

# Q2 2024 REPORT



## **Pengana WHEB Sustainable Impact Fund**

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# WATER UTILITIES – A CARRIER OR A BARRIER TO SOLVING SUSTAINABILITY CHALLENGES

By Ty Lee

Last year, I wrote about how UK water utilities have gone from ‘hero to zero’ over the last few decades.<sup>1</sup> Deregulation and chronic underinvestment have exacerbated the water pollution problem in the UK, severely damaging the reputation of the industry. Several water companies have also been heavily criticised for prioritising shareholder dividends over reinvestment. Since privatisation in 1989, Britain’s water companies have paid out £78 billion in dividends, nearly half of the £190 billion invested in water infrastructure.<sup>2</sup> From 2020 to 2023, water companies underspent 27% of their forecast allowance on water and wastewater enhancement activities.<sup>3</sup> This raises the question: why don’t water utilities invest more in infrastructure improvement?

## The UK’s short-sighted regulation

UK water utilities have struggled with under-investment since the sector was privatised. One primary reason is that the UK’s regulatory model for water is not fit for purpose. It was not designed to address the sustainability challenges the world is currently facing, such as urbanisation, increasing water shortages and more frequent extreme weather conditions.

The UK water regulator, Ofwat, uses the Regulatory Capital Value (RCV) model to set price controls and determine the allowable return on investments for water companies. The RCV represents the total value of a water company’s assets used to provide services to customers. These price controls are intended to balance affordability for consumers with the need for investment.

However, this model often results in a focus on short-term cost management rather than long-term investment. The current system requires regulators to be sceptical of long-term new investment proposals, whose benefits are often difficult to prove.<sup>4</sup> Consequently, priorities are often given to cheaper, short-term solutions.

## Financial prioritisation

This well-intended but poorly designed regulation leads water companies to increase debt and prioritise excessive dividend returns to shareholders.<sup>5</sup> Compared to their US peers, many UK water companies operate with much higher debt-to-equity ratios and dividend payout ratios. This focus on dividends has diverted necessary funds away from upgrading ageing infrastructure, leading to frequent sewage spills and environmental violations.

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<sup>1</sup> <https://www.whebgroup.com/our-thoughts/uk-water-companies-from-hero-to-zero>

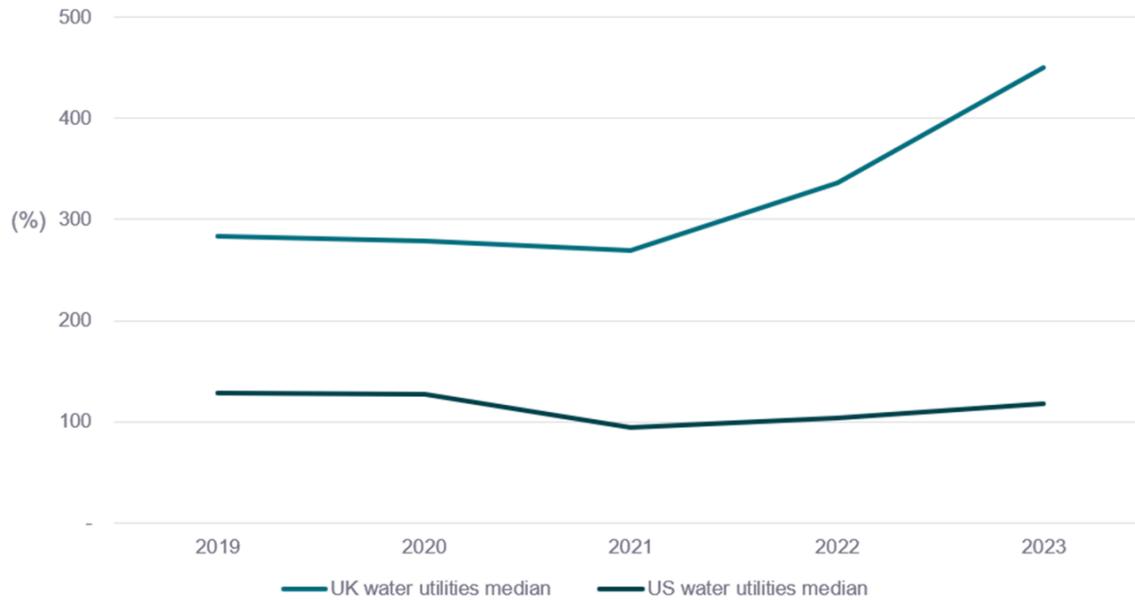
<sup>2</sup> <https://www.ft.com/content/c3cdfefb-c912-4699-bb7f-72c5c6515757>

<sup>3</sup> <https://www.ofwat.gov.uk/wp-content/uploads/2023/09/Water-Company-Performance-Report-2022-23.pdf>

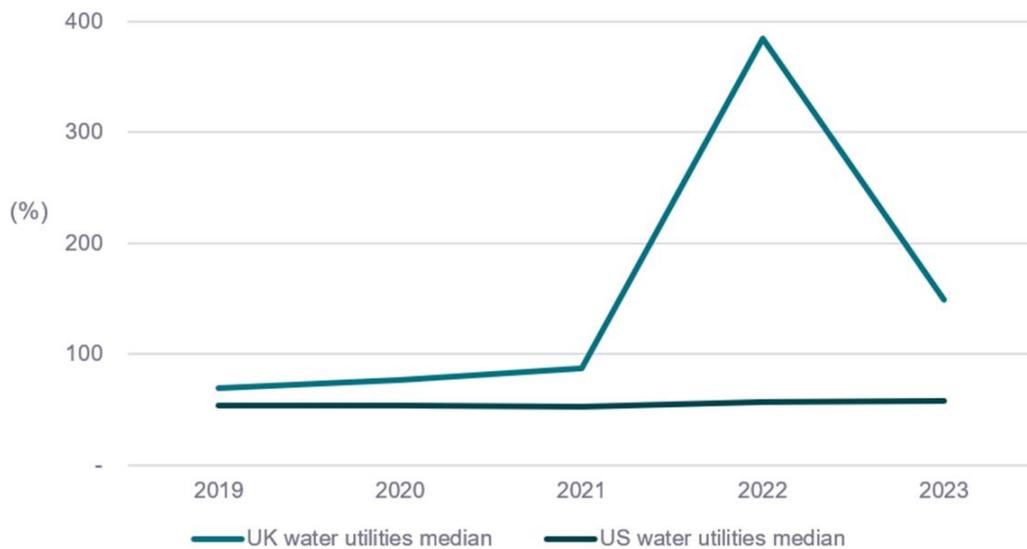
<sup>4</sup> <https://nic.org.uk/app/uploads/NIC-Strategic-Investment-Public-Confidence-October-2019.pdf>

<sup>5</sup> <https://www.ofgem.gov.uk/sites/default/files/docs/2009/10/rcv-critique-%282%29.pdf>

**Figure 1: Debt to equity ratios at water utilities in the UK vs US<sup>6</sup>**



**Figure 2: Dividend payout ratios at water utilities in UK vs US<sup>7</sup>**



<sup>6</sup> Data source: FactSet. UK companies include Pennon, United Utilities and Severn Trent. US companies include American Water Works, California Water Service and American States Water.

<sup>7</sup> *ibid*

## The US: A different paradigm

There is an increasingly widespread view that the privatisation of the UK water utility industry has not worked. However, if we look across the pond, it is the exact opposite. Investor-owned water utilities in the US perform much better than municipality-owned utilities in terms of water quality, efficiency and compliance.<sup>8</sup>

US water infrastructure faces its own challenges including ageing infrastructure, the widespread use of lead in water piping, PFAS contamination and fragmented water systems. Americans also use more water per person than almost anywhere else in the world – more than three times per capita consumption in China and 15 times more than in Denmark.<sup>9</sup>

To address these challenges, US investor-owned water utilities are offered a different set of incentives compared to their UK counterparts. These companies are regulated by state public utility commissions that often allow for higher returns on equity. They typically receive approved returns on equity in the range of 9% to 10%<sup>10</sup> whereas the UK's allowed return on equity is only 6.27%.<sup>11</sup> These attractive returns help attract private investment and ensure that utilities have the necessary capital to maintain and upgrade infrastructure while providing reliable services.

Many states also provide mechanisms like the Infrastructure Surcharge Mechanism (ISM) which allow utilities to recover the costs of infrastructure investments more quickly. This incentivises utilities to invest in upgrading their infrastructure, as they can recoup their expenditures without waiting for lengthy price reviews.

## Case in point: American Water Works

Due to the stark differences in market dynamics and regulatory environments between the UK and the US, our view on the environmental impact of water utilities in these countries diverges significantly. In the US, we observe that investor-owned water utilities generally have a positive impact by accelerating capital investment in water infrastructure which in turn improves drinking water quality.<sup>12</sup>

**American Water Works (AWK)** exemplifies the benefits of the US regulatory environment. It is the largest and most geographically diverse water and wastewater utility company in the US. The company has proactively improved its pipe renewal rate, reducing the replacement cycle from 250 years in 2009 to approximately 125 years by 2028. Its capital investment grew at a 10% compound annual growth rate (CAGR) from 2013 to 2022, compared to just 3.5% for the UK water industry during the same period.<sup>13</sup> In real terms, the capital expenditure by UK water utilities has stagnated over the last three decades.

