Q4 2023 Update

IQEQ

Davy Low Carbon Equity Fund

For Investment Professionals Only

Performance	1 Month (%)	Q4 2023 (%)	1 Year (%)	3 Years P.a. (%)	5 Years P.a. (%)
Davy Low Carbon Equity Fund[1] (net of fees)	4.48	9.08	12.39	6.88	12.24
MSCI World Index[2]	3.62	6.79	19.60	10.99	13.58

Source: IQ EQ Fund Management (Ireland) Limited (Class AA Acc in EUR) as at 29 December 2023.

[1]The Davy Low Carbon Equity Fund (previously named the Davy ESG Ex-Fossil Fuels Fund) is a UCITS fund and was launched on 26 April 2018.
[2]The MSCI World Index shown above does not include fees or operating expenses and you cannot invest in it.
The MSCI World Index captures large and mid-cap representation across 23 Developed Markets (DM) countries. With 1,650 constituents, the index covers approximately 85% of the free float-adjusted market capitalization in each country.

Fund overview

The aim of the **Davy Low Carbon Equity Fund** (the "Fund") is to achieve long-term capital growth. We aim to achieve this by investing in a portfolio of "blue chip" global companies chosen based on carbon emissions criteria. The Fund favours corporate practices that have actively embraced carbon emissions reduction relative to peers. The Fund does not invest in companies which explore, extract and/or profit from the burning of fossil fuels.

Market comment

After marking time during the third quarter of 2023, global equity markets reached all-time highs during the fourth quarter, rising by 6.79%. The year-end rally erased all of 2022's losses and brought the return for 2023 to 19.60%.

Equity markets were buoyed by rapidly falling bond yields, with the benchmark US 10-year yield falling from a 16-year high of 5.0% in October to finish the year at 3.9%. Investors are now expecting a 0.25% cut in US interest rates by the end of March 2024.

The US was the best-performing equity region during the year, driven by a strong performance by the so-called 'Magnificent Seven' stocks – Microsoft Corp., Apple Inc., Amazon.com Inc., Tesla Inc., Meta Platforms Inc., Alphabet Inc., and Nvidia Corp. While their contribution faded somewhat in the fourth quarter, the performance of these stocks accounted for 48.3% of the total return of the c. 1,500-stock MSCI World Index during 2023 – an unusual level of performance concentration in such a broad index.

Many of the seven stocks are seen as probable winners in the development and implementation of Artificial Intelligence ("AI"). Nvidia Corp., which designs and develops processors that are integral to the advancement of AI, was among the best performers in 2023, rising by 228%. These stocks are represented within the Technology, Communications Services and Consumer Discretionary sectors, which were the best performers during 2023.

The Energy sector was the worst performing sector in the fourth quarter as the Brent oil price fell from $97.4 at the beginning of the quarter to end the year at $77.0. The price fall was driven by overt disagreements among OPEC+ members about voluntary production cuts to support the oil price. The Consumer Staples sector also suffered as tepid demand and increasing costs resulted in profit downgrades throughout the sector.

Fund performance

The **Davy Low Carbon Fund** had a strong final quarter to 2023, returning +9.08%, net of fees. This compares to the MSCI World return of +6.79%. Asset Allocation was the main driver of outperformance with Stock Selection and Currency also making positive contributions to return. Positive Asset Allocation came from having no position in the worst performing Energy sector and by being overweight Industrials and the best performing Technology sector. No holding within the second best performing Real Estate sector partially took from Allocation. Stock Selection was most positive within Industrials (Alfen, Vestas, Xylem) and Financials (Blackrock). This more than offset weak selection within the Technology (Oracle, SolarEdge, Cognex) sector. The contribution from Currency was positive as the strategy was underweight a weakening US dollar. Looking at the Low Carbon leader board thematic groupings, the Renewables names bounced back strongly with Alfen, Vestas Wind Systems and Solaria Energia topping the table, although SolarEdge was the worst performing name in quarter. Resource Conservation companies such as Novozymes, Xylem and Fortune Brands also starred high in the table. Sustainable Finance holdings such as Deutsche Boerse and State Street featured mid table whilst Energy Efficiency names were scattered high and low with Assa Abloy and Siemens doing best. In such a strong market the Low Carbon Leaders grouping, which tends to be more defensive, had names spread across the middle to bottom half of the table.

