



CarbonFund

Carbon Fund Fact Sheet – Quarter ending 31 December 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	\$2.66 million
Inception Date	8 November 2018
Portfolio Manager	Paul Harrison
Total Fund Charges (p.a.)	0.96%
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 December 2019

Application	1.0788
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CO2 price on NZX Main Board at 31 December 2019

NZX Close	1.06
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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 December 2019

Carbon credits	97.99%
Cash	2.01%

Fund Performance to 31 December 2019

Period	Fund Return
1 month	9.94%
3 months	9.37%
6 months	14.47%
1 year	7.97%
Since inception p.a.	6.82%

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

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Quarterly Fund Commentary

Dear Fellow Investor,

The December quarter was an important turning point for climate change policy in New Zealand.

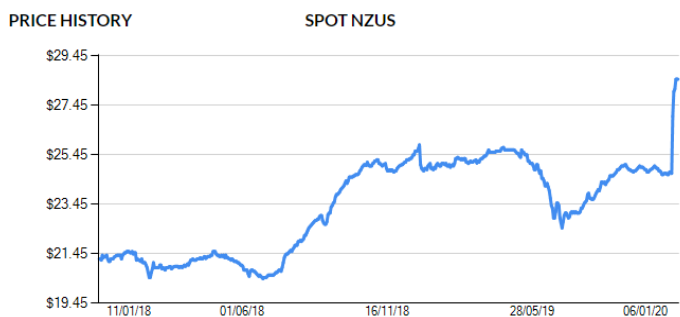
In November we saw the New Zealand parliament pass the Climate Change Response (Zero Carbon) Amendment Bill by virtually a unanimous vote. This was followed up in December with the government unexpectedly releasing its proposed changes to the New Zealand Emissions Trading Scheme (ETS) for consultation.

There is a second amendment bill currently progressing through the parliamentary process. The “Climate Change Response (Emissions Trading Reform) Amendment Bill” is designed to restructure the NZ Emission Trading Scheme to allow a cap to be put on the emissions permitted under the scheme and to reduce that cap in order to meet New Zealand’s climate change targets. The specific settings of the scheme are to be put in place via regulation and the government is seeking feedback on its proposed ETS settings which include:

- Raising the Fixed Price Option (FPO) from the current \$25.00 to \$35.00 for emissions produced in the 2020 calendar year;
- Introducing an auction process for emitters to buy NZUs starting in 2021;
- Having a \$20.00 floor price within the auctioning framework;
- Annual auction volume to be set at around 16 million tonnes for 2021 to 2025;
- Reducing the amount of NZUs it makes available via the auction process during 2021 to 2025 by 27 million tonnes (there is currently a stockpile of 132 million NZUs held in the NZ ETS accounts);
- Using a Cost Containment Reserve (CCR) within the auctioning process that would allow a release of additional NZUs onto the market if a pre-determined price is reached during an auction. The proposed “trigger” price for the CCR is \$50.00 per NZU between 2020 and 2025;
- Setting CCR volume available to the government at 90% of the difference between net emissions and industrial allocation and auctioning;

- Not permitting international units into the NZ ETS in the 2020 to 2025 period (unless the Climate Change Commission recommends otherwise).

The price of NZUs responded positively to the release of the ETS reform proposals. Having started the quarter at \$24.85, NZU’s jumped on the news and finished the December quarter at \$28.50.



Source: CommTrade

The movement in the underlying assets (currently NZUs and cash) saw the net tangible assets (NTA) of the Carbon Fund increase from \$0.9864 to \$1.0788 (+9.4%) during the December Quarter. The traded price of the Carbon Fund on the NZX went from \$1.02 to \$1.06.

The Carbon Fund was an active buyer of NZUs during the quarter, acquiring 11,000 tonnes of NZUs at an average price of \$25.82.

What does all this mean for the next quarter for NZUs?

So, what does this mean for carbon (NZU) pricing? The Government’s proposed ETS changes reflects its desired price range for NZUs for the next five years with a minimum of \$20 and a maximum of \$50 between 2020 and 2025 with an interim FPO of \$35 for emissions in the 2020.¹

With the government offering a \$35 FPO to emitters for their emissions over the 2020 year the market, some commentators are predicting that prices will start heading towards this upper bound.

Thank you for your interest in the Carbon Fund. We have been pleasantly surprised this quarter by the positive steps announced in the NZ ETS and look forward to bringing you more developments in the New Zealand and International carbon markets in the future.

¹ Ministry for the Environment: Reforming the New Zealand Emissions Trading Scheme: Consultation on Proposed Settings. 19 December 2019