



**TARENO**  
Global Water Solutions Fund

# Fund Manager Review – December 2023

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## “All you had to do was stay”

The title of this song by Taylor Swift nicely describes the market action in December. After the strong gains over the previous month, one could have expected the markets to take a breather, but the positive momentum continued well into year end. As the federal reserve signaled that they should be done raising interest rates, major stock markets performed strongly, and interest rates continued to fall. It feels like there is a lot of good news (i.e. rate cuts) priced now, but given the pain we felt in late October, we will not complain about this year's extended Santa Rally.

The Tareno Global Water Solutions Fund posted a performance of +6.21% (W-Euro Tranche) and ended the year 2023 at +13.14%

## A look in the rear-view mirror

Having covered the water sector since 2007, we've observed notable shifts in the industry landscape. One persistent element, however, is the marked dissonance between the thematic enthusiasm surrounding water and the pragmatic realities of an industry comprised mostly of seasoned, cyclical enterprises. Frontline personnel within these companies often appear surprisingly disconnected from the substantial exaggerations and inflated assessments of their profession propagated by investors. In short, even in the investment universe of water, one can be mistaken in their assessment. We are not immune to that either.

Now, where have we been wrong in 2023? We bet on an outperformance of Japanese companies. They trade at very attractive levels compared to their US peers and in the case of the companies we choose are supported by strong tailwinds. Kurita Water, just to name one company, is a key supplier of ultra-pure water treatment systems, that are essential to the manufacturing of Semiconductors. The ongoing trend of nearshoring capacity provides them a solid runway to increase revenues. While this could be seen in their results, the extent of the Yen's weakness caught us off guard (we do not hedge currencies). The most significant negative impact on performance came from the agriculture/irrigation segment. We underestimated the impact of rising interest rates in combination with falling soft commodity prices on the demand for irrigation systems. We have significantly reduced our exposure, but unfortunately, we were a bit too late.

Now, for the good ones: 2023 was a brutal year for water utilities, especially in the US. They typically trade high-beta to interest rates and see their prices falling, as yields go up. We were right to underweight US names and focus on more compelling stories like Sabesp in Brazil, or Veolia, ACEA and EVN AG (one of our best performing names at +73%) out of Europe. We were right to be patient with construction related names, even if the sector came under pressure during the 2nd half of the year. Construction has been the strongest contributor to returns in 2023 with names like Wienerberger, Pentair, Ferguson, and Mueller Industries in top positions regarding contribution. If fundamentals are right, then “all you have to do is stay”. Mueller Industries is emblematic of this Song. They trade at 8.5 P/E, they have about USD 9.- per share in cash on their balance sheet, but nevertheless saw their stock falling 23% from July till October, only to mark a new all-time high in December.

## Outlook

The book is closed for another year and 2024 is upon us. Financial markets will always carry a certain degree of uncertainty, but the picture heading into 2024 appears much clearer than this time last year. Inflation is cooling and interest rates are expected to fall. There is a chance that the US will avoid falling into a prolonged recession and while geopolitics are clearly a risk, I'm optimistic for the market in general. The small and midcap universe has room to run, which is a clear positive, since this is the space where water stocks play. Regulation will be an important driver this year. The EPA has ignited a wave of efforts, both in the US and internationally, to combat the widespread contamination of water supplies with PFAS substances. This will create a

favorable environment for suppliers of activated carbon filters and water treatment systems. As climate change continues to take its toll, there will be investments in water infrastructure to reduce leakage, prevent sewer overflow (UK) and manage stormwater. Our trip to Aquatech in Amsterdam confirmed that A.I. is on the verge of making its way into the industry.

Another topic that is gathering traction is water reuse. In December, California reached a significant milestone by approving its initial standards for transforming sewage into potable water sources for residential and commercial use. This marks a departure from the current practice of mixing recycled water into aquifers or utilizing it for non-drinking purposes like irrigation. Wastewater is produced during a drought and having that source available can be critical. We might not be there yet, but water reuse requires a lot of investment in water technology.

Looking at sectors, 2024 might stage a comeback for US utilities, especially if interest rates start to ease further. We are currently looking at names like Essential Utilities and American Waterworks to build up positions. Finally, Emerging Markets might offer a good entry point.

We believe there is a range of exciting milestones ahead for water companies in 2024 and beyond.

Best regards,



Stefan Schütz



Stefan Schütz has been managing the Tareno Global Water Solutions Fund since July 2021. In addition, he is responsible for fundamental equity research in the investment team. Stefan Schütz started his career in the financial industry in 1997 at Bank CIC before joining the Tareno Investment Team shortly after the launch of the Tareno Global Water Solutions Fund in November 2007. Stefan Schütz is a Certified International Investment Analyst (CIIA).



As ESG analyst, Katja Von Krannichfeldt is responsible for implementing the sustainability strategy in the investment processes. She is also responsible for the management of equity valuation models. Since 2023, Katja Von Krannichfeldt manages the Tareno Global Water Solutions Fund. She holds a Master's degree in International Business Development from the University of Neuchâtel and joined Tareno in 2016. Katja Von Krannichfeldt is a «Chartered Financial Analyst» (CFA) and holds the «CFA UK Certificate in ESG Investing».



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