SALT

Salt Sustainable Global Shares Fund Fact Sheet – May 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'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 May 2024

Fund Assets	$65.07 million
Inception Date	12 July 2021
Underlying Manager	Morgan Stanley Investment Management

Unit Price at 31 May 2024

Application	1.2202
Redemption	1.2152

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 May 2024

Global equities	98.2%
Cash & sundry items	1.8%

Fund Performance to 31 May 2024

Period	Fund Return*	Benchmark Return
1 month	-0.98%	0.61%
3 months	-2.38%	2.95%
6 months	9.21%	15.50%
1 year	14.91%	21.86%
2 year p.a.	13.03%	16.22%
Since inception p.a.	8.43%	10.71%
5 year p.a.*	12.22%	14.10%

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 May 2024. *5 year strategy performance is also gross of fees.

Fund ESG Scores	Portfolio	Index
Sustainable Global Shares	26T CO2 /$m	162T CO2 /$m
Portfolio Carbon Footprint:	16% of 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 31 May 2024, the Portfolio's carbon footprint was 84% lower than that of the Index.

Top 10 holdings	
Microsoft (US)	Alphabet (US)
VISA (US)	Thermo Fisher Scientific (US)
SAP (DE)	RELX (UK)
Accenture (US)	UnitedHealth Group (US)
Intercontinental Exchange (US)	Constellation Software (CA)

Source: MSIM, data as at 31 May 2024.
The Top 10 Holdings represented 40.55% of the total portfolio.

Market Review

- The month of May saw positive returns for both developed market equities and fixed income. Ongoing optimism about a global soft landing supported risk assets while anticipated rate cuts spurred bond markets to a positive return. Developed market equities rose +4.5% (in USD) over the month while the global aggregate bond index was up +1.3% (in USD) over the same period.
- In the US activity data surprised mostly to the downside. Most importantly, April payrolls came in below expectations and the unemployment rate rose. April CPI data was in line with expectations following three months of higher-than-expected numbers. Earlier in the month the Fed kept policy unchanged but highlighted the lack of progress towards the 2% inflation. This was interpreted by markets as a delay in rate cuts, rather than a return to rate hikes.
- Economic activity continues to improve in Europe. PMI data released during the month shows the recovery is being driven by the services sector, but there are also signs of improvement in manufacturing. Despite the annual rates of headline and core inflation accelerating

in May, progress over the last few months is expected to still give the ECB sufficient confidence to start cutting interest rates at their June meeting.

- The weakness in the Yen continues to be a key focus in Japan. While this is usually positive for Japan exports and the export heavy Topix, the very low level of the Yen is starting to impact negatively on consumer confidence. Japanese stocks were one of the regions weakest performers in May.
- Activity data in China is generally surprising to the upside, though a look under the hood reveals a strong performance from exports alongside ongoing weakness in domestic demand. Problems in the real estate sector remain unresolved and pose a key risk to the outlook.
- The Reserve Bank of Australia kept monetary policy unchanged at its May meeting and was less hawkish than expected, despite higher-than-expected March quarter inflation. Policy guidance remained unchanged in “not ruling anything in or out”.
- Labour market conditions continue to deteriorate in New Zealand. The unemployment rate rose from 4% to 4.3% in March while the annual rate of increase in the Labour Cost Index slowed to 3.8%, its lowest level in 18 months. Despite this, the RBNZ remains concerned about sticky domestic inflation pressures, delivering a hawkish statement during the month. This saw market pricing push the first full rate cut out to February 2025.

