

# Nikko AM Wholesale Global Bond Fund

## Fund manager

Goldman Sachs Asset Management Australia Pty Ltd – via Nikko Asset Management New Zealand Limited.

In New Zealand we actively manage around NZ\$5 billion of investments for a diverse group of clients, including superannuation schemes, charitable trusts, KiwiSaver scheme providers, corporations and local government along with providing services to financial intermediaries through wrap platforms. We offer investment management services in domestic sectors (equities, fixed interest and cash) through our Auckland-based investment team and employ offshore managers to manage global sectors (global equities, global bonds and alternative investments).

Nikko AM NZ utilise Goldman Sachs Asset Management Australia Pty Ltd (GSAM) for the management of global fixed interest assets. Established in 1988, GSAM is one of the world's leading asset managers with AUD 1,126 billion in assets under management. GSAM's Global Fixed Income Team manages AUD451 billion of global fixed income assets.

## Fund launch

October 2008

## Investment objective

To construct a portfolio of authorised investments that outperform the Fund's benchmark return by 1.0% per annum over a rolling three year period before fees.

## Benchmark

Bloomberg Barclays Global Aggregate Index (100% hedged into NZD)

## Currency management

Foreign currency exposures created as a consequence of capital markets investment remain hedged to NZD within an operational range of 98.5% to 101.5%.

## Distributions

Generally on calendar quarters, or at any date for any period determined by the Manager.

## Structure and taxation

The Fund vehicle is a Portfolio Investment Entity (PIE) which is priced daily. Investors elect their own Prescribed Investor Rate. Information is provided to the IR and investors on an annual basis.

## Investment process

GSAM's investment philosophy and style is such that they aim to generate outperformance over time without being unduly exposed to one particular investment strategy or market circumstance. GSAM's global approach enables them to capture diverse sources of excess returns and their risk management process ensures the portfolio is not dependent on any particular market inefficiency that may dissipate. The GSAM global fixed interest portfolio is constructed in such a way that aims, over time, to react well to different economic conditions. The management of GSAM's global fixed interest portfolios is team-based with investment decisions taken collectively, following thorough discussion and debate. The investment process encompasses three key steps:

**Step 1:** Build a risk budget that takes account of the investment objectives, guidelines and benchmark of the mandate.

**Step 2:** Identify attractive investment opportunities and implement the best ideas from the specialist top down and bottom up investment strategy teams.

**Step 3:** Monitor risk and attribution to ensure risks are consistent with investment guidelines.

## Management fees

Investment management fees will be negotiated separately with each investor and invoiced outside the Fund. All Fund statutory and operating costs will be met directly by the Manager.

## Buy/sell spread

Nil

## Trustee

Public Trust

## Custodian

Public Trust as legal custodian, BNP Paribas Fund Services Australasia Pty Limited delegated as functional custodian.

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## Performance (NZD gross returns)

	Fund	Benchmark	Excess
1 month	0.69%	0.76%	-0.07%
3 months	1.68%	1.77%	-0.09%
6 months	0.59%	0.36%	0.23%
1 year	3.83%	3.07%	0.76%
2 years (pa)	5.10%	4.53%	0.58%
3 years (pa)	6.22%	6.37%	-0.14%
5 years (pa)	6.27%	6.12%	0.14%
10 years (pa)	7.36%	7.41%	-0.05%

## Fund size

NZ\$246 million

## Asset allocation

Credit quality rating	
AAA	38.1%
AA+, AA, AA-	13.5%
A+, A, A-	32.3%
BBB	15.9%
BB	0.2%

Sector	Fund	Index
Governments	37.3%	50.9%
Agency	7.7%	9.1%
Credit	19.8%	21.0%
Collateralised & MBS	35.7%	12.7%
Emerging market debt	2.6%	6.3%
Cash, derivatives, other	-3.1%	0.0%

## Duration and yield

Duration	Fund 6.57 years versus benchmark 6.80 years
Yield to Maturity	Fund 3.24% versus benchmark 2.93%

## Fund commentary

The fund underperformed its benchmark over the month of April. Duration strategy was the main detractor (-7bps) with cross-sector allocation a small detractor (2bps). Stock selection within the government sector and corporate sector added value, 3bps and 2bps respectively.

## Market commentary

Yields in major **government bond** markets declined in April, with US Treasuries outperforming sovereign bonds in the UK, Germany and Japan. Yields on the 10-year US government bond fluctuated intra-month, reaching a 2017 low of 2.18% on receding inflation expectations, but then rising on positive economic data including strong existing home sales. In Europe, the yield on the 10-year German government bond reached its lowest level this year ahead of the first round of voting in the French presidential election, and rose following the base case outcome to end the month relatively unchanged. The equivalent maturity French, Spanish and Italian government bond yields declined by 13bps, 2bps and 3bps, respectively, to 0.84%, 1.63% and 2.27%. The fund remains underweight US rates on the premise that the market is underpricing the pace of monetary tightening, particularly given strength in the labour market.

The Fed kept policy unchanged at its May meeting and appears to be looking through recent weakness in economic data, which it described as reflecting “transitory factors.” Supportive financial conditions will allow further rate hikes in the US this year. Meanwhile, GSAM expect the ECB and Bank of Japan (BoJ) to maintain low policy rates amid a weak core inflation backdrop, in part driven by low wage growth. The fund is neutral European and Japanese rates.

The fund is overweight rates in Australia and Europe versus the US based on divergent monetary policy outlooks. Near-term monetary tightening in Australia is not expected, due to low inflation and a lack of wage growth despite modest improvements in the labor market. In contrast, labor market strength in the US is expected to support wage inflation and consumption-led growth, thereby warranting monetary tightening. The fund is also underweight long-end UK rates versus European and Swedish rates. GSAM expect UK assets to weaken amid uncertain Brexit negotiations, while central banks in Europe and Sweden to maintain accommodative monetary policy.

**Agency mortgage-backed** securities (MBS) outperformed duration-neutral Treasuries by 2bps in April, supported by low interest rate volatility and increased demand from domestic commercial banks. Within agency MBS, Ginnie Mae mortgages underperformed conventional mortgages due to weak overseas demand. Federal Family Education Loan Program (FFELP) ABS spreads have tightened since the start of the year, benefiting from reduced uncertainty as rating agencies concluded their rating reviews of FFELP ABS securities. Moody's and Fitch respectively downgraded 7% and 21% of previously AAA-rated bonds to below investment grade.

Investment grade **corporate credit** strengthened modestly in April, with spreads on the Bloomberg Barclays Global Aggregate Corporates index tightening by 3bps to 117bps over sovereigns. Regionally, the euro area outperformed, with spreads on the Bloomberg Barclays Euro Aggregate Corporate index tightening by 7bps to 111bps over sovereigns. Factors supporting investment grade credit include improving corporate profit margins and a favorable global growth outlook. That being said, GSAM remain cautious due to stretched valuations, and credit-negative corporate behaviors such as increased leverage and share buybacks. GSAM are also alert to policy challenges in the US and political uncertainties in Europe and the UK. The fund is overweight US dollar-denominated credits, due to a positive near-term US growth outlook. The fund is underweight euro-denominated credits, in part due to excessive valuations stemming from the ECB's asset-buying program. Among sectors, GSAM see value in US banks, which may benefit from an unwind of regulations and rising US rates. For similar reasons the fund is overweight life insurance. GSAM are also constructive on Pipelines, which stand to benefit from a pick-up in US activity, while the fund is underweight the electric and telecom industries.

## Compliance

The Fund complied with its investment mandate during the month.