

SALT

Salt Sustainable Income Fund Fact Sheet – August 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 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 31 August 2024

Benchmark	Bank deposit rates (BNZBIL Index)
Reference portfolio	SAA-weighted component benchmark indices' performance
Fund Assets	\$47.51 million
Inception Date	19 June 2021
Portfolio Manager	Greg Fleming
Prospective distribution yield (cents per unit) / based on Unit Price of 1.09.24	1.125 cents per unit per Quarter / 5.02% per annum

Unit Price at 31 August 2024

Application	0.8977
Redemption	0.8940

Sustainability Metrics

Fund ESG Scores	Portfolio	Category ave
Morningstar ESG score	18.84	21.00

Scores indicate risk level – a lower score reflects a lower ESG multi-factor risk level. ESG score as at 31.08.24. 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 31 August 2024

Global Fixed Interest	34.5%
Australasian Shares	27.5%
Global Listed Property	20.0%
Global Listed Infrastructure	17.0%
Cash or cash equivalents	1.0%

Asset allocation to Fixed Interest + Cash 35.5%

Fund Performance to 31 August 2024

Period	Fund Return (before fees and tax)	Gross Reference Portfolio Return*
1 month	2.40%	1.70%
3 months	6.34%	5.82%
6 months	8.36%	7.71%
1 year	12.27%	10.86%
2 years p.a.	5.23%	4.21%
3 years p.a.	1.11%	0.01%
Since inception p.a.	2.55%	1.42%

Performance is before fees and tax, adjusted for imputation credits. * at 31 Aug.

Top Individual Holdings as at 31 August 2024

US 5Yr Note (CBT) Sep24	Infratil
Goodman Property Trust	Auckland International Airport
US T Note Sep 25	Tower
Fisher & Paykel Healthcare	Kiwi Property Group
Precinct Properties NZ	Argosy Property Trust

SALT FUNDS MANAGEMENT

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Market Commentary

- The volatility that prevailed in markets over July continued into the early part of August. Disappointing US labour market, combined with an interest rate hike from the Bank of Japan saw a sharp sell-off in global equity markets. A degree of order was restored later in the month as markets began to price in more aggressive policy easing from the US Federal Reserve and solid earnings results suggested little chance of imminent US recession.
- Developed market equities ended 2.7% higher over the month while the global aggregate bond index rose 2.8%. Interest rate sensitive asset classes also performed well with the global REITs index up 6.2%. All percentage changes are in USD terms. In NZD terms, however, the 5% gain in NZD/USD led to unhedged global shares declining -2.6% in August month.
- In the US the July jobs report showed the smallest payrolls gain (+144k) in over three years, while a stronger participation rate saw the unemployment rate rise to 4.3%. Recession fears were further fuelled by a weak ISM manufacturing index. This led to market pricing in over 100bp of policy easing by the Federal Reserve at points during the month.
- The Bank of Japan's decision to increase its policy rate by 25bp combined with the hawkish tone set of Governor Ueda led to an abrupt unwinding of carry trade positions, whereby investors relied on cheap borrowing costs in Japan to invest in other higher yielding assets.
- Despite a bounce in the Euro zone composite Purchasing Managers Index because of the Olympics in France, underlying data remained weak across the currency bloc. Earnings from cyclical companies disappointed, adding to the weak tone.
- Property market problems in China continue to weigh on the broader economy. Growth in retail sales increased 2.7% y-o-y in July, up from 2.0% in June. This improvement is largely driven by the low comparison base last year. Despite the improvement, retail sales growth remains weak compared to pre-COVID levels. Policy support remains modest and reactive.
- The Reserve Bank of Australia delivered a hawkish message at its August meeting, again "not ruling anything in or out". Governor Bullock pushed back on suggestions of early rate cuts, saying that "doesn't align with the Board's current thinking".
- In New Zealand, data continued to point to the dire state of the economy. Retail spending contracted sharply in the June quarter and the unemployment rate rose to 4.6%, despite a surprise lift in employment that was at odds with other measures of labour market activity. The RBNZ cut the Official Cash Rate by 25bp to 5.25% and signalled further cuts to come in the months ahead.

