

NIKKO AM INCOME STRATEGY

Applies to the Nikko AM Income Fund

Market Overview

- Bonds gave a modest gain and equity markets fell over the month.
- There are signs that inflation may have peaked and is now looking to moderate.
- Equity markets continued to see high levels of volatility in individual company performances.

Fund Highlights

- The fund owns 14 companies in its equities portfolio; over the month eight fell in price and six increased.
- The duration of the fixed income portfolio was extended slightly - locking into longer term bonds around current levels.

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 2023 is 5.5%. This income will be distributed in four equal amounts each calendar quarter, based on the price on 1 January 2023.

Performance

	One month	Three months	One year	Three years (pa)	Five years (pa)	Ten years (pa)
Retail ¹	-0.18%	1.72%	1.06%	1.82%	0.65%	3.09%
Benchmark ²	0.68%	1.98%	6.76%	4.58%	5.19%	6.26%
Market Index ³	-0.52%	1.36%	3.68%			

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}



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.

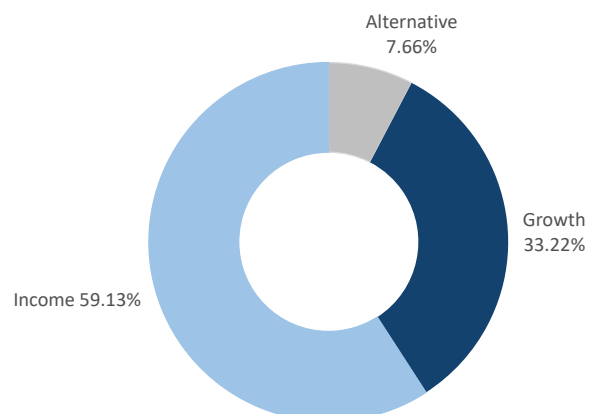
Overview

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 FUND

Top 5 Fixed Income Issuers*	(%)	Duration*	Top 10 Equities	(%)	(%)	
Westpac New Zealand Ltd	10.65	Fund 4.15 years	Infratil Ltd	3.58	Works Finance NZ	2.52
ASB Bank Ltd	5.12%	Yield to Maturity	Spark New Zealand Ltd	3.45	Skellerup Holdings	2.51
Kiwibank Ltd	4.05%	Fund (gross) 6.07%	Contact Energy Limited	2.99	EBOS Group	2.14
Powerco Ltd	3.85%		Heartland Group	2.64	Meridian Energy	2.00
TR Group Ltd	3.31%		Chorus Ltd	2.55	Kiwibank	1.58

*Includes cash holdings.

Fund Commentary

The Income Fund produced a slight loss over May as bonds gave a modest gain and equity markets fell. The S&P/NZX 50 Gross Index fell by 1.7% over the month and the bond sector increased 0.03% as measured by the Bloomberg NZ Bond Credit Index. Interest rate movements continue to be the main driver of returns from bond markets with large moves occurring due to considerable uncertainty and changing expectations for economic growth and central bank actions. The political impasse in the US surrounding negotiations to lift the debt ceiling to enable the government to continue to meet its obligations caused global uncertainty in bond markets. This resulted in higher bond yields in the US and this upward trend also pushed NZ rates higher over the month. Some reversal of these upward moves can be expected as a debt ceiling resolution is reached.

There are signs that inflation may have peaked and is now looking to moderate. At the Reserve Bank's May Monetary Policy Statement, the bank indicated they will hold the cash rate at an elevated level of 5.5% until the second half of 2024 as they monitor incoming economic data. They hope they have done enough to cool consumer demand, inflationary pressures and inflation expectations and further rate rises will not be required. It now seems the RBNZ is looking for reasons not to push cash rates higher. They cite some easing in some wage inflation, weaker global growth, easing international inflation pressures, reduced supply chain constraints, lower export prices, weaker than expected GDP growth and the negative impact on spending from the negative wealth effect, especially housing.

With cash rates peaking, locking into longer term bonds around current levels will likely outperform cash returns as the next significant move is likely to be down in rates but we might have to wait until the second half of 2024 until this occurs in any meaningful way.

Equity markets continued to see high levels of volatility in individual company performances. In general companies and industries that are sensitive to rising interest rates have performed poorly over the past year however as the trend towards higher rates fades these sectors may perform better as the year progresses. The fund owns 14 companies in its equities portfolio, over the month eight fell in price and six increased. Infratil, Stride Property and Mercury Energy saw their share prices advance by over 3% with Infratil being the star performer with a monthly return exceeding 6%. At the other end of the scale, Skellerup, Chorus and EBOS share prices declined by around 5% over the month.

The Option Fund performed well over the month. Bond yields continued to move in a volatile manner as the US debt ceiling approached and political brinkmanship created uncertainty regarding if agreement could be reached in time to ensure the US government avoided defaulting on some of its obligations. Agreement was ultimately reached but not before creating some anxiety in financial markets. The Income Fund will be selling its holding in the Option Fund over the month of June.

We continue to believe investors should seek income from a diverse range of sources. Bond rates are looking attractive and even though some equity prices have fallen over the past year we believe the environment remains acceptable for many companies. 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 dividend income, we expect 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	Estimated annual fund charges (incl. GST)		
Distributions for this fund are defined annually and are effective for the calendar year. The defined rate is 0.80%, refer PDS for more details gross of tax. Distributions are not a taxable event. Tax will be deducted (refunded) at 31 March and on full or partial withdrawals.			
Hedging All investments will be in New Zealand dollars	Buy /Sell spread:	Strategy size \$4m	Strategy Launch October 2007
Exclusions: Controversial weapons.	Click to view		
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 .			

Compliance

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

Contact Us

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