Portfolio Review

- In May, the Portfolio returned -1.01%, while the MSCI World Net Index returned +0.61%. For the year to date (YTD), the portfolio has returned +7.58% versus +12.86%. Our focus is on absolute compounding over the long term.
- Sector allocation was mildly positive in May as the benefit from the underweight in Consumer Discretionary and zero weight in Energy offset the drag from the overweight in Health Care. Stock selection in Information Technology was the largest detractor, given the Portfolio’s tilt toward Software (up only 3% and down excluding Microsoft) and IT Services (down 6%), which combined make up over 75% of the Portfolio’s IT exposure; both were over 10 points behind Hardware (up 13%) and Semis (up 16%), which were boosted by Apple and Nvidia, respectively.
- Health Care, Consumer Staples and Financials detracted to a lesser extent, while Industrials was stronger.
- At a strategy level, four of the largest contributors to absolute performance during the month came from IT. Texas Instruments and TSMC participated in the strong Semis performance, while Microsoft and Constellation Software defied the relative weakness of Software. The fifth was RELX which has been helped by the ongoing shift in business mix towards higher growth analytics and decision tools. IT also provided two of the largest absolute detractors.
- Accenture continued to derate alongside the IT Services subsector due to the continued soft demand for discretionary projects and fears about the lack of significant GenAI revenues, while CDW also derated as it was hit by the 3% downgrade to 2024 earnings. Forward EPS is actually marginally higher than it was at the start of 2024 for the two companies.
- The other leading detractors were IQVIA due to an unhelpful headwind to the otherwise healthy order book from a last-minute trial cancellation,
- Abbott hit by the product recall of HeartMate and Haleon as the market absorbed the GSK sale of 4% of the company.
- The largest contributors to absolute performance during the month were Texas Instruments (+17 basis points [bps]), Microsoft (+16 bps), TSMC (+12 bps), Constellation Software (+11bps) and Experian (+9 bps).
- Three of the largest absolute detractors were the companies mentioned above: Accenture (-40 bps), IQVIA (-28 bps), and SAP (-19 bps). The other two were Abbott Laboratories (-19 bps) and CDW (-18 bps.)

Commentary & Outlook for May 2024 (Morgan Stanley Investment Management)

Global equity markets regained strength in May, with the MSCI World Index returning a healthy +4.47% in U.S. dollars (USD) and +4.07% in local currency (+0.61% in NZD). Information Technology (+9%) and Communication Services (+6%) were both strong, continuing their impressive year to date (YTD) performance, with both now up 35% so far this year. As mentioned, Semis – boosted by NVIDIA, up a mighty +27% in the month – and Hardware were far stronger than Software and Services within IT. Utilities (+8%) also outperformed in the month. At the other end of the spectrum were Energy and Consumer Discretionary (both +0%), which finished as this month’s laggards. All other sectors were within 200 bps of the index.

Turning to geography, the performance pattern was mixed; Switzerland (+8% USD, +6% local currency) and Spain (+6%, +4%) outperformed the index, whilst Italy (+5%, +3%), Germany (+4%, +3%) and the UK (+4%, +2%), although broadly in line in USD, were a touch behind in local currency. France (+3%, +1%) was weaker in both. In Asia, Hong Kong (+3%, +3%) and Japan (+1%, +1%) were relatively weak, while Singapore (+4%, +3%) held up slightly better. The U.S. finished in line with the index (+5%) in the month.

Independent Thinking

The timing of when to be invested in an index is important. Markets are back to high expectations, with high multiples and double-digit earnings growth forecasts for MSCI World for the next two years, on top of peak margins. This brings risk for passive investors, in our view. Three consensus trades dominate today’s markets: being invested in the American economy, owning obvious artificial intelligence plays and that there will be a soft or no landing in the U.S. If anything other than this consensus view prevails, index investors may find themselves in relative difficulty.

For many investors, opting to invest in an index has been an easy decision these last years. An era of historically low interest rates and loose monetary policy meant that as U.S. 10-year treasuries declined from 4% in 2010 to just 0.5% in 2020, the S&P 500 Index’s Price to Earnings (PE) forward multiple rose from 14x to 18x.

Disclaimer: The information in this publication has been prepared from sources believed to be reliable and accurate at the time of preparation but Salt Funds Management Limited, its officers, directors, agents, and employees make no representation or warranty as to the accuracy, completeness, or currency of any of the information contained within, and disclaim any liability for loss which may be incurred by any person relying on this publication. All analysis, opinions and views reflect a judgment at the date of publication and are subject to change without notice. This publication is provided for general information purposes only. The information in this publication should not be regarded as personalised advice and does not take into account an individual investor’s financial situation or goals. An individual investor should, before making any investment decisions, seek professional advice. Past performance is not a reliable indicator of future performance and no representation or warranty, express or implied, is made regarding future performance.

Since 2022's market sell-off, the S&P 500 PE has continued its upward climb and is back at 21x – almost 40% above its 2022 low.1 As a rising tide has helped lift all boats, index investing has reaped substantial rewards; S&P Global's SPIVA research shows that in the U.S., over one, three-, five-, 10- and 15-year periods, passive has beaten most large-cap actively managed funds.2 For the average investor, the transparency and liquidity offered by index investing, as well as its lower cost, have also added to the appeal.

