SALT
Funds Management

Salt NZ Dividend Appreciation Fund Fact Sheet – March 2018

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.

Benchmark

S&P/NZX 50 Gross Index

Fund Assets at 31 March 2018

$57.0 million

Strategy Assets at 31 March 2018

$136.6 million

Includes all Funds and separately managed accounts that employ the same investment strategy as the Salt NZ Dividend Appreciation Fund.

Inception Date

30 June 2015

Portfolio Manager

Matthew Goodson, CFA

Unit Price at 31 March 2018

Application	1.3510
Redemption	1.3455

Investment Guidelines

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

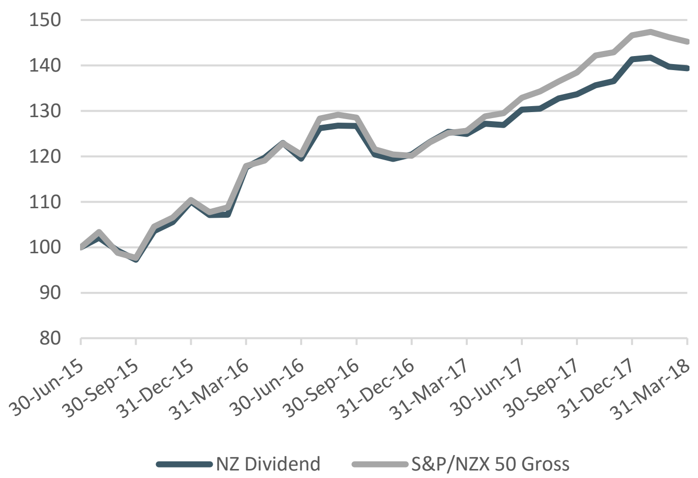
NZ shares	95% – 100%
Cash	0% – 5%
Unlisted securities	0% – 5%
Maximum active position	8%

Fund Performance to 31 March 2018

Period	Fund Return	Benchmark Return
1 month	-0.24%	-0.65%
3 months	-1.38%	-0.94%
6 months	4.26%	4.90%
1 year	11.58%	15.59%
2 year p.a.	8.85%	11.00%
Inception p.a.	12.83%	14.54%

Performance is after all fees and does not include imputation credits or PIE tax.

Cumulative Fund Performance to 31 March 2018



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.

Fund Allocation at 31 March 2018

NZ shares	98.68%
Cash	1.32%

Top Overweights	Top Underweights
Turners Automotive Group	Ryman Healthcare
Tower	Mainfreight
Investore Property	Fisher & Paykel Healthcare
Scales Corporation	Trade Me
Metlifecare	Infratil

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Quarterly Equity Market Commentary

In a marked change to the low volatility and the exponential price path observed into the end of 2017, the MSCI Global Accumulation Index was down -2.2% in March which dragged the performance into negative territory for the quarter (-1.3%). The two largest shocks over the quarter were strong employment and inflation data in the US, stoking fears of higher interest rates, and a brewing trade-war between the US and China which heated up in March.

The S&P 500 finished the quarter down only -1.3%, yet this was 8% below the high achieved in January. The technology heavy Nasdaq ended the quarter up 2.3% but this was also 8% below its mid-March high. Volatility as measured by the CBOE Volatility Index ("VIX") which tracks the annualised volatility of the S&P 500, rose to 22.87 by the end of the quarter from 10.03 at the end of 2017.

Robust employment and inflation data coupled with increased fiscal stimulus requiring more issuance of Treasuries pushed the US 10-year Treasury bond yield up to an intra-quarter high of 2.95% before ending the quarter down slightly lower at 2.74%, +0.33% from the end of 2017.

Over the March quarter, the key Asian markets mostly saw negative returns with Japan's Nikkei 225 -5.6%, Shanghai Composite -4.2% whilst Hong Kong's Hang Seng bucked the trend ending the quarter near flat at +0.6%. European markets were similarly weak with Germany's DAX at -6.3%, France CAC fall of -2.7% and the UK's FTSE down a staggering -8.2% for the quarter.

In Australia the S&P/ASX 200 Accumulation Index had a weak quarter down -3.9% largely driven by a -3.8% return in March. The largest negative contributor was the Financials sector, impacted primarily by the Royal Commission in addition to a slowing housing market and higher interest rate expectations.

The New Zealand equity market had a mildly negative quarter after a strong 2017, returning -0.9%, largely driven by a +54% increase in a2 Milk. Excluding a2 Milk, the market was far more in line with its global peers, being down -4.75% over the quarter.

Quarterly Fund Commentary

The Fund slightly lagged the tepid market over the March quarter, declining by -1.38% after all fees and expenses compared to the -0.94% recorded by the Index.

A major headwind came from the moderate underweight in a2 Milk (ATM, +53.7%) which recorded a stunning ascent following a relatively strong result and a supply deal with Fonterra which saw significant further future growth potential priced into it. This non-dividend paying name has been a real conundrum for the Fund, but it now clearly generates sizeable free cashflow and is considering the payment of a dividend in future. The valuation implies exceptional continued growth for a number of years off what is now a very high base and some evidence of imitators such as Nestle beginning to enter.

Other headwinds came from overweights in Evolve Education (EVO, -34.2%) and Turners (TRA, -7.4%). The EVO decline was driven by a disappointing profit warning which highlighted the operating leverage in their model, where a relatively small decline in child occupancy had a magnified impact on profits thanks to the relatively fixed costs of property rentals and teachers. EVO is now on very low multiples of downgraded earnings and cash-flow, but it is well and truly in the dog-box until stability can be demonstrated. The Turners decline was puzzling as we understand the business continues to trade well but we can only put it down to the continued overhang from a small but poorly managed equity raising last year.

The largest positive by some distance was our Tower (TWR, +20.0%) overweight, which rose sharply on the sale of Suncorp's stake to Bain Capital for $0.80/share. Notably, Bain's SSH notice outlined provisions to make a top-up payment should they choose to initiate a takeover offer within 9 months. In any case, although TWR's share price rose from $0.68 to $0.81, our valuation remains well north of this. NZ home and motor insurance premia have entered a hard cycle, TWR is performing well operationally and is winning share, it is now well capitalised post its rights issue, the dispute with Peak Re has been settled, Christchurch over-cap claims appear to have slowed sharply and the new Government is highly motivated to bring the Christchurch imbroglio to an end.

Other tailwinds came from a series of underweight positions in names that lagged over the period. These included Heartland Bank (HBL, -13.1%) whose result showed a tick up in bad debts and whose multiples remain high versus Australian peers; Infratil (IFT, -6.6%); Sky TV (SKT, -14.8%) whose result showed large subscriber losses and the share price decline saw it fall out of several global ETF's; Fisher & Paykel Healthcare (FPH, -8.0%) which normalised post a major index inclusion; and Fletcher Building (FBU, -20.7%) which had déjà vu all over again with construction sector issues.

Cash levels fell from 3.0% to 1.3% as temporary bouts of weakness were used to lift several holdings. These included a2 Milk, Contact Energy, Z Energy and a tiny new holding in Trustpower. We exited a small rump holding in Trade Me and lowered Fisher & Paykel Healthcare, Restaurant Brands and Sky Network TV.