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<sup>8</sup> <https://nawc.org/wp-content/uploads/2023/09/TFTT-factsheet-ByTheNumbers.pdf>

<sup>9</sup> <https://www.nasdaq.com/articles/state-of-the-water-industry-2021-2021-10-04>

<sup>10</sup> <https://www.spglobal.com/marketintelligence/en/news-insights/research/water-rate-case-activity-how-it-ebbs-and-flows>

<sup>11</sup> <https://www.ofwat.gov.uk/wp-content/uploads/2019/12/PR19-final-determinations-Aligning-risk-and-return-technical-appendix.pdf>

<sup>12</sup> <https://nawc.org/water-industry/water-quality/>

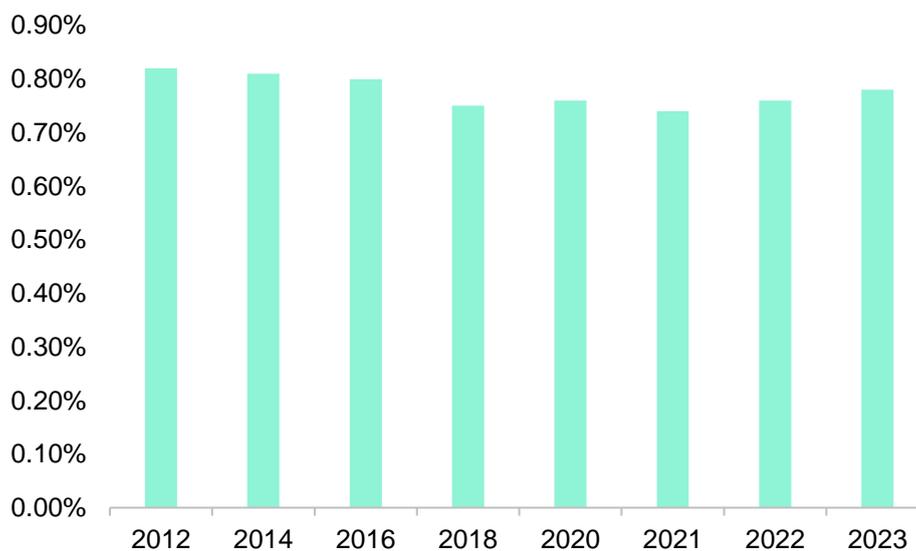
<sup>13</sup> [https://www.ofwat.gov.uk/wp-content/uploads/2022/05/long\\_term\\_data\\_series.xlsx](https://www.ofwat.gov.uk/wp-content/uploads/2022/05/long_term_data_series.xlsx)

**Figure 3: Capital expenditure in the UK water industry (£bn) <sup>14</sup>**



AWK employs a range of advanced tools to enhance water efficiency, including continuous acoustic monitoring of water mains, sensor technologies, improved pressure control, smart distribution systems, and advanced metering infrastructure. As a result of these efforts, the number of main breaks per mile has decreased by 30% from 2014 to 2022.<sup>15</sup> Through leveraging overhead costs and ongoing productivity improvement, it has managed to maintain water bill as % of median household income relatively stable over the years.

**Figure 4: Monthly water bill as % of median household income<sup>16</sup>**



AWK’s consistent investment in infrastructure, driven by favourable regulatory conditions and financial flexibility, solidifies its leadership in the sector. Its strong commitment to sustainability is evident in its superior compliance

<sup>14</sup> ibid

<sup>15</sup> [https://s26.g4cdn.com/750150140/files/doc\\_downloads/esg\\_docs/2023/2021-2022-Sustainability-Report.pdf](https://s26.g4cdn.com/750150140/files/doc_downloads/esg_docs/2023/2021-2022-Sustainability-Report.pdf)

<sup>16</sup> Data source: American Water Works

with drinking water and wastewater standards, as well as its numerous water quality accolades. These compelling attributes make AWK an attractive addition to our portfolio this quarter.

## **Investing for impact**

The comparison between UK and US water utilities highlights a significant divergence in their ability to generate positive environmental impact. While UK water companies struggle under a regulatory framework that limits long-term investment, US investor-owned utilities thrive in a supportive regulatory environment that incentivises infrastructure improvements. By investing in companies like AWK, we aim to support and benefit from the proactive and responsible management of water resources. This investment approach ensures long-term sustainability and resilience in the face of growing global water challenges.

# IMPACT REPORT 2023 – STAYING THE COURSE FOR A MORE SUSTAINABLE FUTURE

*By Seb Beloe*

WHEB's tenth impact report published in early June provides a detailed account of the impact associated with our investment strategy during 2023. Since 2014, when WHEB was one of the first asset managers to produce an impact report, the quality and extent of our reporting has improved dramatically. Initially entirely voluntary, in the last few years regulatory requirements have stepped up significantly. This year, for example, we have included an account of WHEB's performance against the ESG metrics for asset managers as set out by the International Sustainability Standards Board (ISSB).

Next year this will be a requirement of the FCA's Sustainability Disclosure Requirements (SDR). The SDR also requires a sharpening of impact reporting. In this year's report we outline WHEB's 'theory of change'; a step-by-step explanation of how WHEB's investments and our stewardship and engagement activities lead to real world positive outcomes.

## Improving ESG

With many years of reporting now under our belts, trends in performance are now visible. The clearest of these relate to the environmental, social and governance (ESG) performance of the portfolio. Some of the key trends that we see include:

- Steady improvements in the gender diversity of senior executives and board members. This has improved from just 17% in 2018 to 27% in 2023.
- A dramatic increase in the proportion of the portfolio's scope 1 and 2 greenhouse gas (GHG) emissions that are covered by a net zero carbon target. This has risen from just 2% in 2019 to 82% in 2023.
- A dramatic reduction in the financed GHG emissions of the strategy which are down by 79% since 2019.

At the same time, some things remain the same. For example, the strategy has had no exposure to products and services that create social or environmental harm over all these periods. This remains the case today.

## Trends in impact

The principal objective of the strategy is to invest in companies that have a positive impact by providing solutions to critical sustainability challenges. We then use our power as owners of these companies to advocate for changes that enhance this positive impact. We first published data on the positive impact associated with investments in our strategy in 2017. In 2022 we started to source data from an independent group<sup>17</sup>. Throughout this time we estimate that approximately 85% of the revenues earned by companies in the strategy come from products and services that have a positive social or environmental impact. With only two years of reasonably consistent data<sup>18</sup> it would be premature to draw too firm a conclusion on the direction of underlying performance. However, on a normalized

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<sup>17</sup> We use data supplied by Net Purpose (<https://www.netpurpose.com/>) which include a combination of reported data by underlying companies and modelled data.

<sup>18</sup> Before 2022 we collected and reported data ourselves and had this data independently reviewed by the Carbon Trust.

basis many of these metrics have improved over the past year. For example, from 2022 to 2023 the avoided carbon emissions that are associated with a £1 million investment in the strategy increased from 201tCO<sub>2</sub>e to 211tCO<sub>2</sub>e. Similarly, the amount of renewable energy generated also increased from 314MWhs to 322MWhs. These changes are likely to be due to improved performance from underlying companies as well as portfolio changes including sales and purchases as well as changes in position sizes. We hope to provide more detailed attribution analysis as we build up a longer time series of data, and as the quality of the underlying data improves.

Data quality, while much improved in the seven years that we have reported impact data, can still move materially year on year as underlying companies improve their own reporting. This is a point that we explored in an interview with five portfolio companies and contained in the report. It is also underlined by our reporting of wastewater treated per £1 million invested which jumped from 2.8 million litres in 2023 (based on 2022 data) to 15.4 million litres in 2024 (based on 2023 data). This was due to a trebling of the impact reported by one underlying holding and by new data from one company that was spun out from a larger conglomerate that had not previously reported this data.

## Stewardship and engagement

We complement the impact delivered by the companies in which we invest by advocating for improved performance on key issues at investee companies. We also seek to influence regulators, standard-setters and other market actors to make more positive outcomes possible in future – another subject that we address in an interview contained in the report.

Stewardship and engagement is an area of reporting that has also become increasingly standardized over the years. Much of this unfortunately has focused on engagement activities, rather than reporting on real world outcomes. There is a real danger of overclaiming here though. We do not think it is possible – nor desirable – to claim causality. It is extremely rare that a company will change their approach due to WHEB's engagement. Any claim is more likely have been driven by hubris than objective assessment, in our view. Nonetheless, we do seek to report extensively on our engagement activities and seek to draw correlations with the outcomes that we are seeking. In this way we aim to show our contribution to the positive change that we are seeking. We provide an example this approach in our work on net-zero.

## Staying the course

While WHEB has been collating impact data and publishing impact reports for ten years, several of us on the team measure our sustainable investing careers in multiple decades. This longevity provides us with an important perspective on the current travails facing the sector. Disruptions caused by COVID and war in Europe continue to create significant volatility. Meanwhile the advent of artificial intelligence has sucked huge amounts of attention and capital away from sustainability. As a consequence, the 'ESG tourists' – asset managers that stampeded into the sustainability market just a few years ago – are now packing their bags. We are confident though that these markets will return in due course. We have seen these cycles before.

Meanwhile, we plan on staying the course and remain focused on sustainability impact investing. No doubt the tourists will eventually return as markets cycle back in favour of the impactful companies that we continue to support. By then regulatory standards will be higher and early adopters will be established and striving to deliver even stronger social and environmental impacts for our investors.

# DEI EVOLUTION: LOOKING BEYOND GENDER AND FACING THE FACTS

By Rachael Monteiro

The term Diversity, Equity and Inclusion, also known as “DEI”, has become laden with political charge.

If you think that’s an overstatement, then cast your mind back to March this year. Right-wing conservatives in the US were quick to blame ‘Baltimore’s DEI Mayor’ after the city’s bridge collapsed when a 1,000 foot cargo ship collided with it<sup>19</sup>. And only two months earlier, Elon Musk sought to settle a spat with fellow billionaire Mark Cuban about the value of corporate DEI programmes via UFC-style cage fight<sup>20</sup>.

