NIKKO AM NZ CASH 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 0.2% per annum over a rolling three year period before fees, expenses and taxes.

Benchmark

Bloomberg NZBond Bank Bill 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 short term deposits and bonds whilst preserving capital value.

The Fund gains its investment exposures by investing into the Nikko AM Wholesale NZ Cash 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 0.25% 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 0.15% per annum of the Fund's net asset value. As at the time of publication these expenses are estimated to be 0.10% per annum.

Buy/sell spread

Nil

Investment restrictions

Nikko AM Wholesale NZ Cash Fund

- Authorised investments are cash, deposits and debt securities with an interest rate exposure of up to 365 days, issued or guaranteed by any NZ registered bank, SOE, NZ Government, NZ local authority and NZ and overseas corporate.
- Securities issued by corporates and registered banks must have minimum credit rating of A1 short-term and A long term (Standard and Poors). Derivative counterparties must have A or better credit rating and all derivative exposure shall be covered by cash or physical holdings.

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
0.21%	0.66%	1.36%	2.74%

2 years (pa)	3 years (pa)	5 years (pa)	Inception (pa)*
2.90%	3.29%	-	3.31%

* June 2014

Distributions

Cents per unit	Mar	Jun	Sep	Dec
2017	0.65	0.50		
2016	1.00	0.55	0.50	0.65
2015	0.75	0.70	0.90	0.70

Asset allocation (% of fund)

NZ Government, Government Department or Government Guaranteed	13.7%
NZ registered banks	83.2%
Local authorities	2.6%
Corporate bonds & SOEs	0.5%

Credit quality

AA	69.6%
A	30.4%

Top 5 issuers (% of fund)

Kiwibank	17.5%
Westpac Banking Corporation	16.9%
ASB	14.2%
New Zealand Government Departments	13.6%
ANZ	12.5%
Number of issuers in portfolio	**17**

Duration and yield

Duration	Fund 99 days versus benchmark 45days
Yield	Fund (gross) 2.85% versus benchmark 1.87% Fund* (net) 2.50% versus benchmark 1.87%

* After management fee, expenses and GST

Fund commentary

The Fund outperformed its benchmark over the month. The higher than benchmark portfolio yield was the main contributor and should lead to continued strong performance of the fund. Margins on 12-month term deposits remain attractive. Margins on A1 rated commercial paper have widened over the month, driven by an increase in issuance. The secondary market for short terms bonds has been very quiet, and margins have come in slightly adding to performance.

The Fund has held a long duration position for some time now, on the basis that we have not seen any urgent need for RBNZ to hike the OCR, and credit margins being attractive at the 1-year point of the interest rate curve. It is our expectation the RBNZ will maintain its recent projections regarding interest rate hikes starting in 2019.

Market commentary

The short end of the yield curve is upward sloping, indicating the market believes the rate cutting cycle has likely finished for now. The 90-day bill rate ended August unchanged at 1.96% and the 1-year swap rate was down 1 basis point to 2.02%.

In the August Monetary Policy Statement the RBNZ left the OCR unchanged at 1.75%. In its key forecast variables the RBNZ has the OCR on hold until mid-2019 as inflation slowly tracks back to the mid target of 2%. The short end of the curve barely moved over August. Going forward low inflation and the level of the NZD will act to impede a move higher in rates at the short end. The NZ dollar was down around 5% over August, but from a relatively high level due to recent US dollar weakness. The lower NZ dollar has not at this stage changed the market pricing for a rate hike, with a full hike priced in at the end of 2018, 6 months earlier than RBNZ forecasts. The housing market is slowing, and we are seeing tighter credit conditions via increased lending margins and a banking sector generally less willing to lend. New Zealand's economic expansion is ongoing, but at a slower pace.

Business confidence eased over August, but is still at elevated levels. Employment intentions are lower; this is likely a reflection of uncertainty around the upcoming election. We do not see the election as a big risk event, we are however mindful of costly election promises, and proposed policies to address the housing market, along with the downstream impact these may have on the government books, inflation and future direction of short term rates.

The fund has held a long duration position for some time now, on the basis that we have not seen any urgent need for a rise in the OCR, and credit margins being attractive at the 1 year point of the interest rate curve. It is our expectation that the RBNZ maintains its recent forecast regarding interest rate hikes starting in 2019.coupled with a slowing housing market and tighter credit conditions via increased lending margins, and stories of a banking sector less willing to lend, could lead one to believe that an easing bias is on the cards in the MPS. The NZ economy is however looking strong, expansion has slowed but is ongoing, and consumer and business confidence are still at elevated levels. The primary sector and dairy in particular are performing well and migration continues to hit new highs. The market is pricing a full 25 basis point hike by August 2018. This seems appropriate given the recent RBNZ message and the prospect for medium term inflation, however, the risk is that the timing of rate rises is pushed further out.