December 2023

The Alternative Investor

Performance
News
Trends
Regulatory updates

A balancing act like no other...

In this COP28 edition, we look at how financial initiatives can help shift the world to a low carbon economy, with **PwC** on Article 6 and how it will open-up new possibilities to invest in emission reduction projects; **Marex** on the role of technology and innovation to enhance the voluntary carbon market; **Vuelta Carbon** on the compatibility of financial returns and climate action; and **Forestry Linked Securities** on why forestry is such a critical asset class in today's world.

A Brodie Consulting publication in conjunction with Capricorn Fund Managers and RQC Group.

#30

Equities shine while systematic struggles in November

With investor confidence increasing and market participants pricing in 2024 Fed rate cuts, most equity markets had a very good November, while commodity markets struggled. This was reflected in the **HFRI Fund Weighted Composite Index**, which was up +2.2%, although the **Asset Weighted Composite Index** was down -0.6%, as poor macro performances from some of the larger managers weighed on the space.

In such an environment, unsurprisingly, the **Equity Hedge (Total) Index** was the top-performing strategy, +4.1%. Within this, **Quantitative Directional** was up +7.2%, followed by **Fundamental Value**, +4.8, and then **Healthcare** and **Technology**, both +4.6%. The worst performing were the commodity-focused funds, with the **Energy/Basic Materials Index** up only +0.4%.

Event Driven likewise followed equities, with the **Index** up +3.6%. With investors increasingly risk-on, activist-held positions rallied, and the **Activist Index** rose +7.7%; **Special Situations** was also up +4.5% and **Event Driven Directional** +3.6%. **Directional Merger** and **Credit Arbitrage** were more balanced... with the indices up +1.6% and +1.5%, respectively.

This was a more difficult month for **Macro** managers and the Index was down -1.6%. The two worst-performing strategies were **Systematic Directional** -3.6%, followed by **Trend Following Directional**, -2.8%. **Discretionary managers**, however, had a better month, +1.5%. The **Commodity Index** was down, but only marginally, -0.2% and the **Currency Index** fractionally up, +0.1%.

Relative Value also had a good month, +1.5%, led by **Fixed Income Sovereign**, +4.1%, with the only sub-strategy in the red being **Volatility**, down -1.3%.

Turning to the regions and it was **LatAm** that stood out, +9.9%, followed by **India**, +6.0%, which year-to-date is up +26.1%.

Upcoming Events

10 January 2024
Crypto Finance Conference

17 January 2024
Annual Forecasting 2024 (CFA)

21 January 2024
Apex Invest Baha Mar

23 January 2024
UK & Ireland Alternatives and Private Markets Symposium

Click here to see all the listings

€865bn

Size of the global carbon market in 2022

Source: Statista

11,397

China's carbon dioxide emissions 2022 (million metric tons)

Source: Statista

UAE preps $30bn climate fund

With Cop28 just ending, the big financial services story has been the UAE announcing a $30 billion climate-related fund. The **ALTÉRRA Fund** is the largest private investment fund for climate change action. **BlackRock, Brookfield** and **TPG** have each partnered with the UAE to manage the fund, with Cop28 president and, somewhat controversially, chair of UAE oil company **ADNOC**, Sultan Al Jaber, chairing the fund board.

During the fund's lifetime, it is looking to mobilise investments totalling $250 billion by 2030. Of the $30 billion, $25 billion is set to be deployed in **ALTÉRRA Acceleration** to help scale up climate investments and $5 billion **ALTÉRRA Transformation** to improve access to funding for the Global South. Al Jaber said that the fund's "scale and structure will create a multiplier effect in climate-focused investment, making it a vehicle like no other."

Brookfield raises record infrastructure fund

Brookfield has hard capped its latest infrastructure fund at $28 billion. This is yet another record fundraise in private equity, showing a healthy appetite for infrastructure investments. Sam Pollock, Chief Executive of Brookfield's infrastructure business, told the **Financial Times** that the "deglobalising world" has increased the number of infrastructure opportunities as countries increasingly seek to re-shore vital infrastructure at a time of elevated geopolitical uncertainty.

A thriving secondaries market

Pantheon has raised $3.3 billion for its latest secondaries fund, **Pantheon Global Secondaries Fund VII**. This will invest in a blend of LP and a 'growing range of GP-led' secondary stakes and is above the initial fund target of $2.0 billion; it is also Pantheon's largest-ever raise for a private equity secondaries program, with significant flows coming from the firm's private wealth platform. PGSF VII has already deployed 60% of the commitments raised.

Secondaries are fully on trend - as we have been writing in previous editions - with **Blackstone** closing the funding on its secondaries real estate fund, **Strategic Partners Real Estate VIII**, and related committed program vehicles at $2.6 billion. This is a market where Blackstone has said it sees 'substantial and growing opportunities.' **Ares Management** has also raised $3.3 billion for a similar secondaries real estate vehicle, **Landmark Real Estate Fund IX**.

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UPDATES (cont.)

No cost is sacred at Carlyle as Schwartz looks to get the firm back on track

Ten months into the new CEO's tenure at **Carlyle Group** and Harvey Schwartz is wielding the axe to get the firm back on course. Since Kewsong Lee abruptly stepped down as CEO last year, the Washington-based private equity giant has struggled to gain real traction.

While other leading firms have been closing on record-sized funds, Carlyle has failed to hit its $22 billion target for a flagship fund, **Fund VIII**. Unfortunately, after two years of fundraising for this US-focused fund, the firm came up short and closed at around $14.8 billion. Carlyle has also had to lower expectations - by 30% - on its Asia fund target, which has been marketed since mid-2022, and is now looking for $6 billion.

Compared to **KKR**, Carlyle's share price has also underwhelmed this year, but Schwartz has a solid reputation and a plan, although it will take time to get the business on firmer footing.

To achieve this, "no cost is sacred," said CFO John Redett, having already cut $40 million in expenses - reducing headcount, slashing employee compensation and benefits. There is further heavy cost-cutting during this quarter, with Schwartz saying that a great deal is riding on this period, but he "feels the momentum [is] building" and believes the firm will see a "step up."

Bain hits yet another record

As clichéd as it is, all too often we describe private equity fund raises as 'records,' which many are, and now we have another, this time **Bain Capital** raising $7.1 billion for its largest Asian-focused buyout fund. This is for **Bain Capital Asia Fund V**, which is the largest regional fundraise this year and is 40% more than Bain's target; it is also $2 billion larger than the previous vehicle.

Asia accounts for a large part of Bain's business, with 110 regional investment professionals operating out of 14 offices. According to **Pensions & Investments**, investors in this particular fund include **California State Teachers' Retirement System, West Sacramento, Juneau** and **Maryland State Retirement & Pension System**, with Bain also committing $750 million.

NBIM turns to private equity

The **Norway Government Pension Fund Global**, the world's largest sovereign wealth fund, managed by **Norges Bank Investment Management**, is pushing to invest $70 billion in private equity and co-investments over the next ten years.

