RBC BlueBay
Asset Management

RBC European Equity Environmental, Social, & Governance Report 2025

Marketing communication

Contents

Introduction: looking forward and back

In last year's report, as with most years, the European Equity team attempted to give some sense of the themes that we considered most apposite for the upcoming twelve months. It would feel uncritical not to revisit our assumptions and review whether these themes came through, but also whether our concerns were upheld. As is often the case, it appears that we were correct in certain instances, but wide of the mark in others.

Geopolitical volatility was of critical concern to us given the number of elections being held across Europe, as well as the rest of the globe. To some extent this was an undemanding theme to highlight, but it was the nuance of these elections and how they would interact with Responsible Investing (RI) and Environmental, Social, and Governance (ESG) considerations from a corporate perspective that concerned us.

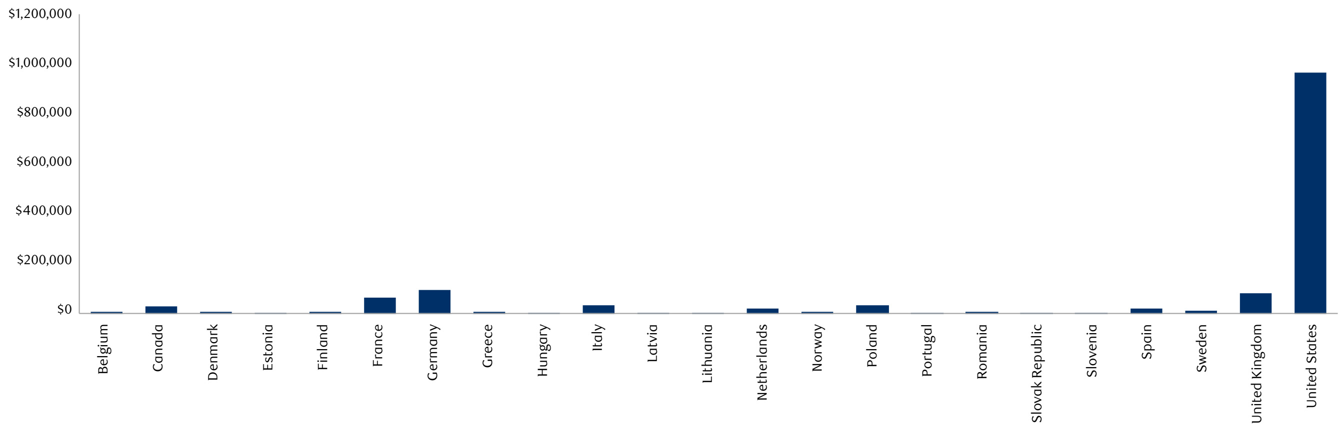
In truth, twelve months is too short a time horizon to draw truly considered conclusions, however there are two elements that are worth commenting on. The first was our analysis that ideological and political lines are blurred in a way unseen in decades; voters remained fixated on a mixture of individual issues, which political parties are utilising to draw in previously unreachable parts of the electorate. This, combined with pronounced anti-incumbent sentiment, resulted in stark instances of political adjustment in countries such as France and Germany within Europe, and the victory of President Trump in the US.

What has accompanied the unexpected elements of these geopolitical shifts is less surprising: the gathering backlash against what some constituents of society deem as the either unnecessary or overreaching nature of certain movements within the RI realm as well as broader net-zero targets.

While the US has seen the most overt instances of anti-ESG legislation, judicial intervention, and media rhetoric, Europe has seen a simmering of discontent regarding how individual country's decarbonisation journeys are interpreted as impinging on how people live their lives and the choices they make. Regardless of how much further this trend has to run, these debates are having profound effects not only on stock sentiment (particularly at an industry level) but also on CapEx as businesses fear political machinations undermining future or indeed existing investment.

Another element that was unexpected was the speed and scale of some companies reducing or scrapping certain targets, whether related to carbon emissions, packaging and plastics, or certain social targets. In some instances, these were done openly and in response to factors out of many management teams' control. However, there were others where, at least superficially, many investors were of the impression that these were opportunistic moves by corporates to take advantage of a less all-prevailing driving narrative. It is these second-order effects that we believe requires close monitoring over the next few years, as the most direct link between the real economy and the broader zeitgeist concerning ESG.

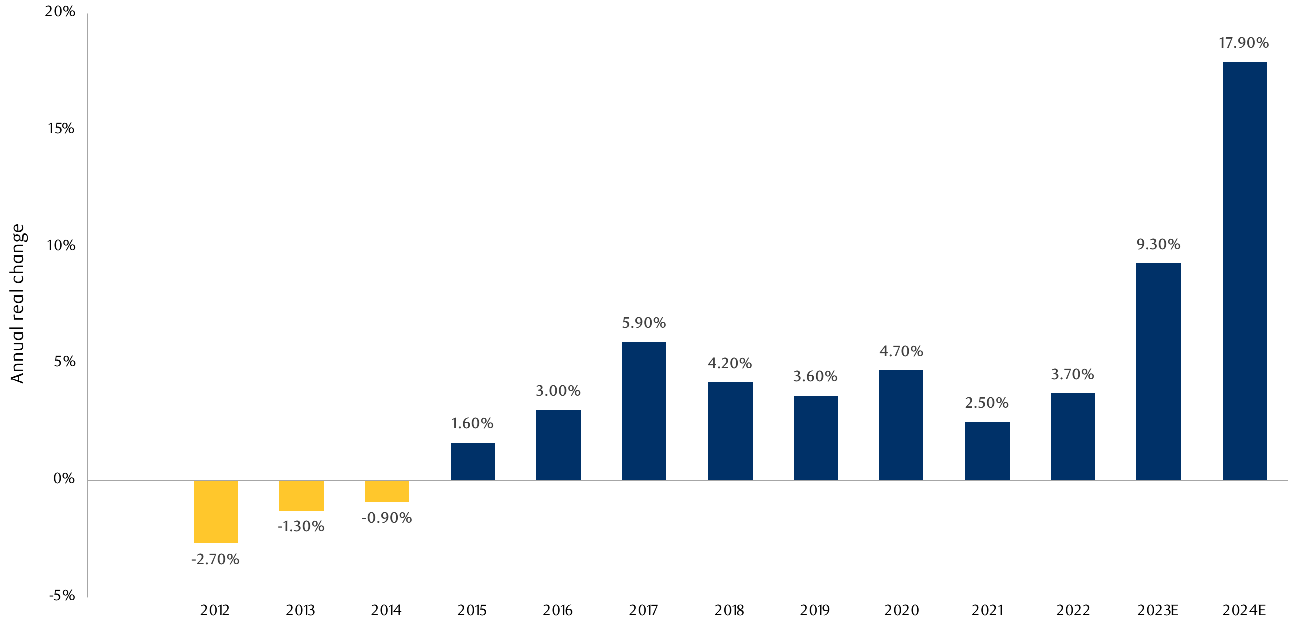
Figure 1: Defence expenditure (USD million)



Source: North Atlantic Treaty Organisation, as at 2024.

