

NIKKO AM NZ CORPORATE BOND STRATEGY

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

Market Overview

- Credit performed well as margins narrowed with NZ bond supply remaining limited.
- NZ interest rates continued to make new record lows, up until a late reversal higher in yields at month end left rates little changed over May.
- Central banks and governments have taken unprecedented actions to try and reduce the negative economic impacts of lock-downs, and confidence has recovered, however there remains considerable uncertainty about the extent of the recovery.

Fund Highlights

- The fund returns were positive for the month with interest rates little changed.
- Credit holdings in general have recovered their lost value plus some post the expansion in credit margins experienced through March.
- The fund has benefited from buying cheaper assets at distressed prices and extending duration through late March and April.

Performance

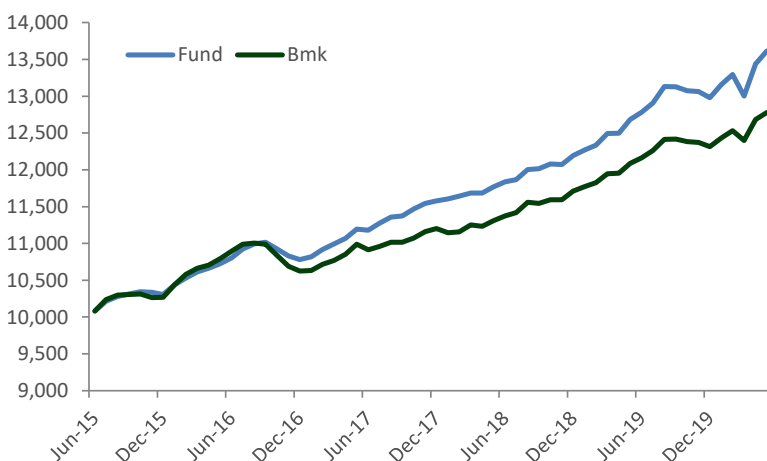
	One month	Three months	One year	Three years (p.a)	Five years (p.a)	Ten years (p.a)
Wholesale ¹	1.28%	2.38%	7.33%	6.73%	6.36%	7.07%
Benchmark ²	0.77%	1.98%	5.73%	5.16%	5.03%	5.37%
Retail ³	1.71%	2.16%	6.48%	5.89%	5.51%	6.17%
KiwiSaver ³	1.70%	2.14%	6.72%			

1. Returns are before tax and before the deduction of fees.

2. Current benchmark: Bloomberg NZBond Credit 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.

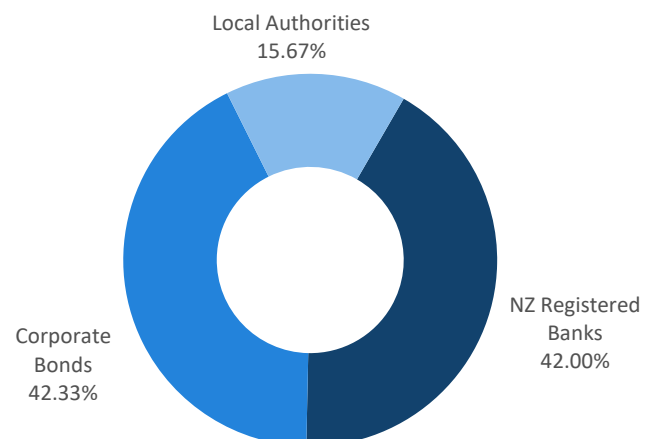
Overview

The strategy aims to generate 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 0.70% per annum before fees, expenses and taxes over a rolling three year period.

Asset Allocation



Top 5 Corporate Issuers	%	Credit Quality (% of fund)	%	Duration
NZ Local Govt Fund Agency	7.06	AAA	1.67	Fund 3.89 years vs Benchmark 3.06 years
Westpac New Zealand Ltd	7.01	AA	41.24	
Fonterra Cooperative Group	5.96	A	30.08	Yield
Bank of New Zealand	5.81	BBB	25.57	
ANZ Bank New Zealand Ltd	5.24	BB	1.44	

Market Commentary

Over the month NZ interest rates finished little changed, and credit continued to perform strongly, as NZ bond supply remained limited and confidence returned to financial markets. The language and actions from Central banks and Governments remain very supportive and financial market asset values have rebounded strongly as buyers have been active in the market. The main driver of returns was the strong performance from credit holdings. NZ interest rates did make new record lows in May, however this was largely reversed by month end as interest rates rebounded higher in yield by 20 to 30 basis points (bps) to finish little changed.

In general credit margins are now narrower than pre-COVID levels as demand has been strong to buy bonds with falling interest rates and investors seeking yield. At the same time that demand has been strong, supply in the NZ bond market has been very limited, and at this stage the supply pipeline of NZ issuers remains negligible.

NZ government bond rates were little changed over the month, the 1-year government bond fell by 3 bps, the 5-year increased 7 bps, and 10-year finished 4 bps lower. Performance across the different sectors of the NZ bond market was more evenly balanced between governments and swaps, with swap spreads contracting slightly and subsequently the better performer. As mentioned above credit was the star performer, for example 5-year senior bank debt in NZ was marked at a credit margin of around 85 bps pre-COVID and traded in excess of 200 bps during March, at the end of April margins were back around 110 bps, and by the end of May margins were 80 bps. The long maturity LGFA and Housing NZ bonds have continued to perform well as their credit spreads compressed to “expensive” levels relative to NZ government bonds. The system remains awash with short-term liquidity with the RBNZ buying bonds back from the market, and demand for new lending is likely to remain slow, which will limit bond issuance from banks.

Financial markets have shown substantial improvement, but we remain cautious and believe that the best strategy is to focus on positioning the funds to outperform over the medium to long term.

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. We contributed to returns by adding quality credit at cheaper levels and extending 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

Wholesale fund: calendar quarter
 Retail fund: calendar quarter
 KiwiSaver fund: does not distribute

Estimated annual fund charges (incl. GST)

Wholesale fund: negotiated outside of unit price
 Retail fund: 0.79%, refer PDS for more details
 KiwiSaver fund: 0.80%, refer PDS for more details

Hedging

All investments will be in New Zealand dollars

Buy / Sell spread:

[Click to view](#)

Strategy size

\$299.7m

Strategy Launch

July 2009

Compliance

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

Contact Us

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