SALT

Salt Sustainable Global Shares Fund Fact Sheet – December 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 Fund's investment objective is to outperform (after fees and expenses but before tax) the MSCI World (Net) Index in New Zealand dollars on a rolling three-year basis. To achieve this, the Fund targets a portfolio of global companies with high total return potential and high Environmental, Social and Governance (ESG) factor scores.

The strategy seeks to provide attractive long-term returns with less long-term volatility than the broader market by reducing the risks associated with poor ESG outcomes. The Fund will seek to achieve its investment objective by investing primarily in global equity.

Fund Facts at 31 December 2023

Benchmark	MSCI World (Net) Index in NZD
Fund Assets	$60.60 million
Inception Date	12 July 2021
Underlying Manager	Morgan Stanley Investment Management

Unit Price at 31 December 2023

Application	1.1391
Redemption	1.1344

Investment Guidelines

The guidelines for the Sustainable Global Shares Fund are:

Global Equities	95% – 100%
Cash	0% – 5%

Target investment Mix

The target investment mix for the Salt Sustainable Global Shares Fund is:

Global equities	100%

Fund Allocation at 31 December 2023

Global equities	98.3%
Cash	1.7%

Fund Performance to 31 December 2023

Period	Fund Return*	Benchmark Return
1 month	1.38%	2.34%
3 months	5.49%	5.73%
6 months	3.17%	4.08%
1 year	22.39%	23.64%
2 year p.a.	2.89%	4.67%
Since inception p.a.	6.67%	7.27%
5 year p.a.*	13.95%	14.11%

Performance is before fees and tax and adjusted for imputation credits. Benchmark performance is gross. Past performance is not a guarantee of future results. Data as of 31 December 2023. *5 year strategy performance is gross of fees.

Fund ESG Scores	Portfolio	Index
Sustainable Global Shares	26T CO2 /$m	162T CO2 /$m
Portfolio Carbon Footprint:	15% of MSCI World Index*	

Source: MISM Quarterly Investment Report & Trucost based on the Scope 1 & 2 carbon emissions per $1million of Portfolio companies' sales, and as weighted average carbon intensity (WACI). *As at December, 2023, the Portfolio's carbon footprint was 85% lower than the MSCI World Index and 86% below AC World.

Top 10 holdings	
Microsoft (US)	Intercontinental Exchange (US)
SAP (DE)	Constellation Software (CA)
VISA (US)	IQVIA (US)
Accenture (US)	Becton Dickinson (US)
Thermo Fisher Scientific (US)	Danaher (US)

Source: MSIM, data as at 31 December 2023.
The Top 10 Holdings represented 43.38% of the total portfolio.

Market Review

- After something of a reality check in the third quarter of the year, the December quarter saw strong returns across nearly all asset classes. Further progress on inflation saw markets anticipating earlier interest rate cuts leading to an 11.5% (in USD) rally in developed market equities and an 8.1% (in USD) return from the global aggregate bond index.
- Asset classes that have struggled most under the interest rate mantra of "higher for longer" such as real estate investment trusts showed some of the highest returns. Global REITS rallied 15.6% over the quarter.
- As the quarter began markets were becoming increasingly convinced that interest rates in the key developed markets had peaked. Softer than expected inflation prints in the US and Europe had markets bringing forward rate cut expectations.
- This expectation was reinforced by a dovish December statement from the US Federal Open Market Committee where the latest projections removed the final hike from prior projections and added an extra cut

into 2024. By the end of the quarter US interest rate markets were anticipating six 25-basis point cuts in the Fed funds rate in 2024, an expectation we think will ultimately be disappointed.

- Activity data in Japan remained somewhat sluggish over the quarter. September quarter GDP data showed weaker-than-expected domestic demand, consumption, and capital expenditure. The focus remains on wage growth where the strength of corporate earnings supports the expectation of further wage growth next year. The Bank of Japan left monetary policy unchanged at its December meeting, though we expect they may end their Yield Curve Control and Negative Interest Rate policies as early as their January meeting. This is based on our view that such moves are as much about policy normalisation as concerns about inflation.

- The sluggish December PMI readings out of China suggest that fourth GDP will likely slip further. Some rebound in the manufacturing PMI in January 2024 is likely with pass-through of the Rmb1trn additional fiscal support to infrastructure projects flows through. However, its sustainability still bears watching. China's reflation journey will remain bumpy and gradual.

- As we expected, the Reserve Bank of Australia resumed rate hikes in November following a run of stronger than expected activity, labour market and inflation data. The 25bp hike took the cash rate to 4.35%. They left rates unchanged at the December meeting, though we continue to expect one further hike to 4.6%, most likely at the February meeting.

- In New Zealand, there was a meaningful softening in labour market pressures with a decline in employment and a rise in the unemployment rate from 3.6% to 3.9% over the September quarter. Wage growth also moderated. The biggest surprise of the quarter came with weaker than expected third quarter GDP growth which was accompanied by significant downward revisions to prior data. This seems to put the nail in the coffin of the one further hike included in the RBNZ's November interest rate projections. However, it does not necessarily bring forward rate cuts. That will depend on whether the weaker growth data will be followed by soft inflation readings, particularly non-tradeable inflation. The next CPI data is due for release on January 24th.

