



MUNRO

Quarterly report

Munro Climate Change Leaders Fund

MCCL.ASX

June 2023



Munro Climate Change Leaders Fund & MCCL.ASX

June 2023 – Quarterly report

MCCL Fund quarter return

5.5%

MSCI quarter return

6.8%

MCCL.ASX Fund quarter return

5.4%

MSCI quarter return

6.8%

QUARTERLY HIGHLIGHTS

- The Munro Climate Change Leaders Fund and MCCL.ASX returned 5.5% and 5.4% respectively in the June quarter.
- Performance for the quarter was again led by Nvidia (195bps), whose GPUs play a significant role in reducing power consumption and increasing energy efficiency in data centres. Other positive contributors from the quarter included clean power generator, Constellation Energy (118bps), grid infrastructure services company Quanta Services (111bps) and industrial waste disposal and recycling company Clean Harbors (79bps). While Enphase Energy (-98bps) and Vestas (-51bps) were the key detractors from performance over the quarter.
- Some of the main news items in the Climate universe included some positive details from the US Treasury on the Inflation Reduction Act, specifically, further guidance on how the tax credits work and how projects qualify, and heavy discounting in electric vehicles led by Tesla, which is likely to result in an inflection in adoption. Further, the Canadian wildfires brought home the seriousness of climate change to many market participants, with cities like Toronto and New York blanketed in thick smoke.
- More broadly, events during the quarter included the positive artificial intelligence (AI) sentiment driven by Nvidia's very strong earnings and outlook commentary; the US debt ceiling resolution; and fears over a banking crisis abating.

MUNRO MEDIA

The Ideas Exchange, 31 May 2023

[AI technology opening new investment opportunities](#)

Livewire Markets, 1 June 2023

[The \\$50 trillion opportunity Munro is chasing](#)

GSFM Conversations, 18 June 2023

[Conversations: Silver Linings, Episode 5 with Mike Harut](#)

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QUARTERLY COMMENTARY

Fund commentary

The Munro Climate Change Leaders Fund returned 5.5% net in the June quarter (MCCL.ASX 5.4% net). The Fund's equity positions contributed to the performance over the period, with the weakening AUD also adding to performance.

Equity markets performed well over the quarter, with earnings from Big Cap Tech fuelling the rally for the perceived winners in AI. The biggest needle mover came from Nvidia, the graphics processing unit (GPU) chip manufacturer. The company saw earnings expectations increase by more than 80%, driven by high demand for the chips going into data centers to increase compute power required to run large language models (LLMs) used in generative AI.

Throughout the quarter, several key 'banana skins' or risks, were avoided. Most importantly, US President, Joe Biden, signed legislation to lift the debt ceiling, averting a catastrophic default on the federal government's debt. Other risks avoided include no further large bank failures, meaning a systemic banking crisis is less likely from here. And finally, the expectation of a much-awaited US recession was pushed further out to late 2023/early 2024, as recent rate hikes have yet to significantly slow the economy.

From a Fund perspective, our performance for the quarter was again led by Nvidia which added 195 basis points to returns. The Fund owns a position in Nvidia because of the role its GPUs play in reducing the power consumption and increasing energy efficiency in data centres (the full details of why we consider Nvidia as enabling decarbonisation are in the [March 2023 Climate quarterly report](#)). Other positive contributors over the quarter include Constellation Energy (118bps), which bounced after a weaker start to the year (see [March 2023 Climate quarterly report](#) for further information), Quanta Services (111bps) and Clean Harbors (79bps), which we provide further information on in the stock stories below. Our largest detractor over the quarter was Enphase Energy (-98bps), the solar energy equipment manufacturer, following their earnings outlook, which saw the demand outlook soften on weak sell through trends in the distributor channel and inflexible cash advance terms to installers.

Some of the main news items in the Climate universe included:

- positive details from the US Treasury on the Inflation Reduction Act (specifically further guidance on how the tax credits work and how projects qualify;
- heavy discounting in Electric Vehicles (EV) led by Tesla, which is likely to result in an inflection in EV adoption; and
- while not financial market specific, the Canadian wildfires which brought the seriousness of climate change home to many market participants, with cities like Toronto and New York blanketed in thick smoke.