Amid these surreal controversies, it’s crucial to remember the purpose of DEI programs. They are meant to strengthen organizations by:

- Embracing diverse identities (for example: gender, ethnicity, age, physical ability, religion, class, neurodiversity, and cognitive diversity).
- Ensuring equity, which involves fair treatment considering individual circumstances.
- Promoting inclusion, creating a culture where all employees feel heard.

In WHEB’s view, improving DEI is the right thing to do from a moral and social standpoint. This view should suffice when seeking DEI-related improvements in investee companies.

Conversely, the broader investment community has preferred to advocate for improvements in DEI based primarily on a business case. Alex Edmans, Professor of Finance, points out<sup>21</sup> that the business case has too often been based on influential yet flawed studies<sup>22, 23, 24</sup>. Specifically, these studies have lacked replicable evidence and face significant methodological issues regarding the link between diversity and improved financial performance.

However, Edmans does highlight evidence suggesting a possible link between DEI-related practices and financial benefits. The 100 Best Companies to Work For in America are found to have higher shareholder returns than their peers. Crucially, though, the correlation is between higher employee satisfaction - which the Best Companies ranking evaluates - and shareholder returns. However, employee satisfaction and good diversity and inclusion share some characteristics.<sup>25, 26</sup>

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<sup>19</sup> <https://www.forbes.com/sites/janicegassam/2024/03/27/baltimore-bridge-collapse-creates-more-dei-attacks-how-allies-can-push-back/>

<sup>20</sup> <https://www.forbes.com/sites/dereksaul/2024/01/09/elon-musk-calls-mark-cuban-racist-over-dei-support-as-feud-continues/?sh=756cfa8d73a3>

<sup>21</sup> <https://medium.com/@alex.edmans/is-there-really-a-business-case-for-diversity-c58ef67ebffa>

<sup>22</sup> McKinsey produced a series of ‘Diversity Matters/Delivers/Wins’ studies correlating ethnic/racial diversity with financial performance <https://www.insurance.ca.gov/diversity/41-ISDGBD/GBDEExternal/upload/McKinseyDivmatters-201501.pdf>

<sup>23</sup> The McKinsey studies have been found to contain basic errors [https://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=3849562](https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3849562)

<sup>24</sup> This study was commissioned by the FRC and claims to show a positive correlation between higher levels of gender diversity and better future financial performance.

<https://downloads.ctfassets.net/hxo16fanegqh/2bnvaruy1KDKblph2XdFIW/2a951715edd7c5d67c9f04dd5ef09ae5/frc-board-diversity-and-effectiveness-in-ftse-350-companies.pdf>

<sup>25</sup> <https://medium.com/@alex.edmans/is-there-really-a-business-case-for-diversity-c58ef67ebffa>

<sup>26</sup> <https://dx.doi.org/10.2139/ssrn.3933687>

## DEI: A great concept but execution leaves room for improvement.

Contrary to the narratives promoted by conservative think tanks in the US<sup>27</sup>, DEI initiatives are not a zero-sum game benefiting some people at the cost of others. Instead, the aim is to create a culture and environment in which all employees feel accepted and free to be themselves, which boosts happiness and, in turn, productivity. This leads to benefits for the business such as improved innovation, creativity and problem-solving. In fact, a need to belong is so hardwired into our DNA that it's been linked with an increase in job performance by over 50%.<sup>28</sup>

But, a hard truth is that poor execution of DEI initiatives undermines its potential. For example, 'quick-fix' interventions, like DEI training, can create a false perception of company commitment, or can alienate others leaving them feeling defensive and insecure.<sup>29</sup> All of this fuels the backlash against DEI and underscores the need for long-term strategy to improve and measure outcomes. Addressing this problem is part of WHEB's investor stewardship duties, which aim to creating long-term client value and benefits for society, the economy and the environment.

## WHEB's approach to DEI to date

WHEB's approach on DEI has predominantly focused on gender diversity. Admittedly, this is a narrower focus than we would like as it is a many-faceted issue. But the reality is that it is one aspect of DEI where data is available and comparable across the portfolio. WHEB's voting policy therefore mandates at least 33% female board-level representation<sup>30</sup>. This leads to 4-12% of votes against management annually, and 6-8% of engagement activity related to gender diversity.

Data from Impact Cubed shows that gender diversity<sup>31</sup> improved in the WHEB strategy from 2018 – 2023, from 19% to 27%<sup>32</sup>. While this progress is clearly not just due to WHEB's stewardship work, it does show a link between our efforts and positive outcomes at our investee companies.

## Looking ahead: refining the framework for DEI

Despite these improvements, gender equality remains elusive and is only one aspect of DEI. With the development of the Impact Research Team in 2022, WHEB is now committed to pushing for broader DEI changes across the portfolio.

As a starting point, we are refining how we approach gender. To do this, we have identified the ten companies with the lowest gender diversity at Board and senior management level<sup>33</sup>. We have also assessed management's priority in addressing the topic, indicated by related targets, commitments or goals, talent pipeline plans, disclosure of diversity data, previous engagement responses and supply-chain diversity efforts (Figure 1). This has helped us to identify the most significant laggards as targets for engagement, as well as potential areas for improvement. WHEB aims to expand this framework to track data changes over time and correlate outcomes with engagement activities.

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<sup>27</sup> <https://www.nytimes.com/interactive/2024/01/20/us/dei-woke-claremont-institute.html>

<sup>28</sup> <https://hbr.org/2019/12/the-value-of-belonging-at-work>

<sup>29</sup> <https://www.forbes.com/sites/teresahopke/2024/01/31/what-companies-are-getting-wrong-about-dei/>

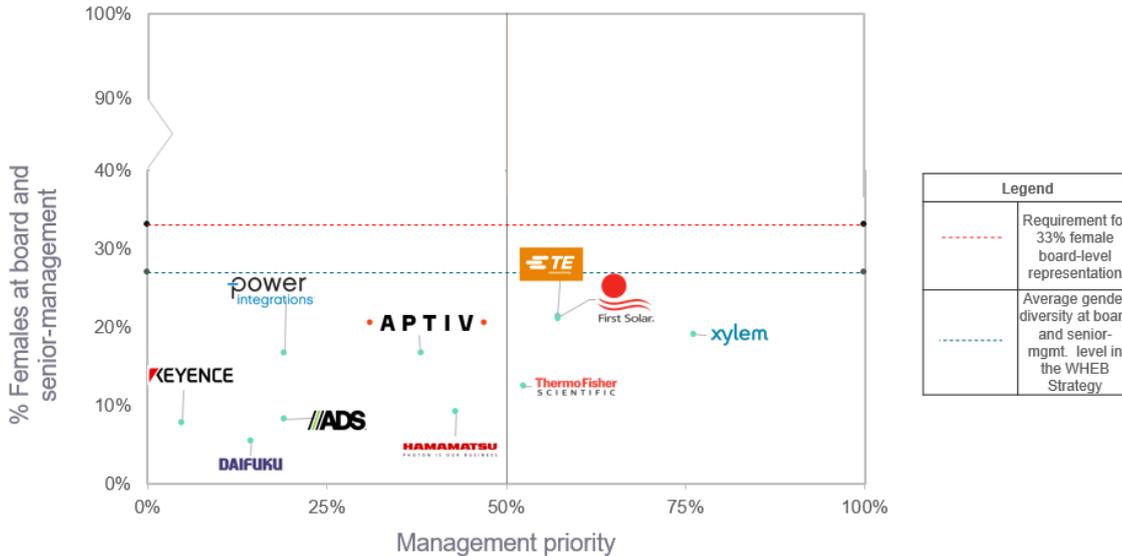
<sup>30</sup> Combined reporting and targets that, for example, report gender and minority ethnic representation in a single number are not acceptable.

<sup>31</sup> This covers gender diversity of both board and senior management positions

<sup>32</sup> We are pleased to be closing the gap between the WHEB Strategy and its benchmark, the MSCI World, which we attribute to a slight overweight in traditionally male-dominated industries and which has seen a slightly smaller improvement of around 6%, from 22% to 28% in the same timeframe.

<sup>33</sup> according to Impact Cubed,

**Figure 1: Mapping gender diversity priorities within the FP WHEB Sustainability Fund**



Reliable data on other diversity characteristics remains scarce. The US Supreme Court ruling effectively banning affirmative action<sup>34</sup> is unlikely to help. In fact, lawyers are advising US companies to reconsider diversity metrics and avoid events targeting specific groups to prevent accusations of “reverse discrimination”.<sup>35</sup>

However, we are committed to applying a similar framework to evaluate companies’ broader DEI approach. As shown by our recent work with Infineon<sup>36</sup>, we are initiating dialogue on DEI alongside developing a framework.

We will likely centre our evaluation on employee satisfaction as an indicator of an inclusive corporate culture; evidence of diversity and employee development programmes; workplace policies to prevent discrimination; and ensuring freedom of association and supplier and community engagement. It is also crucial that companies employ a comprehensive approach that combines immediate actions with sustained efforts to genuinely advance DEI.

## Conclusion

DEI is a critical yet contentious issue. Despite political backlash and execution challenges, well implemented efforts to improve DEI have the potential to foster diverse identities, ensure equity, and promote inclusion, strengthening organizations and society more broadly.

While WHEB has seen positive outcomes in gender diversity within our portfolio, we are also committed to advancing broader DEI goals. To do this, we will continue to leverage our expert knowledge of investee companies, to evaluate their performance and determine priorities.