[1] NATO: Defence Expenditure of NATO Countries (2014-2024).

Figure 2: NATO Europe and Canada – defence expenditure (annual real change, based on 2015 prices and exchange rates)



Source: North Atlantic Treaty Organisation, as at 2024.

As we look forward there remains one key area of change for the European investment market, namely the Aerospace and Defence industry. Although a rising concern since Russia invaded Ukraine in 2022, questions over the place of Defence stocks, particularly within ESG strategies, have become both more urgent and complex. National defence spending is already rising fast in Europe, even before the Trump administration came into power, and this brings pressure to the bloc. It marks a departure from an "era of EU optimism" according to the European Defence Agency, and one that seems unlikely to change, even if the war in Ukraine were to end. With only 23 out of 32 NATO members spending 2% of GDP on defence, and Europe an average of 1.9% , any rise in the NATO target is likely to drive further investment in the space (Figures 1 and 2).

Although the narrative has shifted within Europe, and ESG investing is far from monolithic, the debate surrounding the place of defence names within RI remains a notable one. As the business profiles of Defence stocks continue to improve, corresponding with strong performance and increasing prominence within equity indices, it will be interesting to note whether the ownership of the industry expands from its current base. With governments keen to see further investment in the space, and order backlogs growing dramatically at a company level, it may be that the current geopolitical instability may serve to shift the narrative around defence in the same way that spiking oil prices changed the approach to the energy sector during 2021-2022.

> **"National defence spending is already rising fast in Europe, even before the Trump administration came into power, and this brings pressure to the bloc."**

Our ESG philosophy and process

Short-termism and a view from certain investors that ESG is a separate assessment criterion are both market weaknesses. We believe that ESG criteria should be considered in much the same way as traditional financial criteria in terms of their capacity to affect shareholder value and therefore long-term investment performance.

Some ESG criteria are more relevant to certain industries and sectors, and we therefore believe that investors cannot use a 'one-size-fits-all' approach to ESG analysis and integration. Investment screens can serve a useful purpose for investment managers who are required to screen-out or include certain sectors or activities. However, we believe that through a bottom-up process, without an over-reliance on external data, active managers making informed, explicit decisions on the consideration of material ESG factors can add significant value for investors.

"We believe that investors cannot use a 'one-size-fits-all' approach to ESG analysis and integration."

We look at companies through three lenses: Operational Quality, Competitive Advantages, and Material Issue Management (ESG). The last of these focuses on those ESG factors that we believe are most material and pertinent to the successful performance of the business being analysed. Rather than applying broad analytics, we prefer to look on a fundamental, bottom-up basis at those factors which, based on our proprietary material issue analysis and scoring, may have the greatest impact on a business's return profile. An example of how these factors may be analysed on a company-by-company basis is shown in Figure 3.

The results of this analysis are then integrated into our financial analysis and, ultimately, into the decision to invest – or not – in a business. We remain cognisant that including material ESG factors in our fundamental analysis not only serves as an excellent risk management tool but, just as importantly, can provide us with opportunities both at a corporate and portfolio management level. We believe that this mindset, married to our skillset as active managers, is how we can benefit our investors in the long run.

Figure 3: RBC GAM European Equity investment process: Material issue management (ESG)

Category	Luxury goods - Company A	Capital goods - Company B
Leadership and goverance	▪ Board composition ▪ Executive compensation ▪ Management quality ▪ Disclosure	▪ Board composition ▪ Executive compensation ▪ Management quality ▪ Disclosure
Social capital	▪ Product quality and safety ▪ Data security	▪ Product quality and safety
Human capital	▪ Labour practices	▪ Employee health and safety
Business model and innovation	▪ Supply chain management ▪ Materials sourcing and efficiency	▪ Product design and lifecycle management ▪ Materials sourcing and efficiency
Environmental	▪ Water and wastewater management ▪ Energy management	▪ Energy management ▪ GHG emissions

--- Changing factors in our ESG risk management research

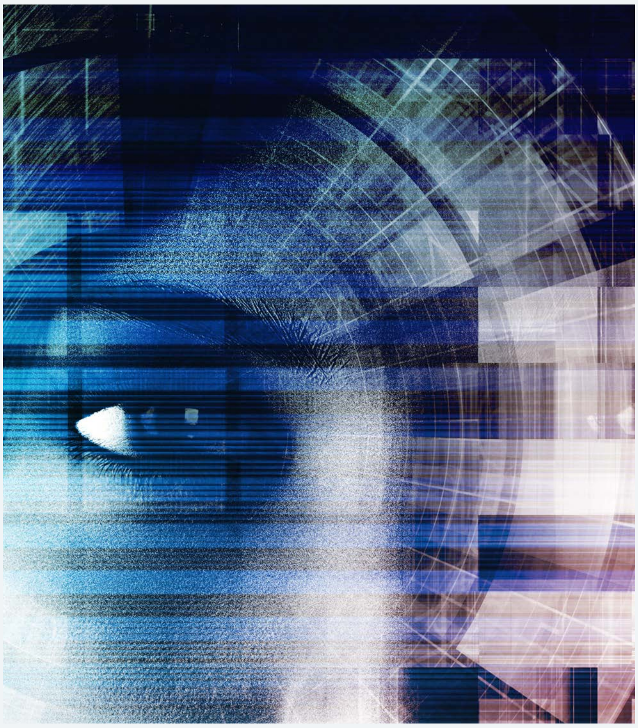
Source:RBC GAM, as at December 2024.

Portfolio ESG themes and events in 2024

Capturing a clean opportunity

Technip Energies led a consortium including GE Vernova and Balfour Beatty to win a major contract for the Net Zero Teesside Power project in the UK. This groundbreaking project aims to be the first gas-fired power station in the world with carbon capture and storage technology, aiming to capture up to two million tonnes of carbon dioxide per year[2]. This is one of the many projects and partnerships Technip announced during the year, as it continues to use its engineering expertise to help develop and deploy sustainable energy solutions.

"This groundbreaking project aims to be the first gas-fired power station in the world, with carbon capture and storage technology, aiming to capture up to two million tonnes of carbon dioxide per year."



