SALT

Salt Sustainable Global Fixed Income Opportunities Fund Fact Sheet – April 2023

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 30 April 2023

Benchmark for ESG purposes	Bloomberg Global Aggregate Index (NZD hedged)
Fund Assets	$58.61 million
Inception Date	10 February 2023
Underlying Manager	Morgan Stanley Investment Management
Average credit rating	Standard & Poor's A- / Moody's A3
Effective Duration	3.5 years

Unit Price at 30 April 2023

Application	1.0052	0.9954
Redemption	1.0041	0.9913

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 30 April 2023

Global fixed income securities	97.8%
Cash	2.2%

Fund Performance to 30 April 2023

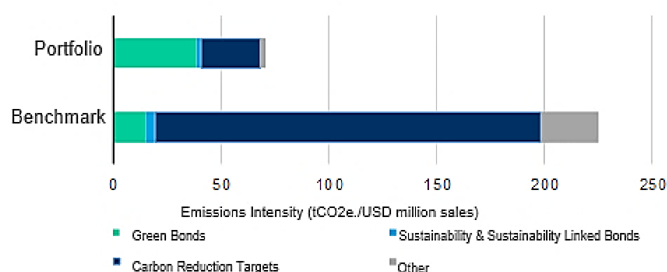
Period	Fund Return (Gross)
1 month	0.43%
Since inception cumulative	0.63%

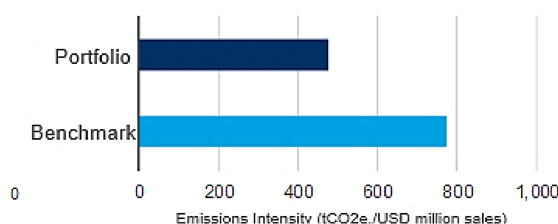
Performance is gross of fees and tax. Past performance is not a guarantee of future results. Data as of 30 April 2023.

Fund ESG Scores	Portfolio	Index	YTD change
MSCI ESG Score (MV%)	96.3%	91.4%	-
MSIM ESG Credit Score	6.10	5.71	-
MSCI ESG Score adj.	7.48	6.34	7.48
- Environment score	7.34	6.16	7.34
- Social score	5.59	5.57	5.59
- Governance score	6.14	5.76	6.14
MSIM ESG Sovereign score	2.12	2.11	-

Source: MISM Monthly Investment Report / MSCI ESG Research as at 30 April.

Fund CO2 Emissions Intensity characteristics at 30 April 2023





Source: MISM Monthly Investment Report / MSCI ESG Research as at 28 April

Labelled sustainable bond major holdings > 1%	MSCI ESG rating
Top 5	
European Union MTN (Social)	A
BNP Paribas MTN (Green)	AA
European Investment Bank (Green)	AAA
Council of Europe Development Bank MTN (Social)	AAA
Export-Import Bank of Korea (Green)	BB

Source: MSIM, data as at 28 April 2023.

Portfolio Review

- In the one-month period ending 30 April 2023, the portfolio returned 0.43% (gross of tax & fees). The performance can be attributed to the following factors:
- The portfolio's positioning in duration was the main positive driver (especially US rates) as yields declined at the 2-10 year part of the yield curve last month.
- Within investment grade credit, spreads tightened with financials outperforming industrials and utilities.
- The portfolio's exposure to high yield credit detracted, with most of the losses stemming from the exposure to industrials.
- Exposure to government related debt added to performance in April, in contrast to March's impact.
- The portfolio's exposure to securitized debt was a large contributor to positive performance.

Strategy Changes

There were no material changes in strategy during the April month.

Portfolio Commentary & Outlook

Developed market rates were mixed in April, with yields largely moving sideways in most economies, with US yields falling slightly.

As volatility declined slightly following March's banking sector stress, the market shifted to interpreting new economic data and predicting the prospect and significance of a credit crunch. In the US, while the labour market data, Employment Cost Index, and PCE inflation data came in stronger than expected, ISM Manufacturing data and JOLTS labour market data came in weaker than expected.

