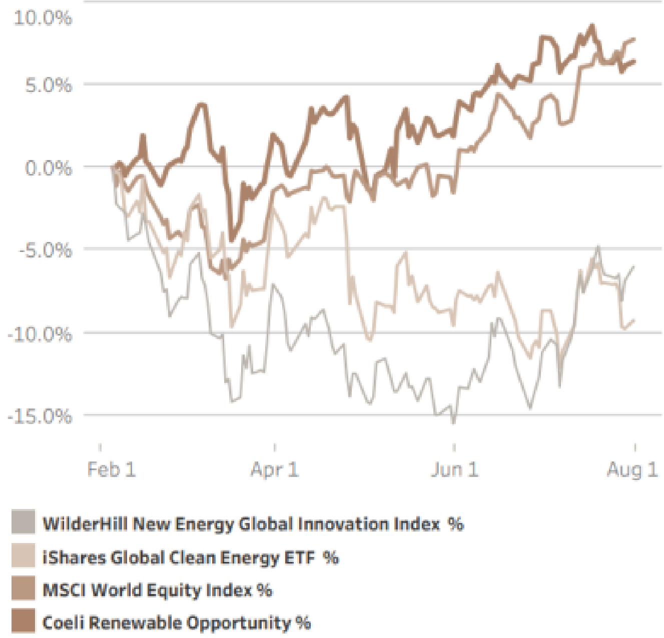
Coeli Renewable Opportunities Monthly Report July 2023 (I USD)

This material is marketing communication.

Note that the information below describes the share class (I USD), which is a share class reserved for institutional investors. Investments in other share classes generally have other conditions regarding, among other things, fees, which affects the share class return. The information below regarding returns therefore differs from the returns in other share classes.

PERFORMANCE, NET OF FEES - IUSD



PERFORMANCE SINCE INCEPTION

ABSOLUTE PERFORMANCE (%)[1]

Coeli Renewable Opportunity	6.4%
IShares Global Clean Energy	-9.3%
WilderHill New Energy Global I	-6.0%
MSCI World Equity	7.7%
MSCI World Small Cap	0.4%

RELATIVE PERFORMANCE (%)[1]

IShares Global Clean Energy	15.7%
WilderHill New Energy Global I	12.4%
MSCI World Equity	-1.3%
MSCI World Small Cap	6.0%

Please note that the indices referred to in this monthly report are included for informational and illustrative purposes only. The fund is not managed in reference to the indices, but the indices are deemed to be relevant and comparable to the fund.

PERFORMANCE IN SHARE CLASS CURRENCY (%)[1]

	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec	Year
2023		0.4%	1.6%	0.3%	-0.4%	5.9%	-1.4%						6.4%

ATTRIBUTION JUL -23

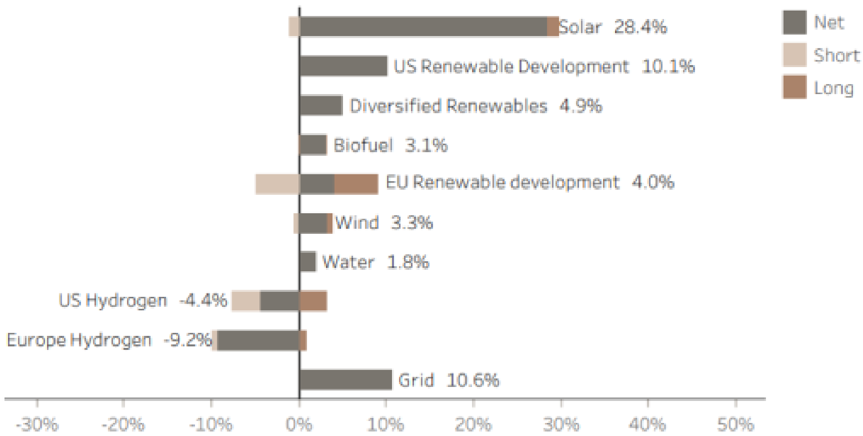
Short	-2.2%
Long	0.8%

MONTH END EXPOSURES

EXPOSURE, MONTH END

No of long positions	24
No of short positions	8
Gross Exposure (%)	101%
Net Exposure (%)	53%
Max. Largest long % NAV	7.7%
Max. Largest short % NAV	5.1%
Top 5 shorts % NAV	-23%
Top 5 longs % NAV	30%

STRATEGY EXPOSURE[1]



Past performance is not a guarantee of future returns. The price of the investment may go up or down and an investor may not get back the amount originally invested.

