



CarbonFund

Carbon Fund Fact Sheet – Quarter ending 30 June 2020

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	\$6.1 million
Inception Date	8 November 2018
Portfolio Manager	Paul Harrison
Total Fund Charges (p.a.)	0.97%
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 on 30 June 2020

Application	1.1745
-------------	--------

CO2 price on NZX Main Board on 30 June 2020

NZX Close	1.17
-----------	------

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 June 2020

Carbon credits	97.80%
Cash	2.20%

Fund Performance to 30 June 2020

Period	Fund Return
1 month	19.17%
3 months	21.47%
6 months	23.31%
1 year	9.25%
Since inception p.a.	10.77%

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 2726 | E: info@carbonfund.co.nz | www.carbonfund.co.nz

Quarterly Fund Commentary

Dear Fellow Investor,

The June quarter saw the Climate Change Response (Emissions Trading Reform) Amendment Bill (now Act) passed into law and we have a clear path forward for the NZ ETS.

The ETS reform includes several necessary changes to limit the total emissions allowed within the ETS per year and align the ETS framework and processes with the targets set in the Zero Carbon Bill, which passed last year.

With the reformed ETS comes a move to a proper Cap & Trade Scheme from 2021, which means annual NZ emissions are capped, and that cap will decrease over time to meet the Paris goals and onwards to a net zero target in 2050. Aptly said by OMF, an NZ carbon credit broker, "The old ETS was a jalopy, the new ETS is a Merc".

Key elements of the amended ETS:

The Fixed Price Option is \$35 for this emission year, 2020 and then lifted for the following 2021 emissions year, on the basis that auctioning starts in 2021.

- The first auction is scheduled to occur in March 2021 and will be open to 2020 and 2021 emitters.
- Price controls are set for auctions with a \$20 floor and \$50 cost containment reserve (CCR) trigger and adjusted for inflation over time.
- The CCR is an allocation of 7 million tonnes in year one that the government can sell should the auction price hit \$50/tonne. If the CCR is exhausted in year one, the government can change both the amount and price in year two.
- A provisional emissions budget for the 2021 – 2025 period has been determined, reflecting 90 million tonnes of CO2 equivalent greenhouse gases for the five years.
- The Climate Change Commission will provide the first three emission budgets by the end of July 2021, which may include a revised budget for the 2021-25 period.

The approval of the ETS Reform brought price volatility in the NZU market with new buyers entering the market at the same time as emitters completed returns and subsequent surrenders. The NZU price climbed 22.5% from \$26.20 at the start of the quarter to \$32.10 by the end. The quarter closed 46% higher than the March low of \$22.



The movement in the underlying assets (currently NZUs and cash) saw the net tangible assets (NTA) of the Carbon Fund increase from \$0.96 to \$1.18 (+22%) during the June quarter. The traded price of the Carbon Fund on the NZX went from \$0.95 to \$1.17.

The Carbon Fund was an active buyer of NZUs during the quarter, purchasing 3,000 tonnes of NZUs at an average price of \$28.00.

The COVID-19 pandemic continues to disrupt and inflict pain throughout the world. Governments are identifying and investing in opportunities to stimulate their economies by pumping trillions of dollars into different sectors to protect jobs and GDP. Global carbon markets have rebounded from the COVID-19 lows observed in March back to basically the same price it was trading at this time last year, €28.96 (as at 10th July 2020).

The outlook for NZUs

The Fixed Price Option is now \$35 and is available for participants to use from the start of 2020 and overlap with the start of auctioning to cover emissions in 2020. Therefore, market commentators expect continued volatility of the NZU price during the transition to the new Cap & Trade Scheme but for the \$35 FPO to have a strong influence over the price until the FPO is lifted and the cost containment reserve kicks in.

The Government has said the first auction is planned for 2021 but should it be pushed out past 2021, so would the \$35 FPO application. In September, we should get clarity around auction timing when the Ministry is expected to publish an auction calendar for the upcoming year, including the volume of NZUs available to be sold at each auction.



Paul Harrison, BCA, MBA, CA