Brain food

Kerry announced a partnership with APC Microbiome Ireland from University College Cork to explore the impacts of diet on cognitive health. The company will leverage biotic technologies expertise to help develop novel solutions focused on the gut-brain axis, which could help with difficulties associated with stress, anxiety, and mood. This will help expand Kerry's ProActive Health catalogue that uses science-backed solutions in consumer products to help promote digestive health, immune health, cognitive health, women's health, and infant health[3].

Listening to the health needs of customers

Essilor Luxottica unveiled its Nuance Audio product, which are fashionable glasses with advanced hearing technology built in. After spending years developing iconic eyewear solutions to help address serious health issues, while reducing the stigma associated with wearing prescription glasses, the company is looking to do the same for hearing loss. Many reject hearing aids because they feel insecure wearing them, and this product can help pave the way to increased adoption of hearing loss solutions[5].

Cooling AI's energy consumption

Schneider Electric announced new solutions to help reduce the energy usage required for AI development. The company co-developed a new data centre reference design with Nvidia to streamline planning and deployment for liquid-cooled, high density AI clusters, using the most energy-efficient infrastructure. It also introduced the Galaxy VXL uninterruptible power supply, which is the most compact, high-density solution designed for AI. With 52% space saving and high-power density, the company will deliver the most efficient solution in a smaller, high-density footprint[4].

Intelligent defence

Experian announced a partnership with Sardine to enhance its fraud prevention product offering with behavioural biometrics and devise intelligence-base fraud prevention technology. As online attacks become more advanced with the use of GenAI deep fakes, bots, and mobile emulators, companies must intensify their Know Your Client and anti-money laundering efforts to prevent fraudulent activity. The technology deployed allows users to track and analyse every customer interaction throughout their journey to identify suspicious activity, while also reducing false positives[6].

2 Technip Energies and GE Vernova awarded a major contract for the Net Zero Teesside Power project.
3 Kerry Partners on biotics with leading microbiome research centre.
4 Schneider Electric announces new solutions to address the energy and sustainability challenges spurred by AI.
5 CES 2024 | EssilorLuxottica.
6 Experian UK&I marks next step in fraud prevention with Sardine partnership.

A future solution?
GLP-1s and their potential impacts beyond weight loss

When Novo Nordisk's Wegovy hit the US market in 2021, its impact was immediate and dramatic. Propelled by viral social media posts and celebrity endorsements, the demand for the drug soared to levels almost unprecedented in medicine, mirroring a frenzy typically associated with limited edition sneaker releases. Such fervour led to widespread shortages of Wegovy and its sister diabetes drug, Ozempic. These shortages were a testament to the public's eagerness for new solutions. Yet, the true potential of Wegovy, and drugs akin to it, extends beyond the sphere of weight loss. Here, we examine the far-reaching implications these treatments may hold for broader society and the economy at large.

Diabetes prevention: a proactive approach

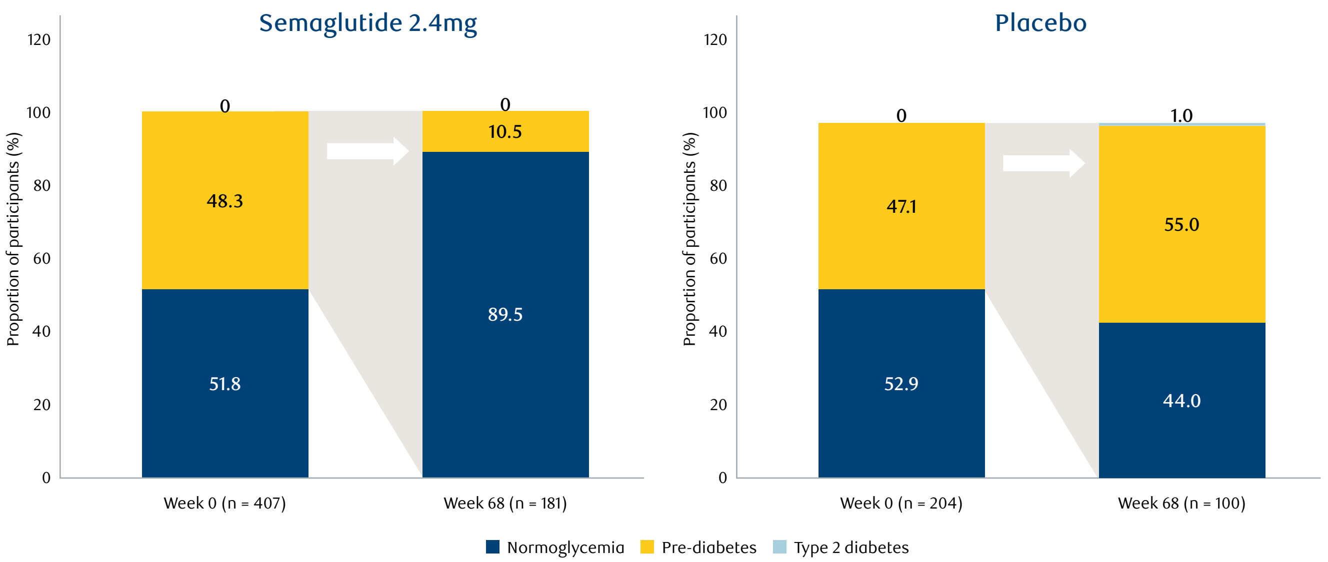
Type 2 diabetes (T2D) is a global health crisis, affecting over half a billion individuals worldwide and posing a substantial burden due to its complications, healthcare costs, and increasing prevalence. In response to this escalating challenge, GLP-1 receptor agonists (GLP-1RAs) have emerged as a transformative force in the treatment of T2D. Their rise to the forefront as the preferred first-line therapy is attributed not only to their exceptional glucose-lowering effects but also to their ability to substantially reduce the risk of serious complications.

These drugs have proven crucial in decreasing the incidence of cardiovascular events[7] and slowing the progression of kidney disease[8], two of the most severe and frequent comorbidities associated with diabetes.

"Type 2 diabetes (T2D) is a global health crisis, affecting over half a billion individuals worldwide and posing a substantial burden due to its complications, healthcare costs, and increasing prevalence."

This advance in treatment is particularly critical at the pre-diabetes stage, which affects around half a billion people globally. GLP-1RAs have made a profound impact here, with medications like Ozempic and Mounjaro cutting the risk of developing T2D by 76% and 93%, respectively[9] (Figure 4). Their increasing accessibility heralds a shift in healthcare strategy, akin to the revolution brought about by statins in cardiovascular disease prevention.

