Factsheet 29 February 2020

NIKKO AM GLOBAL BOND STRATEGY

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

Market Overview (source: GSAM)

- Fixed income markets experienced volatility at the end of February as risk-off investor sentiment resurfaced following an uptick in coronavirus cases outside of China, which continues to unnerve markets this month. In response, rates have rallied, with the 10-year US Treasury yield falling to a new low.
- The coronavirus poses potential near-term downside risks which may be cushioned by a global policy easing campaign.
- Adding to recent market volatility, oil prices declined sharply following a dispute between OPEC and Russia at the March 5-6 OPEC+ Meeting, which led Saudi Arabia to lower the relative price at which it sells crude oil. Risk sentiment and in turn risk asset performance—including corporate credit and equities—continues to fluctuate around economic uncertainty, policy reassurances, and lower oil prices.

Fund Highlights

- The portfolio underperformed its benchmark in February.
- Securitised (6bps) and Corporate (6bps) strategies were the largest contributors in February.
- Cross sector (-15bps), Duration (-4bps), Currency (-4bps) and Residual (-3bps) strategies detracted from performance.

Performance

	One month	Three months	One year	Three years (p.a.)	Five years (p.a.)	Ten years (p.a.)
Wholesale[1]	1.12%	3.02%	11.28%	5.97%	5.59%	6.61%
Benchmark[2]	1.23%	2.84%	9.67%	5.23%	4.92%	6.18%
Retail[3]	0.82%	2.31%	9.79%	4.82%	4.49%	

1. Returns are before tax and before the deduction of fees. Based on actual calendar periods.
2. Benchmark: Bloomberg Barclays Global Aggregate Index, hedged into NZD. No tax or fees.
3. Returns are before tax and after the deduction of fees and expenses and including tax credits (if any). Based on change in unit price.

Investment Manager

Nikko AM NZ uses Goldman Sachs Asset Management Australia Pty Ltd (GSAM) for the management of global fixed interest assets. Established in 1988, GSAM is one of the world's leading asset managers. GSAM's Global Fixed Income Team manages over US$525 billion of global fixed income and currency assets.

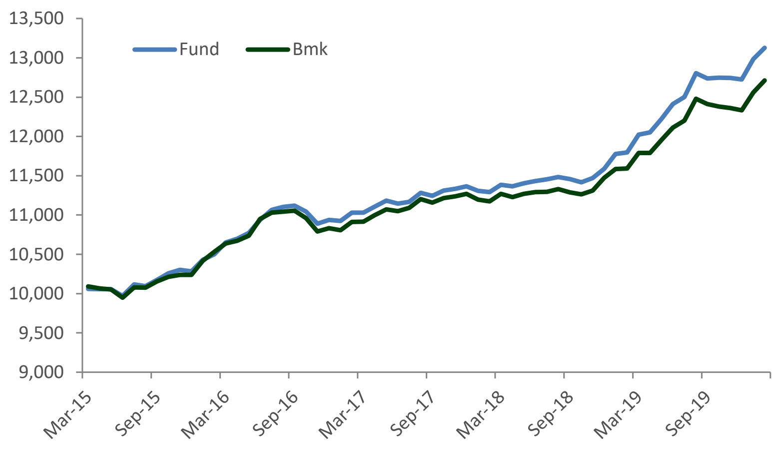
Overview

The Strategy aims to provide investors with regular income by constructing an actively managed investment portfolio of permitted investments, with the potential for capital gain from global fixed interest markets.

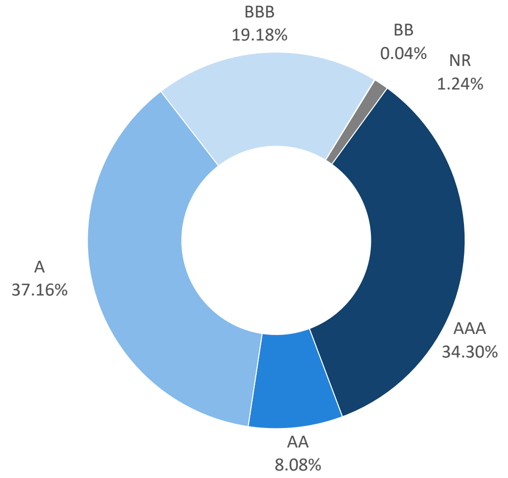
Objective

The Strategy aims to outperform the benchmark return by 1% per annum before fees, expenses and taxes over a rolling three year period.