<sup>34</sup> <https://www.bbc.co.uk/news/world-us-canada-65886212>

<sup>35</sup> <https://www.pionline.com/esg/wall-streets-dei-retreat-has-officially-begun>

<sup>36</sup> <https://www.whegroup.com/infineon-technologies-2024-q1-case-study>

# PERFORMANCE COMMENTARY

## Market review

The MSCI World Index posted a positive return for the quarter, rising 0.3%, buoyed by US equities and AI-related tech stocks.

The performance of global equity markets, and the USA in particular, has been extremely “narrow”, which means that a small number of stocks have done very well, and the large majority have not. In the most popular American benchmark, the S&P 500 with just three stocks (Nvidia, Apple and Microsoft) driving 90% of the growth between them in the second quarter. The equal-weighted version of the S&P 500 actually reported negative performance over the quarter.

Given that global markets are dominated by US markets, and indeed these very large names, this market narrowness phenomenon is affecting global markets. Similarly, a strong earnings season for US tech companies meant growth stocks were the best performing asset class not just there, but also globally. However, growth’s performance was concentrated in the US. Value stocks outperformed growth over the quarter in Europe, the UK and Japan.

Asia ex-Japan was the best performing region over the quarter, supported by strong performance from the AI-exposed Taiwanese stock market.

Technology was by far the strongest sector in the global market, followed by Communication Services while Materials and interest rate-sensitive Real Estate were the laggards.

Despite the positive overall market performance, it was a more challenging time for sustainability themes with comparatively few of the companies that we consider to deliver positive impact, keeping up with the broader market.

## Performance review

The fund delivered negative performance over the quarter, lagging the benchmark.

The very strong performance of the “mega cap” technology stocks that are not qualified for impact investment, was a meaningful headwind. Not owning Nvidia, Apple and Microsoft accounted for much of the gap in performance between the fund and the Index.

Of the stocks that we own, the largest detractor at a thematic level was Resource Efficiency with holdings including **Daifuku** hurting performance. The global material handling systems manufacturer published a new mid-term plan forecasting strong revenue growth. However, expectations of flat margins as well as short-term headwinds in some segments and regions weighed on the stock.

Performance of the Cleaner Energy theme was mixed with **Vestas**, the wind turbine manufacturer, underperforming. The shares were weak as gains by political parties hostile to green energy spooked investors. There was also speculation that the new orders it received in the second quarter would miss expectations.

**First Solar**, on the other hand, was the largest positive contributor at a stock level overall. The company produces solar photovoltaic panels and benefited from several supportive US policy decisions recently to increase the protection of the US solar market from cheap state-subsidised Chinese solar panels.

**Fisher & Paykel**, a medical devices company in the Healthcare theme, also performed well. It increased its guidance for this financial year, citing solid underlying demand trends in both its segments – Hospitals and Home Care.

## **Outlook**

Following the fall in inflation, sentiment in global equities is more positive with markets expecting that central bank tightening is nearing its end. This environment should be more supportive for the generally smaller and more growth-orientated impact stocks we invest in.

Meanwhile, several of our key sustainability markets have cyclical challenges to overcome, as well as repositioning around China's changing role in global manufacturing. We remain convinced that the companies we invest in retain the competitive edge to deliver the transition to a more sustainable economy.

# PORTFOLIO ACTIVITY

We initiated three new positions in the fund. We also exited two existing positions during the quarter.

## Purchases

We initiated a position in **Rockwell Automation** in our Resource Efficiency theme. Rockwell Automation is a world-leading industrial automation company. Its portfolio of technology and services, including flagship brands Allen-Bradley and FactoryTalk, help industrial companies to operate more efficiently and productively. Rockwell Automation have a wide range of customers from a variety of end markets, including electric vehicles, healthcare and manufacturing. Its products comprise of both differentiated hardware and software helping customers optimise performance and simplify operations. In one example from the life sciences value chain, Rockwell created a digital twin to assist with simulation during the pre-clinical drug trial stage. Following this, Rockwell's AI technology transferred digital recipes into useable data for the commercial manufacturing of the drug. During the full-scale manufacturing stage, Rockwell's automation, data and information solutions enabled the company to scale the manufacturing and provided flexibility, quality and operational efficiency.

We also initiated a position in **Gerresheimer** in our Health theme. Gerresheimer is a leading supplier of glass and plastic packaging products as well as medical devices for the pharmaceutical industry. Its broad range of products and solutions includes pharmaceutical packaging and products for the safe, simple administration of medicines including, for example, insulin pens, prefillable syringes, and injection vials. Gerresheimer has a leading position in several key product categories and is set to benefit from the growth of injectables and biologics, including the strong demand for the obesity drugs, GLP-1s.

We also initiated a position in **American Water Works** in our Water Management theme. American Water Works is the largest regulated water and wastewater utility company in the US. It provides water, wastewater and other services to over 14 million people across 24 states. The water industry is fragmented in the US and American Water Works should benefit from consolidation opportunities and economies of scale, as well as delivering stable returns by increasing capital investments for upgrading the ageing water infrastructure. Its strong focus on water quality, and managing scarcity, will also be a competitive advantage as the changing climate increases pressure on water resources.

## Sales

We sold our position in **Cooper Companies** from our Wellbeing theme. Cooper is a global medical device company with two segments: CooperSurgical focuses on women's health and fertility; and CooperVision manufactures and markets contact lenses and other products helping to treat those with vision challenges. Cooper has been held in the strategy for over 13 years and has delivered strong outperformance relative to the MSCI World over that time. However, whilst both segments have delivered strong revenue growth, in recent years the scope for margin improvement has diminished. The company also focuses its growth strategy on CooperVision's contact lenses which, in our opinion, is less impactful than other products and services provided by the company.

We also sold our position in **SolarEdge** in our Cleaner Energy theme. SolarEdge manufactures inverters and power optimisers for residential and commercial solar systems. It also manufactures energy storage solutions and EV chargers for the home and is also growing its position in electrical powertrain units and batteries for EVs themselves.

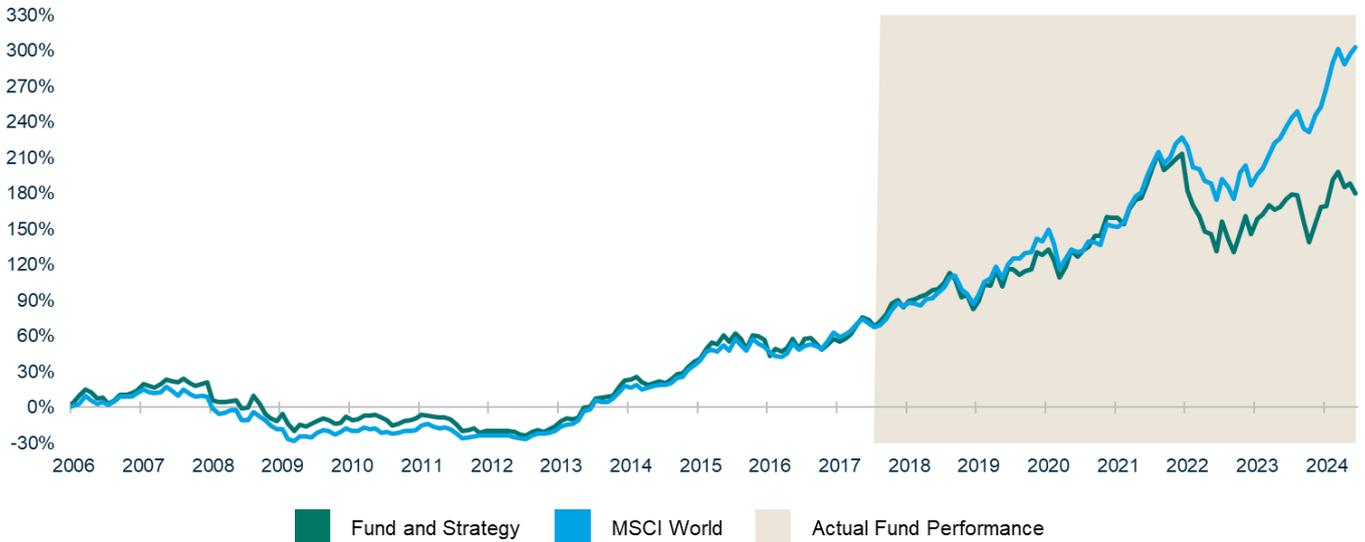
# INVESTMENT PERFORMANCE

## Cumulative Investment Returns

Net performance for periods ending 30 June 2024 (%)

	3 mth	1 yr	3 yrs p.a.	5 yrs p.a.	Since inception p.a.
Fund	-6.0	1.6	-0.9	5.3	
Strategy (partial simulation) <sup>37</sup>					5.7
MSCI World <sup>38</sup>	0.3	19.8	11.1	12.9	7.8

