



WHEB

October 2017

Investment Advisory Committee: Summary minutes

New committee member Ingrid Holmes is a member of the UK Green Finance Initiative and of the EU's High Level Expert Group on Sustainable Finance.

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Attendees:

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Seb Beloe (Head of Research)
Ted Franks (Fund Manager)
George Latham (Managing Partner)

Kelly Clark (Adviser)
Clare Brook (Adviser)
Mike Clark (Adviser)
Rachel Crossley (Adviser)

Apologies:

Geoff Hall (Chair)

1. Advisory Committee changes

George Latham chaired the meeting in Geoff Hall's absence and welcomed Ingrid Holmes as our new committee member. Ingrid is a Director and Board Member at Third Generation Environmentalism (E3G), an independent climate change think tank operating to accelerate the global transition to a low carbon economy. She has over ten years of experience working on energy/energy efficiency policy and financing issues and is a member of the UK Green Finance Initiative and of the EU's High Level Expert Group on Sustainable Finance. Ingrid's appointment brings the Committee back up to full strength with five independent members and chaired by WHEB's non-executive Chairman, Geoff Hall.



Ingrid Holmes, Director E3G

2. Business and market update

George Latham (GL) provided a brief update on the business and reported that the FP WHEB Sustainability fund has grown substantially since the last committee meeting in June and now stands at over £185m. The fund has benefited from healthy in-flows of new money, as well as from strength in underlying markets over the past four months.

3. Fund composition and positioning

Ted Franks (ETF) provided a brief update on the current shape and positioning of the strategy. A particularly prominent aspect of the strategy has been the exposure to companies benefiting from a greater focus on resource efficiency. These businesses, which represent approximately 10-15% of the strategy, have benefited from technology upgrades that have been made to industrial manufacturing in recent years.

A key underlying theme across much of the economy has been the increasingly important role of digitisation in making manufacturing more flexible and efficient. The strategy has also benefited from the same trends in other parts of the economy including in water and electricity infrastructure where digitisation is also enabling much more efficient operations. The Water theme has also benefited from a growing appreciation of the challenges presented by water scarcity and the need to manage water resources more carefully in many parts of the world.

Two trends that have been less helpful for the strategy in recent years have been the exposure to commodities and to healthcare. Commodities exposure tends to come through waste recycling businesses which have suffered as commodity prices have been weak. In certain areas this has begun to change and, if this continues, commodity prices could become a useful tailwind for this part of the strategy.

ETF also pointed to the issues surround the pricing policies that companies have and the role these play in either reducing or increasing the positive impact of products in the market.

Daifuku is highly exposed to efforts to increase the efficiency and productivity of manufacturing and helps to reduce energy and resource use in these activities.

TPI Composites is an outsourced designer and manufacturer of turbine blades for wind turbine manufacturers.

A second theme which has also been weak over the past eighteen months has been healthcare. This has been particularly true in the US where President Trump has sought to repeal the Affordable Care Act. While he has so far been unsuccessful in this regard, his efforts have created an unstable policy environment for much of the sector. WHEB anticipates that this will continue and have sought to gain exposure to parts of the market that are both more insulated from these policy headwinds and that will benefit from underlying demographic drivers of demand which, WHEB believes, will reassert themselves in due course.

- **Reconciling negative impacts with positive impact stocks**

Committee members were interested to understand how the investment team took into account negative impacts associated with businesses, even where the principle impact of the product or service was positive. ETF and SB provided a number of examples of where these issues are addressed. At its heart, the focus is on seeing positive impact as a core driver of the company's business. Using the example of the insulation manufacturer Kingspan, ETF pointed out that the company's long-term performance has been closely linked with the growing demand for building insulation. Negative issues associated with the product, for example as a potentially flammable material in buildings, can be partially addressed by the company by making materials less flammable, but that safe use is also dependent on effective regulation.

ETF also pointed to the issues surround the pricing policies that companies have, and the role these play in either reducing or increasing the positive impact of products in the market. ETF stress that WHEB's objective is to find and invest in companies that are able to exert some pricing power, but that this power is linked to increases in positive impact. The most obvious example of this is through new innovations that improve positive impact and which deliver higher levels of positive impact. ETF presented on this topic at WHEB's Annual Conference in June and a recording of this presentation is available on the WHEB website¹.