1) Share Class I USD

FUND MANAGER COMMENTARY

The Coeli Renewable Opportunities fund lost 1.4% net of fees and expenses in July. It is up 6.4% since the inception on February 6, 2023.

The fund has outperformed the most comparable indices, the Wilderhill New Energy Global index (NEX) by 12.4% and the iShares Global Clean Energy (ICLN) by 15.7% since inception. During July, the fund underperformed the ICLN by 0.7% and underperformed the NEX by 7.2%.

After the strong performance in June where only one theme was down, half of the themes had negative returns in July. The themes that were net short lower quality, non-profitable and higher multiple companies accounted for most of the losses. In aggregate, shorts lost 2.2% and long contribution was 0.8%. Net exposure was around 50-55% in the first week but was reduced to 45-50% before ending the month at 53%. Gross exposure averaged around 100% and ended at 101%.

MARKET COMMENT – GOLDILOCKS ECONOMY CONFIRMED?

The momentum of the market rally rolled into July, with the S&P 500 up 3% and advancing 28% since the bottom in October last year. Nasdaq clocked in another 4% in July, up a staggering 44% so far this year.

In our previous monthly report, we wrote that the market was embracing a goldilocks economy and the latest data points seem to be confirming this view. The durability of US growth continues to surprise on the upside while inflation is receding faster than optimistic expectations. It seems like the remarkable health of the labour market has underwritten both consumption and housing without triggering an inflationary spiral in wages.

As anticipated by the market, the Federal Reserve raised interest rates in July. Although, FED Chairman Powell warned about potential future hikes, he also stated in his speech that the FED would start cutting rates long before inflation hits 2% provided that there is credible and sustainable evidence of inflation decelerating. This statement somewhat shook the “higher for longer” perspective, and the market is now factoring in as many as five rate cuts in 2024. It is somewhat surprising that the bond markets are so confident to see rate cuts while the US economy just printed an acceleration in GDP growth for the second quarter. In fact, after the most aggressive rate hiking cycle in the past four decades, the US economy is not only growing above trend, but it is also reporting a record low unemployment rate and a stock market that keeps hitting new all-time highs. Although concerns in the stock market have predominantly centered on a potential recession, we wonder if the narrative may soon pivot towards worry over a possible resurgence of inflation.

The absence of a recession is also reflected in corporate earnings, which were expected to bottom in the second quarter this year. As about half of S&P 500 had reported Q2 earnings, more companies were beating estimates than on average. However, there are some concerns. Earnings beats were smaller than normal and upgrades following earnings reports were also smaller. Most troubling was maybe that the share price response was surprisingly soft. Companies that beat expectations have historically on average outperformed the market by about 100bps, but as of writing they have this quarter underperformed by as much as 30bps. According to Goldman Sachs, this is unprecedented over the last 18 years of data, excluding the covid years. Moreover, this statistic gets even worse when only looking at tech stocks, which have beaten expectations at a higher rate than ever but are lagging the market by more than 100bps the day following earnings announcements.

This could be viewed both bullish and bearish. On one hand, it is undeniably a positive sign that tech stocks are surpassing earnings expectations after their most impressive rally in over two decades. One can only speculate on the market's reaction had these tech stocks failed to meet earnings expectations. Conversely, the subdued market performance could potentially be attributed to positioning adjustments, profit-taking, and de-leveraging as we move into the summer.

As the S&P 500 is up almost 20% this year, the index is also trading above 20 times earnings, which has only previously happened in the internet bubble and during the covid stimulus surge. However, similar to the internet bubble, this is driven by tech stocks. The seven largest tech stocks are in aggregate up 60% this year while the remaining 493 companies have seen modest growth of only 7-8%. Adjusting out the mega tech stocks, the average PE multiple is in fact only 17 times, which is in line with the 10-year average.

Of course, the risk-free rate over the last 10 years implied in the 10-year average P/E multiple is much lower than the current rate and likely also lower than the risk-free rate in the future. If interest rates should settle at a lower level than today, but at a higher level than in the run up to Covid, the market multiple should also be lower unless earnings growth is significantly higher.

