SALT

Salt Sustainable Global Fixed Income Opportunities Fund Fact Sheet – May 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 primary objective of the Fund is to target and generate an attractive rate of return over a full three-to-five-year market cycle. To achieve this, the Fund targets a portfolio of global fixed income securities with enhanced total return potential and superior Sustainability characteristics.

The objectives of this top-down selection process are to:
1. Reduce exposure to material ESG risk and negative sustainability impacts, through restriction screening of controversial sectors such as weapons, tobacco and some fossil fuels, as well as international norms violations;
2. Tilt the portfolio in favour of the 80% strongest sustainability performers across corporates, by sub- sector, and sovereigns; and
3. Contribute to positive outcomes based on key sustainability themes, with a particular focus on low carbon intensity.

The Fund will invest at least 50% in investment grade bonds, and a minimum of 15% in sustainable bonds. The fund targets its returns to be 100% hedged to the New Zealand dollar.

Fund Facts at 31 May 2023

Benchmark for ESG purposes	Bloomberg Global Aggregate Index (NZD hedged)
Fund Assets	$58.49 million
Inception Date	10 February 2023
Underlying Manager	Morgan Stanley Investment Management
Average credit rating	Standard & Poor's A- / Moody's A3
Effective Duration	3.5 years

Unit Price at 31 May 2023

Application	1.0033
Redemption	1.0023

Investment Guidelines

The guidelines for the Sustainable Global Fixed Income Opportunity Fund are:

Global Fixed Income securities	95% – 100%
Cash	0% – 5%

Fund Allocation at 31 May 2023

Global fixed income securities	98%
Cash	2%

Fund Performance to 31 May 2023

Period	Fund Return (Gross)
1 month	-0.14%
3 month	1.55%
Since inception cumulative	0.49%

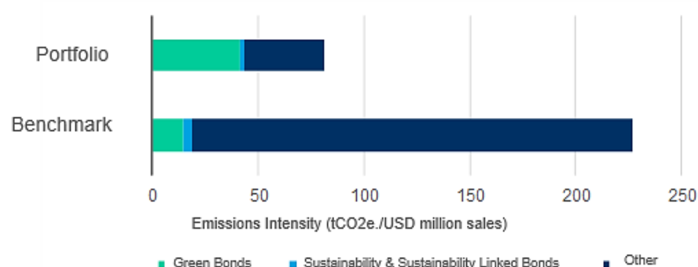
Performance is gross of fees and tax. Past performance is not a guarantee of future results. Data as of 31 May 2023.

Fund ESG Scores	Portfolio	Index	YTD change
MSCI ESG Score (MV%)	96.3%	91.5%	-
Green, plus Social, Sustainability and Sustainability-linked bonds	25.8%	2.6%	
MSCI ESG Score adj.	7.48	6.33	7.48
- Environment score	7.35	6.13	7.35
- Social score	5.60	5.57	5.60
- Governance score	6.12	5.73	6.12
MSIM ESG Sovereign score	2.12	2.10	-

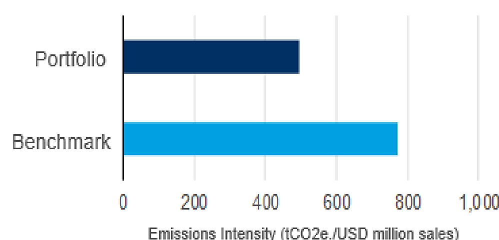
Source: MISM Monthly Investment Report / MSCI ESG Research as at 31 May 23.

Fund CO2 Emissions Intensity characteristics at 31 May 2023

Emissions Intensity - Scope 1&2



Emissions Intensity - Scope 3



Source: MISM Monthly Investment Report / MSCI ESG Research as at 31 May

Labelled sustainable bond major holdings > 1%	MSCI ESG rating
Top 5	
European Union MTN (Social)	A
BNP Paribas MTN (Green)	AA
European Investment Bank (Green)	AAA
Council of Europe Development Bank MTN (Social)	AAA
Export-Import Bank of Korea (Green)	BB

Portfolio Review

- In the one-month period ending 31 May 2023, the portfolio returned -0.14% (gross of tax & fees). The performance can be attributed to the following factors:
- The portfolio's positioning in duration was the main negative driver (especially US rates) as yields rose across the curve last month.
- Within investment grade credit, spreads widened with financials underperforming industrials and utilities.
- The portfolio's exposure to high yield credit had a neutral impact on performance.
- Exposure to government related debt also had a neutral impact on performance in May.
- The portfolio's exposure to securitized debt was again a positive contributor to performance.

