SALT

Salt Sustainable Global Shares Fund Fact Sheet – November 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

To achieve the Fund's investment objectives, 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 30 November 2024

Fund Assets	$82.73 million
Inception Date	12 July 2021
Underlying Manager	Morgan Stanley Investment Management

Unit Price at 30 November 2024

Application	1.4100
Redemption	1.4043

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 Allocations at 30 November 2024

Global equities	97.6%
Cash & sundry items	2.4%

Fund Performance to 30 November 2024

Period	Fund Return	Benchmark Return
1 month	3.57%	5.23%
3 months	7.98%	10.41%
6 months	16.38%	15.56%
1 year	26.96%	33.47%
2 year p.a.	20.49%	23.13%
3 year p.a.	11.80%	13.88%
Since inception p.a.	11.67%	13.82%

Performance is before fees and tax and adjusted for imputation credits.
Benchmark (MSCI World Index in NZD) performance is gross.

Fund holdings

Top 10 holdings	
Microsoft (US)	Accenture (US)
SAP (DE)	L'Oreal (FR)
VISA (US)	Alphabet (US)
Aon (US)	Intercontinental Exchange (US)
Procter & Gamble (US)	United Health Group (US)

Source: MSIM, data as at 30 November 2024.
The Top 10 Holdings represented 41.8% of the total portfolio.

The Portfolio's weighted average carbon intensity (WACI) was 82% lower than the MSCI AC World Index.[A]

Market Review

- Markets were dominated in November by the Republican clean sweep of US elections. This had markets contemplating a more expansionary US fiscal policy and a more nationalist trade policy. US equities gained +6.3%, contributing to a 4.6% rise in developed market equities (in USD terms.)
- Bond markets were less enamoured with the potential inflationary implications, with the global aggregate bond index returning +0.3%.
- Solid economic data also contributed to positive equity markets, feeding the theme of US exceptionalism. The Fed cut by 25bp, citing further progress on disinflation.
- In Europe, the ECB is contending with weak economic fundamentals, while inflation is proving resilient. Political uncertainty in Garmany and France also impacted markets.
- In Japan, expectations of another interest rate hike are building, with a further 25bp increase possible before Christmas although a January hike is more likely.
- In China, highly anticipated fiscal stimulus disappointed the market. While a debt swap arrangement for local governments

was welcome, a lack of meaningful stimulus aimed at boosting consumption was well short of expectations.

- The RBA maintained its hawkish bias in November, stating it needs to remain vigilant to upside risks to inflation. The tight labour market saw the unemployment rate remain at 4.1%.
- In NZ, weak labour market data saw the unemployment rate rise to 4.8%, with a decline in the participation rate preventing a sharper rise. Activity data remained weak, though increasing signs of a bottoming out of recent declines are starting to emerge. The RBNZ cut the OCR by 50bp to 4.25%.

Portfolio Review

- Global equity markets recovered in November, following the resolution of some political uncertainties after the clear Republican Presidential and Congressional electoral victories.
- An additional decline of -0.8% in the NZD/USD in November again lifted the returns in NZ dollar terms for the month.
- In November, the Portfolio returned +3.57%, while the MSCI World Net Index returned +5.23%. We seek to deliver attractive long-term absolute returns.
- The November underperformance was mainly due to stock selection, driven by weakness in Information Technology and to a lesser extent, Financials and Consumer Staples.
- Whilst Health Care was a positive contributor, it was insufficient to compensate. Sector allocation was also negative, driven by the hits from the Health Care overweight and Consumer Discretionary underweight. Combined, these were larger than the positive impact from the Financials overweight and zero weight in Materials.
- At the strategy level, the largest contributors to absolute performance during the month were Visa, up on the back of market expectations of an easier regulatory landscape under a Republican administration, Procter & Gamble, as the company maintained its outlook for solid organic sales growth despite commodity headwinds, demonstrating its strong pricing power, Booking Holdings, maintaining momentum on the back of strong revenue growth, AJ Gallagher, following strong third-quarter results and deregulation hopes, and Aon, which continues to show decent growth after a soft patch earlier in the year.
- The largest contributors' impacts were **Visa** (+51 basis points (bps), **Procter & Gamble** (+34 bps), **Constellation Software** (+30 bps) **Booking Holdings** (+29bps), **Arthur J. Gallagher** (+29 bps).
- At the strategy level, the largest absolute detractors were **L'Oréal,** down due to potential tariffs from the U.S. President-elect and continued low consumer demand in China, **Keyence**, which reported a mixed set of second-quarter results due to a slowing Chinese economy undercutting earnings, **Becton Dickinson**, down despite delivering fourth-quarter results broadly in line with expectations, **AIA**, which weakened along with the China market and **Alphabet**, which was hit by negative headlines as the Department of Justice (DOJ) released its proposed remedies in the antitrust investigation into Google's search business.
- The largest absolute detractors' impacts were **L'Oréal** (-23 bps), **Becton Dickinson** (-12 bps), **AIA** (-11 bps), **CDW** (-6 bps), **Thermo Fisher** (-6 bps.)

Commentary & Outlook for November 2024: US Election and Distortion (Morgan Stanley Investment Management)

In November, we saw global markets respond strongly to the Republican victory in the U.S. election with a "risk-on" rally and a stronger dollar, driven by expectations for deregulation, corporate tax cuts, and an "America First" agenda. The MSCI World Index returned a healthy +4.6% in U.S. dollars (USD) and +5.2% in NZD.

At the sector level, cyclicals were the month's top performers, with Consumer Discretionary (+9%) and Financials (+8%) outperforming the MSCI World, while Information Technology and Industrials (+5%) were roughly in line. Defensive sectors lagged, including Consumer Staples (+2%) and Utilities (+2%). Health Care (-1%) and Materials (-1%) were the only negative sectors in the month.

