

# RIVER AND MERCANTILE EUROPEAN CHANGE FOR BETTER STRATEGY

## INVESTING IN THE FUTURE, AT YESTERDAY'S VALUATIONS

As interest in all things ESG has increased significantly over the past few years, some of the more high-profile, low carbon companies have seen their stock market valuations soar. As **valuation conscious, contrarian investors**, we look at some of the well-known 'ESG darling' stocks with amazement.

Clean is good. Or is it? If society is to hit its climate targets, there is **an unequivocal need to decarbonise polluting sectors** and activities. The bill for doing this is a vast \$6 trillion per annum. Spending on renewable energy, for example, has been growing for decades (unsurprisingly leading to the elevated valuations we encounter) yet in dozens of other sectors and industries it's just about to start. This is our broad investment opportunity then: an **opportunity to make the returns we want** for our investors, and the investment that is going to allow society to **hit its climate targets**.

Put another way, is it better to invest in a company with a low carbon footprint because it is capital light such as a software business or branded goods company, or does it do **more actual good** for the environment to, for example, invest and support a steel manufacturer with the technology to **halve the carbon intensity** of its products or its customers products? The ESG investment industry has tried the former for many years, and yet we have undeniably failed to produce a reduction in carbon emissions we so desperately need to achieve, as we show in figure 1, overleaf.

This new strategy is absolutely focused on changing this, **for the better of society** and **for the better of our clients' investment returns**. This throws wide open a huge number of unloved areas of the market, which are likely to see a far better cycle than they have over the last decade. We call companies with these transitional characteristics '**improvers**' and '**enablers**'. Our approach is a happy confluence of having a positive impact on the world and operating in line with our contrarian, pragmatic philosophy: exposing the strategy to **re-rating potential**. Investing in sustainability in this way is very aligned with a contrarian, valuation-conscious mindset.

In short, this is a much wider opportunity than wind farms and Tesla!

### KEY FACTS

A truly differentiated approach to sustainability investing

A sustainable European Equity strategy (which meets the standards of **SFDR article 9**) that **combines contrarian and value credentials**

Focused on the **transition of polluting activities**, leading to "off the beaten track" ESG investments...

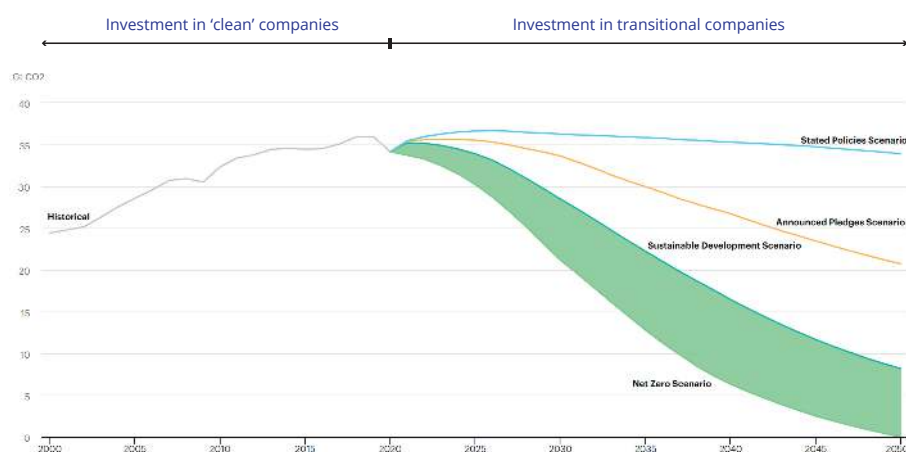
... with **re-rating potential** and an actual **real-world positive impact** on the environment

A **great diversifier for clients** over-exposed to the same narrow set of ESG growth stocks

Run by experienced European equities manager, **James Sym**



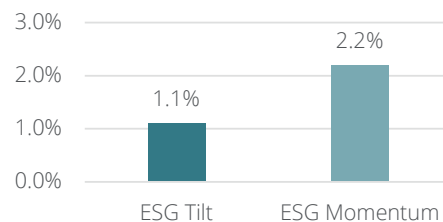
**Figure 1. Investment in 'clean' versus 'transitional' companies.**



Source: IEA, CO2 emissions in the WEO-2021 scenarios, 2000-2050, IEA, Paris <https://www.iea.org/data-and-statistics/charts/co2-emissions-in-the-weo-2021-scenarios-2000-2050>

**Figure 2. Difference between investing in ESG Clean companies and ESG Improvers.**

MSCI Study – Active Return of ESG Tilt and Momentum Strategies (Annualised, Feb-07 to Mar-15)



Source Bernstein. Published April 2021.

Within our investment team we have developed a philosophy and process which integrates **sustainability** at its core, and which we apply to every company we look at to produce our proprietary scores and analysis. Simply put, the key difference is **we are looking for improvement**, and **enablers of that improvement**, rather than 'good' today. Using the MSCI scores as a proxy, this suggests more potential for alpha generation (figure 2).

This strategy is **concentrated, unconstrained** and focused on companies where the climate agenda offers a **game-changing opportunity**. With ESG investing having become very concentrated in the highest valued, most crowded growth stocks, our strategy offers the opportunity to **diversify valuation-risk** while enhancing the ESG contribution of the portfolio, as well as being a potentially **exciting alpha opportunity** in its own right. We are investing in the companies of tomorrow, at yesterday's valuations.

**This is Change for Better.**

RIVER AND MERCANTILE

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