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



Credit Quality



Sector Allocation (% of fund)	Fund	Index
Governments	28.63%	49.04%
Agency	4.51%	8.08%
Collateralised & MBS	38.57%	11.73%
Credit	31.31%	20.71%
Emerging market debt	8.76%	10.44%
Cash, derivatives, other	-11.78%	0.00%

Duration
Fund 6.72 years vs Benchmark 7.13 years

Yield to Maturity
Fund (gross) 1.92% vs Benchmark 1.34%

Market Commentary (source: GSAM)

Over the month of February, global rates rallied as risk-off sentiment resurfaced following an uptick in coronavirus cases outside of China. US rates outperformed amid a flight-to-quality market mode, with the US 10-year Treasury falling to a record low. In the UK, Gilt yields initially rose in February due to increased expectations for fiscal expansion but this reversed towards the end of the month as a result of risk-off sentiment that led to the decline in sovereign bond yields globally. More recently, the Fed lowered its policy rate by 50bps to 1-1.25% citing "evolving risks" to economic activity from the coronavirus. Among other G10 central banks, RBA and BoC also lowered their policy rates in response to the uncertain evolution of the coronavirus and its potential economic ramifications. Interest rates continued to decline, particularly in the US, in early March.

The Bloomberg Barclays US Mortgage Backed Securities (MBS) Index returned 1.04% in February. Agency MBS underperformed US Treasuries as rates reached all-time lows. The rally in rates reignited concerns around prepayment activity. A spike in market volatility and elevated MBS supply also weighed on the sector. Ginnie Mae MBS prepayment speeds continue to be elevated. We believe recently issued Ginnie Mae MBS are most vulnerable to refinancing as they approach the peak of prepayment risk relative to higher coupons.

The Barclays US High Yield 2% Issuer Cap Index delivered a total return of -1.41% in February with option adjusted spreads widening 110bps to 500bps over Treasuries. February marked the worst monthly total return for US high yield corporate credit since December 2018 as risk-off market sentiment resurfaced.

Investment grade corporate credit weakened in February as spreads on the Bloomberg Barclays Global Aggregate Corporate Index widened 20bps to 123bps over sovereigns. Risk sentiment was challenged by concerns of a potential global growth slowdown as the coronavirus showed increasing signs of spreading outside China.

Fund Commentary (source: GSAM)

The portfolio underperformed its benchmark in February. Our Securitised (6 basis points) and Corporate (6bps) strategies were the largest contributors to performance over the month, while Cross sector (-15bps), Duration (-4bps), Currency (-4bps) and Residual (-3bps) strategies detracted from value.

We remain overweight investment grade corporate credit and continue to see value in holding credit risk balanced with long exposure to rates, particularly given recent underperformance in the asset class. We have not made significant positioning changes to investment grade credit portfolios in light of the most recent episode of market volatility related to coronavirus.

We reduced our overweight exposure to agency MBS over the month as we believe the market is still under-pricing prepayment risks. Our coupon selection continues to favor discount coupon MBS which we perceive to be relatively isolated from prepayment risk. We believe prepayment speeds of higher coupon MBS should continue to slow as they move past the peak of the prepayment ramp. In the securitized credit space, we have been adding exposure to collateralized loan obligations (CLO).

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: 0.90%, refer PDS for more details

Hedging

All investments will be hedged to New Zealand dollars within an operational range of 98.5% - 101.5%.

Buy / Sell spread

0.00% / 0.00%

Strategy size

$339.87m

Strategy Launch

October 2008

Exclusions: Investments in tobacco manufacturers and 'controversial weapons'.

Compliance

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

Contact Us

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