SALT

Salt Long Short Fund Fact Sheet – December 2024

Manager Profile

Salt Funds Management is a boutique investment management firm wholly owned by its employees which specialises in actively seeking to maximise returns while managing the risks of the investment.

Investment Strategy

The Fund aims to deliver positive absolute returns in all market environments. In addition to holding "long-only" NZ and Australian securities, the Fund may, at our discretion, short sell shares, hold cash, lever its assets and utilise active currency management to generate returns (although generally the Fund's assets will be fully hedged).

Fund Facts at 31 December 2024

Benchmark	RBNZ Official Cash Rate +5% p.a.
Fund Assets	$102 million
Inception Date	31 July 2014
Portfolio Manager	Matthew Goodson, CFA

Unit Price at 31 December 2024

Application	2.9191
Redemption	2.9074

Investment Limits

Gross equity exposure	0% - 400%
Net equity exposure	-30% - 60%
Unlisted securities	0% - 5%
Cash or cash equivalents	0% - 100%
Maximum position size	15%

Number of Positions at 31 December 2024

Long positions	51
Short positions	28

Exposures at 31 December 2024

Long exposure	87.73%
Short exposure	41.43%
Gross equity exposure	129.17%
Net equity exposure	46.30%

Investment Risk to 31 December 2024

Fund volatility[1]	6.55%
NZ50G / ASX200AI volatility[1]	13.41%
NZ50G / ASX200AI correlation	0.048

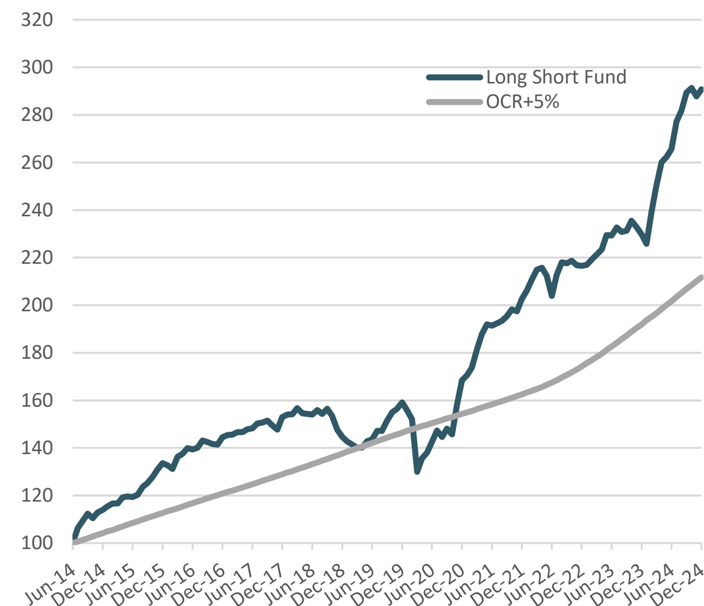
1. Annualised standard deviation since fund inception.

Fund Performance[2] to 31 December 2024

Period	Fund Return	OCR+5% Return	NZ50G/ASX 200AI Return[3]
1 month	1.04%	0.78%	-1.41%
3 months	0.46%	2.33%	2.28%
6 months	9.48%	4.98%	9.36%
1-year p.a.	26.56%	10.28%	11.41%
2 years p.a.	15.87%	10.19%	9.17%
3 years p.a.	12.79%	9.19%	3.61%
5 years p.a.	12.82%	7.64%	6.07%
7 years p.a.	9.60%	7.33%	7.64%
10 years p.a.	9.82%	7.34%	8.85%
Inception p.a.	10.70%	7.40%	8.96%

2. Fund performance is after all fees and before PIE tax.
3. NZ50G/ASX200AI is a 50/50 blend of the S&P/NZ50 Gross Index and the S&P/ASX 200 Accumulation Index and is for comparison purposes only.

Cumulative Fund Performance to 31 December 2024

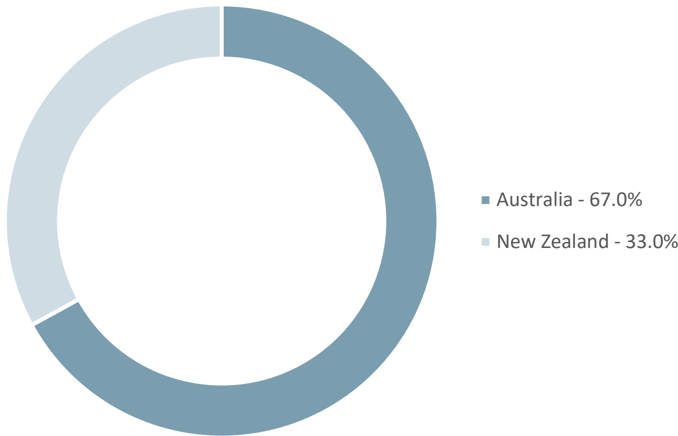


Fund performance has been rebased to 100 from inception.
Past performance is not a reliable indicator of future performance and no representation or warranty, express or implied, is made regarding future performance.

