

SALT

Salt Sustainable Income Fund Fact Sheet – April 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 Fund aims to provide a gross fixed quarterly income (after fees and expenses but before tax) in excess of bank deposit rates, along with a positive return on capital on a rolling three-year basis. Deposit rates are proxied by the NZ Bank Bill Index.

A Reference Portfolio is provided, medium-term outperformance of which is a secondary objective, consisting of the weighted sum of components.

The Fund targets a diversified mix of growth and defensive assets, with a focus on securities with Environmental, Social and Governance features & reliable income generation. The Fund's strategy is to invest in a quality asset mix to provide regular, sustainable income and a positive return on capital. The value of the fund will fluctuate in line with listed market developments, but the primary focus is enhanced income and thus, shorter-term variability is an expected feature. Income is prioritized above capital gain in the fund, nevertheless, the allocation to both growth and yielding assets allows for both objectives to operate over the medium- and longer-term horizons.

Fund Facts at 30 April 2024

| | |
|----------------------------------------------------------------------------------|-------------------------------------------------------|
| Benchmark | Bank deposit rates (BNZBIL Index) |
| Reference portfolio | SAA-weighted component benchmark indices' performance |
| Fund Assets | \$44.37 million |
| Inception Date | 19 June 2021 |
| Portfolio Manager | Greg Fleming |
| Prospective distribution yield (cents per unit) / based on Unit Price of 1.05.23 | 1.125 cents per unit per Quarter / 5.21% per annum |

Unit Price at 30 April 2024

| | |
|-------------|--------|
| Application | 0.8680 |
| Redemption | 0.8644 |

Sustainability Metrics

| Fund ESG Scores | Portfolio | Category ave |
|-----------------------|-----------|--------------|
| Morningstar ESG score | 21.19 | 22.00 |

Scores indicate risk level – a lower score reflects a lower ESG multi-factor risk level. ESG score as at 30.04.24. Sustainability provides issuer-level ESG Risk analysis used in the calculation of Morningstar's Sustainability Score. Sustainable Investment Mandate information is derived from the fund prospectus.

Investment Guidelines

| Sector | Target | Range |
|------------------------------|--------|-----------|
| Global Fixed Interest | 35% | 0% – 60% |
| Australasian Shares | 30% | 15% – 45% |
| Global Listed Property | 15% | 0% – 35% |
| Global Listed Infrastructure | 15% | 0% – 35% |
| Cash or cash equivalents | 5% | 0% – 20% |

See "Salt Statement of Investment Policy and Objectives, 30 June 2022"

Fund Allocation at 30 April 2024

| | |
|------------------------------|-------|
| Global Fixed Interest | 32.0% |
| Australasian Shares | 29.0% |
| Global Listed Property | 21.0% |
| Global Listed Infrastructure | 17.0% |
| Cash or cash equivalents | 1.0% |

Asset allocation to Fixed Interest + Cash 33.0%

Fund Performance to 30 April 2024

| Period | Fund Return (before fees) | Gross Reference Portfolio Return |
|----------------------|---------------------------|----------------------------------|
| 1 month | -0.84% | -1.82% |
| 3 months | 1.02% | 0.19% |
| 6 months | 9.09% | 8.96% |
| 1 year | 2.63% | 1.13% |
| 2 years p.a. | -0.36% | -0.63% |
| Since inception p.a. | -0.72% | -0.70% |

Performance is before fees and tax, adjusted for imputation credits. Reference Portfolio return is gross.

Top Individual Holdings at 30 April 2024

| | |
|----------------------------|---------------------------------|
| US 5Yr Note (CBT) Jun24 | Infratil |
| Goodman Property Trust | Auckland International Airport |
| US 2YR Note (CBT) Jun24 | Spark New Zealand |
| Fisher & Paykel Healthcare | Vital Healthcare Property Trust |
| Precinct Properties NZ | Kiwi Property Group |