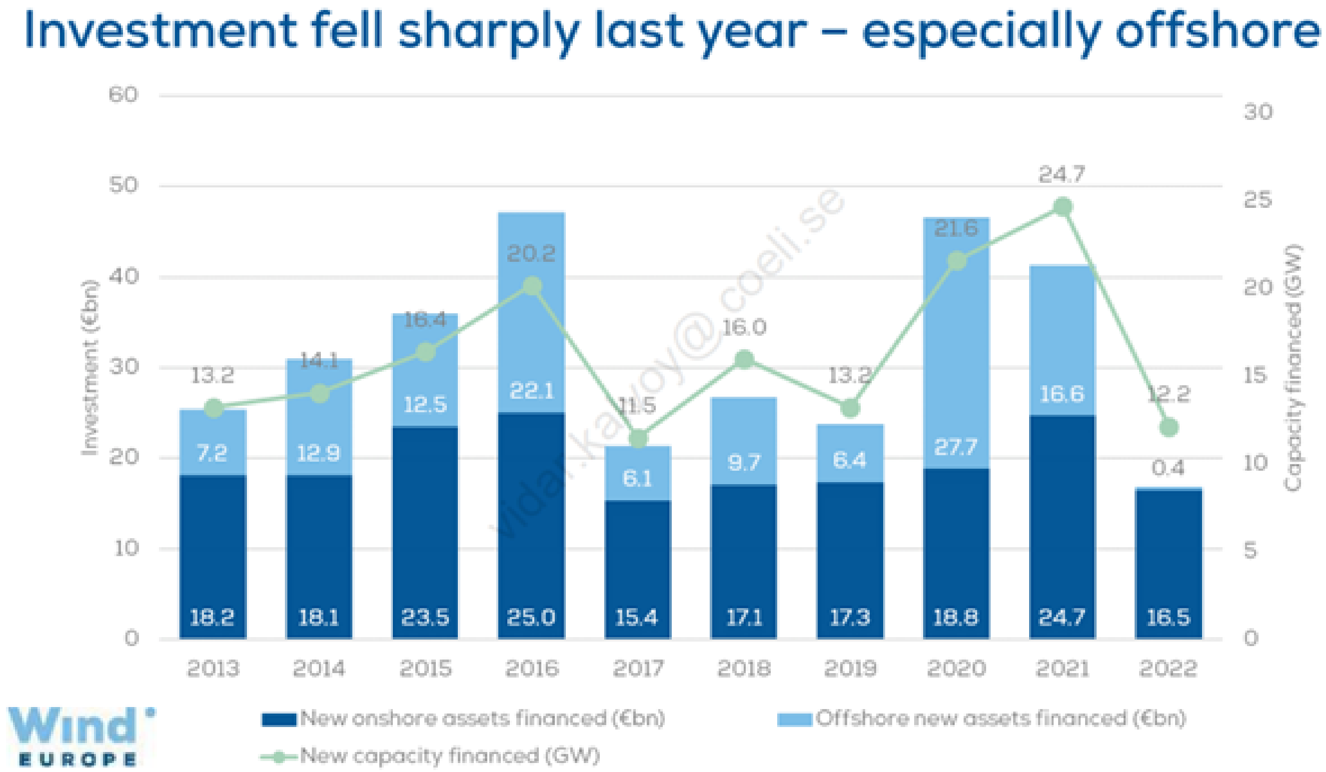
The 'Goldilocks' narrative, which denotes an economic state that perfectly balances inflation and growth, appears to have been fully embraced and is arguably priced into the market. While this may seem positive, it also suggests that if conditions are already near-perfect, the potential for further upside could be limited, at least in the short term.

RENEWABLE ENERGY – HEADWINDS AND TAILWINDS IN OFFSHORE WIND

Offshore wind technology plays a pivotal role in the drive to decarbonize our electricity supply. Although it today generates less than 1% of total electricity production, there is an ambition that it should account for approximately 15% of a much larger total electricity production in 2050.

Governments on both sides of the Atlantic have optimistic capacity targets. The EU Commission's latest is for installed offshore wind capacity to grow from 16GW in 2022 to as much as 111GW in 2030 and 300GW in 2050. In the US, the Biden administration is targeting 30GW in 2030, up from a paltry 0.1GW generated by only seven turbines last year.

However, despite the increased urgency following the Russian invasion of Ukraine and the skyrocketing energy prices, investments in wind capacity, particularly offshore, slowed down significantly. As can be seen from the graph below from Wind Europe, a European industry lobbyist, offshore wind investments were virtually non-existent last year.



To make it worse, the wind developers are also trying to renegotiate previously entered contracts that are no longer profitable. Last month, Vattenfall, Sweden's largest utility, decided to suspend development of its UK Norfolk Boreas 1.4GW offshore wind farm. It will impair the project by as much as SEK 5.5bn (USD 520m) as development and capital costs have soared since it won the tender only a year earlier.

