

NIKKO AM NZ BOND STRATEGY

Assets are held in the Nikko AM Wholesale NZ Bond Fund. The Nikko AM NZ Bond Fund (retail) invest in units in the wholesale fund, which the commentary refers to.

Market Overview

- The returns from NZ bonds were strong over the month as interest rates moved much lower in yield.
- Market sentiment was negative on concerns about coronavirus.
- In contrast, on a positive note economic data has generally been improving with monetary and fiscal stimulus adding to the prospects for a pick-up in activity for 2020.

Fund Highlights

- The fund outperformed its benchmark over the month.
- Credit margin dynamics look supportive with a shortage of supply.
- A higher running yield through holding quality credit should continue to benefit the fund.

Performance

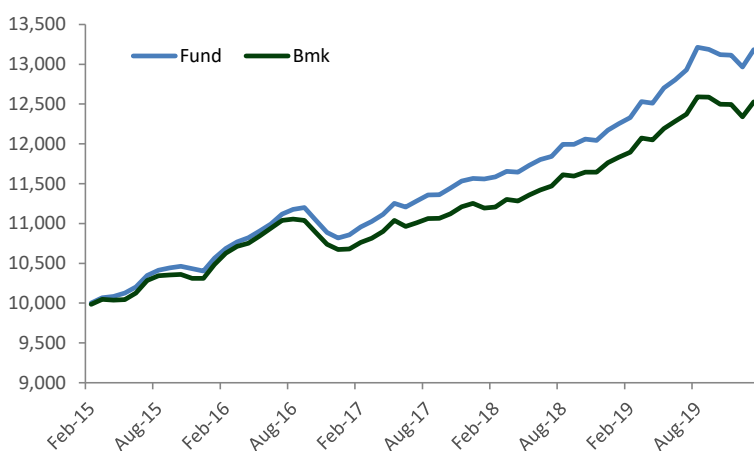
	One month	Three months	One year	Three years (p.a)	Five years (p.a)	Ten years (p.a)
Wholesale ¹	1.70%	0.48%	7.59%	6.69%	5.68%	6.71%
Benchmark ²	1.52%	0.24%	5.87%	5.47%	4.61%	5.41%
Retail ³	1.63%	0.29%	6.79%	5.91%	4.86%	

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.

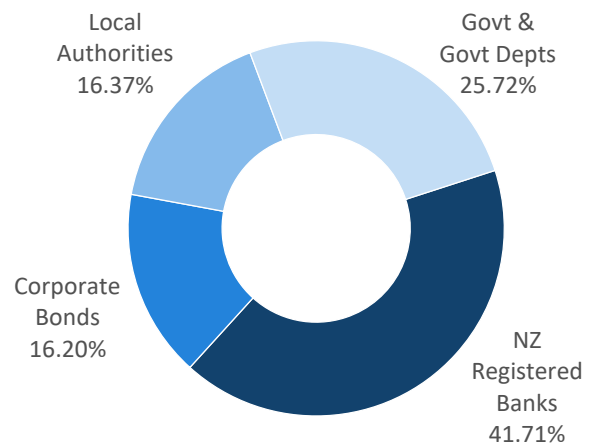
Overview

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
NZ Local Govt. Fund Agency	11.35%	AAA	12.46%	Fund 4.97 years vs Benchmark 4.39 years
Westpac New Zealand	7.11%	AA	60.66%	
Bank Of New Zealand	6.79%	A	22.43%	Yield
Fonterra Cooperative Group	5.67%	BBB	4.45%	Fund (gross) 1.74% vs Benchmark 1.41%
ANZ Bank New Zealand	5.28%			

*excludes central government

Market Commentary

The returns from NZ bonds were strong over the month as interest rates moved much lower in yield. The positive contribution from duration was the primary driver of returns as NZ yields unwound the move higher in yields that occurred at year end 2019. It would be fair to say the markets focus is currently on the negative. Concern over the coronavirus in China and what impact that could have on economic activity dominated market sentiment, resulting in lower bond yields by the end of January. There remains a considerable amount of uncertainty about what the impact of the virus will be, and the market typically isn't very good at handicapping events with open ended risks.

In contrast, on a positive note economic data has generally been improving with monetary and fiscal stimulus adding to the prospects for a pick-up in activity for 2020. Both NZ GDP and inflation data were stronger than the markets and RBNZ's expectations. Annual inflation is now at 1.9% and near the midpoint of the target band and house prices look to be rising. Additionally sentiment factors had been improving with Brexit and US/China trade tensions relaxing, and in NZ business and consumer confidence have also tentatively improved. Late last year market expectations were generally for the RBNZ to be leave rates on hold and yield curves to steepen as the economy improved.

Over the month the NZ 10-year government bond fell by 34 basis points (bps) to 1.30% and the longer maturity 2037 bond by 43 bps to 1.67%, the US 10-year bond fell by 41 bps to 1.51%. Shorter duration bonds underperformed longer maturity bonds as they had smaller moves lower in yield and the impact of falling yields is also less for shorter duration assets. On a sector basis both inflation linked and nominal Government bonds performed well. The swap curve flattened with the spread between 2 and 10-year rates declining from 52 to 31 bps. Overall Swap rates performed in line with similar maturities of government bonds. Corporate bonds continued to perform well as margins remain supported by a lack of supply and continuing demand. Bond Portfolios that had a longer duration had a good start to the year recovering from the sell-off in December. Interest rate markets have remained reasonably volatile over the past months, although as expected short bond maturities have remained more anchored by expectations for cash rates to stay low. Longer term bond rates will likely continue to be more influenced by the direction of offshore bonds. In a low yield environment the direction of interest rates and subsequent gain or loss from duration tends to more heavily dominate the return in comparison to other return drivers such as yield.

Fund Commentary

The fund outperformed its benchmark over the month. The main positives were the longer duration and yield curve positioning, also supported by higher yield from credit and some margin contraction. 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

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

\$347.4m

Strategy Launch

October 2007

Compliance

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

Contact Us

www.nikkoam.co.nz | nzenquiries@nikkoam.com

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