Figure 4: Reduction in pre-diabetes levels



Source: Effect of semaglutide on regression and progression of glycemia in people with overweight or obesity but without diabetes in the SELECT trial | Diabetes Care | American Diabetes Association, as at June 2024.

7 Semaglutide and cardiovascular outcomes in patients with Type 2 diabetes | New England Journal of Medicine.
8 Effects of semaglutide on chronic kidney disease in patients with Type 2 diabetes | New England Journal of Medicine.
9 Effect of semaglutide on regression and progression of glycemia in people with overweight or obesity but without diabetes in the SELECT trial | Diabetes Care | American Diabetes Association, Tirzepatide for obesity treatment and diabetes prevention | New England Journal of Medicine.

By proactively addressing T2D and its associated comorbidities, GLP-1RAs are poised to significantly reduce the economic and health burdens of diabetes. The annual global health expenditure due to diabetes is close to USD1 trillion[10]. The enhanced adoption of GLP-1RAs reflects a transformative shift in diabetes management, with the promise of broader public health benefits and economic savings.

Neurodegeneration: a new frontier

The potential applications of GLP-1RAs may extend beyond obesity and diabetes, as burgeoning research hints at their relevance in treating neurodegenerative conditions like Alzheimer's disease (AD). A debilitating and increasingly prevalent disease due to ageing populations, it represents a substantial societal burden. The interest in GLP-1RAs for AD arises from the observed connection between metabolic dysfunction and neuroinflammation, both hallmarks of AD. Furthermore, the disease's correlation with diabetes is so strong that some experts refer to Alzheimer's as 'Type 3 diabetes,' drawing parallels with insulin resistance, a common thread in both conditions.

The indirect evidence linking GLP-1RAs to potential benefits in AD is noteworthy. One observational study analysing electronic health records in the US discovered that patients with T2D who were prescribed Ozempic experienced a 67% reduction in the risk of receiving an Alzheimer's diagnosis compared to those on other diabetes medications[11]. Additionally, a meta-analysis of randomised controlled trials (RCT) indicated that T2D patients treated with Ozempic had a 53% lower risk of developing dementia than those receiving a placebo[12].

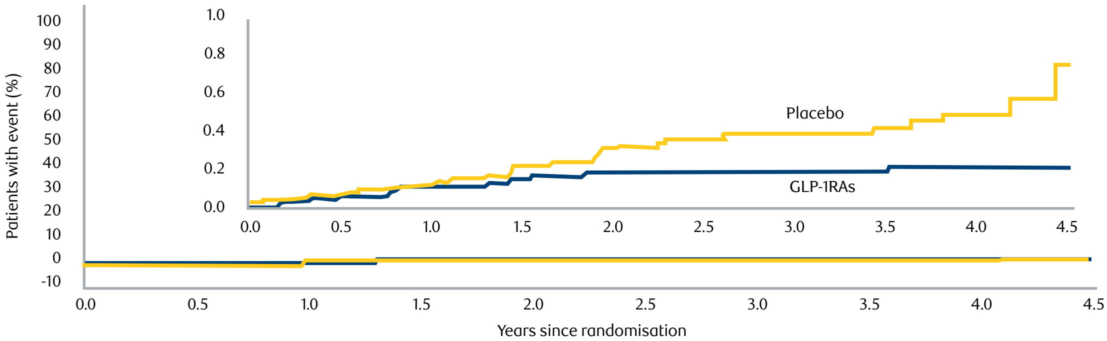
Furthermore, in a clinical trial involving an earlier generation GLP-1RA administered to AD patients, those on the GLP-1RA therapy showed better preservation of cortical volume and cognitive function relative to the placebo group (Figure 5).

The ongoing phase 3 Evoke and Evoke+ trials by Novo Nordisk are particularly noteworthy. These studies are focused on assessing the effects of oral semaglutide, the active ingredient in Ozempic and Wegovy, on the progression of early-stage AD. The potential of GLP-1RAs to provide a more tolerable treatment option compared to the current intravenous therapies, which are often associated with significant side effects, is a promising development in the field. The outcomes of these trials could have a significant impact on shaping future treatment approaches for AD.

"Should clinical trials validate the effectiveness of GLP-1RAs in altering the progression of AD, it could represent a significant therapeutic breakthrough for patient care."

As the medical community anticipates the outcomes of the Evoke and Evoke+ trials, the potential application of GLP-1RAs as a preventive approach to AD is under consideration. Their generally well-tolerated side effect profile, coupled with an increasing body of evidence supporting their role in the prevention of T2D and other chronic diseases, positions these drugs as candidates for further study. Should clinical trials validate the effectiveness of GLP-1RAs in altering the progression of AD, it could represent a significant therapeutic breakthrough for patient care.

Figure 5: Difference in rate of dementia diagnosis on GLP-1RA in RCT compared to placebo



Number at risk										
GLP-1 RA	7,907	7,852	7,763	6,479	6,064	4,441	4,373	4,312	1,716	483
Placebo	7,913	7,843	7,740	6,438	6,016	4,394	4,321	4,251	1,700	460

Source: N rgaard et al. 2022.

[10] Global increase in diabetes prevalence imposes a substantial health and economic burden | Journal of Health Economics and Outcomes Research
[11] Associations of semaglutide with first-time diagnosis of Alzheimer's disease in patients with Type 2 diabetes: Alzheimer's & Dementia - Wiley Online Library.
[12] Treatment with glucagon-like peptide-1 receptor agonists and incidence of dementia: Alzheimer's & Dementia: Translational Research & Clinical Interventions - Wiley Online Library.

Substance use disorders: GLP-1RAs as a novel therapeutic avenue

Substance use disorders represent a critical challenge for public health systems worldwide. Characterised by compulsive use, high relapse rates, and significant societal impact, these disorders require innovative treatment strategies. GLP-1RAs are emerging as a potentially transformative tool in this battle.

Recent studies illuminate the promise of GLP-1RAs in reducing the incidence of behaviours associated with substance use disorders. Notably, T2D patients on GLP-1RAs such as Ozempic exhibited a 32% reduction in tobacco use requiring medical intervention compared to those receiving insulin treatments[13]. The benefits may be even more substantial in the context of opioid use, with GLP-1RAs linked to a remarkable 42-68% decrease in the risk of overdose[14].

The impact of GLP-1RAs extends to alcohol use as well. Research indicates a 29% reduction in alcohol consumption among individuals treated with these agents[15]. Moreover, neuroimaging studies suggest that GLP-1RAs may attenuate the neural response to alcohol cues in regions like the ventral striatum and septal area, which are implicated in addiction and relapse. This finding hints at the potential of GLP-1RAs to diminish the allure of alcohol and support recovery.

