nikko am
Nikko Asset Management

NIKKO AM NZ BOND FUND

Monthly Fact Sheet 30 June 2017

Investment objective

The objective of the Fund is to construct a portfolio of permitted investments that outperform the Fund's benchmark return by 1.0% per annum over a rolling three year period before fees, expenses and taxes.

Benchmark

Bloomberg NZ Bond Govt 0+ Yr Index (from 1 July 2016)

Fund description

The Fund vehicle is a NZ domiciled Portfolio Investment Entity (PIE) which is priced daily. The Fund aims to provide investors with regular income by constructing an actively managed investment portfolio of New Zealand bonds, deposits and cash with the potential for capital gain from New Zealand dollar fixed interest markets.

The Fund gains its investment exposure by investing into the Nikko AM Wholesale NZ Bond Fund which is managed by the Nikko AM NZ Fixed Income team.

Distributions

Quarterly. Last business days of March, June, September and December.

Management fees and other charges

A management fee of 0.60% per annum calculated as a percentage of the net asset value of the Fund will be deducted from the Fund.

Nikko AM may also recover expenses (including the Trustee fee) from the Fund up to a maximum of 0.25% per annum of the Fund's net asset value. As at the time of publication these expenses are estimated to be 0.125% per annum.

Buy/sell spread

Nil

Investment restrictions

Nikko AM Wholesale NZ Bond Fund

- A minimum of 25% of the wholesale fund is to be invested in securities issued or guaranteed by the New Zealand Government or securities accepted by the RBNZ's Overnight Reserve Repo Facility.
- A minimum of 50% of the wholesale fund is restricted to debt securities with a credit rating equal to or higher than New Zealand Government.
- Minimum of 95% of the wholesale fund to be invested in assets rated A- or better.
- Portfolio modified duration range of +/- 1.5 years around index duration.
- Cash and cash equivalent investments must have a minimum credit rating of Standard & Poor's A1 short-term and A long-term.

Refer to the SIPO for full details of permitted investments and restrictions.

Performance

(NZD returns; before tax, after fees and expenses)

1 month	3 months	6 months	1 year
-0.47%	1.43%	3.21%	1.17%

2 years (pa)	3 years (pa)	5 years (pa)	Inception (pa)*
3.94%	5.34%	4.61%	5.68%

* January 2011

Distributions

Cents per unit	Mar	Jun	Sep	Dec
2017	0.20	1.00		
2016	1.40	1.25	1.05	1.25
2015	0.90	1.25	1.15	1.30
2014	0.90	0.50	0.80	0.80

Asset allocation (% of fund)

Government, Govt Depts & Govt guaranteed	27.8%
SOE and local authority	17.5%
NZ registered banks	28.2%
Corporate debt	26.5%

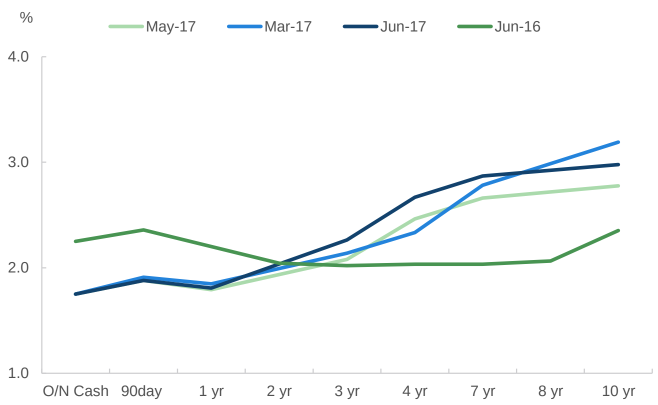
Credit quality (% of fund)

AAA	10.3%
AA	65.9%
A	19.2%
BBB	4.6%

Duration and yield

Duration	Fund 4.13 years vs benchmark 4.62 years
Yield	Fund (gross) 3.50% vs benchmark 2.31%

New Zealand yield curve



Top 5 corporate issuers (% of fund)*

NZ Local Government Funding Agency	13.0%
BNZ	7.4%
Fonterra Co-operative	6.2%
RaboBank	6.1%
Westpac Banking Corporation	6.0%

* excludes central government

Fund commentary

Bonds sold off over the month, however the fund outperformed the benchmark. The underweight duration position was a positive contribution to performance. The higher portfolio running yield and a moderate contraction in credit margins also contributed to performance. We favour credit to perform better than similar maturities of Governments and we are currently holding close to minimum levels of NZ Government bonds.

Market commentary

The month of June saw the Government Bond Index return -0.70% points, as the NZ Government 10-year bond increased in yield by 26 points, ending the month at 2.97%. The NZX 1-10 year swaps returned -0.40% and the Corporate A -0.22%.

NZ Government bonds were a global outperformer in the first three weeks of the month. However at the end of the month the European Central Bank, the Bank of England, and to a lesser extent the US Fed, issued co-ordinated statements around the future path of interest rates and monetary conditions. In a nut shell the Central Bankers have said that they see inflation reappearing, and monetary conditions normalising in due course. This was likely in response to a global market that did not appear to believe this to be the case, as evident in the recent global bond rally. As a result of this global bonds have sold off, and the yield curve steepened out to the long end. New Zealand bonds have followed suit. Swap yields have also gone higher, but have outperformed bonds.

NZ credit margins continued to contract in spread, and credit has generally outperformed similar maturities of swap and government bonds since the start of this year. The portfolios have benefited from having higher weightings to credit with both a higher running yield and margin contraction. We continue to have a positive view on credit and expect having a higher portfolio running yield will be one of the main attributors to outperformance over the course of this year. We prefer to hold more mid curve maturity (4-7 years) credit rather than longer government bonds that have a lower yield and greater interest rate risk.

The RBNZ re-iterated the OCR is firmly on hold. GDP growth was 0.5% for the March quarter and below forecasts of 1.1%. The construction sector lagged, while dairy and the primary sector had a strong positive contribution. Growth per capita remains modest. It is worth noting that quarterly GDP numbers can be heavily influenced by short term movements in particular sectors, and are subject to being volatile. Consumer and business confidence are both at good levels, albeit down from recent highs. Wage inflation remains moderate, but is expected to increase due to labour market capacity constraints. The housing market, particularly in Auckland, has slowed and will likely continue to do so as we come up to the election. The main take away from this is that the economy is growing modestly, not roaring away unsustainably, and that the OCR at these levels and the RBNZ forecast of being on hold for the foreseeable seems entirely appropriate.

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