March 2022

# Investment Advisory Committee: Summary minutes

## Attendees:

Seb Beloe (Head of Research)
George Latham (Managing Partner)
Ty Lee (Associate Fund Manager)
Victoria MacLean (Associate Fund Manager)
Rachael Monteiro (Business Development)

Alice Chapple (Member)
Ray Dhirani (Member)
Carole Ferguson (Member)
Jayne Sutcliffe (Chair)

## 1. Business update

*The most notable development in recent months has been the launch of the WHEB Environmental Impact Fund in December.*

George Latham (GL) update the Committee on recent developments in WHEB's business. The previous period has been a more difficult time for WHEB's investment strategy which is characterized by growth-oriented businesses. Notwithstanding the market environment (see Ty Lee's commentary below), WHEB has continued to see fund net inflows, although at a more muted pace than in previous periods. Assets under management (AuM) as of the middle March stand at approximately £1.4bn.

The most notable development in recent months has been the launch of the WHEB Environmental Impact Fund in December. With approximately $40m invested in this fund, it is still at an early stage. The fund is based on WHEB's core strategy, but focuses on the five environmental themes (Cleaner energy, Environmental services, Resource efficiency, Sustainable transport and Water management).

The WHEB team has also expanded since the Committee's last meeting in October 2021. Since then, Sandhuni Correa has joined the Operations team as a Management Accountant. WHEB is also on the point of recruiting a new Client Services Manager and a Human Resources Manager in the Business Development and Operations teams respectively. The team are also in the process of recruiting an Impact Analyst to support the Investment Team.

Sandhuni Correa, WHEB

GL also reported that WHEB are in the final stages of launching a deferred equity plan for employees that will enable them to buy into the firm's equity. This will share ownership of the company across participating employees and enable them to benefit directly from the company's growth.

*The formal capacity of the strategy has been revised up to $8bn. This is based upon the minimum market capitalization threshold for the strategy as well as conservative assessments of liquidity.*

Finally, GL also pointed out to Committee members that the formal capacity of the strategy has been revised up to $8bn. This is based upon the minimum market capitalization threshold for the strategy as well as conservative assessments of liquidity. WHEB will continue monitor the capacity and its impact on liquidity as the strategy grows.

## 2. Overall strategy performance and composition

Ty Lee provided an updated on the strategy's performance over the past four months as well as key features of the strategy's key holdings. Overall, the strategy has struggled in current markets. The key causes of this have been concerns about inflation which has resulted in strong performance from oil and gas companies and from financial sectors. These are two parts of the market where the WHEB strategy has no exposure.

In addition, there has been a strong rotation in the market away from 'growth' oriented companies and towards 'value'. The WHEB strategy is focused primarily on growth – companies that provide solutions to sustainability challenges are typically companies that are characterized by strong growth. This inherent bias within the investment strategy has also hurt the strategy's performance in recent months.

*HelloFresh announced a significant capital expenditure to capture market share in their fast-growing market. While we believe that this is positive in the long-term, it has created margin pressure in the short term which causes the stock to sell-off.*

### Thematic attribution

The themes that were largely responsible for the underperformance in the period included Wellbeing, Resource efficiency, Cleaner energy and Health.

Well-being was particularly weak due to stock specific reasons. Orpea, an operator of elderly care homes, fell dramatically following the publication of a book detailing allegations of abuse in the company's homes (see section 4 below). Another holding, HelloFresh, also performed poorly. The company announced significant capital expenditure to capture market share in their fast-growing market. While we believe that this is positive in the long-term, it has created margin pressure in the short term which causes the stock to selloff.

Resource efficiency and Cleaner energy were both weak due to a shift away from 'growth' in the market, as well as concerns about raw material cost inflation combined with supply-chain disruption. Since the Russian invasion of Ukraine, however, Cleaner energy has made significant gains as European governments have emphasised the important role renewable energy can play in replacing Russian fossil fuels.

