

Factsheet 31 January 2020

# NIKKO AM NZ INCOME STRATEGY

Applies to: Nikko AM Income Fund (retail).

## Market Overview

- A 'flight to safety' saw significant falls in global bond yield with the US 10-year bonds falling.
- Concern over the coronavirus in China and what impact that could have on economic activity and world growth completely dominated market sentiment, resulting in a large reversal lower in bonds yields over the end of January.
- Markets are already pricing in a fall in economic growth mainly resulting from lower service sector activity and also from lower trade and tourism numbers, however this pricing could be reversed if the worst fears of the spread of the virus do not materialise.

## Fund Highlights

- The Fund underperformed its benchmark this month.
- The Option Fund posted a negative return over the month as bond yields dropped significantly as the implications of the coronavirus became more apparent.
- The Corporate Bond fund outperformed its benchmark over the month. A higher running yield through holding quality credit should continue to benefit the fund.

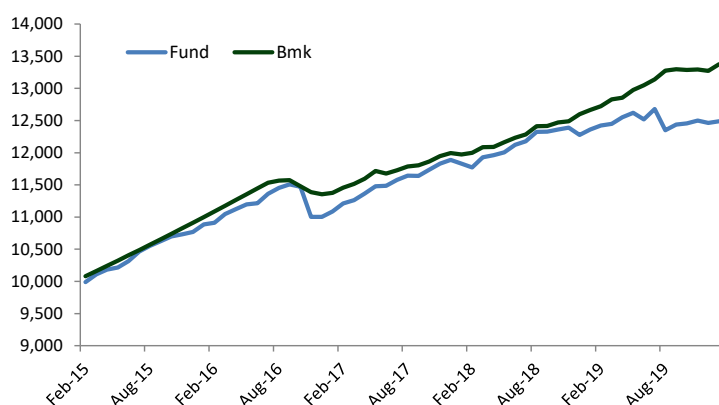
## Performance

	One month	Three months	One year	Three years (p.a)	Five years (p.a)	Ten years (p.a)
Retail <sup>1</sup>	0.19%	0.27%	1.04%	4.04%	4.55%	5.78%
Benchmark <sup>2</sup>	0.79%	0.67%	5.63%	5.54%	5.99%	7.98%

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

2. Current benchmark: Composite of (from 1 July 2016) of 70% Bloomberg NZBond Credit 0+ Yr Index and 30% Bloomberg NZ Bond Bank Bill Index plus 4%pa. No tax or fees.

## Five Year Cumulative Performance, \$10,000 invested<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 and Matthew Johnson, Fixed Income Manager.

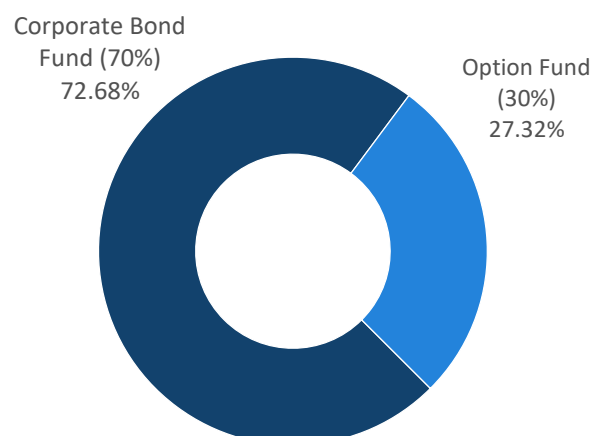
## Overview

The strategy aims to provide investors with regular income from an actively managed investment portfolio while protecting the capital value of investors' funds.

## Objective

From 01 January 2020 the objective of this fund is to outperform the RBNZ Official Cash Rate by 2.50% p.a. over a rolling three year period before fees, expenses and taxes.

## Asset Allocation



Top 5 Issuers*	(%)	Credit Quality*	(%)	Yield – Corporate Bond Fund
ASB New Zealand	11.51	AAA	1.25	Fund (gross) 2.21% vs Benchmark 1.84%
Westpac New Zealand	11.29	AA	51.78	
Kiwibank	7.81	A	25.34	
Bank of New Zealand	7.02	BBB	18.55	
ANZ Bank New Zealand	6.44	Collateral & options & NR	3.08	

\*Aggregation of Option and Corporate Bond Funds

## Option Fund Commentary

A ‘flight to safety’ saw significant falls in global bond yield with the US 10-year bonds falling from a high point of 1.94% before closing at the monthly low of 1.51%. The lasting impact the coronavirus will have on economic activity is unknown and this uncertainty is reflected in lower global interest rates and share markets. Markets are already pricing in a fall in economic growth mainly resulting from lower service sector activity and also from lower trade and tourism numbers, however this pricing could be reversed if the worst fears of the spread of the virus do not materialise.

Federal Reserve Chairman Jerome Powell commented that the outbreak of the coronavirus will likely hit the Chinese economy and could spill wider, but it was too early to judge what impact it would have on the US.

Against the backdrop of the widening virus crisis the Fed kept its key interest rate unchanged and continued to signal monetary policy would stay on hold for the time being while also stressing the need for US inflation to reach 2%. Officials kept the target range of the benchmark federal funds rate at 1.5% to 1.75% and called the stance appropriate to support sustained expansion of economic activity. The market is currently pricing in that the Fed will need to cut at least once in 2020 especially if the coronavirus takes hold outside of China. The stable to lower outlook for short term interest rates is likely to limit any sustained movement in longer term interest rates. If current levels of volatility are maintained, income generated by the fund should remain at satisfactory levels. The speed and magnitude of yield changes in the US 10-year Treasury bond will continue to determine the total return of the fund in the months ahead.

The fund posted a negative return over the month as bond yields dropped significantly as the implications of the coronavirus became more apparent. Bond yields traded through a number of call option strikes and volatility increased. Income levels generated from selling options increased over the past month and year. It remains above its medium term average as a result of greater volatility in Treasury bond interest rates and uncertainty pervading financial markets. If volatility remains elevated for an extended period the income generating potential of the fund looks attractive but as mentioned above the frequency and cost of options being struck will also determine the total return of the fund.

## Corporate Bond Fund Commentary

The fund outperformed the Bloomberg NZ Bond Credit benchmark over the month. The longer duration positioning, and yield curve positioning were the main contributors to outperformance. We will continue to focus on maintaining a higher portfolio yield through buying quality non-government bond issues. We expect credit to remain well supported with a shortage of supply to market.

## Key Fund Facts

<b>Distributions</b>	<b>Estimated annual fund charges (incl. GST)</b>		
Retail fund: Calendar quarter	Retail fund: 1.07%, refer PDS for more details		
<b>Hedging</b>	<b>Buy / Sell spread:</b>	<b>Strategy size</b>	<b>Strategy Launch</b>
All investments will be in New Zealand dollars	0.0% / 0.0%	\$12.8m	October 2007

## Compliance

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

## Contact Us

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