4. Changes to the investment portfolio

ETF and SB explained recent purchases and sales from the fund over the past four months. During the period, three companies were sold including two businesses in the Health theme **Mednax** and **Ship Healthcare** and one business in the Cleaner Energy theme, **Canadian Solar**. SB explained that Canadian Solar had been a holding in the fund for four years. Over that period the company had proved itself to be one of the more adept operators in successfully driving down the cost of solar module manufacturing and diversifying its business geographically and by developing a downstream project business. Notwithstanding these efforts and the rapid growth that the business continues to enjoy, it is WHEB's view that the solar industry will remain a very difficult place to make money given the still intense pressure on manufacturing costs.

Meanwhile, two new companies were bought during the period. These two are described below.



Daifuku (Resource Efficiency) is a Japanese business that manufactures material handling systems including storage systems, conveyors and automatic sorters. The company's products are used primarily in the automation of warehousing and manufacturing facilities. The company is highly exposed to efforts to increase the efficiency and productivity of these elements in global supply chains and helps to reduce energy and resource use in these activities.

TPI Composites (Cleaner Energy) is an outsourced designer and manufacturer of turbine blades for wind turbine manufacturers. The company originally supplied materials for power boat manufacturers but switched to turbine blades over the last 18 years. Since 2001, the company has manufactured over 32,000 blades at four sites in the US, China, Mexico and Turkey.



The committee agreed that they were happy with the two additions to the portfolio over the period and were pleased to see the updated portfolio holdings document including clearer descriptions for each of the portfolio holdings².

¹ <http://www.whebgroup.com/another-chance-to-see-the-presentations-from-whebs-2017-annual-investor-conference/>

² <http://www.whebgroup.com/investment-strategy/fp-wheb-sustainability-fund/fund-holdings/>

The committee agreed on the importance of the idea of 'provable intentionality'. That is that the intention behind the business should be connected to the positive impact of the final product, and that this be provable.

5. Investing in rapid change in the auto-sector

SB presented the Committee with a description of how the WHEB investment strategy seeks to invest in companies that enable and benefit from the profound changes taking place in the automotive sector. In particular, this is expected to involve a shift from internal combustion (ICE) vehicles to battery electric vehicles (BEVs) over the coming years.

As this transition unfolds, it will present a profound challenge for the automotive industry. As the electrification trend accelerates, these businesses are expected to experience price deflation in their legacy internal combustion engine (ICE) models as well as potential market share losses and higher R&D and development costs from new models.

Many of these issues will also affect tier 1 automotive suppliers who have significant businesses in ICE components and systems. These suppliers will have to cannibalise their own ICE business as the BEV components business grows. WHEB's investment strategy has been focused on tier 2 suppliers which are less dependent on the automotive industry and sell products such as wire harnesses, fuses, cables, connectors and sensors into a range of end markets. These companies do not have large legacy businesses focused on ICE technology and are well positioned to gain content as vehicles transition to hybrid and then full BEVs.

Committee members felt that this strategy represented a sensible approach even where the companies being invested in may be multiple steps away from the positive impact associated with the final product. The committee also discussed the wider social ramifications of the very significant disruption that these trends are expected to create including through lost jobs, changes to public tax revenues and the various and sometimes conflicting impacts on citizens, investors and employees. The committee agreed on the importance of the idea of 'provable intentionality'. That is that the intention behind the business should be connected to the positive impact of the final product, and that this be provable.



• Action points and next meeting

Committee members asked to see a copy of the latest Engagement and Voting Report. Subsequent to the meeting it was agreed that the next meeting be scheduled to take place at WHEB's offices at 7 Cavendish Square, London W1G 0PE in February at a date yet to be confirmed.

Investment Advisory Committee Members



Clare Brook:
CEO, Blue Marine Foundation



Geoff Hall:
Chairman of WHEB Asset Management. Former CIO at Allianz Insurance Plc



Kelly Clark:
Director of the Finance Dialogue and advisor to Carbon Tracker and the Ashden Trust



Mike Clark:
Founder, Ario Advisory & Advisor at Oxford Smith School. Formerly Director, Responsible Investment at Russell Investments



Rachel Crossley
Founder of Broadwaters, Senior Advisor to the Access to Nutrition Foundation & Trustee of C3 Collaborating for Health



Ingrid Holmes
Director at E3G working on climate finance and investment. Adviser to UK Government and EU Commission