Finally, the Health theme has also been weak. TL argued that this is perhaps surprising, given the more defensive characteristics of many health-focused businesses. Many of these companies, however, have been strong beneficiaries of action to tackle the coronavirus pandemic. As the threat posed by the virus has waned, so investors have sought to take profits and invest in other areas.

Members asked what impact recent developments in the market and in Eastern Europe had had on investor concerns and interest. GL confirmed that WHEB had received a lot of incoming questions from clients on the strategy's exposure to Russia and that WHEB has published an article setting out how the strategy has been affected.[1] However, it is WHEB's clear impression that recent developments have not had a chilling effect on client interest in sustainability which remains as strong as ever.

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#### - Cleaner energy

Committee members were also interested to understand the performance of Cleaner energy and in particular whether WHEB was expecting to see improved performance from this theme. TL confirmed that WHEB's conviction in these companies comes from their central role in dramatically reducing the carbon intensity of power production and, in turn, the central role that low carbon power plays in enabling the transition to a zero-carbon economy. In the shorter term though these companies have been hit very hard by challenges in securing logistics and freight services at reasonable cost. In addition, the failure to agree supportive policy in the US has hurt sentiment in clean energy stocks.

WHEB has also sought to identify companies in the Cleaner energy value chain with stronger competitive positions. This has been a key element in WHEB's decision to sell their holding in TPI Composites and switch into SolarEdge (see below).

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## 3. Buys and sells in the period

Seb Beloe and Ty Lee introduced the new purchases made during the period. The number of purchases has been significantly higher in the recent period due to the team taking advantage of volatility in the market to buy into high quality companies at attractive valuations.

**Fisher & Paykel (Health)** designs and sells respiratory equipment and humidifiers for people suffering from respiratory conditions. The company sells equipment to hospitals and to individuals to help treat chronic conditions such as obstructive sleep apnea.

**Globus Medical (Health)** is the market leader in making spinal implants and surgical instruments for musculoskeletal disorders. The company has also developed the ExcelciusGPS, the first robotic device supporting surgeons in spinal surgery.

**Hamamatsu Photonics (Health)** based in Japan, Hamamatsu is a leader in photonics technology supplying optical sensors, lasers and photonic components into medical instruments as well as industrial equipment and environmental testing markets.

1 – See https://www.whebgroup.com/russias-invasion-of-ukraine-implications-for-whebs-investment-strategy/

**Power Integrations (Resource efficiency)** makes integrated power supply technology including gallium nitride (GaN) technology. This is highly efficient both in reducing the number of components needed in products and in transmitting power. Applications include consumer products and charging devices where power usage can be reduced by over 80%.

**SolarEdge (Cleaner energy)** manufactures inverters and power optimisers for residential and commercial solar systems. The products convert DC power produced by solar panels into AC power and help to increase the overall performance of a solar system.

*Members agreed that all the additions were consistent with the philosophy and policies of the strategy. One Member also commented on Trane's reputation as one of the best quality companies in the HVAC industry.*

**Spirax-Sarco Engineering (Resource efficiency)** is a UK company that specialises in providing products and services that help manufacturing businesses use and recover heat very efficiently. The company also provides electric thermal and fluid control technology.

**Trane Technologies (Resource efficiency)** provides high efficiency air conditioning systems and services. The company serves both residential and commercial end markets as well as climate-controlled transport solutions.

**Trimble (Resource efficiency)** provides location-based sensors, systems and software to clients in the construction, agriculture and transport markets. Trimble's products and services help clients by enabling more precise activities (e.g. in applying fertiliser in agricultural operations).

Sales in the period included Cerner (Health), Hikma (Health), Horiba (Environmental services), Lennox (Resource efficiency), Littelfuse (Safety), Orpea (Wellbeing), Premier (Health), Strategic Education (Education), TPI Composites (Cleaner energy) and WABTEC (Sustainable transport).

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## 4. Discussion paper – Care homes and home health

*Following the accusations at Orpea, the investment team has conducted a review of other holdings in the portfolio to consider if any of the issues that were raised at Orpea also present risks to other businesses.*

Victoria Maclean introduced a discussion paper that WHEB had prepared setting out the investment team's approach to assessing operational risks in the home health sector.