The US Treasury and IRS have continued to clarify exactly how the tax credits in the Inflation Reduction Act will work.

During the quarter, the IRS confirmed domestic content requirements for solar and wind. Specifically, it was confirmed that 40% of manufactured solar and onshore wind products must be domestically produced (rising to 55% for projects that begin construction after 2026) to claim the bonus credit. We see this as a win for US based manufacturers that supply renewables projects, including First Solar, a US-based panel manufacturer and a fund holding. It is also a positive for developers like NextEra as it gives them clarity on the supply chains they need to have in place to capture the benefit for new projects.

To date, many companies have been reluctant to formally announce projects ahead of tax clarity, and few companies have officially upgraded financial guidance. We still expect this will filter through slowly, but as the tax clarity comes through, we expect to see a real pick up in orders and backlogs. Ultimately, this will feed to earnings for the companies and hence stock price performance.

QUARTERLY COMMENTARY

Fund commentary

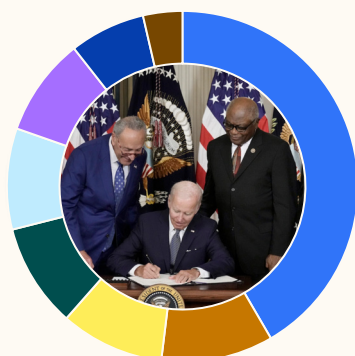
We also saw continued discounting in the US and Chinese EV markets this quarter, kicked off by Tesla and supported further by clarity on how the IRA's generous US\$7,500 consumer credit will work. Together these bring down the average selling price of EVs and make them more competitive with internal combustion engines. As adoption increases, it should increase economies of scale and battery production and help further lower cost. It will also spur demand for EV infrastructure, which will reduce 'range anxiety' as more – and more convenient – public charging infrastructure is built.

US IRA underpins a constructive and resilient policy backdrop

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IRA PROVIDES \$386B+ OF POLICY SUPPORT OVER 10+ YEARS

EXPECT MORE CLIMATE POLICY ACTION



- Clean Electricity
- Pollution, Transport and Infrastructure
- Individual Clean Energy Incentives
- Clean Manufacturing
- Clean Fuel and Vehicles
- Rural Development and others
- Building Efficiency and others
- Other



The EU “will respond in an adequate and well-calibrated manner to the Inflation Reduction Act”
Ursula von der Leyen, President of European Commission



“We will not be left behind.” C\$80bn committed over 10 years.
Canadian budget 2023



Landmark “30% by 2030” goals agreed at COP15 on biodiversity, signed by 190 countries

Source: Committee for a Responsible Federal Budget, whitehouse.gov, Financial Times, SEC, Morgan Stanley.
 (“30% by 2030” refers to a goal to achieve protection and conservation of 30% of land and oceans by 2030. Biodiversity loss is accelerated by climate change.)

QUARTERLY COMMENTARY

Market Outlook

Global markets have made a solid start to the year in 1H2023, with the second quarter building on gains from the first quarter. Since the middle of Q1, we have become incrementally more bullish on markets. As discussed last quarter, in our view we are close to the peak in long-term interest rates, and a significant amount of time has now passed since the beginning of the bear market. The last key indicator that we had previously been focused on was for earnings estimates to come down. Over the course of the year, we have been becoming more confident that earnings estimates had come down enough – using the S&P500 as a proxy for the market - earnings bottomed in late February and have been steadily revised up since then, whilst not back at the highs, many of the constituents are. Looking into the second half of the year, the market's key macro question is whether the global economy will have a 'soft' or 'hard' landing following the significant monetary tightening.