SALT FUNDS MANAGEMENT

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Market Commentary

- After a generally positive first quarter of 2024, the second quarter is off to a rough start. In the US, continued higher-than-expected inflation and a GDP print that, while weak at first blush, revealed still strong private demand. This fuelled fears that central banks will not ease monetary policy as quickly as previously hoped.
- Both equity and bond markets reacted negatively to this development with developed market equities down -3.7% (in USD) over the month and the global aggregate bond index down -2.5% (in USD).
- There was no US Federal Reserve meeting in April, though there were plenty of opportunities for FOMC members to voice their opinions. The most important of these was Chair Powell's observation that recent data had shown a lack of further progress on inflation, and it was therefore appropriate to give restrictive monetary policy more time to work.
- In Europe the annual rate of CPI inflation was unchanged at 2.4% in April, but the policy-critical services component fell from 4.0% to 3.7%.
- This, combined with low growth in the Euro area, has given markets confidence that a rate cut in June is still likely, though there are now fewer cuts priced in over 2024 than previously.
- Japanese equities gave up some of their recent gains in April. Ongoing downward pressure on the Yen in leading to fears of higher imported inflation weakening domestic demand.
- China's official manufacturing and non-manufacturing PMI indices for April weren't great but weren't bad either. Both came in lower than March but still in expansion territory (over 50). That suggests that growth is stabilising rather than sprinting ahead. That's consistent with the modest stimulus deployed to date. And given the ongoing issues in the property sector, stability isn't a bad thing.
- March quarter inflation came in hotter than expected in Australia. This led to speculation the RBA may be forced to hike interest rates again. Indeed, markets shifted from pricing in rate cuts this year to a chance the next move could be a hike.
- In New Zealand, March quarter inflation printed in line with expectations. The annual rate of CPI inflation fell to 4.0%, though the disinflationary process remains unbalanced. Tradeable (imported) inflation came in at 1.6% for the year while non-tradeable (domestic) inflation came in at 5.8%. However, economic activity remains weak allowing the RBNZ a degree of confidence that monetary policy is working, and that message was reflected in the statement following the April RBNZ Monetary Policy Review.

Salt Sustainable Income Fund Commentary

The Sustainable Income Fund's rebound paused in April, with a return of -0.84% (before fees) in the month, which led its quarterly return to 1.02%, its six-month gain to 9.09% and its one-year return to 2.63% (before fees.) April's broad market weakness in equities and bonds reflects reconsiderations in markets as to the likely scale of lower central bank interest rates. Uncertainty on central banks' easing timing has influenced the listed Real Asset and Bond returns within the portfolio, after their strong late-2023 gains.

For the three-month period to 30 April, the Sustainable Income Fund was ahead of its reference index, outperforming by 0.83% (on a gross basis.) The six-month period since November was strong, with the fund gaining 9.09% (gross) which was slightly ahead of the reference portfolio. For the year to 30 April, the portfolio's reference index rose by 1.13% which was -1.50% behind the Sustainable Income fund's 2.63% one-year gross return.

As inflation progressively shows signs of a definitive down-shift, we expect component asset classes to improve further, as global central banks will ultimately embark on interest rate easings. Volatility across markets is ever-present but sentiment is much less fragile. Central banks around the world remain vigilant but have scope to assess the impact of high rates on inflation pressures positively, and incrementally lower rates. We expect value recoveries in interest-rate sensitive assets to continue in H2 2024.

However, markets expressed excessive optimism in late-2023 as to how swiftly those central bank rate cuts are likely to eventuate. A more realistic turn in Q1 2024 explains the moderating returns from the most interest rate-sensitive asset components of the Income fund.

April month saw small negative returns contributions from all components of the Income Fund except the NZ Dividend Appreciation Fund, which contributed +0.06%. The Salt Sustainable Global Infrastructure Fund, which subtracted -0.23% and the Enhanced Property Fund, -0.30%. The Global Fixed Interest Opportunities Fund made a small negative monthly contribution of -0.19% and the Sustainable Global Property Fund had a negative impact of -0.18%, In April.

Salt Sustainable Income Fund outlook

Markets got ahead of themselves in late-2023 in anticipating central bank rate cuts, though these are still expected for later this year. We believe bond yields have now adjusted sufficiently (via a volatile and uncertain route in the last 18 months) for us to move progressively toward a higher bond positioning within the Sustainable Income Fund. We consider inflation risk now poses a reduced danger to the capital valuations of bond portfolios. The allocation to bonds is now 32% vs a 35% SAA. Our next step will be to increase this even closer toward a Neutral allocation.