Elsewhere, in New Zealand, yields fell as CPI data came in softer than expected, while in contrast, yields in the UK rose on the back of stronger inflation data. In terms of central bank meetings, the RBNZ surprised markets, hiking by 50bps vs the 25bps expected. The RBA and BoC kept rates the same as expected. The Riksbank raised rates by 50bps as anticipated. Finally, the BoJ, in Ueda's first meeting as governor, kept the policy the same, including the YCC.

While the acute stress from the banking sector issues has mitigated, the problems have not fully gone away, thus will continue to impact the economy. Despite the lack of clarity regarding the magnitude of the economic impact, credit conditions are likely to tighten even further. Therefore, we continue to monitor the situation and we will be closely watching the upcoming quarterly SLOOS data in the US. The market is pricing scenarios where the Fed goes much higher (i.e. taking rates to 5.75%/6%), as well as pricing in a greater likelihood of a recession.

Unfortunately for the Fed, while the banking issues will likely be disinflationary, CPI, ECI, and PCE data again confirmed that inflation and wages are still elevated and sticky. Given the uncertainty, it is difficult to concretely express an outright view on interest rates, and it may be wise to be patient for now, awaiting further clarification while taking advantage of more relative dislocations. In terms of foreign exchange, coming into this situation, we thought the US dollar could weaken, which it has continued to do. We still believe that dollar weakness could continue.

Euro Investment Grade (IG) spreads outperformed US IG spreads this month amidst elevated credit market volatility driven by several aforementioned factors. Main themes included US bank volatility and weaker US economic data. European data remained more robust, reflecting the reduced impact of supply chain disruption and the continued support of fiscal programs like the European Recovery Fund. Similarly global labour markets remain strong supporting consumption and labour price inflation leading to continued rate hike expectations/tighter monetary policy. Q1 reporting mostly outperformed expectations with Financials benefitting from higher net interest margin, while non-financials highlighted continued pricing power, the benefits of the re-opening (airlines) and the impact of prior cost cutting (cyclicals).

Volatility in the US and global high yield markets receded in April and the demand for credit risk generally improved amid lackluster secondary trading volume and renewed capital markets activity. Investors took advantage of still historically attractive yields and the higher-beta segments of the high yield market generally outperformed
Our base case view remains that we are compensated to own credit as we view corporate fundamentals to be resilient and the macro backdrop to likely improve as monetary policy tightening pauses and China re-opens. We view companies as having built liquidity in recent quarters and implemented cost efficiencies under the COVID-era.
We expect profit margins to be pressured by increased costs (although Q1 reporting suggests companies are protecting margins in the short term) and top line revenue to be challenging but given the starting point we believe corporates will be able to manage a slowdown without significant downgrades or defaults (base case low default and low growth). Supportive for the IG Credit market is demand for high quality fixed income assets at absolute yields not seen for a number of years.

We remain cautious on the high-yield market as we progress through the second quarter of 2023. Episodic weakness accompanied by volatile spread movement seems to be the most likely path forward due to several factors, starting with clear evidence of existing cracks in the US economy and what we view as the increasing likelihood of a hard economic landing. After the volatility and spread widening in March, the securitized markets stabilized in April, although spreads remain materially wider over the past two months. We continue to believe that the fundamental credit conditions of residential housing loan markets remain sound, but also believe that higher risk premiums are warranted across all credit assets given projected economic weakness. We remain concerned about global economic conditions, and we expect employment rates to decline and households to experience greater stress. We expect home prices to fall another 5-10% for the remainder of 2023. US residential credit remains our favourite sector and we remain more cautious of commercial real estate, especially office, which continues to be negatively impacted in the post-pandemic world.

Emerging Markets debt delivered positive returns for the month. Many emerging markets currencies strengthened during the month, spreads tightened in EM corporates and were flat in hard currency sovereign but the rally in US Treasury yields contributed to performance.
The volatility stemming from banking stresses in developed markets has put a damper on the macro picture to some degree. That said, we remain constructive on the asset class. Growth, inflation, and policy are quite differentiated among countries and credits within the emerging markets universe so bottom-up analysis is critical to uncover value.

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