SALT
Funds Management

# Salt Enhanced Property Fund Fact Sheet – September 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 Enhanced Property Fund targets a portfolio of shares of New Zealand and Australian property trusts, companies and other property related securities with exposure to commercial, residential, retail, tourism, industrial, medical, educational, rural, retirement, and other property sectors. The Fund may also, at our discretion, short sell securities, hold cash, lever its assets and utilise active currency management to generate returns.

## Fund Facts at 30 September 2018

| | |
|---|---|
| Benchmark | S&P/NZX All Real Estate Gross Index |
| Fund Assets | $6.3 million |
| Inception Date | 11 November 2014 |
| Portfolio Manager | Matthew Goodson, CFA |
| Associate PM/Analyst | Andrew Bolland, CFA |

## Unit Price at 30 September 2018

| | |
|---|---|
| Application | 1.4840 |
| Redemption | 1.4779 |

## Investment Limits

The limits for the Enhanced Property Fund are shown below:

| | |
|---|---|
| Gross Equity Exposure[1] | 70% – 200% |
| Net Equity Exposure[1] | 70% – 100% |
| Unlisted securities[1] | 0% – 5% |
| Cash or cash equivalents | 0% – 30% |

[1]To NZ and Australian property and property related securities.

## Fund Exposures at 30 September 2018

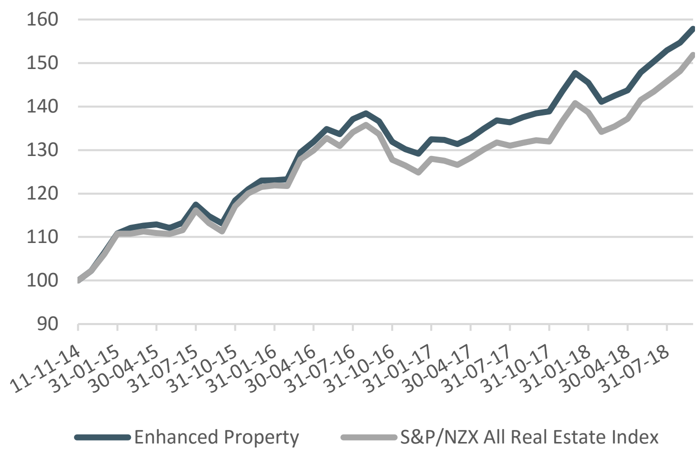
| | |
|---|---|
| Long Exposure | 101.97% |
| Short Exposure | 9.00% |
| Gross Equity Exposure | 110.97% |
| Net Equity Exposure | 92.97% |

## Fund Performance to 30 September 2018

| Period | Fund Return | Benchmark Return |
|---|---|---|
| 1 month | 2.05% | 2.50% |
| 3 months | 5.02% | 5.86% |
| 6 months | 10.80% | 12.16% |
| 1 year p.a. | 14.04% | 14.82% |
| 2 years p.a. | 7.50% | 6.60% |
| 3 years p.a. | 11.75% | 10.91% |
| Inception p.a. | 12.49% | 11.36% |

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

## Cumulative Fund Performance to 30 September 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 30 September 2018

| | |
|---|---|
| NZ Listed Property Shares | 86.75% |
| AU Listed Property Shares | 6.48% |
| Cash | 6.77% |

| Top Overweights | Top Underweights/Shorts |
|---|---|
| Centuria Metropolitan REIT | Property for Industry |
| Investore Property | Goodman Property Trust |
| Unibail-Rodamco-Westfield/CDI | Precinct Properties |
| Asset Plus | Kiwi Property Group |
| Garda Diversified Property Fund | Argosy Property Trust |

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## Quarterly Property Market Commentary

### *Summary*

- The Fund advanced by +5.02% after all fees and expenses for the quarter.
- The NZD weakened and interest rates fell following dovish commentary by the RBNZ Governor, Adrian Orr.
- The Fund had strong long stock selection in the Australian market, with those positions contributing +0.39%, and sharply outperforming their index.

The S&P/NZX All Real Estate Gross Index posted a second quarter in a row of stellar performance in September, rising by +5.86% following its +5.95% advance in June. Despite something of a selloff in global bond yields late in the quarter, the domestic backdrop was supportive, with the NZ 10-year yield rallying from 2.85% to 2.65%. Surprisingly dovish commentary by new RBNZ Governor, Adrian Orr saw the NZD weaken and interest rates fall right across the yield curve. The quest to find yield remains very supportive of the sector. In stark contrast to domestic strength, the global FTSE EPRA/NAREIT index fell by -0.52%, with less supportive bond yields, shopping centre travails and emerging market weakness all weighing. The Australian REIT Index rose by a middling +1.86%.