The fund has historically avoided private equity, but given its size and diversification requirements, is having to look further afield. The decision now comes down to the Ministry of Finance and should they give NBIM the green light, the first move will be to co-invest alongside private equity funds, similar to **ADIA** and **QIA**. Such a move makes fees more negotiable, with the fund renowned for not appreciating some of the generous manager fees, but there is also the opportunity to make more selective investments based on geography and sector.

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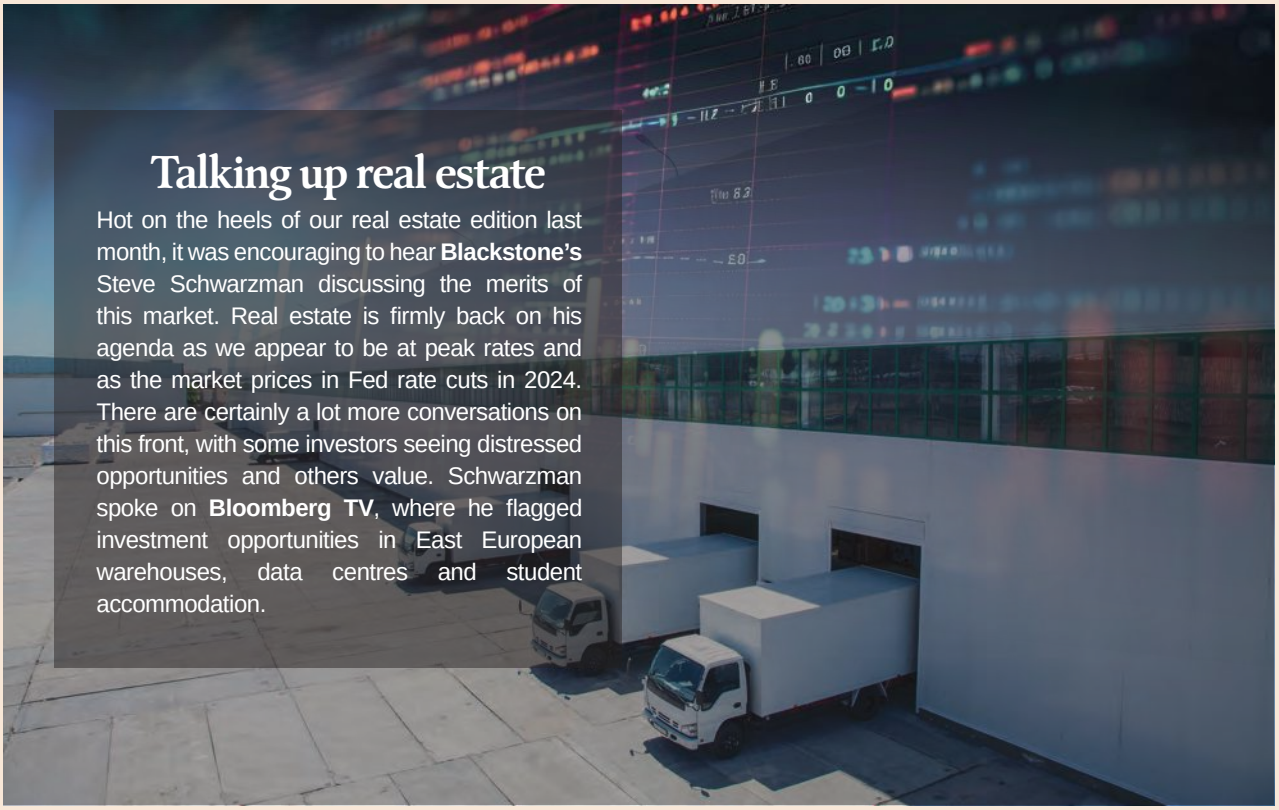


Talking up real estate

Hot on the heels of our real estate edition last month, it was encouraging to hear **Blackstone's** Steve Schwarzman discussing the merits of this market. Real estate is firmly back on his agenda as we appear to be at peak rates and as the market prices in Fed rate cuts in 2024. There are certainly a lot more conversations on this front, with some investors seeing distressed opportunities and others value. Schwarzman spoke on **Bloomberg TV**, where he flagged investment opportunities in East European warehouses, data centres and student accommodation.

Shorting Blackstone's Mortgage Trust

Short seller Carson Block is less enamoured about the near-term future of real estate than Steve Schwarzman, having taken a short position against **Blackstone Mortgage Trust (BXMT)**. In a report, Here Comes the Cliff, Block writes that the REIT is facing the 'perfect macro storm' and, even with interest rate cuts, 'is at risk of being completely wiped out,' with borrowers unable to refinance and repay BXMT. Block was using his platform at the **Sohn Investment Conference** in London to flag the position and this report, saying that the second half of next year would be the Trust's crunch time.

KPS raises $9.7bn for special sits

New York based **KPS Capital Partners** has raised $9.7 billion for two special situations strategy funds.

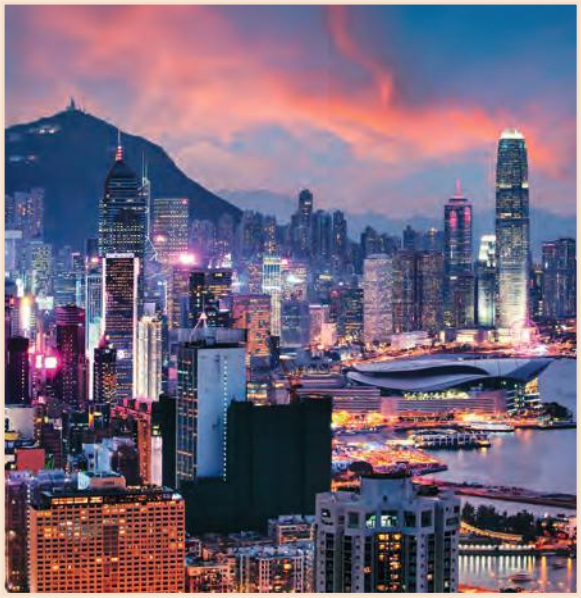
KPS Special Situations Fund V1 and **Mid Cap Fund II** were oversubscribed and will invest in corporate carve-outs, turnarounds, restructurings, and other special situation investments.

KKR sees big private credit opportunities in Asia

Having just released their private credit report, Private Credit in Asia Pacific: A Region on the Rise, **KKR** has highlighted what they see as an under-penetrated and under-allocated market that lacks the same access to private credit channels as Europe and the US.

Citing **Preqin** data, the report writes: 'The ratio of private equity to private debt assets under management is 30.8x for APAC compared to 5.2x and 3.5x in the US and Europe, respectively.'

With US and Europe private credit markets increasingly saturated, KKR sees real opportunities in APAC, where 'performing credit capital so far outstrips supply' and investors can lend to 'large, market-leading companies with covenanted structures, governance rights, and other protective elements that would not be as commonly available in Western markets.'



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UPDATES (cont.)

Managers flock to the UAE

TCI is the latest big-name hedge fund to set up an office in the UAE.

According to a **Financial Times** report, there are now around 500 funds with a physical presence in the region, including the likes of **Millennium, Balyasny, King Street** and **Brevan Howard.**.

