

# 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 interest rates have continued lower as expectations for further rate cuts and the possibility of a negative cash rate was priced into markets.
- Credit has performed strongly, and may find some stability around current levels.
- The actions and language of central banks and governments continues to have a strong influence on bond markets.

## Fund Highlights

- Fund returns were strong over the month as interest rates moved lower in yield.
- Credit holdings of NZ issuers have continued to perform well with supply limited.
- The fund continue to perform well relative to benchmark.

## Performance

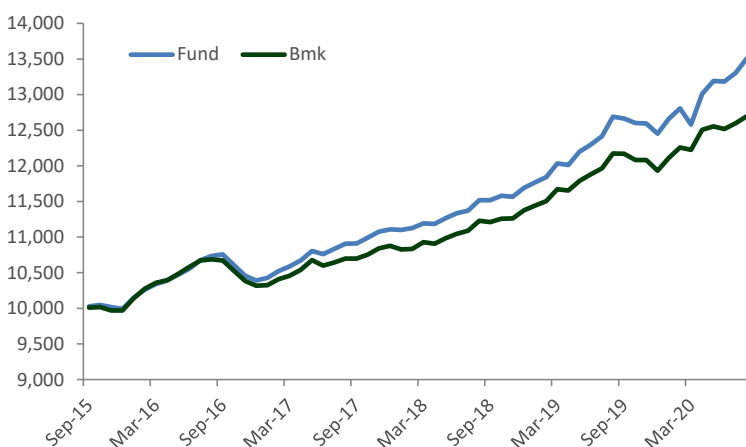
	One month	Three months	One year	Three years (p.a)	Five years (p.a)	Ten years (p.a)
Wholesale <sup>1</sup>	1.54%	2.40%	6.45%	7.39%	6.20%	6.67%
Benchmark <sup>2</sup>	0.78%	1.16%	4.29%	5.88%	4.89%	5.30%
Retail <sup>3</sup>	1.49%	2.23%	5.67%	6.60%	5.40%	

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.

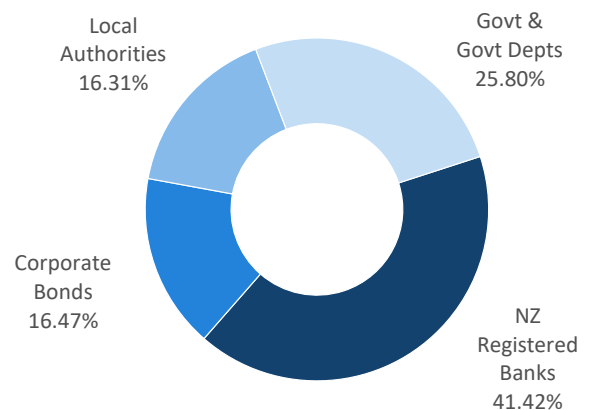
## Overview

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



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Top 5 Corporate Issuers*	(%)	Credit Quality	(%)	Duration
NZ Local Govt. Funding Agency	12.11%	AAA	13.35%	Fund 5.92 years vs Benchmark 5.35 years
Bank of New Zealand	6.63%	AA	59.61%	
Fonterra Cooperative Group	5.21%	A	23.03%	
Westpac New Zealand	5.04%	BBB	2.50%	
Kommunalbanken	5.03%	BB	1.51%	
				Yield
				Fund (gross) 0.84% vs Benchmark 0.48%

\*excludes central government

## Market Commentary

NZ bonds returns were strong for the month of August both in absolute terms and relative to benchmark. The key drivers of strong returns over the month were the move lower in interest rates and continuing strong performance from credit holdings as margins contracted.

NZ was again one of the better performing bond markets as the actions and language of the Reserve Bank of New Zealand have been very supportive of bonds. In their August commentary the RBNZ again surprised markets with a more “dovish” outlook than market expectations. Interest rates fell, particularly bonds out to 5-years in maturity as expectations for further rate cuts and the possibility of a negative cash rate was priced into markets. Most commentators have now changed their forecasts to expect further rate cuts, although this may be 6 months away. The RBNZs’ QE bond buying programme has also been ramped up, which remains supportive with expectations that a lot of the large government bond issuance is already done for this year. Local Government Funding Authority (LGFA) bond buying has been at a faster pace than issuance which has helped to further support local credit markets.

On a sector basis NZ government bonds performed better than swap over the month. Credit holdings were generally the strongest performing bonds. The yield curve has remained steep in slope as the move lower in yields was greater in the short to mid curve than for longer maturity bonds. The 3-year government bond decreased by 20 basis points (bps), the 5-year fell 20 bps, and 10-year finished 12 bps lower. It is however important to note that longer maturity bonds increase more in value than shorter maturities when yields fall due to their longer duration exposure and resultant greater leverage to interest rate movements. Credit remained a strong performer, for example 5-year senior bank debt in NZ was marked at a credit margin of around 60-65 bps at the end of July, and finished August another 15 to 20 bps lower in margin. The financial system remains awash with short term liquidity, and demand for bonds continues to dominate supply. New corporate bond issues have ramped up, and although we don’t expect credit margins to widen they may stabilise some after such a strong run.

## Fund Commentary

The fund outperformed its benchmark over the month. The main positive contributors to returns were the longer duration positioning, and strong performance from credit supported by higher fund yield. We extended duration and added some long maturity bonds when yields were higher and the yield curve steep. Credit margins have performed strongly with supply very limited. We will continue to focus on maintaining a higher portfolio yield through buying quality non-government bond issues.

## 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: 0.70%, refer PDS for more detail

### Hedging

All investments will be in New Zealand dollars

### Buy / Sell spread

[Click to view](#)

### Strategy size

\$379.5m

### Strategy Launch

October 2007

## Compliance

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

## Contact Us

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