## Performance Since Strategy Inception

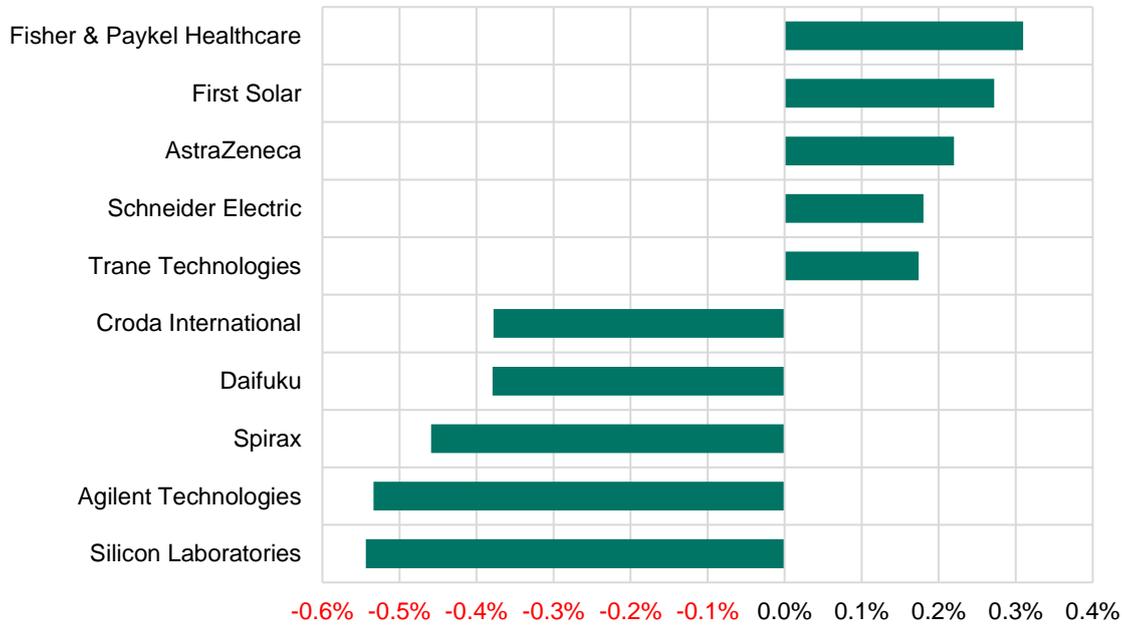


<sup>37</sup> From August 2017, performance figures are those of the Pengana WHEB Sustainable Impact Fund's class A units (net of fees and including reinvestment of distributions). The strategy's AUD performance between January 2006 and July 2017 has been simulated by Pengana from the monthly net GBP returns of the Henderson Industries of the Future Fund (from 1 January 2006 to 31 December 2011) and the FP WHEB Sustainability Fund (from 30 April 2012 to 31 July 2017). This was done by: 1) converting the GBP denominated net returns to AUD using FactSet's month-end FX rates (London 4PM); 2) adding back the relevant fund's monthly ongoing charge figure; then 3) deducting the Pengana WHEB Sustainable Impact Fund's management fee of 1.35% p.a. The WHEB Listed Equity strategy did not operate between 1 January 2012 and 29 April 2012 – during this period returns are zeroed. The Henderson Industries of the Future Fund's and the FP WHEB Sustainability Fund's GBP net track record data is historical. Past performance is not a reliable indicator of future performance. The value of the investment can go up or down.

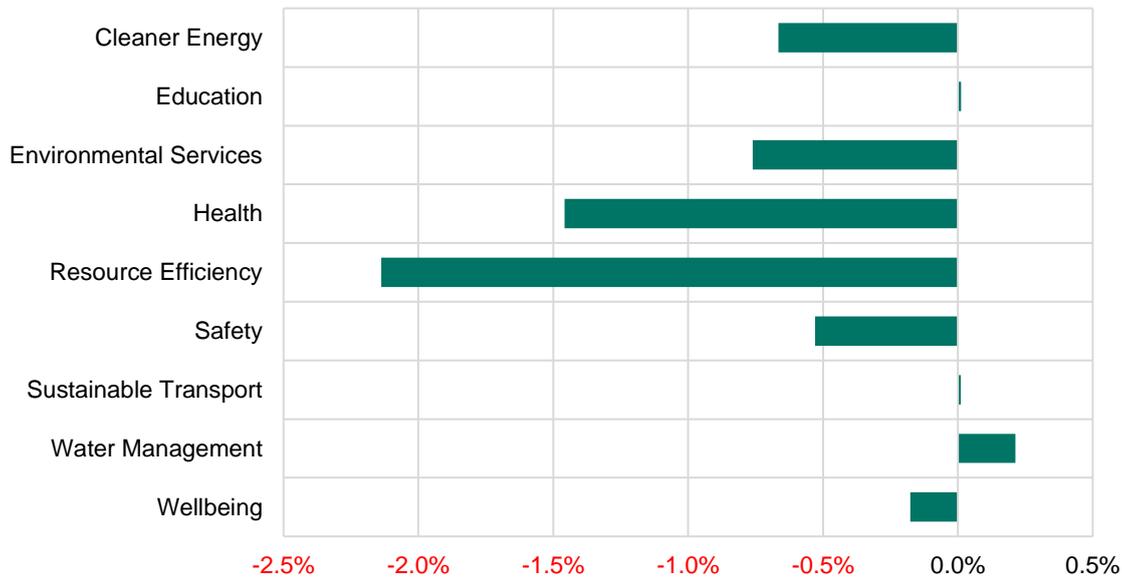
<sup>38</sup> MSCI World Total Return Index (net, AUD unhedged).

## Quarterly Performance

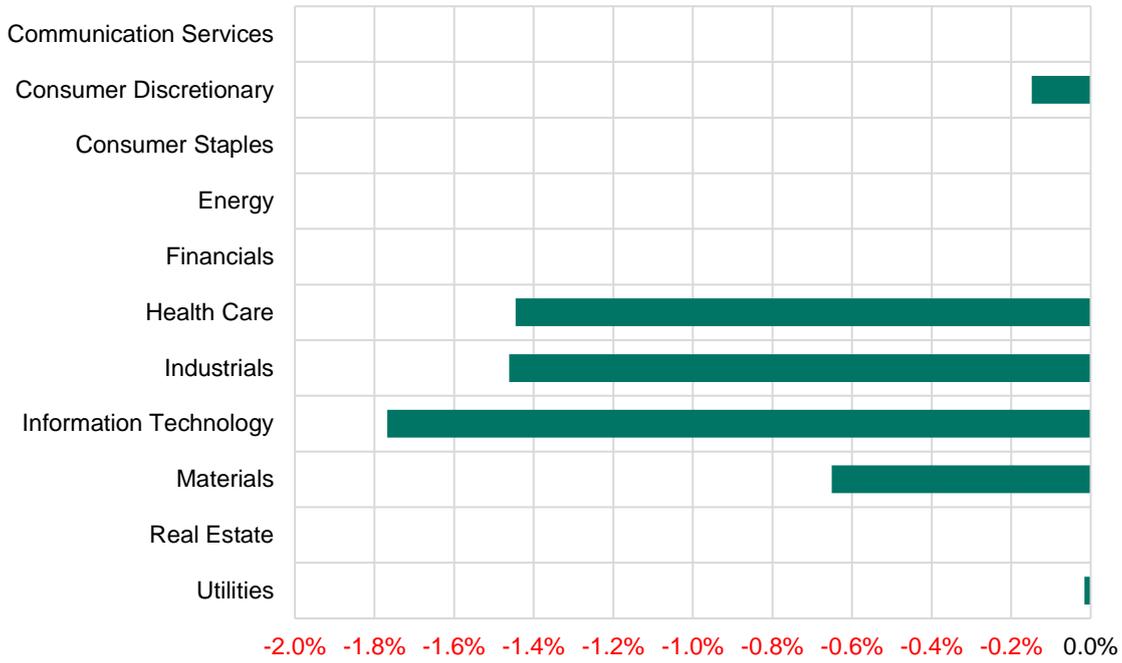
### Contribution to Return by Stock (Top 5 & Bottom 5)



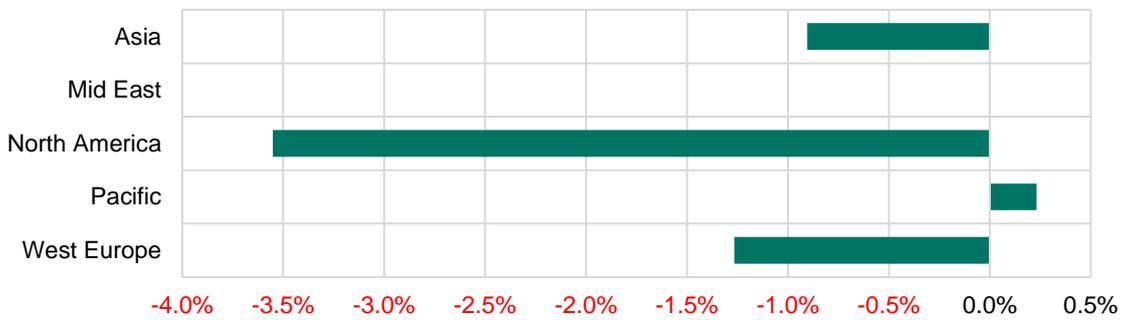
### Contribution to Return by Sustainability Theme