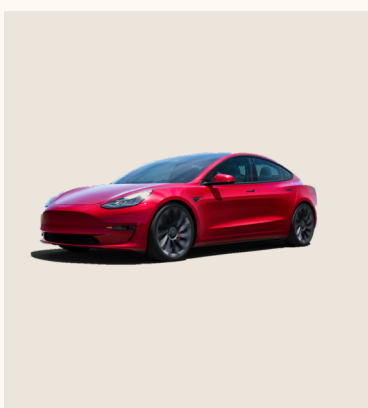
Headwinds that would see the economy have a hard landing include constrained household spending and lower business expansion from higher rates. Tailwinds, drivers of a soft landing, include the proliferation of productivity growth driven by a new AI super-cycle, along with growth out of the Chinese economy as it re-opens following COVID lockdown measures last year, and industrial growth driven by spending plans in the US including the Inflation Reduction Act and the CHIPS Act. Regardless of the outcome, with long-term rates peaking, the market has been going back to a more normalised environment, whereby share prices are following earnings – which bodes well for the Fund.

As highlighted above we see the Fund as exposed to many different idiosyncratic growth drivers such as EV adoption, and the US IRA incentivising investments in decarbonisation. So we feel well positioned for the 2H of 2023 regardless of the economic outcome from here. Some of these investments are shown in the slide below. The EV penetration rates accelerating ultimately as positive of the EV original equipment manufacturers (OEMs) like Tesla and their suppliers like the battery companies (Samsung SDI) and power semiconductor companies (Onsemi). The shift to EVs requires more electricity, which is a tailwind for the clean energy generators like Nextera and service providers like Quanta. Then lastly, we think the US / China trade war is an interesting tailwind for a number of US companies that feed into decarbonisation spending, because they are now protected from cheap Chinese competition.

Three changes in 2023

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EV PENETRATION ACCELERATING



THE GRID NEEDS TO KEEP UP



30 YEARS OF GLOBALISATION REVERSING



SUB AREA OF INTEREST: **CIRCULAR ECONOMY**MARKET CAP: **\$9B**

Clean Harbors added 79 bps to quarterly performance.

Clean Harbors is the largest hazardous waste disposal company in the US, with over 100 facilities across the US. Unlike other waste management companies in the Munro Climate Change Leaders strategy, Clean Harbors is a hazardous industrial waste company, rather than residential or commercial waste.

In the US, captive incineration facilities (those owned by the companies that create the waste) have been closing over time and being outsourced to specialists like Clean Harbors. Today, the company owns an estimated two-thirds of US hazardous waste incineration capacity, and the related collection and remediation services, which has enabled them to increase incineration price by around 10% p.a. in the last 4 years.

The company also operates in a highly regulated industry where new supply of hazardous waste management facilities comes via hard-to-obtain permits, of which Clean Harbors has over 500.

We initiated our position ahead of their capital markets day in late March, anticipating that the new Co-CEOs would release long-term earnings guidance, which the company had not done previously. Pleasingly, they announced a goal of doubling earnings, including M&A to US\$2bn 2027, a neat fit into Munro's strategy of investing in companies whose earnings have potential to double in five years.

Interestingly, the guidance does not yet include opportunities related to PFAS chemicals. These are a set of widely used chemicals that break down very slowly in the environment. In the US, the Environmental Protection Agency's (EPA) plan to tackle PFAS includes US\$50b to investments in water infrastructure, US\$5b to clean up legacy contamination at sites and upcoming rulemaking on acceptable levels.

This presents a potential revenue opportunity for Clean Harbors to remediate sites such as chemical factories, as well as airports and military facilities contaminated with PFAS from fire-fighting foam during exercises. They also have an incineration opportunity, having demonstrated that their incinerators can destroy over 99% of these chemicals. This is likely a multi-decade opportunity, which will become clearer as the EPA's rulemaking is hopefully finalised later this year.

In terms of climate change mitigation, their re-refining of used motor oil, incineration of ozone depleting substances and solvent recycling outweigh their scope 1 and 2 emissions (as shown below).

In terms of ESG more broadly, biodiversity has become a topic of increasing investor focus. In our view, Clean Harbors is a biodiversity champion through its environmental clean-up activities and the destruction or safe disposal of dangerous chemical waste.

