Sustainable Growth Mandate Update

Q2 2026

In a Nutshell

Global conflict demands a renewed focus on energy security and self-sufficiency, which alongside AI and data-led growth opportunities should sustain investor interest

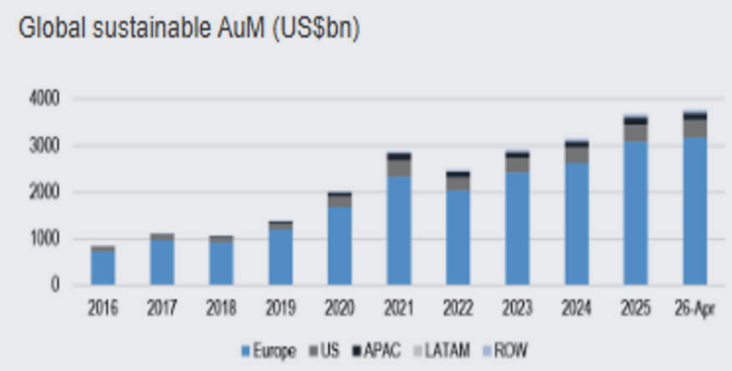
Summary

Strong Q2 performance heralded a return to form for the sustainable strategy, inadvertently aided by one of it's most vocal opponents. We continue to unearth opportunities to capture structural growth tailwinds ranging from AI beneficiaries to clean energy providers to resource security, despite ongoing political headwinds.

Market Review

Global equity markets rebounded strongly in the second quarter, as the world's most broadly defined "peace" deal offered temporary respite to energy prices, muting their impact on inflation expectations and thus the potential for interest rate rises. Market participants also seemed to tire of the war, reverting to the sexier story surrounding potential AI dominance, not least due to impressive Q1 earnings results. The S&P 500 recorded its biggest quarterly gain since 2000.

The sustainable arena largely participated in this rally. Ironically, given his disdain for the theme, one of the key drivers was President Trump's decision to bomb Iran, which according to the world's leading energy economist, Fatih Birol, may have changed the fossil fuel debate forever. Energy security and economics certainly now lead the clean energy charge. Wind and solar are produced entirely within national boundaries, avoiding the fallout from wars and trade retribution which is unfortunately becoming an increasingly accepted modus operandi. Decarbonising the global economy has thus become a geopolitical imperative, since the oft derided yet surely more important "survival of the species" one seemed to stop hitting home.



Source: JP Morgan, Morningstar

Renewed enthusiasm caused sustainable AUM to stabilise despite the clamour for higher-growth tech stocks. European funds are c.85% of the total

Performance & Activity

The Sustainable Growth mandate rose approximately 14% in Q2, making returns for the year to date of 10% and 23% for the twelve months to end June (figures for individual IMPs may vary slightly).

Significant price movers in Q2 included Gresham House Battery Storage Trust, up 21.5%. Alongside encouraging self-help, the award of a 25-year contract from Ofgem and broker upgrades, on the final day of the quarter PrimeStone Capital, holder of 7% of shares and founded by three former partners from the Carlyle Group, sent a public letter to the Board expressing their view that GRID's intrinsic value could be in excess of 140p per share (you can find the letter here: **PrimeStone**).

