SALT

Salt Sustainable Global Fixed Income Opportunities Fund Fact Sheet – January 2024

Manager Profile

Salt Funds Management is a boutique investment management firm wholly owned by its employees which specialises in actively seeking to maximise returns while managing the risks of the investment. Salt examines investments for their environmental and social impact as well as the quality of their governance.

Investment Strategy

The primary objective of the Fund is to target and generate an attractive rate of return over a full three-to-five-year market cycle. To achieve this, the Fund targets a portfolio of global fixed income securities with enhanced total return potential and superior Sustainability characteristics.

The objectives of this top-down selection process are to:
1. Reduce exposure to material ESG risk and negative sustainability impacts, through restriction screening of controversial sectors such as weapons, tobacco and some fossil fuels, as well as international norms violations;
2. Tilt the portfolio in favour of the 80% strongest sustainability performers across corporates, by sub- sector, and sovereigns; and
3. Contribute to positive outcomes based on key sustainability themes, with a particular focus on low carbon intensity.

The Fund will invest at least 50% in investment grade bonds, and a minimum of 15% in sustainable bonds. The fund targets its returns to be 100% hedged to the New Zealand dollar.

Fund Facts at 31 January 2024

Benchmark for ESG purposes	Bloomberg Global Aggregate Index (NZD hedged)
Fund Assets	$84.75 million
Inception Date	10 February 2023
Underlying Manager	Morgan Stanley Investment Management
Average credit rating	Standard & Poor's A- / Moody's Baa1
Effective Duration	3.04 years

Unit Price at 31 January 2024

Application	1.0311
Redemption	1.0300

Investment Guidelines

The guidelines for the Sustainable Global Fixed Income Opportunity Fund are:

Global Fixed Income securities	95% – 100%
Cash	0% – 5%

Fund Allocation at 31 January 2024

Global fixed income securities	97.3%
Cash & FX hedging	2.7%

Fund Performance to 31 January 2024

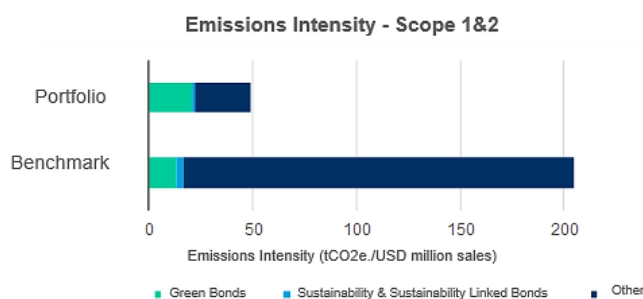
Period	Fund Return (Gross incl. ICs)
1 month	0.29%
3 month	4.63%
6 month	3.90%
Since inception cumulative	5.52%

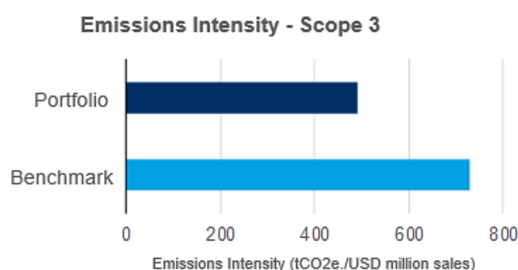
Performance is gross of fees and tax. Data as of 31 January 2024.

Fund ESG Dashboard	Portfolio	Index	Monthly change
MSCI ESG Score (MV%.)	98.3%	91.7%	0.0%
Exposure to Corporates with CO2 footprint reduction targets	95%	88%	
Green, plus Social, Sustainability and Sustainability-linked bonds	20.5%	2.6%	+3.0%
Sustainable SBTi approved / committed targets	46.8%	37.9%	+0.1%
CO2 Footprint Scope 1&2 (tCO2e/$mn emission intensity)	46	201	-5.2%
CO2 Footprint Scope 3 (tCO2e/$mn emission intensity	492	724	+0.2%
MSCI ESG Score (Adjusted)	7.58	6.33	-0.03
- Environment score	7.75	6.14	-0.05
- Social score	5.52	5.51	-0.04
- Governance score	6.31	5.78	+0.04

Source: MISM Monthly Investment Report/ MSCI ESG Research as at 31 Jan. 24

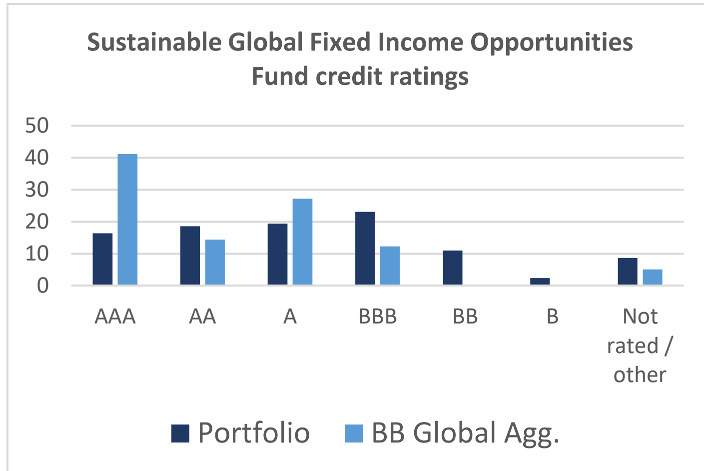
Fund CO2 Emissions Intensity characteristics at January 2024





Source: MISM Monthly Investment Report as at 31 January 2024

Fund credit ratings vs. Bloomberg Barclays Global Agg.