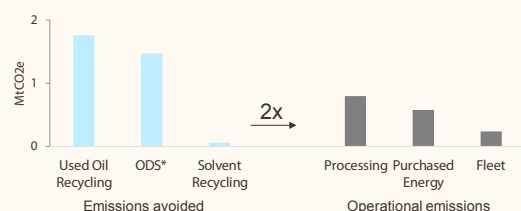
Industrial waste management – a hidden climate solution

MUNRO

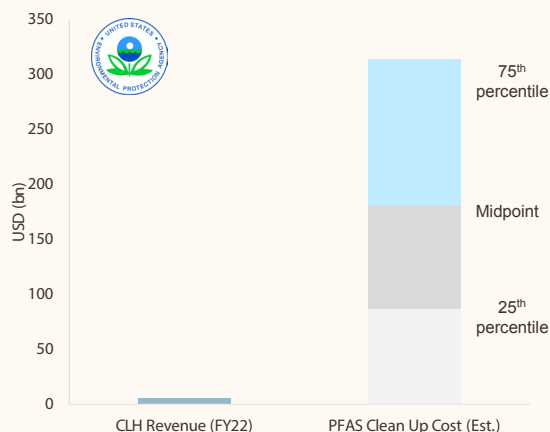
STRUCTURAL TAILWINDS



CLIMATE SOLUTION: HELPS AVOID 2X OPERATIONAL EMISSIONS



POTENTIAL PFAS CLEAN UP OPPORTUNITY



SUB AREA OF INTEREST: **CLEAN ENERGY**MARKET CAP: **\$28B**

Quanta Services added 111 bps to quarterly performance.

Quanta Services provide a range of infrastructure solutions to the electric power industry, from design and installation to the repair and maintenance of transmission and distribution systems. They service their customers with over 38,000 skilled workers, more than their next three largest competitors combined. This is a key competitive advantage, especially given the industry-wide labour supply shortages, and providing this scarce capacity allows them to capture the majority of economic rents.

Although often overlooked, Quanta is arguably one of the most important companies in the energy transition, as they provide the 'picks and shovels' that enable the electrification of everything. We anticipate that the US will need to spend around \$2T on the electrical grid alone if they are to electrify their economy by 2050. A significant portion of this spending creates a revenue opportunity for Quanta, as they solve some of the biggest bottlenecks in the energy transition.

Decarbonisation requires electrification, and electrification, whether it be how we refuel our cars, heat our homes or power our industries – requires a grid that is reliable. However, 70% of grid lines in the US are over 25 years old, and outages are currently running at record levels. Climate change itself only exacerbates this issue, with blackouts from severe weather increasing 78% over the past decade. Therefore, it is critical that the US grid is modernised and hardened to ensure resilience to extreme weather and an uninterrupted electricity supply, especially as its importance in our lives grows.

It is also critical to upgrade the grid, as electrical load requirements in a net zero economy will be far greater than they are today. We met with Quanta's CEO at their headquarters in Houston, Texas in March, and he told us that simultaneously charging as few as 2 to 3 electric vehicles in a street has caused parts of the grid to breakdown at the transformer level. Further, an all-electric household, with electric vehicle charging and electric heating and cooling, will need more than 2.25 times as much electricity versus today's average. Therefore, investment in electrical load must accelerate this decade.

Finally, the shift to renewable energy sources creates a robust backlog of grid interconnection work for Quanta. Most of these renewable projects are in remote areas and require extensive transmission and distribution infrastructure to connect to the grid. Interconnection queues have also been growing rapidly over the last decade, with the number of renewable projects in these queues having increased 2.5 times. Furthermore, given wind and solar are intermittent, supply and demand matching will be critical to ensuring adequate baseload power.

We see Quanta as the cornerstone of the energy transition and expect revenue and earnings to materially accelerate as the US rushes to lay the foundational infrastructure for an electrified economy. This opportunity is underscored by multiple Federal stimulus packages, such as the Bipartisan Infrastructure Law that allocates \$73bn towards power infrastructure and clean energy transmission, which provide long-term earnings visibility.

The US power grid isn't ready for the transition...

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EXISTING GRID CHALLENGES...



70% of US grid lines are >25 years old



78% increase in blackouts due to climate change



Intermittency of renewables poses balance issues

IT'S ONLY GOING TO GET WORSE...



+150mn EVs

Electricity demand will grow...