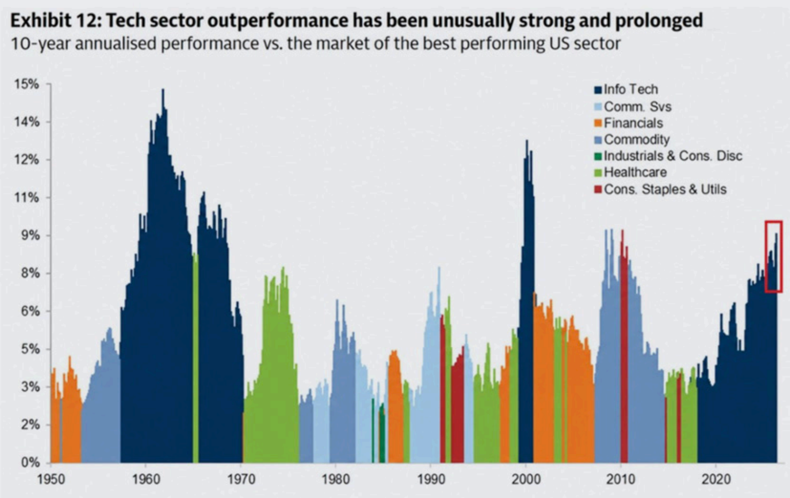
The Baillie Gifford Positive Change fund gained 20% as companies at the foundation of the AI infrastructure build-out performed strongly (Arm, TSMC, ASML). The T Rowe Price US Impact fund gained almost 19%, whilst our allocation to the Franklin S&P 500 UCITS ETF added 17.5%. Polar Biotech continued its meteoric rise, up 15% in the quarter and more than 80% over the last year.

Underperformers include KBI Global Sustainable Infrastructure Fund, up just under 2% as their largest sector, utilities, posted flat returns. The defensively focused Healthcare ETF added 7%, not surprising once a risk-on mentality returned to the market following a questionable and now defunct Iran-US détente. We added to the Healthcare ETF during the period and continue to see significant upside versus the overall market.

Fundsmith Stewardship fund returned around 8% in Q2 but we sold it post quarter end, in mid-July, due to an unexpected change to fund manager Terry Smith's investment approach (you can find further details in his semi-annual letter to shareholders, here: Documents | Fundsmith). His about-turn may or may not bear fruit but we invested in it for specific reasons and those reasons have been significantly watered down. We still find the macroeconomic Quality theme attractive and have therefore reinvested the proceeds into the iShares Edge MSCI World Quality Factor ETF.

Outlook

The current bout of AI enthusiasm has resulted in generally elevated equity valuations and very high expectations for future earnings. As Apollo Chief Economist Torsten Slok recently put it: "This AI thing better work out".

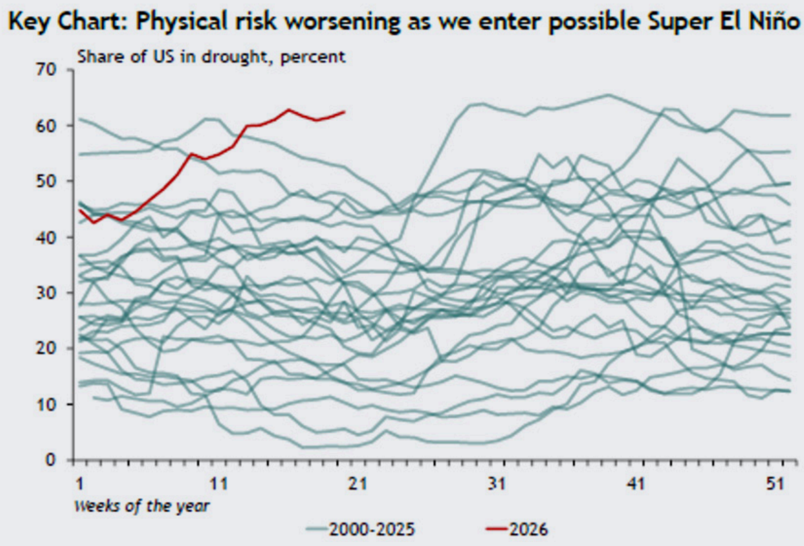


Source: Pinnacle, Goldman Sachs, Kenneth French

Prolonged Technology sector outperformance has led to elevated valuations and demanding forward-looking expectations