In terms of geography, unsurprisingly given geopolitical events, the U.S. (+6%) outperformed the index, although Singapore was the best performing country +8% in U.S. dollars (USD), and +9% in local currency. Other Asian markets underperformed the MSCI World, including Japan (+1%, -1%) and Hong Kong (- 4%, -4%). Elsewhere performance was weak; Germany (-0%, +3%), Switzerland (-2%, -0%), Spain (-4%, -1%) and France (-4% -2%) were all behind the index in both USD and local currency terms. The UK showed a slightly positive return (+1%, +3%) but also lagged.

The Great Distortion

We're in a charged and unpredictable landscape. East-West tensions simmer, the Middle East remains a powder keg, and the Russia-Ukraine war looks set to enter another harsh winter as tensions escalate. Meanwhile, Donald Trump is to return to the White House, backed by an emboldened Republican party holding both House and Senate. All eyes are on the potential economic and societal shifts this new administration may bring.
We saw markets swiftly respond to Trump's victory with a "risk-on" rally in the U.S. and a stronger dollar, driven by expectations for deregulation, corporate tax cuts, and an "America First" agenda. While there may well be positives for U.S. markets from the "Trump agenda", there are also many potential negatives, not least the inflationary risks inherent in many of his proposed policies.

For example, tariffs could push up consumer prices and corporate costs, while mass deportations could increase labour costs in the U.S. Should an inflationary environment result, the Federal Reserve may need to alter its current path and hold rates higher for longer, potentially constraining economic growth and pressuring weaker balance sheets. In addition, tax cuts may boost corporates' profits at the expense of a higher government deficit, intensifying long-term concerns about U.S. fiscal sustainability.

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Whatever the resulting policies and their ramifications, markets are facing greater uncertainty; uncertainty that does not seem to be reflected in prices, not least in the VIX Index – the measure of expected S&P 500 volatility – which is currently trading below 15[1].

Any current unusual happenings are not just confined to politics. As we have previously covered, investors are having to contend with an increasingly narrow market environment. While the MSCI World Index is designed to be globally representative, capturing large- and mid-cap stocks across 23 developed markets, its market-cap weighted methodology has led it to become increasingly distorted, with the dominance of U.S. techy giants (aka the "Magnificent Seven"), propelling the U.S. to 70% of the overall index.[2]:

Index distortion impacts valuation. The 10 largest companies in the index, which account for 25% of MSCI World's total market capitalisation and are nearly all tech or tech adjacent, trade at an average 34x next 12 months (NTM) earnings[3]. If you compare this to the broader MSCI World Index which trades at a near historical high of 19x NTM earnings, the equal weight index at 15.4x, and the ex-U.S. segment at just 14x, it becomes glaringly obvious that size and geography matter.[4]

The valuation gap between the MSCI USA Index and the MSCI World ex-U.S. Index is now at its widest this century, with the U.S. trading at more than a 50% premium to the rest of the world.[5]

Index huggers beware. For managers closely tied to the index, a tracking error-focused approach driven by recency bias may be far riskier in absolute terms than it may appear. In our experience, markets tend not to worry about high multiples so long as strong earnings growth perseveres. However, any knock or fade to earnings may spell trouble, particularly for a distorted index which seems to be priced for perfection

As we explained in our June Global Equity Observer ("GEO") "Independent Thinking", we've always been cautious about the index. Though it appears diversified, it can steer investors toward a concentrated set of today's winners, chasing where the pendulum has swung, rather than to where it may swing.

The index disregards quality and valuation and prioritises size over conviction. With this you own everything – indiscriminately, an approach that doesn't align with our long-term absolute investment approach.

The case for active

As active managers, recent market distortions have presented opportunities and we've been able to take advantage of these for the Portfolio. So far this year, we've added eight new names from seven different industries, all at attractive valuations. Together, these companies' forward price to earnings (PE) ratio aligns with that of the broader market, yet they boast more than double the market average in both return on operating capital and gross margin (our key quality characteristics).

Examples include AutoZone, the leading auto parts retailer in the U.S. with an exceptional capital allocation record, and CME, the leading U.S. futures exchange with incredibly high barriers to entry due to its network effects.[6]

Turning to sales from the Portfolio, increased valuations this year, combined with careful reviews of companies' fundamentals, have led us to exit certain positions where we felt either the multiple or business quality no longer justified ownership.

Our benchmark agnostic approach is grounded in rigorous fundamental research. Over more than a quarter of a century of high-quality investing, we have weathered it all – from recessions and wars to credit crises, pandemics, inflation and deflation, and now five U.S. Presidents. Over these 28 years, we have remained committed to our disciplined investment philosophy focusing on the relentless pursuit of quality and a commitment to avoid overpaying. In these unusual times, our focus remains on what drives strong long-term performance – the compounding of high-quality company fundamentals.

Sources

A. Source: Trucost. WACI is calculated using Scope 1 & 2 emissions per $m of company revenue. The term carbon refers to greenhouse gas (GHG) emissions, measured in metrics tonnes of carbon dioxide equivalent (CO_2e) emissions. Our data provider's methodology follows the GHG protocol and includes carbon dioxide (CO_2), methane (CH_4), nitrous oxide (N_2O), hydrofluorocarbons (HFCs), perfluorocarbons (PFCs), sulphur hexafluoride (SF_6) and Nitrogen Trifluoride

1. Source: FactSet. Data as of 29 November 2024.
2 Source: FactSet. Data as of 29 November 2024.
3 Source: FactSet. Date 29 November 2024. NTM earnings are estimated.
4 Source FactSet. Date 29 November 2024. NTM earnings are estimated.
5 Source FactSet. Date 29 November 2024.

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