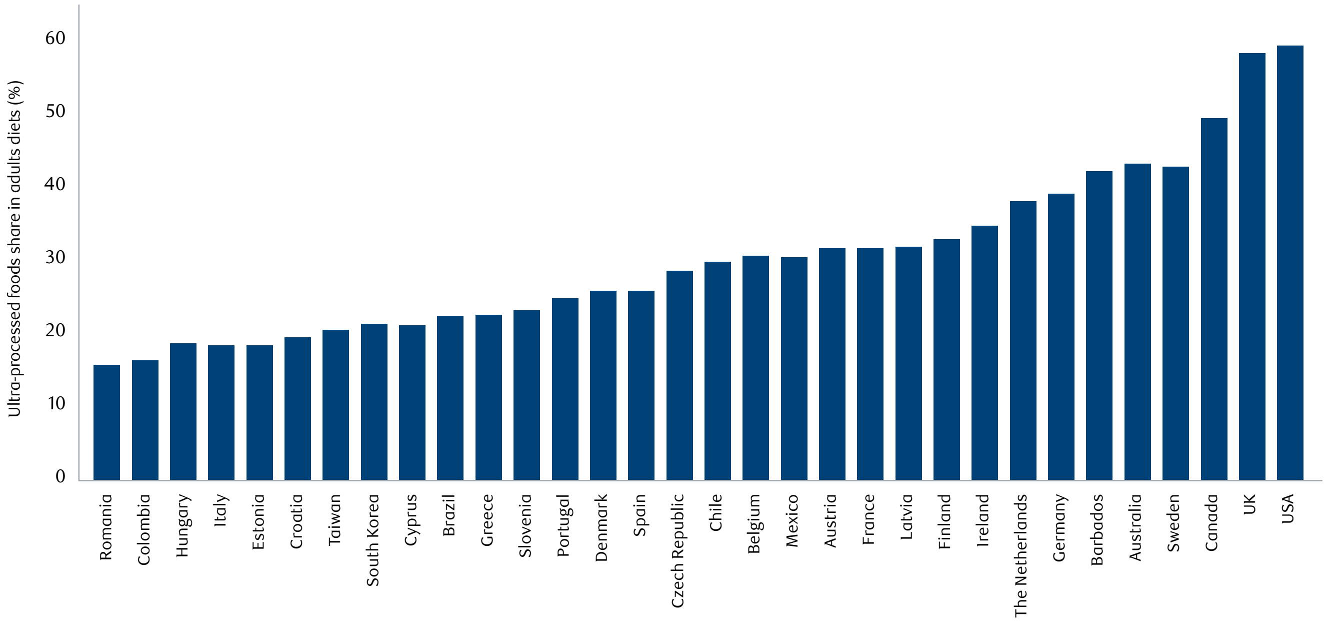
Ongoing clinical trials are further exploring the effects of GLP-1RAs on alcohol consumption and alcohol-related liver damage. Given the established efficacy of these drugs in non-alcoholic liver disease, there is a hopeful prospect that GLP-1RAs could serve as a universal therapeutic for various forms of liver injury. As the evidence base expands, the role of GLP-1RAs in managing substance use disorders could revolutionise treatment paradigms, offering new hope for those grappling with addiction and reducing the broader societal and economic impacts of these disorders.

GLP-1RAs: the quiet catalyst of societal change

The influence of GLP-1RAs is set to extend well beyond personal health, potentially marking the start of a subtle but significant shift in societal behaviours. What we are observing is the emergence of a medication-induced evolution, one that could gently recalibrate economic patterns, reshape consumer industries, and subtly redefine our collective relationship with food and health.

Envision a near future where the widespread use of GLP-1RAs nudges the public towards healthier choices, not through forceful disruption but through a gradual reorientation of preferences. By steering consumers towards more nutritious alternatives, this shift has the potential to pose challenges for the ultra-processed food industry, which is responsible for more than 50% of the calorie intake in the UK and US (Figure 6).

Figure 6: The share of ultra-processed foods in diets varies greatly among countries worldwide



Source: Ultra-processed foods and cardiometabolic health (BMJ), as at October 2023.

[13] Association of semaglutide with tobacco use disorder in patients with Type 2 diabetes: PubMed.
[14] Treatment with glucagon-like peptide-1 receptor agonists and incidence of dementia: Alzheimer's & Dementia: Translational Research & Clinical Interventions - Wiley Online Library.
[15] Association between glucagon-like peptide-1 receptor agonists use and change in alcohol consumption: a systematic review - eClinical Medicine.

Food industry giants are already positioning themselves to adapt to this new wave of health consciousness. Nestle's Vital Pursuit and ADMs venture into GLP-1 companion products are early signs of a market adapting to the nuanced demands of a health-aware consumer base. The same advanced fermentation techniques that produce GLP-1RAs are also being harnessed to create nutrient-rich foods, aligning dietary trends with medical innovation.

This is not an overnight revolution but a gradual reformation, where the impact of GLP-1RAs could be likened to a steady reshaping of the current landscape, rather than a sudden deluge. The potential for these medications to influence a broad range of behaviours holds the promise of a healthier society, with economic and social implications that, while not immediately dramatic, could be deeply transformative over time.

Conclusion

In conclusion, the journey of GLP-1RAs from diabetes care to obesity management underscores the remarkable versatility of this class of molecules. With the potential to further impact conditions such as AD and substance use disorders, GLP-1RAs stand at the forefront of a potential shift in therapeutic applications.

The potential of these drugs extends to wider societal benefits, including reduced healthcare costs and improved quality of life for individuals with chronic conditions. The ripple effects could be seen in the diminishing prevalence of lifestyle-related diseases and the associated economic burden on society. As we anticipate the outcomes of ongoing trials, the promise of GLP-1RAs to foster a healthier society becomes ever more apparent, marking a significant step towards a future where proactive healthcare and preventive measures are the norm. The full impact of GLP-1RAs on global health and society remains to be seen, but the possibilities are as broad as they are profound.

