SALT

Salt NZ Dividend Appreciation Fund Fact Sheet – June 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 30 June 2020

Benchmark	S&P/NZX 50 Gross Index
Fund Assets	$91 million
Inception Date	30 June 2015
Portfolio Manager	Matthew Goodson, CFA

Unit Price at 30 June 2020

Application	1.6159
Redemption	1.6094

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 30 June 2020

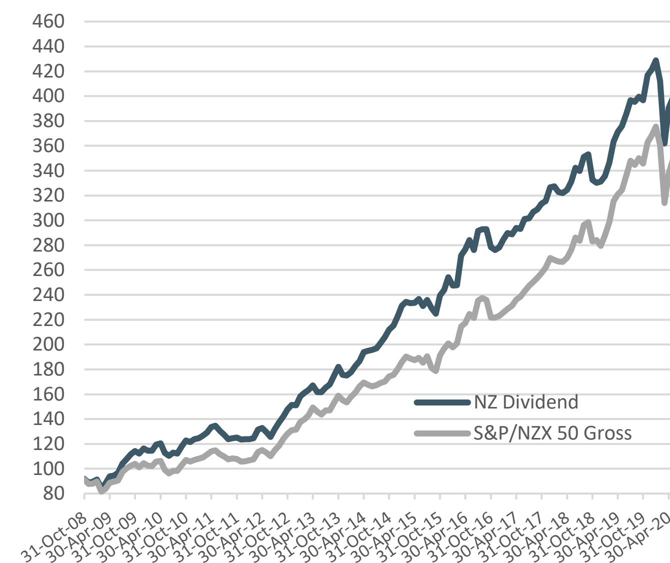
NZ shares	99.02%
Cash	0.98%

Fund Performance to 30 June 2020

Period	Fund Return*	Benchmark Return
1 month	5.05%	5.23%
3 months	15.69%	16.89%
6 months	-0.64%	-0.35%
1 year	8.49%	9.05%
2-year p.a.	10.55%	13.16%
3 years p.a.	11.58%	13.62%
5 years p.a.	12.60%	14.87%
7 years p.a.	14.56%	14.49%
10 years p.a.	14.24%	14.44%
Inception p.a.	12.95%	11.80%

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 30 June 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	Ryman Healthcare
Investore Property	Ports of Tauranga
Turners Automotive	Fisher & Paykel Healthcare
Marsden Maritime Holdings	Auckland Airport
Spark	Pushpay Holdings

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NZ Market Commentary

The "don't fight the Fed" momentum trade continued through June to as the heroic market come-back put the March lows firmly in the rear-view mirror, for now at least. Early in the quarter, the consensus of the shape of the recovery was skewing to a "U" or "W" but markets appear to have priced in a strong "V" as confidence reappeared faster than expected and concurrent activity indicators held up better than expected. Global equities as measured by the MSCI ACWI climbed +19.4% however they remained down -5.8% year-to-date.

The S&P500 surged +20.4% in the quarter, to be down -3.1% YTD and 8.6% below recent all-time highs at a time when unemployment went from record lows to 20 million. Whilst some stocks are experiencing significant increases in demand, various sectors (airlines, leisure, hotels, energy etc) have been crushed and overall demand is likely to need time to rebuild back to 2019 levels. The Fed has signalled its intent to expand its balance sheet via a broader menu of assets and fiscal stimulus has gone some way to keep the economy ticking over. Volatility may re-remerge as Covid-19 cases resurge, we edge closer to the election and trade war rhetoric escalates.

Meanwhile China has, in many people's eyes, effectively ended the one-country two -systems regime in Hong Kong. For now, this has been met with a mild market reaction. Hong Kong's Hang Seng rose a mere +3.5% over the quarter and remains down -13.3% year-to-date.

Australia's S&P/ASX200 rose +16.5% over the quarter but remains in negative territory year-to-date (-10.4%). Tech (+48%), Consumer Discretionary (+30%) and Energy (+28%) led the charge, whereas defensive Healthcare (+2%), Consumer Staples (+7%) and Utilities (+4%) lagged with single digit returns. Capital raisings continued as companies rebuilt balance sheets.