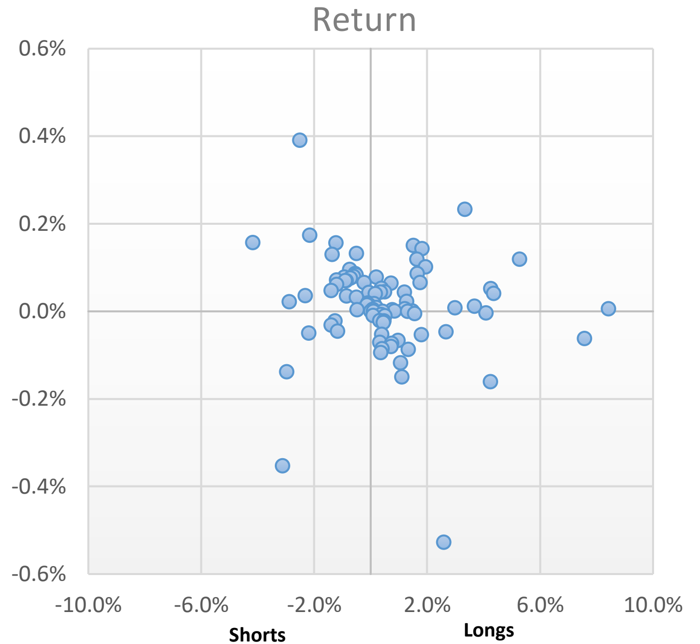
Largest Longs	Largest Shorts
Tower	Commonwealth Bank of Australia
GDI Property Group	Breville Group
Turners Automotive Group	Auckland International Airport
Servcorp	Wesfarmers
Challenger Limited	Reece

SALT FUNDS MANAGEMENT
Level 3, The Imperial Buildings, 44 Queen Street | PO Box 106-587, Auckland 1143
Email: info@saltfunds.co.nz | www.saltfunds.co.nz

Country Allocation at 31 December 2024 (Gross Equity Exposure)



December 2024 Individual Stock Contribution



Fund Commentary

Dear Fellow Investor,

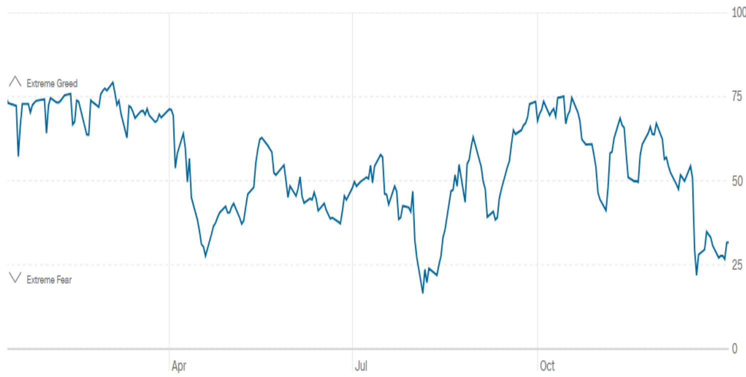
December was a solid month for the Fund, with a return after all fees and tax of +1.04%. While far from stellar, this provided a pleasing alternative to the returns of +0.3% from NZ equities and a sharp -3.2% retracement from the rather bubbly Australian market, which gave back most of its November advance.

Our crystal ball for 2025 is hazy at best. To quote a former English PM, Harold McMillan, the greatest challenge that lies ahead is, "events, dear boy, events." We suspect that the key for 2025 will be understanding and responding to events quickly.

While just about every Wall St firm has the obligatory +10%-15% outlook for 2025, we would be inclined to take that and run. Many global equity markets are expensive, investors are all-in, there is a classic narrative around AI to justify aspects of the fervour, inflation risks are proving somewhat persistent, bond yields are going the wrong way, China is battling a deflationary sinkhole and then we have dear old President Trump.