Proof of the region's importance is the high quality of the regional teams, with TCI's head of Investor Relations and newly appointed Director of **TCI Fund Management (AD) Limited**, Bronwyn Owen, moving to Abu Dhabi from New York to head up the new office.

Chris Hohn, TCI founder, said: "The Middle East is a vital market for the investment management industry, both from a talent and asset growth perspective, as well as a critical partner in global efforts to reduce carbon emissions and climate change."

Another manager talking up the merits of the UAE is **Brevan Howard's** Alan Howard, who has said that it is not only the access to sovereign funds, family offices and ultra-high net worth crowd, the timezone is also the best in the world to trade macro strategies, given its geographical location to Asia and the US.

Schonfield pulls plug

A premature story we wrote last month was **Schonfield Strategic Advisers** 'imminent' move to join **Millennium Management**, which had looked virtually signed and sealed; but after several months, this deal has fallen through.

Schonfield pulled out after receiving verbal commitments of $3 billion from new and existing investors. The **Financial Times** wrote that this money will 'replenish' Schonfield's 'assets after its investors redeemed more than $2 billion this year to October,' which had made the $11.7 billion firm uneconomical to run. Whether this is kicking the proverbial can down the road, only time will tell, but Schonfield has since announced that, even with the additional commitments, it is cutting around 150 employees.

This is not the first time these two firms have failed to strike a deal, with earlier discussions held in 2020.

Hintze calls last orders

A big UK story of the past month in hedge land has been the announced sale of **CQS's** credit platform and brand to **Manulife**, the giant Toronto-based financial services firm. This includes $13.5 billion of assets under management; with Michael Hintze keeping his **Directional Opportunities** fund and various other mandates, which will soon move to a new company and brand.

Life has been tricky for Hintze over the past few years, with questions hanging over performance and difficulties raising assets. Earlier this year, **Bloomberg** had written that Hintze was working with advisers on the future of the business. With this deal, Manulife acquires a strong industry brand with a storied history that will become **Manulife | CQS Investment Management**, which gives them a solid structure, track records, experienced team members and highly regarded investment processes.

The transition to the next growth phase was always going to be difficult for CQS, so this move does make sense, and for Manulife, it speeds up the buildout of its alternative credit arm. In terms of continuity, CQS will still be led by the very impressive Soraya Chabarek as CEO, alongside Senior Partners Craig Scordellis, CIO Credit, and Jason Walker, CIO ABS. The deal is due to close in early 2024.

Hintze may be saying goodbye to his CQS, but it is unlikely to be the last you will hear of him.

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> Now you have just an avalanche of data and so forth. In fact, the unique aspect of the Ukraine war is that it's the most transparent in history. Everyone has a smartphone, access to the internet, and social media and websites under which you can upload video and so forth...the trick is to fuse it, to bring it together.

General Petraeus (Former CIA Director)

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UPDATES (cont.)

Chanos hangs up his hat

One of the most challenging jobs in running a successful private asset management firm is a succesful handover to the next generation. Remarkably few firms achieve this cleanly and, all too often, they fail.

There are many examples in today's asset management world of managers divided internally on direction, leading to acrimony, messy divorces and in some cases forced closure.

Unlike Michael Hintze, who has chosen to sell **CQS** to **Manulife**, Jim Chanos has opted for the most straightforward method: closing the shop door after 38 years in business.

Chanos will always be seen as the eponymous short seller and the model for many of today's activist investors. However, the past few years have been rough, with a sizeable fall in assets. His positions may have made sense on paper but didn't always pan out, **Tesla** in particular; but he made a lot of money over the years and was the one who found **Enron** wanting.

Chanos did not always fight the cause publicly. He was an out-and-out pure short seller, an intellectual champion. Knowing that he was shorting your business put the fear of god into CEOs. To do what Chanos did for so many years required a lot of backbone and big balls.

Inclusive proves less conclusive

Inclusive Capital Partners, once lauded as a ground-breaking manager set to drive environmental and societal change, has closed after only a few very short and unfortunately unsuccessful years.

From an investor's perspective - family office and institutional - Inclusive's proposition had looked solid, with a crack team using an environment and social investing lens to actively push for change.

At launch, it was so on trend and in the spirit of where the market was looking to go; that it was set up by Jeff Ubben, co-founder of **ValueAct Capital**, only added to the story. As the **Financial Times** points out, Jeff unfortunately tied himself to the wrong crowd and took a few wrong turns. Ultimately, Inclusive Capital Partners was a case of the right idea, but poor execution.

Jeff will be back - he truly believes in the importance of long-term sustainable investing - but it will be a different vehicle, with different priorities and a tighter mandate.

Barker raises $3.5bn for small pod shop

One of this year's biggest hedge fund launches is Todd Barker's **Freestone Grove Partners**, which has raised $3.5 billion and is set to start trading in January. **Bloomberg** has been closely monitoring developments, having first reported in March that Barker was looking to raise more than $1 billion for the multimanager business.

Barker has a quality pedigree, having spent five years heading **Citadel Surveyor Capital**, Citadel's fundamental equities arm. Compared to most new multimanagers, Bloomberg writes, Freestone has fewer 'investing pods,' which will run more money and appears to have hired various Citadel employees, including Ravi Paidipaty, former Surveyor Capital Portfolio Manager, as the firm's Deputy Chief Investment Officer.

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UPDATES (cont.)

Changing of the guard as Multi-Strategy looks to take top spot

Long/Short Equity is about to lose its position as the largest hedge fund strategy in the coming months, according to **eVestment** data, as assets continue to flow to the Multi-Strategy managers.

In the October Flow Report, Long/Short Equity saw the most significant outflows (-$5 billion), taking the sector's assets under management to $678 billion vs $677 billion for Multi-Strategy funds as at 31 October. Where there were inflows were to Relative Value Credit, $1.3 billion, followed by Convertible Arbitrage and Managed Futures, both of which saw inflows of $0.4 billion.

This is a historical shift in the alternative fund space, with Long/Short Equity the original hedge fund strategy, and it has only been relatively recently that you have seen a surge in assets heading to Multi-Strategy.

Silly money

Remuneration has always been a contentious subject in the alternative investor space and the fast-growing multimanager siloed businesses have taken this up a notch. In the last few weeks, there have been critical comments from big industry figures about the size of pay packets. First up was **Marshall Wace's** Paul Marshall, who said that some of the numbers he saw were just plain silly, on par with signing Cristiano Ronaldo. Perhaps Marshall is talking his book, not wanting to pay top dollar for talent joining Marshall Wace, but he was quickly followed by Bob Elliott, former **Bridgewater** executive, who, speaking to **Financial News**, said that the performance these individuals generated didn't match the compensation, creating an industry "imbalance."

Marex expands prime broking business

Marex impressively continues to build out its prime broking capabilities, having completed the acquisition of **Cowen's** prime brokerage business.

