

Factsheet 31 October 2022

NIKKO AM INCOME STRATEGY

Applies to: Nikko AM Income Fund (retail).

Market Overview

- Longer term corporate bond yields moved higher over the month as central banks around the globe indicated they will keep interest rates elevated for an extended period to ensure inflation pressures and inflation expectations fall. Government bonds were the best performing sector of the bond market as buying demand increased as NZ government bonds entered some global bond indices.

Fund Highlights

- The Income Fund increased modestly over October. Equity markets performed well over the month as company earnings continue to be at or above expectations and perhaps the top of the interest rate tightening cycle is in sight.

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 2022 is 3.5%. This income will be distributed in four equal amounts each calendar quarter, based on the price at 1 January 2022.

Performance

	One month	Three months	One year	Three years (pa)	Five years (pa)	Ten years (pa)
Retail ¹	0.26%	-2.79%	-6.47%	-0.82%	0.70%	3.30%
Benchmark ²	0.53%	1.49%	4.68%	4.19%	4.83%	6.41%
Market Index ³	0.71%	-1.95%	-6.43%	-	-	-

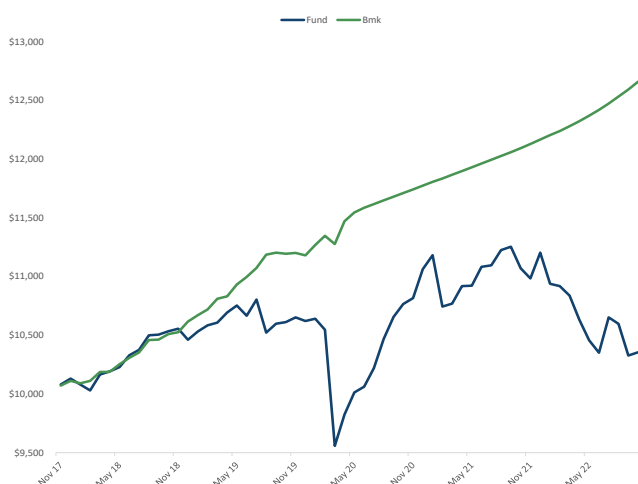
1. Returns are before tax and after the deduction of fees and expenses and including tax credits (if any).

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

3. Current appropriate market index: 62.5% Bloomberg NZBond Credit 0+ Yr Index, 30% 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.

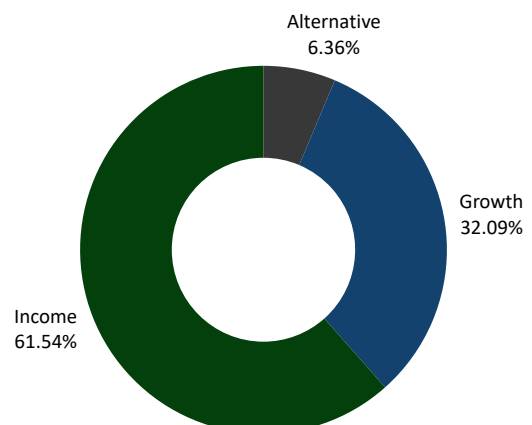
Overview

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 2020 these were amended to include equities.

Asset Allocation



NIKKO AM NZ INCOME STRATEGY

Top 5 Fixed Income Issuers*	(%)	Duration*	Top 10 Equities	(%)	(%)
Westpac New Zealand Ltd	7.36	Fund 4.01 years	Heartland Group	3.09	Contact Energy Ltd 2.40
Bank of New Zealand	4.70	Yield to Maturity	Skellerup Ltd	3.02	Chorus Limited 2.20
ASB Bank Ltd	4.31	Fund (gross) 5.59%	Spark New Zealand Ltd	2.91	Works Finance NZ 2.20
New Zealand Local Govt Funding	3.89		Infratil Ltd	2.66	Scales Corp Ltd 1.87
Contact Energy Ltd	3.41		Stride Stapled	2.48	EBOS Ltd 1.60

*Includes cash holdings.

Fund Commentary

The Income Fund increased modestly over October. Equity markets performed well over the month as company earnings continue to be at or above expectations and perhaps the top of the interest rate tightening cycle is in sight. Longer term corporate bond yields moved higher over the month as central banks around the globe indicated they will keep interest rates elevated for an extended period to ensure inflation pressures and inflation expectations fall. Government bonds were the best performing sector of the bond market as buying demand increased as NZ government bonds entered some global bond indices.

The S&P/NZX 50 Gross Index increased by almost 2.5% over the month. The bond sector, as measured by the Bloomberg Corporate Bond Index fell by 0.13%. The Option Fund returns were up over the month. Looking at the performance of some individual equity names in the fund, Chorus was a standout, gaining 9.3%. The fund owns 14 companies in its equity portfolio and over the month 9 increased in price and 5 declined. Skellerup and Stride Property were the laggards, both falling around 4%.

There was a notable difference in performance across bond sectors with NZ government bonds strongly outperforming corporate bonds. NZ Government bonds performed strongly through the month with their 31 October inclusion in the WGBI bond index which drove some strong buy-side support from locals and offshore managers. NZ credit margins have remained stable and with year-end fast approaching there will likely be a shortage of new issuance which should be supportive until supply resumes in the new year.

A higher terminal cash rate around 5% is looking more likely as there has been little improvement in inflation, and the labour market remains tight. What will dominate the direction of bond markets in the short term remains difficult to forecast. Investor focus continues to swing from being concerned about high inflation to concern about the negative impact tightening monetary conditions may have on growth. It looks likely volatility remains high in the near term until we get more certainty from economic data.

We may be closer to a plateau in peak cash rate expectations. However, how long short rates remain elevated for is uncertain, and the fate of longer-term bond rates are likely to remain much more heavily influenced by offshore direction. In this environment it still makes sense to not have too much risk to the direction of interest rate moves however bonds with yields in the mid 5% range and above look attractive to us as they will likely out-perform the returns from cash over the medium term. We continue to believe investors should seek income from a diverse range of sources. Bond rates are looking attractive and even though most equity prices have fallen over the past year we believe the environment remains acceptable for equities although we concede catalysts for new growth remain elusive and an economic slowdown looks inevitable. The Income Fund remains invested in a range of NZ companies listed on the NZX that pay a consistent level of dividends or who have the likelihood of doing so in the future. In addition to the fund receiving a steady stream of dividend income, we expect that over time the industry sectors and business models adopted by these companies should be rewarded by a steady or rising share price.

Key Fund Facts

Distributions 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.	Estimated annual fund charges (incl. GST) 0.80%, refer PDS for more details		
Hedging All investments will be in New Zealand dollars	Buy / Sell spread: Click to view	Strategy size \$4.7m	Strategy Launch October 2007
Restrictions: Adult entertainment, gambling, fossil fuels, alcohol stocks, tobacco stocks. For more information please refer to the Statement of Investment Policy and Objectives (SIPO) which can be found on our website https://www.nikkoam.co.nz/invest/retail .			
Exclusions: Securities that conduct activities listed on the Schedule to Cluster Munitions Prohibition Act 2009. Tobacco manufacturers.			

Compliance

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

Contact Us

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