Factsheet 30 April 2020

NIKKO AM NZ INCOME STRATEGY

Applies to: Nikko AM Income Fund (retail).

Market Overview

- Interest rates on US 10-year Treasury bonds traded in a more modest range than we have seen in recent months as the initial reaction to the economic shock caused by COVID-19 subsided.
- Markets continue to be focused on the economic and financial market impact of COVID-19. The impacts have been greater than anticipated, as has the governmental and central bank response.
- Bond and equity prices recovered strongly as buyers returned to the market - bargain hunting assets which had become cheaper following the March sell-off.
- NZ interest rates fell to record lows, supported by the Reserve Bank bond buying programs.

Fund Highlights

- The fund returned 2.8% in April, 1% ahead of its benchmark.
- The Option Fund posted a positive return over April after some months of disappointing returns. Bond yields dropped to record lows in March but financial markets have subsequently been calmed by significant central bank and governmental support.
- The Corporate Bond Fund outperformed its benchmark over the month. The recovery of credit margins, longer duration positioning, and yield curve positioning were all contributors to outperformance as yields fell to record lows.

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

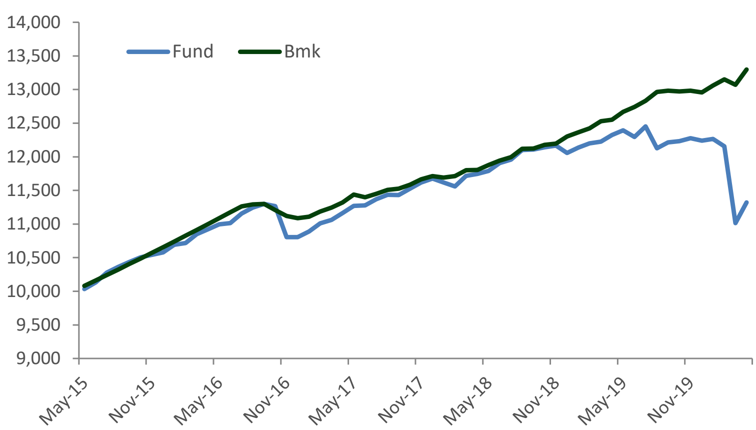
From 01 January 2020 the objective of this fund is to outperform the RBNZ Official Cash Rate by 2.50% p.a. over a rolling three year period before fees, expenses and taxes.

Performance

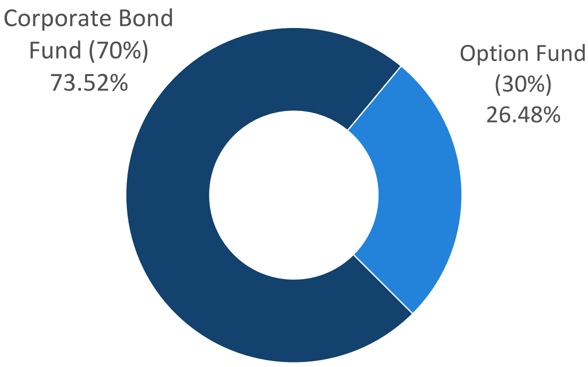
	One month	Three months	One year	Three years (p.a)	Five years (p.a)	Ten years (p.a)
Retail[1]	2.79%	-7.68%	-8.13%	0.48%	2.52%	4.71%
Benchmark[2]	1.72%	1.80%	5.94%	5.51%	5.86%	7.91%

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[1,2]



Asset Allocation



Top 5 Issuers*	(%)
Westpac New Zealand	18.76
Kiwibank	6.80
ASB New Zealand	6.69
ANZ New Zealand	5.90
NZ Local Govt Fund Agency	5.67

Credit Quality*	(%)
AAA	1.19
AA	43.51
A	29.85
BBB	19.27
Collateral & options & NR	6.18

Yield – Corporate Bond Fund
Fund (gross) 1.90% vs Benchmark 1.28%

*Aggregation of Option and Corporate Bond Funds

Option Fund Commentary

The fund posted a positive return over April after some months of disappointing returns. Bond yields dropped to record lows in March but financial markets have since been calmed by significant Central Bank and Governmental support. Large government stimulus packages will need to be funded and the first port of call is to issue more bonds. The question of who would buy all these new bond was answered when central banks embarked on a range of new Quantitative Easing programmes which include large scale bond purchase schemes. Investor nerves were soothed by the large step up in Quantitative Easing programmes around the globe resulting in less volatile and stressed markets over April.

Federal Reserve Chairman Jerome Powell said the coronavirus has brought the economy to an abrupt halt and it was uncertain how long the slowdown would last. The Fed held rates near zero and has pledged to keep them there until the nation was back on track. He went on to say that the economy may need more support from all of us if the recovery is to be a robust one. He emphasised several times the importance of fiscal policy to help what central banks are doing and highlighted the plight of those who are losing their jobs. Recent US labour data indicated a jobless rate of 22%, this is the worst since the Great Depression and more than twice the 10% peak seen in 2009. With the labour market hurting this badly it is difficult to see a time when the Fed will start to reverse their low interest rate stance. With volatility reducing from the extreme levels seen in prior months the fund returned to a more normal level of return.

The precise impact COVID-19 will have on economic activity is unknown, what we do know at this stage is the impact will be large and unfavourable. Even though governments and central banks are providing unprecedented levels of stimulus and support it is unlikely economic activity will return to pre-virus levels quickly. In this environment interest rates are expected to stay low.

Income levels generated from selling options has increased over the past few months .The income earning capacity of the fund remains well above its medium term average as a result of greater volatility in Treasury bond interest rates and uncertainty pervading financial markets. This elevated income will over time help restore the value of the fund. If volatility remains elevated for an extended period the income generating potential of the fund looks attractive however the frequency and cost of options being struck will also determine the total return.

Corporate Bond Fund Commentary

The fund outperformed its benchmark over the month. The recovery of credit margins, longer duration positioning, and yield curve positioning were all contributors to outperformance as yields fell to record lows. Credit in general outperformed similar maturities of governments and swap as margins contracted significantly. Contributing to the fund's return were the addition of quality credit at cheaper levels and an extended duration. We will continue to focus on maintaining a higher portfolio yield through buying quality non-government bond issues. The credit quality of the fund remains strong. Over the medium term it is likely returns will be supported by a higher yield, and some further improvement in credit margins.

Key Fund Facts

Distributions

Retail fund: Calendar quarter

Estimated annual fund charges (incl. GST)

Retail fund: 1.07%, refer PDS for more details

Hedging

All investments will be in New Zealand dollars

Buy / Sell spread:

Click to view

Strategy size

$4.0m

Strategy Launch

October 2007

Compliance

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

Contact Us

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