This has added 160 employees to **Marex Capital Markets**, with the Cowen PB business continuing to be led by Jack Seibald and Mike Rosen, who have run the business since its inception in the mid-1990s, then sold. Marex's Capital Markets business was formed in 2022 after **ED&F Man Capital Markets** was acquired. Today, **Marex Prime Services** operates a direct and introduced prime brokerage business.

Crypto is back

With bitcoin once more closing on $45,000, crypto funds are again the best performing in the sector. Earlier this year, this was a difficult sector to be in. Back in August, data from **21e6 Capital AG** showed 13% of crypto funds had shut down year-to-date. Since then, while many funds have held their high cash balances, most have benefited very handsomely from crypto's rise, with bitcoin up more than 160% and ether 100%.

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LETTER FROM AMERICA

prosek

Alt Snowbirds Head South as Florida Continues to Become Anything but Alternative

It's December with winter approaching on the East Coast, which means focus now turns South and often to Florida, a one-time short-term "snowbird" haven for Wall Street, especially along the Palm Beach/Miami corridor.

That focus still exists but the 75-mile strip of beach, freeway and light rail for speedier passage between Palm Beach and Miami is decidedly more crowded and less seasonal after the migration from New York to Florida during Covid. That's when financial-services firms and many private equity shops and hedge funds moved operations for higher temperatures and lower taxes.

> ... the state of Florida is now ranked as the 14th largest economy in the world and clearly not just for the retired with the average age at a surprisingly low 39 years old in West Palm Beach, an area seeing a big surge in growth.

Today, the migration from New York continues but at a seemingly slower pace, so it's worthwhile to take a look at some interesting data points behind the move to help understand the current state of the Sunshine State. Is this temporary or permanent -- and the answer will impact the larger private-market ecosystem for meetings, conferences, business development and real-estate decisions?

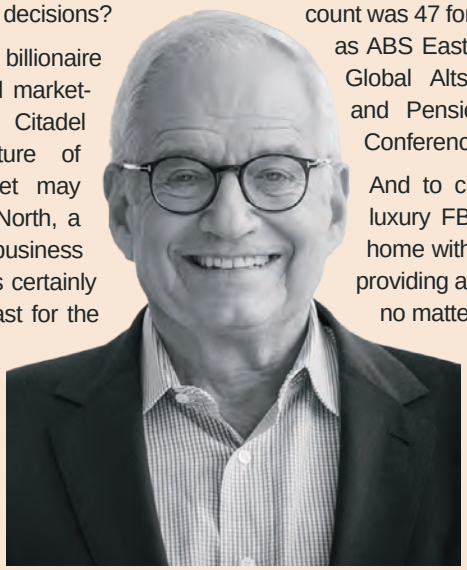
In a recent interview Ken Griffin, the billionaire founder and CEO of hedge fund and market-making businesses Citadel and Citadel Securities, called Miami the "future of America" and said that Wall Street may one day be referred to Brickell Bay North, a nod to the growing residential and business neighborhood center of Miami. That is certainly a stamp of approval or at least a boast for the Brickell district, where he is building a $1-billion headquarters.

He may not be too far off, though, especially if you look along the corridor. According to statistics from the Business Development Board of Palm Beach County, the area now has some 150 finance companies, mostly from New York City and supports nearly 74,000 jobs in finance. Big moves have included not only Citidal but Point72 Asset Management, Apollo Global Management, Blackstone, Icahn Capital Management and Cathy Woods' ARK Investment Management, to name a few.

What's more, the state of Florida is now ranked as the 14th largest economy in the world and clearly not just for the retired with the average age at a surprisingly low 39 years old in West Palm Beach, an area seeing a big surge in growth. Miami also was recently listed at No. 24 on the Global Financial Centers index, not a bad showing for a city mostly known until recently for Spring Break and art fairs such as Art Basel Miami.

But maybe the biggest indicator is the number of financial conferences taking place in the state each year, mostly in Palm Beach and Miami. Last count was 47 for 2024 with significant gatherings such as ABS East, Barron's 100 Summit, iConnections Global Alts, Milken South Florida Dialogues and Pension & Investments Private Markets Conferences.

And to cater to jet-setting snowbirds, a new luxury FBO from Embassair is making Miami home with a state-of-the-art private jet terminal, providing all with the ultimate alternative to travel, no matter the time of year.



Mark Kollar
Partner, Prosek Partners

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GUEST ARTICLES

How Article 6 will improve global carbon markets

Ian Milborrow, Partner, Sustainability, PwC UK

In a joint White Paper with the World Economic Forum (WEF) released for COP28, we have looked at how the implementation of Article 6 is improving global carbon markets, what this means for businesses as potential participants, and the steps companies can take to increase awareness and assess options to get involved.

Article 6 of the Paris Agreement is designed to provide flexibility for countries to meet their climate commitments, often collaborating with others in pursuit of lower cost (albeit high quality) emission reductions where possible. In contrast to voluntary carbon markets, or VCM, which have evolved on the basis of consensus-based standards, the Article 6 market will be compliance-grade. Scrutiny has heightened in how both these markets operate over the last year and it is important that the final sets of rules promote high integrity, traceability and an equitable distribution of proceeds to the parties involved[1].

Article 6 can be challenging to understand, but in broad terms there are two distinct elements. The first involves sovereign-to-sovereign trades, such as those announced in recent weeks[2] and tends to be decentralised in determining what project activities are deemed eligible to generate carbon credits. The second involves creation of a new global carbon market infrastructure overseen by a UN-governed Supervisory Body. The rules for market operation for this aspect are expected to be finalised in mid-2024.

The robust frameworks under development should not only establish greater trust, transparency and credibility in the carbon markets, but should also encourage international cooperation and capital mobilisation at scale from the private sector. From a business perspective, these mechanisms provide an additional route through which to source high quality credits to deal with their residual emissions i.e. those remaining after internal efforts to decarbonise are exhausted.

For alternative investors, Article 6 opens up a whole new set of possibilities for investing in emissions reduction projects. Such projects may be seen through various

[1] See for example link
[2] See for example link

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GUEST ARTICLES (cont.)

lenses such as a capital growth story in the underlying assets that generate the reductions (such as a landfill gas capture facility or afforestation of degraded lands reserve) or more of a commodities trading proposition since the monetisation horizon for carbon credits is typically 10 years or more.

WEF and PwC are seeking to bring together businesses and governments to drive the development of regional carbon markets based on Article 6. There are three key ways that business leaders can help to drive this progress:

- Build knowledge of Article 6 markets and support their development (for example through participating in national and international consultations);
- Engage national government to press for the implementation of institutions needed to support Article 6 transactions; and
- Understand how using carbon credits can enhance a company's net-zero journey not just in terms of lowering cost but in creating a community to help advance global efforts to achieve carbon reduction and other environmental benefits.

Click this link to read the Briefing Paper: Better Carbon Credits on the Horizon?

Download the full White Paper: Navigating Article 6: Opportunities for the Middle East and North Africa

Ian Milborrow, Partner, Sustainability, PwC UK

Ian is a Sustainability Partner at PwC UK with 25 years management consulting experience in the areas of strategy and policy, corporate finance and program implementation. An economist by training, Ian spent much of his early career in policy analysis and risk management, working extensively in emerging markets. He then spent eight years in PwC Corporate Finance to form a dedicated carbon markets group, executing transactions with a total value of around $200Mn.

