Salt Sustainable Income Fund Fact Sheet – October 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 October 2024

Benchmark	Bank deposit rates (BNZBIL Index)
Reference portfolio	SAA-weighted component benchmark indices' performance
Fund Assets	$47.99 million
Inception Date	19 June 2021
Portfolio Manager	Greg Fleming
Prospective distribution yield (cents per unit) / based on Unit Price of 1.11.24	1.125 cents per unit per Quarter / 5.01% per annum

Unit Price at 31 October 2024

Application	0.9055
Redemption	0.9018

Sustainability Metrics

Fund ESG Scores	Portfolio	Category avge
Morningstar ESG score	18.81	21.00

Scores indicate risk level – a lower score reflects a lower ESG multi-factor risk level. ESG score as at 30.09.24. 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 October 2024

Global Fixed Interest	35.0%
Australasian Shares	27.5%
Global Listed Property	18.5%
Global Listed Infrastructure	17.0%
Cash or cash equivalents	2.0%
Asset allocation to Fixed Interest + Cash	**37.0%**

Fund Performance to 31 October 2024

Period	Fund Return (before fees and tax)	Gross Reference Portfolio Return*
1 month	0.30%	-0.72%
3 months	3.56%	2.12%
6 months	7.75%	7.53%
1 year	18.33%	17.16%
2 years p.a.	8.38%	6.85%
3 years p.a.	1.92%	0.33%
Since inception p.a.	2.76%	1.47%

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

Top Individual Holdings as at 31 October 2024

US 5Yr Note (CBT) Dec14	NZD Cash
Fisher & Paykel Healthcare	Auckland International Airport
Goodman Property Trust	US 10Yr Ultra Fut Dec24
Infratil	Contact Energy
Precinct Properties NZ	Argosy Property Trust

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Market Commentary

- October was a volatile month for markets. Developed market equities gave back some of their gains of 2024 thus far, falling -2.0% over the month. The global aggregate bond index also posted a negative return for the month, falling -1.5% (NZD-hedged.) This was largely on the back on the recalibration of the likely pace of interest rate cuts by the US Federal Reserve.
- In the US, inflation data for September came in hotter than expected. Headline CPI posted its lowest annual rate in over three years, though core remained sticky at 3.3% y/y. Activity and labour market data also came in stronger than expected. This has seen markets pare back the likely pace of US interest rate cuts. After cutting the Fed Funds rate by 50bp in September, markets now expect the Fed to deliver smaller 25bp moves in November and December.
- US election uncertainty also contributed to higher bond yields. Market focus is on fiscal sustainability and likely bond issuance, as well as the prospect of tariffs after a Trump victory.
- In Europe, annual inflation moved up to 2.0% in October, but this was primarily due to energy base effects. There were signs of weakening economic momentum over the month, particularly in the manufacturing sector. This prompted the European Central Bank to deliver a third 25bp cut in the deposit rate, taking it to 3.25%.
- In the UK, headline inflation fell to 1.7% y/y, though core remained higher at 3.2%. The labour market remains tight with the unemployment rate falling to 4.0%, while the UK Budget announcement put upward pressure on Gilts.
- The Bank of Japan left interest rates unchanged in October, though the tone of the statement was hawkish. Annual Tokyo inflation came in at 1.8% y/y, supporting the case of higher wage increases flowing through into more generalised inflation.
- The Chinese authorities announced further support measures for the ailing property market over the month. Collective stimulus measures to-date should result in improved activity levels, but we still think more is required, particularly more meaningful action to boost consumption.
- The labour market remains tight in Australia. Jobs growth beat expectations for the sixth consecutive month in September. For now, that demand is being met by increased labour supply. The disinflation process is continuing, but the risk for the central bank is that labour supply growth cools before demand does, reigniting wage inflation. No interest rate cuts are expected here until next year.
- In New Zealand annual CPI inflation came in at 2.2% in the year to September, the first time it has been in the RBNZ's 1-3% target band since the March quarter of 2021. Most of the work has been done by the lower cost of imports and import competing goods (-1.6% y/y), while non-tradeable inflation remains too high (+4.9% y/y). The RBNZ will be watching the latter closely as they now muse on the challenge of sustaining inflation within the target band.

Salt Sustainable Income Fund Commentary

The Sustainable Income Fund gained in October month, with a return of +0.3% (before fees / tax) in the month, which took its three-month gain to +3.56% and its one-year return to 18.33% (before fees / tax.) The month's return was positively impacted by gains in NZ domestic component assets, as global shares and bonds weakened. Markets continue to focus on lower inflation permitting central bank interest rate reductions. Data affecting central banks' easing timing has influenced the listed Real Asset and Bond returns within the portfolio. However, a more pronounced easing path from the RBNZ can assist NZ equity assets through the remainder of this year and allow additional catch-up with global asset returns. Diversification of income sources remains effective.

As inflation progressively confirms a definitive down-shift, we expect component asset classes to improve further, as more global central banks 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 through Q4 2024 and into 2025.

October saw NZ domestic asset types recording further positive returns, which offset the month's softer returns contributions from the global components of the Income Fund. The NZ Dividend Appreciation Fund contributed +0.5% and the Enhanced Property Fund, +0.2% October. The Salt Sustainable Global Infrastructure Fund detracted -0.1% as did the Sustainable Global Property Fund. The Global Fixed Interest Opportunities Fund made the largest negative monthly contribution of -0.3% as bond interest rates rose sharply around the world.

Salt Sustainable Income Fund outlook

Central bank rate cuts are continuing to broaden this year and next, with the Federal Reserve and Bank of England both cutting by -0.25% in early November. We believe bond yields adjusted sufficiently (via a volatile and uncertain route in the last 24 months) for us to have instituted a neutral 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 at the neutral 35% SAA weight. Due to fiscal risks, particularly surrounding the policies of the incoming Trump administration, we would move overweight only incrementally.

The NZ economy is still 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. Now that the domestic easing cycle is underway, there is scope for improved NZ returns, especially next- year, and the latest RBNZ Official Cash Rate Review confirmed a clear policy rate reduction path ahead.

Diversified Income Funds containing an allocation to domestic equities generally experienced limited capital value gains in early 2024, but that has now improved. Income yields remain attractive by historical standards. NZ equities had a very good Third quarter and a resilient October, but better economic activity is needed to lift corporate earnings and justify the re-pricing seen.

We anticipate the longer-term capital growth strategies within the Sustainable Income Fund will 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. Hence, the sourcing of Fund income from a globally-diversified set of yielding securities.

The phase of meaningful interest rate reductions from central banks is however well underway, and when economies respond with asset revaluations, 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 will be paid out / reinvested in November.

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 have followed and should progress incrementally later this year and into 2025.

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 stable through periods of market turbulence. This trend exemplifies the incremental return of some "risk premia" into certain asset classes, which had previously been unappetizing compared with risk-free assets. However, global credit spreads are now very narrow, limiting potential revaluation upside from both Investment Grade and lower rated bonds.

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.

Finally, the lowering of the NZ Official Cash Rate has substantially reduced the Term Deposit rates offered by domestic banks, and we anticipate the downtrend in the indicative benchmark of the NZ Bank Bill rate and the 6-month Term Deposit rates to persist throughout 2025.