Salt Sustainable Growth Fund Fact Sheet – October 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 31 October 2022

Benchmark	NZ CPI +5% over 5 years
Reference Portfolio	SAA-weighted component benchmark indices' performance
Fund Assets	$50.17 million
Inception Date	15 September 2021
Portfolio Manager	Greg Fleming

Unit Price at 31 October 2022

Application	0.9071
Redemption	0.9033

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 31 October 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 31 October 2022

Period	Fund Return	Reference Portfolio Return
1 month	2.06%	2.72%
3 months	-6.15%	-3.43%
6 months	-6.35%	-3.82%
1 year	-9.93%	-7.22%
Since inception	-9.49%	-7.74%

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 31 October 2022

Microsoft	Auckland International Airport
Fisher & Paykel Healthcare	Accenture
Spark New Zealand	Infratil
VISA	Mainfreight
Danaher Corp	SAP

Holdings stated as at 31.10.22, excludes consolidated International Fixed Interest component of the Sustainable Growth Fund, due to its large number of securities.

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Market Commentary

- October month saw a moderate rebound in many markets, following the sharp corrections of the third quarter. Fixed Interest assets stabilized while equities made gains on corporate earnings.
- Despite a rough start to the month, developed market equities ended October 7% higher (in USD terms). It was a tough month for emerging markets which ended 3% lower, dragged down primarily by weakness in China.
- Bond yields continued to push higher, making new cyclical peaks of 4.2% in the US, 2.4% in Germany and 4.7% in New Zealand. Yields rallied into the close of the month.
- Inflation, central banks, recession risk and geopolitical tensions were all key foci over the month. Good news came in the form of a further reduction in supply chain constraints.
- The combination of high inflation and tight labour markets saw further aggressive action from central banks over the month. The European Central Bank hiked by 75bp, with the US Federal Reserve and the Bank of England widely expected to hike by similar amounts in early November. The Reserve Bank of New Zealand delivered a hawkish 50bp hike in the sense that the bank actively considered a larger 75bp hike.
- The interest rate outlook and rising geopolitical tensions saw the US dollar continue its inexorable rise. USD strength was most notable against the Japanese Yen and the Chinese renminbi, the currencies of the two central banks that continue to maintain an accommodative stance.
- The US economy showed signs of softening over the month, particularly in the housing market as higher mortgage rates started to bite. Flash PMIs were soft, with all forward-looking components weak. However, inflation came in stronger than expected and the labour market remains tight, keeping pressure on the FOMC. The Committee is expected to signal a slower pace of tightening into the end of the year, though the peak terminal rate remains uncertain.
- Europe announced further plans to address the energy crisis, including a proposed price cap and a common purchases system. Both should support the recent downside in energy prices. PMI data moved into recessionary territory. The ECB is continuing to prioritise inflation over growth and is expected to continue tightening, though probably at a slower pace than recently.
- Growth in China rebounded in the third quarter, though continued Covid lockdowns has seen a softening in the higher frequency activity data. Inflation remains low which we expect will lead to further interest rate cuts by the PBoC. As expected, President Xi was reappointed at 20th Party Congress.
- In Australia, activity data continues to slow. However, a higher-than-expected inflation print for the September quarter has challenged the recent decision by the RBA to reduce the pace of interest rate increases. The RBA hiked by only 25bp at its October meeting. Maintaining this slower pace risks needing to become more aggressive further down the track and causing a sharper economic downturn.
- Activity data continues to slow in New Zealand, while September quarter inflation came in stronger than expected. The HLFS report for the same period showed the labour market remains tight with very strong wage growth. Market pricing expects the RBNZ to lift its forecast terminal OCR rate at its 23 November meeting and deliver a 75bp hike.

Salt Sustainable Growth Fund Commentary

The Sustainable Growth Fund benefited from the turnaround in investor sentiment in October, after a generally weak market environment in the September quarter. The fund rebounded 2.1% (after fees) for the month, although it remains in negative territory over other periods since inception last September. The rolling three-month return declined to -6.15% which was almost fully due to the -5.6% drop in September month.

The moderate October gain brought the one-year fund return to -9.93% (net) up to 31 October, and the since inception return to -9.49% (net.)

Internationally, major central banks are now communicating and swiftly enacting the desirable course of carrying through meaningful interest rate increases, sufficient to anchor inflation expectations, and this continues to unnerve markets. This is partly because notwithstanding a mid-year, short-lived dip, in 2022 bond yields moved sharply upward in the third quarter, strongly impacting valuations, and slowing demand worldwide. Investors fear profit slippage as economies slow, although internationally profit growth forecasts, whilst lowered, remain positive. We target investments with defensible profits in difficult periods and believe active management will be needed in years ahead. Fixed interest value is increasing, and the time to buy additional bond exposure within the fund is approaching.

As global growth showed more definitive signs of cooling, the price of oil has retreated somewhat from its June highs of above USD 110 per barrel, declining -20% to around USD 88/bbl in late October. US Natural Gas prices have retreated sharply, falling 17% in October (still, they remain up +115% YTD) but European gas prices remained elevated, being more influenced by the Russia-Ukraine situation than is the case for American supply. This is now having highly disruptive political and market consequences, and it remains too early to predict when the hostilities may diminish. Heating oil and gasoline prices are still very high as the Norther winter advances.

October's tentative positivity in markets which had become very volatile during the September quarter lifted most of the Sustainable Growth fund's component assts, with just the International bond holding registering a flat monthly return. The strongest individual contribution for the month came from the Sustainable Global Shares Fund, at +0.76%. The returns in the Sustainable Growth Fund's Global Equities component are indicative of the portfolio structure of the Morgan Stanley Investment Management strategy. 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. The full benefit of the defensiveness is beginning to positively impact, though this has taken time to emerge, as the evidence on US recession risk is not yet 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 rates for an extended period.

That is more the focus of this portfolio strategy, rather than directly hedging against shocks to global bond yields. Quality companies are more resilient over the full economic cycle, and compounders reward the patient holders.

For October, other Sustainable Growth fund components making a positive contribution were the Core NZ Shares Fund (+0.54%) and the Real Asset class funds of Sustainable Global Property (+0.38%) and Global Infrastructure (+0.42%.)

The Global Fixed Interest fund component detracted -0.03% in October, which was offset by a small positive return provided to the Sustainable Growth fund by our own Salt Carbon Fund, +0.03%. Recent strength in the Carbon Fund reflects the better monthly performance in that alternative / diversifier asset as investors continue to seek holdings with low correlation to the main global investment types, and the climate change mitigation agenda continues to gather international adherence.

Greg Fleming, MA