Between 2010 and 2013, Ian was based in Washington, DC where he built PwC's US Sustainability team, establishing capability in key regional markets. Since returning to London, Ian holds client, sector and technical responsibilities and leads a 200-strong mission driven team based in London. He advises clients across a range of topics including Net Zero strategy and business transformation and the design and delivery of climate finance initiatives.

> **For business leaders, the Article 6 framework opens up a new set of possibilities for investing in high quality emissions reduction projects. With appropriate rules and safeguards, investors can develop carbon credit asset portfolios to meet the future needs of both sovereign states and companies who have made Net Zero commitments.**
>
> Ian Milborrow, PwC UK

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GUEST ARTICLES (cont.)

Technology and innovation can only strengthen the voluntary carbon market

Dr Guy Wolf, Global Head of Market Analytics, Marex

As corporations navigate the journey to net zero and seek to reduce emissions, the final step can only be taken with the use of offsets. Carbon 'gross zero' is a scientific impossibility and hence corporations will need to look to the voluntary carbon market (VCM) to offset these unavoidable emissions.

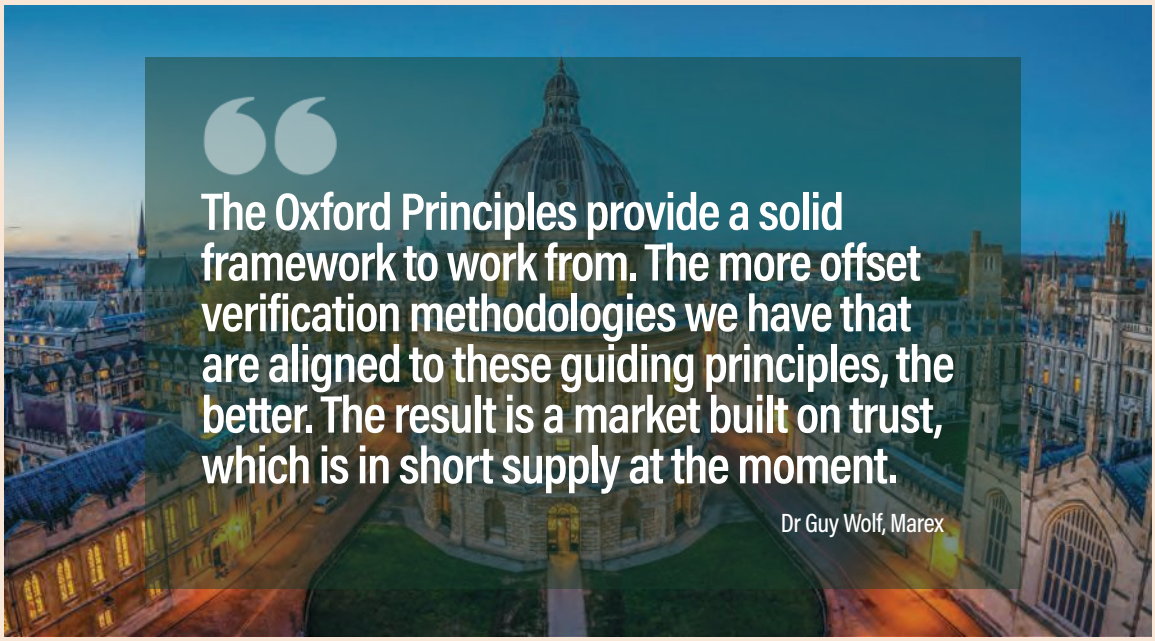
While the VCM market has evolved over the last 20 years, it is still a comparatively young market. Recent high-profile issues with offset verification mechanisms have opened a debate around transparency and regulatory oversight, leading to scepticism towards the role that the VCM will play in the net-zero transition. In addition, too many users of offsets have seen this as an easier alternative to emission reduction, a concept known as 'greenwashing', despite the Oxford Principles for Carbon Offsetting clearly opposing this practice. Whilst various initiatives are underway to try and restore confidence to the market, it is the negative examples that typically grab the headlines.

Declining confidence in offset verification has undermined the potential of the market and this has fundamentally hit demand over the past 12-18 months. We have seen a significant reduction in the price of perceived low-quality voluntary offsets, particularly in avoided deforestation projects.

Despite these issues, the role that offsets will play in accelerating net zero is undeniable. A well-functioning VCM can incentivise innovation in new decarbonisation technologies, whilst helping to steer capital towards scaling existing solutions. It can facilitate capital flows into developing countries that do not currently have the means to accelerate their own emissions reductions. The inherent challenge for companies in substantiating genuine offsetting claims boils down to accurately measuring real-world carbon impact.

To better substantiate claims, we need better verification mechanisms. The only way to get there is to drive innovation and steer capital towards scaling high-tech solutions.

In an ideal world, a regulatory power would have the capacity to prosecute deceptive offsetting practices, ensuring suppliers are held to account. The knock-on effect would be one of restoring confidence amongst buyers, and ultimately raising demand. But while strong



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GUEST ARTICLES (cont.)

> Automating data collection, analysis and validation will provide more reliable and consistent data far more quickly. This will in turn reduce the costs and time associated with issuing new carbon credits – and in having them assessed/audited/verified by independent third parties.
>
> Dr Guy Wolf, Marex

regulation should be an important aim, better technology for offset verification must be a priority now because we already have the tools.

The Oxford Principles provide a solid framework to work from. The more offset verification methodologies we have that are aligned to these guiding principles, the better. The result is a market built on trust, which is in short supply at the moment. Today's conventional verification techniques involve time-consuming manual processes and analogue data capture through in-person auditing of sits.

There are innovative solutions out there that utilise remote sensing, satellite systems, and greenhouse gas inventory software, but they only account for fraction of the verification market. For example, the Global Mangrove Trust carbon-offset project in Indonesia, funded by Marex, is an inaugural project for OxCarbon, a not-for-profit spin-out from the University of Oxford, and uses ultra-high resolution satellite data to give a more accurate measure of the carbon sink. The technology, developed by Kumi Analytics, has already been acknowledged by Google Cloud through the award of a 'Sustainability Partner' designation. As with many technology-driven solutions, units costs will decline exponentially as volume is scaled up.

Automating data collection, analysis and validation will provide more reliable and consistent data far more quickly. This will in turn reduce the costs and time associated with issuing new carbon credits – and in having them assessed/audited/verified by independent third parties. These solutions are already cheaper than the status quo today, even without mass adoption – if we are to unlock the amount of capital required to fix the climate crisis, we need solutions that can scale dramatically.

An increased appetite to embrace innovation and better technology will help market participants more easily discern quality, which will in turn boost both demand for carbon credits and improve quality of supply as well as liquidity in the market. There's a way to go, but the VCM will certainly remain of critical importance to the net zero cause.

