

Factsheet 30 June 2020

# 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

- NZ credit issues remain in tight supply, with the exception of offshore supranational, sovereign and agency bonds issuing in NZD.
- NZ interest rates finished the month higher in yield.
- The actions and language of central banks and governments continues to have a strong influence on bond markets.

## Fund Highlights

- The fund returned 4.8% over the quarter. Returns were negative for the month as interest rates moved higher in yield.
- Credit holdings of NZ issuers have continued to perform well with supply limited.
- The fund continues to perform well relative to benchmark.

## Performance

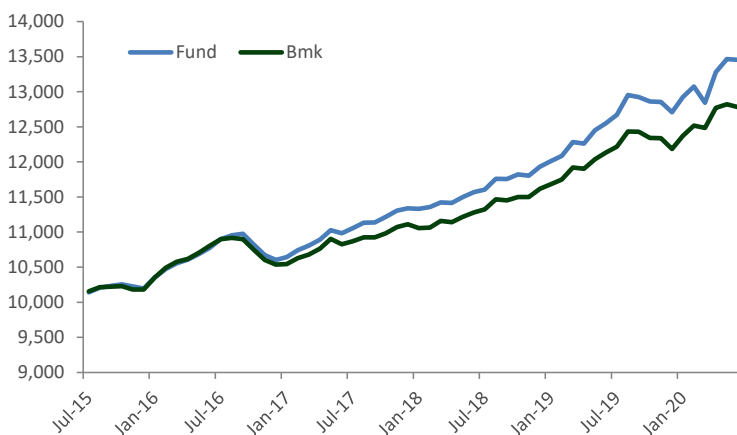
	One month	Three months	One year	Three years (p.a)	Five years (p.a)	Ten years (p.a)
Wholesale <sup>1</sup>	-0.07%	4.77%	7.20%	7.00%	6.11%	6.64%
Benchmark <sup>2</sup>	-0.29%	2.39%	5.36%	5.69%	5.03%	5.33%
Retail <sup>3</sup>	-0.12%	4.58%	6.42%	6.21%	5.30%	

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<sup>1&2</sup>



## 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.

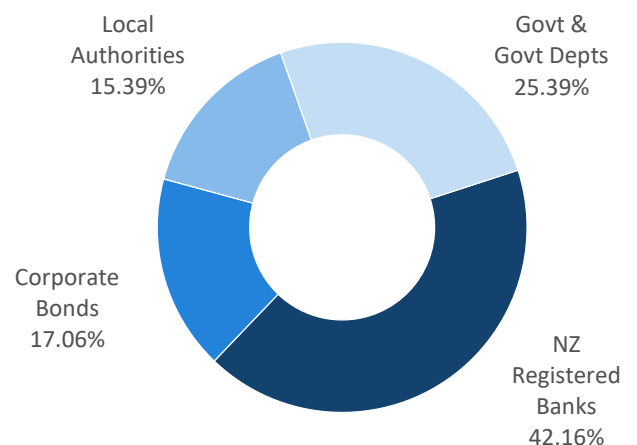
## Overview

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	11.06%	AAA	14.81%	Fund 5.35 years vs Benchmark 5.03 years
Bank Of New Zealand	7.00%	AA	57.09%	
Westpac New Zealand	5.90%	A	23.89%	Yield Fund (gross) 1.13% vs Benchmark 0.71%
Fonterra Cooperative Group	5.41%	BBB	2.65%	
Housing New Zealand	4.23%	BB	1.56%	

\*excludes central government

## Market Commentary

Returns from NZ bonds were low to negative for June, although the fund performed well relative to benchmark. In NZ over the month interest rates finished higher in yield, and credit continued to perform well as the supply of issuers remains limited. The language and actions of central banks and governments continue to have a strong influence on bond markets.

The main driver of lower absolute returns over the month was the move higher in longer term interest rates. On a positive note the fund’s higher yield and credit holdings continue to support returns. Longer maturity NZ interest rates have moved higher in yield for a number of reasons; the pricing of negative interest rates has reduced, the rebound in the economy is looking stronger, and NZ had got expensive on a relative basis compared to other markets. There is also a syndication of a new 2041 Government bond in mid-July. Typically the market will cheapen before a volume of new bond issuance to find a level that is more attractive to prospective buyers. Offshore investors will be needed to participate in the new bond to make it a success, and they will likely be looking at relative value versus Australia which is currently higher in yield than NZ.

NZ credit margins are looking expensive as in many cases they are now at narrower than pre-COVID levels, however demand to buy bonds has been strong with interest rates falling 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 bonds underperformed both the swap and credit sectors over the month. The 1-year government bond increased by 12 basis points (bps), the 5-year increased 6 bps, and 10-year finished 10 bps higher. While government bonds moved higher in yield, swap spreads have contracted and are currently around 7 to 18 bps lower in yield than similar maturities of government bonds. Credit remained a strong 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 June margins were around 75 bps with strong secondary demand seeing transactions going through well below mid pricing. The banking system remains awash with short term liquidity with the RBNZ buying bonds back from the market, and demand for new lending slow, bond issuance from banks is likely to be limited.

## Fund Commentary

The fund returned 4.8% for the quarter, and outperformed its benchmark by 238 basis points. The main positive contributor to returns was the strong performance from credit holdings and higher fund yield. Credit margins have performed strongly with supply very limited. We sold some bonds that looked expensive and switched into slightly longer duration SSA bonds at better levels, also marginally extending duration. We will continue to focus on maintaining a higher portfolio yield through buying quality non-government bond issues. It is likely future returns will be supported by a higher yield, and some further improvement in credit margins over the medium to long term.

## Key Fund Facts

<b>Distributions</b>		<b>Estimated annual fund charges (incl. GST)</b>	
Wholesale fund:	Calendar quarter	Wholesale:	Negotiated outside of unit price
Retail fund:	Calendar quarter	Retail:	0.70%, refer PDS for more detail
<b>Hedging</b>		<b>Buy / Sell spread</b>	<b>Strategy size</b>
All investments will be in New Zealand dollars		<a href="#">Click to view</a>	\$362.75m
			<b>Strategy Launch</b>
			October 2007

## Compliance

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

## Contact Us

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