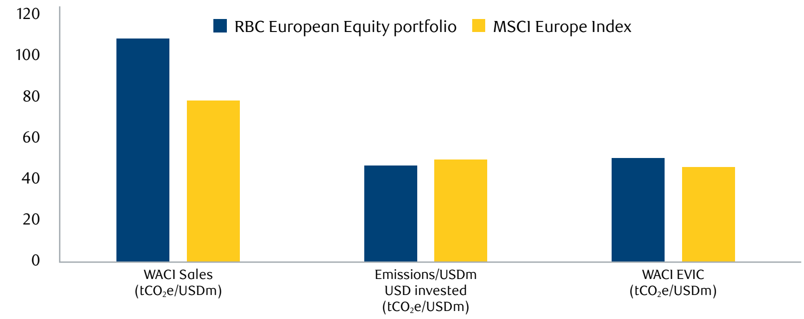
"The promise of GLP-1RAs to foster a healthier society becomes ever more apparent, marking a significant step towards a future where proactive healthcare and preventive measures are the norm."

Portfolio ESG analysis

Carbon

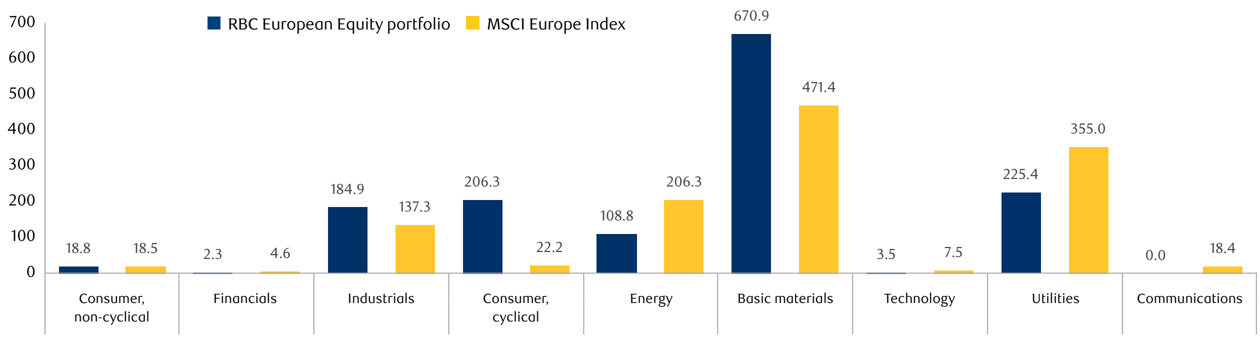
Our portfolios continue to exhibit lower carbon emissions intensity than the broader benchmark for some metrics, although not for weighted average carbon intensity. While we do not have a specific target related to these metrics, they are considered as an additional data input to our fundamental, bottom-up research in constructing investment cases for individual companies as well as the construction of our portfolios as a whole.

Figure 7: Carbon emissions analysis



Source: Source: RBC European Equity Fund versus MSCI Europe Index. RBC GAM analysis based on MSCI Climate Change Research, as at 31 December 2024, , MSCI®.
*Reflects most recently-available data for each company on the date of running the report. WACI stands for Weighted Average Carbon Intensity.

Figure 8: Sector weighted average carbon intensity (sales), tCO2 e/USD$M sales



Source: RBC European Equity Fund versus MSCI Europe Index. RBC GAM analysis based on MSCI Climate Change Research, as at 31 December 2024, MSCI®.

Relative ESG ratings

With Europe the highest scoring ESG region in the world when it comes to corporate-level sustainability, as defined by Morningstar, we note that the portfolio continues to score well on a relative basis[16]. However, we are aware of the limits of external third-party vendor scores so, as with our carbon intensity, we place more value on our fundamental processes, although we believe that this data provides a useful sense check to our work.

Figure 9: RBC GAM European Equity ESG scoring

MSCI ESG scoring							
Overall ESG score - portfolio	Overall ESG score - peers	Environment - portfolio	Environment - peers	Social - portfolio	Social - peers	Governance - portfolio	Governance - peers
8.3	N/A	6.6	6.4	5.2	5.3	6.9	6.6

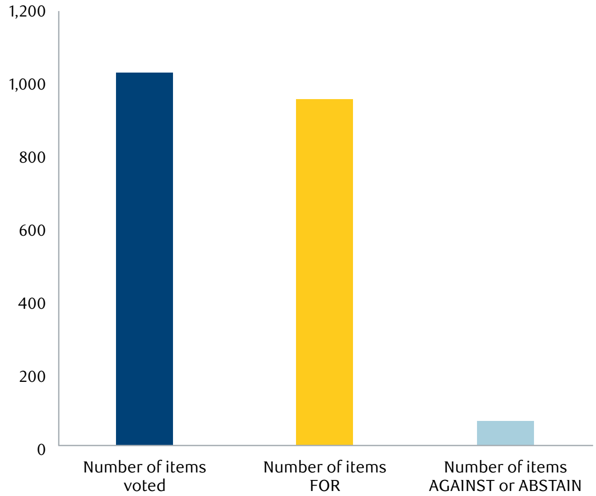
Source: RBC GAM analysis based on MSCI ESG Research, as at 31 December 2024 MSCI®. MSCI data shows the relative scores of the RBC European Equity strategy versus those of MSCI peers, 'Equity Europe'.

[16] Morningstar/Sustainalytics Sustainability Atlas, April 2024.

Voting record

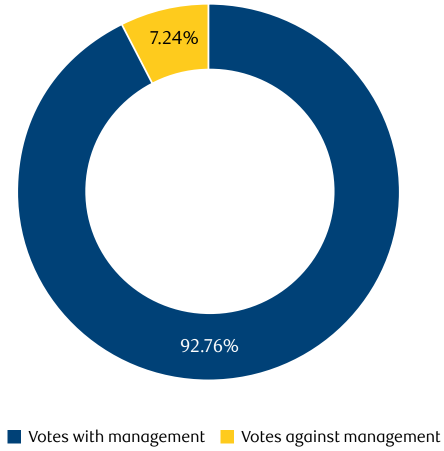
Proxy voting remains an important tool for us alongside our engagement with management. While RBC GAM has a set of custom Proxy Voting Guidelines for many markets[17], in Europe, RBC GAM uses the local proxy voting guidelines of a research provider. We work closely with the Responsible Investment (RI) team to review every ballot item and ensure that proxies are voted in accordance with best practices in corporate governance and in the best interests of our clients, with a view to enhancing the long-term value of securities that are held. The proxy voting process ensures that we make voting decisions based upon our deep knowledge of the companies that we invest in, while benefiting from the ESG expertise of the team.

Figure 10: 2024 proxy voting record



Source: RBC GAM. Data as at December 2024.

Figure 11: European Equity team votes (% of total)



Source: RBC European Equity strategy. Data as at December 2024. Total may not add to 100% due to rounding.