Dr. Guy Wolf, Global Head of Market Analytics, Marex

Through Marex's position in the global commodities sector, clients access the world's major commodity markets, including a broad range of environmental products comprising renewable energy, recycled metals and circular economy sectors. Working in both traditional and green industries, and facilitating and innovating in these markets, Marex is ideally placed to work beyond market silos, make a fundamental difference to the sustainability of commodity markets and support the decarbonisation of the economy.

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GUEST ARTICLES (cont.)

Carbon markets: An investment opportunity like no other

Simon Crooks & Lee Bostock, Founding Partners, Vuelta Carbon

Carbon markets are one of the most important tools at our disposal when it comes to mitigating greenhouse gas emissions. Accordingly, as we approach 2030, public interest and scrutiny are intensifying. So too are the opportunities – for both enabling the fight against climate change and for investment.

Carbon credits are ultimately about one thing – financing decarbonisation. In the regulator-driven world of compliance markets like the EU ETS, polluting entities are mandated to match their emissions with corresponding credits via a cap-and-trade mechanism. This allows for a shortfall in credits to be covered by purchasing on the open market and an excess of credits to be sold. These have been very successful at reducing emissions by putting a cost on pollution and by reducing credit supply over time.

The other form of carbon credits is that of "offsets", which are effectively a security issued to a climate-positive project, quantifying the projects climate impact in terms of the number of tonnes of emissions either avoided or removed from the atmosphere. Despite recent interest, the concept has been around for over 30 years and remains the most direct way of financing climate action. The direct manner of these securities attracts interest and investment because they enable individuals and corporations to invest in projects that have positive climate impact as a balance against their emissions. The quantifiable nature of the credits allows for an accounting mechanism and a netting, or 'offsetting' of those emissions by way of cancelling ('retiring') the purchased offsets.

Simon Crooks, Vuelta Carbon

Historically, such use of offsets has been unregulated and non-mandated, coining the term the Voluntary Carbon Market (VCM). It is important to note that their use allows for lower overall net emissions whilst the emitter endeavours to reduce those emissions, not as a way of allowing continued emissions. They are part of the puzzle, not a replacement for it.

The market for offsets in 2022 was estimated to be $2billion. However, with increasing numbers of corporations making net zero pledges, and decarbonisation proving difficult for many industries, the size of the offset market is forecast to explode in coming years. To put a number on it, current annual global emissions outstrip offset issuance by around 18,000%.

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GUEST ARTICLES (cont.)

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In recent years the VCM has developed dramatically. An ecosystem of rating agencies, insurance, industry bodies and a secondary market with established brokers and exchanges has the hallmark of all other established markets like those of equities and fixed income. Suddenly we find ourselves in a world where the transparency and reliability that is rightly demanded by institutional capital is becoming a reality, and a reality that will bring scale which has huge potential for investors. People are waking up the reality that, as part of the broader toolkit, offsets are absolutely necessary to keep corporations and governments "on-track" with their climate goals. More notably, institutional investors are beginning to view this market as an ideal way of balancing long-term sustainable goals with financial gains. The UAE recently launched a $30bn climate fund, demonstrating how significant interest in the wider climate space is growing.

But the market remains nascent and navigating its complexities and changing landscape requires expertise. One thing is clear, though – that with the right approach, financial returns and climate action are perfectly compatible.

Lee Bostock, Vuelta Carbon

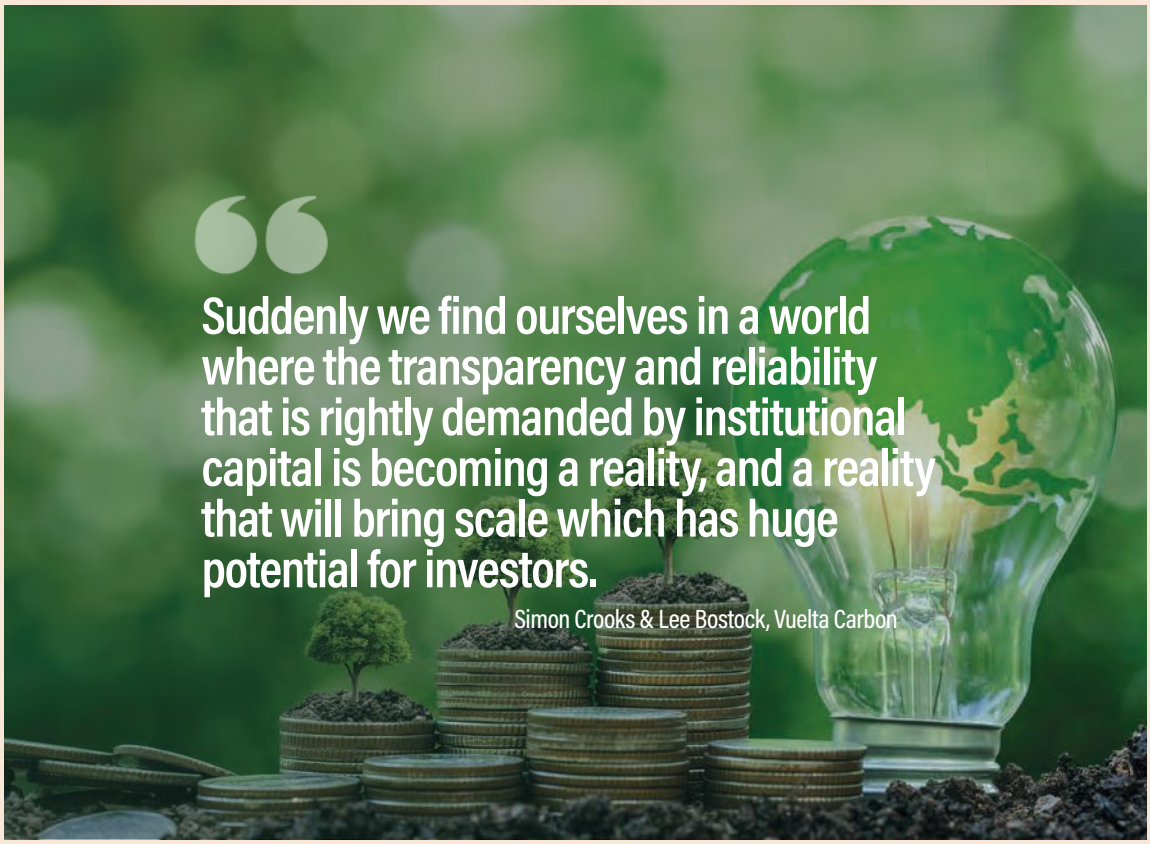
Simon Crooks & Lee Bostock
Founding Partners, Vuelta Carbon

Vuelta Carbon is an investment firm that focuses on climate change mitigation. It leverages in-house quantitative skills and knowledge of carbon markets to identify and invest in projects that generate offsets and reduce emissions. It's mission is to create positive environmental and social impact through considered and profitable investments.

Simon is a founding partner of Vuelta Carbon. He has spent the last 20 years in quantitative investments and trading. Before finance, Simon was a climate scientist at Oxford University where he was a contributing author to the IPCC's 4th Assessment Report, which was awarded a Nobel Prize. He holds a DPhil in Physics from Oxford University and has published several climate-related papers in peer-reviewed journals.