### Contribution to Return by Sector

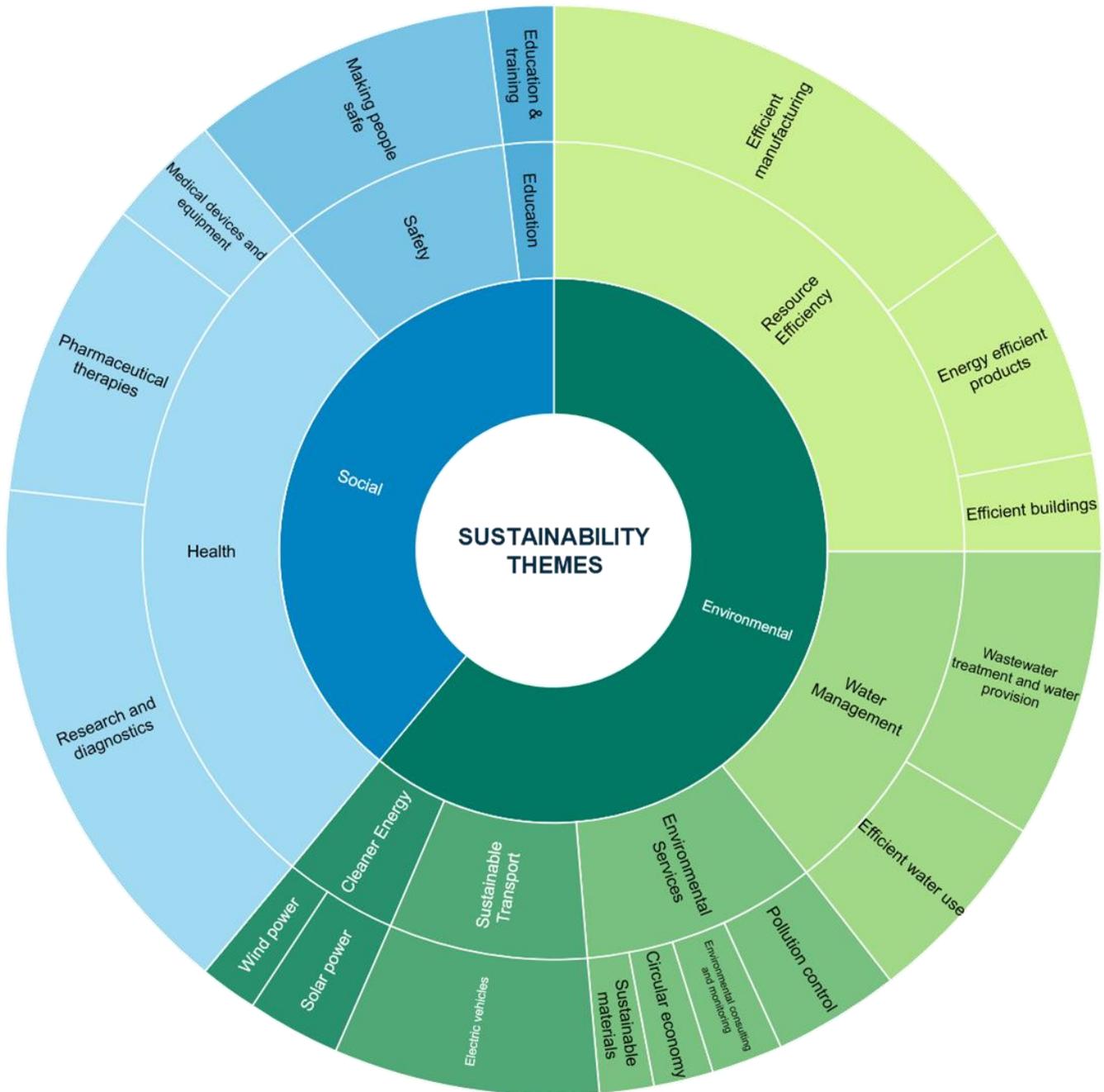


### Contribution to Return by Geography

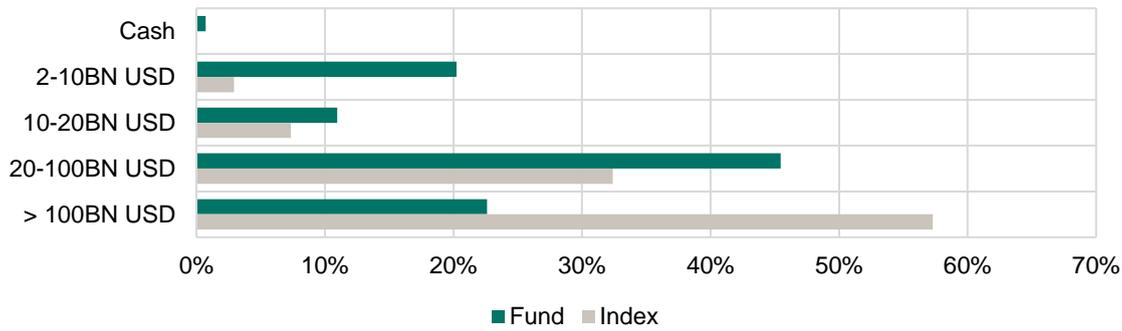


# PORTFOLIO ANALYSIS AND POSITIONING OF STRATEGY

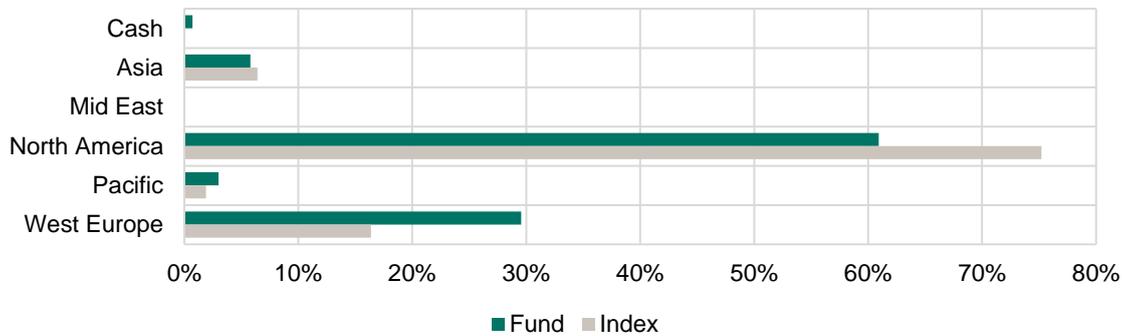
## Exposure by Sustainability Theme



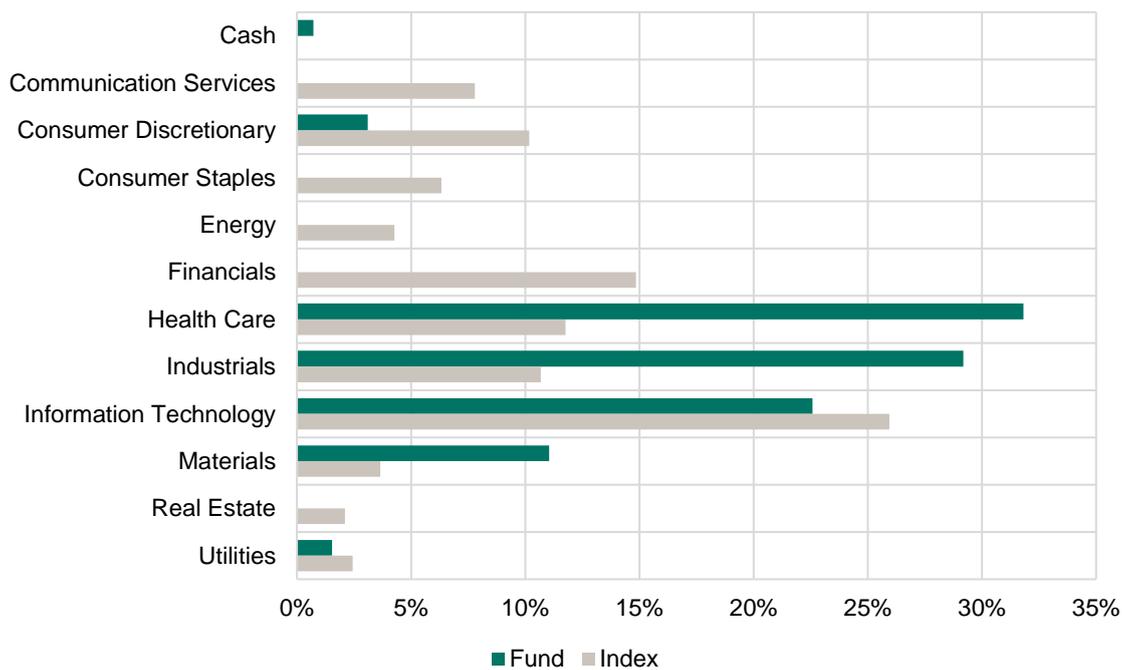
### Exposure by Market Capitalisation



### Exposure by Region



### Exposure by Sector



## Largest 10 Positions

Name	Sustainable Investment Theme	Description
ICON PLC	Health	Research and diagnostics
Xylem Inc/NY	Water Management	Wastewater treatment and water provision
Ecolab Inc	Water Management	Efficient water use
Schneider Electric SE	Resource Efficiency	Energy efficient products
Agilent Technologies Inc	Health	Research and diagnostics
Thermo Fisher Scientific Inc	Health	Research and diagnostics
Linde PLC	Environmental Services	Pollution control
MSA Safety Inc	Safety	Making people safe
Autodesk Inc	Resource Efficiency	Efficient manufacturing
Keyence Corp	Resource Efficiency	Efficient manufacturing