The easier calls are relative ones. NZ is 6-12 months ahead of Australia in the monetary easing cycle, business confidence is rebounding and we have reasonable spare capacity to sustain at least a moderate return to economic and earnings growth. Our market composition also has markedly less expensive technology and banks exposure than Australia and it is hard to enthuse about resources (ex gold and uranium) given the state of China. After 3 years of lagging the West Island, we would be inclined to back NZ in 2025. Further, it seems to be the case across almost all markets that large cap equities are historically expensive relative to their smaller peers. Perhaps this continues due to the fell hand of passive funds but valuations have a funny way of winning in the end.

The CNN Fear & Greed Index fell into "fear" territory in the back half of December, with the "Magnificent 7" rising by a mere +5.2% in the month but they did finish -7% below their intra-month highs. We tend to interpret this "fear" in the second derivative – investors are long and maybe just starting to be a little concerned about that.

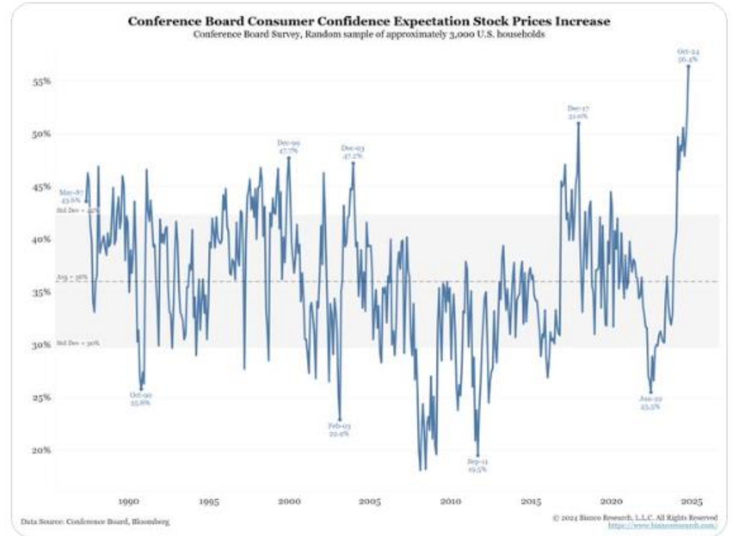


Signs abound that large market components are in a speculative fervour. In the past, we have argued that the price of bitcoin is a useful proxy for the amorphous concept of “liquidity”, and it has boomed, rising by +113% in the 2024 year and by +47% in the December quarter alone. Worse, this is the price in US$, a currency which has soared against most others.

However, we did see an interesting contrarian indicator in mid-December, with the 160 year-old AMP Australia announcing they had invested A$27m in bitcoin. The intersection of the bitcoin price with that of the $77bn market cap Microstrategy, which keeps raising at a NTA premium to buy more bitcoin, would gladden the heart of a deceased US/Italian gentleman whose surname begins with P.

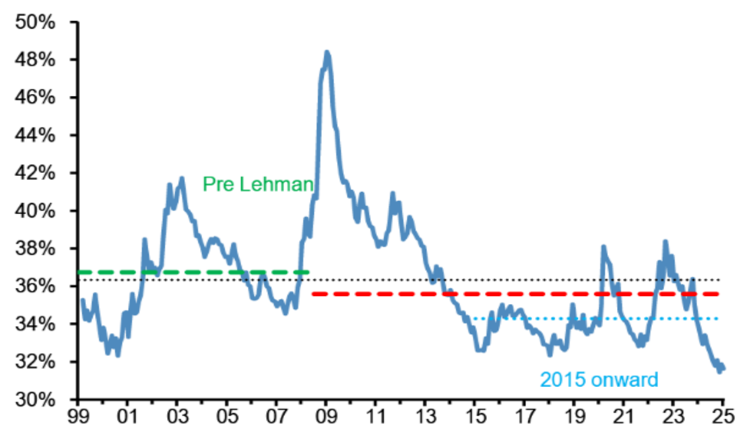
Even worse, it doesn’t take a sniffer-dog to detect a malodorous air, when as shown below, the price of Fartcoin has ripped from $0.02 to $1.25 since October. It now has a $1.25bn market cap. No wonder the Fed is beginning to resile from its easing stance.

This rampant speculation appears highly correlated with retail activity in the equity market. US households’ confidence at end-October that share prices will increase now surpasses all previous highs. Funnily enough, they have been right so far but this has been a great contrarian indicator.

