Nikko Asset Management

NIKKO AM NZ BOND FUND

Monthly Fact Sheet 31 August 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
0.62%	0.77%	3.27%	0.90%

2 years (pa)	3 years (pa)	5 years (pa)	Inception (pa)*
3.61%	5.18%	4.58%	5.73%

* 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	28.6%
SOE and local authority	17.5%
NZ registered banks	36.9%
Corporate debt	17.0%

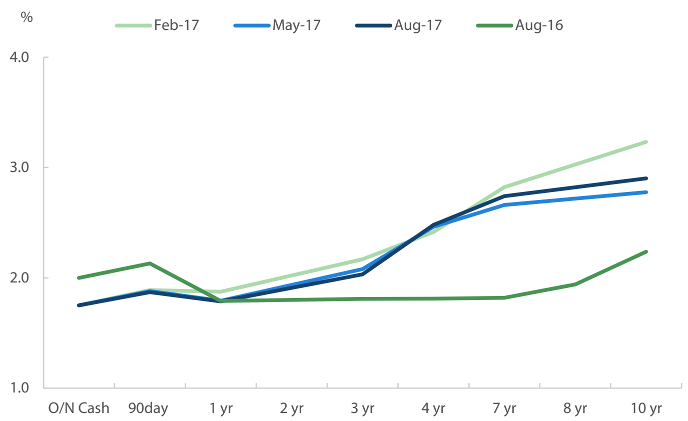
Credit quality (% of fund)

AAA	10.0%
AA	67.4%
A	18.3%
BBB	4.3%

Duration and yield

Duration	Fund 4.19 years vs benchmark 4.46 years
Yield	Fund (gross) 3.10% vs benchmark 2.32%

New Zealand yield curve



Top 5 corporate issuers (% of fund)*

NZ Local Government Funding Agency	13.1%
BNZ	7.9%
Westpac Banking Corporation	6.8%
Fonterra Cooperative Group	5.9%
Rabobank	5.9%

* excludes central government

Fund commentary

The fund performed well over the month. Longer maturity bonds were some of the best performers through August as interest rates moved marginally lower in yield. Previously we had extended duration through switching some LGFA and bank bonds longer in maturity. Credit margins were stable but corporate bond holdings continued to add value.

Market commentary

The Bloomberg NZ Bond Govt 0+ Yr Index returned +0.51% for August as interest rates moved marginally lower during the month. The Bloomberg 1-10 year swaps returned +0.60% and the Bloomberg Credit Index +0.56%.

The move lower in NZ interest rates during the month of August was fairly consistent across maturities with NZ government bond rates finishing approximately 7bps lower in yield. On a sector basis similar maturities of swap performed slightly better than government bonds as swap margins contracted (1 to 5bps) relative to governments. Longer dated maturities of swap were the better performers contracting more in margin than shorter maturities. The tightening in local credit margins appears to have stalled with margins relatively stable over the month. NZ credit outperformed offshore credit where there was some widening in margins due to risk-off sentiment. With a near parallel shift lower in interest rates in the government yield curve, and some small contraction in swap margins, the best performing bonds over the month were longer dated maturities that have more price gain exposure to falling interest rates. Higher yielding maturities of credit also continued to perform well.

Interest rates have remained in a relatively narrow range so far this year and volatility in financial markets has been subdued with the events and geopolitical concerns that the market was concerned passing with little disruption. Potential "bumps in the road ahead" could be an escalation of North Korean tensions and the unwinding of the Fed's bond buying program. At the same time financial market expectations have become increasingly positive that economies appear to be recovering. Central banks are on hold neutral, or moving closer to a slow and cautious approach for reducing stimulus. In contrast, lower than expected or dormant inflation outcomes have effectively reduced expectations for higher interest rates.

We remain happy to extend the duration of credit maturities out to mid curve through spending cash and selling shorter maturities when pricing makes sense. 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.

The RBNZ continues to maintain their view that the OCR is firmly on hold and this should help to support short to medium term bond maturities from moving much higher in yield. Longer maturity bonds will continue to be more heavily influenced by the direction of offshore markets, particularly by movements in the US 10 year bond. We don't expect a significant impact to NZ financial markets from the upcoming election, although some investors may stay on the side-lines until there is more clarity. A change of government could lead to more government bond supply, a steeper curve and potentially reduced liquidity. Over the medium to long term there may be more potential impacts to consider depending on government policy.