Salt NZ Dividend Appreciation Fund Fact Sheet – March 2020

Manager Profile

Salt Funds Management is a boutique investment management firm wholly owned by its employees which specialises in managing NZ/Australian equity and listed property mandates for wholesale and retail clients.

Investment Strategy

The Salt NZ Dividend Appreciation Fund targets a portfolio of shares of New Zealand companies that may, in our opinion, pay high and sustainable dividends. A considerable body of robust research suggests that stocks with strong and sustained dividend policies tend to generate higher free cash flow than average and outperform their index benchmarks over time. The strategy is not intended to naively generate the highest possible yield but rather to generate a high and sustainable dividend yield.

Fund Facts at 31 March 2020

Benchmark	S&P/NZX 50 Gross Index
Fund Assets	$78.52 million
Inception Date	30 June 2015
Portfolio Manager	Matthew Goodson, CFA

Unit Price at 31 March 2020

Application	1.416
Redemption	1.4103

Investment Guidelines

The guidelines for the NZ Dividend Appreciation Fund are shown below:

NZ shares	95% – 100%
Cash	0% – 5%
Unlisted securities	0% – 5%
Maximum active position	8%

Target investment Mix

The target investment mix for the Salt Dividend Appreciation Fund is:

Australasian Equities	100%

Fund Allocation at 31 March 2020

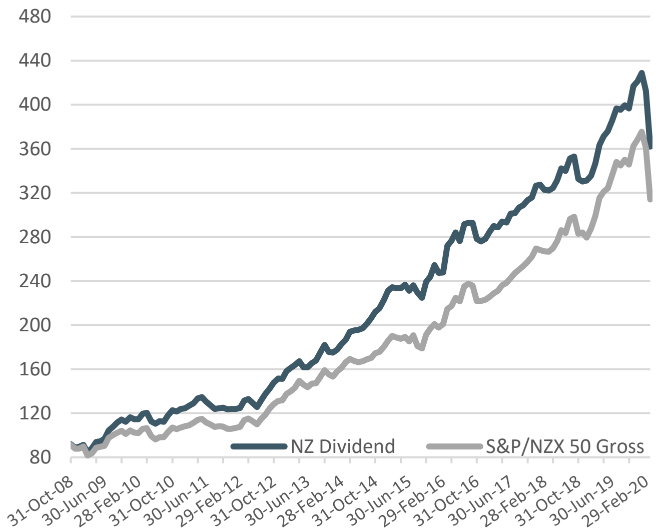
NZ shares	96.60%
Cash	3.40%

Fund Performance to 31 March 2020

Period	Fund Return*	Benchmark Return
1 month	-12.26%	-13.00%
3 months	-14.12%	-14.75%
6 months	-9.41%	-10.33%
1 year	-0.50%	-0.49%
2-year p.a.	5.96%	8.52%
3 years p.a.	7.80%	10.83%
5 years p.a.	9.16%	10.92%
7 years p.a.	12.00%	12.03%
10 years p.a.	11.72%	11.61%
Inception p.a.	11.83%	10.56%

Performance is after all fees and does not include imputation credits or PIE tax.
*From 1 November 2008 to 30 June 2015, performance is from a fund with the same strategy and the same portfolio manager.

Cumulative Fund Performance to 31 March 2020*



Fund performance has been rebased to 100 from inception.
Past performance is not a reliable indicator of future performance and no representation or warranty, express or implied, is made regarding future performance.

Top Overweights	Top Underweights
Tower	Fisher & Paykel Healthcare
Turners Automotive	Ryman Healthcare
Scales Corporation	Auckland International Airport
Investore Property	Ports of Tauranga
Marsden Maritime Holdings	Goodman Property Trust

SALT FUNDS MANAGEMENT
Level 3, The Imperial Buildings, 44 Queen Street | PO Box 106-587, Auckland 1143
P: +64 9 967 7276 | E: info@saltfunds.co.nz | www.saltfunds.co.nz

NZ Market Commentary

Stocks around the world were aggressively sold off over March for the third consecutive month as confirmed Covid-19 cases surged past 800,000 and deaths surpassed 40,000. To highlight the speed at which this is unfolding, in the six days post quarter-end, there have been more than 400,000 new cases and 26,000 deaths globally. The MSCI All World Accumulation Index fell -13% in March to end the quarter down -21%.

As governments around the world have implemented measures to “flatten the curve” from light touch to full lockdowns they have created enormous uncertainty as huge swathes of the global economy have been virtually switched off. Huge fiscal stimulus plans were laid out in the form of wage subsidies to protect jobs and loan guarantees and are continuously being updated and upscaled by affected countries. Central Banks stepped up in quick succession cutting rates if they could and promising new rounds of QE and financial system support. Economists slashed growth forecasts, predicting widespread pain and high unemployment for at least the next 2 quarters. A key question for investors is the degree to which this temporary shock has a permanent effect.

US 10-year yields fell to record lows of a mere 0.66%. Oil fell off a cliff as demand collapsed and storage facilities filled to the point that oil fell to negative prices in some locations globally. Gold rose during a volatile quarter as liquidation of all assets did battle with those seeking a safe haven and protection against the debasement of fiat currencies.

