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Atoms: Identifying Structural Long-Term Trends Driving Sustainable Investing

Sebastien Beguelin, Senior Fund Manager at Royal London Asset Management, discusses how the physical world is undergoing a once-in-a-generation investment boom.

Atoms, bytes and genes represent our way of thinking about the evolution of the physical, digital and natural worlds, which constitute everything around us. Ample evidence suggests that trends in these areas will drive growth in the corporate world for many years to come. We explore these areas in a three-part series.

We live in an increasingly uncertain environment driven by a changing macroeconomic environment and financial market structure. From a macroeconomic standpoint, the 2010s were a unique period characterised by a very stable environment of low growth, low inflation and low interest rates. The pandemic was the trigger to exit this environment; what the new environment is, only time will tell. Meanwhile, financial markets are increasingly driven by passive, algorithmic trading which is creating significant short-term volatility.

Yet, while this environment of increased uncertainty and volatility is confusing a lot of investors, we believe the microeconomic trends are strengthening, and focusing on them makes it easier for us to understand the world. Our framework to analyse these microeconomic trends is via atoms, bytes and genes.

What are Atoms?

From a fund manager point of view, we define Atoms as investments into the physical world. These investments are very diverse and can include industrial production capacities in the form of factories, like Taiwan Semiconductor Manufacturing (TSMC) spending $100bn to build advanced semiconductor fabrication plants in Arizona[1], and infrastructure investments like the Ofwat-approved £104bn upgrade to the UK's water system[2].

They can also take the form of investments into energy like the €300bn REPowerEU Plan that will support investments into renewables with the aim of doubling the amount of solar energy[3].

We see increased focus on investments, and politicians wanting to reindustrialise: the UK government talking about Britain building again; the US Administration is using tariffs to facilitate reshoring; and large technology companies are investing – an example being Microsoft spending $80bn into data centres to meet demand for cloud computing and artificial intelligence (AI)[4]. We believe overall these investments are only starting to happen given they are propelled by structural themes.

1 TSMC Intends to Expand Its Investment in the United States to US$165 Billion to Power the Future of AI
2 Ofwat approves £104bn upgrade for the water sector - Water Magazine
3 Two years of REPowerEU: Strengthening Europe's energy resilience - European Commission
4 Microsoft plans to invest $80 billion on AI-enabled data centers in fiscal 2025 | CNN Business

Why is it happening?

The first long-term driver is energy transition which requires a fundamental reshaping of the way we produce and consume energy. From a production perspective, more than 80% of global energy consumption is still coming from fossil fuels, however the IEA estimates renewables accounted for 38% of the growth in energy supply in 2024. On the consumption side, some estimates call for energy-efficiency gains to double to reach Paris Agreement targets. These includes not only renewables but also investments into rail infrastructure, which provides a low-CO_2 alternative to aeroplanes and cars; battery and storage to stabilise the grid and to support renewable penetration.

The second long-term theme is that Western countries are suffering from a chronic under-investment in infrastructure. After the global financial crisis, corporates and governments shunned capital investments and so a decade of underinvestment has now culminated in today's supply side issues – these will require significant investments to correct for this error.

The US being a prime example – according to the American Society of Civil Engineers, the US has a $2.6tr infrastructure investment gap and that underinvestment could cost US$10 trillion in GDP and three million jobs by 2039[5].

The third was triggered by the pandemic which showed a long period of optimisation has resulted in fragile supply chains that are not able to withstand exogenous shocks and so companies need to rebuild redundancy and resilience. Lastly, geopolitics are also playing a role with increased tensions globally as many countries want to reduce external reliance in strategic sectors.

How can investors benefit?

The physical world is undergoing a once in a generation investment boom and we believe this is well aligned with sustainability and our objective of investing into companies making the world cleaner, healthier, safer and more inclusive. We like several companies from our portfolios that fit into this investment theme.

A few examples include:

Schneider Electric: a leader in energy management and industrial automation offers solutions to digitise, electrify and decarbonise operations, significantly contributing to a cleaner society.

Core & Main: a distributor of US water products will help support investments into the aging US water infrastructure where water networks are estimated to lose 2.1 trillion gallons of water a year (5.9 billion gallons a day, or 17 gallons per person per day)!

Wabtec: a provider of rail locomotives, the company is at the forefront of making locomotives more fuel efficient and is also developing battery powered locomotives.

At a time of considerable uncertainty, we believe our atoms, bytes and genes framework helps us identify the structural long-term trends and combined with our disciplined approach support us in navigating increasingly uncertain and volatile markets.

5 Source: OECD

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