Salt Sustainable Income Fund Fact Sheet – March 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 March 2024

Benchmark	Bank deposit rates (BNZBIL Index)
Reference portfolio	SAA-weighted component benchmark indices' performance
Fund Assets	$45.01 million
Inception Date	19 June 2021
Portfolio Manager	Greg Fleming
Prospective distribution yield (cents per unit) / based on Unit Price of 1.02.23	1.125 cents per unit per Quarter / 5.16% per annum

Unit Price at 31 March 2024

Application	0.8753
Redemption	0.8717

Sustainability Metrics

Fund ESG Scores	Portfolio	Category avge
Morningstar ESG score	20.94	22.00

Scores indicate risk level – a lower score reflects a lower ESG multi-factor risk level. ESG score as at 31.03.24. 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 March 2024

Global Fixed Interest	32.0%
Australasian Shares	29.0%
Global Listed Property	21.0%
Global Listed Infrastructure	17.0%
Cash or cash equivalents	1.0%
Asset allocation to Fixed Interest + Cash	**33.0%**

Fund Performance to 31 March 2024

Period	Fund Return (before fees and tax)	Gross Reference Portfolio Return
1 month	2.47%	2.45%
3 months	2.05%	1.49%
6 months	8.53%	8.20%
1 year	5.87%	4.22%
2 years p.a.	0.32%	-1.02%
Since inception p.a.	0.94%	-0.13%

Performance is before fees and tax, adjusted for imputation credits.
Reference Portfolio return is gross.

Top Individual Holdings at 31 March 2024

US 5Yr Note (CBT) Jun24	Infratil
Goodman Property Trust	Auckland International Airport
OSFI Futures Offset (Intl Bonds)	Spark New Zealand
Fisher & Paykel Healthcare	Vital Healthcare Property Trust
Precinct Properties NZ	Kiwi Property Group

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Market Commentary

- The first quarter of 2024 was a positive period for equity markets as activity data around the world was supportive of a soft landing. In response, developed market equities rose 9.0% (in USD) over the quarter. A 5% fall in NZD/USD boosted unhedged returns in Q1 2024.
- It was a more challenging period for bond investors as the resilient growth along with sticky inflation prints and a less dovish Federal Reserve saw the global aggregate bond index returning -2.1% (in USD) over the three-month period.
- The most obvious implication of the strong activity/sticky inflation scenario was reflected in the shift in market pricing of the number of US rate cuts expected in 2024. At the end of 2023 seven rate cuts were expected in the US in 2024. By the end of the quarter that had been brought into line with the Fed's "dot plot" of three cuts.
- The best performing equity market of the quarter was once again Japan, with the Topix up 18.1% over the three months. That's despite the Bank of Japan beginning normalisation of its monetary policy in March. The central bank announced the end of its negative interest rate policy, yield curve control, and its purchases of equity exchange traded funds and real estate investment trusts.
- Inflation in the Euro area continued its downward trajectory, coming in at 2.6% in February. The ECB left interest rates on hold in March, with President Lagarde saying the ECB was unlikely to be able to cut rates in April, though June remains live for a first cut.
- The Swiss National Bank became the first developed central bank to ease policy, surprising the market with a 25bps cut in its policy rate to 1.5%. This was in the context of inflation already having fallen back to below the central bank's 2% target. The annual rate of increase in headline inflation came in at 1.2% in February.
- The Chinese economy appears to be responding to recent stimulus. Official data on retail sales, industrial production and fixed asset investment for January and February beat expectations across the board. However, we continue to believe further stimulus will be required if the official target of around 5% GDP growth in 2024 is to be met.
- In Australia, Q4 GDP data confirmed a subdued end to 2023. More recent partial indicators point to ongoing below-trend growth in early 2024. With the effects of tight monetary policy increasingly evident in activity data and inflation trending in the right direction, monetary policy is expected to remain on hold for the foreseeable future.
- In New Zealand, December 2023 quarter GDP came in at -0.1% q/q and -0.3% y/y. The economy has now contracted in four of the last five quarters. This justified the RBNZ's decision to keep rates on hold at its February Monetary Policy Statement, where it also signalled a reduced probability of future interest rate increases. We continue to believe the next move is a cut, but not until November.

