the last twelve months in many cases. Headlines highlighted a Wall Street rout around $5 trillion.

Ethical portfolios benefited from the under exposure to the Magnificent Seven shares (such as Alphabet, Amazon, Apple etc), in addition to no exposure to the recently hyped defence sector, which enabled a recovery in relative performance at least. We referred to the "Trump bump" as a knee jerk reaction in our last report and this proved to be the case. It began to turn in February and the DeepSeek news further crimped expectations for the overheated AI sector. Simultaneously, the consumer weakened in the US (first noted by the airline industry) leading to a rotation away from US equities.

European and UK equities benefited, especially after elections in Germany and Europe's new found love of defence (regarded as fiscal stimulus). Sacred debt rules were abruptly relaxed to allow defence expenditure, rattling bond markets whilst global defence stocks soared (but subsequently fell back in the Tariff rout). Asian and emerging market investments were mixed, Hong Kong saw a strong recovery in the tech sector but this was based on Chinese social media (and has since fallen back), whilst India and Japan have lagged. As you will have seen from re-balance commentary, we had been shifting some exposure out of India given valuations, with a bigger focus on China. Given the declines we have seen in Indian equities through Q4 and Q1, they are now reaching levels that are more attractive.

With the general outperformance of value over growth, Schroders Global Sustainable Value and Janus Henderson UK responsible Income funds were the standout performers in the quarter, returning +3.76% and +2.46% respectively.

With global equity markets largely declining for the quarter and global bonds rallying on safe haven flows, our re-balance in February where we cut equity across the board in favour for fixed income, has helped the portfolios during February and March's declines, as well as into April.

In fixed income we favoured shorter dated bonds which left us less exposed to rising long term interest rates. Tariffs have re-ignited inflation risk just as economies begin to weaken, leaving less headroom for Central Banks. We suspect interest rates will have to respond to the weaker economy and therefore a higher risk premium will be demanded by longer date bond investors.

Portfolios alternative exposure provided some ballast during the volatility, with RM Alternative Income fund returning +1.23% in the quarter. We shifted portfolios infrastructure exposure at the re-balance in February to solely RM after selling Foresight (with the latter returning -1.77% in the quarter).

Recent Events and Outlook

Markets began pricing in the in the increased uncertainty during the quarter, yet despite this, the shock of liberation day has led to some extreme market movements. As always, the reality is more nuanced than the headlines but a number of factors have contributed to the recent volatility.

There were three very crowded trades in the market that exacerbated the volatility. The first was known as American exceptionalism, where the US economy was regarded as the only investable major economy that was growing, and US listed equities were being weighted at 79% of global indices, a record high. The economic data for the US remains strong, but increased anecdotal evidence, especially the reports from the Airline sector and some staple names began to signal a slowdown. In January, airlines were reporting strong revenue growth from both higher traffic and increased fairs, but towards the end of February the story had changed to lower demand. This led to funds moving from the US to Europe, as noted above.

The other crowded trade was around both the Magnificent Seven and the wider AI sector. The news that DeepSeek had been able to achieve comparable results with far less resource hit the chip sector hard, as fewer chips would be needed. In both sectors valuations were already high and these sectors began to move lower. The fall after liberation day was exacerbated by news from Microsoft they were going to reduce their investment in AI datacentres.

The electrification theme has been one of the strongest performing outside water and waste. A lot of this has been led by datacentre build outs, so the DeepSeek news has been highly volatile and placed pressure on stocks such as Schneider Electric. These stocks have previously spent vast sums de-risking their supply chains, which started during the previous trump era and continued throughout covid. Electrification is not a theme that's going to go away. The IEA predicted that Data centres were only going to account for 10%-20% of global electricity demand growth over the next 5 years. Outside of this, transport, EVs, heavy industry offers a lot of opportunities. And particularly in the face of nationalisation, reshoring will lead to smarter localised factories which will also play a part in future earnings.

Even before "Liberation Day" markets were weaker, not just in anticipation, but also as profits were taken and safer havens were sought. The main issue with "Liberation Day" was its breadth, creating uncertainty across a number of sectors, both for the businesses involved and also for the scope of retaliation. This uncertainty remains.

After the initial response from markets, the following day margin calls (where investment account values fall below minimum required balances) led to more selling in some of the overheated sectors, impacting stocks around the world. The overheated sectors in particular, AI, Magnificent seven, defence and chip makers continued to be hit hard. At the same time some businesses announced their plans as they worked through the impact of the tariffs.

Interest rates remain in a flux, the inflation risks have risen, but so have the recession risks. There are higher expectations that short term interest rates will fall, longer term interest rates are less certain, and it is from these that business investment decisions are made.

From April 11th we begin to get real life corporate results again, starting with US banks but throughout April and early May, US, European and UK listed companies will be reporting or updating the market. Whilst the results reflect the past, their outlooks for the future will be scrutinised. In many cases markets still expect companies to raise their profits next year, but this is being called increasingly into question as the economic outlook becomes less certain and markets need to price in the increased

global friction. As this slowly gets quantified, markets can at least work from that and re-value companies. This period will be more important than usual, and in the fast-changing geo-political world, two months is a long time, but from here markets will get the framework they need to re-evaluate investments. Change is a fact of life, and markets are just having to cope with a lot in a short period of time.

Our stance is more defensive, but ethical investments did not feature heavily in the crowded trades (where they were it was around electrification), but they will benefit from government spending and increased demand for energy which is a certainty from the general electrification theme.

Batteries, Electric Vehicles (EV) and Renewable Energy have certainly not been in the crowded trade bucket, and have faced continued weakness over the last couple of years. Whilst the roll out continues, it's at a much slower pace than had previously been anticipated, which has led to overcapacity and oversupply, and price wars in order to compete. Outside of China, it's been a major struggle for companies to compete, with battery costs as much as 50% higher and that's been evident in high profile bankruptcies, most notably Northvolt.

With the collapse of Lithium prices, the International Energy Agency expect a new demand cycle for batteries to begin, which are increasingly cost competitive to combustion engines. The fortunes of this very much linked to the fortunes of the EV sector. Whilst the global tariff fiasco throws major doubts over this, we have begun to see some signs of a bottoming out.

Solar has been a victim of the rising rate environment, but also any growth has been held back by grid bottlenecks, particularly in Europe. For the equipment makers, there has been price competition and weaker demand in residential which has led to supply gluts.

The outlook for alternative energy and valuations are much more reasonable now, and if anything, very attractive not only for sustainable investors, but general investors as well. This comes on top of the private money looking at the sector. Looking at a leading alternative energy index, there's been a huge de-rating and forward earnings sit on single digit P/Es with year over year earnings growth in the 25-30% levels. A broadening of returns and lower rates are an obvious positive whilst clarity on US tax support may actually be supportive – all eyes will be on this on the 15th April.

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