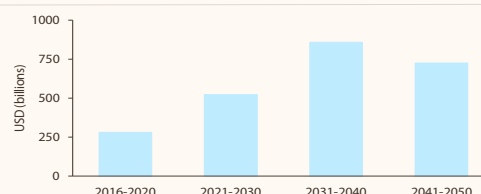
2.7x

...by 2050



+3,000GW

AVERAGE ANNUAL SPENDING ON POWER GRIDS REQUIRED TO HIT NET ZERO

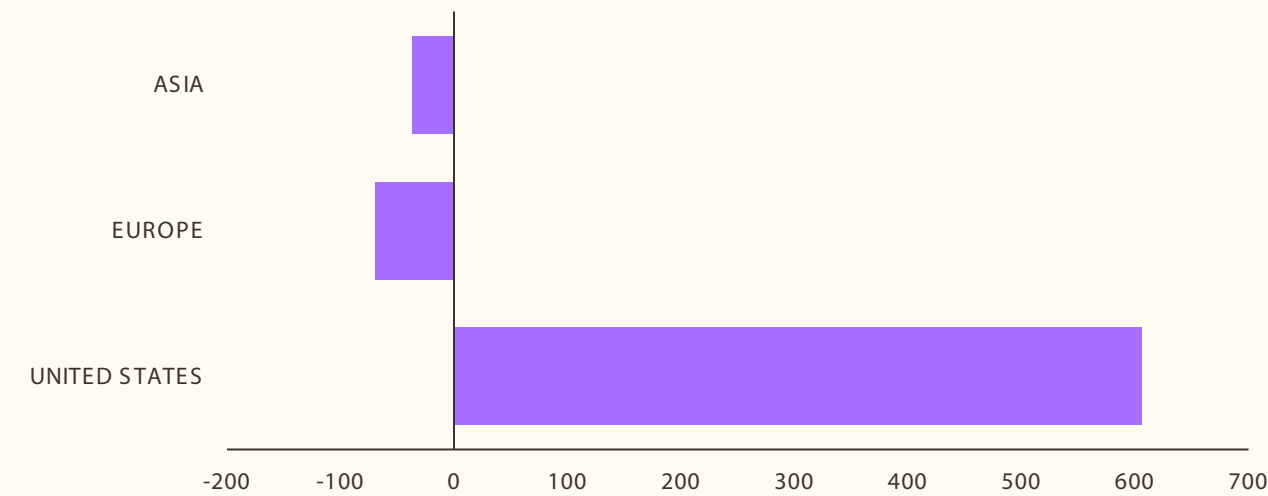


Source: HSBC, Bloomberg, IEA; 19 April 2023

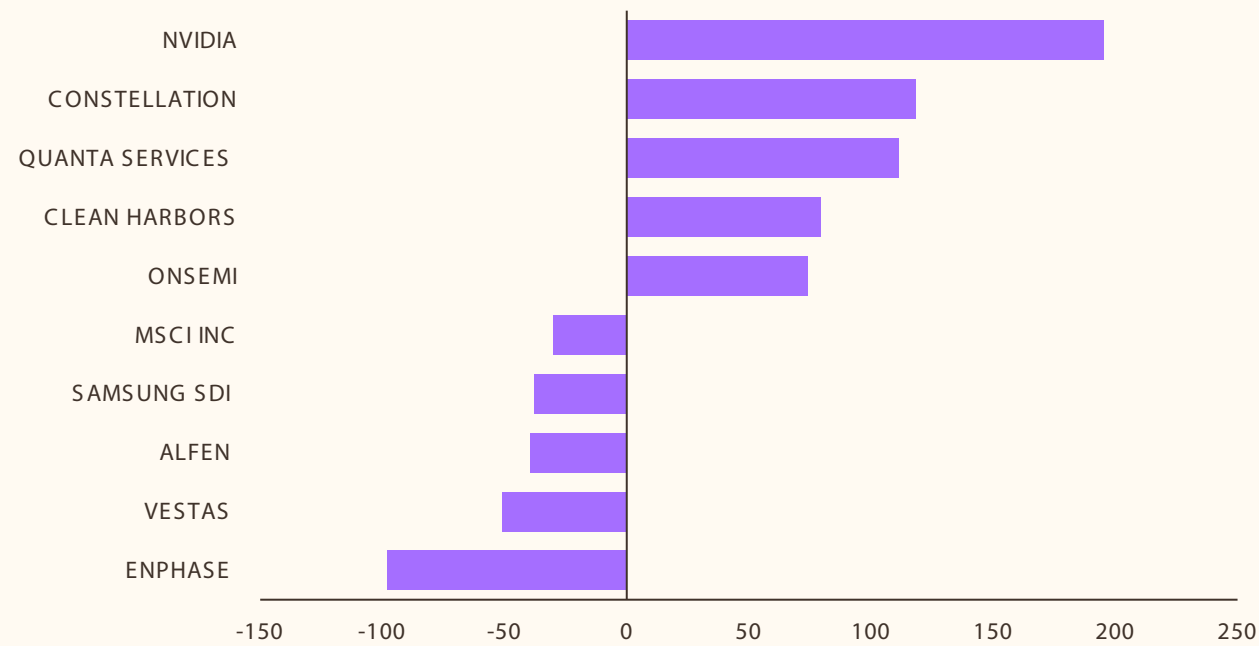


QUARTERLY FUND ATTRIBUTION (BASIS POINTS)

Region (equities only)



Top & bottom contributors



QUARTEREND EXPOSURE

Category

EQUITIES	97.2%
CASH	2.8%
NO. OF LONG POSITIONS	21

Region

	LONG
UNITED STATES	66.4%
EURO AREA	27.3%
GERMANY	14.9%
IRELAND	5.9%
SWITZERLAND	1.0%
DENMARK	5.5%
