CarbonFund

Carbon Fund Fact Sheet – Quarter ending 31 March 2019

Manager Profile

Salt Funds Management is a boutique investment management firm wholly owned by its employees. We are active managers. Our shared investment philosophy is centred on the belief that market inefficiencies exist that can be exploited over time to deliver superior risk-adjusted returns.

Further, the consideration of environmental, social and governance (ESG) factors is integral to the research we carry out. Salt analysts consider the potential for ESG factors to influence long term returns on invested capital (positively and negatively).

Investment Strategy

The Fund's aim is to provide investors with a total return exposure to the price of carbon credits. The Fund has the ability to buy carbon credits in emissions trading schemes in New Zealand and offshore.

The Fund gains its exposure to the price of carbon credits in the NZ ETS through purchasing and holding carbon credits on the NZ ETS. We may also use swaps or other derivatives to gain exposure to the NZ ETS.

The Fund will also have the ability to buy carbon credits in international emission trading schemes, as well as futures, swaps or other derivatives that provide exposure to international schemes. As a result, the Fund may also provide exposure to the price of carbon offshore.

The Fund is actively managed by us. This means we buy and sell carbon credits on emission trading schemes, or hold cash based on our own analysis and assessment of the market. This includes our assessment of the price of carbon credits relative to the demand and supply of carbon credits and other factors including technological advancements, politics, regulation, fuel prices and even global weather and climate change.

Fund Details

Fund Assets	$1.5 million
Inception Date	8 November 2019
Portfolio Manager	Paul Harrison
Total Fund Charges (p.a.)	0.95%
NZX Code	CO2

Who is involved?

Supervisor	The New Zealand Guardian Trust Company Limited
Custodian	The New Zealand Guardian Trust Company Limited
Administration Manager	MMC Limited
Unit registrar	Link Market Services Limited
Investment Manager	Salt Funds Management Limited

Net Tangible Assets (NTA) Value at 31 March 2019

Application	1.0125

CO2 price on NZX Main Board at 31 March 2019

NZX Close	1.04

Investment Guidelines

The guidelines for the Carbon Fund are shown below:

Carbon credits	0% – 100%
Cash	0% – 100%

Target investment Mix

The target investment mix for the Carbon Fund is:

Carbon credits	98.00%
Cash	2.00%

Fund Allocation at 31 March 2019

Carbon credits	99.94%
Cash	0.06%

Fund Performance to 31 March 2019*

Period	Fund Return*
1 month	1.26%
3 months	1.34%
Since inception p.a.	3.19%

Performance is based on NTA movement and is after all fees and 28% PIE tax.

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Factsheet March 2019

Quarterly Fund Commentary

Summary

- NZUs have traded above the $25 Fixed Price Option for all the first quarter of 2019.
- Expect announcements from the government around ETS changes over the coming quarter.

Dear Fellow Investor,

Over the quarter ending March 2019, the core underlying asset of the Fund, New Zealand Units (NZUs), experienced price appreciation of +2.30%, closing at $25.75. This represented a level just 10 cents off all-time highs of $25.85 struck in December 2019 and 85 cents above the $25 Fixed Price Option (FPO) level. The Fund remains near fully invested with a cash weighting of less than 1%.

The first quarter of any given year is typically short on political news flow, and this quarter was no different. Possibly the most meaningful announcement with respect to changes within the Emission Trading Scheme (ETS) was targeted at the forestry sector. The incumbent ETS forestry rules in principle left participants that had registered under the ETS liable to make payments for NZU's earned, should they harvest their forest, or even if it was lost due to fire or weather events. The liability that this rule placed on foresters in our view, discouraged potential forestry ETS participants and has added to the challenge of meeting emissions reductions targets set out under the Paris Agreement. Under the new rules, foresters may use an "averaging" methodology when receiving NZUs associated with their forestry sequestration (removal of carbon from atmosphere). Ultimately, this reduces the liability that foresters faced, and provides certainty in the sector. We welcome this decision made by the Government as it provides additional rigour to the New Zealand ETS rule set, while providing a key "supply-side" participant the certainty required to invest in the market.

We continue to await more material changes to the ETS to be announced by the Government with respect to the auctioning of NZUs currently allocated for free to emissions intensive trade-exposed entities, and a change to the current $25 fixed price option. Minister Shaw continues to work on the introduction of the Zero Carbon Bill, while the Interim Climate Change Commission are nearing the completion of their report to the Minister. Some market commentators are suggesting that a delay in the Government's budget delivery to May 30th has been made to coincide with the end of the emitters NZU surrender period. Given the financial impact this can have on the Budget, this may in turn be used to deliver any changes to the ETS. It would not seem unreasonable to see emitters elect to pay the penalty option while retaining their NZUs for future use, resulting in a cash flow contribution to the Government accounts. As we have discussed in the past, this is equivalent to the Government subsidising the country's emitters, which we expect both the Government and the general taxpayer will find equally uncomfortable.

We continue to watch Australian market developments closely in what is potentially a watershed climate policy year as the General Election approaches in May. The Australian Labor Party recently released their climate change policy to the public. While we await more detail, at a high level the policy intends to dramatically reduce the allowable emissions cap from 100,000 tonnes to 25,000 tonnes per year and introduces more emitters into the scheme. In aggregate, this would contribute to emissions reductions of 45% relative to 2005 levels, compared to the current target of 27%. Labor's intention appears to be to create a tradable offset market where Australian participants can buy and sell amongst each other dependent on their respective emission footprints. No matter the election outcomes, we expect clarity on carbon reduction and pricing to be a feature of the respective election campaigns.

Finally, European Emission Allowances continue to trade strongly at a New Zealand dollar equivalent price of $45.35 (€26.73)

Thank you for your interest and support in the Carbon Fund. We look forward to bringing you more developments in the New Zealand and international carbon markets in the future.