Ninety One

Investing for a world of change

# Opportunities at a low point in the sentiment cycle

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## How would you sum up 2024 for decarbonisation investors?

It has been a mixed year. Generally, the equity market has been extremely narrow, with performance driven by a small number of stocks. In decarbonisation-related sectors specifically, higher interest rates have pressured returns, particularly in the US and Europe. Partly as a consequence, sentiment towards clean-tech sectors has been very negative. This has been made worse by policy uncertainty, which intensified after the US election.

## What does weaker sentiment typically mean for decarbonisation investors?

We have been here before, of course. This is probably the third major 'sentiment cycle' I have witnessed in my career. For example, sentiment towards clean-tech sectors also became extremely negative in 2009/10, 2013/14 and 2014/15. Such periods often present the most attractive entry points to allocate to decarbonisation companies.

This part of the equity market may be out of favour, but most investors still ascribe some probability to a transition to net zero, not least because of the increasing frequency of extreme weather events. And if we are going to address carbon emissions and move along the net-zero pathway, that will be a tailwind for companies enabling decarbonisation. We think investors are likely underappreciating the future growth from decarbonisation companies, making this an attractive, countercyclical entry opportunity.

## What can investors in decarbonisation expect from Trump 2.0?

It will be crucial to separate 'noise' from 'signal' – i.e., to distinguish between headline-grabbing statements and policy decisions, and the issues that are material to investments. For example, a swift US withdrawal from the Paris Agreement may harm sentiment but it will not directly affect our company forecasts. The Inflation Reduction Act (IRA), the most significant piece of US climate legislation, is more important. But while it will likely face scrutiny, we have already seen a number of Republicans in Congress back the act, so it will be very difficult to dismantle. Even if the IRA is partially repealed, this won't necessarily affect the bottom line of all decarbonisation companies. For example, the largest renewables producer in the US has locked in tax credits for the next four years, insulating it from potential fall-out.

There has also been a lot of discussion about the potential impact of tariffs. Our biggest concern is that tariffs could ultimately result in higher long-term interest rates, which would be a headwind given the very large capital investment required to decarbonise the economy. On the other hand, deregulation, such as changes to the planning framework, could accelerate investment in renewable infrastructure, as happened during Trump's first term.

## How should decarbonisation investors approach China in 2025?

The Chinese decarbonisation value chain is already subject to high tariffs, and as a consequence no Chinese electric vehicles (EVs) are being sold in the US. But large numbers of EVs are being sold in China itself. We have increasingly focused our China allocations on companies with strong positions in China's huge and fast-growing domestic clean-tech market, and that are also well-placed to export to the rest of the world – to countries like Thailand, Brazil, Vietnam and India. These markets are all moving quickly towards electrification, not primarily because of subsidies but for economic reasons. Many of these emerging markets now have significantly higher EV penetration than the US, which is a direct result of the availability of appealing and very keenly priced Chinese EVs.

More broadly, climate policy continues to be strongly supported in China, and other nations such as India are rapidly stepping up their energy transitions. In Europe, the picture is more mixed, but countries like the UK are moving to accelerate climate investment.

## How will changes in technology and consumer behaviour influence decarbonisation in 2025?

Technological innovation and shifting consumer behaviour continue to reshape the decarbonisation landscape. In China, battery advancements are enabling EV ranges up to 1,000 kilometres, eliminating range anxiety. We are also seeing important innovations in energy efficiency, especially to enable data centres to handle the power demands of artificial intelligence (AI). This is an area where we have been adding exposure in the portfolio.

## Where are you finding new or underappreciated investment opportunities?

Recent negativity towards decarbonisation has created opportunities to invest in high-quality companies with structural growth potential that we do not believe is being priced by the market. As a result, we have added more stocks to the portfolio in the most recent quarter than ever before. The portfolio is now cheaper than at any point since inception, while its quality has improved.

Areas where we are finding particularly interesting opportunities include companies supporting the power needs of AI and hyperscale data centres. These include renewables developers and battery manufacturers, as well as firms supplying efficient electrical and cooling equipment, and handling the permitting and planning for new data centre projects.

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