In 2024, as in previous years, our percentage of votes in support of management sits at just over 90%. With an investment philosophy grounded in investing in excellent companies, run by management teams we both understand and trust to increase the long-term value of the businesses, we would expect this number to remain high. Despite this, however, we are always prepared to vote against management when we deem it necessary.

[17] Proxy Voting Guidelines.

2024: notable corporate engagements

Redeia

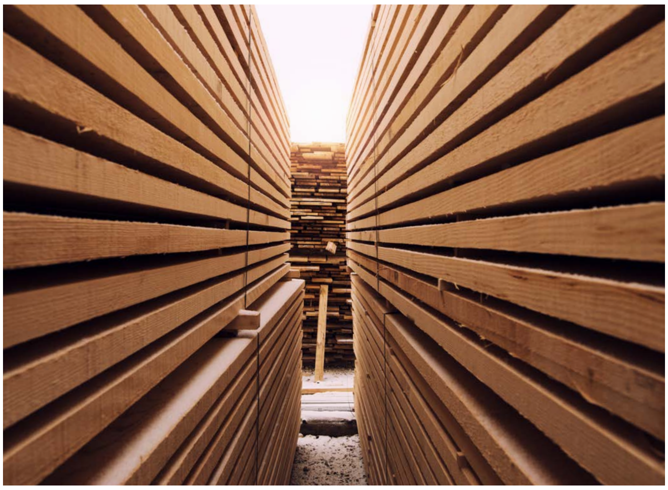
The CEO explained how the company is playing a key role in enabling Spain's transition to renewables through the development of the Spanish electricity transmission grid. The country's government is making its emissions reduction targets and renewable energy targets more aggressive. The company also sees potential to help the rest of Europe decarbonise through interconnector projects, such as the Bay of Biscay project, which will enable the exchange of electricity between Spain and France. It is actively investigating further interconnector projects, which will come online in the 2030-34 timeframe.

Alimak

We discussed a tragic accident in Stockholm that occurred late last year that resulted in a fatality while someone was using the company's equipment. Safety is fundamental to its business. The initial investigation from the incident found it did not occur due to a fault with the equipment, but the company using the equipment did not install it properly as it failed to bolt it in two places. Alimak ran crisis management straight after the incident and was quick to work with authorities where needed. An incident like this has never occurred before, but the company is now working as a group to see how it can make customers more aware. This could be done by potentially giving bolts different colours or digitalising them so installers must make sure they are being bolted in.

DNB

Given some recent issues in the UK market with the mis-selling of motor finance products, we asked the company about customer duty and the proper use of customer data. Given the collection of customer data, it could be quite easy for DNB to use the data to cross-sell products in other areas. The bank reiterated the fact that it is not allowed to do "forced" cross-selling, including repackaged products. Consent is based on data usage and requires customers to opt-in before they can interlink products. Regulators are aware of the digital movement, but it clearly shows deep rooted disdain for repackaged products, so the company is making sure it is not misusing the customer data to avoid treating customers unfairly and finding itself under scrutiny.



Howden Joinery

We conducted a site visit with the company. We visited one of their depots and it was clear there was an engaged workforce, with some employees having been there for over 25 years and an average tenure of more than 11 years. We also visited one of the main distribution centres, where the company hasn't had a lost time incident in seven years. It has implemented a continuous improvement program on a variety of safety measures and has used employee input to make improvements where necessary. We were also able to speak to members of the operations team who went through some of the initiatives the company is undertaking to reduce its carbon footprint in distribution. From an inbound supply point it brings in 95% of its European supplies via rail to reduce carbon footprint. The company also now has 15 LNG trucks and two EV trucks in its fleet, and is looking to expand this to reduce emissions in its outbound logistics as well.

BE Semiconductor

We met with the CEO of Besi, who has built this company over the last 30 years, as there are key man risk concerns given he is now over 70 years old. The company has a 40-person management team and two product groups with ownership within the group. He thinks they are set up well for when he decides to retire. His goal is to create an independent company for the indefinite future. He helped ease our concerns around succession risks, and we believe the company is built to last when he decides to retire.

"The company also sees potential to help the rest of Europe decarbonise through interconnector projects, such as the Bay of Biscay project, which will enable the exchange of electricity between Spain and France."

Our recent ESG research and articles

We produced a number of papers and articles on important ESG topics in 2024. As ESG becomes both broader in scope and more widely accepted, so we have increasingly delved deeper into areas that may in the future prove important in this regard.

Japan: a new dawn?

During an episode of our Sustainability Podcast, Freddie Fuller and David Soh, Head of Research on the Asian Equity desk in Hong Kong, discussed recent changes in Japan's economic and corporate landscape, especially in relation to corporate governance. They noted that Japan's main stock market index has surpassed its all-time high from the late 1980s, indicating a shift in investor sentiment towards Japanese equities. This change is attributed, in part, to improvements in corporate governance in Japan, drawing parallels with Europe where strong governance has historically been a tailwind for the region's performance.

David discussed how Japan faced numerous challenges after the real estate bubble burst in the late 1980s, including a heavily indebted economy, unfavourable demographics, and a deflationary environment. However, from around 2021 or 2022, and particularly in 2023, the TOPIX and Nikkei indices began reaching new highs. The pandemic served as an exogenous shock that helped pull Japan's economy out of decades of deflation.

A significant shift is occurring within Japanese corporate governance, with companies paying more attention to profitability and competitive positioning on a global scale. The traditional 'three walls of hierarchy' in Japanese corporate culture are being challenged due to global inflation and domestic labour shortages. The government is actively seeking to attract foreign capital and has taken measures to improve the business environment for overseas investors, including hosting the UN PRI in Person 2023 conference in Tokyo. David also highlighted the Tokyo Stock Exchange's initiatives, such as the "PBR1x" campaign and the PRIME Index, which aim to encourage companies to enhance capital efficiency and highlight top value-creating companies. Additionally, Japan's NISA program is designed to incentivise retail investors to move their savings from cash into equities.

Despite these positive developments, a valuation gap remains, with Japanese equities trading at lower price-to-book ratios compared to their US and European counterparts. This is particularly evident among companies in the TOPIX index that continue to trade below book value. The conversation concluded with the observation that these changes, particularly in governance, may present a compelling case for diversification away from the US market for North American investors.

Read more here

Responsible investing: a landscape of bright spots and shadows

In another episode of our podcast, Freddie Fuller had a conversation with Melanie Adams, Head of Responsible Investment at RBC GAM. They discussed the varying landscapes of responsible investing in North America and Europe, particularly focusing on regulatory and societal trends in 2024.