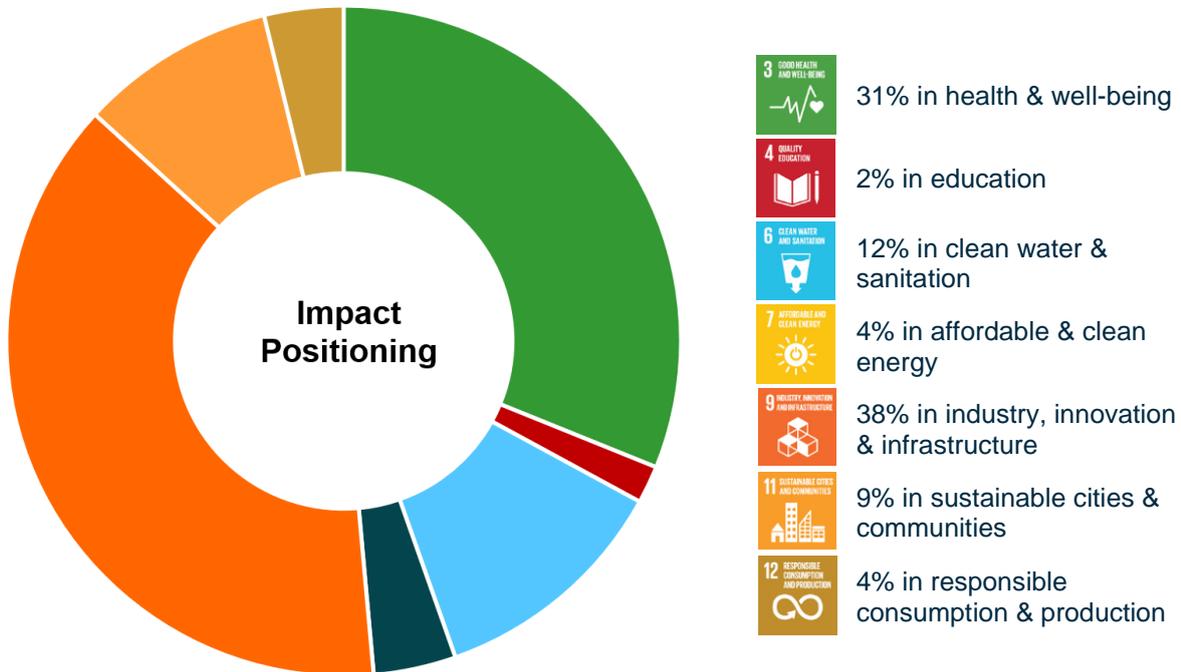
## Strategy Characteristics

	WHEB	MSCI
FY1 Price/Earnings (PE)	29.78	22.85
FY2 Earnings Growth	24.4	22.03
FY1 PE/FY2 Earnings Growth (PEG)	1.22	1.04
3-year Volatility	17.53	17.23
Beta (predicted)		1.02
1-year Tracking Error (predicted)		5.76
5-year Tracking Error (ex-post)		8.70

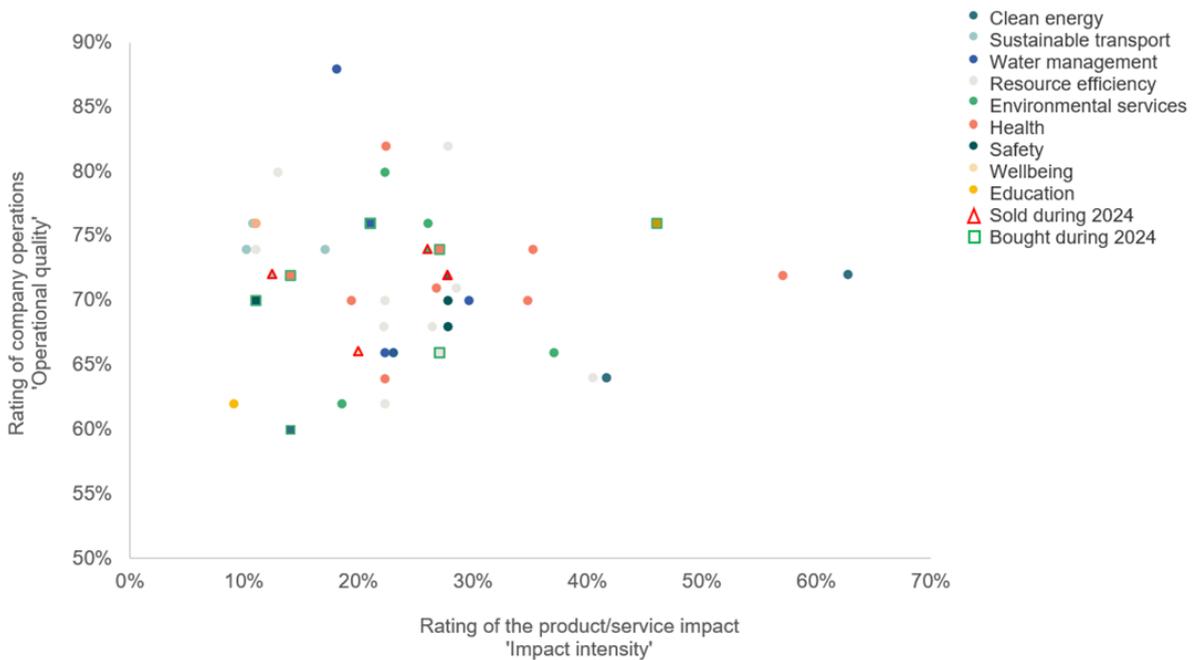
## Trading Activity – Significant Portfolio Changes

Stock Name	Purchase or sale	Theme	Brief description or sale rationale
Rockwell Automation	Purchase	Resource Efficiency	Company is entering higher growth phase with opportunity for margin expansion, presenting valuation opportunity.
Gerresheimer	Purchase	Health	Well positioned to capture the growth of the GLP-1 medication market at an attractive valuation.
Cooper Companies	Sale	Well-being	Lower conviction compared to Gerresheimer, which has a clear growth story.
American Water Works	Purchase	Water Management	Proactive and responsible approach to water quality, infrastructure and treatment services, while maintaining water bill stability relative to household income.
SolarEdge	Sale	Cleaner Energy	Stock reached our minimum market value threshold and so there was a requirement to sell.

## Impact Positioning: Supporting the UN Sustainable Development Goals<sup>39</sup>



## Impact Map of the strategy's portfolio following quarterly changes<sup>40</sup>



<sup>39</sup> For descriptions of impact mapping methodologies please see WHEB's impact reports, available at <https://impact.whebgroup.com/methodology/>. The SDG mapping methodology is described in the 2019 Impact Methodology Report, available at <https://impact.whebgroup.com/methodology/>, and the impact positioning graph is described in detail in the 2019 impact report.

<sup>40</sup> As above.

## ESG profile of WHEB's investment strategy



## Quarterly ESG performance

	WHEB Strategy	Proportion reported	MSCI world
Weighted average carbon intensity (scope 1 and 2)	97.5 tCO <sub>2</sub> e/£1m of revenue	75%	183 tCO <sub>2</sub> e/£1m of revenue
Scope 3 carbon efficiency	1,851 tCO <sub>2</sub> e/£1m of revenue	71%	913 tCO <sub>2</sub> e/£1m of revenue
Waste efficiency	13 tonnes / £1m of revenue	63%	407 tonnes / £1m of revenue
Water efficiency	6,357m <sup>3</sup> of fresh water/£1m of revenue	76%	9,464m <sup>3</sup> of fresh water/£1m of revenue
Gender equality	27% of board and top management positions are occupied by women	93%	26% of board and top management positions are occupied by women
Executive pay	74x – ratio of executive pay to employee pay	80%	101x - ratio of executive pay to employee pay
Board Independence	76% of board members are independent	86%	74% of board members are independent
Environmental good	37% of portfolio invested in environmental solutions	100%	12% of portfolio invested in environmental solutions
Social good	24% of portfolio allocated to help alleviate social issues	100%	11% of portfolio allocated to help alleviate social issues
Avoiding environmental harm	<1% of portfolio in industries that aggravate social issues	100%	6% of portfolio in environmentally destructive industries
Avoiding social harm	0% of portfolio in industries that aggravate social issues	100%	3% of portfolio in industries that aggravate social issues
Economic development <sup>41</sup>	\$51,500 – median income of portfolio-weighted area of economic activity	100%	\$50,800 – median income of portfolio-weighted geography of economic activity
Avoiding water scarcity <sup>42</sup>	2.4 – geographic water use	100%	2.5 – geographic water use
Employment <sup>43</sup>	4.51% - unemployment in portfolio-weighted area of economic activity	100%	4.47% - unemployment in portfolio-weighted area of economic activity
Tax gap	3.23% - estimated % of tax avoided by corporate tax mitigation schemes	100%	3.51% - estimated % of tax avoided by corporate tax mitigation schemes

<sup>41</sup> A lower figure demonstrates that the strategy is more exposed to activities in lower income communities.

<sup>42</sup> A lower figure demonstrates that the strategy is less exposed to water scarce areas (based on the World Resources Institute scale of 0-5 from least to most water scarce areas).

<sup>43</sup> A higher figure demonstrates that the strategy is more exposed to activities in communities suffering from higher unemployment.