The paper was developed following the allegations of patient abuse made against the European care home operator Orpea. The developments at Orpea and the action taken by the investment team will be summarized in WHEB's quarterly report.[2] Following the accusations at Orpea, the investment team has conducted a review of other holdings in the portfolio to consider if any of the issues that were raised at Orpea also present risks to other businesses. The investment team's conclusion from this review was that investments in home health businesses, while materially different, are also vulnerable to similar issues. The discussion paper set out the team's view on the nature of these risks and how these might be mitigated.

The paper focused on the investment in a US home health business called LHC Group. This company provides home health services across much of the country supporting patients recovering from healthcare procedures. Home health is strongly preferred by both patients and healthcare professionals. The company also provide a range of other services including hospice care which is also preferred as an end-of-life choice.

2 - https://www.whebgroup.com/investment-strategy/fund-options/fp-wheb-sustainability-fund/quarterly-reports/

### Company and sector risks

Notwithstanding the positive impact that home health and hospice services can provide to patients and residents, there are significant risks associated with the care of patients and the elderly. VM presented the key risks affecting the sector.

**Business models** – the reimbursement rate is set by the government and so profit margins are largely dependent on how home health businesses manage their costs including, in particular, labour.

**Payment models** – payment is typically fee-for-service based (eg per visit) which may reinforce pressure on care quality. Value-based care models, which involve payment on the basis of positive outcomes, theoretically rewards higher quality care, but this will remain uncommon until 2024/25.

**Staffing** – home health is very dependent on in-person service delivered by healthcare professionals. There is though a structural shortage of qualified nurses which has been made worse by the COVID pandemic.

**Vulnerability of patients** – the patient population that receives home health is typically over the age of 65 with two-third suffering a physical disability and a further third suffering a behavioural or neurological condition. While this group is not in the extreme vulnerability category as the elderly in care homes, hospice patients do fall into this category.

Recognising these risks at both an industry and company level, VM presented a risk mitigation framework that has been developed by the investment team. This framework seeks to identify policies and performance data that demonstrate that a company operating in the home health sector has effective processes for mitigating the risks identified above. The framework covers internal processes, regulatory requirements and performance data covering areas such as independent ratings, peer comparisons, data quality, company strategy and performance data on employee satisfaction, turnover etc.

### Discussion

Committee members broadly felt that the questions within the framework were sensible and suggested some additional areas that should be covered. Key areas were felt to be around complaints procedures and staff retention. VM argued that while there is clearly some relevance from the Orpea case, regulatory oversight in the US is more exacting and that a shift to value-based care would further reduce inherent risk in the sector. Members also encouraged the team to get beyond general platitudes offered by companies to understand the underlying performance data and culture.

Overall, Members felt that the sector does offer an important positive social impact and that support for better actors that are open to investor engagement and that help raise standards across the sector were particularly important.

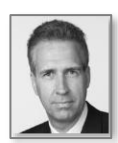
That said, Members also cautioned that there are structural barriers created by the business and payment models that increase risks of poor practice. Furthermore, there will be a limit to how much visibility is available to listed equity investors. Members were not in favour of an exclusion of the sector overall. They did argue, however, that companies operating in the sector should only qualify for investment where they are able to show strong practices and performance in managing the inherent risks effectively and that they should be open to engagement on key areas of risk.

## 7. Any other business

The next Advisory Committee meeting is scheduled for the 14th July.

## Investment Advisory Committee Members

**Jayne Sutcliffe:**
Non-executive Chair of WHEB Asset Management. Former CEO at Charlemagne Capital



**Kingsmill Bond:**
Energy Strategist – Senior Principal,
Rocky Mountain Institute

**Alice Chapple:**
Director, Impact Value, Chair of Investor Watch, and Independent Director of the Schroders BSC Social Impact Trust

**Ray Dhirani:**
Director of Climate and Sustainable Finance, Wallbrook and former Head of Sustainable Finance, WWF-UK

**Carole Ferguson:**
Managing Director, Industry Tracker