Salt Sustainable Income Fund Fact Sheet – June 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 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 June 2023

Benchmark	Bank deposit rates (BNZBIL Index)
Reference portfolio	SAA-weighted component benchmark indices' performance
Fund Assets	$44.48 million
Inception Date	19 June 2021
Portfolio Manager	Greg Fleming
Prospective distribution yield (cents per unit) / based on Unit Price of 1.6.23	1.125 cents per unit per Quarter / 5.19% per annum

Unit Price at 30 June 2023

Application	0.8782
Redemption	0.8746

Sustainability Metrics

Fund ESG Scores	Portfolio	Category avge
Morningstar ESG score	20.56	21.00

Scores indicate risk level – a lower score reflects a lower ESG multi-factor risk level. ESG score as at 30.06.23. Sustainalytics 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 June 2023

Global Fixed Interest	27%
Australasian Shares	30%
Global Listed Property	23%
Global Listed Infrastructure	18%
Cash or cash equivalents	2%
Asset allocation to Fixed Interest + Cash	**29%**

Fund Performance to 30 June 2023

Period	Fund Return (after fees)	Gross Reference Portfolio Return
1 month	1.45%	1.03%
3 months	0.73%	0.18%
6 months	2.86%	2.47%
1 year	2.74%	2.10%
Since inception p.a.	-3.21%	-2.02%

Performance is after all fees and does not include imputation credits or PIE tax. Reference Portfolio return is gross.

Top Individual Holdings at 30 June 2023

Goodman Property Trust	Argosy Property Trust
Fisher & Paykel Healthcare	Infratil
Kiwi Property Group	US 5Yr Note (CBT) Sep 23
Precinct Properties NZ	Auckland International Airport
Spark NZ	Property for Industry

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Market Commentary

June saw global equities strengthen sharply, though they rose by less in NZD terms. The mood was buoyed by better growth and inflation signals and by expectations for reduced monetary tightening.

- June month saw global stocks rebounding 6.1% and by 7.0% for the June quarter, in USD terms. Global markets overcame uncertainty over economic slowing, still-elevated inflation and central bank policy and focused on now-lower recession probabilities.
- The first half of 2023 has been much better for balanced portfolios than the challenging 2022 year. A 9.1% (in NZD) gain for developed market equities over the quarter leaves them 18.8% higher year to date. Global sovereign bonds have lagged but are still doing better than last year rising 1% (in USD) YTD.
- The positive tone in markets this year has been driven by a generally improving outlook for global growth as economies have proven to be more resilient than expected to the recent aggressive tightening in monetary conditions. However, underlying inflation has also proven to be more persistent, so we are not out of the woods yet.
- US inflation has fallen sharply from a peak of 9% to 4%, but mostly due to lower oil prices. Core inflation has remained stickier as the labour market has remained tight and wage growth in excess of the level consistent with target inflation.
- The US consumer has continued to spend, reflecting still high excess cash, lower savings and continued employment gains that have averaged 314,000 per month since the start of the year. Weaker business investment intentions and weak corporate loan demand pose risks for growth going forward.
- Economic activity in Europe has proven stronger than expected as the lower energy prices has delivered real income gains back to consumers. However, in order to contain still problematic underlying inflation pressures, what lower oil prices have delivered to consumers, the European Central Bank has had to take away. With core inflation still in excess of 5% the ECB has raised interest rates to 3.5%, with more hikes still to come.
- After the end of the zero-Covid bounce in activity in China, macro data over the June quarter has pointed to a renewed slowdown. We think that the slowing reflects the payback of front-loaded production and policy easing, which are one-off factors, but the recovery is far from over, given that the job market recovery is incomplete. Given that the recovery has remained fragile, we believe the authorities would stand ready to support growth as needed.
- In Australia there are increasing signs that the activity is slowing after a very strong period of growth in 2022. The labour market has remained resilient though it typically lags growth. The RBA is taking a stop-start approach to raising interest rates. We think they have more work to do; we see the cash rate rising to 4.6% in the next few months.

Salt Sustainable Income Fund Commentary

The Sustainable Income Fund experienced a positive return of 1.45% (after fees) in June month and a 0.73% net return over the rolling 3-month period, reflecting stronger returns in both the equity and fixed interest components of the portfolio. For the year, the fund gained 2.74% (after fees) which was 0.64% ahead of its gross reference portfolio return.

Despite a range of headwinds for markets, 2023 has so far proved a much better investing environment than 2022. As inflation progressively shows signs of a definitive peak, we expect component asset classes to improve, as has occurred in the first half of 2023, with periodic interruptions. Volatility across markets is ever-present and sentiment remains fragile.

June month saw better returns from listed real assets. The Global Listed Infrastructure fund made a positive individual contribution of +0.42% while the top contributor for the month was the Salt Enhanced Property Fund with +0.65%. The third-strongest contributor in June was the Salt NZ Dividend Appreciation fund, which added +0.23%. The Sustainable Global Property fund added 0.10%, reversing the negative May impact. On the bond side, the Sustainable Global Fixed Income Opportunities fund contributed 0.03%.

Salt Sustainable Income Fund outlook

We believe bond yields have now adjusted upwards enough, to have lowered our previous underweight bond positions within the Sustainable Income Fund. The allocation to bonds is now 28% 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 paused in lifting the Official Cash Rate though core inflation is persisting, so domestic yields and discount rates are likely to stay quite elevated. This is supressing returns from NZ equities this year, and the relative weakness of NZ shares compared to global equities is now notable.

Nevertheless, the Fund's income level has been enhanced. We anticipate the longer-term capital growth strategies within the Sustainable Income Fund to resume performance, as inflation conditions stabilize. However, there could well be a mild recessionary period to traverse en route to that outcome. The phase of actual interest rate reductions from central banks is still some time into the future and we expect a major beneficial capital growth impact of such will only become apparent only from the last part of 2023 or even early in 2024.

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 increased to 1.125 cents per unit / quarter

Higher component asset yields have enabled us to again lift the quarterly cents-per-unit distribution from the fund, to 1.125 cpu from the next quarterly distribution date (paid in August) onwards. This will be updated again in November, dependent on the outlook for fund income at that time.

As noted earlier, the silver lining in the bond repricing is that the yield received from bond investments is also now higher and 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 last phase of interest rate increases, sufficient to anchor inflation expectations, and this does unnerve markets at times. While the resultant volatility requires fortitude from investors, the objective of securing an inflation-resilient income level now 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 indeed been commensurately rising through the recent periods of market turbulence. This trend exemplifies the incremental return of some “risk premia” into asset classes, though this has further to go. The fund’s income is still modestly above its prospective distribution yield.

The equity capital value components of the Income Fund have adjusted to weaker economies in the year ahead, yet the Real Asset components of Infrastructure and Property are better-suited to an economically uncertain and inflation-affected period, once central bank policy rates begin to fall or there is a downward shift at the short end of the yield curve. If, as expected, global central banks increasingly pause their interest rate tightening cycles, defensive merit should be re-asserted in coming months through continuing positive demand for these specific “Real Asset” equity types, along with the sustainable dividend-payers in the broader Australasian market.

Greg Fleming, MA