Salt Sustainable Growth Fund Fact Sheet – June 2022

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 total return (after fees and expenses but before tax) above the Reserve Bank of New Zealand's Consumer Price Index + 5% benchmark on a rolling five-year basis. To achieve this, the Fund targets a diversified mix of growth and defensive assets, with a focus on securities with strong Environmental, Social and Governance credentials.

The Fund also aims to maximise its total return by outperforming, over the long term, the weighted average return of the market indices used to measure performance of the underlying funds/assets in which the Fund invests: the Reference Portfolio.

Medium-term capital growth is prioritized above income 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 June 2022

Benchmark	NZ CPI +5% over 5 years
Reference Portfolio	SAA-weighted component benchmark indices' performance
Fund Assets	$50.28 million
Inception Date	15 September 2021
Portfolio Manager	Greg Fleming

Unit Price at 30 June 2022

Application	0.9120
Redemption	0.9083

Investment Guidelines

Sector	Target	Range
New Zealand Fixed Interest	10%	0% – 25%
International Fixed Interest	5%	0% – 30%
Australasian Shares	24%	10% – 40%
International Shares	35%	20% - 50%
Global Listed Property	10%	0% – 25%
Global Listed Infrastructure	10%	0% – 25%
Alternative Diversifiers	0%	0% - 15%
Cash or cash equivalents	5%	0% – 10%

Fund Allocation at 30 June 2022

New Zealand Fixed Interest	0%
International Fixed Interest	9%
Australasian Shares	25%
International Shares	35%
Global Listed Property	16%
Global Listed Infrastructure	12%
Alternative Diversifiers	2%
Cash or cash equivalents	1%

Fund Performance to 30 June 2022

Period	Fund Return	Reference Portfolio Return
1 month	-3.77%	-4.13%
3 month	-7.32%	-7.71%
9 month	-8.27%	-8.28%
Since inception	-8.99%	-9.50%

Performance is after all fees and does not include imputation credits or PIE tax.
Past performance is not a reliable indicator of future performance and no representation or warranty, express or implied, is made regarding future performance.

Top Individual Holdings at 30 June 2022

Fisher & Paykel Healthcare	Mainfreight
Microsoft	Accenture
Spark New Zealand	Danaher Corp
VISA	SAP
Reckitt Benckiser Group	Infratil

Holdings stated as at 30.06.22, excludes consolidated International Fixed Interest component of the Sustainable Growth Fund.

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Market Commentary

It has been a tough June quarter for markets following what was already a difficult March quarter. This marks the worst first half of the year for developed market equities in 50 years. To make matters worse, bond prices have also fallen significantly, failing to give investors the protection they usually seek from this asset class.

- Central banks continue to play catch-up with inflation, which is contributing to growing risks to growth, though those risks remain greater in Europe than the United States. Labour markets remain tight but negative real wage growth continues to squeeze household incomes. Margins are coming under pressure, especially for consumer-facing companies, with pricing power an increasingly important factor in relative equity performance.
- In the U.S. the Federal Reserve has signalled its clear intention to tame inflation by signalling interest rates will need to rise to 3.8%. Despite unemployment being low and wages increasing, consumer confidence has slumped, contributing to recession concerns. The Fed believes the unemployment rate will need to rise to just above 4% (currently 3.6%) to meet its inflation mandate. U.S. headline inflation came in higher than expected at 9.1% y/y in June.
- Consumer confidence has also slumped in Europe, though the biggest recession risk is the reduction in gas supplies from Russia. Prices have risen sharply, and some form of rationing may have to be implemented. This prospect is already having a negative impact on business confidence.
- The Chinese authorities continue to adopt a Covid-zero strategy, though there has been some easing in quarantine restrictions. With lockdown restrictions easing in some regions, recent economic data has improved. We expect the authorities will continue to back away from Covid-zero, most likely following the Communist Party National Congress later in the year. The Reserve Bank of Australia raised interest rates for the first time this cycle at the May meeting, raising the cash rate 25bps. Labour market and activity trends during 2022 thus far suggest solid economic fundamentals amid building inflationary pressures. We expect ongoing interest rate increases and a step up to 50bp hikes was seen in the first meeting in June, to 0.85%.
- After some short-term softness in economic data and pullback in activity due to the Omicron variant, recent consumer and labour data indicate that the outlook for the New Zealand economy remains solid. The inflation outlook has heated up as well, which will keep the RBNZ on track for further rate hikes this year. We expect a 50bp hike in July, after which the RBNZ will likely slow the pace of rate hikes to 25bps for a terminal rate of 3.0-3.5%.

