SALT
Funds Management

Salt Enhanced Property 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 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 31 March 2018

Benchmark	S&P/NZX All Real Estate Gross Index
Fund Assets	$5.5 million
Inception Date	11 November 2014
Portfolio Manager	Matthew Goodson, CFA
Associate PM/Analyst	Andrew Bolland, CFA

Unit Price at 31 March 2018

Application	1.3702
Redemption	1.3646

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 31 March 2018

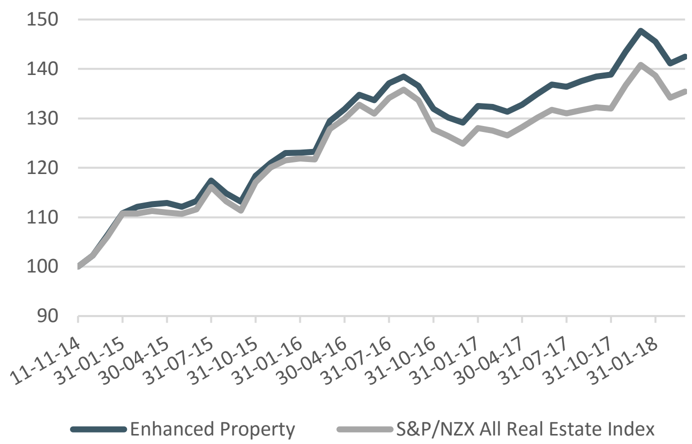
Long Exposure	100.75%
Short Exposure	-4.69%
Gross Equity Exposure	105.44%
Net Equity Exposure	96.07%

Fund Performance to 31 March 2018

Period	Fund Return	Benchmark Return
1 month	0.98%	0.93%
3 months	-3.54%	-3.85%
6 months	2.92%	2.37%
1 year p.a.	8.47%	6.98%
2 years p.a.	4.90%	2.90%
3 years p.a.	8.16%	6.76%
Inception p.a.	11.05%	9.38%

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 Listed Property Shares	87.47%
AU Listed Property Shares	8.71%
Cash	3.82%

Top Overweights	Top Underweights/Shorts
Centuria Metropolitan REIT	Property for Industry
Investore Property	Goodman Property Trust
Viva Energy REIT	Kiwi Property Group
NPT Ltd	Vital Healthcare Property Trust
Garda Diversified Property Fund	Goodman Group (short)

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Quarterly Property Market Commentary

The S&P/NZX All Real Estate Gross Index declined by -3.85% in the March quarter as rising global bond yields amidst gradually tightening monetary conditions placed defensive sectors under pressure around the world. The global FTSE EPRA/NAREIT Index fell by a sharp 5.2%.

Interestingly, NZ 10-year bond yields actually fell slightly from 2.75% to 2.74% although they did test 3.0% at their intra-period peak. Despite this, NZ property stocks came under pressure from the global weakness. The story was even more pronounced in Australia, with their index plunging -6.4% despite relative to flat bond yields. This reflected the heavy weighting of shopping centre entities in the Australian index, with this segment coming under particularly sharp global pressure.

Specific NZ property company news was dominated by reporting season for Precinct (PCT), Property For Industry (PFI) and Vital Healthcare Property (VHP). PCT showed solid evidence of rental growth but made no further leasing progress on the office tower component of their Downtown development. Higher tax payments across all three companies was another notable aspect and this seems likely to continue across the sector. A number of companies also announced NTA increases, with the average uplift being +5.7% but the market paid little heed to these as share prices moved to discounts to NTA. Given the relatively late stage of the cycle this was perhaps to be expected.

We are seeing the return of share buybacks as a theme. This was most pronounced in Australia, with Mirvac, Lend Lease, Scentre Group and Dexus all committing to them. In NZ, Investore would appear the most likely to pull the trigger given recent property sales at well above NTA, while their share price languishes well below it. If the gap between listed company share prices and private asset prices persists, we would expect asset sales by listed companies.

Whilst shopping centre assets are somewhat on the nose globally, NZ has less square meterage per head, which coupled with population growth, means the sector is still in expansion mode. The quarter saw a massive expansion committed to at Westfield Newmarket along with expansions at Botany Town Centre and The Galleria (Sylvia Park). The initial yield at the latter is projected to be a somewhat meagre 5.7% as building costs have continued to rise.

Outperformers during the quarter were Augusta (AUG, -0.0%) and Property For Industry (PFI, -1.1%), while Argosy (ARG, -6.1%), Precinct (PCT, -4.7%) and Kiwi Property (KPG, -4.6%) brought up the tail.

Quarterly Fund Commentary

The Fund modestly outperformed the weak benchmark return over the quarter, declining by -3.54% after all fees and expenses compared to the Index move of -3.85%. Unsurprisingly in a weak quarter, the largest contributions to outperformance came from a variety of underweight and short positions.

The Fund's collection of shorts collectively added 0.25% to performance, with larger contributors being Dexus, (DXS, -4.4%), Bunnings Warehouse Property (BWP, -2.3%) and Charter Hall (CHC, -4.8%). With these all falling by slightly less than the Australian index, it is fair to say that this contribution owes more to market movement than stock selection. The weakest names during the period were the large shopping centre REITs such as Vicinity and Scentre but these were showing up as fair value rather than expensive in our relative value modelling. Standout contributors amongst the NZ underweights were Argosy (ARG, -6.1%) and Precinct (PCT, -4.7%).

More interestingly, several overweights actually added value in what was a rather difficult period. The largest of these was our holding in Garda Capital Group (GCM, +11%), which is the management company of the strongly performing Garda Property Trust. A second winner was a return to our old friend Propertylink (PLG, +0.5%), which we acquired near its lows during the quarter and which closed strongly on renewed M&A speculation. Millennium & Copthorne ordinaries and preferreds (MCK, MCKPA, +4.0%) rose following a strong result, that saw NTA rise from $3.49 to $4.19 per security. Both the listed MCK instruments trade in the mid-$2.80 region – a highly attractive discount. The outlook will likely see lower land development earnings but strong growth from the dominant hotels business.

Finally, while we have no holdings in NZ retirement villages, a moderate stake in Ingenia Communities (INA, +2.6%) also worked well. This Australian retirement developer's model is to build a village and make a one-off development profit when a pre-fab house is sold outright to an incoming resident. More importantly, they charge a CPI-indexed land rental, with this generally being paid out of a resident's means-tested pension and accommodation supplement. Current cap rates on the land are circa 8%, which seems very high to us when you have a CPI-indexed land rental stream for many decades into the future.

Conversely, headwinds came entirely from several of our main overweight positions. The largest of these was Centuria Metropolitan Office (CMA, -2.7%). CMA stands out by some distance in our relative valuation matrix with its yield being unduly high relative to its free cashflow generation, its portfolio quality and its gearing. We also view its suburban office assets as being some way from a cyclical peak as tenants flee quite extraordinary CBD rentals. Investore (IPL, -4.8%) and Viva Energy REIT (VVR, -8.6%) also weighed on the Fund.

The Fund's net position was little changed at 96% in the quarter, while the gross fell from 109.4% to 105.4%. We are actively looking for more short positions but would like to see greater relative valuation divergence from potential longs on the other side. We used weakness to cover shorts in Dexus and Mirvac, while undue strength following the Goodman Group result saw us lift that from the short-side. Elsewhere, we used temporary weakness to lift holdings in Argosy, Precinct, Abacus and Garda Capital, while we bought a new holding in Propertylink. We lightened Goodman Property, Kiwi Property, Stride and Vital Healthcare Property.