

Factsheet 30 June 2021

NIKKO AM INCOME STRATEGY

Applies to: Nikko AM Income Fund (retail).

Market Overview

- The NZ economy is recovering well and the outlook for a global economic recovery is looking promising.
- Returns from the bond sector were modestly positive, however the equity sector delivered strong returns and contributed significantly to the fund's monthly return.
- Longer term bonds performed strongly as NZ long term interest rates followed global trends and decreased. Short term bonds struggled.

Fund Highlights

- The Income Fund returned 2.9% over the quarter.
- The share portfolio of the Income Fund increased in value over June by around 3.7%. Ten of the twelve holdings gained in value with the best performers being Heartland and Skellerup, both advancing by more than 7%.
- The bond sector of the fund is invested primarily in medium to longer duration assets.

Distributions

- The defined distribution rate (which is used to calculate the distribution you receive from the fund) is set at the start of each calendar year, based on the price of the fund at that point.
- The defined distribution rate for 2021 is 3.0% p.a. This income will be distributed in four equal amounts each calendar quarter, based on the price as at 1 January 2021.

Performance

	One month	Three months	One year	Three years (p.a)	Five years (p.a)	Ten years (p.a)
Retail ¹	1.47%	2.91%	10.15%	2.37%	3.01%	4.68%
Benchmark ²	0.26%	0.81%	3.25%	5.09%	4.39%	7.16%
Market Index ³	0.99%	0.36%	3.48%			

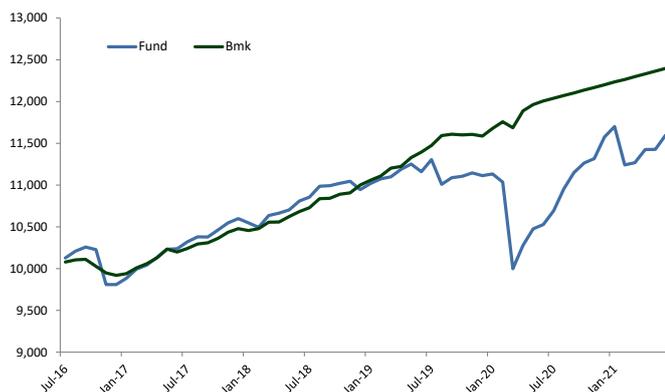
1. Returns are before tax and after the deduction of fees and expenses and including tax credits (if any).

2. Current benchmark: RBNZ Official Cash Rate +3.00% p.a.

3. Current appropriate market index: 62.5% Bloomberg NZBond Credit 0+ Yr Index, 7.5% S&P/NZX 50 Gross Index, 7.5% Alternatives exempt.

Five Year Cumulative Performance, \$10,000 invested^{1,2}

Change of investment strategy 01/07/2020



Portfolio Manager

Fergus McDonald,
Head of Bonds and Currency



Fergus is responsible for the investment of the Bond, Cash and Currency mandates. Fergus has been actively involved in the NZ financial markets since 1981. The portfolio management team for the domestic fixed income funds includes Ian Bellew, Fixed Income Manager and Matthew Johnson, Fixed Income Manager.

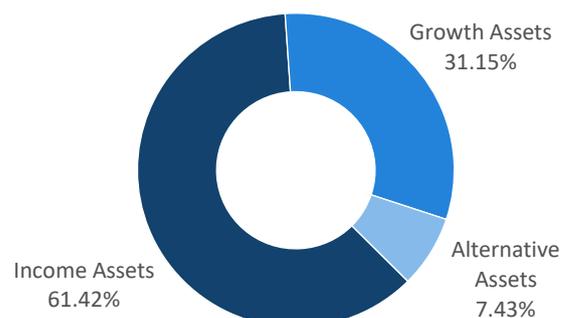
Overview

The strategy aims to provide investors with regular income from an actively managed investment portfolio. The fund invests in NZ fixed interest, Australasian equities and property. Equities with a good dividend stream and a focus on growing value over time are selected as an attractive alternative to fixed income securities. Equity selection is determined by the NZ investment team.

Objective

The objective of this fund is to outperform the RBNZ Official Cash Rate by 3.00% p.a. over a rolling three year period before fees, expenses and taxes. Prior to June 2020, the objective and strategic asset allocation of fund were materially different. From 1 July these were amended to include equities.