While active versus passive is a well-worn debate, it needn't be an either/or decision. In fact, we would argue that there's a strong case for both index investing and active management to co-exist in portfolios. How they are balanced can be determined by an investor's investment objective, preferred time horizon, and appetite for risk – whether the definition is tracking error or losing money.

The active/passive conundrum

The decision to opt for passive is still an active decision. According to the Index Industry Association3, there are over three million stock indices in the world – over 50 times more indices than stocks4! Choosing to track an index, or combination of indices, still requires an investor to make an active decision.

Then there's risk. By owning more, an investor may hope to benefit from the positive effects of diversification. But is owning everything regardless of quality or valuation really the best way for investors to diversify a portfolio? Equally, with the focus of so many managers and investors on relative risk, the market has provided a comfortable place to take shelter. But is weighting a bet based on size sensible, given that most widely recognised and invested indices are typically market-cap weighted? An investor may hope for the wisdom of the crowd but instead get a crowded trade.

In bull markets, market-cap weighted indices in particular can become increasingly biased and lopsided as valuations for those stocks perceived as "winners" are stretched beyond fundamental rationality, and the "winners'" weights mechanically increase in the passive indices. Recent research from Morgan Stanley observed that S&P 500 concentration is at an historical extreme, increasing its vulnerability to a steep correction as the cycle or "theme du jour" turns.

This risk is further compounded by the connected aspects of the largest stocks that dominate several equity indices. In the S&P 500, the recent fortunes of some of the largest market constituents have been driven by euphoric earnings expectations around the promise of generative artificial intelligence. Of course, an investor may attempt to diversify some of this thematic risk by tracking a global index, but with the U.S. weighting in global indices at an all-time high6, they may not achieve the diversification expected. Attempting to work around this by using an equal-weighted alternative may come at the expense of missing the opportunity that recent distortions have presented.

The benefit of being selective

While passive funds provide broad-based exposure and nimble, cheap access to tactical themes, there is still an opportunity to be selective – particularly given indices' biases. When stock prices become disconnected from fundamentals, skilled stock pickers can take advantage… that is, of course, provided they have the luxury of a longer time horizon if a lopsided multiples-powered bull run still has momentum.

As with passive options, investors face a plethora of choice when it comes to picking an active equity manager, not least because the tracking error constraints some active managers have in place can reduce the active/passive "balance" an investor may be seeking to achieve. We believe that our team's concentrated, benchmark agnostic strategies offer a useful counterbalance to index investing. Why?

- We seek to own what we believe to be the highest quality companies in the world. Our focus is on high quality companies at reasonable prices, those that have the ability, in our view, to sustain their already high returns on operating capital, compound their earnings and cashflows steadily over time, and exhibit resilience in tough times.
- Selecting a long-term, high conviction, high active share portfolio offers a commitment device to remain invested and resist behavioural biases to buy high and sell low. We seek to act as owners for the long term, not tactical renters for the short term.
- We pay attention to the fundamentals of what we own more than the current price or performance of what we don't. Our focus is, and always has been, on the absolute: absolute price, absolute performance, and absolute quality.
- Our focus on company fundamentals has seen us take advantage of the market's recent bias towards the more 'tech-y' stocks. The lagging of defensive sectors, notably Consumer Staples and Health Care, and the accompanying dispersion in valuations provided us with an attractive entry point for four buys in our global portfolios in Q1: two in Health Care, and one in Consumer Staples.
- Investors who seek minimal tracking error participate fully in the market's ups, but just as crucially, fully in the market's downs. Investing in an active portfolio of high-quality companies whose earnings can compound steadily over time offers reduced risk of permanent loss of capital.
- Managing concentrated portfolios with a long investment horizon enables us to represent our clients effectively as shareholders, seeking to engage with companies on financially material matters ranging from capital allocation to compensation and incentives, strategy, risk and opportunity, and to check that the company's ability to compound remains intact.

Disclaimer: The information in this publication has been prepared from sources believed to be reliable and accurate at the time of preparation but Salt Funds Management Limited, its officers, directors, agents, and employees make no representation or warranty as to the accuracy, completeness, or currency of any of the information contained within, and disclaim any liability for loss which may be incurred by any person relying on this publication. All analysis, opinions and views reflect a judgment at the date of publication and are subject to change without notice. This publication is provided for general information purposes only. The information in this publication should not be regarded as personalised advice and does not take into account an individual investor's financial situation or goals. An individual investor should, before making any investment decisions, seek professional advice. Past performance is not a reliable indicator of future performance and no representation or warranty, express or implied, is made regarding future performance.