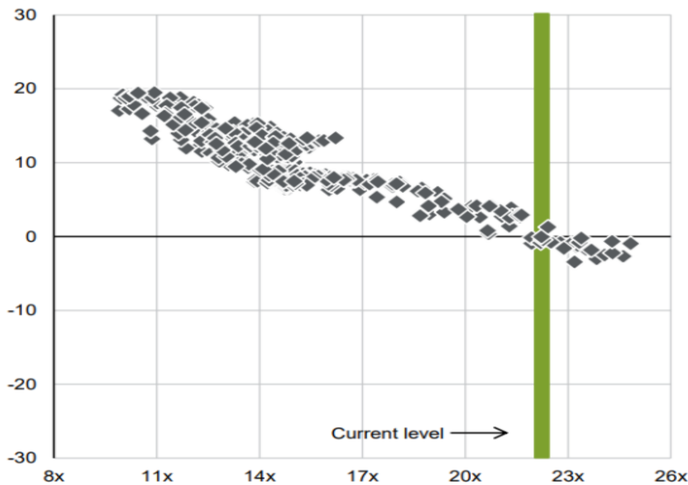


Rather than following the herd, we would be inclined to follow Warren Buffett, who we highlighted last month as having moved to a record proportion of cash. Similarly, company insiders have been selling hand over fist in both the US and in a number of Australian stocks.

Finally here, the chart below from JP Morgan suggests that the broader investor universe has also jumped on board the momentum train. Cash is at its lowest level in decades and this is at a time when cash interest rates are at above-average levels. We don’t know when this will change, or what will spark it, but markets are certainly vulnerable to “events, dear boy, events.”



With investors being all-in on equities, it should be no surprise that valuations are very extended. A WSJ article mid-month cited several investment banks in arguing that the CAPE (cyclically adjusted PE) is at its third highest level ever. Last month, we showed that the CAPE for the Australian market is at its third highest point since 1924 and that NZ’s overall PE (albeit not median PE) is also very extended. Does this matter?



The chart above shows that despite valuation having almost no predictive power on a one-year view, it means almost everything over a longer time period. It uses IBES earnings estimates for the S&P500, with the forward PE of around 22x being consistent with near-zero returns over the next ten years.

Bulls will argue that it's different this time due to the impact of Artificial Intelligence and technology more broadly. Maybe, but the extreme capital intensity of data centre investments feels a lot more akin to previous historical booms in the likes of railroads and automobiles. Many firms will no doubt eventually make money but trying to identify just who is very difficult in advance and many early players fall by the wayside. There is also little proof that AI investments are yet driving any spillovers into a measurable economy-wide upswing in productivity growth. We do wonder if 2025 will see a wake-up call when investors start saying show me the returns.

Since the Fed pivoted to an easing bias in September, the US 10-year bond yield has surged from around 3.7% to 4.6%. The bond market is sending a very clear message about the risks of stubborn inflationary pressures, which still sit above 3%. These pressures will likely be exacerbated by the polices of President Trump, with deregulatory benefits likely paling in significance relative to the impact of tax cuts, an even larger deficit, tariff driven inflation and more stringent immigration policies driving higher wage inflation.

The Fed has noticed this and their 25bp rate cut in December was pitched as hawkishly as it could be, with their dot plot changing to project two rather than four rate cuts in 2025. This was enough for the rampant US equity market to finally take some notice of the concerns that had been projected by the bond market for months, with a weak end to December.

While January has so far seen a return to the former bubbly optimism, its longevity may be brief if the bond vigilantes are correct.

Another key risk in 2025 comes from the increasing possibility of a debt-deflation trap in China, which is the exact opposite of US over-heating concerns. The Chinese 10-year bond yield fell from 2.5% to 1.6% over the course of 2024. This is a very different trajectory to US yields and one would think that the yuan may come under more pressure given that it is pegged relative to a basket of currencies including the USD.

Chinese efforts to stimulate their economy have underwhelmed investors so far and actually seen an accelerating decline in Chinese yields towards the end of the year. They have shifted their policy stance from "prudent" to "moderately loose", with this phrase last being used following the GFC. Their degree of success or failure will be very important to markets in general and Australian resources in particular in 2025. We lean on the side of failure given the sheer size of the debt-funded overinvestment that they have to grapple with.

Put all this together and the potential concerns in NZ and Australia seem almost quaint in comparison to the roller-coaster that lies ahead in the US, the debt-deflation battle in China and the basket-cases that France, Germany and the UK have turned into. Our debates revolve around shades of monetary policy grey.

We enter 2025 with valuations at historical extremes and with investors being over-exposed to equities. We are very much tilted to shorting the extremities of exuberance, while being long a range of names on perfectly reasonable valuations which have interesting growth outlooks relative to their multiples. While the Fund is still net long at face value, the very different attributes of our long versus our short books should see us continue to provide solid defensive characteristics.