August result season saw generally solid outcomes. Property For Industry (PFI) had a slightly better than expected H1 result but full year guidance was unchanged as they grapple with vacancy at their Carlaw Park asset. Revaluations ex-Carlaw Park were +8.3% as investors are currently paying extremely tight cap rates for industrial assets.

Precinct (PCT) reported a further six-month delay at Commercial Bay but did make leasing progress taking the office occupancy up from 66% to 78% and the retail from 46% to 76%. Their decision to devote two floors of such a prime asset to office suites was interesting given their bullish market outlook. Market rents implied from PCT's valuation cap rates also appeared relatively flat. PCT committed to a NZ$298m redevelopment of the HSBC Tower into a smaller amount of office and a large Intercontinental Hotel.

Vital Healthcare's (VHP) solid result showed no impact from the currently weak conditions in the Australian hospital sector. VHP provided details of how it will share the costs of the 10% stake held in Healthscope (HSO) together with its manager, North-West. This could prove problematic given that HSO announced that they will seek a co-investor into a new unlisted trust that they will retain majority ownership of. Investore (IPL) announced a buyback of up to 5% of its issued equity and highlighted the discount at which it trades to its $1.64 NTA. The transactional highlight was the purchase by Goodman Property of the Foodstuffs Distribution Centre in Mt Roskill for $93m at a passing yield of around 5%.

Outperformance was shared amongst three stand-outs, Stride Property (SPG, +8.1%), Goodman Property (GMT, +8.1%) and Precinct Properties (PCT, +7.9%). Underperformers were Augusta (AUG, +3.2%) and Kiwi Property (KPG, +3.3%).

## Quarterly Fund Commentary

The Fund slightly lagged the surge in the benchmark in the quarter, advancing by +5.02% after all fees and expenses compared to the +5.86% returned by the Index.

### *Contributors*

The Fund had strong long stock selection in the Australian market, with those positions contributing +0.39%, and sharply outperforming their index. Our large long-held position in Centuria Metropolitan REIT (CMA, +3.8%) did well again and it remains attractive on our relative valuation modelling. The late-cycle nature of its suburban office assets and some very loosely-sourced press speculation that it may be a takeover target aided its performance. Similarly, our long-held position in Garda Property (GDF, +6.7%) continued to outperform as its highly capable management team are adding value by developing in markets where it is cheaper to build than buy.

In NZ, the stand-out was a long-held position in Millennium & Copthorne Hotels preference shares (MCKPA, +8.4%). There was no new news during the period but a strong interim result in early August saw their NTA per share rise to $4.35 versus the closing share price of $3.36.

### *Detractors*

The key culprits for lagging the benchmark were our underweights in the booming industrial sector, in the form of Goodman Property (GMT, +8.1%) and Property For Industry (PFI, +4.8%). There is little doubt that the NZ industrial property segment is red-hot at present, with cap rates having contracted sharply on rampant investor demand. However, at a time when business confidence has fallen sharply, the historic cyclicality of industrial property coupled with each property's lack of unique characteristics appear to have been forgotten.

Unsurprisingly, in a moderately positive quarter for Australia, our shorts in that market delivered a slightly negative contribution of -0.16%. Our main problem was Goodman Group (GMG, +6.4%) which rallied hard following a result that we thought was mixed. GMG appears to be viewed by many investors as being a dependable "machine" which reliably churns out 7% EPS growth. While we are attracted to GMG's low gearing, the market overlooks the pro forma nature of their numbers which benefit from utilising sizeable debt restructuring savings (with the costs taken below the line) and the highly material employee share costs of $126m are not expensed. GMG retains a strong future pipeline of performance fees and its FuM has grown strongly thanks to contracting cap rates but paying a 21x PE multiple for top-of-cycle metrics strikes us as being well over-extended.

Our gross position of 111% was little changed over the quarter, while the net exposure fell slightly from 95.5% to 93% as we lightened some very fully priced NZ names. Argosy Property and Kiwi Property stood out here, while we used short-lived pullbacks to cover a little of our Goodman Property and Vital Healthcare Property underweights. We opportunistically used a sell-down to purchase a small holding in the retirement village operator, Oceania Healthcare. There were a bevy of moderate changes in our Australian holdings, with the standouts being selling a little of our very large Centuria Metropolitan REIT position into strength; using strength to put new shorts on Dexus and Mirvac; using a brief pullback to halve the Goodman Group short; and adding a new long in Unibail Rodmaco-Westfield, which is extraordinarily cheap on our relative valuation modelling.