Portfolio Review

- In December month, the Portfolio returned +1.38% (NZD/Gross), behind the MSCI World Net Index which returned +2.34%. The Portfolio delivered strong absolute performance for the full year 2023, returning +22.39%, but did not quite keep up with the index's +23.64% full year performance.

- Given the Portfolio is designed for long-term capital appreciation through compounding and reduced downside participation, lagging the index in such a sharp up year can occur, as it previously did during the second half of 2020.

- The slight Q4 2023 underperformance was due to stock selection, as weakness in Financials and Information Technology outweighed the strength in Industrials. Sector allocation was positive as the benefits from the zero weight in Energy and overweight in Information Technology counteracted the drag from the overweight in Health Care.

- The largest contributors to absolute performance during the quarter were Microsoft (+82 basis points [bps]), SAP (+66 bps), Accenture (+56 bps), Constellation Software (+48 bps) and Equifax (+47 bps).

- The largest absolute detractors were Aon (-39 bps), Becton Dickinson (-38 bps), Reckitt Benckiser (-26 bps) and ADP (-19 bps) and Veralto (-13 bps).

- For 2023 overall, underperformance was due to stock selection, largely driven by Information Technology's very healthy 46% return which nevertheless trailed the 58% offered by the index, whilst Financials also detracted.

- Sector allocation was positive, mainly due to the overweight in Information Technology, while the avoidance of lower quality, more cyclical sectors, notably Energy, also helped.

- This more than offset the negative from the overweight in Health Care which ended the year 20% behind the index. Another way of looking at impact of allocation is that the Portfolio only owned Microsoft and Alphabet out of the Magnificent Seven, leaving the Portfolio with less than 10% combined versus the 17% weight the Seven had in the index, negatively impacting relative performance by -400 basis points.

- The largest contributors to absolute performance in 2023 as a whole were Microsoft (+366 basis points [bps]), SAP (+265 bps), Accenture (+188 bps), Constellation Software (+183 bps) and Alphabet (+156 bps). The largest absolute detractors were Baxter Int'l (-53 bps), AIA (-25 bps), PayPal (-23 bps), Thermo Fisher (-21 bps) and Aon (-16 bps).

Commentary & Outlook (Morgan Stanley Investment Management)

Global equity markets finished the year with another strong quarter, with the MSCI World Index returning +11.4% (USD), and an impressive +23.8% for the year.

2023 started with fears of a recession, followed by the expectation of extended high interest rates, with the anticipated year-end U.S Federal Funds (fed funds) rate rising from 4.5% to 5.5% by March. Silicon Valley Bank blew up in the spring triggering fears of a credit crunch, but as these fears eased, the markets rejoiced in ideas of an AI-driven productivity boom. By the autumn, "higher for longer" was back even stronger, with the expected end 2024 fed funds rate approaching 5% and stocks suffering. Then the year finished with the U.S Federal Reserve's "Fed Pivot", the market penciling in six to seven rate cuts for 2024 and the markets stringing together nine positive weeks in a row.

Those of a sunny disposition can point to many positives going into 2024. Inflation now seems to be falling fast without a significant rise in unemployment, which remains below 4% in the U.S. The U.S. real gross domestic product (GDP) is now estimated to have grown 2.3% in 2023, versus the near-zero forecasts in late 2022. The 2024 estimate has risen to 1.3%, twice the growth rate expected back in the summer, while consumer confidence is finally improving, perhaps helped by rising real wages. "Team transitory" seems to be winning the inflation argument, perhaps explaining the Federal Reserve's (Fed's) recent dovish tone.

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Generative AI seems to be offering the prospect of a productivity boom (which could help reduce inflation) and in the shorter term a capex boom, as the hyperscalers frantically roll-out data centers to deal with demand and the U.S. CHIPS Act and foreign equivalents incentivise the building of semiconductor fabrication plants. The Magnificent Seven, or at least the five of them that grew earnings in 2023, should continue to be a driver of earnings growth.

A more cloudy view would suggest that the U.S. has yet to complete the soft landing. Soft landings are minority events, with three quarters of U.S. monetary tightening periods since the Second World War ending in recession. The labour market is still tight, with unemployment below 4% and the Federal Reserve Bank of Atlanta's wage growth tracker still above 5%, which may make service inflation tough to conquer, compared with the goods part of the economy which is already at zero inflation. On the other side of the ledger, the full negative effects of the recent 525 bps interest rate rise may still eventuate, given they have historically had a one-to-two-year lag, and something may still break in the financial system as we adjust away from the "free money" world.

Things are also less rosy outside of the U.S.; European economies are close to stall speed, with sub-1% growth penciled in for 2024 and purchasing manager indices in negative territory. China continues to wrestle with the massive hangover from its decades-long real estate boom, and potentially long-lasting impaired consumer sentiment as the combination of falling house prices and stock prices further impact household wealth after the recent COVID hit.

In addition, continued falls in inflation may pressure corporate margins if companies now struggle to raise prices even if a recession is avoided, particularly if wage rises prove sticky. This is all before considering the volatile geopolitical environment, not least with two billion people voting this year in elections across 64 countries.

We have no clear view as to where on the sunny/cloudy spectrum the world economy will fetch up. However, we would argue that the market is clearly basking on the sunny side of the street. MSCI World Index earnings are expected to rise close to 10% in 2024 and then by 11%+ in 2025.[2] This looks demanding given expected 2024 nominal GDP growth in developed markets of 3-4% and seems to imply that margins will have to rise further from already close to peak levels.

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