SOUTH KOREA	3.6%
TOTAL	97.2%
CASH	2.8%

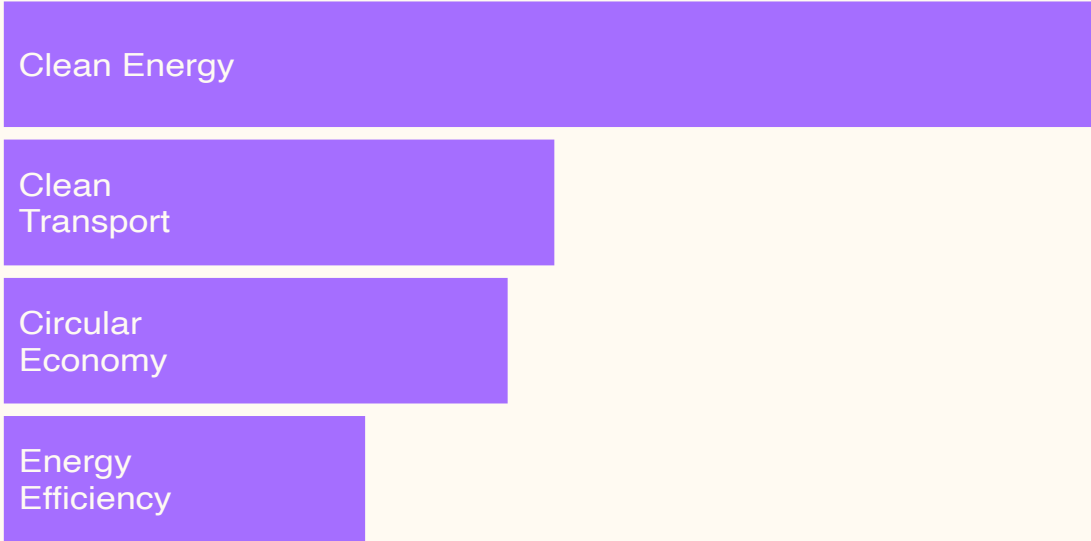
Sector

INDUSTRIALS	38.9%
INFORMATION TECHNOLOGY	26.0%
UTILITIES	19.6%
OTHER	12.8%

Holdings

TOP 5 HOLDINGS	
WASTE MANAGEMENT	7.5%
NEXTERA ENERGY	6.9%
CONSTELLATION ENERGY	6.8%
INFINEON	6.7%
QUANTA	6.7%

Sub-areas of interest



0%10%20%30%40%50%



Net Performance - MCCL

	3MTHS	6MTHS	1YR	INCEPT P.A.	INCEPT CUM.
MUNRO CLIMATE CHANGE LEADERS FUND (AUD)	5.5%	13.1%	21.3%	-2.3%	-3.8%
MSCI ACWI TR INDEX (AUD)	6.8%	16.1%	20.4%	3.9%	6.5%
EXCESS RETURN	-1.4%	-3.0%	0.9%	-6.1%	-10.3%

