

# Nikko AM Wholesale Option Fund

## Fund manager

Nikko Asset Management New Zealand Limited (Nikko AM NZ).

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).

## Fund launch

April 2007 – a similar portfolio has been operated by Nikko AM since September 2003.

## Investment objective

To invest the portfolio in the authorised investments such that the portfolio earns a gross return of Bloomberg NZBond Bank Bill Index plus 4.0% per annum over a rolling three year period before fees.

## Benchmark

Bloomberg NZBond Bank Bill Index plus 4.0% per annum (from 1 July 2016)

## Investment process

The Fund invests into cash deposits and bank bills with highly rated financial institutions. The assets are then used as collateral security for derivatives, in particular, selling options on long-term NZ, US, UK, Euro bloc or Australian government stock.

Most options are written for one month and provide the institutional purchaser with a payout if interest rates move by more than a prescribed margin in one particular direction. The Fund earns a premium for writing (selling) the options. The Fund will write options on government bonds with maturities between 5 and 15 years.

## Structure

The Fund vehicle is a NZ domiciled 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.

## Distributions

Generally does not distribute but may do so at Nikko AM NZ's discretion.

## Currency management

All premium income is converted into NZD upon receipt and any currency margin deposits are hedged to NZD within an operational range of 98.5% to 101.5%.

## Management fees and other charges

Investment management fees and performance 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	1.63%	0.50%	1.13%
3 months	3.59%	1.49%	2.10%
6 months	-4.13%	3.06%	-7.19%
1 year	1.71%	6.40%	-4.68%
2 years (pa)	9.43%	6.84%	2.59%
3 years (pa)	8.64%	7.18%	1.46%
5 years (pa)	10.25%	7.06%	3.20%

\* S&P/NZX Bank Bills 90 Day Index plus 4.0% per annum prior to 1 July 2016

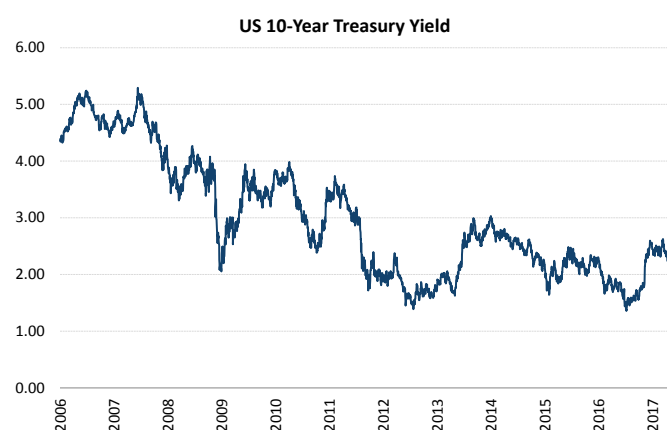
### Fund size

NZ\$180 million

### Compliance

The Fund complied with its investment mandate during the month.

### Treasury yield



### Fund Performance

The Option Fund returned 1.63% over April. The US 10-year Treasury Bond traded over a modest range moving between a high of 2.39% and an intraday low of 2.16%. The Fund benefitted from an increase in premium income in the week preceding the French Presidential election as the possibility of an unexpected result unsettled markets. Income levels fell away again as the result became known. The income the Fund receives from writing options on US Treasury bonds continues to be at the lower end of historical levels but should provide the basis for an acceptable level of returns over the months ahead.

### Market Commentary

Increased geopolitical risk, softer US data and investor anxiety ahead of the French election saw the US 10-year Treasury bond rate fall to a 2.16%, a fresh low for the year. The rate increased to 2.28% by month end as some uncertainties receded.

The month was an eventful one with the US bombing of a Syrian airfield being closely followed by Trump upping his rhetoric against North Korea. Market reactions to these events were short lived, however they remain a reminder of how quickly global conflicts can escalate. The two significant political events were; Prime Minister May announcing a UK snap election as the Conservative Party seeks to increase the size of its majority as the UK negotiates to leave the EU; and the first round of the French Presidential election being completed without further surprises.

The US market remained focused on the outlook for Fed policy. After a run of positive economic data the good news stalled with March CPI missing expectations to the downside and the core CPI showing its first monthly fall since 2010. This caused some to question the Fed's resolve to hike rates a further two times over the rest of the year however the Fed seems resolved to follow through with rate rises. Our view remains that it is unlikely that the full package of economic stimulation will be implemented by the Trump administration. If this is the case bond rates look to remain within recent trading ranges over the months ahead.