GIB ASSET MANAGEMENT

Equity versus Credit:

Why we sold Nvidia in Q2 2023

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Combining thematic and valuation frameworks to uncover sustainable credit opportunities

As sustainability-focused investors, we support companies that aim to solve the world's greatest challenges and deliver cutting-edge technological innovation. At the same time, we're cautious of business models and sectors facing large capital expenditure either as the result of changing regulatory environments, the impacts climate change or other long-term headwinds.

"Okay, fine", you may be thinking, "so you're saying that the resulting portfolio will be overweight tech and underweight old economy issuers like commercial real estate?"

Without doubt, this would have been a favourable positioning in equities. We know this first hand, as it has been a significant positive contributor to the performance of GIB AM's Sustainable World Fund, which utilises the same overarching multi-thematic approach that underpins our investment process. Like our equity counterparts, the over-arching Themes and Sub-Themes help our team identify the long-term winners of shifting dollar spend. Fundamentally, this directs us to sectors benefitting from structural tailwinds.

Given the limited upside in credit, a systematic and disciplined focus on assessing sector-wide valuations via our Long Term Valuation Framework is crucial. While often areas of the market may appear challenged, this approach ensures we review the most attractive opportunities within each theme from a valuation perspective.

Once we have identified a sub-set of companies that we believe are under-valued, we then deploy bottom-up analysis, focusing on both financial resilience and sustainability factors, to identity the highest quality issuers and underlying instruments. We believe our approach is unique, as it allows us to utilise both our proprietary thematic work to identify tailwinds while relying on our valuation framework to ensure we don't overpay.

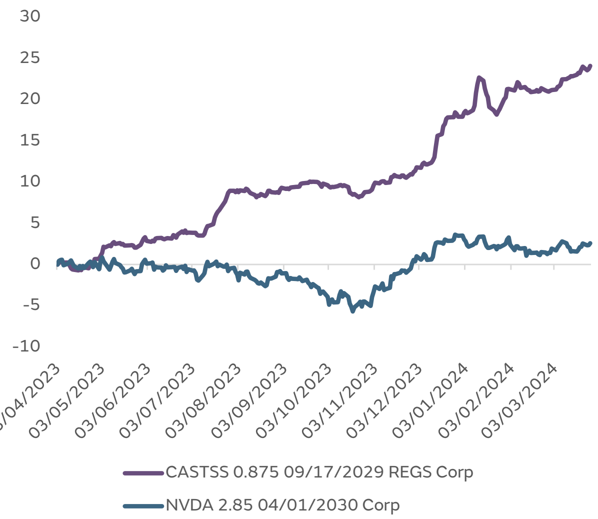
Let's take the example of Nvidia. We held Nvidia in 2022 and part of 2023 (see recent research on the Frontier Technologies sub-theme) but divested due to valuations looking tight when assessed over the long-term. Around the same time, we took a position in the Swedish Commercial Real Estate company, Castellum. Castellum is one of the largest listed property companies in the Nordics, managing and developing office and logistics real estate. The company owns prime and environmentally certified office buildings, predominantly in Sweden and is part of our Efficiency theme and Buildings sub-theme. Due to its high-quality portfolio and forward-looking sustainable focus, the company secured a significant capital increase in April 2023 and delivered an increase in like-for-like operating income of almost 9%. This is not bad, but modest compared to Nvidia's more than 100% revenue increase for 2023.

So how have the two credits performed?

Credit is the upside down world

Since we bought Castellum (2029 EUR bond) in early April 2023, this has generated a total return of 24.1% while Nvidia (2030 USD bond) has returned 2.6%[i]

Chart 1: Tech vs CRE: Castellum vs Nvidia



Source: Bloomberg 28.03.2024. Past performance is not a guide to future performance.

This discrepancy is not anecdotal: looking at the sector returns for the US Technology sector versus European Real Estate, the picture is similar, albeit less pronounced.

[i]We have here presented total return in local currency for simplicity. Excess return numbers in USD do not materially change the outcome: Excess return in USD for Castellum is 24.5% vs 4.8% for Nvidia. Period is April 3rd 2023 to March 27th.

Since April 3rd 2023, European Real Estate has returned 12.4%, whereas the US Technology index returned 3.5%. The top-down valuation focus helped us pick the right sector, and then the majority of the return resulted from picking the right issuer, i.e., the bottom-up process.

Don't overpay and do the bottom-up credit work

When investing in sustainable credit, it is crucial to let valuations drive your overall risk and sector allocation. Investing in sectors that are fundamentally challenged and generally shunned can be daunting. Yet, buying good companies in undervalued sectors can often yield some of the best returns in credit. We find that combining our Thematic and Valuation Frameworks, alongside our sustainability led bottom-up focus, enable us identify a host of attractive opportunities and limit downside risk.

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