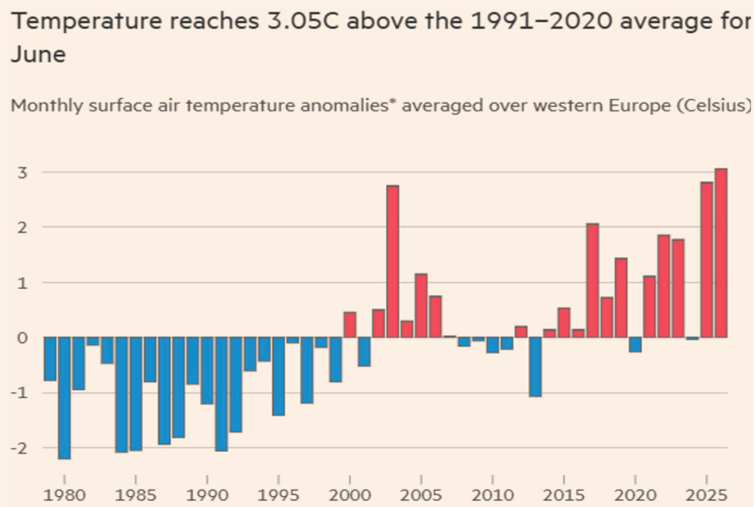
Simultaneously, valuations in many areas of the sustainable universe have compressed. This combination of reasonable valuations and a renewed urgency to ensure energy self-sufficiency combine to offer a distinctive return profile, particularly versus a wider market exhibiting an unusual degree of region (US) and sector (Technology) concentration risk. Sustainable funds tend to be underweight the technology sector and overweight areas such as industrials, healthcare and utilities, no bad thing today. Earnings growth should drive medium term returns, although valuation expansion could also emerge courtesy of renewed investor enthusiasm. Either would produce satisfactory returns on its own; both would be a real bonus.

Global policy remains generally supportive of sustainability, unsurprising given the clear evidence of worsening climate damage.



Source: ASR

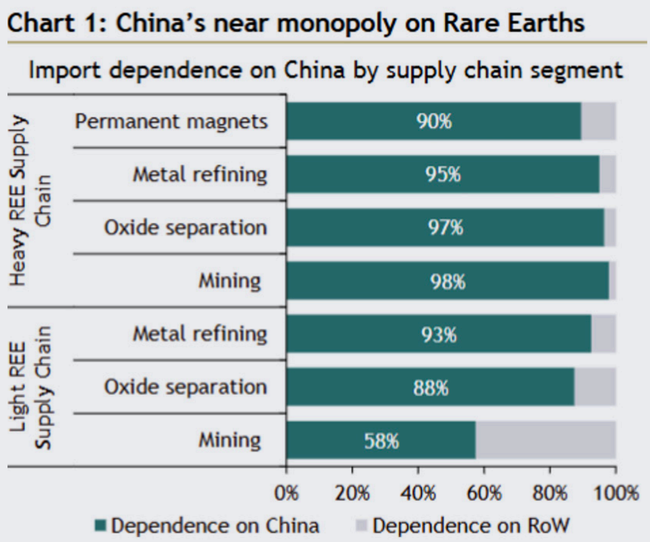
A record share of the US was in drought at the end of May, ahead of what may be a Super El Nino



Source: Financial Times

There were also higher temperatures in Europe. Lower water levels in vital arteries such as the Rhine increase shipping costs. Even French winemakers are suffering as "Europe's grapes wither in the heat" (WSJ)

The EU continues to shift to more pragmatic delivery whilst capacity additions in US renewables and storage are expected to exceed those in 2025 despite headwinds from the current administration. China's President Xi is urging faster development of a new energy system emphasising wind, solar power and hydropower to safeguard energy security. In the rest of Asia, governments and regulators continue to improve both governance and sustainability reporting, whilst the UK is also tightening its net zero pathway, targeting almost 90% emission reduction by 2038-2042 versus 1990. In addition, the King's Speech on 13th May placed energy security right at the heart of the UK Government's legislative agenda and the Energy Independence Bill marks a shift towards clean power and domestic renewables amidst ongoing global instability.