Central Banks' shift in tone to a more inflation-adverse stance, combined with the Ukraine crisis, and energy / food cost spikes, has challenged investor sentiment throughout much of 2022 so far. It appears unlikely that such factors darkening the global growth outlook for the present will clear quickly, and sentiment depends on robustness of corporate earnings and a moderation in cost pressures.

June Quarter compounded market weakness from March

After a mediocre rally in May, global equity markets continued to plummet in June, with the MSCI World Index finishing down 8.7% in U.S. dollars (USD) for the month (-7.8% in local currency and - 4.4% in NZD), with every sector in the red – and five of the 11 sectors with double digit drawdowns. Perhaps unsurprisingly, the fall saw defensive plays hold up better, with Health Care (-3%) and Consumer Staples (-3%) leading in the month. At the other end of the spectrum, recessionary fears took their largest toll on the more cyclical Materials (-16%) and Energy (-15%) sectors. The other sectors were more tightly bunched, all closing within 2% of the index. Turning to geographies, the U.S. was just ahead of the overall World index (-8%) in the month, meaning other major markets tended to be behind.

Q2 overall was another difficult quarter for markets, with the MSCI World Index finishing down 16.2% in USD (-14.3% in local currency and -6.24% in NZD). The index is now down more than 20% YTD in USD, and down 18% in local currency. As in the month, defensive areas held up better: the International Shares Portfolio's key defensive positions in **Consumer Staples** (-6%) and **Health Care** (-7%), while down on the quarter, were ahead of the overall index, as was Utilities (-7%). Weakness in the month left **Energy** (-5%) down for the quarter, though the sector is still up 24% for the year – the only sector with positive YTD performance. Meanwhile, the growth-tilted and high multiple Consumer Discretionary (-24%) and Information Technology (-22%) sectors were, as in previous months, among the worst performers, both now down 30% for the year.

The regional performance pattern was more mixed. As in the month, Hong Kong (-1% local currency) was the standout performer, while the UK -3%) and Switzerland (-11%) also finished ahead. Japan's loose monetary policy continued to put downward pressure on the yen, leaving the market down 15% in USD, but only -4% in local currency, while the U.S. (-17%) was just behind MSCI World Index.

Salt Sustainable Growth Fund Commentary

The Sustainable Growth Fund was negatively affected by weak global investor sentiment in June month, declining -3.77% (after fees.) The fund remains in negative returns territory over a three-month period, at -7.32%. This has brought the since-inception fund return to -8.99%, as strong Q4 2021 returns reversed in the course of H1 2022.

Internationally, major central banks are now communicating the desirable course of carrying through several meaningful interest rate increases, sufficient to anchor inflation expectations, and this will unnerve markets at times. This is partly because bond yields moved sharply upward, impacting valuations which had been elevated, and slowing demand worldwide. Investors fear profit slippage as economies slow, although internationally profit growth forecasts, while lowered, remain positive.

In June month, the monthly return was lowered most by the performance of the Salt Sustainable Global Property Fund (which made a negative impact of -1.21% on the Growth Fund.) The Salt Sustainable Global Shares Fund contributed -0.74% to the Growth Fund, while the Global Infrastructure Fund was relatively modest at -0.60%) The NZD fell by 4.1% versus USD, buffering the unhedged fund return from Global Shares over the month. Weakness in NZD/USD assists returns and YTD the decline in NZD is -8.5%.

Near-term declines in the Global Equities component are indicative of the portfolio structure of the Morgan Stanley Investment Management strategy within this asset class. Due to the prioritisation of low carbon-footprint investments within that fund, the strategy has above-benchmark holdings in Info Tech, Health Care and Consumer Staples sectors. IT has repriced negatively across the board. The full benefit of the defensiveness in Staples and Health Care is beginning to positively impact, though this has taken time to emerge, as the evidence on US recession risk is not definitive.

We believe that the specific companies favoured in the Sustainable Global Shares Fund will be able to protect their pricing power in an inflationary environment and will give them comparative resilience to changes in the global economic cycle, including higher inflation and interest rate. That is more the focus of this portfolio strategy, rather than directly hedging against shocks to global bond yields.

The Sustainable Global Infrastructure Fund, by contrast, benefits from safe-haven appeal and should continue to diversify Growth Fund risks. The other exposure within the Sustainable Growth Fund with a flat June month and June Quarter performances (albeit small) was the Salt Carbon Fund, which made a -0.05% for the month while being flat over the second quarter.

Weaker recent returns from Property partially reflect the surge in global long-bond interest rates, as yield competitors for Real Assets. We expect a phase of listed real estate weakness which is characteristic of the early stages of a monetary policy tightening cycle such as we are presently seeing develop across the world. Nevertheless, Property's scope for inflation-hedging and other longer-term advantages of the asset class outweighs the near-term impact of higher bond yields on prices, in our view.

Greg Fleming, MA