Fund Performance in December

Returning to the Fund's performance in the month of December, our overall return of circa +1.2% pre fees and tax was very much the reverse of the previous month. Our long book return of -0.3% was unsurprisingly a little weak along with markets but this was more than offset by a strong +1.6% from our shorts. Our overall "winners to losers" ratio was an exceptionally strong 68%. This would normally result in a very strong month but there was a skew to our modest number of detractors being larger than our winners.

Our gross exposure fell from 141% to a relatively low 129% as we closed out a number of positions from both sides of the ledger. It will likely rise from here especially if result season in February provides some overbought and oversold opportunities. Our net position rose from 42% to 46% but this is still very much market-neutral in terms of the outcomes it is delivering. We remain solidly net long NZ and are more neutral in the expensive Australian market.

Led by Australia's weakness, there were a high eleven negative days for the 50/50 index of Australia and NZ in December. The average return for the market on those days was -0.49%. Our Fund carried on marching to the beat of its own drum, being up on five of those days and with a near-zero average return on all of them of +0.01%. There continues to be no measurable correlation between the performance of the Fund and that of the market.

Unlike the previous few months, we had no massive standouts in terms of individual positive contributions. Rather, we had a large array of more modest tailwinds. The strongest of these came from our long-held short in Reece Limited (REH, -13.1%) which continued to fall away on weakness in the US housing market, with the Australian cycle also starting to look a touch shaky. They are still on a Jun25 PE of 37.8x. The seemingly universal admiration for them as a "quality" name seems to have induced too much amnesia about the economic cycle. Similar comments apply to our smaller short in James Hardie (JHX, -10.9%).

The largest winner amongst our longs was our good-sized position in Monash IVF (MVF, +5.8%). There was no news of any great note although monthly IVF numbers were reasonably solid. MVF remains one of our favourite longer term structural growth names and we tend to alter our position size as investors' views towards it oscillate.

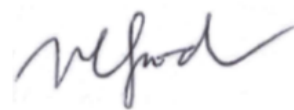
Other smaller positives came from a moderate long in our old friend Intelligent Monitoring Group (IMB, +8.7%) which we repurchased in their recent equity raising and weakness around that. They continue to look to consolidate the industry as they purchase companies on low private multiples. Shorts in Scentre Group (SCG, -6.8%), Commonwealth Bank (CBA, -3.4%) and Hub24 (HUB, -7.7%) also assisted. 27 out of 33 shorts worked in the month thanks to Australian "darling stocks" experiencing a minor moment.

The largest detractor was again our mid-sized long in DUG Technology (DUG, -16.5%). DUG has gone from $0.50 to over $3.00 and has now retraced all the way back to the $1.30 region. A growth darling is rapidly becoming a value stock as they are being clobbered by impatient investors, many of whom no doubt participated in their equity raising at $1.90 in October. We continue to gradually buy back what we sold at the much higher levels. We view DUG as having an edge in their super-computer enabled seismic processing technology as well as some blue-sky lottery tickets in their cooling technology and modular edge data centres.

The second headwind of note was the relatively large short we have built up in Auckland Airport (AIA, +12.1%) which has risen sharply since the sale of the Auckland Council stake. This is a straight valuation call, with AIA being well above pre-Covid multiples but traffic is still only returning gradually to those levels and their terminal is no longer a booming infant formula/honey emporium. Australian investors appear to misunderstand and overpay for the material portion of the business that is regulated, with it being the unregulated parts such as shopping and parking that are required for excess returns. AIA rose unusually sharply in the last four days of the quarter.

Other detractors were all relatively modest. Our large short in the "darling stock" Breville (BRG, +5.4%) defied the market weakness for reasons that weren't obvious. Also hurting were a good-sized long in Challenger (CGF, -3.4%) and a small long in Domain Holdings (DHG, -12.2%), which is a speculative dabble on Nine Entertainment perhaps restructuring its 60% holding.

Thank you for your continued support and interest in the Fund. December was a solid month, with a pleasingly widespread array of contributors. We are cautiously optimistic on the outlook for NZ equities in 2025 given easing monetary policy conditions and a return to moderate growth. However, this is against a backdrop of potential volatility from the overpriced and overblown markets in the USA and Australia and the contrasting risks of a debt-deflation trap in China. 2025 may prove volatile but we will continue to do our level best to extend the Fund's long-term track record of delivering equity-like returns, with far less volatility and no correlation to long-only equity markets.



Matthew Goodson, CFA

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