Similarly, in the US, Iberdrola, through its subsidiary Avangrid, recently paid a USD 49m penalty fee to exit a 1.2GW offshore wind program in Massachusetts. Bloomberg New Energy Finance (BNEF) calculated that the levelized cost of energy (LCOE) for the project has increased by 48% from the time it was signed in 2021. The investment tax credit in the meantime increased from 30% to 40%, but without this lift, the LCOE would have increased by as much as 57%.

It is evident that wind fundamentals have deteriorated despite improved government incentives. The main problem for all developers is the soaring cost inflation in the wind supply chain. Post-pandemic, prices for steel, labour, and transportation have surged, adversely affecting anticipated internal rates of return (IRR). The second problem is the increased funding cost. Offshore wind projects are very capital intensive with most of the capex upfront. With aggressive interest rate hikes over the past 18 months, projects grapple with greater interest payments, and the weighted average cost of capital (WACC) has risen with an elevated risk-free rate.

The difference between the expected IRR and the WACC is the profit for the developers. This spread is likely negative for some offshore wind projects entered into in 2020-2022, which often, but not always, means that it is better to write off the loss and exit the project.

To top it off, the industry in Europe also suffered from regulatory uncertainty in 2022. As power prices spiked due to the Ukraine war, European politicians introduced wind-fall taxes on renewable energy to subsidise energy demand, often generated by fossil fuels. Although the final tax burden was relatively small in the end, it sent a signal to the industry that the regulatory framework is uncertain and could be swayed by populist politicians. The risk premium in the cost of capital must go even higher.

While the wind sector seems inundated with discouraging news and headwinds, there are however glimmers of hope and signs of some tailwind.

First, we believe it is positive for the industry that developers chose to write off costs and pay exit fees rather than continuing with unprofitable projects. Most of the developers with projects facing negative profitability will try to renegotiate the existing contracts, which we believe will have mixed success, but we are confident this will help accelerate the recalibration of price expectations on future contracts. In fact, according to LevelTen Energy, a renewable energy consultancy, the average purchasing power agreement (PPA) for offshore wind is up as much as 85% since 2020.

Second, although Vestas, the largest wind turbine installer, increased prices on new orders by 20-30% year over year for three quarters in a row, the average selling price have stabilized in the last two quarters. Steel and other commodity prices have also decreased and supply chain issues that impacted margins for both turbine manufactures and the developers in 2022 are in the rear-view mirror.

Third, there are also regulatory tailwinds. We have in previous monthly reports discussed the strong focus on speeding up permitting for renewable projects. Considering that a typical wind project takes nine years, with only two years dedicated to construction, faster permitting could speed up projects significantly and boost projects profitability.

On that note, Germany has taken the lead in making the new EU regulation agreed upon in January this year into national law. Some of the most important changes are the introduction of a two-year binding deadline for permits, expedited permitting in designated ‘acceleration areas’, and a digitalisation requirement for a process that remains largely paper based. This has already resulted in 65% more permits issued in Germany in Q1/23 than in the first quarter of 2022 and 2021. The other EU nations are expected to introduce similar regulations in the forthcoming months.

Similarly, in the US, the Federal Energy Regulatory Commission (FERC) some weeks ago issued a sweeping new rule aimed at speeding up permitting for interconnection to the US power grid, a very important development for all renewables including offshore wind. We discussed this in our march-23 monthly report ‘Grid connection the next bottleneck?’ and expressed that we were hopeful this reform would be implemented.

The essence of the new rules is that projects will be assessed on its readiness and not when it entered the queue. The US will go from ‘first come, first serve’ to ‘first ready, first serve’. The new framework also imposes penalties on developers for retracting speculative projects, potentially reducing future wait times. Simultaneously, FERC will penalize transmission providers failing to complete timely interconnection studies. This reform marks one of the most substantial shifts in FERC’s near half-century history. As of the close of 2022, over 2000GW of generation and storage projects awaited connection, equivalent to the entire existing US power generation capacity. Clearly, an accelerated permitting process that trims years of development will boost profitability (IRR), reduce the uncertainty (lower cost of capital) and result in more value creation for the developers.

Finally, a last positive factor worth mentioning is that most European countries are moving to contract for differences (CFDs) as the favoured method for awarding offshore wind projects. CFDs ensure a fixed price for developers; when spot energy prices exceed this rate, the excess is returned to the government, but if prices drop below, the shortfall is covered by the government. Essentially, the government absorbs the price risk and the developer bear the volume risk.