The top five equity contributors to relative performance during the quarter were: Microsoft, Siemens AG, Vestas Wind Systems, Alfen, Xylem Inc. The bottom five equity detractors from relative performance during the quarter were: Energy Recovery Inc., SolarEdge Technologies Inc., Unilever, Thermo Fisher, Oracle

Microsoft Corp. (MS) the software giant, gained over +14.3% in the fourth quarter, reached an all-time high in November and was the top contributor to returns. Better-than-expected quarterly earnings results at the end of October continued to drive performance as headlines showed a reacceleration in Azure growth to +28% which was driven by better-than-expected contributions from AI-enabled services. Other areas such as Commercial Office and Gaming also exceeded expectations with the more cyclical areas such as LinkedIn ahead, and Advertising in line. The company seems able to invest at scale, driving growth while defending the bottom line. Microsoft is a beneficiary of AI, where they can enhance their product range and bring AI to the masses. It will also help accelerate top line growth. Our thesis remains intact as we expect the company to exit any recession stronger than peers. Their 2030 target to reduce Scope 1&2 emissions by 75% by 2030 will help avoid over 10m metric tons of carbon emissions. Following an updated Suppliers Code, 87% of their suppliers now report to CDP. Azure is also driving the transition to “smart cities”, with exposure to reductions in energy usage, water management, waste management, carbon emissions management and crisis management for extreme weather events. Microsoft fits the strategy theme of Energy Efficiency.

Vestas Wind Systems A/S (Vestas), which develops, manufactures and markets wind turbines that generate electricity, was a top contributor to return in Q4, returning over +41%. Sentiment towards the renewables sector had been negatively impacted by project delays, bottlenecks, profit warnings and impairments throughout 2023 until October when a rebound in the share price over the quarter overcame the weakness of the previous 9 months. This rebound coincided with risk sentiment gaining ground as the prospect of interest rate cuts in 2024 rose, and a Q3 earnings report which beat market expectations in November. A December update from Vestas shows that the company had a strong end to the year securing over 7GW of turbine orders in Q4. Importantly for 2023, US onshore orders rose substantially which shows the company's strong presence in the US and the competitiveness and reliability of its products. The strong order momentum and margin improvement reaffirms our confidence in Vestas which is a natural fit for our Renewables theme within the Low Carbon strategy.

Energy Recovery is the gold standard in seawater desalination but was the main detractor from returns in the 3-month period, down almost 15%. An abrupt announcement in October that the CEO, Bob Mao, is to be replaced and is to step down as chairman was a surprise. The shares fell 16%. Mao will remain on the board. The change in leadership, however, does reflect the company's changing needs as it faces the next phase of its growth using its technology in refrigeration, where it is replacing HFC refrigerants with CO_2, and wastewater treatment. Q3 results were better than expected and guidance for the full year 2023 was reaffirmed. Guidance for 2024 is cautious and second half loaded which was better than feared. The company's selling point is that it can design and manufacture solutions that reduce waste and energy consumption for its customers. For example, in seawater desalination Energy Recovery can reduce energy consumption by 60% and its technology is about 25% the cost of the now outdated thermal process. Indeed, many thermal plants are transitioning to seawater reverse osmosis and to Energy Recovery's pressure exchangers. By 2030 the UN estimates that there will be a 40% shortfall in the freshwater needs of the world. Energy Recovery is a high-quality company with high topline growth and attractive margins and comes under the theme of Clean Technology, Energy Efficiency.

SolarEdge Technologies Inc. (SolarEdge) was also a detractor to returns in the quarter, declining almost 31%. SolarEdge fits within our Renewables thematic as the company designs and sells solar power optimisers and inverters for residential and small-scale solar power plants. It is a leader in the US solar rooftop market. However, the company preannounced Q3 results well below expectations in October due to substantial unexpected cancellations and push-outs of existing backlogs from European distributors, high inventory levels and slower installation rates. Higher interest rates have also impacted the US residential market. On the day the shares fell 27% and were down over 41% in October. The magnitude of the weakness in 2H 2023 surprised the market with a recovery unlikely to be seen well into 1H 2024. Q3 results in November were in line with October's pre-announcement. However, Q4 guidance was below expectations as inventories remained high. SolarEdge is one of the few solar stocks that is consistently profitable, generates cash and has a solid balance sheet. They are also well positioned to benefit from the US Inflation Reduction Act and REPowerEU where solar will play an important role. The company is a long-term winner in this space and the current valuation looks very attractive. We will look to add to the name as visibility on the outlook improves.