Source: MISM as at 31 January 2024

Portfolio Review

- In the one-month period ending January 31, 2024, the portfolio returned 0.29%. The performance can be attributed to the following factors:
- Macro Decisions were mixed while sector spreads (long credit risk) contribution were positive this month.
- The portfolio's duration positioning in Developed Markets (DM) rates (USD, GBP) was negative as yields rose.
- The allocation to Investment Grade (preference for EUR over USD, bias to financials, focused on significantly important institutions), and high yield corporates (predominantly industrials) both contributed given tighter spreads in the US and Europe.
- Within securitized assets, the allocation to ABS and non-agency RMBS was positive.
- Positioning in currencies was broadly negative (short USD and short CAD).

Market Review

- January was a month of two halves in developed market fixed income. In the eurozone, European Central Bank (ECB) Governing Council members in Davos repeatedly stressed the extent to which inflation is still above target in attempts to pour cold water on hopes of a rate cut by spring.
- Towards the end of the month, however, policy communication turned more dovish as President Lagarde acknowledged softer-than-expected inflation prints and a weakening labour market at the January ECB policy meeting. Even her traditionally hawkish colleagues acknowledged progress on prices and hinted a willingness to consider earlier cuts, depending on the data.
- In the U.S., a steady grind higher in yields reversed as investors became more convinced the U.S. Federal Reserve (Fed) would ease policy aggressively over the next two years, even as a March cut was seen as less likely. Finally, at the end of January, worries about the health of U.S. regional banks led to a risk-off move in markets that pushed yields even lower.
- After a round trip, U.S. Treasury yields ended January 2 basis points (bps) higher than at the end of December, while German bunds (+15 bps) and U.K. gilts (+24 bps) lagged; the U.S. and eurozone yield curves were slightly steeper.
- On foreign exchange, the dollar continued to appreciate against peers over the course of the month. Sterling was another strong performer as December inflation posted a large upside surprise and yields on gilts climbed.

Portfolio Commentary & Outlook

- There were no material changes in strategy during the month. Overall, the duration of the portfolio was reduced (-0.32 years) from December to 3.04 years as at end-January.
- The beginning of the developed market easing cycle now appears in sight, with central bank communication – especially at the ECB – becoming more dovish. That said, with data remaining generally resilient, it remains to be seen how quickly and how far central banks feel they need to cut rates.
- We continue to see opportunities in several cross-market rates trades, with Canadian and U.S. rates expected to converge further based on valuations and still-sticky inflation in the former. With the market now focused on likely normalisation by the Bank of Japan in the first half of this year, Japanese duration looks set to underperform, and indeed failed to follow the rally in other developed markets in late January.
- In January, euro investment grade spreads marginally outperformed U.S. investment grade spreads, as credit market spreads broadly tightened. Market sentiment in the month was driven by several factors. Firstly, the positive credit market backdrop was maintained by the growing expectations that central bank monetary policy had shifted to easing financial conditions/lower interest rates with the focus pivoting from inflation concerns to growth.
- Secondly, there was no further escalation in geopolitical concerns, with news in the Middle East/Red Sea viewed as a regional and non-systemic event. Thirdly, merger and acquisition (M&A) rumours, unfavourable legal rulings and earnings revisions created single-name credit volatility.
- Finally, technicals were supportive, driven by strong inflows into investment grade credit alongside the large new issue pipeline. Initially this caused some volatility, but supply was matched with strong demand, as evidenced by falling new issue premiums, which supported the move tighter in credit spreads.
- The U.S. and global high yield markets recorded a sluggish return in January as performance sputtered. January was characterised by a surge in primary issuance, continued retail flows and several high-profile liability management exercises. The lower quality segments of the market generally underperformed in January.

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- Our base case remains constructive for credit against an improving macro backdrop following the central bank pivot from concern about inflation to concern about growth, and the positive momentum driven by inflows into the asset class. Considering valuation, we see a market that is fairly priced but cheap relative to other markets, and hence we see carry as an attractive return opportunity. But given the uncertain medium-term fundamental backdrop, we have less confidence in expected spread tightening. In high yield, our outlook remains relatively cautious given the valuations that, on average, nearly fully reflect a perfectly soft economic landing. The silver lining is the historically high all-in yield that supports a positive return for high yield investors in 2024, even in our bear case scenario analysis.

- Securitised credit spreads continued to tighten in January as demand remained very strong and new issue deals were consistently oversubscribed. Consumer credit delinquencies continue to rise, especially for lower-income, lower-credit-score borrowers, but overall delinquencies remain non-threatening at current levels. European securitised market activity remained slow in January, although we have seen an uptick in U.K. residential mortgage-backed securities (RMBS) issuance. European securitised spreads continue to trade tighter than comparable U.S. securitised spreads due to lack of supply.

- After several months of spread tightening across securitised products, we expect spreads to stabilise at current levels in February. Overall demand levels remain strong, but we believe it will be challenging to push spreads much tighter from current levels.

- Performance was mixed for emerging markets (EM) debt for the first month of 2024. The U.S. dollar strengthened, and most EM currencies weakened during the period while sovereign spreads widened, and corporate spreads tightened. Several EM central banks in Latin America (Brazil, Colombia and Chile) and Europe, Middle East, Africa (Armenia and Hungary) cut rates as inflation continued to recede.

- The Fed steered away from the idea of a rate cut in the next few months, but a tightening cycle is still on the horizon. We believe EM assets are positioned to be a favourable asset class this year as valuations remain attractive and as developed markets start to cut rates, which will likely support a favourable environment for emerging markets to continue on their rate cutting path.

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