Asset Allocation



Top 5 Fixed Income Issuers*	(%)	Duration*	Top 10 Equities	(%)	(%)
NZ Local Govt Funding Agency	6.30%	Fund 4.02 years	Heartland Group	3.27	Works Finance NZ Ltd 2.30
Kiwibank Ltd	4.34%	Yield to Maturity	Spark New Zealand Ltd	3.14	Mercury NZ Ltd 2.10
Infratil Ltd	3.41%	Fund (gross) 2.02%	Skellerup Holdings Ltd	2.92	Argosy Property Ltd 2.06
Liberty Finance	3.24%		Stride Stapled Grp	2.86	Infratil Ltd 2.00
Fonterra Co-Operative	3.16%		Contact Energy Ltd	2.58	Scales Corp Ltd 1.94

*Applies to the portfolio of directly held fixed income assets only.

Fund Commentary

The Income Fund returned 2.9% over the quarter. Returns from the bond sector were modestly positive, however the equity sector delivered strong returns and contributed significantly to the fund's return. Longer term bonds performed strongly as NZ long term interest rates followed global trends and decreased. The fall in rates occurred as investors started to agree with the Central Bank's view that any rise in inflation is likely to be transitory and will not become a significant problem. In addition, longer term interest rates have already risen a lot since reaching their low points in September and October 2020. In contrast the rates on shorter term bonds have started to rise in anticipation of a rise in the Official Cash Rate, possibly in the first half of 2022.

The share portfolio of the Income Fund increased in value over June by around 3.7%. Ten of the twelve holdings gained in value with the best performers being Heartland and Skellerup, both advancing by more than 7%, Genesis Energy and Investore Property decreased by around 1% each. Late in June we added Infratil to the share portfolio. Meridian remains the smallest exposure and Heartland the largest.

We continue to believe that even though the NZ economy is recovering well and the outlook for a global economic recovery is looking promising, short term rates will stay low over 2021 and into 2022 before rising. Economic activity is returning to pre-COVID levels and therefore, the COVID inspired cut in the Official Cash Rate from 1% to 0.25% over 2020 can expect to be taken back in 2022, before rising to perhaps 2% in 2023 where rises should top out. We see the peak in the interest rate cycle being much lower than in previous tightening cycles. As mentioned above, we see the OCR peaking at 2% with longer term rates perhaps moving higher from current levels but not by much. With the prospect of interest rates remaining low relative to historical levels, we continue to believe it is appropriate for investors to seek income from more diverse sources than just interest rates alone. Even though some equity prices have fallen we believe the growth environment remains attractive for the equity market. This means the Income Fund will remain invested in a range of NZ companies listed on the NZX that pay an acceptable level of dividends or who have the likelihood of doing so in the future. In addition, it is expected that over time the industry sectors and business models adopted by these companies should see a steady or rising share price.

The bond sector of the fund is invested primarily in medium to longer duration assets. We are happy to have exposure to longer term assets as the Official Cash Rate looks likely to remain low over the next year or two and longer-term rates have already risen significantly in response to the strong economic recovery. The prospect of low cash rates coupled with the RBNZ continuing to buy bonds in the secondary market and their desire to see a sustainable recovery in labour markets across all sectors of the community, will likely keep a lid on the size of future interest rate rises. The managers of the fund will continue to look for opportunities to add value and income. Low and stable short-term interest rates represent both a threat and an opportunity. High levels of liquidity in the banking system has left many investors looking for a home for their money that gives them an opportunity to earn more than bank deposits. This search for income is likely to be an enduring theme for the next few years and we believe this environment should create opportunities for the fund to deliver an enhanced level of performance.

Distributions	Estimated annual fund charges (incl. GST)
Distributions for this fund are defined annually and are effective for the calendar year. The defined rate is gross of tax. Distributions are not a taxable event. Tax will be deducted (refunded) at 31 March and on full or partial withdrawals.	0.80%, refer PDS for more details
Hedging	Buy / Sell spread: Strategy size Strategy Launch
All investments will be in New Zealand dollars	Click to view \$4.6m October 2007

Compliance

The fund complied with its investment mandate and trust deed during the quarter.

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