



CarbonFund

Carbon Fund Fact Sheet – Quarter ending 30 September 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	\$1.96 million
Inception Date	8 November 2019
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 30 September 2019

Application	0.9864
-------------	--------

CO2 price on NZX Main Board at 30 September 2019

NZX Close	1.020
-----------	-------

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 30 September 2019

Carbon credits	94.40%
Cash	5.60%

Fund Performance to 30 September 2019

Period	Fund Return
1 month	-0.08%
3 months	4.67%
6 months	-2.58%
Since inception p.a.	-1.52%

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

SALT INVESTMENT FUNDS LIMITED

Level 3, The Imperial Buildings, 44 Queen Street | PO Box 106-587, Auckland 1143

P: +64 9 967 7276 | E: info@carbonfund.co.nz | www.carbonfund.co.nz

Quarterly Fund Commentary

Dear Fellow Investor,

The September quarter saw a solid rise in the price of carbon traded on the New Zealand Emissions Trading Scheme (NZ ETS), known as New Zealand Units (NZUs). Having started the quarter at \$22.90, NZU's steadily climbed back to \$24.85 to sit just under the government's Fixed Price Option (FPO) of \$25.00. The movement in the underlying assets (currently NZUs and cash) saw the net tangible assets (NTA) of the Carbon Fund increase from \$0.9424 to \$0.9864 during the September Quarter. The traded price of the Carbon Fund on the NZX went from trading at a discount to its NTA to a premium, bouncing from 92 cents to \$1.02 as investors became more bullish about the prospects of meaningful change in the NZ ETS.

The Carbon Fund was an active buyer of NZUs during the quarter, acquiring 15,300 tonnes of NZUs at an average price of \$23.93.

The quarter also saw the government release its decision on its improvements to the ETS. The most significant were:

- the phase out of free allocations of NZUs to "Emissions Intensive Traded Exposed" companies.
 - It's a slow phase out but it sends a strong signal.
 - As previously announced, in the future (maybe as early as late 2020) there will be an auctioning of NZUs. The auction process will include a "Cost Containment Reserve" whereby the government can flex the level of NZUs it makes available in the auction in order to reduce price volatility. Once this is in place it would make sense for the Fixed Price Option to be discontinued.
 - There is currently ongoing debate as to whether agriculture will be included in the ETS from 2021. This is despite the government's initial proposal of a 95% free allocation if this did occur meaning that there would be only around 2 million tonnes of NZUs required to be made good by the agriculture sector out of the 40 million tonnes of emissions that are linked to agriculture.
- the introduction of an averaging method for calculating how forest owners can claim carbon credits for growing trees.
 - This method is only applicable to forests planted from 2001 and only if these forests weren't already in the ETS. The result is that a significant amount of the NZUs held by owners of older

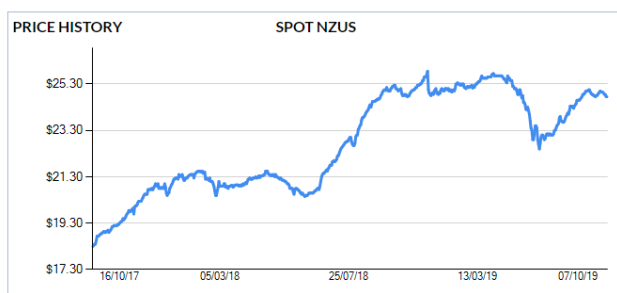
forests already in the ETS will need to be handed back when these forests are harvested. OMF estimates that "last year, harvesting (and some who exited the ETS) accounted for 1.5 million NZUs being handed back". The harvest profile increases dramatically over the next few years as the large forests planted in the 1990s mature and as these trees are cut down, the amount of NZUs required to be surrendered will increase, limiting the supply of NZUs.

The Zero Carbon (Climate Change Response Amendment) Bill is expected to be back in front of Parliament in late October for its second reading and Climate Change Minister James Shaw has been quoted as being confident he can get the Bill passed by the end of the year.

These changes are viewed as positive for carbon prices and a stronger carbon price will encourage more rapid transition to a low carbon economy.

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

The emissions accounting period runs from January to December so most emitters will have good estimates of what their final emissions for 2019 will be. The emitters have between now and the end of March 2020 to acquire the NZUs they will be required to submit to the government under the ETS. There is a view that many New Zealand corporates will not want to be seen as avoiding their climate change responsibilities by simply paying the "FPO fee". A desire to portray a positive corporate image could see these emitters purchase NZUs on the ETS.



Source: commtrade.co.nz

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