Wind Europe, a wind lobbyist, has calculated that in today's debt market a typical project's breakeven might be EUR 92/MWh, but it would drop by almost 80% to EUR 50/MWh if the price risk was carried by the government. This should be a low hanging fruit for any country keen on expanding offshore wind capacity.

To sum up the potential tailwinds, as price expectations are reset higher and developing costs are declining, developers' profitability (IRR) on new projects is likely to improve. IRRs will be further boosted by accelerated permitting reducing the development time of projects. Funding costs will come down as CFDs become the preferred way to award government contracts. If forecasts about the FED slashing interest rates five times next year are accurate, we can anticipate a further drop in capital costs for upcoming projects, enhancing the cash flow value of future offshore wind projects.

Certainly, it will take some time before you see the effect of higher prices, lower funding cost and faster permitting in the accounts of the likes of **RWE (RWE GR), EDP RENOVAVEIS (EDPR PL)** and **Orsted (ORSTED DC)**. However, as the stock market's current valuations assigns limited value to any capacity growth, we believe the risk reward of investing in this area is improving. We are likely to increase our exposure in the upcoming months.

FUND PERFORMANCE – SQUEEZE IN NON-PROFITABLE TECH HURT PERFORMANCE

The fund lost 1.4% (I USD) in July, and there were two investment themes accounting for most of the damage. Both were skewed short companies that can be characterized as non-profitable tech, which had a great month as there were tendencies to short squeezes and meme stock trading among retail investors.

The top underperforming theme was 'EU Hydrogen' which deducted 1.2% from NAV. It was the first down month for the theme this year and although it was a relatively large loss compared to its invested capital, it has already recouped 70-80% of the July loss in early August.

Our other hydrogen theme, 'US Hydrogen' which is also skewed net short, did surprisingly well adding 0.3% to NAV despite a couple of shorts squeezing. The main reason was that our only long in the theme, **Plug Power (PLUG),** rose 26% during the month. We have taken some profit and reduced this position significantly into earnings in August.

The second worst performing theme in July was 'EU Renewable Development' which was hit by a double whammy as a short position squeezed by 20% and longs like **RWE, EDPR** and **Orsted** were down small or flat on the month. As we discussed in the previous section, we maintain our conviction that these developers will continue to experience profitable growth in the future and that their current valuation is mainly reflecting their installed base and the capacity under construction.

The 'Solar' theme, our largest theme by gross exposure had mixed performance in July. It lost 0.3% of NAV, but it could have been much worse had we not reduced our long positions in **Enphase Energy (ENPH)** and **Solaredge Technologies (SEDG)**. We have been writing about the weakness in the US residential market for most of this year. First, the introduction of new net metering rules in California, the largest solar market in the US, pulled forward demand to the first half of the year and as the new rules were introduced, there was an expected air-pocket in new originations. Second, higher borrowing costs and general cost inflation made residential solar investments less attractive across the US.

However, the downturn is worse than we expected at the start of the year. **ENPH** guided its Q3 revenue to decline by 20% sequentially and by 10% year-on-year. This can be compared to the same quarter last year when revenues grew by 20% sequentially and by 80% year-on-year. After experiencing robust growth in the past years and extended lead times for customers seeking equipment, the situation has reversed. Consequently, the distributor channel is oversupplied with both solar panels and inverters. While this oversupply is not unprecedented, what is crucial is evaluating the underlying growth in each market. The US market appears to be plateauing for now and perhaps into 2024, whereas the EU market is likely to grow by 30-40% this year.

SEDG with a much smaller share of its revenues from the US residential market and a larger share in Europe than **ENPH** is currently better positioned. However, **SEDG** highlighted on its earnings call that while a price reduction this year is unlikely, there is a possibility for it to occur in 2024. This exacerbated the selloff in the stock. Our position in **ENPH** is minimal, but we still hold a decent position in **SEDG** as we prefer its positioning in Europe, its stronger Commercial and Industrial market share, and its relative valuation.

The best performing theme for the second month in a row was ‘Diversified Renewables’. It added only 0.6% to NAV this month though versus 2.9% in June. The theme still contains only one long position, **Chart Industries (GTLS).** We have discussed the investment case for this company in previous monthly letters and although we are still very positive to the company and the stock, we have reduced the position. It is no longer our largest, but at month end still among the top five positions on the long side.

We look forward to updating you again next month.

Sincerely,

Vidar Kalvoy & Joel Etzler
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