Strategy Changes

There were no material changes in strategy during the May month.

Portfolio Commentary & Outlook

Developed market rates were broadly higher in May while German Bunds outperformed, down 3 bps on the month following weaker than expected economic and inflation data in Europe. By May, the banking sector stress in the US from March largely went away, with the market shifting to a focus on the US debt ceiling debate briefly. While the conflict again created volatility in the market (especially in the bill market), the situation was resolved with a deal at the end of the month and the market centred its attention on economic data again.

Overall, much of the data depicted economic resilience and sustained inflationary pressure as shown for example in the US, Australia, and especially the UK. The well anticipated Senior Loan Officer Opinion Survey showed that credit conditions had tightened, but perhaps not as severely as the market was expecting. In terms of central bank meetings, the Fed, ECB, BoE, and the Norges bank opted for 25 bps as expected by markets. The Antipodean central banks decisions were more surprising to markets, with the RBA first surprising markets by hiking 25 bps after pausing the month before. In contrast, the RBNZ slightly surprised markets by only hiking 25 bps vs a potential 50 bps while keeping the policy path the same vs expectations for a more hawkish policy path.

Now that the acute issues related to the banking sector seem to have settled down and the debt ceiling has been resolved, the market has shifted to focusing on interpreting new economic data. Additionally, in the US, the market is now assessing the implications of the Treasury General Account (TGA) rebuild following the debt ceiling resolution. While the banking sector crisis has calmed, credit conditions are still tight and may tighten even further, putting increased pressure on borrowers. With that said, despite the tighter credit conditions and expectations for a slowdown, hard economic data has yet to deteriorate significantly, and the market is again starting to price in higher terminal rates and price out cuts.

Given the uncertainty, it is difficult to concretely express an outright view on interest rates. We recommend patience, awaiting further clarification while taking advantage of more relative dislocations. In terms of foreign exchange, with a more resilient US economy and more confidence in the US banking system, the dollar strengthened during May. We expect the U.S. dollar to continue weakening and have tactically made adjustments where attractive.

IG spreads outperformed Euro IG spreads this month amidst elevated credit market volatility driven by several factors. Firstly, concerns over the US debt ceiling negotiation were key for most of the month, though it resolved within a few weeks. Secondly, US regional banking volatility remains elevated despite sentiment improving over the month as First Republic was taken over by JPM (market has been impacted by tighter lending conditions as evidenced by the Senior Loan Officer Survey). Economic data continues to weaken over the month globally (PMI's particularly weak in manufacturing), similarly inflation data remaining sticky to the upside which led to rate hikes in both the US and Europe. Finally weaker equity and commodity markets ex Technology that benefitted from the focus on the multiple uses of AI.

U.S. and global high yield markets were weaker in May, with the weakness generally attributable to higher rates versus emerging credit concerns. The technical conditions in high yield continued to improve in May amid reduced volatility.

Looking forward, our base case is a likely mild economic slowdown. The magnitude and impact on downgrades/defaults is likely to be low as a combination of strong employment and conservative corporate management support markets. Finally, the demand for high quality fixed income remains robust as the strong supply continues to be matched. We remain cautious on the high-yield market as we progress through the second quarter of 2023.

Securitized yields remain at historically wide levels, and we believe these wider spreads offer more than sufficient compensation for current market risks. Fundamental credit conditions remain stable despite recession risks.

We continue to believe that the fundamental credit conditions of residential mortgage markets remain sound, but also believe that higher risk premiums are warranted across all credit assets given projected economic weakness. We remain more cautious of commercial real estate, especially office, which continues to be negatively impacted in the post-pandemic world.

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