	JUL	AUG	SEP	OCT	NOV	DEC	JAN	FEB	MAR	APR	MAY	JUN	TOTAL
2022FY					3.5%	0.8%	-10.5%	-3.9%	0.2%	-4.5%	-1.1%	-6.6%	-20.7%
2023FY	10.6%	0.7%	-2.4%	3.3%	2.9%	-7.2%	-0.5%	1.6%	6.2%	-1.8%	4.1%	3.1%	21.3%

Net Performance - MCCL.ASX

	3MTHS	6MTHS	1 YEAR	INCEPT P.A.	INCEPT CUM.
MCCL.ASX (AUD)	5.4%	13.1%	21.3%	1.2%	1.8%
MSCI ACWI TR INDEX (AUD)	6.8%	16.1%	20.4%	3.9%	5.7%
EXCESS RETURN	-1.4%	-3.0%	0.9%	-2.7%	-3.9%

	JUL	AUG	SEP	OCT	NOV	DEC	JAN	FEB	MAR	APR	MAY	JUN	TOTAL
2022FY							-1.1%	-3.9%	0.2%	-4.5%	-1.1%	-6.6%	-16.1%
2023FY	10.6%	0.7%	-2.4%	3.3%	2.9%	-7.2%	-0.5%	1.6%	6.2%	-1.8%	4.1%	3.1%	21.3%

Differences in performance between the Munro Climate Change Leaders Fund (unlisted fund) and MCCL (ASX quoted fund) relate to their respective inception dates, the buy/sell spread around the iNAV for MCCL, and the timing difference between the issuing of units during the day on the ASX for MCCL. This may result in reporting small differences in performance.

IMPORTANT INFORMATION: Past performance is provided for illustrative purposes only and is not a guide to future performance. Data is as at 30 June 2023 unless otherwise specified. GSFM Responsible Entity Services Limited ABN 48 129 256 104 AFSL 321517 (GRES) is the responsible entity of the Munro Climate Change Leaders ARSN 654 018 952 APIR GSF1423AU (Fund) (MCCL). GRES is the issuer of this information. Unit class A (MCCL) is an unlisted class of units in the Fund and Unit class E (MCCL.ASX) is an ASX Quoted class of units in the Fund. The inception date of MCCL is 29 October 2021, and the inception date of MCCL.ASX is 20 January 2022. Returns of the Fund are net of management costs and assumes distributions have been reinvested. Numbers may not sum due to rounding or compounding returns. The MSCI ACWI Index AUD refers to the MSCI All Country World Index Total Return Net Index in Australian Dollars. BPS refers to Basis Points. AOIs refers to Areas of Interest. EM refers to Emerging Markets (including China). This information has been prepared without taking account of the objectives, financial situation or needs of individuals. Before making an investment decision in relation to the Fund, investors should consider the appropriateness of this information, having regard to their own objectives, financial situation and needs and read and consider the target market determination (TMD) and the product disclosure statement (PDS) for the relevant class of units of the Fund. The MCCL TMD is dated 9 November 2022, the PDS and Additional Information Booklet are dated 10 December 2021, the MCCL.ASX PDS is dated 10 December 2021, these documents may be obtained from www.gsfm.com.au, www.munropartners.com.au or by calling 1300 133 451. None of GRES, Munro Partners, their related bodies or associates nor any other person guarantees the repayment of capital or the performance of the Funds or any particular returns from the Funds. No representation or warranty is made concerning the accuracy of any data contained in this document. This document is issued on 14 July 2023.