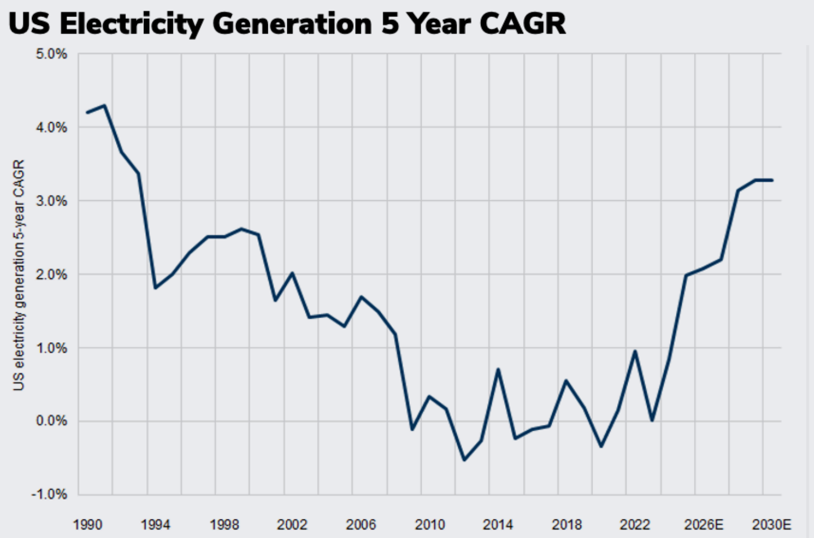


Source: ASR

It is not only the Strait of Hormuz that is a potential chokepoint – China uses Rare Earth Elements (REEs) as a geopolitical tool. All sorts of domestic security are starting to look essential

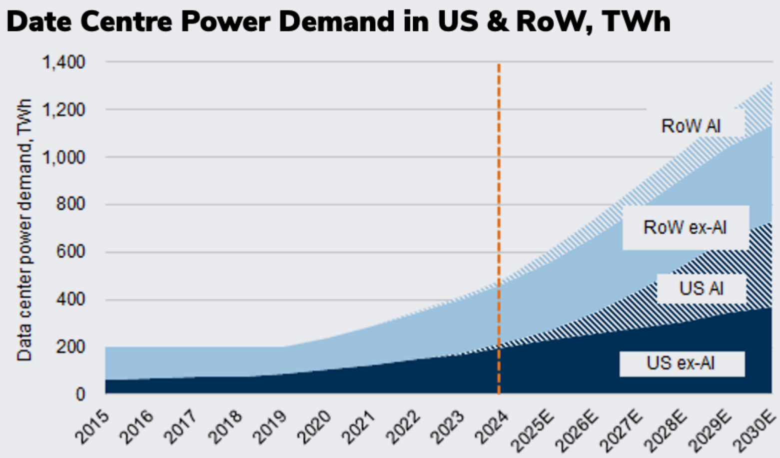
Looking forward, we expect far greater focus on sources of energy efficiency and clean technology as lower pricing and Chinese exports enable implementation cheaper than ever before. Countries, particularly emerging markets, will take time to forget the last few years, not only with the closure of the Strait of Hormuz but also with the weaponisation of the US dollar as Russia invaded the Ukraine. The upshot is a desire to reduce dependence on the US dollar and all oil and gas producers.

Thus, somewhat unintentionally President Trump looks to have escalated the global race to renewable energy. As the AI infrastructure build out continues apace, this combination creates many opportunities in areas ranging from clean energy generation to data centre efficiency.



Source: Goldman Sachs

Some estimates project accelerating US electricity consumption through the end of the decade to levels not seen in 20+ years



Source: Goldman Sachs

Demand for power is a big bottleneck for many data centre operators as they build out their AI infrastructure

Positioning

We spread our Sustainable Growth investments across a variety of passive investments, core generalist funds and more specialist thematic subsectors. We believe this is the optimal way to balance the need for diversity across a very broad industry, whilst maintaining sufficient size in key areas poised to generate significant returns for investors in the years ahead.

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