The S&P500 marked its fastest ever 20% fall and circuit breakers limiting falls of >7% were triggered twice. The index declined -12.4% in March and -19.6% for the quarter. On some days the market rallied on stimulus hopes only to fade on an acceleration in Covid19 case numbers. Immediately post quarter-end, the market has bounced somewhat as cases show clear signs of peaking but the economic fallout will be the next question to be wrestled with.

European markets were hard hit given unsuccessful Covid-19 containment, with London’s FTSE -24%, Germany’s DAX30 -25% and France’s CAC40 -26% for the quarter. Asian bourses were a tad less affected with Hong Kong’s Hang Seng -16% and Japan’s Nikkei -20%.

The Australian market saw its worst six days in 40 years and worst month since 1987 with the S&P/ASX200 falling -20.7% in March and -23.1% for the quarter. Intra-day volatility was extreme with a 13% move registered on one day. The traditional defensive hiding place in REITS were crushed, down 35% in March alone. The Energy sector was worst hit down 49% over the quarter. The only sector that was up over the quarter was Health Care +1.5%.

NZ’s S&P/NZX50 Gross Index did relatively well by falling only 13% in March to end the quarter down 14.8%. The best performer was Fisher & Paykel Healthcare (FPH +37%) which will enjoy a modest increase in ventilator sales, a2 Milk (ATM +14%) on a strong result and Chorus (CNU +14%) on a sound guidance and capex update. The biggest declines have a common theme of high costs and almost no revenue for some time and possibly requiring fresh equity capital, being Air New Zealand (AIR -71%), Tourism Holdings (THL -68%) and Vista (VGL -68%).

Salt NZ Dividend Fund Commentary

Despite falling sharply in line with markets globally, the Fund outperformed its benchmark in the March quarter, declining by -14.12% compared to the -14.75% for the S&P/NZX50 Gross Index. This was perhaps a touch disappointing given the nature of the Fund but it reflects the unusual extreme outperformance of the two low/non-yielding large caps Fisher & Paykel Healthcare (FPH, +36.8%) on a marginal guidance upgrade and positive Covid-19 exposure and a2 Milk (ATM, +14.4%) on a solid result.

There was a quite staggering dispersion between the S&P/NZX Large Cap Gross performance of -7.7% and that of the Mid Cap Gross which fell by a sharp -24.8%. Using forward PE estimates sourced from Jarden, we now estimate that the market as a whole is on a one year forward PE of 32.5x versus the median PE of just 14.5x. Given this extreme dispersion, we had already been drawn somewhat to a number of clear opportunities in the mid cap space and see this setting the stage for strong future returns as the economy first bottoms and begins to eventually turn up again.

Contributors

In a quarter that saw remarkable returns dispersion, the largest tailwinds unsurprisingly came from underweights in some of the expensive underperformers. These included two of the companies that are most directly impacted by Covid-19 in the form of Air NZ (AIR, -71%) and Auckland International Airport (AIA, -43%). Post quarter-end, the Fund neutralised its position in the latter at levels that will prove attractive on a through-the-cycle basis. We remain wary of equity-holders in Air NZ being sharply diluted. Other notable positive contributors were underweights in Ryman Healthcare (RYM, -36.9%), Port of Tauranga (POT, -22.7%), Heartland Bank (HGH, -42.8%) and Fletcher Building (FBU, -31.5%).

Detractors

Our key headwinds came mainly from our larger overweights that are exposed to the economic shutdown in response to Covid-19. Turners (TRA, -41.5%) led the way here. Frustratingly, they had been trading strongly prior to the enforced shutdown. The business will clearly recover and we expect their expansion of market share in the NZ used car industry to dramatically increase post-shutdown but we first have to get through the lost sales and the potential for bad debts in their loan book.

Other headwinds came from being underweight the aforementioned Fisher & Paykel Healthcare (FPH, +36.8%) which is now on a staggering forward PE of 58x for earnings that have a one-off element to them from Covid-19. A modest overweight in NZ Refining (NZR, -58.5%) ran into a Covid-induced collapse in refining margins rather than the sharp bounce we had expected from new fuel oil regulations. A final key low light was a modest overweight in Kiwi Property (KPG, -39.7%) which we had established on clear relative value grounds but instead ran headlong into the heaviest exposure of the property names to the shutdown.

Portfolio Positioning

The Fund’s largest overweight at quarter-end was in Tower Limited (TWR) which underperformed slightly in the quarter despite having strong defensive attributes. It will be hurt slightly by lower interest rates and short-term hardship relief on some insurance premia but we expect this to be more than offset by a collapse in claims costs as cars aren’t being crashed and homes aren’t being burgled. It will shortly begin paying a sizeable sustainable dividend with years of growth to come. Turners, Spark, Scales, Marsden Maritime and Contact Energy are other overweights of note. Underweights are led by Ryman Healthcare. We have re-established an underweight in the overall retirement sector as the critically important outlook for house sales and prices appears very difficult indeed in a post-Covid world.