

ESG: Down But By No Means Out

After a tough start to the year for ESG investing, we are pleased to see a TAM ESG balanced portfolio outperform TAM's mainstream balanced benchmark over a three- and six-month period as we closed in on the end of the third quarter.

To provide some context, the wider market, from the outset of the third quarter, has seen the S&P 500 rally nearly 15% from the lows in Q2 then sell off back to those same levels. Much of the euphoria seen in the third quarter's 15% rally has been down to a large sell off in the price of oil which feeds directly into petrol pump prices, which in turn feeds directly into lower inflation numbers. This move lower in oil and pump prices gave investors the confidence that, with inflation consistently coming down, central banks would feel less pressure to raise interest rates to the extent that a recession is caused. This in turn caused a strong rally in global sustainable equities, which particularly benefit from an outlook of lower rates, as well as the wider market.

The selloff set in at the back end of September as inflation numbers failed to come down to match the levels priced in amid the summer's positivity. ESG and sustainable stocks were no exception here but the

high-quality companies that TAM have sought to exposure our clients' assets to fared better than the more speculative, super growth names.

The main drivers of relative protection in these two periods can be derived by three key factors:

- Firstly, TAM implemented an equity underweight early into the year, favouring cash, which is illustrative of both TAM's active approach but also that capital protection is valued just as highly as potential positive returns.

- Secondly, TAM shifted portfolios away from the high-growth focus on disruptors within the impact and sustainable space, by moving out of the Baillie Gifford Positive Change fund and into a strategy which looks for equally innovative strategies, but through a high-quality lens seeking current profitability as well as sustainable business models.

- Lastly, Q3 has seen TAM reap the rewards from our hard work in seeking to take advantage of the rapidly growing universe of innovative ESG strategies. The first we discovered was the Pictet Climate Government Bond fund. We invested while the fund was in its nascency. We initiated a position akin to both the medium-term view that government debt would hold up well in a recession, and the longer-term focus of the portfolio on allocating capital towards those countries that are doing the best work on adapting to, as well as mitigating, climate change.

This growing focus on climate change in portfolios was bolstered in Q3 by the introduction of a highly innovative climate market neutral fund from Wellington. This strategy focuses on companies and their navigation of climate change and has the ability to go long or short depending on their plans, and the market's pricing/mispricing of those plans, in adapting to and mitigating the climate crisis. In a year where traditional stock and bond funds have struggled, we have made it our priority to find relative diversifiers, within the ESG space, which have the tools to navigate the further market turbulence we expect in 2022. We believe this fund has the credentials to fulfil that mandate and are excited to be a seed investor, accessing a discounted founders share class for our clients.

As we progress through Q4 and beyond, we are building client portfolios through both the lenses of financial markets and long-term opportunities within the sustainable space. But also, with a keen eye on the evolving regulatory landscape surrounding ESG and sustainable investing. The FCA have scheduled an announcement on the much-anticipated Sustainability Disclosure Requirements (SDR) at the end of October. We expect these to follow closely the European SFDR regulation and hope they will add clarity for investors around sustainability labelling as well as managing risks and opportunities. TAM have been running ESG focused portfolios for almost a decade and feel confident and prepared to continue to evolve with adaptations to global sustainability frameworks.

From a market perspective, our outlook for Q4 remains to expect heightened volatility, just as we have been prepared for all year. Why? The global economy appears to be slowing down, but inflation does not, and markets seem to be waking up to the idea that central banks are going to raise rates into a recession if that is what it takes to control inflation. If volatility does remain in Q4 it will oscillate around economic indicators such as unemployment numbers, wage inflation, everyday goods inflation, consumer

sentiment, house prices and interest rates.

Market volatility does, however, breed opportunity and we are beginning to see these opportunities emerge to start to invest cash now, with research ongoing in house around some multi-year themes such as the energy transition, biodiversity, and social change. We remain very excited about the incredible opportunities available in this space which we can begin to gain greater exposure to as the market has repriced these companies almost solely on market factors, rather than the strength and vast opportunity of the world's most innovative companies, driving a more sustainable future.

However, any increase in risk within portfolios remains tentative and measured as we do envisage some more challenging months ahead and thus remain very much in defensive investments which are suited to protecting investors in times of stock market volatility. TAM remain best placed to provide flexible, innovative strategies to navigate market factors, gain exposure to long-term opportunities and navigate evolving regulation in the sustainable space. TAM's performance is battling back, and the gloves are off.