Lee is a Founding Partner at Vuelta Carbon and has worked in trading and investment management since 2000. After a career as a structured credit trader he worked in quantitative trading across a variety of asset classes. He is fascinated by both the similarities and differences between the carbon market and other asset classes. Lee holds a PhD in Quantitative Finance from Imperial College, London.

Simon and Lee have worked together since 2009.



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GUEST ARTICLES (cont.)

Why sustainable forestry is a critical asset class in today's world

Charlie Sichel, Managing Partner, Forestry Linked Securities (FLS®)

I have recently returned from COP28, the Conference of the Parties in Dubai. Set in the Dubai Exhibition Centre built for Expo 2020, I was overwhelmed by its scale and the collective levels of energy brought together, in a way that only the United Arab Emirates (UAE) could host with such finesse. The announcement of Alterra's USD 30 bn fund set the tone, followed by more pledges at a scale previously unseen, now totalling almost USD 100 bn.

The next phase, however, is about action. How do we convert this pledged capital into carbon sequestration with a sustainable business model? After all, any fund or carbon credit is only as good as its underlying project. There is no single answer, and whilst direct air capture proposals may be more appealing to those tech-minded venture investors, our belief is that sustainable forestry remains the core building block of the solution. Our job, therefore, is to make sustainable forestry investable.

To clarify, we refer to greenfield afforestation or reforestation, which one must blend with natural conservation, often in a mosaic format, ideally through the conversion of degraded cattle-grazing land into part working forest, part areas of conservation. The outcome is an ecosystem which offers attractive commercial and financial return, long-term carbon sequestration, biodiversity net gain, long-term employment opportunities, and positive social impact.

The commercial rationale is driven by a global wood supply deficit. According to the FAO, the required CAPEX for afforestation until 2050 is between USD 3 and 5 trillion.[1] Market fundamentals have been set for several decades, driven predominantly by demand for pulp and paper. Beyond that, we see China and India's growing appetite for sawn lumber, a whole new movement in construction material

[1] FAO: "The State of the World's Forests 2022", FLS analysis

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GUEST ARTICLES (cont.)

technology (for the likes of cross laminated timber), not to mention bioenergy becoming a critical energy source in the future.

In parallel, afforestation and reforestation have the potential to capture substantial amounts of CO_2 from the atmosphere and are to date, the cheapest, most effective and proven method of carbon removal.

"Is this additional?" I hear you ask. The answer is an overwhelming "yes", mostly because these projects typically take place in the Global South, and will only take place at a sufficient scale and in compliance with ESG principles with the support of carbon finance.

My Global South activity has recently focused on South America - in particular, Paraguay. A diamond in the rough, Paraguay has established itself as a beacon of fast-growing potential across the region, whilst its neighbours yoyo between political regimes. The country boasts some of the best ecological conditions in the world. Critically, one can grow a commercially productive tree in 6 years. Beyond that, land is available, water supply is abundant, and its legal framework is favourable and stable. In our view, Paraguay offers amongst the best opportunities in sustainable forestry today.

In conclusion, forestry as an asset class is no revelation; in both the US and the UK it has retained a small but committed investor community. Many of these investments however, have been restricted by a fund's duration of 7 to 10 years, and have disregarded carbon sequestration and biodiversity in the process. By tweaking the design and structure of the underlying forestry asset to include a carbon sequestration strategy, we can establish a perpetual asset class from nature, which offers stable cash yield, sequesters carbon, prevents deforestation and increases biodiversity. Forestry has the potential to become the alternative asset of the future.

Charlie Sichel

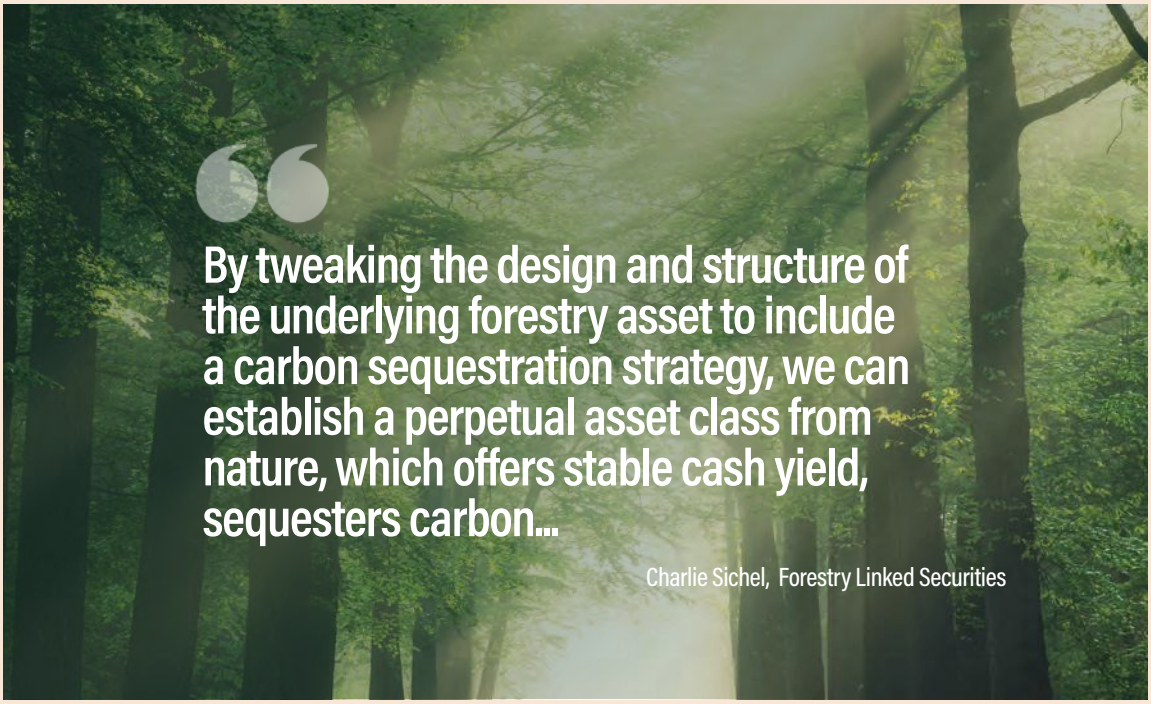
Charlie is a Managing Partner of Forestry Linked Securities (FLS®)

FLS® is a capital markets platform that develops and structures forestry investments for capital market investors, offering attractive returns, carbon sequestration, and best-in-class analytics and reporting.

The mission of FLS® is to turn sustainable forestry into a mainstream asset class and increase global allocation of financial assets to approx. 3% of worldwide Assets Under Management.

FLS® currently operates from offices in Switzerland, United Kingdom and Paraguay.

www.forestry.earth



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REGULATION

Presented by RQC GROUP

Sustainability disclosure, labelling and anti-greenwashing regime confirmed by the FCA

The FCA has published a Policy Statement that contains the final rules and guidance on sustainability disclosures, investment labels and the anti-greenwashing rule.