Salt Sustainable Income Fund Commentary

The Sustainable Income Fund gained in August, with a return of +2.40% (before fees / tax) in the month, which took its three-month gain to +6.34% and its one-year return to 12.27% (before fees / tax.) August's return was positively impacted by gains in all component assets; notably, the Salt Enhanced Property Fund. Markets continue to focus on when lower inflation will permit more central bank interest rate reductions. Data affecting central banks' easing timing has influenced the listed Real Asset and Bond returns within the portfolio, but this has now shifted to positive impacts. However, an easing bias from the RBNZ can assist NZ equity assets through the remainder of this year and allow some catch-up with global returns.

As inflation progressively confirms signs of a definitive down-shift, we expect component asset classes to improve further, as more global central banks embark on or advance their interest rate easings. Volatility across markets is ever-present but sentiment is much less fragile. We expect value recoveries in interest-rate sensitive assets to continue into Q4 2024.

August saw NZ domestic asset types recording further positive returns, which supplemented the returns contributions from the global components of the Income Fund. The NZ Dividend Appreciation Fund contributed +0.12% and the Enhanced Property Fund, 1.13% in August. The Salt Sustainable Global Infrastructure Fund contributed 0.55%. The Global Fixed Interest Opportunities Fund made a positive monthly contribution of 0.33% and the Sustainable Global Property Fund also had a small positive (+0.15%) impact for the month.

Salt Sustainable Income Fund outlook

Earlier markets had gotten ahead of themselves anticipating central bank rate cuts. Now these are expected to broaden this year and next. We believe bond yields adjusted sufficiently (via a volatile and uncertain route in the last 18 months) for us to move progressively toward a higher bond positioning within the Sustainable Income Fund. We consider inflation risk now poses a much-reduced danger to the capital valuations of bond portfolios. The allocation to bonds is now almost at the neutral 35% SAA.

Much of the softer returns patches from the Income Fund were due to the still-weak state of the NZ economy, straining under mild recessionary forces. The Reserve Bank of New Zealand was "on hold" until August with the Official Cash Rate, so domestic yields and discount rates were until recently fairly elevated. This suppressed returns from NZ equities through 2023 and early 2024. There is scope for improved NZ returns later this year, and the latest RBNZ Official Cash Rate Review, confirmed a policy rate reduction path ahead, whilst markets have priced in even more easing.

Diversified Income Funds containing an allocation to domestic equities generally experienced low overall capital value gains in early 2024, although their income yields remain attractive by historical standards, as the NZ equity market moved sideways overall for the last two years. NZ equities had good months in July and August, but better economic activity is really needed to lift corporate earnings and justify the re-pricing seen.

We anticipate the longer-term capital growth strategies within the Sustainable Income Fund to boost performance, as inflation conditions are improving. However, there is still a mildly recessionary period to traverse en route to that outcome in New Zealand. The phase of actual interest rate reductions from central banks has now begun, and when easing is more

broadly underway, we expect more beneficial capital growth impacts. This positive portfolio role will likely be a key feature of total returns into 2025.

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 of 1.125 cents per unit / quarter retained

Higher component asset yields enabled us to retain the quarterly cents-per-unit distribution from the fund, at 1.125 cpu, for the latest quarterly distribution which was paid out / reinvested in August.

As noted earlier, the silver lining in the bond market's repricing is that the yield received from bond investments shifted into a higher range and that 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 phase of interest rate adjustments, sufficient to anchor inflation expectations, has been successful. Recently, the balance of evidence has been on the better side globally, particularly suggesting that the US Federal Reserve is well on track to deliver an economic "soft landing." Rate reductions will follow incrementally later this year. In New Zealand, the timing is uncertain, as the Reserve Bank will need to assess the trajectory of inflation in mid-2024 and may not actually move the OCR down until the last quarter of the year.

While the data-driven market volatility at times requires fortitude from investors, the objective of securing an inflation-resilient income level 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 been commensurately rising through periods of market turbulence. This trend exemplifies the incremental return of some "risk premia" into asset classes.

The fund's modelled income received from coupons and dividends is still above its prospective distribution yield. We regard this as prudent, in a still-uncertain environment.

The Real Asset components of Infrastructure and Property are well-suited to the immediate period ahead, as central bank policy rates progressively fall. Defensive merit should continue to be asserted in coming months through renewed demand for these specific "Real Asset" equity types, along with the sustainable dividend-payers in the broader Australasian market.