Salt Sustainable Income Fund Commentary

The Sustainable Income Fund's rebound resumed in March, with a return of 2.47% (before fees) in the month, which led its quarterly return to 2.05%, its six-month gain to 8.53% and its one-year return to 5.87% (before fees and tax.) The gain in March more than recovered small declines in January and February, which reflects reconsiderations in bond markets as to the likely speed of lower central bank interest rates. Uncertainty on central banks' easing timing has influenced the listed Real Asset returns within the portfolio, after their strong late-2023 gains.

For the three-month period to 31 March, the Sustainable Income Fund was ahead of its reference index. For the year to 31 March, the portfolio's reference index rose by 4.22% which was behind the fund's 5.87% one-year gross return (before fees / tax.)

As inflation progressively shows signs of a definitive down-shift, we expect component asset classes to improve further, as global central banks will ultimately embark on interest rate easings. Volatility across markets is ever-present but sentiment is much less fragile. Central banks around the world remain vigilant but have scope to assess the impact of high rates on inflation pressures positively, and incrementally lower rates. We expect value recoveries in interest-rate sensitive assets to continue in 2024.

However, markets expressed excessive optimism in late-2023 as to how swiftly those central bank rate cuts are likely to eventuate. A more realistic turn in 2024 explains the moderating returns from the most interest rate-sensitive asset components of the Income fund.

March month saw positive returns contributions from all components of the Income Fund. The strongest element was the Salt Sustainable Global Infrastructure Fund, which contributed 0.69% and the Dividend Appreciation Fund, which provided 0.68%. Salt's Enhanced Property Fund contributed 0.55% in March, and the Global Fixed Interest Opportunities Fund and Sustainable Global Property Fund, which contributed 0.22% and 0.13%, respectively.

Salt Sustainable Income Fund outlook

Markets got ahead of themselves in late-2023 in anticipating central bank rate cuts, though these are still expected for later this year. We believe bond yields have now 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 reduced danger to the capital valuations of bond portfolios. The allocation to bonds is now 29.5% 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 remained "on hold" with the Official Cash Rate, as core inflation is persisting, so domestic yields and discount rates are likely to stay fairly elevated. This suppressed returns from NZ equities through 2023, and the relative weakness of NZ shares compared to global equities was a notable feature last year. There is some scope for improved NZ returns later this year, and the latest RBNZ Monetary Policy Statement indicated a less aggressively-restrictive tone than feared.

Diversified Income Funds containing an allocation to domestic equities have generally experienced low overall capital value gains in early 2024, although their income yields remain attractive by historical standards, as the NZ equity market has moved sideways overall for the last two years.

Until a catalyst for a resumption in NZ equity market performance emerges, much of the medium-term capital growth objective of the Fund will be driven by international assets, which comprise half of the Portfolio at current allocation weightings.

We anticipate the longer-term capital growth strategies within the Sustainable Income Fund to boost performance, as inflation conditions are stabilizing. However, there is still a mildly recessionary period to traverse en route to that outcome (in New Zealand, if not globally.) The phase of actual interest rate reductions from central banks is still some months into the future but when that is underway, we expect more beneficial capital growth impacts. This positive portfolio role will likely be a key feature of total returns in 2024-5.

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 February. This will be updated again in May 2024, dependent on the outlook for overall Fund's income.

As noted earlier, the silver lining in the bond market's repricing is that the yield received from bond investments have shifted to 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 engineer 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 early 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, though this has further to go.

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

The equity capital value components of the Income Fund have adjusted to reflect weaker economies overall, yet the Real Asset components of Infrastructure and Property are well-suited to the subdued immediate period ahead, as central bank policy rates will begin to 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.

In late March, we lowered the Fund's allocation to the Enhanced Property Fund by 2.5% and lifted the Fund's investment in the Sustainable Global Fixed Income Opportunities Fund by 2.5%. This increased the Defensive allocation within the Income Fund to 33%, in line with the economic outlook. The yield impact on the Dynamic Asset Allocation switch was negligible, but we think that Sustainable Global Bonds still have upside potential, and lower volatility risk than Australasian listed property stocks.