

Factsheet 30 September 2018

# NIKKO AM NZ BOND STRATEGY

Applies to: Nikko AM Wholesale NZ Bond Fund and Nikko AM NZ Bond Fund (retail)

## Market Overview

- NZ interest rates moved lower in yield over the quarter increasing bond returns.
- Local economic data showed some tentative rebound and was better than expected.
- The correlation between the NZ and US 10-year bond rates has been unusually low.

## Fund Highlights

- Credit was generally the best performing sector over the quarter.
- Shorter bonds outperformed longer maturities as interest rates moved higher.
- We have been buying bonds to maintain a higher yield when interest rates look attractive.

## Performance

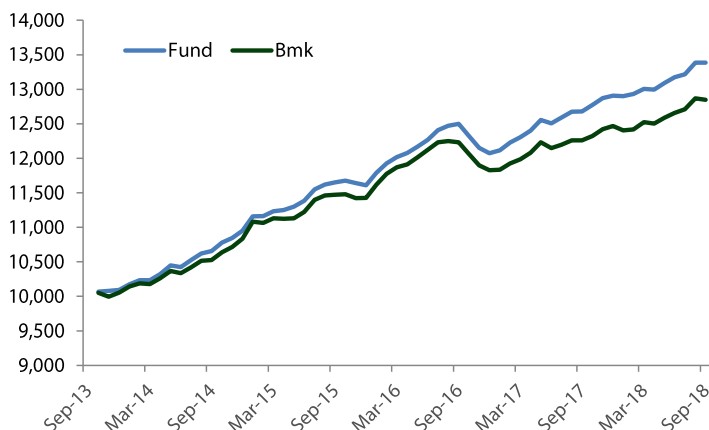
	One month	Three months	One year	Three years (p.a)	Five years (p.a)	Ten years (p.a)
Wholesale <sup>1</sup>	-0.01%	1.61%	5.57%	4.73%	6.00%	6.68%
Benchmark <sup>2</sup>	-0.15%	1.51%	4.79%	3.85%	5.14%	5.54%
Retail <sup>3</sup>	-0.08%	1.42%	4.81%	3.93%	5.14%	

1. Returns are before tax and before the deduction of fees

2. Benchmark: Bloomberg NZBond Govt 0+ Yr Index. No tax or fees.

3. Returns are before tax and after the deduction of fees and expenses and including tax credits (if any)

## Five Year Cumulative Performance<sup>1&2</sup>



## Portfolio Manager

**Fergus McDonald,**  
Head of Bonds and Currency



Fergus is responsible for the investment of the Bond, Cash and Currency mandates. Fergus has been actively involved in the NZ financial markets since 1981. The portfolio management team for the domestic fixed income funds includes Ian Bellew, Fixed Income Manager.

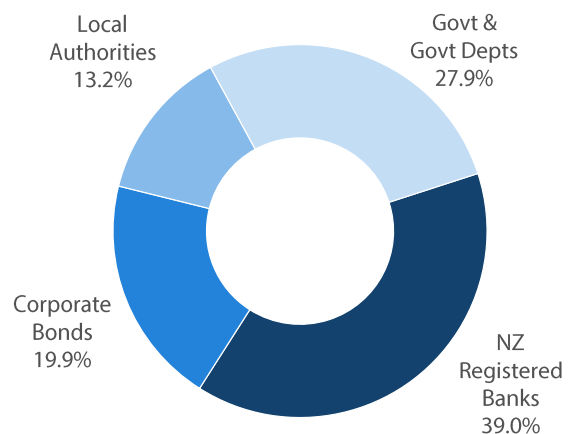
## Overview

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.

## Objective

The fund aims to outperform the benchmark return by 1.00% per annum before fees, expenses and taxes over a rolling three year period.

## Asset Allocation



Top 5 Corporate Issuers*	(%)	Credit Quality	(%)	Duration
Bank of New Zealand	7.99	AAA	15.0	Fund 4.42 years vs Benchmark 4.77 years
Local Government Funding Authority	7.66	AA	62.1	
Fonterra Cooperative Group	6.51	A	18.6	Yield Fund (gross) 2.93% vs Benchmark 2.09%
Westpac Banking Corporation	5.41	BBB	4.3	
ANZ Bank New Zealand	4.91			

\*excludes central government

## Market Commentary

NZ bonds had a weaker month as interest rates moved higher in yield, and consequently funds with shorter duration positioning performed better than longer duration positions. Following higher than expected Q2 GDP and an improvement in business confidence there was some pare back from the strong rally lower in interest rates in August. The size of the moves higher along the yield curve were around 6 to 9 basis points higher at month end. Shorter maturity bonds out to 1-year were little changed with the Reserve Bank reiterating a similar statement to the previous MPS that interest rates will most likely be on hold for some time and the next move could be either up or down.

Over the quarter there wasn't a large difference across the breakdown of bond sector returns. Credit holdings continued to perform well with the higher running yield, and the positive shape of the yield curve supportive of accrual trades. New bond issuance has been relatively limited, although there has been an increase in unrated bond deals which has been soaking up retail money, and may potentially reduce demand for new deals. The shape of the swap curve was little changed although there was some limited narrowing of swap margins. NZ Government bonds struggled performance wise - up until the end of the month when they recovered some losses rallying lower following strong demand in the Government bond tender.

The correlation between long maturity NZ bonds and US bonds has weakened considerably, although we haven't seen much demand reduction for NZ bonds yet even though NZ interest rates are well below the US. With the economies at different stages of the cycle local factors have become much stronger drivers in understanding the direction of our longer maturity interest rates. Volatility has remained muted in bond markets despite a reasonable amount of uncertainty with Trump policy, and trade tariffs etc.

## Fund Commentary

The fund outperformed the NZ government bond benchmark. The underweight duration positioning was a positive. Also the higher running yield and performance of the credit holdings helped the fund. We have been buying some longer maturity bonds on opportunities when yields have been higher to maintain a higher running yield on the portfolio and maintain duration. Maintaining a modest relative duration position and higher running yield through good quality credit should continue to add value while interest rates remain in a fairly modest range and the yield curve remains positively shaped.

## Key Fund Facts

<b>Distributions</b>		<b>Estimated annual fund charges</b>	
Wholesale fund:	Calendar quarter	Wholesale:	Negotiated outside of unit price
Retail fund:	Calendar quarter	Retail:	0.725%, refer PDS for more detail
<b>Hedging</b>		<b>Buy / Sell spread</b>	<b>Strategy size</b>
All investments will be in New Zealand dollars		0.00% / 0.00%	\$279.4m
			<b>Strategy Launch</b>
			October 2007

## Compliance

The Fund complied with its investment mandate and trust deed during the month.

## Contact Us

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