

Factsheet 31 August 2019

NIKKO AM NZ BOND STRATEGY

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

Market Overview

- NZ bond markets produced strong returns over August due to large falls in NZ interest rates.
- There were some significant moves lower in bond rates globally with negative news about slowing economic growth and increasing uncertainty around global trade dominating the direction of financial markets.
- The NZ Reserve Bank expressed their concerns around potential headwinds to growth, surprising the market with a 50 basis point cut in the cash rate taking it to a record low of 1%.

Fund Highlights

- NZ bonds delivered very strong returns as yields fell.
- The supply/demand dynamics remain supportive of credit holdings as investors seek yield.
- A higher running portfolio through holding quality credit continues to benefit the fund.

Performance

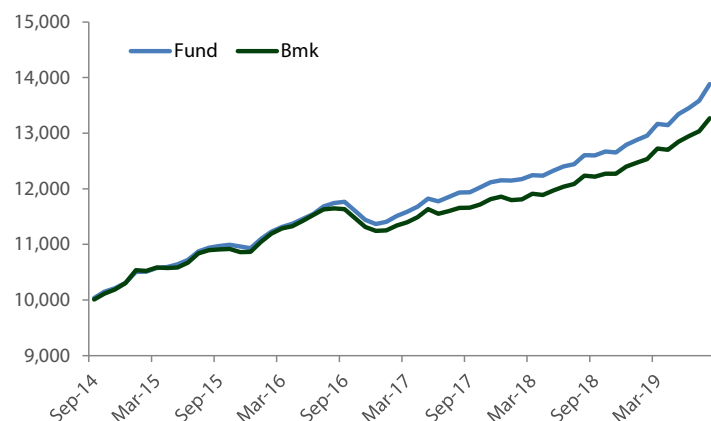
	One month	Three months	One year	Three years (p.a)	Five years (p.a)	Ten years (p.a)
Wholesale ¹	2.21%	4.04%	10.16%	5.74%	6.78%	7.08%
Benchmark ²	1.77%	3.29%	8.43%	4.43%	5.82%	5.74%
Retail ³	2.15%	3.84%	9.35%	4.98%	5.94%	

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

2. Current benchmark: Bloomberg NZBond Composite 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, \$10,000 invested^{1&2}



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 and Matthew Johnson, Fixed Income Manager.

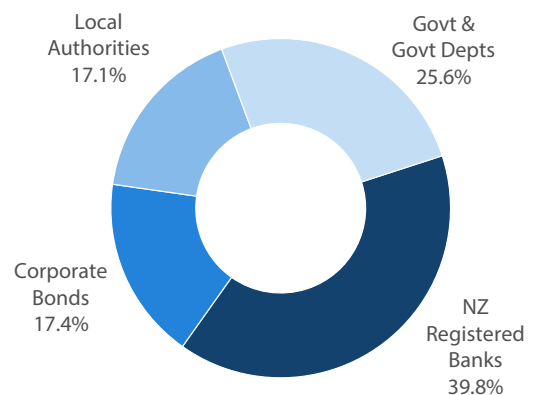
Overview

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 0.60% per annum before fees, expenses and taxes over a rolling three year period.

Asset Allocation



Top 5 Corporate Issuers*	(%)	Credit Quality	(%)	Duration
Local Government Funding Agency	10.75	AAA	12.67	Fund 5.07 years vs Benchmark 4.49 years
Bank of New Zealand	8.17	AA	61.80	
ANZ Bank New Zealand	5.96	A	20.87	Yield Fund (gross) 1.57% vs Benchmark 1.18%
Fonterra Co-Operative Group	5.44	BBB	4.65	
Westpac Banking Corporation	5.28			

*excludes central government

Market Commentary

NZ bond markets produced strong returns over August due to large falls in NZ interest rates. There were some significant moves lower in bond rates globally with negative news about slowing economic growth and increasing uncertainty around global trade dominating the direction of financial markets. During the month the US 10-year bond rate plummeted 50 basis points (bps) in 2 weeks and volatility spiked on geopolitical news. There is no doubt we are in unusual times with interest rates at record lows, and this has extended the search for yield across equities and other asset classes.

NZ government bond rates finished the month from 22 to 44 bps lower in yield across the curve with longer maturities falling more than shorter bonds. Swap rates outperformed similar maturities of government bonds falling an additional 2 to 5 bps reducing their spread above government bonds. There is now little slope or yield pickup along the government and swap yield curve apart from investing in credit. Credit was generally the best performing sector over the month, benefiting returns through a higher running yield and some credit margin contraction.

Locally the NZ Reserve Bank expressed its concerns around potential head winds to growth and took an activist approach surprising the market with a 50 basis point cut in the cash rate taking it to a record low of 1%. The RBNZ believes that if it acts earlier in providing stimulus this will hopefully encourage an upswing in spending and investment and will likely make any potential future dip in growth shallower. It also noted that monetary policy need friends and they would like the government to bring forward and increase spending to provide additional support to the economy. Although growth has slowed expectations are that NZ GDP will still be around the 2 to 2.5% range which isn't bad. While growth is below potential and inflation low, the bank appears to see little risk from adding stimulus to the economy sooner rather than later, we however expect the bank may pause before cutting interest rates further. We believe the prospect of NZ having negative interest rates remains a low probability at this stage.

Fund Commentary

The fund strongly outperformed the Bloomberg NZ Bond Composite benchmark over the month. A longer duration positioning, higher portfolio yield plus margin contraction on credit holdings added value to the portfolio as NZ interest rates fell markedly. We expect further modest declines in interest rates and our focus will be on maintaining a higher portfolio yield through buying quality non-government bond issues. We believe there are still some good opportunities to pick up yield through selling short to maturity bonds and investing longer in maturity along the credit curve.

Key Fund Facts

Distributions

Wholesale fund: Calendar quarter
Retail fund: Calendar quarter

Estimated annual fund charges (incl GST)

Wholesale: Negotiated outside of unit price
Retail: 0.74%, refer PDS for more detail

Hedging

All investments will be in New Zealand dollars

Buy / Sell spread

0.00% / 0.00%

Strategy size

\$346.71m

Strategy Launch

October 2007

Compliance

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

Contact Us

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