Sample portfolio transactions

We sold out of Tractor Supply and Thermo Fisher to fund higher conviction solution providers such as TSMC, Assa Abloy and Siemens. We also started a new position in Greencoat Renewables which gives us access to euro area private renewable assets.

The QQE perspective

We have been observing a remarkably high degree of performance concentration within the equity market during 2023. By the fourth quarter it had a name – the 'Magnificent Seven'. These, mostly US-based AI-related shares were driving global equity market performance to a degree not seen in the past. At one point in October these seven shares were contributing 60% of the total year-to-date return of the MSCI World Index.

By and large, the Magnificent Seven companies had strong consistent cash flows or, in the case of Tesla Inc., growing cash flows. Microsoft Corp., Apple Inc. and Alphabet Inc. had also shown earnings resilience through downturns in the past and all scored highly on our Quality model, which is comprised of four sub-pillars reflecting the attributes that we believe will drive long-term performance for our clients: Profitability, Persistence, Protection and People. Investors had been paying up for growth and consistency during the year, which drove the performance of our Profitability and Persistence pillars. However, the Magnificent Seven do not score well on valuation, due in part to the dearth of dividends from the group and relatively high PEs.

We had observed a hiatus in the momentum of these stocks in Q3 of 2023 as our People pillar outperformed for the first time in 2023.

Things changed somewhat in the third quarter when the People pillar, which represents companies that manage their capital well and reward shareholders with distributions, recovered some performance. Sectors such as Financials, Healthcare and Energy are represented within the pillar and these performed strongly during the third quarter before much of that relative performance was given up again as the Magnificent Seven surged again in October and into November. However, in the weeks of the year-end rally the People pillar has held its own. This may be an early sign that the performance concentration which we have seen in 2023 may not be such a feature in the year ahead.

Calendar year performance	2023 (%)	2022 (%)	2021 (%)	2020 (%)	2019 (%)
Davy Low Carbon Equity Fund (Net of fees) (EUR)	12.4	-14.6	27.1	10.8	31.7
MSCI World Index (EUR)	19.6	-12.8	31.1	6.3	30.0
Alfen N.V.	-28.4	-4.6	6.8	402.4	33.5
Energy Recovery Inc.	-8.1	-4.7	57.6	39.3	45.5
Microsoft Corp.	58.2	-28.0	52.5	42.5	57.6
Oracle Corp	30.9	-4.6	36.9	24.2	19.3
Siemens AG	34.9	-12.6	33.3	15.4	24.4
SolarEdge Technologies Inc.	-67.0	1.0	-12.1	235.6	170.9
Thermo Fisher Scientific Inc.	-3.4	-17.3	43.5	43.7	45.5
Unilever plc	3.0	3.5	-1.6	0.0	11.5
Vestas Wind Systems A/S	6.0	1.2	-30.1	116.8	38.5
Xylem Inc.	4.8	-6.6	18.9	30.9	19.6

Source: IQ EQ Fund Management (Ireland) Limited (Class AA Acc in EUR) and Bloomberg as at 29 December 2023. Performance is quoted in local currency unless otherwise stated.

Warning: Past performance is not a reliable guide to future performance. The value of the investment can reduce as well as increase and, therefore, the return on the investment will also be variable. Changes in exchange rates may have an adverse effect on the value price or income of the product.

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The Davy Low Carbon Equity Fund (previously named the Davy ESG Ex-Fossil Fuels Fund, the name changed effective as at 12 July 2019) is a sub-fund of Davy Funds plc, an open-ended umbrella investment company with variable capital and segregated liability between sub-funds incorporated with limited liability under the Companies Acts 2014, authorised by the Central Bank of Ireland as an Undertaking for Collective Investment in Transferrable Securities (UCITS). The Prospectus, Supplement and Key Investor Document for the fund are available in English from IQ EQ Fund Management (Ireland) Limited, 5th Floor, 76 Sir John Rogerson’s Quay, Dublin Docklands, Dublin 2, D02 C9D0, Ireland or https://www.iqeq.com/davy-funds-plc/. Investors should be aware that some of the Directors of the Company (Davy Funds plc) are also employed by the Investment Manager, Promoter and Distributor. Further information in relation to the management of potential conflicts of interest is available upon request.

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*Information correct as of 24 February 2023

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