# QUARTERLY ENGAGEMENT AND VOTING ACTIVITY

## Voting Record

The table below summarises the voting record at companies held in WHEB's investment strategy over the quarter. Full details of how we voted on each of the individual votes are detailed on our website: <https://pengana.com/our-funds/wheb-sustainable-impact-fund/>

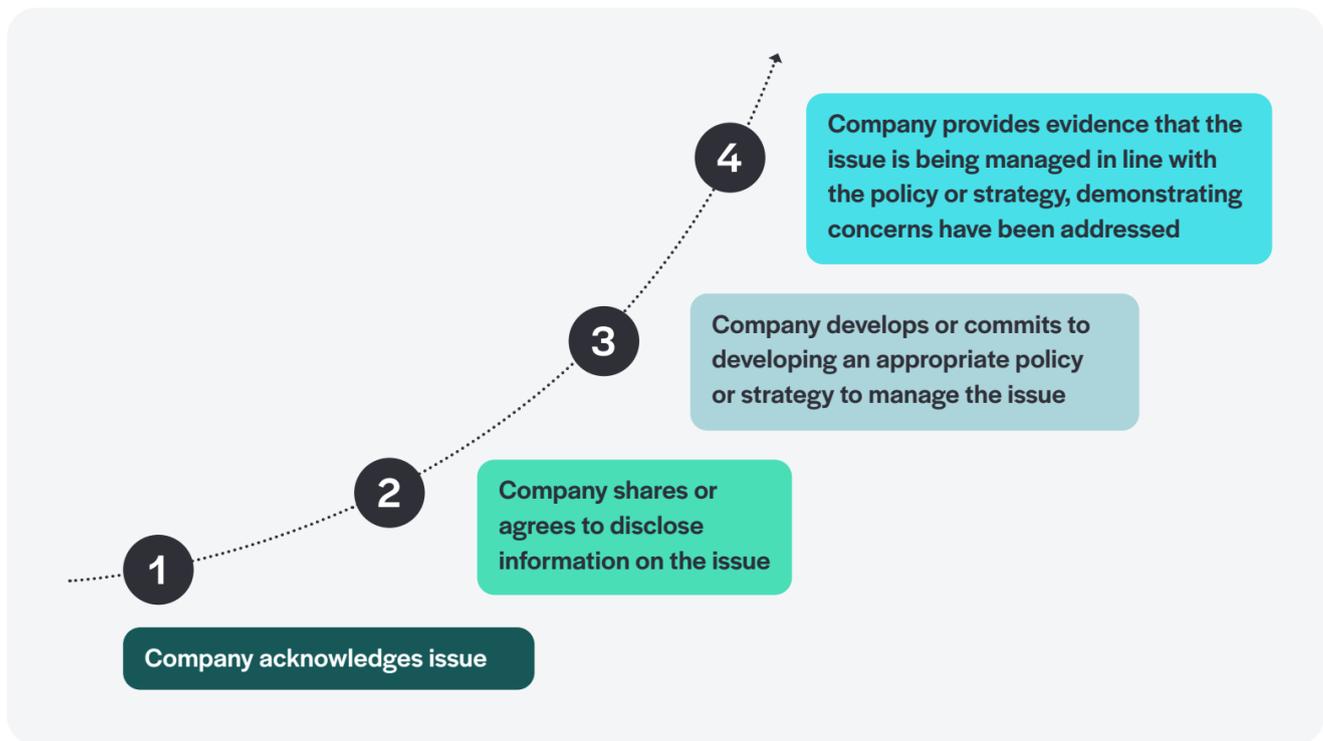
Meetings	No. of meetings	%
# votable meetings	40	
# meetings at which votes were cast	40	100%
# meetings at which we voted against management or abstained	38	95%

Resolutions	No. of resolutions	%
# votes cast with management	514	78%
# votes cast against mgmt. or abstained (see list in appendix)	144	22%
# resolutions where votes were withheld	6	<1%

## Company Engagement

Engagement Summary	Count	%
# Companies engaged	24	
# Engagements	79	
# Milestone 0 – company does not acknowledge issue	37	47%
# Milestone 1 – company acknowledges issue	14	18%
# Milestone 2 – company shares or agrees to disclose information on the issue	17	22%
# Milestone 3 – company develops or commits to developing an appropriate policy or strategy to manage the issue	8	10%
# Milestone 4 – Company provides evidence that the issue is being managed in line with the policy or strategy, demonstrating concerns have been addressed	3	4%

## WHEB’s engagement milestones



Company	Topic	Objective	Method	Milestone
Cooper Companies	Carbon - Net Zero Target/Strategy	Set a Net Zero Carbon position	Email	M1
Aptiv	Remuneration - Excessive pay	Pay is 1,545 x median	Vote/AGM Letter	M0
	Remuneration - Sustainability/ESG metrics	LTI is now linked to 2025 ESG targets	Vote/AGM Letter	M4
	Director Independence/Overboarding	Separation of CEO and Chair and reduce number of board commitments	Vote/AGM Letter	M0
	Auditor Independence	Change Auditor; EY has been in place since 2006	Vote/AGM Letter	M0
	Diversity – Gender	Board level female representation now at 40%; pushing for improvements across the business	Vote/AGM Letter	M4
	Human capital	Ensuring fair pay and freedom of association for Mexican employees	Vote/AGM Letter	M0
Arcadis	Director Independence/Overboarding	For Barbara Dugainer to reduce number of non-executive board positions	Vote/AGM Letter	M2
AstraZeneca	Remuneration - Excessive pay	Reduce egregious pay practices in the interest of shareholders	Email	M2
	Remuneration - Sustainability/ESG metrics	Link executive compensation to ESG/Sustainability targets	Email	M2
	Director Independence/Overboarding	Marcus Wallenberg to reduce number of non-executive board positions.	Email	M2

Croda International	Carbon - Net Zero Target/Strategy	To discuss Croda's response to the NZEI letter sent by IIGCC, and discuss further questions the group had regarding net zero.	Collaborative	M3
Daifuku	Remuneration - Excessive pay	Vote/AGM Letter	M0	
	Remuneration - Sustainability/ESG metrics	To include sustainability targets in management compensation relating to material issues and amounting to 10% to 30% of compensation.	Vote/AGM Letter	M0
	Board Independence	Minimum 50% board independence	Vote/AGM Letter	M0
	Diversity - Gender	Minimum 33% female board-level representation	Vote/AGM Letter	M0
Danaher Corporation	Other	Commending the company for Cepheid's Xpert test price reduction, and ensuring that the independent validation of the cost of the product is conducted annually. The letter also asks that Danaher set up a committee of stakeholders to give advice on and be informed of the process and methodology used for the audit.	Collaborative	M2
	Director independence/overboarding	Reduce number of board positions of several directors	Vote/AGM Letter	M0
	Sustainability Leadership	Board-oversight of sustainability required	Vote/AGM Letter	M0
	Auditor Independence	Rotate auditor	Vote/AGM Letter	M0
	Remuneration - Excessive pay	Reduce CEO pay (currently 322x median employee pay)	Vote/AGM Letter	M0
	Remuneration - Sustainability/ESG metrics	To include sustainability targets in management compensation relating to material issues and amounting to 10% to 30% of compensation.	Vote/AGM Letter	M0
	Shareholder Rights	Reduce ownership threshold to improve minority shareholder engagement and communication	Vote/AGM Letter	M0
	Diversity - Other	Greater transparency on Diversity, Equity and Inclusion, to allow better evaluation the talent management effectiveness.	Vote/AGM Letter	M0
Ecolab	Remuneration - Excessive pay	Reduce CEO pay (currently 316 median employee pay)	Vote/AGM Letter	M0
	Remuneration - Sustainability/ESG metrics	To include sustainability targets in management compensation relating to material issues and amounting to 10% to 30% of compensation.	Vote/AGM Letter	M0
	Director independence/overboarding	Improve director independence by addressing overboarding for several directors; ensure the Chair is independent	Vote/AGM Letter	M0
	Auditor Independence	PwC has been the auditor since 1970; rotate the auditor	Vote/AGM Letter	M0
	Environmental Pollution - Hazardous chemicals	Prep call with ChemSec as part of IIHC; request for call with Ecolab to discuss strategy for phase out of hazardous chemicals	Collaborative	M2
First Solar	Auditor Independence	Rotate the auditor	Meeting	M2
	Director independence/overboarding	Improve director independence by reducing director tenure.	Meeting	M2
	Diversity - Gender	Minimum 33% female board-level representation	Vote/AGM Letter	M0
	Remuneration - Sustainability/ESG metrics	Add clear incentives to CEO's pay package to deliver on annual GHG emission reduction targets	Vote/AGM Letter	M0
	Carbon - Net Zero Target/Strategy	For the company to become an off-taker of green electricity	Meeting	M3

Gerresheimer	Product impact - negative	Reduce end of life product impact	Meeting/Conference Call	M2
	Board Independence	Address concerns about independence of various directors	Meeting/Conference Call	M4
	Combined CEO and Chair	Separate CEO and Chair positions	Meeting/Conference Call	M3
	Carbon - Net Zero Target/Strategy	Confirm SBTi aligned targets	Meeting/Conference Call	M3
Grand Canyon Education	Combined CEO and Chair	Separate CEO and Chair positions	Vote/AGM Letter	M1
	Auditor Independence	Change Auditor; tenure exceeds 10 years	Vote/AGM Letter	M1
	Remuneration - Sustainability/ESG metrics	To include sustainability targets in management compensation relating to material issues and amounting to 10% to 30% of compensation.	Vote/AGM Letter	M1
	Diversity – Gender	Separation of gender from other diversity characteristics in disclosures	Vote/AGM Letter	M1
Keyence	Carbon - Net Zero Target/Strategy	Set a 2050 Net Zero Carbon target	Vote/AGM Letter	M0
	Diversity - Gender	Minimum 33% gender diversity	Vote/AGM Letter	M0
	Sustainability Leadership	Minimum one member of the board with a clear responsibility for sustainability	Vote/AGM Letter	M0
Power Integrations	Remuneration - Excessive Pay	Address egregious pay practices.	Meeting	M3
	Auditor Independence	Rotate auditor	Meeting	M1
	Tax	Remuneration - Sustainability/ESG metrics	To include sustainability targets in management compensation relating to material issues and amounting to 10% to 30% of compensation.	M1
Schneider Electric	Director Independence/Overboarding	Reduce director tenure and for Anders Runevad to reduce number of executive board positions	M1	
Siemens Healthineers	Animal Rights	Enquiry into allegations of animal abuse and encouraging the company to publish an animal welfare policy	Collaborative/E mail	M2
Smurfit Westrock	Biodiversity	Ongoing NA100 engagement	Collaborative	M2
SolarEdge	Carbon - Net Zero Target/Strategy	For the company to set a SBTi Validated 2050 Net Zero Carbon target	Call/Conference Call	M3
	Auditor Independence	Rotate Auditors	Vote/AGM Letter	M1

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