NZ's S&P/NZX50 Gross Index posted a +16.9% return over the quarter to bring the year-to-date performance to nearly flat (-0.5%). The key performers were Pushpay (PPH +159%) due to two small guidance upgrades, Tourism Holdings (THL +82%) on cost-out and avoiding a capital raise thus far, and Air New Zealand (AIR +55%) as it recovered from depressed levels and amid a torrent of retail buying. The key laggards were NZ Refining (NZR -6%) due to uncertainty around the strategic review, Z Energy (ZEL -7%) on weak volumes and margins, and Precinct Property (PCT -7%) given likely pressure on Auckland CBD rents.

Salt NZ Dividend Fund Commentary

The Fund lagged the benchmark in the extremely strong June quarter, rising by +15.69% compared to the +16.89% turned in by the S&P/NZX50 Gross Index. The quarter saw sharp outperformance by a barbell that can perhaps best be titled "diamonds and rust", with several high multiple growth names and several low-quality names with significant balance sheet challenges. The Fund is not naturally an owner of either end of this barbell but this was largely offset by strong performance from a number of our overweights.

The largest headwind was having no holding in Pushpay Holdings (PPH, +159.3%). This soared as it delivered a result at the bottom-end of expectations but this came with better than expected guidance as the Covid crisis has accelerated the channel shift from physical to digital church donations that their app powers. Growth and momentum investors fell over themselves in aggressively chasing the share price even though the segment is competitive and does not have a limitless growth runway as the share price is now implying.

Although having relatively small index weights, sharp bounces in Tourism Holdings (THL, +81.7%) and Air New Zealand (AIR, +55.2%) were also somewhat painful. The latter in particular has a severely challenged balance-sheet but it was swarmed by mass-market retail investors on the misapprehension that the Government somehow has AIR's back. Other notable detractors were the large underweight in Ryman Healthcare (RYM, +28.2%) and having no holding in the ultra-expensive Port Of Tauranga (POT, +27.3%), whose earnings outlook is far from riskless. The Ryman pain was more than offset by our overweight in Oceania Healthcare (OCA, +30.4%) which outperformed other retirement sector stocks with the exception of the corporate target, Metlifecare (MET, +35.3%) which made a slight positive contribution to the Fund.

The largest positive by some distance was the Fund's overweight in the high-yielding Turners (TRA, +52.9%) which recovered from a good deal of the punishment meted out to it in the March quarter. TRA delivered a March 2020 year result that was in line with pre-Covid guidance despite the end of March being hindered. More importantly, after business dwindling to near nothing during the Level 4 lockdown, they began to experience a recovery during the latter part of the June quarter, with the month of June being ahead of June 2019. The used car market has not experienced the huge post-lockdown bounce of some other segments but Turners is clearly gaining market share. Importantly, we had viewed their finance book as being a risk but their bad and doubtful debt experience has not been problematic. Consensus forecasts have Turners on a forward PE of 9.5x and our long-term thesis of them becoming by far the largest player in the huge and fragmented used car market remains very much intact.

Other notable positives came from overweights in Spark (SPK, +11.6%), Tower (TWR, +8.7%) Scales (SCL, +10.1%) and Marsden Maritime (MMH, +18.6%).

As this is written, the NZ market is on a record forward PE for the "core" market (ex-property, Infratil and Air NZ) of a staggering 38x although the median PE is a far more appealing 19.5x. With 10-year bond yields below 1.0%, the impact on this fair value of a small change in the bond yield is extreme. The quarter was notable for the "FOMO" trade, where a fear of missing out saw a number of previously beaten-up stocks rally sharply on hopes that the worst is over for them. Relatively safe yield stocks generally did little or even underperformed but we expect an extended period of ultra-low interest rates to see the FOMO trade morph into "TINA" – there is no alternative. The Fund has hung in there solidly over the last couple of quarters despite sharp outperformance by "diamonds" (high multiple growth stocks) and "rust" (deeply challenged balance sheets).

Matthew Goodson, CFA

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