Melanie highlighted that North America's approach to RI and ESG differs significantly from Europe's. In Canada, regulations have increased, emphasising transparency rather than prescriptive disclosures. The philosophy is to encourage asset managers to be clear about their ESG integration and exclusion criteria without mandating specific data disclosure. However, there continues to be movement, with the International Sustainability Standards Board (ISSB) standards being considered for adoption in Canada (referred to as the CSSB).

The US, in contrast, has experienced a backlash against ESG, with allegations of antitrust activities linked to some collaborative initiatives (such as Climate Action 100+). In some cases, these allegations have led to increased scrutiny and the departure of some participants. States have raised concerns about potential boycotts of certain industries, leading to a challenging environment for asset managers to navigate while maintaining their fiduciary duty.

Melanie also commented on the differences between the US and Canada, noting that Canada has not experienced the same level of ESG backlash. She mentioned that while Canada has a significant energy sector which has been under environmental scrutiny, there is a general sentiment that risks need to be assessed and managed appropriately.

Looking ahead to 2025, there was a prediction of a continued divergence between the regulatory approaches in Europe and the US. We anticipate more "greenhushing" or ESG-hushing, where companies may become less forthcoming with their policies and practices. Melanie emphasised the importance of asset managers engaging with issuers to understand their policies fully.

In Europe, more regulation is expected, particularly with the new version of the Sustainable Finance Disclosure Regulation (SFDR) and other related regulations. Pushback from market participants due to the burden of additional reporting has also suggested that governments may reassess regulatory complexity to ensure it adds value and aids understanding of sustainability risks and opportunities.

They concluded by acknowledging the challenges ahead for corporates and asset managers, with a focus on the need for meaningful reporting and the risks of over-regulation potentially deterring investment in Europe. They agreed that the next 12 months will be interesting, with substantial changes expected in corporate sustainability targets and investment strategies.

Listen to the podcast here

Should politics matter for European investors?

In this article, Freddie Fuller explored the significance of political factors for European investors and the impact of politics on European equities.

The article highlights a common criticism of European equities: their perceived vulnerability to political shifts. However, it points out that European companies often generate a significant portion of their revenue from international markets, which diminishes the impact of domestic political changes on their performance. For instance, European firms earn over 55% of their revenues abroad, with emerging markets contributing 30% of total European revenues[18]. This international exposure suggests that European stocks may be less tied to the continent's politics and more to global economic trends.

Despite this, it is acknowledged that recent years have seen increased state intervention in Europe's economy, following crises like the financial meltdown of 2008, sovereign debt issues, and the pandemic. This resurgence of state involvement presents both risks and opportunities for businesses.

The key point explored involves the evolving European political landscape, where voters are increasingly influenced by specific issues rather than traditional left-right ideologies. Five key concerns were identified: the climate emergency, the migration crisis, economic turmoil, the war in Ukraine, and the pandemic. The way political parties address these issues is shaping electoral outcomes across Europe, with the electorate becoming more issue focused. This shift is evidenced by the varied success of far-right parties, which have capitalised on individual issues such as the economy and migration.

In summary, while European equities are influenced by international rather than domestic revenues, suggesting a degree of insulation from European politics, the changing nature of state intervention and the electorate's focus on specific issues indicate that politics still matters to investors. Political developments can affect market perceptions and investor confidence, making it a factor that cannot be entirely disregarded by European investors.

Read more here

Conclusion

We believe that ESG issues will continue to permeate areas of the investment, regulatory and corporate landscapes for the foreseeable future, often in surprising ways. Themes will wax and wane, but we stand firm in our belief that investing in the best companies that pay attention to the fundamentals of ESG – in the way that they run their businesses – will continue to contribute to robust returns for investors. In the meantime, we continue to assess and evolve our own views and processes to ensure that we can be as ahead of the curve as possible on behalf of our own clients.

[18] Morgan Stanley, Global Exposure Guide, 2023.

Authors

Freddie Fuller

Product Specialist

12 years of experience

Diploma in Investment Management (ESG) (2020); IMC (2013); BA (English Literature and Language) (2012), University of Leeds, UK.

Freddie is a product specialist on the European and International Equities team at RBC GAM. Prior to joining the organization in 2018, Freddie was head of Investment Oversight for the London local authorities' collective investment vehicle. In that role, he oversaw the pooling and management of up to £35 billion of pension strategy assets, with a focus on investment analysis, manager selection and oversight. Freddie had earlier worked at an investment management company and a large British multinational investment bank. He started his career in the investment industry in 2013.

Lukas Harrison, CFA

Portfolio Manager

13 years of experience

CFA (2015); CIPM (2014); BComm (Finance) (2011), Carleton University, Canada.

Lukas is a Portfolio Manager on the European Equities team at RBC GAM. In this role, he is responsible for coverage across the European equity universe, with an emphasis on mid-cap securities. Lukas joined his current team in 2017, having earlier worked as part of RBC GAM's performance team in London and as a performance analyst in Canada since joining the firm in 2012, which is when he started his career in the investment industry.

Ola Ayeko

Analyst

5 years of experience

Master of Research in Bioengineering from Imperial College, London; BA (Preclinical Medicine), University of Oxford.

Ola is an analyst on the RBC European Equities team at RBC GAM. In this role, he is responsible for coverage across the European equity universe, with an emphasis on Pharma, TMT, Utilities, and Capital Goods equities. Prior to joining the organization in 2023, Ola worked as an equity research associate at a global asset management firm, which is where he started his career in the investment industry in 2020.

Holdings as at 31 December 2024. Carbon Intensity is calculated tonnes/$1million USD in Sales. Emissions data year is latest on record from MSCI ESG. Includes Scope 1 + 2 emissions. Where an issuer does not report its own emissions, MSCI ESG provides a proprietary estimate. This report contains information (the “Information”) sourced from MSCI Inc., its affiliates or information providers (the “MSCI Parties”) and may have been used to calculate scores, ratings or other indicators. The Information is for internal use only and may not be reproduced/redisseminated in any form, or used as a basis for or a component of any financial instruments or products or indices. The MSCI Parties do not warrant or guarantee the originality, accuracy and/or completeness of any data or Information herein and expressly disclaim all express or implied warranties, including of merchantability and fitness for a particular purpose. The Information is not intended to constitute investment advice or a recommendation to make (or refrain from making) any investment decision and may not be relied on as such, nor should it be taken as an indication or guarantee of any future performance, analysis, forecast or prediction. None of the MSCI Parties shall have any liability for any errors or omissions in connection with any data or Information herein, or any liability for any direct, indirect, special, punitive, consequential or any other damages (including lost profits) even if notified of the possibility of such damages.

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