Commonly known as 'SDR' (the 'Sustainability Disclosure Requirements'; notwithstanding that disclosure is just one element of the framework), the regime will directly impact 'fiduciaries' – asset managers, life insurers and pension providers – when taking climate-related matters into account in the management or administration of assets.

Whilst the regime has a consumer focus, there are elements that also apply – or potentially apply – to non-retail asset managers including alternative asset managers that manage or sub-manage AIFs and UCITS.

The requirements can be summarised as follows:

- **Anti-greenwashing rule:** This applies to all FCA authorised firms. It reinforces the existing 'fair, clear and not misleading' requirement for financial promotions and other communications, allying this concept specifically to sustainability-related claims. The requirement takes effect on 31 May 2024.
- **Four labels:** This is an optional regime designed to assist consumers navigate the investment product landscape. The four labels – 'Sustainability Focus', 'Sustainability Improvers', 'Sustainability Impact' and 'Sustainability Mixed Goals' – are each subject to eligibility criteria and can be used from 31 July 2024.
- **Naming and marketing rules:** These rules are designed to ensure that the use of sustainability-related terms in product names and in marketing materials is accurate. This takes effect on 2 December 2024.
- **Consumer-facing information:** These are designed to provide consumers with better, more accessible information to help them understand the key sustainability features of a product.
- **Detailed information:** Firms with asset managers with AUM of £5 billion or more will be required to make additional disclosures at the pre-contractual, ongoing product and ongoing entity levels. This takes effect from 2 December 2025 for firms with AUM of £50 billion or more and 2 December 2026 for firms with AUM of between £5 billion and £50 billion.
- **Requirements for distributors:** This aims to ensure that product-level information is made available to consumers.

There are some key jurisdictional and product/service limitations. Aside from the anti-greenwashing rule, the requirements apply to UK AIFMs with UK AIFs, but not to non-UK AIFMs and/or non-UK AIFs. Hence, for example, a UK AIFM to a Cayman domiciled AIF would be out-of-scope. Discretionary and advisory managed account services are also out-of-scope, albeit the FCA is looking to consult on this in 2024, as are certain elements of the regime where the fund is not promoted to retail clients.

The regime will form part of a global 'patchwork' quilt of sustainability required frameworks, both mandatory (e.g., regulatory requirements) and voluntary. The FCA has aimed to align SDR with the existing EU equivalent, the Sustainability Finance Disclosure Regulation (SFDR) albeit differences between the respective regimes remain.

Embedding "Guiding Principles" for ESG and sustainable investment funds: FCA finds further work required

In advance of the publication of final rules on SDR, the FCA published a Multi-firm Review of Authorised Fund Managers ("AFMs"), to assess their embedding of the "Guiding Principles" in ESG and sustainable investment funds. The review found – as they often do - that while most AFMs worked hard to meet the FCA's expectations on the design, delivery and disclosure of their ESG and sustainable funds, further improvement was needed.

The FCA expects firms to address the good and poor practices in the report to meet the requirements of SDR; and of the Consumer Duty, which took effect in July 2023.

'Good practice' includes the development and use of appropriate ESG and sustainability scoring systems and benchmarks; and, where fund managers conduct thorough due diligence on third party data providers.

'Poor practice' focuses on disclosure and clarity of information provided to retail investors. Other examples relate to inconsistencies between fund holdings and a fund's ESG or sustainability objectives; and, difficulties in identifying the aim of stewardship activities and how these were aligned to fund objectives.

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REGULATION (cont.)

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'Must do better'… FCA's observations on IFPR implementation

The FCA has published its final report on how firms are implementing requirements on certain aspects of the Investment Firms Prudential Regime ('IFPR'), including the Internal Capital Adequacy and Risk Assessment ('ICARA') process.

IFPR, which took effect on 1 January 2022, is a prudential regime for investment firms and certain asset managers including UK AIFMs that also conduct non-AIF management activities.

The report follows on from earlier observations made in February 2023, and focusses on capital adequacy, liquidity adequacy and wind-down planning.

The key 'areas for improvement' are:

- Insufficient consideration of cashflows and liquidity stresses, meaning that some firms were at risk of running out of cash in stressed conditions;
- Internal intervention points do not ensure that actions would be triggered in a timely fashion to mitigate harm, particularly from firm failure;
- Wind-down assessments applied inadequate consideration of the impact of group membership; and,
- Failings in the application of capital models for operational risk.

Conduct and accountability – the net grows wider

Recent developments, such as clarifying the parameters of non-financial misconduct, expanding the range of individuals caught by corporate financial crimes, and an enforcement action against former Barclays CEO James Staley, serve to bring into sharper focus the UK's conduct and accountability regime for financial services personnel.

A recent article from RQC Group considers the implications of this and offers some key take-aways for firms.

Click here.

SEC and CFTC enforcement actions – over $9 billion in fines

The U.S. regulators, the Securities and Exchange Commission ('SEC') and the Commodities and Futures Trading Commission ('CFTC'), have each released their enforcement findings for financial year 2023.

The SEC filed 784 enforcement actions, obtained orders for nearly $5 million in financial remedies, and distributed nearly $1 billion to harmed investors.

The actions covered a wide range of areas, including Marketing Rule violations, failure to timely file required SEC forms, misstatements, market abuse, crypto, cybersecurity, ESG, and bribery and corruption.

The CFTC filed 96 enforcement actions resulting in over $4.3 billion in penalties, restitution, and disgorgement.

The actions concerned digital assets, manipulative and deceptive conduct, reporting and risk management and misconduct involving confidential information, among other topics.

High-profile cases included charging Sam Bankman-Fried, FTX and others, with an alleged fraudulent scheme involving digital asset commodities, and charging Binance, its founder and former Chief Compliance Officer with operating an illegal digital assets derivatives exchange.

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REGULATION (cont.)

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SEC charges CCO of investment adviser firm with multi-year fraud

The U.S. Securities and Exchange Commission ('SEC') announced charges against the president and CCO of registered investment adviser Prophecy Asset Management LP ("Prophecy"), for engaging in a multi-year scheme that concealed hundreds of millions of dollars in investor losses.

Prophecy was an adviser firm to several hedge funds with a reported AUM of over $500 million.

The SEC's order alleges that the CCO led investors to believe their investments were protected from loss because the fund's capital was spread amongst dozens of sub-advisers trading in liquid securities, all of which posted cash collateral to offset trading losses. In actuality, most of the fund's capital was directed to one sub-adviser investing in highly illiquid investments, resulting in losses in excess of $350 million by 2020 and the suspension of investor redemptions by Prophecy.

The CCO concealed those fund losses by engaging in sham transactions, falsifying documents, and telling investors their money was diversified in two other funds while collecting more than $15 million in fees.

The SEC's order finds that the CCO committed fraud, breached his fiduciary duties to investors, and therefore violated the antifraud provisions of federal securities laws. The SEC has sought a permanent injunction, disgorgement of ill-gotten gains with interest and civil penalties, and an officer and director bar.

In parallel, the U.S. Attorney's Office for the District of New Jersey also announced criminal charges.

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