Factsheet 31 January 2020

NIKKO AM NZ CASH STRATEGY

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

Market Overview

- Fear increased as the Coronavirus outbreak developed across the month. A resulting rally in bonds occurred with significant reductions in yields seen for longer bonds however thus far bank bill rates have remained relatively unaffected ending January at similar levels to where they started.
- 4Q19 Inflation came in slightly stronger than expected at 0.5% bringing annual inflation to 1.9% just shy of the RBNZs 2% target midpoint.
- China is an increasingly important trading partner for New Zealand. Should the Coronavirus outbreak intensify NZ could be affected through a number of channels notably tourism, education services and export of commodities.

Fund Highlights

- The fund continues to perform well, benefiting from a higher yield than its benchmark.
- We favour investing in one-year maturities as they continue to provide the highest returns. The fund has been positioned longer than its benchmark resulting in performance benefits following OCR rate cuts.
- Returns will likely reduce over coming months as longer dated securities mature and the proceeds are reinvested at current market rates.

Performance

	One month	Three months	One year	Three years (p.a)	Five years (p.a)	Ten years (p.a)
Wholesale[1]	0.19%	0.54%	2.63%	2.83%	3.14%	3.66%
Benchmark[2]	0.11%	0.29%	1.56%	1.83%	2.24%	2.59%
Retail[3]	0.15%	0.44%	2.24%	2.45%	2.76%	
KiwiSaver[3]	0.15%	0.42%	2.45%			

1. Returns are before tax and before the deduction of fees.
2. Benchmark: Bloomberg NZBond Bank Bill Index. No tax or fees.
3. Returns are before tax and after the deduction of fees and expenses and including tax credits (if any).

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.

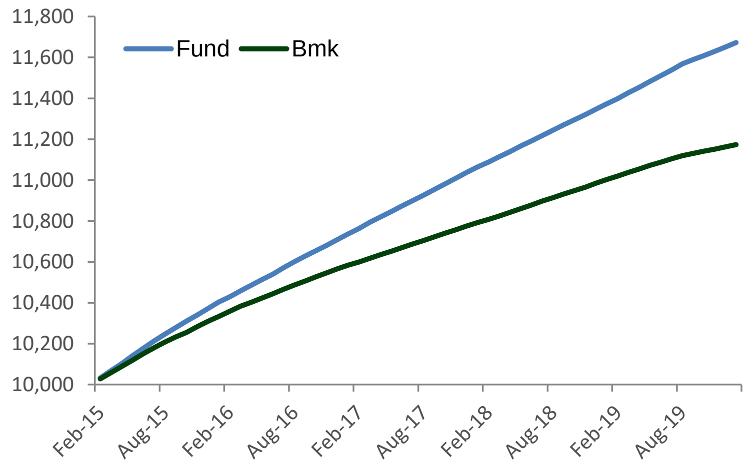
Overview

The strategy aims to generate income by constructing an actively managed investment portfolio of short-term deposits and bonds whilst preserving capital value.

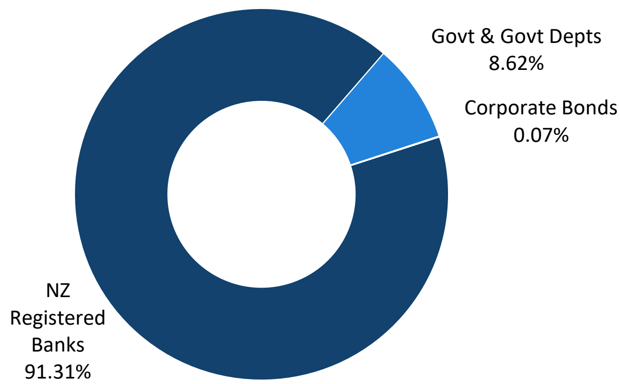
Objective

The fund aims to outperform the benchmark return by 0.20% per annum before fees, expenses and taxes over a rolling three year period.

Five Year Cumulative Performance, $10,000 invested[1, 2]



Asset Allocation



Top 5 Issuers	(%)
Westpac New Zealand	22.26
Kiwibank	19.26
ASB Bank	10.47
Rabobank	7.40
Bank of New Zealand	6.88

Credit Quality	(%)
AAA	-
AA	60.31
A	39.69
BBB	-

Duration
Fund 83 days vs Benchmark 45 days

Yield
Fund (gross) 2.22% vs Benchmark 1.20%

Market Commentary

The interest rate markets were primarily focused on developments around the Coronavirus “2019-nCov” outbreak in China. As the month progressed it became increasingly apparent that an outbreak had occurred. Unsurprisingly the market has looked to previous viral outbreaks to draw inferences on the potential human and economic costs with the more recent viral outbreaks SARS (2003), H1N1 (2009) and MERS (2012) featuring in the media and commentaries.

Notable observations include:

- When the SARS outbreak occurred in 2003, China’s GDP was only 4% of the global total – today it sits at 17%. The economic potential impact on the world’s economy will be larger than SARS particularly if the outbreak intensifies.
- The scale of policy response in China is remarkable with restrictions on travel and quarantine on a province of 11 million people. A similar response would be difficult to execute in the Western world.
- 2019-nCov has a low infection rate with a R0 (number of people, on average, each infected person goes on to infect) estimated at between 2 and 2.5, this is higher than the common cold at ~1.3 but lower than SARS estimated between 2 and 5.
- 2019-nCov has a low fatality rate ~2% which will likely fall as generally the more severe cases are identified at the start of an outbreak.

We can draw some comfort from the features of the virus and the strong policy response. The most important areas of risk to New Zealand’s economy are in our exposure to China through export of commodities and in domestic services we provide including tourism and educational services. It is important to note New Zealand’s exposure to China in these areas is significantly higher than during the SARS outbreak of 2003. This can be seen in the massive increase in the proportion of New Zealand’s commodity exports going into China. Prominent amongst these are: Forestry increasing 5x to 46.1%, Beef increasing 137x to 46.1%; Sheep meat increasing 18x to 41.6%; Seafood increasing 9x to 35.2% and Dairy increasing 6x to 32.5%. In relation to tourism we note Chinese visitors account for 10% of all arrivals (3% in 2003) and their associated spend on travel services is estimated to account for ~1% of NZs nominal GDP. In the event of a more mild play out of the Coronavirus we expect a limited temporary impact with growth returning as the outbreak is brought under control. We would expect the Reserve Bank to look through any impacts on growth, employment and inflation in this scenario. Should the outbreak intensify in its severity and geographic dispersion, the impact would be larger and a policy response may be elicited from the Reserve Bank.

Fund Commentary

The fund continued to outperform its benchmark returning 0.19% vs 0.11%. With short term rates relatively unchanged across the month a higher portfolio yield positively contributed to January’s return.

Over time we expect a longer duration with its associated pickup in yield to positively contribute to performance. We continue to favour holding term deposits up to one year in maturity as they offer superior relative returns and will perform well if interest rates fall further. Liquidity is actively managed by ensuring a significant proportion of the fund is in readily marketable securities in high credit quality names and by staggering term deposit maturities.

Key Fund Facts

Distributions

Wholesale fund:	Calendar quarter
Retail fund:	Calendar quarter
KiwiSaver fund:	Does not distribute

Estimated annual fund charges (incl. GST)

Wholesale:	Negotiated outside of unit price
Retail:	0.35%, refer PDS for more details
KiwiSaver:	0.46%, refer PDS for more details

Hedging	Buy / Sell spread	Strategy size	Strategy Launch
All investments will be in New Zealand dollars	0.00% / 0.00	$820.5m	October 2007

Compliance

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

Contact Us

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