The Reserve Bank of New Zealand has remained "on hold" with the Official Cash Rate, as core inflation is persisting, so domestic yields and discount rates are likely to stay fairly elevated. This suppressed returns from NZ equities through 2023 and early 2024, and the relative weakness of NZ shares compared to global equities remains a notable feature. There is some scope for improved NZ returns later this year, and the latest RBNZ Monetary Policy Statement indicated a less aggressively-restrictive tone than had been feared. Domestic inflation pressures are slow to fade out.

Diversified Income Funds containing an allocation to domestic equities have generally experienced low overall capital value gains in early 2024, although their income yields remain attractive by historical standards, as the NZ equity market has moved sideways overall for the last two years.

Until a catalyst for a resumption in NZ equity market performance emerges, much of the medium-term capital growth objective of the Fund will be driven by international assets, which comprise half of the Portfolio at current allocation weightings.

We anticipate the longer-term capital growth strategies within the Sustainable Income Fund to boost performance, as inflation conditions are improving. However, there is still a mildly recessionary period to traverse en route to that outcome (in New Zealand, if not globally.) The phase of actual interest rate reductions from central banks is still some months into the future but when that is underway, we expect more beneficial capital growth impacts. This positive portfolio role will likely be a key feature of total returns in 2024-5.

As the primary objective of the Salt Sustainable Income Fund is to invest in quality sustainable yield payers, minimizing short-term capital price fluctuation is secondary. Market volatility allows us to acquire high quality and defensible dividend-paying assets for the Fund at better prices.

Distribution of 1.125 cents per unit / quarter retained

Higher component asset yields enabled us to retain the quarterly cents-per-unit distribution from the fund, at 1.125 cpu, for the latest quarterly distribution which is paid out / reinvested in May. This will be updated again in September 2024, dependent on the outlook for overall Fund's income.

As noted earlier, the silver lining in the bond market's repricing is that the yield received from bond investments have shifted to a higher range and that supports the Sustainable Income Fund's forward distribution path. This is characteristic of a transition into a mid-level interest rate regime which may endure for years, rather than months, ahead.

Internationally, major central banks are now communicating the phase of interest rate adjustments, sufficient to anchor inflation expectations, has been successful. Recently, the balance of evidence has been on the better side globally, particularly suggesting that the US Federal Reserve is well on track to deliver an economic "soft landing." Rate reductions will follow incrementally later this year. In New Zealand, the timing is uncertain, as the Reserve Bank will need to assess the trajectory of inflation in mid-2024 and may not actually move the OCR down until the last quarter of the year.

While the data-driven market volatility at times requires fortitude from investors, the objective of securing an inflation-resilient income level means that equity market fluctuations and corrections over short periods are inevitable. Over the medium-term, moderate capital gains in addition to income advantages are expected, and the Sustainable Income Fund is positioned to harvest them.

It is crucial to note that the Income level from equity dividends and bond coupons received into the fund has been commensurately rising through periods of market turbulence. This trend exemplifies the incremental return of some "risk premia" into asset classes.

The fund's modelled income received from coupons and dividends is still modestly above its prospective distribution yield. We regard this as prudent, in a still-uncertain environment.

The equity capital value components of the Income Fund have adjusted to reflect weaker economies overall, yet the Real Asset components of Infrastructure and Property are well-suited to the subdued immediate period ahead, as central bank policy rates will begin to fall. Defensive merit should continue to be asserted in coming months through renewed demand for these specific "Real Asset" equity types, along with the sustainable dividend-payers in the broader Australasian market.

In late March, we lowered the Fund's allocation to the Enhanced Property Fund by 2.5% and lifted the Fund's investment in the Sustainable Global Fixed Income Opportunities Fund by 2.5%. This increased the Defensive allocation within the Income Fund to 33%, in line with the economic outlook. The yield impact on the Dynamic Asset Allocation switch was negligible, but we think that Sustainable Global Bonds still have upside potential, and lower volatility risk than Australasian listed property stocks.